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. Group companies that generate credit and/or financial risks are assigned autonomy limits and each has its own control structure. For the main Group subsidiaries these functions are performed, on the basis of an outsourcing contract, by the Parent Company's risk control functions, which periodically report to the Board of Directors and the Audit Committee of the subsidiary.
The risk measurement and management tools together define a risk-monitoring framework at Group level, capable of assessing risks assumed 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.
Risk hedging, given the nature, frequency and potential impact of the risk, is based on a constant balance between mitigation/hedging action, control procedures/processes and capital protection measures.

BASEL 2 REGULATIONS AND THE INTERNAL PROJECT

In June 2004, the Basel Committee on Banking Supervision published the final version of the Capital Accord ("Basel 2"), endorsed by the European Union at the end of 2005 through the Capital Adequacy Directive and in Italy by Law Decree 297 of 27 December 2006.
In 2007, Intesa Sanpaolo launched the "Basel 2 Project" to prepare the Group for the adoption of advanced approaches, building on the pre-merger experience of Intesa and Sanpaolo IMI. In 2008, it began the approval process for their adoption.
With regard to credit risks, a "first scope" of Group entities that use approaches based on internal models was identified. For these entities, the Group obtained authorisation to use the IRB Foundation approach for the Corporate segment, starting from the report as at 31 December 2008. The rating models and credit processes for the SME Retail and Retail (Residential mortgages) segments were also implemented in 2008. With the release of the Loss Given Default (LGD) model, now being completed, by the end of the first half of 2010 it will be possible to adopt the Advanced IRB approach for the SME Retail and Retail (Residential mortgages) segments.
Rating model development for other segments and extension of the business application scope is in progress, in line with a gradual programme for the adoption of advanced approaches submitted to the Supervisory Authority.
With regard to operational risks, implementation of the AMA approach for some Group Companies (which include Banks and Companies of the Banca dei Territori Division, Leasint, Eurizon Capital and VUB Banka) was completed. Moreover, authorisation to use the internal Advanced Measurement Approach (AMA) in the calculation of the capital requirements has been requested to the Bank of Italy.
With respect to the Internal capital adequacy assessment process (i.e., ICAAP of Pillar 2 of the Basel 2 Accord), the Group presented the interim and final reports for 2008, 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. The reports show satisfactory capital adequacy under both ordinary and stress conditions.
As part of the adoption of "Basel 2" by the Italian banking system, Bank of Italy Circular 263 of 27 December 2006 "New regulations for the prudential supervision of banks" sets out the procedures that must be adopted by Italian banks and banking groups in public disclosures on capital adequacy, risk exposure and the general features of the risk identification, measurement and management systems

(Basel 2 - Pillar 3).
In brief, the new instructions envisage the drawing up of a separate report on banking group risk in addition to that already included in the financial statements. This disclosure, drawn up in accordance with the provisions of the aforementioned circular, which incorporates the provisions of Annex XII to EU Directive 2006/48, is published in accordance with the rules laid down by the Bank of Italy with the following frequency:
– figures as at 31 December: full qualitative and quantitative disclosure;
– figures as at 30 June: update of the quantitative disclosure (as Intesa Sanpaolo is among the groups that have adopted IRB and/or AMA approaches for credit and operational risk);
– figures as at 31 March/30 September: update of the information relating to capital and capital adequacy (as Intesa Sanpaolo is among the groups that have adopted IRB and/or AMA approaches for credit and operational risk).
The Intesa Sanpaolo Group publishes the Basel 2 Pillar 3 disclosure and subsequent updates on its website at the address: group.intesasanpaolo.com.

CREDIT RISK

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.
In particular, with respect to loans to customers, risk is measured using rating models which change according to the segment to which the counterparty belongs.
The policies applied by the Group in financing the economy are aimed at:
– coordination of actions to achieve a sustainable objective, consistent with the Group's risk appetite and value creation;
– portfolio diversification, limiting the concentration of exposures on single counterparties/groups, single sectors or geographical areas;
– efficient selection of the single borrowers via an attentive creditworthiness analysis aimed at containing default risk, notwithstanding the objective of privileging commercial lending or loans to support new production capacity with respect to merely financial interventions.
The management of credit risk profiles of the loan portfolio is assured, starting from the analysis and granting phases, by:
– checking the existence of the necessary conditions for creditworthiness, with particular focus on the customer's current and prospective capacity to produce satisfactory income and congruous cash flows, considering the course of the relationship already in progress;
– applying the regulations on Credit policies;
– assessing the nature and size of proposed loans, considering the actual requirements of the counterparty requesting the loan, the course of the relationship already in progress, the presence of any relationship between the client and other borrowers and the Credit Policies defined;
– controlling the relationships, by means of information technology procedures and systematic surveillance of the relationships which present irregularities, both aimed at rapidly identifying any signs of deterioration in risk exposures.

Constant monitoring of the quality of the loan portfolio is also ensured by specific operating checks for all the phases of loan management: these actions are aimed at monitoring the transition of exposures from performing to non-performing status and vice-versa, including through the deterioration of the rating, following the calculation/confirmation of the group administrative position.

Credit quality

The overall non-performing loan portfolio is continually monitored through a predetermined control system and periodic managerial reporting. In particular, such activities are performed using measurement methods and performance controls that allow the production of synthetic risk indicators. They allow timely assessments 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. Last, non-performing loans include loans past due by over 90 or 180 days which exceeded the warning threshold, as set out by the Bank of Italy.

