The Italian NPL market

The Place To Be

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Foreword

The Italian NPL market is now definitively “The Place To Be”, due to the volumes of NPL, the highest in Europe yet (€ 324bn of GBV at the end of 2016) and the recent trends in the Italian NPL arena. Ailing banks are going through a restructuring process, significant banks are engaged in massive NPL deleverage plans, overall the NPL management is passing through a prominent overhaul under new ECB guidelines and the NPL servicers are experiencing a deep evolution and facing consolidation manoeuvres.

On one hand, ailing Italian banks are going through a **restructuring phase** ultimately affecting the NPL market. In May 2017 UBI acquired three regional lenders (Banca Marche, BPEL and CariChieti) and BPER acquired the regional bank CariFerrara, following their rescue in 2015 by Italian Authorities and the sale of their NPL to the bad bank “REV”(€10.3bn) in 2015 and to Atlante Fund (€2.2bn) in 2017.

Restructuring measures for other entities overburdened by their Bad Loans as MPS (€29.4bn), Banca Popolare di Vicenza (€5.1bn), Veneto Banca (€3.3bn), are currently in progress but, once occurred, they will affect the NPL market in the near future. Even smaller regional banks, as CariCesena, Carim and Carismi (totaling €2.8bn of Bad Loans), are committed in the research of restructuring solutions to address the issue of their non-performing exposures. We need to see how the recent urgent measures enacted by the Government to liquidate the NPL of Banca Popolare di Vicenza and Veneto Banca (€ 16.8bn at the end of 2016) will affect the wider banking sector.

On the other hand, big Italian banks started to **implement deleverage** plans aimed at reducing their NPL ratios. Unicredit, Intesa Sanpaolo and Banco BMP implemented their plans to sell €17.7bn, €2.5bn and €0.8bn of NPL respectively. The deleverage phase introduced new trends in the market as the sale of portfolios composed by mixed asset class as well as portfolios made by a limited number of borrowers specialised in real estate developments and sale of single names under restructuring (Unlikely To Pay exposures).

These latest trends in the market witnesses the importance the Italian banks are gradually attributing to the issue of their Unlikely to Pay exposures (GBV equal to €117bn and NBV to €87bn). In this respect, ECB guidelines provide a great opportunity to renovate and improve the proactive management of NPL to address the issue of their massive stock. ECB guidelines will require the adoption and implementation of a renovated strategic management along with a structured deleverage approach. Furthermore IFRS9, in place from 1 January 2018, will lead to an «early warning» and «forward looking» approach, which could likely result in higher reclassification of performing loans to NPL and overall higher provisions.

The credit management industry, in particular the NPL servicing segment, is experiencing a strong evolution. The role of independent specialized NPL servicers is gaining importance driven by increasing volumes of portfolio disposals from Banks to Investors, together with growing outsourcing of recovery activities by banks driven by lack of capacity, and fostered by the implementation of ECB guidelines. As a result, the servicing market displays, on one hand, consolidation movements among the players and, on the other hand, new M&A opportunities.

Lastly, the recent amendments of the Italian law on securitization on June 2017, allowing the SPVs to purchase the asset securing securitized receivables (including assets subject to leasing agreements), will result in a higher number of transactions by encouraging more players, both originators and investors, to enter this market.

Based on the trends and movements observed in the market, we expect that the NPL transactions’ volumes could easily reach and overcome € 60 billion in 2017.

Looking at the current trends, we see the Italian NPL market as “The Place To Be”. The environment became vibrant and dynamic and it is where the need and the long for innovative solutions will lead to deals, restructuring and internal reorganization opportunities, to not miss out, for a wide audience.

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The terms of NPL ("Non Performing Loans") and NPE ("Non Performing Exposures") are used interchangeably within this study. This recommendation was even explained in the "Guidance to banks on non-performing loans (March 2017)" released by ECB – Banking Supervision*

Content

Macroeconomic Scenario	5
Italian Real Estate Market	8
Legal and regulatory framework update	12
Italian NPL Market	16
Italian Banks overview	20
Focus on UTP Italian Market	27
The Servicing Market	34
Regulatory changes	44
Recent market activity and outlook	46
Non Performing Exposures classification	49
Appendix	51

* "Guidance to banks on non-performing loans (March 2017)" by ECB, par. 1.2, pag.6 "Scope of this Guidance"and par. 5.1, pag. 47 "Purpose and Overview"

Macroeconomic Scenario

Key Message: in 2017 the domestic demand is expected to raise contributing to the economic growth. Other factors are the supportive monetary policy, which produces a low interest rate environment, and the decrease of the unemployment rate.
Inflation is expected to climb and then to slightly reduce, while investments are set to increase.

Despite several concerns about growth in emerging markets, exceptionally weak world trade, terrorist attacks and the UK's vote to leave the European Union, the European economy is expected to continue growing in 2017 and 2018, driven mainly by domestic demand.

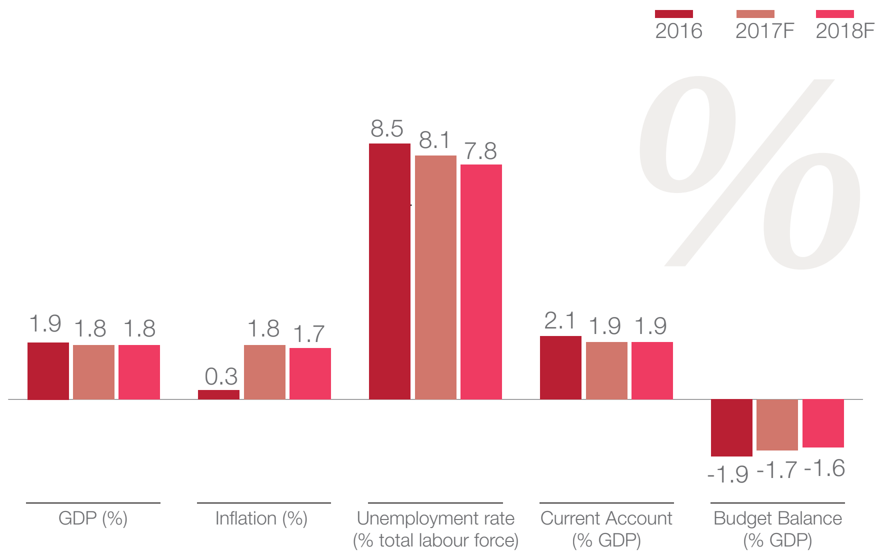
GDP in Italy is predicted to be 0.9% in 2017 and 1.1% in 2018, supported by a low interest rate environment and a stronger external demand, while structural weaknesses hinder a stronger recovery. Moreover, the overall private consumption is set to benefit from further, although slower, employment creation. However, some issues related to the political uncertainty and the slow adjustment of the banking sector are likely to compromise the growth prospects.

Overall, **GDP** growth is forecasted to stand at 1.8% in 2017 and 2018 in the Euro area, mainly driven by a supportive monetary policy and acceleration in global demand.

Inflation is flat at 1.8% in 2017 in the Euro area thanks to the depreciation of the euro against the US currency and the rising in the prices of global input. However, this effect will fade in 2018, when the forecasted inflation is set to reduce to 1.7%. Inflation in Italy is set to climb to 1.4% in 2017, dragged down by the rise in energy prices, and stabilize at 1.3% in 2018.

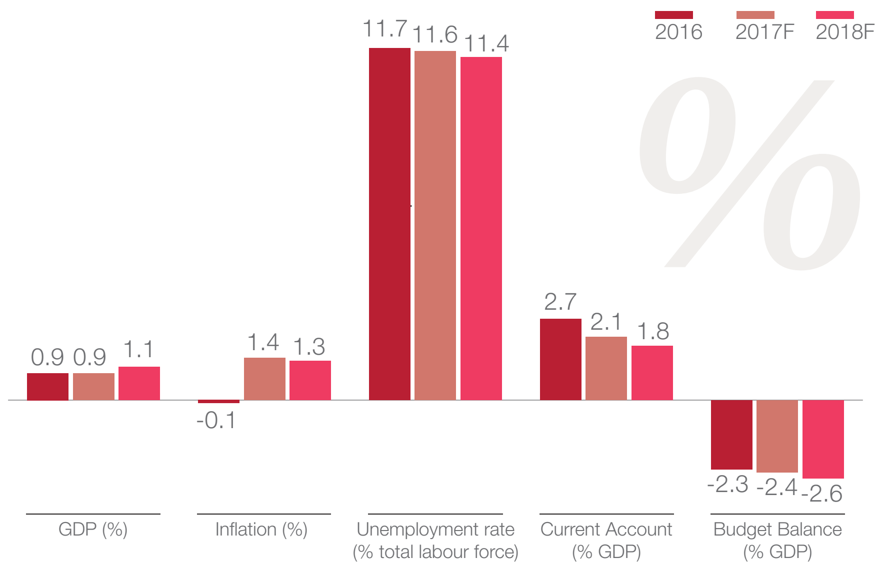
Unemployment rate in Italy is set to reduce thanks to past reforms such as the permanent reduction of labor taxation. The rate is forecasted to stand at above 11.6% in 2017 and 11.4% in 2018, well above the average European level.

Chart 1: EU main economic drivers



Source: PwC analysis on European Economic Forecast Winter 2017. Unemployment rate as a % of total labour force, current account balance and budget balance as a % of GDP.

Chart 2: Italian main economic drivers



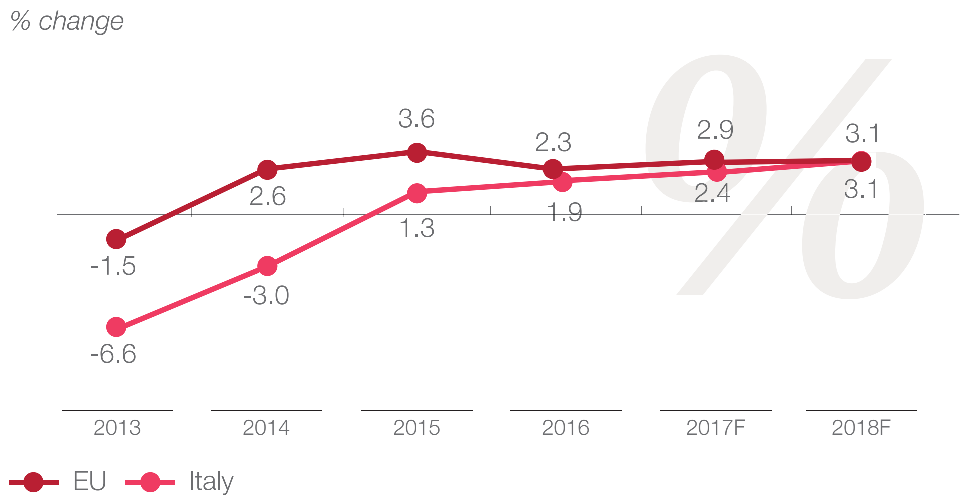
Source: PwC analysis on European Economic Forecast Winter 2017. Unemployment rate as a % of total labour force, current account balance and budget balance as a % of GDP.

Current account surplus in Italy is foreseen to be 2.1% in 2017, above the average for the European member states (1.9%), and 1.8% in 2018, slightly below the European average. (1.9%).

Investment is set to increase by 2.4% in 2017 and 3.1% in 2018, as it benefits from measures in the 2017 budget and from the Investment Plan for Europe, gradually shrinking the gap with European levels.

Forecast suggest that the **Government gross debt ratio** is expected to slightly reduce both in Italy and in EU in the next years.

Chart 3: Total investments volume trend



Source: PwC analysis on European Economic Forecast Winter 2017.

Table 1: Government gross debt ratio per country

Government gross debt ratio (% GDP)	2013	2014	2015	2016	2017F	2018F	Trend 2017-2018F
Italy	129	131.9	132.3	132.8	133.3	133.2	▼
EU	91.3	93.4	92.6	91.5	90.4	89.2	▼
Spain	95.4	100.4	99.8	99.7	100.0	99.7	▼
France	92.3	95.3	96.2	96.4	96.7	97.0	▲
UK	86.2	88.1	89.0	88.6	88.1	87.0	▼
Germany	77.5	74.9	71.2	68.2	65.5	62.9	▼

Source: PwC analysis on European Economic Forecast Winter 2017.

Italian Real Estate Market

Key Message: In 2016, the Italian Real Estate market registered a 18.4% growth compared to 2015, mainly driven by transactions related to residential assets. Rome and Milan continue to be the main city markets, representing ca 44% of total transactions. Investments in Real Estate reached €9.1 bn in 2016, with offices continuing to represent the major asset class for investment.

Volume of Real Estate transactions in 2016

In 2016, the Italian real estate market has been continuing on its positive trend, driven mainly by sales of residential properties and appurtenances (which include garages, basements and parking spots). It hasn't happened since 2011 that the yearly real estate transactions exceeded million unities (1,141,012 NTN in 2016).

The most significant percentage growth, compared to the previous year, was recorded in the industrial building sector, a 22.1% increase. See Table 2.

Residential sales in 2016 have increased throughout each region of Italy with respect to 2015. The North showed the greatest positive results, with a 22.3% increase over 2016, which was followed by the South and Centre with 16.2% and 14.6% growth, respectively. See Table 3.

During 2016, non residential asset classes showed double digit increases, accounting for growth of 19.2% compared to 2015. While continuing to account for a small proportion of the total, the office segment is the sector registering the highest growth rate, at 24.1%. See Table 4.

Table 2: Italian NTN[1] comparison by sector

Asset type	Q1 2016	Q2 2016	Q3 2016	Q4 2016	Total 2016	H1 2015	H2 2015	Total 2015	Delta (%) 15-16
Residential	115,194	143,298	123,476	146,896	528,864	211,968	232,657	444,625	18.9%
Office	2,025	2,413	2,510	3,000	9,948	4,097	4,744	8,841	12.5%
Retail	6,776	7,598	7,188	9,024	30,586	12,634	13,594	26,228	16.6%
Industrial	2,121	2,897	2,565	3,704	11,287	4,230	5,012	9,242	22.1%
Appurtenances[2]	87,554	110,015	94,007	119,427	411,003	163,887	181,003	344,890	19.2%
Other[3]	30,828	38,687	35,719	44,090	149,324	61,746	68,363	130,109	14.8%
Total	**244,498**	**304,908**	**265,465**	**326,141**	**1,141,012**	**458,562**	**505,373**	**963,935**	**18.4%**

Source: PwC publication "Real Estate Market Overview – Italy 2017"
1. NTN is the number of standardized real estate units sold, taking into account the share of the property transferred
2. Appurtenances comprehend properties such as basements, garages or parking spots
3. The sector "Other" includes hospitals, clinics, barracks, telephone exchanges and fire stations

Table 3: Residential NTN by geographic area

Area	Region	Year 2016	H1 2016	H2 2016	Delta (%) 15-16	Delta (%) H1 15-16	Delta (%) H2 15-16
North	Provinces	89,901	44,762	45,131	23.7%	27.8%	20.0%
	No Provinces	192,015	91,888	100,111	21.7%	22.9%	20.4%
	Total	**281,916**	**136,650**	**145,242**	**22.3%**	**24.5%**	**20.3%**
Center	Provinces	51,577	25,414	26,148	13.5%	17.7%	9.7%
	No Provinces	58,159	28,286	29,855	18.6%	21.7%	15.8%
	Total	**109,736**	**53,700**	**56,003**	**16.2%**	**19.8%**	**12.9%**
South	Provinces	38,921	19,713	19,198	14.7%	19.8%	9.9%
	No Provinces	98,292	48,317	49,930	14.6%	18.1%	11.4%
	Total	**137,213**	**68,030**	**69,128**	**14.6%**	**18.6%**	**10.9%**
Italy	Provinces	180,400	89,888	90,476	18.7%	23.0%	14.6%
	No Provinces	348,465	168,491	179,896	19.1%	21.3%	17.0%
	Total	**528,865**	**258,379**	**270,372**	**18.9%**	**21.9%**	**16.2%**

Source: PwC publication "Real Estate Market Overview – Italy 2017"

Table 4: Non residential NTN by geographic area

NTN 2016 Office	Q1 2016	Q2 2016	Q3 2016	Q4 2016	2016	2015	Delta (%) 15-16
North	1,186	1,413	1,579	1,918	6,096	4,733	28.8%
Center	417	505	488	559	1,969	1,650	19.3%
South	422	494	442	523	1,881	1,632	15.3%
							24.1%

NTN 2016 Retail	Q1 2016	Q2 2016	Q3 2016	Q4 2016	2016	2015	"Delta (%) 15-16"
North	3,309	3,619	3,633	4,442	15,003	12,753	17.6%
Center	1,451	1,700	1,620	2,051	6,822	5,996	13.8%
South	2,016	2,279	1,953	2,531	8,779	7,478	17.4%
							16.7%

NTN 2016 Industrial	Q1 2016	Q2 2016	Q3 2016	Q4 2016	2016	2015	Delta (%) 15-16
North	1,396	1,867	1,710	2,371	7,344	6,258	17.4%
Center	361	430	449	628	1,868	1,561	19.7%
South	361	600	406	706	2,073	1,423	45.7%
							22.1%

Source: PwC publication "Real Estate Market Overview – Italy 2017"

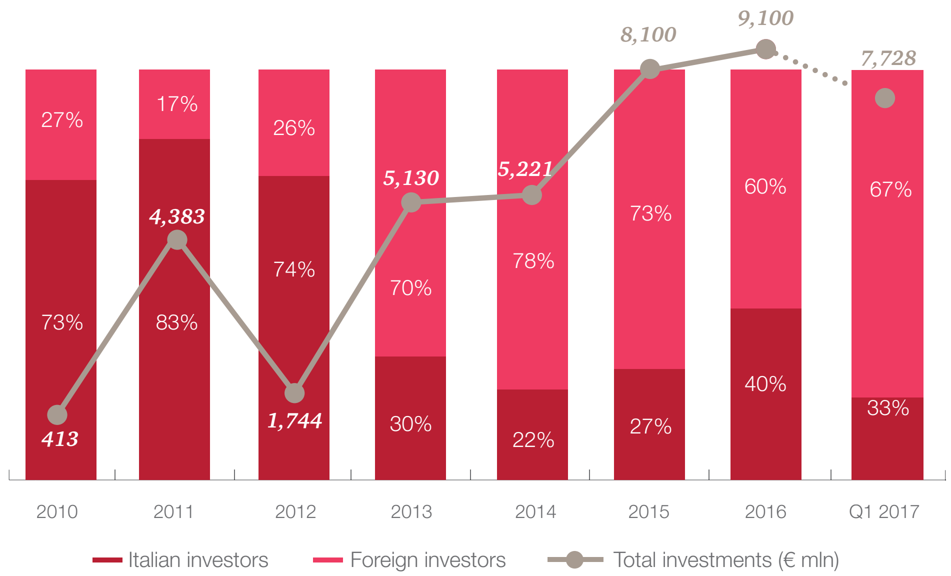
Investments in the non residential Real Estate market

In 2016, the Italian commercial real estate market recorded a transaction volume of € 9.1 billion, up circa 12% from 2015, confirming the increasing investor confidence and demand for Italian real estate. The investment recovery has started in 2013 reaching the highest point in 2016, that has proven to be the second best year for Italian real estate investment after the record level of € 10 billion in 2007. Investments in the non residential Real Estate industry in Q1 2017 amounted to €1.9bn, about 12% higher than Q1 2016.

The strong growth was driven by ca 23% increase in the Office sector, which continues to represent the lion's share of the investments, with ca 44% of the total volumes of transactions. The Retail sector registered an increase by 58% over the same period. Industrial estates (+270%) is growing fast, but the lack of supply across the country obliges the investors to widen their areas of interest and to concentrate on value added operations.

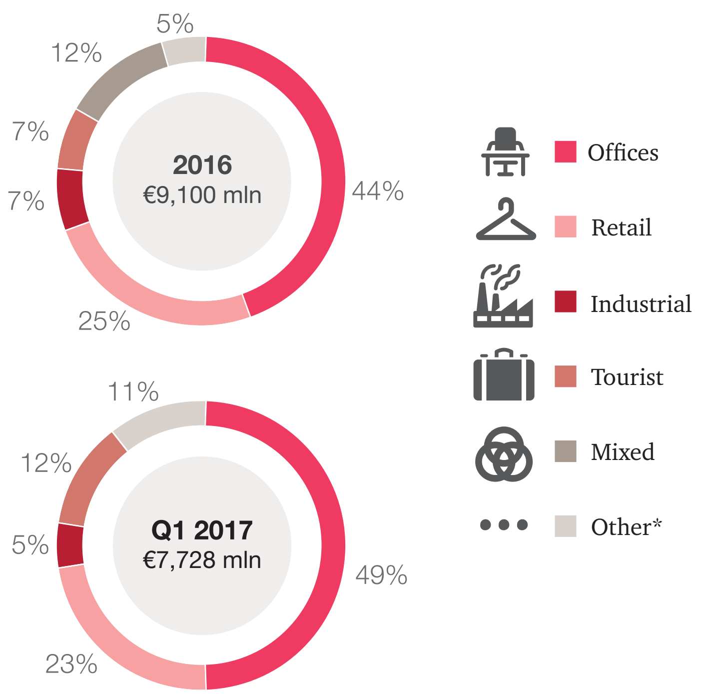
Rome and Milan still represent key markets for investments, accounting for 34% and 17% of the total investment volume in 2016, respectively. However, some investors have adapted their strategies to the dynamic market and started to consider secondary locations as well.

Chart 4: Investments in the non residential Real Estate industry - Investor type



Source: PwC publication "Real Estate Market Overview – Italy 2017
* Q1 2017 value is normalized

Chart 5: Investments in the non residential Real Estate industry - Asset type



Source: PwC publication "Real Estate Market Overview – Italy 2017"
*"Other" includes banks, public administration and sovereign funds
* Q1 2017 value is normalized

Legal and regulatory framework update

NPL Guidelines: On 20th March 2017, the ECB released the final guidelines for the banks on non-performing loans. The guidelines concern some crucial aspects for the resolution of NPL issues and are considered applicable from the moment of their publication

The ECB guidelines on NPLs come to "disrupt" the "banking scenery"

Even though the ECB guidelines constitute a recommendation for all credit institutions, they are generally addressed to all **significant institutions** (SIs) under the SSM and specifically to banks with a **high level of NPL** (especially for strategy and governance issues).

Banks with a gross NPL ratio above 7% are considered "High NPL banks".

A bank can also be considered as high NPL in case of:

- High level of NPL inflows
- High level of forbearance and foreclosed assets
- Low levels of provision coverage
- High texas ratio

Given the significance of the guidelines, it is highly advised for all institutions to adopt the most critical aspects of these best practices, taking into consideration the principle of proportionality.

SSM supervisory priorities for 2017 include:

- Business models and profitability drivers
- Credit risk with an NPL and concentration focus
- Risk management

The **significance of these guidelines** is in particular related to the fact that they:

- May result in **additional supervisory measures** in case of any possible non compliance (in absence of reasonable justification)

- Have been drafted taking into **consideration comments and queries** arising from a diverse range of directly affected parties such as financial and credit institutions, market and banking associations during the consultation process

- Highlight the importance it has to be given to the **forbearance** measures granted in order to avoid a misrepresentation of the quality of the loan positions

- Provide guidance to banks aimed at establishing **a clear strategy** and **operational plan** in order to reduce its consistencies in a credible, feasible and timely manner

- Prepare banks to **confront future challenges** by encouraging them to take into consideration the competitive landscape as well as the external operating environment

12th September 2016
Commencement of public consultation concerning the guidelines on non-performing loans (NPL)

7th November 2016
Public auditioning with senior representatives of the ECB to provide clarifications as part of the consultation

15th November 2016
End of public consultation on the NPL guidelines

1st March 2017
First complete draft of the NPL guidelines **send to ECB Governing** Council in order to proceed with its adoption

8th March 2017
Adoption of the document by the **ECB Governing Council**

20th March 2017
Publication of the official final guidelines as well as the **feedback on the comments** received during consultation

The "disruptive" nature of the Guidelines 1/2

From **evidence on the Italian banking sector** it can be derived that the guidelines have already had and are going to have a significant impact on the way banks manage their non performing positions not only on the short term but also with regard to the medium to long term.

