Risk management

BASIC PRINCIPLES

The policies relating to risk acceptance are defined by the Parent Company's Administrative Bodies (Supervisory Board and Management Board), with support from specific Committees.
The Parent Company is in charge of overall direction, management and control of risks, whereas Group companies that generate credit and/or financial risks operate within the assigned autonomy limits and have their own control structures. A service agreement governs the risk control activities performed by the Parent Company's functions on behalf of the main subsidiaries. These functions report directly to the subsidiary's management bodies.
The risk measurement and management tools together define a risk-monitoring framework at Group level, capable of assessing the risks assumed by the Group from a regulatory and economic point of view. The level of absorption of economic capital, defined as the maximum "unexpected" loss that could be borne by the Group over a period of one year, is a key measure for determining the Group's financial structure and for guiding operations, ensuring a balance between risks assumed and shareholder returns. It is estimated on the basis of the current situation and also as a forecast, based on the Budget assumptions and projected economic scenario under ordinary and stress conditions. The capital position forms the basis for business reporting and is submitted quarterly to the Group Risk Governance Committee, the Management Board and the Control Committee, as part of the Group's Risks Tableau de Bord.
Given the nature, frequency and potential impact of the risk, risk hedging is based on a constant balance between mitigation/hedging action, control procedures/processes and capital protection measures.

BASEL 2 REGULATIONS AND THE INTERNAL PROJECT

Within the Basel 2 Project, the purpose of which is to prepare the Group for the adoption of advanced approaches, an "initial scope" of companies that use approaches based on internal models has been identified. For this scope, the Group secured permission to use the IRB Foundation approach for the Corporate segment, effective from the report as at 31 December 2008.
In 2009, the Group initiated a process of expanding the scope of application of internal models by securing permission for the use of the IRB Foundation approach by network banks belonging to the former Cassa di Risparmio di Firenze Group (effective from the report as at 31 December 2009) and by Intesa Sanpaolo Bank Ireland (effective from the report as at 31 March 2010) and also submitted an application to start the procedure for the international subsidiaries CIB Bank and VUB Banka and the Italian Banca IMI.

In 2008, the Group had implemented rating models and credit processes for the SME Retail and Retail segments (residential mortgages), and in 2009 it completed development of the LGD (Loss Given Default) model, which will allow for the adoption in 2010 of the IRB approach for the Retail Mortgage segment, followed by the adoption of the IRB approach for the SME Retail segment and the advanced IRB approach for the Corporate segment.
The Group is also proceeding with development of the rating models for the other segments and the extension of the scope of companies for their application in accordance with the gradual roll-out plan for the advanced approaches presented to the Supervisory Authority.
On the subject of operational risk, it should be noted that the Group secured permission, effective from the report as at 31 December 2009, to use the Advanced AMA Approach (internal model) to determine the associated capital requirement on an initial scope that includes the Banks and Companies of the Banca dei Territori Division (excluding network banks belonging to Cassa di Risparmio di Firenze Group, except for Casse del Centro), Leasint, Eurizon Capital and VUB Banka. The remaining companies, which currently employ the Standardised approach, will gradually migrate to the Advanced approaches beginning in 2010.
Furthermore, in the first quarter of 2010 the Group presented its Internal Capital Adequacy Assessment Process Report as a "class 1" banking group, according to Bank of Italy classification, based on the extensive use of internal methodologies for the measurement of risk, internal capital and total capital available.

As part of its adoption of Basel 2, the Group publishes information concerning capital adequacy, exposure to risks and the general characteristics of the systems aimed at identifying, monitoring and managing them in a document entitled "Basel 2 - Pillar 3" or simply "Pillar 3".
As Intesa Sanpaolo is among the groups that have adopted validated internal approaches for credit, market and operational risk, the document is published on the website each quarter, at the address: group.intesasanpaolo.com.

CREDIT RISK

The Group's strategies, powers and rules for the granting and management of loans are aimed at:
- coordinating actions to achieve sustainable growth of lending operations consistent with the risk appetite and value creation;
- diversifying the portfolio, limiting the concentration of exposures on single counterparties/groups, single sectors or geographical areas;
- efficiently selecting economic groups and individual borrowers through a thorough analysis of their creditworthiness aimed at limiting the risk of insolvency;
- favouring lending of a commercial nature or intended for new investments in production, provided that they are sustainable, over those of a merely financial nature;
- constantly monitoring relationships, through the use of both IT procedures and systematic surveillance of positions that show irregularities with the aim of detecting any symptoms of performance deterioration in a timely manner.

The Intesa Sanpaolo Group has developed a set of techniques and tools for credit risk measurement and management which ensures analytical control over the quality of loans to customers and financial institutions, and loans subject to country risk.
With particular reference to loans to customers, risk is measured using rating models which change according to the segment to which the counterparty belongs.

Credit quality

Constant monitoring of the quality of the loan portfolio is pursued through specific operating checks for all the phases of loan management.
The overall non-performing loan portfolio is accurately monitored through a predetermined control system and periodic managerial reporting. In particular, these activities are performed using measurement methods and performance controls that allow the production of synthetic risk indicators. They allow timely assessments to be formulated when any anomalies arise or persist and interact with processes and procedures for loan management and for credit risk control.
Positions to which the synthetic risk indicator attributes a persistent high-risk rating are intercepted (manually or automatically) and included in an operational category based on their risk profile. They are classified in the following categories: doubtful loans, i.e., exposures to borrowers in default or in similar situations; substandard loans, i.e., exposures to borrowers in temporary difficulty, deemed likely to be settled in a reasonable period of time; restructured loans, i.e., positions for which, due to the deterioration of the economic and financial position of the borrower, the bank (or pool of banks) agrees to modify the original contractual terms giving rise to a loss. Lastly, non-performing loans also include past due positions that have exceeded objective payment terms as established by the Bank of Italy.

(millions of euro)

	31.03.2010			31.12.2009			Changes
	Gross exposure	Total adjustments	Net exposure	Gross exposure	Total adjustments	Net exposure	Net exposure
Doubtful loans	17,604	-11,723	5,881	16,459	-11,094	5,365	516
Substandard loans	12,274	-2,518	9,756	12,970	-2,600	10,370	-614
Restructured loans	3,349	-218	3,131	2,402	-109	2,293	838
Past due loans	2,412	-142	2,270	2,577	-160	2,417	-147
Non-performing loans	**35,639**	**-14,601**	**21,038**	**34,408**	**-13,963**	**20,445**	**593**
Performing loans	332,034	-2,446	329,588	337,503	-2,442	335,061	-5,473
Performing loans represented by securities	19,410	-555	18,855	19,083	-556	18,527	328
Loans to customers	**387,083**	**-17,602**	**369,481**	**390,994**	**-16,961**	**374,033**	**-4,552**

Figures restated where required by international accounting standards and, where necessary, considering the changes in the scope of consolidation and discontinued operations.