(in millions of euro)

	30.09.2009			31.12.2008			Changes
	Gross exposure	Total adjustments	Net exposure	Gross exposure	Total adjustments	Net exposure	Net exposure
Doubtful loans	15,336	-10,477	4,859	13,047	-9,079	3,968	891
Substandard loans	11,531	-2,514	9,017	7,011	-1,720	5,291	3,726
Restructured loans	2,083	-89	1,994	534	-135	399	1,595
Past due loans	2,272	-174	2,098	2,022	-156	1,866	232
Non-performing loans	**31,222**	**-13,254**	**17,968**	**22,614**	**-11,090**	**11,524**	**6,444**
Performing loans	344,093	-2,472	341,621	370,611	-2,442	368,169	-26,548
Performing loans represented by securities	18,876	-569	18,307	15,863	-367	15,496	2,811
Loans to customers	**394,191**	**-16,295**	**377,896**	**409,088**	**-13,899**	**395,189**	**-17,293**

Figures restated on a consistent basis, considering the changes in the scope of consolidation.

As at 30 September 2009, the Group recorded an increase in non-performing loans both in gross terms (+38.1%) and net of adjustments (+55.9%). This trend led to a higher incidence of net non-performing loans on total net loans to customers, increasing from 2.9% to 4.8%. As at 30 September 2009, the coverage of non-performing loans, pursued through prudent provisioning policies extended to all commercial banks, totalled approximately 42%, compared to the 49% recorded at the end of 2008. The decrease is mainly due to the inclusion of a position of a significant amount under restructured loans, deemed fully recoverable following the restructuring transaction.

In more detail, doubtful loans net of adjustments totalled 4,859 million euro, with an 891 million euro rise from the beginning of the year (+22.5%); the incidence on total loans was 1.3%, with a coverage ratio of 68.3%.

Substandard loans, 9,017 million euro net of adjustments, recorded a 70% rise with respect to 31 December 2008. This is due to new positions of a significant amount, assisted by guarantees, which required limited provisions; the incidence on total loans was 2.4%, with a coverage ratio of approximately 22%.

Restructured loans, 1,994 million euro net of adjustments, showed an increase over the 399 million euro as at 31 December 2008, mainly due to the above-mentioned restructuring transaction. The related coverage ratio is 4.3%.

Past due loans amounted to 2,098 million euro net of adjustments with a 232 million euro increase (+12.4%) and an approximate 7.7% coverage ratio.

Cumulated collective adjustments on performing loans came to 0.7% of gross exposure relating to loans to customers, stable with respect to the figure at the end of the previous year. 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

The activities for the quantification of trading risks are 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 indexes;
- investment funds;
- foreign exchange rates;
- implied volatilities;
- spreads in credit default swaps (CDSs);
- spreads in issued bonds;
- correlation instruments;
- dividend derivatives;
- asset-backed securities (ABSs);
- commodities.

Other Group subsidiaries hold smaller trading books with a marginal risk (around 6% 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 abovementioned risk factors, the Supervisory authority validated the internal models for the regulatory measurement of capital absorption of both Intesa Sanpaolo (internal model extended during 2007 to the books of the former Sanpaolo IMI Finance Department) and Banca IMI (the internal model, previously validated for the former Banca Caboto component, was extended, in the first quarter of 2008, to the former Banca IMI portfolios).
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.
The analysis of market risk profiles relative to the trading book uses various quantitative indicators, VaR being the most important one. 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 simulation of illiquid parameters.

In the third quarter of 2009, market risks generated by Intesa Sanpaolo and Banca IMI decreased with respect to the averages for the second quarter of 2009. The average VaR for the period totalled 36.4 million euro.

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

(in millions of euro)

	2009					2008			
	average 3rd quarter	minimum 3rd quarter	maximum 3rd quarter	average 2nd quarter	average 1st quarter	average 4th quarter	average 3rd quarter	average 2nd quarter	average 1st quarter
Intesa Sanpaolo	25,8	24,5	26,6	27,9	32,3	42,1	31,5	37,9	29,4
Banca IMI	10,6	8,5	14,1	15,7	18,0	18,3	10,1	12,9	9,0
Total	**36,4**	**34,1**	**39,9**	**43,6**	**50,3**	**60,4**	**41,6**	**50,8**	**38,4**

[(a)] Each line in the table sets out past estimates of daily operational 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.

