1.1 CREDIT RISK

QUALITATIVE INFORMATION

The Group's strategies, credit risk appetite, powers and rules for credit granting and management are aimed at:
- achieving sustainable growth of lending operations consistent with the risk appetite and value creation;
- diversifying the portfolio, limiting the concentration of exposures on single counterparties/groups, single economic sectors or geographical areas;
- efficiently selecting economic groups and individual borrowers through a thorough analysis of their creditworthiness aimed at limiting the risk of insolvency;
- given the current economic climate, privileging lending business aimed at supporting the real economy and production system;
- constantly monitoring relationships, through the use of both IT procedures and systematic surveillance of positions, with the aim of detecting any symptoms of imbalance and promoting corrective measures geared towards preventing possible deterioration of the relationship in a timely manner.

Constant monitoring of the quality of the loan portfolio is also pursued through specific operating checks for all the phases of loan management.

Credit risk management policies

Organisation

Within the Intesa Sanpaolo Group, a fundamental role in managing and controlling credit risk is played by the corporate bodies, which, to the extent of their respective competences, ensure adequate coverage of credit risk by setting strategic guidelines and risk management policies, verifying that they remain constantly efficient and effective and assigning tasks and responsibilities to the company functions and units involved in the processes.
The coverage and governance of credit ensured by the corporate bodies is reflected in the current organisational structure, which identifies areas of central responsibility attributable to:
- Chief Lending Officer
- Chief Risk Officer
- Chief Financial Officer

They ensure that risk control activities are managed and implemented, with an appropriate level of segregation, in addition to the establishment of the supporting processes and applications.
The Chief Lending Officer assesses the creditworthiness of the loan applications received and, where applicable, approves them or issues a compliance opinion; ensures the proactive management of credit, under his/her responsibility, and the management and monitoring of non-performing loans not in bad loan status; establishes the Credit Granting and Management Rules; ensures that positions classified as non-performing, under his/her responsibility, are properly measured for financial reporting purposes; allocates the ratings to the positions that require specialist assessments and assesses the improvement override proposals made by the competent departments; and defines operating credit processes, in collaboration with the subsidiary Intesa Sanpaolo Group Services, also on proposal from the Group's various functions/structures.
The Chief Risk Officer is responsible for adapting the Risk Appetite Framework to the management of credit risk, in accordance with company strategies and objectives, as well as for measuring and controlling the Group's risk exposures, defines the metrics used to measure credit risk, provides risk-adjusted pricing models and guidelines for expected loss, economic capital (ECAP), RWA and acceptance thresholds, formulates proposals for assigning Credit Granting and Managing Powers, and it carries out II level credit monitoring and controls, including rating controls. With specific regard to the collective measurement of performing loans and the measurement of non-performing loans on a statistical basis, he or she supervises credit risk measurement models.
The activities are performed directly by the Chief Risk Officer Governance Area for both the Parent Company and the main subsidiaries, according to a service contract.
In accordance with the strategic guidelines and risk management policies set by the Board of Directors, the Chief Financial Officer coordinates the process of formulating credit strategies (a process in which the other chiefs and the business units participate) and oversees pricing from a risk/return standpoint according to value creation objectives. The Chief Financial Officer is also responsible for identifying and implementing hedging transactions for the risk exposures of the asset classes in the loan portfolio by taking advantage of the opportunities presented by the secondary credit market with a view towards active management of company value.
In addition, within the framework of the loan assessment process, the Administration and Tax Head Office Department, under the Chief Financial Officer, is responsible for incorporating the assessments of loan positions formulated, on a collective or individual basis, by the competent departments, as well as for coordinating the process of assessing loans for financial reporting purposes.
Lastly, as is the case for all the risk areas and above all for credit risk, the Internal Auditing Head Office Department performs internal audits aimed at identifying breaches of the procedures and regulations and periodically assessing the completeness, adequacy, functioning (in terms of efficiency and effectiveness) and reliability of the internal control system and the ICT system (ICT audit), at preset intervals according to the nature and extent of the risks.

Credit granting autonomy limits, which incorporate the amount of loans granted (EAD), the risk level of the customer (PD), the loss rate in the event of a default by the borrower, possibly mitigated by the presence of guarantees (LGD), and maturity, are defined in terms of risk-weighted assets and reflect the risks assumed/to be assumed by the Intesa Sanpaolo Group towards the Economic Group.
Intesa Sanpaolo, as the Parent Company, has set out codes of conduct in relation to credit risk acceptance, in order to prevent excessive concentrations, limit potential losses and ensure credit quality.
In the credit-granting phase, coordination mechanisms have been introduced with which Intesa Sanpaolo exercises its direction, governance and support of the Group:
- the system of Credit Granting and Management Powers and Credit Rules Lending governing the ways in which credit risk to customers is assumed;

- the "Credit-ceiling", intended as the overall limit of lines of credit which may be granted by companies of the Intesa Sanpaolo Group to the larger Economic Groups;
- the "Advisory opinion" on credit-granting to large customers (single name or Economic Group) by Group subsidiaries which exceeds certain thresholds;
- the "Rules on Credit Risk Appetite" that regulate the application of the CRA, whose purpose is to achieve growth in sustainable loans.

The exchange of basic information flows between different Group entities is assured by the Group's "Centrale Rischi" (exposure monitoring and control system) and by the "Posizione Complessiva di Rischio" (global risk position), which highlight and analyse credit risks for each counterparty/economic group both towards the Group as a whole and towards individual Group companies.

Management, measurement and control systems

Intesa Sanpaolo has developed a set of instruments which ensure analytical control over the quality of loans to customers and financial institutions, and of exposures subject to country risk.

Risk measurement is performed by means of different rating models according to borrower segment (Corporate, Retail SME, Retail Mortgage, Other Retail, Sovereigns, Italian Public sector entities and Financial institutions). These models make it possible to summarise the counterparty's credit quality in a value, the rating, which reflects the probability of default over a period of one year, adjusted on the basis of the average level of the economic cycle. These ratings are then made comparable with those awarded by rating agencies, by means of a uniform scale of reference.

A number of rating models are used for the Corporate segment:

- models differentiated according to the market (domestic or international) and size bracket of the company are applied to most businesses;
- specific models are in use for specialised lending, one for real-estate initiatives, one for project-finance transactions and one for LBO/acquisition-finance and asset-finance transactions.

In general terms, the structure of these models requires the integration of multiple modules:

- a quantitative module that processes financial and behavioural data;
- a qualitative module that requires the manager to fill in a questionnaire;
- an independent assessment by the manager, organised as a structured process, which triggers the override procedure if there is a discrepancy with respect to the integrated rating.

Ratings are generally assigned on a decentralised basis by the Manager, who is the main figure in the process of assigning a rating to a counterparty. The validation of any improvement override proposals is performed by the Specialist Rating Sub-Department within the Credit Coordination Head Office Department. This sub-department is responsible for, among other duties, the task of assigning what are known as "centralised ratings" provided for in the rating assignment processes according to the corporate method and of intervening in the calculation of ratings with specialist models.

The models applied to the Retail portfolio are as follows:

- for the Retail SME segment, since the end of 2008 a Group rating model by counterparty has been used, following a scheme similar to that of the Corporate segment, meaning that it is extremely decentralised and its quantitative-objective elements are supplemented by qualitative-subjective elements; in 2011, the service model for the Small Business segment was redefined, by introducing in particular a sub-segmentation of Micro and Core customers according to criteria of size, simplicity, and a partial automation of the granting process. This required an adjustment of the rating model, which was divided into the two above-mentioned sub-segments, taking advantage of the opportunity to update the data sources and historical series used in development;
- for the Retail Mortgage segment (residential mortgages for private individuals), the Group model processes information relating to both the customer and the contract. It differentiates between initial disbursement, where the acceptance model is used, and the subsequent assessment during the lifetime of the mortgage (performance model), which takes into account behavioural data;
- for products aimed at individuals (the Other Retail segment), a new approval model was made available in September 2014 for operational purposes, which is applied to all new disbursements (such as personal loans, credit cards, and credit facilities on current accounts).

The rating model for the Sovereign portfolio supports the assignment of an assessment of creditworthiness for over 260 countries. The structure of the model involves:

- a quantitative module for assessing country risk, which takes account of the structural rating assigned by the major international agencies, the risk implicit in market quotations of sovereign debt, a macroeconomic assessment of countries identified as strategic and the international scenario;
- a qualitative opinion component, for which the Sovereign Rating Working Group is responsible, supplementing the qualitative opinion with elements drawn from the broader scope of publicly available information concerning the political and economic structure of individual sovereign countries.

The framework is completed by the class of regulatory exposures consisting, on the one hand, of banks (and other financial companies attributable to banking groups) and near banking companies (companies that engage in leasing, factoring and consumer credit), and, on the other, public entities:

- in the Banks segment, from the standpoint of determining probability of default, the key decision was to differentiate the models for banks in mature economies and banks in emerging countries, the structure of which, however, is highly similar. In short, these consist of a quantitative part and a qualitative part, differentiated according to mature and emerging countries, a country rating component relating to systemic risk, a component relating to specific country risk for banks most closely correlated with country risk, and finally, a module (the "manager's opinion") that allows the rating to be modified in certain conditions;
- in the Public Entities segment, the models of reference have been differentiated according to the type of counterparty. Accordingly, default models have been developed for municipalities and provinces and shadow rating models for regions. An extensive approach has been adopted for local healthcare authorities and other sector entities, starting with the legally superior entities, with possible notching based on statistical assessments of financial statements.

Experience-based models are used for counterparties belonging to the Non-Banking Financial Institutions portfolio.
The LGD model is based on the concept of "Economic LGD", namely the present value of the cash flows obtained in the various phases of the recovery process net of any administrative costs directly attributable to the exposure as well as the indirect management costs incurred by the Group, and consists, in brief, of the following elements:
– estimate of a Bad LGD Model: starting from the LGD observed on the portfolio, namely "Workout LGD", determined on the basis of the recoveries and costs, a regression econometric model of the LGD is estimated on variables considered to be significant for the determination of the loss associated to the Default event;
– application of a correction factor, known as "Danger Rate": the Danger Rate is a multiplying correction factor, used to recalibrate Bad LGD with the information available on the other default events, in order to calculate an LGD representative of all the possible default events and their evolution;
– application of an additional correction factor, known as "Final Settlement Component": this component is used as an add-on to the estimate recalibrated for the Danger Rate in order to consider the loss rates associated with positions not evolved to the Bad Loan status (Unlikely to pay or Past Due positions).

LGD is determined according to differentiated models, specialised by operating segment (Corporate, Retail SME, Retail Mortgage, Other Retail, Factoring, Leasing and Public Entities).
The Banks LGD model partly diverges from the models developed for the other segments, given the peculiarities of the segment, which has a low number of defaults ("low-default portfolios"). The estimation model is a market LGD approach, based on the market price of debt instruments observed 30 days after the official date of default for a sample of defaulted banks from all over the world. The market data are provided by an external provider. The model is completed by an econometric estimate aimed at determining the most significant drivers, in accordance with the practice in use for the other models.

The rating models (PD and LGD) for the Retail Mortgage segment received authorisation for transition to the IRB approach effective from June 2010 report, while rating models for the Retail SME segment received authorisation for transition to the IRB approach effective from December 2012 report. The rating models for the Corporate segment received authorisation for the use of the AIRB approach to calculate capital requirements effective from 31 December 2010 reporting date (the FIRB approach had been used since December 2008), while the LGD Corporate models for Leasing and Factoring products received authorisation for transition to the AIRB approach effective from the June 2012 report.
For information on the plan to extend the IRB approach to other portfolios, refer to the paragraph concerning the Basel 3 Project.
PD and LGD models have been adopted for the counterparties of the International Subsidiary Banks, partly derived from the Parent Company and partly adapted to the local situation which was entirely developed by the subsidiaries concerned.

The rating system also includes a risk monitoring process, calculated on a monthly basis. It interacts with processes and procedures for loan management and credit risk control and allows timely assessments when any anomalies arise or persist. The positions to which the synthetic risk index attributes a high risk valuation, which is confirmed over time, are intercepted by the Proactive Management process.
Starting from July 2014 the new Proactive Credit Management process was activated, setting up a specialised dedicated chain in the Regional Governance Centres, the CIB Division and the CLO structures.
The objective is to promptly identify performing positions with early signs of difficulty and immediately implement the most suitable actions to remove the anomalies and restore the relationship of trust. The introduction of Proactive Management has also significantly simplified the processes, with the removal of the old non-performing loan statuses.
During the year, the project named "IT Infrastructure in Support of the Single Supervisory Mechanism (SSM)" was completed with the release of the new Early Warning System model for intercepting and classifying defaults, for the Corporate portfolio, also developed to meet the requirements arising from the 2014 Comprehensive Assessment (AQR impairment trigger). This model replaces the previous IRIS model. The proactive credit management processes were also reviewed at the same time.
The entire loan portfolio is also subject to a specific periodic review carried out by the competent central or peripheral structures based on the credit line limits for each counterparty/economic group.

Through specific monitoring, control, guidance and coordination activities, the Internal Validation and Controls Head Office Department, within the Chief Risk Officer Governance Area, oversees the credit granting and management processes for the performing loans portfolio at the Group level and through controls on individual positions assesses that loans are properly classified. It also carries out monitoring and controls on the rating assignment and update processes.

Country risk is an additional component of an individual borrower's insolvency risk, measured by credit risk control systems. This component is linked to losses potentially resulting from international lending operations caused by events in a country that are partly or entirely within the control of the government concerned, but not that of the individual residents of the country in question. Country risk therefore takes the form of both transfer risk for non-sovereign counterparties, due to the freezing of international payments, and sovereign risk, which is measured through an assessment of the sovereign states' creditworthiness. This definition includes all forms of cross-border lending to entities residing in a given country, whether they are the government, a bank, a private enterprise or an individual.
The country risk component is assessed in the context of the granting of credit to non-resident entities in order to obtain a preliminary evaluation of the absorption of country risk limits set on an ex-ante basis. Such limits, expressed in terms of economic capital, identify the maximum acceptable risk for the Group, defined on an annual basis as the result of an exercise aimed at optimising the risk implicit in the Group's cross-border lending operations.

Counterparty risk is a particular kind of credit risk associated with OTC derivative contracts that refers to the possibility that a counterparty may default before the contract matures. This risk, which is often referred to as replacement risk, is related to the case in which the market value of a position has become positive and thus, were the counterparty to default, the solvent party would be forced to replace the position on the market, thereby suffering a loss.
Counterparty risk also applies to securities financing transactions (repurchase agreements, securities lending, etc.).

In 2010 a specific project was launched to ensure that the Banking Group has an internal model for measuring counterparty risk, both for operational and regulatory purposes. The organisational functions involved, as described in the Bank's internal regulations, are:

- the Chief Risk Officer Governance Area, which is responsible for the counterparty risk measurement system by defining calculation methods, producing and analysing measures of exposure;
- the Level I and Level II control functions that use the measurements produced to monitor the assumed positions;
- the marketing and credit functions that draw on the foregoing measures as part of the granting process to determine the limits of the lines of credit.

The project yielded the following results:
- the Banking Group set up a suitably robust IT, methodological and regulatory infrastructure, in accordance with the use test requirement set out by regulations on internal models;
- the Banking Group integrated the risk measurement system into decision-making processes and the management of company operations;
- cutting-edge methods were adopted for calculating drawdowns on credit lines;
- the Supervisory Authority validated the Parent Company's and Banca IMI's use of the internal model for calculating the counterparty requirement in the first quarter of 2014. The first report using the internal model (with a view to Basel 3) was made on 31 March 2014, relating to the scope of Parent Company and Banca IMI OTC derivatives.
- the banks of the Banca dei Territori Division were authorised to use the internal model for the capital requirement with effect from the report as at 31 December 2016.
- the Group obtained authorisation to use the internal model for the capital requirement for SFT – Securities Financing Transactions instruments with effect from the report as at 31 December 2016.