As at 31 March 2010, the Group recorded a slight increase in non-performing loans both in gross terms (+3.6%) and net of adjustments (+2.9%).
This trend led to a higher incidence of net non-performing loans on total net loans to customers, increasing from 5.5% to 5.7%. As at 31 March 2010, the hedging of non-performing loans, pursued through prudential provisioning policies extended to all commercial banks, stood at approximately 41%, compared to 40.6% at the end of 2009.
In more detail, doubtful loans net of adjustments totalled 5,881 million euro, with a 516 million euro rise from the beginning of the year (+9.6%); the incidence on total loans was 1.6%, with a coverage ratio of approximately 67%.
Substandard loans, net of adjustments, amounted to 9,756 million euro, down by approximately 5.9% compared to the end of 2009, attributable in part to the reaching of restructuring agreements that resulted in the classification of several positions among restructured loans. Substandard loans came to 2.6% of the total, showing a coverage ratio of 20.5%.
Restructured loans, 3,131 million euro net of adjustments, showed an increase over the 2,293 million euro as at 31 December 2009 due to the abovementioned restructuring agreements. The related coverage ratio is 6.5%.
Past due loans amounted to 2,270 million euro net of adjustments with a 147 million euro decrease (-6.1%) and an approximate 5.9% coverage ratio.
Cumulated collective adjustments on performing loans came to 0.74% of gross exposure relating to loans to customers, up slightly compared to 0.72% as at December 2009. The risk associated with the performing loan portfolio is calculated collectively on the basis of the risk configuration of the entire portfolio analysed by means of models that consider the Probability of Default (PD) and Loss Given Default (LGD) for each loan.

MARKET RISKS

TRADING BOOK

Quantification of trading risks is based on daily and period estimates of sensitivity of the trading portfolios of Intesa Sanpaolo and Banca IMI, which represent the main portion of the Group's market risks, to adverse market movements of the following risk factors:
- interest rates;
- equity and market indices;
- investment funds;
- foreign exchange rates;
- implied volatilities;
- spreads in credit default swaps (CDSs);
- spreads in bond issues;
- correlation instruments;
- dividend derivatives;
- asset-backed securities (ABSs);
- commodities.

Some of the other Group subsidiaries hold smaller trading portfolios with a marginal risk (around 2% of the Group's overall risk). In particular, the risk factors of the international subsidiaries' trading books were interest rates and foreign exchange rates, both relating to linear pay-offs.

For some of the risk factors indicated above, the Supervisory Authority has validated the internal models for the reporting of the capital absorptions of both Intesa Sanpaolo and Banca IMI.
In particular, the validated risk profiles for market risks are: (i) generic on debt securities and generic/specific on equities for Intesa Sanpaolo and Banca IMI, (ii) position risk on quotas of UCI solely with reference to the quotas in CPPI (Constant Proportion Portfolio Insurance) for Banca IMI, and (iii) optional risk and specific risk for the CDS portfolio for Intesa Sanpaolo.
From the third quarter of 2009 the scope of the validated risk profiles was extended to dividend derivatives for Intesa Sanpaolo and Banca IMI.
The analysis of market risk profiles relative to the trading book uses various quantitative indicators and VaR is the most important. Since VaR is a synthetic indicator which does not fully identify all types of potential loss, risk management has been enriched with other measures, in particular simulation measures for the quantification of risks from illiquid parameters (dividends, correlation, ABS, hedge funds).
VaR estimates are calculated daily based on simulations of historical time-series, a 99% confidence level and 1-day holding period.
The following paragraphs provide the estimates and evolution of VaR, defined as the sum of VaR and of the simulation on illiquid parameters, for the trading book of Intesa Sanpaolo and Banca IMI.

In the first quarter of 2010, the market risks generated by Intesa Sanpaolo and Banca IMI decreased slightly compared to the averages for the last quarter of 2009. The average VaR for the period totalled 29.3 million euro.

Daily VaR of the trading book for Intesa Sanpaolo and Banca IMI[(a)]

(millions of euro)

	2010			2009			
	average 1st quarter	minimum 1st quarter	maximum 1st quarter	average 4th quarter	average 3rd quarter	average 2nd quarter	average 1st quarter
Intesa Sanpaolo	19.5	17.7	23.0	21.8	25.8	27.9	32.3
Banca IMI	9.8	6.8	13.0	10.1	10.6	15.7	18.0
Total	**29.3**	**25.7**	**33.5**	**31.9**	**36.4**	**43.6**	**50.3**

(a) Each line in the table sets out past estimates of daily VaR calculated on the quarterly historical time-series respectively of Intesa Sanpaolo and Banca IMI; minimum and maximum values for Intesa Sanpaolo and Banca IMI are estimated using aggregate historical time-series and therefore do not correspond to the sum of the individual values in the column.

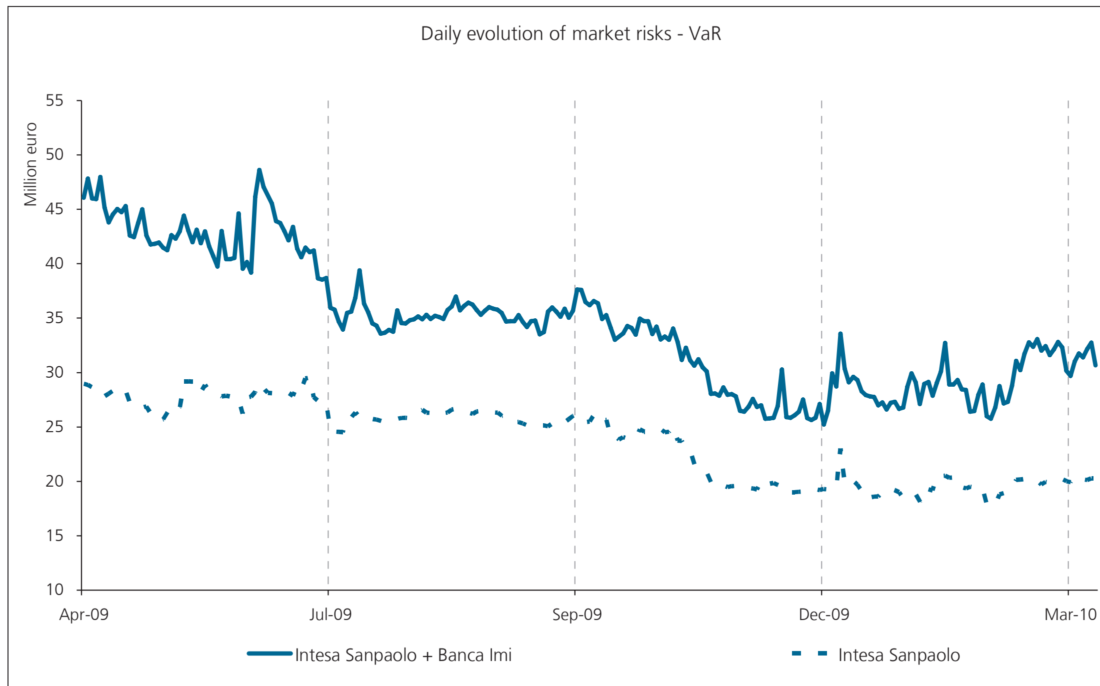
For Intesa Sanpaolo and Banca IMI, the breakdown of risk profile in the first quarter of 2010 with regard to the various factors shows the prevalence of the hedge fund risk, which accounted for 66% of total VaR; for Banca IMI, credit spread risk was the most significant, representing 37% of total VaR.