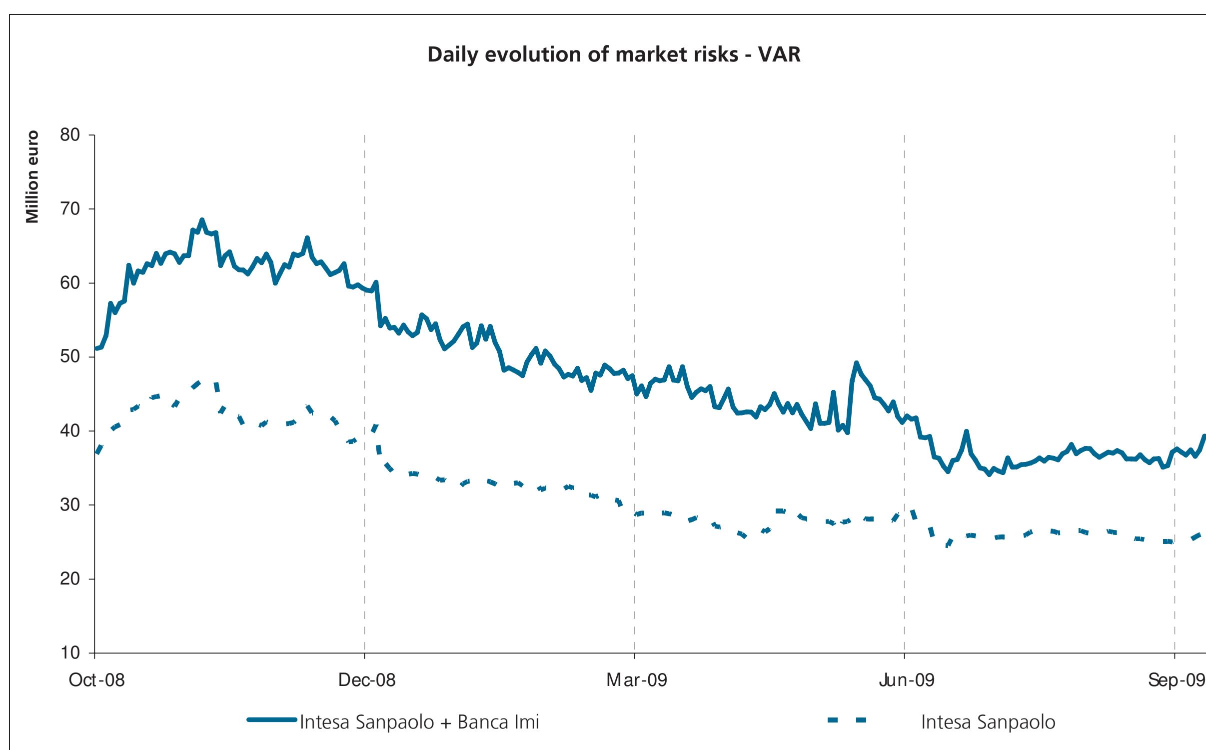
For Intesa Sanpaolo and Banca IMI the breakdown of risk profile in the third quarter of 2009 with regard to the various factors shows the prevalence of the hedge fund risk, which accounted for 58% of total VaR; for Banca IMI interest rate risk was the most significant representing 36% of total VaR.

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

3rd quarter 2009	Shares	Rates	Credit spread	Foreign Exchange	Hedge fund	Other parameters
Intesa Sanpaolo	10%	10%	6%	1%	58%	15%
Banca IMI	29%	36%	19%	2%	-	14%
Total	**18%**	**20%**	**12%**	**2%**	**34%**	**14%**

[(a)] Each line in the table sets out the contribution of risk factors considering the overall VaR 100%, calculated as the average of daily estimates in the second quarter of 2009, broken down between Intesa Sanpaolo and Banca IMI and indicating the distribution of overall VaR.

VaR in the last twelve months is set out below. The third quarter of 2009 recorded a drop in VaR, primarily from operations (a decrease in certain exposures and greater hedge effectiveness) and a different impact on volatilities on historic simulation scenarios.
As indicated in the chapter on balance sheet aggregates, a reclassification to LR (Loans & Receivables) was performed in October 2008, as permitted by IAS, on certain highly illiquid securities (mainly ABSs).
The average VaR in the third quarter of 2009 for this portfolio, not included in the VaR limit monitoring and the above statistics, was approximately 9.8 million euro.



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 September 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 4 million euro loss;
- on interest rate exposures, a parallel +25 basis point shift in the yield curve would have led to a 17 million euro loss, whereas a parallel -25 basis point shift would have led to a 17 million euro gain;
- on exposures sensitive to credit spread fluctuations, a 25 basis point widening in spreads would have led to a 23 million euro loss, 10 million euro of which attributable to structured credit products, whereas a 25 basis point contraction of the spreads would have led to a 24 million euro gain, 10 million euro of which attributable to SCP;

– on foreign exchange exposures, the portfolio would have recorded a 13 million euro gain in the event of exchange depreciation (-10%). A foreign exchange appreciation (+10%) would have led to a 1 million euro loss;
– lastly, on commodity exposures a 3 million euro loss would have been recorded had there been a 50% decrease in prices.

(in 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	0	-4	17	-17	24	-23	13	-1	-3	6
of which SCP					*10*	*-10*				

BANKING BOOK

Market risk originated by the banking book arises primarily in the Parent Company and in the main subsidiaries that carry out retail and corporate banking. The banking book also includes exposure to market risks deriving from the equity investments in listed 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 sight 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 (i) at protecting the banking book from variations in the fair value of loans and deposits due to movements in the interest rate curve or (ii) 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 the 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 one 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 nine months of 2009, interest rate risk generated by the Intesa Sanpaolo Group's banking book, measured through shift sensitivity analysis, registered an average value of 484 million euro settling at 458 million euro at the end of September, almost entirely concentrated on the euro currency; these figures compare with 484 million euro at the end of 2008.
Sensitivity of the interest margin – in the event of a 100 basis point rise in interest rates – amounted to +184 million euro (-180 million euro in the event of reduction) at the end of September 2009; these values

record an increase compared to the 2008 year-end figures of +102 million euro and -92 million euro, respectively, in the event of an increase/decrease in interest rates.
Interest rate risk, measured in terms of VaR, averaged 155 million euro in the first three quarters of 2009 (177 million euro at the end of 2008) and reached a value of 141 million euro at the end of September, with minimum and peak values of 86 million euro and 178 million euro, respectively.
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 143 million euro (120 million euro at the end of 2008) in the first nine months of 2009, with minimum and peak values of 87 million euro and 180 million euro respectively. VaR at the end of September amounted to 158 million euro.
Last, 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 September 2009.