When verifying a bank's current business model with its conformity to the main ECB indications the **main impacts** are on the strategy, the organisational structure, the operational model and the data management of a bank.

Strategy
- Integration
- Medium to long term planning
- Valuation of available options

Organisational Structure
- Specialisation
- Coordination
- Independence

Operating Model
- Automatization
- Monitoring
- Strategic management options of the portfolios

Data
- Univocal database
- Data Quality
- Data Availability

Strategy

Integration
For an NPL strategy to be successful, a centralised management of the strategy across the various NPL Units is required along with the integration of the policies and procedures in place, to set common grounds that are communicated and adopted throughout the bank.

Medium to long term planning
The NPL strategy that a bank adopts should contain objectives that aim at reducing its NPL levels not only short term but also in the medium (3 years) term. These objectives are to be part of a realistic operating plan reinforced by incentives given to the dedicated Units in connection to the reduction of the NPLs. When planning the NPL strategy a key element for banks is to analyse and project the capital implications that such a strategy may have.

Valuation of available options
Both the external (macroeconomic environment, investors…) and internal (resources, processes, composition of portfolio…) operating environment play a vital role in valuating the possible strategic options (impairment, sale, write offs, appropriation of guarantees, legal options, securitisation, etc.) that a bank will follow. Given the rapid pace and the constant developments of the sector, the possible strategic options need to be regularly reviewed and updated taking into consideration the positioning of the bank in the market and the general market evidence.

Organisational Structure

Specialisation
The bank needs to establish specialised NPL dedicated Unit(s) for an effective management of the NPLs, distinct from the commercial Units. The NPL dedicated Unit(s) need to be supported by an articulate approach for an adequate segmentation of the portfolios per type of debtor.

Coordination
An important aspect is for the different functions involved in the NPL process to have a clear view and distinct boundaries of their role and responsibilities in relation to the other functions, establishing a regular communication as a common practice. Moreover, specific criteria need to be set for the correct classification and passage of the positions within the different dedicated Units.

Independence
The NPL dedicated Unit(s) need to be independent from the Units responsible to the granting of credit. Taking always into account the concept of proportionality, the people involved in managing NPL loans should not be involved in the day to day activities related to the management of performing loans and credit granting.

The “disruptive” nature of the Guidelines 2/2

The main objective is to allow debtors to exit their non-performing status and/or prevent their deterioration.

Forbearance: banks before granting forbearance measures should apply a «decision tree» allowing to take into consideration and value the implications of granting other possible options as well. Forbearance measures should be closely monitored and clear criteria should be established for exiting a forborne status

UTP: «Tailor made» solutions aimed at a proactive management as well as implementation of standard procedures for the appropriate classification and segmentation

Strategy
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Operating Model

Automatization
Given the complexity and size of data processed, a bank needs to ensure that its operating model is supported by adequate automated systems and processes. Simulations, where appropriate, should be run allowing to plan taking into considerations future scenarios.

Monitoring
A continuous monitoring both at a debtor and at a portfolio level is crucial. Such monitoring can have a direct consequence on the NPL strategy as the resulting evidences can alter the underlying hypothesis of the NPL strategy. For an effective monitoring of the adequacy of the operating model in place key performance indicators (KPIs) play a vital role. The KPIs not only allow for the bank to position itself in the market but also to measure the progress made on NPL recoveries (either internal or external through oursourcers).

Early warning indicators (EWIs) can anticipate the evolution of the loan position, becoming an integral part of the NPL recovery guidelines and policies

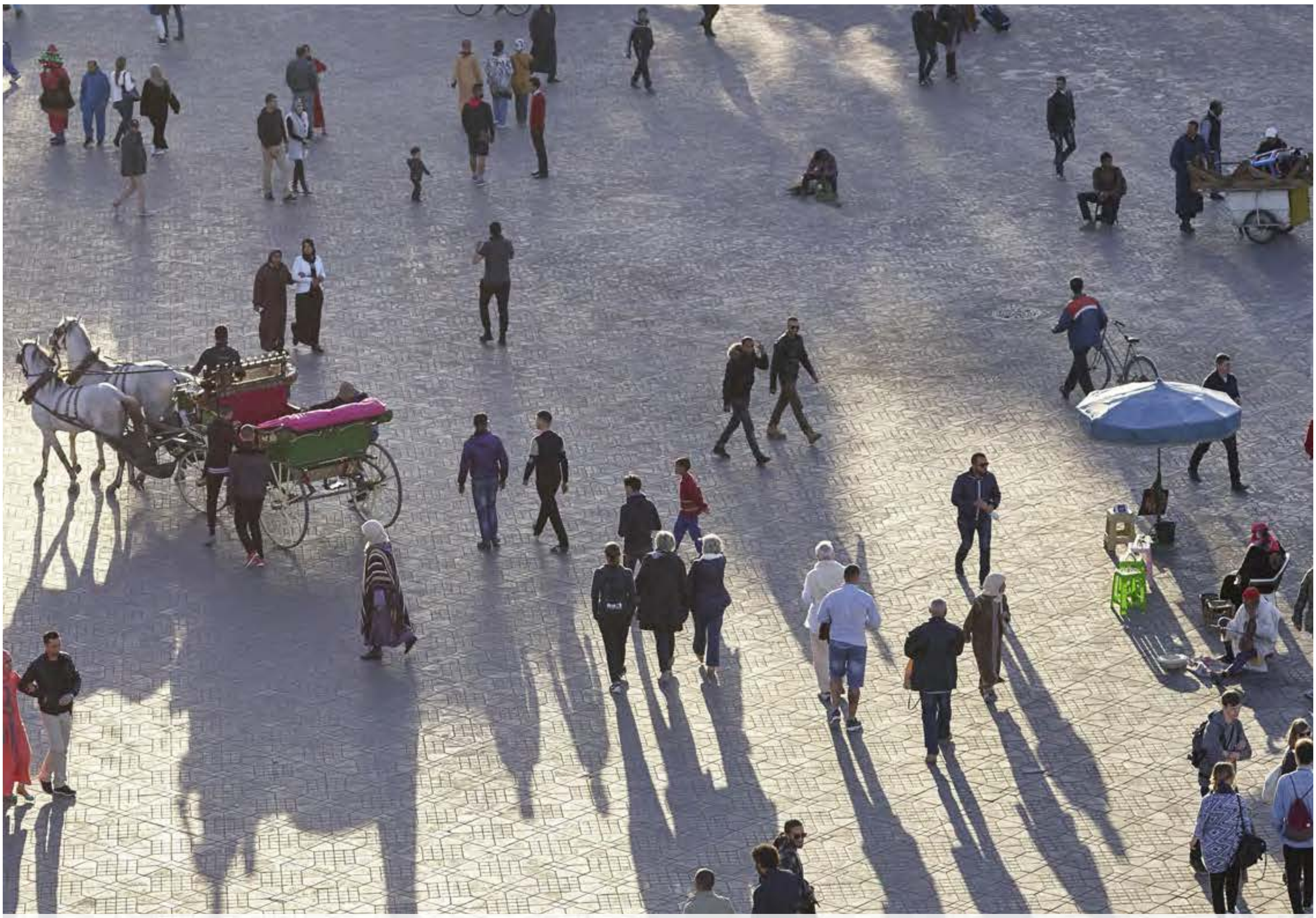
Strategic management of the positions
Both KPIs and EWIs are an integral part in the formulation of the course of action adopted for the bank’s NPL. Extraordinary operations, outsourcing, real estate vehicles as well as automatic write-offs should be all be considered when deciding on the strategic management of the single positions.

Data

Univocal database
The challenge for the banks lays in creating a unique database containing all the relevant information of the portfolios, updated at a frequent basis. Such a database should be enriched by all the relevant Units and should be able to allow an adequate level of historical information and contain all the information for allowing a focused and granular management of the portfolio.

Data Quality
Fundamental for the proper utilisation of the univocal database is the quality of the data that is enriched with. A critical point of the process is the moment that the database is created ensuring the consistency of the data inputs across the various databases and Units of the bank.

Data Availability
Readily available data, updated at frequent intervals is fundamental for the effective management of the bank’s NPLs.



Italian NPL Market

Key Message: The NPL volume in the Italian banking sector is the highest in the European market reaching the value of €324bn (GBV) at the end of 2016. After reaching the peak at the end of 2015, totaling € 341bn, the NPE volume experienced a slight but firm decline during 2016 (-5%). Within the NPL categories, the Unlikely to Pay volumes, still lower than Bad Loans in terms of GBV (€ 117 bn vs € 200 bn) are by now overcoming the Bad Loans in terms of NBV (€ 87bn)

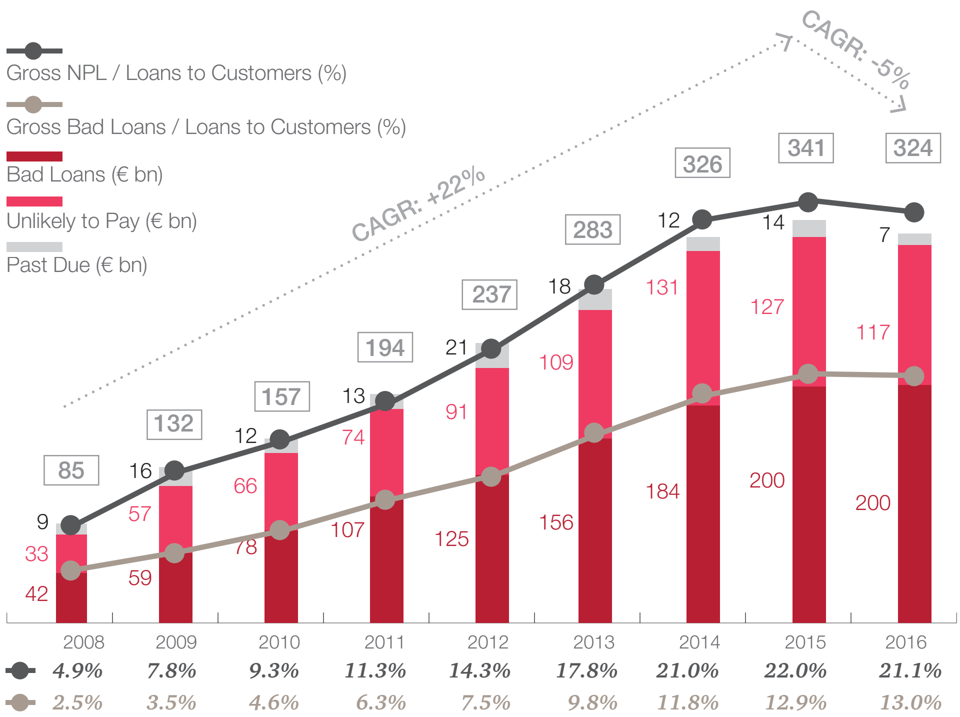
Asset Quality

As shown in Chart 6, after reaching its maximum at YE-2015 (€341bn), total NPE stock has finally registered a reduction at YE-2016, to €324bn.

Gross Bad Loans, which account for €200bn of total gross NPL were at the same level as YE-2015. On the other side, Unlikely to Pay and Past Due are considerably declining reaching €117bn (from €127bn at YE-2015) and €7bn (from €14bn at YE-2015) at YE-2016.

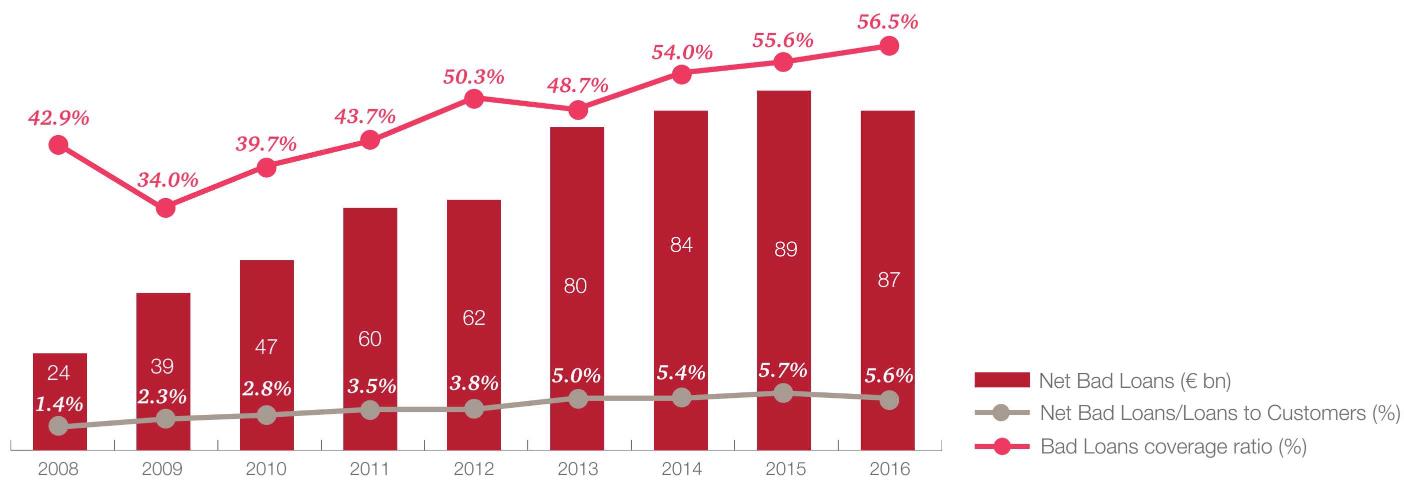
Chart 7 indicates that net Bad Loans registered a €2bn reduction from YE-2015 due to the Bad Loans' coverage ratio reached 56.5% growing of almost 1% from YE-2015.

Chart 6: Gross NPE and Bad Loans trend



Source: PwC analysis data of Bollettino Statistico di Banca d'Italia and ABI Monthly Outlook

Chart 7: Net Bad Loans Trend

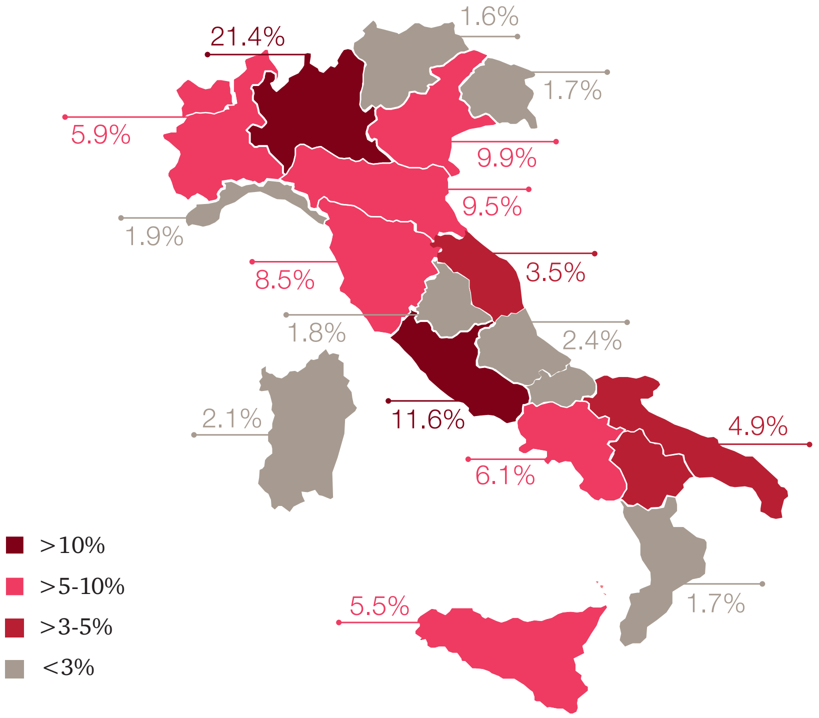


Source: PwC analysis data of ABI Monthly Outlook

Looking at the Bad Loans stock composition:

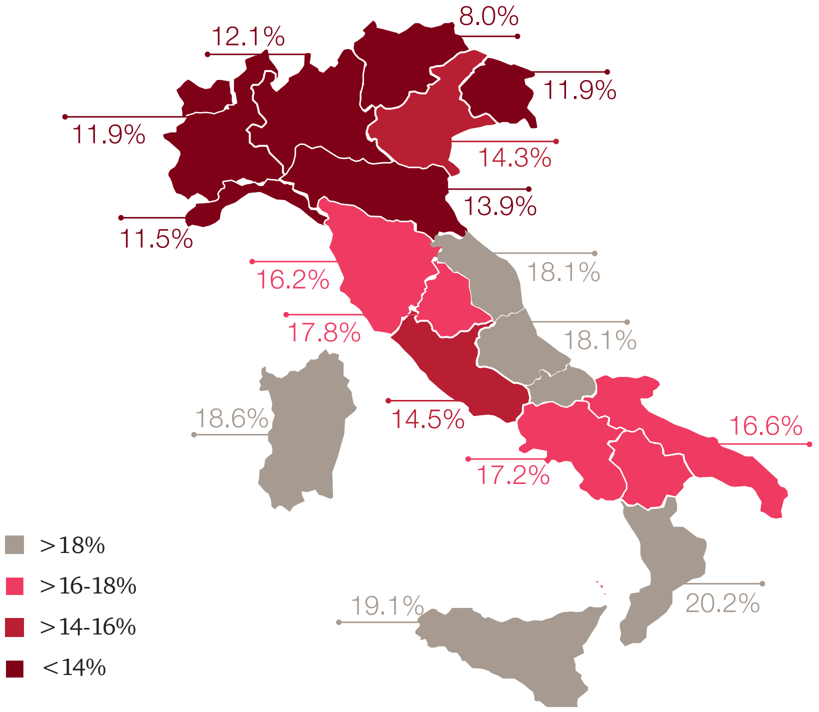
- "Corporate & SME" continue to represent the greatest share of gross Bad Loans reaching 73% at YE-2016;
- the Lombardy (21.4%) and Lazio (11.6%) regions have the highest concentration of stock;
- at the same time Lombardy and Lazio has respectively 12.1% and 14.5% of Gross Bad Loans ratio;
- the South of Italy has the highest percentage of Gross Bad Loans ratio;
- Trentino Alto Adige, Friuli Venezia Giulia, Liguria, Umbria, Marche, Calabria and Sardegna has a percentage of gross Bad Loans lower than 3%;
- the percentage of secured Bad Loans is increasing from 36% in 2008 to 48% at YE-2016.

Chart 8a: Breakdown of Gross Bad Loans by region* (YE-2016)



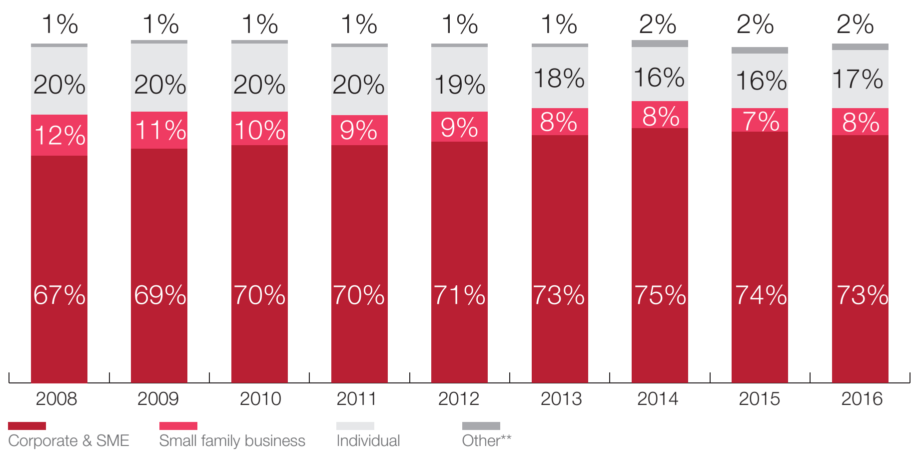
Source: PwC analysis on data of "Bollettino Statistico" of Bank of Italy

Chart 8b: Breakdown of Gross Bad Loans Ratio by region* (YE-2016)



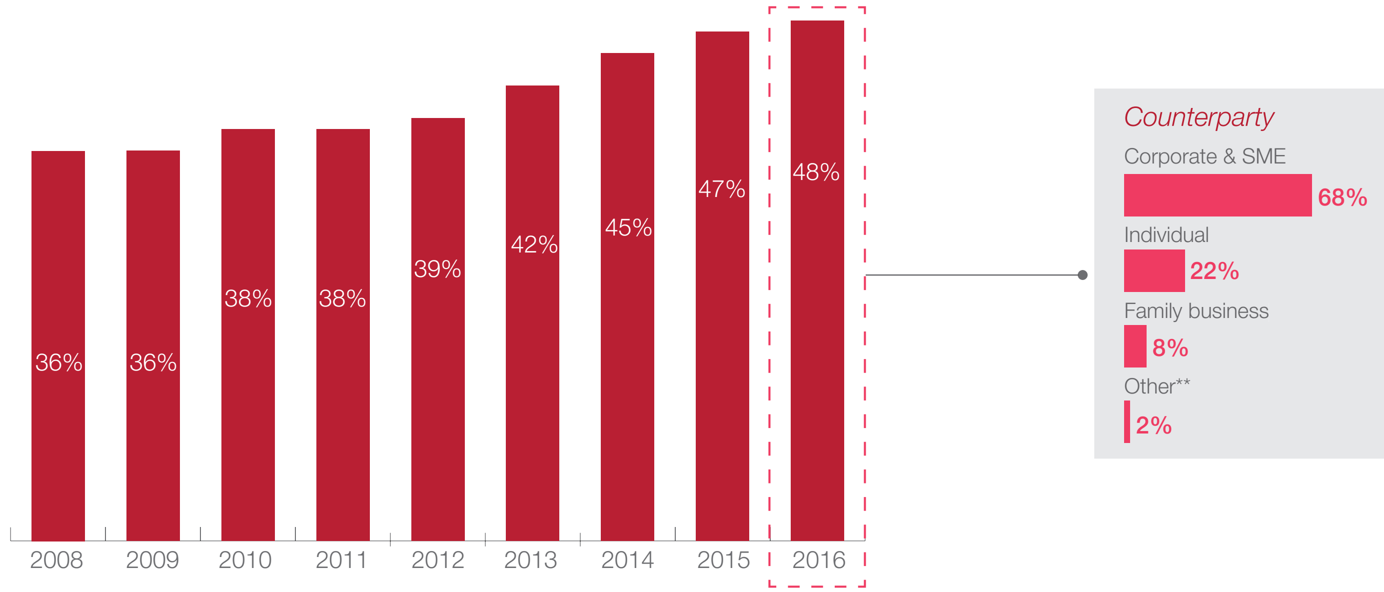
Source: PwC analysis on data of "Bollettino Statistico" of Bank of Italy
* Unified percentage for 1) Valle d'Aosta and Piemonte, 2) Abruzzo and Molise, 3) Puglia and Basilicata

Chart 9: Breakdown of Gross Bad Loans by counterparty (YE - 2016)