Contribution of risk factors to overall VaR [(a)]

1st quarter 2010	Shares	Hedge funds	Rates	Credit spreads	Foreign exchange rates	Other parameters
Intesa Sanpaolo	7%	66%	5%	11%	2%	9%
Banca IMI	14%	0%	35%	37%	4%	10%
Total	**10%**	**37%**	**19%**	**22%**	**3%**	**9%**

(a) Each line in the table sets out the contribution of risk factors considering 100% the overall capital at risk, calculated as the average of daily estimates in the first quarter of 2010, broken down between Intesa Sanpaolo and Banca IMI and indicating the distribution of overall capital at risk.

VaR in the last twelve months is set out below. During the first quarter of 2010, the average performance was stable, with peaks primarily associated with turbulence on sovereign risks.



Risk control with regard to the trading activities of Intesa Sanpaolo and Banca IMI also uses scenario analyses and stress tests. The impact on the income statement of selected scenarios relating to the evolution of stock prices, interest rates, credit spreads, foreign exchange rates and commodity prices as at the end of March are summarised in the following table.

In particular:
– on stock market positions, a bullish scenario, that is a 5% increase in stock prices with a simultaneous 10% decrease in volatility would have led to a 1 million euro loss;
– on interest rate exposures, a parallel +25 basis point shift in the yield curve would have led to a 22 million euro loss, whereas a parallel -25 basis point shift would have led to a 24 million euro gain;
– on exposures sensitive to credit spread fluctuations, a 25 basis point widening in spreads would have led to a 94 million euro loss, 5 million euro of which attributable to structured credit products, whereas a 25 basis point contraction of the spreads would have led to a 95 million euro gain, 5 million euro of which attributable to SCP;
– with regard to foreign exchange exposures, the portfolio would have recorded an 11 million euro gain in the event of exchange depreciation (-10%). The positive effect in the case of foreign exchange appreciation (+10%) would amount to 5 million euro;
– lastly, on commodity exposures a 7 million euro loss would have been recorded had there been a 50% increase in prices.

(millions of euro)

	EQUITY		INTEREST RATES		CREDIT SPREADS		FOREIGN EXCHANGE RATES		COMMODITIES	
	volatility +10% and prices -5%	volatility -10% and prices +5%	-25bp	+25bp	-25bp	+25bp	-10%	+10%	-50%	+50%
Total	4	-1	24	-22	95	-94	11	5	7	-7
of which SCP					*5*	*-5*				

BANKING BOOK

Market risk originated by the banking book arises primarily in the Parent Company and in the main Group companies involved in retail and corporate banking. The banking book also includes exposure to market risks deriving from the equity investments in quoted companies not fully consolidated, mostly held by the Parent Company and by Equiter, IMI Investimenti and Private Equity International.
The following methods are used to measure financial risks of the Group's banking book:
- Value at Risk (VaR);
- Sensitivity analysis.

Value at Risk is calculated as the maximum potential loss in the portfolio's market value that could be recorded over a 10-day holding period with a 99% confidence level (parametric VaR).
Shift sensitivity analysis quantifies the change in value of a financial portfolio resulting from adverse movements in the main risk factors (interest rate, foreign exchange, equity). For interest rate risk, an adverse movement is defined as a parallel and uniform shift of ±100 basis points of the interest rate curve. The measurements include an estimate of the prepayment effect and of the risk originated by customer demand loans and deposits.
Furthermore, sensitivity of the interest margin is measured by quantifying the impact on net interest income of a parallel and instantaneous shock in the interest rate curve of ±100 basis points, over a period of 12 months. This measure highlights the effect of variations in interest rates on the portfolio being measured, excluding assumptions on future changes in the mix of assets and liabilities and, therefore, it cannot be considered a predictor of the future levels of the interest margin.

Hedging of interest rate risk is aimed at protecting the banking book from variations in the fair value of loans and deposits due to movements in the interest rate curve, or at reducing the volatility of future cash flows related to a particular asset/liability. The main types of derivative contracts used are interest rate swaps (IRS), overnight index swaps (OIS), cross-currency swaps (CCS) and options on interest rates stipulated with third parties or with other Group companies. The latter, in turn, cover risk in the market so that the hedging transactions meet the criteria to qualify as IAS-compliant for consolidated financial statements.
Hedging activities performed by the Intesa Sanpaolo Group are recorded using various hedge accounting methods. A first method refers to the fair value hedge of assets and liabilities specifically identified (micro-hedging), mainly bonds issued or acquired by the bank and loans to customers. In addition, macro-hedging is carried out on the stable portion of on demand deposits and in order to hedge against fair value changes intrinsic to the instalments under accrual generated by floating rate operations. The Bank is exposed to this risk in the period from the date on which the rate is set and the interest payment date.
Another hedging method used is the cash flow hedge which has the purpose of stabilising interest flow on floating rate funding to the extent that the latter finances fixed-rate investments (macro cash flow hedge). In other cases, cash flow hedges are applied to specific assets or liabilities.
The Risk Management Department is in charge of measuring the effectiveness of interest rate risk hedges for the purpose of hedge accounting.