Potential exposure (estimated with the actual average PFE - Potential Future Exposure) has been adopted by the entire Banking Group for the purposes of operational measurement of uses of lines of credit for derivatives. The Financial and Market Risks Department produces daily risk measurement estimates for counterparty risk, for the measurement of the uses of credit lines for OTC derivatives for the Parent Company, Banca IMI and the banks of the Banca dei Territori Division. It should be noted that the PFE method, in simplified form, is used for the banks of the International Subsidiary Banks Division.
In addition, the following company processes were implemented to complete the risk analysis process for the exposure measures implemented over time following the developments discussed above:
- definition and periodic calculation of stress tests on market scenarios and joint market/credit scenarios on counterparty risk measures;
- definition and periodic analysis of Wrong-Way Risk, i.e. the risk of a positive correlation between the future exposure to a counterparty and that counterparty's probability of default;
- definition and monitoring of management limits;
- contribution of collateral inflow/outflow risk measures, calculated on the basis of the internal counterparty risk model, for OTC derivatives transactions with collateral agreements (CSA);
- periodic reporting to the management of measures calculated using the internal exposure model, capital requirement, level of use of management limits, results of stress tests and analyses of wrong-way risk.

Directional control of credit risks is achieved through a portfolio model which summarises the information on asset quality in risk indicators, including expected loss and capital at risk.
The expected loss is the product of exposure at default, probability of default (derived from the rating) and Loss Given Default.
The expected loss represents the average of the loss statistical distribution, whereas the capital at risk is defined as the maximum "unexpected" loss that the Group may incur with particular confidence levels. These indicators are calculated with reference to the current status of the portfolio and on a dynamic basis, by determining the projected level, based on both the forecast macroeconomic scenario and on stress scenarios.
The expected loss, transformed into "incurred loss", as indicated by IAS 39, is used in the collective provisioning, while capital at risk is the fundamental element in the assessment of the Group's capital adequacy. Both indicators are also used in the value-based management reporting system.
The loan portfolio model allows the level of expected loss to be measured with the chosen confidence interval, or capital at risk. The latter reflects not only the risk level of individual counterparties but also the effects of undesired concentration due to the geographical/sector composition of the Group's loan portfolio.

The Group dedicates special attention to assessing concentration risk deriving from the exposure to counterparties, groups of related counterparties and counterparties in the same business segment or that engage in the same business or operate in the same geographical region. In the annual update of the Risk Appetite Framework, such counterparties are subject to stress tests aimed at identifying and assessing threats for the Group and the most appropriate mitigating actions:
- aimed at defining exposure limits for specific geographical areas and sets of counterparties (top 20);
- aimed at ex ante limitation of exposures with significant concentration effects, in particular with reference to "large risks" and to credit lines subject to country risk;
- aimed at ex post correction of the profile, through the secondary loan market, through specific judgement metrics based on the maximisation of overall portfolio value.

The Group's lending activity is focused on Italian customers (83% of the total) and is primarily aimed at households and small and medium enterprises. In addition, it shows strong diversification, especially as regards certain business sectors and geographical areas, as well as loans to countries at risk.

Credit risk mitigation techniques

Mitigation techniques are adopted in order to reduce the Loss Given Default. In particular, they include guarantees and certain types of contracts that result in a reduction in credit risk.

The evaluation of the mitigating factors is performed through a procedure that assigns a loss given default to each individual exposure, assuming the highest values in the case of ordinary non-guaranteed financing and decreasing in accordance with the strength given to any mitigating factors present. The Loss Given Default values are subsequently aggregated at customer level in order to provide a summary evaluation of the strength of the mitigating factors on the overall credit relation.

During the credit granting and managing process, the presence of mitigating factors is encouraged for counterparties with non-investment grade ratings or some types of transactions, namely medium-/long-term transactions.

The mitigating factors that have the greatest impact include pledges of financial assets and residential mortgages. Other forms of risk mitigation are pledges of non-financial assets and non-residential mortgages.

The strength of the personal guarantees issued by rated parties, typically banks/insurance companies, Credit Guarantee Consortia and corporations, is instead assessed on the basis of the type of guarantee and guarantor's credit quality.

Detailed processes govern the material acquisition of individual guarantees, identifying the responsible structures as well as the methods for correct finalisation of guarantees, for filing documentation and for complete and timely reporting of the related information in the applications.

The set of internal regulations and organisational and procedural controls is aimed at ensuring that:

– all the fulfilments are planned to ensure the validity and effectiveness of the credit protection;
– for generally and normally used guarantees, standard contracts are defined, accompanied by instructions for use;
– the methods for approving guarantee documents deviating from the standard by structures other than those in charge of commercial relations with the customer are identified.

An overall revision of the rules, processes and instruments concerning guarantees received and, more generally, instruments that mitigate credit risk is underway. The goal of these activities is to increase the efficiency of management, reduce the related operational risks and increase the level of eligibility of the guarantees. Following a detailed analysis, the requirements and architecture of a new application platform to manage all the phases in the lifecycle of a guarantee (acquisition, modification, extinction, enforcement, control, monitoring and custody) were defined.

After the release of the module for the management of the personal guarantees of the Italian banks and international branches, in 2016 the part relating to real estate collateral was completed with the creation of a group register of real estate assets, integrated with the portal that manages the valuations, together with a module for the management of the guarantees.

The granting of credit with the acquisition of collateral is subject to internal rules and processes – for the evaluation of the asset, the acceptance of the guarantee and the control of its value. The enforcement of the guarantee is handled by specialist departments, which are responsible for credit recovery.

In any case, the presence of collateral does not grant exemption from an overall assessment of the credit risk, mainly concentrated on the borrower's ability to meet the obligations assumed, irrespective of the associated guarantee.

The assessment of the pledged collateral is based on the actual value, namely the market value for financial instruments listed in a regulated market, or, otherwise, the estimated realisable value. The resulting value is multiplied by the haircut percentage rates, differentiated according to the financial instruments accepted as collateral.

For real-estate collateral, the prudential market value is considered; for properties under construction, the construction cost is considered, net of prudential haircuts according to the intended use of the property.

Assets are appraised by internal and external experts. The external experts are included in a special list of professionals accredited on the basis of an individual verification of their capabilities, professionalism and experience. The valuation of residential properties used as collateral for mortgage loans to private individuals is mainly assigned to specialised companies. The work of the experts is monitored on an ongoing basis, by means of statistical verifications and spot checks carried out centrally.

The experts are required to produce estimates on the basis of standardised expert reports, differentiated according to the valuation method to be applied and the characteristics of the asset, in accordance with the Property Valuation Code ("Property Valuation rules for credit purposes") prepared by the Bank. The content of the internal Code is consistent with the "Guidelines for the valuation of properties securing credit exposures" promoted by the Italian Banking Association and with the "European Valuation Standards" (EVS2012).

Property valuations are managed through a specific integrated platform covering the entire expert analysis phase, ensuring that assignments are properly awarded, on an independent basis and according to objective criteria, the workflow is thoroughly monitored, valuation standards are correctly applied and all information and documents regarding real estate are kept.

The market value of collateral property is recalculated periodically through various statistical valuation methods, which apply prices/ratios provided by an external supplier offering proven skills and a solid reputation for surveying and measuring the market prices of Italian real-estate assets.

Asset value is constantly monitored. The experts carry out inspections and verify the work progress for properties under construction. The valuation is updated in the event of limitation or splitting of the mortgage, of damage to the property, significant impairment losses reported by market indicators used to monitor fair value and, in any case, every three years for major exposures.

In order to limit the risks of absence or termination of the protection, specific safeguards are in place, including: restoration of a pledge when the assets decrease below their initial value or, for mortgages, an obligation to carry insurance cover against fire damage and the presence of adequate monitoring of the property's value.

Guarantees are subject to accurate, regular control using a specific application, the CRM verifier, in which a series of tests have been implemented to confirm the effective compliance with the requirements set by prudential supervision regulations.

The support application verifies whether the guarantees received are eligible with reference to each of the three methods permitted by the regulations for calculating capital requirements. Based on the specifics of each category, the eligibility results are defined at the level of individual guarantee for unfunded guarantees (usually personal guarantees) or, for collateral, for each asset or financial instrument.

To mitigate the counterparty risk associated with OTC (i.e., unregulated) derivatives and SFTs (securities financing transactions, i.e. securities lending and repurchase agreements), the Group uses bilateral netting agreements that allow for credit and debt positions to be netted against one another if a counterparty defaults.
This is achieved by entering into ISDA and ISMA/PSA agreements, which also reduce the absorption of regulatory capital in accordance with supervisory provisions.
The Group also establishes collateral agreements, typically calling for daily margins, to cover transactions in OTC derivatives and SFTs (respectively the Credit Support Annex and Global Market Repurchase Agreement).
With regard to substitution risk, to mitigate risk exposure to specific counterparties, the Bank acquires protection through single name Credit Default Swaps. Furthermore, the Bank also purchases single name CDS or CDS on indexes to mitigate the risk of adjustment of the valuation of the credit or CVA.

A project was started for International Subsidiary Banks with the aim of guaranteeing a consistent approach at Group level to the use of the credit risk mitigation techniques. In further detail, the gap analysis of seven International Subsidiary Banks was completed for the main types of guarantees. For five of these, an action plan was drawn up and is now being implemented.

In 2016 the Parent Company continued its activities relating to the "GARC" (Active Credit Risk Management) project, involving a platform for monitoring credit risk in performing portfolios. The initiative involved the systematic acquisition of guarantees (both personal guarantees and collateral) to support lending of SMEs, a segment which, as a result of the crisis, was hit by significant difficulties in access to credit.
A tranched cover synthetic securitisation was initiated during the year – also under the "GARC" Project – on a newly-issued portfolio promoted by the Piedmont Regional Authority under the 2007/2013 Regional Operational Programme of the European Regional Development Fund, Objective "Regional competitiveness and employment" – Axis 1 – Activity I.4.1 Measure to support access to credit for piedmontese SMEs through the establishment of the Tranched Cover Piemonte Fund.

Both these types of transactions provide synthetic hedging of default risk (past-due, unlikely to pay and bad) of granular portfolios and freeing up of economic and regulatory capital, as envisaged by the current Supervisory Regulations on the matter (EU Regulation 575/2013 and Bank of Italy Circular 285/2013).
For details of the transactions carried out in 2016 under the GARC Project, see the description provided in paragraph C. Securitisations of this chapter.

Performing loans
Collective measurement is compulsory for all loans for which there is no objective evidence of impairment. Such loans must be measured collectively in homogeneous portfolios, i.e. with similar characteristics in terms of credit risk.
The concept of "loss" to which to refer when measuring impairment is that of incurred loss, as opposed to expected or future losses. In the case of collective measurement, this means that reference should be made to the losses already included in the portfolio, although these cannot be identified with reference to specific loans, also defined as "incurred but not reported losses".
In any event, as soon as new information allows the loss to be assessed at the individual level, the financial asset must be excluded from collective measurement and subject to individual measurement.
Although international accounting standards do not explicitly refer to the methods developed in the context of supervisory regulations, the definition of the elements to which to refer when classifying loans into groups to be subject to collective measurement has many points of contact with the Basel 3 regulations and the possible synergies are therefore evident. Through exploitation of such synergies, a measurement model has been structured involving the use of risk parameters (Probability of Default and Loss Given Default) essentially similar to those of Basel 3.
Therefore, in accordance with regulatory provisions, the method calls for expected loss (EL) to be determined according to the risk parameters estimated for the AIRB models under banking supervision regulations.
Expected loss calculated for the purposes of the collective loan measurement procedure differs from that calculated for reporting purposes inasmuch as the LGD used in incurred loss does not (in accordance with international accounting standards) include indirect recovery costs and calibration on the negative phase of the cycle ("LGD downturn").
For loans to customers only, the expected loss (EL) is transformed into incurred loss (IL) by applying factors that capture the loss confirmation period (LCP) and economic cycle of the portfolio:
– the LCP is a factor that represents the time interval between the event that gives rise to the default and the occurrence of the sign of default, which allows the loss to be transformed from expected to incurred;
– the cyclical coefficient is an annually updated coefficient estimated on the basis of the economic cycle, made necessary by the fact that ratings, which are calibrated according to the long-term expected average level throughout the economic cycle, only partially reflect current conditions. This coefficient, which is determined by regulatory segment according to the methods described in the Group Accounting rules, is equal to the ratio between the default rates, estimated for the following 12 months (according to the available forecast and the methods set out in the ICAAP), and the current probabilities of default.

The cyclical coefficients were reviewed for the collective valuation of performing loans for the 2016 Financial Statements and were examined and approved by the Chief Risk Officer. The Loss Confirmation Period factors, on the other hand, remained unchanged.

The illustrated measurement method has also been extended to guarantees and commitments. In the case of the latter, the unused margins on revocable lines of credit are not included in the basis of calculation.
The method and assumptions used are subject to periodic revision.
The internal rating and LGD models are subject to internal validation process by the Internal Validation Service and a level three control by the Internal Auditing Department. The control functions produce a report for the Supervisory Authority on the compliance of the models with the supervisory regulations, which also verifies deviations of the ex-ante estimates and the effective ex post values. This report, approved by the Board of Directors of Intesa Sanpaolo, confirms the existence of the compliance requirements.

Non-performing financial assets

Non-performing financial assets include those loans which, due to events that occur after their granting, show objective evidence of possible impairment.

On 9 January 2015, on the proposal of the European Banking Authority (EBA), the European Commission approved the "final" version of the "Final Draft Implementing Technical Standards on Supervisory reporting on forbearance and non-performing exposures under article 99(4) of Regulation (EU) No. 575/2013".

Following this decision, the Bank of Italy issued an update to its corpus of regulations that, in line with the previous representation of the risk statuses of non-performing loans, fully reflects the new Community regulations with effect from 1 January 2015.

Based on the regulatory framework, supplemented by internal implementing rules, non-performing financial assets are classified into three categories, based on their level of severity: "bad loans", "unlikely to pay" and "non-performing past due exposures".

The type "exposures subject to concessions - forbearance" has also been established. These are exposures subject to renegotiation and/or refinancing due to financial difficulties (evident or in the process of becoming evident) of the debtor, which effectively constitute a subgroup of both non-performing exposures (non-performing exposures with forbearance measures) and performing exposures (other forborne exposures).

Non-performing exposures with forbearance measures do not represent a separate category of non-performing assets, rather, they are an attribute of the above categories of non-performing assets.

The process of managing such exposures, in close accordance with regulatory provisions concerning classification times and methods, is assisted by an IT tool that ensures pre-established, autonomous and independent management procedures.

Non-performing assets undergo an individual measurement process, or the calculation of the expected loss for homogeneous categories (identified as a function of the risk status, duration of default and significance of the exposure) and analytical allocation to each position, and the amount of the adjustment of each loan is the difference between its carrying value at the time of measurement (amortised cost) and the present value of expected future cash flows, discounted using the original effective interest rate.

This measurement is performed upon classification of the assets at the occurrence of significant events and, in any event, is periodically revised in accordance with the criteria and methods illustrated in Part A.2 – Accounting Policies, Main financial statement captions, Loans, to which specific reference should be made.

With reference to past due loans and unlikely to pay loans, the structures responsible for their management are identified, on the basis of pre-determined thresholds of increasing significance, directly at the operating points that handle the accounts, or within peripheral organisational units that perform specialist activities and within the Head Office units, which are responsible for the overall management and coordination of these matters.

On the subject of bad loans, in the first half of 2015 the Group adopted a new organisational model according to which almost all (in terms of total exposure) new bad loan flows are to be managed by the Group's Loan Recovery Department. In particular, this model calls for:

– the assignment to the Loan Recovery Department of coordination of all loan recovery activities and direct management (for Intesa Sanpaolo and all banks in the Banca dei Territori Division) of all positions that it manages and customers classified to the bad loan category from May 2015 (with the exception of a portion of loans with individual exposures below a given threshold, collectively representing an insignificant percentage in terms of exposure with respect to total bad loans, which are assigned for management to new external servicers under a specific agreement and with pre-defined limits);
– the suspension (with limited exceptions) from May 2015 of assignment to Italfondiario S.p.A. of new bad loan flows, without prejudice to its management of the bad positions assigned to it until 30 April 2015;
– for bad positions of limited amounts, routine factoring without recourse to third-party companies on a monthly basis when they are classified as bad loans, with some specific exceptions.

The Loan Recovery Department relies on its own specialist units throughout the country to manage recovery activity for loans entrusted directly to it. As part of these activities, in order to identify the optimal strategies to be implemented for each position, judicial and non-judicial solutions have been examined in terms of costs and benefits, also considering the financial impact of the estimated recovery times.