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 supranational and national Supervisory authorities. As for the previous reports, reference is made to the requirements of the Bank of Italy (communication of 18 June 2008), and Consob (letter of 23 July 2008), also considering the recommendations contained in the Report of the Financial Stability Forum of April 2008, referred to by both Supervisory Authorities.

DETERMINATION OF THE FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

General Principles

IAS/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[1] represents the best evidence of fair value and these prices must be used with priority (effective market quotes) for the registration of financial assets and liabilities in the trading portfolio.

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);
- valuations performed using – even partly – 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).

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.

Hierarchy of fair value

As described above, the hierarchy of measurement models, i.e. of the approaches adopted for fair value measurement, attributes absolute priority to effective market quotes for valuation of assets and liabilities or for similar assets and liabilities (comparable approach) and a lower priority to non-observable and, therefore, more discretional inputs (Mark-to-Model Approach).

1. *Effective market quotes*

In this case the valuation is the price of the same financial instrument to be measured on the basis of prices quoted on an active market.

The percentage (determined in relation to fair value in case of derivatives) of instruments valued with this methodology on the total of instruments measured at fair value is set out below:

Financial assets:	
- cash	75.7%
- derivatives	1.8%

Financial liabilities:	
- cash	34.0%
- derivatives	3.7%

2. *Valuation Techniques: Comparable Approach*

In this case the valuation is not based on the price of the same financial instrument to be measured, but on prices or credit spreads presumed from official quotes of instruments which are similar in terms of risk factors, using a given calculation methodology (pricing model).

The use of this approach requires the search for transactions on active markets in relation to instruments that, in terms of risk factors, are comparable with the instrument to be measured.

The calculation methodologies (pricing models) used in the comparable approach reproduce prices of financial instruments quoted on active markets (model calibration) and do not contain discretional

[1] A financial instrument is considered as quoted on an active market if the quotations, reflecting normal market transactions, are promptly and regularly available through organised markets (exchanges), brokers, intermediaries, companies operating in the sector, quotation services or authorised bodies, and such prices represent effective and regular market transactions taking place over a normal period of reference.

parameters – parameters for which values may not be inferred from quotes of financial instruments present on active markets or fixed at levels capable of reproducing quotes on active markets – that significantly influence the final valuation.
The percentage of the instruments valued with this method (determined in relation to fair value in the case of derivatives) in the total of the instruments measured at fair value is as follows:

Financial assets:
- cash 21.2%
- derivatives 97.8%

Financial liabilities:
- cash 66.0%
- derivatives 94.7%

3. Valuation Techniques: Mark-to-Model Approach

In this case valuations are based on various inputs, which are not presumed directly from parameters which may be observed on the market and therefore imply estimates and assumptions on the part of the valuator.
In particular, with this approach the valuation of the financial instrument uses a calculation method (pricing model) based on specific assumptions of:
– the development of future cash-flows, which may be affected by future events that may be attributed probabilities presumed from past experience or on the basis of the assumed behaviour;
– the level of specific input parameters not quoted on active markets, for which information acquired from prices and spreads observed on the market is in any case preferred. Where this is not available, past data on the specific risk of the underlying asset or specialised reports are used (e.g. reports prepared by Rating agencies or primary market players).

The percentage of the instruments valued with this method (determined in relation to fair value in the case of derivatives) in the total of the instruments measured at fair value is as follows:

Financial assets:
- cash 3.1%
- derivatives 0.4%

Financial liabilities:
- cash -
- derivatives 1.6%

The cash financial assets include investments in equities of 1.4 billion euro, classified as securities available for sale.

STRUCTURED CREDIT PRODUCTS

The business model: objectives, strategies and relevance

The positive elements that emerged during the second quarter were confirmed in the third quarter. In particular, the positive credit spread trend strengthened and an overall contraction was seen in all the main asset classes.
The secondary market made a further recovery, especially for the higher rating classes, which ensured continuation of the portfolio disposal strategy already in progress. Confirming this is the closure of other transactions through market disposal or after counterparty exercise of a repurchase option.
Signs that the market is resettling were also seen in the reduction of the difference between secondary and primary spreads. The demand for new issues, no longer purely for funding purposes, was widespread among investors.
However, the reference framework is still characterised by elements that suggest caution, particularly the high unemployment rates and the related impact on delinquency and default on assets used as collateral for structured credit products.

Highlights

Before describing the results as at 30 September 2009, please note that the qualitative and quantitative composition of investments in structured credit products, penalised to various extents by the events that affected financial markets from the second half of 2007, has changed with respect to the information disclosed as at the end of last year and at the end of the first half of this year. Compared to 30 June 2009, despite the downgrade of a growing portion of these investments (approximately 24%), the good quality of the portfolio is confirmed, as shown by the following indicators:

- 87% of exposure is Investment Grade;
- 43% of this exposure has a Super senior (13%) or AAA (30%) rating; these percentages decreased considerably with respect to 31 December 2008;
- 13% has a rating of BBB or lower;
- 34% of the exposure has a pre-2005 vintage[2];
- 31% has a 2005 vintage;
- only 10 % of exposure refers to the US Residential segment, and 29% to the US non-residential segment;
- the remaining exposure (61% of the total) is mostly (53%) European.

Considering underlying contract types, approximately two thirds of the exposure is represented by CLOs (30%) and CDOs (32%); the rest is made up of ABSs (16%) and RMBSs (17%); CMBS represent 5% of the total.