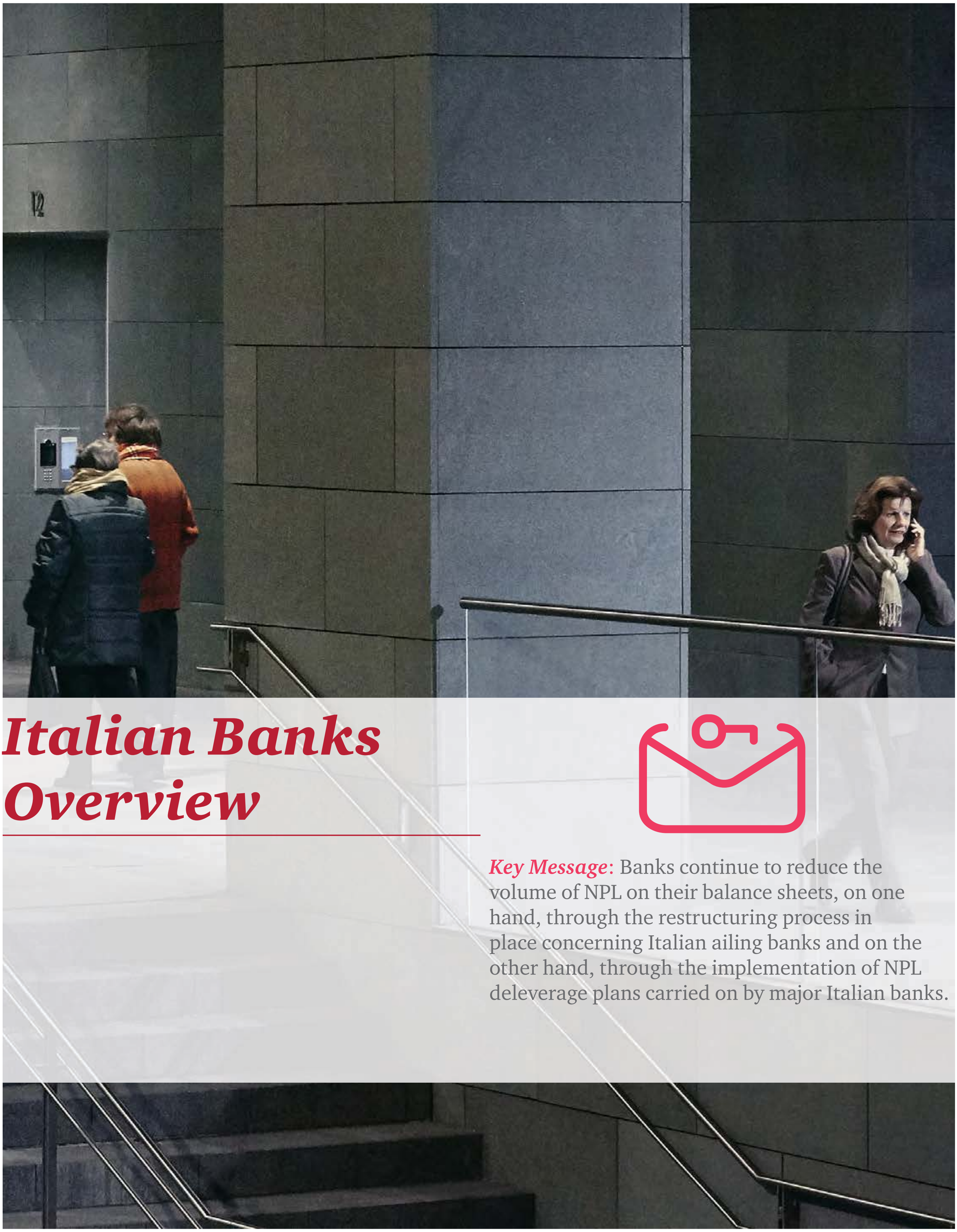


Source: PwC analysis on data of "Bollettino Statistico" of Bank of Italy
** "Other" includes PA and financial institutions

Chart 10: Secured Gross Bad loans trend (% on total Bad loans)



Source: PwC analysis on data of "Bollettino Statistico" of Bank of Italy
** "Other" includes PA and financial institutions



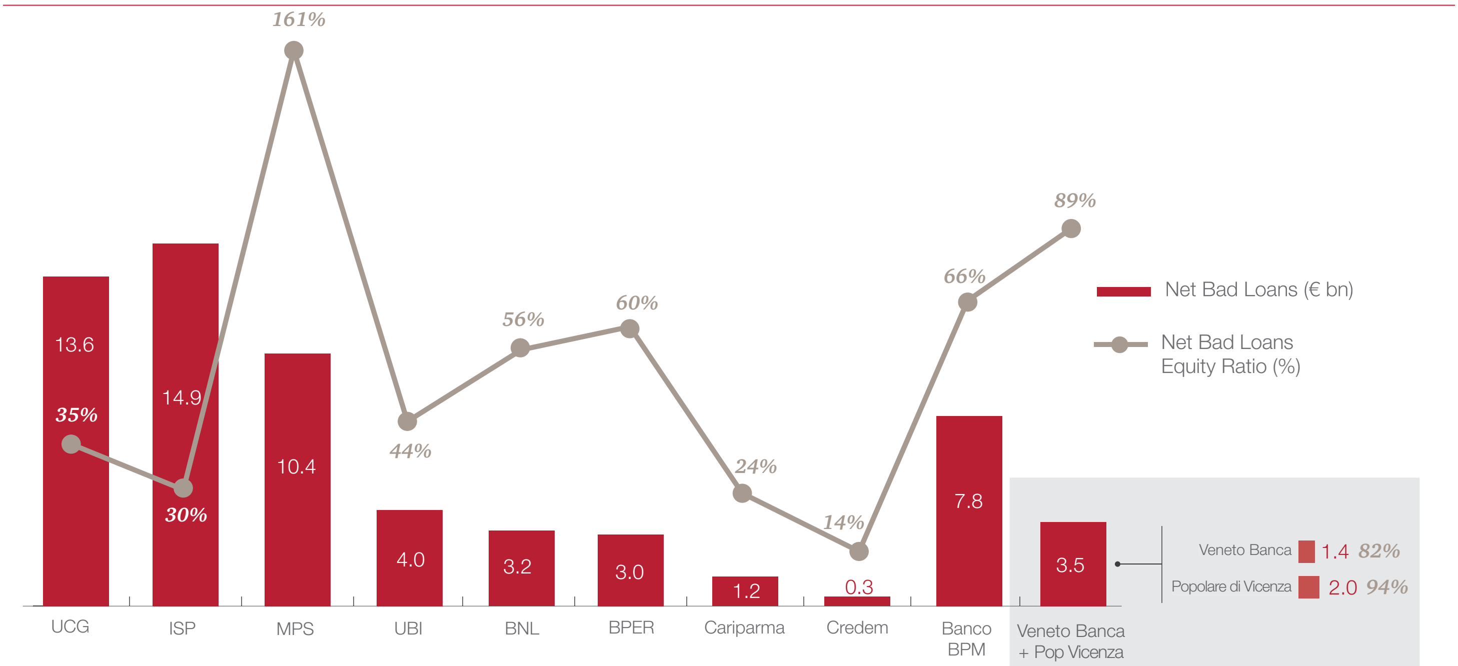
Italian Banks Overview

Key Message: Banks continue to reduce the volume of NPL on their balance sheets, on one hand, through the restructuring process in place concerning Italian ailing banks and on the other hand, through the implementation of NPL deleverage plans carried on by major Italian banks.

Recent Events

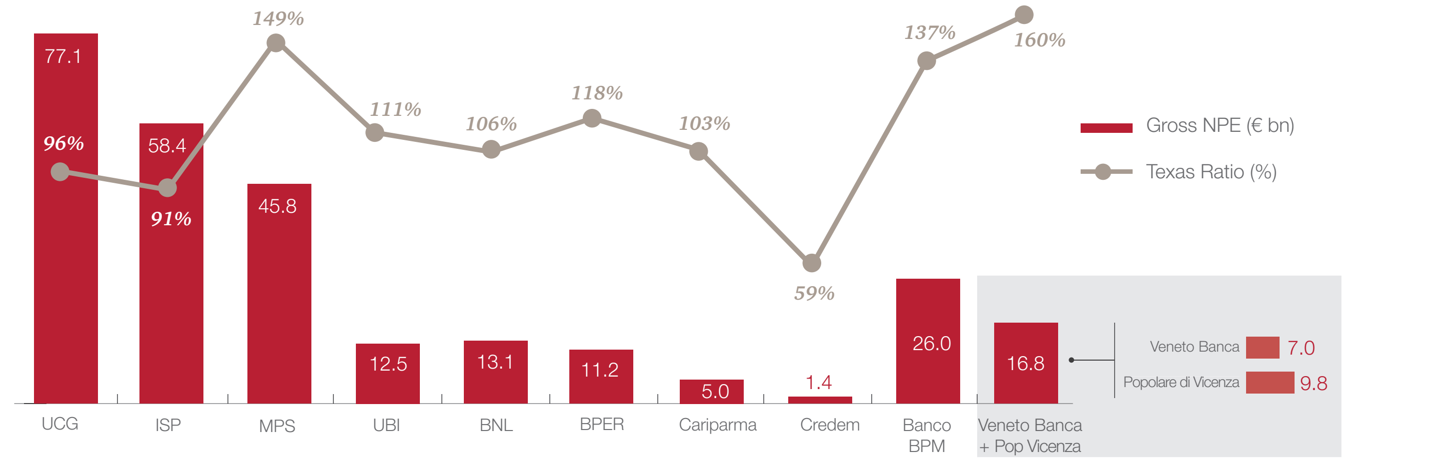
- Early this year, UCI completed the sale of €17.7bn euros bad loan portfolio to two separated securitization vehicles built, respectively, by Fortress Investment Group and Pimco, with the seller retaining a minority stake in each vehicle.
- In the meantime, ISP has closed the largest Italian NPL deal not involving a securitization this year, with Christofferson, Robb & Co. and Bayview buyers of ca €2.5bn (Project Beyond the Clouds).
- Algebris Investments reached an agreement to buy €750m from Banco BPM (Project Rainbow).
- In May 2017 UBI acquired three regional lenders (Banca Marche, BPEL and CariChieti) and BPER acquired the regional bank CariFerrara, following their rescue in 2015 by Italian Authorities and the sale of their NPL to the bad bank "REV"(€10,3bn) in 2015 and to Atlante Fund (€2,2bn) in 2017.
- MPS will dispose of its entire NPL portfolio, with a GBV of ca €29.4bn at the end 2016. The Board of Directors of MPS resolved to grant exclusive NPL securitisation talks to Quaestio Capital Management, on behalf of Atlante II.
- On 25 June 2017, the Italian Government enacted the Decree n.98 stating the acquisition of certain asset (excluding NPE) and liabilities of Banca Popolare di Vicenza and Veneto Banca by Intesa Sanpaolo as well as the liquiditation of their NPL (€ 16.8bn at the end of 2016) through the public Bad Bank "SGA".

Chart 11: Net Bad Loans and Equity for the Top 10 Italian Banks



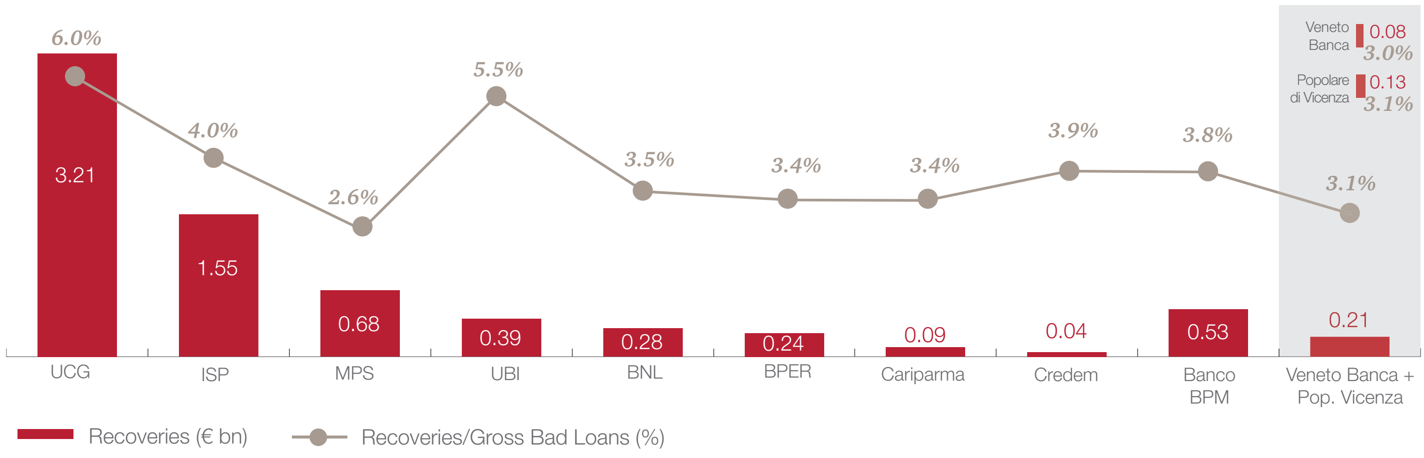
Source: Financial Statements as of YE-2016. Data affected by different write-off policies.

Chart 12: Gross NPE and Texas ratio for the Top 10 Italian Banks



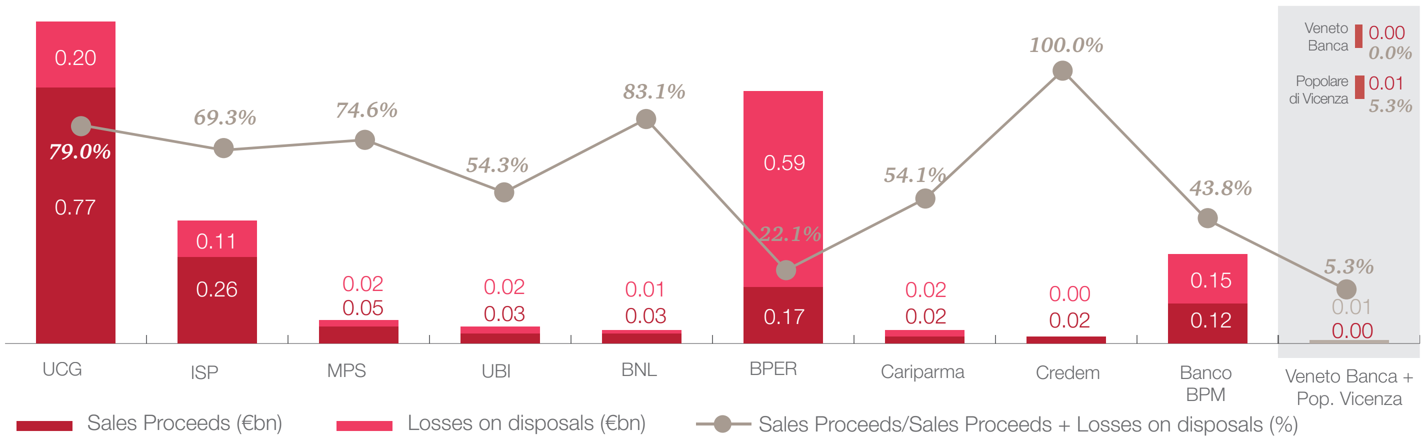
Source: Financial Statements as of YE-2016. Data affected by different write-off policies.
* Texas ratio defined as the ratio between total Gross NPE and the sum of CET1 and provisions

Chart 13: Recoveries/Gross Bad Loans for the Top 10 Italian Banks



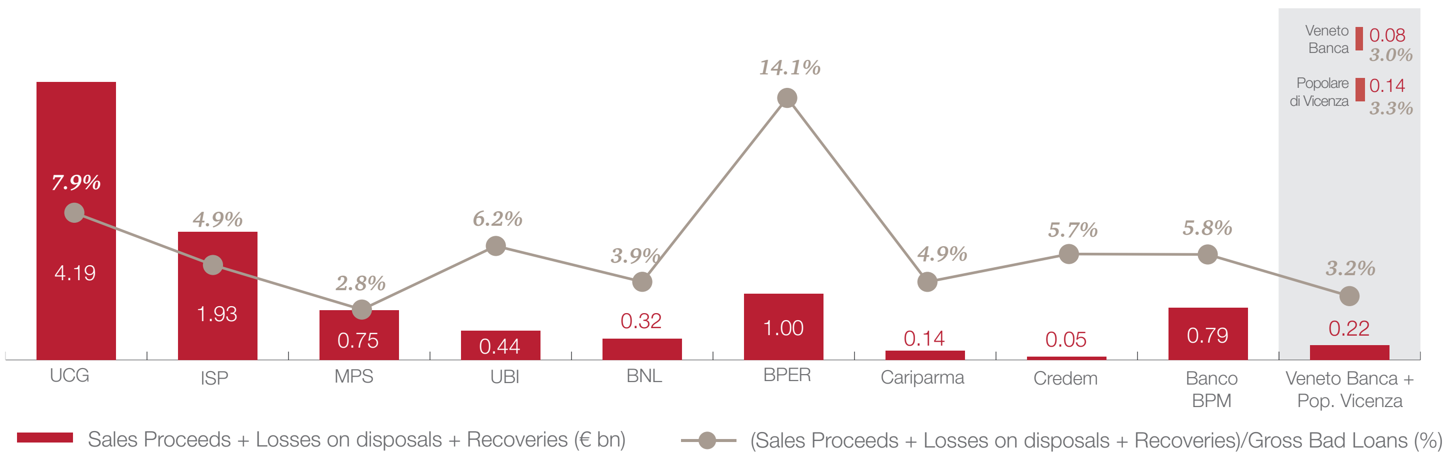
Source: Financial Statements as of YE-2016. Data affected by different write-off policies

Chart 14: Sales Proceeds/(Sales Proceeds + Losses on disposals) for the Top 10 Italian Banks



Source: Financial Statements as of YE-2016. Data affected by different write-off policies

Chart 15: (Sales Proceeds + Losses on disposals + Recoveries)/Gross Bad Loans for the Top 10 Italian Banks

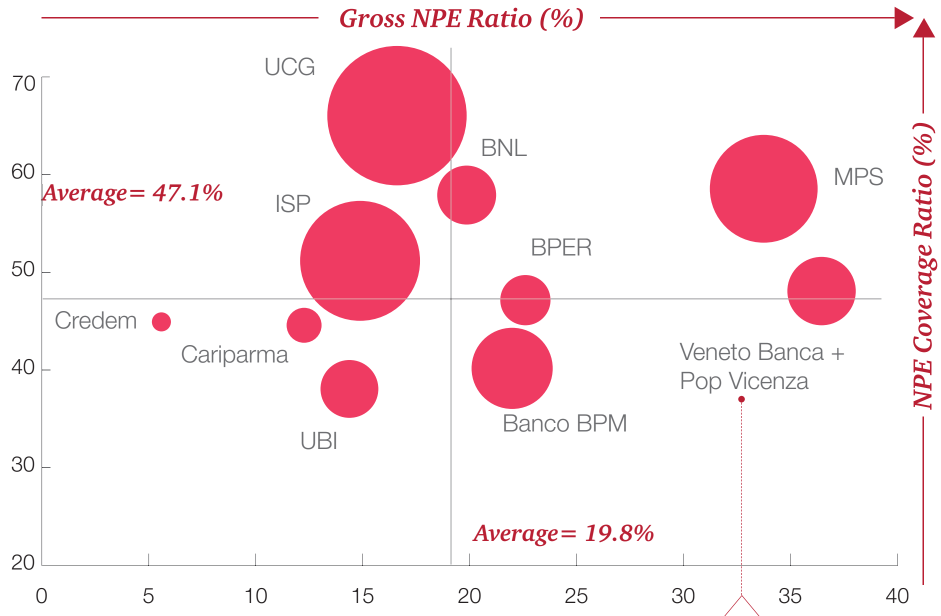


Source: Financial Statements as of YE-2016. Data affected by different write-off policies

Chart 16 provides a snapshot of the Top 10 Italian banks' positioning considering the gross NPL ratio, with an average of 19.8%, and the coverage ratio, with an average of 47.1%.Is clear that there is a strong variance among Italian banks analyzed; in fact, there is a huge gap in terms of gross NPL ratio: Veneto Banca with Popolare di Vicenza reaches the highest point (36.9%) while Credem shows the lower extreme (5.8%).On the other hand, considering the NPL coverage ratio, UGC reaches the peak of 62.8% while UBI stands at 35.7%. However, we note that the coverage ratio is not directly comparable as it is influenced by several factors which vary among the different banks (such as policies on write-offs, level of collateralization of the loans, vintage of the portfolio).

Chart 17 illustrates the Bad Loans ratio and coverage ratio for the banks analyzed. Also in this case there are significant differences comparing the banks. MPS shows the highest ratio for the gross Bad Loans with 22.1% where the average is 11.9% (Credem is the last one in this special rank with 3.5%). Considering the bad loans coverage ratio, which average is equal to 58.8%, at the maximum extreme there is still MPS with 64.8%, while at the minimum UBI with 45.1%.

Chart 16: Top 10 Italian Banks – NPL Peer Analysis as of YE-2016

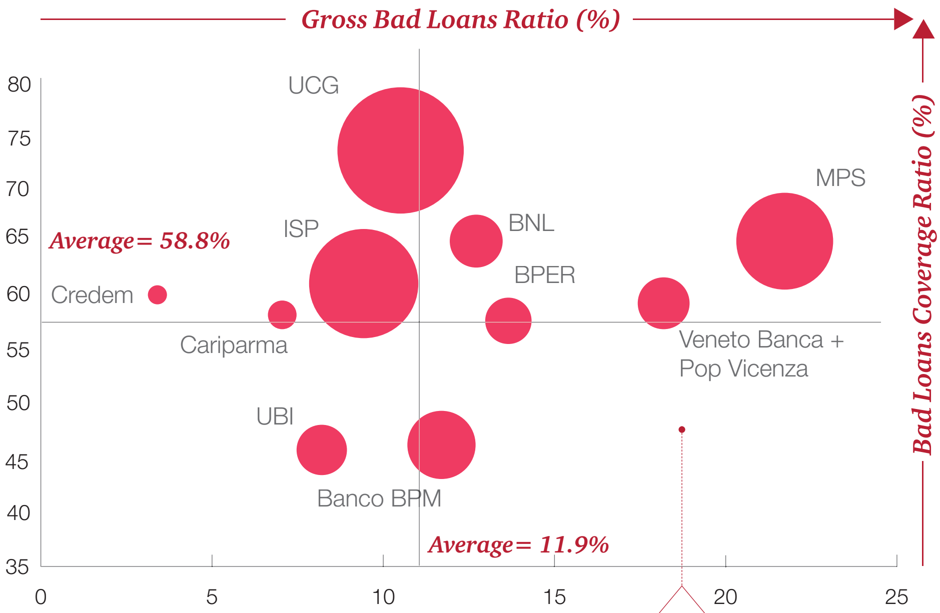


Bubble size: Gross NPE

Bank	Gross NPE Ratio (%)	NPE Coverage Radio (%)	Gross NPE (€bn)
Veneto Banca	38.5%	43.4%	6,967
Pop Vicenza	35.8%	47.3%	9,800

Source: Financial statements as of YE-2016. Data affected by different write-off policies

Chart 17: Top 10 Italian Banks – Bad Loans Peer Analysis as of YE-2016



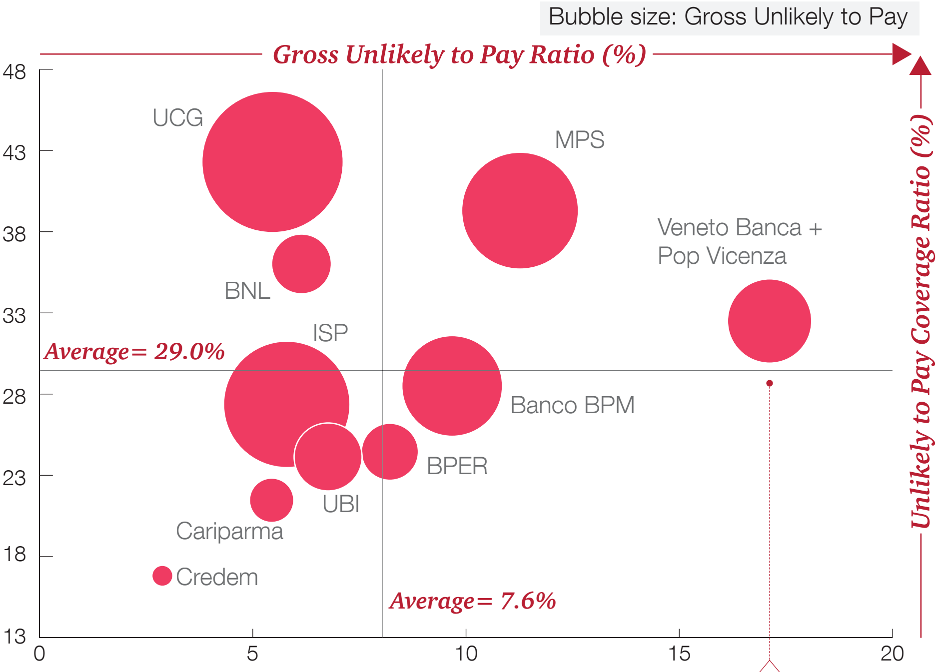
Bubble size: Gross Bad Loans

Bank	Gross Bad Loans Ratio (%)	Bad Loans Coverage Radio (%)	Gross Bad Loans (€bn)
Veneto Banca	18.3%	56.7%	3.313
Pop Vicenza	18.7%	60.5%	5.116

Source: Financial statements as of YE-2016. Data affected by different write-off policies

Chart 18 provides an image of the gross Unlikely to Pay ratio and its Coverage ratio. Veneto Banca with Popolare di Vicenza shows the highest ratio with 17.9%. At the same time the lowest is Credem with 2.1% (average 7.6%). The situation is different when comparing the Coverage ratio: UGC is at 43.1% and at the bottom of these banks Credem is at 15.6% (average 29%). Comparison among banks needs to consider the underlying type of borrower and credit concern, probability of default estimate and rating of the borrower as well as criteria / policy used to grant a restructuring and the type of restructuring.