The assessment of the loans is reviewed whenever events capable of significantly changing recovery prospects become known to the Bank. In order to identify such events rapidly, the information set relative to borrowers is periodically monitored and the development of out-of-court agreements and the various phases of the judicial procedures under way are constantly monitored.

The activity of Italfondiario S.p.A. and the new external servicers in managing the loans entrusted to them under management mandate was monitored by the responsible internal units of the Group. In particular, it should be noted that the individual measurement of loans has been conducted using similar procedures to those established for the internal management of positions, and the other management activities are subject to the guidelines similar to those established for the internally managed positions.

The classification of positions within non-performing financial assets is undertaken on proposal of both central and local territorial structure owners of the commercial relation or of specialised central and local territorial structures in charge of loan monitoring and recovery. Classification involves the use of automatic mechanisms when given objective default thresholds are exceeded. This occurs in cases of past-due loans, which are identified at the Group level, and performing positions with other forborne exposures, if such exposures become relevant for the purposes of regulatory provisions concerning reallocation to the non-performing category.

Automatic mechanisms detect any mismatches, thereby ensuring that material non-performing loans to counterparties shared between the Group's various intermediaries are subject to the required uniform convergence of management aims. Significance is represented by exceeding a pre-established warning threshold for loans classified as at the greatest risk, with respect to the overall exposure.

Automatic mechanisms within the system also ensure that positions are allocated to the risk status most representative of their creditworthiness (bad loans excluded) as significant default continues.

The return to performing status of non-performing exposures is governed by the Supervisory Authority and specific internal regulations, and takes place on the proposal of the Structures responsible for their management, upon verification that the critical conditions or state of default no longer exist.
Exposures classified amongst "past-due loans" automatically become performing when payment is received. The same mechanism is applied to exposures of moderate amounts previously classified as unlikely to pay when automatic mechanisms detect that the conditions that triggered reclassification no longer apply.
Non-performing loans are constantly monitored and controlled, also through II level sample controls on single positions, by the Internal Validation and Controls Head Office Department of the Chief Risk Officer Governance Area.

QUANTITATIVE INFORMATION

A. CREDIT QUALITY

For the purposes of quantitative information about credit quality, the term "credit exposures" is understood to exclude equities and units of UCI, whereas "exposures" includes these items. The only exception is table A.2.1 related to credit exposures by external rating classes, which includes units of UCI.

A.1. Performing and non-performing credit exposures: amounts, adjustments, changes, economic and geographical breakdown

The data shown in the following tables (A.1.1, A.1.2 and in the subsequent one referring to performing positions by past-due bracket), refer to all companies within the scope of consolidation for accounting purposes. In the tables A.1.1 and A.1.2, figures for the banking group are stated net of all intragroup dealings, including those with other companies within the scope of consolidation.

A.1.1. Breakdown of credit exposures by portfolio classification and credit quality (book values)

(millions of euro)

Portfolios/quality	Bad loans	Unlikely to pay	Non performing past due exposures	Performing past due exposures	Other performing exposures	TOTAL
1. Financial assets available for sale	1	-	-	-	131,592	131,593
2. Investments held to maturity	-	-	-	-	1,241	1,241
3. Due from banks	-	-	-	-	53,146	53,146
4. Loans to customers	14,895	14,438	435	6,922	328,023	364,713
5. Financial assets designated at fair value through profit and loss	-	-	-	-	5,005	5,005
6. Financial assets under disposal	-	-	-	-	4	4
Total 31.12.2016	**14,896**	**14,438**	**435**	**6,922**	**519,011**	**555,702**
Total 31.12.2015	**14,974**	**17,094**	**1,022**	**8,656**	**466,983**	**508,729**

With respect to non-performing assets in the portfolio "Loans to customers", forborne exposures amounted to 1,089 million euro amongst bad loans, 7,053 million euro amongst unlikely to pay loans and 62 million euro amongst non-performing past due exposures.
The forborne exposures included among performing assets in the portfolio "Loans to customers" amounted to 7,924 million euro.

A.1.2. Breakdown of credit exposures by portfolio classification and credit quality (gross and net values)

(millions of euro)

Portfolio / quality	NON-PERFORMING ASSETS			PERFORMING ASSETS			TOTAL (net exposure)
	Gross exposure	Individual adjustments	Net exposure	Gross exposure	Collective adjustments	Net exposure	
A. Banking group							
1. Financial assets available for sale	33	-32	1	131,592	-	131,592	131,593
2. Investments held to maturity	-	-	-	1,241	-	1,241	1,241
3. Due from banks	6	-6	-	53,207	-61	53,146	53,146
4. Loans to customers	58,137	-28,369	29,768	336,582	-1,637	334,945	364,713
5. Financial assets designated at fair value through profit and loss	-	-	-	X	X	5,005	5,005
6. Financial assets under disposal	-	-	-	4	-	4	4
Total 31.12.2016	**58,176**	**-28,407**	**29,769**	**522,626**	**-1,698**	**525,933**	**555,702**
Total 31.12.2015	**63,162**	**-30,072**	**33,090**	**472,268**	**-2,117**	**475,639**	**508,729**

Portfolio / Quality	ASSETS OF EVIDENTLY LOW CREDIT QUALITY		OTHER ASSETS
	Cumulated capital losses	Net exposure	Net exposure
1. Financial assets held for trading	**87**	**350**	**41,544**
2. Hedging derivatives	**-**	**-**	**6,234**
Total 31.12.2016	**87**	**350**	**47,778**
Total 31.12.2015	**73**	**218**	**55,483**

The amount of partial derecognition of non-performing loans came to 5,940 million euro as at 31 December 2016.

Performing financial assets may be broken down by portfolio and past due bracket as follows:

(millions of euro)

Credit exposures	Past due up to 3 months	Past due from 3 months up to 6 months	Past due from over 6 months up to 1 year	Past due by over 1 year	Total
1. Financial assets available for sale	-	-	-	-	-
2. Investments held to maturity	-	-	-	-	-
3. Due from banks	-	-	-	-	-
4. Loans to customers	5,356	484	589	493	6,922
5. Financial assets designated at fair value through profit and loss	-	-	-	-	-
6. Financial assets under disposal	-	-	-	-	-
Total performing exposures (net exposure)	**5,356**	**484**	**589**	**493**	**6,922**

In accordance with regulations, the exposures presented in the foregoing table also include the portion of debt that has not yet come due, amounting to 3,100 million euro for the bracket "up to three months", to 322 million euro for the bracket "between three and six months", to 454 million euro in the bracket "between six months and one year" and to 364 million euro in the bracket "over one year".

During 2016, the Intesa Sanpaolo Group purchased an insignificant amount of non-performing loans. Accordingly, the outstanding amounts as at 31 December 2016 were immaterial.

A.1.3. Banking group - On- and off-balance sheet credit exposures to banks: gross and net values and past-due brackets

(millions of euro)

Type of exposure/value	GROSS EXPOSURE					INDIVIDUAL ADJUSTMENTS	COLLECTIVE ADJUSTMENTS	NET EXPOSURE
	Non-performing assets				Performing assets			
	Up to 3 months	*Between 3 and 6 months*	*Between 6 months and 1 year*	*Over 1 year*				
A. ON-BALANCE SHEET EXPOSURES								
a) Bad loans	**-**	**-**	**-**	**2**	**X**	**-2**	**X**	**-**
Of which: forborne exposures	-	-	-	-	*X*	-	*X*	-
b) Unlikely to pay	**-**	**-**	**-**	**4**	**X**	**-4**	**X**	**-**
Of which: forborne exposures	-	-	-	-	*X*	-	*X*	-
c) Non-performing past due exposures	**-**	**-**	**-**	**-**	**X**	**-**	**X**	**-**
Of which: forborne exposures	-	-	-	-	*X*	-	*X*	-
d) Performing past due exposures	**X**	**X**	**X**	**X**	**-**	**X**	**-**	**-**
Of which: forborne exposures	*X*	*X*	*X*	*X*	-	*X*	-	-
e) Other performing exposures	**X**	**X**	**X**	**X**	**57,034**	**X**	**-61**	**56,973**
Of which: forborne exposures	*X*	*X*	*X*	*X*	-	*X*	-	-
TOTAL A	**-**	**-**	**-**	**6**	**57,034**	**-6**	**-61**	**56,973**
B. OFF-BALANCE SHEET EXPOSURES								
a) Non-performing	**-**	**-**	**-**	**-**	**X**	**-**	**X**	**-**
b) Performing	**X**	**X**	**X**	**X**	**50,653**	**X**	**-30**	**50,623**
TOTAL B	**-**	**-**	**-**	**-**	**50,653**	**-**	**-30**	**50,623**
TOTAL (A + B)	**-**	**-**	**-**	**6**	**107,687**	**-6**	**-91**	**107,596**

On-balance sheet exposures include all on-balance sheet financial assets claimed from banks, irrespective of their portfolio of allocation: trading, available for sale, held to maturity, loans and receivables, assets designated at fair value through profit and loss or assets under disposal.

Off-balance sheet exposures include all financial activities that are not on the balance sheet (guarantees given, commitments, derivatives, etc.) but entail the assumption of credit risk, regardless of the purpose of such activities (trading, hedging, etc.). Off-balance sheet exposures also include counterparty risk associated with securities lending operations, repurchase agreements and lending transactions with margins within the notion of SFTs (Securities Financing Transactions) defined in prudential regulations.

A.1.4. Banking group – On-balance sheet credit exposures to banks: changes in gross non-performing exposures

(millions of euro)

Reason/Categories	Bad loans	Unlikely to pay	Non performing past due exposures
A. Initial gross exposure	**6**	**9**	**-**
- of which exposures sold not derecognised	-	-	-
B. Increases	**-**	**-**	**-**
B.1 inflows from performing exposures	-	-	-
B.2 transfers from other non-performing exposure categories	-	-	-
B.3 other increases	-	-	-
B.4 business combinations	-	-	-
C. Decreases	**-4**	**-5**	**-**
C.1 outflows to performing exposures	-	-	-
C.2 write-offs	-4	-	-
C.3 repayments	-	-5	-
C.4 credit disposals	-	-	-
C.5 losses from disposals	-	-	-
C.6 transfers to other non-performing exposure categories	-	-	-
C.7 other decreases	-	-	-
C.8 business combinations	-	-	-
D. Final gross exposure	**2**	**4**	**-**
- of which exposures sold not derecognised	-	-	-

A.1.4bis Banking group - On-balance sheet credit exposures to banks: changes in gross forborne exposures broken down by credit quality

(millions of euro)

Reason/Categories	Forborne exposures: non-performing	Forborne exposures: performing
A. Initial gross exposure	**7**	**2**
- of which exposures sold not derecognised	**-**	**-**
B. Increases	**2**	**-**
B.1 inflows from non-forborne performing exposures	**-**	**-**
B.2 inflows from forborne performing exposures	**-**	X
B.3 inflows from non-performing forborne exposures	X	**-**
B.4 other increases	**2**	**-**
B.5 business combinations	**-**	**-**
C. Decreases	**-**	**-2**
C.1 outflows towards non-forborne performing exposures	X	**-**
C.2 outflows towards forborne performing exposures	**-**	X
C.3 outflows towards non-performing forborne exposures	X	**-**
C.4 write-offs	**-**	**-**
C.5 collections	**-**	**-**
C.6 gains on disposal	**-**	**-**
C.7 losses on disposal	**-**	**-**
C.8 other decreases	**-**	**-2**
C.9 business combinations	**-**	**-**
D. Final gross exposure	**9**	**-**
- of which exposures sold not derecognised	**-**	**-**

A.1.5. Banking group – On-balance sheet non-performing credit exposures to banks: changes in total adjustments

(millions of euro)

Reason/Categories	Bad loans	Of which: forborne exposures	Unlikely to pay	Of which: forborne exposures	Non performing past due exposures	Of which: forborne exposures
A. Initial total adjustments	**6**	**-**	**6**	**-**	**-**	**-**
- of which exposures sold not derecognised	-	-	-	-	-	-
B. Increases	**-**	**-**	**-**	**-**	**-**	**-**
B.1 impairment losses	-	-	-	-	-	-
B.2 losses on disposal	-	-	-	-	-	-
B.3 transfers from other non-performing exposure categories	-	-	-	-	-	-
B.4 other increases	-	-	-	-	-	-
B.5 business combinations	-	-	-	-	-	-
C. Decreases	**-4**	**-**	**-2**	**-**	**-**	**-**
C.1 recoveries on impairment losses	-	-	-2	-	-	-
C.2 recoveries on repayments	-	-	-	-	-	-
C.3 profits on disposal	-	-	-	-	-	-
C.4 write-offs	-4	-	-	-	-	-
C.5 transfers to other non-performing exposure categories	-	-	-	-	-	-
C.6 other decreases	-	-	-	-	-	-
C.7 business combinations	-	-	-	-	-	-
D. Final total adjustments	**2**	**-**	**4**	**-**	**-**	**-**
- of which exposures sold not derecognised	-	-	-	-	-	-

A.1.6 Banking group - On- and off-balance sheet credit exposures to customers: gross and net values and past-due brackets

(millions of euro)

Type of exposure/value	GROSS EXPOSURE Non-performing assets: *Up to 3 months*	*Between 3 and 6 months*	*Between 6 months and 1 year*	*Over 1 year*	Performing assets	INDIVIDUAL ADJUSTMENTS	COLLECTIVE ADJUSTMENTS	NET EXPOSURE
A. ON-BALANCE SHEET EXPOSURES								
a) Bad loans	**355**	**59**	**160**	**37,293**	**X**	**-22,970**	**X**	**14,897**
Of which: forborne exposures	*135*	*19*	*29*	*2,215*	*X*	*-1,309*	*X*	*1,089*
b) Unlikely to pay	**8,857**	**554**	**1,612**	**8,963**	**X**	**-5,334**	**X**	**14,652**
Of which: forborne exposures	*5,765*	*312*	*700*	*2,707*	*X*	*-2,227*	*X*	*7,257*
c) Non-performing past due exposures	**106**	**145**	**240**	**63**	**X**	**-120**	**X**	**434**
Of which: forborne exposures	*29*	*7*	*34*	*4*	*X*	*-11*	*X*	*63*
d) Performing past due exposures	**X**	**X**	**X**	**X**	**7,077**	**X**	**-155**	**6,922**
Of which: forborne exposures	*X*	*X*	*X*	*X*	*396*	*X*	*-12*	*384*
e) Other performing exposures	**X**	**X**	**X**	**X**	**404,341**	**X**	**-1,458**	**402,883**
Of which: forborne exposures	*X*	*X*	*X*	*X*	*7,739*	*X*	*-173*	*7,566*
TOTAL A	**9,318**	**758**	**2,012**	**46,319**	**411,418**	**-28,424**	**-1,613**	**439,788**
B. OFF-BALANCE SHEET EXPOSURES								
a) Non-performing	**1,216**	**-**	**-**	**-**	**X**	**-165**	**X**	**1,051**
b) Other	**X**	**X**	**X**	**X**	**141,346**	**X**	**-153**	**141,193**
TOTAL B	**1,216**	**-**	**-**	**-**	**141,346**	**-165**	**-153**	**142,244**
TOTAL (A + B)	**10,534**	**758**	**2,012**	**46,319**	**552,764**	**-28,589**	**-1,766**	**582,032**

On-balance sheet exposures include all on-balance sheet financial assets claimed from customers, irrespective of their portfolio of allocation: trading, available for sale, held to maturity, loans and receivables, assets designated at fair value through profit and loss or assets under disposal.

Off-balance sheet exposures include all financial activities that are not on the balance sheet (guarantees given, commitments, derivatives, etc.) but entail the assumption of credit risk, regardless of the purpose of such activities (trading, hedging, etc.). Off-balance sheet exposures also include counterparty risk associated with securities lending operations, repurchase agreements and lending transactions with margins within the notion of SFTs (Securities Financing Transactions) defined in prudential regulations.

Net performing on-balance sheet exposures to customers include 6,413 million euro in dealings between the banking group and other companies within the scope of consolidation.

Net on-balance sheet exposures to customers classified as "unlikely to pay" include 214 million euro, adjusted for 24 million euro, in dealings between the banking group and other companies within the scope of consolidation.

