Banks
Italy/Commercial banks

HSBC Global Research

Italian banks

2009 annus horribilis

- **Our recent visit to Italy yielded evidence of even more severe deterioration in net profit than we previously expected**
- **We are reducing our core EPS estimates by 21% on average in 2009e, and expect no recovery in 2010 (+0%)**
- **We downgrade Credem to Neutral and MPS to UW (V) and upgrade UBI to Overweight; Unicredit stays Neutral (V); ISP is our preferred stock – OW (V)**

Core revenue to fall 6% on average in 2009. We expect lower interest rates to weaken margins as Italian banks will probably be unable to offset reduced liability yield with aggressive asset re-pricing. Margin pressure will worsen over the course of 2009. We also expect fee and commission margins to decline in all product segments.

Government capital support to dilute net profit by 4% on average. Assuming an after-tax cost of 12% for the government-funded instrument, we estimate an average negative net profit impact of 4% for 2009. A cEUR9bn capital injection would place core Tier 1 at 7% in 2008 on our estimates and would be equivalent to 13% of market cap.

Earnings momentum negative; no triggers for stocks to re-rate. The sector is trading at a 20% discount to book value (ex ISP) reflecting expectations of returns below the cost of equity. We think current prices are already discounting most of the bad news to come. Although we argue that some stocks are now cheap, valuation alone is not enough to overweight the sector given currently low visibility on the economic outlook.

Ratings and price targets (EUR)

	Price	Rating (old)	Rating (new)	Old PT	New PT	Change	Potential Return
BP	4.5	UW (V)	UW (V)	6.0	3.9	-36%	-15%
BPM	4.0	UW (V)	UW (V)	3.4	3.4	0%	-15%
CE	3.2	OW	N	6.3	3.6	-44%	10%
ISP	2.6	OW (V)	OW (V)	3.3	3.1	-7%	20%
MPS	1.2	N (V)	UW (V)	1.3	1.0	-25%	-18%
UBI	10.1	N	OW	11.7	11.6	-1%	15%
UC	1.4	N (V)	N (V)	1.9	1.5	-21%	6%

Source: HSBC estimates

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Investment thesis

- Core revenue to fall 6% on average in 2009, driven by lower net interest, and fee and commission margins; we expect this trend to continue into 2010 affecting revenue recovery (+3% on average)
- We expect government's capital support to cause slight net profit dilution of 4% on average; capital shortage less of an issue in Italy: cEUR9bn needed to push core T1 to 7% (13% of MV)
- Downgrading Credem and MPS; upgrading UBI to Overweight; ISP remains our preferred stock

In our previous report (*Italian banks – Surviving recession, part 2 – from recession to depression?* 1 December 2008) we anticipated a gloomy outlook for Italian banks in 2009, characterised by poor growth in net interest income, weak fees and commissions, no recovery in trading profits and rising provisions.

We estimated that operating profits would remain essentially flat for our universe in 2009 – a more resilient result than in the 1992 recession. We were, however, more pessimistic than consensus on credit quality.

What has changed?

Our recent visit to Italy not only supported our thesis, but provided evidence for even more severe net profit deterioration than we initially expected. As the recession gains pace and expectations of a stronger impact gather momentum, the worsening outlook for revenue growth is mostly driven by declining net interest income and fees and commissions as margin pressure grows in all product segments. Our analysis suggests that sector revenue is set to contract by 6% in 2009, driven by average y-o-y declines of 5% in net interest income and 8% in fees and commissions. We expect operating profit to fall 10%.

Lower liability yield cannot be offset with aggressive asset repricing. We calculate that declining interest rates will have a detrimental impact on margins as Italian banks will probably be unable to offset reduced liability yield with aggressive asset repricing. We believe margin pressure will grow over the course of 2009. In November the sector's deposit spread narrowed to 86bp m-o-m (137bp y-o-y) while the lending spread widened 74bp m-o-m (115bp y-o-y). Our recent conversations with the management of Italian banks suggest that this trend is set to continue throughout 2009 as competition for deposits accelerates; at the same time, it will be more difficult to widen lending spreads than in previous years given weaker credit demand and declining rates.

Declining fee and commission margins in all product segments. Margins on asset management commissions declined by 8bp y-o-y in H1 2008 versus a 10bp fall for traditional banking services and other fees (adjusted for Credem). This trend continued in Q3 2008 and we believe it will remain a feature of 2009 and 2010, driven by customers' decision to focus on low-margin products. We are increasingly worried about this trend as fees and commissions account for 37% of total average core revenue for our banks.

Estimating only slight net profit dilution for government capital support. We still have no indication about the timing of the government's intervention to strengthen the sector's capital requirement. The features of this instrument seem to have been largely decided but the political implications (ie, the obligation to provide credit to certain lending segments) probably have yet to be finalised. We nevertheless expect the plan to be made public over the next three to four weeks. Assuming an after-tax cost of 7.5% for this instrument, we calculate that the intervention will be slightly dilutive for net profits (we estimate 4% on average for 2009) as the banks would use the proceeds at lower returns.

Capital shortage less of an issue in Italy. Judging by the recent stock outperformance, we conclude that Italian banks are still more defensive than their European peers despite their perceived capital shortage. In our view this is not as negative as some may believe and we estimate that a cEUR9bn capital injection would push core Tier 1 to 7% in 2008. This would be equivalent to 14% of market capitalisation – not a dramatic impact in our view.

Performance relative to European banks and core T1

	1m	3m	YTD	Core T1 08e
BP	-3	-25	1	6.2%
BPM	2	18	5	6.4%
CE	-5	-12	-3	7.0%
ISP	6	34	9	5.7%
MPS	-18	9	-13	6.1%
UBI	2	11	8	6.8%
UC	-9	10	-10	6.6%

Source: HSBC estimates, Datastream

Reducing our core EPS estimates by 21% in 2009. Our analysis prompts us to cut our previous core EPS estimates by 21% for 2009 and 24% for 2010 on average. Our new forecasts are 27% below consensus. We now expect EPS to contract by 34% in 2009 compared to consensus of 4%.

Core EPS changes (EUR)

	2009e			2010e		
	Old	New	chg	Old	New	chg
BP	0.84	0.57	-32%	0.90	0.57	-36%
BPM	0.32	0.33	3%	0.37	0.33	-10%
CE	0.37	0.27	-26%	0.28	0.26	-8%
ISP	0.33	0.27	-20%	0.38	0.27	-29%
MPS	0.16	0.15	-9%	0.17	0.15	-11%
UBI	1.13	0.71	-37%	1.14	0.70	-39%
UC	0.22	0.16	-28%	0.24	0.16	-33%
AVG			**-21%**			**-24%**

Source: HSBC estimates

Downgrading Credem, MPS, while upgrading UBI to Overweight. ISP remains our preferred stock. We have cut our target prices by 18% on average. We are downgrading Credem from Overweight to Neutral, MPS from Neutral (V) to Underweight (V). Unicredit remains on a Neutral (V) rating. We are upgrading UBI from Neutral to Overweight.

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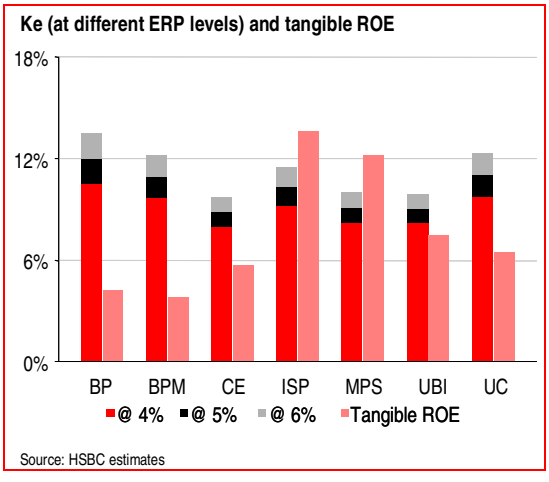
Valuation and risks

- Prices are already factoring in a much gloomier scenario than consensus envisages
- Sector rating is attractive, but valuation is not a key driver for overweighting the sector given current uncertainty about the economic outlook
- Our stance on the sector therefore remains unchanged as we believe that short-term earnings momentum is negative and we see no triggers for stocks to re-rate

On our new 2009 estimates the sector is trading at 0.8x PTBV with an average expected ROE of 8%. We believe, however, that the average is not entirely representative of the sector, given the large rating discrepancies among the stocks in our universe.



ISP is the sole stock which in our view justifies a premium rating to book value given its superior expected returns at different levels of equity risk premium (ERP), 4%, 5% and 6%. On the other hand, all the other stocks should be trading at a discount to their book value, except UBI, which we think should be in line.

According to our analysis Italian banks should be able to make a positive net profit contribution to book value between 2008 and 2010 even on our worse-than-consensus assumptions, thereby providing minimum core capital growth. This should also be the case even if the banks opt for government intervention, which we expect to dilute earnings significantly.

We therefore think that current prices are already discounting most of the bad news to come. We nonetheless maintain our prudent stance on the sector as we believe earnings momentum is still negative and we see no triggers for the stocks to re-rate. Although we argue that some stocks have become cheap, valuation alone does not justify overweighting the sector given currently low visibility on the economic outlook.

