Company value and solidity

THE 2018-2021 BUSINESS PLAN

Intesa Sanpaolo, thanks to the results achieved during the 2014-2017 Business Plan, has laid the foundations for confirming its leading role in Italy, while reinforcing its competitiveness at an international level, through the transformation of its business model and significant investments in digital technology, playing a key role in the current macroeconomic scenario.

The 2018-2021 Business Plan seeks to maintain solid and sustainable value creation and distribution for all stakeholders. In addition, Intesa Sanpaolo, already a leader in the field of Corporate Social Responsibility, is seeking to become an exemplary group in terms of social and cultural responsibility. The new Business Plan integrates the commitments set by the Group, by defining measures to contribute to global development, in order to support its customers, promote the development and well-being of people and communities, and protect the environment, including through combating climate change. In particular, Intesa Sanpaolo wishes to become an exemplary group for society, through a series of initiatives aimed at, among other things, granting loans to groups who have difficulty accessing credit despite their potential, ensuring support to those who need it most, mitigating the consequences of natural disasters for households and businesses, supporting the Circular Economy's development, and making the most of the artistic, cultural and historical heritage of the Group to promote art and culture in Italy and abroad. In this sense, the Group, including in its strategy, takes into consideration the Sustainable Development Goals (SDGs) set by the United Nations, and therefore wishes to provide a concrete response not only in wording, but also in implementing the commitments undertaken, whose results have now become an integral part of the Bank's sustainable and responsible business model. Intesa Sanpaolo thus intends to seize every opportunity to strengthen the central role of sustainability and social and environmental responsibility within its overall strategy.

The Plan focuses on reinforcing the Group's resilient and highly-diversified business model, particularly to position the Group as a significant player in wealth management & protection.

In a new, highly digitalised and competitive world, the Bank is continuing to achieve its goals by relying upon its values and the proven implementation capacity of a results-oriented delivery machine.

The new strategy hinges on a number of priorities that are now part and parcel of Intesa Sanpaolo, which aims to confirm its leadership as a Bank of the real economy, supporting households and businesses. With a strong balance sheet and a leading position, the Group fulfils requests for credit and responsibly manages customers' savings. Intesa Sanpaolo wishes to be a Bank with sustainable profitability, in which the operating results, productivity, risk profile, liquidity and soundness/leverage are carefully balanced.

The new 2018-2021 Business Plan is based on three central pillars:

- significant de-risking at no cost to Shareholders;
- cost reduction through further simplification of the operating model;
- revenue growth seizing new business opportunities.

The enabling factors are people, who continue to be Intesa Sanpaolo's most important resource, and the completion of the digital transformation, which will make it possible to increase the levels of efficiency and offer advanced, high-quality products and services to customers.

People, in particular, will benefit from a series of initiatives aimed at strengthening their involvement, promoting inclusion and ongoing dialogue with the company, developing the best talents, improving skills, maintaining employment levels, promoting internal fairness and facilitating a work/life balance through flexibility initiatives (see 2018 Financial Statements, page 68 [i]).

Through the new Business Plan, Intesa Sanpaolo has set itself goals which will generate value for its stakeholders. As a solid Bank that is increasingly profitable, Intesa Sanpaolo is able to make a positive contribution for the interests of its shareholders and all its stakeholders.

These objectives are detailed in the various sections of the document, together with the progress achieved during 2018. These include:

Stakeholder	Benefits	2018 results	Plan Objectives for 2021 Cumulative value 2018-2021
Shareholders	Cash payout ratio	85%	85% in 2018, 80% in 2019, 75% in 2020 and 70% in 2021
Households and businesses	New medium/long-term credit granted to the real economy	~60 billion euro	~250 billion euro
Employees	Personnel expenses	~5.8 billion euro	~24 billion euro
Suppliers	Procurement and investments	~2.7 billion euro	~11 billion euro
Public sector	Direct and indirect taxes	~2.5 billion euro	~13 billion euro

ECONOMIC AND FINANCIAL PERFORMANCE AND DISTRIBUTION OF VALUE ADDED

ECONOMIC AND FINANCIAL PERFORMANCE[1]

The results for 2018 need to be interpreted bearing in mind the major change with respect to the 2017 Financial Statements, consisting of the adoption, for the first time, of IFRS 9 from 1 January 2018. This adoption has resulted in a change to the accounting standard governing the classification and assessment of financial instruments, as well as the adoption of new financial statement formats, with changes to the content of some of their items.