Regarding the valuation methods adopted, unfunded positions are measured using the Mark-to-Model Approach. For funded products, the use of valuation methods involved the Comparable Approach in 59% of cases and the Mark-to-Model Approach (41% of cases). For further details on adopted valuation methods see details on the determination of the fair value of financial assets and liabilities provided in the 2008 Annual Report.

The structured credit products affected by the financial crisis are indicated by segregating the part classified under Financial assets held for trading and available for sale from those classified as Loans[3]. The tables illustrate the impact on the income statement of both aggregates.

The information set out below refers to the entire Group; where present, any effects and positions, which are in any case immaterial, 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 30 September 2009 and income statement captions (sum of realised charges and profits, write-downs and write-backs) of the year, compared with the corresponding values recorded as at 31 December 2008.

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. For a more complete description of exposures of this type see the specific paragraphs Monoline risk and Non-monoline packages.

The translation to euro of values expressed in USD as at 31 December 2008 occurred at an exchange rate of 1.3917 euro per dollar, and as at 30 September 2009 at an exchange rate of 1.4643 euro per dollar.

[2] 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.

[3] 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

(in millions of euro)

Financial assets held for trading	30.09.2009		31.12.2008	
	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	**32**	**21**	**23**	**-4**
Contagion area	**230**	**-71**	**207**	**-166**
- Multisector CDOs	155	-72	125	-103
- Alt-A	-	-	-	-
- TruPS	75	1	82	-63
- Prime CMOs	-	-	-	-
Other structured credit products	**1,730**	**-27**	**3,056**	**-327**
- Funded European/US ABS/CDOs	365	37	430	-53
- Unfunded super senior CDOs	1,422	-51	3,043	-249
- Other	-57	-13	-417	-25
Total	**1,992**	**-77**	**3,286**	**-497**
in addition to:				
Positions of funds	-	10	-	41
Total Financial assets held for trading	**1,992**	**-67**	**3,286**	**-456**

Loans	30.09.2009		31.12.2008	
	Risk exposure (**) (including write-downs and write-backs)	**Income Statement**	**Risk exposure** (*) (including write-downs and write-backs)	**Income Statement**
US subprime exposure	**7**	**-1**	**6**	**-**
Contagion area	**110**	**-**	**138**	**-5**
- Multisector CDOs	14	-	12	-
- Alt-A	62	-	78	-2
- TruPS	-	-	-	-
- Prime CMOs	34	-	48	-3
Other structured credit products	**2,323**	**8**	**1,973**	**-57**
- Funded European/US ABS/CDOs	1,436	-4	1,729	-57
- Funded super senior CDOs	740	12	-	-
- Other	147	-	244	-
Total	**2,440**	**7**	**2,117**	**-62**
in addition to:				
Positions of funds	-	-	-	-
Total Loans	**2,440**	**7**	**2,117**	**-62**
Total	**4,432**	**-60**	**5,403**	**-518**

(*) 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 value of the security, equal to fair value at the reclassification date, plus accrued interest calculated at the actual interest rate net of net value adjustments to the portfolio.

b) Exposure in packages

(in millions of euro)

Detailed table	30.09.2009		31.12.2008	
	Credit exposure to protection seller (CDS fair value) post write-down	**Income Statement** Profits (Losses) on trading	**Credit exposure to protection seller** (CDS fair value) post write-down	**Income Statement** Profits (Losses) on trading
Monoline risk	14	27	-	-94
Non monoline packages	96	4	154	-
Total	**110**	**31**	**154**	**-94**

Structured credit products improved, reaching -29 million euro as at 30 September 2009 (of which -60 million euro funded and unfunded ABS/CDOs and +31 million euro in package exposure).
Regarding the first of these, the impact affected “Profits (Losses) on trading – Caption 80” by -67 million euro (10 million euro of which attributable to fund positions). The negative result for this segment is essentially due to the negative contribution of funded and unfunded positions associated with the “Contagion Area” (-71 million as at 30 September 2009), mitigated only in part by the positive results in its related fund positions. The deterioration in this segment (-31 million euro in the third quarter of 2009, including -2 million euro associated with fund positions), must be considered alongside the improvement recorded in the US Subprime segment (21 million euro as at 30 September 2009, 24 million euro of which in the third quarter). This different illustration of the effect these two areas had on the income statement is due to the change in the percentage of US RMBS since the start of the year on total collateral assets, to one position split between the two segments, and to the change in market figures used for estimates, in turn affected by the narrowing difference between spreads seen in recent months. Added to this is the negative effect generated in the first nine months of the year by unfunded positions in the “Other structured credit products” area (-64 million euro as at 30 September 2009, of which -51 million euro under unfunded super senior CDOs and -13 million euro under other unfunded positions), affected by the downgrade and default on assets included in the positions as collateral. These phenomena weakened a little in the third quarter, as seen in the positive contribution (22 million euro) of the segment.
On the other hand, there was the positive contribution of European and US funded ABS/CDOs to profit/loss for the period as at 30 September 2009 (37 million euro). This result benefited mainly from the good portfolio performance of the subsidiary Banca IMI (23 million euro) and profits from the market disposal of a number of positions (12 million euro). In the third quarter of 2009 these positions made a positive 12 million euro contribution to the income statement.
As at 30 September 2009 securities reclassified under the loan portfolio recorded profits on market disposals of 14 million euro and losses for impairment of securities of 7 million euro. The contribution of this segment in the third quarter of 2009 was a positive 9 million euro.
The contribution of the “Monoline risk” and “Non-monoline packages” was also positive with a total result of 31 million euro as at 30 September 2009 (+12 million euro in the third quarter), thanks to the progressive reduction of exposure to counterparties and a slight improvement in their creditworthiness.
As at 30 September 2009, this aggregate included bonds classified as loans for a total nominal value of 2,672 million euro and risk exposure of 2,440 million euro. Of this amount, 184 million euro referred to securities reclassified from available for sale to the loans portfolio. As at 30 September 2009 their fair value was 134 million euro. The positive impact of this transaction on the Valuation reserve under Shareholders' Equity was 50 million euro. The remaining 2,256 million was reclassified from the trading book to the loans portfolio. The fair value of this aggregate as at 30 September 2009 was 1,950 million euro, with a positive effect on the income statement of 306 million euro, 299 million euro of which referring to 31 December 2008. Had the loans portfolio not been reclassified, the negative result for structured products would have increased to -36 million euro in the first nine months of 2009.
For a detailed illustration of the various product types, please refer to the information provided in the Half-yearly Report as at 30 June 2009.