Target price and rating changes

We continue to base our price targets on book value adjusted for expected returns, earnings

growth and capital adequacy according to the coefficients listed in the next table. A premium to book value is attributed to those companies with low additional capital requirements and relatively higher earnings visibility/growth. A discount is attributed to those companies with a shortage of capital and constrained earnings growth. In both cases we also took into consideration expected ROE versus cost of capital. It should therefore come as no surprise that, despite our aggressive earnings downgrade, the change in some of the targets price has been less drastic.

Target prices

	PTBV	adj coeff	PTBV adj	Implied PT (EUR)
BP	0.4	-15%	0.4	3.9
BPM	0.6	-15%	0.5	3.4
CE	0.6	10%	0.7	3.6
ISP	1.5	20%	1.8	3.1
MPS	0.8	-18%	0.7	1.0
UBI	1.1	15%	1.2	11.6
UC	0.5	10%	0.6	1.5

Source: HSBC estimates

We cut our price targets by 18% on average as shown in the table below. We are downgrading Credem from Overweight to Neutral and MPS from Neutral (V) to Underweight (V). We are upgrading UBI from Neutral to Overweight. ISP remains our preferred stock.

Ratings and price targets (EUR)

	Rating (old)	Rating (new)	Old PT	New PT	Change	Potential Return
BP	UW (V)	UW (V)	6.0	3.9	-36%	-15%
BPM	UW (V)	UW (V)	3.4	3.4	0%	-15%
CE	OW	N	6.3	3.6	-44%	10%
ISP	OW (V)	OW (V)	3.3	3.1	-7%	20%
MPS	N (V)	UW (V)	1.3	1.0	-25%	-18%
UBI	N	OW	11.7	11.6	-1%	15%
UC	N (V)	N (V)	1.9	1.5	-21%	6%

Source: HSBC estimates

Risks to our ratings

All the stocks we cover are likely to be affected by the economic slowdown, which would hurt volumes, revenue and provisions. Other specific risks are detailed below.

Banco Popolare. Despite the looming recession, BPLodi's successful integration should continue, supporting future earnings growth. We believe new management may ultimately reduce exposure to Italease and accelerate its disposal, thereby improving capital adequacy. This potential positive impact is not reflected in our figures.

Banca Popolare di Milano. Management efforts could increase revenue growth, ultimately causing surprises on the upside. Also, despite expectations of deteriorating provisions, the company may prove more resilient than the sector average, based on its historically different market position and track record. Higher-than-expected pressure on fees and commissions, on the other hand, could further depress revenue growth.

Credito Emiliano. Newly acquired branches may take longer than we currently expect to turn around in a recession, slowing revenue growth. Provisions may also grow faster than we expect, given the different positioning of the new branches.

Intesasanpaolo. Earnings growth from CEE countries could disappoint, as could asset quality. We have factored in a scrip dividend, as the bank's capital adequacy is lower than that of peers. Disposals may be difficult to achieve even in 2009, limiting the amount of excess capital available.

Monte dei Paschi. A faster-than-expected integration of Antonveneta could lead to positive earnings surprises. On the other hand, the company may be not being able to complete its asset disposals on time, increasing the risk of additional capital requirements.

UBI. Higher-than-expected lending growth following the successful integration of Banca Lombarda. Fees and commissions could continue to decline as market conditions remain tough. Provisions growth may prove worse than expected, although the company has a lower risk profile than the sector average.

Unicredit. Earnings growth and asset-quality deterioration from CEE countries could prove disappointing. The ABS portfolio could result in additional provisions in 2009. Exposure to southern Italy (via the former Capitalia) may affect provisions in 2009-10. Goodwill impairment from recently acquired CEE banks could hit capital adequacy.

HSBC rating model

Under our research model, for stocks without a volatility indicator, the Neutral band is five percentage points above and below the hurdle rate for Italian stocks of 8.5%, hence a Neutral band of 3.5% to 13.5% potential total return implied by our target price.

For volatile ratings, defined as stocks having historical volatility (defined as the past month's average of the daily 365-day moving average volatilities) of over 40%, the Neutral band is ten percentage points above and below the hurdle rate for Italian stocks of 8.5%, hence a Neutral band of -1.5% to 18.5% potential total return implied by our target price

Ratings

	core EPS		Tang. BVPS		DPS			Tangible ROE			
	2008e	2009e	2008e	2009e	2007	2008e	2009e	2007	2008	2009	2010
BP	1.08	0.57	10.3	10.8	0.60	0.00	0.20	15%	15%	4%	4%
BPM	0.42	0.33	6.7	6.8	0.40	0.10	0.10	11%	5%	4%	5%
CE	0.49	0.27	5.4	4.8	0.40	0.20	0.10	17%	11%	6%	5%
ISP	0.33	0.27	1.7	1.9	0.38	0.00	0.05	29%	18%	14%	13%
MPS	0.22	0.15	1.5	1.1	0.21	0.08	0.05	20%	19%	12%	12%
UBI	0.90	0.71	9.4	9.6	0.95	0.40	0.40	15%	10%	7%	7%
UC	0.30	0.16	2.6	2.4	0.26	0.00	0.05	17%	12%	6%	6%
Average								**18%**	**13%**	**8%**	**8%**

	Price	core PE		PTBV		Yield		core EPS CAGR		
		2008e	2009e	2008e	2009e	2008e	2009e	08/10e	wev	Prem/disc
BP	4.5	4.2	8.0	0.4	0.4	0.0%	4.4%	-27%	0.1	223%
BPM	4.0	9.6	12.1	0.6	0.6	2.5%	2.5%	-11%	0.1	486%
CE	3.2	6.6	12.0	0.6	0.7	6.2%	3.1%	-27%	0.5	30%
ISP	2.6	7.7	9.6	1.5	1.3	0.0%	2.0%	-10%	1.4	4%
MPS	1.2	5.4	8.1	0.8	1.0	6.8%	4.2%	-17%	1.5	-46%
UBI	10.1	11.2	14.3	1.1	1.1	4.0%	4.0%	-12%	0.7	45%
UC	1.4	4.6	8.9	0.5	0.6	0.0%	3.6%	-27%	0.4	25%
Average		**7.0**	**10.4**	**0.8**	**0.8**			**-19%**		

Source: HSBC estimates

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As recession gains pace, pressure on revenue grows

- A low interest rate environment would be detrimental for Italian banks given the limited scope to reduce the liability spread (53bp) and the difficulty of aggressively repricing assets
- Pressure on fee and commission margin set to increase in all product segments, with a slower-than-expected recovery in 2010
- High sensitivity to spread and RWA changes (6% and 15% of net profit on average) make our estimates vulnerable to downgrade should the economic outlook worsen further

Worsening outlook as recession gathers pace

In our previous report (*Italian banks – Surviving recession, part 2*, 1 December) we offered a gloomy outlook for Italian banks in 2009, characterised by poor net interest income growth, weak fees and commissions, no recovery in trading profits and rising provisions.

Our recent visit to Italy not only supported our thesis but yielded evidence of even more severe net profit deterioration than we expected. As the recession gains pace and expectations of a more severe impact gather momentum, the worsening outlook for revenue growth is mostly driven by two elements: (1) worse-than-expected margin pressure in all product segments; and (2) a continued decline in assets under management (AUM). In this note we analyse in detail these two elements and the impact on our forecasts.

Reducing net interest margins as assets repricing may not offset pressure on deposit spread

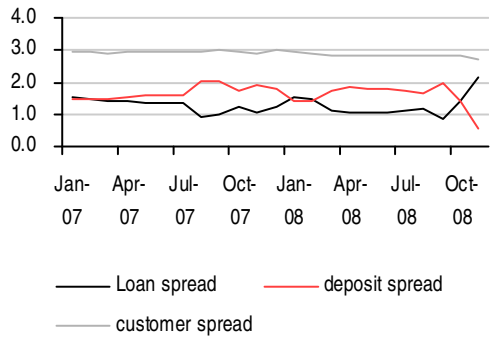
In 2008, Italian banks defended customer spread relatively successfully, posting a decline of 29bp against 83bp for the 3M Euribor. This was also reflected in our universe, which posted flat net interest margins (-1bp) in 9M 2008.

In light of consensus and our expectations about the BCE's easing policy, we calculate that margin pressure will worsen over 2009. Bank of Italy figures suggest that the deposit spread narrowed 83bp (m-o-m) in November, more than offsetting the 74bp rise in the lending spread.

Our recent conversations with the management of Italian banks suggest that this trend should continue throughout 2009 as competition for deposits will accelerate and it will be more difficult to widen lending spreads than in previous

years, given weaker credit demand and an environment of declining rates.

Italian banking sector – Spread trend (bp)



Source: Bank of Italy

With a deposit spread down to c50bp we would argue that a further rate cut would take a heavy toll on margins, ultimately leading to a severe impact on revenue. At the end of October, sight deposits accounted for 36% of the total and medium-term deposits for 24%, while the remainder were bonds. Assuming that sight and medium-term deposits are the categories most affected by a rate cut, we estimate that a 25bp cut in interest rates would have an 18% impact on this source of revenue.

