Pillar 3 Disclosure

Update as at
31 December 2015

MONTE
DEI PASCHI
DI SIENA
BANK SINCE 1472

Pillar 3 Disclosure

Update as at
31 December 2015

Banca Monte dei Paschi di Siena SpA
Company Head Office in Siena, Piazza Salimbeni 3, www.mps.it
Recorded in the Siena Company Register – Registration no. and tax code 00884060526
Member of the Italian Interbank Deposit Protection Fund. Bank Register no. 5274
Parent Company of the Monte dei Paschi di Siena Banking Group, registered with the Banking Groups Register

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Introduction

The New Regulations for the Prudential Supervision of banks and banking groups entered into force as of 1 January 2014.

The regulations aim to align national requirements with the changes introduced to the International regulatory framework, following reforms in the Basel Committee agreements (Basel 3), particularly the European Union's New Regulatory and Institutional Framework for Banking Supervision.

In particular, the contents of the "Basel 3 framework" have been adopted within the EU through two capital requirement rules:

- ✓ CRR – Capital Requirements Regulation (EU) 575/2013 of the European Parliament and Council of 26 June 2013 regarding prudential requirements for credit institutions and investment firms, which amends Regulation (EU) 648/2012;
- ✓ CRD IV – Capital Requirements of the European Parliament and Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

The new regulatory package includes application criteria, set out in the Regulatory Technical Standards (RTS) and Implementing Technical Standards (ITS) adopted by the European Commission, upon the proposal of the European Supervisory Authorities.

At national level, the new harmonized framework has been implemented by Bank of Italy with:

- ✓ Circular 285 of 17 December 2013 – Supervisory Provisions for Banks;
- ✓ Circular 286 of 17 December 2013 – Instructions for Prudential reporting for banks and securities' firm;
- ✓ Circular 154 of 22 November 1991 – 59th Update, 7 August 2015 – Supervisory reports of banks and financial institutions. Reporting templates and instructions for transmission of information flows.

The new regulatory framework aims to improve the ability of banks to absorb shocks arising from financial and economic stress, whatever the source, improve risk management and governance and strengthen the bank's transparency and disclosures, while taking into account developments from the financial crisis.

The Basel Committee has maintained a three Pillars-based approach which was at the basis of the previous capital accord known as "Basel 2", but has integrated and strengthened it to increase the quantity and quality of banks' capital base and introduce countercyclical supervisory tools as well as new standards for liquidity risk management and financial deleveraging.

More specifically, Pillar 3 was designed on the notion that Market Discipline can be harnessed to reinforce capital regulation to promote stability and soundness in banks and financial systems.

Pillar 3, therefore, aims to complement the minimum capital requirements (Pillar 1) and supervisory review process (Pillar 2) by developing a set of transparent disclosure requirements which will allow market participants to have access to key, fully comprehensive and reliable information on capital adequacy, risk exposures and risk identification, measurement and management processes.

Public Disclosure (Pillar3) is now governed directly by European Regulation no. 575/2013 of 26 June 2013 of the European Parliament and Council, Part 8 and Part 10, Title I, Chapter 3 (hereinafter referred to as "The Regulations" or "CRR").03

The previous Regulations (Bank of Italy Circular 263/06, Paragraph IV) along with the reporting templates and rules provided therein are to be considered no longer applicable.

Under the new regulations, the CRR requires banks to publish information at least on an annual basis along with their financial statements and to evaluate the need to publish some or all disclosures more frequently than once a year depending on their specific activities. Institutions are to assess the possible need for more frequent disclosure of items of information laid down in Article 437 (Own Funds), and Article 438 (Capital Requirements), and information on risk exposure and other items prone to rapid change.

The EBA (European Banking Authority) subsequently issued its guidelines (EBA/GL/2014/14 of 23-12-2014), pursuant to 16 of EU Regulation no.1093/2010, on the need to publish information more frequently than once a year.

In view of the above regulations and in the interest of transparency and continuity, the Group publishes summary information on its Own Funds, Capital Requirements and Leverage in its quarterly reports, providing further information on exposures subject to internal models in its half-year report..

This document provides a full update as at 31 December 2015 and presents the new disclosure templates provided for by the new regulatory framework.

Information must be both qualitative and quantitative in nature and be structured so as to provide a comprehensive overview of the risks assumed, the features of the management and control system and the capital adequacy of the Montepaschi Group.

Pillar 3 Disclosure is prepared at consolidated level by the Parent Company.

Unless otherwise indicated, all the amounts in this report are stated in TEUR (thousand Euros).

Data as at 31 December 2014 contained in this document may, in some cases, be different from the data published in previous publications on account of the restatement of the Alexandria transaction as a CDS derivative, at the request of Consob. The transaction was previously recognised as a long term repo. The restated values reflect the changes made in accordance with the provisions of IAS 8 (Accounting policies, changes in accounting estimates and errors) as illustrated in the section "Restatement of prior period accounts in compliance with IAS 8 (Accounting policies, changes in accounting estimates and errors)" of the Consolidated Notes to the Group's Consolidated Financial Statements as at 31 December 2015.

As an aid to understanding and clarifying certain terms and abbreviations used in this report, please refer to the Glossary provided at the end of the document.

Given the public relevance of this disclosure, the document is submitted by the Manager responsible for preparing the financial reports to the corporate bodies competent for approval. This document is therefore subject to the related attestation, pursuant to art. 154-bis of Legislative Decree no. 58/98 (Consolidated Law on Finance, "TUF").

The Montepaschi Group regularly publishes its Pillar 3 disclosure on its website at: www.mps.it/investors.

Additional information required under the CRR is published in the Annual Report as at 31 December 2015, the Corporate Governance Report and the Remuneration Report. Based on art. 434 of the CRR, which provides for the possibility to make reference to other public disclosure documents, the Group makes use of this opportunity to complete the information, appropriately stating the reference to other documents. In particular, the the different types of risk to which the Banking Group is exposed are also reported in Part E of the Notes to the Consolidated Financial Statements based on the provisions of IFRS 7 and related instructions issued by the Bank of Italy (Circular 262 and its updates). Part E reports on:

- credit risk (Part E – Information on risks and hedging policies: Section 1 – Risks of the Banking: 1.1 Credit risk);
- market risk (Part E – Information on risks and hedging policies: Section 1 – Risks of the Banking: 1.2 Market risk);
- Banking Group Liquidity risk (Part E – Information on risks and hedging policies: Section 1 – Risks of the Banking: 1.3 Liquidity risk).

The Corporate Governance Report, published under the Corporate Governance section of the Group's website at, www.mps.it/investors/corporategovernance, contains all the information required by paragraph 2 of art. 435 of the CRR:

- the number of directorships held by members of the management body;
- the recruitment policy for the selection of members of the management body and their actual knowledge, skills and expertise;
- the policy on diversity with regard to selection of members of the management body, its objectives and any relevant targets set out in that policy, and the extent to which these objectives and targets have been achieved;
- whether or not the institution has set up a separate risk committee and the number of times the risk committee has met;

- the description of the information flow on risk to the management body.

The Remuneration Report, published under the section Corporate Governance/ Governance Systems and Remuneration Policies of the Group's website at www.mps.it/investors/corporategovernance/sistema-digovernanceepolicy, includes all the information required by art. 450 of the CRR regarding the remuneration policy and practices of the Group for those categories of staff whose professional activities have a material impact on its risk profile.

Data from the indicators used at the end of 2015 to identify global systemically important banks will also be published on the Group's website by 30 April 2016 at: http://b.mps.it/go/gsibs15.

1. Risk management objectives and policies

Executive Summary

Key Regulatory Metrics

Common Equity Tier 1	Tier 1 Capital	Own Funds
€ 8.5bn *up 32%* *Dec-14: € 6.5bn*	€ 9.1bn *up 41%* *Dec-14: € 6.5bn*	€ 11.3bn *up 16%* *Dec-14: € 9.8bn*
CET 1 Ratio	Tier 1 Ratio	Total Capital Ratio
12.01% *Dec-14: 8.45%*	12.85% *Dec-14: 8.45%*	15.95% *Dec-14: 12.81%*
Total RWA	Credit Risk EAD	
€ 70.8 bn *down -7%* *Dec-14: € 76.3bn*	€ 178.9 bn *down -9%* *Dec-14: € 197.3bn*	

The core objective of this disclosure is to provide a comprehensive description of the Montepaschi Group's risk profile as well as information on capital management and underlying risk drivers in addition to that already contained in the Annual Financial Report.

The annual disclosure provides detailed information on the Montepaschi Group's capital adequacy (under Pillar I) and on the assessment of risk using Risk Management models. The Group manages its capital by ensuring that the capital base and correlated ratios are consistent with the risk profile assumed and compliant with regulatory requirements. The assessment of regulatory capital adequacy is based on the constant monitoring of own funds and risk weighted assets (RWAs) as well as on a comparison with the minimum regulatory requirements, including the additional requirements to be maintained over time and communicated to the Group following the SREP and the additional capital reserves introduced by the new regulatory framework.

RWA and asset optimisation is achieved through the simultaneous monitoring the trend in volumes and changes in related risk metrics. The Group believes increasingly crucial oversee the evolution of the credit quality of the portfolio in the macroeconomic scenario.

As of 31 December 2014, disclosure has been prepared on the basis of the new harmonised regulatory framework for banks and investment firms contained in the CRR and CRDIV. As mentioned earlier, the two rules (hereinafter, the new regulatory framework) implement within the EU the "Basel 3 framework which establishes more stringent criteria for the capital adequacy levels of banks.

The introduction of the new regulatory framework, CRR/CRD IV, is subject to a transition period that extends the full application of the rules to 2019 (2022 for the phase-out of certain capital instruments) and during which the new rules will be applied in an increasing proportion. In particular, there are several elements that will be eligible for full inclusion or deduction from common equity when the framework is fully effective, but currently only have a partial percentage effect on Common Equity; generally, the residual percentage, after the applicable portion, is included in/deducted from Additional Tier 1 Capital (AT1) or Tier 2 capital (T2), or is factored into risk-weighted assets.

Specific transitional provisions have also been established for subordinated instruments that do not meet the requirements envisaged in the new regulatory provisions, aimed at the gradual exclusion of instruments no longer regarded as eligible from Own Funds (over a period of 8 years).

Accordingly, the prudential ratios as at 31 December 2015 and 2014 published in this document take account of the adjustments envisaged by the transitional provisions.

Under Prudential requirements, as of January 2014 all banks must comply with a CET1 ratio of at least 4.5%, a Tier 1 ratio of at least 6% (5.5% as of 2014) and a Total capital Ratio of at least 8% of the Group's total risk exposure. Additionally, Banks are also required to hold the following buffers against Pillar 1 risks:

- as of 1 January 2014, a *capital conservation buffer of* 2.5% (to be added to the CET1 requirement);
- as of 2016, a specific countercyclical capital buffer for the bank in periods of excessive credit growth at the time and up to the first quarter of 2016 of 0%;
- a *G-SII* capital buffer (1% – 3.5%; as of 2016) and a *O-SII* capital buffer (0% – 2%). The Montepaschi Group falls under the group of Other Systemically Important Institutions (O-SII), for which the Bank of Italy has established a buffer of 0% for 2016;
- a non-cyclical systemic risk or macroprudential buffer of at least 1%.

Buffers are calculated by Member States (Bank of Italy) on the basis of the new regulatory framework (Bank of Italy) and are to be added to Common Equity Tier 1 capital. There is also an additional Common Equity Tier 1 component, held against Pillar 2 risks and established subsequent to the annual SREP. Failure to comply with the combined capital requirements entails restrictions on dividend distributions and the need to adopt a capital conservation plan.

In accordance with regulatory provisions, as at the date of this document the Group's CET1 requirement is determined as the sum of the following components:

- CET1 of 4.5% against Pillar 1 risks, as defined by art. 92 of the CRR;
- a capital conservation buffer of 2.5%, set by the Bank of Italy in accordance with art. 129 CRDIV, for all banks as of 2014;
- a component of CETI to be held in excess of CET1 against Pillar 2 risk, as required by art. 16 of EU Regulation no. 1024/2013 and established subsequent

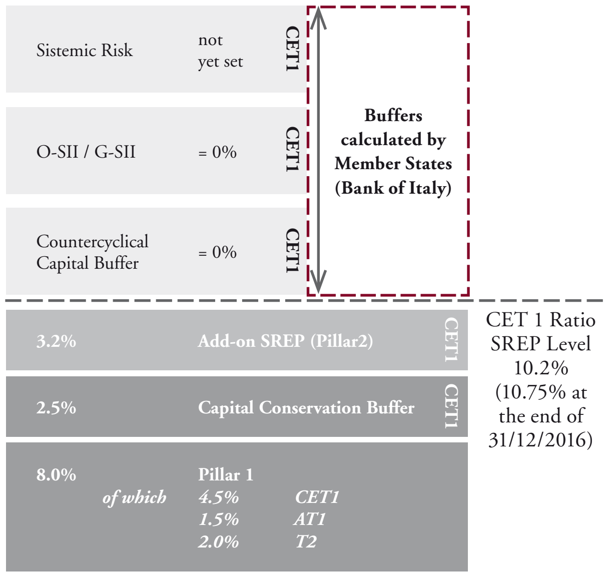
to the annual SREP at 3.20% until 31 12 2016 and 3.75% as of 31 December 2016;

- a countercyclical capital buffer set by the Bank of Italy at 0% for the first quarter of 2016.

  The following buffers have been added as of 2016.

- an additional CET 1 capital buffer for systemically important insitutions (O-SII) such as the MPS group, set by the Bank of Italy at 0% for 2016;
- a capital buffer to be held against systemic risk to be added to CET1, to be determined by the member states and not yet set by the Bank of Italy

Therefore, until 31 12 2016 the MPS Group is required to maintain a CET1



SREP ratio of 10.2% (10.75% at the end of 2016) and comply with the other minimum requirements of Pillar 1. For further details on the outcome of the SREP, please refer to chapter 4 of this report.

Executive Summary on Own Funds and Capital Requirements

Data in thousands of euros

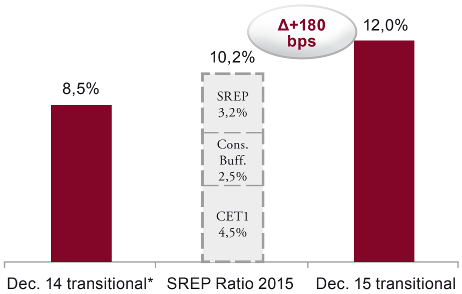
			Delta vs. 31-12-2014	
Own Funds	**dec-15**	**dec-14****	**Absolute**	**%**
Common Equity Tier 1 (CET1)	8,503,145	6,451,243	2,051,902	31.8%
Additional Tier 1 Capital (AT1)	598,309	-	598,309	-
Tier 2 Capital (T2)	2,196,269	3,321,069	-1,124,800	-33.9%
Own Funds	**11,297,723**	**9,772,312**	**1,525,411**	**15.6%**
↳ *of which Delta PA**	*2,084*	*174,843*	*-172,759*	*-98.8%*
Capital Requirements				
Credit and Counterparty Risk	4,624,341	4,988,031	-363,690	-7.3%
↳ *of which Standardised Approach*	*1,949,684*	*2,656,791*	*-707,107*	*-26.6%*
↳ *of which Airb Approach*	*2,674,657*	*2,331,240*	*343,417*	*14.7%*
Market Risk	274,556	286,106	-11,550	-4.0%
↳ *of which Standardised Approach*	*274,556*	*286,106*	*-11,550*	*-4.0%*
↳ *of which Airb Approach*	-	-	-	-
Operation Risk	702,894	708,267	-5,373	-0.8%
↳ *of which Foundation Approach*	*18,507*	*20,212*	*-1,705*	*-8.4%*
↳ *of which Advanced Approach*	*684,387*	*688,055*	*-3,668*	*-0.5%*
CVA Risk	64,487	118,750	-54,263	-45.7%
Concentration Risk	-	3,036	-3,036	-100.0%
Regulatory Capital Requirements	**5,666,278**	**6,104,190**	**-437,912**	**-7.2%**
Risk-weighted assets	**70,828,477**	**76,302,378**	**-5,473,901**	**-7.2%**
			Delta vs. 31-12-2014	
Capital Ratio			**in bp**	**in %**
CET1 Capital Ratio	**12.01%**	**8.45%**	**356**	**3.6%**
Tier 1 Ratio	**12.85%**	**8.45%**	**440**	**4.4%**
Total Capital Ratio	**15.95%**	**12.81%**	**314**	**3.1%**

** The value represents the total contribution of the Delta PA, understood as the sum of the positive and deductions, to the determination of the Own Funds under the new regulatory framework. The total amount of the Delta PA amounts to 2,084 € / thousand (174,843 € / thousand as at 31 December 2014).*

*** Data as at the end of December 2014 differ from those published previously since they reflect the changes resulting from the different accounting treatment of the Alexandria transaction.*

As at 31 December 2014, the MPS Group showed an adequate level of capitalisation to cover the minimum requirements for Own Funds established by the new regulatory framework, with a total capital surplus of EUR 5.3bn (+501 bps) compared to the minimum CET1 (4.5%) and of EUR 1.3bn (+180 bps) compared to the minimum required level of CET1 SREP Ratio (including the capital conservation buffer).

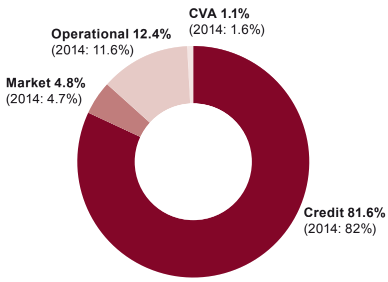
CET 1 Ratio



**Dec -14 transitional: post restatement*

Capital ratios also show a significant increase from the previous year, largely owing to the rights issue in June 2015 following the AQR results, the increased share capital issued to the MEF for payment of the coupon on the New Financial Instruments (NFIs) accrued in 2014 and to the profit generated in the period. A negative impact came from the repayment of the last tranche of NFIs and deactivation of the "excess of deduction from AT1 items", which was in force in 2014. RWAs, totalling EUR 70,828 million, were down by approximately EUR 5,474 million from December 2014, mainly due to the decrease in credit and counterparty risk (-7.3%) as a result of changes in the performing portfolio and the conversion of DTAs into tax credits in the second quarter of 2015. A breakdown of RWAs by type of risk shows a large concentration in Credit Risk (81.6%), notwithstanding the overall year-on-year decrease of 7.2% in absolute terms.

RWA by risk type



In 2015, the Group further developed the overall internal reference framework for the determination of its risk appetite: the Risk Appetite Framework (RAF).

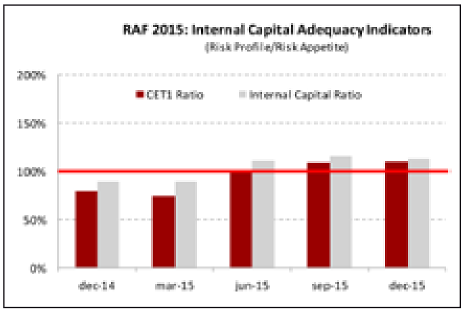
The objective of the RAF is to ensure alignment between the Group's actual risk profile and the risk appetite defined by the Board of Directors, taking into account pre-established risk tolerance levels and in any event within the maximum admissible limits (risk capacity) deriving from regulatory requirements or other restrictions imposed by the Superviosry Authorities (e.g. the ECB's SREP Decisions).

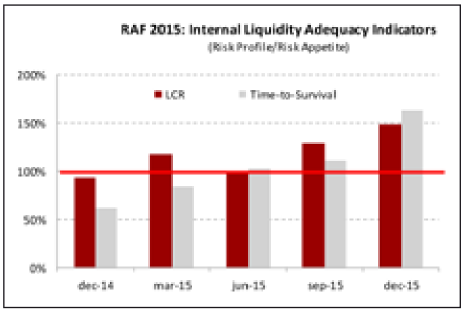
The RAF for 2015 involved the approval of a risk appetite by the Board of Directors and the implementation of an internal process aimed at identifying, defining, measuring and monitoring a number of Key Risk Indicators (KRI) at Group level. For each KRI, higher and more conservative target appetite thresholds compared to the minimum capacity thresholds were set ex-ante.

All RAF targets were met at the end of 2015. Moreover, several KRIs reflected values which were far higher than the established thresholds, especially those for short-term liquidity.

The tables below report a number of selected RAF indicators, where, - to ensure a like-for-like comparison – the values actually recognised for each quarter (risk profile) are seen against the corresponding target threshold (risk appetite); values exceeding 100% mean that risk appetite targets, and therefore the corresponding risk capacity values, have been exceeded.

Given also the capital strengthening transaction at the end of the first half of the year, the overall risk profile of the Montepaschi Group in 2015 was therefore in line with internal objectives and corporate strategy and the risk management and measurement systems were proven suitable for risk profile monitoring.





1.1 Risk Governance in the Montepaschi Group

The Group attaches the utmost importance to the process of identifying, monitoring, measuring, controlling and mitigating risks.

Risk governance strategies are implemented in line with the Group's business model, Business Plan medium-term objectives and legal and regulatory requirements.

Policies relating to the assumption, management, coverage, monitoring and control of risk are established by the Board of Directors of the Parent Company. In particular, the BoD regularly defines and approves the strategic risk governance guidelines and establishes the total risk appetite of the entire Group in line with the annual and multi-year projections.

In 2015, the Montepaschi Group further developed its internal framework for calculating risk appetite: the Risk Appetite Framework (RAF).

The objective of the RAF is to ensure the continuous alignment between the Group's actual risk profile and the risk appetite determined by the Board of Directors, taking into account pre-established risk tolerance levels and, in any event, within the maximum admissible limits (risk capacity) deriving from regulatory requirements or other restrictions imposed by the Supervisory Authorities.

The RAF takes into account all of the Group's key strategic areas:

- Pillar 1 and Pillar 2 Capital Adequacy;
- Short- and Long-term Liquidity Profile;
- Level of Financial Leverage;
- Risk-adjusted Performance, Reputation and Positioning.

The overall RAF system is broken down in terms of the Group's main Business Units and Legal Entities, also in terms of operating limits for the various business areas, and formalised in governance policies and processes for the management of the various corporate risks.

The Risk Appetite Process is structured so as to ensure consistency with the ICAAP and ILAAP as well as with Planning and Budget and Recovery processes, in terms of governance, roles, responsibilities, metrics, stress testing methods and the monitoring of key risk indicators.

Group Risk governance is provided centrally by the Parent Company's Board of Directors, which also supervises and is responsible for the updating and issue of internal policies and regulations in order to promote and guarantee a continuously greater and more widespread risk culture at all levels of the organisation. Awareness of risks and the correct knowledge and application of the internal processes and models governing those risks - especially for those validated for regulatory purposes - are fundamental requirements for effective, sound and prudent business management.

The incorporation of macro risk and risk-adjusted performance indicators, consistent with the RAF, within staff remuneration and incentive policies represents an additional tool to promote awareness of the conduct of all resources and the cultivation of a healthy risk culture.

The Montepaschi Group is among the Italian banks subject to the ECB's Single Supervisory Mechanism.

For a more thorough account of the Group's corporate governance structure and detailed information pursuant to Art. 435, paragraph 2 of the CRR, please refer to the Corporate Governance Report available on the Group's website at (http://www.mps.it/investors/corporate-governance).

1.2 Internal Control System and Risk Management Process

The general framework of controls within the Group is internally regulated by the Internal Controls System Policy, which defines a set of rules, functions, structures, resources, processes and procedures to ensure the sound and prudent management of the company.

The **Internal Controls System** plays a crucial role within the organisation in that it:

- constitutes a key source of knowledge for the Corporate Bodies to ensure full situational awareness and effective Corporate risk management;
- directs the changes in strategic guidelines and company policies and ensures the consistent alignment of the organisational framework;
- monitors the efficiency of operational systems and compliance with prudential supervisions requirements;
- it promotes a culture of risk awareness, compliance with the law and the respect of corporate values.

Consequently, the Internal Controls System plays a strategic role for the Group and the issue of controls assumes an important position within the framework of corporate values, involving all levels of the organisation (governing bodies, business units/structures, hierarchical levels, staff) in developing and applying the logical and systematic methods for identifying, measuring, disclosing and managing risk.

The **risk management process** is designed to identify and correctly map all current and future risks that the Montepaschi Group incurs or may incur, model and meaure these risks, ensure an effective level of controls as well as an adequate flow of operational and management reporting, support the implementation of proper risk mitigation and management actions.

The fundamental principles of the Montepaschi Group's risk management process are based on a clear-cut distinction of the roles and responsibilities of the different functions at first, second and third-levels of control and include the Business Functions.

The Board of Directors of the Parent company is responsible for defining and approving strategic guidelines and risk management policies and, at least once a year, quantitatively expresses the Group's overall risk appetite in terms of Internal Capital.

The Board of Statutory auditors and the Risk Committee are responsible for evaluating the level of efficiency and adequacy of the internal control Systems with particular regard to risk control.

The CEO/General Management is responsible for ensuring compliance with risk policies and procedures.

The Director in charge of the internal control and risk management system, appointed in compliance with the Corporate Governance Code for listed companies, is responsible for creating and maintaining an effective system of internal control and risk management.

Specific management committees responsible for risk issues have been established in order to promote efficiency and flexibility in the decision-making process and facilitate interactions between the various corporate departments involved:

- The Risk Management Committee establishes risk management policies and ensures overall compliance with the limits defined for the various operating levels. It is responsible for assessing initiatives for capital allocation and submitting them to the Board of Directors as well as assessing risk profile and, therefore, capital consumption (Regulatory and Internal) at both Group level and individual Group company level. The Risk Management Committee also analyses the risk-return performance indicators;
- The Finance and liquidity committee of the Parent company has the task of setting the principles and providing strategic guidance for Proprietary Finance. Furthermore, it deliberates and submits proposals concerning the interest rate and liquidity risk exposure of the banking book and defines capital management actions required;
- The Credit, Credit Policies and Credit Assessment Committee formulates credit process guidelines and expresses an opinion, at least once a year, on credit policies by verifying their commercial sustainability and consistency with risk appetite levels. At least once a year, it approves company policies pertaining to credit assessment, including for the purpose of subsequent reporting in the financial statements;
- In the exercise of its delegated powers, the Significant Loans Committee is responsible for decisions concerning the provision of credit facilities and the management of problem loans and assets.

Five permanent and independent Corporate Control Functions (CCFs) have been set up within the Internal Controls System:

- Compliance;
- Risk Management;
- I• nternal Validation;
- Anti-Money Laundering;
- Internal Audit.

To ensure the proper implementation of activities carried out by the Corporate Control Functions (CCFs), the Montepaschi

Group has identified the following basic requirements to be complied with by each CCF:

- Appointment and Dismissal of the Head of each CCF by the corporate governing bodies;
- Independence and authority: the Heads of the CCFs are placed in appropriate hierarchical, functional positions. They have no direct responsibility for the operating areas subject to control, nor are they hierarchically subordinate to the Heads of these areas;
- Separation of duties: the impartiality and independence of the various CCFs are ensured by their organizational segregation;
- Resources: the CCFs have the authority, resources (including financial resources, which may be independently managed with period reporting to the Corporate bodies) and skills required to perform their duties;
- Remuneration: In order not to compromise the impartiality and independence of the Heads of the CCFs, their remuneration is decided on by the corporate governing bodies by way of a specific incentive system that differs from the one established for the other corporate functions. The incentive system is based on duty-related objectives and not on the achievement of corporate targets.

As part of the internal control system, third-level controls are carried out by the Internal Audit Division, second-level controls by the Risk Management Division and Compliance Area and first-level controls by the Business Control Units (BCUs).

The Internal Audit Division, which reports directly to the BoD, performs an independent and objective "assurance" and advising activity, aimed both at monitoring operations compliance and risk trends (including through on-site audits) as well as assessing the efficiency of the overall internal control system in order to improve the effectiveness and efficiency of the organisation.

The **Risk Division**, which reports directly to the CEO, includes a risk management department, an anti-money laundering department and an internal validation department. This Division therefore has the following tasks:

- guarantee the overall functioning of the risk management system;
- verify capital adequacy based on the ICAAP and liquidity adequacy based on the ILAAP process;
- participate in the definition and control of the Risk Appetite Framework (RAF);
- ensure that significant transactions are consistent with the RAF;
- define strategic policies for the loan portfolio;
- perform the internal validation duties;
- perform the anti-money laundering duties required by Law;
- ensure the necessary reporting flows to the Group's Corporate Bodies and Top Management.

The task of the **Compliance Area** is to monitor the Parent Company's compliance with regulations. The department is directly responsible for managing risks relating to the violation of the most significant rules in bank-customer relations and it periodically reports to the company's top management and supervisory authorities regarding the overall state of compliance of the Bank's systems and operations. In accordance with supervisory provisions, the Compliance function has been incorporated under the Risk Division and reports directly to the CEO.

Outer **Business Control Units (BCU)**, which are internal to the Group subsidiaries or the main business areas of the Parent company, carry out compliance checks on transactions and are the first level of organisational supervision of operations within the more general system of internal controls.

In compliance with the requirements of autonomy and independence of each participating function, there is also a Function Coordination Committee with control responsibilities. The Committee promotes and shares operational and methodological aspects to identify possible synergies in control activities carried out by second and third-level Functions, coordinate methods and timing for planning and reporting to the Corporate Bodies and project initiatives connected with the Internal Control System, and share areas for improvement identified by all Functions with control responsibilities as well as the Supervisory Authorities.

In 2015, the **Staff Regulatory Relationship**, reporting directly to the CEO, was also established for the centralized oversight of the management of relations with and assessments by the Supervisory Authorities, coordinating and monitoring the planning of commitments undertaken and the main lines of development in the Eurpean regulatory framework.

1.3 Principal Covered Risk Factors and Internal Models for regulatory purposes

The main types of risk incurred by the Montepaschi Group in its day-to-day operations can be summarised as follows:

- credit risk;
- market risk (Trading Book + AFS);
- operational risk;
- Banking Book interest rate risk;
- counterparty risk;
- real estate risk;
- issuer risk;
- concentration risk;
- equity investments risk;
- strategic risk;
- liquidity risk;
- reputational risk.

Risks inherent in investment products/ services for the Group's customers are also monitored, to protect the customer and prevent any potential repercussions in terms of reputation.

Each risk factor corresponds to a model that has been developed and is used internally for operational or regulatory purposes. For an account of strategies, processes and management models for the various risks, please refer to the paragraphs below.

From a regulatory standpoint, in accordance with the principles contained in the New accord on capital adequacy (Basel 2) in relation to First Pillar risks, in the first half of 2008, the Montepaschi Group completed its work on the internal models for credit and operational risks. Pursuant to circular letter 263/2006 of the bank of Italy, on 12 June 2008 the Montepaschi Group was officially authorised under regulation no. 647555 to use the advanced models for the measurement and management of credit risk (AIRB - Advanced Internal Rating Based) and operational risk (AMA – Advanced Measurement Approach) as of the first consolidated report at 30-06-2008. Over time, these models have been further developed and their scope of application extended to Group entities not originally included in the initial scope of validation. As at 31-12-2014, the following portfolios/ entities of the Montepaschi Group had been validated for regulatory purposes:

Credit Risk: regulatory treatment

Legal Entity	Corporate AIRB	Retail AIRB
Banca MPS	PD, LGD	PD, LGD
MPS CS	PD, LGD	PD, LGD
MPS L&F	PD, LGD	PD, LGD

The Group has adopted the standard approach for the remaining credit risk exposures/entities for regulatory purposes.

Operational Risk: regulatory treatment

Legal Entity	AMA	BIA
Banca MPS	✓	-
MPS CS	✓	-
MPS L&F	✓	-
COGMPS	✓	-
Other Entity	-	✓

The Group has adopted the standard approach to calculate capital requirements relative to market risk. Instead, capital requirements relating to counterparty risk are calculated using the current market value for OTC derivatives and long settlement transactions (LST) as well as the comprehensive method for securities financing transactions (SFT).