In the net performing off-balance sheet exposures the amount of the transactions between the Banking Group and the other companies in the scope of consolidation is 3,136 million euro.

Non-performing exposures with forbearance measures in the past-due bracket by "up to three months" include 4,585 million euro that do not present past-due amounts during the "cure period".

A.1.7 Banking group – On-balance sheet credit exposures to customers: changes in gross non-performing exposures

(millions of euro)

Reason/Categories	Bad loans	Unlikely to pay	Non performing past due exposures
A. Initial gross exposure	**39,183**	**22,959**	**1,238**
- of which exposures sold not derecognised	*23*	*144*	*3*
B. Increases	**6,603**	**7,491**	**2,600**
B.1 inflows from performing exposures	175	3,018	2,367
B.2 transfers from other non-performing exposure categories	4,799	2,442	100
B.3 other increases	1,629	2,031	133
B.4 business combinations	-	-	-
C. Decreases	**-7,919**	**-10,464**	**-3,284**
C.1 outflows to performing exposures	-122	-1,802	-670
C.2 write-offs	-4,830	-492	-3
C.3 repayments	-1,554	-2,612	-185
C.4 credit disposals	-257	-51	-4
C.5 losses from disposals	-114	-16	-1
C.6 transfers to other non-performing exposure categories	-228	-4,759	-2,354
C.7 other decreases	-814	-732	-67
C.8 business combinations	-	-	-
D. Final gross exposure	**37,867**	**19,986**	**554**
- of which exposures sold not derecognised	-	-	-

The “other increases” mainly include the application of penalty interest, increases in balances for charges, collections of loans derecognised in full (through “Repayments”) and the revaluation of positions in foreign currency following the change in the exchange rate.
The "other decreases" mainly refer to the decrease in the balances in foreign currency due to changes in the exchange rate and the collection of penalty interest assessed in previous years.

A.1.7bis Banking group - On-balance sheet credit exposures to customers: changes in gross forborne exposures broken down by credit quality

(millions of euro)

Reason/Categories	Forborne exposures: non-performing	Forborne exposures: performing
A. Initial gross exposure	**11,090**	**8,083**
- of which exposures sold not derecognised	-	-
B. Increases	**4,339**	**5,355**
B.1 inflows from non-forborne performing exposures	251	3,179
B.2 inflows from forborne performing exposures	913	X
B.3 inflows from non-performing forborne exposures	X	894
B.4 other increases	3,175	1,282
B.5 business combinations	-	-
C. Decreases	**-3,473**	**-5,303**
C.1 outflows towards non-forborne performing exposures	X	-2,197
C.2 outflows towards forborne performing exposures	-905	X
C.3 outflows towards non-performing forborne exposures	X	-981
C.4 write-offs	-307	-96
C.5 collections	-1,264	-1,259
C.6 gains on disposal	-43	-2
C.7 losses on disposal	-34	-
C.8 other decreases	-920	-768
C.9 business combinations	-	-
D. Final gross exposure	**11,956**	**8,135**
- of which exposures sold not derecognised	-	-

For the non-performing forborne exposures, the “Other increases” mainly include the transfers from non-forborne exposures to forborne exposures, within each risk status.

A.1.8. Banking group – On-balance sheet credit exposures to customers: changes in total adjustments

(millions of euro)

Reason/Categories	Bad loans		Unlikely to pay		Non performing past due exposures	
		Of which: forborne exposures		*Of which: forborne exposures*		*Of which: forborne exposures*
A. Initial total adjustments	**24,209**	**944**	**5,658**	**2,208**	**216**	**21**
- of which exposures sold not derecognised	*8*	-	*22*	-	-	-
B. Increases	**5,779**	**762**	**2,969**	**1,061**	**418**	**54**
B.1 impairment losses	3,197	359	2,150	729	323	42
B.2. losses on disposal	114	10	16	5	1	-
B.3 transfers from other non-performing exposure categories	1,582	252	487	87	33	2
B.4 other increases	886	141	316	240	61	10
B.5 business combinations	-	-	-	-	-	-
C. Decreases	**-7,018**	**-397**	**-3,293**	**-1,042**	**-514**	**-64**
C.1 recoveries on impairment losses	-1,044	-77	-822	-431	-53	-2
C.2 recoveries on repayments	-226	-19	-148	-64	-2	-
C.3 profits on disposal	-83	-9	-14	-10	-	-
C.4 write-offs	-4,830	-88	-492	-167	-3	-
C.5 transfers to other non-performing exposure categories	-107	-30	-1,573	-249	-423	-61
C.6 other decreases	-728	-174	-244	-121	-33	-1
C.7 business combinations	-	-	-	-	-	-
D. Final total adjustments	**22,970**	**1,309**	**5,334**	**2,227**	**120**	**11**
- of which exposures sold not derecognised	-	-	-	-	-	-

The “other increases” mainly include the application of penalty interest, collections of loans derecognised in full (through “recoveries on repayments”) and increases in balances of funds in foreign currency following the change in the exchange rate.
The sub-caption “Other increases” under “of which forborne exposures” includes the transfers from non-forborne positions to forborne positions, within each risk status.
The "other decreases" consist mainly of collection of overdue interest applied in previous years, losses on disposal not covered by the allowance and the decrease in the balances of funds in foreign currency due to changes in the exchange rate.

Conversion of loans into equity instruments

During the year, loans were converted into equity instruments as part of restructuring agreements for non-performing positions. Gross loans converted into equity instruments, shares and units of mutual funds amounted to 100 million euro. The adjustments directly attributable to the conversion process amounted to 91 million euro, partly made during previous years and partly during the current year. Equity instruments were recognised at their fair value of 9 million euro at the execution date among assets available for sale.

A.2. Classification of exposures based on external and internal ratings

A.2.1. Banking group - Breakdown of on- and off-balance sheet credit exposures by external rating classes

The Intesa Sanpaolo Group uses the ratings supplied by the following external rating agencies for the portfolios subject to reporting: Standard & Poor’s Ratings Services, Moody’s Investors Service, Fitch Ratings and DBRS Ratings.
These agencies are valid for all Group banks. In compliance with the regulations, if there are two ratings for the same customer, the most prudential of the two is used, when three ratings are available, the middle rating is adopted, and when all ratings are available, the second-best is taken.
The Class 6 rating column includes non-performing loans.

(millions of euro)

Exposures	EXTERNAL RATING CLASSES						UNRATED	TOTAL
	Class 1	Class 2	Class 3	Class 4	Class 5	Class 6		
A. On-balance sheet exposures	**31,639**	**24,162**	**120,111**	**13,984**	**4,412**	**30,213**	**274,321**	**498,842**
B. Derivatives	**1,392**	**1,582**	**5,561**	**529**	**162**	**18**	**3,657**	**12,901**
B.1. Financial derivatives	1,392	1,582	5,561	461	162	18	3,649	12,825
B.2. Credit derivatives	-	-	-	68	-	-	8	76
C. Guarantees given	**943**	**1,350**	**5,026**	**4,383**	**494**	**577**	**26,330**	**39,103**
D. Commitments to lend funds	**11,823**	**24,288**	**51,652**	**4,875**	**1,372**	**806**	**43,808**	**138,624**
E. Other	**105**	**1,293**	**78**	**46**	**1**	**-**	**716**	**2,239**
Total	**45,902**	**52,675**	**182,428**	**23,817**	**6,441**	**31,614**	**348,832**	**691,709**

It should be noted that the exposures presented in the table also include units of UCI for 2,082 million euro.
The following tables show the mapping of risk classes and the external ratings.

Mapping of long-term ratings issued by external rating agencies

Long-term ratings for exposures to: central governments and central banks, supervised issuers, public-sector entities, local authorities, multilateral development banks, enterprises and other parties

	ECAI	
	Moody's	**Fitch Standard & Poor's DBRS**
Credit quality step		
1	from Aaa to Aa3	from AAA to AA-
2	from A1 to A3	from A+ to A-
3	from Baa1 to Baa3	from BBB+ to BBB-
4	from Ba1 to Ba3	from BB+ to BB-
5	from B1 to B3	from B+ to B-
6	Caa1 and lower	CCC+ and lower

Short-term ratings for exposures to supervised issuers and enterprises

	ECAI			
	Moody's	**Fitch**	**Standard & Poor's**	**DBRS**
Credit quality step				
1	P -1	F1 +, F1	A -1 + , A -1	R -1
2	P -2	F2	A -2	R -2
3	P -3	F3	A -3	R -3
from 4 to 6	NP	lower than F3	lower than A -3	R-4 R-5 R-6

Ratings for exposures to UCI

	ECAI		
	Moody's	**Fitch**	**Standard & Poor's**
Credit quality step			
1	from Aaa to Aa3	from AAA to AA-	from AAA m/f to AA - m/f
2	from A1 to A3	from A+ to A-	from A + m/f to A - m/f
3 and 4	from Baa1 to Ba3	from BBB+ to BB-	from BBB + m/f to BB - m/f
5 and 6	B1 and lower	B+ and lower	B + m/f and lower

Standardised approach - Long-term ratings for exposures to securitisations

	ECAI	
	Moody's	**Fitch Standard & Poor's**
Credit quality step		
1	from Aaa to Aa3	from AAA to AA-
2	from A1 to A3	from A+ to A-
3	from Baa1 to Baa3	from BBB+ to BBB-
4	from Baa1 to Ba3	from BB+ to BB-
5	B1 and lower	B+ and lower

Standardised approach - Short-term ratings for exposures to securitisations

	ECAI		
	Moody's	**Fitch**	**Standard & Poor's**
Credit quality step			
1	P -1	F 1 +, F 1	A -1 + , A -1
2	P -2	F2	A -2
3	P -3	F3	A -3
from 4 to 6	NP	lower than F3	lower than A -3

IRB approach - Long-term ratings for exposures to securitisations

	ECAI	
	Moody's	Fitch Standard & Poor's
Credit quality step		
1	Aaa	AAA
2	Aa	AA
3	A1	A+
4	A2	A
5	A3	A-
6	Baa1	BBB+
7	Baa2	BBB
8	Baa3	BBB-
9	Ba1	BB+
10	Ba2	BB
11	Ba3	BB-
12	Ba3 and lower	BB- and lower

IRB approach - Short-term ratings for exposures to securitisations

	ECAI		
	Moody's	Fitch	Standard & Poor's
Credit quality step			
1	P -1	F 1 +, F 1	A -1 + , A -1
2	P -2	F2	A -2
3	P -3	F3	A -3
All other credit quality steps	NP	lower than F3	lower than A -3

A.2.2. Banking group - Breakdown of on- and off-balance sheet exposures by internal rating classes

As indicated above in the paragraph entitled "Basel 3 regulations and the Internal Project" of Qualitative information, the Intesa Sanpaolo Group has a set of ratings that have been validated in respect of the Corporate, Retail Mortgages (residential mortgages for private individuals) and Retail SME portfolios.

The breakdown of exposures by internal rating classes shown in the following table is based on all ratings available in the credit risk management and control system, in addition to ratings for validated models. These ratings include credit ratings assigned by external agencies for counterparties in customer segments for which an internal model is not available.

Unrated exposures account for 10.5% of all exposures to performing counterparties and refer to customer segments for which a rating model is not yet available, to counterparties for which the roll-out of new internal models is still underway, to Group companies whose mission is not related to credit and loans, and to international subsidiaries, which have yet to be fully integrated into the credit risk management system.

For the purposes of calculating the risk indicators, unrated counterparties are assigned an estimated rating on the basis of the average probabilities of default, deriving from the past experience of the respective sectors.

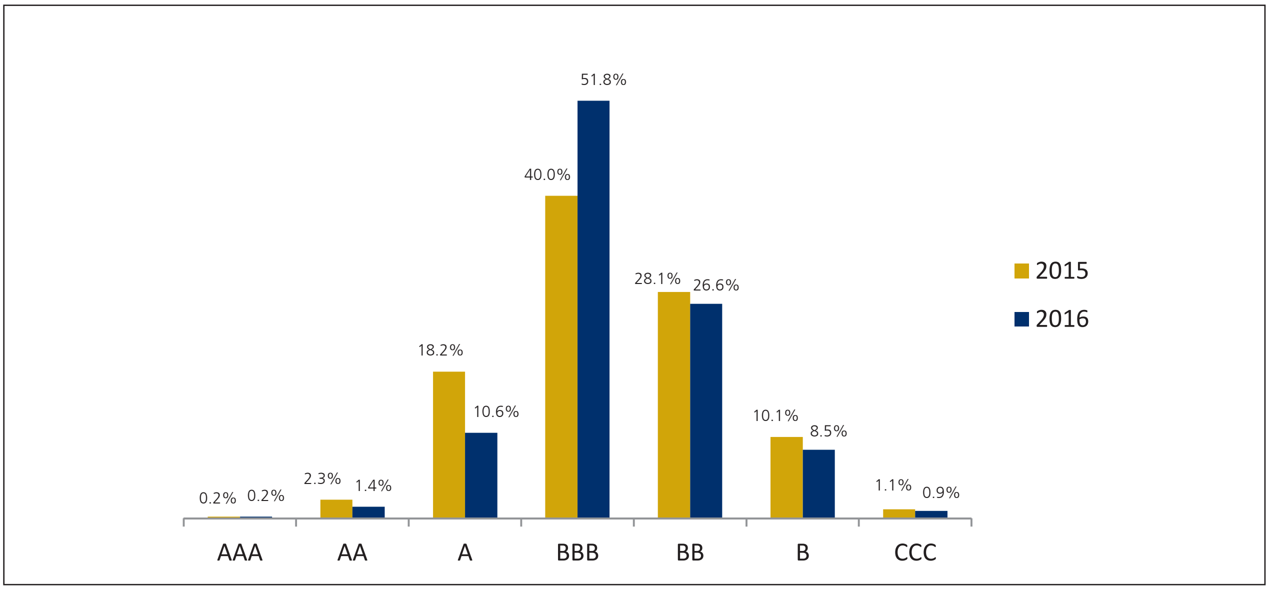
When unrated counterparties and non-performing loans are excluded, there is a high concentration of investment grade classes (classes 1, 2 and 3, representing ratings between AAA and BBB-) at 74.4% of the total, whilst 19.1% fall within the BB+/BB- range (class 4) and 6.5% fall under higher risk classes (of which around 0.8% are below B-).

