Morgan Stanley

April 13, 2016

# Italian Banks

## More needed to improve confidence

MORGAN STANLEY & CO. INTERNATIONAL PLC+
**Alvaro Serrano**
Alvaro.Serrano@morganstanley.com +44 20 7425-6942
**Antonio Reale**
Antonio.Reale@morganstanley.com +44 20 7425-2138
**Philippine Assemat-Tessandier**
Philippine.Assemat-Tessandier@morganstanley.com +44 20 7677-9026

Banks

Europe

**IndustryView** **In-Line**

We believe the €3-6bn Atlante fund could be effective to reduce short term risk of bank failure, but it doesn't fully resolve the NPL issue in Italy and isn't enough to address concerns on Monte Paschi. Effective bankruptcy law reforms are needed we think. We remain cautious on Italian banks.

**€3-6bn bank rescue fund to be created by 28th of April.** According to the Italian press (**Il Sole 24 Ore**, April 12), the fund (Atlante) will have a minium €3bn AuM contribution from banks, foundations, CDP (Italian development bank) and Insurance companies. It will be put together in time to cover the capital raises of Popolare Vicenza (May) and Veneto Banca (June) for a total consideration of €2.5bn (we note that the FT reported weak market demand for the Popolare Vicenza capital call, April 10). The rest, up to a maximum fund of €6bn will be used to buy NPLs from the system and/or cover capital needs of other banks if necessary.

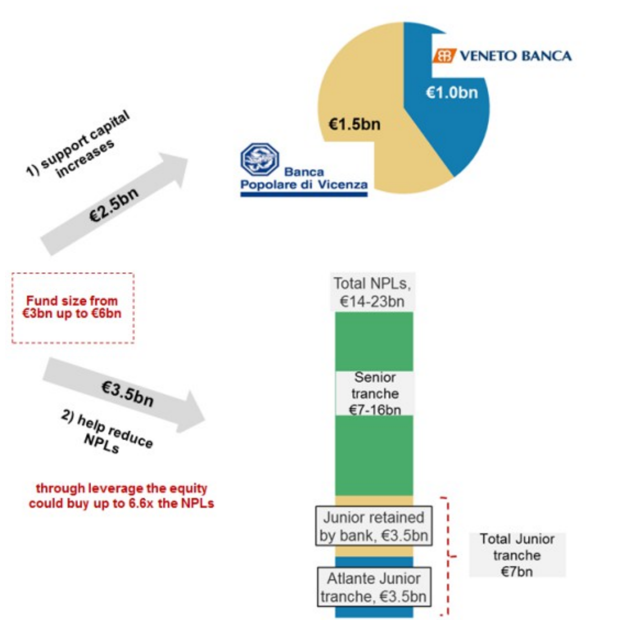
**Not enough to cover €6-11.5bn of capital needed for the system.** Although the creation of the fund reduces the risk of bank failures in the short term, we believe the size is barely sufficient to cover the potential capital needs of Monte Paschi alone, which in our report **Italian Banks: Addressing the NPL problem in Italy** (26 Jan 2016) we estimated could be €2-7bn.

**We estimate €14-23bn of NPLs could be purchased.** Using the bad bank framework (GACS) we estimate the remaining €3.5bn funds could be leveraged 4-6.7x to buy up to €14-23bn of NPLs, compared to a net amount in the system of €200bn (€360bn gross amount or 19% NPL ratio). We believe: (1) the limited size; and (2) the need to have an investment grade rating in the senior tranche meaning the transaction price cannot be subsidised, both limit the effectiveness of the fund to address the system's NPL problem.

**More effective bankruptcy reform is needed.** We believe current prices on secured NPLs are at 20-30c on the dollar vs. a carrying value of c. 50-65c (35-50% coverage), so any large scale transactions would create a capital shortfall for the more troubled banks, in our view. This is why we believe additional reforms to reduce time to repossess assets is crucial. We remain sceptical, despite the government announcing it is working on further reforms, given the reforms last year proved ineffective.

**Intesa our top pick in Italy, but prefer Spain and high dividend paying names in Europe.** We believe ultimately the fund will focus its purchases on Monte Paschi (the most systemic of the weaker banks) to maximize impact. However the high levels of NPLs in the system and the perception that healthy banks are paying the bill will also dampen investor appetite until visibility improves, in our view. We believe consolidation is the most effective way to accelerate balance sheet clean up in Italy as we argued **Italian Banks: M&A finally kicking off?** (15 Jan 2016).

**Exhibit 1:** Assuming a 30-50% junior tranche the fund could buy 4-6.6x the amount of NPLs




Source: Morgan Stanley Research estimates; Note: Funds contribution as disclosed on Il Sole 24 Ore (12/04/2016); Other banks excludes Mediobanca, Pop Vicenza, Veneto Banca, Carige and BMPS according to the same press report.

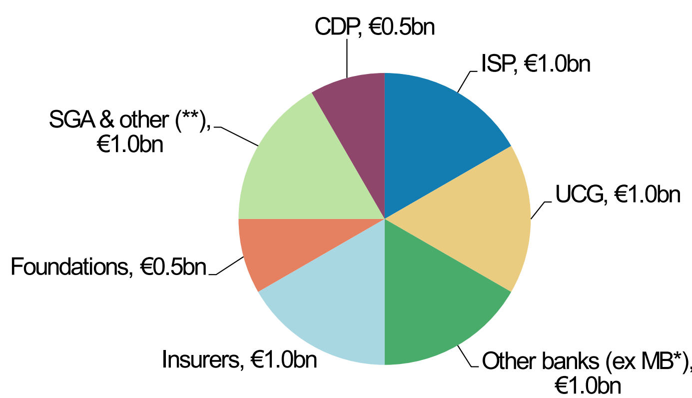
## Italian Fund "Atlante" Reduces Tail Risk for the Sector

**Il Sole 24 Ore** (12/04/2016) has reported on the structure of the banks rescue fund being put together in Italy to support recapitalisation efforts and potentially NPL purchases. The details are broadly in-line with previous press reports. Main details of the fund:

- The fund will have a minimum size of €3bn and could go to €6bn depending on needs and opportunities arising in the future. It can also be leveraged.

- Participating institutions will be Banks, CDP (Casa Depositi e Prestiti), Insurance companies, Foundations and other players. Il Sole 24 Ore reported Intesa and Unicredit would lead with €1bn each. This has not been confirmed by the companies.