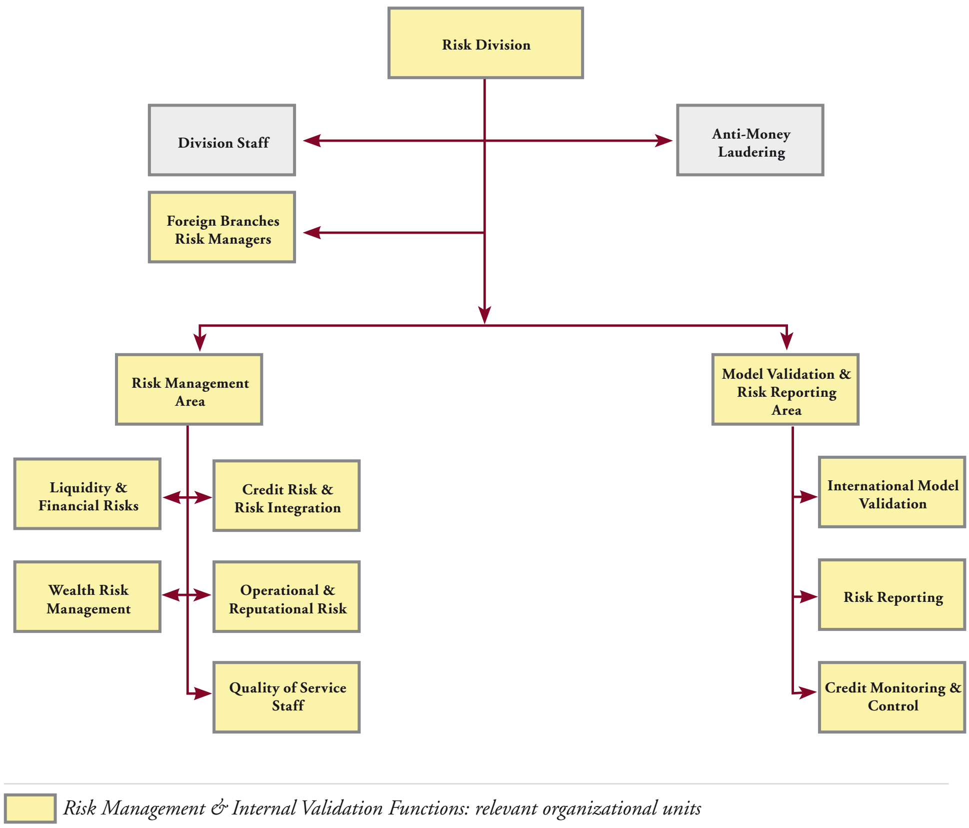
1.4 Organization of the Risk Management Function

In the course of 2015, the Risk Division was subject to further organisational changes aimed at achieving regulatory compliance, strengthening its role, powers and headcount and streamlining its structure in line with the growing importance of risk management and control within the Montepaschi Group.
As at 31 December 2015, the Risk Division was organised into the following structures:

- Risk Management Area,
- Risk Reporting and Validation Area,
- Anti-Money Laundering Area,
- Risk Division support staff.

As it currently stands, the Risk Division includes all second-level Corporate Control Functions, with the exception of the Compliance Function, as established by Supervisory Regulations regarding the Internal Controls System.
Autonomy and independence are ensured through relational mechanisms and functional connections with the Corporate Bodies having duties of strategic supervision, management and control.
In particular, the Head of the Risk Division of the Parent Company is appointed/ removed by the BoD, on the advice of the Risk Committee, with the support of the Appointments Committee, and having obtained the opinion of the Board of Statutory Auditors.
The remuneration of the Head of the Risk Division of the Parent Company is determined by the BoD, on the proposal of the Appointments Committee, having heard the opinion of the Risk Committee and having consulted with the Board of Statutory Auditors.
In addition to being the Head of the Risk Management Function, the Head of the Risk Division oversees the coordination of all the second-level Corporate Control Functions with a view to optimising the flow of information between the Functions, supports the planning of control activities and facilitates the implementation of remedial actions.

In this document, the Risk Division structures relevant for the identification of the **Risk Management Function** and **Internal Validation Function** are represented by the Head of the Risk Division, the Risk Management Area structures and the Validation, Monitoring and Risk Reporting Area.


Risk Division
Division Staff
Anti-Money Laudering
Foreign Branches Risk Managers
Risk Management Area
Model Validation & Risk Reporting Area
Liquidity & Financial Risks
Credit Risk & Risk Integration
Wealth Risk Management
Operational & Reputational Risk
Quality of Service Staff
International Model Validation
Risk Reporting
Credit Monitoring & Control
Risk Management & Internal Validation Functions: relevant organizational units

The Parent Company's **Risk Management Area** (hereinafter RMA) oversees and monitors overall risk for the Montepaschi Group. The Risk Management Area develops and implements the operational and regulatory systems for the measurement of both proprietary risk and customer-related risks, assessing compliance with and adequacy of mitigation measures. The Area also oversees the development of internal and regulatory risk measurement models and systems in order to determine internal operational capital and regulatory capital requirements, based on the existing regulatory options.

The Risk Management Area also oversees criteria for verification of MiFID compliance for investment products and services offered to customers, as well as those for risk and performance measurement and monitoring of products and portfolios held by customers.

As at 31 December 2015, the Risk Management Area was structured into the following segments:

- Credit Risk and Risk Integration Service;
- Liquidity and Financial Risk;
- Operational and Reputational Risk;
- Wealth Risk Management Service;
- Risk Management Quality Monitoring staff, whose duty it is to support the Area Head in cross-divisional activities.

Credit Risk and Risk Integration has the task of:

- defining, developing and updating models (PD, LGD, EAD, Maturity and haircuts) for the measurement of credit risk, by monitoring the internal model in compliance with qualitative and quantitative requirements provided for by the Supervisory authorities;
- monitoring Credit VaR measurements for each individual business unit and at Group level;
- quantifying the effects of expected and unexpected loss on credit risk and therefore on absorbed internal capital of the Group portfolio and of the individual business units and proposing corrective actions, considering the effects of mitigation actions;
- defining, developing and updating the methodologies underlying the various internal management models inherent in the Group's counterparty risk profile;
- overseeing and validating the production of counterparty risk measures at the level of individual business units, Group companies and at Group-wide level;
- defining, developing and updating the internal model of exposure to counterparty risk, in accordance with the qualitative and quantitative requirements set by the Supervisory Board;
- determining the internal capital measure used to calculate risk-adjusted performance measures;
- defining the strategic guidelines for the loan portfolio and direct the Group's lending activities;
- overseeing the calculation of collective loan impairments for subsequent recognition in the Balance Sheet;
- participating in the process to define the Group's overall Risk Appetite;

- developing and maintaining the methodologies used for identifying and mapping the Group's significant and non-significant risks, both by individual business units and legal entities, for the purpose of risk integration and support to the ICAAP process;
- measuring risks for the Group and individual business units;
- defining, developing and updating the risk integration models used to quantify the overall Internal capital;
- developing and implementing, from an operational point of view, Pillar 2 stress and scenario testing methodologies, supporting and coordinating forecast scenario methodologies for the ICAAP process;
- measuring the overall internal capital allocated to -and absorbed by- individual legal entities, business units and the Group (current, prospective and under stress conditions);
- reconciling internal and regulatory capital requirements for the pertinent individual risks;
- assessing the risk components of products during the design phase of new product development;
- a ssessing the appropriateness of risk adjusted industrial pricing, singling out the main risk components of products for the company; assessing Significant Transactions;

coordinating credit risk management and mitigation activities as well as all Stress Tests.

Liquidity and Financial Risks has the task of:

- defining, developing and updating the methodologies underlying the various internal management models inherent in the Group's market and counterparty risk profile;
- monitoring and validating the production of market risk measurements for each business unit, Group company and for the Group as a whole;
- defining the structure of operating limits for market and counterparty risk in compliance with the Group's risk measurement system and for the purpose of financial instruments holding, by verifying the methodological alignment of their overall structure with the Group's risk objectives;
- monitoring the limits established by the board of directors of the Parent company in relation to market and counterparty risk at all delegated levels and verifying the application of corrective actions taken due to any overdrafts or other vulnerable factors that emerge when monitoring risk;
- defining risk assessment and measurement methods for new financial instruments (product approval process);
- defining, determining and validating the methodologies chosen for aspects relating to the fair value of financial instruments traded by the Group: valuation models, usage criteria and hierarchy of pricing sources, rules, variables and methodologies feeding into market

parameters, criteria and rules for fair value hierarchy classification;

- controlling and validating the designation at fair value of financial instruments contained in the Trading Book and in the financial assets of the Banking Book;
- ontrolling and validating the market parameters used to assess and measure the risk of financial instruments held by the Group;
- validating P&L data at mark-to-market;
- defining, developing and updating the internal Trading Book market risk model for regulatory purposes in compliance with qualitative and quantitative requirements set out by the Supervisory authorities;
- quantifying market risk scenario analyses and stress tests for operational and regulatory purposes;
- c• arry out financial checks over the activities of business units;
- defining, developing and updating the risk measurement models inherent in the Group's interest rate and liquidity risk (ALM Banking Book);
- measuring the Liquidity regulatory indicators (LCR, NSFR);
- measuring the exposure to interest rate and liquidity risk, monitoring compliance with operational limits and implementing all appropriate actions to achieve overall optimisation, based also on appropriate scenario analyses;
- supervising the ILAAP;
- quantifying the scenario analyses and stress tests on market, ALM and liquidity risk.

Operational and Reputational Risks has the task of:

- defining, developing and updating operational risk measurement models, with the internal model being monitored against the qualitative and quantitative requirements set out by the Supervisory authorities;
- coordinating the data collection process for operational losses, the risk assessment process as well as the process used to identify the more critical operational areas on the basis of scenario analyses;
- monitoring the measurements of internal capital in relation to operational risks for each business unit and for the Group in its entirety (Operational VaR);
- quantifying the effects of the Group's operational-risk mitigating actions on absorbed internal capital;
- defining, implementing, managing and updating the mathematical/statistical algorithms underlying the various measurement models and quantifying the scenario analyses and stress tests on operational risks;
- defining mitigation strategies and coordinating the development of IT risk models;
- identifying reputational risks inherent in the overall range of Group activities;
- developing models to monitor 'other' Second Pillar measurable 'risks';
- developing statistical-mathematical risk models partly in support of other organisational units.

Wealth Risk Management has the task of:

- defining metrics to assess and monitor the risk/performance of investment products, portfolios and services offered to customers;
- defining and developing methodologies and models to assess risk and performance of investment products, portfolios and services, making sure they are measured and monitored over time;
- defining and developing methodologies for verifying the appropriateness / adequacy of investment products, portfolios and services, so as to ensure consistency between the customer's risk profile and the risk profile of the financial instruments;
- assigning a risk class to products on offer by the Group in addition to other parameters which are relevant for adequacy checks;
- ensuring that all products invested in on the customer's initiative be assigned a risk class and measured against any other parameters required for adequacy checks;
- periodically compiling and updating the list of highest-risk companies/issuers (a.k.a. "MLR list"), whose financial instruments are deemed ineligible and inappropriate to be offered on an advisory basis;
- defining and monitoring the risk/performance framework of operational limits applied to products, portfolios, wealth management lines, customer segments, etc.
- performing checks to monitor customer operations (operating limits, concentration, "gaps", etc.);
- monitoring changes in the risk class of investment products/services for the purpose of disclosure to customers;
- performing checks and monitoring activities on operations by customers of the Financial advisory Network;
- preparing the relative management and operating reports.

The Parent Company's **Validation, Monitoring and Risk Reporting Area** (hereinafter, **VMRRA**) continuously verifies the reliability of results obtained from the advanced risk measurement systems as well as their constant alignment with regulatory requirements. It prepares the required disclosure and management disclosure on risks. It performs second-level controls on the Group's credit exposures.

As at 31 December 2014, the VMRRA was organised into the following structures:

- Validation and Monitoring Service;
- Risk Reporting Service;
- Credit Exposures Control Service.

The **Internal Validation** Function has the task of:

performing the internal validation procedure on the Internal Rating System and preparing the annual report on the Internal Credit Risk Model for regulatory purposes, to be submitted for approval by the Boards;

- performing the internal validation procedure and preparing the annual report on the Internal Operational Risk Model for regulatory purposes, to be submitted for approval by the Boards;

- performing the internal validation procedure on the other risk models not used for regulatory purposes;
- analysing results from the efficiency testing of advanced systems and evaluating the adequacy of any remedial actions to be implemented.

The **Risk Reporting** Function has the task of:

- defining and monitoring the methods and modes used to produce disclosure on Group risk;
- coordinating and preparing the Pillar 3 Disclosure Report;
- coordinating, preparing and drawing up risk disclosure for official, external purposes (e.g., Budget, European Commissions, Rating Companies);
- coordinating and preparing Group Risk Disclosures for the governing bodies;
- monitoring and guiding risk management regulations and serve as liaison with the General Secretariat and Director in charge of risk management controls.

The **Credit Exposures Control Function** has the task of:

- carrying out second-level monitoring and control activities on credit exposures;
- expressing an opinion regarding the qualitative and quantitative compliance of the loan portfolio and, where necessary, triggering or initiating remedial actions for areas not deemed adequate.

The Risk Division of the Parent Company, which, as illustrated above, carries out Risk Management and Internal Validation Functions had an overall headcount of 121 units as at 31 december 2015. Staff had an average age of 39 and an average seniority in the banking sector of approximately 12 years. Resources show to have taken professional paths also outside

the risk management area with significant experience gained in Group credit, finance, planning and sales functions. In terms of academic background, there is a prevalence of degrees in Economics/Banking/Business subjects (55%), followed by degrees in Mathematics/Statistics (14%), Engineering (9%), Physics and IT (4%), qualifications, diplomas or degrees in other subjects

(15%). The majority of resources hold a post-degree qualification (Masters or Phd) or an international professional certification (e.g. FRM certification issued by GARP).

1.5 Credit Risk

The Budgeting, Planning, Capital and Risk Management processes of the Montepaschi Group are based on the "Risk Adjusted Performance Management" (RAPM) logic. In the development of these management processes, the definition of adequate credit policies – under the responsibility of the Parent company's credit management area – plays a relevant role which finds its operational expression in the implementation of the strategies (i.e. credit portfolio quality objectives), to be applied to the credit processes.

The Montepaschi Group's strategies in risk management mainly aim at limiting the economic impact of default on the loan book, exploiting, in particular, the full potential of the internal rating models and loss given default estimates. Strategies are defined on a yearly basis, together with the definition of Risk Appetite, except as otherwise provided under exceptional circumstances due to external conditions, and are identified for two main areas:

- loan disbursement strategies (definition of quality targets for access to credit);
- credit monitoring strategies (definition of minimum quality targets for maintenance of the loan disbursed).

The definition of customer acceptance policies, based on the analysis of the customer's prospective solvency, plays a major role in loan disbursement strategies. Only after having identified the customer with the required creditworthiness are other credit risk mitigation factors (guarantees) taken into account. Information on client quality and transaction risk is essential in identifying the decision-making body for loan granting.

The follow-up strategies are based on systems used on a daily/monthly basis to detect changes in the customer's risk profile. The identification of events likely to affect credit risk triggers a set of obligations for the distribution network, who is assigned the key task of keeping communication channels with the customer open and obtaining all useful information needed to verify the changes in the credit risk profile. If changes are confirmed, the client account manager is supported by personnel specialised in credit quality management and legal matter to define the credit risk management procedures required.

The quantitative identification of credit risk is mainly applied, at operational level, to the measurement of the risk-adjusted return of each individual operating unit. This process is carried out with operational control instruments. The credit risk identification and quantification instruments allow the Montepaschi Group to define hedging policies mainly consisting in defining "risk-adjusted pricing" which includes risk coverage and planned 'return on capital'.

Risk mitigation policies are defined as part of the Credit Risk Mitigation (CRM) process, whereby the legal, operational and organisational conditions necessary to use collateral guarantees for credit risk-mitigation purposes are identified and met. Three sets of guarantees complying with mitigation requirements are defined in the process: Personal securities, Financial collaterals and mortgage collaterals. Other types of credit protection guarantees do not mitigate credit risk. With specific regard to collaterals, a system has been developed to monitor the value of the collateralised asset, based on the measurement of market value (daily for securities and annual for real estate).

Within the credit-granting process, the Montepaschi Group has adopted a risk adjusted system for borrower identification, which is sensitive to the customer's rating and to the presence of collaterals. Should the value of the collateralised asset be subject to market or foreign exchange rate risk, a "safety margin" is used, i.e. a percentage of the end-of-period value of the collateral pledged, which is a function of the volatility of the collateralised asset. The only portion of the loan covered by the value of the assets net of the differential is considered as guaranteed during the approval phase. In the monitoring stages, an adjustment is required on guarantees for which the market value results as being lower than the authorized value net of the safety margin; notification of this step is channelled into the implementation process of the credit monitoring strategies. For further insight into risk

mitigation Techniques, see Paragraph 5.5 below.

Credit Risk Management policies and disbursement processes are governed by specific Group directives. Credit risk analysis is performed internally for operational purposes using the Credit Portfolio Model, developed within the Parent Company, which produces detailed outputs in the form of traditional risk measures such as Expected and Unexpected Loss, both operational (intra-risk diversified with a time horizon of one year and a confidence interval calibrated to the target rating of the Group itself) and regulatory. There are several inputs: probability of default (PD), obtained through validated and non-validated models, LGD rates (operational and regulatory), number and types of guarantees supporting the individual credit facilities, regulatory and operational CCFs on the basis of which regulatory and operational EAD are estimated.

In accordance with the provisions of the Second Pillar of Basel 2, the Montepaschi Group is committed to the continuing development of methodologies and models in order to assess the impact on the loan book of stress conditions produced using sensitivity analyses with respect to individual risk factors or through scenario analyses.

Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Committee, Top Management and Corporate Governing Bodies.

For further information, especially regarding the Internal AIRB Model, please refer to Paragraph 5.3.

1.6 Operational Risk

The Montepaschi Group has adopted an advanced management system for operational risk, with the aim of guaranteeing effective risk prevention and mitigation measures.

The risk management system consists in a structured process which identifies, assesses and monitors operational risks. This process is defined in the Group's Operational Risk Governance and Control Directive.

The operational risk management system adopted by the Group is divided into the following macro-processes:

- identification,
- measurement,
- monitoring,
- management and control,
- maintenance,
- internal validation,
- review.

Each process is clearly documented and is subject to the responsibility of a specific corporate function. The organizational units of the various Group subsidiaries are also involved in the processes.

Corporate policies and procedures assign the task of operational risk control to the risk management area. As previously illustrated, the Operational and Reputational risks Service has been set up within this area and is responsible for:

- defining, developing and updating operational risk management and measurement systems;
- coordinating data collection and storage systems;
- the reporting system on operational risks;
- assessing the operational risk profile and measuring the relative capital adequacy requirements at both individual and consolidated levels;
- ensuring operational supervision of IT and reputational risk.

The management and measurement model designed and implemented by the Montepaschi Group incorporates the following four components:

- internal data on operational loss;
- external data on operational loss;
- factors regarding the operating context and the internal controls system;
- scenario analysis.

Classification of this data adopts the event and business line model established by the Basel accord and adds further classifications such as process, organisational unit, geographical area etc. The bank has defined a loss data collection (LDC) process aimed at collecting and storing operational risk data: this includes both information relating to the four components strictly provided for by the measurement system and other information considered significant for operating purposes.

The loss data collection process has been designed to ensure that data is complete, reliable and up-to-date and, therefore, that the management and measurement system using it is effective.

The single operational risk management application and the related database are also subject to business continuity and disaster recovery plans.
As far as the external data on operational loss is concerned, the Montepaschi Group has opted for a strongly prudential approach. External data derives from the Italian Operational losses database (Italian:
DI PO) consortium to which the Montepaschi Group has belonged since its founding in 2003. In addition to the complete utilization of external loss data, the DI PO is also used for methodological purposes and for resolving any doubts in interpretation.
The analysis of contextual and control factors identifies the operational vulnerabilities to which the bank is exposed. In order to provide greater granularity of analysis, which is carried out with the individual process owners through annual self-assessments of operational risk control, the identification of vulnerabilities is a prospective evaluation aimed at highlighting the difficulties inherent in day-to-day operations.
Lastly, the Montepaschi Group carries out scenario analyses for its Top management on a yearly basis: the forward-looking analyses are aimed at measuring - in terms of capital - exposure to individual vulnerabilities with a view to capturing developments in the business and organisational framework.
To ensure the correct application of this methodology and its compliance with current regulations, the operational risk internal validation process has been allocated to the Validation, Monitoring and Risk Reporting Area. The quality of operational risk management and measurement systems is assessed on an ongoing basis as is their compliance with regulatory provisions, company needs and trends in the market of reference. Within this framework, it is also particularly important not only to verify the reliability of the methodology used in calculating capital adequacy, but also to ascertain the actual use of this system in decision-making processes as well as in the daily operational risk management systems.
Furthermore, the risk management area is in charge of producing reports on the operational risk measurement and control system, both for internal units and Supervisory authorities.
Each macro-process in which the system is structured produces its own report within a wider reporting framework. By defining a grid of contents, recipients and frequency of updates, the objective of this activity is to ensure timely horizontal and vertical communication of information on operational risks among the different corporate units concerned.
Corporate regulations allocate the activity of internal auditing to the Internal Audit Division. This consists in periodic checks on the overall functioning of the Montepaschi Group's operational risk management and control systems, so as to achieve an independent, comprehensive adequacy assessment in terms of efficiency and effectiveness. Once a year, the Internal Audit Division compiles a report updating the

various company entities on the auditing activities carried out, specifically highlighting vulnerabilities identified, corrective measures proposed and related findings.
Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Management Committee, Top Management and Corporate Governing Bodies.
For more insights on operational risk, see also the following Chapter 12.

1.7 Market Risk in the Trading Book

The Montepaschi Group's Regulatory Trading Portfolio (RTP), or Trading book, is made up of all the Trading books managed by the Parent bank (BMPS), MPS Capital Services (MPSCS). The portfolios of the other retail subsidiaries are immune to market risk since they only contain their own bonds held to service retail customers. Trading in derivatives, which are brokered on behalf of the same customers, also calls for risk to be centralised at, and managed by MPSCS.
Market risks in the trading book are monitored in terms of Value-at-Risk (VaR) for operational purposes. Market risk assumption, management and monitoring are governed group-wide by a specific resolution approved by the board of directors. The Group's Finance and liquidity committee is responsible for directing and coordinating the overall process of managing the Group's proprietary finance thereby ensuring that the management strategies of the various business units are consistent.
Operating limits to trading activities are defined and set by the board of directors of the Parent company, in consistency with the Risk Appetite, and are expressed by level of VaR delegated authority, which is diversified by risk factors and portfolios, and in terms of monthly and annual Stop loss. The limits are monitored on a daily basis.
In addition to being included in VaR computations and in respective limits for the credit spread risk component, *Trading book* credit risk is also subject to specific operating limits of issuer and bond concentration risk, which specify the maximum notional amounts by type of guarantor and rating class on all investments in debt securities (bonds and *credit derivatives*).

Referring to the Parent Company specifically, the business area entrusted with trading activities is the Finance, Treasury and Capital Management Area (FTCMA), which reports directly to the Chief Executive Officer. Trading activities for MPSCS are performed by the Global Markets Division.
The Business Units manage a proprietary

portfolio which takes trading positions on interest rates, credit, shares, indices, commodities and foreign exchanges. In general, interest rate positions are taken by purchasing or selling bonds, and by creating positions in listed derivatives (futures) and OTCs (IRS, swap options). Trading is carried out exclusively on the Bank's own behalf, with objectives of absolute return, in compliance with the delegated limits of monthly and yearly VaR and Stop Loss.
In particular, the FTCMA operates in the short-term portion of the main interest rate curves, mostly through bonds and listed derivatives.
With regard to credit risk in the trading book, the equity positions are generally managed through the purchase or sale of bonds issued by companies or by creating synthetic positions in derivatives. The activity is oriented to achieving a long or short position on individual issuers, or a long or short exposure on specific commodities. The activity is carried out solely on the Bank's own behalf with objectives of absolute return and in compliance with other specific issuer and concentration risk limits approved by the Board of Directors.
The Montepaschi Group's Trading Book is subject to daily monitoring and reporting by the Parent Company's Risk Management on the basis of proprietary systems. VaR for management purposes is calculated separately from the operating units, using the internal risk measurement model implemented by the Risk Management function in keeping with international best practices. However, the Group uses the standardised methodology in the area of market risks solely for reporting purposes.
Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Management Committee, Top Management and Corporate Governing Bodies.
For further quantitative details on market risk, please refer to Chapter 7.

1.8 Counterparty Risk

Counterparty risk is linked to potential losses due to the default of counterparties in financial transactions prior to settlement and is associated with financial instruments which have a positive value at the time of counterparty's default. The financial instruments which point to this kind of risk:

- generate an exposure that is equal to their positive fair value;
- have a market value which evolves over time depending on underlying market variables;
- generate an exchange of payments or an exchange of financial instruments or goods against payment.

The prudential treatment of counterparty risk is applied to the following types of financial instruments:

- credit and financial derivative instruments traded Over The Counter (OTC derivatives);
- Securities Financing Transactions (SFTs), such as: repos and reverse repos on securities or commodities, securities or commodities lending or borrowing transactions and borrowing on margin;
- Long Settlement Transactions (LSTs), such as: forward transactions in which a counterparty commits to delivering (receiving) a security, commodity or foreign currency against receipt (delivery) of cash payment, other financial instruments or goods with settlement upon a pre-established contractual date, later than the one determined by market practice for these types of transaction.

The scope of measurement for counterparty risk includes all banks and subsidiaries belonging to the Group and refers to positions held in the Banking Book and the Trading Book. As referred to in the Supervisory regulations, when measuring exposure to counterparty risk, the Montepaschi Group adopts the regulatory market value method to determine the Exposure at Default (EAD) for OTC and lST transactions and the comprehensive approach to calculate EAD for SFT transactions.

Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Committee, Top Management and Corporate Governing Bodies.

For further quantitative details on counterparty risk and related management processes, please refer to Chapter 6.

1.9 Interest Rate Risk in the Banking Book

In accordance with international best practices, the Banking Book refers to all of the commercial operations of the Parent bank in relation to the transformation of maturities of balance-sheet assets and liabilities, Treasury, foreign branches, and hedging derivatives of reference. The scope of the Banking Book (in line with that for the regulatory book) and the ALM centralisation process are defined in a resolution by the board of directors of the Parent bank which sets rules for centralized Asset & Liability Management and operating limits for the interest rate risk of the Group banking book. It is to be noted that the banking book also includes active bonds held for investment purposes, classified as either AFS or L&R. The same ALM rate risk metrics of measurement used for other commercial accounts were also applied to this aggregate.

The operational and strategic choices for the Banking Book, adopted by the Finance and Liquidity committee and monitored by the Risk Management Committee of the Parent bank, are based first on exposure to interest rate risk by a variation in the economic value of the banking book assets and liabilities and Net Interest income analysis, applying different scenarios on rate curves.

The Group adopts a rate risk governance and management system which, in accordance with the provisions of the Supervisory authority, avails itself of:

- a quantitative model, which provides the basis for calculation of risk indicators for the interest rate risk exposure of the Group and Group companies/entities;
- risk monitoring processes, aimed at the ongoing verification of compliance with the operational limits assigned to the Group overall and to the individual business units;
- risk control and management processes, geared toward bringing about adequate initiatives for optimising the risk profile and activating any necessary corrective actions.

Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Management Committee, Top Management and Corporate Governing Bodies.

For further details on the methodologies developed in relation to the interest rate risk in the banking Book (Banking Book ALM) and related quantitative findings, please refer to Chapter 8.

1.10 Liquidity Risk

The Montepaschi Group structurally addresses liquidity risk with a formal LR management policy which also complies with the Basel 2, Pillar 2 requirements.

The Group adopts a liquidity risk governance and management system which, in accordance with the provisions of the Supervisory authority, pursues the following objectives:

- ensure the solvency of the Group and all its subsidiaries, both in 'business as usual' and in crisis conditions;
- optimise the cost of funding in relation to current and future market conditions;
- adopt and maintain risk mitigation instruments.

Within the above system, the following responsibilities are centralised in the Parent bank:

- definition of policies for Group liquidity management and liquidity risk control;
- coordination of Group policies' implementation by the companies included in the scope;
- governance of the Group's short-, mid and long-term liquidity position, both overall and at individual company level, through centralised operational management;
- governance of Group liquidity risk, both short- and long-term, ultimately guaranteeing the solvency of all subsidiaries.

In its steering function, the Parent bank therefore defines criteria, policies, responsibilities, processes, limits and instruments for managing liquidity risk, both in business as usual and in liquidity stress and/or crisis conditions, formalizing the Group's *Liquidity Risk Framework*.

The Group's Liquidity Risk Framework is intended as the set of tools, methodologies, organisational and governance setups which ensures both compliance with national and international regulations and adequate liquidity risk governance in the short and medium/long term, under business-as-usual and stress conditions.

Management of the Group's Operating Liquidity is intended to ensure the Group is in a position to meet cash payment obligations in the short term. The essential condition for a normal course of business in banking is the maintenance of a sustainable imbalance between cash inflows and outflows in the short term. The benchmark metric in this respect is the difference between net cumulative cash flows and Counterbalancing Capacity, i.e. reserve of liquidity in response to stress conditions over a short time horizon. From the extremely short-term perspective, during the year a system was formalised for the analysis and monitoring of intraday liquidity, with the goal of ensuring normal development during the day of the bank's treasury and its capacity to meet its intraday payment commitments.

Management of the Group's Structural

Liquidity is intended to ensure the structural financial balance by maturity buckets over a time horizon of more than one year, both at Group and individual company level. Maintenance of an adequate dynamic ratio between medium/long term assets and liabilities is aimed at preventing current and prospective short-term funding sources from being under pressure. The benchmark metrics, mitigated by specific internal operating limits set by the Board of Directors, include gap ratios which measure both the ratio of total loans over more-than-1-year and more-than-5-year maturity deposits and the ratio of loans to retail/corporate deposits regardless of their maturities. During the year, the Group defined and formalised the asset encumbrance management and monitoring framework with the goal of analysing:

- the overall degree of encumbrance of total assets;
- the existence of a sufficient quantity of assets that may be encumbered but which are free, with respect to what is defined in the Liquidity Risk Tolerance;
- the Group's capacity to transform bank assets into eligible assets (or in an equivalent manner, to encumber non-eligible assets in bilateral transactions).

The liquidity position is monitored under both business-as-usual conditions and under specific and/or system-wide stress scenarios. The exercises have the twofold objective of timely reporting the Bank's major vulnerabilities in exposure to liquidity risk and allowing for prudential determination of the required levels of Counterbalancing Capacity (liquidity buffer). During the year, intraday liquidity stess tests were also defined.

The Contingency Funding Plan, drafted by the Finance, Treasury & Capital Management Area, is the document which describes the set of tools, policies and processes to be enforced under stress or liquidity crisis conditions.

As part of the overall budgeting process and particularly within the scope of Risk Appetite, the Liquidity Risk Framework identifies the tolerance thresholds for liquidity risk, that is to say the maximum risk exposure deemed sustainable in a business-as-usual scenario and under stress conditions. The short/ medium and long-term liquidity risk limits derive from the setting of these risk appetite thresholds.

The short-term limit system is organised into three different levels that provide for a timely reporting of proximity to the operating limits, i.e. the maximum liquidity risk appetite set within the annual Risk Tolerance process.

In order to immediately identify the emergence of vulnerabilities in the Bank's position, the Group has developed a range of Early Warnings, classified as generic or specific depending on whether the individual indicator is designed to detect potential vulnerabilities in the overall economic context of reference or in the Group structure. The triggering of one or more early warning indicators is a first level of alert and contributes to the overall assessment of the Group's short-term level of liquidity.

The Group companies included in the scope of application, to the extent that they exhibit a liquidity risk deemed significant, are responsible for abiding by the liquidity policies and limits defined by the Parent bank and the capital requirements set by the relevant Supervisory authorities.

Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Management Division and submitted to the Parent Company's Risk Committee, Top Management and Corporate Governing Bodies.

1.11 Equity Investment Portfolio Risk

Equity investment risk is credit risk concerning exposures in equity instruments. To calculate Internal Capital against such exposures, Montepaschi Group has adopted the standardised approach, in line with the new methodological framework for estimating Internal Capital. This approach requires that exposures in equity instruments be assigned a risk weight of 100 % or 150% for particularly high risk positions, unless they are to be deducted from Own Funds.

Therefore, holdings included in the calculation are only those which do not fall under the system of deductions from Own Funds.

This system has been upgraded by the new supervisory rules (CRD4/CRR) which further expanded the scope of deductions to include non-significant investments in financial sector entities (<10%) and including indirect and synthetic investments along with direct investments. The new regulations also provide for exemptions from deduction. For non-significant investments in CET1 instruments, AT1 instruments and T2 instruments in other financial sector entities, the amount deducted is calculated by comparing the total aggregate with the exemption, which is then divided in proportion to the weight% of each type of investment on the total class of instruments and the amount of the exemption is weighted at 100% or 150% if high risk. For significant investments (>10%) in other financial sector entities, the new regulations provide for a double exemption (together with temporary non-convertible DTAs) in the calculation of the deducted amount and a risk weight of 250% of the amount not deducted.

The Internal Capital is quantified by the Risk Management Area of the Parent Company.

Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Management Committee, Top Management and Corporate Governing Bodies.

For further accounting details on risk in the Equity Investments Portfolio, please refer to Chapter 9.

1.12 Strategic Risk

Strategic Risk is defined as the risk linked to a potential downturn in profits or capital due to changes in the business framework or incorrect business decisions, inadequate implementation of decisions and lack of responsiveness to changes in the competitive environment.