(millions of euro)

Exposures	INTERNAL RATING CLASSES							UNRATED	TOTAL
	Class 1	Class 2	Class 3	Class 4	Class 5	Class 6	Non-performing exposures		
A. On-balance sheet exposures	**34,621**	**49,894**	**222,664**	**81,932**	**28,194**	**2,650**	**29,983**	**46,823**	**496,761**
B. Derivatives	**1,671**	**1,665**	**6,265**	**1,583**	**480**	**67**	**-**	**1,170**	**12,901**
B.1. Financial derivatives	1,671	1,665	6,265	1,515	480	67	-	1,162	12,825
B.2. Credit derivatives	-	-	-	68	-	-	-	8	76
C. Guarantees given	**3,093**	**5,630**	**15,914**	**9,715**	**1,832**	**135**	**555**	**2,229**	**39,103**
D. Commitments to lend funds	**11,760**	**26,431**	**57,946**	**18,785**	**3,182**	**1,646**	**496**	**18,378**	**138,624**
E. Other	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**2,239**	**2,239**
Total	**51,145**	**83,620**	**302,789**	**112,015**	**33,688**	**4,498**	**31,034**	**70,839**	**689,628**

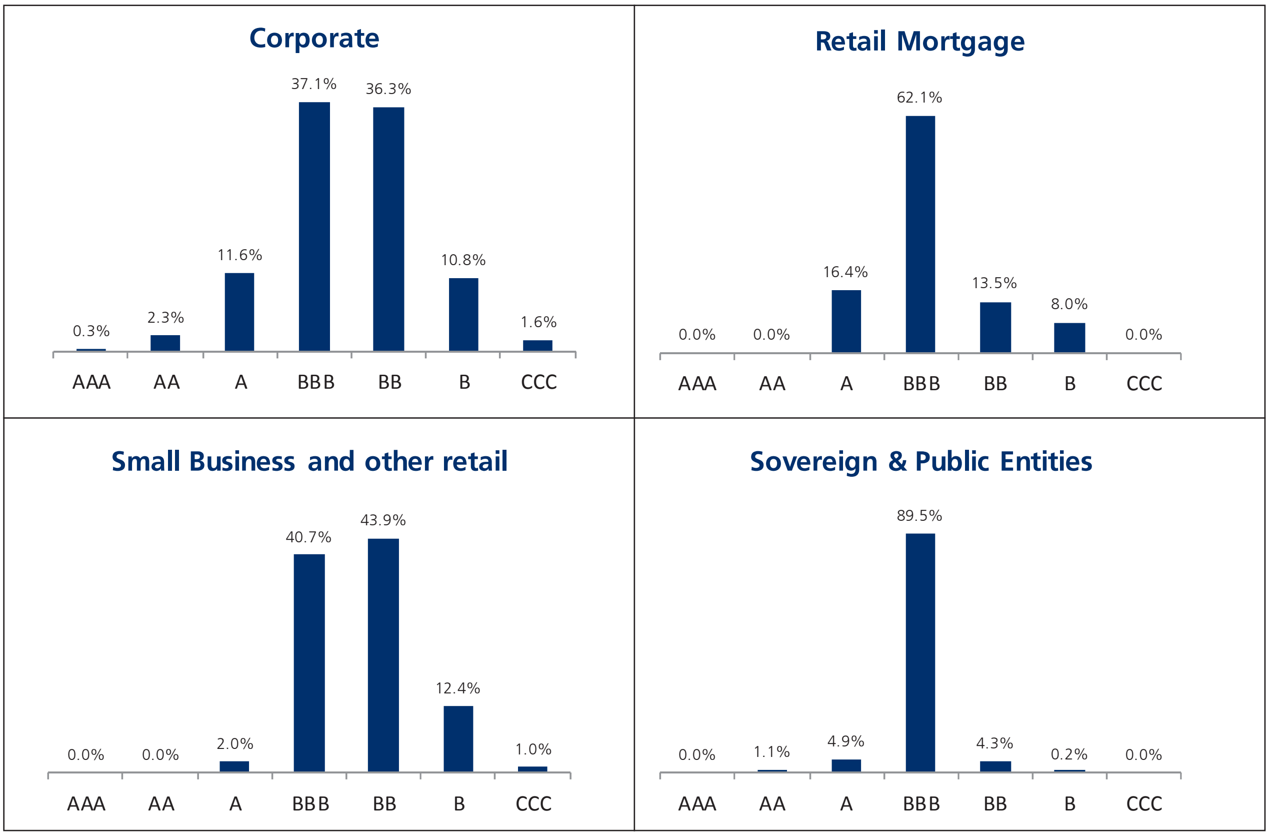
In addition to the tables required by the financial reporting regulations, the rating allocation for performing credit exposures to customers attributable to banks with internal models is shown below.

As at 31 December 2016, performing loans to customers assigned an individual rating internally or by an external agency accounted for 96% of the loans of banks with internal models and for 87% of the entire aggregate at the Group level.



The allocation shows a high level of investment grade exposures of 64.0%, up compared to the previous year (60.7%).

The breakdown of the following portfolios by rating is presented below: Corporate, Retail Mortgage (residential mortgages for individuals), Retail SME and other retail, Sovereign & Public Sector Entities.



Investment grade positions account for 51.4%, 78.6%, 42.7% and 95.4% of the above portfolios, respectively.

A.3. Breakdown of guaranteed credit exposures by type of guarantee

A.3.1. Banking group - Guaranteed credit exposures to banks

(millions of euro)

	GUARANTEED ON-BALANCE SHEET CREDIT EXPOSURES				GUARANTEED OFF-BALANCE SHEET CREDIT EXPOSURES				TOTAL
	Totally guaranteed		Partly guaranteed		Totally guaranteed		Partly guaranteed		
		of which non-performing		*of which non-performing*		*of which non-performing*		*of which non-performing*	
NET EXPOSURE	**4,209**	**-**	**142**	**-**	**8,902**	**-**	**3,220**	**-**	**16,473**
COLLATERAL[(1)]									
Real estate assets	3	-	-	-	-	-	-	-	3
Mortgages	-	-	-	-	-	-	-	-	-
Financial leases	*3*	-	-	-	-	-	-	-	*3*
Securities	3,975	-	-	-	4,045	-	11	-	8,031
Other	-	-	-	-	4,844	-	2,843	-	7,687
GUARANTEES [(1)]									
Credit derivatives									
Credit-linked notes	-	-	-	-	-	-	-	-	-
Other derivatives									
- Governments and Central Banks	-	-	-	-	-	-	-	-	-
- Other public entities	-	-	-	-	-	-	-	-	-
- Banks	-	-	-	-	-	-	-	-	-
- Other counterparties	-	-	-	-	-	-	-	-	-
Guarantees given									
Governments and Central Banks	*52*	-	*31*	-	-	-	-	-	*83*
Other public entities	-	-	-	-	-	-	-	-	-
Banks	*120*	-	*61*	-	*12*	-	-	-	*193*
Other counterparties	*56*	-	*9*	-	-	-	-	-	*65*
TOTAL	**4,206**	**-**	**101**	**-**	**8,901**	**-**	**2,854**	**-**	**16,062**

(1) Fair Value of the collateral/guarantee or, if difficult to calculate, contractual value, the latter stated - as required by the regulations - up to the net exposure value.

A.3.2. Banking group - Guaranteed credit exposures to customers

(millions of euro)

	GUARANTEED ON-BALANCE SHEET CREDIT EXPOSURES				GUARANTEED OFF-BALANCE SHEET CREDIT EXPOSURES				TOTAL
	Totally guaranteed		Partly guaranteed		Totally guaranteed		Partly guaranteed		
		of which non-performing		*of which non-performing*		*of which non-performing*		*of which non-performing*	
NET EXPOSURE	**204,764**	***21,918***	**17,992**	***1,922***	**19,781**	***503***	**2,971**	***67***	**245,508**
COLLATERAL[(1)]									
Real estate assets	131,115	*17,377*	1,541	*472*	2,595	*271*	192	*8*	135,443
Mortgages	*118,779*	*14,786*	*1,479*	*439*	*2,571*	*270*	*145*	*8*	*122,974*
Financial leases	*12,336*	*2,591*	*62*	*33*	*24*	*1*	*47*	-	*12,469*
Securities	35,596	*277*	2,107	*201*	6,904	*18*	245	*1*	44,852
Other	9,665	*889*	754	*44*	1,286	*7*	314	*13*	12,019
GUARANTEES [(1)]									
Credit derivatives									
Credit-linked notes	-	-	-	-	-	-	-	-	-
Other derivatives									
- Governments and Central Banks	-	-	-	-	-	-	-	-	-
- Other public entities	-	-	-	-	-	-	-	-	-
- Banks	-	-	-	-	-	-	-	-	-
- Other counterparties	-	-	-	-	*140*	-	-	-	*140*
Guarantees given									
Governments and Central Banks	*3,651*	*122*	*1,838*	*40*	*662*	-	*12*	*1*	*6,163*
Other public entities	*259*	*8*	*105*	*6*	-	-	-	-	*364*
Banks	*446*	*35*	*794*	*2*	*109*	*2*	*10*	*3*	*1,359*
Other counterparties	*22,966*	*3,016*	*3,398*	*574*	*7,404*	*82*	*939*	*9*	*34,707*
TOTAL	**203,698**	***21,724***	**10,537**	***1,339***	**19,100**	***380***	**1,712**	***35***	**235,047**

(1) Fair Value of the guarantee or, if difficult to be determined, contractual value, the latter stated - as required by the regulations - up to the net exposure value.

B. BREAKDOWN AND CONCENTRATION OF CREDIT EXPOSURES

B.1. Banking group - Breakdown by sector of on- and off-balance sheet credit exposures to customers (book value)

(millions of euro)

Exposures/Counterparties	GOVERNMENTS			OTHER PUBLIC ENTITIES			FINANCIAL COMPANIES			INSURANCE COMPANIES			NON-FINANCIAL COMPANIES			OTHER ENTITIES		
	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments	Net exposure	Individual adjustments	Portfolio adjustments
A. ON-BALANCE SHEET EXPOSURES																		
A.1. Bad loans	7	-3	X	184	-94	X	167	-340	X	1	-1	X	12,305	-20,097	X	2,233	-2,435	X
- *of which forborne exposures*	1	-	X	-	-	X	16	-46	X	-	-	X	930	-1,081	X	142	-182	X
A.2. Unlikely to pay	1	-1	X	151	-21	X	550	-179	X	-	-	X	12,490	-4,540	X	1,460	-593	X
- *of which forborne exposures*	-	-	X	54	-3	X	435	-110	X	-	-	X	6,191	-1,978	X	577	-136	X
A.3. Non-performing past due exposures	-	-	X	4	-	X	5	-2	X	-	-	X	282	-64	X	143	-54	X
- *of which forborne exposures*	-	-	X	-	-	X	-	-	X	-	-	X	55	-10	X	8	-1	X
A.4. Performing exposures	76,512	X	-8	15,673	X	-31	61,889	X	-147	1,516	X	-	167,792	X	-1,187	86,423	X	-240
- *of which forborne exposures*	24	X	-	152	X	-	663	X	-26	-	X	-	6,077	X	-144	1,034	X	-15
Total A	**76,520**	**-4**	**-8**	**16,012**	**-115**	**-31**	**62,611**	**-521**	**-147**	**1,517**	**-1**	**-**	**192,869**	**-24,701**	**-1,187**	**90,259**	**-3,082**	**-240**
B. OFF-BALANCE SHEET EXPOSURES																		
B.1. Bad loans	-	-	X	-	-	X	2	-	X	-	-	X	162	-71	X	5	-8	X
B.2. Unlikely to pay	-	-	X	-	-	X	6	-1	X	8	-	X	851	-82	X	6	-2	X
B.3. Other non-performing assets	-	-	X	-	-	X	-	-	X	-	-	X	10	-	X	1	-1	X
B.4. Other exposures	17,391	X	-	1,234	X	-	35,898	X	-6	1,093	X	-	80,588	X	-139	4,463	X	-8
Total B	**17,391**	**-**	**-**	**1,234**	**-**	**-**	**35,906**	**-1**	**-6**	**1,101**	**-**	**-**	**81,611**	**-153**	**-139**	**4,475**	**-11**	**-8**
TOTAL (A+B) 31.12.2016	**93,911**	**-4**	**-8**	**17,246**	**-115**	**-31**	**98,517**	**-522**	**-153**	**2,618**	**-1**	**-**	**274,480**	**-24,854**	**-1,326**	**94,734**	**-3,093**	**-248**
TOTAL 31.12.2015	**75,651**	**-4**	**-12**	**18,060**	**-97**	**-32**	**78,589**	**-706**	**-174**	**2,570**	**-**	**-1**	**268,344**	**-26,042**	**-1,668**	**89,097**	**-3,457**	**-312**

B.2. Banking group - Breakdown by geographical area of on- and off-balance sheet credit exposures to customers (book value)

(millions of euro)

Exposures/Geographical areas	ITALY		OTHER EUROPEAN COUNTRIES		AMERICA		ASIA		REST OF THE WORLD	
	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments
A. ON-BALANCE SHEET EXPOSURES										
A.1. Bad loans	14,334	-21,699	556	-1,150	2	-27	1	-6	4	-88
A.2. Unlikely to pay	13,218	-4,619	1,049	-588	183	-65	52	-11	150	-51
A.3. Non-performing past due exposures	375	-92	33	-22	3	-1	19	-5	4	-
A.4. Performing exposures	296,884	-1,123	84,372	-373	19,052	-45	4,599	-19	4,898	-53
Total A	**324,811**	**-27,533**	**86,010**	**-2,133**	**19,240**	**-138**	**4,671**	**-41**	**5,056**	**-192**
B. OFF-BALANCE SHEET EXPOSURES										
B.1. Bad loans	154	-66	13	-8	-	-	-	-	1	-6
B.2. Unlikely to pay	797	-60	52	-23	20	-	-	-	3	-1
B.3. Other non-performing assets	10	-	1	-1	-	-	-	-	-	-
B.4. Performing exposures	63,591	-71	60,365	-61	13,769	-17	1,239	-1	1,703	-3
Total B	**64,552**	**-197**	**60,431**	**-93**	**13,789**	**-17**	**1,239**	**-1**	**1,707**	**-10**
TOTAL (A+B) 31.12.2016	**389,363**	**-27,730**	**146,441**	**-2,226**	**33,029**	**-155**	**5,910**	**-42**	**6,763**	**-202**
TOTAL 31.12.2015	**368,850**	**-29,156**	**119,957**	**-2,884**	**31,639**	**-122**	**4,646**	**-52**	**7,219**	**-290**

B.2 bis Breakdown of relations with customers resident in Italy by geographical area (book value)

(millions of euro)

Exposures/Geographical areas	NORTH-WEST		NORTH-EAST		CENTRE		SOUTH AND ISLANDS	
	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments
A. ON-BALANCE SHEET EXPOSURES								
A.1. Bad loans	4,693	-7,190	3,141	-4,741	3,299	-4,776	3,201	-4,992
A.2. Unlikely to pay	5,239	-1,802	2,394	-744	3,163	-1,076	2,422	-997
A.3. Non-performing past due exposures	106	-22	50	-10	89	-20	130	-40
A.4. Performing exposures	92,063	-472	44,726	-189	120,649	-249	39,446	-213
Total A	**102,101**	**-9,486**	**50,311**	**-5,684**	**127,200**	**-6,121**	**45,199**	**-6,242**
B. OFF-BALANCE SHEET EXPOSURES								
B.1. Bad loans	35	-13	54	-28	58	-22	7	-3
B.2. Unlikely to pay	377	-16	109	-26	242	-15	69	-3
B.3. Other non-performing assets	7	-	1	-	1	-	1	-
B.4. Performing exposures	19,449	-4	5,958	-16	35,880	-45	2,304	-6
Total B	**19,868**	**-33**	**6,122**	**-70**	**36,181**	**-82**	**2,381**	**-12**
TOTAL (A+B) 31.12.2016	**121,969**	**-9,519**	**56,433**	**-5,754**	**163,381**	**-6,203**	**47,580**	**-6,254**
TOTAL 31.12.2015	**122,531**	**-10,161**	**58,162**	**-6,189**	**140,486**	**-6,285**	**47,671**	**-6,521**

B.3 Banking group - Breakdown by geographical area of on- and off-balance sheet credit exposures to banks (book value)

(millions of euro)

Exposures/Geographical areas	ITALY		OTHER EUROPEAN COUNTRIES		AMERICA		ASIA		REST OF THE WORLD	
	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments
A. ON-BALANCE SHEET EXPOSURES										
A.1. Bad loans	-	-	-	-2	-	-	-	-	-	-
A.2. Unlikely to pay	-	-	-	-	-	-	-	-4	-	-
A.3. Non-performing past due exposures	-	-	-	-	-	-	-	-	-	-
A.4. Performing exposures	28,557	-11	21,039	-27	3,595	-15	2,276	-5	1,506	-3
Total A	**28,557**	**-11**	**21,039**	**-29**	**3,595**	**-15**	**2,276**	**-9**	**1,506**	**-3**
B. OFF-BALANCE SHEET EXPOSURES										
B.1. Bad loans	-	-	-	-	-	-	-	-	-	-
B.2. Unlikely to pay	-	-	-	-	-	-	-	-	-	-
B.3. Other non-performing assets	-	-	-	-	-	-	-	-	-	-
B.4. Performing exposures	6,945	-1	36,727	-9	2,715	-2	1,896	-7	634	-11
Total B	**6,945**	**-1**	**36,727**	**-9**	**2,715**	**-2**	**1,896**	**-7**	**634**	**-11**
TOTAL (A+B) 31.12.2016	**35,502**	**-12**	**57,766**	**-38**	**6,310**	**-17**	**4,172**	**-16**	**2,140**	**-14**
TOTAL 31.12.2015	**13,993**	**-7**	**62,942**	**-47**	**10,328**	**-15**	**4,526**	**-24**	**2,525**	**-11**

B.3 Bis Breakdown of relations with banks resident in Italy by geographical area (book value)

(millions of euro)

Exposures/Geographical areas	NORTH-WEST		NORTH-EAST		CENTRE		SOUTH AND ISLANDS	
	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments	Net exposure	Total adjustments
A. ON-BALANCE SHEET EXPOSURES								
A.1. Bad loans	-	-	-	-	-	-	-	-
A.2. Unlikely to pay	-	-	-	-	-	-	-	-
A.3. Non-performing past due exposures	-	-	-	-	-	-	-	-
A.4. Performing exposures	2,064	-3	1,120	-3	25,370	-5	3	-
Total A	**2,064**	**-3**	**1,120**	**-3**	**25,370**	**-5**	**3**	**-**
B. OFF-BALANCE SHEET EXPOSURES								
B.1. Bad loans	-	-	-	-	-	-	-	-
B.2. Unlikely to pay	-	-	-	-	-	-	-	-
B.3. Other non-performing assets	-	-	-	-	-	-	-	-
B.4. Performing exposures	1,199	-1	194	-	5,541	-	11	-
Total B	**1,199**	**-1**	**194**	**-**	**5,541**	**-**	**11**	**-**
TOTAL (A+B) 31.12.2016	**3,263**	**-4**	**1,314**	**-3**	**30,911**	**-5**	**14**	**-**
TOTAL 31.12.2015	**4,653**	**-3**	**1,689**	**-2**	**7,464**	**-1**	**187**	**-1**

B.4 Large exposures

Large exposures	
a) Book value (millions of euro)	132,223
b) Weighted value (millions of euro)	11,652
b) Number	8

Based on regulatory provisions, the number of large exposures presented in the table was determined by the reference to unweighted "exposures" in excess of 10% of eligible capital as defined by EU Regulation 575/2013 (CRR). The "exposures" are defined as the sum of on-balance sheet assets at risk and off-balance sheet transactions (excluding those deducted from eligible capital) with a customer or a group of related customers, without applying weighting factors.
Such presentation criteria result in the inclusion in the financial statement table for large exposures of entities that - even with a weighting of 0% - present an unweighted exposure in excess of 10% of eligible capital for the purposes of large risks.