Chart 18: Top 10 Italian Banks – Unlikely to Pay Peer Analysis as of YE-2016

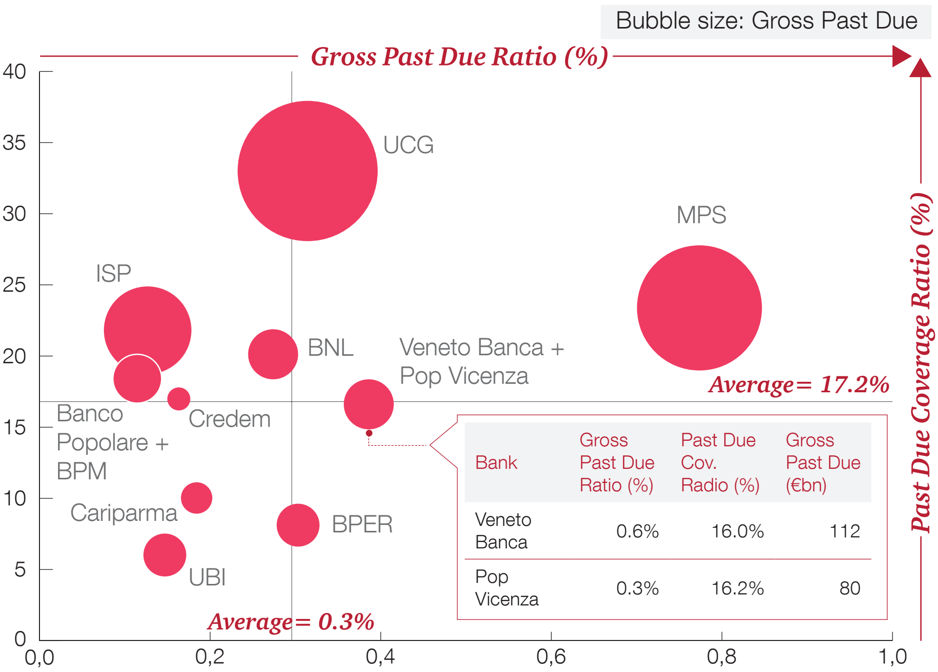


Bank	Gross Unlikely to Pay Ratio (%)	Unlikely to Pay Cov. Radio (%)	Gross Unlikely to Pay (€bn)
Veneto Banca	19.6%	31.7%	3,542
Pop Vicenza	16.8%	33.3%	4,603

Source: Financial statements as of YE-2016. Data affected by different write-off policies

Chart 19 illustrates the Past Due ratio and the coverage for the banks analyzed. The average for the first of them is 0.3% and for the second 17.2%. The Past Due Coverage ratio shows a gap from UCG with 32.9% to UBI with 5.7%.Differently from all the other cases, small variance exists among the banks, with the exception of MPS which records the highest gross Past Due Ratio (0.8%).

Chart 19: Top 10 Italian Banks – Past Due Peer Analysis as of YE-2016



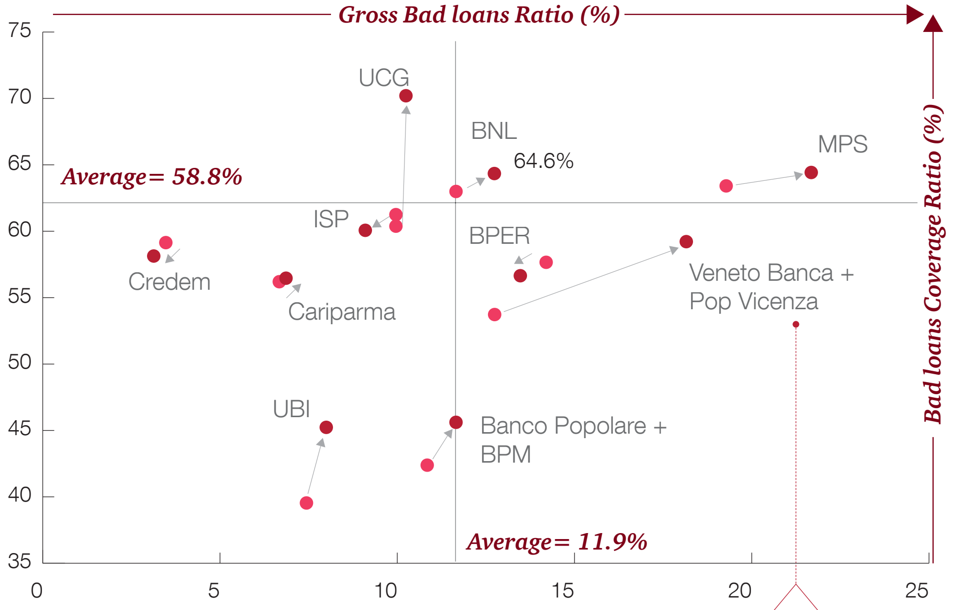
Bank	Gross Past Due Ratio (%)	Past Due Cov. Radio (%)	Gross Past Due (€bn)
Veneto Banca	0.6%	16.0%	112
Pop Vicenza	0.3%	16.2%	80

Source: Financial statements as of YE-2016. Data affected by different write-off policies

Chart 20 shows that, compared to YE-2015, the YE-2016 snapshot indicates that UCG (+20,2%), UBI (+16,7%), Banco Popolare + BPM (+8,4%) and Veneto Banca + Pop Vicenza (9,7%) have substantially increased their Bad Loans coverage level whereas Veneto Banca + Pop Vicenza (+40,4%) and MPS (+12,1%) have both worsened their gross Bad Loans ratio compared to YE-2015. Slight or no material changes have been recorded for other banks.

● YE 2015 ● YE 2016

Chart 20: Top Italian Banks – Bad Loans movements (YE-2015 vs YE-2016)



Bank	Gross Bad Loans Ratio (%)	Bad loans Cov. Ratio (%)	
Veneto Banca	11.9%	53.4%	YE 2015
Pop Vicenza	14.2%	54.0%	

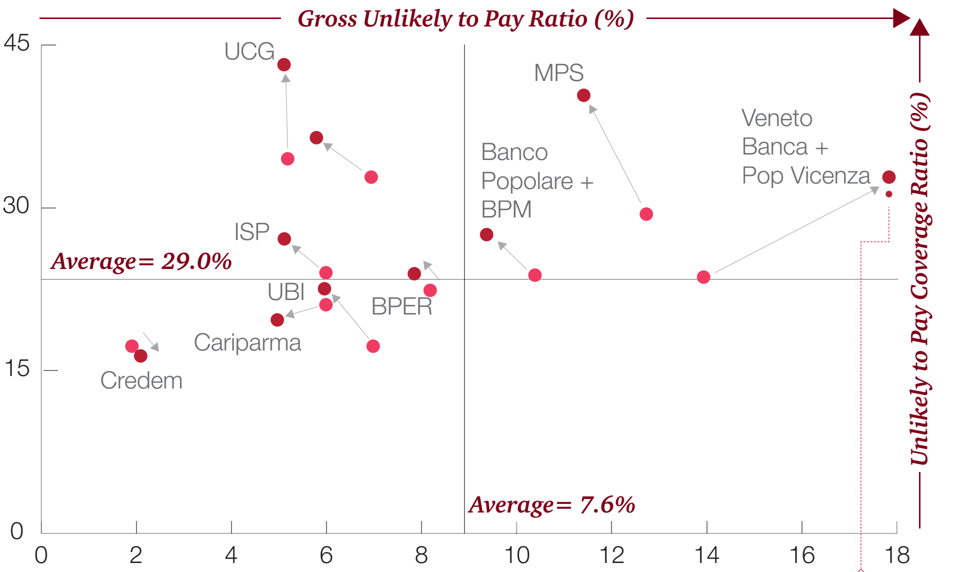
Bank	Gross Bad Loans Ratio (%)	Bad loans Cov. Ratio (%)	
Veneto Banca	18.3%	56.7%	YE 2016
Pop Vicenza	18.7%	60.5%	

Source: Financial Statements as of YE-2015 (Rose), YE-2016 (Burgundy). Data affected by different write-off policies

Chart 21 illustrates the movements in the Unlikely to Pay NPL ratio and the Unlikely to Pay Coverage ratio between 2015 and 2016. Veneto Banca and Popolare Vicenza shows the highest value of the Unlikely to Pay Ratio in 2016 (17.9%), while UCG has the highest Unlikely to Pay Coverage ratio (43.1%) in the same period. The average net change between 2015 and 2016 in the Unlikely to Pay NPL Ratio is -3.4% and +17.5% in the Unlikely to Pay Coverage ratio. The average Unlikely to Pay NPL Ratio stands at 7.6% in 2016, while the Unlikely to Pay Coverage ratio is 29.0% in the same period.

● YE 2015 ● YE 2016

Chart 21: Top Italian Banks – Unlikely to Pay movements (YE-2015 vs YE-2016)



Bank	Unlikely to Pay NPL Ratio (%)	Unlikely to Pay Cov. Ratio (%)	
Veneto Banca	12.1%	22.7%	YE 2015
Pop Vicenza	15.3%	25.8%	

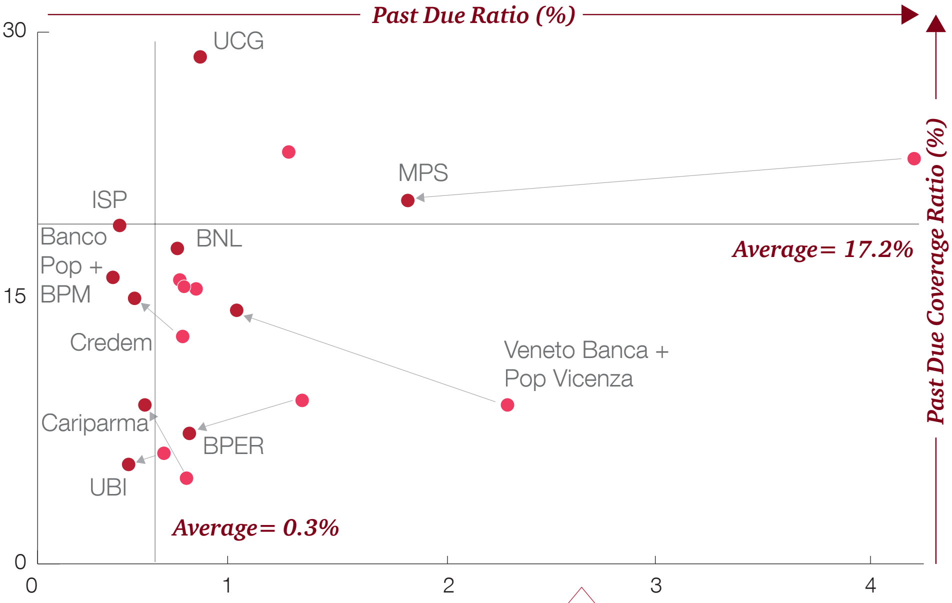
Bank	Unlikely to Pay NPL Ratio (%)	Unlikely to Pay Cov. Ratio (%)	
Veneto Banca	19.6%	31.7%	YE 2016
Pop Vicenza	16.8%	33.3%	

Source: Financial Statements as of YE-2015 (Rose), YE-2016 (Burgundy). Data affected by different write-off policies

Chart 22 shows the movements in the Past Due ratio and Past Due Coverage ratio. It is easy to note a strong reduction in the Past Due ratio (change of – 50.6%) between 2015 and 2016, while the Past Due Coverage ratio increase significantly (14.0% change) in the same period. The average Past Due Ratio in 2016 is 0.3%, halved compared to the previous year value, while the Past Due Coverage ratio for the same year stands at 17.2%. In 2016, MPS shows the highest Past Due Ratio (0.8%), while UCG is the most solid bank among those considered in terms of Past Due Coverage ratio (32.9%).

● YE 2015 ● YE 2016

Chart 22: Top Italian Banks – Past Due movements (YE-2015 vs YE-2016)

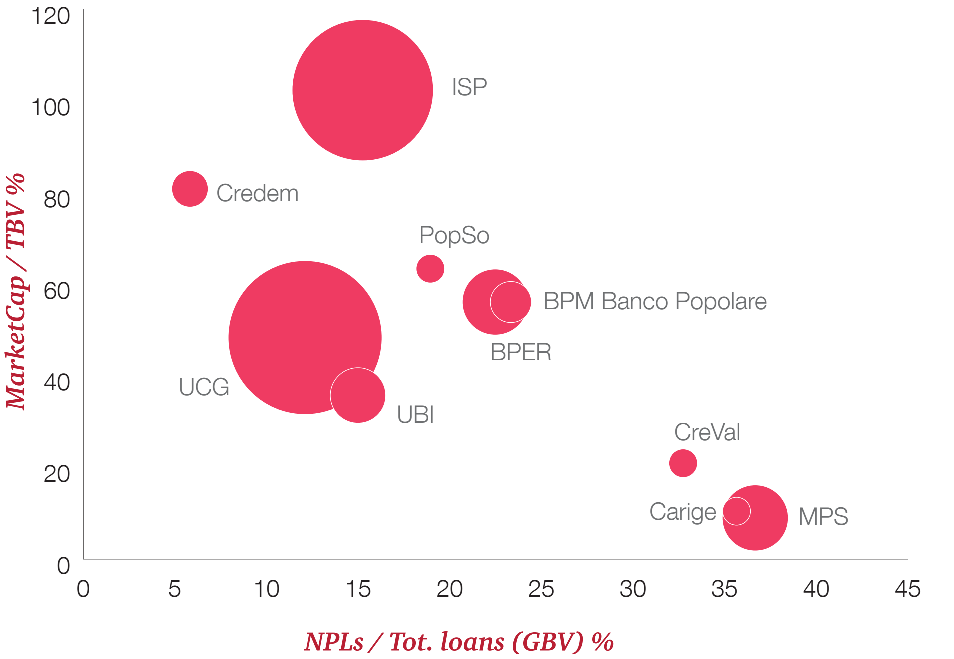


Bank	Past Due Ratio (%)	Past Due Coverage Ratio (%)		Bank	Past Due Ratio (%)	Past Due Coverage Ratio (%)	
Veneto Banca	1.8%	8.9%	YE 2015	Veneto Banca	0.6%	16.0%	YE 2016
Pop Vicenza	0.5%	12.2%		Pop Vicenza	0.3%	16.2%	

Source: Financial Statements as of YE-2015 (Rose), YE-2016 (Burgundy). Data affected by different write-off policies

Chart 23 shows the relation between the market cap of listed Italian Banks and their NPL ratios.

Chart 23: Relation between MarketCap/TBV and NPL ratio



Source: Financial Statements as of YE-2016. Data affected by different write-off policies

Focus on UTP Italian market

Key Message: Unlikely to Pay exposures are the new challenge for the Italian banks within the NPL sector. At the end of 2016, the UTP volumes, still lower than Bad Loans in terms of GBV (€ 117 bn vs € 200 bn) are by now overcoming the Bad Loans in terms of NBV (€ 87bn). Only by a renovated proactive management of these exposures, the Italian banks could find the most effective deleverage solutions to address the issue of their volumes.

Our view

The volume of UTP, lower than bad loans in terms of GBV (€117bn vs €200bn) but by now overcoming the Bad Loans in terms of NBV (€87bn), will require the adoption and implementation of a renovated strategic management and deleverage approach by the Italian banks.

ECB guidelines provide a great opportunity to renovate and improve the proactive management of NPE to address the issue of their massive stock.

Moreover IFRS9, in place from 1 January 2018, will lead to an «early warning» and «forward looking» approach, which could likely result in higher reclassification of performing loans to NPE/UTP and overall higher provisions.

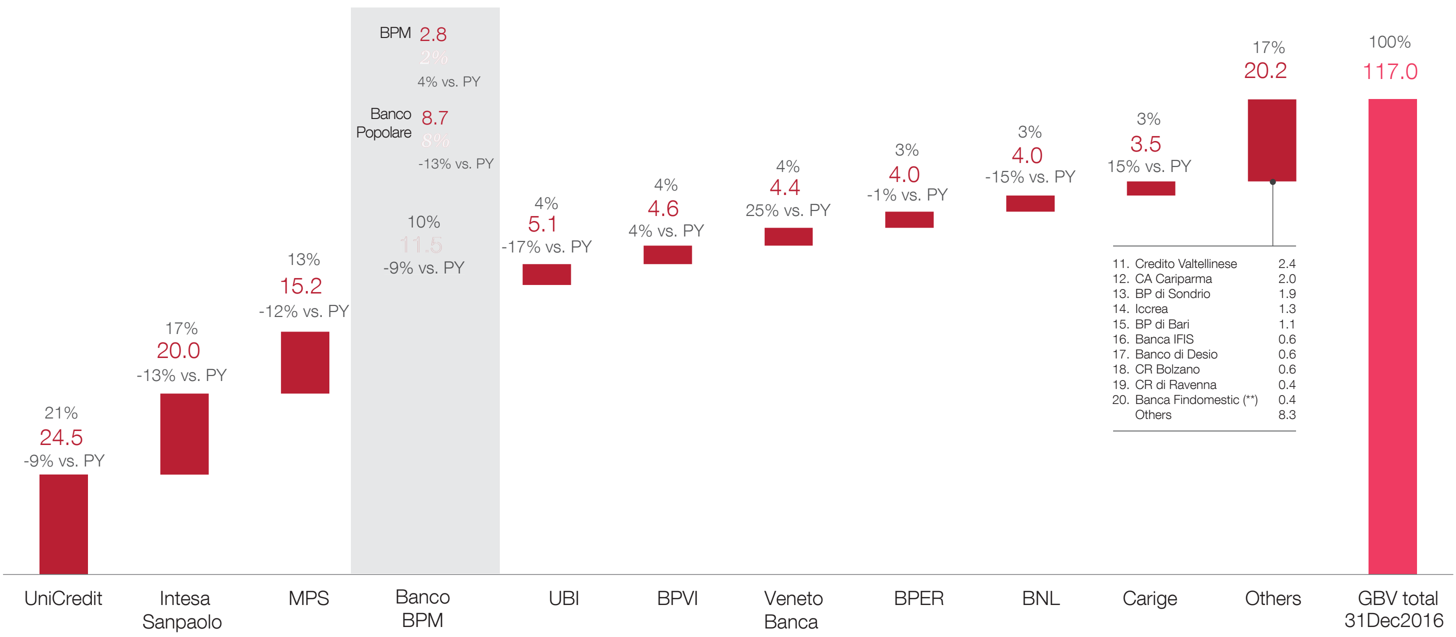
Only by focusing the efforts in the proactive management of their UTP exposures, the Italian banks could aim at deleveraging their UTP, through higher collection, higher cure rates to performing loans, lower danger rates to bad loans.

The proactive management of UTP should cover three main issues: (i) data quality and preliminary strategic portfolio segmentation, (ii) accurate analysis of the borrowers and integrated single names' management and (iii) implementation of the most appropriate strategic option to identify among forbearance measures, cash injection (equity/ debt) even through third investors, loan sales and liquidation procedures.

In other words, the proactive management of UTP is without a doubt a complex issue entailing and requiring due diligence, data quality, restructuring, turnaround management and M&A/special situation expertise.