The methodology applied for determining the Strategic Risk requirement is to simulate the impact of the failure to execute each of the significant assumptions contained in the business plan and obtain the requirement from the synthetic measurement of losses resulting from the various scenarios.

Internal Capital is quantified by the Risk Management Area of the Parent company.

Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Management Committee, Top Management and Corporate Governing Bodies.

1.13 Real Estate Risk

Real Estate Risk is defined as the risk of incurring potential losses from unexpected changes in the value of the real estate portfolio as a result of real estate market performance in general. Internal Capital for Real Estate Risk is represented by regulatory capital. The choice not to use internal models is the result of a general principle which the Montepaschi Group has decided to apply to all situations included from a regulatory perspective in Credit and Counterparty Risk.

The Internal Capital is quantified by the Risk Management Area of the Parent company.

Results from the analyses performed on this category of risk are regularly included in the more general flow of risk reporting produced by the Risk Division and submitted to the Parent Company's Risk Management Committee, Top Management and Corporate Governing Bodies.

1.14 Risk inherent in investment products/services and management of Reputational Risk associated with investment services

The risks associated with investment services are directly or indirectly reflective of the risks incurred by customers in the provision of investment services and activities.

Consequently, governance of these risks is aimed at protecting customers while preventing any potential repercussions on the Group in terms of operational and reputational risk.

Organisational responsibility at Group level for supervising financial risk measurement, monitoring and control activities and for mapping investment products/services for the purposes of MiFID adequacy is an integral part of the Group's integrated risk management responsibilities ans is centralized to the Wealth Risk Management Service within the Parent Company's Risk Division. This is to ensure centralised governance of the direct and indirect risks which the Group incurs during the course of its operations.

"Wealth risk management" focuses on the comprehensive set of operational and management processes as well as measurement and monitoring tools/methods used to ensure overall consistency between customers' risk profiles and the risk of investment products and portfolios offered to -or in any case held by- customers.

The main regulatory framework consists of the European MiFID and the relative implementation regulations (in particular, the Consob Regulation on Intermediaries no. 16190/2007). With regard to the third-level regulatory framework, Consob Communication no. 9019104/2009 (Level 3 - Illiquid financial products) plays an important role, along with the 2009 Inter-Association Guidelines on illiquid financial products, and Consob Communication no. 97966/2014 on the distribution of complex financial products to retail customers.

The investment products (of the Group and of third parties), whether or not included in the overall offering to the Group's customers, are mapped for risk on the basis of quantitative measurements of market and credit risk factors; liquidity and complexity assessments are also conducted on these products. Product mapping is one of the guiding criteria for carrying out investment adequacy checks as part of the consulting service offered.

For the sake of simplicity, investment product risk mapping, performed with reference to individual risk macro-factors, is grouped under specific risk categories.

A special focus is given by the Bank to the monitoring and prevention of potential financial and reputational risks which investment services, particularly in a context of financial crisis such as the one experienced over the last few years, may generate as a consequence of increased market volatility. The fast-moving and not always predictable market trends may result in rapid changes in product risks and generate potential financial losses, as well as prompting a changing attitude by customers towards their own financial investments.

Customers are regularly informed of changes in the risk of financial instruments held, so as to ensure timely informational transparency and facilitate possible decisions aimed at rebalancing the risk profile of their investments. .

Advisory services on offer, customer risk profile and risk of investment products/ portfolios

The strategic choice of the Banca MPS is to combine the placement of financial products with advisory so as to ensure the highest level of protection for the investor and, at the same time, enhance the role played by relationship managers. Again, with a view to protecting customers, the obligation to verify appropriateness has also been extended to the trading activities on the secondary market of the certificates issued by the Group.

Banca MPS offers two types of advisory services:

- "Basic" transactional advisory is aimed at verifying the suitability of the individual investments recommended in relation to the risk of the customer's investment portfolio as a whole. As part of this, the new transactional adequacy model was rolled out in early 2015 and essentially adopts a multivariate control logic on the individual risk factors, based on the customer's portfolio risk, including the investment product that is being recommended;
- "Advanced" advisory is instead aimed at verifying the suitability of the overall set of transactions, advising on them based on their impact on a suggested investment portfolio of the customer in order to obtain optimum asset allocation and maximised prospective returns over a certain time horizon, given the customer's risk profile.

Wealth risk management activities cover the entire distribution scope of the branch network of Banca MPS and investment services operated by Banca Widiba and MPS Capital Services.

Through its responses to the MiFID profiling questionnaire, the Customer provides the Bank with information on their particular characteristics and needs (including their investment objective, knowledge, experience and time horizon), which helps determine the customer's general risk profile.

1.15 Analysis of the Montepaschi Group's Internal Capital and Risk Integration Model

The Overall Internal Capital (or Overall Absorbed Capital) is the minimum amount of capital resources required to cover economic losses resulting from unforeseen events caused by the simultaneous exposure to different types of risk.
All of the types of risk mentioned above are involved in quantifying the Overall Internal Capital, with the exception of liquidity and reputational risk that, instead, are mitigated through organisational policies and processes.

The Risk Management Area regularly quantifies the Group's Internal Capital for each type of risk and periodically reports these to the Risk Management Committee and to the Governing Bodies as part of the reporting flows prepared by the Risk Division.
In the first half of 2015, some significant changes were introduced to the estimating's methods of Internal Capital. The main one consists of the move from a Pillar 2 approach to one known in the literature as "Pillar 1 Plus". In essence, the Pillar 1 requirements for Credit and Counterparty Risk and for Operational Risk, which already include the requirements relating to Issuer Risk on the Banking Portfolio (BP), Investment Risk and Real Estate Risk, are increased by the requirements from internal models relating to Market Risks, Banking Book Interest Rate Risk, Concentration Risk and Strategic Risk.
Overall Internal Capital is calculated without considering the inter-risk diversification, by directly adding together the contributions of the individual risks. This approach tends to incorporate the indications in the SREP (Supervisory Review and Evaluation Process) Guidelines document published by the EBA in December 2014.

1.16 Stress Test Analysis

In compliance with the guidelines set forth by the Basel committee and *best practices*, new prudential supervisory provisions for banks require credit institutions to carry out adequate *stress testing* exercises. *Stress testing* is commonly described as "the set of quantitative and qualitative techniques with which banks assess their vulnerability to exceptional but plausible events".
The objective is thus to evaluate the impact of a "state of the world" that is considered extreme, but which, despite a low probability of occurrence, may generate significant economic consequences for the Group.

Among the events considered plausible for the definition of tension-inducing scenarios, the following are to be taken into consideration:

- *trend-based scenarios:* assumptions are made of shocks that are due to a combination of risk factors which were historically observed in the past and whose recurrence and plausibility retain a certain degree of likelihood and recurrence;
- *discretionary scenarios:* assumptions are made of shocks due to a combination of risk factors which may emerge in the near future, depending on the foreseeable environmental, social and economic developments.

Under 'exceptional events', low-frequency circumstances are considered, whose occurrence would have an extremely serious impact on the banking Group. Within this area, the Montepaschi Group's methodological approach to *stress-testing* is based upon the identification of main risk factors whose objective is to select events or combinations of events (scenarios) which reveal specific vulnerabilities at Group-level.

To this end, specific *stress test* plans have been put in place for both individual stand-alone risks and joint risks – starting with the macroeconomic scenarios – on all First and Second Pillar Risks, as defined in the ICAAP and Risk Appetite Framework.

With regard to credit risk in particular, the Montepaschi Group has defined a macroeconomic regression model to estimate the variations in the Probability of Default as a function of changes in the main *credit drivers*. *Credit drivers* which significantly describe PD variations are identified beforehand.

On the basis of the regression model, credit driver disturbances are then estimated according to the current and prospective economic situation. The shock applied to the *credit drivers* determines the change in loan book PD, triggering the simulation of a hypothetical counterparty *downgrading*, with consequent risk variations in terms of Expected Loss, Unexpected Loss and Input from new Defaults.

With regard to Operational risk, appropriate historical scenarios are defined, which are relevant in terms of both *severity* and *frequency*. In this way, it is possible to evaluate the Group's vulnerability to exceptional events - in the case of severity -and plausible events, in terms of frequency.

As for market risk, stress tests consist in the definition of historical scenarios (main crises historically observed in international markets), or discretionary, isolating those components towards which the Group is particularly exposed and, therefore, more vulnerable. These stress events are applied and simulated upon Equity, Commodity, Credit Spread, Forex and interest rate on a daily basis.

In terms of Counterparty, Concentration and Issuer risk, a stress scenario has been defined that is consistent with the scenario used for credit risk. It is noted that a market stress event for EAD is also applied to counterparty risk based on a discretional scenario of changes in market drivers.

With regard to interest rate risk in the Banking Book, stress scenarios are defined and differentiated shocks are applied to the individual nodes of the curves for the terms of reference. The results from the stress tests are submitted to the Top Management and Board of Directors. They are formally examined by the BoD as part of the ICAAP annual report approval process, with a view to providing a self-assessment of the current and prospective capital adequacy of the Montepaschi Group.

1.17 The Risk Disclosure Process

The importance of formalising an adequate internal process for the communication of relevant data is explicitly required by national legislation and by the main international bodies for the purpose of increasing the awareness of corporate bodies with regard to risk management at banking group level.

With regard to the Risk Disclosure Process, the Montepaschi Group has, over the years, prepared an overall framework of reference, through the following organisational and governance solutions:

- creation of specialised structures within the Risk Division for the governance of risk disclosure (Risk Reporting Service);
- regulations governing the operations of the Parent company's Risk Management Committee, with the explicit intention to regulate communication to the BoD of the documents discussed and the major decisions taken;
- regulations envisaging adequate risk reporting to be incorporated, for internal and external purposes, in all major Group Policy concerning risk, internal models, Financial accounting and Public disclosure;
- Provision of specific reporting flows to the Chairman of the BoD, the Sub-Board Risk Committee, the Board of Statutory Auditors and the CEO, with a periodic summary submitted to the BoD. These reporting flows should be intended as forming part of the Risk Management Division's regular disclosure on risk control. In this way, the intention was to further reinforce the risk communication process towards the Group's senior management.

The Risk management division includes the Risk Reporting Service, who have the task of supervising, developing and coordinating the Group's risk disclosure model, through the identification of all relevant players, systems, processes and reports. The model is structured into two levels. At a first level:

- each Service of the risk management area produces and validates its own risk metrics based on its internal management models and autonomously governed procedures;
- each Service of the risk management area produces its own operating risk reporting for internal operating purposes (i.e. validation report, control of operating limits) and for reconciliation with the BUs.

On a second level, the Risk Reporting Service starts from results produced by the Risk Management Area and:

- summarises the management risk reporting for internal and external purposes;
- integrates the management risk reporting with "key risk messages" highlighting issues of particular/critical significance, for submission to the Top management and other corporate bodies;
- interfaces with investor relations, units under the relevant manager in charge/CFO, the General Secretariat and corporate affairs area on risk reporting issues.

The overall reporting framework includes at least one Group-wide report ("Risk Management Report"), with details of the following key items.

With regard to **Internal Capital**, analyses are carried out on a quarterly basis in order to:

- quantify and determine the absorption of the Montepaschi Group's diversified Internal capital by risk factor and Bank/BU;
- compare against previous periods;
- compare against budgeted risk appetite.

As far as credit risk is concerned, analyses are mainly conducted on the following:

- risks of the performing and defaulting loan portfolio by Legal Entity, Client Segment, Master Scale and Industrial Clusters;
- trends in the risks of the performing and defaulting loan portfolio;
- *quality breakdown* of the risks of the performing loan portfolio and composition of the defaulting loan portfolio;
- geographical and sectorial concentration analysis into different areas of economic activity.

With regard to **Assets & Liabilities Management and Liquidity risk**, the main analyses carried out relate to the following:

- impact on the economic value and on net interest income, by legal Entity, BU, curve bucket, technical form and currency;
- analysis of on demand accounts and related options;
- position of operational and structural liquidity;
- regulatory liquidity indicators;
- Liquidity Stress Test;
- monitoring of operating limits of interest rate and liquidity risks.

As for **Trading Book Market Risk**, analyses are mainly focused on:

- trends in the market risk profile of the Group's Trading book: operational Var and P&L analysis;
- Var disaggregation by legal Entity and risk Factor, diversified and non-diversified Var;
- main portfolio exposures; analysis of issuer risk;
- VaR actual backtesting;
- Stress test;
- monitoring of operating limits.

In terms of operational Risk, analyses are mainly conducted on the following:

- data on losses (quantitative information);
- major-impact losses tracked in the quarter and analysis of causes;
- operational VaR analysis on different regulatory event types.

In the course of 2015, a new section on the quarterly **Monitoring of RAF indicators** was developed, as required by regulations, policies and internal processes concerning the Risk Appetite Framework.

The Risk Management Report is regularly supplemented with specific monitoring activities on Risk in customer investment products/services (Wealth Risk Management). In particular, this section illustrates the risk profile of -and products held by- customers, according to the internal classification and service model adopted by the Montepaschi Group. Details of volumes under management or custody are provided, with a special focus on products included in MPS' active offerings. Portfolio advisory insight is also given into recommended optimal asset allocation as well as into the outcomes of portfolio adequacy checks and wealth management monitoring.

As needed, the Risk Management report is integrated with specific points/issues of attention (i.e. "ad hoc" simulations, Scenario analyses / Stress tests, etc.). The report also provides information with regard to progress made by the relevant units on main projects underway, as well as regulatory updates and in-depth reviews of primary topics of interest that, on a case by case basis, result as being of particular importance.

The basic contents of the report enable the Top Management and the Corporate Bodies to gain a sufficiently complete – though concise – overview of the Montepaschi Group's main risks, highlighting any possible vulnerabilities in the overall risk profile and its development over time, risk concentration in specific segments or business units, tensions in terms of 'erosion' of the operating limits delegated to the BoD, exposures to new markets/risk factors. Analysis of the actual Internal capital, in particular, makes it possible to assess the actual and prospective absorption at both cumulative level and with regard to each individual risk factor, even with reference to Second Pillar risks which fall within the assessment of Group capital adequacy for ICAAP purposes. Reporting is subject to continuous improvement with a view to making it increasingly more in line with control, operating guidance and corporate governance requirements.

1.18 Governance of the 'Pillar 3 (Basel Pillar 3) – Disclosure to the Public' process

Pillar 3 Disclosure to the Public") is internally governed by the Montepaschi Group in regulation no. 1 of the Parent company and a specific Group directive. The Bod, in its capacity as the Group's **Strategic Supervision Body**:

- defines the Public Disclosure process; approves the organisational policies, procedures and units identified, as well as Group guidelines on the definition of the disclosure contents;
- approves periodic updates to the Public Disclosure.

With regard to the Public Disclosure process, the **Managing Body**, represented by the Parent company's MD/CEO:

- defines the objectives, roles and responsibilities of the Group's units involved in the process;
- assesses if the Pillar 3 Disclosure to the Public Disclosure provides market participants with a comprehensive picture of the Group's risk profile.
- issues the statements required by art. 435 of the CRR;
- submits periodic disclosure report updates to the BoD.

The Risk Reporting Service, for the Parent Company's Risk Management Area, is responsible for the overall supervision and general coordination of the above-described process and for the final drafting of the report. To this end, it avails itself of support from the following functions: Balance Sheet, Supervisory Reporting, Capital Adequacy Control and all other designated Group functions which contribute to and validate the information falling within their spheres of competence.

In the Montepaschi Group, a statement of responsibility by the Chief Reporting Officer is envisaged for the "Disclosure to the Public Pillar3" pursuant to paragraph 2 of art. 154-bis of the Consolidated Law on Finance.

The Pillar3 report as a whole is shared by and between the Risk Management Area, the CFO and the Chief Reporting Officer. It is then submitted to the CEO who presents it to the BoD for final approval. Once BoD approval is obtained, the report is published on the Group's website, as provided for by supervisory regulations.

The coordination function supports investor relations on Pillar3 related issues and collaborates in dealing with any feedback from the market on these issues.

In accordance with external provisions and with the internal controls system model adopted by the Montepaschi Group, the Internal Audit Division reviews the entire process with a view to verifying its setup and making sure that implementation is appropriate and effective and results are correct.

2. Scope of application

The disclosure contained in this document (disclosure to the Public) refers solely to the Monte dei Paschi di Siena "Banking Group" as defined by Supervisory provisions. The "prudential" scope of consolidation is determined according to prudential regulations and differs from the scope of the consolidated financial statements, determined under IAS/IFRS. For the calculation of regulatory capital and prudential requirements it identifies the prudential scope of consolidation and this can create mismatches between the data disclosed in this document and that included in the Consolidated Financial Statements..

These differences are mainly attributable to:

- consolidation, using the line-by-line method in the IAS/IFRS financial statements of companies not included in the Register of Banking Groups and consolidation with the equity method for prudential supervision;
- consolidation with the equity method in the IAS/IFRS financial statements of the company Integra S.p.A. operating in financial assets and jointly controlled. The company is proportionately consolidated in prudential supervision.

It should be further noted that there are no non-consolidated companies within the Montepaschi Group.

It is noted no restrictions or other impediments exist that may prevent a prompt transfer of regulatory capital or funds within the Group.

The following table reports all entities included in the scope of consolidation as at 31 December 2015.

Tab. 2.1 – Scope of application at 31.12.2015

	Registered Office	Sector	Shareholding %	Type of relationship (a)	Voting rights % (b)	Treatment in the Balance Sheet	Treatment for Supervisory Purposes
BANCA MONTE DEI PASCHI DI SIENA S.p.a.	Siena	Banking				Full	Full
MPS LEASING E FACTORING S.p.a.	Siena	Leasing and factoring	100.00	1	100.00	Full	Full
BANCA MONTE PASCHI BELGIO S.A.	Bruxelles	Banking	100.00	1	100.00	Full	Full
MONTE PASCHI BANQUE S.A.	Parigi	Banking	100.00	1	100.00	Full	Full
MPS CAPITAL SERVICES - BANCA PER LE IMPRESE S.p.a	Firenze	Banking	99.92	1	99.92	Full	Full
WISE DIALOG BANK S.p.a. - WIDIBA	Milano	Banking	100.00	1	100.00	Full	Full
MONTE PASCHI FIDUCIARIA S.p.a	Siena	Trust company	100.00	1	100.00	Full	Full
INTEGRA S.p.a	Firenze	Consumer credit	50.00	7	50.00	Consolidate at Equity	Proportional
MPS TENIMENTI POGGIO BONELLI e CHIGI SARACINI SOCIETÀ AGRICOLA S.p.a	Siena	Wine industry	100.00	1	100.00	Full	Consolidate at Equity
MPS PREFERRED CAPITAL I LLC	Delaware	Financial vehicle	100.00	1	100.00	Full	Full
MPS CAPITAL TRUST I	Delaware	Financial vehicle	-	4	-	Full	Full
MPS PREFERRED CAPITAL II LLC	Delaware	Financial vehicle	100.00	1	100.00	Full	Full
MPS CAPITAL TRUST II	Delaware	Financial vehicle	-	4	-	Full	Full
MONTE PASCHI CONSEIL FRANCE SOCIETE PAR ACTIONS SEMPLIFIEE	Parigi	Financial intermediary	100.00	1	100.00	Full	Full
MONTEPASCHI LUXEMBOURG S.A.	Lussemburgo	Financial vehicle	100.00	1	100.00	Full	Full
ANTONVENETA CAPITAL LLC I	Delaware	Financial vehicle	100.00	1	100.00	Full	Full
ANTONVENETA CAPITAL LLC II	Delaware	Financial vehicle	100.00	1	100.00	Full	Full
ANTONVENETA CAPITAL TRUST I	Delaware	Financial vehicle	100.00	1	100.00	Full	Full
ANTONVENETA CAPITAL TRUST II	Delaware	Financial vehicle	100.00	1	100.00	Full	Full
CIRENE FINANCE S.r.l	Conegliano	Special purpose vehicle	60.00	1	60.00	Full	Full
MAGAZZINI GENERALI FIDUCIARI MANTOVA S.p.a	Mantova	Deposit and custody warehouses (for third parties)	100.00	1	100.00	Full	Full
CONSORZIO OPERATIVO GRUPPO MPS	Siena	IT and Information services	99.91	1	99.91	Full	Full
PERIMETRO GESTIONE PROPRIETÀ IMMOBILIARI S.c.p.a.	Siena	Real estate	100.00	1	100.00	Full	Full
MPS COVERED BOND S.r.l	Conegliano	Special purpose vehicle	90.00	1	90.00	Full	Full
MPS COVERED BOND 2 S.r.l	Conegliano	Special purpose vehicle	90.00	1	90.00	Full	Full
G.IMM.ASTOR S.r.l	Lecce	Real estate renting	52.00	1	52.00	Full	Full
IMMOBILIARE VICTOR HUGO S.C.I.	Parigi	Real estate	100.00	1	100.00	Full	Full

Tab. 2.1 – Scope of application 31.12.2015

	Registered Office	Sector	Shareholding %	Type of relationship (a)	Voting rights % (b)	Treatment in the Balance Sheet	Treatment for Supervisory Purposes
AIACE REOCO S.r.l.	Siena	Real estate	100.00	1	100.00	Full	Full
ENEA REOCO S.r.l.	Siena	Real estate	100.00	1	100.00	Full	Full
CO.E.M. COSTRUZIONI ECOLOGICHE MODERNE S.p.a.	Roma	Real estate	40.20	4	40.20	Full	Consolidate at Equity
CONSUM.IT SECURITISATION S.r.l.	Conegliano	Special purpose vehicle	100.00	1	100.00	Full	Full
SIENA MORTGAGES 07-5 S.p.a.	Conegliano	Special purpose vehicle	7.00	4	7.00	Full	Full
SIENA MORTGAGES 09-6 S.r.l.	Conegliano	Special purpose vehicle	7.00	4	7.00	Full	Full
SIENA MORTGAGES 10-7 S.r.l.	Conegliano	Special purpose vehicle	7.00	4	7.00	Full	Full
SIENA CONSUMER S.r.l.	Conegliano	Special purpose vehicle	10.00	4	10.00	Full	Full
SIENA CONSUMER 2015 S.r.l.	Conegliano	Special purpose vehicle	10.00	4	10.00	Full	Full
SIENA PMI 2015 S.r.l.	Conegliano	Special purpose vehicle	10.00	4	10.00	Full	Full
SIENA LEASE 2015 2 S.r.l.	Conegliano	Special purpose vehicle	10.00	4	10.00	Full	Full
CASAFORTE S.r.l.	Roma	Special purpose vehicle	-	4	-	Full	Full
PATAGONIA FINANCE S.A.	Lussemburgo	Financial vehicle	-	4	-	Full	Consolidate at Equity

(a) Type of relationship:
1 majority of voting rights at ordinary shareholders' meetings
2 dominant influence at ordinary shareholders' meetings
3 agreements with other shareholders
4 other forms of control
5 unified management under art. 26.1 of Decree 87/92
6 unified management under art. 26.2 of Decree 87/92
7 joint control
(b) Actual voting rights in ordinary shareholders' meetings.

3. Own Funds

Own funds, an element of Pillar 1, are calculated according to Basel 3 rules implemented in Europe through a comprehensive body of regulations, consisting of the Capital Requirements Regulation (CRR), European Regulation no. 575/2013, and related integrations, by the Capital Requirements Directive (CRD IV), by Regulatory Technical Standards and Implementing Technical Standards issued by the EBA, and by supervisory instructions issued by Bank of Italy (specifically, Circular nos. 285 and 286). The introduction of a new regulatory framework is subject to a transition period that extends the full application of the rules to 2019 (2022 for the phase-out of certain capital instruments) and during which the new rules will be applied in an increasing proportion.

Own funds, calculated according to the transitional arrangements in force, differ from the net equity book value since prudential regulations aim to protect the quality of assets and reduce any potential volatility caused by the application of IAS/IFRS. The items that constitute own funds, therefore, must be fully available to the Group so that they may be used to cover risks and losses without any restrictions. Institutions are, in fact, required to demonstrate the quality and quantity of own funds in compliance with applicable European legislation.

The Bank's Own Funds is made up of the following:

- ✓ Tier 1 (T1) capital, consisting of Common equity Tier 1 (CET1) and Additional Tier 1 (AT1);
- ✓ Tier 2 (T2).

For a detailed description of the items included in Own Funds (CET1, AT1, T2) whether relating to transitional or final requirements, and of the NFIs, please refer to the Annual Financial Report as at 31 December 2015 - Notes to Part F – Information on consolidated shareholders' equity. As provided for in Circular 285 of 17 December 2013, in January 2014 MPS Group exercised the option to exclude from CET1 the unrealised profits and losses on exposures with central governments classified in the AFS portfolio, until approval by the European Commission of the IFRS that replaces IAS 39 following the introduction of national discretion rules provided for by the CRR established as part of the transition requirements by Bank of Italy.

Unrealised gains relating to exposures to central administrations of the European Union classified as AFS and not included in The calculation of own funds amount to Euro 51.5 mln.

With regard to events of 2015, in June the Parent Company completed a share capital increase to be offered for a total of EUR 3 bn. Due to this capital increase and to the authorisations received by the Bank of Italy and the Ministry of Economy and Finance, the Parent Company redeemed a nominal value of EUR 1,071 mln of New Financial Instruments for EUR 1,116 mln, which includes the effects from the terms and conditions of the prospectus following the sale of shares by Fondazione Monte dei Paschi di Siena.

Moreover, on 1 July, 117,997,241 ordinary shares, equal to 4% of the share capital, were issued in favour of the Ministry of Economy and Finance (MEF) for interest accrued as at 31 December 2014, pursuant to the regulations on NFIs, with a simultaneous increase in share capital of EUR 243 mln.

Below are the main features of the financial instruments which are included in Common Equity Tier 1.

Features of CET 1 instruments

Order No.	Features of the instruments	Interest rate	Step up	Issue Date	Expiration Date	Early repayment starting from	Currency	Grandfathering	Original Amount (€/thousand)	Contribution to regulatory capital (€/thousand)
-	Paid-up Capital	N.A.	NO	N.A.	N.A.	N.A.	EUR	NO	9,001,757	8,803,949
Total Capital Instruments (CET 1)										**8,803,949**

Below are the main features of the financial instruments which are included in Additional Tier 1.

Featurs of Additional Tier 1 instruments

Order No.	Features of the instruments	Interest rate	Step up	Issue Date	Expiration Date	Early repayment starting from	Currency	Grandfathering	Original Amount (€/thousand)	Contribution to regulatory capital (€/thousand)
-	F.R.E.S.H. 2008 - not computable in CET 1 capital share	N.A.	NO	N.A.	N.A.	(a)	EUR	NO	197,808	181,985
1	F.R.E.S.H. (Floating Rate Equity-Linked Subordinated Hybrid)	Euribor 3m + 88 bps.	NO	30/12/03	N.A.	(b)	EUR	NO	700,000	27,915
2	Capital Preferred Securities I^ tranche	Euribor 3m +6,3%	YES	21/12/00	N.A.	(c)	EUR	YES	80,000	54,420
3	Capital Preferred Securities II^ tranche	Euribor 3m +6,3%	YES	27/06/01	N.A.	(c)	EUR	YES	220,000	106,503
4	Preferred Capital I LLC	Euribor 3m +6,3%	YES	07/02/01	N.A.	(d)	EUR	YES	350,000	241,133
	Total Capital Instruments (AT 1)									**611,956**

(a) F.R.E.S.H. 2008 refers to the EUR 950 mln capital increase reserved to JP Morgan. By virtue of a usufruct contract between the Bank and JP Morgan, the latter only has the bare ownership of the shares, while the Bank is entitled to the voting rights and the dividends. Under this contract, in the event of profits subject to distribution the Bank shall pay a fee to the counterparty. Following a free share capital increase of EUR 750 mln approved in 2012 applicable to the share premium reserve, the portion of the 2008 reserved capital increase that has AT1 characteristics as at 31 December 2015 amounts to EUR 182 mln.

(b) The innovative capital instruments F.R.E.S.H. (Floating Rate Equity-linked Subordinated Hybrid notes) issued by the vehicle "MPS Preferred Capital II LLC", for an original nominal value of EUR 700 mln, are perpetual instruments and as such contain no redemption or step-up clauses but are convertible into shares. In September of each year from 2004 through 2009 and however, at any time effective as of 1 September 2010, the instruments are convertible upon the investor's initiative. In addition, an automatic conversion clause is provided for in the event that, after the seventh year from date of issue, the reference price of the ordinary shares should exceed a set amount. For the portion still outstanding, it is noted that the return is non-cumulative, with an option for it not to be paid if, during the previous year, the Bank did not register any distributable profits and/or did not pay any dividends to its shareholders. Any unpaid consideration shall be considered as forfeited. The rights of the note holders are guaranteed on a subordinated basis. In the event of liquidation of the Parent Bank, the rights of the investors will be subordinated to all of the Parent Bank's creditors who are not equally subordinated, including holders of securities coming under Tier 2 capital and will override the rights of Parent Bank's shareholders. In virtue of these characteristics, these instruments are eligible for inclusion in core Tier1. Within the overall structure, a limited liability company and a business Trust were set up, which have respectively issued convertible preferred and convertible trust securities. The Parent Company underwrote an on-lending contract in the form of a subordinated deposit agreement. The conditions of the on-lending agreement are substantially the same as the conditions of the convertible preferred securities. For these securities, the issuer exercised the option not to proceed with payment of interest accrued on the coupon dates scheduled, as of 30 September 2013.

(c) Capital Preferred Securities, Antonveneta Capital Trust I and Antonveneta Capital Trust II are non-redeemable securities. For these securities, the issuer exercised the option not to proceed with payment of interest accrued on the coupon dates scheduled, as of 21 September 2013 and 27 September 2013 respectively.

(d Preferred Capital Shares I LLC are non-redeemable. For these securities, the issuer exercised the option not to proceed with payment of interest accrued on the coupon dates scheduled, as of 7 February 2013.

Below are the main features of the financial instruments which are included in Tier 2.

Features of Tier 2 instruments

Order No.	Features of the instruments	Interest rate	Step up	Issue Date	Expiration Date	Early repayment starting from	Currency	Grandfathering	Original Amount (€/thousand)	Contribution to regulatory capital (€/thousand)
5	Subordinated Bond Loan	4,875% fixed	NO	31/05/06	31/05/16	N.A.	EUR	NO	750,000	49,128
6	Subordinated Bond Loan	5,750% fixed	NO	31/05/06	30/09/16	N.A.	GBP	NO	200,000	13,350
7	Subordinated Bond Loan	Euribor 6m+2,50%	NO	15/05/08	15/05/18	N.A.	EUR	NO	2,160,558	961,343
8	Subordinated Bond Loan	5,6% fixed	NO	09/09/10	09/09/20	N.A.	EUR	NO	500,000	355,425
9	Subordinated Bond Loan	Euribor 3m+0,40 % until 30/11/2012, then Euribor 3m+1%	NO	30/11/05	30/11/17	30/11/12	EUR	NO	500,000	141,198
10	Subordinated Bond Loan	7% fixed	NO	04/03/09	04/03/19	N.A.	EUR	NO	500,000	317,360
11	Subordinated Bond Loan	5% fixed	NO	21/04/10	21/04/20	N.A.	EUR	NO	500,000	317,596
12	Subordinated Bond Loan	Euribor 3m+2,8%	NO	10/10/06	10/10/16	10/10/11	EUR	NO	400,000	62,212
	Total Capital Instruments (Tier 2)									**2,217,612**

Grandfathering
A gradual exclusion from the relevant capital level is envisaged for capital instruments issued previously and calculated in regulatory capital through 31 December 2013 that do not meet the requirements of the new regulatory framework. Specifically, 80% of the nominal value outstanding in 2014 may be included in the CET1, AT1 and T2 calculation, decreasing 10% per year until its full exclusion in 2022, for those instruments issued or calculated in the regulatory capital prior to 31 December 2011 that do not meet the new requirements.

The following tables contain the complete terms and conditions of all Common Equity Tier 1, Additional Tier 1 and Tier 2 capital instruments, according to the disclosure template provided for in the COMMISSION IMPLEMENTING REGULATION (EU) No 1423/2013 of 20 December 2013. The latter lays down the implementing technical standards for the disclosure of Own Funds requirements according to Regulation (EU) No 575/2013 of the European Parliament and of the Council.