C. SECURITISATIONS

This section does not include securitisations where the originators are Intesa Sanpaolo Group banks and all the liabilities (e.g. ABS securities, loans at the warehousing stage) issued by the vehicle companies are subscribed at the time of issue by one or more Group companies. For a description of these types of transaction, see the section on liquidity risk in Part E of the Notes to the consolidated financial statements.

Qualitative information

The securitisations carried out in 2016 are summarised below:

GARC Securitisations

In 2016 the Parent Company continued its activities relating to the "GARC" (Active Credit Risk Management) project, involving a platform for monitoring credit risk in performing portfolios. The initiative involved the systematic acquisition of guarantees (both personal guarantees and collateral) to support lending of SMEs, a segment which, as a result of the crisis, was hit by significant difficulties in access to credit. As part of these operations, during the year the junior risk relating to a total portfolio of 3.7 billion euro in loans to approximately 8,200 businesses in the Corporate and SME Corporate segments, valued using internal models (Advanced IRB), was sold to specialist investors through several transactions.

Tranched Cover Piemonte Securitisation

A tranched cover synthetic securitisation was initiated during the year – also under the "GARC" Project – on newly-issued portfolios promoted by the Piedmont Regional Authority under the 2007/2013 Regional Operational Programme funded by the European Regional Development Fund, for the objective "Regional competitiveness and employment" – Axis 1 – Activity I.4.1 Measure to support access to credit for piedmontese SMEs through the establishment of the Tranched Cover Piemonte Fund. The operation provided for the granting of a total portfolio of new loans of 60 million euro to around 350 enterprises in Piedmont.

Towers Securitisation

In 2016, Intesa Sanpaolo completed a securitisation via the sale without recourse of two portfolios of performing consumer loans for around 2.6 billion euro, through Accedo, a wholly-owned consumer credit company dedicated to consumer credit distribution channels outside the Group. The two portfolios – one relating to loans against one-fifth salary assignments and the other to car and special-purpose loans – were sold to two specially created vehicle companies, independent of the Intesa Sanpaolo Group and managed by a third-party servicer, which funded the purchase price by issuing asset-backed securities. The senior and mezzanine securities of the portfolio consisting of loans against one-fifth salary assignments have a Moody's rating of Aa2 and A2 respectively.
The junior tranches were subscribed by the leading investment company Christofferson Robb & Company, whereas the senior and mezzanine tranches were subscribed by a pool of international banks, led by Banca IMI and also made up of Citigroup, Goldman Sachs International and JP Morgan. Accedo subscribed for 5% of each of the tranches issued, in accordance with the CRR Directive.

Automotive, Electronics and Mechanics Securitisation

This securitisation was expanded during 2016, bringing the nominal value of securitised loans from 490 to 535 million euro. For these transactions, the Group used the vehicles Trade Investment Receivable Vehicle S.a.r.l., Hermes Trade Receivables S.a.r.l., Lana Trade Receivables S.a.r.l. and the vehicle Duomo Funding Plc. The securities issued are unrated

K-Equity Securitisation

In 2015, Intesa Sanpaolo and another leading Italian bank jointly carried out a securitisation transaction involving the transfer of their credit exposures to specifically established third-party entities, in order to enable the leveraging of their value through financial and industrial restructuring.
The exposure is accounted for (a) on one hand, by loan portfolios essentially deriving from medium and long-term loans to specific debtors and, (b) on the other, by equity exposures, essentially represented by participating financial instruments (PFI) issued by said debtors. That transfer specifically fulfils the purpose of ensuring the management of said exposures by entities established and managed by specialised third parties to optimise the recovery of the overall exposure by using the know-how and experience of the parties involved in the financial and industrial restructuring processes and, possibly, the granting of new financing to benefit the transferred debtors.
The transaction involves, *inter alia,* the use of a) a securitisation company established pursuant to Law 130/99, Pillarstone Italy SPV S.r.l., which shall purchase and securitise the credit exposures, as well as, where necessary, disburse new financing to the benefit of the assigned debtors and, b) a newly-established company, Pillarstone Italy Holding S.p.A, controlled by third parties, which shall purchase and hold (through assigned assets specifically established pursuant to Article 2447-bis, paragraph 1, letter a) of the Italian Civil Code) the PFIs transferred by the banks, as well as any additional equity exposures subscribed as part of future restructuring operations of transferred debtors.
The Group holds no investments in the abovementioned third-party companies which, therefore, are independent from Intesa Sanpaolo.
Pillarstone Italy SPV shall execute as many securitisations as there are individual assigned debtors, by issuing Senior and Junior notes, fully subscribed by each bank. Therefore, each securitisation already regards the loans due to the assigning banks from a single debtor. Pillarstone Italy Holding's methods of acquiring the equity instruments of the selected debtors may be in cash or through deferred payment, by leveraging the value of the transferred financial instruments.
In 2016, the Group sold around 355 million euro of non-performing exposures to Pillarstone Italy SPV. The exposures sold have not been derecognised either from the financial statements or for prudential purposes. Against said sales, in addition to the notes mentioned above, Super Senior notes subscribed by third parties were also issued. All the securities issued are unrated. The Group

also sold its interest in the capital of a transferred debtor to Pillarstone Italy Holding, and this interest has been derecognised from the financial statements.

Quantitative information

C.1. Banking Group - Breakdown of exposures deriving from the main "originated" securitisations by type of securitised asset and by type of exposure

On-balance sheet

(millions of euro)

Type of securitised asset/ Exposure	ON-BALANCE SHEET EXPOSURES					
	Senior		Mezzanine		Junior	
	Book value	Adjust./ recoveries	Book value	Adjust./ recoveries	Book value	Adjust./ recoveries
A. Fully derecognised	**159**	**-**	**11**	**-**	**32**	**-5**
– Other assets	47	-	7	-	-	-
– Residential mortgage loans (*)	-	-	-	-	17	-5
– Consumer credit	112	-	4	-	15	-
B. Partly derecognised	-	-	-	-	-	-
C. Not derecognised	**4,028**	**-**	**334**	**8**	**130**	**-**
– Trade receivables	2	-	24	-	11	-
– Residential mortgage loans	-	-	33	1	53	-
– Loans to businesses (including SMEs) (**)	4,026	-	277	7	66	-
TOTAL	**4,187**	**-**	**345**	**8**	**162**	**-5**

(*) The amount also refers to non-performing financial assets fo 12 million euro.

(**) The amounts also include non-performing financial assets of 35 million euro for Senior exposures, 277 million euro for Mezzanine exposures and 49 million euro for Junior exposures. The caption "Loans to businesses (including SMEs)" also includes the amounts for the GARC synthetic securitisation transactions relating to the performing exposures.

The securitisations in the above table include those for which the Group availed itself of the exemption from compliance to IAS/IFRS permitted on first-time adoption by IFRS 1. Based on this exemption, assets or liabilities sold and not derecognised, based on previous accounting principles and deriving from securitisations prior to 1 January 2004, have not been recorded in the financial statements, even if derecognition does not meet the requirements of IAS 39.

Off-balance sheet

(millions of euro)

Type of securitised asset/ Exposure	GUARANTEES GIVEN						CREDIT LINES					
	Senior		Mezzanine		Junior		Senior		Mezzanine		Junior	
	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries
A. Fully derecognised	**-**	**-**	**-**	**-**	**-**	**-**	**441**	**-**	**28**	**-**	**-**	**-**
– Consumer credit	-	-	-	-	-	-	441	-	28	-	-	-
B. Partly derecognised	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
C. Not derecognised	**-**	**-**	**-**	**-**	**-**	**-**	**2,037**	**-**	**-**	**-**	**-**	**-**
– Trade receivables (*)	-	-	-	-	-	-	2,037	-	-	-	-	-
TOTAL	**-**	**-**	**-**	**-**	**-**	**-**	**2,478**	**-**	**28**	**-**	**-**	**-**

(*) Amount referring to liquidity lines granted to cover loans which did not meet the criteria for derecognition pursuant to IAS 39

C.2. Banking Group - Breakdown of exposures deriving from the main "third party" securitisations by type of securitised asset and by type of exposure

On-balance sheet

(millions of euro)

Type of securitised asset/ Exposure	ON-BALANCE SHEET EXPOSURES					
	Senior		Mezzanine		Junior	
	Book value	Adjust./ recoveries	Book value	Adjust./ recoveries	Book value	Adjust./ recoveries
Other assets (*)	4,925	-	6	-	-	-
Securitisations	96	-4	-	-	-	-
Consumer credit	66	-	32	-	-	-
Trade receivables	220	-	-	-	-	-
Leases	35	-	21	-	14	-
Commercial mortgage loans	154	-	71	-5	19	-
Residential mortgage loans	1,227	10	231	-	2	-
Loans to businesses (including SMEs)	398	1	129	-	16	-
TOTAL	**7,121**	**7**	**490**	**-5**	**51**	**-**

(*) The amount also includes the 4,764 million euro in Romulus securities held in the portfolio of the Banking Group, generally shown under third party securitisations. For more details regarding the type of underlying assets, refer to section 3 - RISKS of OTHER COMPANIES in this PART E

Off-balance sheet

(millions of euro)

Type of securitised asset/ Exposure (*)	GUARANTEES GIVEN						CREDIT LINES					
	Senior		Mezzanine		Junior		Senior		Mezzanine		Junior	
	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries	Net exposure	Adjust./ recoveries
Duomo ABCP Conduit transactions	-	-	-	-	-	-	*2,507*	-	-	-	-	-
Total	**-**	**-**	**-**	**-**	**-**	**-**	**2,507**	**-**	**-**	**-**	**-**	**-**

(*) In addition to the information shown in the table, the Group's trading portfolio as at 31 December 2016 also contains off-balance sheet transactions represented by credit default swaps with exposures to securitisations as underlyings for a nominal value of 21 million euro.

C.3. Banking Group - Stakes in securitisation vehicles

(millions of euro)

SECURITISATION/ SPECIAL PURPOSE VEHICLE	REGISTERED OFFICE	CONSOLIDATION (a)	ASSETS (b)			LIABILITIES (b)		
			Loans	Debt securities	Other	Senior	Mezzanine	Junior
Adriano Lease Sec S.r.l.	Conegliano Veneto (TV)	(c)	2,169	-	111	-	2,137	-
Intesa Sanpaolo SEC SA (c)	Luxembourg	Consolidated	61	-	265	310	-	16
Intesa Sanpaolo Securitisation Vehicle S.r.l. (c) (d)	Milan	Consolidated	100	-	15	89	-	159
Intesa Sec 3 S.r.l.	Milan	Consolidated	(e)	(e)	(e)	(e)	(e)	(e)
Intesa Sec NPL S.p.A.	Milan	Consolidated	(e)	(e)	(e)	(e)	(e)	(e)
Augusto S.r.l. (f)	Milan	(g)	2	-	2	14	-	-
Colombo S.r.l.(f)	Milan	(g)	23	-	7	7	20	10
Diocleziano S.r.l. (f)	Milan	(g)	3	-	4	58	-	-
CR Firenze Mutui	Milan	(g)	(h)	(h)	(h)	(h)	(h)	(h)
Trade Receivables Investment Vehicle S.a.r.l.	Conegliano Veneto (TV)	Not consolidated	(h)	(h)	(h)	(h)	(h)	(h)
TIBET CMBS S.r.l.	Luxembourg	Not consolidated	(h)	(h)	(h)	(h)	(h)	(h)
ISP OBG S.r.l. (former ISP Sec 4 S.r.l.) (i)	Milan	Consolidated	22,597	-	3,503	25,726		
ISP CB Ipotecario S.r.l. (i)	Milan	Consolidated	16,921	-	4,519	19,464		
ISP CB Pubblico S.r.l. (i)	Milan	Consolidated	4,453	2,369	2,910	9,312		

(a) Consolidation method referring to the "prudential" scope.

(b) Figures gross of any intercompany relations.

(c) Self-securitisation vehicle described in Section 1.3 Banking Group - Liquidity Risk, Quantitative Information, paragraph 4.

(d) This vehicle (former Intesa Lease Sec S.r.l.) has been used to a transaction - completed at the end of 2014 - which entailed the sale without recourse of a portfolio of loans backed by guarantees and mortgages originated by the subsidiary CIB Hungary, also in currencies other than the euro, for a total of 343 million euro.

(e) For the financial statement disclosure concerning this vehicle, see the prospectus published in Section C.6 of these Notes to the consolidated financial statements.

(f) The amounts shown under assets and liabilities refer to the latest financial statement data available (31.12.2015).

(g) Vehicle consolidated at equity.

(h) For the financial statement disclosure concerning this vehicle, see the prospectus published in Section C.4 of these Notes to the consolidated financial statements.

(i) Vehicle used for the covered bond issue by the Intesa Sanpaolo Group. For more information, see Section E.4 in Part E of these Notes to the consolidated financial statements.

C.4 Banking group – Not consolidated securitisation vehicles

With reference to not consolidated structured entities used for securitisation transactions, the Group reports its residual investments in the vehicles Augusto, Colombo, Diocleziano and CR Firenze Mutui, consolidated at equity. The first three vehicles are entities used to implement securitisations of assets, primarily land and public works financing, of a company subject to joint control and sold in previous years.

The Group holds a residual investment in the vehicles. There are no agreements in place which could result in the obligation of the Group to provide financial support to said vehicles.

The vehicles Trade Receivables Investment Vehicle S.a.r.l. and Tibet CMBS S.r.l. are classified under unconsolidated securitisation vehicles.

CR Firenze Mutui

Securitisation of performing residential mortgages

(millions of euro)

A. Securitised assets	**24**
A.1 Loans	24
A.2 Securities	-
A.3 Other assets	-
B. Investments of the funds collected from loan management	**5**
B.1 Debt securities	-
B.2 Equities	-
B.3 Other	5
C. Securities issued	**23**
C.1 Class A	7
C.2 Class B	8
C.3 Class C	8
C.4 Class D	-
D. Financing received	**1**
E. Other liabilities	**5**
F. Interest expense on securities issued	**-**
G. Commissions and fees	**5**
G.1 Servicing	5
G.2 Other services	-
H. Other expenses	**2**
I. Interest income on securitised assets	**1**
L. Other revenues	**6**

Trade Receivables Investment Vehicle S.a.r.l.

