MMCG - TLTRO

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AGENDA

- TLTRO – Expected Impact on Excess Liquidity
- TLTRO – Substitution from existing Operations
- Changes in the Banks and Investors Behaviour : Impact on Market Segmentation
- Expected Impact on interest Rates

TLTRO – Expected impact on excess liquidity

- We expect ca. EUR 350bn to be allotted at the first two T-LTROs and an additional EUR 360bn to be allotted at the quarterly operations scheduled from March 2015 until June 2016. In Italy the estimated volume for the first TLTRO-amount is € 75 bln.

- Excess liquidity in the EMU could rise back above EUR 200bn as a result of the first two T-LTROs. The next few months' trend remains very uncertain though due to the speed and size of weekly repayments of 3Y LTRO funds as well as to the path of autonomous factors.

- The biggest potential for a rise in excess liquidity arises from the 3rd to 8th T-LTROs, so from March 2015 onwards. Excess liquidity might rise towards EUR 400bn by mid-2016 and to stay positive for years.

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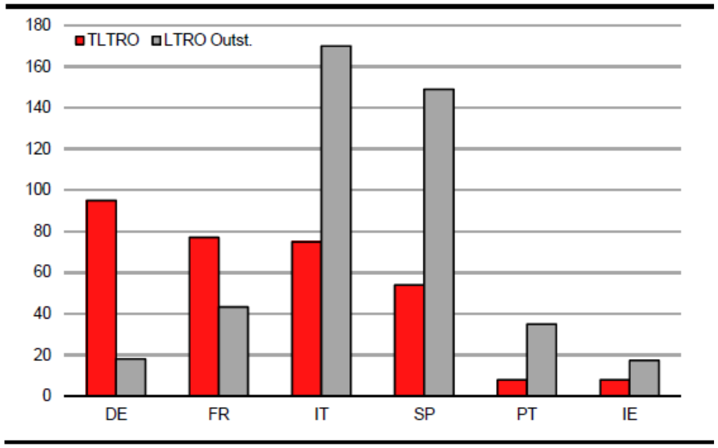
TLTRO – Substitution from existing operations

- The first two T-LTROs will lead to a sizable increase in excess liquidity for core banks, while switches from the 3Y LTRO to the T-LTRO will imply a more modest impact for the periphery.

3Y LTRO VS. FIRST TWO T-LTRO ALLOWANCE (EUR BN)



- Under the aggressive assumption that banks will fully reimburse their outstanding 3Y LTRO balances with weekly repayments (i.e. they will not switch 3Y LTRO funds in excess of the T-LTRO allotment into shorted-dated operations), excess liquidity in the EMU could go to zero but only for a brief period.

- Note that it would be very unlikely to observe such an aggressive repayment path as, if shrinking excess liquidity leads to pressure on MM rates, banks would arbitrage this out using ECB operations. Under the more realistic assumption that banks will only in part reimburse their outstanding 3Y LTRO balances, excess liquidity would remain positive until March 2015, and beyond.

Changes in the banks and investors behaviour : Impact on market segmentation

- TLTROs borrowing to be prudentially considered as medium term funding with maturity up to 2years, instead of 4 years due to the "forced early repayment" clause linked to lending development
- In case of volatile dynamics of eligible net loans leading to a cumulative net growth of the lending from May14 to Apr16 below the benchmark, the TLTROs amount should be early reimbursed in Sep16
  - concentration risk per maturity related to all the funding instruments should be carefully evaluated
  - possible reputational risk in case of forced reimbursement due to poor net lending developments
- Possible positive impact on PL in case of partial substitution of other medium term funding on the market with TLTRO that is cheaper for both 2 and 4 years maturity (depending on the cost of funding for counterparties located in periphery or core countries)
- As TLTRO borrowing should be considered as funding with 2 years maturity, partially substituting other medium long term funding sources, it could be used for commercial lending financing. prioritizing, in terms of FTP, products according to the banks core activity (ML term, ST term, consumer financing)
- Access to the 2nd TLTRO in December 2014 gives time to collect more precise information on the expected lending dynamics and therefore on the risk of early repayment, but may also imply loosing ground with respect to competitors, in case of peers large participation to the 1st TLTRO.
- Even if Counterbalancing Capacity decay and encumbrance has to be analyzed, banks could increase their pool of guaranties using the new eligible commercial loans.
- In case of liquidity excess generation connected with TLTRO access or future Balance Sheet development, a possible review of the investment strategy (e.g. on Govies exposure) may be necessary following local market circumstances (core vs. periphery)

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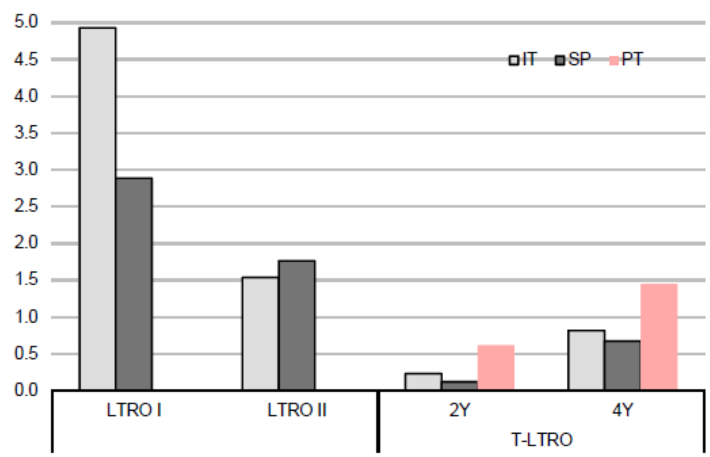
How does market cope with negative rates

- The need to park liquidity at least temporarily for core banks will support short dated spread products across core markets and possibly interbank lending.

- Opportunities for carry trades across periphery would be more attractive. Sovereign curves in the periphery start offering a positive carry already at relatively short tenors (ca. 1Y for the Italian curve). However, net liquidity injections in the periphery after the first two T-LTROs are likely to be very small (due to switches from the 3Y LTRO), so we do not expect a sizable contribution to spread tightening from this source.

- The OIS curve should keep flat and OIS rates subdued (and below the refi rate) for a prolonged period of time.

Carry Trades



Spread vs. LTRO cost of a bond with matched maturity (in %)

5Y 1Y OIS