At the end 2016, the UTP exposure amounted to €117bn showing a declining trend vs YE2015 (-8%). 93% of the overall amount is concentrated within the Top 20 Banks

Chart 24: Unlikely to Pay distribution among Top 20 banks (FY16;€bn)



UniCredit	Intesa Sanpaolo	MPS	Banco BPM	UBI	BPVI	Veneto Banca	BPER	BNL	Carige	
32%	34%	33%	44%	41%	47%	48%	36%	30%	48%	Gross UTP/Gross NPE
15%	15%	34%	22%	14%	36%	39%	22%	19%	34%	Gross NPE Ratio

Banco Popolare	BPM
44%	44%
24%	17%

(*) Volumes of Banco BPM were calculated as sum of the figures of Banco Popolare and BPM (merged together in Banco BMP from 1 January 2017)
(**) Banca Findomestic UTP exposure as at 31Dec15; ICCREA UTP exposure as at 30 Jun16

Inflows and outflows

In 2016, total outflows of the Top 20 Italian banks slightly decreased from €51.1bn to €49.9bn primarily driven by lower outflows to bad loans: 23% in 2015 vs 21% in 2016. (*)

The inflows in 2016 decreased as well (from € 52.1bn to 41.5bn) mainly due to the lower inflows from performing exposures. (*)

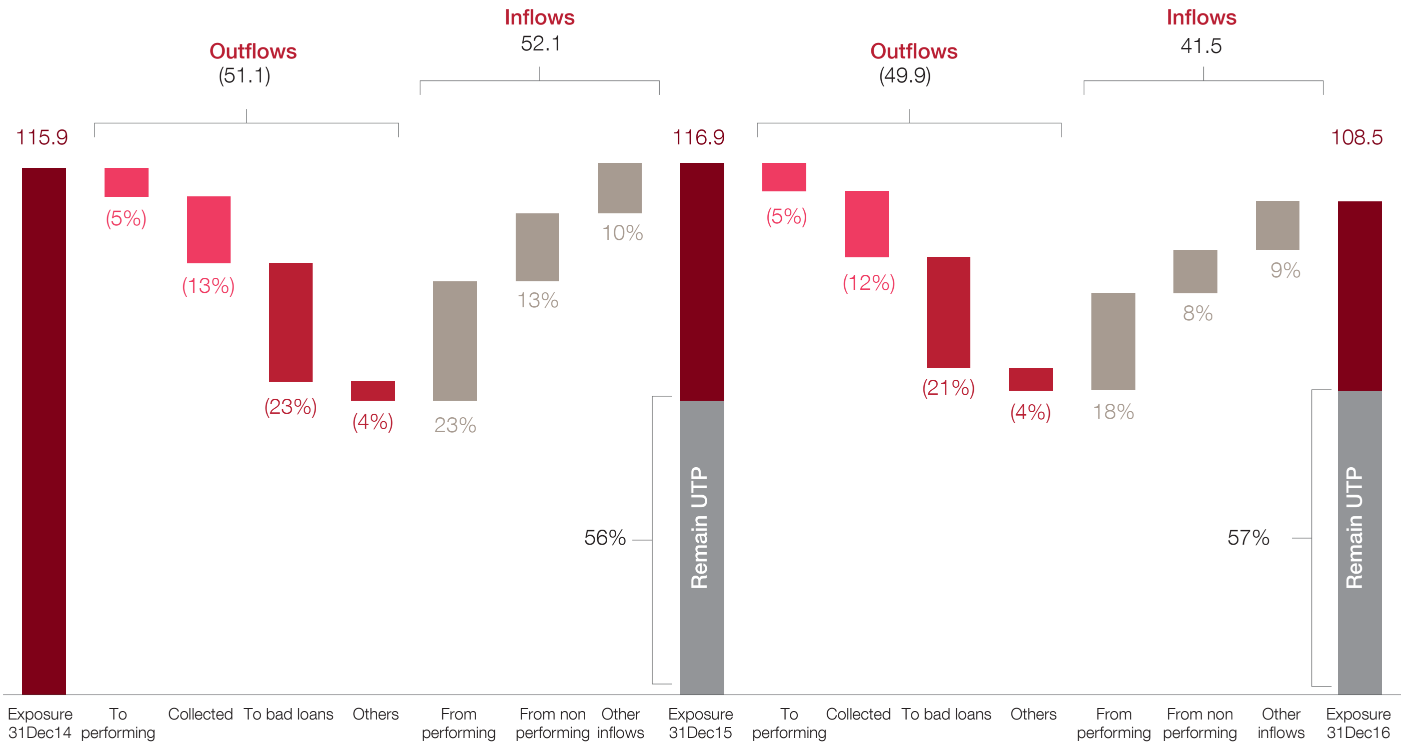
As for the outflows, the UTP gauged a firm decline of inflows from performing loans over the last 2-year period: 23% in 2015 vs 18% in 2016.

UTP which remained UTP during 2016 amounted to €61.8bn i.e. 57%, proving how the main issue for the Italian UTP lies mainly in their massive stock and a management not yet able to target deleveraging solutions.

In particular, according to Bank of Italy, 62.5% of the restructuring agreements (which qualify most of the UTP exposures) after 3 years are still in place (49% after 4 years) and did not result in a positive and conclusive outcome (i.e. after 4 years 40.9% of the restructuring agreements resulted in liquidation/bankruptcy procedures).

At the end of 2016, despite the decreased outflows to bad loans (-2%) and inflows from performing (-5%) compared to 2015, 57% of UTP remained as such. The UTP challenge lies in the management of their massive stock.

Chart 25: Unlikely to Pay inflows and outflows from 2014 to 2016 - Top 20 banks FY16 (€bn)



$$\% \ flows = \frac{In/Outflow}{Initial\ exposure}$$

(*) Inflows and outflows in 2016 for ICCREA and Banca Findomestic were estimated equal to the flows occurred in 2015 (to date their financial statements as at 31Dec16 are not yet available)

Performance Top 20 and total Italian Market

For the Top 20 Italian banks, the portions of UTP returned to performing slightly increased from 2014 (3.8%) to 2016 (3.9%).

A similar trend for the cure rate was confirmed even for the Italian banking market (3.6% in 2014 v.s. 3.7% in 2015).

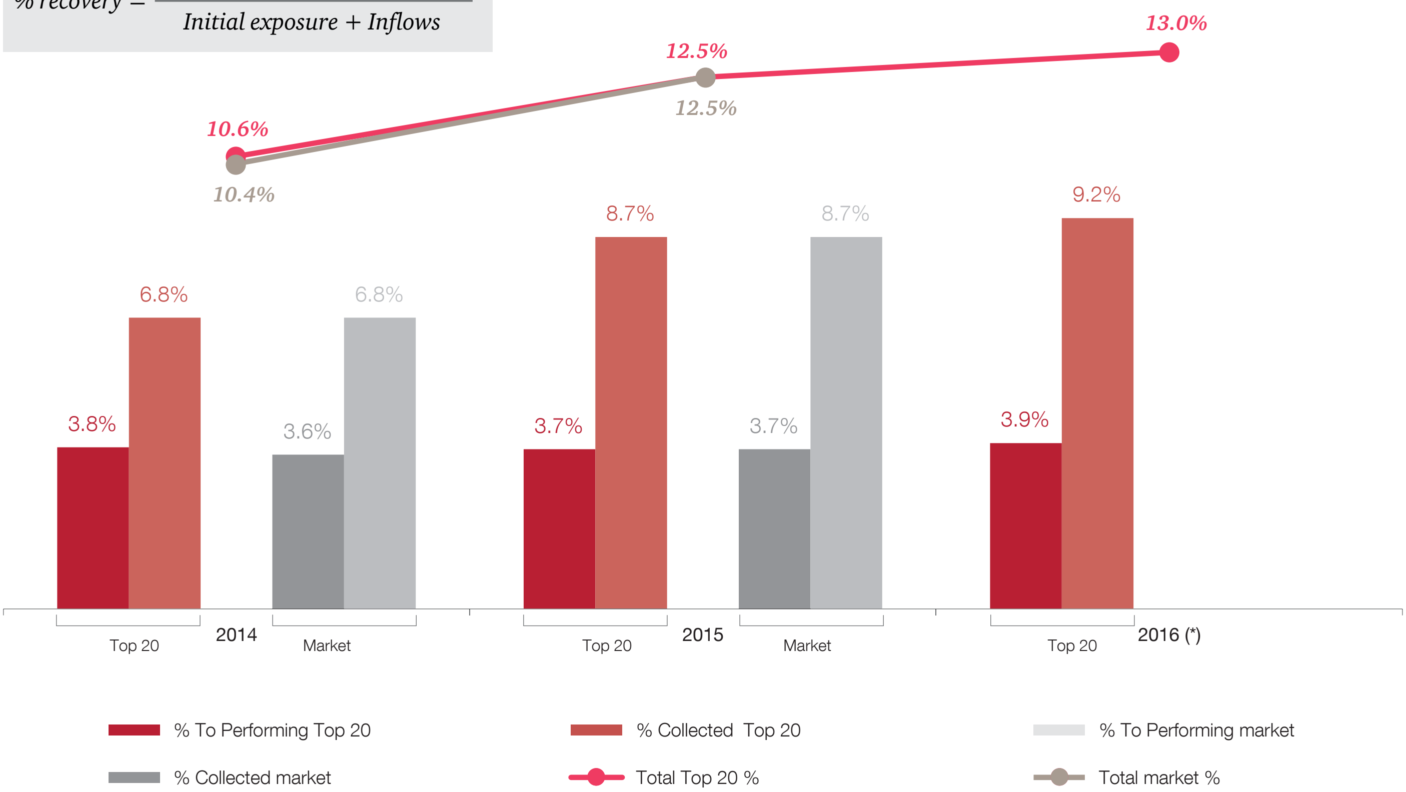
For the Top 20 Italian banks, the collections of UTP increased regurarly over the period 2014/2016 from 6.8% to 9.2%.

A similar trend is confirmed for the overall Italian banking sector.

UTP collections and returns to performing increased from 2014 to 2016, even if the figures are still low. Solely through a proactive management of UTP, cure rates and collections could further arise.

Chart 26: UTP performance from 2014 to 2016 – collections and returns to performing

$$\%\ recovery = \frac{Exit\ to\ performing\ /\ collection}{Initial\ exposure + Inflows}$$



(*) Figures for 2016 do not include returns to performing and collections for ICCREA and Banca Findomestic

Our view about what banks should do for a proactive management of UTP

1. Carry on portfolio segmentations for
(i) a better understanding of the asset quality of their UTP,
(ii) a proper classification of the portfolio and
(iii) a preliminary identification of management strategies

2. Perform analysis on borrowers' financial statements/ updated quarterly reports/ Business Plan, Budget and any further financial documentation about the borrowers' performance and financial position.

3. Regularly monitor the Central Credit Register to be informed on the total exposure to the system and relevant movements (overdraft withdrew or decrease, bad loan classification).

4. Use early warning indicators: from internal (companies and individuals) and external sourcer.

5. Produce and regularly update an overall rating on borrowers' overall risk based upon info gathered from several sources.

Market risks
(external variables such as those regarding the environment where the borrowers operate)

Operational risks
(risks concerning the operational structure of the borrowers)

Financial risks
(financial soundness of the borrowers and / or relevant customers and / or suppliers)

6. Implement improved NPE operating model: dedicated workout units, procedures for classification and segmentation, tailor made management strategies on a single name basis.

UTP need to be moved out of their hybrid condition. Banks should carry on portfolio segmentation to better understand their UTP asset quality as well as implement a due diligence approach on a single name basis to identify the most effective and efficient deleverage strategy for their UTP. Different options might be available and vary case by case.

Our view on the available strategies for UTP

The strategic options identified through the on going due diligence carried out by the bank on the borrower's case could result in the return of the loan in the performing category or in the sale of the loan or in the classification of the exposure as bad loans (thus requiring the prompt liquidation of the borrower's asset through judicial procedures).

Sale of UTP could be even executed through portfolios transactions which require preliminary strategic segmentation to maximize loans' value for the banks.

Following the improved proactive management, banks could identify the most effective and efficient solutions to deleverage their UTP (e.g. return to performing, collection) among several strategic options. Solely a proactive management of UTP could lead to the right "tailor made" strategic solution.

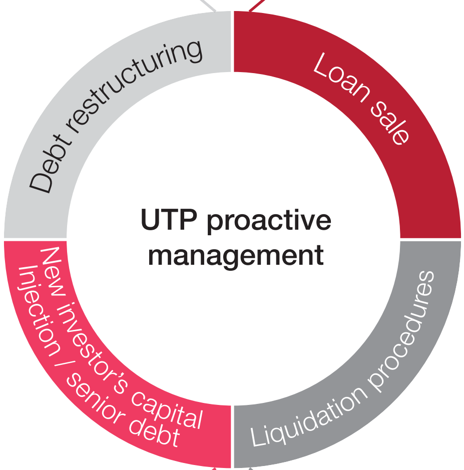
Potential return to performing

Forbearance measures

- Grace period / Payment moratorium
- Extension of maturity / term
- Debt consolidation
- New credit facilities
- Recovery plan ex art 67 Italian Bankruptcy Law
- Debt restructuring ex art 182bis
- Italian Bankruptcy Law

Investor's equity injection / underwriting of senior debt

- Industrial partner to revamp and establish the underlying borrower's business (long term approach)
- Financial partner to inject cash within a strategic exit plan (short/medium term approach)



Loan sale

- True sale (full derecognition purposes)
- Securitisation (to attract wider investors' base)
- Partial loan transfer (to share risks and opportunities with new investors)

Liquidation procedures

- Voluntary liquidation of collateral by the debtor (also foreseen within the forbearance measures)
- Judicial procedures to sell the borrower's (guaranteed) asset after preliminary assessment of liquidation value and timing of the procedure

Classification to bad loan

Our view on the requirements arisen from the adoption of IFRS9 for the Italian banks

The transition to IFRS 9 (from IAS 39) will be critical as banks will be required to accrue provisions based on expected losses and not only upon the occurrence of specific events (e.g. "impairment tests"). Banks will be asked to adopt a "forward looking" approach and as such to anticipate losses at the first signals of deterioration.

As a result, specific instruments as well as right structure and skilled people to proactively monitor borrowers' performances will be required.

Starting from 2018, we expect that a higher portion of loans might be at risk to be reclassified in loans' higher risk categories following the introduction of a different valuation approach (from "ex post" to "forward looking").

Classification

New classification criteria will lead to 3 new classes of loans ("Hold to collect", "Hold to collect and sale", "Trading"). The need to properly classify their exposures will require the bank to review and strategically refine their business model associated to the loans' management:

- On the one hand, for the "portfolio to hold", banks should strenghten the internal credit monitoring functions in terms of expertise as well as of renovated tools of credit risk measurement (e.g. KPI, index, advanced CRM solutions).

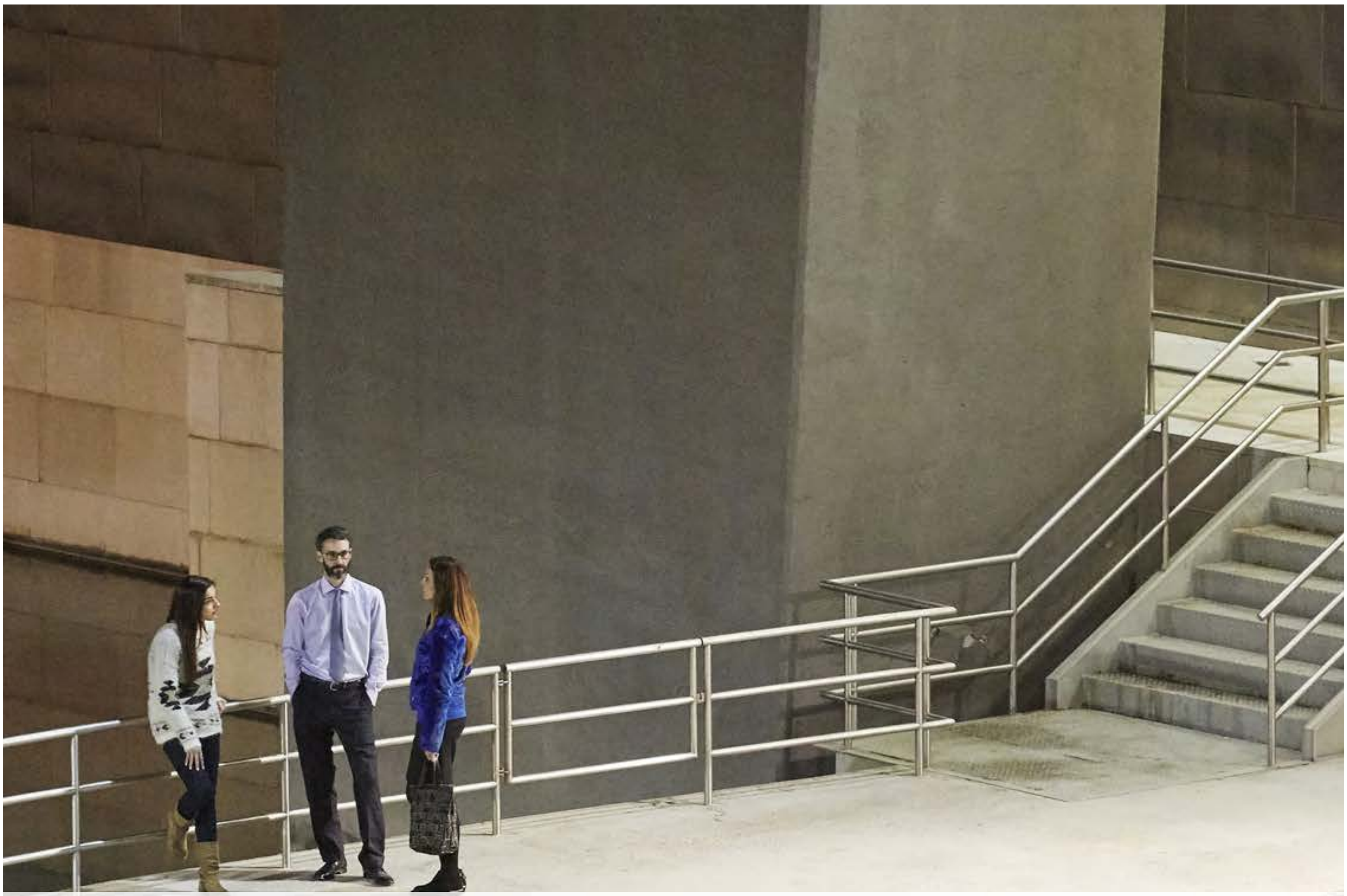
- On the other hand, for the "portfolio to sell", banks should implement specialised units in charge of the structuring and execution of loans' sale transactions (e.g. data preparation and remediation, securitisation).

Impairment

- New impairment criteria, based on the "expected loss" and "forward looking“ approach, will result in certain portions of the current portfolio classified in loans' higher risk categories (e.g. from performing to UTP/ bad loans).

- Higher impairment (by collective and analytical provisioning) will result through the "forward looking" approach which will move up losses to be incurred over the loans' lifetime.

- Need to foresee the lifetime losses will require the banks to implement proactive actions to preliminarly assess borrowers' likelyhood to pays their debts and avoiding further danger rate from performing to UTP and bad loans.



The Servicing Market

Key Message: The credit management industry, in particular the NPL servicing segment, is experiencing a strong evolution, mainly driven by several independent (non-captive) players. As a result, the servicing market displays, on one hand, consolidation movements among the players and, on the other hand, new M&A opportunities. Furthermore, new UTP exposures' deleverage approach carried out by Italian banks could drive further opportunities to the NPL servicing industry.

The NPLs and the credit servicing structures

The growth of non performing loans in the last decade has not been followed, at the same pace, by the evolution of the industrial recovery capacity, both under a qualitative and quantitative perspective. As recently outlined by Bank of Italy in a research note on bad loans ("Note di stabilità finanziaria e di vigilanza", January 2017), recovery rates are found to vary significantly from bank to bank, confirming the urgency to improve credit management and recovery processes.

Managing and recovering NPLs requires significant resources and investments, and Banks are responding with different approaches. While some are strengthening internal recovery capabilities, others are either disposing non-performing assets to Investors such as PE funds, or outsourcing recovery activities entering in relationships with independent servicers.

Independent servicers (we identify independent servicers as players not under the control of the Bank('s) originating the NPL) play a key role in supporting both Banks and Investors in improving recovery performance and reducing management costs. Despite recent improvements in the servicing sector in terms of structure and capabilities, there is still a long way to go to develop a robust service offering, able to support credit management of one of the largest NPL markets in Europe with total gross bad loan gross to be recovered, estimated in the range of 260bn, including other financial institutions and Investor portfolios.

The credit management industry, in particular the NPL servicing segment, is experiencing a strong evolution. The role of independent specialized NPL servicers is gaining importance driven by increasing volumes of portfolio disposals from Banks to Investors, together with growing outsourcing of recovery activities by Banks driven by lack of capacity, and fostered by the implementation of ECB guidelines.

Today around 40% of the Banks' bad loans are managed by specialized player; according to our estimates the percentage will progressively grow, reaching up to 60% by 2021.

Overall, independent servicers manage around €135-155bn of bad loans owned by Banks, other financial institutions and investors. Total AuM are expected to grow reaching around €200bn in the next 3 years.

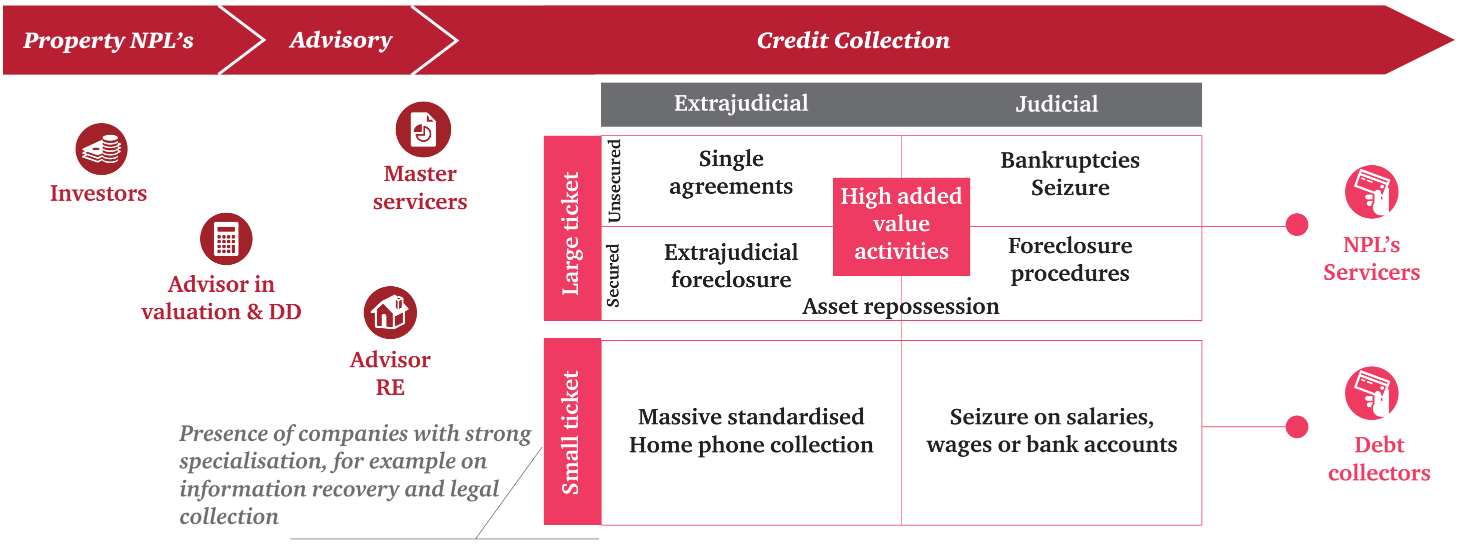
The industry structure is consequently changing, with a growing number of m&a transactions (roughly ten the most relevant ones in 2016 and 2017, usually involving international players), the establishment of new important players and the evolution of strategic positioning among different segments and business models: master servicing, special servicing, specialized services.

Furthermore, additional important growth opportunities may be connected with recovery activities of the unlikely-to-pay segment and of the performing loans, as proven by some important transactions in the segment.

Independent servicers: industry structure and ongoing dynamics

Many players, with different specialization and approach, are active in the servicing landscape. We identify three clusters: NPLs servicers, Debt Collectors and other specialized players (Chart 27).

Chart 27: Credit collection clusters, depending on size, collateral and phase of collection



- **NPL Servicers**: a limited number of specialists has a wide coverage of different non- performing loan segments, in particular corporate and secured loans. They are able to activate comprehensive and diversified credit recovery strategies, judicial and extrajudicial, with due diligence and portfolio valuation competencies. Such players, usually rated by international agencies, are often active as regulated entities (Banks or Financial intermediaries pursuant to art. 106) and/or listed in the stock market. Based on such capabilities, they have almost exclusive access to large outsourcing strategic initiatives by Banks, and provide support to investors in big portfolio acquisition or securitization processes. There is a large gap between sector leader (doBank, following the acquisition of Italfondiario) and other players, with opportunity for additional M&A and consolidation.
- **Debt Collectors**: more than 1,000 companies are active in debt collection, of which around 200 are UNIREC members representing over 80% of total revenues. They are mainly active in the unsecured/ small ticket segment, serving Banks, Financial companies (consumer lending) and Utilities. Smaller players, with local geographical reach, often operate as outsourcers of the larger DCAs.
- **Other specialized players**: other specialized or "mixed" business models are present in the Industry: investors with internally developed credit servicing platforms, master servicers (active for administrative-accounting activities, for securitization transactions and/or in the role of asset manager as general contractor for the selection and management of special servicers), real estate/legal specialists, business information specialists.