Securitisation of trade receivables

(millions of euro)

A. Assets	**78**
A.1 Receivables	73
A.2 Other assets	5
B. Liabilities	**78**
B.1 Class A securities issued	73
B.2 Class B securities issued	-
B.3 Other liabilities	5
C. Interest charge	**8**
D. Interest income	**8**

Tibet CMBS
Securitisation of residential mortgage loans

(millions of euro)

A. Securitised assets	**197**
A.1 Loans	197
A.2 Securities	-
A.3 Other assets	-
B. Investments of the funds collected from loan management	**11**
B.1 Deposits with banks	10
B.2 Credits to be recognised	-
B.3 Prepayments and accrued income	1
C. Securities issued	**197**
C.1 Class A securities	102
C.2 Class B securities	26
C.3 Class C securities	10
C.4 Class D securities	59
C.5 Class X securities	-
D. Financing received	**9**
E. Other liabilities	**2**
E.1 Sundry payables	-
E.2 Accrued expenses and deferred income	1
E.3 Charges of losses on segregated assets	-
E.4 Gains/losses on segregated assets	1
F. Interest expense on securities issued	**8**
G. Commissions and fees	**-**
G.1 Servicing	-
G.2 Securities placement commissions	-
H. Other expenses	**-**
H.1 Interest expense	-
H.2 Forecast losses on loans	-
H.3 Additional return	-
I. Interest income on securitised assets	**8**
L. Other revenues	**-**
L.1 Interest income	-

C.5. Banking Group - Servicer activities – originated securitisations: collection of securitised loans and repayment of securities issued by the securitisation vehicle

SERVICER	SPECIAL PURPOSE VEHICLES	SECURITISED ASSETS (period-end figure) (millions of euro)		COLLECTIONS OF LOANS IN THE YEAR (millions of euro)		PERCENTAGE OF REIMBURSED SECURITIES (period-end figure)					
						Senior		Mezzanine		Junior	
		Non-performing	Performing	Non-performing	Performing	Non-performing loans	Performing loans	Non-performing loans	Performing loans	Non-performing loans	Performing loans
Intesa Sanpaolo	Intesa Sec	52	48	2	46	0%	49%	0%	0%	0%	0%
Intesa Sanpaolo	Intesa Sec 3	32	314	8	128	100%	0%	0%	88%	0%	0%
Italfondiario	Intesa Sec NPL	12	-	4	-	100%	0%	46%	0%	0%	0%
CR Firenze	Cr Firenze Mutui	1	23	1	6	0%	60%	0%	0%	0%	0%
Total		**97**	**385**	**15**	**180**						

C.6. Banking Group – Consolidated securitisation vehicles

Intesa SEC 3
Securitisation of performing residential mortgage loans

(millions of euro)

A. Securitised assets	**347**
A.1 Loans	346
A.2 Securities	-
A.3 Other assets	1
B. Investments of the funds collected from loan management	**137**
B.1 Debt securities	-
B.2 Equities	-
B.3 Liquidity	137
C. Securities issued	**338**
C.1 Class A1	-
C.2 Class A2	-
C.3 Class A3	194
C.4 Class B	72
C.5 Class C	72
D. Financing received	**49**
E. Other liabilities	**101**
E.1 Amounts due for services rendered	-
E.2 Due to customers	-
E.3 Due to Parent Company	52
E.4 Due to securitisation vehicle	-
E.5 "Additional return" allowance	48
E.6 Accrued expenses – interest on securities issued	-
E.7 Other accrued expenses	1
F. Interest expense on securities issued	**-**
G. Commissions and fees	**1**
G.1 Servicing	1
G.2 Securities placement commissions	-
H. Other expenses	**9**
H.1 Interest expense	9
H.2 Forecasted losses on loans	-
H.4 Additional return	-
I. Interest income on securitised assets	**-**
L. Other revenues	**3**
L.1 Interest income	3

Intesa SEC NPL
Securitisation of non performing mortgage loans

(millions of euro)

A. Securitised assets	**14**
A.1 Loans	12
A.2 Securities	-
A.3 Other assets	2
B. Investments of the funds collected from loan management	**2**
B.1 Debt securities	-
B.2 Equities	2
B.3 Liquidity	-
C. Securities issued	**155**
C.1 Class A	-
C.2 Class B	-
C.3 Class C	-
C.4 Class D	114
C.5 Class E	41
D. Financing received	**6**
E. Other liabilities	**71**
E.1 Amounts due for services rendered	1
E.2 Accrued expenses – interest on securities issued	-
E.3 Other accrued expenses	70
E.4 Floor option premium received	-
F. Interest expense on securities issued	**-**
G. Commissions and fees	**1**
G.1 Servicing	1
G.2 Other services	-
H. Other expenses	**23**
H.1 Interest expense	1
H.2 Other expenses	1
H.3 Losses on penalty interest	-
H.4 Losses on loans	21
H.5 Forecasted losses on loans	-
I. Interest income on securitised assets	**6**
L. Other revenues	**17**
L.1 Interest income	-
L.2 Recovery of legal expenses	16
L.3 Write-backs	1
L.4 Other income	-

D. INFORMATION ON STRUCTURED ENTITIES (OTHER THAN SECURITISATION VEHICLES)

In line with IFRS 12, the Group considers structured entities to be entities set up to achieve a narrow, well-defined objective, defined through contractual arrangements which often impose strict restrictions on decision-making powers of the entity's management bodies. In that sense, structured entities are designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, as they refer to administrative tasks, while the relevant operating activities are directed by means of contractual arrangements agreed on at the time of structuring the structured entity, which are difficult to modify. The characteristics of a structured entity include:

– limited activities;
– a narrow and well-defined objective;
– insufficient equity to permit the structured entity to finance its activities without subordinated financial support.

The structured entities through which the Group operates are mainly Special Purpose Entities (SPEs) and UCIs.

D.1 Consolidated structured entities

There are no structured entities consolidated in the accounts other than securitisation companies that fall within the scope of the Intesa Sanpaolo Banking Group.

D.2 Structured entities not consolidated in the accounts

D.2.1 Structured entities consolidated for regulatory purposes

There are no structured entities that are not consolidated in the accounts but are consolidated for regulatory purposes.

D.2.2 Other structured entities not consolidated for regulatory purposes

Qualitative information

As indicated above, the Group's operations through structured entities are also carried out through SPEs. To that end, SPEs are understood as legal entities established to pursue a specific, well-defined and limited objective:

– to raise funds on the market by issuing specific financial instruments;
– to develop and/or finance a specific business initiative, capable of generating, through an economic activity, cash flows which permit the complete reimbursement of the debt;
– to finance the acquisition of a target company which, through its economic activity, will be capable of generating cash flows for the SPEs which permit the complete reimbursement of the debt.

For the purposes of this section, operations carried out through securitisation vehicles, that is vehicles established to acquire, sell and manage specific assets, separating them from the financial statements of the Originator, for the purpose of carrying out securitisations of assets or for acquiring funding through self-securitisations and issues of Covered Bonds (CB), shall not be relevant. For that types of vehicle companies, reference should be made to section "C. Securitisations" and section "E. Sales" of Part E of the Notes to the consolidated financial statements.

In some cases, the Group sponsors the SPE by structuring the transaction to pursue specific objectives, such as raising funds, securitising its own assets also for the purposes of funding or offering financial services to customers.

In detail, the Group's operations are carried out through the following types of structured entities represented by special purpose entities (SPEs).

Project Financing SPEs

These are financing instruments for capital intensive projects, which are based on the economic or financial validity of the industrial or infrastructural project, and are independent from the standing/creditworthiness of the sponsors who developed the "entrepreneurial" idea. The financing of the initiative is based on the project's capacity to generate positive cash flows, sufficient to reimburse loans received and guarantee an adequate risk-adjusted return on invested capital.
The Intesa Sanpaolo Group finances entities of this type, as normal borrowers, without acting as sponsor.

Asset Backed SPEs

These are transactions aimed at acquisition/construction/management of physical assets by SPEs financed by one or more entities. Their recovery prospects mostly depend upon the cash flows generated by the assets. The assets generate cash flows in their recurring operations (e.g. rentals, goods transportation contracts, etc.) or in their non-recurring operations (e.g. a real estate development or disposal plan). Generally, the assets are also the collateral for the financing disbursed to the vehicle.
The Intesa Sanpaolo Group finances entities of this type, as normal borrowers, without any direct equity investments or any other interests which might lead to presume the role of sponsor. The risk undertaken is always a normal credit risk and the benefits are represented by the return on the financing granted.

Leveraged & Acquisition Finance SPEs

This category includes exposures (loans granted and disbursed in relation to structured financing operations, normally medium/long-term) to legal entities in which the majority of share capital is held by private equity funds.
These are mainly positions in support of Leveraged Buy Out projects (therefore with high financial leverage), i.e. linked to the full or partial acquisition of companies through recourse to SPEs created for this purpose. After acquisition of the target company's shares/quotas package, these SPEs are normally merged into the target. The target companies generally have good economic prospects, stable cash flows in the medium term and low original leverage levels. The Intesa Sanpaolo Group finances entities of this type, as normal borrowers, without acting as sponsor.

The Intesa Sanpaolo Group also has investments in/exposures to structured entities represented by UCIs.
The main cases include the Group's investments in several funds managed by IMI Fondi Chiusi SGR, which sponsors and manages closed-end private equity funds, in the form of UCIs reserved to qualified operators, specialised in investment in Small and Medium-Sized Enterprises, operating in two complementary business lines: Private Equity and Venture and Seed Capital.
In the area of Private Equity, there are several operating funds dedicated to investment in SMEs throughout the country and in specific geographical areas.
In the area of Venture and Seed Capital, the sponsored funds operate in the following areas:
– participation in new business initiatives characterised by sound technological profiles;
– participation in projects to introduce process or product innovation using digital technology;
– investments in businesses with high forecast growth rates and cutting-edge technological development, both through direct investments in Seed Capital (financing the assessment and development of a business idea prior to the start-up phase) and indirect investments in UCI units with an investment policy matching the Fund's objectives or in business incubators/accelerators.

Investments in these types of funds derive from the Group's willingness to subscribe unplaced units offered during the placement to qualified investors, to ensure that the initiatives are successful, in any event, while maintaining suitable separation of management in organisational terms.
The closed-end funds in question finance their activities exclusively using the capital that investors committed to paying in at the time of placement, without using any types of debt.

The Group made further investments in UCIs through the subsidiary Eurizon Capital SGR, in line with the financial portfolio management policies issued by the company, in agreement with the Intesa Sanpaolo Group Guidelines. In detail, the asset management company has both temporary and structural available funds deriving from company equity that is not permanently invested in equity investments or other fixed assets, and from the ordinary cash flows. Based on that set out in the guidelines for managing the financial portfolio, as part of Treasury management activities, structural and temporarily available funds linked to the trend in short-term and on demand cash flows make up the liquidity portfolio net of the amount held in current accounts or invested in term deposits. In relation to the activities carried out by the asset management company and the characteristics of the available funds in question, excess liquidity must be invested in assets with moderate risk that can be easily liquidated. That portfolio includes investments in short-term money market and bond funds, both specialising in the Eurozone, established and/or managed by Eurizon Capital SGR or by its subsidiaries. The Group's investments in UCIs managed by a subsidiary do not prejudice the operational autonomy and capacity of the asset management company to act in the exclusive interest of investors, considering the specific provisions set out in sector regulations and by the Supervisory Authorities.

The exposures to UCIs also include the investments in units of real estate funds deriving from transactions to contribute portions of the Group's real estate portfolio.

The investments in UCIs also include the amounts held in the Atlante Fund, an alternative investment fund created with the dual purpose of investing in banks with inadequate capital endowment and that, therefore, realise, on the request of the Supervisory Authorities, capital strengthening actions via capital increases and non-performing loans value enhancement transactions.

The Intesa Sanpaolo Group also invests in hedge funds. For more information, reference is made to the specific section in Part E of the Notes to the consolidated financial statements.

Quantitative information

(millions of euro)

Captions / Type of structured entity		Accounting portfolios under assets	Total assets (A)	Accounting portfolios under liabilites	Total liabilities (B)	NET BOOK VALUE (C = A-B)	Maximum exposure to risk of loss (D)	Difference between exposure to risk of loss and book value (E = D - C)
1.	**Special purpose vehicle**		**4,211**		**36**	**4,175**	**6,420**	**2,245**
		Financial assets held for trading	44	Due to customers	36			
		Financial assets designated at fair value through profit and loss	-	Financial liabilities held for trading	-			
		Financial assets available for sale	20		-			
		Loans to customers	4,147		-			
2.	**UCI**		**2,753**		**85**	**2,668**	**3,315**	**647**
		Financial assets held for trading	586	Due to customers	74			
		Financial assets designated at fair value through profit and loss	119	Financial liabilities held for trading	11			
		Financial assets available for sale	1,377		-			
		Loans to customers	671		-			

The maximum exposure to risk, representing the maximum exposure of the Group to losses deriving from its interests in structured entities, is generally equal to the net book value, to which, where applicable, several types of off-balance sheet exposures are

added (ex. committed credit lines or guarantees given). The net book value equals the exposure in the financial statements net of value adjustments recorded during the current and previous years.
For UCIs, the maximum risk exposure also includes the Group's commitments, not yet called up by the fund, to subscribe additional units.
The table below shows the amount and type of revenues earned over the year by sponsored structured entities for which no exposures or equity investments were posted in the financial statements at the reporting date. Specifically, these are revenues recognised by the Group in the form of fees deriving from the management and placement of the UCIs sponsored and managed by the Group's asset management companies and placed with customers. The fees in question are charged by the asset management company to the funds managed and partly reversed to the distribution network for the placement service. The Group had no interests in the funds
in question at the reporting date.

(millions of euro)

Type of structured entity sponsored	Interest	Fees and commissions	Dividends	Other revenue	TOTAL
UCI	-	1,809	-	-35	1,774
Special-purpose vehicles	140	27	-	203	370

E. SALES

A. Financial assets sold not fully derecognised

Qualitative information

For a description of the operations shown in tables E.1, E.2 and E.3 below, reference is made to the information shown below the relevant tables.

Conversely, for operations in debt securities against medium-/long-term repurchase agreements, reference is made to the information in Part B of the Notes to the consolidated financial statements.

Quantitative information

E.1. Banking group - Financial assets sold not derecognised: book value and full value

(millions of euro)

Type / Portfolio	CASH ASSETS				DERIVATIVES	31.12.2016		31.12.2015	
	Debt securities	Equities	UCI	Loans		Total	*of which non-performing assets*	Total	*of which non-performing assets*
FINANCIAL ASSETS HELD FOR TRADING	**4,758**	**-**	**-**	**-**	**-**	**4,758**	**-**	**6,080**	**-**
- Financial assets sold totally recognised (book value)	4,758	-	-	-	-	4,758	-	6,080	-
- Financial assets sold partly recognised (book value)	-	-	-	-	-	-	-	-	-
- Financial assets sold partly recognised (full value)	-	-	-	-	-	-	-	-	-
FINANCIAL ASSETS MEASURED AT FAIR VALUE	**-**	**-**	**-**	**-**	**X**	**-**	**-**	**-**	**-**
- Financial assets sold totally recognised (book value)	-	-	-	-	X	-	-	-	-
- Financial assets sold partly recognised (book value)	-	-	-	-	X	-	-	-	-
- Financial assets sold partly recognised (full value)	-	-	-	-	X	-	-	-	-
FINANCIAL ASSETS AVAILABLE FOR SALE	**19,091**	**-**	**-**	**-**	**X**	**19,091**	**-**	**10,961**	**-**
- Financial assets sold totally recognised (book value)	19,081	-	-	-	X	19,081	-	10,961	-
- Financial assets sold partly recognised (book value)	5	-	-	-	X	5	-	-	-
- Financial assets sold partly recognised (full value)	5	-	-	-	X	5	-	-	-
INVESTMENTS HELD TO MATURITY	**-**	**X**	**X**	**-**	**X**	**-**	**-**	**-**	**-**
- Financial assets sold totally recognised (book value)	-	X	X	-	X	-	-	-	-
- Financial assets sold partly recognised (book value)	-	X	X	-	X	-	-	-	-
- Financial assets sold partly recognised (full value)	-	X	X	-	X	-	-	-	-
DUE FROM BANKS	**-**	**X**	**X**	**-**	**X**	**-**	**-**	**-**	**-**
- Financial assets sold totally recognised (book value)	-	X	X	-	X	-	-	-	-
- Financial assets sold partly recognised (book value)	-	X	X	-	X	-	-	-	-
- Financial assets sold partly recognised (full value)	-	X	X	-	X	-	-	-	-
LOANS TO CUSTOMERS	**826**	**X**	**X**	**710**	**X**	**1,536**	**397**	**2,082**	***140***
- Financial assets sold totally recognised (book value)	826	X	X	710	X	1,536	397	2,082	140
- Financial assets sold partly recognised (book value)	-	X	X	-	X	-	-	-	-
- Financial assets sold partly recognised (full value)	-	X	X	-	X	-	-	-	-
Total 31.12.2016	**24,675**	**-**	**-**	**710**	**-**	**25,385**	**397**	**X**	***X***
Total 31.12.2015	**18,550**	**-**	**-**	**573**	**-**	**X**	**X**	**19,123**	***140***

Covered bond transactions where the selling bank and the lending bank are the same are not included in this caption.