Until now we believed Italian banks would be able to offset pressure on deposit spreads through a significant repricing of their asset base and, as a result, we factored flat spreads into our forecasts for 2009. On the basis of our analysis and our discussions with management we are now adopting a more negative view on net interest margins. Hence we have reduced our net interest margin estimates by an average of 17bp for 2009 and 15bp for 2010, as shown in the following table.

Net interest margin changes (bp)

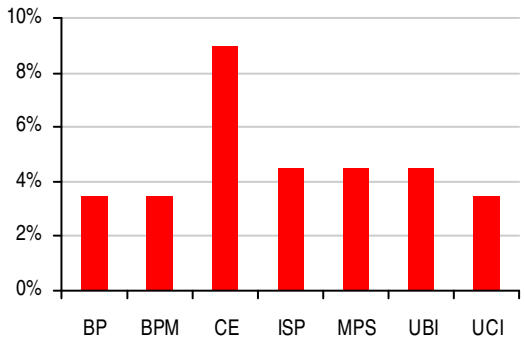
	2009e			2010e		
	Old	New	chg	Old	New	chg
BP	284	261	-23	285	261	-25
BPM	273	252	-21	276	252	-24
CE	264	248	-16	256	243	-13
ISP	319	301	-19	303	299	-5
MPS	333	327	-7	334	328	-7
UBI	114	103	-11	112	100	-12
UC	335	310	-25	332	310	-22
AVG			**-17**			**-15**

Source: HSBC estimates

Volume growth cannot offset spread decline

We have recently downgraded our lending estimates for the industry (*Italian banks, Main economic indicator*, 14 January) forecasting a 3% lending contraction for the industry in 2009 followed by 1% growth in 2010. However, we left our volume growth estimates for our universe unchanged, as we believe banks with a more diversified product mix and presence across Italy should be able to gain more market shares than smaller local players.

Lending growth 2010e/2008e (CAGR)



Source: HSBC estimates

As shown in the previous chart we expect marginal lending growth for our universe; the relatively high figures for Credem take into consideration the branches recently acquired from Citigroup and Unicredit. Our analysis suggests that net interest income is set to suffer in 2009 as volume growth will be unable to offset spread decline. This is a key issue, in our view, as net

interest income accounts for 60% of the total core revenue on average. Given still-limited visibility on volume growth we believe our estimates and consensus forecasts remain vulnerable to further downgrades over the course of the year should the recession prove longer than we currently expect.

Our sensitivity analysis suggests that, for every 1% change in RWAs (all other things being equal) net income would suffer an average 6% impact, while a 10bp change in the net interest margin would have a more detrimental impact of 15% on net profit. BP, BPM, Credem and Unicredit are the banks with the highest sensitivity, while ISP and UBI have the lowest.

Net interest income sensitivity (2009e)

	1% RWAs	10bp spread
BP	7%	19%
BPM	9%	23%
CE	6%	16%
ISP	5%	9%
MPS	4%	10%
UBI	3%	14%
UC	7%	16%
average	**6%**	**15%**

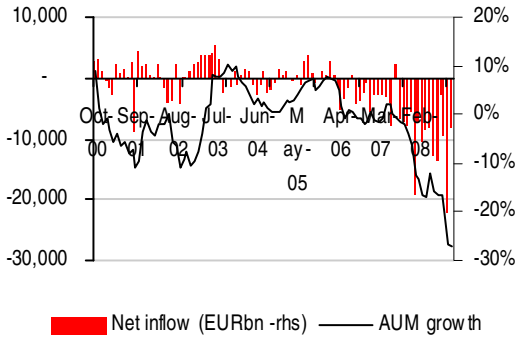
Source: HSBC estimates

Fee and commission margins to shrink in 2009, but recovery will be slow

In H1 2008, fees and commissions fell 11% y-o-y on average owing to a contraction in both asset management commissions (-19 y-o-y) and traditional banking services and other fees (-5% y-o-y). These trends worsened during Q3 and we expect them to persist throughout 2009 and 2010 owing to the combined effect of declining AUM and margin pressure on all product segments – rather than just a contraction in asset under management fees, as generally believed.

AUM posted a further EUR30.3bn outflow between September and November 2008, falling 12% from end-Q3 2008 levels (and 27% y-o-y). Considering the industry's performance over the past two years, we believe customers will continue to exit financial products. This trend is also supported, in our view, by the banks' need to capture additional liquidity to deleverage their balance sheets. Although we do not assume that banks will be able to fully capture these outflows, anecdotal evidence suggests that a large part of these assets are likely to be regained by the banks in the form of deposits.

Asset under management growth and outflows (EURbn)

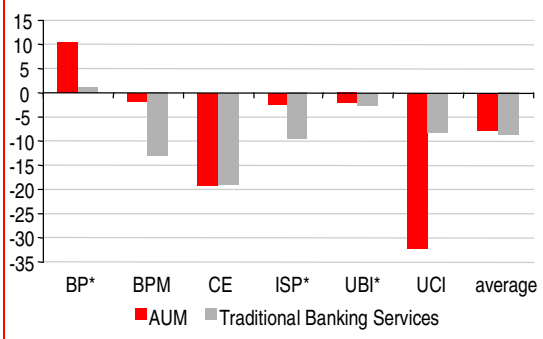


Source: Assogestioni

The fee and commission margin from asset management for our universe declined 8bp on average (annualised) in H1 2008 as customers opted for a more conservative product mix. At end-June 2008 the industry's equity funds accounted for 21% of total assets under management compared with 26% in June 2007. This downward trend continued in the following months and, as equity funds still accounted for 17% of the total at end-November, we believe ample room remains for a further reshuffle in the product mix towards more conservative products with lower margins. Hence margins should also drop in 2009.

More importantly, all our banks (except Banco Popolare) suffered margin compression on their traditional banking services commissions during H1 2008. We are increasingly worried about this trend, as this source of revenue accounts for 37% of total core revenue for all our banks. In our view this is a further indication of the difficulty of repricing products and/or selling more value-added products in this particular phase of the economic cycle.

Fee and commission margin changes H1 2008/H1 2007 (bp)



*Pro forma figures
Source: Company data

Between 2008 and 2010, we estimate that fee and commission margins will shrink by an average of 7bp in the asset management products segment and 5bp in traditional banking services and other commissions. As our forecast indicates, we estimate a mild recovery in 2010 (+1bp growth y-o-y) in traditional banking services commissions but remain negative on the asset management industry in Italy (-2bp growth y-o-y).

Fee and commission margin change y-o-y (bp)

	Asset management		Traditional banking serv. + others	
	2009e	2010e	2009e	2010e
BP	-7	-3	-3	0
BPM	-1	-4	-5	1
CE	-7	0	1	1
ISP	-3	-3	-11	3
UBI	-5	-1	-7	0
UC	-4	-1	-9	-1
average	**-5**	**-2**	**-6**	**1**

Source: HSBC estimates

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Government-supplied capital may be dilutive

- Visibility on timing still very low, although the instrument's structure seem to have been largely decided
- We calculate that BP, BPM, ISP and MPS are the banks with the highest capital needs (15% of MV on average)
- A high cost of capital (we estimate 7.5%) could prove 4% earnings dilutive; BP and BPM would be the banks most affected

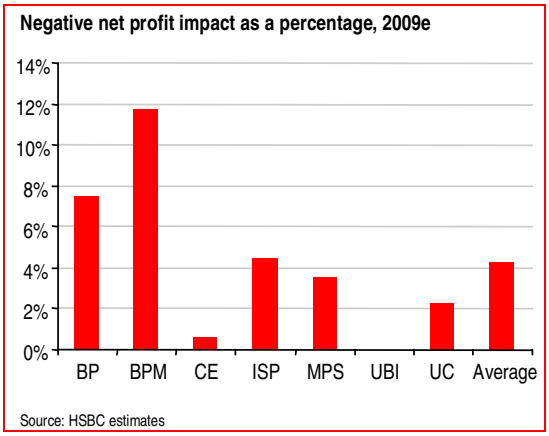
We still have no indication about the timing of the government intervention to provide additional capital to the banking sector. Although no formal announcements have been made, the features of the instrument seem to have been largely decided. These will focus on two elements.

The financials. The instrument will be a core T1 subordinated perpetual convertible bond with a variable coupon that is not tax deductible (see our 28 November note, *Italian banks, Government capital injection to support listed banks*). It seems that this instrument will guarantee an after-tax coupon of 7.5% (as reported by *Il sole 24 ore*, 18 January 2009), with a step-up mechanism and a premium in the event of reimbursement.

The politics. This is the most controversial issue as banks using this instrument will have to comply with certain criteria, such as to provide credit to both SMEs and households.

In this section we calculate the capital requirement for the banking sector, assuming an adequate core capital level of 7%. We estimate the sector core T1 at 6.3% for 2008 and 6.6% for 2009, implying that Italian banks would need an additional 70bp and 60bp, respectively, assuming a core T1 of 7% – or EUR9bn and EUR7bn based on 2008e and 2009e figures, respectively. This would translate into 13% of the sector's market capitalisation in 2008 and 8% in 2009. As shown in the table overleaf, BP, ISP and MPS would be the banks with the highest capital requirements. In this section we included 2008 figures, as we believe banks will present pro-forma numbers for 2008 if the government intervention is adopted in the next few weeks.