**Exhibit 2:** Atlante's fund contribution could reach up to €6bn, with an initial €3bn at inception




Source: Morgan Stanley Research estimates; Note: Funds contribution as disclosed on Il Sole 24 Ore (12/04/2016); (*) Other banks excludes Mediobanca and Pop Vicenza, Veneto Banca, Carige and BMPS according to the same press report. (**) SGA, Societa' di Gestione dellle Attivita was founded in 1997 to rescue Banco di Napoli (now part of Intesa's group).

- The fund will be set up by 28th of April, in time to support the recapitalisation of Popolare di Vicenza and Veneto Banca. We note that the FT reported weak market demand for the Popolare Vicenza capital call (April 10).

- The fund does not constitute government aid as participation is voluntary and CDP contribution is done at market conditions.

- In the case of the banks the participations would be fully deducted from capital.

### Reduces short term risks of bank failures...

According to our estimate, based on press reports and capital raises already announced, Italian banks have between €6-11.5bn of capital requirements. The fund is designed to address the capital needs of Vicenza and Veneto Banca for an amount of €2.5bn, in our view, and would leave the rest to the private sector.

Popolare di Vicenza has an underwriting commitment from Unicredit for its required IPO of €1.5bn which needs to be completed by May, and Veneto Banca is seeking €1bn in its IPO in June which is underwritten by Intesa and a pool of banks (both according to company disclosures - the terms are not public). Given the reported lack of interest from investors to participate in the IPOs it is possible that the initial €3bn capital outlay would only be enough to support these two capital raises.

We think this is enough to avoid the risk of short-term failure of banks, as the presentation explains, but it is not obvious it would provide capacity to inject funds into other banks if they were to require capital. In particular, we believe it would not be enough to recapitalise Monte Paschi, which we believe would need €1.1-5.5bn further provisions if its *sofferenze* were sold at market prices (see our note **Italian Banks: Addressing the NPL problem in Italy**, 26 Jan 2016), plus further restructuring.

**Exhibit 3:** According to our estimate and based on press reports, and disclosures from the companies, Italian banks have between €6-11.5bn of capital needs

| Bank | Tot Assets | Gross NPLs | NPL ratio % | Cov. ratio % | Equity required | Source |
|---|---|---|---|---|---|---|
| Carige | 30,299 | 6,824 | 28% | 42% | €500m | Offered by Apollo (Bloomberg 29/03/16) |
| Veneto | 33,349 | 7,555 | 28% | 35% | €1bn | Company |
| PopVi | 39,783 | 8,963 | 31% | 41% | €1.5bn | Company |
| BMPS | 169,012 | 46,861 | 35% | 48% | €2-7bn | MSe (Italian Banks: Addressing the NPL problem in Italy 26 Jan 2016) |
| BAPO | 120,510 | 20,645 | 24% | 33% | €1bn | Company |
| ***Total*** | ***392,952*** | ***90,848*** | ***42%*** | ***40%*** | ***€6-11bn*** | |

Source: Company data, Morgan Stanley Research estimates

We believe the equity story of the merger of Banco Popolare and Popolare Di Milano, means their €1bn announced capital will be covered by private investors, and unconfirmed press reports (Bloomberg, March 31) point to private money interest in Carige, which would leave Monte Paschi as the biggest outstanding issue, in our view.

## ... but the NPL problem in Italy remains unaddressed

The fund could reach up to €6bn in size, of which we expect €2.5bn to be allocated to fund the capital increases of Popolare di Vicenza and Veneto Banca and the remaining €3.5bn could be invested in the junior tranche of the SPV (bad bank), leveraging on the government guarantee.

We estimate the fund, even if fully subscribed, could buy a maximum of €14-23bn of net NPLs, just under 10% of the outstanding; however, any sizable transaction at current market prices would trigger capital needs, and we don't believe the vehicle is able to influence the price using the bad bank vehicle (GACS) as the need for the senior tranche to be investment grade forces market discipline, in our view.

The recently approved bad bank vehicle requires the NPLs to be transferred to an SPV with an Equity tranche and a Senior tranche. The government would guarantee the Senior tranche with the condition that the banks sell at least 50% of the Junior tranche and the Senior debt has an investment grade rating (see our **Italian Banks: Bad Bank reduces tail risks for the sector,** 28 Jan 2016). This last condition, in our view, limits the leverage you can put in place in the vehicle and ensures transactions are done close to market prices.

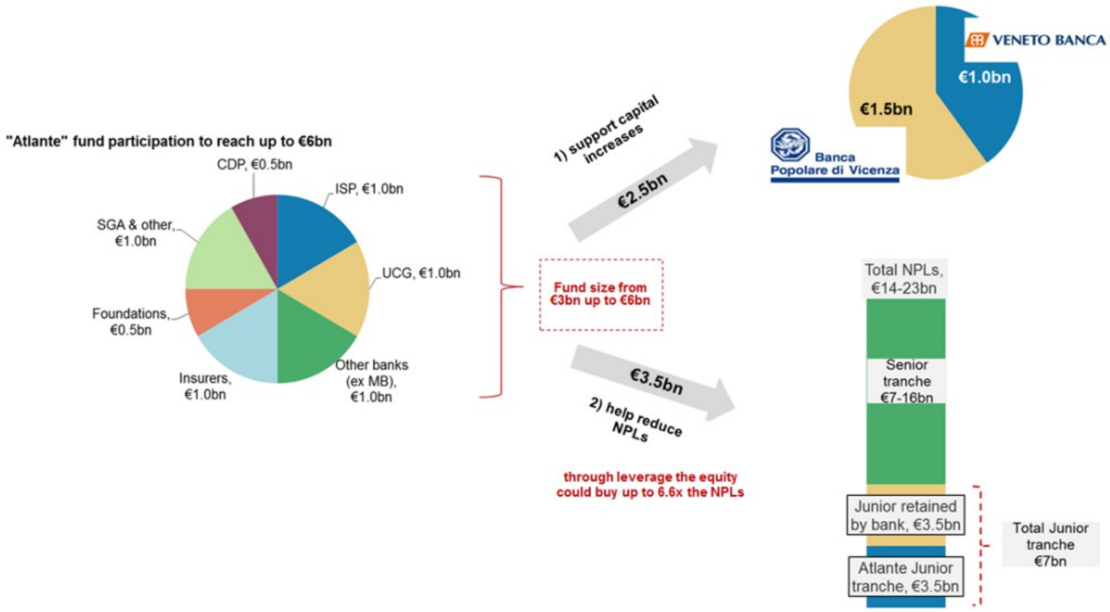
Assuming the Equity tranche is 30-50% of the total NPLs and the fund buys 50% of it (enough to de-consolidate), we believe the fund could leverage 4-6.7x. If there are €3.5bn funds available to buy NPLs, it could participate in the acquisition of €14-23bn. This compares to €200bn net NPLs in the system we estimate and €360bn gross NPLs.