In the first three months of 2010, interest rate risk generated by the Intesa Sanpaolo Group's banking book, measured through shift sensitivity analysis, registered an average value of 460 million euro settling at 504 million euro at the end of March, almost entirely concentrated on the euro; these figures compare with 560 million euro at the end of 2009.
Sensitivity of the interest margin – in the event of a 100 basis point rise in interest rates – amounted to +149 million euro (-169 million euro in the event of reduction) at the end of March 2010; these values record a slight increase compared to the 2009 year-end figures of +119 million euro and -120 million euro, respectively, in the event of an increase/decrease in interest rates.
Interest rate risk, measured in terms of VaR, averaged 89 million euro in the first quarter of 2010 (131 million euro at the end of 2009) and reached 101 million euro at the end of March, which also was the peak value for the period (the minimum value was 82 million euro).
Price risk generated by minority stakes in listed companies, mostly held in the AFS (Available for Sale) category and measured in terms of VaR, recorded an average level of 105 million euro (126 million euro at the end of 2009) in the first three months of 2010, with minimum and peak values of 94 million euro and 115 million euro respectively. VaR at the end of March amounted to 94 million euro.
Lastly, an analysis of banking book sensitivity to price risk, measuring the impact on Shareholders' Equity of a price shock on the above quoted assets recorded in the AFS category shows sensitivity to a 10% negative shock equal to -82 million euro at the end of March 2010.

INFORMATION ON FINANCIAL PRODUCTS

The following information on credit and market risk exposure, in various forms, directly or through vehicles, is provided in line with the requests for utmost transparency made by international and national Supervisory authorities.

DETERMINATION OF THE FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

General Principles

IFRS state that financial products in the trading portfolio must be measured at fair value through profit and loss. The existence of official prices in an active market represents the best evidence of fair value, and these prices must be used with priority (effective market quotes – level 1) for the registration of financial assets and liabilities in the trading book.
If there is no active market, fair value is determined using valuation techniques aimed at ultimately establishing what the transaction price would have been on the measurement date, in an arm-length exchange, motivated by normal business considerations. Such techniques include:

– reference to market values indirectly connected to the instrument to be valued and presumed from products with the same risk profile (comparable approach – level 2);
– valuations performed using – even partially – inputs not identified from parameters observed on the market, which are estimated also by way of assumptions made by the person making the assessment (Mark-to-Model – level 3).

The choice between the aforesaid methodologies is not optional, since they must be applied according to a hierarchy: if a published price quotation in an active market is available then the other valuation approaches may not be used.
For a more detailed description of the fair value measurement methods used, please refer to the Accounting policies section of the 2009 financial statements.

The following table shows the fair value hierarchy in relation to the measurement of the various categories of financial instruments.

(millions of euro)

Financial assets / liabilities designated at fair value	31.03.2010			31.12.2009		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
1. Financial assets held for trading	33,110	47,733	2,088	24,777	43,668	1,380
2. Financial assets designated at fair value through profit or loss	21,753	1,415	194	20,345	1,408	212
3. Financial assets available for sale	32,884	4,351	2,059	30,359	3,841	1,695
4. Hedging derivatives	-	8,236	-	-	7,008	-
Total	**87,747**	**61,735**	**4,341**	**75,481**	**55,925**	**3,287**
1. Financial liabilities held for trading	4,616	43,239	480	2,878	38,898	473
2. Financial liabilities designated at fair value through profit or loss	460	24,749	-	464	25,423	-
3. Hedging derivatives	-	5,996	-	-	5,179	-
Total	**5,076**	**73,984**	**480**	**3,342**	**69,500**	**473**

STRUCTURED CREDIT PRODUCTS

The business model: objectives, strategies and relevance

Continuing the strategies adopted in previous years, the management of this portfolio is aimed at reducing the existing positions to the extent permitted by the activity in this market.
Spreads contracted further in the first quarter, resulting in a positive impact of approximately 22 million euro on the income statement.
However, there remain grounds for concern relating to the weak economic scenario and the tensions registered on international markets after the end of the quarter, especially surrounding the deterioration of sovereign risk and the contagion effect that it may have on financial institutions.

Highlights

Before illustrating the results as at 31 March 2010, it should be specified that activity aimed at reducing the portfolio of structured credit products continued in the first quarter through the closing of two transactions. The effects in terms of risk exposure were partly offset by the impact of changes in the exchange rate. The positions still outstanding as at 31 March 2010, which have been downgraded by 6.3% (down from 27% as at 31 December 2009), remain of good quality, as shown by the following indicators:

- 71% of the exposure was Investment Grade, compared to 73% as at 31 December 2009;
- 37% of the exposure had a Super senior (3%) or AAA (34%) rating. The percentage of Super senior fell slightly compared to 31 December 2009;
- 30% had a BBB rating or less, compared to 27% as at 31 December 2009;
- 26% of the exposure had a pre-2005 vintage[1];
- 37% had a 2005 vintage;
- only 9% of the exposure related to the US Residential segment, and 22% to the US non-residential segment;
- the remaining exposure (69% of the total) was mostly European (61%).

In terms of underlying contract types, just over half the exposure consisted of CLOs (33%) and CDOs (23%); the rest was almost entirely made up of ABSs (18%) and RMBSs (21%), with CMBSs representing 5% of the total.
With regard to valuation methods, unfunded positions were measured using the Mark-to-Model Approach (Level 3 of the Fair Value hierarchy) with the sole exception of positions on CMBX and LCDX indices, which were measured on the basis of the Comparable Approach (Level 2 of the Fair Value hierarchy). As for funded products, around 9% of the exposure was measured on the basis of Effective Market Quotes (Level 1), however, in 91% of cases, valuation methods were adopted. Specifically, 50% of the exposures were measured through the Comparable Approach (Level 2) and the remaining 41% through the Mark-to-Model Approach (Level 3).
The structured credit products are indicated by separating the part classified under financial assets held for trading and available for sale from those classified as Loans[2]. The tables illustrate the impact on the income statement of both aggregates.
The information set out below refers to the entire Group. Any effects and positions ascribable to entities other than the Parent Company are specifically highlighted in the comments and/or in the detailed tables.
In the summary tables provided below, table (a) sets out risk exposure as at 31 March 2010 and income statement captions (sum of realised charges and profits, write-downs and write-backs) in the first quarter of 2010, compared with the corresponding values recorded as at 31 December 2009.
Table (b) sets out figures related to structured packages, normally made up of an asset (security) whose credit risk is entirely hedged by a specific credit default swap. Risk exposure in the table refers to the protection seller and not to the issuer of the asset hedged.
The conversion into euro of values expressed in USD as at 31 March 2010 occurred at an exchange rate of 1.3479 euro per dollar and as at 31 December 2009 at an exchange rate of 1.4406 euro per dollar.