Capital instruments' main feature template

	Order No.	1	2	3
1	Issuer	MPS Capital Trust 2	Antonveneta Capital Trust 1	Antonveneta Capital Trust 2
2	Unique identifier	XS0180906439	XS0122238115	XS0131739236
3	Governing law(s) of the instrument	Instrument: Law of the State of Delaware. Subordination clauses: Italian law	Instrument: Law of the State of Delaware. Subordination clauses: Italian law	Instrument: Law of the State of Delaware. Subordination clauses: Italian law
	Regulatory treatment			
4	Transitional CRR rules	Additional Tier 1	Additional Tier 1	Additional Tier 1
5	Post-transitional CRR rules	Additional Tier 1	Inegible	Ineligible
6	Eligible at solo/(sub-)consolidated/ solo & (sub-)consolidated	Consolidated	Consolidated	Consolidated
7	Instrument type	Mandatory convertible - Art 51	Preferred Securities - Art 51 e 484 CRR	Preferred Securities - Art 51 e 484 CRR
8	Amount recognised in regulatory capital (€/thousand)	28	54	107
9	Nominal amount of instrument	700,000,000	80,000,000	220,000,000
9a	Issue price	3.28	98.35%	100.00%
9b	Redemption price	N/A	100.00%	100.00%
10	Accounting classification	Separated: liabilities at amortized cost and equity instrument	Liabilities - Amortised cost	Liabilities - Amortised cost
11	Original date of issuance	30/12/03	21/12/00	27/06/01
12	Perpetual or dated	Irredeemable	Irredeemable	Irredeemable
13	Original maturity date	No expiration	No expiration	No expiration
14	Issuer call subject to prior supervisory approval	Yes	Yes	Yes
15	Optional call date, contingent call dates and redemption amount	"Tax Event" - at par "Regulatory Event" - at par "Change in law event" - at par	21/03/11 "Tax Event" - at par "Regulatory Event" - at par "Change company act event" - at par	27/09/11 "Tax Event" - at par "Regulatory Event" - at par "Investment company act event" - at par
16	Subsequent call dates, if applicable	N/A	Each interest payment date	Each interest payment date
	Coupons / dividends			
17	Fixed or floating dividend/coupon	Floating	Floating	Floating
18	Coupon rate and any related index	Eur 3M + 88 bps	Eur 3M + 630 bps	Eur 3M + 630 bps
19	Existence of a dividend stopper	No	No	No
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Partially discretionary	Partially discretionary	Partially discretionary
	Fully discretionary, partially discretionary or mandatory (in terms of timing) - reasons	Lack of distributable income, ban imposed by the applicable law, non-compliance of the total capital requirement; "dividend pusher"	Lack of distributable income, ban imposed by the applicable law, non-compliance of the total capital requirement; "dividend pusher"	Lack of distributable income, ban imposed by the applicable law, non-compliance of the total capital requirement; "dividend pusher"
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	Partially discretionary	Partially discretionary	Partially discretionary
21	Existence of step up or other incentive to redeem		Yes	Yes
22	Noncumulative or cumulative	Noncumulative	Noncumulative	Noncumulative
23	Convertible or non-convertible	Convertibile	Non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	At the request of the Bondholder: automatically if certain trends in the market price of the share; 'capital deficiency event'	N/A	N/A
25	If convertible, fully or partially	In whole or in part	N/A	N/A
26	If convertible, conversion rate	15.95	N/A	N/A
27	If convertible, mandatory or optional conversion	Mandatory / optional at the request of bondholders	N/A	N/A
28	If convertible, specify instrument type convertible into	Ordinary shares	N/A	N/A
29	If convertible, specify issuer of instrument it converts into	Banca Monte dei Paschi di Siena	N/A	N/A
30	Write-down features	No	Yes	Yes
31	If write-down, write-down trigger(s)	N/A	Capital deficiency	Capital deficiency
32	If write-down, full or partial	N/A	Fully	Fully
33	If write-down, permanent or temporary	N/A	Permanent	Permanent
34	If temporary write-down, description of write-up mechanism	N/A	In the event of liquidation	In the event of liquidation
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Tier 2	Tier 2	Tier 2
36	Non-complaint transitioned features	No	Yes	Yes
37	If yes, specify non-compliant features		Step up; payment coupons not fully discretionary ("dividend pusher")	Step up; payment coupons not fully discretionary ("dividend pusher")

N/A: The information does not apply to the instrument.

	Order No.	4	5	6
1	Issuer	MPS Capital Trust 1	Banca Monte dei Paschi di Siena S.p.A.	Banca Monte dei Paschi di Siena S.p.A.
2	Unique identifier	XS0121342827	XS0255820804	XS0255817685
3	Governing law(s) of the instrument	Instrument: Law of the State of Delaware.	Instrument: English Law. Subordination clauses: Italian law	Instrument: English Law. Subordination clauses: Italian law
	Regulatory treatment			
4	Transitional CRR rules	Additional Tier 1	Tier 2	Tier 2
5	Post-transitional CRR rules	Ineligible	Tier 2	Tier 2
6	Eligible at solo/(sub-)consolidated/ solo & (sub-)consolidated	Consolidated	Individual and Consolidated	Individual and Consolidated
7	Instrument type	Preferred Securities - Art 51 e 484 CRR	Tier 2 - Art 62	Tier 2 - Art 62
8	Amount recognised in regulatory capital (€/thousand)	241	49	13
9	Nominal amount of instrument	350,000,000	750,000,000	200,000,000
9a	Issue price	100.00%	99.22%	99.92%
9b	Redemption price	100.00%	100.00%	100.00%
10	Accounting classification	Liabilities - Fvo	Liabilities - Amortised cost	Liabilities - Amortised cost
11	Original date of issuance	07/02/01	31/05/06	31/05/06
12	Perpetual or dated	Irredeemable	At maturity	At maturity
13	Original maturity date	No expiration	31/05/2016	30/09/2016
14	Issuer call subject to prior supervisory approval	Yes	Yes	Yes
15	Optional call date, contingent call dates and redemption amount	07/02/2011 “Tax Event” - at par “Regulatory Event” - at par “Investment company act event” - at par	N/A “Tax Event” - at par	N/A “Tax Event” - at par
16	Subsequent call dates, if applicable	Each interest payment date	N/A	N/A
	Coupons / dividends			
17	Fixed or floating dividend/coupon	Fixed to Floating	Fixed	Fixed
18	Coupon rate and any related index	Eur 3M + 630 bps	4.875%	5.75%
19	Existence of a dividend stopper	No	No	No
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Partially discretionary	Partially discretionary	Partially discretionary
	Fully discretionary, partially discretionary or mandatory (in terms of timing) - reasons	Lack of distributable income, ban imposed by the applicable law, non-compliance of the total capital requirement; “dividend pusher"	Non-payment of dividends	Non-payment of dividends
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	Partially discretionary	Partially discretionary	Partially discretionary
21	Existence of step up or other incentive to redeem	Yes		
22	Noncumulative or cumulative	Noncumulative	Cumulative	Cumulative
23	Convertible or non-convertible	Non-convertible	Non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	N/A	N/A	N/A
25	If convertible, fully or partially	N/A	N/A	N/A
26	If convertible, conversion rate	N/A	N/A	N/A
27	If convertible, mandatory or optional conversion	N/A	N/A	N/A
28	If convertible, specify instrument type convertible into	N/A	N/A	N/A
29	If convertible, specify issuer of instrument it converts into	N/A	N/A	N/A
30	Write-down features	Yes	N/A	N/A
31	If write-down, write-down trigger(s)	Capital deficiency	N/A	N/A
32	If write-down, full or partial	Fully or partially	N/A	N/A
33	If write-down, permanent or temporary	Temporary	N/A	N/A
34	If temporary write-down, description of write-up mechanism	Revalued when is restored Minimum Capital or in the event of liquidation	N/A	N/A
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Tier 2	Lower Tier 2	Lower Tier 2
36	Non-complaint transitioned features	Yes	No	No
37	If yes, specify non-compliant features	Step up; payment coupons not fully discretionary ("dividend pusher")		

N/A: The information does not apply to the instrument.

	Order No.	7	8	9
1	Issuer	Banca Monte dei Paschi di Siena S.p.A.	Banca Monte dei Paschi di Siena S.p.A.	Banca Monte dei Paschi di Siena S.p.A.
2	Unique identifier	IT0004352586	XS0540544912	XS0236480322
3	Governing law(s) of the instrument	Italian Law	Instrument: English Law. Subordination clauses: Italian law	Instrument: English Law. Subordination clauses: Italian law
	Regulatory treatment			
4	Transitional CRR rules	Tier 2	Tier 2	Tier 2
5	Post-transitional CRR rules	Tier 2	Tier 2	Tier 2
6	Eligible at solo/(sub-)consolidated/ solo & (sub-)consolidated	Individual and Consolidated	Individual and Consolidated	Individual and Consolidated
7	Instrument type	Tier 2 - Art 62	Tier 2 - Art 62	Tier 2 - Art 62
8	Amount recognised in regulatory capital (€/thousand)	961	355	141
9	Nominal amount of instrument	2,160,558,000	500,000,000	500,000,000
9a	Issue price	100.00%	99.01%	99.68%
9b	Redemption price	100.00%	100.00%	100.00%
10	Accounting classification	Liabilities - Amortised cost	Liabilities - Amortised cost	Liabilites - Amortised cost
11	Original date of issuance	15/05/08	09/09/10	30/11/05
12	Perpetual or dated	At maturity	At maturity	At maturity
13	Original maturity date	15/05/18	09/09/20	30/11/17
14	Issuer call subject to prior supervisory approval	Yes	Yes	Yes
15	Optional call date, contingent call dates and redemption amount	N/A	N/A "Tax Event" - at par	30/11/12 "Tax Event" - at par
16	Subsequent call dates, if applicable	N/A	N/A	N/A
	Coupons / dividends			
17	Fixed or floating dividend/coupon	Floating	Fixed	Floating
18	Coupon rate and any related index	Eur 6M + 250 bps	5.60%	Eur 3M + 100 bps
19	Existence of a dividend stopper	No	No	No
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Partially discretionary	Mandatory	Mandatory
	Fully discretionary, partially discretionary or mandatory (in terms of timing) - reasons	Negative operating performance, to the extent necessary to prevent or limit the operating loss		
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	Partially discretionary	Mandatory	Mandatory
21	Existence of step up or other incentive to redeem			
22	Noncumulative or cumulative	Cumulative	Noncumulative	Noncumulative
23	Convertible or non-convertible	Non-convertible	Non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	N/A	N/A	N/A
25	If convertible, fully or partially	N/A	N/A	N/A
26	If convertible, conversion rate	N/A	N/A	N/A
27	If convertible, mandatory or optional conversion	N/A	N/A	N/A
28	If convertible, specify instrument type convertible into	N/A	N/A	N/A
29	If convertible, specify issuer of instrument it converts into	N/A	N/A	N/A
30	Write-down features	N/A	N/A	N/A
31	If write-down, write-down trigger(s)	N/A	N/A	N/A
32	If write-down, full or partial	N/A	N/A	N/A
33	If write-down, permanent or temporary	N/A	N/A	N/A
34	If temporary write-down, description of write-up mechanism	N/A	N/A	N/A
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Lower Tier 2	Senior	Senior
36	Non-complaint transitioned features	No	No	No
37	If yes, specify non-compliant features			

N/A: The information does not apply to the instrument.

	Order No.	10	11	12
1	Issuer	Banca Monte dei Paschi di Siena S.p.A.	Banca Monte dei Paschi di Siena S.p.A.	Banca Monte dei Paschi di Siena S.p.A. (previously BAPV loan from ABN)
2	Codice identificativo (1)	XS0415922730	XS0503326083	Sub Loan
3	Governing law(s) of the instrument	Instrument: English Law. Subordination clauses: Italian law	Instrument: English Law. Subordination clauses: Italian law	Instrument: Dutch Law. Subordination clauses: Italian law
	Regulatory treatment			
4	Transitional CRR rules	Tier 2	Tier 2	Tier 2
5	Post-transitional CRR rules	Tier 2	Tier 2	Tier 2
6	Eligible at solo/(sub-)consolidated/ solo & (sub-)consolidated	Individual and Consolidated	Individual and Consolidated	Individual and Consolidated
7	Instrument type	Tier 2 - Art 62	Tier 2 - Art 62	Tier 2 - Art 62
8	Amount recognised in regulatory capital (€/thousand)	317	318	62
9	Nominal amount of instrument	500,000,000	500,000,000	400,000,000
9a	Issue price	100.00%	99.01%	100.00%
9b	Redemption price	100.00%	100.00%	100.00%
10	Accounting classification	Liabilities - Amortised cost	Liabilities - Amortised cost	Liabilities - Amortised cost
11	Original date of issuance	04/03/09	21/04/10	10/10/06
12	Perpetual or dated	At maturity	At maturity	At maturity
13	Original maturity date	04/03/19	21/04/20	10/10/16
14	Issuer call subject to prior supervisory approval	Yes	Yes	Yes
15	Optional call date, contingent call dates and redemption amount	N/A "Tax Event" - at par	N/A "Tax Event" - at par	10/10/11 "Tax Event" - at par "Regulatory Event" - at par
16	Subsequent call dates, if applicable	N/A	N/A	Each interest payment date
	Coupons / dividends			
17	Fixed or floating dividend/coupon	Fixed	Fixed	Floating
18	Coupon rate and any related index	7.00%	5.00%	Eur 3M + 280 bps
19	Existence of a dividend stopper	No	No	No
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Mandatory	Mandatory	Mandatory
	Fully discretionary, partially discretionary or mandatory (in terms of timing) - reasons			
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	Mandatory	Mandatory	Mandatory
21	Existence of step up or other incentive to redeem			
22	Noncumulative or cumulative	Noncumulative	Noncumulative	Noncumulative
23	Convertible or non-convertible	Non-convertible	Non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	N/A	N/A	N/A
25	If convertible, fully or partially	N/A	N/A	N/A
26	If convertible, conversion rate	N/A	N/A	N/A
27	If convertible, mandatory or optional conversion	N/A	N/A	N/A
28	If convertible, specify instrument type convertible into	N/A	N/A	N/A
29	If convertible, specify issuer of instrument it converts into	N/A	N/A	N/A
30	Write-down features	N/A	N/A	N/A
31	If write-down, write-down trigger(s)	N/A	N/A	N/A
32	If write-down, full or partial	N/A	N/A	N/A
33	If write-down, permanent or temporary	N/A	N/A	N/A
34	If temporary write-down, description of write-up mechanism	N/A	N/A	N/A
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Senior	Senior	Senior
36	Non-complaint transitioned features	No	No	No
37	If yes, specify non-compliant features			

N/A: The information does not apply to the instrument.

Quantitative disclosure

Below is the quantitative information on Own Funds, reported according to the Transitional Own funds disclosure template provided for in the EBA's instructions. (Attachment VI of the European Commission's (EU) Implementing Regulation No. 1423/2013.

Data as at 31 December 2014 contained in this document is different from the data published in previous publications on account of the restatement of the Alexandria transaction as a CDS derivative, at the request of Consob. The transaction was previously recognised as a long term repo. The restated values reflect the changes made in accordance with the provisions of IAS 8 (Accounting policies, changes in accounting estimates and errors) as illustrated in the section "Restatement of prior period accounts in compliance with IAS 8 (Accounting policies, changes in accounting estimates and errors)" of the Consolidated Notes to the Group's Consolidated Financial Statements as at 31 December 2015.

As at 31 December 2014, the official data, without taking into consideration the Alexandria restatement, showed CET1, AT1 and T2 of EUR 6,607.6 mln, zero and EUR 3,292.6 mln, respectively.

Tab. 3.1.1 - Transitional own funds disclosure template

	Common Equity Tier 1 (CET1) capital: instruments and reserves	dec-2015 (A) - Amount at disclosure date	dec-2015 (C) - Amounts subject to pre-regulation (EU) no. 575/2013 treatment or prescribed residual Amount of regulation (EU) No 575/2013	dec-2014 (A) - Amount at disclosure date	dec-2014 (C) - Amounts subject to pre-regulation (EU) no. 575/2013 treatment or prescribed residual Amount of regulation (EU) No 575/2013
1	Capital instruments and the related share premium accounts	8,810,274	-	12,297,339	-
	of which: Ordinary Shares	*8,803,949*	-	*12,295,049*	-
2	Retained earnings	607,090	-	-763,996	-
3	Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses under the applicable accounting standards)	-390,959	-	-557,915	-
4	Amount of qualifying items referred to in Article 484 (3) and the related share premium accounts subject to phase out from CET1	-	-	-	-
	Public sector capital injections grandfathered until 1 January 2018	-	-	1,071,000	-
5	Minority Interests (amount allowed in consolidated CET1)	-	-	-	-
5a	Independently reviewed interim profits net of any foreseeable charge or dividend	388,096	-	-	-
6	**Common Equity Tier 1 (CET1) capital before regulatory adjustments**	**9,414,501**		**12,046,428**	
	Common Equity Tier 1 (CET1) capital: regulatory adjustments				
7	Additional value adjustments	-31,030	-	-61,317	-
8	Intangible assets (net of related tax liability)	-449,927	-	-511,727	-
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability where the conditions in Article 38 (3) are met)	-106,671	-160,007	-74,428	-297,712
11	Fair value reserves related to gains or losses on cash flow hedges	138,603	-	184,473	-
12	Negative amounts resulting from the calculation of expected loss amounts	-5,066	-7,599	-	-
14	Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	-142,277	-	-124,338	-
16	Direct and indirect holdings by an institution of own CET1 instruments	-	-	-	-
17	Holdings of the CET1 instruments of financial sector entities where those entities have reciprocal cross holdings with the institution designed to inflate artificially the own funds of the institution	-	-	-	-
18	Direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution does not have a significant investment in those entities (amount above the 10% threshold and net of eligible short positions)	-	-	-	-
19	Direct, indirect and synthetic holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount above 10% threshold and net of eligible short positions)	-	-	-	-
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability where the conditions in 38 (3) are met)	-	-	-	-
22	Amount exceeding the 15% threshold	-21,292	-38,361	-21,051	-121,897
23	*of which: direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities*	*-13,551*	*-20,326*	*-15,593*	*-62,371*
25	*of which: deferred tax assets arising from temporary differences*	*-7,741*	*-18,035*	*-5,458*	*-59,525*
25a	Losses for the current financial year	-	-	-1,079,731	4,318,924
26	Regulatory adjustments applied to Common Equity Tier 1 in respect of amounts subject to pre-CRR treatment	-214,550	-	-173,554	-
26a	Regulatory adjustments relating to unrealised gains and losses pursuant to Articles 467 and 468	-149,558	-	-10,114	-
	of which: unrealised losses on UCITS	-	-	*1,084*	-
	of which: unrealised losses on EU government bonds	-	-	*-175,532*	-
	of which: unrealised losses on debt securities	-	-	*164,334*	-
	of which: unrealised losses on Equity Investments	-	-	-	-
	of which: unrealised losses	*5,516*	-	-	-
	of which: unrealised gains	*-103,607*	-	-	-
	of which: other	*-51,467*	-	-	-
26b	Amount to be deducted from or added to Common Equity Tier 1 capital with regard to additional filters and deductions required pre CRR	70,411	-	88,014	-
27	Qualifying AT1 deductions that exceed the AT1 capital of the institution	-	-	-3,811,411	-
28	**Total regulatory adjustments to Common equity Tier 1 (CET1)**	**-911,356**		**-5,595,184**	
29	**Common Equity Tier 1 (CET1) capital**	**8,503,145**		**6,451,243**	

Tab. 3.1.2 - Own Funds: Additional Tier 1 (AT1) capital

	Additional Tier 1 (AT1) capital: instruments	dec-2015 (A) - Amount at disclosure date	dec-2015 (C) - Amounts subject to pre-regulation (EU) no. 575/2013 treatment or prescribed residual Amount of regulation (EU) No 575/2013	dec-2014 (A) - Amount at disclosure date	dec-2014 (C) - Amounts subject to pre-regulation (EU) no. 575/2013 treatment or prescribed residual Amount of regulation (EU) No 575/2013
30	Capital instruments and the related share premium accounts	209,900	-	217,073	-
31	*of which: classified as equity under applicable accounting standards*	*181,985*	-	*181,985*	-
32	*of which: classified as liabilities under applicable accounting standards*	*27,915*	-	*35,088*	-
33	Amount of qualifying items referred to in Article 484 (4) and the related share premium accounts subject to phase out from AT1	402,056	-	321,347	-
	Public sector capital injections grandfathered until 1 January 2018	-	-	-	-
34	Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in row 5) issued by subsidiaries and held by third parties	-	-	-	-
35	*of which: instruments issued by subsidiaries subject to phase out*	-	-	-	-
36	**Additional Tier 1 (AT1) capital before regulatory adjustments**	**611,956**		**538,421**	**-**
	Additional Tier 1 (AT1) capital: regulatory adjustments				
37	Direct and indirect holdings by an institution of own AT1 Instruments	-	-	-	-
38	Holdings of the AT1 instruments of financial sector entities where those entities have reciprocal cross holdings with the institution designed to inflate artificially the own funds of the institution	-	-	-	-
39	Direct and indirect holdings of the AT1 instruments of financial sector entities where the institution does not have a significant investment in those entities (amount above the 10% threshold and net of eligible short positions)	-	-	-	-
40	Direct and indirect holdings by the institution of the AT1 instruments of financial sector entities where the institution has a significant investment in those entities (amount above the 10% threshold net of eligible short positions)	-	-	-	-
41	Regulatory adjustments applied to additional tier 1 in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out as prescribed in Regulation (EU) No 575/2013 (i.e. CRR residual amounts)	-	-	-	-
41a	Residual amounts deducted from Additional Tier 1 capital with regard to deduction from Common Equity Tier 1 capital during the transitional period pursuant to article 472 of Regulation (EU) No 575/2013	-13,647	-	-4,349,831	-
	of which: Losses for the current financial year	-	-	-	-
	of which: Significant financial instruments	*-9,848*	-	*-30,907*	-
	of which: Residual amount related to the excess of expected losses vs loan loss provisions for IRB positions	*-3,799*	-	-	-
41b	Residual amounts deducted from Additional Tier 1 capital with regard to deduction from Tier 2 capital during the transitional period pursuant to article 475 of Regulation (EU) No 575/2013	-	-	-	-
41c	Amount to be deducted from or added to Additional Tier 1 capital with regard to additional filters and deductions required pre-CRR	-	-	3,811,411	-
42	Qualifying T2 deductions that exceed the T2 capital of the institution	-	-	-	-
43	**Total regulatory adjustments to Additional Tier 1 (AT1) capital**	**-13,647**		**-538,421**	
44	**Additional Tier 1 (AT1) capital**	**598,309**		**-**	
45	**Tier 1 capital (T1 = CET1 + AT1)**	**9,101,454**		**6,451,243**	

Tab. 3.1.3 - Own Funds: Tier 2 (T2) capital

	Tier 2 (T2) capital: instruments and provisions	dec-2015 (A) - Amount at disclosure date	dec-2015 (C) - Amounts subject to pre-regulation (EU) no. 575/2013 treatment or prescribed residual Amount of regulation (EU) No 575/2013	dec-2014 (A) - Amount at disclosure date	dec-2014 (C) - Amounts subject to pre-regulation (EU) no. 575/2013 treatment or prescribed residual Amount of regulation (EU) No 575/2013
46	Capital instruments and the related share premium accounts	2,351,275	-	3,182,232	-
47	Amount of qualifying items referred to in Article 484 (5) and the related share premium accounts subject to phase out from T2	-	-	-	-
	Public sector capital injections grandfathered until 1 January 2018	-	-	-	-
48	Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties	-	-	-	-
49	*of which: instruments issued by subsidiaries subject to phase out*	-	-	-	-
50	Credit risk adjustments	14,749	-	174,843	-
51	**Tier 2 (T2) capital before regulatory adjustments**	**2,366,023**		**3,357,075**	
	Tier 2 (T2) capital: regulatory adjustments				
52	Direct and indirect holdings by an institution of own T2 instruments and subordinated loans	-133,663	-	-5,867	-
53	Holdings of the T2 instruments and subordinated loans of financial sector entities where those entities have reciprocal cross holdings with the institution designed to inflate artificially the own funds of the institution	-	-	-	-
54	Direct and indirect holdings of the T2 instruments and subordinated loans of financial sector entities where the institution does not have a significant investment in those entities (amount above 10% threshold and net of eligible short positions)	-	-	-	-
55	Direct and indirect holdings by the institution of the T2 instruments and subordinated loans of financial sector entities where the institution has a significant investment in those entities (net of eligible short positions)	-63,598	-	-68,516	-
56	Regulatory adjustments applied to tier 2 in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out as prescribed in Regulation (EU) No 575/2013 (i.e. CRR residual amounts)	-	-	-	-
56a	Residual amounts deducted from Tier 2 capital with regard to deduction from Common Equity Tier 1 capital during the transitional period pursuant to article 472 of Regulation (EU) No 575/2013	-13,647	-	-30,907	-
	of which: Losses for the current financial year	-			
	of which: Significant financial instruments	*-9,848*	-	-	-
	of which: Residual amount related to the excess of expected losses vs loan loss provisions for IRB positions	*-3,799*	-	-	-
56b	Residual amounts deducted from Tier 2 capital with regard to deduction from Additional Tier 1 capital during the transitional period pursuant to article 475 of Regulation (EU) No 575/2013	-	-	-	-
56c	Amount to be deducted from or added to Tier 2 capital with regard to additional filters and deductions required pre CRR	41,153	-	69,284	-
	of which: unrealised gains	*41,153*	-	*69,284*	-
57	**Total regulatory adjustments to Tier 2 (T2) capital**	**-169,755**		**-36,006**	
58	**Tier 2 (T2) capital**	**2,196,269**		**3,321,069**	
59	**Total capital (TC = T1 + T2)**	**11,297,723**		**9,772,312**	

Tab. 3.1.4 - Own Funds: Capital ratios and buffers

	Capital ratios and buffers	dec-2015 (A) - Amount at disclosure date	dec-2014 (A) - Amount at disclosure date
60	**Total risk weighted assets**	**70,828,477**	**76,302,378**
61	Common Equity Tier 1 (as a percentage of risk exposure amount)	12.01%	8.45%
62	Tier 1 (as a percentage of risk exposure amount)	12.85%	8.45%
63	Total capital (as a percentage of risk exposure amount)	15.95%	12.81%
64	Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus the systemically important institution buffer (G-SII or O-SII buffer), expressed as a percentage of risk exposure amount)	7.00%	7.00%
65	*of which: capital conservation buffer requirement*	*2.50%*	*2.50%*
66	*of which: countercyclical buffer requirement*	-	
67	*of which: systemic risk buffer requirement*		
67a	*of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer*	-	-
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	7.51%	4.17%
	Amounts below the thresholds for deduction (before risk weighting)		
72	Direct and indirect holdings of the capital of financial sector entities where the institution does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	50,420	62,505
73	Direct and indirect holdings by the institution of the CET 1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	760,037	919,278
74			
75	Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability where the conditions in Article 38 (3) are met)	78,282	766,226
	Applicable caps on the inclusion of provisions in Tier 2		
76	Credit risk adjustments included in T2 in respect of exposures subject to standardized approach (prior to the application of the cap)	-	-
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	-	-
78	Credit risk adjustments included in T2 in respect of exposures subject to internal ratings-based approach (prior to the application of the cap)	14,749	981,903
79	Cap for inclusion of credit risk adjustments in T2 under internal ratings-based approach	200,585	174,843
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2013 and 1 Jan 2022)		
80	Current cap on CET1 instruments subject to phase out arrangements	-	-
81	Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	-	-
82	Current cap on AT1 instruments subject to phase out arrangements	650,000	650,000
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	-	-
84	Current cap on T2 instruments subject to phase out arrangements	-	-
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)	-	-

Tab. 3.2 - Reconciliation of shareholders' equity and the Common Equity Tier 1

Voci	dec-2015	dec-2014
Items	9,596,447	5,768,918
Group Equity	26,259	23,625
Minority Equity	**9,622,707**	**5,792,543**
Net Assets of the Balance Sheet		
Adjustments for instruments computable in AT1 or T2		
- Capital share computable in AT1	-197,808	-192,160
- Minority interests computable	-26,259	-23,625
- Own shares included in the regulatory adjustments		
- Other components non computable in regime	154,426	184,473
Common Equity Tier 1 (CET1) before the regulatory adjustments	**9,553,065**	**5,761,231**
Regulatory adjustments (including adjustments of the transitional period)	-1,049,920	690,013
Common Equity Tier 1 (CET1) net of regulatory adjustments	**8,503,145**	**6,451,243**

Tab. 3.3 – Full reconciliation of the components of Common Equity Tier 1, Additional Tier 1 and Tier 2 capital, as well as the filters and deductions applied to the institution's own funds and the balance sheet of the financial statements

Items (Euro mln)	Financial Statement	Prudential Statement	Information about differences	Relevant amount for the purpose of Own Funds	See Table "Transitional Disclosure Template"
ASSETS					
100. Equity investments	908	1,013	105	-84	23, 41a, 56a
of which: implicit goodwill	*50*	*50*		*-50*	*8*
130. Intangible assets	400	400		-400	8
of which: goodwill	*8*	*8*		*-8*	*8*
of which: other intangible assets	*392*	*392*		*-392*	*8*
140. Tax assets	5,543	5,543		-115	10, 25
of which: tax assets that rely on future profitability and do not arise from temporary differences net of the related deferred tax liability	*2,389*	*2,389*		*-107*	*10*
Liabilities and Shareholders' Equity					
30. Debt securities issued	29,394	29,394		2,476	32, 33, 46, 52
50. Financial liabilities designated at fair value	2,074	2,074		175	33
140. Valuation reserves	-22	-22		8	3, 11, 26a, 56c
of which: AFS	*93*	*93*		*49*	*3, 26a, 56c*
of which: CFH	*-139*	*-139*		*0*	*11*
of which: legally-required revaluations	*11*	*11*		*11*	*3*
of which: other	*13*	*13*		*-52*	*26a*
170. Reserves	222	222		222	2, 3
180. Share premium reserve	6	6		6	1
190. Share Capital	9,002	9,002		9,002	1, 2, 31
220. Profit/loss of the period	388	388		388	5a
Fair value gains and losses arising from the institution's own credit risk related to derivative liabilities				-142	14
Value adjustments due to the requirements for prudent valuation				-31	7
IRB Shortfall of credit risk adjustments to expected losses				-13	12, 41a, 56a
IRB Excess of provisions over expected losses eligible				15	50
Filter on double tax realignment				-215	26
Filter for IAS 19				70	26b
Direct and indirect holdings of Tier 2 instruments of financial sector entities where the institution has a significant investment				-64	55
Indirect investments					
Total Own Funds				**11,298**	

The information was summarized according to the methodology described in Annex I of the Implementing Regulation (EU) No.1423/2013 which establishes technical standards implementation with regard to the disclosure on Own Funds.

4. Capital requirements, liquidity ratios and leverage

The Montepaschi Group pursues strategic objectives focused on quantitative and qualitative strengthening of capital, structuring rebalancing of liquidity and achievement of sustainable levels of profitability. In this perspective, capital management, planning and allocation activities play a crucial role in ensuring compliance over time with the minimum capitalisation requirements set by the regulations and the supervisory authorities, as well as with the risk appetite level approved by the Group's strategic supervision body.

This is the purpose served by the Risk Appetite Framework (RAF) through which the target capitalisation levels are estimated on a yearly basis and capital is allocated to the business units according to expected development and estimated risk levels, making sure that the allocated capital is sufficient to ensure compliance with minimum requirements, under both normal and stress conditions.

In the context of the RAF, prospective capital adequacy assessments are performed over a multiyear period, under both normal and stress conditions.

The achievement of objectives and compliance with regulatory minimum requirements is constantly monitored throughout the year.

The formal corporate processes to which the RAF is applied at least on an annual basis are the budget, the risk appetite and the ICAAP.

The Budgeting, Planning, Capital and Risk Management processes of the Montepaschi Group are based on the "Risk Adjusted Performance Management" (RAPM) logic.

The Montepaschi Group defines its targets on the basis of a Risk Adjusted Performance Measurement (RAPM), which measures profitability net of the cost of capital to be held for regulatory purposes relative to the assumed risk level.

The definitions of equity applied are those used in Supervisory Regulations: Common Equity Tier 1, Tier 1 and Capital; moreover, the RAPM metrics also include Invested Capital, i.e. the amount of Shareholders' equity needed to achieve Common Equity Tier 1 values, whether determined ex ante as target levels or realised ex post. The Capital Risk concepts applied are those in the regulatory requirements, corresponding to the risk weighted assets (RWAs), determined on the basis of the rules set out in the supervisory regulations, and the economical capital estimated on the basis of the "Pillar1 Plus approach. Both measurements are used as part of RAPM metrics.

Following the implementation of the "Basel 3" regulatory framework, Pillar 1 was strengthened through a more harmonised definition of capital as well as higher capital requirements. In the face of more stringent capital requirements that more accurately reflect the potential risk of certain activities (e.g. securitisations and trading book), a definition of higher quality capital has been added, essentially focused on common equity. Capital reserves are added to this definition, which function is to conserve primary capital, provide counter-cyclical buffers, and hedge against greater losses for systemically important financial institutions. These reserves are envisaged at the discretion of Supervisory Authorities, net of the mandatory capital conservation buffer of 2.5%.