**Exhibit 4:** We estimate up to €14-23bn of NPLs being purchased assuming the fund buys 50% of the junior tranche

| Available funds to Buy NPLs | Equity tranche % | Participation in the SPV % | Leverage in (x) | NPLs purchased | System net NPLs | System gross NPLs |
|---|---|---|---|---|---|---|
| €3.5bn | 50% | 50% | 4.0x | €14bn | €200bn | €360bn |
| €3.5bn | 30% | 50% | 6.7x | €23bn | | |

Source: Morgan Stanley Research estimates

**Exhibit 5:** Assuming a 30-50% junior tranche the fund could buy 4-6.6x the amount of NPLs




Source: Morgan Stanley Research estimates; Note: Funds contribution as disclosed on Il Sole 24 Ore (12/04/2016); Other banks excludes Mediobanca and Pop Vicenza, Veneto Banca, Carige and BMPS according to the same press report. SGA, Societa' di Gestione dellle Attivita was founded in 1997 to rescue Banco di Napoli (now part of Intesa's group).

## Further reform to narrow bid-ask spread is key

The transfer price of NPLs remains the main obstacle to accelerate the rundown of non-performing loans. We think the current bid on distressed loans range between 20-30% of gross book value. With NPL coverage levels at 35-50% on average for secured *sofferenze*, this suggests that market prices need to lift further.

A transfer of NPLs from Monte Paschi to the vehicle, using a 20-40c price range, would create a capital shortfall. In February we estimated that the disposal of all the *sofferenze* NPLs at Monte Paschi would create a capital need of €1.3-5.7bn. On top of that, restructuring needs in the event of M&A would increase total capital requirements to €2-7bn.

**Exhibit 6:** Using the 20-40c price range for secured sofferenze and 5-15c for unsecured, as a range of potential transfer prices, on a sofferenze coverage of 63%, we believe a transfer would require additional provision for €1.3-5.7bn

| 4Q15 €'mn | Total Sofferenze | o/w secured | o/w unsecured |
|---|---|---|---|
| Gross value | 26,627 | 17,840 | 8,787 |
| Estimated provisions | 16,894 | 9,812 | 7,082 |
| Coverage | 63.4% | 55% | 81% |
| Net Carrying value | 9,733 | 8,028 | 1,705 |
| ***Possible transfer price ranges*** | | | |
| Higher range | 31.8% | 40% | 15% |
| Mid range | 23.4% | 30% | 10% |
| Lower range | 15.1% | 20% | 5% |
| ***Transfer value*** | | | |
| Higher range | 8,454 | 7,136 | 1,318 |
| Mid range | 6,231 | 5,352 | 879 |
| Lower range | 4,007 | 3,568 | 439 |
| ***Provision shortfall*** | | | |
| Higher range | 1,279 | | |
| Mid range | 3,502 | | |
| Lower range | 5,726 | | |

Source: Morgan Stanley Research estimates

The lack of sufficient capital to meet market prices means banks will have to manage the recovery of NPLs themselves and we think it will take some time before we see the NPL fund execute on transactions. It is also crucial that the new bankruptcy reform reduces time to repossess assets in order to improve pricing.

As argued in previous reports, recovering the collateral in Italy can take 7-8 years on average, which has contributed to NPLs reaching €360bn at system level. By accelerating the court proceedings we think recoveries should improve, allowing banks to start the rundown of NPLs. Current market prices for secured portfolios are at 20-30c, so the success of the NPL fund, we think, will be a direct function of the government's decree. We think market reforms are much more important than the setting up of this fund. The much expected legal changes could be implemented in coming days and as early as April 18th according to Il Sole 24 Ore (12/04/2016).

**Exhibit 7:** Bankruptcy reform so far has been unsuccessful at improving NPL pricing: The government has tried to work on (1) inefficient judicial system (2) removing tax impediments to provisioning and (3) facilitate creditor coordination

**#1 JUDICIAL SYSTEM**

| Current | What was changed |
| --- | --- |
| Recovering the collateral value in Italy is notoriously a cumbersome and often slow process. Timing varies considerably from court to court across regions. Average time to foreclose can be 7-8 years or more in southern regions, which we think is responsible for a large proportion of the difference in the bid-ask spread in NPL transactions. | The decree aimed at reducing the length of judicial proceedings by introducing priority / 'fast track' procedure and out-of-court resolutions. Also to relieve the burden on the courts, notaries (*curatore fallimentare* ) are empowered vs. judicial administrators *(commissario giudiziale* ) both to grant third-party independence and incentivize execution within the terms, failure to deliver can result in revocation. |

**#2 TAX WEDGE**

| Current | What was changed |
| --- | --- |
| We believe tax incentives could make it attractive for both investors and banks, which should get a better price for their assets. This has allowed schemes in other countries, such as Spain but also Japan and Sweden, to provide a better price. Currently LLPs can be deducted from the tax bill in a linear amortization over the next 5 years. | Loan loss provisions are deducted over a shorter window of 1 year, which would also speed up the rundown of deferred tax credits and incentivize banks to absorb provisions timely. Registration tax - the purchase of a real estate asset at a court auction will be subject to a fixed EUR200 registration tax in lieu of the 9% registration tax usually applicable, provided that the real estate will be sold within 24 months of the purchase date (the tax advantage applies until Dec 2016) |

**#3 COORDINATE ACROSS MULTIPLE CREDITORS**

| Current | What was changed |
| --- | --- |
| Firms tend to enter insolvency with their assets fully encumbered by secured debt. The secured debt is held by many creditors, which can make coordination difficult and partly explains the liquidity issue. | The proposal contemplated the reach of an agreement with 75% of creditors provided they represent at least half of total debt undertaken and that non-financial creditors e.g. suppliers, are paid in full. |

Source: Governo Italiano, Morgan Stanley Research. See our Italian Banks: NPL workout accelerated, bad bank the next step? (25 Jun 2015) for more details.

**The fund contribution could cost Intesa and Unicredit 26-35bp of CET1 B3.** A draft presentation that was published by **Il Messaggero** suggests the full deduction from common equity tier 1 of the fund's contribution. Based on the breakdown published on **Il Sole 24 Ore**, we estimate a capital charge of 35bp for Intesa and 26bp for Unicredit assuming a contribution to the fund of €1bn each.