INFORMATION ON ACTIVITIES PERFORMED THROUGH SPECIAL PURPOSE ENTITIES (SPEs)

For the purpose of this analysis, legal entities established to pursue a specific, clearly defined and limited objective are considered Special Purpose Entities:
- to raise funds on the market by issuing specific financial instruments;
- to acquire, sell, manage specific assets, separating them from the financial statements of the Originator;
- to develop and/or finance a specific business initiative, capable of generating, through an economic activity, cash flows which permit the complete reimbursement of the debt;
- to finance the acquisition of a target company which, through its economic activity, will be capable of generating cash flows for the SPEs which permit the complete reimbursement of the debt;
- to manage the credit risk connected to their portfolio of financial assets through protection purchases and sales with counterparties represented by SPEs (used by both the American market and the European market for synthetic portfolio securitisations). In such transactions the Bank accepts credit risk or counterparty risk with the SPEs, depending on the nature of the transaction.

The sponsor of the transaction is normally an entity which requests the structuring of a transaction in a SPE for the purpose of reaching certain objectives. In some cases the Bank is the sponsor and establishes a SPE with the objective of raising finance, securitising its assets or offering customers a financial service.
No changes in consolidation criteria have been made with respect to the previous year.

The types of transactions in SPEs related to Intesa Sanpaolo's current operations are set out below.

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.
These SPEs, which are controlled by Intesa Sanpaolo and are part of the Group's scope of consolidation as per IAS 27, are: Intesa Funding LLC, San Paolo IMI Financial CO., IntesaBCI Preferred Capital Company LLC III and SanPaolo IMI Capital Company LLC 1. All these SPEs are based in the USA.
There has been no change to the figure recorded in the Half-yearly Report as at 30 June 2009.

The total SPE assets are almost fully represented by loans to the Parent Company Intesa Sanpaolo and as at 30 September 2009 totalled 13,490 million euro (12,533 million as at 30 June 2009). The total securities issued – 100% guaranteed by the Parent Company – amounted to 13,349 million as at 30 September 2009 (12,415 million as at 30 June 2009).

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 has been no change in the number of consolidated companies or in their total assets from that recorded in the Half-yearly Report as at 30 June 2009.

Securitisation SPEs

These are SPEs which permit an entity to raise funds for 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. Funding raised in this way is reversed to the seller while commitments to underwriters are met by using the cash flows generated by the loans sold.
SPEs of this type, which are part of the scope of consolidation as at 30 September 2009 pursuant to IAS 27 or SIC 12, are: Intesa Sec S.p.A., Intesa Sec 2 S.r.l., Intesa Sec 3 S.r.l., Intesa Sec NPL S.p.A., Intesa Lease Sec S.r.l., Split 2 S.r.l., ISP CB Pubblico S.r.l., Adriano Finance S.r.l. – Series 1 and 2 – and Adriano Finance 2 S.r.l..
These companies, incorporated under Italian law, have been used to securitise the performing assets (mortgage loans, leasing contracts) or non-performing assets (mortgage loans) of Intesa Sanpaolo or Group companies.
Augusto, Colombo and Diocleziano are securitisation vehicles of assets (residential mortgages), mostly to finance long-term mortgages and public works, of companies subject to joint control and later sold.
The securities held have been measured at fair value, as in previous years, except for securities issued by the vehicles Adriano Finance S.r.l. and Adriano Finance 2 S.r.l., that are classified to the loans portfolio and

valued at amortised cost.
For the securitisations prior to 1 January 2004 (Intesa Sec, Intesa Sec 2, Intesa Sec Npl and Intesa Lease Sec.), the Group used the exemption from compliance to IAS/IFRS permitted on first-time adoption by IFRS 1, and therefore the assets or liabilities sold and derecognised, based on previous accounting principles and deriving from securitisations, have not been recorded in the financial statements. For transactions stipulated after that date, the provisions of IAS 39 on derecognition of financial assets and liabilities are applied.
The securitised assets of this type of vehicle are represented as follows: performing mortgages - Intesa Sec S.p.A.; performing residential mortgages - Intesa Sec 2 S.r.l., Intesa Sec 3 S.r.l., Adriano Finance S.r.l. and Adriano Finance 2 S.r.l.; non-performing mortgages – Intesa Sec NPL S.p.A., performing loans and cash commitments – Intesa Lease Sec S.r.l. and Split 2 S.r.l.. Total assets of Augusto, Colombo and Diocleziano are instead almost entirely made up of land financing.
Note that:
- ISP CB Ipotecario S.r.l. and ISP Sec 4 S.r.l. were no longer operative as at 30 September 2009;
- the securitisation of Adriano Finance 3 S.r.l. is being defined.