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[1] Date of generation of the collateral underlying the securitisation. It is an important factor in the assessment of the risk of the mortgages underlying securitisations since, especially in the US, the phenomenon of mortgages granted to entities with inadequate income and with low prior assessment of documentation became significant as of 2005.

[2] This segregation is the result of the reclassification completed in 2008 after the IAS 39 amendments in October 2008. Added to these are the reclassifications of securities completed after the restructuring of unfunded positions during 2009.

Structured credit products: summary tables

a) Exposure in funded and unfunded ABS/CDOs

(millions of euro)

Financial assets held for trading	**31.03.2010**		**31.12.2009**	
	Risk exposure (*) (including write-downs and write-backs)	**Income Statement** Profits (Losses) on trading	**Risk exposure** (*) (including write-downs and write-backs)	**Income Statement** Profits (Losses) on trading
US subprime exposure	**30**	**-**	**28**	**19**
Contagion area	**168**	**1**	**164**	**-68**
- Multisector CDOs	82	-3	88	-71
- Alt-A	-	-	-	-
- TruPS	86	4	76	3
- Prime CMOs	-	-	-	-
Other structured credit products	**1,287**	**16**	**1,235**	**-27**
- European/US ABS/CDOs	475	4	479	36
- Unfunded super senior CDOs	803	10	834	-51
- Other unfunded positions	9	2	-78	-12
Total	**1,485**	**17**	**1,427**	**-76**
in addition to:				
Positions of funds	-	5	-	15
Total Financial assets held for trading	**1,485**	**22**	**1,427**	**-61**

Loans	**31.03.2010**		**31.12.2009**	
	Risk exposure (**) (including write-downs and write-backs)	**Income Statement**	**Risk exposure** (**) (including write-downs and write-backs)	**Income Statement**
US subprime exposure	**7**	**-**	**7**	**-1**
Contagion area	**107**	**-**	**107**	**-**
- Multisector CDOs	15	-	15	-
- Alt-A	60	-	59	-
- TruPS	-	-	-	-
- Prime CMOs	32	-	33	-
Other structured credit products	**2,310**	**-5**	**2,321**	**4**
- Funded European/US ABS/CDOs	1,367	-5	1,476	-11
- Funded super senior CDOs	812	-	714	15
- Other Romulus funded securities	131	-	131	-
Total	**2,424**	**-5**	**2,435**	**3**
in addition to:				
Positions of funds	-	-	-	-
Total Loans	**2,424**	**-5**	**2,435**	**3**
TOTAL	**3,909**	**17**	**3,862**	**-58**

(*) The column "Risk exposure" sets out: for securities, fair value; for derivatives, the nominal value of the contract, net of write-downs and write-backs recorded at reference date. Such amounts correspond, for "long" positions, to the maximum potential loss (in the event of a 100% default and a recovery rate of 0). For "short" positions, vice versa, they indicate the maximum potential gain (in the same scenario in terms of default and recovery levels).

(**) For assets reclassified to loans, exposure to risk is provided by the carrying amount of the security, equal to fair value at the reclassification date, plus accrued interest calculated at the effective interest rate net of net value adjustments to the portfolio.

b) Exposure in packages

(millions of euro)

Detailed table	**31.03.2010**		**31.12.2009**	
	Credit exposure to monoline insurers (CDS fair value post write-down for CRA)	**Income Statement** Profits (Losses) on trading	**Credit exposure to monoline insurers (CDS fair value post write-down for CRA)**	**Income Statement** Profits (Losses) on trading
Monoline risk	14	5	10	31
Non monoline packages	94	-	98	4
TOTAL	**108**	**5**	**108**	**35**

The overall risk exposure of structured credit products rose from 3,862 million euro as at 31 December 2009 to 3,909 million euro as at 31 March 2010, in addition to an exposure of 108 million euro in connection with structured packages.
With reference to the income statement perspective, structured credit products improved, reaching +22 million euro as at 31 March 2010 compared to a loss of -23 million euro as at 31 December 2009.
The exposure in funded and unfunded ABSs/CDOs had an effect on "Profits (Losses) on trading – Caption 80" of +22 million euro. The profit on this segment was essentially a result of the positive effects of:

– the unfunded positions included in the area "Other structured credit products" (+12 million euro as at 31 March 2010, of which +10 million euro in unfunded super senior CDOs and +2 million in Other unfunded positions);
– funded and unfunded positions associated with the "Contagion Area" (+1 million euro); this result is further improved if the positions in funds attributable to the segment are also considered (+5 million euro);
– European and U.S. funded ABSs/CDOs (+4 million), also included in the area "Other structured credit products", the effect of which on the income statement is entirely attributable to the subsidiary Banca IMI.

The securities reclassified to the loan portfolio and included among European ABSs/CDOs showed impairment losses as at 31 March 2010 that resulted in adjustments of 5 million euro, recognised under caption 130 "Net impairment losses on loans".
The contribution of the "Monoline risk" and "Non-monoline packages" was also positive with a total result of 5 million euro as at 31 March 2010, thanks to the constant improvement in the creditworthiness of counterparties.
It should be noted that the "Structured credit products" aggregate was identified in 2007, immediately following the outbreak of the "subprime phenomenon" and, in disclosure to the market, has been kept essentially constant (the reduction corresponds to the effective disposal of assets and not to changes in the area in question).
As at 31 March 2010, the aggregate included bonds classified as loans for a total nominal value of 2,489 million euro and a risk exposure of 2,289 million euro[3]. This amount included 165 million euro for securities reclassified from available for sale to the loans portfolio. As at 31 March 2010 their fair value was 94 million euro. The positive impact of this reclassification on the Valuation reserve under Shareholders' Equity was 71 million euro. The remaining 2,124 million was reclassified from the trading book to the loans portfolio. The fair value of this aggregate was 1,956 million euro as at 31 March 2010, with a positive effect on the income statement of a total of 262 million euro, of which 299 million euro in benefits attributable to 2008, 7 million euro in benefits attributable to 2009 and a lesser benefit of 44 million euro attributable to the first quarter of 2010. Had the loans portfolio not been reclassified, the result for structured credit products would have been a positive 66 million euro in the first quarter of 2010.

[3] In addition, there is 135 million euro in securities classified to the loan portfolio since initial recognition and included in the portfolios of the Parent Company and its subsidiaries Banca Fideuram and Eurizon Vita.