Operations mainly refer to the use of securities held for short and medium/long-term repurchase agreements and loans to customers assigned as part of the SEC 3 and K-Equity securitisations.

E.2. Banking group - Financial liabilities corresponding to financial assets sold not derecognised: book value

(millions of euro)

	DUE TO CUSTOMERS		DUE TO BANKS		SECURITIES ISSUED		Total 31.12.2016	Total 31.12.2015
	Fully recognised	Partly recognised	Fully recognised	Partly recognised	Fully recognised	Partly recognised		
Financial assets held for trading	3,112	-	911	-	-	-	4,023	6,570
Financial assets measured at fair value	-	-	-	-	-	-	-	-
Financial assets available for sale	13,815	-	5,269	-	-	-	19,084	10,802
Investments held to maturity	-	-	-	-	-	-	-	-
Due from banks	-	-	-	-	-	-	-	189
Loans to customers	21	-	771	-	363	-	1,155	1,570
Total	**16,948**	**-**	**6,951**	**-**	**363**	**-**	**24,262**	**19,131**

Covered bond transactions where the selling bank and the lending bank are the same are not included in this caption.
The financial liabilities corresponding to financial assets sold not derecognised (shown in the columns Due to Customers and Due to Banks) mainly relate to repurchase agreements for securities recorded under assets. On the other hand, in accordance with the regulations, the liabilities issued as part of the related securitisations by the SEC3 vehicle (included within the scope of consolidation) and those relating to the K-Equity securitisation, are shown under securities issued.
However, they do not include the repurchase agreements relating to securities received under reverse repurchase agreements.

E.3. Banking group - Sales with liabilities having recourse exclusively on the assets sold: fair value

(millions of euro)

Type / Portfolio	FINANCIAL ASSETS HELD FOR TRADING		FINANCIAL ASSETS DESIGNATED AT FAIR VALUE THROUGH PROFIT AND LOSS		FINANCIAL ASSETS AVAILABLE FOR SALE		INVESTMENTS HELD TO MATURITY (fair value)		DUE FROM BANKS (fair value)		LOANS TO CUSTOMERS (fair value)		Total 31.12.2016	Total 31.12.2015
	Financial Assets sold:		Financial Assets sold:		Financial Assets sold:		Financial Assets sold:		Financial Assets sold:		Financial Assets sold:			
	fully recognised	partly recognised	fully recognised	partly recognised	fully recognised	partly recognised	fully recognised	partly recognised	fully recognised	partly recognised	fully recognised	partly recognised		
A. Cash assets	**4,758**	**-**	**-**	**-**	**19,081**	**5**	**-**	**-**	**-**	**-**	**1,567**	**-**	**25,411**	**18,959**
1. Debt securities	4,758	-	-	-	19,081	5	-	-	-	-	845	-	24,689	18,367
2. Equities	-	-	-	-	-	-	X	X	X	X	X	X	-	-
3. UCI	-	-	-	-	-	-	X	X	X	X	X	X	-	-
4. Loans	-	-	-	-	-	-	-	-	-	-	722	-	722	592
B. Derivatives	**-**	**-**	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**X**	**-**	**-**
Total Assets	**4,758**	**-**	**-**	**-**	**19,081**	**5**	**-**	**-**	**-**	**-**	**1,567**	**-**	**25,411**	**18,959**
C. Associated liabilities	**4,023**	**-**	**-**	**-**	**19,096**	**-**	**-**	**-**	**-**	**-**	**1,146**	**-**	**X**	**X**
1. Due to customers	3,112	-	-	-	13,815	-	-	-	-	-	21	-	X	X
2. Due to banks	911	-	-	-	5,281	-	-	-	-	-	762	-	X	X
3. Securities issued	-	-	-	-	-	-	-	-	-	-	363	-	X	X
Total Liabilities	**4,023**	**-**	**-**	**-**	**19,096**	**-**	**-**	**-**	**-**	**-**	**1,146**	**-**	**24,265**	**19,128**
Net Value 2016	**735**	**-**	**-**	**-**	**-15**	**5**	**-**	**-**	**-**	**-**	**421**	**-**	**1,146**	**X**
Net Value 2015	**-490**	**-**	**-**	**-**	**146**	**-**	**-**	**-**	**-189**	**-**	**364**	**-**	**X**	**-169**

Covered bond transactions where the selling bank and the lending bank are the same are not included in this caption.

B. Financial assets sold fully derecognised with recognition of continuing involvement

This type of exposure did not exist as at 31 December 2016.

E.4. Banking group - Covered bond transactions

The Intesa Sanpaolo Group uses Covered Bonds (CB) to prudently establish eligible assets with Central Banks, or as a type of funding, by placing Covered Bonds on the market.
Transactions are structured by selling assets (loans, mortgages) to a vehicle, with the simultaneous granting of a subordinated loan for payment of the sale price. In the Intesa Sanpaolo Group, in this phase the seller is always the same entity as the lender. Securities are issued by the Parent Company, relating to assets sold to the vehicle by other Group companies.
In accordance with IAS 39, these transactions do not represent sales without recourse for accounting purposes, as the Group companies involved maintained all the risks and rewards connected to the loans sold. Therefore, when recording the transactions, Bank of Italy provisions are applied, according to which, where the originator and the lender are the same entity, the separate assets of the vehicle, provided as security for the issues of Covered Bonds, are consolidated in the separate financial statements.

Over time, the Intesa Sanpaolo Group has carried out three Covered Bond issue programmes.

The first programme, launched at the end of July 2009, had an amount of 20 billion euro (the original amount was 10 billion euro). The guarantor of the Covered Bonds is the vehicle ISP CB Pubblico, to which a portfolio of performing loans and securities to the public sector, originated by the former subsidiary Banca Infrastrutture Innovazione e Sviluppo, now Intesa Sanpaolo, was transferred. In detail, performing loans and securities to the public sector with a total original nominal value of around 14.3 billion euro (net of retrocessions of assets of 0.5 billion euro) were sold, the last of which (amounting to around 1 billion euro) in April 2013. As at 31 December 2016 loans and securities sold to the vehicle had a book value of 6.6 billion euro.
Against these sales, Covered Bonds were issued over time for a total nominal value of 22.6 billion euro (of which 3 billion euro relating to a covered bond which matured in the fourth quarter of 2011, 12 billion euro relating to issues acquired by the Parent Company and cancelled or subject to early redemption and 3.2 billion euro relating to an exchange offer to investors during 2012). During 2016:
– the early repayment of the eighth series of CB was carried out, for a nominal value of 2.2 billion euro which, as it was fully subscribed by the Parent Company Intesa Sanpaolo, was already cancelled from the accounts;

- the early repayment of the ninth series of CB was carried out, for a nominal value of 1 billion euro which, as it was fully subscribed by the Parent Company Intesa Sanpaolo, was already cancelled from the accounts;
- The eleventh series of Covered Bonds was issued, for a nominal value of 1.1 billion euro. The notes, with floating rate and 2-year maturity, were fully subscribed by the Parent Company. The bonds are listed on the Luxembourg Stock Exchange with Moody's A2 rating, and are eligible for Eurosystem transactions;
- The twelfth series of Covered Bonds was issued, for a nominal value of 1.3 billion euro. The notes, with floating rate and 7-year maturity, were fully subscribed by the Parent Company. The bonds are listed on the Luxembourg Stock Exchange with Moody's A1 rating, and are eligible for Eurosystem transactions;

Therefore, as at 31 December 2016 a total nominal amount of 7.6 billion euro of issues made as part of the Covered Bond Programme of the vehicle ISP CB Pubblico was outstanding, of which 7.3 billion repurchased and 0.3 billion placed with third party investors.

In the second programme, amounting to a maximum of 20 billion euro, the guarantor of the Covered Bonds is the vehicle ISP CB Ipotecario S.r.l., to which Italian residential mortgage loans, government bonds and Adriano Finance S.r.l. bonds originated by Intesa Sanpaolo were transferred with a total original nominal value of 24.8 billion euro (net of retrocessions). During 2016, Intesa Sanpaolo transferred residential mortgage loans to the vehicle in May, for a total original nominal value of approximately 3.7 billion euro.
As at 31 December 2016 loans sold to the vehicle had a book value of 21.2 billion euro.
Over time, against the sale of these assets, Intesa Sanpaolo carried out issues of Covered Bonds for a total nominal value of approximately 27.7 billion euro (of which 1 billion euro relating to a covered bond that reached maturity in the fourth quarter of 2015 and 8.2 billion euro subject to early redemption in 2012).
During 2016:

- the second series of CB reached maturity, with a nominal value of 2.5 billion euro;
- in March, series 19 of CB was issued in the form of a fixed-rate bond (0.625%) for a nominal value of 1.25 billion euro, with a 7-year maturity, listed on the Luxembourg Stock Exchange with Moody's Aa2 rating. The bond was placed with institutional investors;
- in September, series 20 of CB was issued in the form of a floating-rate bond for a nominal value of 1.25 billion euro, with a 4-year maturity, listed on the Luxembourg Stock Exchange with Moody's Aa2 rating. The bond was subscribed by Intesa Sanpaolo for Eurosystem refinancing transactions;
- in November, series 21 of CB was issued in the form of a floating-rate bond for a nominal value of 2.2 billion euro, with a 8-year maturity, listed on the Luxembourg Stock Exchange with Moody's Aa2 rating. The bond was subscribed by Intesa Sanpaolo for Eurosystem refinancing transactions.

As at 31 December 2016, a total nominal amount of 16 billion euro of issues made as part of the Covered Bond Programme of the vehicle ISP CB Ipotecario was outstanding, of which 12.6 billion placed with third party investors and 3.4 billion subscribed by Intesa Sanpaolo.

In 2012 the new multi-originator CB issue programme was launched, secured by mortgages totalling 30 billion euro. Aimed at retained issues, the programme provides for the issue of unrated securities which thus benefit from the rating of the issuer Intesa Sanpaolo. The portfolio used to collateralise the issues of Covered Bonds is composed of mortgages originated by Intesa Sanpaolo, Banco di Napoli, Cassa di Risparmio del Veneto, Banca dell'Adriatico, which was merged by incorporation into Intesa Sanpaolo in May 2016, Cassa di Risparmio in Bologna and Banca CR Firenze. In particular:

- Intesa Sanpaolo sold mortgages to the vehicle with a total original nominal value of 15.4 billion euro, of which 2.4 billion euro sold in June 2016;
- Banco di Napoli sold mortgages to the vehicle for a total original nominal value of 9.4 billion euro, of which 1.1 billion euro sold in March 2016;
- Cassa di Risparmio del Veneto sold mortgages to the vehicle for a total original nominal value of 3.9 billion euro, of which 0.4 billion euro sold in June 2016;
- The former Banca dell'Adriatico sold mortgages to the vehicle with an original nominal value of 1.6 billion euro. No sales were made during 2016; in May 2016, the bank was merged by incorporation into Intesa Sanpaolo;
- Cassa di Risparmio in Bologna sold mortgages to the vehicle for a total original nominal value of 1.9 billion euro, of which 0.7 billion euro sold in June 2016;
- Cassa di Risparmio del Veneto sold mortgages to the vehicle for an original nominal value of 2.2 billion euro, of which 0.6 billion euro sold in June 2016;

As at 31 December 2016 loans sold to the vehicle had a book value of 22.6 billion euro.

Over time, against the sales of these assets, Intesa Sanpaolo carried out issues of Covered Bonds for a total nominal value of approximately 46.9 billion euro (of which 25 billion euro subject to early redemption and reimbursed). During 2016:

- in May, the seventh series of CB reached maturity, with a value of 1.375 billion euro;
- in August, the eighth series of CB reached maturity, with a value of 1.375 billion euro;
- in June, the 20th series of CB was issued with a nominal value of 1.6 billion euro. This is a 7-year, floating-rate bond;
- in September, the 21st series of CB was issued with a nominal value of 1.750 billion euro. This is an 8-year, floating-rate bond;
- in September, the 22nd series of CB was issued with a nominal value of 1.750 billion euro. This is a 9-year, floating-rate bond.

All securities issued as part of the multi-originator programme are listed on the Luxembourg Stock Exchange and, as noted above, benefit from the rating of the issuer Intesa Sanpaolo. The characteristics of the issues make them eligible for Eurosystem refinancing transactions.
As at 31 December 2016 a total nominal amount of 21.9 billion euro of issues made as part of the Covered Bond Programme of the vehicle ISP OBG was outstanding, fully repurchased by Intesa Sanpaolo.

The key figures for ISP CB Pubblico, ISP CB Ipotecario and ISP OBG as at 31 December 2016 are shown in the table below.

(millions of euro)

COVERED BONDS		VEHICLE DATA		SUBORDINATED LOAN [1]	COVERED BONDS ISSUED	
		Total assets	Cumulated write-downs on securitised	amount	Nominal amount [2]	Book value [2]
ISP CB PUBBLICO	Performing public sector loans and securities	9,731	6	9,312	284	314
ISP CB IPOTECARIO	RMBSs (Performing residential mortgages)	21,440	100	19,464	12,576	13,651
ISP OBG	Performing mortgages	26,100	223	11,564	-	-

[1] This caption includes the subordinated loan granted by the originator for the purchase of the portfolio lodged as collateral for the CB. In accordance with the IFRS, this loan has been recognised in the separate financial statements of the originator and the consolidatd financial statements of the Intesa Sanpaolo Group. The figure reported also includes the amount of the subordinated loans disbursed during the year, with respect to which no issues have yet been made.

[2] The nominal amount and the book value shown in the table are to be considered net of securities repurchased.

In addition to this type of Covered Bonds, provided for by Italian law (Law 80/2005), there are some mortgage bonds issued by the Slovak investee VUB. These are securities whose nominal value and returns are guaranteed by mortgage loans, i.e. loans with maturity of four to thirty years, backed by a pledge on property located in the Slovak Republic, including property under construction, at least 90% of the value of which is financed by the issue of these securities.
Each issue has specific coverage, and the entire nominal value of the issue, including interest, must be backed by mortgages on local properties on at least 90% of their nominal value, and the remaining 10% by liquidity deposits with the National Bank of Slovakia or with other resident banks, by government securities or other mortgage bonds.
As at 31 December 2016 the subsidiary VUB had issued 1.8 billion euro in this type of securities, booked in the financial statements at a value of approximately 1.7 billion euro.

F. BANKING GROUP - MODELS FOR THE MEASUREMENT OF CREDIT RISK

As at 31 December 2016, the expected loss on core banks (Basel 3 validation area) amounted to 0.52% of disbursed loans, a 0.02 percentage point decrease on the figure as at the end of 2015. The economic capital corresponded to 3.9% of disbursed loans, an increase of 0.2% compared to the figure in 2015.

In particular, the improvement in the expected loss was due to management action aimed at shifting the composition of the portfolio towards the best exposures and reclassifications to non-performing loans, which contribute to eliminating customers with worse ratings from the performing loans portfolio. These effects offset the downgrading of the ratings due to the continuing difficult economic scenario. The increase in economic capital is justified by the effect of concentration risk, caused by the increase in use.

The internal rating, LGD and EAD models are subject to internal validation process by the Internal Validation Sub-Department and a level three control by the Internal Auditing Department. The control functions produce an annual report for the Supervisory Authority on the compliance of the models with the supervisory regulations, which also verifies deviations of the ex-ante estimates and the effective ex post values. This report, approved by the Board of Directors of Intesa Sanpaolo, confirms the existence of the compliance requirements.