We calculate that this additional capital may be earnings dilutive as, based on an after-tax coupon of 7.5%, it would be below the expected returns made in 2009 (3%). It may also prove difficult to use these proceeds profitably at this point in the cycle given declining returns and the banks' currently high risk aversion. Hence, assuming a 3% after-tax return, we calculate that the use of the government instrument would take an average 4% toll on profits in 2009, ultimately penalising ROE as well.



We are not diluting our EPS figures as we believe the government instrument may not be subject to mandatory conversion; equally we are not calculating a reimbursement premium either. We expect it to have a clause that will allow the banks to reimburse the debt after a number of years. Our view is based on recent press articles (as published by *Il sole 24 ore*, 18 January 2009) indicating that the government intervention should be temporary and should maximise returns for the state. This leads us to believe that the government will be more interested in capital and interest repayments than in playing an active role by becoming a shareholder in the listed banks.

Our calculation suggests that BP and BPM would be the banks with a highest earnings dilution under our base-case scenario, while UBI and Credem would have a nil impact as these banks have no need for additional capital.

Capital requirement with core T1 @ 7% (EURbn)

	Core T1 (bp)		additional cap need		cap need in % MV	
	2008e	2009e	2008e	2009e	2008e	2009e
BP	78	56	637	476	22%	16%
BPM	62	69	244	278	15%	17%
CE	3	6	5	13	0%	1%
ISP	127	78	4,937	3,147	16%	10%
MPS	88	54	1,125	708	14%	9%
UBI						
UC	38	21	2,060	1,152	10%	6%
Weight. Avg.	**70**	**45**	**9,008**	**5,772**	**13%**	**8%**

Source: HSBC estimates

HSBC

Core 2009e EPS forecasts cut 21% on average

- We expect core revenue to decline by 6% and operating profit by 9% in 2009
- We cut our core EPS estimates by 21% in 2009 and 24% in 2010 on average; we now expect EPS to fall 34% in 2009 and post no growth in 2010.
- Unrealistic consensus: 4% y-o-y decline in core EPS in 2009 against HSBC's forecast of a 34% fall; we are now 27% below consensus

As the recession is gathering pace worldwide and its effects are proving more severe than previously expected, we once again cut our earnings estimates. On average, we are downgrading core EPS by 21% for 2009 and 24% for 2010.

Core EPS estimates changes (EUR)

	2009e			2010e		
	Old	New	chg	Old	New	chg
BP	0.84	0.57	-32%	0.90	0.57	-36%
BPM	0.32	0.33	3%	0.37	0.33	-10%
CE	0.37	0.27	-26%	0.28	0.26	-8%
ISP	0.33	0.27	-20%	0.38	0.27	-29%
MPS	0.16	0.15	-9%	0.17	0.15	-11%
UBI	1.13	0.71	-37%	1.14	0.70	-39%
UC	0.22	0.16	-28%	0.24	0.16	-33%
AVG			**-21%**			**-24%**

Source: HSBC estimates

Our estimate changes are detailed in the table on page 16 and are based on the analysis described in the previous pages. Our downgrade is based on expectations of reduced revenue growth attributable largely to the following:

- **Lower net interest margins**. Our economists forecast that ECB will continue its easing policy, cutting the base rate from 4.25% (September 2008) to 1.25% by the end of 2009. This, coupled with the difficulty of widening asset spread proportionately – as suggested by the latest Bank of Italy data – should increase pressure on customer spread. We therefore factored in lower net interest margins for our banks.
- **Lower AUM**. Admittedly, it is difficult to forecast stocks of AUM by 2010 given currently low market visibility. However, for the sake of prudence, we have further reduced our AUM forecasts for all companies. On average we expect growth at a CAGR of -4% between 2008 and 2010.
- **Lower fee and commission margin**. Fees and commissions from asset management declined on average 12 bp (annualised) in H1 2008. This trend continued in Q3 2008 and our conversations with management support our view that it will continue throughout 2009.

Based on our new estimates, we now expect net income to be 39% lower than our previous forecasts; our core EPS for our universe is now 27% below consensus for 2009. We are more pessimistic on all the stocks in our universe.

EPS- HSBC estimates versus consensus (EUR)

	2008e			2009e			growth 09/08	
	HSBC	IBES	diff.	HSBC	IBES	diff.	HSBC	IBES
BP	1.08	0.80	34%	0.57	0.83	-31%	-47%	3%
BPM	0.42	0.47	-11%	0.33	0.50	-33%	-21%	6%
CE	0.49	0.55	-11%	0.27	0.41	-34%	-45%	-25%
ISP	0.33	0.35	-5%	0.27	0.32	-17%	-20%	-8%
MPS	0.22	0.13	65%	0.15	0.14	5%	-34%	4%
UBI	0.90	1.21	-25%	0.71	1.11	-36%	-22%	-8%
UC	0.30	0.30	2%	0.16	0.29	-44%	-48%	-4%
AVG			**7%**			**-27%**	**-34%**	**-4%**

Source: HSBC estimates, IBES

The gap between our forecasts and consensus still stands at 27% in 2009. Although our forecasts for a 34% drop in core EPS may be considered too pessimistic, we are puzzled to see consensus assuming nearly flat core EPS growth in 2009 – at a time when we are expecting one of the worst recessions in 50 years.

HSBC

Estimate changes in detail (EURm)

	2008e			2009e			2010e			growth 09/08	
	Old	New	chg	Old	New	chg	Old	New	chg	Old	New
Banco Popolare											
Revenue	4105	4044	-1%	3860	3576	-7%	4014	3671	-9%	-6%	-12%
Operating costs	-2340	-2340	0%	-2292	-2292	0%	-2339	-2339	0%	-2%	-2%
Operating income	1765	1703	-3%	1568	1284	-18%	1675	1332	-20%	-11%	-25%
LLProvisions	-556	-556	0%	-696	-696	0%	-766	-766	0%	25%	25%
Net profit	867	831	-4%	457	285	-38%	500	292	-42%	-47%	-66%
EPS Core (EUR)	1.13	1.08	-5%	0.84	0.57	-32%	0.90	0.57	-36%	-26%	-47%
BPM											
Revenue	1703	1696	0%	1666	1670	0%	1742	1726	-1%	-2%	-2%
Operating costs	-1161	-1161	0%	-1181	-1181	0%	-1197	-1197	0%	2%	2%
Operating income	543	535	-1%	484	489	1%	545	529	-3%	-11%	-9%
LLProvisions	-184	-184	0%	-234	-234	0%	-268	-279	4%	27%	27%
Net profit	193	152	-22%	133	106	-20%	150	135	-10%	-31%	-30%
EPS Core (EUR)	0.47	0.42	-11%	0.32	0.33	3%	0.37	0.33	-10%	-31%	-21%
Credito Emiliano											
Revenue	986	989	0%	998	940	-6%	1030	976	-5%	1%	-5%
Operating costs	-686	-686	0%	-725	-711	-2%	-768	-734	-5%	6%	4%
Operating income	299	302	1%	274	229	-16%	261	242	-7%	-9%	-24%
LLProvisions	-86	-86	0%	-107	-107	0%	-123	-123	0%	23%	23%
Net profit	159	161	2%	121	89	-26%	94	86	-8%	-23%	-44%
EPS Core (EUR)	0.48	0.49	2%	0.37	0.27	-26%	0.28	0.26	-8%	-24%	-45%
Intesasanpaolo											
Revenue	18828	18614	-1%	19283	18060	-1%	20507	18504	-10%	2%	-3%
Operating costs	-10624	-10624	0%	-10450	-10450	0%	-10375	-10375	0%	-2%	-2%
Operating income	8204	7990	-3%	8833	7610	-14%	10132	8129	-20%	8%	-5%
LLProvisions	-1998	-1998	0%	-2993	-2993	0%	-3545	-3545	0%	50%	50%
Net profit	4508	4359	-3%	4002	3156	-21%	4652	3260	-30%	-11%	-28%
EPS Core (EUR)	0.34	0.33	-3%	0.33	0.27	-20%	0.38	0.27	-29%	-3%	-20%
Monte Paschi											
Revenue	5070	5800	14%	5677	6293	11%	6012	6619	10%	12%	9%
Operating costs	-3092	-3660	18%	-3131	-3954	26%	-3200	-4043	26%	1%	8%
Operating income	1977	2140	8%	2546	2339	-8%	2812	2576	-8%	29%	9%
LLProvisions	-842	-734	-13%	-1002	-1068	7%	-1172	-1250	7%	19%	46%
Net profit	1112	1329	20%	1066	893	-16%	1139	948	-17%	-4%	-33%
EPS Core (EUR)	0.17	0.22	30%	0.16	0.15	-9%	0.17	0.15	-11%	-5%	-34%
UBI											
Revenue	4324	4172	-4%	4526	4092	-10%	4683	4178	-11%	5%	-2%
Operating costs	-2691	-2606	-1%	-2731	-2637	-9%	-2777	-2681	-11%	2%	1%
Operating income	1633	1566	-4%	1795	1455	-19%	1906	1497	-21%	10%	-7%
LLProvisions	-384	-480	25%	-486	-557	15%	-582	-613	5%	26%	16%
Net profit	700	591	-16%	702	452	-36%	731	448	-39%	0%	-24%
EPS Core (EUR)	1.09	0.90	-17%	1.13	0.71	-37%	1.14	0.70	-39%	4%	-22%
Unicredit											
Revenue	27485	27494	0%	27731	26782	-3%	29305	27585	-6%	1%	-3%
Operating costs	-17139	-16755	-2%	-17517	-16695	-5%	-17917	-16801	-6%	2%	0%
Operating income	10347	10738	4%	10215	10087	-1%	11388	10784	-5%	-1%	-6%
LLProvisions	-3822	-3822	0%	-4447	-5449	23%	-5057	-6159	22%	16%	43%
Net profit	4253	4375	3%	3259	2295	-30%	3642	2384	-35%	-23%	-48%
EPS Core (EUR)	0.29	0.30	7%	0.22	0.16	-28%	0.24	0.16	-33%	-23%	-48%