In addition to the system of capital requirements aimed at covering credit, counterparty, market and operational risk, there is now a plan to introduce leverage caps (including off-balance sheet exposures) as a backstop to capital requirements based on risk and to reduce excessive leverage across the system.

The new regulatory framework also introduces new liquidity risk monitoring requirements and tools which focus on short-term liquidity resilience (Liquidity Coverage Ratio - LCR) and longer term structural balance (Net Stable Funding Ratio - NSFR) as well as providing standards for liquidity risk management and monitoring at both individual and system-wide level.

Minimum capital requirements

The minimum capital requirements for 2015 are as follows:

- CET1 ratio of at least 4.5% of the Group's total risk exposure;
- AT1 ratio of at least 6% of the Group's total risk exposure (in 2014 the threshold was 5.5%);
- Total Capital ratio of at least 8% of the Group's total risk exposure.

Additionally, the new regulations envisage that banks must have the following reserves:

- *capital conservation buffer* - aimed at conserving the minimum level of regulatory capital during difficult periods in the market, through the allocation of high quality capital in periods in which there are no market tensions. This reserve is mandatory and must be at least 2.5% of the Bank's total risk exposure. The reserve consists of CET1 capital;
- *countercyclical capital buffer* - aimed at protecting the banking sector in phases of excessive growth in loans. The buffer provides for the accumulation of CET1 capital during phases of rapid growth in the credit cycle, which can then be used to absorb losses in the downward phase of the cycle. As opposed to the capital conservation buffer, the countercyclical buffer is imposed only during periods of loan growth and is calculated according to pre-established criteria. Currently and until the first quarter of 2016, the countercyclical capital buffer ratio has been established at zero;
- G-SII buffer for global systemically important banks and O-SII buffer for

other systemically important institutions - impose higher capital requirements on those entities based on their systemic relevance, at a global or national level, which pose greater risks for the financial system and for which a crisis could have impacts on contributors. The Group is not a Global Systemically Important Institute (G-SII) but is classed as an Other Systematically Important Insitution (O-SII), as defined by the Bank of Italy. For each bank or banking group, this identification took into consideration the four characteristics (size, relevance for the Italian economy, complexity and interconnection with the financial system) specified in the EBA guidelines to establish the systematic relevance of each entity at the level of individual jurisdiction. The Bank of Italy's decision established an O-SII buffer of zero percent for 2016;

- a component of CETI to be held in excess of CET1 against Pillar 2 risk, as required by art. 16 of EU Regulation no. 1024/2013 and established subsequent to the annual SREP at 3.20% until 31 12 2016 and 3.75% at the end of 2016.

Capital adequacy

As to the definition of regulatory capital requirements, in June 2008 the Montepaschi Group was authorised to use the Advanced Internal Rating Based (AIRB) models for the measurement of capital requirements against credit risk in the retail and corporate portfolios and the Advanced Measurement Approach (AMA) for operational risk.

The Montepaschi Group uses the standard approach ratios for Exposure at default (EAD) pending validation by the Supervisory Authorities,

the Group is instead authorised to use:

- Internal Probability of Default (PD) estimates, for the portfolio of exposures to corporates and retail exposures;
- internal Loss Given Default (LGD) estimates for the portfolio of exposures to corporates and retail exposures. For portfolios other than those mentioned above, the standard approach will be used and applied according to the roll-out plan submitted to the Supervisory authorities.

The AIRB model's scope of application currently includes the Parent Company Banca MPS, MPS Capital Services Banca per le Imprese and MPS Leasing & Factoring, for the regulatory portfolios "Retail Exposures" and "Exposures to corporates". For the remaining portfolios and Group entities, capital requirements against Credit risk are calculated using the standard approach. Capital requirements against Counterparty risk are calculated independently of the portfolio. More specifically, the Market value method is applied for OTC derviatives and the comprehensive approach for the treatment of financial collateral is used for repos, sell-buy backs and security lending.

Capital requirements against CVA risk

are calculated according to the standard approach.

Capital ratios for Operational Risk are calculated almost completely according to the AMA – Advanced Measurement Approach. The standardized approach is used for the remaining part of the scope.

Capital requirements in relation to market risk are instead calculated for all Group entities by adopting the standardized approach.

The ECB's Supervisory Review and Evaluation Process (SREP) for the year 2015 was completed. In the SREP Decision, the ECB notified BMPS on 25 November 2015 that it should maintain the minimum capital requirement, in terms of the Common Equity Tier 1 Ratio, at 10.20% on a consolidated basis, until 31 December 2016 when it will be raised to 10.75%.

In addition to the minimum capital requirements noted above relating to the CET 1 Ratio, with the SREP Decision the ECB confirmed the fulfilment of requirements to continue exercising the supervisory powers attributed to it by art. 16, paragraph 2 of Regulation (EU) no. 1024/2013 of 15 October 2013, with the objective of maintaining capital requirement standards exceeding those set forth by prudential regulations and strengthening the Bank's means, processes, mechanisms and strategies, requiring in particular:

(i) Restrictions on the payment of dividends to shareholders and cash flows to holders of AT1 instruments. In this respect, the Bank notes that these requirements are substantially analogous to those set forth in the SREP Final Decision of 10 February 2015;

(ii) Active continuation of initiatives intended to handle non-performing exposures (NPE), along with restructuring initiatives, including business combinations. In this regard, as is well known, the Bank has been committed for some time to reducing the percentage of non-performing loans, also through specific assignments, and it is also exploring possible business combinations;

(iii) Strengthening of strategies and processes to assess, maintain and distribute internal capital;

(iv) Implementation of initiatives meant to effectively monitor, and guarantee on an ongoing basis, the capital adequacy of the subsidiaries MPS Capital Services and MPS Leasing & Factoring, as well as the implementation of corrective measures to ensure compliance with the regulatory limits established for Large Exposures;

(v) Implementation of a documented liquidity and funding risk strategy by 28 February 2016. In this regard, as highlighted in its periodic reporting, the Bank has already seen a significant improvement in its liquidity profile, and it is committed to remaining on that path, as well as providing the required information to the ECB.

The MPS Group submitted its 2015 Capital Plan to the Supervisory Authority at the end of

December 2015. The Plan does not provide for any extraordinary measures to achieve a CET1 Ratio of 10.75% by 31 December 2016 - as required by the SREP Decision - since the updated forecast for 2016-2018 confirms the Bank's capital adequacy along with a buffer covering the time horizon of the projections. Nevertheless, a number of management actions were identified in case of need and may be activated to help achieve the required threshold. They are mainly optimisation actions aimed at reducing the levels of underlying risk and which would lead to a recovery in terms of RWAs.

The target ratios required by the EBC must be complied with at all times when the Authority's Decision is in force; similarly, at those times the Parent Company may not distribute dividends to shareholders or pay cash flows to holders of AT1 instruments.

The data on capital adequacy provided below includes the positive impact from profit for the period. The table reports on the Group's capital adequacy according to the disclosure templates introduced by the new regulatory framework.

Quantitative information

Tab. 4 – Capital requirements and Regulatory capital ratios

Regulatory Capital Requirements	dec-15	dec-14
Credit and Counterparty Risk	**4,624,341**	**4,988,031**
Standard Approach	1,949,684	2,656,791
Advanced IRB Approach	2,674,657	2,331,240
Market Risks	**274,556**	**286,106**
Standardised Approach	274,556	286,106
Internal Models	-	-
Operational Risk	**702,894**	**708,267**
Foundation Approach	18,507	20,212
Standardised Approach	-	-
Advanced Approach	684,387	688,055
CVA Risk	**64,487**	**118,750**
Originary Exposure Method (OEM)	-	-
Standardised Approach	64,487	118,750
Advanced Approach	-	-
Concentration Risk	**-**	**3,036**
Settlement Risk	**-**	**-**
Regulatory Capital Requirements	**5,666,278**	**6,104,190**
Risk-weighted assets	**70,828,477**	**76,302,378**
CET1 Capital Ratio	**12.01%**	**8.45%**
Tier1 Capital Ratio	**12.85%**	**8.45%**
Total Capital ratio	**15.95%**	**12.81%**

The tables below provide details on the Group's different capital requirements as at 31 December 2015. Further information on exposures (non-weighted amounts)" and RWAs (weighted amounts), are reported:

- for exposures subject to the standard approach – credit risk in Section 5.2 (which also contains the amounts of off-balance sheet transactions after weighting by credit conversion factors – CCF);
- for exposures subject to internal credit risk models in section 5.3;
- for exposures in securitisation positions subject to the standard approach and AIRB approach in section 11.

The Capital Requirement for Counterparty Risk amounts to 207,369 €/thousand and has been calculated on both the Trading Portfolio and the Banking Book. The requirement, summarised by methodology in table 4.1, is reported in the individual regulatory portfolios of the Standard Appoach and the AIRB Approach in talbe 4.2.

Tab. 4.1 – Capital requirements for Credit and Counterparty Risk

	dec-15	dec-14
	Req	Req
Standard Approach		
Standard Approach Total	1,949,684	2,656,791
of which: Counterparty Risk	*157,979*	*235,055*
IRB Approach		
IRB Approach Total	2,674,657	2,331,240
of which: Counterparty Risk	*49,390*	*38,616*
Total	**4,624,341**	**4,988,031**
of which: Counterparty Risk	***207,369***	***273,671***

Table 4.2 shows the capital requirements for credit risk and counterparty risk broken down by approach and class of exposure.

Tab. 4.2 – Capital requirements for Credit and Counterparty Risk

Standard Approach	dec-2015	dec-2014
Exposures to central governments and central banks	289,817	494,345
Exposures to regional governments and local authorities	34,177	34,147
Exposures to public sector entities	31,706	30,288
Exposures to Multi-lateral development banks	-	-
Exposures to International Organisations	-	-
Exposures to Supervised institutions	205,362	312,946
Exposures to Corporates	476,702	633,173
Retail Exposures	113,250	199,176
Exposures secured by mortgages on immovable property	40,965	54,423
Exposures in Default	160,299	222,053
Exposures associated with high-risk	14,753	6,141
Exposures in the form of covered bonds	12,811	15,985
Exposures to institutions and corporates with a short-term credit assessment	-	-
Exposures to UCITs	47,302	69,695
Equity Exposures	216,551	231,789
Other Exposures	301,734	338,904
Securitization positions	3,910	13,093
Exposures to Central Counterparties in the form of pre-funded contributions to the guarantee fund	345	633
Standard Approach Total	**1,949,684**	**2,656,791**
AIRB Approach		
Exposures to or secured by corporates:	1,773,752	1,467,873
- SMEs	855,834	751,742
- Other companies	797,457	716,132
- Specialized lending	120,461	-
Retail exposures:	900,716	863,367
- secured by real estate: SMEs	231,626	241,168
- secured by real estate: Individuals	261,201	213,701
- Qualifying revolving	96	77
- Other retail exposures: SMEs	372,679	377,765
- Other retail exposures: Individuals	35,114	30,656
Securitization positions	189	-
AIRB Approach Total	**2,674,657**	**2,331,240**
Credit and Counterparty Risk Total	**4,624,341**	**4,988,031**

Below is a breakdown of capital requirements for Credit and Counterparty Risk (IRB method) – Specialised Lending - slotting criteria, for Market Risk and Operational Risk.

Tab. 4.3 – Capital requirements for Credit and Counterparty Risk (IRB methods) – Specialised lending - slotting criteria

Risk weight	dec-2015	dec-2014
Category 1 - 50%	-	-
Category 1 - 70% with residual maturity ≥ 2.5 years	978	-
Category 2 - 70% with residual maturity < 2.5 years	6,778	-
Category 2 - 90%	67,871	-
Category 3 - 115%	34,974	-
Category 4 - 250%	9,859	-
Category 5 - 0%	-	-
Total Specialised lending - slotting criteria	**120,461**	**-**

Tab. 4.4 – Capital Requirements for Market Risk

Standardised Approach	dec-2015	dec-2014
Position risk on debt instruments	166,257	173,170
Position risk on equity	70,022	75,456
Foreign exchange risk	24,090	29,734
Commodities risk	14,187	7,745
Total Standardised Approach	**274,556**	**286,106**
Internal models		
Total Internal models	**-**	**-**
Total Market Risks	**274,556**	**286,106**

The capital requirement included in Marekt Risk for securitisaiton positions in the Regulatory Trading Portfolio amount 3,211 (expressed in thousands of Euros) for 2015.

Tab. 4.5 – Capital requirements for Operational Risk

Standardised Approach	dec-2015	dec-2014
Foundation Approach	18,507	20,212
Standardised Approach	-	-
Advanced Measurement Approach	684,387	688,055
Total Operational Risk	**702,894**	**708,267**

Liquidity Ratios and Leverage Ratio

With reference to the liquidity indicators, Liquidity Coverage Ratio and the Net Stable Funding Ratio, the observation period by the Supervisory Authorities began in March 2014. As of October 2015, the minimum obligatory requirement for the Liquidity Coverage Ratio came into force, with a level that gradually increases over the years: 60% in 2015; 70% in 2016; 80% in 2017; 90% in 2018 and 100% in 2019. The Liquidity Cover Ratio was 222.15% as at 31 December 2015, well above the minimum of 60% required for the year 2015 As regards the Net Stable Funding Ratio, the minimum obligatory requirement will come into force on 1 January 2018. In addition to the system of capital requirements aimed at covering credit, counterparty, market, operational, CVA and regulatory risks, it is expected that the new regulatory framework will introduce a limit on leverage (including off-balance sheet exposures) with a twofold purpose to limit the accumulation of debt within the banking industry so as to avoid destabilizing deleveraging process which may harm the financial system and the economy in general, and to strengthen the system of capital requirements associated with risk with a simple backstop measure that is not based on risk profile.

To this end, Circular no. 285 of 17 December 2013 of the Bank of Italy, "supervisory Provisions for banks" requires banks to calculates their leverage ratio.

The Leverage Ratio is calculated as a ratio between Tier1 and a denominator that is based on the non-risk weighted assets calculated at the end of the quarter.. The exposures must be reported net of the regulatory adjustments included in the calculation of T1 in order to avoid any double counting. In fact, items fully deducted from capital do not contribute to the Leverage Ratio and are deducted to the extent of the exposure. The basis for the calculation is the simple arithmetic average of the monthly leverage ratios for the quarter; during the transitional period between 1 January 2014 and 31 December 2017, the quarter-end figure may be used instead of the simple arithmetic average. The indicator will become binding in 2018 and the transition observation phase will last until 31 December 2017. At present, the minimum thresholds for the Leverage Ratio have not yet been established by the Supervisory Authorities. However, as of 1 January 2015, quarterly disclosure has become obligatory in addition to the disclosure requirement already in force. From the first quarter onwards, Banks are required to publish all the data necessary to calculate the indicator: numerator, denominator and leverage ratios (see table 4.3).

The Group's leverage ratio was 5.22% as at 31 December 2015. Using regulatory capital calculated by applying the rules established for full implementation, the ratio stands at 4.93%.

In accordance with public disclosure requirements, the basic data necessary for its calculation is provided below.

The information is provided via the application of the current Leverage Ratio calculation rules for reporting purposes. The templates used to report the information are those provided for by the ITS on Disclosure (*see* "EBA FINAL draft Implementing Technical Standards on disclosure of the leverage ratio under Article 451(2) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR) - Second submission following the EC's Delegated Act specifying the LR" - link) published by the EBA on 15/06/2015.

The tables below show the financial leverage ratio as at 31 December 2015 as well as a breakdown of the total exposure measure in the main categories, as required by articles 451(1)(a), 451(1)(b) and 451(1)(c). The figures shown relate to the calculation of the leverage ratio according to applicable transitional provisions.

Tab. 4.6.1 – Financial leverage: LR Sum (Summary reconciliation of accounting assets and leverage ratio exposure)

		31/12/15
1	Total assets as per published financial statements	169,011,978
2	Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	-86,054
3	(Adjustment for fiduciary assets recognised on the balance sheet pursuant to the applicable accounting framework but excluded from the leverage ratio exposure measure in accordance with Article 429(13) of Regulation (EU) No 575/2013 "CRR")	-
4	Adjustments for derivative financial instruments	-1,193,330
5	Adjustments for securities financing transactions "SFTs"	-6,090,849
6	Adjustment for off-balance sheet items (ie conversion to credit equivalent amounts of off-balance sheet exposures)	13,400,283
EU-6a	(Adjustment for intragroup exposures excluded from the leverage ratio exposure measure in accordance with Article 429 (7) of Regulation (EU) No 575/2013)	-
EU-6b	(Adjustment for exposures excluded from the leverage ratio exposure measure in accordance with Article 429 (14) of Regulation (EU) No 575/2013)	-
7	Other adjustments	-761,670
8	**Total leverage ratio exposure**	**174,280,357**

"Other adjustments" includes 782,726 €/thousand of "Deductions from the Capital Class 1 related to balance sheet assets", present at the row 2 of Table 4.6.2.

Tab. 4.6.2 – Financial leverage: LR Com (Leverage ratio common disclosure)

		31/12/15
	On-balance sheet exposures (excluding derivatives and SFTs)	
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	153,000,764
2	(Asset amounts deducted in determining Tier 1 capital)	-782,726
3	**Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets) (sum of lines 1 and 2)**	**152,218,037**
	Derivative exposures	
4	Replacement cost associated with all derivatives transactions (ie net of eligible cash variation margin)	2,578,623
5	Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	2,203,506
EU-5a	Exposure determined under Original Exposure Method	
6	Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the applicable accounting framework	
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	
8	(Exempted CCP leg of client-cleared trade exposures)	
9	Adjusted effective notional amount of written credit derivatives	
10	(Adjusted effective notional offsets and add-on deductions for written credit derivatives)	
11	**Total derivative exposures (sum of lines 4 to 10)**	**4,782,129**
	Securities financing transaction exposures	
12	Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	
13	(Netted amounts of cash payables and cash receivables of gross SFT assets)	
14	Counterparty credit risk exposure for SFT assets	3,879,908
EU-14a	Derogation for SFTs: Counterparty credit risk exposure in accordance with Article 429b (4) and 222 of Regulation (EU) No 575/2013	
15	Agent transaction exposures	
EU-15a	(Exempted CCP leg of client-cleared SFT exposure)	
16	**Total securities financing transaction exposures (sum of lines 12 to 15a)**	**3,879,908**
	Other off-balance sheet exposures	
17	Off-balance sheet exposures at gross notional amount	50,743,733
18	(Adjustments for conversion to credit equivalent amounts)	-37,343,450
19	**Other off-balance sheet exposures (sum of lines 17 to 18)**	**13,400,283**
	Exempted exposures in accordance with CRR Article 429 (7) and (14) (on and off balance sheet)	
EU-19a	(Exemption of intragroup exposures (solo basis) in accordance with Article 429(7) of Regulation (EU) No 575/2013 (on and off balance sheet))	
EU-19b	(Exposures exempted in accordance with Article 429 (14) of Regulation (EU) No 575/2013 (on and off balance sheet))	
	Capital and total exposures	
20	Tier 1 capital	9,101,454
21	**Total leverage ratio exposures (sum of lines 3, 11, 16, 19, EU-19a and EU-19b)**	**174,280,357**
	Leverage ratio	
22	Leverage ratio	5.22%
	Choice on transitional arrangements and amount of derecognised fiduciary items	
EU-23	Choice on transitional arrangements for the definition of the capital measure	Transitional
EU-24	Amount of derecognised fiduciary items in accordance with Article 429(11) of Regulation (EU) NO 575/2013	

Tab. 4.6.3 – Financial leverage: LR Spl (Split-up of on balance sheet exposures, excluding derivatives, SFTs and exempted exposures)

		31/12/15
EU-1	**Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:**	**153,000,764**
EU-2	Trading book exposures	9,363,675
EU-3	Banking book exposures, of which:	143,637,088
EU-4	*Covered bonds*	*816,345*
EU-5	*Exposures treated as sovereigns*	*25,721,052*
EU-6	*Exposures to regional governments, MDB, international organisations and PSE NOT treated as sovereigns*	*2,626,874*
EU-7	*Institutions*	*4,911,928*
EU-8	*Secured by mortgages of immovable properties*	*40,833,603*
EU-9	*Retail exposures*	*13,566,143*
EU-10	*Corporate*	*22,499,937*
EU-11	*Exposures in default*	*24,149,531*
EU-12	*Other exposures (eg equity, securitisations, and other non-credit obligation assets)*	*8,511,676*

Process used to manage the risk of excessive leverage

(in accordance with article 451(1) letter d) of the CRR)

The Group's Risk Appetite Framework (RAF) constitutes the basic risk management framework in the Montepaschi Group. The RAF is governed at Group level by a regulatory framework that establishes a system of governance, processes, tools and procedures for fully managing the Group's risk. Leverage risk is included in the RAF and is therefore subject to the control procedures contained therein. The Leverage Ratio is one of the Key Risk Indicators monitored within the RAF for 2016. In the second half of 2015, the Group's leverage registered an improvement due increase in Tier 1 and the ongoing deleveraging of assets by the group, in line with Restructuring Plan objectives. The latter was also impacted by the unwinding of the so-called "Alexandria transaction" (-4 bn in loans compared to December 2014). The increase in Tier 1 is largely due to the rights issue carried out during the second quarter of 2015, the higher share capital issued to the MEF as payment of the coupon on the New Financial Instruments and to the overall profit generated in the period.

5. Credit Risk

5.1 Credit Risk: general disclosure

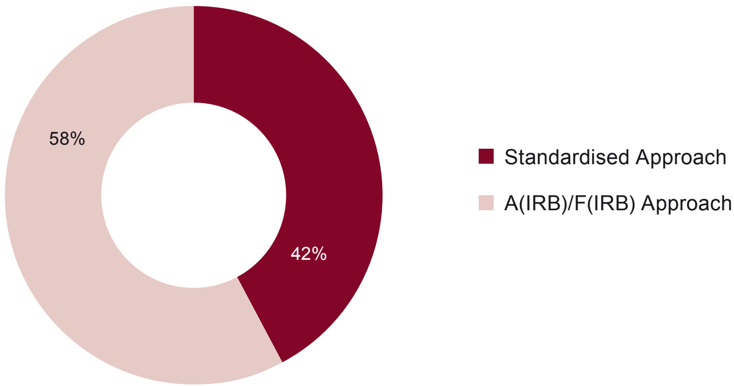
The MPS group gives special attention to the management and measurement of Credit Risk, which represents the greatest risk to which the Group is exposed, accounting for approximately 82% of total capital requirements. The main objective of the Credit Risk Management function is to promote a culture of "responsible lending" within the Group and pursue a sustainable growth in lending transactions that is in line with risk appetite and value creation. The Group's strategies in the area of risk management are aimed at limiting the economic impact from defaulting loans and containing the cost of credit. The credit risk management function is involved in defining credit policy guidelines by identifying the customer segments with greater opportunities from risk-return perspective, promoting risk diversification, limiting the concentration of risk exposure in single business groups/sectors and geographical areas. The function also defines the supports available to Credit disbursement strategies. The use and allocation of ratings is crucial, since they are the synthetic measurement of a customer's creditworthiness both during the loan disbursement and monitoring processes. This forms the basis of the preliminary procedure that is followed as a loan proposal is processed and then subsequently monitored. The assignment of a rating to each borrower means that borrowers can be classified into actual levels of risk and that both an overall or broken-down objective assessment of risk components may be made; this system, therefore, provides the basis of information for supporting both strategic decisions and the ordinary management of risk positions. Credit policy guidelines are thus provided by the sales network according to customer segments, rating categories, business sector, Regional Area, loan type and types of collateral used.

In addition, operational guidelines are structured into quantitative and qualitative objectives to develop and reclassify the loan portfolio, according to business sector and regional units. The Credit Risk Management function is also involved in the monitoring phase and verifies that the Network Structures achieve their goals of credit quality and alignment with established benchmarks, identifying the appropriate remedial actions to be implemented, reviewing objectives and, on a more general level, analysing trends in the quality of the loan portfolio in terms of market/product/customer segment and related causes. For a detailed description of the tasks of the Credit Risk function, *see* Chapter 1.

As concerns capital requirements, for credit risks the Group uses the Advanced Internal Rating Based (AIRB) method with reference to the "Credit Exposures to Retail" and "Credit Exposures to Entities" regulatory portfolios. The scope of application of the AIRB method currently includes the Parent Company Banca MPS, MPS Capital Services Banca per le Imprese and MPS Leasing & Factoring. For the remaining portfolios and Group entities, capital requirements relative to credit risks are calculated according to the standard method.

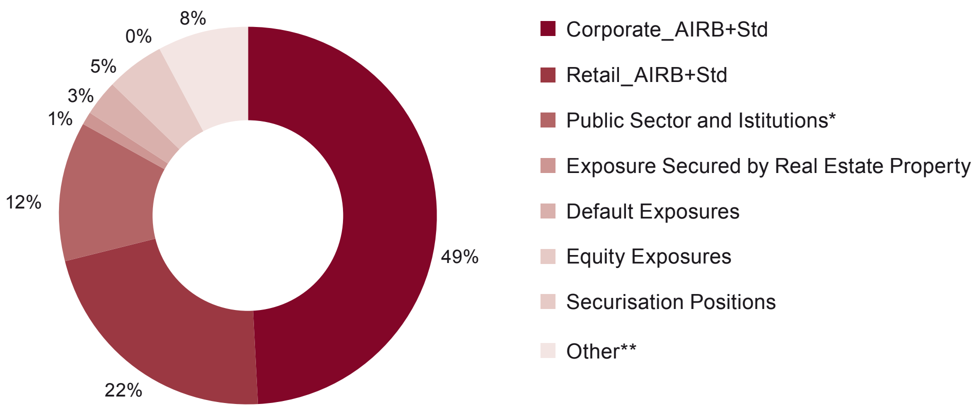
RWAs by credit risk show a prevalence of exposures treated under the advanced approach (58%) over those subject to the Standardised Approach (42%).

Credit risk's RWA by approach



An analysis by type of exposure reveals that 71% of Credit Risk refers to the Corporate and Retail portfolios. The remaining 29% is mainly concentrated in the Public Sector and Institutions (12%).

RWA by type of exposure



* *Includes the following portfolios: Central Governments and Central Banks, Regional Governments and Local Authorities, Public sector entities, Multi-lataral Development Banks, International Organisations, Supervised institutions.*

** *Includes the following portfolios: Exposures associated with high-risk, Exposures in the form of covered bonds, Exposures to institutions and corporates with a short-term credit assesment, Exposures UCITS, Exposures to Central/Counterparties in the form of pre-funded contributions the guarantee fund. Other exposures.*

The following table shows a breakdown of exposures and RWAs by approach (Standard/ AIRB) and by regulatory portfolio. In compliance with regulatory standards, in the case of the standard approach, the EAD value corresponds to the value of the exposure, which takes account of the prudential filters, risk mitigation techniques and credit conversion factors. In the case of the internal ratings- based approach, the EAD value reported corresponds to the "Exposure At Default" calculated according to the rules of prudential supervision and therefore expressed gross of value adjustments and without the impacts from risk mitigation techniques which, in the case of exposures subject to an internal models-based approach, are directly included in the weighting factor applied. Instead, the EAD value takes into account the credit conversion factors for guarantees issued and commitments to disburse funds.

Tab. 5.1.1 – EAD and RWA overview between Credit Risk and Counterparty Risk

	dec-15		dec-14			
	EAD	RWA	EAD	RWA	Δ EAD	Δ RWA
Standard Approach						
Standard Approach Total	60,748,209	24,371,056	79,538,422	33,209,889	-18,790,213	-8,838,833
of which: Counterparty Risk	*6,208,174*	*1,974,733*	*9,584,495*	*2,938,189*	*-3,376,321*	*-963,455*
IRB Approach						
IRB Approach Total	118,185,352	33,433,210	117,732,184	29,140,499	453,168	4,292,711
of which: Counterparty Risk	*810,934*	*617,377*	*902,840*	*482,703*	*-91,906*	*134,674*
Total	178,933,561	57,804,266	197,270,606	62,350,388	-18,337,045	-4,546,122
of which: Counterparty Risk	*7,019,107*	*2,592,111*	*10,487,335*	*3,420,892*	*-3,468,227*	*-828,781*

The following table shows a breakdown of exposures and RWAs by approach (Standard/ AIRB) and by regulatory portfolio.

Tab. 5.1.2 – Exposure and RWA Distribution of Credit and Counterparty Risk

Regulatory portfolios	dec-15		dec-14	
Standard Approach	EAD	RWA	EAD	RWA
Exposures to central governments and central banks	26,573,189	3,622,709	34,958,256	6,179,327
Exposures to regional governments and local authorities	2,136,800	427,216	2,135,614	426,836
Exposures to public sector entities	579,495	396,327	490,029	378,596
Exposures to Multi-lateral development banks	41,783	-	34,291	-
Exposures to International Organisations	-	-	-	-
Exposures to Supervised institutions	10,799,807	2,567,026	15,537,563	3,911,818
Exposures to Corporates	6,475,505	5,958,779	8,121,044	7,914,657
Retail Exposures	1,932,479	1,415,627	3,371,548	2,489,700
Exposures secured by mortgages on immovable property	1,269,170	512,066	1,698,495	680,286
Exposures in Default	1,601,248	2,003,736	2,350,096	2,775,664
Exposures associated with high-risk	122,941	184,411	51,179	76,768
Exposures in the form of covered bonds	816,345	160,143	986,309	199,813
Exposures to institutions and corporates with a short-term credit assessment	-	-	-	-
Exposures to UCITs	591,269	591,269	871,192	871,192
Equity Exposures	1,629,637	2,719,834	1,745,153	2,897,361
Other Exposures	6,174,626	3,758,727	7,133,564	4,236,295
Securitization positions	3,914	48,879	54,088	163,665
Exposures to Central Counterparties in the form of pre-funded contributions to the guarantee fund	-	4,308	-	7,911
Standard Approach Total	**60,748,209**	**24,371,056**	**79,538,422**	**33,209,889**
AIRB Approach				
Exposures to or secured by corporates:	53,998,435	22,171,901	50,358,660	18,348,417
- SMEs	34,404,460	10,697,928	32,276,311	9,396,770
- Other companies	16,995,323	9,968,215	18,082,349	8,951,647
- Specialized lending	2,598,652	1,505,758	-	-
Retail exposures:	64,177,053	11,258,949	67,373,524	10,792,082
- secured by real estate: SMEs	9,104,309	2,895,329	10,486,140	3,014,598
- secured by real estate: Individuals	29,135,293	3,265,009	30,106,751	2,671,257
- Qualifying revolving	7,664	1,195	8,868	968
- Other retail exposures: SMEs	20,845,566	4,658,490	21,969,599	4,722,059
- Other retail exposures: Individuals	5,084,221	438,926	4,802,167	383,200
Securitization positions	9,865	2,360	-	-
AIRB Approach Total	**118,185,352**	**33,433,210**	**117,732,184**	**29,140,499**
Credit and Counterparty Risk Total	**178,933,561**	**57,804,266**	**197,270,606**	**62,350,388**

5.2 Credit Risk: Standard approach

The Montepaschi Group uses the following official rating agencies for legal entities not subject to airb validation as well as for statutory portfolios, for which the advanced internal rating system to calculate capital absorption on credit risk is not used, to measure the level of reliability of different borrowers:

- Standard & Poor's;
- Moody's Investor Service;
- Fitch Rating.

When determining capital requirements, it should be noted that if there are two evaluations of the same customer, the more conservative one is adopted. In the case of three evaluations, the intermediate is used.

At present the standard approach is applied to all portfolios and entities of the Group with the exception of the portfolios, Exposures to corporates and retail exposures, belonging to the following entities:

- *Banca Monte dei Paschi di Siena*
- *MPS Capital Services Banca per le Imprese*
- *MPS Leasing & Factoring*

for which the advanced IRB model is adopted, details of which are described in paragrapf 5.5.

The table below summarises the list of ECAIs (External Credit Assessment Institutions) and ECAs (Export Credit Agencies) used in the standardised approach as well as the portfolios of exposures in which the ratings of the exposures themselves have been applied.

Portfolios	ECA/ECAI	Rating characteristics (a)
Exposures to governments and central banks	✓ Standard & Poor's Moody's Investor Service Fitch Ratings	Solicited/Unsolicited
Exposures to multilateral development banks		
Exposures to International organisations	✓ Standard & Poor's Moody's Investor Service Fitch Ratings	Solicited
Exposures to corporates and other persons		
Exposures to undertakings for collective investment in transferable securities (UCITS)		

(a) • ***solicited rating:*** *a rating assigned for a fee following a request from the entity evaluated. Ratings assigned without such a request shall be treated as equivalent to solicited ratings if the entity had previously obtained a solicited rating from the same ECAI;*
• ***unsolicited rating:*** *a rating assigned without a request from the entity evaluated and without payment of a fee.*

Extension of issuer and issue credit assessment to comparable assets not included in the regulatory trading portfolio

In accordance with EU Regulation 575/2013 (CRR), a set of criteria – as summarised below – has been established for the use of issue and issue\r credit when assessing the risk of exposures and the mitigation of guarantees. In order to assess the risk weight to be assigned to the exposures (in general for all regulatory portfolios), the rules provide for the priority use of the issue rating. Where the issue rating does not exist and where the conditions laid down by the Regulation are met, the issuer rating is used.