In a scenario of a slowing economic cycle and high volatility on financial markets, the Intesa Sanpaolo Group reported a net income of 4,050 million euro in 2018, up by 6% on the like-for-like figure in the previous year, excluding, in the interest of uniformity of comparison, the public contribution of 3,500 million euro to offset the impact on capital ratios of the acquisition of certain assets and liabilities and certain legal relationships of Banca Popolare di Vicenza and Veneto Banca.

In detail, operating income rose slightly (+0.2% on the like-for-like figure at 17.9 billion), attributable to the profits on financial assets and liabilities (around +25%) and income from insurance business (around +16%), which was fully offset by the decrease in interest and fee (around -2%) and commission income (around -2%).

Operating costs, which are carefully monitored, were down compared to the like-for-like figure (-3.6%), both for personnel expenses (-3.3%) and administrative expenses (-5.1%).

As a result of these revenue and cost trends, the operating margin amounted to 8.4 billion, up by 4.8%.

Net adjustments to loans decreased overall (around -28%) due to lower adjustments to bad loans, with net provisions and net impairment losses on other assets also falling (around -20%).

Other income (expenses) includes the capital gain of 443 million euro relating to the finalisation, in December, of the agreement with Intrum for the strategic partnership regarding the non-performing loans.

The expenses aimed at maintaining the stability of the banking system also had a negative impact, of 340 million euro, albeit to a lesser degree than the previous year.

With regard to the balance sheet aggregates, loans to customers as at 31 December 2018 totalled 394 billion euro and were slightly down overall (-1.5%) on the like-for-like figure as at 1 January 2018, which includes the effects of the first-time adoption of IFRS 9. In terms of funding, direct deposits from banking business came to 415 billion euro (-2%) at the end of 2018. Direct deposits from insurance business, which include technical reserves, were also slightly down overall compared to the beginning of the year (-2%), at 149 billion euro.

1 Commentary refers, unless otherwise specified, to the reclassified data published in the 2018 Consolidated Financial Statements of the Intesa Sanpaolo Group. Changes in annual percentages are based on 2017 figures, restated, where necessary and if they are material, to take into account changes in the scope of consolidation. Amounts are in millions of euro. For additional details or information, see the 2018 Consolidated Financial Statements of the Intesa Sanpaolo Group.

Indirect customer deposits amounted to approximately 496 billion euro, down (-4.8%) from the beginning of the year, essentially due to the negative trend on the markets. In addition to a moderate decline in assets under management (-2.6%), the negative performance of this aggregate was driven above all by assets under administration (-8.8%). The persisting complexity of the macroeconomic environment and the marked volatility of financial markets call for constant control of the factors enabling the Group to pursue sustainable profitability: high liquidity, funding capacity, low leverage, adequate capital base and prudent asset valuations.
Group liquidity remains high: as at 31 December 2018, both the regulatory indicators, the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR), also adopted as internal liquidity risk measurement metrics, had reached a level well above fully phased-in minimum requirements. At the end of the year, the Central Banks' eligible liquidity reserves came to 175 billion euro (171 billion euro in December 2017), of which 89 billion euro, net of haircut, was unencumbered (98 billion euro at the end of December 2017). The loan to deposit ratio at the end of 2017, calculated as the ratio of loans to customers to direct deposits from banking business, stood at 95%.
In terms of funding, the widespread branch network remains a stable, reliable source: 75% of direct deposits from banking business come from retail operations (313 billion euro). Moreover, over the year, 2.5 billion US dollars of unsecured senior bonds, 46.6 billion Yen of unsecured senior bonds, and 2.25 billion euro of unsecured senior bonds were placed, along with 1 billion euro in covered bonds.
With regard to the targeted refinancing operation Targeted Longer-Term Refinancing Operations II (TLTRO II), at the end of December 2018, the Group's participation amounted to 61 billion euro.
The Intesa Sanpaolo Group's leverage ratio was 6.3% as at 31 December 2018.
The capital base also remains high. At the end of the year, the Total Capital Ratio stood at 17.7%, while the ratio of the Group's Tier 1 capital to its total risk-weighted assets (Tier 1 ratio) was 15.2%. The ratio of Common Equity Tier 1 capital (CET1) to risk-weighted assets (the Common Equity Tier 1 ratio) was 13.5%.