Source: HSBC estimates

HSBC

Company profiles

HSBC

Financials & valuation: Banco Popolare

Underweight (V)

Financial statements

Year to	12/2007a	12/2008e	12/2009e	12/2010e
P&L summary (EURm)				
Net interest income	2,264	2,426	2,207	2,273
Net fees/commissions	1,210	1,085	950	942
Trading profits	624	218	120	138
Other income	210	315	299	317
Total income	4,308	4,044	3,576	3,671
Operating expense	-2,425	-2,340	-2,292	-2,339
Bad debt charge	-546	-556	-696	-766
Other	-675	-227	-118	-83
HSBC PBT	662	920	471	483
Exceptionals	629	500	0	0
PBT	1,291	1,420	471	483
Taxation	-607	-540	-169	-174
Minorities + preferences	-49	-50	-16	-17
Attributable profit	635	831	285	292
HSBC attributable profit	6	331	285	292
Balance sheet summary (EURm)				
Ordinary equity	10,672	12,233	12,268	12,554
HSBC ordinary equity	10,672	12,233	12,268	12,554
Customer loans	84,551	79,478	81,862	85,137
Debt securities holdings	0	0	0	0
Customer deposits	93,229	92,297	95,066	98,868
Interest earning assets	107,608	109,641	108,656	112,265
Total assets	128,393	124,491	127,891	132,060
Capital (%)				
RWA (EURm)	92,346	82,164	84,408	87,160
Core tier 1	4.0	6.2	6.4	6.9
Total tier 1	5.2	7.6	7.8	8.2
Total capital	8.7	11.2	11.3	11.6

Ratio, growth & per share analysis

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Year-on-year % change				
Total income	5.8	-6.1	-11.6	2.7
Operating expense	3.0	-3.5	-2.1	2.1
Pre-provision profit	9.7	-9.5	-24.6	3.7
EPS				
HSBC EPS	-99.0	5413.9	-13.9	2.5
DPS		-100.0		0.0
NAV (including goodwill)	-5.3	14.6	0.3	2.3
Ratios (%)				
Cost/income ratio	56.3	57.9	64.1	63.7
Bad debt charge	0.7	0.7	0.9	0.9
Customer loans/deposits	90.7	86.1	86.1	86.1
NPL/loan	2.4	3.0	3.9	4.9
NPL/RWA	2.2	2.8	3.7	4.7
Provision to risk assets/RWA	-1.2	-1.9	-2.3	-2.4
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	-56.2	-68.9	-63.3	-52.6
ROE (including goodwill)	0.1	2.9	2.3	2.4
Per share data (EUR)				
EPS reported (fully diluted)	0.99	1.30	0.44	0.46
HSBC EPS (fully diluted)	0.01	0.52	0.44	0.46
DPS	0.60	0.00	0.20	0.20
NAV	6.62	10.26	10.76	11.62
NAV (including goodwill)	16.66	19.10	19.15	19.60

Core profitability (% RWAs) and leverage

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Net interest income	2.5	2.8	2.7	2.6
Trading profits	0.7	0.3	0.1	0.2
Other income	0.2	0.4	0.4	0.4
Operating expense	-2.6	-2.7	-2.8	-2.7
Pre-provision profit	2.0	2.0	1.5	1.6
Bad debt charge	-0.6	-0.6	-0.8	-0.9
HSBC attributable profit	0.0	0.4	0.3	0.3
Leverage (x)	8.2	7.6	6.8	6.9
Return on average tier 1	0.1	5.3	4.3	4.1

Valuation data

Year to	12/2007a	12/2008e	12/2009e	12/2010e
PE*	484.6	8.8	10.2	10.0
Pre-provision multiple	1.5	1.7	2.3	2.2
P/NAV	0.7	0.4	0.4	0.4
Equity cash flow yield (%)	-222.1	35.9	4.4	3.4
Dividend yield (%)	13.2	0.0	4.4	4.4

Note: * = Based on HSBC EPS (fully diluted)

Issuer information

Share price (EUR)	4.54	Target price (EUR)	3.90	Potent'l tot rtn (%)	-14.1
Reuters (Equity)	BAPO.MI		Bloomberg (Equity)		BP IM
Market cap (USDm)	3,845		Market cap (EURm)		2,908
Free float (%)	100				
Country	Italy		Sector		Commercial Banks
Analyst	Carlo Digrandi		Contact		44 20 7991 6843

Notes: price at close of 28 Jan 2009

HSBC

Financials & valuation: Banca Popolare di Milano

Underweight (V)

Financial statements

Year to	12/2007a	12/2008e	12/2009e	12/2010e
P&L summary (EURm)				
Net interest income	1,028	1,052	1,018	1,058
Net fees/commissions	586	533	511	517
Trading profits	-67	-173	-104	-99
Other income	304	284	245	250
Total income	1,851	1,696	1,670	1,726
Operating expense	-1,136	-1,161	-1,181	-1,197
Bad debt charge	-127	-184	-234	-279
Other	-32	-25	-21	-17
HSBC PBT	555	326	234	233
Exceptionals	0	-34	-50	0
PBT	556	292	184	233
Taxation	-220	-134	-73	-93
Minorities + preferences	-12	-6	-4	-5
Attributable profit	324	152	106	135
HSBC attributable profit	324	172	136	135
Balance sheet summary (EURm)				
Ordinary equity	3,475	3,426	3,457	3,516
HSBC ordinary equity	3,475	3,426	3,457	3,516
Customer loans	29,767	32,743	33,726	35,075
Debt securities holdings	0	0	0	0
Customer deposits	21,616	22,048	22,710	23,391
Interest earning assets	38,906	42,145	44,313	45,830
Total assets	43,627	46,890	48,087	49,989
Capital (%)				
RWA (EURm)	35,009	39,388	40,393	41,991
Core tier 1	6.8	6.4	6.3	6.2
Total tier 1	7.2	7.5	7.5	7.3
Total capital	9.4	9.5	9.4	9.2

Ratio, growth & per share analysis

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Year-on-year % change				
Total income	2.7	-8.4	-1.5	3.4
Operating expense	1.3	2.2	1.8	1.3
Pre-provision profit	4.9	-25.1	-8.6	8.3
EPS				
HSBC EPS	-14.1	-46.8	-20.7	-1.0
DPS	14.3	-75.0	0.0	0.0
NAV (including goodwill)	3.5	-1.4	0.9	1.7
Ratios (%)				
Cost/income ratio	61.4	68.4	70.7	69.3
Bad debt charge	0.5	0.6	0.7	0.8
Customer loans/deposits	137.7	148.5	148.5	149.9
NPL/loan	1.5	1.9	2.6	3.1
NPL/RWA	1.3	1.6	2.2	2.7
Provision to risk assets/RWA	0.9	1.0	1.1	1.4
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	71.1	61.3	51.5	51.1
ROE (including goodwill)	9.5	5.0	4.0	3.9
Per share data (EUR)				
EPS reported (fully diluted)	0.78	0.37	0.26	0.33
HSBC EPS (fully diluted)	0.78	0.41	0.33	0.33
DPS	0.40	0.10	0.10	0.10
NAV	6.81	6.70	6.77	6.91
NAV (including goodwill)	8.37	8.26	8.33	8.47

Core profitability (% RWAs) and leverage

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Net interest income	3.1	2.8	2.6	2.6
Trading profits	-0.2	-0.5	-0.3	-0.2
Other income	0.9	0.8	0.6	0.6
Operating expense	-3.4	-3.1	-3.0	-2.9
Pre-provision profit	2.1	1.4	1.2	1.3
Bad debt charge	-0.4	-0.5	-0.6	-0.7
HSBC attributable profit	1.0	0.5	0.3	0.3
Leverage (x)	9.7	10.8	11.6	11.8
Return on average tier 1	12.8	5.8	4.5	4.4

