

Equities

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Unione Banche Italiane (UBI.MI)

Alert: UBI Banca 3Q10 Results: Initial Reaction

■ Company Update

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- **Results Ahead** – UBI posted a €96m net profit in 3Q, better than consensus estimates (€80m). GOP is 7% ahead of consensus expectations due to stronger NII, better costs and lower provisions. Higher taxes and lower commissions have partially offset a good progression in core profitability.
- **The Strongest NII** – UBI shows a strong progression in NII QoQ, up 4% QoQ, 1.3% ahead of consensus expectations. This increase is driven by volume growth (+1% QoQ) and margin expansion. UBI has shown the strongest increase in NII within our Italian universe, this is in line with our expectations, and reflects the bank's simple retail-based business model, which benefits from rising Euribor and lending volumes. NII should continue to improve in 4Q.
- **Weaker Commission, Stronger Trading** – Similarly to other Italian banks, UBI has shown weaker-than-expected commission and stronger trading income. Overall total revenues are in line with consensus expectations. Commission has been weaker than expected as a result of seasonality and a lack of third-party bond placement fees. UBI expects commission to increase significantly in 4Q.
- **A Positive Surprise from Costs** – Operating costs are 3% below consensus showing decreasing staff costs and other administrative expenses. Cost to asset ratio decreased further to 1.78% in 3Q from 1.88% in 2Q.
- **Lower Cost of Risk, Still Rising NPLs** – Bad debt provisions are well below consensus expectations (c-20%) at 53bp on loans annualised, below our 67bp estimates and the 76bp reported in 2Q. Total Net NPLs increased c.7% QoQ, showing a still-rising NPL ratio (5.1% in 3Q vs 4.8% in 2Q), mostly due to rising sofferenze (+9% QoQ), while showing decreasing Incagli (-1.3% QoQ).
- **Increasing Capital** – Core Tier 1 increased to 7.6% in 3Q from 7.3% in 2Q, due to increasing profitability and disposals impact, and also including dividend accrual.
- **4Q Outlook** – UBI has provided an outlook for 4Q, based on higher NII, recovery in commissions, and still focus on costs. On cost of credit, UBI indicates it around 70bp for 2010FY (vs c60bp in 9M10, allowing for a seasonal worsening in 4Q). This seems broadly in line with our expectations.
- **Conference Call** – Management will host a conference call this afternoon at 3:30pm Milan time, dial in +39 805 88 11.

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Figure 1. UBI Banca – Quarterly Key Data

Profit and Loss Account (Euro m)	3Q09	2Q10	3Q10	3Q10 vs Cons	3Q10 vs 2Q10	3Q10 vs 3Q09	3Q10 Cons	3Q10 vs Citi	3Q10E Citi
Net Interest Income	588	533	557	+1%	+4%	-5%	550	+1%	549
Dividends and Other Income	6	17	2	-	nm	nm		nm	3
Income (Loss) from Equity Investments	9	6	8	-	nm	nm		nm	14
Net Commission Income	297	314	264	-7%	-16%	-11%	285	-8%	288
Trading Results	26	(1)	19	-	nm	-27%		nm	10
Insurance Result	9	0	0	-	nm	nm		nm	0
Other Net Operating Income	24	17	25	-	+48%	+4%		+15%	22
Total Revenues	960	886	877	+0%	-1%	-9%	875	-1%	886
Personnel Costs	(373)	(376)	(360)	-	-4%	-4%		-1%	(365)
Other Operating Expenses	(175)	(200)	(184)	-	-8%	+5%		+6%	(173)
D&A	(42)	(43)	(42)	-	-3%	+0%		-0%	(42)
Total Operating Costs	(590)	(619)	(585)	-3%	-6%	-1%	(602)	+1%	(580)
Operating Profit	370	267	292	+7%	+9%	-21%	273	-5%	306
Net Bad Debt Charges	(197)	(190)	(134)	-21%	-29%	-32%	(170)	-21%	(169)
Net Impairment on Assets	(1)	(19)	(0)	-	nm	nm		nm	0
Provisions for Risk/ Charges	(3)	(4)	(5)	-	+22%	nm		nm	(2)
Sale of Assets	(0)	(2)	80	-	nm	nm		nm	65
PBT	169	52	232	-	+348%	+37%		+16%	200
Taxes	(78)	(45)	(114)	-	+150%	+46%		+61%	(71)
Integration Costs and PPA	(21)	(21)	(20)	-	nm	nm		nm	(21)
Impact from Discontinued Op	0	83	0	-	nm	nm		nm	0
Minorities	(9)	(5)	(3)	-	-31%	-62%		nm	(8)
Net Profit	61	64	96	+20%	+50%	+56%	80	-5%	101
Core revenues	885	847	821	-2%	-3%	-7%	835	-2%	837
GOP after provisions	173	77	158	+53%	+104%	-9%	103	+15%	137
Core profitability	98	38	102	+62%	+168%	+4%	63	+16%	88
Balance Sheet (Em)									
Assets	125,501	132,099	131,744	-	-0%	+5%		-1%	133,420
Customer Loans	96,555	100,158	101,195	-	+1%	+5%		+0%	101,159
Deposits	95,547	103,362	103,876	-	+0%	+9%		-1%	105,071
Ratios									
Revenues / Assets (ann)	3.06%	2.68%	2.66%		-0.0%	-0.4%		0.0%	2.66%
Cost/ Income Ratio	61%	70%	67%		-3%	+5%	70%	1%	65%
Cost to Asset Ratio (ann)	1.88%	1.88%	1.78%		-0.1%	-0.1%		+0.0%	1.74%
Cost of Risk (bps, ann)	82	76	53		-23	-29		-14	67
Loan to Deposit Ratio	101%	97%	97%		+1%	-4%		1%	96%
Tax Rate	46%	87%	49%		nm	+3%		9%	40%
Core tier 1	7.3%	7.3%	7.6%		0.2%	0.2%		0.2%	7.4%