**Exhibit 8:** CET1 B3 consumption could be 35bp at Intesa and 26bp at Unicredit on a €1bn exposure

| 4Q15 €'m | Fund contribution | CET1 B3 | RWA | CET1 B3 % | Capital consumption |
|---|---|---|---|---|---|
| Intesa | 1,000 | 36,908 | 284,319 | 13.0% | 0.35% |
| Unicredit | 1,000 | 42,732 | 390,599 | 10.9% | 0.26% |
| **Total fund size** | **6,000** | | | | |

Source: Morgan Stanley Research estimates; Note: Funds contribution as disclosed on Il Sole 24 Ore (12/04/2016)

*Morgan Stanley & Co. International plc ("Morgan Stanley") is currently acting as financial advisor to Unicredit S.p.A. ("Unicredit") in relation to the combination of Pioneer Global Asset Management S.p.A.and Santander Asset Management UK Limited as announced on 23rd April 2015. Unicredit has agreed to pay fees to Morgan Stanley for its financial services. Please refer to the notes at the end of the report.*

**ISP.MI**

**Valuation methodology for our Intesa PT of €3.25.** We Use A Gordon Growth Model Per Division On 2018e Earnings And Use Three Scenarios Based On Different Underlying Macro Outcomes, As Specified Below. We Weight The Outcome 80% To The Base Case, 10% Bear Case And 10% Bull Case. We Assume A CoE Of 9% And Apply A -1% / +1% Impact For Bull And Bear Case. We Assume A Zero Growth Rate.

**Risks**

• The resurgence of a political risk premium in Italy could have an impact on the stock's valuation.

• Volatility in Italian sovereign spreads will continue to affect valuation both positively and negatively.

# Disclosure Section

Morgan Stanley & Co. International plc, authorized by the Prudential Regulatory Authority and regulated by the Financial Conduct Authority and the Prudential Regulatory Authority, disseminates in the UK research that it has prepared, and approves solely for the purposes of section 21 of the Financial Services and Markets Act 2000, research which has been prepared by any of its affiliates. As used in this disclosure section, Morgan Stanley includes RMB Morgan Stanley (Proprietary) Limited, Morgan Stanley & Co International plc and its affiliates.

For important disclosures, stock price charts and equity rating histories regarding companies that are the subject of this report, please see the Morgan Stanley Research Disclosure Website at www.morganstanley.com/researchdisclosures, or contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Research Management), New York, NY, 10036 USA.

For valuation methodology and risks associated with any price targets referenced in this research report, please contact the Client Support Team as follows: US/Canada +1 800 303-2495; Hong Kong +852 2848-5999; Latin America +1 718 754-5444 (U.S.); London +44 (0)20-7425-8169; Singapore +65 6834-6860; Sydney +61 (0)2-9770-1505; Tokyo +81 (0)3-6836-9000. Alternatively you may contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Research Management), New York, NY 10036 USA.

## Analyst Certification

The following analysts hereby certify that their views about the companies and their securities discussed in this report are accurately expressed and that they have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report: Alvaro Serrano.

Unless otherwise stated, the individuals listed on the cover page of this report are research analysts.

## Global Research Conflict Management Policy

Morgan Stanley Research has been published in accordance with our conflict management policy, which is available at www.morganstanley.com/institutional/research/conflictpolicies.

## Important US Regulatory Disclosures on Subject Companies

As of March 31, 2016, Morgan Stanley beneficially owned 1% or more of a class of common equity securities of the following companies covered in Morgan Stanley Research: Banco Popolare, Bank of Ireland, BBVA, BNP Paribas, Commerzbank AG, Credit Suisse Group AG, CYBG Plc, Deutsche Bank, ING, KBC Group NV, Lloyds Banking Group, Nordea, Santander, Societe Generale, UniCredit S.p.A..

Within the last 12 months, Morgan Stanley managed or co-managed a public offering (or 144A offering) of securities of ABN AMRO Group NV, Bank of Ireland, BBVA, CaixaBank SA, Credit Agricole S.A., Credit Suisse Group AG, CYBG Plc, Deutsche Bank, HSBC, ING, Intesa SanPaolo S.p.A., Lloyds Banking Group, Royal Bank of Scotland, Santander, Societe Generale, Svenska Handelsbanken, UBS Group AG.

Within the last 12 months, Morgan Stanley has received compensation for investment banking services from ABN AMRO Group NV, Bank of Ireland, Barclays Bank, BBVA, BNP Paribas, CaixaBank SA, Credit Agricole S.A., Credit Suisse Group AG, CYBG Plc, Deutsche Bank, HSBC, ING, Intesa SanPaolo S.p.A., Lloyds Banking Group, Nordea, Royal Bank of Scotland, Santander, SEB, Societe Generale, Standard Chartered Bank, Svenska Handelsbanken, UBS Group AG.

In the next 3 months, Morgan Stanley expects to receive or intends to seek compensation for investment banking services from ABN AMRO Group NV, Banca Monte dei Paschi di Siena S.p.A., Banca Popolare di Milano S.c.a.r.l., Banco Popolare, Banco Popular (ES), Banco Sabadell, Bank of Ireland, Bankia SA, Bankinter, Barclays Bank, BBVA, BNP Paribas, CaixaBank SA, Commerzbank AG, Credit Agricole S.A., Credit Suisse Group AG, CYBG Plc, Danske Bank, Deutsche Bank, DNB, HSBC, ING, Intesa SanPaolo S.p.A., Julius Baer, KBC Group NV, Lloyds Banking Group, Mediobanca Banca Di Credito Finanziario, Natixis, Nordea, Royal Bank of Scotland, Santander, SEB, Societe Generale, Standard Chartered Bank, Svenska Handelsbanken, Swedbank, UBS Group AG, UniCredit S.p.A., Unione di Banche Italiane SCPA.

Within the last 12 months, Morgan Stanley has received compensation for products and services other than investment banking services from ABN AMRO Group NV, Banca Monte dei Paschi di Siena S.p.A., Banca Popolare di Milano S.c.a.r.l., Banco Popolare, Banco Popular (ES), Banco Sabadell, Bank of Ireland, Bankia SA, Bankinter, Barclays Bank, BBVA, BNP Paribas, CaixaBank SA, Commerzbank AG, Credit Agricole S.A., Credit Suisse Group AG, CYBG Plc, Danske Bank, Deutsche Bank, DNB, HSBC, ING, Intesa SanPaolo S.p.A., Julius Baer, KBC Group NV, Lloyds Banking Group, Mediobanca Banca Di Credito Finanziario, Natixis, Nordea, Royal Bank of Scotland, Santander, SEB, Societe Generale, Standard Chartered Bank, Svenska Handelsbanken, Swedbank, UBS Group AG, UniCredit S.p.A., Unione di Banche Italiane SCPA.