INFORMATION ON ACTIVITIES PERFORMED THROUGH SPECIAL PURPOSE ENTITIES (SPEs)

For the purpose of this analysis, legal entities agreed to pursue a specific, clearly defined and limited objective are considered Special Purpose Entities (raising funds on the market, acquiring/selling/managing assets, developing and/or financing specific business initiatives, undertaking leveraged buy-out transactions or managing credit risk inherent in an entity's portfolio).
The sponsor of the transaction is normally an entity which requests the structuring of a transaction that involves the SPE for the purpose of achieving certain objectives. In some cases the Bank is the sponsor and establishes a SPE to achieve one of the objectives cited above. There have been no changes in the scope of consolidation beyond those reported in the 2009 financial statements.

Funding SPEs

These are entities incorporated abroad to raise funds on specific markets. The SPEs issue financial instruments, normally guaranteed by Intesa Sanpaolo, and transfer the funds raised to the Parent company.
Changes compared to the situation reported as at 31 December 2009 include the extinction of the notes issued by Sanpaolo IMI US Financial Co. in February 2010. There were no changes to report in the other names included in the aggregate.

SPEs for insurance products

These are entities (UCITS) established for the purpose of investing internal funds of unit-linked and index-linked products of Eurizon Vita and Eurizon Life who retain the majority of the risks and rewards; SPEs for insurance products are consolidated according to IAS 27 / SIC 12.
There were no changes in this segment compared to the situation reported as at 31 December 2009.

Securitisation SPEs

These are funding SPEs that enable an entity to raise funds through the securitisation of part of its assets. In particular, this involves the spin-off of a package of balance sheet assets (generally loans) and its subsequent transfer to a vehicle which, to finance the purchase, issues securities later placed on the market or through a private placement. The resources raised in this way are returned to the seller, whereas the commitments to the subscribers are met using the cash funds generated by the loans sold.
The scope of the SPEs included in this category has not changed compared to the situation reported as at 31 December 2009. The only matter worthy of note is the sale of approximately 2 billion euro in loans to the public sector to the vehicle ISP CB Pubblico on 30 March 2010, effective 1 April 2010.
Intesa Sanpaolo controls, pursuant to SIC 12, the vehicles Romulus Funding Corporation and Duomo Funding Plc. The figures and information for these two vehicles did not undergo significant changes in the first quarter of 2010. An analysis of the distribution of the two vehicles' assets by geographical area shows an increase in the percentage of assets claimed from Italian entities and a decrease in those claimed from North American entities. An analysis of their distribution by rating indicates that there has been a significant rise in the percentage of assets rated Aaa (from 2% in December 2009 to 13% in March 2010), along with a concurrent increase in the percentage of unrated assets (from approximately 46% in December 2009 to 58% in March 2010).
In addition, there were no significant changes in the data and information for the vehicle SPQR II S.r.l. as compared to the situation reported at the end of 2009.

Financial Engineering SPEs

These SPEs carry out investment and funding transactions that achieve better risk/return combinations than those generated by standard transactions, through special structures aimed at optimising accounting, tax and/or regulatory aspects. These structures have been set up to respond to the needs of primary customers and provide solutions that offer financing at competitive interest rates and investments with higher returns.
The only vehicle of this kind controlled by Intesa Sanpaolo, Intesa Investimenti S.p.A., is in a situation entirely similar to that described as at 31 December 2009.

Other unconsolidated Special Purpose Entities

With regard to the other unconsolidated SPEs (Project Financing, Asset Backed, Leveraged & Acquisition Finance and Credit Derivatives) reference should be made to the Financial statements as at 31 December 2009.

LEVERAGED FINANCE TRANSACTIONS

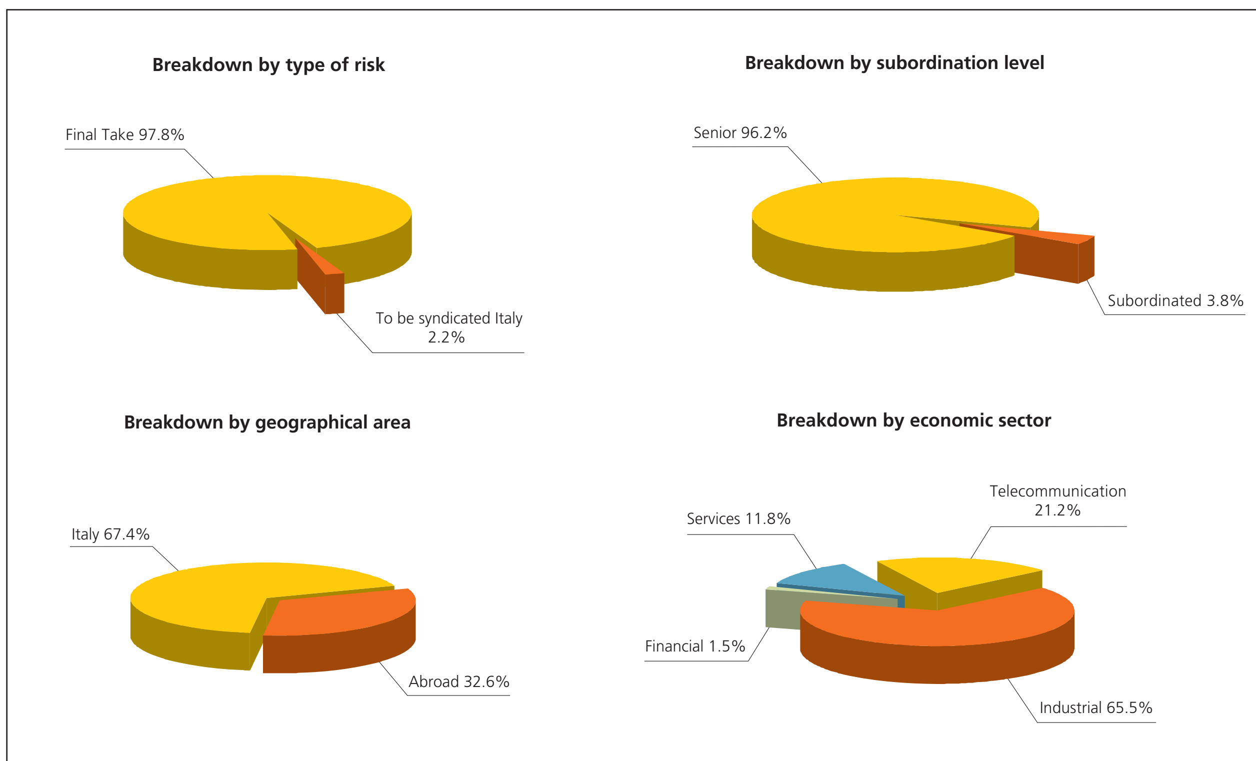
Since there is no univocal and universally agreed-upon definition of leveraged finance transactions, Intesa Sanpaolo decided to include in this category the exposures (loans granted and disbursed in relation to structured financing, normally medium/long term) to legal entities in which the majority of share capital is held by private equity funds.