Valuation data

Year to	12/2007a	12/2008e	12/2009e	12/2010e
PE*	5.1	9.7	12.2	12.3
Pre-provision multiple	2.3	3.1	3.4	3.1
P/NAV	0.6	0.6	0.6	0.6
Equity cash flow yield (%)	4.7	-8.1	4.0	1.4
Dividend yield (%)	10.0	2.5	2.5	2.5

Note: * = Based on HSBC EPS (fully diluted)

Issuer information

Share price (EUR)	4.00	Target price (EUR)	3.40
Potent'l tot rtn (%)	-15.1		
Reuters (Equity)	PMII.MI	Bloomberg (Equity)	BPM IM
Market cap (USDm)	2,198	Market cap (EURm)	1,662
Free float (%)	98		
Country	Italy	Sector	COMMERCIAL BANKS
Analyst	Carlo Digrandi	Contact	44 20 7991 6843

Notes: price at close of 28 Jan 2009

HSBC

Financials & valuation: Credito Emiliano

Neutral

Financial statements

Year to	12/2007a	12/2008e	12/2009e	12/2010e
P&L summary (EURm)				
Net interest income	491	515	535	557
Net fees/commissions	377	260	251	255
Trading profits	-171	-174	-176	-179
Other income	365	385	388	396
Total income	1,062	986	998	1,030
Operating expense	-662	-686	-725	-768
Bad debt charge	-53	-86	-107	-123
Other	-13	-2	2	4
HSBC PBT	334	211	169	142
Exceptionals	-7	-2	0	0
PBT	327	209	169	142
Taxation	-78	-50	-47	-48
Minorities + preferences	0	0	0	0
Attributable profit	250	159	121	94
HSBC attributable profit	254	160	121	94
Balance sheet summary (EURm)				
Ordinary equity	1,543	1,888	1,945	1,965
HSBC ordinary equity	1,543	1,888	1,945	1,965
Customer loans	15,763	17,497	19,247	20,786
Debt securities holdings	5,442	8,000	8,640	9,331
Customer deposits	11,240	11,577	11,924	12,401
Interest earning assets	23,895	27,261	31,000	33,569
Total assets	26,233	31,098	33,781	36,336
Capital (%)				
RWA (EURm)	16,221	19,659	20,268	21,802
Core tier 1	8.1	7.0	7.0	6.6
Total tier 1	8.1	7.0	7.0	6.6
Total capital	9.3	8.0	8.0	7.5

Ratio, growth & per share analysis

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Year-on-year % change				
Total income	-0.3	-7.2	1.3	3.1
Operating expense	2.7	3.7	5.6	6.0
Pre-provision profit	-5.0	-25.3	-8.5	-4.6
EPS				
HSBC EPS	8.2	-46.5	-24.0	-22.8
DPS	14.3	-37.5	12.0	7.1
NAV (including goodwill)	10.3	4.0	3.0	1.0
Ratios (%)				
Cost/income ratio	62.3	69.6	72.6	74.6
Bad debt charge	0.4	0.5	0.6	0.6
Customer loans/deposits	140.2	151.1	161.4	167.6
NPL/loan	0.8	0.9	1.1	1.3
NPL/RWA	0.7	0.8	1.0	1.3
Provision to risk assets/RWA	0.5	0.6	0.9	1.0
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	63.6	75.9	89.5	80.2
ROE (including goodwill)	17.4	9.3	6.3	4.8
Per share data (EUR)				
EPS reported (fully diluted)	0.88	0.48	0.37	0.28
HSBC EPS (fully diluted)	0.90	0.48	0.37	0.28
DPS	0.40	0.25	0.28	0.30
NAV	5.26	4.66	4.81	4.87
NAV (including goodwill)	5.46	5.68	5.85	5.91

Core profitability (% RWAs) and leverage

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Net interest income	3.1	2.9	2.7	2.6
Trading profits	-1.1	-1.0	-0.9	-0.9
Other income	2.3	2.1	1.9	1.9
Operating expense	-4.2	-3.8	-3.6	-3.7
Pre-provision profit	2.6	1.7	1.4	1.2
Bad debt charge	-0.3	-0.5	-0.5	-0.6
HSBC attributable profit	1.6	0.9	0.6	0.4
Leverage (x)	10.7	10.5	10.4	10.8
Return on average tier 1	19.4	11.7	8.6	6.5

Valuation data

Year to	12/2007a	12/2008e	12/2009e	12/2010e
PE*	3.6	6.7	8.8	11.4
Pre-provision multiple	2.3	3.6	3.9	4.1
P/NAV	0.6	0.7	0.7	0.7
Equity cash flow yield (%)	15.4	-7.5	7.3	-1.3
Dividend yield (%)	12.4	7.7	8.7	9.3

Note: * = Based on HSBC EPS (fully diluted)

Issuer information

Share price (EUR)	3.23	Target price (EUR)	3.60
Potent'l tot rtn (%)	10%		
Reuters (Equity)	EMBI.MI	Bloomberg (Equity)	CE IM
Market cap (USDm)	1,420	Market cap (EURm)	1,074
Free float (%)	28		
Country	Italy	Sector	COMMERCIAL BANKS
Analyst	Carlo Digrandi	Contact	44 20 7991 6843

Notes: price at close of 28 Jan 2009

HSBC

Financials & valuation: Intesasanpaolo

Overweight (V)

Financial statements

Year to	12/2007a	12/2008e	12/2009e	12/2010e
P&L summary (EURm)				
Net interest income	10,277	12,192	12,139	12,588
Net fees/commissions	5,944	5,834	5,342	5,291
Trading profits	447	72	61	71
Other income	527	516	518	554
Total income	17,195	18,614	18,060	18,504
Operating expense	-10,213	-10,624	-10,450	-10,375
Bad debt charge	-1,045	-1,998	-2,993	-3,545
Other	-338	130	243	307
HSBC PBT	5,599	6,122	4,861	4,891
Exceptionals	3,306	150	-300	-200
PBT	8,905	6,272	4,561	4,691
Taxation	-1,549	-1,756	-1,323	-1,360
Minorities + preferences	-106	-157	-82	-70
Attributable profit	7,250	4,359	3,156	3,260
HSBC attributable profit	3,944	4,209	3,456	3,460
Balance sheet summary (EURm)				
Ordinary equity	51,558	51,475	54,107	56,178
HSBC ordinary equity	51,558	51,475	54,107	56,178
Customer loans	335,273	391,224	406,873	427,217
Debt securities holdings	114,964	114,213	119,924	125,920
Customer deposits	346,483	383,556	402,733	422,870
Interest earning assets	0	0	0	0
Total assets	572,902	638,646	662,043	691,173
Capital (%)				
RWA (EURm)	371,532	389,574	403,846	421,616
Core tier 1	5.9	5.7	6.2	6.5
Total tier 1	6.5	6.6	7.1	7.3
Total capital	9.6	10.4	10.7	10.8

Ratio, growth & per share analysis

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Year-on-year % change				
Total income	-6.2	8.3	-3.0	2.5
Operating expense	-6.3	4.0	-1.6	-0.7
Pre-provision profit	-5.9	14.4	-4.8	6.8
EPS				
HSBC EPS	-7.7	6.7	-17.9	0.1
DPS	72.7	-100.0		100.0
NAV (including goodwill)	-7.9	-0.2	5.1	3.8
Ratios (%)				
Cost/income ratio	59.4	57.1	57.9	56.1
Bad debt charge	0.3	0.6	0.8	0.8
Customer loans/deposits	96.8	102.0	101.0	101.0
NPL/loan	3.0	5.7	6.3	7.1
NPL/RWA	2.8	5.8	6.5	7.5
Provision to risk assets/RWA	2.0	2.8	2.6	3.1
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	71.5	48.1	40.6	41.1
ROE (including goodwill)	7.3	8.2	6.5	6.3
Per share data (EUR)				
EPS reported (fully diluted)	0.57	0.34	0.25	0.26
HSBC EPS (fully diluted)	0.31	0.33	0.27	0.27
DPS	0.38	0.00	0.05	0.10
NAV	2.02	1.71	1.92	2.08
NAV (including goodwill)	4.03	4.03	4.23	4.40

Core profitability (% RWAs) and leverage

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Net interest income	2.8	3.2	3.1	3.1
Trading profits	0.1	0.0	0.0	0.0
Other income	0.1	0.1	0.1	0.1
Operating expense	-2.8	-2.8	-2.6	-2.5
Pre-provision profit	1.9	2.1	1.9	2.0
Bad debt charge	-0.3	-0.5	-0.8	-0.9
HSBC attributable profit	1.1	1.1	0.9	0.8
Leverage (x)	6.7	7.4	7.5	7.5
Return on average tier 1	16.2	16.3	12.0	11.2

Valuation data

Year to	12/2007a	12/2008e	12/2009e	12/2010e
PE*	8.2	7.6	9.3	9.3
Pre-provision multiple	4.6	4.0	4.2	4.0
P/NAV	1.2	1.5	1.3	1.2
Equity cash flow yield (%)	8.2	9.4	7.8	7.0
Dividend yield (%)	15.1	0.0	2.0	4.0