The industry structure and strategies of the various players are undergoing significant changes, adapting to the market evolution. Just as an example, many third party servicers have recently started investing directly and enlarging their capabilities (Creditech of Mediobanca Group, recently renamed as MBCredit Solutions). Other players are looking at combining these models, including master servicing (Cerved), advisory and direct investments (Credito Fondiario); in other cases, NPL management and servicing businesses have been leveraged to develop wider banking services platforms, focused on specialized lending and corporate restructuring (Banca Ifis).

Many transactions have been completed in recent years (Chart 28), while others are in progress, confirming increasing interest of investors for the sector and horizontal integration, in particular in the debt collector sector.

Chart 28: Credit collection clusters, depending on size, collateral and phase of collection

2013					
Italfondiario	**Cerved**				
Acquisition of a minority stake in BCC Gestione crediti from ICCREA	Acquisition of Tarida, specialized in consumer finance collections vith 1.9bn AuM and 250k tickets				
2014					
Hoist Finance	Banca Sistema	Cerved			
Acquisition of 100% of TRC from private shareholders. Specialized in consumer finance	Acquisition of 2 servicing platform Candia & Sting from private shareh. and merger (CS Union)	Acquisition of 80% of Recus. Specialized in collection for telcos and utilities			
2015					
Fortress	Lonestar	Cerved			
Acquisition of UniCredit captive servicing platform (UCCMB)	Acquisition of CAF a servicing platform with €7bn AuM from private shareholders	Acquisition of 100% of Fin. San Giacomo part of Credito Valtellinese group			
2016					
Axactor	Lindorff	Arrow	Kruk	doBank	Dea Capital
Acquisition of CS Union from Banca Sistema	Acquisition of CrossFactor, a small factoring and credit servicing platform	Acquisition of 100% of Zenith Service, a master servicing platform	Acquisition of 100% of Credit Base	Acquisition of 100% of Italfondiario	Acquisition of 66,3% of SPC Credit Management
2017					
Kkr	Lindorff	Bain Capital	Varde		
Acquisition of Sistemia	Acquisition of Gextra, a small ticket player from doBank	Acquisition of 100% of HARIT, servicing platform specialized in secured loans	Acquisition of 33% of Guber		

Source: Mergermarket, companies annual reports and websites

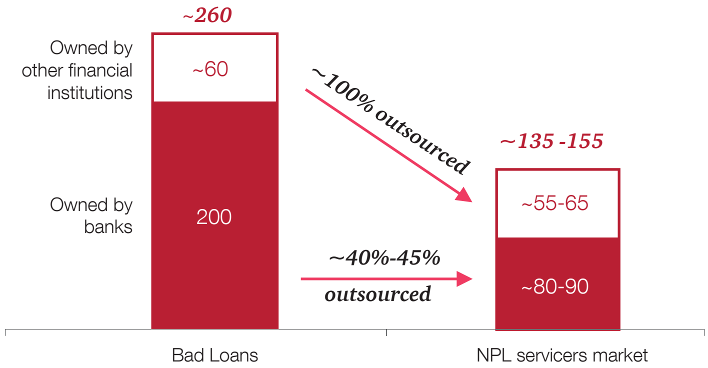
Industry size and evolution perspective

According to our estimates, as of YE 2016 NPL servicers manage approximately €135-155bn GBV of financial institutions' NPL: around €85bn GBV is outsourced by Banks (~40%-45% of bad loans owned by Banks) while the rest (~€60bn) is outsourced by Investors and other financial institutions that have limited direct servicing capabilities. We expect the share of bad loans managed by independent NPL servicers will continue to rise in the near future, reaching around €200bn by 2018. In our estimate, such growth will be mainly due to two key drivers:

1. Shift of bad loan portfolios from Banks to Investors: while total bad loans are expected to slightly decrease in the next 5 years, the increase of disposals from Banks to Investors will be a key factor for the growth of the NPL servicing market.
2. Increasing outsourcing from Banks: in the medium term, additional dynamics are likely to emerge from "make or buy" strategic initiatives regarding bad loan servicing platforms of Banks. In our view, both the implementation of ECB guidelines on the management of NPLs and GACS legislation, which requires independent special servicers for bad loans securitized under GACS scheme, will drive increasing research for specialization and quality of servicing. This will push outsourcing levels and generate opportunities for high quality outsourcers.

Additional opportunities for NPL servicers may arise from the large stock of Unlikely to Pay. The adoption and implementation of a renovated strategic management and deleveraging approach of UTP by the Italian Banks may in fact bring new additional volumes to the NPL servicing industry.

Chart 29: Bad loans managed by NPL servicers – data in €bn as of YE2016



Source: PwC analysis on data of "Bollettino Statistico" of Bank of Italy and data provided by players

Table 5: Overview of main servicers (data at 31/12/2016) – Ranking by special servicing total Bad Loans AuM[1]

Company	Bank of Italy Surveillance	Special Servicing		Servicing Performing AuM (€bn)	Master Servicing AuM (€bn)	Revenues (€m)	Ebitda (€m)	Net Equity (€m)	Main activities				Rating
		Total Bad Loans AuM (€bn)	Other NPLs AuM[2] (€bn)						NPL servicing	Debt collection	Debt purchasing	Master servicing	
doBank[3]	Bank	77.2	1.8	1.9	-	206	64.3	211	✓				✓
Cerved Credit Management	115	12.4	3.1	9.2	-	85	24.4	31	✓	✓			✓
CAF	115	8.1	-	0.2	-	19	6.8	6	✓				✓
FBS	106	7.9	0.1	-	-	18	7.3	14	✓		✓		✓
Guber	115	7.4	-	-	-	40	19.4	44	✓				✓
Hoist Italia	115	6.6	-	-	-	17	0.8	1	✓	✓	✓[6]		
Sistemia	115	4.9	-	-	-	17	3.9	5	✓				
Advancing Trade	106/115	4.3	-	-	-	34	5.4	n.a.	✓	✓	✓		
MBCredit Solutions	106	4.1	-	-	-	60	-	n.a.	✓	✓	✓		
Prelios	106	3.3	-	-	7.2	9	(0.2)	5	✓			✓	✓
Finint Revalue	106	2.9	-	-	-	6	0.5	5	✓				
Kruk Italia	115	2.7	-	-	-	n.a.	n.a.	n.a.	✓	✓	✓[6]		
Fire	115	2.6	1.0	0.7	-	40	1.4	11	✓	✓	✓		✓
Bayview Italia	115	2.2	-	-	-	n.a.	n.a.	n.a.	✓				
Primus Capital	106	2.2	-	-	-	4	n.a.	n.a.	✓				
Link Financial	106	2.1	0.1	0.1	-	5	n.a.	-		✓			✓
Officine CST	115	1.8	-	1.1	-	11	3.9	8	✓[5]				
Cribis Credit Management	115	1.4	11.2	8.2	-	22	n.a.	n.a.		✓			
Credito Fondiario	Bank	1.2	1.1	1.2	12.8	27	n.a.	89	✓		✓	✓	✓
AZ Holding	115	1.1	-	-	-	8	2.8	n.a.		✓			
Fides	115	1.0	-	0.3	-	-	n.a.	n.a.		✓			
Parr Credit	115	0.9	0.2	-	-	20	2.5	n.a.		✓			
CS Union	106	0.7	0.3	-	-	9	1.8	3		✓	✓		
SiCollection	115	0.6	0.2	-	-	5	n.a.	1		✓	✓		
Gextra - Lindorff group[4]	115	0.5	0.1	-	-	4	0.4	0		✓			
Securitisation Services	106	0.5	0.1	1.7	24.6	18	9.8	13				✓	✓
Serfin	115	0.5	0.1	0.6	-	19	n.a.	n.a.		✓			
Centotrenta Servicing	106	-	-	-	4.9	3	0.5	3				✓	✓
Zenith Service	106	-	-	-	14.9	-	-	n.a.				✓	

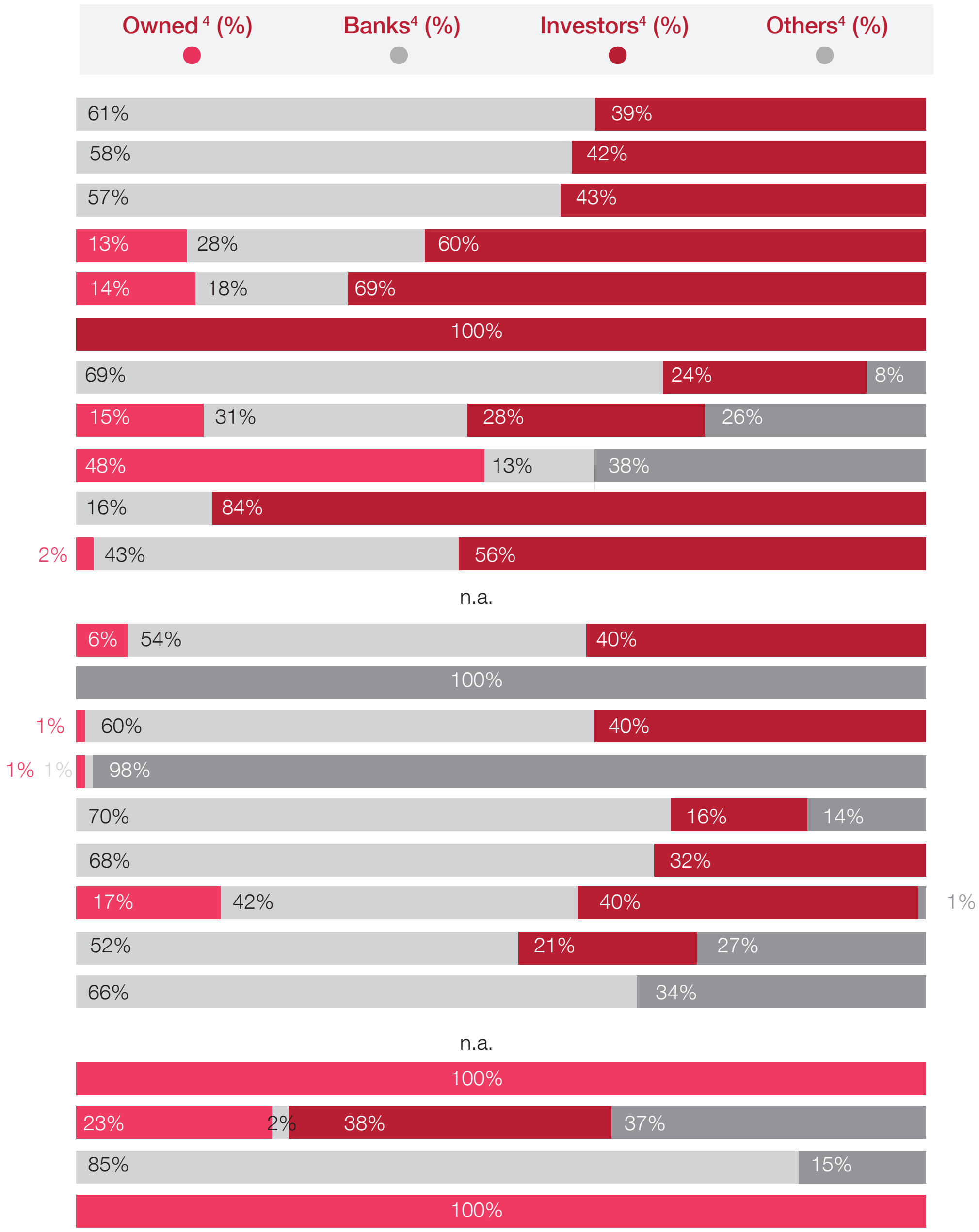
Source: PwC analysis on data provided by Servicers as of 31/12/2016; data have been directly provided by Servicers and have not been verified by PwC. Servicers present highly heterogeneous organizational, industrial and operating structures. Comparing the information presented above requires a correct analysis and understanding of the competitive landscape and servicers business model

1 Includes both owned and third parties portfolios
2 Includes Unlikely to Pay + Past Due more than 90 days
3 doBank group figures include Italfondiario
4 Gextra activities have been acquired from doBank by Lindorff Group on May 2017 (data have been extracted from doBank financial statement but not subtracted from doBank results above displayed)
5 Officine CST is specialised mainly in PA credit servicing
6 Debt purchasing activities are conducted via Special Purpose Vehicles
Note: Double counting may arise when adding NPL AuM as some servicers outsource part of their portfolios to others due to capacity and/or specialization issues

Table 6: Breakdown of servicers' Total Bad Loans AuM[1] (data at 31/12/2016)

Company	Total Bad Loans AuM (€bn)	Average ticket (k€)	Secured[4] (%)	Unsecured[4] (%)
doBank[2]	77.2	108	29%	71%
Cerved Credit Management	12.4	14	46%	54%
CAF	8.1	33	32%	68%
FBS	7.9	37	22%	78%
Guber	7.4	54	44%	56%
Hoist Italia	6.6	7[5]	1%	99%
Sistemia	4.9	17	68%	32%
Advancing Trade	4.3	2		100%
MBCredit Solutions	4.1	2	2%	98%
Prelios	3.3	391[5]	54%	46%
Finint Revalue	2.9	20	89%	11%
Kruk Italia	2.7	9		100%
Fire	2.6	4	8%	92%
Bayview Italia	2.2	94	42%	58%
Primus Capital	2.2	168	59%	41%
Link Financial	2.1	6	10%	90%
Officine CST	1.8	14	50%	50%
Cribis Credit Management	1.4	41	64%	36%
Credito Fondiario	1.2	13[5]	37%	63%
AZ Holding	1.1	6		100%
Fides	1.0	3		100%
Parr Credit	0.9	4		100%
CS Union	0.7	8		100%
SiCollection	0.6	5		100%
Gextra - Lindorff group[3]	0.5	7	7%	93%
Serfin	0.5	1		100%

Source: PwC analysis on data provided by Servicers as of 31/12/2016; data have been directly provided by Servicers and have not been verified by PwC; Servicers present highly heterogeneous organizational, industrial and operating structures. Comparing the information presented above requires a correct analysis and understanding of the competitive landscape and servicers business model
1 Includes both owned and third parties portfolios
2 doBank group figures include Italfondiario
3 Gextra activities have been acquired from doBank by Lindorff Group on May 2017 (data have been extracted from doBank financial statement but not subtracted from doBank results above displayed)
4 Percentages are based on total NPL portfolio: breakdown for Master and Special servicing activities have not been provided
5 Data refers only to Special servicing average Ticket

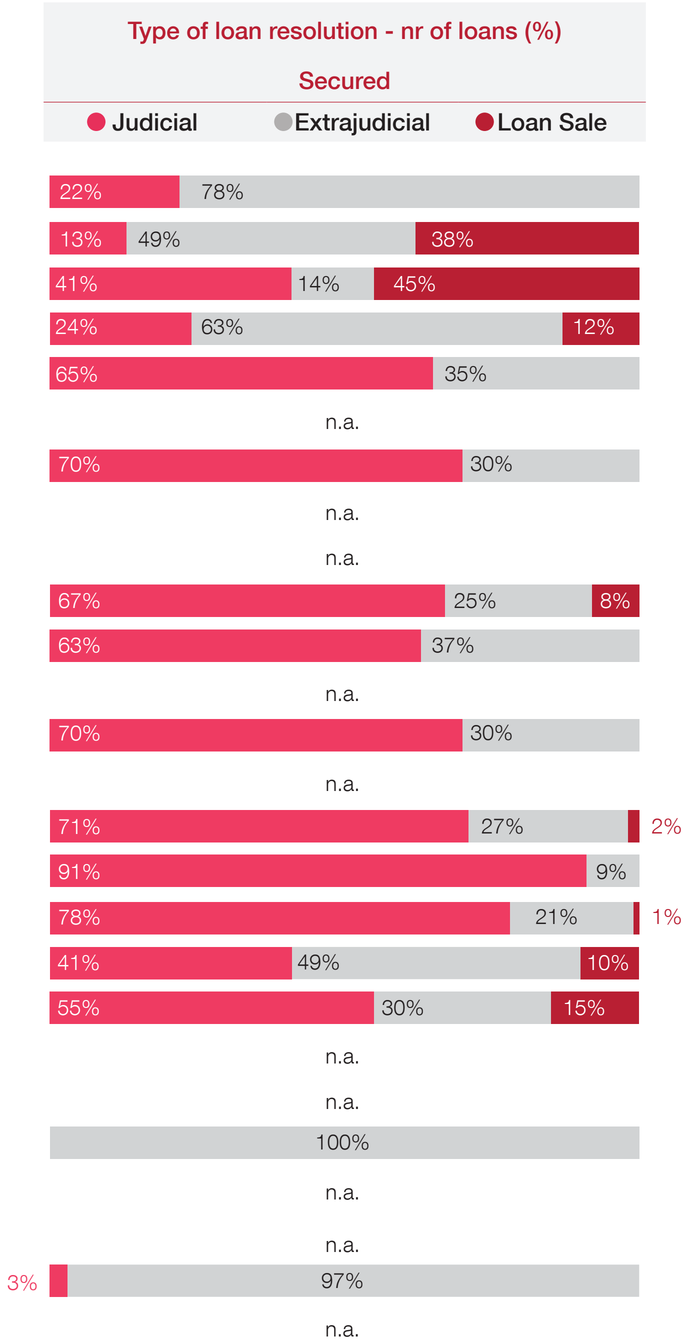


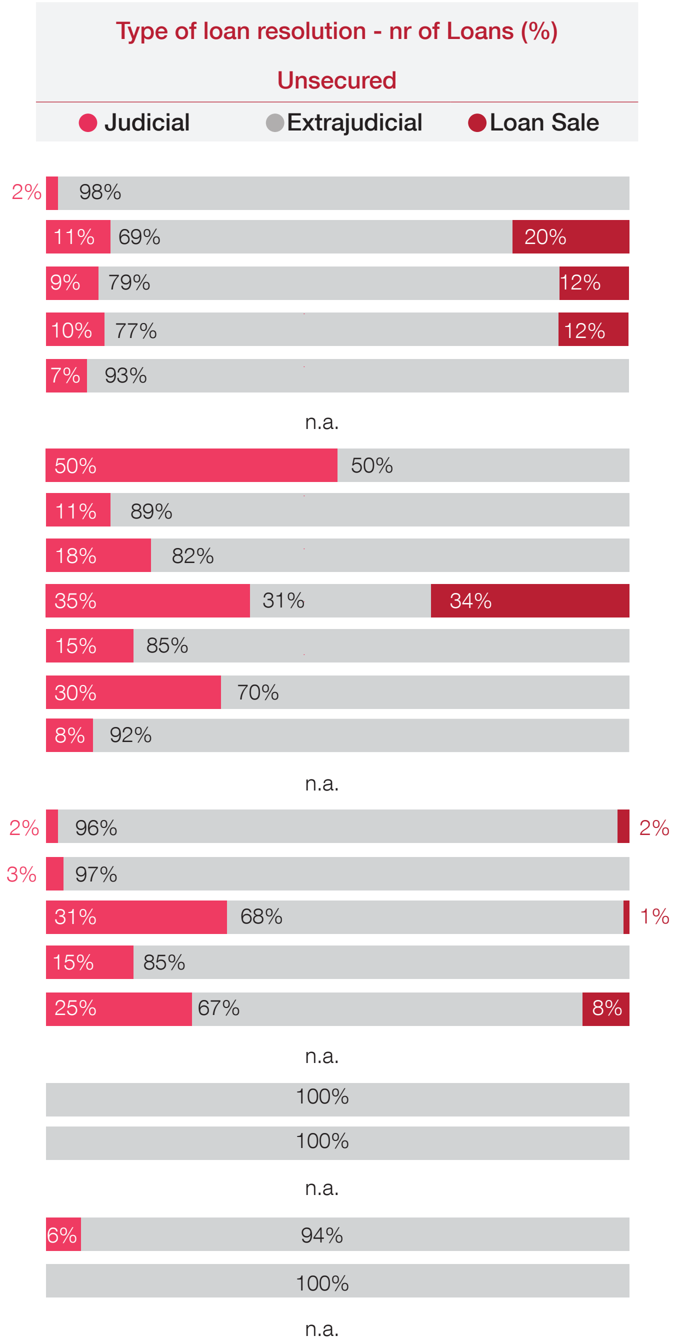
Owned⁴ (%)
Banks⁴ (%)
Investors⁴ (%)
Others⁴ (%)
61% 39%
58% 42%
57% 43%
13% 28% 60%
14% 18% 69%
100%
69% 24% 8%
15% 31% 28% 26%
48% 13% 38%
16% 84%
2% 43% 56%
n.a.
6% 54% 40%
100%
1% 60% 40%
1% 1% 98%
70% 16% 14%
68% 32%
17% 42% 40% 1%
52% 21% 27%
66% 34%
n.a.
100%
23% 2% 38% 37%
85% 15%
100%

Table 7: Breakdown of servicers' Total Bad Loans AuM[1] (data at 31/12/2016)

Company	Geographical NPL breakdown (%) North[4]	Centre[5]	South[6]
doBank[2]	46%	23%	31%
Cerved Credit Management	41%	21%	38%
CAF	40%	35%	25%
FBS	27%	37%	37%
Guber	41%	39%	20%
Hoist Italia	40%	23%	37%
Sistemia	n.a.		
Advancing Trade	41%	20%	39%
MBCredit Solutions	22%	37%	42%
Prelios	24%	24%	51%
Finint Revalue	54%	29%	17%
Kruk Italia	35%	25%	40%
Fire	30%	22%	49%
Bayview Italia	58%	20%	22%
Primus Capital	33%	48%	19%
Link Financial	21%	36%	43%
Officine CST	36%	18%	46%
Cribis Credit Management	46%	21%	33%
Credito Fondiario	52%	30%	18%
AZ Holding	35%	38%	27%
Fides	19%	23%	58%
Parr Credit	36%	20%	44%
CS Union	n.a.		
SiCollection	47%	21%	32%
Gextra - Lindorff group[3]	34%	24%	41%
Serfin	30%	50%	20%

Source: PwC analysis on data provided by Servicers as of 31/12/2016; data have been directly provided by Servicers and have not been verified by PwC; Servicers present highly heterogeneous organizational, industrial and operating structures. Comparing the information presented above requires a correct analysis and understanding of the competitive landscape and servicers business model
1 Includes both owned and third parties portfolios
2 doBank group figures include Italfondiario
3 Gextra activities have been acquired from doBank by Lindorff Group on May 2017 (data have been extracted from doBank financial statement but not subtracted from doBank results above displayed)
4 Includes: Piemonte, Valle d'Aosta, Lombardia, Veneto, Trentino Alto Adige, Friuli Venenzia Giulia, Liguria, Emilia Romagna
5 Includes: Toscana, Umbria, Marche, Lazio
6 Includes: Abruzzo, Molise, Campania,Puglia,Basilicata, Calabria,Sicilia,Sardegna


Type of loan resolution - nr of loans (%)
Secured
Judicial
Extrajudicial
Loan Sale
22% 78%
13% 49% 38%
41% 14% 45%
24% 63% 12%
65% 35%
n.a.
70% 30%
n.a.
n.a.
67% 25% 8%
63% 37%
n.a.
70% 30%
n.a.
71% 27% 2%
91% 9%
78% 21% 1%
41% 49% 10%
55% 30% 15%
n.a.
n.a.
100%
n.a.
n.a.
3% 97%
n.a.