To complete the information, C.R. Firenze Mutui S.r.l., a securitisation vehicle with its own underlying assets (performing mortgages) should also be mentioned.
The total assets of this type of vehicle, there were no significant changes in the total securities issued and total securities repurchased by the Intesa Sanpaolo Group from the figures recorded as at 30 June 2009.

Furthermore, pursuant to the above-mentioned SIC 12, Intesa Sanpaolo controls:
- Romulus Funding Corporation, a company based in the USA that purchases financial assets, represented by loans or securities with predefined eligibility criteria originating from Bank customers, and finances purchases by issuing Asset Backed Commercial Papers;
- Duomo Funding PLC, an entity which performs an activity similar to that of Romulus Funding Plc. but is limited to the European market and is financed through funding contracts with Romulus.

As at 30 September 2009, Romulus total assets amounted to 1,861 million euro (1,628 million euro as at 31 December 2008). The vehicle’s assets include loans to customers of 1,684 million euro, of which 1,202 million euro to Duomo. The vehicle’s securities portfolio is classified entirely under loans. As at 30 September 2009, the securities had a nominal value of 190 million euro, valued at amortised cost. Their carrying amount at the same date was 160 million euro. These securities are all included among structured credit products. Liquidity and other assets amounting to approximately 17 million euro (of which 15 million euro for positive fair value derivatives) also form part of the assets. Note that the commercial papers issued by the company for a total of 1,780 million euro (1,670 million as at 31 December 2008) have been fully placed on the market. Total Duomo assets amounted to approximately 1 billion euro (essentially in line with the December 2008 figure).
Intesa Sanpaolo holds no interest in SPQR II S.r.l. (CBO 1) and SPQR II S.r.l. (CBO II), but the companies were consolidated as the Group retains the majority of costs and benefits (SIC 12).
The vehicle assets are almost entirely made up of a portfolio of bonds issued by Italian public entities, sold to the vehicle by Banca OPI (now Banca Infrastrutture Innovazione e Sviluppo - BIIS). The vehicle, in turn, issued senior and junior securities; both security types were repurchased by BIIS, which allocated the senior classes as collateral to its funding with the European Central Bank, via transactions closed through the Parent Company Intesa Sanpaolo.
The overall total of SPQR II S.r.l. assets and securities issued remained unchanged from the figure recorded as at 30 June 2009.

Intesa Sanpaolo acquired protection on its credit risk exposure from the synthetic securitisation vehicle “Da Vinci" to hedge and actively manage risk exposure in the aircraft and aeronautic sector.

Financial Engineering SPEs

These SPEs make investments and funding which allow better risk/return combinations than those generated by standard transactions, due to their particular structure aimed at optimising accounting, tax and/or regulatory issues. These structures have been established to meet the needs of top customers and to provide solutions that offer financing at competitive interest rates and investments with higher returns.
Intesa Sanpaolo controls and consolidates Intesa Investimenti S.p.A., a company established to invest in quotas of Italian and international UCITS, in quotas and shares of other Italian and international entities and in Government securities of G7 countries, with the simultaneous subscription of a commitment to resell at a future date and at a predetermined price; all assisted by swaps aimed at assuring an adequate profitability of the investment. Intesa Sanpaolo replicates every transaction, again with a repurchase agreement with Intesa Investimenti, whose shares are in turn the object of an analogous contract with

investing customers. The company is currently inoperative.
From the second quarter of 2009, Lunar Funding Plc, a vehicle set up in Ireland and used for repackaging operations by a leading bank, entered the scope of consolidation.
The assets of the vehicle are almost entirely made up of term deposits with the Parent Company Intesa Sanpaolo, and remain unchanged since June 2009.

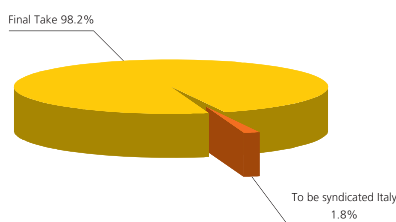
Other unconsolidated Special Purpose Entities

With regard to the other unconsolidated SPEs (Project Financing, Asset Backed, Leveraged & Acquisition Finance and Credit Derivatives) reference should be made to the Half-yearly Report as at 30 June 2009.

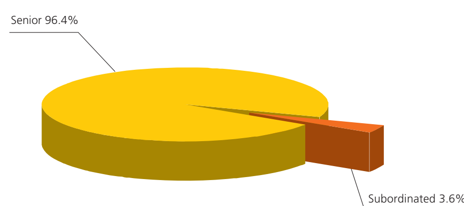
LEVERAGED FINANCE TRANSACTIONS

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), linked to full or part acquisition of the 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 30 September 2009, around 110 transactions, for a total amount granted of 4,786 million euro, met the above definition.
Such exposures are mostly classified in the loan portfolio. These also include the portions of syndicated loans underwritten or under syndication destined from the outset to be sold. In line with disclosure requirements, breakdown of exposures by geographical area, economic sector and by level of subordination is set out below.