Note: * = Based on HSBC EPS (fully diluted)

Issuer information

Share price (EUR)	2.52	Target price (EUR)	3.10
Potent'l tot rtn (%)	23.3		
Reuters (Equity)	ISP.MI	Bloomberg (Equity)	ISP IM
Market cap (USDm)	41,635	Market cap (EURm)	31,484
Free float (%)	70		
Country	Italy	Sector	COMMERCIAL BANKS
Analyst	Carlo Digrandi	Contact	44 20 7991 6843

Notes: price at close of 28 Jan 2009

Financials & valuation: Monte dei Paschi

Underweight (V)

Financial statements

Year to	12/2007a	12/2008e	12/2009e	12/2010e
P&L summary (EURm)				
Net interest income	2,914	3,859	4,282	4,488
Net fees/commissions	1,515	1,667	1,700	1,751
Trading profits	-170	-229	-287	-258
Other income	746	503	598	638
Total income	5,005	5,800	6,293	6,619
Operating expense	-3,127	-3,660	-3,954	-4,043
Bad debt charge	-614	-734	-1,068	-1,250
Other	5	122	164	182
HSBC PBT	1,270	1,528	1,435	1,508
Exceptionals	735	410	-80	-70
PBT	2,005	1,938	1,355	1,438
Taxation	-552	-581	-447	-475
Minorities + preferences	-16	-27	-15	-16
Attributable profit	1,438	1,329	893	948
HSBC attributable profit	997	1,099	973	1,018
Balance sheet summary (EURm)				
Ordinary equity	8,579	8,348	15,212	15,534
HSBC ordinary equity	8,579	8,348	15,212	15,534
Customer loans	106,322	146,725	152,594	160,224
Debt securities holdings	31,111	28,000	28,560	29,702
Customer deposits	60,437	78,568	81,710	84,979
Interest earning assets	143,426	170,863	192,502	200,243
Total assets	161,984	205,519	218,506	228,221
Capital (%)				
RWA (EURm)	113,385	127,209	131,104	136,933
Core tier 1	5.8	6.1	6.5	6.4
Total tier 1	6.1	6.4	6.7	6.7
Total capital	8.4	10.6	11.0	10.8

Ratio, growth & per share analysis

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Year-on-year % change				
Total income	-0.4	15.9	8.5	5.2
Operating expense	0.2	17.1	8.0	2.2
Pre-provision profit	-1.4	13.9	9.3	10.1
EPS				
HSBC EPS	10.4	-44.8	-11.5	4.6
DPS	23.5	-61.9	-37.5	20.0
NAV (including goodwill)	1.5	-51.3	82.2	2.1
Ratios (%)				
Cost/income ratio	62.5	63.1	62.8	61.1
Bad debt charge	0.6	0.6	0.7	0.8
Customer loans/deposits	175.9	186.7	186.7	188.5
NPL/loan	3.8	5.2	5.8	6.5
NPL/RWA	3.7	6.2	6.9	7.8
Provision to risk assets/RWA	1.9	3.6	3.3	3.8
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	51.6	58.3	48.1	48.1
ROE (including goodwill)	12.2	13.0	7.6	6.7
Per share data (EUR)				
EPS reported (fully diluted)	0.43	0.20	0.13	0.14
HSBC EPS (fully diluted)	0.30	0.17	0.15	0.15
DPS	0.21	0.08	0.05	0.06
NAV	2.24	0.11	1.14	1.19
NAV (including goodwill)	2.57	1.25	2.28	2.33

Core profitability (% RWAs) and leverage

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Net interest income	2.7	3.2	3.3	3.4
Trading profits	-0.2	-0.2	-0.2	-0.2
Other income	0.7	0.4	0.5	0.5
Operating expense	-2.9	-3.0	-3.1	-3.1
Pre-provision profit	1.8	1.8	1.8	2.0
Bad debt charge	-0.6	-0.6	-0.8	-0.9
HSBC attributable profit	0.9	0.9	0.8	0.8
Leverage (x)	13.1	14.2	10.1	8.7
Return on average tier 1	14.4	13.5	11.0	11.1

Valuation data

Year to	12/2007a	12/2008e	12/2009e	12/2010e
PE*	4.0	7.2	8.1	7.7
Pre-provision multiple	2.1	3.7	3.4	3.1
P/NAV	0.5	10.5	1.0	1.0
Equity cash flow yield (%)	1.2	2.0	10.8	9.4
Dividend yield (%)	17.8	6.8	4.2	5.1

Note: * = Based on HSBC EPS (fully diluted)

Issuer information

Share price (EUR)	1.18	Target price (EUR)	1.00
Potent'l tot rtn (%)	-15.4		
Reuters (Equity)	BMPS.MI	Bloomberg (Equity)	BMPS IM
Market cap (USDm)	8,586	Market cap (EURm)	6,493
Free float (%)	30		
Country	Italy	Sector	COMMERCIAL BANKS
Analyst	Carlo Digrandi	Contact	44 20 7991 6843

Notes: price at close of 28 Jan 2009

HSBC

Financials & valuation: UBI

Overweight

Financial statements

Year to	12/2006a	12/2007e	12/2008e	12/2009e
P&L summary (EURm)				
Net interest income	2,513	2,690	3,005	2,905
Net fees/commissions	1,326	1,335	1,166	1,044
Trading profits	243	102	-31	92
Other income	268	312	194	184
Total income	4,350	4,440	4,335	4,225
Operating expense	-2,444	-2,558	-2,552	-2,582
Bad debt charge	-239	-346	-384	-557
Other	-32	-47	-82	-70
HSBC PBT	1,635	1,489	1,316	1,016
Exceptionals	74	165	10	0
PBT	1,709	1,654	1,326	1,016
Taxation	-670	-606	-477	-386
Minorities + preferences	-89	-107	-86	-66
Attributable profit	951	940	763	564
HSBC attributable profit	876	776	753	564
Balance sheet summary (EURm)				
Ordinary equity	11,582	11,790	11,710	11,688
HSBC ordinary equity	11,582	11,790	11,710	11,688
Customer loans	83,063	92,729	99,220	103,189
Debt securities holdings	0	0	0	0
Customer deposits	48,119	49,696	51,684	53,234
Interest earning assets	104,797	106,939	108,572	111,957
Total assets	117,312	121,469	122,599	125,965
Capital (%)				
RWA (EURm)	91,338	97,912	98,823	101,536
Core tier 1	0.0	7.0	7.0	7.0
Total tier 1	7.0	7.5	7.6	7.6
Total capital	10.1	10.1	10.3	10.3

Ratio, growth & per share analysis

Year to	12/2006a	12/2007e	12/2008e	12/2009e
Year-on-year % change				
Total income		2.1	-2.4	-2.5
Operating expense		4.6	-0.2	1.2
Pre-provision profit		-1.2	-5.3	-7.9
EPS				
HSBC EPS		-52.3	-2.9	-25.1
DPS		26.7	-42.1	-18.2
NAV (including goodwill)		-45.1	-0.7	-0.2
Ratios (%)				
Cost/income ratio	56.2	57.6	58.9	61.1
Bad debt charge	0.3	0.4	0.4	0.5
Customer loans/deposits	172.6	186.6	192.0	193.8
NPL/loan	1.6	1.6	1.6	1.7
NPL/RWA	1.5	1.6	1.6	1.7
Provision to risk assets/RWA	0.8	0.8	1.0	1.0
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	57.0	54.0	61.4	56.3
ROE (including goodwill)	7.6	6.6	6.4	4.8
Per share data (EUR)				
EPS reported (fully diluted)	2.76	1.47	1.19	0.88
HSBC EPS (fully diluted)	2.54	1.21	1.18	0.88
DPS	0.75	0.95	0.55	0.45
NAV	27.78	9.65	9.70	9.84
NAV (including goodwill)	33.62	18.45	18.32	18.29

Core profitability (% RWAs) and leverage

Year to	12/2006a	12/2007e	12/2008e	12/2009e
Net interest income	2.8	2.8	3.1	2.9
Trading profits	0.3	0.1	0.0	0.1
Other income	0.3	0.3	0.2	0.2
Operating expense	-2.7	-2.7	-2.6	-2.6
Pre-provision profit	2.1	2.0	1.8	1.6
Bad debt charge	-0.3	-0.4	-0.4	-0.6
HSBC attributable profit	1.0	0.8	0.8	0.6
Leverage (x)	7.9	8.1	8.3	8.6
Return on average tier 1	13.8	10.5	10.0	7.4

Valuation data

Year to	12/2006a	12/2007e	12/2008e	12/2009e
PE*	4.0	8.3	8.6	11.4
Pre-provision multiple	1.8	3.4	3.6	3.9
P/NAV	0.4	1.0	1.0	1.0
Equity cash flow yield (%)	-85.6	4.9	10.7	5.8
Dividend yield (%)	7.4	9.4	5.5	4.5

Note: * = Based on HSBC EPS (fully diluted)