Type of loan resolution - nr of Loans (%)
Unsecured
Judicial
Extrajudicial
Loan Sale
2% 98%
11% 69% 20%
9% 79% 12%
10% 77% 12%
7% 93%
n.a.
50% 50%
11% 89%
18% 82%
35% 31% 34%
15% 85%
30% 70%
8% 92%
n.a.
2% 96% 2%
3% 97%
31% 68% 1%
15% 85%
25% 67% 8%
n.a.
100%
100%
n.a.
6% 94%
100%
n.a.

Regulatory changes

Key Message: Competitive pressure, pursuit of efficiency and size consistent with the challenges of a new regulation always more intense, need to seize the opportunities provided by new digital technologies: these are the main drivers of a violent process that is deeply involving the Italian banking system.

On June 2017, new aspects were inaugurated by Article 7.1*. In particular, the new article develops the ambit of operation of the 130 SPV (Italian securitization vehicles), to help the sale of impaired receivables (transferred by Italian banks or financial intermediaries registered to Article 106 of the Legislative Decree No 385 of the 1993, the "Italian Banking Act"), in case of recovery or restructuring operations and in case of securitisation transactions concerning receivables arising inter alia from financial leasing agreements.

The main aspects are:

1. NPLs securitisation

In the framework of NPLs securitisation, sold by banks or financial intermediaries (ex Article 106 of the mentioned above Italian Banking Act), the 130 SPV will be able to assign loans to significant debtors with the explicit aim to help their prospects for Collectability of the receivables and improve them returning current in bonis. The debtors must meet some conditions:

- the borrowers shall be identified by a bank or a financial intermediary enrolled with the register held pursuant to Article 106;
- the notes issued to finance the granting of loans shall be subscribed by qualified investors;
- the bank or the financial intermediary (ex Article 106) shall retain a considerable economic interest in the transaction (retention rate of 5%).

2. Securitisation

During the restructuring agreement, composition or recovery procedure (set by Articles 124, 160, 182-bis e 186-bis of the Bankruptcy Law or other similar procedures), the SPV 130 would be capable to purchase or sign equity or quasi-equity instruments issued by the assignors. The purposes are making a debt-to-equity swap and grant loans to the significant debtors, with the aim to develop their prospects for collectability of the receivables and assist them returning current in (bonis). The 130 SPV shall indicate a person in the securitisation prospectus who meets the necessary competence requirements and authorizations provided by the law and if this subject is a bank or financial intermediary the compliance of the activities undertaken shall be monitored. The amount deriving from the purchase/subscription of mentioned instruments is considered as payments from debtors exclusively aimed to satisfy the rights in the notes issued and the payment of the securitisation transaction costs.

3. ReoCo

It is also possible to set up SPV corporations, called ReoCo, having the aim of purchasing, managing and increase the value of real estate, registered movable assets and any other asset securing securitized receivables (including also assets subject to leasing agreements). The value generated by these activities is segregated to the benefit of the noteholders and for the payment of the securitization costs.

The SPV are subject to the Italian fiscal laws on leasing corporations. Moreover, the real estate transfers concluded by such SPV are subject to the tax benefits provided for the corporations carrying out leasing activities.

In case the aforesaid assets and the relevant leasing agreements are transferred, the SPV should:

- fully consolidated in the balance sheet of a bank;
- set-up solely for the purposes of concluding the securitization transactions;
- liquidated once at the end of the securitization transaction.

4. Publicity system

The receivable purchased by the 130 SPV are published through the registration in the undertakings register. The notice of the transfer is publicized in the Official Journal.
The mentioned notice should mention information as: names both of the assignor and the assignee, date of transfer, information on the relationships of the receivables origination and the period, the internet site where the assignor and assignee will make available the information regarding the receivables and the confirmation of their transfer to the debtor.

* approved by the Italian Parliament on the Draft Bill No. 2853, converting the Decree Law No 50/2017 and amending, inter alia, the Law No 130 of the 1999 the "Italian Securitisation Law"

Recent market activity and outlook

Key Message: 2017 volumes are expected to reach more than €60bn, mainly driven by the huge prospective MPS deleveraging (€29.4bn). We foresees that from 2017 onwards the transactions likely will include not only bad loans ("NPL"), but also the other categories of Non Performing Exposures such as Unlikely to Pay and Foreborne. In other words, we expect new trends in the market as the sale of portfolios composed by mixed asset class as well as portfolios made by a limited number of borrowers specialised in real estate developments and sale of single names under restructuring.

Banks continue to reduce the volume of NPL on their balance sheets,

- on one hand, through the restructuring process in place concerning Italian ailing banks (e.g. the “four regional banks” rescued by the Italian Authorities in 2015 and eventually acquired by UBI and BPER in May 2017, which ultimately opened new opportunities in the market, mainly through the Bad bank created to held and sell their NPL);
- on the other hand, through the implementation of deleverage plans carried on by significant Italian banks (e.g. Unicredit, Intesa Sanpaolo, Banco BPM).

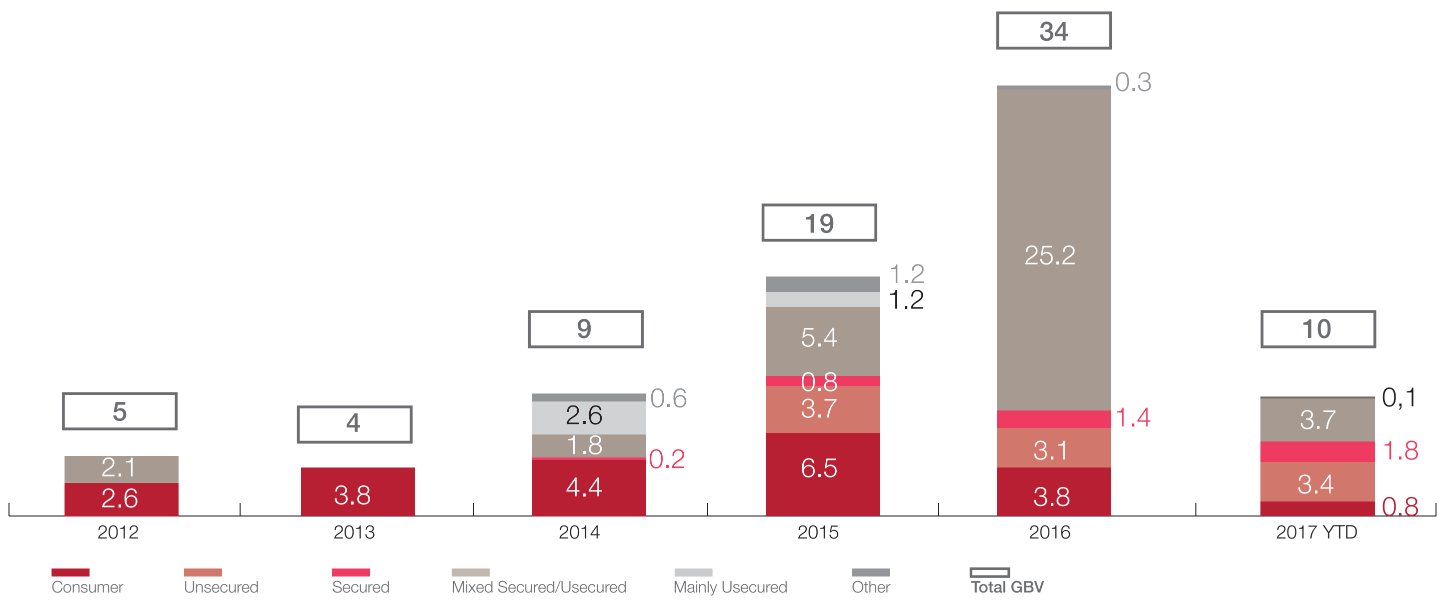
The restructuring measures for MPS, overburdened by €29.4bn (GBV) of Bad Loans is currently in progress and we expect a decisive solution to be implemented by the end of 2017. The stock of €10.3bn (GBV) of NPL acquired by the Bad Bank REV from the “four regional banks” rescued by the Italian Authorities in 2015, are expected to come to market in 2017, via separate transactions.

The NPL of Banca Popolare di Vicenza and Veneto Banca (totalling as a whole €16.8bn at the end of 2016) will be liquidated through a public Bad Bank following the Decree enacted by the Italian Government on 25 June 2017 stating the acquisition of certain asset (excluding NPL) and liabilities of the two banks by Intesa Sanpaolo.

Banco BPM planned to deleverage a NPL portfolio (GBV of €2.0bn) composed by unsecured SME loans. Creval is in the early process to deleverage, through securitization, a NPL mixed portfolio of secured and unsecured loans (GBV equal to €1.5bn).

Intesa Sanpaolo is in the process of selling, through securitization, a corporate NPL portfolio mainly residential (real estate development) highly concentrated with 80 borrowers for €1.35bn of GBV.

Chart 30: Trend of main NPL transactions in the Italian market (€ bn)



Source: PwC market analysis

Hypo Alpe Adria foresees to deleverage circa €1.0bn of NPL during the third quarter of 2017.

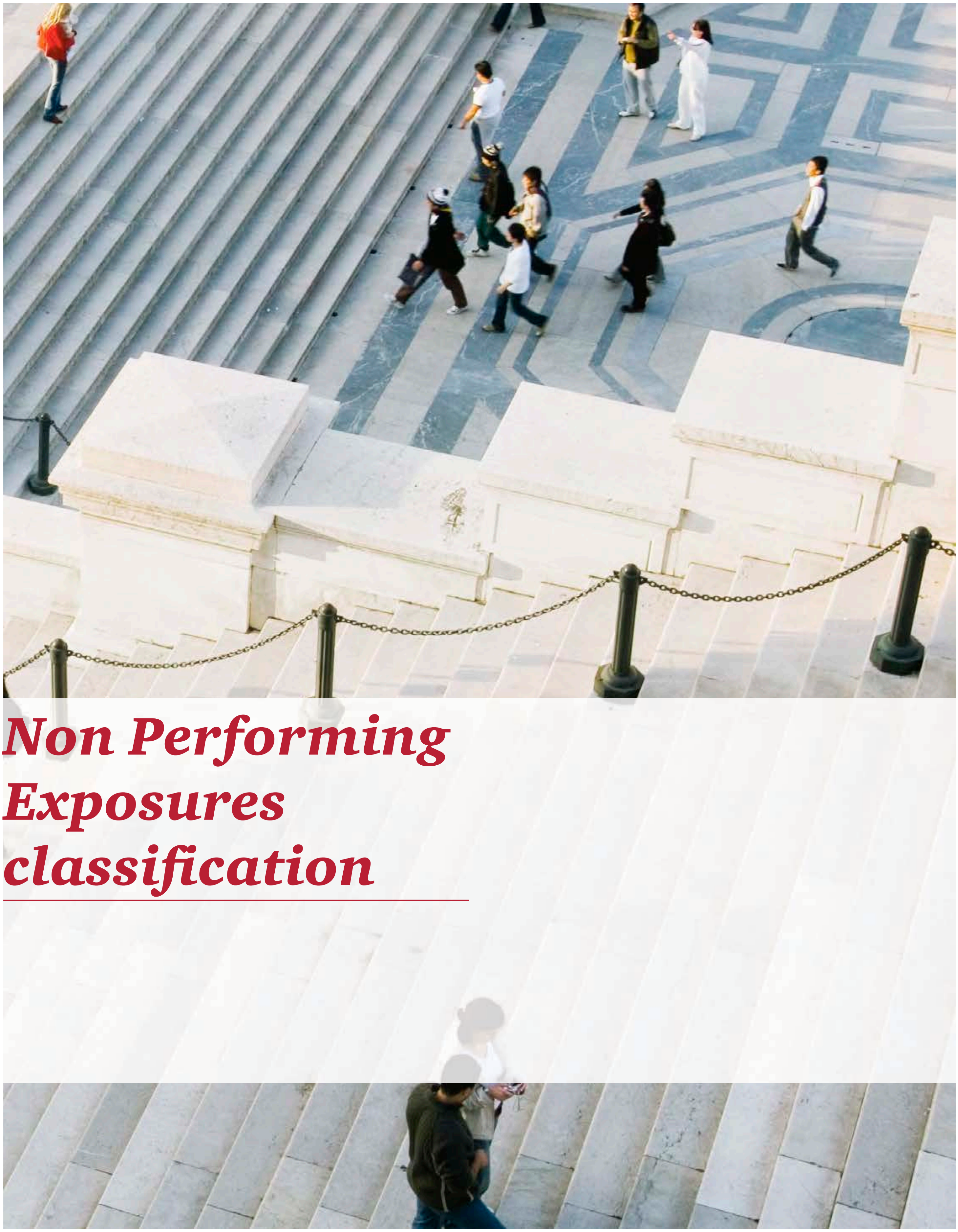
Carige could start a deleverage process for portions of its Bad Loans portfolio (totaling €3.7bn).

Cassa Centrale Banca is about to put in the market a portfolio including NPL originated by several rural saving banks for an amount equal to €0.5bn.

Banca Popolare di Bari, which closed in 2016 the deleverage of a portion (€0.47bn) of its NPL through the first Italian securitization sealed with the recourse to GACS, is in the process to carry on the deleverage of further €0.3bn of NPL.

These volumes remain modest compared to banks' total stocks of Bad Loans, but we expect portfolio disposals to further increase. As mentioned earlier, the new ECB guidelines are set to have a great impact on the banks NPEs' deleverage programme.

Date	Seller	Volume (€m)	Macro asset class	Buyer
2017 Q2	Banco BPM	750	Secured	Algebris
2017 Q2	Banca Mediocredito FVG	400	Secured	Bain Capital
2017 Q2	Banca Sella	126	Mixed Secured/Unsecured	B2 Holding
2017 Q2	Barclays	190	Unsecured	Banca IFIS
2017 Q2	Unicredit Leasing	500	Unsecured	MBCredit Solutions
2017 Q2	Intesa SanPaolo	2,500	Mixed Secured/Unsecured	CRC
2017 Q2	Confidential	22	Unsecured	Axactor
2017 Q2	Intesa SanPaolo Provis	280	Secured	Credito Fondiario
2017 Q2	Confidential	302	Unsecured	Banca IFIS
2017 Q2	Confidential	112	Unsecured	Banca IFIS
2017 Q1	Deutsche Bank	413	Mixed Secured/Unsecured	Banca IFIS
2017 Q1	CreVal	50	Secured	Confidential
2017 Q1	Banca IFIS	750	Consumer	Kruk Italia
2017 Q1	Deutsche Bank	130	Unsecured	Kruk Italia
2017 Q1	Unicredit	50	Other	Kruk Italia
2017 Q1	Santander	160	Unsecured	Banca IFIS
2017 Q1	HETA	657	Mixed Secured/Unsecured	Bain Capital
2017 Q1	Barclays	177	Secured	AnaCap
2017 Q1	Agos Ducato	350	Unsecured	Hoist Finance
2017 Q1	BNL	1,000	Unsecured	Banca IFIS
2017 Q1	Banco Popolare	641	Unsecured	Hoist Finance



Non Performing Exposures classification

Non-Performing Exposures

The commonly used term non-performing loans ("NPL") is based on different definitions across Europe.
To overcome problems, EBA has issued a common definition of Non-Performing Exposures ("NPE") which is used for supervisory reporting purposes.

In Italy, banks are also required to distinguish among different classes of NPE: (i) Bad Loans, (ii) Unlikely to Pay and (iii) Past Due; the sum of these 3 categories corresponds to the Non-Performing Exposures referred to in the EBA ITS.

The terms of NPL ("Non Performing Loans") and NPE ("Non Performing Exposures") are used interchangeably within this study, as even provided in the Guidance to banks on non-performing loans (March 2017) by ECB – Banking Supervision.

Old

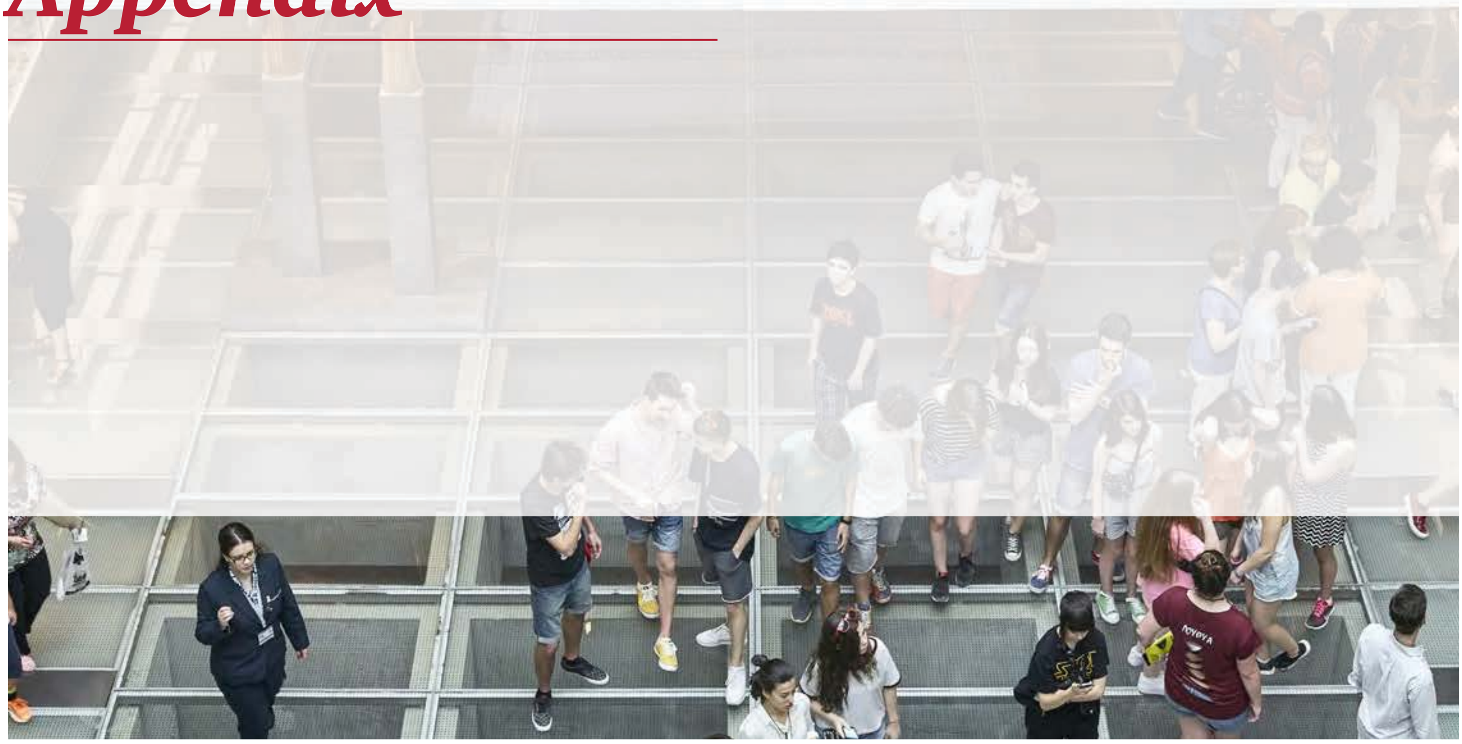
New

Old	New	NPL
Past Due *Esposizioni scadute* *> 90 giorni*	Past Due more than 90 days loans (debt) *Esposizioni scadute*	• Exposure to any borrower whose loans are not included in other categories and who, at the date of the balance sheet closure, have Past Due amounts or unauthorized overdrawn positions of more than 90 days. • A sub-segment is now represented by the Forborne Non-Performing Exposures ("FNPE"), credits granted to a counterparty in financial difficulty and which are not classified as Bad Loans and have been subject to the modification of the terms and conditions of the contract or refinancing.
Restructured *Crediti ristrutturati* Sub standard *Incagli*	Unlikely to Pay *Inadempienze probabili* Including FNPE (*)	• The classification of loans in this category is the result of the judgment of the bank about the debtors' unlikelihood to fulfil its credit obligations. This category substitutes the old sub-standard loans ("Incagli") and restructured loans ("Crediti Ristrutturati"). • A sub-segment of the Unlikely to Pay is now represented by the FNPE.
Bad Loans *Sofferenze*	Bad Loans *Sofferenze* Including FNPE (*)	• Exposure to a borrower in a position of insolvency (not necessarily recognised by a Court) or a substantially similar situation, irrespective of the presence of any collateral. Same as previous classification of Bad Loans or "Sofferenze". • A sub-segment of the Bad Loans is now represented by the FNPE.