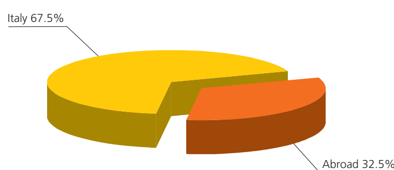
Breakdown by type of risk



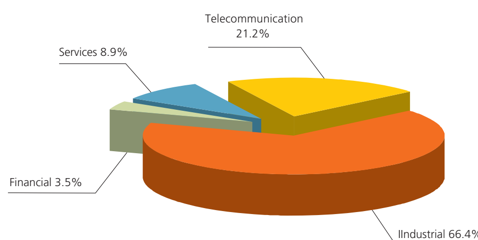
Breakdown by subordination level



Breakdown by geographical area



Breakdown by economic sector



DISCLOSURE ON INVESTMENTS IN HEDGE FUNDS

As at 30 September 2009, the Hedge Funds portfolio totalled 684 million euro, down on the 852 million euro recorded at year-end 2008. The decrease is also due to disposals totalling 314 million euro and to new positions amounting to 141 million euro.

At the same date, the contribution of these investments to Profits (Losses) on trading doubled compared to the figure recorded for the first half of the year: the total as at 30 September 2009 was 112 million euro (of which 10 million euro included in the disclosure of structured credit products). Of these net profits:

– 27 million euro refers to profits on trading of funds for the first nine months of the year (including 4 million euro in the structured credit products disclosure);
– 94 million euro arises from net valuation of positions remaining at the end of the quarter (including 6 million euro in the structured credit products disclosure);
– 9 million euro from other net charges.

Taking into account the net capital gains on the final residual amount (94 million euro), these are spread across 43 positions, 7 of which recording capital losses (-26 million euro) and 36 capital gains (120 million euro).

INFORMATION ON TRADING TRANSACTIONS IN DERIVATIVES WITH CUSTOMERS

Considering only relations with customers, as at 30 September 2009, 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, considering netting agreements, of 3,359 million euro (2,524 million euro as at 31 December 2008). The notional value of such derivatives totalled 48,774 million euro (47,076 million euro as at 31 December 2008). Please note that the positive fair value of structured contracts outstanding with the 10 customers with the highest exposures was 1,136 million euro (688 million euro as at 31 December 2008).

Conversely, negative fair value determined with the same criteria, for the same types of contracts and with the same counterparties, totalled 376 million euro at 30 September 2009 (443 million at 31 December 2008).

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"). With regard to contracts outstanding as at 30 September 2009, this led to adjustments of 74 million euro being recorded under profits (losses) on trading in the income statement, compared to 65 million euro as at 31 December 2008, with a negative impact during the period of 9 million euro. Adjustments are recorded, for every single contract, at 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 risks include 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 Group has a centralised function within the Risk Management Department for the management of the Group's operational risks. 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 regulations, the Group's individual business units are involved, each assigned responsibilities for the identification, assessment, management and mitigation of its operational 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 Group's Internal Model is designed to combine all the main quantitative (internal and external historical loss data) and qualitative information sources (self-assessment: scenario analysis and operational environment assessment). The quantitative component is based on the assessment of historical data on internal and external events (including participation in consortium initiatives such as "Database Italiano Perdite Operative" – Italian Operational Loss Database – managed by the Italian Banking Association and Operational Riskdata eXchange Association).
The qualitative component focuses on the forward-looking assessment of the risk exposure of each unit and is based on the structured collection of subjective estimates with the aim of assessing relevant scenarios identified starting from the proprietary risk classification system based on the types of events provided for by the New Capital Accord.
Capital at Risk is therefore identified as the minimum amount at Group level, net of insurance cover, 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 and qualitative figures with a 1-year holding period, and on a 99.90% confidence level.
The Group has activated a traditional operational risk transfer policy (insurance) with the objective of mitigating the effect of any unexpected losses, therefore helping to reduce the Capital at Risk.
As at the end of September the capital absorption for operational risks was determined with the Traditional Standardised Approach, with an approximate 2.3 billion euro incidence at Group level.

Legal risks

There were no significant changes in legal risks as at the end of September 2009 compared to either the Intesa Sanpaolo Group Annual Report 2008 or the Half-yearly Report, to which reference should be made for the main current 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.

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 Asset Liability Management (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 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 30 September 2009 the investment portfolios of Group companies, recorded at book value, amounted to 46,880 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 19,344 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 27,536 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, 94.3% of assets, i.e. approximately 18,354 million euro, were bonds, while assets subject to equity risk represented 4.4% of the total and amounted to 859 million euro. The remaining part (259 million euro) consisted of investments relating to UCI, Private Equity and Hedge Funds (1.3%).

The fair value of derivatives came to approximately -128 million euro, around -127 million of which in hedging derivatives and close to -1 million in other derivatives.
At the end of the third quarter of 2009, investments of EurizonVita and SudPoloVita free capital amounted to approximately 1,062 million euro at market value, and presented a risk in terms of VaR (99% confidence level, 10-day holding period) equal to 25 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 5.3 years. The reserves associated to profit contracts have an average modified duration of approximately 4.2 years. The related portfolios of assets have a modified duration of around 4.4 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 911 million euro. On the basis of this hypothetical scenario, the value of hedging derivatives in the portfolio undergoes an approximate 120 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 76.6% of total investments and A bonds approximately 13.1%. Low investment grade securities (BBB) were approximately 3.8% of the total and the portion of speculative grade or unrated was minimal (approximately 0.8%).
The analysis of the exposure in terms of the issuers/counterparties produced the following results: securities issued by Governments and Central banks represented approximately 75.4% of total investments, while financial companies (mostly banks) contributed to the exposure by almost 11.8% and industrial securities made up approximately 7.1%.
As at the end of the third quarter of 2009, 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 -996 million euro, -836 million euro due to government issuers and -160 million euro to corporate issuers (financial and industrial companies).