Key indicators [millions of euro]

Economic indicators	2018	2017*
Loans to customers	393,550	399,539
Direct deposits from banking business	415,082	423,738
Direct deposits from insurance business and technical reserves	149,358	152,403
Consolidated shareholder's equity	54,024	53,268
Consolidated net income	4,050	7,316
Dividends	3,449	3,419
Stock Exchange average capitalisation	44,947	44,820
Total assets	787,721	794,528
Economic value generated	16,986	21,003
Economic value distributed	-14,852	-16,082

* The restated figures of the balance sheet reflect the impact of the first-time adoption of the IFRS 9 accounting standard (01.01.2018).

CALCULATION AND DISTRIBUTION OF ECONOMIC VALUE

The economic value generated is calculated in accordance with ABI ("Italian Banking Association") instructions and consistent with international reference standards. The calculation is done by reclassifying consolidated income statement items recorded in the financial statements, as required under Bank of Italy Circular no. 262, which, for 2018, were updated to take into account the introduction of accounting standard IFRS 9.

The economic value generated, which in 2018 was approximately 17 billion euro, came from net income from financial operations and the insurance business – which therefore takes into account the impairment losses on loans and other financial assets – plus the realised gains and losses on investments and other operating income. The amount of the economic value generated expresses the value of the wealth produced, most of which distributed among the stakeholders with which the Group interacts in various ways on a day-to-day basis. In particular:

- employees and other staff benefited from almost 39% of the economic value generated, for a total of 6.6 billion euro. In addition to staff pay, the total also includes payments to the network of financial advisors;
- suppliers received approximately 16% of the economic value generated, for a total of 2.7 billion euro in payments for goods and services;
- The Government, Organisations and Institutions recorded a total flow of funds of 1.8 billion euro, around 11% of the economic value generated, over 900 million euro of which referring to indirect taxes and duties, almost 500 million euro to taxes on income from continuing operations, and over 400 million to levies and other charges concerning the banking industry, consisting of contributions to resolution and guarantee funds. There were also numerous social and cultural initiatives and other actions taken to support the charity funds and issue disbursements by way of social and cultural contributions;
- approximately 22% of the economic value generated was allocated to Shareholders, holders of equity instruments and third parties, largely due to the proposed dividend, for a total of 3.7 billion euro.

The remaining amount, over 2.1 billion euro, was withheld by the corporate system and mainly comprises deferred tax assets and liabilities, amortisation and depreciation, provisions for risks and charges, and retained earnings. Self-financing is to be considered an investment that other stakeholder categories make each year to maintain efficiency and allow development of the Bank as a whole.

BREAKDOWN OF 2018 ECONOMIC VALUE

ECONOMIC VALUE	Millions of euro	
ECONOMIC VALUE GENERATED	16,986	100.0%
ECONOMIC VALUE DISTRIBUTED	-14,852	87.4%
Employees	-6,601	38.8%
Suppliers	-2,732	16.1%
Government, organisations and institutions, communities	-1,849	10.9%
Shareholders, holders of equity instruments and third parties	-3,670	21.6%
ECONOMIC VALUE RETAINED	**2,134**	**12.6%**