Source: Citi Investment Research and Analysis, Bloomberg, Reuters Consensus.

Unione Banche Italiane (UBI.MI; €7.25; 2H)

Unione Banche Italiane

Valuation

We have an €8.50 target price for UBI shares, based on a DDM calculation. In valuing UBI, we focus primarily on a DDM valuation using a c12% cost of equity and a c11% sustainable tangible ROE, also taking into account the group's capital position. We cross-check this with a price-to-book methodology. At our target price, the stock would trade at c0.9x price to tangible book valuation, a premium to most other Italian banks, reflecting UBI's defensive business mix and balance sheet characteristics, despite low profitability.

Risks

We have a High Risk rating on UBI shares. Any revenue slippage would impact UBI's profits. Net interest income is the major revenue generator; NII margin and profitability are at risk in the event of movement of the ECB rate and movement in the credit market rates, or of more pricing pressure in Italy. Among the potential risks for the stock, we would highlight: a weaker-than-expected Italian economy, slowdown in dividend payments, deterioration in asset quality, rising provisions, market fears about the capital requirements for banks and any speculation indicating UBI as a possible partner in case of a rescue merger of any of its peers. If the impact on the company from any of these factors proves to be more or less negative than we anticipate, the stock could deviate significantly from our target price. The recent management change should not represent a key risk for the stock.

Appendix A-1

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Covered since May 5 2010

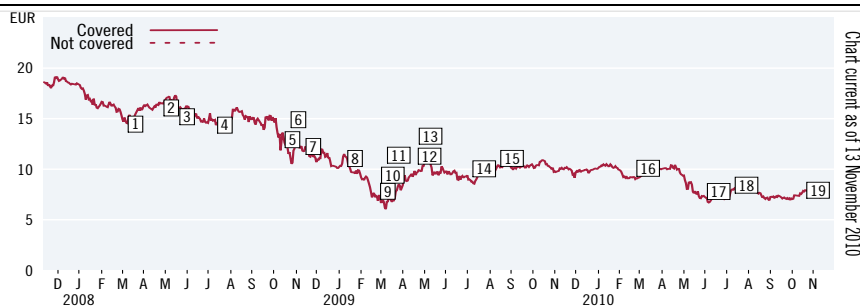


Chart current as of 13 November 2010

	Date	Rating	Target Price	Closing Price
1	20-Mar-08	2M	*16.72	15.47
2	9-May-08	2M	*17.70	16.84
3	2-Jun-08	*1M	*18.49	16.14
4	24-Jul-08	1M	*17.70	14.86
5	28-Oct-08	1M	*13.77	10.64
6	5-Nov-08	1M	*15.24	12.79
7	26-Nov-08	1M	*13.77	11.22

	Date	Rating	Target Price	Closing Price
8	23-Jan-09	1M	*11.31	9.57
9	11-Mar-09	1M	*8.85	6.81
10	18-Mar-09	*1H	8.85	6.93
11	26-Mar-09	1H	*10.03	8.52
12	8-May-09	1H	*13.28	11.29
13	11-May-09	1H	*12.59	10.48
14	24-Jul-09	*2H	*10.80	9.56

	Date	Rating	Target Price	Closing Price
15	2-Sep-09	2H	*10.50	10.13
16	12-Mar-10	2H	*10.00	9.72
17	20-Jun-10	2H	*8.00	7.60
18	29-Jul-10	2H	*9.00	8.32
19	8-Nov-10	2H	*8.50	7.40

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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