These are mainly positions in support of Leveraged Buy Out projects (therefore with high financial leverage), i.e. linked to the full or part acquisition of companies through recourse to SPEs created for this purpose. After acquisition of the target company's securities package, these SPEs are normally merged into the target. The target companies generally have good economic prospects, stable cash flows in the medium term and low original leverage levels. Intesa Sanpaolo has financed entities of this type, as normal borrowers, without acting as sponsor.

None of these SPEs is consolidated, since the guarantees to support the transaction are solely instrumental for the granting of the financing and are never directed to the acquisition of direct or indirect control over the vehicle.

As at 31 March 2010, slightly fewer than 110 transactions, for a total amount granted of 4,529 million euro, met the above definition.

These exposures are classified under the loan portfolio. They also include the portions of syndicated loans underwritten or under syndication. In line with disclosure requirements, breakdown of exposures by geographical area, economic sector and by level of subordination is set out below.



DISCLOSURE ON INVESTMENTS IN HEDGE FUNDS

The hedge funds portfolio as at 31 March 2010 totalled 780 million euro, compared to the 740 million euro recorded at year-end 2009. Changes to the portfolio in the first quarter of the current year included both the management of outstanding units and new acquisitions.

As at the same date, the contribution to "Profits (Losses) on trading – Caption 80" of these investments was further confirmed to be positive, coming to 33 million euro (including 5 million euro in the structured credit products disclosure) compared to the 19 million euro recognised in the first quarter of 2009 and the 135 million euro at the end of the previous year. Of these net profits:

– 1 million euro is represented by net profits realised during the year from fund trading;
– 29 million euro related to net valuations of positions remaining at the year-end (including 5 million euro in the structured credit products disclosure);
– 3 million euro from other net income.

Taking into account the net capital gains on the final residual amount (29 million euro), these were spread across 48 positions, 5 of which recording capital losses (-2 million euro) and 43 capital gains (+31 million euro).

INFORMATION ON TRADING TRANSACTIONS IN DERIVATIVES WITH CUSTOMERS

Considering only relations with customers, as at 31 March 2010, the Intesa Sanpaolo Group presented, in relation to derivatives trading with retail customers, non-financial companies and public entities (therefore excluding banks, financial and insurance companies), a positive fair value, including netting agreements, of 3,146 million euro (3,008 million euro as at 31 December 2009). The notional value of these derivatives totalled 46,320 million euro (47,107 million euro as at 31 December 2009). Please note that the positive fair value of structured contracts outstanding with the 10 customers with the highest exposures was 1,003 million euro (1,117 million euro as at 31 December 2009).

Conversely, negative fair value determined with the same criteria, for the same types of contracts and with the same counterparties, totalled 420 million euro at 31 March 2010 (327 million at 31 December 2009). The notional value of these derivatives totalled 9,429 million euro (8,321 million euro as at 31 December 2009).

The fair value of derivative financial instruments stipulated with customers was determined considering, as for all other OTC derivatives, the creditworthiness of the single counterparty ("Credit Risk Adjustment"). On contracts outstanding as at 31 March 2010, this resulted in the recognition in the income statement, under profits from trading, of a net adjustment of 10 million euro, in addition to the 104 million euro recognised in previous years, bringing the total adjustment to 114 million euro.

Adjustments are recorded, for every single contract, on the market value determined using the risk free curves.

OPERATIONAL RISK

Operational risk is defined as the risk of suffering losses due to inadequacy or failures of processes, human resources and internal systems, or as a result of external events. Operational risk includes legal risk, that is, the risk of losses deriving from breach of laws or regulations, contractual, out-of-contract responsibilities or other disputes; strategic and reputation risks are not included.
The Intesa Sanpaolo Group has long defined the overall operational risk management framework by setting up a Group policy and organisational process for measuring, managing and controlling operational risk.
Effective from the disclosure at 31 December 2009, the Group was authorised by the Supervisory Authority to use the Advanced Measurement Approach (AMA) to determine capital requirements for operational risk on an initial scope that includes the Banks and Companies of the Banca dei Territori Division (with the exception of Banca CR Firenze but including Cassa del Centro banks), Leasint, Eurizon Capital and VUB Banka. The remaining companies, which currently employ the Standardised approach, will gradually migrate to the Advanced approach beginning in 2010.
The control of operational risk was attributed to the Management Board, which identifies risk management policies, and to the Supervisory Board, which is in charge of their approval and verification, as well as of the guarantee of the functionality, efficiency and effectiveness of the risk management and control system.
The tasks with which the Group Compliance and Operational Risk Committee is charged include periodically reviewing the Group's overall operational risk profile, authorising any corrective measures, coordinating and monitoring the efficacy of the main mitigation activities and approving operational risk transfer strategies.
The Group has a centralised function within the Risk Management Department for the management of the Group's operational risk. This function is responsible for the definition, implementation, and monitoring of the methodological and organisational framework, as well as for the measurement of the risk profile, the verification of mitigation effectiveness and reporting to Top Management.
In compliance with current requirements, the individual Organisational Units are responsible for identifying, assessing, managing and mitigating risks. Specific officers and departments have been identified within these business units to be responsible for Operational Risk Management (collection and structured census of information relative to operational events, scenario analyses and evaluation of the business environment and internal control factors).
The Integrated Self-Assessment Process, which has been conducted on an annual basis, has allowed the Group to:

- identify, measure, monitor and mitigate operational risk; and
- create significant synergies with the specialised functions of the Organisation and Security Department that supervise the planning of operational processes and business continuity issues and with control functions (Compliance and Auditing) that supervise specific regulations and issues (Legislative Decree 231/05, Law 262/05) or conduct tests of the effectiveness of controls of company processes.