Issuer information

Share price (EUR)	10.08	Target price (EUR)	11.60
Potent'l tot rtn (%)	15.1		
Reuters (Equity)	UBI.MI	Bloomberg (Equity)	UBI IM
Market cap (USDm)	8,520	Market cap (EURm)	6,443
Free float (%)	100		
Country	Italy	Sector	COMMERCIAL BANKS
Analyst	Carlo Digrandi	Contact	44 20 7991 6843

Notes: price at close of 28 Jan 2009

HSBC

Financials & valuation: Unicredit

Neutral (V)

Financial statements

Year to	12/2007a	12/2008e	12/2009e	12/2010e
P&L summary (EURm)				
Net interest income	13,965	17,967	17,210	17,877
Net fees/commissions	9,462	9,098	8,486	8,518
Trading profits	1,846	-1,024	154	230
Other income	2,162	1,452	932	959
Total income	27,435	27,494	26,782	27,585
Operating expense	-15,657	-16,755	-16,695	-16,801
Bad debt charge	-2,141	-3,822	-5,449	-6,159
Other	-955	-827	-714	-684
HSBC PBT	8,682	6,089	3,924	3,941
Exceptionals	530	800	0	0
PBT	9,212	6,889	3,924	3,941
Taxation	-2,534	-1,998	-1,334	-1,261
Minorities + preferences	-717	-517	-294	-296
Attributable profit	5,961	4,375	2,295	2,384
HSBC attributable profit	5,431	3,575	2,295	2,384
Balance sheet summary (EURm)				
Ordinary equity	57,724	61,371	63,052	64,030
HSBC ordinary equity	57,724	61,371	63,052	64,030
Customer loans	574,206	620,143	632,546	664,173
Debt securities holdings	263,826	252,907	257,965	263,124
Customer deposits	390,633	398,446	410,399	426,815
Interest earning assets	839,490	955,765	980,192	1,011,228
Total assets	1,021,758	1,043,882	1,067,640	1,108,977
Capital (%)				
RWA (EURm)	558,639	542,819	555,173	576,668
Core tier 1	5.8	6.6	6.8	6.7
Total tier 1	6.5	7.4	7.6	7.5
Total capital	10.1	11.2	11.4	11.2

Ratio, growth & per share analysis

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Year-on-year % change				
Total income	16.9	0.2	-2.6	3.0
Operating expense	18.1	7.0	-0.4	0.6
Pre-provision profit	15.4	-8.8	-6.1	6.9
EPS				
HSBC EPS	8.5	-45.1	-44.7	3.9
DPS	8.3	-100.0		0.0
NAV (including goodwill)	40.1	-11.3	-11.5	1.6
Ratios (%)				
Cost/income ratio	57.1	60.9	62.3	60.9
Bad debt charge	0.4	0.6	0.9	0.9
Customer loans/deposits	147.0	155.6	154.1	155.6
NPL/loan	4.7	4.6	5.1	5.9
NPL/RWA	5.0	5.4	6.1	7.0
Provision to risk assets/RWA	3.3	3.9	4.2	4.4
Net write-off/RWA	0.0	0.0	0.0	0.0
Coverage	66.3	72.2	69.0	62.7
ROE (including goodwill)	12.1	6.1	3.7	3.8
Per share data (EUR)				
EPS reported (fully diluted)	0.54	0.33	0.15	0.15
HSBC EPS (fully diluted)	0.49	0.27	0.15	0.15
DPS	0.26	0.00	0.05	0.05
NAV	2.47	2.59	2.35	4.15
NAV (including goodwill)	5.20	4.61	4.08	4.15

Core profitability (% RWAs) and leverage

Year to	12/2007a	12/2008e	12/2009e	12/2010e
Net interest income	2.8	3.3	3.1	3.2
Trading profits	0.4	-0.2	0.0	0.0
Other income	0.4	0.3	0.2	0.2
Operating expense	-3.2	-3.0	-3.0	-3.0
Pre-provision profit	2.4	1.9	1.8	1.9
Bad debt charge	-0.4	-0.7	-1.0	-1.1
HSBC attributable profit	1.1	0.6	0.4	0.4
Leverage (x)	10.9	9.3	8.8	8.9
Return on average tier 1	14.8	8.9	5.5	5.5

Valuation data

Year to	12/2007a	12/2008e	12/2009e	12/2010e
PE*	2.9	5.2	9.5	9.1
Pre-provision multiple	1.3	1.7	2.2	2.0
P/NAV	0.6	0.5	0.6	0.3
Equity cash flow yield (%)	-21.8	24.9	7.6	4.7
Dividend yield (%)	18.5	0.0	3.6	3.6

Note: * = Based on HSBC EPS (fully diluted)

Issuer information

Share price (EUR)	1.41	Target price (EUR)	1.50
Potent'l tot rtn (%)	6.5		
Reuters (Equity)	CRDI.MI	Bloomberg (Equity)	UCG IM
Market cap (USDm)	24,915	Market cap (EURm)	18,841
Free float (%)	70		
Country	Italy	Sector	COMMERCIAL BANKS
Analyst	Carlo Digrandi	Contact	44 20 7991 6843

Notes: price at close of 28 Jan 2009

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Disclosure appendix

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Important disclosures

Stock ratings and basis for financial analysis

HSBC believes that investors utilise various disciplines and investment horizons when making investment decisions, which depend largely on individual circumstances such as the investor's existing holdings, risk tolerance and other considerations. Given these differences, HSBC has two principal aims in its equity research: 1) to identify long-term investment opportunities based on particular themes or ideas that may affect the future earnings or cash flows of companies on a 12 month time horizon; and 2) from time to time to identify short-term investment opportunities that are derived from fundamental, quantitative, technical or event-driven techniques on a 0-3 month time horizon and which may differ from our long-term investment rating. HSBC has assigned ratings for its long-term investment opportunities as described below.

This report addresses only the long-term investment opportunities of the companies referred to in the report. As and when HSBC publishes a short-term trading idea the stocks to which these relate are identified on the website at www.hsbcnet.com/research. Details of these short-term investment opportunities can be found under the Reports section of this website.

HSBC believes an investor's decision to buy or sell a stock should depend on individual circumstances such as the investor's existing holdings and other considerations. Different securities firms use a variety of ratings terms as well as different rating systems to describe their recommendations. Investors should carefully read the definitions of the ratings used in each research report. In addition, because research reports contain more complete information concerning the analysts' views, investors should carefully read the entire research report and should not infer its contents from the rating. In any case, ratings should not be used or relied on in isolation as investment advice.

Rating definitions for long-term investment opportunities

Stock ratings

HSBC assigns ratings to its stocks in this sector on the following basis:

For each stock we set a required rate of return calculated from the risk free rate for that stock's domestic, or as appropriate, regional market and the relevant equity risk premium established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the implied return must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

*A stock will be classified as volatile if its historical volatility has exceeded 40%, if the stock has been listed for less than 12 months (unless it is in an industry or sector where volatility is low) or if the analyst expects significant volatility. However,

stocks which we do not consider volatile may in fact also behave in such a way. Historical volatility is defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility has to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Prior to this, from 7 June 2005 HSBC applied a ratings structure which ranked the stocks according to their notional target price vs current market price and then categorised (approximately) the top 40% as Overweight, the next 40% as Neutral and the last 20% as Underweight. The performance horizon is 2 years. The notional target price was defined as the mid-point of the analysts' valuation for a stock.

From 15 November 2004 to 7 June 2005, HSBC carried no ratings and concentrated on long-term thematic reports which identified themes and trends in industries, but did not make a conclusion as to the investment action that potential investors should take.

Prior to 15 November 2004, HSBC's ratings system was based upon a two-stage recommendation structure: a combination of the analysts' view on the stock relative to its sector and the sector call relative to the market, together giving a view on the stock relative to the market. The sector call was the responsibility of the strategy team, set in co-operation with the analysts. For other companies, HSBC showed a recommendation relative to the market. The performance horizon was 6-12 months. The target price was the level the stock should have traded at if the market accepted the analysts' view of the stock.

Rating distribution for long-term investment opportunities

As of 28 January 2009, the distribution of all ratings published is as follows:

Overweight (Buy)	41%	(29% of these provided with Investment Banking Services)
Neutral (Hold)	37%	(35% of these provided with Investment Banking Services)
Underweight (Sell)	22%	(21% of these provided with Investment Banking Services)

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HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
BANCA POPOLARE DI MILANO	PMII.MI	3.76	27-Jan-2009	2, 4, 11
BANCO POPOLARE	BAPO.MI	4.25	27-Jan-2009	6, 7
INTESASANPAOLO	ISP.MI	2.35	27-Jan-2009	2, 5, 6, 7, 11
MONTE DEI PASCHI DI SIENA	BMPS.MI	1.14	27-Jan-2009	2, 5, 6, 11
UBI	UBI.MI	9.70	27-Jan-2009	2, 5
UNICREDIT	CRDI.MI	1.26	27-Jan-2009	2, 5, 6, 7, 11

Source: HSBC

1 HSBC* has managed or co-managed a public offering of securities for this company within the past 12 months.
2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.
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8 A covering analyst/s has received compensation from this company in the past 12 months.
9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.
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Additional disclosures

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2 All market data included in this report are dated as at close 27 January 2009, unless otherwise indicated in the report.
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