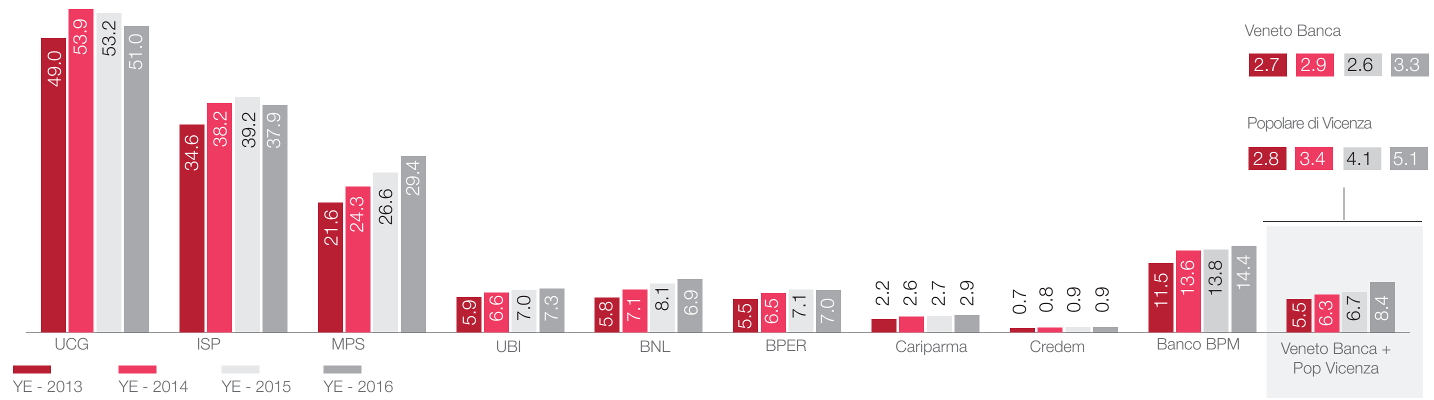
FNPE may become a Forborne Performing Exposure if:
- 12 months have passed from last allowance
- No past due from last allowance occurred

(*) FNPE: Forborne Non-Performing Exposures Source: EBA, EBA/ITS/2013/03/rev1

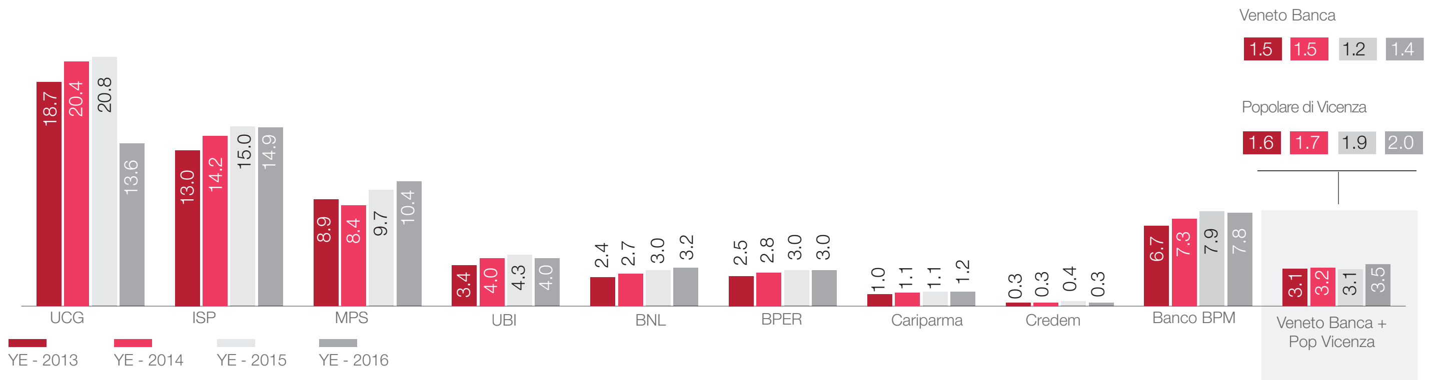
Appendix



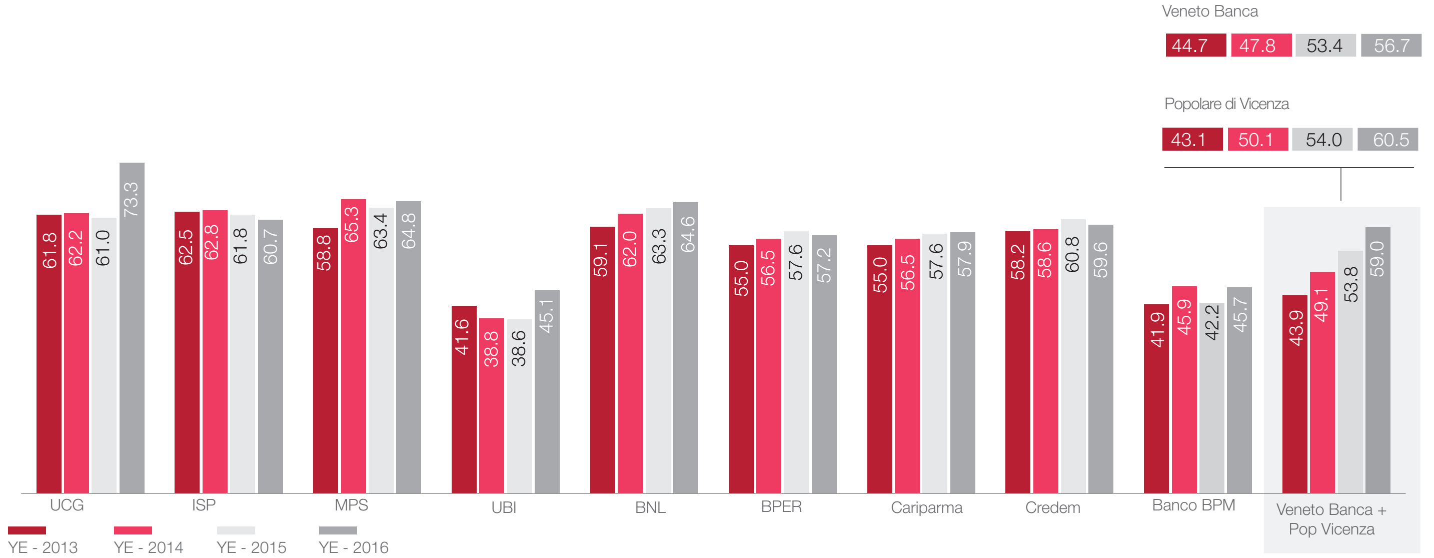
Gross Bad Loans volume (€ bn)



Net Bad Loans volume (€ bn)



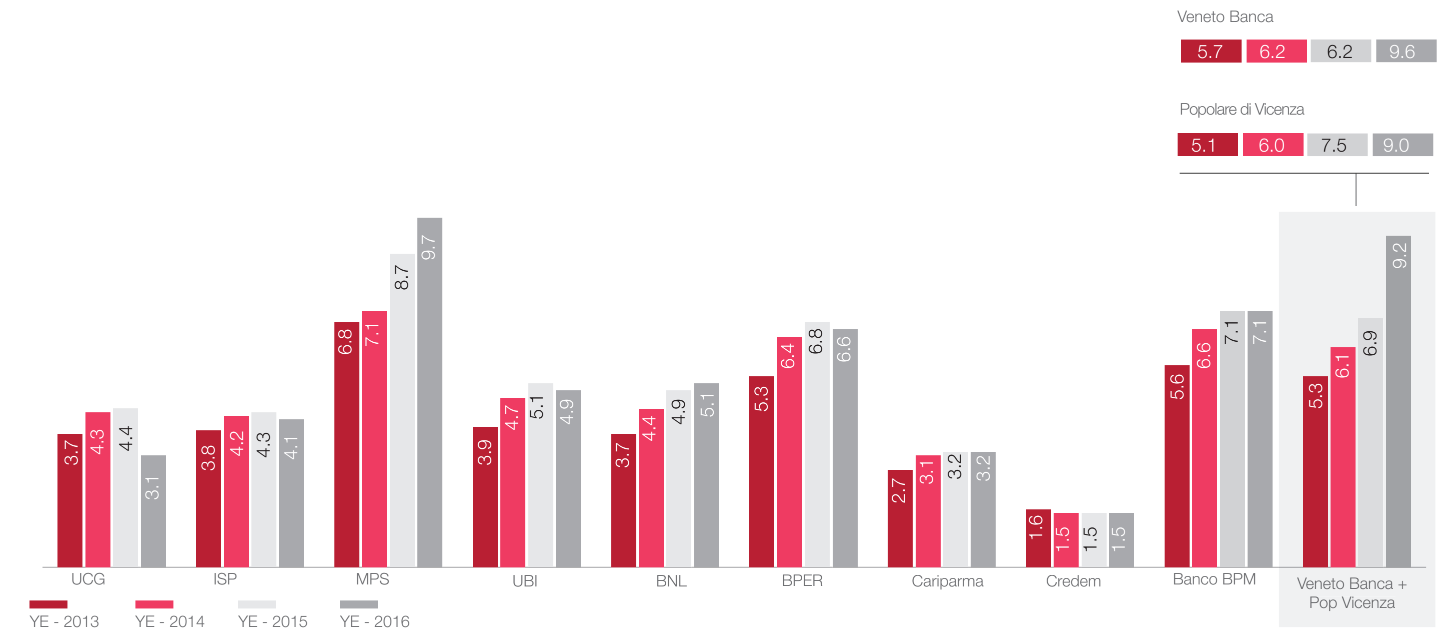
Bad Loans Coverage ratio (%)



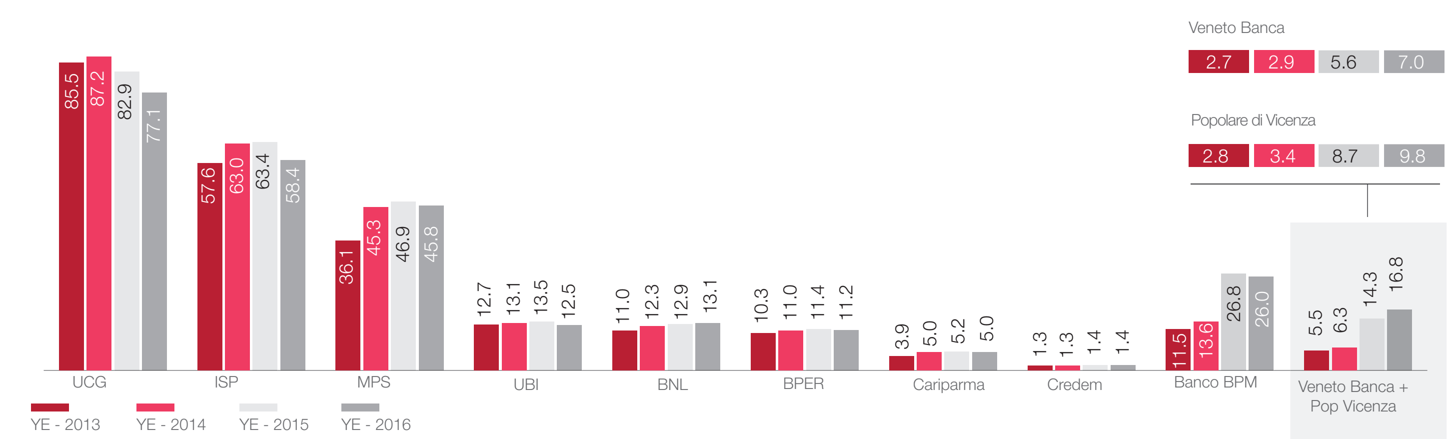
Source: Financial Statements as of YE-2016, YE-2015, YE-2014, YE-2013.

Gross Bad Loans ratio (%)

Net Bad Loans ratio (%)

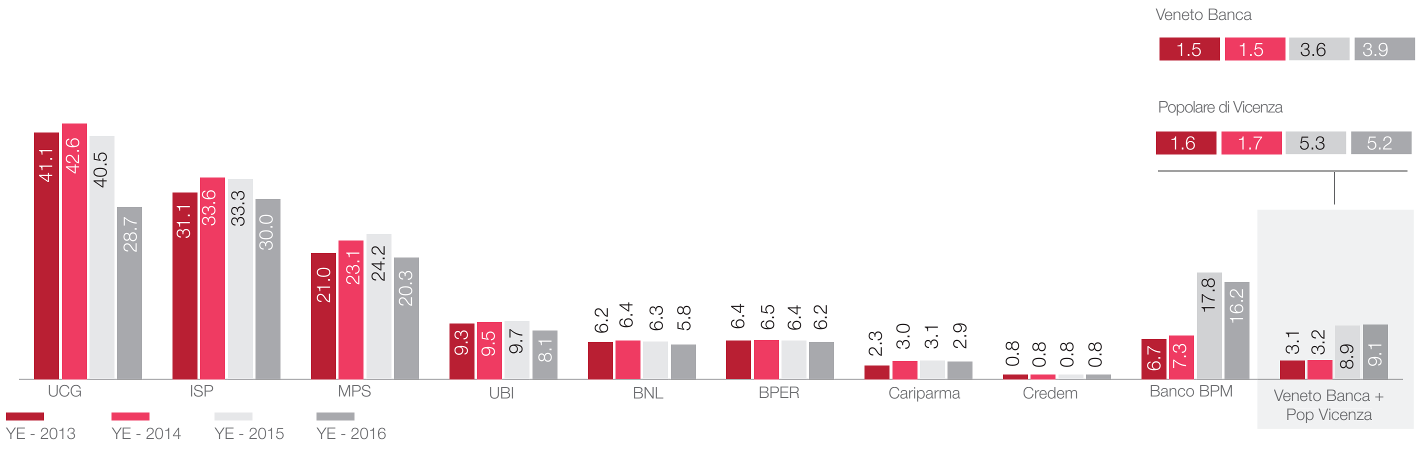


Gross NPL volume (€bn)

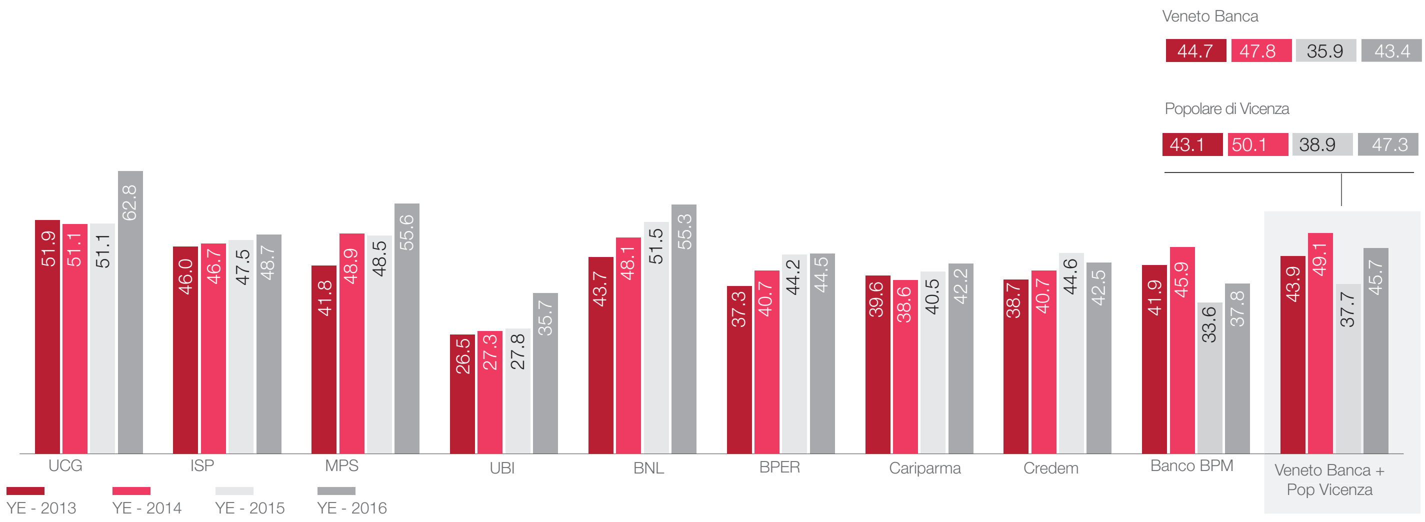


Source: Financial Statements as of YE-2016, YE-2015, YE-2014, YE-2013.

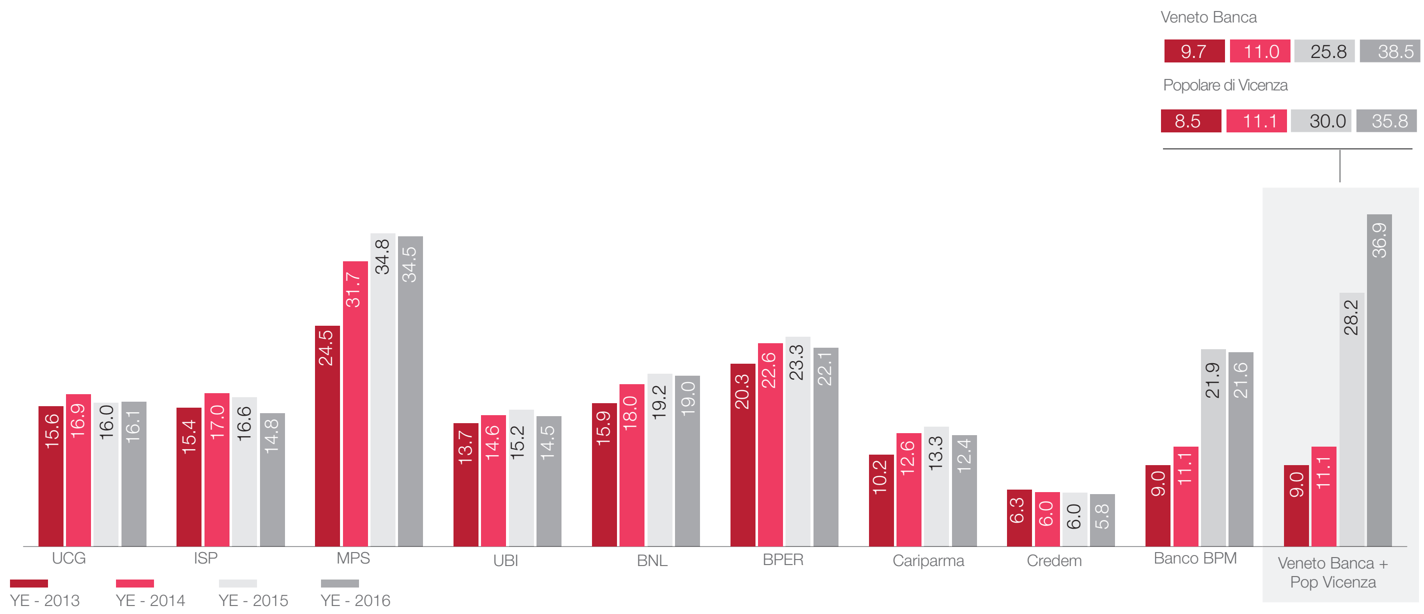
Net NPL volume (€ bn)



NPL Coverage ratio (%)

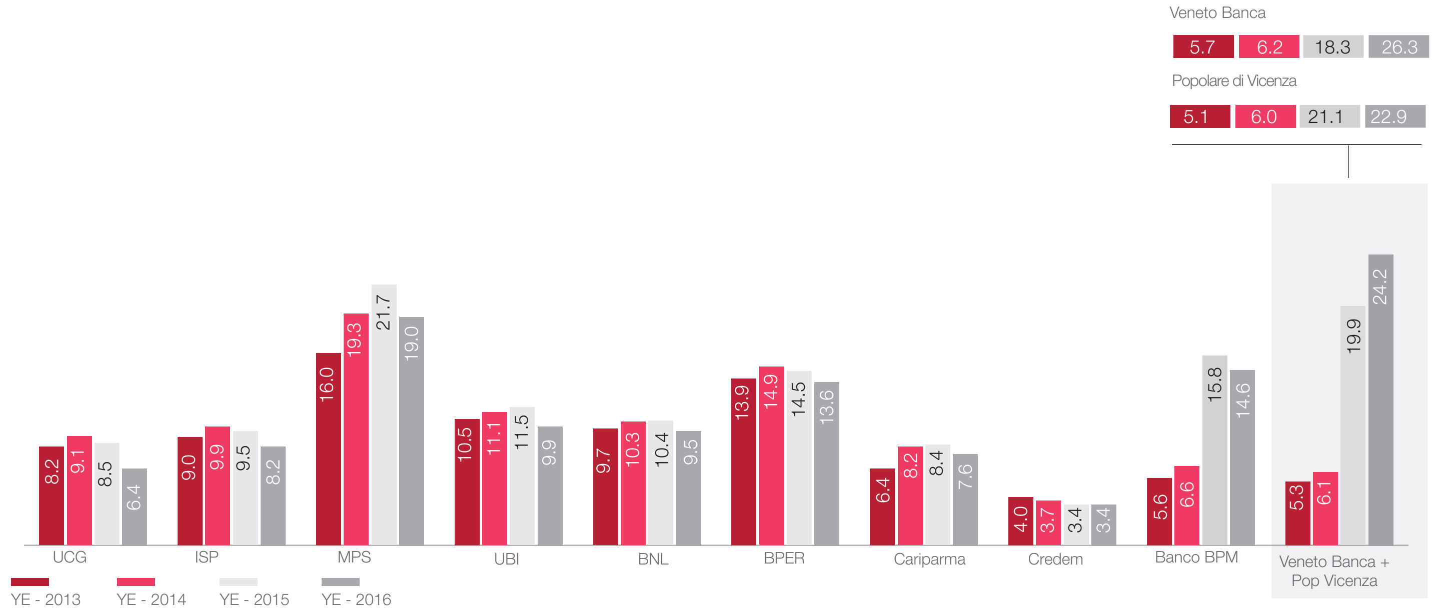


Gross NPL ratio (%)

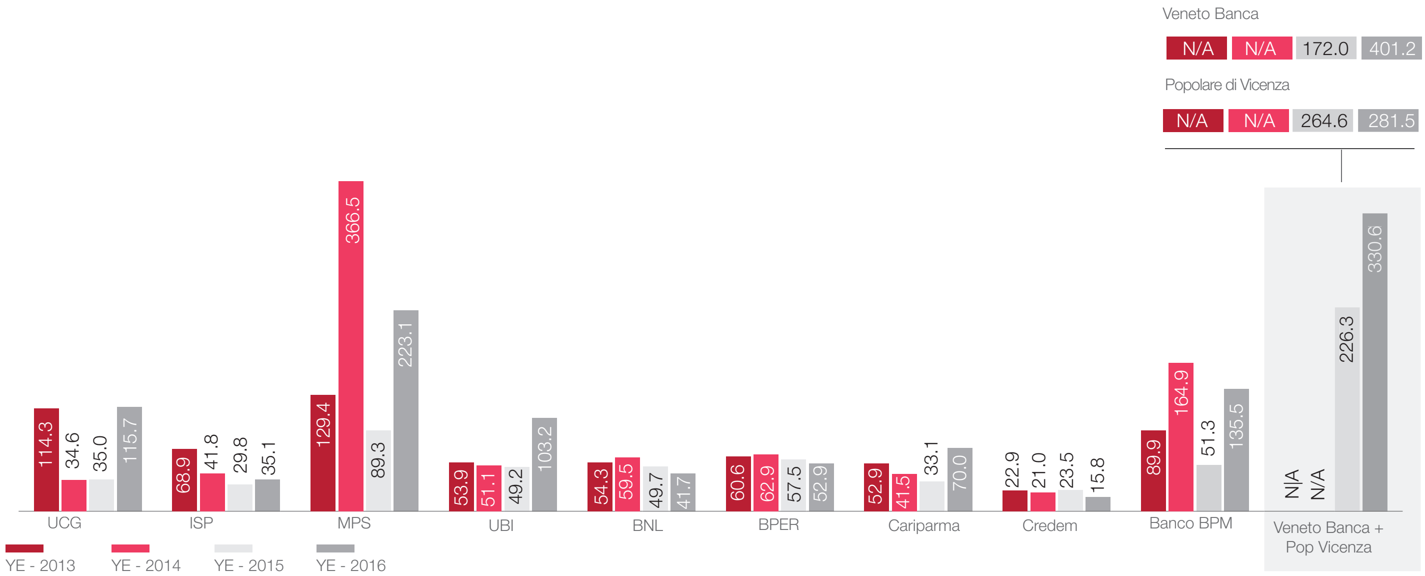


Source: Financial Statements as of YE-2016, YE-2015, YE-2014, YE-2013.

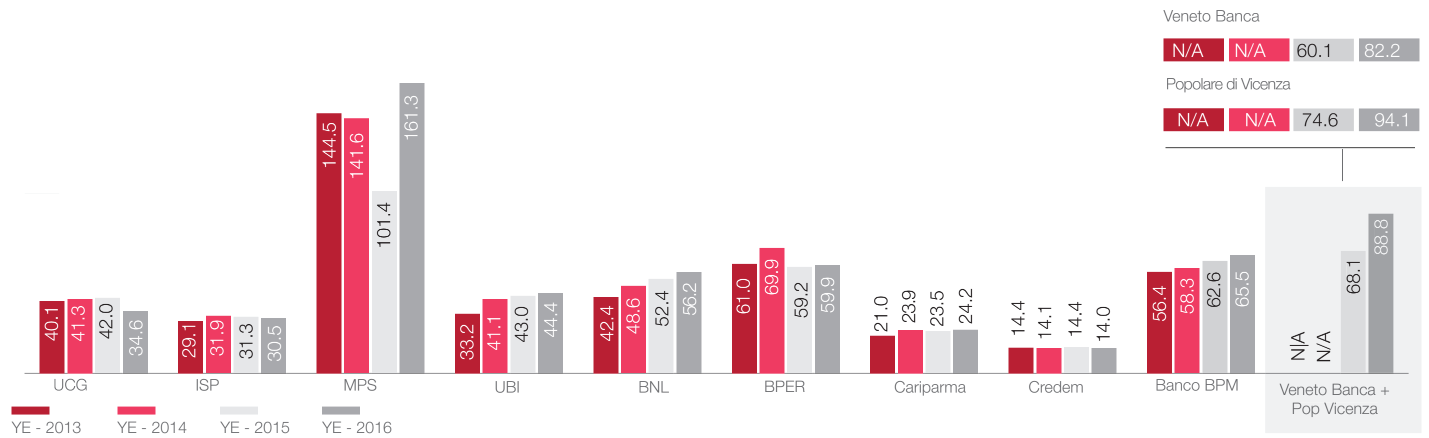
Net NPL ratio (%)



Yearly Loan Loss Provision / Net Interest Margin (%)



Net Bad Loans/Equity (%)



Source: PwC analysis on data provided by Servicers as of H1-2016

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