The Self-Assessment Process identified a good overall level of control of operational risks and contributed to enhancing the dissemination of a business culture focused on the ongoing control of these risks.
The internal model for calculating capital absorption is conceived in such a way as to combine all the main sources of quantitative and qualitative information (self-assessment).
The quantitative component is based on an analysis of historical data concerning internal events (recorded by organisational units, appropriately verified by the central function and managed by a dedicated IT system) and external events (the Operational Riskdata eXchange Association).
The qualitative component (scenario analyses) focuses on the forward-looking assessment of the risk exposure of each unit and is based on the structured, organised collection of subjective estimates expressed directly by management (subsidiaries, Parent company's business areas, the Corporate Centre) with the objective of assessing the potential economic impact of particularly serious operational events. Capital-at-risk is therefore identified as the minimum amount at Group level required to bear the maximum potential loss (worst loss); Capital-at-risk is estimated using a Loss Distribution Approach model (actuarial statistical model to calculate the Value-at-risk of operational losses), applied on quantitative data and the results of the scenario analysis assuming a one-year estimation period, with a confidence level of 99.90%; the methodology also applies a corrective factor, which derives from the qualitative analyses of the risk of the evaluation of the business environment and internal control factors, to take account of the effectiveness of internal controls in the various organisational units.
Monitoring of operational risks is performed by an integrated reporting system, which provides management with the information necessary for the management and/or mitigation of the operational risk.
In order to support the operational risk management process on a continuous basis, a structured training programme was fully implemented for employees actively involved in the process of managing and mitigating operational risk.
To determine its capital requirements, the Group employs a combination of the methods allowed under applicable regulations. The capital absorption resulting from this process amounts to approximately 2,249 million euro.

Legal risks

There were no significant changes in legal risks as at 31 March 2010 compared to the 2009 financial statements, to which reference should be made for a description of the main ongoing disputes.

INSURANCE RISKS

Life business

The typical risks of a life insurance portfolio can be divided into three main categories: premium risk, life underwriting risk and reserve risk.
Premium risks are managed initially during definition of the technical features and product pricing, and over the life of the instrument by means of periodic checks on sustainability and profitability (both at product level and at portfolio level, including liabilities).
Actuarial and demographic risks are guarded against by a regular statistical analysis of the evolution of liabilities, divided by type of risks and through simulations of expected profitability on the assets which cover technical reserves.
Reserve risk is managed through the exact calculation of mathematical reserves, with a series of detailed checks as well as overall verifications, by comparing results with the estimates produced on a monthly basis.
The mathematical reserves are calculated on almost the entire portfolio, on a contract-by-contract basis, and the methodology used to determine the reserves takes account of all the future commitments of the company.

Non-life business

The risks of the non-life insurance portfolio are essentially premium risk and reserve risk.
Premium risks are managed initially during definition of the technical features and product pricing, and over the life of the instrument by means of periodic checks on sustainability and profitability (both at product level and at portfolio level, including liabilities).
Reserve risk is guarded against through the exact calculation of technical reserves.

Asset and Liability Management (ALM) and financial risks

In line with the growing focus in the insurance sector on the issues of value, risk and capital in recent years, a series of initiatives has been launched with the objective of both strengthening risk governance and managing and controlling risk-based capital.
With reference to investment portfolios, set up both as coverage of obligations with the insured and in relation to free capital, the Investment Policy is the control and monitoring instrument for market and credit risks.
The Policy defines the goals and the operating limits that are needed to distinguish the investments in terms of eligible assets and asset allocation, breakdown by rating classes and credit risk, concentration risk by issuer and sector, market risks, in turn measured in terms of sensitivity to variations in risk factors and Value at Risk on a 1-year holding period.
In order to measure and manage all risks (underwriting and financial), a simulation tool - the Financial Analysis Program (FAP)-, is also used with the aim of measuring the intrinsic value, fair value of the liabilities and economic capital. The FAP is based on a dynamic ALM model and, through this engine, it fully recognises the sensitivity of liabilities to changes in market risk factors and permits an effective management of hedging assets.

Investment portfolios

The investments of the Intesa Sanpaolo Group companies operating in the insurance segment (EurizonVita, EurizonTutela, EurizonLife, SudPoloVita and CentroVita) are made with their free capital and to cover contractual obligations with customers. These essentially refer to traditional revaluable life insurance policies, Index- and Unit-linked policies, pension funds and non-life policies.
At 31 March 2010 the investment portfolios of Group companies, recorded at book value, amounted to 50,736 million euro; of these, the share regarding traditional revaluable life policies, non-life policies and free capital (Class C portfolio or portfolio at risk) amounted to 21,962 million euro, while the other component (Class D portfolio or portfolio with total risk retained by the insured) mostly comprised investments related to pension funds, index- and unit-linked policies and totalled 28,774 million euro.
Considering the various types of risks, the analysis of investment portfolios, described below, concentrates on the assets included in the "at-risk portfolio".
In terms of breakdown by asset class, net of derivative positions, 93.3% of assets, i.e. approximately 20,648 million euro, were bonds, while assets subject to equity risk represented 3.5% of the total and amounted to 771 million euro. The remaining part (717 million euro) consisted of investments relating to UCI, Private Equity and Hedge Funds (3.2%).
The fair value of derivatives came to approximately -150 million euro, around -136 million of which in hedging derivatives and close to -14 million in other derivatives.
At the end of the first quarter of 2010, investments of EurizonVita, SudPoloVita and CentroVita free capital amounted to approximately 1,458 million euro at market value, and presented a risk in terms of VaR (99% confidence level, 10-day holding period) equal to approximately 47 million euro.
The Modified duration of the bond portfolio, calculated by means of the sensitivity to uniform and parallel variations of the interest rate curve of ±25 basis points, is 5.9 years. The reserves associated to profit contracts have an average modified duration of approximately 4.8 years. The related portfolios of assets have a modified duration of around 5.1 years.
The breakdown of the bond portfolio in terms of fair value sensitivity to interest rate changes showed that a +100 bp parallel shift in the curve leads to a decrease of approximately 1,133 million euro. On the basis of this hypothetical scenario, the value of hedging derivatives in the portfolio undergoes an approximate 126 million euro rise which partly offsets the corresponding loss on the bonds.
The investment portfolio had a high credit rating. AAA/AA bonds represented approximately 78.6% of total investments and A bonds approximately 9.1%. Low investment grade securities (BBB) were approximately 4.8% of the total and the portion of speculative grade or unrated was minimal (approximately 0.8%).

Analysis of the exposure in terms of the issuers/counterparties showed that: securities issued by Governments and Central banks represented approximately 72.8% of the total investments, while financial companies (mostly banks) contributed almost 13.5% of exposure and industrial securities made up approximately 7%.
At the end of the first quarter of 2010, the fair value sensitivity of bonds to a change in issuer credit rating, intended as a market credit spread shock of +100 basis points, was -1,215 million euro, -1,027 million euro due to government issuers and -188 million euro to corporate issuers (financial institutions and industrial companies).