Quantitative disclosure

The table below shows the details of the banking Group's exposures subject to credit risk – standard approach, determined according to the rules of Prudential Supervision and including the effects from risk mitigation techniques (netting agreements, guarantees, etc.).

The quantitative disclosures in this Section complement those provided in the section on Risk mitigation techniques. In fact, each regulatory portfolio provided for by regulations under the standard approach is broken down as follows:

– amount of on- and off-balance exposures, "without" the risk mitigation (Exposure before CRM), which does not take into account the decrease in exposure arising from application of collateral and guarantees; in the case of guarantees, which transfer risk in respect of the guaranteed portion, reference is made to the guarantor's regulatory portfolios and weightings, while as to the residual exposure, reference is made to the guaranteed party's information;

– amount of the same exposures "with" the risk mitigation effect (Exposure after CRM), i.e. net of the guarantees mentioned in the previous point. The difference between exposures "with" and "without" credit risk mitigation thus represents the amount of approved guarantees, disclosed also in the section on Risk mitigation techniques. The below information is listed in the "with" and "without" credit risk mitigation columns and credit risk mitigation techniques.

Tab. 5.2.1 – Standard approach: Ante and Post CRM Exposure Value

Regulatory Portfolio (Standard Approach)	Ante CRM Exposure	Post CRM Exposure	Credit Risk Mitigation Techniques
Exposures to central governments and central banks	26,604,117	26,604,117	-
Exposures to regional governments and local authorities	2,231,534	2,231,534	-
Exposures to public sector entities	951,732	936,520	-15,211
Exposures to Multi-lateral development banks	71,783	71,783	-
Exposures to International Organisations	-	-	-
Exposures to Supervised institutions	57,845,680	16,398,488	-41,447,193
Exposures to Corporates	11,426,706	10,303,764	-1,122,942
Retail Exposures	2,866,026	2,854,015	-12,011
Exposures secured by mortgages on immovable property	1,275,685	1,275,239	-446
Exposures in Default	1,903,136	1,882,370	-20,767
Exposures associated with high-risk	122,941	122,941	-
Exposures in the form of covered bonds	816,345	816,345	-
Exposures to institutions and corporates with a short-term credit assessment	-	-	-
Exposures to UCITs	673,209	671,959	-1,250
Equity Exposures	1,629,637	1,629,637	-
Other Exposures	6,174,626	6,174,626	-
Securitization positions	3,914	3,914	-
Total 31/12/2015	**114,597,070**	**71,977,251**	**-42,619,819**
Total 31/12/2014	**133,994,792**	**91,968,362**	**-42,026,430**

The Table shows the Banking Group's exposures reported by regulatory exposure classes and also contains off-balance sheet exposures relating to guarantees and commitments before the application of credit conversion factors (CCF).

As at 31 December 2015, the total amount of exposures deducted from Funds came to EUR 147.7 million. The exposures reported in the table also include the off balance-sheet exposures relating to guarantees and commitments (including undrawn credit lines) subsequent to the application of the Credit Conversion Factors (CFFs) required by prudential regualtions. The off-balance sheet exposures in relation to guarantees and commitments are disclosed side by side with the counterparty weighting factor. The exposure value shown in the tables of this section is stated net of adjustments in accordance with the prudential regulations. The tables below provide the Post CRM exposures broken down by weighting factor.

Tab. 5.2.2 – Standard approach: Distribution in classes of creditworthiness (post CRM)

Regulatory Portfolio (Standard Approach)	Classes of creditworthiness (Weighting Factors)								Total
	0%	up to 20%	35%	50%	75% - 100%	150%	225% -250%	1250%	
Exposures to central governments and central banks	23,764,333	17	-	30,251	2,225,927	-	552,661	-	26,573,189
Exposures to regional governments and local authorities	-	2,136,800	-	-	-	-	-	-	2,136,800
Exposures to public sector entities	-	228,960	-	-	350,536	-	-	-	579,495
Exposures to Multi-lateral development banks	41,783	-	-	-	-	-	-	-	41,783
Exposures to International Organisations	-	-	-	-	-	-	-	-	-
Exposures to Institutions	82,206	8,421,684	-	2,208,780	85,920	1,217	-	-	10,799,807
Exposures to Corporates	42,735	362,792	-	224,028	5,760,691	85,259	-	-	6,475,505
Retail Exposures	-	-	-	-	1,932,479	-	-	-	1,932,479
Exposures secured by mortgages on immovable property	-	-	678,368	583,973	6,829	-	-	-	1,269,170
Exposures in Default	54	-	-	-	796,110	805,084	-	-	1,601,248
Exposures associated with particularly high-risk	-	-	-	-	-	122,941	-	-	122,941
Exposures in the form of covered bonds	-	795,441	-	20,904	-	-	-	-	816,345
Exposures to institutions and corporates with a short-term credit assessment	-	-	-	-	-	-	-	-	-
Exposures to UCITs	-	-	-	-	591,269	-	-	-	591,269
Equity Exposures	-	-	-	-	889,890	-	726,799	-	1,616,689
Other Exposures	1,072,354	1,679,147	-	494	3,435,540	38	-	-	6,187,574
Items representing securitization positions	3	-	-	-	-	-	-	3,910	3,914
Total 31/12/2015	**25,003,469**	**13,624,842**	**678,368**	**3,068,429**	**16,075,191**	**1,014,539**	**1,279,460**	**3,910**	**60,748,209**
Total 31/12/2014	**31,028,850**	**17,465,519**	**984,128**	**4,412,567**	**23,123,891**	**954,093**	**1,565,280**	**4,094**	**79,538,422**

The Table shows the Banking Group's exposures reported by regulatory exposure classes and also contains off-balance sheet exposures relating to guarantees and commitments following the application of credit conversion factors (CCF).

5.3 Credit Risk: use of the AIRB approach

AIRB Authorization

With decree no. 647555 of 12 June 2008, the bank of Italy authorised the Montepaschi Group to use advanced internal rating based (AIRB) systems to calculate the capital requirements for credit and operational risk. In particular, whereas the Montepaschi Group uses the standard approach ratios for Exposure at default (EAD) pending validation by the Supervisory Authorities, the Group is instead authorised to use:

- Internal Probability of Default (PD) estimates, for the portfolio of exposures to corporates and retail exposures;
- internal Loss Given Default (LGD) estimates for the portfolio of exposures to corporates and retail exposures.

For portfolios other than those mentioned above, the standard approach will be used and applied according to the roll-out plan submitted to the Supervisory authorities. As for legal entities, the scope of application of the authorised approaches shall be the following:

AIRB: Banca Monte dei Paschi di Siena, MPS Capital Services, MPS Leasing & Factoring;

the remaining legal entities of the Montepaschi Group use the standard approach.

Internal rating system architecture

The Montepaschi Group began using internal rating systems for the measurement of credit risk in 2002. The first Probability of default (PD) models were developed for the small and medium-sized enterprises (SMEs) and Small businesses (SB) portfolios which still remain the "core business" of the Group; subsequently, rating models were also estimated for other types of exposure and a loss Given default (LGD) estimation model was implemented.

Finally, an Exposure at Default (EAD) estimation model was implemented and subsequently updated, as with other internal models pending validation by the Supervisory Authorities. The rating system has thus become, over time, one of the main elements of assessment for all units involved in the credit industry, both at Head Office level (risk management, chief Financial Officer, General management, Risk Management committee, board of directors) and at outer level (credit management area, rating units and relationship managers).

Thanks to the experience accumulated, the Montepaschi Group has decided to further invest in internal rating systems, starting, at the beginning of 2006, with the Basel II Project aimed at improving the existing internal procedures by adjusting them to the new prudential supervisory regulations for banks which came into force on January 1, 2007 with legislative decree no. 297 dated 27 December 2006. This project ended in 2008 with the authorisation from the bank of Italy to use advanced internal rating systems (AIRB) for PD and LGD with a view to calculating capital requirements for portfolios of "non-financial companies" and "retail exposures" for Banca Monte dei Paschi di Siena and MPS Capital Services. Over the following years, in line with an internal overall 'advancement plan', the MPS Group continued the process of refinement/ revision of its rating models for Corporate and Retail clients, leading it to obtain authorization by the Supervisory body (with decree of 25/08/2010) to use advanced internal rating based systems for the Group's new entity, "Banca Antonveneta" (acquired in 2008 and merged into Banca MPS in April 2013) and for Montepaschi Leasing & Factoring and BiverBanca by ruling of 06.07.2012. The latter was subsequently sold by the Group to Cassa di Risparmio di Asti and as of the end of 2012 is no longer part of the MPS Group.

Internal rating system description

The development of the internal rating systems involved the adoption of strict and advanced statistical methodologies in compliance with the requirements set out in the regulations; at the same time, models were selected in such a way as to make results consistent with the historical experience of the bank in credit management. Lastly, in order to optimise the proper use of these new instruments, the rating models were shared with a top-down approach – from risk management down to individual client managers by means of intense training.

Estimation of the LGD model was based on internal data relative to capital flows, recoveries and expenses actually incurred on positions transferred to the non-performing portfolio. Results obtained from model application were then compared with data recorded by MPS Gestione Crediti Banca, a company of the Group dedicated to the management and recovery of non-performing loans. The introduction of advanced rating systems in the credit process was an important cultural step forward which is now becoming a well-established practice for all business units of the Group. The main characteristics of the advanced rating systems are as follows:

- for all regulatory portfolios subject to validation, the rating is calculated with a counterparty-based approach for each individual borrower, in line with the accepted management practice which provides for the assessment of credit risk, both in the disbursement and monitoring phases;
- ratings are based upon a Group logic: each individual counterparty is assigned a single rating at banking Group level, based on the data set pertaining to all lending banks within the AIRB scope; there is one LGD reference definition for retail banks while there are different reference definitions for product companies;
- LGD reflects the economic (and not only the accounting) loss incurred; for this reason, LGD estimates must also include

the costs incurred for the recovery process and a time factor;

- the rating model segmentation is defined in such a way as to make the individual model clusters consistent with business objectives, credit process logics and regulatory portfolios set out in the regulations;
- loss given default is differentiated by type of loans and an LGD value is assigned at the level of each individual transaction;
- customer segmentation for LGD estimation and assignment follows the same logics as with the rating models; for clusters to acquire significance, segments were aggregated together under "retail" for retail exposures and "corporate" for exposures to non-financial corporates;
- the loss rate is differentiated by geographical area since historical and current recovery rates are different among Northern Italy, central Italy and Southern Italy and islands;
- loss on defaulted positions other than non-performing loans is estimated with a cure rate approach. With regard to counterparties whose exposures are administratively classified as Watchlist, restructured and Past due, the percentage of exposures reverting back to a performing status was calculated and used to adjust LGD estimated from NPL positions;
- changes in exposure after the first transition to default are included in the cure rate estimate;
- calculation of the final rating is differentiated by type of counterparty. The credit process envisages a level of in-depth analysis proportional to counterparty risk: the assessment of loan disbursements is based on a complex multi-level structure for medium-large Corporate counterparties (SME and Large Corporate (LC) segments), whose exposure and concentration risks are higher, and a simplified structure for Small SMEs (companies with a turnover of up to EUR 10 mln) and retail clients;
- in line with this process, the final rating for SMEs and LC is the result of a number of different factors: statistical rating, qualitative rating, overrides and valuation of the 'economic group' which businesses belong to; for Small SMEs, SB and retail counterparties the rating is calculated only on the basis of statistical factors;
- the rating has a 12-month internal validity period and is usually reviewed on a yearly basis, except for rating reviews following well-structured codified practices or that are brought forward on client managers' request or following serious counterparty deterioration.

The Montepaschi Group has adopted one master Scale for all types of exposures: this enables all units involved in credit management to immediately compare the risk level associated with different counterparties or portfolios; furthermore, the probabilities of default of internal rating classes were mapped against Standard & Poor's external rating scale so as to make internal risk measurements comparable to those available on the financial market.

Rating Class	PD	PD Class
AAA	0.01%	1
AA1	0.03%	
AA2	0.05%	
AA3	0.09%	
A1	0.13%	
A2	0.20%	2
A3	0.30%	
B1	0.46%	
B2	0.69%	3
B3	1.05%	
C1	1.59%	
C2	2.42%	
C3	3.99%	4
D1	6.31%	
D2	9.95%	
D3	16.03%	
E1	22.12%	5
E2	31.63%	
E3	45.00%	
Default	100.00%	6

The table shows a breakdown by PD band - with related central PDs - identified by the MPS Group in order to allow for a significant differentiation of credit risk.

Under prudential standards, the PD for the Corporate segment cannot be below 0.03% whilst for Retail, the MPS Group has decided to assign a PD of at least 0.13% for prudential purposes.

The rating system development and monitoring activities are functionally assigned to risk management. The estimation procedure is carried out according to an internal development protocol to make sure that estimation activities are transparent and visible for the internal controls and auditing departments.

Risk Management and Internal Validation Function periodically carry out monitoring/backtesting analyses on the internal models to verify their performance stability over time. Should significant vulnerabilities emerge from the analyses, model fine-tuning or 'reestimation' procedures are put in place.

Montepaschi Group currently has 15 rating models (14 validated and one pending validation) and one LGD model (differentiated by geographical area, type of loan, type of guarantee, guarantee coverage ratio and exposure at default) for the measurement of risk in validated regulatory portfolios.

For the calculation of capital absorption against credit risk, the Montepaschi Group uses **internal rating systems** for the following regulatory classes:

- corporates,
- retail exposures.

Internal rating model for Corporates

PD models

For the estimation of PD models, the Montepaschi Group adopted a default-based methodology. Among the statistical techniques used in the estimation of models with dichotomous bad/good target variables, a logistic regression was selected, characterized by the optimal trade-off between statistical soundness and interpretability of results.

The "non-financial businesses" portfolio includes all balance-sheet and unsecured exposures to companies relating to the banks, Monte dei Paschi, MPS Capital Services and MPS Leasing and Factoring.

The data source observation period for Corporate is 7 years (2008-2014).

Model segmentation

Corporate customers were segmented beforehand in order to obtain consistent clusters by risk profile. To this end, a size logic was used (based on the legal form of a company and its turnover) which appears to be consistent from both the statistical and operational point of view. Any information on turnover is obtained from the company balance sheet prepared in accordance with the Fourth EEC directive in relation to the last available annual report. The segment of Small businesses (one-man businesses and partnerships) consists of companies which are not subject to the obligation of preparing balance sheets for legal purposes; tax data are not currently used in the segmentation.

Definition of default

During the stage of development of the PD models, the following definition of default was used: defaulting counterparties are a sub-group of customers with an exposure (credit line granted or drawn) which, in an ordinary condition in a specific month of the year, shows at least one impairment anomaly within the following twelve months. The anomalies contained in the definition of default include nonperforming loans, watchlist loans, restructured loans. Past-due positions for a period in excess of 90 days are included as of 2006, the year from which the reporting of such positions became mandatory. Furthermore, the decision was taken to use an internal definition of past due, so called "technical", to identify instances not representative of a state of financial difficulty that is liable to generate an economic loss (option granted to banks by the regulations at issue), in line with client managers' actual business-based expectations of economic loss. The rules applied, and subjected to review in the course of last year, allowed a sub-set of alerts to be identified, involving vulnerabilities similar to other impairment states (particularly watchlist); the rationale adopted was aimed at integrating defaulting positions with positions which show no temporary anomaly but are characterised by aspects featuring in other states of impairment. The definition of 'technical past due loans' was used consistently for PD and LGD estimates. Defaulting positions are identified at MPS banking Group level.

Development stages of the rating models

Two main stages of development are

envisaged for each rating model: score model estimate and calibration.

- **Score model estimate**

All information sources available are taken into account for the estimate of each rating model. A modular approach was adopted to maximise the prediction power of each information source, i.e. a (financial, internal trend, industry trend) standard module was estimated for each information source with the following determination of the final model as a combination of all modules. The information sources used for Corporate models are the following:

- balance sheet reports,
- internal trend data,
- industry data (Central Credit Registers of the Bank of Italy).

As far as the balance sheet is concerned, a set of indicators covering all areas of inquiry contemplated by corporate financial analysis was determined, including: debt coverage, financial structure, liquidity, profitability, productivity, development. With reference to lending trend components, the variables normally used by the account managers for risk valuation were restated: types of use of loan forms, account movements, number of irregularities found. The variables are calculated for each type of loan (callable, self-liquidating, upon maturity etc.) and are determined at the Group level over a time horizon of 12/6/3 months. As for the internal practice, the stage of development follows all procedures contemplated by a statistical inquiry: determination of a development sample (70%) and a test sample (30%), fact-finding analyses and preliminary data treatment, univariate analyses, correlation analyses and short list determination, multivariate analyses, model selection and review of out of sample performances.

- **Calibration**

Calibration is a process for estimating the function which transforms the score models output into default probability, i.e. the probability that a counterparty is in default within one year. The approach used by the MPS Group was based on two main steps:

- Estimate of the anchor point. The *anchor point* determines the average PD used by the model;
- Calculation of the calibration function for adjustment of the scoring model parameters.

The calibration function essentially defines how expected PD will vary according to the model score. Calibration in fact envisages a new default rate (anchor point) and is therefore inseparable from the need to adjust the parameters of the scoring algorithm so as to enable this latter value to be calculated instead of the estimated value. The default rate of the sample should therefore be adjusted in order to take account of the preset target rate (anchor point).

To this end, the MPS Group has identified a methodology, substantially based on the use of a ‘calibration’ function, whose final output is an intercept and slope value to be applied to the initial algorithm.

The anchor point represents the level of risk traditionally associated with the specific segment which the model is calibrated on.

It is calculated on the basis of the long term default rate and qualitative considerations the analyst deems appropriate to introduce. The estimated calibration function is used to calculate the point-in-time PD which is subsequently mapped on the Montepaschi Group Master Scale; each counterparty is assigned a PD level corresponding to its rating class.

LGD models

As required by regulations, the loss rate estimate is the long term average of realised losses, weighted by the number of counterparties and not by exposure. The Group uses a work-out model based on historical evidence of sets of defaulting transactions with similar characteristics. The database used to estimate the parameter includes all balance-sheet and unsecured exposures relating to the banks within the scope of validation, that were classed as “non-performing” from 01/01/1999 to 31/12/2014, for which either the recovery process has terminated or, if still active, whose balance is zero or seniority exceeds 15 years. The relevant clusters for the estimates include the geographic area, type of customers, loans, exposures transitioning to a default state, guarantees and their percentage of coverage.

- **Definition of default**

During the stage of development of the LGD model, the definition of default used was the same as the one for rating models: defaulting counterparties are a sub-group of customers with an exposure (credit line granted or drawn) which, in an ordinary condition in a specific month of the year, show at least one impairment anomaly within the following twelve months.

- **Development stages of the LGD model**

The LGD estimate includes three main stages: (i) the measurement of the loss rate actually registered in the history of each individual legal entity in relation to the nonperforming customers, (ii) the calculation of the LGD downturn, i.e. an indicator which takes account of the adverse phases of the economic cycle; (iii) the calculation of the LGD for all loan statuses other than non-performing loans.

- **Loss Rate for non-Performing Positions**

Realised collections minus the costs incurred with respect to defaulting exposures are compared to calculate the LGD rate actually observed on non-performing positions. Considering that reference is made to the registered economic loss, and not only to the accounting loss, all movements are discounted as of the date the loan is classified as non-performing. The interest rate used for discounting is the risk free rate plus an appropriate spread which remunerates the opportunity cost of each bank resulting from the non-use of the capital not repaid by the customer. As provided for by the regulations, a lower limit of 0% is set since the average LGD cannot be negative.

- **LGD Downturn**

The relation between collection rates and default rates was analysed to determine the adjustment to be made to the LGD estimates in case of a possible downturn of the economic cycle; once a negative relation between the two series was ascertained, a regression model was clearly formulated between collection rates and macroeconomic variables. Once the collection rates of expansionary and recessive cycles are determined, the downturn LGD is calculated as long-term default-weighted average, suitable for the recessive phases of the economic cycle.

- **Total LGD**

The estimated loss rates on defaulting positions other than non-performing loans starts from the estimated cure rate, i.e. the percentage of Watchlist loans, restructured loans, or Past due loans reverting to performing loan status. All positions included in the rating model calibration population that became defaulted within the analysis period were selected for this purpose. A weighted average of the downturn LGD was calculated, using the cure rates multiplied by the probabilities of default as weights, to determine the LGD rates for the different statuses of default. The LGD to be applied to all loan transactions of performing customers was determined by using the calibration clusters of the rating models.

Internal rating model for Retail exposures

PD models

A default-based methodology has also been adopted for “retail exposures”. The portfolio includes all balance-sheet and unsecured exposures relating to loans granted by the banks, Monte dei Paschi, MPS Capital Services and MPS Leasing & Factoring to retail customers (natural persons or joint co-obligations of natural persons). The data source observation period for the estimation of PD is 5 years (2010-2014).

- **Model segmentation**

The retail portfolio was segmented drawing a distinction between jointly liable individuals and individual natural persons. The criteria were selected on the basis of the risk profile associated to the cluster and internal historical records.

- **Definition of default**

The Group used the definition of default adopted for the corporate models also in relation to the PD models applied to the portfolio of retail exposures.

- **Development stages of the rating models**

Following on from what was previously reported, only the specific features are shown for Retail models, which have been developed and calibrated using the same methods applied for Corporate models.

For the Retail segment, the main sets of information regarding developments are those relating to loans granted by the Group (overdraft facilities, mortgages and small loans) and to the personal data available on the Customer and related parties.

LGD models

The LGD model for retail exposures includes the stages contemplated for the corporate model. The comments on the estimate data base are only in relation to the retail segment and the cure rate estimate population was the calibration population of rating models.

Main changes to the internal rating system in recent years

Following are the main actions implemented over recent years to the MPS Group's internal rating system.

In 2012, the MPS Group performed a full re-assessment of its corporate and retail models with a view to developing the segmentation of corporate models and aligning all models with the new regulatory definition of default which, as of 1 January 2012, provides for the application of a 90-day limit in place of the prior 180-day limit for the reporting of "non-performing" past due and/ or overdue exposures on loans to businesses and retail loans.

In accordance with the roll-out plan, in 2013 the Montepaschi Group carried out an estimation of Rating models for the Non-Banking Financial Institution (NBFI) segment. Furthermore, the Corporate and Retail models were calibrated by including data from the last few years (most representative of the current economic recession) in the time series.

In 2014, the MPS Group continued to update and revise its internal rating system in order to implement the several events which marked 2014 and which, either directly or indirectly, impacted the loan portfolio's risk parameters:

- Firstly, regulatory provisions profoundly changed the framework of prudential supervision in order to strengthen capital requirements and incorporate the new Basel III standards;
- The economic cycle continued to be very severe, with further significant impacts on the level of risk at both system-wide level and on the MPS portfolio. The impact affected risk in the performing portfolio which continued to show very high default rates and a decline in its ability to recover non-performing positions;
- The regulatory exercise known as the «Comprehensive Assessment» and, in particular, the Asset Quality Review

(AQR) revealed a significant impact for the Montepaschi Group;

- Finally, there was a reduction in the closure of non-performing positions, which contributed to increasing the vintage of loans.

The combination of these events led to the need for maintenance actions to be implemented on risk parameters to incorporate a fuller and more up-to-date set of information, as per regulatory requirements.

In the light of these events, the MPS Group decided to adjust all its rating models so that the first AQR results (from the Credit File Review – CFR) could already be included in the 2014 estimates and the LGD model could be re-estimated in line with internal protocol and Group practice which, over the last few years, have always provided for the annual re-estimation/calibration of all models as a result of the persisting economic cycle.

As for LGD, in order to incorporate the most recent findings, a stock of significant positions not yet closed – but for which the recovery process can essentially be considered as closed - was included in the estimation sample (so-called incomplete work-outs). To this end, the percentage of adjustments of operational positions was identified, assuming that the recovery process was essentially concluded for over a certain percentage of coverage. In this connection, a level of coverage in excess of or equal to 99% was identified as significant.

In 2015, as soon as the default detection actions were concluded, the MPS Group recalibrated all of its Corporate and Retail rating models and re-estimated all LGD models in order to fully incorporate the AQR impacts. In particular, the time series used for PD and LGD estimations were shifted by one year so as to include the actual data relating to 2014; given the timing of activities (first quarter), it was not necessary to assess prospective TDs as it was for calibrations in the second half of the year, where they were not available.

The operation at the end of 2014 (incorporated in the recalibration of PD models and re-estimation of LGD models) involved the reclassification of a high number of counterparties from performing to non-performing status and within the non-performing cateogires, which significantly affected the default rate for 2014 as well as the cure rates. The shift in the time series meant that the effects of the operation were fully included in the new calibration.

Moreover, in the course of 2015, the supervisory slotting criteria approach was used to determine capital requirements for Specialized Lending transactions of more than 5 €/mln. Finally, as provided for in the roll-out plan, the Montepaschi Group went ahead with the estimation of Rating models for the "Banks" segment.

Use of Internal Models

Prior to authorisation from the bank of Italy enabling the Montepaschi Group to calculate capital absorptions according to the rules set out for the advanced internal rating systems, the Group used the parameters underlying the calculation of risk Weighted assets also for other operational and internal management purposes. The basic principle called for the use of Basel 2 input factors –as much in line with operating requirements as possible- even though, for obvious reasons, operational practices naturally diverge from supervisory standards, with some methodological fine-tunings and adjustments required for internal purposes and calculation systems. in particular, "across-the board" parameters used for both "supervisory reporting" and "operational" practices are in relation to the Probabilities of default (PD) resulting from internal rating systems and the loss rates on the "impaired" portfolio (LGD). The latter provide the basis of calculation for different systems of measurement and monitoring, and specifically for:

- **Measurement of economic capital for credit risk.** Among the inputs used for the credit model and related VaR output to be operational, the same PD and LGD variables are applied as those that are also used for regulatory purposes. it is clear that certain adjustments have been necessary, such as the use of probabilities of default "not subject" to validation for portfolios other than "corporate" and "retail", resulting from internal rating systems not yet subject to validation or from main rating agencies, appropriately re-mapped to the internal master scale. With regard to LGD, the Group uses parameters estimated on the basis of portfolios subject to validation according to provisions set out by supervisory authorities, although excluding the economic downturn effect that is contemplated only for regulatory purposes; out-of-validation portfolios use parameters estimated on the basis of medium-long term recovery rates, if any, or LGD rates in line with those set out by internal provisions under the FIRB approach. Although EAD for supervisory purposes follows the standard approach as it is pending validation, it is calculated as the sum of drawn amounts plus undrawn balance (committed amount – drawn amount) multiplied by a Credit Conversion Factor (CCF) if this margin is higher than 5% of the committed amount, whilst for margins below this threshold, the EAD is determined as the drawn amount multiplied by a factor (K). Both types of ratios distinguish between Legal Entity, Segment, Type of Exposure, size class and rating class. For Financial and Commercial Signature loans, the EAD is multiplied by a factor (RC), which expresses the probability that the committed amount does not become a balance sheet exposure upon default of the counterparty.

- For **the calculation of risk-adjusted performance and measurement of value creation**, the Group follows the same calculation logic as used in the loan portfolio model both for legal entities subject to validation and for those that are excluded from the scope. Furthermore, whenever new estimates or re-adjustments are made to the internal rating systems subject to validation, adjustment results are incorporated in the Vbm procedures which ensure continuous output alignment with the latest updates.

- The parameters which feed the calculation model for the **risk-adjusted pricing process** are the same as those used for the loan portfolio model, even though with some extensions implicit in the pricing model. The pricing model which price-marks different types of loans with different maturities, requires input not only from the annual Probability of default but also from marginal, forward and multi-period Pds. For these reasons, the Montepaschi Group has developed specific calculation methodologies for these default probabilities, all in compliance with the annual Pd resulting from the validated rating systems. Similarly, lGd calculation is based on the same criteria as those used and mentioned above for the loan Portfolio model, though not taking account of economic downturns.

- In relation to **credit process monitoring**, the following should be noted:
  - processes of loan disbursement to customers included in the airb scope of application have been completely 'reengineered' with the Electronic Credit Facility record software. The Montepaschi Group's counterparty rating is the result of a process which evaluates - in a transparent, structured and consistent manner -all the economic financial, 'behavioural' and qualitative information relative to customers who generate credit risk exposures. The Official rating thus determined has ordinary validity up to the twelfth following month and shall be reviewed by the end of that month. However, the rating review in the monitoring process may be prompted at an earlier date during the validity period if ongoing, major monthly statistical Pd variations – exceeding specific cut-offs -are intercepted. The loan disbursement system is organised into several 'paths', depending on the type of customer and transaction requested, which envisage the possibility of executing the process of assigning a rating to each counterparty and do not allow for any decision-making powers to be exercised in the absence of a valid rating;
  - credit is monitored by using a synthetic Performance Risk Indicator

(it. *Indicatore di Rischio Andamentale*), which is based on internal and external information regarding the customer's trends and behaviours. When given PRI thresholds are exceeded, the position is intercepted within a process whereby the operator is required to comply with certain activities in order to address the irregularities identified;

- the Simplified renewal process is used for low-risk situations and lower amounts. This process is applied to all counterparties with credit facilities subject to revision, which have matured or will mature in the month of reference;
- the principle underlying decision-making powers provides for levels to be assigned on the basis of individual counterparty ratings, the amount of the credit facility requested, the level of risk measured for the Group to which the counterparty belongs, the type of the type of credit facility requested or guarantees required and, finally, the nature of the borrower;
- on the basis of these levels, the system for assigning powers identifies a nominal amount for each risk aggregate: power of approval is assigned to the decision-making bodies, making reference to the combination of rating class and type of loan granted according to the principle of delegating the decision-making powers for the worst ratings to the uppermost levels. Exception to this rule is made for the board of directors, which has the highest level of decision-making powers, and for the levels of approval assigned to corporate decision-making bodies.

The policies for recognition of credit risk mitigation guarantees are implemented through a dedicated IT process which is applied for reporting purposes and does not overlap with the rules for managing guarantees and collaterals applicable to the loan disbursement process.

The IT application manages all rules for the admissibility of guarantees. The process is based on a first step registry of all guarantees, which outlines the Group operational framework. At a later stage, the data of each individual guarantee is assessed through an analysis of its specific characteristics. In particular, the following general requirements are verified:

- legal certainty;
- enforceability of Guarantee against third parties;
- timely liquidation;
- compliance with organisational requirements.

The importance of the internal ratings for operating purposes made it necessary to set up a rating system control and validation unit within the Montepaschi Group, which is organisationally independent from - and acts as a point of reference and guidance for- the unit established for the systems' development, maintenance and review. This unit meets the "credit risk control unit" requirements of statutory regulations for validation controls to be fulfilled.

Control Management model on Internal Rating System

An advanced internal rating system, according to current regulations in force should provide for appropriate forms of review and inspection at all levels of control activities.

The AIRB system used by the Montepaschi Group provides for the execution of automatic controls, i.e. controls regulated by specific operational protocols (e.g. hierarchical controls), within the operating units involved in the process of rating assignment. These controls are aimed at making sure that activities preliminary to rating assignment are properly performed (i.e. selection of a model suitable for customer or transaction assessment, identification of economic or legal relations between customers, compliance with internal procedures oriented to obtaining the information necessary for the assignment and updating of the rating).

The Validation, Monitoring and Risk Reporting

Area (Function Internal Validation) within the Risk Division, shall be responsible for the following levels of review contemplated by the regulations. The Service unit Validation and Monitoring steadily evaluates whether the estimates of all important risk

components are accurate related to internal models. and produces the annual internal rating System (hereinafter IRS) Validation report of the Montepaschi Group expressing an opinion on the regular operations, prediction power and overall performance of the IRB system adopted. The opinion expressed by the Internal Validation Function is then examined by the Corporate Control Functions Coordination Committee, also for the purpose of sharing and agreeing on any remedial actions required. The "Annual Validation Report" is subsequently submitted for approval by the Parent Company's Board of Directors. Furthermore, the Internal Audit Department was assigned the task of assessing the efficiency of the overall structure of controls for the rating system (responsible for review controls).

The methods adopted by the above operating units in relation to the operational procedures of validation and review are briefly illustrated below.