Within the last 12 months, Morgan Stanley has provided or is providing investment banking services to, or has an investment banking client relationship with, the following company: ABN AMRO Group NV, Banca Monte dei Paschi di Siena S.p.A., Banca Popolare di Milano S.c.a.r.l., Banco Popolare, Banco Popular (ES), Banco Sabadell, Bank of Ireland, Bankia SA, Bankinter, Barclays Bank, BBVA, BNP Paribas, CaixaBank SA, Commerzbank AG, Credit Agricole S.A., Credit Suisse Group AG, CYBG Plc, Danske Bank, Deutsche Bank, DNB, HSBC, ING, Intesa SanPaolo S.p.A., Julius Baer, KBC Group NV, Lloyds Banking Group, Mediobanca Banca Di Credito Finanziario, Natixis, Nordea, Royal Bank of Scotland, Santander, SEB, Societe Generale, Standard Chartered Bank, Svenska Handelsbanken, Swedbank, UBS Group AG, UniCredit S.p.A., Unione di Banche Italiane SCPA.

Within the last 12 months, Morgan Stanley has either provided or is providing non-investment banking, securities-related services to and/or in the past has entered into an agreement to provide services or has a client relationship with the following company: ABN AMRO Group NV, Banca Monte dei Paschi di Siena S.p.A., Banca Popolare di Milano S.c.a.r.l., Banco Popolare, Banco Popular (ES), Banco Sabadell, Bank of Ireland, Bankia SA, Bankinter, Barclays Bank, BBVA, BNP Paribas, CaixaBank SA, Commerzbank AG, Credit Agricole S.A., Credit Suisse Group AG, CYBG Plc, Danske Bank, Deutsche Bank, DNB, HSBC, ING, Intesa SanPaolo S.p.A., Julius Baer, KBC Group NV, Lloyds Banking Group, Mediobanca Banca Di Credito Finanziario, Natixis, Nordea, Royal Bank of Scotland, Santander, SEB, Societe Generale, Standard Chartered Bank, Svenska Handelsbanken, Swedbank, UBS Group AG, UniCredit S.p.A., Unione di Banche Italiane SCPA.

Within the last 12 months, Morgan Stanley has either provided or is providing non-securities related services to and/or in the past has entered into an agreement to provide services or has a client relationship with the following company: Commerzbank AG.

Morgan Stanley & Co. LLC makes a market in the securities of Barclays Bank, BBVA, Credit Suisse Group AG, Deutsche Bank, HSBC, ING, Lloyds Banking Group, Royal Bank of Scotland, Santander, UBS Group AG.

Morgan Stanley & Co. International plc is a corporate broker to Royal Bank of Scotland.

The equity research analysts or strategists principally responsible for the preparation of Morgan Stanley Research have received compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors, firm revenues and overall investment banking revenues.

Morgan Stanley and its affiliates do business that relates to companies/instruments covered in Morgan Stanley Research, including market making, providing liquidity, fund management, commercial banking, extension of credit, investment services and investment banking. Morgan Stanley sells to and buys from customers the securities/instruments of companies covered in Morgan Stanley Research on a principal basis. Morgan Stanley may have a position in the debt of the Company or instruments discussed in this report.

Certain disclosures listed above are also for compliance with applicable regulations in non-US jurisdictions.

## STOCK RATINGS

Morgan Stanley uses a relative rating system using terms such as Overweight, Equal-weight, Not-Rated or Underweight (see definitions below). Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight, Not-Rated and Underweight are not the equivalent of buy, hold and sell. Investors should carefully read the definitions of all ratings used in Morgan Stanley Research. In addition, since Morgan Stanley Research contains more complete information concerning the analyst's views, investors should carefully read Morgan Stanley Research, in its entirety, and not infer the contents from the rating alone. In any case, ratings (or research) should not be used or relied upon as investment advice. 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.

## Global Stock Ratings Distribution

(as of March 31, 2016)
For disclosure purposes only (in accordance with NASD and NYSE requirements), we include the category headings of Buy, Hold, and Sell alongside our ratings of Overweight, Equal-weight, Not-Rated and Underweight. Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight, Not-Rated and Underweight are not the equivalent of buy, hold, and sell but represent recommended relative weightings (see definitions below). To satisfy regulatory requirements, we correspond Overweight, our most positive stock rating, with a buy recommendation; we correspond Equal-weight and Not-Rated to hold and Underweight to sell recommendations, respectively.

| | COVERAGE UNIVERSE | | INVESTMENT BANKING CLIENTS (IBC) | | |
|---|---|---|---|---|---|
| STOCK RATING CATEGORY | COUNT | % OF TOTAL | COUNT | % OF TOTAL IBC | % OF RATING CATEGORY |
| **Overweight/Buy** | **1219** | **36%** | **305** | **41%** | **25%** |
| **Equal-weight/Hold** | **1405** | **41%** | **333** | **45%** | **24%** |
| **Not-Rated/Hold** | **81** | **2%** | **5** | **1%** | **6%** |
| **Underweight/Sell** | **691** | **20%** | **95** | **13%** | **14%** |
| **TOTAL** | **3,396** | | **738** | | |

Data include common stock and ADRs currently assigned ratings. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months.

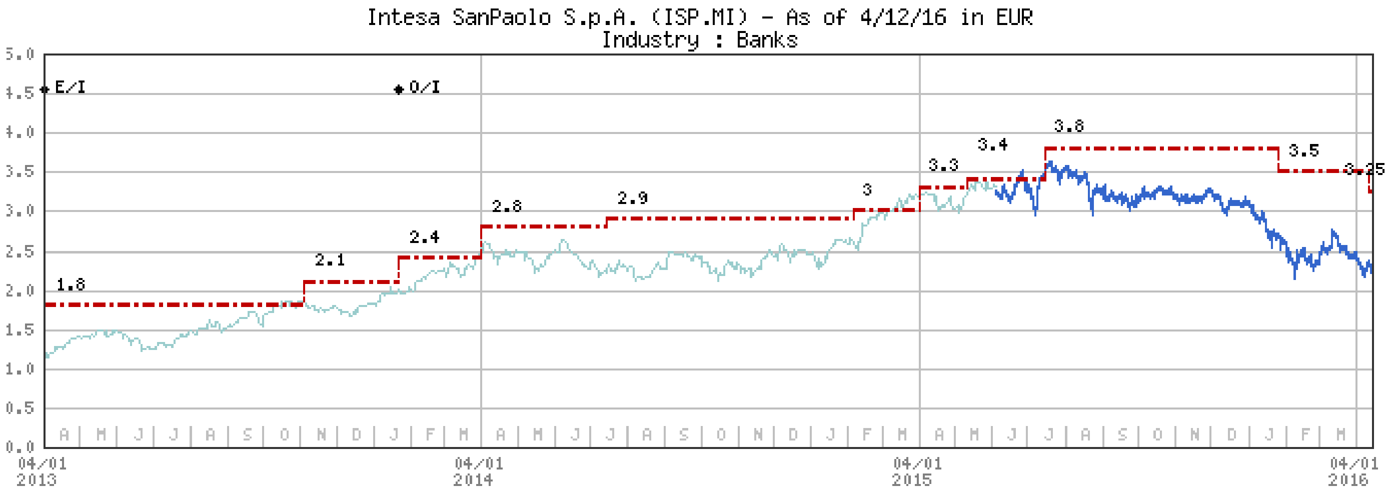
## Analyst Stock Ratings

Overweight (O). The stock's total return is expected to exceed the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Equal-weight (E). The stock's total return is expected to be in line with the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Not-Rated (NR). Currently the analyst does not have adequate conviction about the stock's total return relative to the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Underweight (U). The stock's total return is expected to be below the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

## Analyst Industry Views

Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.
In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.
Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.
Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index or MSCI sub-regional index or MSCI AC Asia Pacific ex Japan Index.

## Stock Price, Price Target and Rating History (See Rating Definitions)




Stock Rating History: 4/1/13 : E/I; 1/22/14 : O/I

Price Target History: 1/22/13 : 1.8; 11/4/13 : 2.1; 1/22/14 : 2.4; 3/31/14 : 2.8; 7/14/14 : 2.9; 2/5/15 : 3; 4/1/15 : 3.3; 5/12/15 : 3.4; 7/15/15 : 3.8; 1/26/16 : 3.5; 4/11/16 : 3.25

Source: Morgan Stanley Research Date Format : MM/DD/YY Price Target -- No Price Target Assigned (NA)
Stock Price (Not Covered by Current Analyst) Stock Price (Covered by Current Analyst)
Stock and Industry Ratings (abbreviations below) appear as ◆ Stock Rating/Industry View
Stock Ratings: Overweight (O) Equal-weight (E) Underweight (U) Not-Rated (NR) No Rating Available (NA)
Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

Effective January 13, 2014, the stocks covered by Morgan Stanley Asia Pacific will be rated relative to the analyst's industry (or industry team's) coverage.

Effective January 13, 2014, the industry view benchmarks for Morgan Stanley Asia Pacific are as follows: relevant MSCI country index or MSCI sub-regional index or MSCI AC Asia Pacific ex Japan Index.

## Important Disclosures for Morgan Stanley Smith Barney LLC Customers

Important disclosures regarding the relationship between the companies that are the subject of Morgan Stanley Research and Morgan Stanley Smith Barney LLC or Morgan Stanley or any of their affiliates, are available on the Morgan Stanley Wealth Management disclosure website at www.morganstanley.com/online/researchdisclosures. For Morgan Stanley specific disclosures, you may refer to www.morganstanley.com/researchdisclosures.

Each Morgan Stanley Equity Research report is reviewed and approved on behalf of Morgan Stanley Smith Barney LLC. This review and approval is conducted by the same person who reviews the Equity Research report on behalf of Morgan Stanley. This could create a conflict of interest.

## Other Important Disclosures

Morgan Stanley & Co. International PLC and its affiliates have a significant financial interest in the debt securities of Banca Popolare di Milano S.c.a.r.l., Banco Popolare, Banco Popular (ES), Banco Sabadell, Bank of Ireland, Bankia SA, Barclays Bank, BBVA, BNP Paribas, CaixaBank SA, Commerzbank AG, Credit Agricole S.A., Credit Suisse Group AG, Danske Bank, Deutsche Bank, HSBC, ING, Intesa SanPaolo S.p.A., KBC Group NV, Lloyds Banking Group, Mediobanca Banca Di Credito Finanziario, Natixis, Nordea, Royal Bank of Scotland, Santander, SEB, Societe Generale, Standard Chartered Bank, Svenska Handelsbanken, Swedbank, UBS Group AG, UniCredit S.p.A., Unione di Banche Italiane SCPA.

Morgan Stanley is not acting as a municipal advisor and the opinions or views contained herein are not intended to be, and do not constitute, advice within the meaning of Section 975 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Morgan Stanley produces an equity research product called a "Tactical Idea." Views contained in a "Tactical Idea" on a particular stock may be contrary to the recommendations or views expressed in research on the same stock. This may be the result of differing time horizons, methodologies, market events, or other factors. For all research available on a particular stock, please contact your sales representative or go to Matrix at http://www.morganstanley.com/matrix.

Morgan Stanley Research is provided to our clients through our proprietary research portal on Matrix and also distributed electronically by Morgan Stanley to clients. Certain, but not all, Morgan Stanley Research products are also made available to clients through third-party vendors or redistributed to clients through alternate electronic means as a convenience. For access to all available Morgan Stanley Research, please contact your sales representative or go to Matrix at http://www.morganstanley.com/matrix.

Any access and/or use of Morgan Stanley Research is subject to Morgan Stanley's Terms of Use (http://www.morganstanley.com/terms.html). By accessing and/or using Morgan Stanley Research, you are indicating that you have read and agree to be bound by our Terms of Use (http://www.morganstanley.com/terms.html). In addition you consent to Morgan Stanley processing your personal data and using cookies in accordance with our Privacy Policy and our Global Cookies Policy (http://www.morganstanley.com/privacy_pledge.html), including for the purposes of setting your preferences and to collect readership data so that we can deliver better and more personalized service and products to you. To find out more information about how Morgan Stanley processes personal data, how we use cookies and how to reject cookies see our Privacy Policy and our Global Cookies Policy (http://www.morganstanley.com/privacy_pledge.html).

If you do not agree to our Terms of Use and/or if you do not wish to provide your consent to Morgan Stanley processing your personal data or using cookies please do not access our research.