Internal Rating System Validation Process

The responsibility for IRS validation has been allocated to the Head of the Internal Validation Function, which is supported by the Validation and Monitoring Service in carrying out operational activities that are required for validation. Key findings which emerge from the validation controls carried out during the year by the Staff unit are

included in the "Annual Validation Report".
The Validation and Monitoring Service was set up in February 2014 with the specific task of validating certain risk measurement models – regulatory and non-regulatory – by constantly verifying the reliability of results obtained and maintaining alignment with regulatory requirements.
The results of these controls are documented, formalised and transmitted directly to the structures concerned as well as to the Internal Audit Department. Once a year these results are included in the "annual internal rating System Validation report" which expresses an overall opinion on the position of the IRS with respect to the supervisory requirements.
The validation process, within which the abovementioned controls are carried out with a view to finally validating the rating System, consists of the following formal validations:

- validation of processes: checks compliance of the internal rating assignment process with the minimum organisational requirements of CRR and circular no. 285 of the Bank of Italy, with a specific focus on the following aspects:
  - design of allocation processes and, where possible, the backtesting of process results while checks on the efficiency of the processes themselves are performed by the Internal Audit Function;
  - analysis of consistency between the changes in ratings made by an operator and the guidelines issued by the units responsible for the assignment of ratings;
  - verifying the actual use of the rating system within the company, identifying the players and processes involved with a particular focus on the loan disbursement and renewal process;
- validation of **models**: checks that the statistical models for the production of the risk parameters used by the Group MPS maintain specific performance levels and comply with the minimum organisational and quantitative requirements provided for by the rules; and in particular the following is verified:
  - representativeness: checks the consistency between the application population's characteristics in the production of models and the sample used for the estimation;
  - concentration: assesses the level of concentration of counterparties and exposures within the individual rating class, determined by the application of models;
  - performance: assessment of the prediction power of the model and therefore its power to separate highly solvent customers from potentially hazardous customers;
  - calibration: check the risk preliminarily assigned for each class of rating and at

overall level vs. the observed historical risk;

- stability: assessment of the stability of the assigned ratings over time;
- stress testing: review of stress testing activities carried out on the models by the model development unit;

benchmarking: check consistency of ratings assigned internally with those assigned by outside structures on portfolios having a low number of counterparties;

- validation of data: reviews compliance with the minimum requirements set out by the regulations for monitoring the quality of data used by the IRS.

The process of validation involves the preparation of questionnaires for each scope of action identified, with the objective of checking compliance of each aspect of the IRS with regulatory requirements. The detailed positions on each requirement are collated in an overarching opinion of validation through a system of scoring replies and weighting questions, which is part of the framework that has been established and formalized.

The methods chosen meet the requirement of making the process of validation transparent and objective, not only with respect to the Supervisory authorities but especially to each operating unit which develops the IRS and is informed of any faults in the system, for correction. This ensures easier action on the gaps and consequently a better control of the proper operations of the IRS by SVM.

Process of Internal Review of the Internal Rating System

In line with the existing regulations, the Internal Audit Division of the Montepaschi Group adopts the professional Standards and guidelines of the main domestic and international entities, through an independent and objective activity of assurance and advice aimed at controlling, also through on site inspections, the regular operations and risk trend and assessing the functional efficiency and compliance of the Internal Control Systems in order to improve the effectiveness and efficiency of the organisation. The introduction of advanced systems of risk measurement and management determined an extension of activities mandated to the internal audit unit and related responsibilities. The overall review approach focuses on the objective of providing a coherent assessment of adequacy, in terms of both effectiveness and efficiency, of the control systems of the rating-based process of governance and management of credit risk. In particular, the responsibilities assigned to the internal audit unit by the above-mentioned circular, with reference to the review of the advanced models for credit risk assessment and management can be summarised in three following points:

1) assessment of the overall functional efficiency of the control system of the AIRB approach;

2) assessment of the functional efficiency and regularity of the internal validation process;
3) review of system compliance with the requirements for regulatory use of risk estimates.

However, the main operating components attributable to the adoption of an internal rating system require that the review of that process be considered as part of a larger analysis and assessment of the whole loan management process. The objective is to ensure the materialisation of important synergies from the point of view of the actual cost of implementation and, above all, the overall and coherent observation of the events analysed which share different audit findings on the rating process stemming from the reviews carried out in the distribution network and Group companies. The audit controls to be carried out for an assessment of the above-mentioned aspects are guided by efficiency and compliance checks. As a result of the different kinds of control, the internal audit unit performs its responsibilities which consist in reviewing the validity of the whole IRS and the validation process, as well as compliance of the system with regulatory requirements.

Quantitative information

The following table reports the Group's exposure to credit risk – AIRB , as at 31 December 2015 divided by classes of regulatory activities. The exposure values reported are determined according to prudential supervisory requirements and as such are inclusive of value adjustments and do not factor in the effects of risk mitigation techniques which, in the case of exposures subject to an internal models-based approach, are directly included in the risk-weighting factor applied. As for guarantees issued and commitments to disburse funds, the values reported take into account credit conversion factors. Following are the values of risk weighted assets (RWA), expected loss (PA) and actual losses (PE) as at the end of 2015. It is noted that the amount of value adjustments on general-purpose and special-purpose receivables relating to securitisation exposures are not included in the calculation of the Expected Loss Delta, as required by the CRR.

Tab. 5.3.1 – IRB Approach: Summary of Exposures, RWAs, expected and actual losses

Regulatory Portfolio	Exposure	RWA	PA	PE
Exposures to or secured by corporates:	53,998,435	22,171,901	12,867,768	12,455,378
- SMEs	34,404,460	10,697,928	9,382,505	9,355,221
- Other companies	16,995,323	9,968,215	2,906,152	2,734,044
- Specialized lending	2,598,652	1,505,758	579,110	366,114
Retail exposures:	64,177,053	11,258,949	9,142,986	9,557,460
- secured by real estate: SMEs	9,104,309	2,895,329	901,732	778,582
- secured by real estate: Individuals	29,135,293	3,265,009	375,335	399,835
- Qualifying revolving	7,664	1,195	130	126
- Other retail exposures: SMEs	20,845,566	4,658,490	6,311,296	6,573,850
- Other retail exposures: Individuals	5,084,221	438,926	1,554,492	1,805,068
Securitization exposures	9,865	2,360	-	215
IRB Approach Total 31/12/2015	**118,185,352**	**33,433,210**	**22,010,753**	**22,013,053**
IRB Approach Total 31/12/2014	**117,732,184**	**29,140,499**	**19,444,112**	**20,426,015**

The table below shows the breakdown by PD class, identified by the MPS Group to allow for a significant distinction to be made for credit risk (*see* para. 5.3) by Group exposures and regulatory portfolio.

Tab. 5.3.2 – IRB Approach: Exposures, expected and actual losses distribution by regulatory portfolio and PD classes (except for Specialized lending)

	dec-2015				
PD Classes	Exposures vs. Corporates	Retail Exposures	AIRB Total Exposures	AIRB Total EL	AIRB Total AL
Class 01	1,119,353	10,698,176	11,817,529	2,358	2,164
Class 02	4,583,895	10,239,207	14,823,102	12,525	14,941
Class 03	10,552,565	13,045,357	23,597,922	77,905	74,937
Class 04	8,279,562	9,895,937	18,175,499	260,945	265,871
Class 05	1,623,501	1,926,366	3,549,866	215,331	196,237
Class 06	25,240,907	18,372,009	43,612,916	20,862,579	21,092,573
Total	**51,399,783**	**64,177,053**	**115,576,836**	**21,431,643**	**21,646,724**
Total	**50,358,660**	**67,373,524**	**117,732,184**	**19,444,112**	**20,426,015**

The following table shows a breakdown by PD band with quantitative details for the advanced IRB approach of the Portfolio “Exposures to or guaranteed by businesses” divided by regulatory asset class:

- *SMEs,*
- *Other companies,*
- *Specialized lending – slotting criteria.*

Tab. 5.3.3 – IRB approach: Exposures to or secured by corporates - SMEs

Rating Class	Nominal Value	Exposure Value	Revocable and Irrevocable Margins	CCF% (Average)	Weighted Average PD (%)	Weighted Average LGD(%)	Average Risk Weight % (RW%)
Class 01	694,032	402,845	316,937	8.12%	0.10%	37.19%	21.09%
Class 02	2,779,726	1,873,235	1,037,947	12.67%	0.35%	36.63%	41.59%
Class 03	6,243,883	5,053,479	1,571,335	24.24%	1.22%	33.50%	63.55%
Class 04	6,874,261	6,102,146	965,113	20.00%	4.91%	30.80%	85.53%
Class 05	1,133,964	1,016,830	152,646	23.26%	22.47%	29.78%	137.97%
Class 06	20,584,155	19,955,923	1,022,860	38.58%	100.00%	44.08%	-
Total 31/12/2015	**38,310,021**	**34,404,460**	**5,066,839**	**18.96%**	**4.13%**	**32.61%**	
Total 31/12/2014	**35,522,390**	**32,276,311**	**4,050,870**	**18.66%**	**4.31%**	**28.71%**	

(a) For reporting purposes, Unused Margin refer to issued guarantees and revocable and irrevocable commitments to disburse funds
(b) The weighted average PD (%) and weighted average LDG (%) under Total does not include class 6

Tab. 5.3.4 – IRB approach: Exposures to or secured by corporates - Other companies

Rating Class	Nominal Value	Exposure Value	Revocable and Irrevocable Margins	CCF% (Average)	Weighted Average PD (%)	Weighted Average LGD(%)	Average Risk Weight % (RW%)
Class 01	3,628,196	716,508	3,224,030	9.69%	0.09%	42.83%	24.17%
Class 02	7,677,760	2,710,659	5,500,231	9.69%	0.36%	42.16%	52.97%
Class 03	9,704,740	5,499,086	5,240,698	19.75%	1.09%	41.48%	84.99%
Class 04	3,153,266	2,177,415	1,212,551	19.52%	4.03%	41.07%	126.93%
Class 05	878,688	606,670	414,449	34.37%	18.64%	28.69%	151.93%
Class 06	5,913,239	5,284,984	866,486	27.49%	100.00%	52.70%	-
Total 31/12/2015	**30,955,889**	**16,995,323**	**16,458,443**	**14.49%**	**2.31%**	**40.98%**	
Total 31/12/2014	**32,587,536**	**18,082,349**	**17,357,417**	**15.95%**	**2.03%**	**37.09%**	

(a) For reporting purposes, Unused Margin refer to issued guarantees and revocable and irrevocable commitments to disburse funds
(b) The weighted average PD (%) and weighted average LDG (%) under Total does not include class 6

Tab. 5.3.5 – IRB approach: Specialized lending – slotting criteria

Risk weight	Nominal Value	Exposure Value	RWA	Value adjustments	Expected Loss
Category 1 - 50%	-	-	-	-	-
Category 1 - 70% equal to or greater than 2.5 years	17,465	17,465	12,225	102	70
Category 2 - 70% less than 2.5 years	125,169	121,029	84,720	879	484
Category 2 - 90%	973,826	942,657	848,391	11,157	7,541
Category 3 - 115%	408,536	380,156	437,180	10,029	10,644
Category 4 - 250%	57,364	49,297	123,242	136	3,944
Category 5 - 0%	1,170,061	1,088,049	-	343,811	556,427
Total 31/12/2015	**2,752,421**	**2,598,652**	**1,505,758**	**366,114**	**579,110**
Total 30/06/2015	**3,551,700**	**3,203,242**	**1,775,481**	**388,621**	**704,969**
Total 31/12/2014	**-**	**-**	**-**	**-**	**-**

The following table shows a breakdown by PD band with quantitative details for the advanced IRB approach of the Portfolio "Retail Exposures" divided by regulatory asset class:

- *Secured by real estate - SMEs,*
- *Secured by real estate - Individuals,*
- *Qualifying revolving,*
- *Other retail exposures - SMEs,*
- *Other retail exposures - Individuals.*

Tab. 5.3.6 – IRB approach: Retail Exposures Secured by real estate - SMEs

Rating Class	Nominal Value	Exposure Value	Revocable and Irrevocable Margins	CCF% (Average)	Weighted Average PD (%)	Weighted Average LGD(%)	Average Risk Weight % (RW%)
Class 01	50,674	49,618	2,111	50.00%	0.11%	19.41%	4.26%
Class 02	513,700	506,220	14,740	49.25%	0.37%	19.88%	11.47%
Class 03	2,243,223	2,206,752	70,316	48.13%	1.22%	19.89%	26.35%
Class 04	2,959,576	2,891,715	133,260	49.08%	4.45%	20.23%	55.93%
Class 05	642,123	613,067	57,519	49.49%	25.39%	20.50%	103.78%
Class 06	2,886,553	2,836,936	84,498	41.28%	100.00%	25.72%	-
Total 31/12/2015	**9,295,849**	**9,104,309**	**362,445**	**48.94%**	**5.00%**	**20.10%**	
Total 31/12/2014	**10,737,321**	**10,486,140**	**507,733**	**52.38%**	**4.79%**	**18.62%**	

(a) For reporting purposes, Unused Margin refer to issued guarantees and revocable and irrevocable commitments to disburse funds
(b) The weighted average PD (%) and weighted average LDG (%) under Total does not include class 6

Tab. 5.3.7 – IRB approach: Retail Exposures Secured by real estate - Individuals

Rating Class	Nominal Value	Exposure Value	Revocable and Irrevocable Margins	CCF% (Average)	Weighted Average PD (%)	Weighted Average LGD(%)	Average Risk Weight % (RW%)
Class 01	10,106,583	10,095,276	20,238	44.13%	0.13%	13.12%	4.04%
Class 02	7,879,830	7,857,429	40,678	44.93%	0.31%	12.80%	7.42%
Class 03	6,731,422	6,712,889	33,528	44.73%	1.00%	12.38%	16.22%
Class 04	1,880,147	1,870,131	17,320	42.17%	4.47%	12.79%	40.40%
Class 05	596,598	593,069	4,625	23.69%	26.59%	12.36%	72.60%
Class 06	2,027,580	2,006,499	22,632	6.85%	100.00%	15.47%	-
Total 31/12/2015	**29,222,159**	**29,135,293**	**139,021**	**43.48%**	**1.27%**	**12.80%**	
Total 31/12/2014	**30,153,942**	**30,106,751**	**93,781**	**58.81%**	**0.95%**	**12.39%**	

(a) For reporting purposes, Unused Margin refer to issued guarantees and revocable and irrevocable commitments to disburse funds
(b) The weighted average PD (%) and weighted average LDG (%) under Total does not include class 6

Tab. 5.3.8 – IRB approach: Qualifying revolving Retail Exposures

Rating Class	Nominal Value	Exposure Value	Revocable and Irrevocable Margins	CCF% (Average)	Weighted Average PD (%)	Weighted Average LGD(%)	Average Risk Weight % (RW%)
Class 01	19,650	852	18,798	0.00%	0.13%	31.47%	2.50%
Class 02	16,942	1,486	15,456	0.00%	0.33%	29.24%	4.94%
Class 03	19,072	1,707	17,365	0.00%	1.05%	28.45%	11.85%
Class 04	9,234	3,197	6,038	0.00%	4.10%	21.66%	24.24%
Class 05	1,218	155	1,062	0.00%	23.58%	28.40%	79.30%
Class 06	2,295	267	2,028	0.00%	100.00%	31.72%	-
Total 31/12/2015	**68,411**	**7,664**	**60,747**	**0.00%**	**2.59%**	**26.02%**	
Total 31/12/2014	**16,713**	**8,868**	**7,846**	**0.00%**	**1.91%**	**22.65%**	

(a) For reporting purposes, Unused Margin refer to issued guarantees and revocable and irrevocable commitments to disburse funds
(b) The weighted average PD (%) and weighted average LDG (%) under Total does not include class 6

Tab. 5.3.9 – IRB approach: Other retail Exposures - SMEs

Rating Class	Nominal Value	Exposure Value	Revocable and Irrevocable Margins	CCF% (Average)	Weighted Average PD (%)	Weighted Average LGD(%)	Average Risk Weight % (RW%)
Class 01	1,854,069	399,875	1,558,790	6.71%	0.10%	43.01%	8.78%
Class 02	4,100,134	1,481,756	2,817,051	7.05%	0.35%	42.57%	20.56%
Class 03	6,678,442	3,542,629	3,500,135	10.41%	1.18%	41.93%	38.69%
Class 04	6,818,372	4,670,293	2,337,839	8.12%	4.72%	41.63%	52.44%
Class 05	782,173	640,744	153,058	7.60%	21.34%	41.32%	77.87%
Class 06	10,607,365	10,110,270	536,650	7.37%	100.00%	61.12%	-
Total 31/12/2015	**30,840,555**	**20,845,566**	**10,903,522**	**8.38%**	**3.77%**	**41.89%**	
Total 31/12/2014	**33,351,530**	**21,969,599**	**12,585,229**	**9.75%**	**3.94%**	**38.28%**	

(a) For reporting purposes, Unused Margin refer to issued guarantees and revocable and irrevocable commitments to disburse funds
(b) The weighted average PD (%) and weighted average LDG (%) under Total does not include class 6

Tab. 5.3.10 – IRB approach: Other retail Exposures - Individuals

Rating Class	Nominal Value	Exposure Value	Revocable and Irrevocable Margins	CCF% (Average)	Weighted Average PD (%)	Weighted Average LGD(%)	verage Risk Weight % (RW%)
Class 01	621,802	152,554	470,588	0.28%	0.13%	22.23%	7.07%
Class 02	749,516	392,316	374,895	4.72%	0.34%	25.12%	14.88%
Class 03	1,010,607	581,381	448,036	4.20%	1.13%	23.18%	25.52%
Class 04	597,358	460,601	189,559	27.85%	4.36%	25.10%	38.39%
Class 05	85,738	79,330	6,589	2.75%	24.13%	23.37%	56.19%
Class 06	3,447,360	3,418,038	31,017	5.47%	100.00%	43.75%	-
Total 31/12/2015	**6,512,380**	**5,084,221**	**1,520,683**	**6.10%**	**2.84%**	**24.09%**	
Total 31/12/2014	**6,136,025**	**4,802,167**	**1,432,718**	**6.95%**	**2.92%**	**20.93%**	

(a) For reporting purposes, Unused Margin refer to issued guarantees and revocable and irrevocable commitments to disburse funds
(b) The weighted average PD (%) and weighted average LDG (%) under Total does not include class 6

Exposures subject to the AIRB approach broken down by geographical location

The Montepaschi Group operates almost exclusively in the domestic market. If the geographical location of the counterparties is considered, 99.99% of AIRB exposures are towards counterparties resident in Italy.

For the purposes of this disclosure and in accordance with Article 452 of the CRR, the relevant geographical location of credit exposures means exposures in the Member States in which the institution has been authorised and Member States or third countries in which institutions carry out activities through a branch or subsidiary. As far as credit risk is concerned, the Group is currently authorized to use internal estimates of PD, LGD parameters for portfolios of loans to locals Counterparties (Companies and Retail Exposures) of the main Italian subsidiaries of the Group, namely Banca Monte dei Paschi di Siena, MPS Capital Services and MPS Leasing & Factoring. The other foreign subsidiaries (MP Banque and MP Belgio) adopt standard models and their exposures are included among those subject to credit risk – the standard approach. The Group also operates in Member States or third countries via foreign branches, whose operations focus on supporting the expansion of Italian businesses and investments abroad and in the major foreign financial markets. AIRB credit exposures (net of default) held by foreign branches amount to 0.003% and are entirely towards local counterparties (with headquarters/residence or domicile in Italy). The exposures are towards counterparties that were assigned an internal PD and LGD estimate since they are already counterparties of Italian subsidiaries and are reported under the Parent Company Banca MPS for regulatory purposes Accordingly, the values of the exposure-weighted average PD and LGD by geographical location coincide with those reported in the tables above which show the AIRB exposures of authorised Italian subsidiaries broken down by class of exposure. Reported below are the credit exposures subject to the AIRB approach (net of default) according to the definition of geographical location described above, i.e. by Member State in which the institution has been authorised (Italy) and by Member State or third country in which the insitution operates through a branch.

Tab. 5.3.11 – IRB approach: Exposures to or secured by corporates – Geographic Segmentation

		EAD	Incidence	Weighted Average PD	Weighted Average LGD
Exposures to or secured by corporates	Italy	26,157,091	99.99%	3.32%	36.35%
	Other EU Countries	275	0.00%	0.07%	48.11%
	America	1,510	0.01%	1.05%	44.74%
	Total	**26,158,876**	**100.00%**	**3.32%**	**36.35%**

Tab. 5.3.12 – IRB approach: Retail Exposures – Geographic Segmentation

		EAD	Incidence	Weighted Average PD	Weighted Average LGD
Retail exposures	Italy	45,804,958	100.00%	2.43%	21.03%
	Other EU Countries	0	0.00%	6.31%	11.63%
	America	85	0.00%	9.95%	44.74%
	Total	**45,805,043**	**100.00%**	**2.43%**	**21.03%**

Comparison between expected loss and actual loss

As part of the backtesting of the parameters of AIRB models, the MPS Group makes a comparison between the expected loss estimated at 31 December of the previous year and the actual loss observed at year end. In order to clarify the results of the comparison it should be noted that although the two amounts are comparable, they are calculated on the basis of different logics.

Expected Loss (PA) is the average loss that the bank expects to face against a loan or loan portfolio classified as performing at the end of the previous year. It is calculated as the product between PD, LGD and EAD estimated in compliance with the prudential requirements; in particular, PD is estimated using a longer time series and thus better reflects risk in the portfolio on a through-the-cycle (TCC) basis.

Actual Loss is calculated as the total amount of provisions which were actually registered and recognised in the income statement on performing exposures as at 31 December of the previous year subsequently classified to default status one year later.

Taking into account what has been observed, i.e., that the expected loss expresses an estimation of loss essentially calculated on a TTC basis whereas the actual loss refers to what has been registered and recognised in a specified year, a comparison is provided between expected loss and actual loss ex-post in 2012, 2013, 2014, 2015 on corporate and retail exposures.

Tab. 5.3.13 – Comparison Expected Loss – Actual Loss

Reference Year	Portfolio	Expected Loss	Actual Loss	EL vs AL (var %)
2012	Exp. vs Corporates	542,000	738,000	36.1%
	Retail Exp.	332,000	272,000	-18.1%
	TOTAL	**874,000**	**1,009,000**	**15.5%**
2013	Exp. vs Corporates	507,000	784,000	54.7%
	Retail Exp.	276,000	232,000	-15.9%
	TOTAL	**783,000**	**1,016,000**	**29.8%**
2014	Exp. vs Corporates	425,000	1,371,000	222.8%
	of which implementing AQR	*140,000*	*933,000*	*567.2%*
	of which not implementing AQR	*285,000*	*438,000*	*53.7%*
	Retail Exp.	251,000	489,000	94.6%
	of which implementing AQR	*35,000*	*276,000*	*687.9%*
	of which not implementing AQR	*216,000*	*213,000*	*-1.4%*
	TOTAL	**676,000**	**1,860,000**	**175.2%**
	of which implementing AQR	*175,000*	*1,209,000*	*591.4%*
	of which not implementing AQR	*501,000*	*651,000*	*29.9%*
2015	Exp. vs Corporates	504,000	586,000	16.3%
	of which SMEs	*169,000*	*207,000*	*22.6%*
	of which Other companies	*91,000*	*85,000*	*-5.6%*
	of which secured by real estate: SMEs	*66,000*	*81,000*	*21.6%*
	of which Other retail exposures: SMEs	*178,000*	*213,000*	*19.4%*
	Retail Exp.	44,000	97,000	120.4%
	of which secured by real estate: Individuals	*33,000*	*74,000*	*128.1%*
	of which Other retail exposures: Individuals	*11,000*	*23,000*	*98.6%*
	TOTAL	**548,000**	**683,000**	**24.6%**

Expected loss and actual loss values refer respectively to the expected loss registered at the start of the year and the actual loss registered at year-end on a sample of exposures analysed. The sample relates to the exposures of positions which at the start of the year were classified as performing and which transitioned to default status in the course of the year. Corporate exposures also include regulatory classes of exposures secured by real estate - SMEs and other retail exposures - SMEs.

The comparison shows that the difference between actual loss and expected loss for 2012 and 2013 is due to the different logics applied in calculating the two amounts; the largest difference between actual loss and expected loss registered in 2013 for the corporate segment (exposures vs. corporates) largely relates to the higher default rates and the significantly lower levels of recovery for non-performing loans vs. the PD rate estimated at the beginning of the period, resulting from a strongly recessive and worse-than-expected economic cycle when compared to the expectations included in the models. Expected loss calculated with TTC AIRB models does not fully reflect the challenging economic conditions registered in 2013. An even greater difference between actual and expected loss is shown for 2014 since, in addition to the items already reported in 2013, there were additional non-recurring provisions relating to the AQR remedial actions at the end of 2014, designed to incorporate the results of the Asset Quality Review.

Indeed, in 2014 the MPS Group implemented these extraordinary actions on provisioning levels in the portfolios which had been subject to review and included, in its 2014 financial statements, the ECB requirements communicated to the MPS Group (October 2014) upon completion of the AQR exercise. The logics for reviewing assets on the basis of ECB supervisory guidelines resulted in a tougher assessment of the level of credit risk and a consequent increase in coverage levels on exposures. During 2015, the more stringent criteria for the identification of forbearance and the economic conditions of the negative cycle led to an additional element of conservatism in the identification of defaulting flows, which remains high For these reasons, the expected loss calculated using the AIRB TTC models is approximately 25% lower than the actual expected loss.

Comparison between estimated and actual results of backtesting

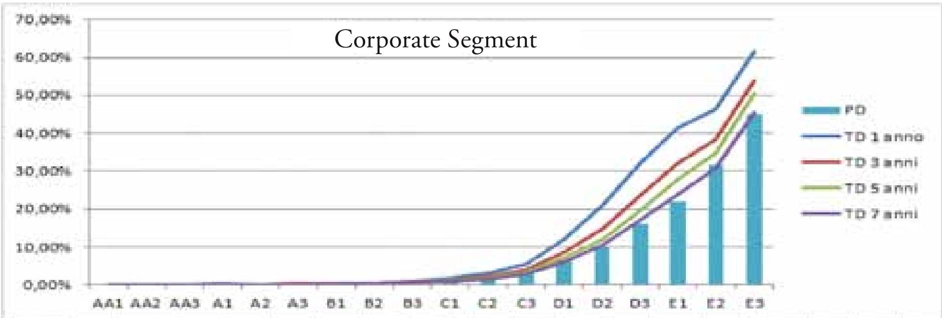
As previously pointed out, the Monte dei Paschi Group adopts advanced models to determine capital requirements for 'corporate' and 'retail' portfolios. Internally estimated PD (Probability of Default) and LGD (Loss Given Default) parameters are therefore used for both portfolios.

A comparison of estimated vs. actual losses is made on a yearly basis within the framework of PD and LGD backtesting by internal first and second level control functions.

As for PD, statistical models are monitored using a structured automated algorithm. Monitoring consists in a determined number of tests aimed at assessing whether the characteristics of the models in the implementation/production environment continue to be similar to those found in the development phase, in terms of representativeness and performance. Within the monitoring process, estimated PDs are compared against observed default rates through a set of tests designed to verify the alignment between the Probability of Default and Default Rates both for the latest period of reference and for the time series equal to the one used for estimation, in line with the development methodological approach based on long-term average values. The impact on any underestimated default rates on the variables used to measure credit risk (Expected Loss and Regulatory Capital) is also quantified. The overall outcome is formulated on the basis of an internal protocol, which also includes the actions to be put in place in the event of a negative outcome.

Comparison between PD and Default Rates observed by rating class for the Corporate segment

The following tables show the comparison between regulatory PD and default rates observed by rating class for the Corporate segment on different time series.



CLASSE	AA1	AA2	AA3	A1	A2	A3	B1	B2	B3	C1	C2	C3	D1	D2	D3	E1	E2	E3
TD 1 anno	0,00%	0,00%	0,08%	0,21%	0,12%	0,31%	0,26%	0,37%	1,01%	1,68%	3,04%	5,54%	11,82%	20,98%	31,95%	41,47%	46,16%	61,65%
TD 3 anni	0,00%	0,00%	0,05%	0,13%	0,08%	0,20%	0,25%	0,43%	0,74%	1,24%	2,21%	4,11%	8,61%	14,74%	23,54%	32,04%	38,45%	53,99%
TD 5 anni	0,00%	0,00%	0,05%	0,10%	0,09%	0,16%	0,22%	0,37%	0,63%	1,02%	1,79%	3,34%	7,01%	12,04%	19,66%	27,82%	34,70%	50,42%
TD 7 anni	0,00%	0,00%	0,07%	0,11%	0,10%	0,14%	0,20%	0,34%	0,56%	0,92%	1,57%	2,90%	6,09%	10,53%	17,00%	23,97%	30,00%	45,53%
PD	0,03%	0,05%	0,09%	0,13%	0,20%	0,30%	0,46%	0,69%	1,05%	1,59%	2,42%	3,99%	6,31%	9,95%	16,03%	22,12%	31,63%	45,00%

The comparison shows how the alignment between regulated PD calculated on a TTC basis and average default rates on different time series' is gradually reduced as the time series used in calculating the average default rates decreases. This shows that regulatory PDs calculated on a TTC basis are immediately comparable with default rates calculated on long-term time horizons, whereas comparability tends to decrease as the time horizon applied decreases.

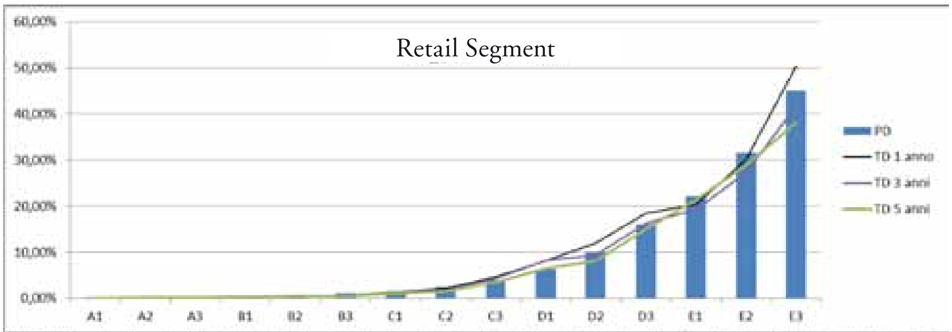
The results of the annual calibration tests were not satisfactory for the Corporate models, particularly for the Construction sector (Multiannual) and Small Business segment which registered misalignments between the estimated PD and default rates observed.

Multiannual tests (on a TTC basis), instead, confirmed a satisfactory level of alignment between PD and Default Rate.

The performances of Corporate models in terms of discriminative power were, on the other hand, fully positive and confirmed the good grading ability of the models, with levels of accuracy that were very much in line with the ranges recognised in AIRB PD model best practices.

Comparison between PD and Default Rates observed by Rating Class for the Retail segment

The information shown for the Retail segment is similar to that reported for the Corporate models.



CLASSE	A1	A2	A3	B1	B2	B3	C1	C2	C3	D1	D2	D3	E1	E2	E3
TD 1 anno	0,08%	0,12%	0,20%	0,39%	0,53%	0,60%	1,43%	2,13%	4,68%	8,10%	12,09%	18,41%	20,43%	30,00%	50,48%
TD 3 anni	0,11%	0,18%	0,28%	0,41%	0,50%	0,59%	1,25%	1,82%	4,31%	8,23%	9,44%	16,27%	19,30%	27,38%	41,64%
TD 5 anni	0,10%	0,17%	0,27%	0,38%	0,46%	0,55%	1,08%	1,36%	3,55%	6,41%	8,10%	15,07%	21,42%	28,85%	38,22%
PD	0,13%	0,20%	0,30%	0,46%	0,69%	1,05%	1,59%	2,42%	3,99%	6,31%	9,93%	16,03%	22,12%	31,63%	45,00%

The default rates observed for the Retail segment are broadly in line with regulatory PD and show an essentially flat rend which increases as rating class risk exposures increase.

The performances of Retail models in terms of discriminative power were positive and confirmed the good grading ability of the models, with levels of accuracy that were in line with the ranges recognised in AIRB PD model best practices.

5.4 Credit Risk: value adjustments

For classification of impaired loans into the various categories of risk (non-performing, unlikely-to-pay and non-performing past due exposures), the Montepaschi Group refers to the regulations issued by the bank of Italy, as supplemented with internal provisions which set out automatic criteria and rules for the transfer of receivables from and to different risk categories.

In particular, classification is carried out by bodies within the loan decision-making chain based on a process that provides for a series of codified controls aiming to guarantee proper asset classification, except for loans more than 90 days past due, which are measured using automated procedures.

In line with supervisory definitions, non-performing loans are intended to include the following:

- Non-performing past due loans,
- Unlikely to pay,
- Doubtful loans.

Non-performing loans also include some of the loans concerned by the general concept of restructuring, namely:

- Forborne exposures (as set out in Bank of Italy Circular no. 272);
- debt settlement via borrower substitution or debt-for-equity swap.

In compliance with Bank of Italy regulations, "forborne exposures" are debt contracts in respect of which forbearance measures have been extended. Forbearance measures consist of concessions – the modification and/or refinancing of a troubled debt contract – towards a debtor facing or about to face difficulties in meeting its financial commitments (financial difficulties).