Morgan Stanley Research does not provide individually tailored investment advice. Morgan Stanley Research has been prepared without regard to the circumstances and objectives of those who receive it. Morgan Stanley recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. The appropriateness of an investment or strategy will depend on an investor's circumstances and objectives. The securities, instruments, or strategies discussed in Morgan Stanley Research may not be suitable for all investors, and certain investors may not be eligible to purchase or participate in some or all of them. Morgan Stanley Research is not an offer to buy or sell or the solicitation of an offer to buy or sell any security/instrument or to participate in any particular trading strategy. The value of and income from your investments may vary because of changes in interest rates, foreign exchange rates, default rates, prepayment rates, securities/instruments prices, market indexes, operational or financial conditions of companies or other factors. There may be time limitations on the exercise of options or other rights in securities/instruments transactions. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realized. If provided, and unless otherwise stated, the closing price on the cover page is that of the primary exchange for the subject company's securities/instruments.

The fixed income research analysts, strategists or economists principally responsible for the preparation of Morgan Stanley Research have received compensation based upon various factors, including quality, accuracy and value of research, firm profitability or revenues (which include fixed income trading and capital markets profitability or revenues), client feedback and competitive factors. Fixed Income Research analysts', strategists' or economists' compensation is not linked to investment banking or capital markets transactions performed by Morgan Stanley or the profitability or revenues of particular trading desks.

The "Important US Regulatory Disclosures on Subject Companies" section in Morgan Stanley Research lists all companies mentioned where Morgan Stanley owns 1% or more of a class of common equity securities of the companies. For all other companies mentioned in Morgan Stanley Research, Morgan Stanley may have an investment of less than 1% in securities/instruments or derivatives of securities/instruments of companies and may trade them in ways different from those discussed in Morgan Stanley Research. Employees of Morgan Stanley not involved in the preparation of Morgan Stanley Research may have investments in securities/instruments or derivatives of securities/instruments of companies mentioned and may trade them in ways different from those discussed in Morgan Stanley Research. Derivatives may be issued by Morgan Stanley or associated persons.

With the exception of information regarding Morgan Stanley, Morgan Stanley Research is based on public information. Morgan Stanley makes every effort to use reliable, comprehensive information, but we make no representation that it is accurate or complete. We have no obligation to tell you when opinions or information in Morgan Stanley Research change apart from when we intend to discontinue equity research coverage of a subject company. Facts and views presented in Morgan Stanley Research have not been reviewed by, and may not reflect information known to, professionals in other Morgan Stanley business areas, including investment banking personnel.

Morgan Stanley Research personnel may participate in company events such as site visits and are generally prohibited from accepting payment by the company of associated expenses unless pre-approved by authorized members of Research management.

Morgan Stanley may make investment decisions that are inconsistent with the recommendations or views in this report.

To our readers in Taiwan: Information on securities/instruments that trade in Taiwan is distributed by Morgan Stanley Taiwan Limited ("MSTL"). Such information is for your reference only. The reader should independently evaluate the investment risks and is solely responsible for their investment decisions. Morgan Stanley Research may not be distributed to the public media or quoted or used by the public media without the express written consent of Morgan Stanley. Information on securities/instruments that do not trade in Taiwan is for informational purposes only and is not to be construed as a recommendation or a solicitation to trade in such securities/instruments. MSTL may not execute transactions for clients in these securities/instruments. To our readers in Hong Kong: Information is distributed in Hong Kong by and on behalf of, and is attributable to, Morgan Stanley Asia Limited as part of its regulated activities in Hong Kong. If you have any queries concerning Morgan Stanley Research, please contact our Hong Kong sales representatives.

Morgan Stanley is not incorporated under PRC law and the research in relation to this report is conducted outside the PRC. Morgan Stanley Research does not constitute an offer to sell or the solicitation of an offer to buy any securities in the PRC. PRC investors shall have the relevant qualifications to invest in such securities and shall be responsible for obtaining all relevant approvals, licenses, verifications and/or registrations from the relevant governmental authorities themselves.

Morgan Stanley Research is disseminated in Brazil by Morgan Stanley C.T.V.M. S.A.; in Mexico by Morgan Stanley México, Casa de Bolsa, S.A. de C.V which is regulated by Comision Nacional Bancaria y de Valores. Paseo de los Tamarindos 90, Torre 1, Col. Bosques de las Lomas Floor 29, 05120 Mexico City; in Japan by Morgan Stanley MUFG Securities Co., Ltd. and, for Commodities related research reports only, Morgan Stanley Capital Group Japan Co., Ltd; in Hong Kong by Morgan Stanley Asia Limited (which accepts responsibility for its contents) and by Bank Morgan Stanley AG, Hong Kong Branch; in Singapore by Morgan Stanley Asia (Singapore) Pte. (Registration number 199206298Z) and/or Morgan Stanley Asia (Singapore) Securities Pte Ltd (Registration number 200008434H), regulated by the Monetary Authority of Singapore (which accepts legal responsibility for its contents and should be contacted with respect to any matters arising from, or in connection with, Morgan Stanley Research) and by Bank Morgan Stanley AG, Singapore Branch (Registration number T11FC0207F); in Australia to "wholesale clients" within the meaning of the Australian Corporations Act by Morgan Stanley Australia Limited A.B.N. 67 003 734 576, holder of Australian financial services license No. 233742, which accepts responsibility for its contents; in Australia to "wholesale clients" and "retail clients" within the meaning of the Australian Corporations Act by Morgan Stanley Wealth Management Australia Pty Ltd (A.B.N. 19 009 145 555, holder of Australian financial services license No. 240813, which accepts responsibility for its contents; in Korea by Morgan Stanley & Co International plc, Seoul Branch; in India by Morgan Stanley India Company Private Limited; in Indonesia by PT Morgan Stanley Asia Indonesia; in Canada by Morgan Stanley Canada Limited, which has approved of and takes responsibility for its contents in Canada; in Germany by Morgan Stanley Bank AG, Frankfurt am Main and Morgan Stanley Private Wealth Management Limited, Niederlassung Deutschland, regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin); in Spain by Morgan Stanley, S.V., S.A., a Morgan Stanley group company, which is supervised by the Spanish Securities Markets Commission (CNMV) and states that Morgan Stanley Research has been written and distributed in accordance with the rules of conduct applicable to financial research as established under Spanish regulations; in the US by Morgan Stanley & Co. LLC, which accepts responsibility for its contents. Morgan Stanley & Co. International plc, authorized by the Prudential Regulatory Authority and regulated by the Financial Conduct Authority and the Prudential Regulatory Authority, disseminates in the UK research that it has prepared, and approves solely for the purposes of section 21 of the Financial Services and Markets Act 2000, research which has been prepared by any of its affiliates. RMB Morgan Stanley (Proprietary) Limited is a member of the JSE Limited and regulated by the Financial Services Board in South Africa. RMB Morgan Stanley (Proprietary) Limited is a joint venture owned equally by Morgan Stanley International Holdings Inc. and RMB Investment Advisory (Proprietary) Limited, which is wholly owned by FirstRand Limited. The information in Morgan Stanley Research is being disseminated by Morgan Stanley Saudi Arabia, regulated by the Capital Market Authority in the Kingdom of Saudi Arabia , and is directed at Sophisticated investors only.

Morgan Stanley Bank AG currently acts as a designated sponsor for the following securities: Deutsche Bank.

Morgan Stanley Hong Kong Securities Limited is the liquidity provider/market maker for securities of HSBC listed on the Stock Exchange of Hong Kong Limited. An updated list can be found on HKEx website: http://www.hkex.com.hk.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (DIFC Branch), regulated by the Dubai Financial Services Authority (the DFSA), and is directed at Professional Clients only, as defined by the DFSA. The financial products or financial services to which this research relates will only be made available to a customer who we are satisfied meets the regulatory criteria to be a Professional Client.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (QFC Branch), regulated by the Qatar Financial Centre Regulatory Authority (the QFCRA), and is directed at business customers and market counterparties only and is not intended for Retail Customers as defined by the QFCRA.

As required by the Capital Markets Board of Turkey, investment information, comments and recommendations stated here, are not within the scope of investment advisory activity. Investment advisory service is provided exclusively to persons based on their risk and income preferences by the authorized firms. Comments and recommendations stated here are general in nature. These opinions may not fit to your financial status, risk and return preferences. For this reason, to make an investment decision by relying solely to this information stated here may not bring about outcomes that fit your expectations.

The trademarks and service marks contained in Morgan Stanley Research are the property of their respective owners. Third-party data providers make no warranties or representations relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages relating to such data. The Global Industry Classification Standard (GICS) was developed by and is the exclusive property of MSCI and S&P.

**INDUSTRY COVERAGE: Banks**

| COMPANY (TICKER) | RATING (AS OF) | PRICE* (04/12/2016) |
|---|---|---|
| **Alice Timperley, CFA** | | |
| Danske Bank (DANSKE.CO) | O (04/21/2015) | DKr 174.10 |
| DNB (DNB.OL) | E (01/26/2016) | NKr 97.80 |
| Nordea (NDA.ST) | E (03/28/2011) | SKr 76.40 |
| SEB (SEBa.ST) | O (07/23/2014) | SKr 78.15 |
| Svenska Handelsbanken (SHBa.ST) | U (09/21/2015) | SKr 100.50 |
| Swedbank (SWEDa.ST) | E (07/23/2014) | SKr 165.70 |
| **Alvaro Serrano** | | |
| Banca Monte dei Paschi di Siena S.p.A. (BMPS.MI) | U (07/14/2014) | €0.52 |
| Banca Popolare di Milano S.c.a.r.l. (PMII.MI) | O (07/14/2014) | €0.58 |
| Banco Popolare (BAPO.MI) | U (07/15/2015) | €5.33 |
| Banco Popular (ES) (POP.MC) | E (02/09/2016) | €2.18 |
| Banco Sabadell (SABE.MC) | U (06/30/2015) | €1.44 |
| Bankia SA (BKIA.MC) | O (09/17/2015) | €0.78 |
| Bankinter (BKT.MC) | U (09/26/2014) | €6.16 |
| BBVA (BBVA.MC) | O (11/24/2014) | €5.50 |
| CaixaBank SA (CABK.MC) | O (01/18/2016) | €2.51 |
| Intesa SanPaolo S.p.A. (ISP.MI) | O (01/22/2014) | €2.24 |
| Mediobanca Banca Di Credito Finanziario (MDBI.MI) | E (10/28/2015) | €6.25 |
| Santander (SAN.MC) | E (11/13/2013) | €3.77 |
| UniCredit S.p.A. (CRDI.MI) | O (01/22/2013) | €2.98 |
| Unione di Banche Italiane SCPA (UBI.MI) | E (01/22/2014) | €3.13 |
| **Bruce Hamilton** | | |
| ABN AMRO Group NV (ABNd.AS) | O (01/04/2016) | €18.22 |
| BNP Paribas (BNPP.PA) | O (04/22/2015) | €42.56 |
| Credit Agricole S.A. (CAGR.PA) | ++ | €9.24 |
| ING (ING.AS) | U (03/31/2016) | €10.37 |
| KBC Group NV (KBC.BR) | E (08/14/2014) | €46.70 |
| Natixis (CNAT.PA) | O (10/09/2014) | €4.44 |
| Societe Generale (SOGN.PA) | E (12/07/2014) | €31.36 |
| **Canset A Eroglu** | | |
| Commerzbank AG (CBKG.DE) | E (05/05/2015) | €7.75 |
| **Chris Manners, ACA** | | |
| Bank of Ireland (BKIR.I) | E (09/18/2014) | €0.25 |
| Barclays Bank (BARC.L) | E (11/20/2015) | 156p |
| HSBC (HSBA.L) | U (02/08/2016) | 420p |
| Lloyds Banking Group (LLOY.L) | O (08/08/2013) | 67p |
| Royal Bank of Scotland (RBS.L) | O (08/26/2015) | 217p |
| Standard Chartered Bank (STAN.L) | U (02/28/2014) | 471p |
| **Fiona Simpson, CFA** | | |
| CYBG Plc (CYB.AX) | O (03/15/2016) | A$3.91 |
| CYBG Plc (CYBGC.L) | E (03/15/2016) | 211p |
| **Huw Van Steenis** | | |
| Credit Suisse Group AG (CSGN.S) | E (02/05/2016) | SFr 13.42 |
| Deutsche Bank (DBKGn.DE) | E (10/11/2010) | €13.98 |
| Julius Baer (BAER.S) | E (02/17/2014) | SFr 39.17 |
| UBS Group AG (UBSG.S) | O (01/18/2012) | SFr 14.68 |

Stock Ratings are subject to change. Please see latest research for each company.
* Historical prices are not split adjusted.