Non-performing exposures with forbearance measures, pursuant to the ITS, are those exposures which represent a sub-category of, depending on the case, doubtful loans, unlikely to pay or non-performing past due; they do not make up their own category of non-performing exposures.

During the year, the new rules for identifying forborne exposures were integrated within the Electronic Loan File. If a new facilitation or a change in the credit line which amounts to a new concession is requested, the manager is asked to evaluate the counterparty's financial difficulty. With support from the procedure, the manager establishes whether the borrower is in financial difficulty and how severe it is. If the financial difficulty is serious, the manager should decide, in addition to the concession, on whether to change the counterparty's classification to unlikely to pay.

As an alternative to the previously described options (renegotiations due to borrower difficulties and re-negotiations for commercial reasons/practice Bank and the borrower may agree on settlement of the original debt via:

- novation or assumption of the loan by another borrower (release from debt liability);
- substantial modification of loan terms involving a debt-equity swap.

Said events, involving a substantial modification of contractual terms, provide for cancellation of the pre-existing loan agreement from an accounting standpoint, and consequent booking of the new agreement at fair value, recognising through profit or loss an amount corresponding to the difference between the fair value of assets received and the book value of the cancelled loan.

There are then other loans concerned by the general concept of restructuring which, instead, fall under the status of performing exposures and are, therefore, excluded from the category of non-performing loans. These are forborne performing exposures pursuant to the ITS and involve the renegotiation of loans granted by the bank to performing customers. The renegotiation is substantially equated with the opening of a new position, if it is granted essentially for commercial reasons rather than for the borrower's economic-financial difficulties and provided that the interest rate applied is a market rate as at the date of renegotiation.

The classification of positions into the different categories of non-performing assets is carried out upon proposals by both the sales and distribution network and outer and central specialist units responsible for credit control and management.

On the other hand, as far as non-performing past due loans are concerned, the classification under non-performing status occurs automatically when given default conditions are exceeded.

The return of non-performing exposures to performing status occurs on the initiative of the above-mentioned units in charge of credit control and management, with the prior confirmation that the critical/default conditions no longer apply. As regards the non-performing past due loans, the return to performing status occurs automatically once the exposure is reimbursed.

Doubtful loans, unlikely-to-pay loans and non-performing past due loans that have exposures exceeding a given threshold value are subject to an individaul assessment process. For all non-performing exposures below a given threshold value, a statistic-based assessment is carried using parameters determined by the Risk Management Function.

The assessment is performed during their classification or upon the occurrence of a significant event and is revised on a regular basis.

Methodology for determining value adjustments

At each balance-sheet date, in linea con lo IAS 39, the financial assets not classified as held-for-trading or designated at fair value are evaluated to check whether there is objective evidence of impairment that might render the book value of these assets not entirely recoverable.

A financial asset has suffered a reduction in value if there is objective evidence of a reduction in future cash flows compared with those originally estimated as a result of one or more specific events that have occurred after initial recognition; the loss should be determined reliably and in relation to recent events.

The reduction in value may also be caused not by a single separate event but by the combined effect of several events.

The objective evidence that a financial asset or group of financial assets has suffered a reduction in value includes measurable data that arise from the following events:

- significant financial difficulty of the issuer or debtor;
- breach of contract, for example non-fulfilment or failure to pay interest or principal;
- granting beneficiary a credit facility that the Group has taken into consideration primarily for economic or legal reasons related to the beneficiary's financial difficulties and that would not have been granted otherwise;
- a reasonable probability that the beneficiary will file for bankruptcy or other financial restructuring procedures.

For the purpose of determining adjustments to the book-value of loans (customer loans, loans to banks, unsecured loans), an analytical and collective valuation is carried out considering the various levels of impairment as indicated below.

An **analytical assessment** is performed on exposures which exceed a given threshold, according to the following categories:

- doubtful loans;
- unlikely to pay;
- non-performing past due loans.

Conversely, the following are subject to collective assessment:

- performing loans;
- non-perfroming loans below a given threshold value not subject to analytical or individual assessment;
- exposures subject to country risk.

For loans subject to **analytical assessment**, the amount of value adjustment for each loan is equal to the difference between the loan book value at the time of measurement (amortised cost) and the current value of estimated future cash flows, as calculated by applying the original effective interest rate. Where the original rate is not directly available, or if retrieving it is excessively costly, the best approximation is applied. For all fixed-rate positions, the interest rate determined in this way is kept constant also in subsequent years, while for variable-rate positions, the interest rate is updated according got the variable component of reference whilst keeping the originally stipulated spread steady.

Expected cash flows take account of the expected repayment schedule, the expected recovery value of collaterals, if any, as well as the costs expected to be incurred for the recovery of the credit exposure.

The value adjustments are booked to the profit and loss statement under item "130 - Net impairment losses (reversals)".

If the quality of the non-performing receivable has improved to such a point that there is no reasonable certainty of timely recovery of the principal and interest, its initial value is recycled in the following years to the extent in which the reasons determining the adjustment disappear, provided that such valuation can be objectively linked with an event which occurred after the adjustment. The reversal is posted to the profit and loss statement an may not in any case exceed the amortised cost that the receivable would have had without prior adjustments.

Receivables with no objective evidence of loss are subject to a collective assessment of impairment. Such assessment is carried out by category, with receivables grouped together according to credit risk, and the relative loss percentages are estimated taking into account time-series based on elements observed on the date of assessment which allow the value of latent loss in each category to be estimated. The segmentation drivers used for this purpose consist of: economic sectors of activity, geographical location and customer segments (turnover); on the basis of the latter indicator, the main segments of the portfolio are differentiated as follows:

- Retail;
- Small and Medium Enterprise Retail;
- Small and Medium Enterprise Corporate;
- Corporate;
- Large Corporate;
- Nbfi;
- Banks;
- Other.

The rate of loss is determined for each portfolio segment, using the historical experience of the Group as reference.

In particular, the impairment for the year of each loan belonging to a particular category is given by the difference between the book value and the recoverable amount on the date of valuation, with the latter being determined by using the parameters of the calculation method provided for by the new supervisory provisions, represented by PD (probability of default) and LGD (loss given default).

Value adjustments determined collectively are posted to the income statement. Any additional write-downs or write-backs are recalculated on a differential basis, at year-end or on the dates of interim reports, with reference to the entire loan portfolio on the same date.

For further information on the loan accounting policies, *please refer* to Part A of the Notes to the Consolidated Financial Statement as at 31.12.2015. For further information regarding value adjustments, *please refer* to the Notes to the Consolidated Financial Statements as at 31.12.201, Part E, Quantitative Information, A. Credit Quality.

In particular reference should be made to:

- table A.1.1 of this section of the Consolidated Financial Statements for a breakdown of credit exposures by portfolio (material exposure class) and credit quality (art. 442 para. d of the CRR);
- table B.2/B.3 of this section of the Consolidated Financial Statements for a breakdown of credit exposures by material exposure class, credit quality and significant area (art. 442 para. d/h of the CRR);
- table B.1 of this section of the Consolidated Financial Statements for a breakdown of credit exposures by significant industry or counterparty type, disclosing the amount of impaired exposures and specific and general credit risk adjustments (art. 442 para.g/ i) ii) of the CRR);
- tables 1 and 2 in section 1.3 – Liquidity Risk of Part E of the Notes to the Consolidated Financial Statements for residual maturity breakdown of all exposures (art. 442 para.f of the CRR);
- tables A.1.5 and A.1.8 of Section A. Credit Quality, Part E of the Notes to the Consoldiated Finanical Statements as at 31.12.2015 for a description of gross non-performing exposures (art. 442 para. i of the CRR).

Quantitative information

The table below shows a summary of non-performing and performing exposures, adjustments (specific and by portfolio) and net values subject to Standard and AIRB methods.

Tab. 5.4.1 – Credit Risk: value adjustments

Supervisory Perimeter	dec-15 Not Performing Exposures	Performing Exposures	Adjustments	Net Values
AIRB	**44,700,965**	**73,484,387**	**22,013,053**	**96,172,300**
of which Off-Balance Sheet (guarantees and liabilities)	*-*	*5,174,310*	*181,067*	*4,993,243*
SMEs	19,955,923	14,448,537	9,355,221	25,049,239
Other companies	5,284,984	11,710,339	2,734,044	14,261,279
Specialized lending - Slotting criteria	1,088,049	1,510,604	366,114	2,232,538
Secured by real estate - SMEs	2,836,936	6,267,373	778,582	8,325,727
Secured by real estate - Individuals	2,006,499	27,128,795	399,835	28,735,459
Qualifying revolving Retail Exposures	267	7,397	126	7,538
Other retail Exposures - SMEs	10,110,270	10,735,297	6,573,850	14,271,717
Other retail Exposures - Individuals	3,418,038	1,666,182	1,805,068	3,279,153
Securitization exposures	-	9,865	215	9,650
STD	**2,991,857**	**59,301,980**	**1,545,628**	**60,748,209**
of which Off-Balance Sheet (guarantees and liabilities)	*14,785*	*1,636,163*	*6,687*	*1,644,262*
Total 31/12/2015	**47,692,822**	**132,786,368**	**23,558,681**	**156,920,508**

Supervisory Perimeter	dec-14 Not Performing Exposures	Performing Exposures	Adjustments	Net Values
AIRB	**41,713,971**	**76,018,213**	**20,426,015**	**97,306,169**
of which Off-Balance Sheet (guarantees and liabilities)	*-*	*5,262,320*	*184,717*	*5,077,603*
SMEs	17,955,440	14,320,871	8,356,708	23,919,603
Other companies	5,691,176	12,391,173	2,906,474	15,175,875
Secured by real estate - SMEs	3,104,366	7,381,774	823,962	9,662,178
Secured by real estate - Individuals	1,840,530	28,266,221	349,734	29,757,017
Qualifying revolving Retail Exposures	202	8,666	90	8,778
Other retail Exposures - SMEs	10,053,113	11,916,486	6,371,460	15,598,138
Other retail Exposures - Individuals	3,069,144	1,733,022	1,617,587	3,184,579
STD	**4,899,256**	**77,431,357**	**2,792,191**	**79,538,422**
of which Off-Balance Sheet (guarantees and liabilities)	*243,121*	*1,750,316*	*25,417*	*1,968,020*
Total 31/12/2014	**46,613,226**	**153,449,571**	**23,218,206**	**174,876,571**

5.5 Credit Risk: use of risk mitigation techniques

With reference to the retail and corporate loan portfolio, the Montepaschi Group does not apply any netting processes to the credit risk exposures with on- or off-balance sheet items with opposite sign. The Montepaschi Group adopts policies reducing the counterparty risk with institutional counterparties, by entering into netting agreements and collateral agreements both in relation to derivatives and repos *(repurchase agreements)*.

The Montepaschi Group has fulfilled the obligations set out by the New regulations for Prudential Supervision for the purpose of recognition of risk mitigation effects produced by any existing collaterals securing the loan.

The disbursement of loans secured by collaterals is subject to specific control measures, differentiated by type of guarantee pledged, which are applied during the phase of disbursement and monitoring. Two main types of guarantees, subject to different regulations, can be identified by volumes of loans granted and number of customers, namely Mortgages and Pledges (cash and Securities).

With reference to compliance with the main organisation requirements for the mitigation of risk, the Group ensured:

- the presence of an IT system in support of the life cycle phases of the guarantees (acquisition, valuation, management, revaluation and enforcement);
- regulated policies for the management of guarantees (principles, practices, processes), available to the users;
- the presence of regulated, documented procedures for the management of guarantees (principles, practices, processes), available to the users;
- independence of the customers' insolvency risk (internal rating) from any existing collaterals.

For the purpose of limiting residual risks (termination or non-existence of the value of protection), the Montepaschi Group requires that:

- in the case of a mortgage guarantee, the acquisition of the right be flanked by the underwriting of insurance policies (catastrophic events) in relation to the assets covered by the guarantee, and a report prepared by reliable experts;
- in the case of a pledge, the original value should be reinstated (ensuring the continuity of the guarantee through papers amending the original guarantee) in view of the depreciation of goods pledged in the case of redemption of the pledge, the repayment should be made at the bank (collection).

The Montepaschi Group identified a set of technical forms (by purpose of the loan/type of customer) providing for the admissibility of mortgage guarantees. Within the IT system, the proposal of financing one of these types of loans triggers a request for detailed information on the characteristics of the real estate subject to guarantee (valuation) which, after loan approval, will make the acquisition steps compulsory.

In the specific case of mortgage loans to retail customers, the loan is disbursed according to specific disbursement processes, characterized by a standardised valuation/ inquiry process, which gather all information necessary for the proper management of real estate guarantees.

The Montepaschi Group has developed one single process for the acquisition of collaterals which is at the same time a working instrument and the expression of the Group's management policies. The instrument can activate different paths on the basis of the type of guarantee. The management of guarantees starts after loan disbursement approval, the process of which is broken down into different stages:

- acquisition (also multiple acquisition); the controls of (formal and amount) consistency with the guarantees proposed during the authorisation phase are performed in this stage;
- adjustment/change/amendment; useful to amend the characteristics of a guarantee without interrupting loan protection;
- query; gives information about the present data and the historical trend of guarantees received;
- repayment/cancellation.

In this respect, it is important to underline that an assessment is made on the assets pledged as collateral during the mortgage loan approval stage. In the specific case of Retail mortgage loans, a dedicated disbursement process subordiantes disbursement to the submission of a technical survey on the asset pledged, thus ensuring the fulfillment of obligations and compliance with relevant validity requirements upon acquisition of the guarantee.

A system to monitor the value of the collaterals on the basis of market values is in place. Monitoring of pledge transactions is carried out on a daily basis for listed securities deposited with the bank.

As regards mortgage collateral, an IT platform integrated within the Parent Company's systems has been introduced which is used to automatically transfer information about the property acquired from appraisers directly to the bank's systems. The platform automatically updates all of the bank's loan management applications and digitally archives the appraiser's documentation. It is also capable of standardising the set of information provided by the appraisers.

Appraisers are selected based on an individual analysis of their abilities, professional skill and experience, and are placed on a dedicated list of accredited professionals; their work is monitored continuously, including by checking any divergence between surveyed values and benchmark market data. Appraisers are required to prepare their estimates using valuation methods consistent with the Italian Banking Association's Guidelines for the appraisal of properties backing credit exposures.

For the phase of monitoring the assets pledged, the Group has a policy establishing the amounts of the secured exposure and the age of the appraisal, beyond which the properties are appraised again. For exposures lower than the thresholds defined, the Group in any event conducts half-yearly monitoring of the property value based on market data.

If the value of the property pledged as a guarantee is subject to market or foreign exchange risks, the Montepaschi Group uses the concept of guarantee differential, which is understood as a percentage of the value of the guarantee offered, determined as a function of asset value volatility. The only portion of the loan covered by the value of the assets net of the differential is considered as guaranteed during the approval phase. The monitoring phase requires the adjustment of the guarantees with a market value lower than the value approved, net of the differential. This is notified through a process of daily credit monitoring which alerts the Network with events which may modify risk perception. The availability of collaterals does not alter the valuation of the insolvency risk of a customer. However, it has an impact on the approval process since loan disbursements with mitigated risk are subject to different discretionary powers (this difference at Banca MPS is even more marked due to the introduction of authorization levels dedicated only to Land and Building credit).

The Montepaschi Group accepts different instruments to protect loans which can be summarised in the following categories:

- Pledge of sums deposited with the bank;
- Pledge of securities and mutual funds deposited with the bank;
- mortgages on immovables (real estate);
- mortgages on movables;
- Pledge of sums deposited with other banks;
- Pledge of securities deposited with other banks;
- Pledge on other entitlements (insurance policies not intermediated by Companies of the Group and Portfolios under management);
- Pledge on loans;
- Pledge on commodities;
- Other forms of collaterals (Insurance, Guarantee funds).

As at today, the first three categories (accounting for more than 98% of the nominal amount of the collaterals received) are compliant with regulatory/legal/organisational requirements set out by the New Supervisory Regulations for the enforcement of credit risk mitigation standards. All types that may be received by the Montepaschi Group are entered into a structured collateral management process, under which all sub-steps are operationally shared. If the measures of monitoring of the collaterals show operational irregularities during the acquisition phase or any inadequacies/losses of the values received as a pledge, events falling within the scope of credit monitoring policies are put in place, which trigger operational obligations of credit risk assessment.

The Montepaschi Group has fulfilled the obligations set out by the New Regulations for Prudential Supervision for the purpose of recognition of credit risk mitigation effects produced by any personal collaterals securing the loan. Personal credit protection consists of personal collaterals, personal collaterals issued by third parties and credit derivatives. At Group level, personal collateral - as highlighted in the quantitative disclosure - covers a limited portion of the overall credit exposure. The main type of personal collateral consists of Guarantees (including omnibus guarantees and personal collateral issued by third parties) provided they are issued by the parties listed below:

- Sovereign governments and central banks;
- Public sector and local agencies;
- Multilateral development banks;
- Regulated intermediaries;
- Businesses that have a creditworthiness rating by an ECAI (External Credit Assessment Institution) of not less than 2 on the creditworthiness rating scale;
- Companies and individuals, if this type of customer has a probability of default determined using the same rules as for guaranteed exposures;
- Guarantee institutions, provided they are:
  - the Guarantee Fund for SMEs managed by Mediocredito Centrale (the guarantee appears as an incentive from the Ministry of Economic Development – this applies both to direct guarantees and counter-guarantees acquired through the Intermediaries listed below);
  - SACE SpA (the portion guaranteed is a public incentive since, like the Guarantee Fund, it ultimately provides for State aid);
  - Entities registered in a section of the list provided by art. 106 of the consolidated law on banking, having at least one of the following conditions:
    - an associated external rating of not less than 2;
    - issue a first demand guarantee backed by a counter-guarantee, on first demand, by Governments or Central Banks.

The activities that the MPS Group puts in place for compliance with the main organisational requirements are attributable to the similar activities envisaged for collateral other than real estate.

Under current regulations, banks which adopt the "advanced IRB" model may use the collateral as credit risk mitigation according to two different approaches:

- substitution of weighting or the probability of default (PD) of the debtor with the weighting or the PD of the protection provider
- substitution of personal LGD for unsecured LGD.

In both cases, mitigation is allowed on condition that the guarantor's PD is better than that of the main underlying obligor and that the requirement for personal guarantee admissibility is met, whereby capital absorption for the beneficiary of the guarantee should not be lower than capital absorption caused to the guarantor.

Based on Group internal regulations on CRM, the MPS Group has introduced two different policies for treatment of the exposures backed by personal guarantees, which fall within the AIRB scope: Policy 1 and Policy 2. Policy 1 applies to all exposures falling within the AIRB scope, to businesses and consumers, backed by personal collaterals issued by:

- Public Administration and Central Banks,
- Local Institutions,
- Public Sector Entities,
- Multilateral Development Banks,
- International Organisations,
- Regulated Intermediaries,

- Businesses that have a creditworthiness rating by an ECAI (External Credit Assessment Institution) of not less than 2 on the creditworthiness rating scale and that are not currently included in the internal models scope (e.g. Insurance Companies and UCITS).

Personal collateral issued by these groups/ individuals are treated by transferring the guaranteed exposure from the AIRB portfolio to the portfolio of the guarantor who then adopts standard treatment procedures.

Policy 2 applies to all those exposures falling within the AIRB scope, businesses and consumers, backed by personal collaterals issued by:

- Corporates,
- Consumers.

In this case, collateralised exposures see the application of an internally estimated loss rate for exposures secured by personal collateral (personal LGD), instead of the loss rate estimated for unsecured positions (LGD unsecured).

The Montepaschi Group accepts different instruments to protect loans which can be summarised in the following categories:

- Guarantees (including omnibus guarantees and personal guarantees issued by third parties);
- Endorsement;
- Guarantee policy;
- Credit mandate;
- Strong/binding patronage letters;
- Negotiable instruments;
- Performance bond agreement;
- Debt delegation;
- Expromission;
- Assumption of debt;
- Personal Collateral governed by foreign law;
- Credit derivatives:
  - credit default swap;
  - total return swaps;
  - credit linked notes.

Debt delegation, expromission and assumption of debt are considered valid for the purpose of credit risk mitigation if equivalent to the transfer of credit.

Fifth-of-salary backed loans can be considered as loans secured by personal collateral, if all requirements for this form of credit protection are met in the overall transaction structure.

Concentration of collaterals

The main concentration of collaterals is linked with Retail mortgage loans. However, it cannot be referred to as risk concentration by virtue of the principle of risk fragmentation which is implicit in this type of customer. Special provisions are in force on mortgage loans for Retail customers with amounts exceeding Euro 3 mln, a threshold beyond which the value of the collateral is kept up-to-date with regular appraisals of the property.

For transactions falling below the materiality threshold, the value of real estate is updated through the measurement of the average values of the real estate market. Any information on the evaluations is provided, on an annual basis, by specialised industry operators (extraordinary updates may be generated by significant variations in the very short period).

Quantitative information

The values shown below refer to the exposures of the banking group considered for credit risk purposes, Standard approach and IRB approach, secured by financial collaterals, personal guarantees and credit derivatives. The exposures taken into consideration are determined according to prudential supervisory regulations, net of any netting agreements. Therefore, the values do not include all types of guarantees; for example, exposures guaranteed by real estate are not included since they are not recognised for the purpose of risk mitigation and are directly reported in the same class, as shown in table 5.2.2 and table 5.3.1. Collateral on transactions secured by real estate are for marginal additional collateral received on these types of transactions. The Montepaschi Group does not have credit exposures hedged with credit derivatives, which are valid for the purpose of risk mitigation techniques. It follow, therefore, that the values reported under Personal Guarantees and credit derivatives refer to collateral received in the form of personal guarantees.

Tab. 5.5.1 – Credit risk mitigation techniques (Standard approach)

Regulatory Portfolio (Standard Approach)	dec-2015 Financial Collaterals	dec-2015 Personal Guarantees and Credit Derivatives	dec-2014 Financial Collaterals	dec-2014 Personal Guarantees and Credit Derivatives
Exposures to central governments and central banks	-	17	-	-
Exposures to regional governments and local authorities	-	-	-	-
Exposures to public sector entities	15,211	8,521	13,194	9,170
Exposures to Multi-lateral development banks	-	-	-	-
Exposures to International Organisations	-	-	-	-
Exposures to Supervised institutions	41,447,193	65,455	40,911,645	68,897
Exposures to Corporates	1,122,942	197,967	1,056,087	76,833
Retail Exposures	12,011	36,566	32,865	808
Exposures secured by mortgages on immovable property	446	29,377	798	-
Exposures in Default	20,767	8,571	5,177	2,347
Exposures associated with high-risk	-	-	-	-
Exposures in the form of covered bonds	-	-	-	-
Exposures to institutions and corporates with a short-term credit assessment	-	-	-	-
Exposures to UCITs	1,250	-	6,663	-
Equity Exposures	-	-	-	-
Other Exposures	-	-	-	-
Securitization positions	-	-	-	-
Exposures to Central Counterparties in the form of pre-funded contributions to the guarantee fund	-	-	-	-
Total	**42,619,819**	**346,473**	**42,026,430**	**158,056**

The column Financial Guarantees in the above table is a supplement to the Post CRM exposure reported in table (values of exposures pre and post CRM), which shows the portion of exposure outstandiong not covered by these collaterals. Please note that, pursuant to regualtions, if the line-by-line method is applied, the collateral reduces risk exposure, whereas personal guarantees (simplified approach) transfer the related risk to the regulatory portfolio of the guarantor; thus the representation of personal guarantees in table 5.5.1 is under the guarantor and does not entail a reduction in the value of the exposure.

Tab. 5.5.2 – Credit risk mitigation techniques (IRB approach)

	dec-2015		dec-2014	
Regulatory Portfolio (IRB Approach)	Financial Collaterals	Personal Guarantees and Credit Derivatives	Financial Collaterals	Personal Guarantees and Credit Derivatives
Exposures to or secured by corporates:	432,456	1,856,976	707,597	1,529,313
- SMEs	233,798	889,641	283,329	772,139
- Other companies	198,658	967,336	424,269	757,174
Retail exposures:	575,001	1,469,092	765,655	1,745,960
- secured by real estate: SMEs	10,706	16,320	17,347	39,295
- secured by real estate: Individuals	6,837	1,529	7,814	1,816
- Qualifying revolving	-	-	-	-
- Other retail exposures: SMEs	355,903	1,421,312	452,695	1,652,636
- Other retail exposures: Individuals	201,555	29,930	287,798	52,213
Total	**1,007,457**	**3,326,068**	**1,473,252**	**3,275,274**

6. Counterparty Risk

6.1 Counterparty Risk: general disclosure

The Montepaschi Group is committed to monitoring counterparty risk, understood as the risk that the counterparty in a transaction involving specific financial instruments (i.e. OTC derivatives, *securities financing transactions* and long settlement transactions) is in default before the settlement of the transaction.

In conformity with regulatory requirements, the Montepaschi Group uses the "market value" method to calculate the value of exposures for OTC derivatives and long settlement transactions. This method consists in calculating current and potential exposure using the market value as the current exposure and the regulatory add-on to represent, in a simplified manner, the potential future exposure.

For SFTs *(securities financing transactions)*, the comprehensive method with supervisory volatility adjustments is used.

The Group has adopted credit risk mitigation measures such as netting agreements, collaterals, break clauses, etc. to substantially limit the risk assumed.

From an operational point of view, activities relevant for the purpose of counterparty risk may be broken down into two macro segments on the basis of both counterparty characteristics (ordinary clients and institutional counterparties) and the operational and monitoring methods put in place by the Group.

With regard to business with financial institutions, counterparty risk exposure on individual credit lines is monitored on a daily basis by the control units of the various business units. In short, the process involves:

- granting credit lines to counterparties on the basis of requests from business unit staff, with a periodical review of the limits set;
- inserting the limits in the management systems;
- inserting the deals and collaterals according to ISDA/ISMA standards and related credit Support annexes (CSA) and Global Master Repurchase Agreements (GMRA) or Global Master Securities Lending Agreement (GMSLA) signed with each counterparty;
- daily activities to monitor and exchange collaterals with counterparties in relation to the market value of outstanding positions (Collateral Management);
- daily monitoring of drawn and overdrawn amounts - also in real time - considering, the guarantees pledged or received;
- the legal function periodically checking whether netting clauses and collaterals set out in the bilateral agreements signed with the counterparties are judicially and administratively valid in the event of their default, by making reference to the case law of their respective countries.

Please note that a downgrading of the

Montepaschi Group does not impact the amount of guarantees to be provided;

- verifying the eligibility of collateral against counterparty risk falls under the broader management of Credit Risk Mitigation described in paragraph 5.5.

As at the date of this document, no operational limits exist in terms of internal capital for counterparty credit exposures. For 2016, the Group has also included the monitoring of regulatory limits on RWAs for counterparty risk in the RAF.

With regard to liquidity risk, assessments are carried out on any additions to the guarantees required by institutional counterparties should the Montepaschi Group be downgraded as a result of signed CSA and GMRA agreements. The process for derivative transactions with ordinary clients is based on the distinction of roles and responsibilities among the different entities within the Group. Trading in derivatives with customers provides for centralization of product factors and market risk monitoring within MPS Capital Services, with allocation, management and monitoring of counterparty credit risk for customers in the bank's networks.

To this end, Retail Banks:

- authorise the credit facilities granted to customers;
- manage each transaction in their books;
- take care of the related documents and regulatory requirements;
- review the amounts drawn with respect to the credit facilities granted.

With regard to products offered to customers, from a general point of view, a series of common elements are typical of most operations. Specifically, the products traded are:

- not of a speculative nature;
- are for the exclusive purpose of covering risk;
- are associated with an underlying position, even if they are contractually and administratively separate from it;
- show limited elements of complexity;
- on the overall position covered, they hold no financial leverage.

To reduce counterparty risk since 2010, MPS Capital Services has indirectly joined the swap clear service managed by the central counterparty, LCH Clearnet London for activities with OTC derivatives. The centralisation of a part of trading in OTC derivatives to LCH makes it possible to considerably reduce the risk of default from these activities since LCH is the guarantor and direct manager of flows deriving from the contracts. Any default of a direct member of the service is covered by the guarantee funds and backup systems of LCH. A project is under way to identify and manage exposure that is adversely correlated with counterparties' credit quality (i.e. *wrong way risk*) for the definition of related internal policies.

6.2 Quantitative information

The following table shows the value of exposures in derivatives, long-term settlement transactions and Security Financing Transactions (SFTs), broken down by method of assessment for regulatory purposes and counterparty portfolio. Specifically, the methods applied are as follows:

- *Market value method*: derivatives and long-term settlement transactions;
- *Comprehensive method with supervisory volatility adjustments:* SFTs.

Tab. 6.2.1 – Counterparty Risk: summary

	dec-2015		dec-2014	
	Exposure Total	Capital Requirements	Exposure Total	Capital Requirements
Market value method				
Derivative e op. with LT reg.				
of which: Standard Approach	2,406,345	79,866	2,547,901	129,880
of which: AIRB Approach	666,728	48,745	696,594	38,499
Market value method	**3,073,074**	**128,611**	**3,244,495**	**168,378**
Comprehensive method				
SFT Operations				
of which: Standard Approach	3,801,828	78,113	7,036,594	105,176
of which: AIRB Approach	144,205	645	206,246	117
Comprehensive method Total	**3,946,033**	**78,758**	**7,242,840**	**105,293**
Total	**7,019,107**	**207,369**	**10,487,335**	**273,671**

In the Market Value method (transactions in derivatives and Long term repos) the Exposure is a value determined according to rules of prudential supervision and is based on the positive fair value net of nettings; this value is increased by the future credit exposure (add-on) and reduced by the effects of the guarantee agreements. The future credit exposure takes account of the probability that in future the current value of the contract, if positive, may increase or, if negative, may become a credit position. This probability is linked with the volatility of the underlying market factors and the residual maturity of the contract. In other terms, it is calculated on the basis of the notional amount of all the derivatives taken into consideration, both with a positive and negative fair value. The capital requirement for counterparty risk, shown in the above table, relates to the regulatory trading portfolio and banking book and is reported for the individual regulatory portfolio of reference and also summarised in the table on capital adequacy for credit risk under the standard approach and AIRB approach (*see* tab 4.2; tab 5.1.1).

Tab. 6.2.2 – Counterparty Risk: derivatives

	Gross Positive Fair value (book values)	Effect of nettings agreements	Netted Fair value	Effect of collateral arrangement	Net Credit Exposure
Derivatives as at 31/12/2015	6,286,216	3,667,967	2,618,249	1,897,409	2,380,962
Derivatives as at 31/12/2014	7,966,169	5,106,348	2,859,821	1,918,631	3,212,165

Table 6.2.2 shows the gross positive fair of the contracts, the advantages resulting from the netting agreements, the netted fair value and the net credit exposure of the Banking Group to counterparty risk for derivative instruments. All the financial and credit derivatives traded over the counter (OTC) with any counterparty institutional, corporate, retail counterparties etc.) are included in the table irrespective of the regulatory (trading and banking) portfolio they belong to. In particular, the "gross positive fair value" corresponds to the book value of the above-mentioned contracts and therefore is inclusive of the netting agreements. The Nettings" represent the gross positive fair value amount, which as a result of the agreements executed with the counterparties, is offset with negative value transactions. The net "netted fair value" indicates the positive fair value amount remaining after the nettings.

Table 6.2.3 shows the breakdown of the gross positive fair value of OTC derivatives by type of underlying.

Tab. 6.2.3 – Derivatives: breakdown of positive fair value by type of underlying

	Interest rates	Foreign currencies and gold	Equity securities	Credits	Other	Total
Derivatives as at 31/12/2015	5,707,041	199,708	249,011	79,363	51,092	6,286,216
Derivatives as at 31/12/2014	6,555,918	183,081	672,319	526,230	28,621	7,966,169

It should be noted that as at the date of this document, the Group did not have any transactions in credit derivatives hedging loan book exposures.

Tab. 6.2.4 – Credit Derivatives: notional amounts

Group of Products	Banking Portfolio		Regulatory Trading Book	
	Protection purchases	Protection sales	Protection purchases	Protection sales
Credit default swap	-	-	2,753,549	5,772,022
Total rate of return swap	-	-	-	7,825
Total 31/12/2015	**-**	**-**	**2,753,549**	**5,779,846**
Total 31/12/2014	**-**	**-**	**13,074,118**	**13,813,319**

The table 6.2.4 shows the notional values of credit derivative contracts, by portfolio (banking and trading book) and the role played by the Montepaschi Group (buyer/ seller of protection). For more details on derivatives, see Part E – Section 1.2.4 Derivative instruments of the Consolidated Financial Statements 31.12.2015.

7. Market Risk

7.1 Trading Book Market Risk: general disclosure

The Group's Regulatory Trading Portfolio (RTP), or Trading Book, is made up of all the Regulatory Trading Books managed by the Parent Bank (BMPS) and MPS Capital Services (MPSCS). The Trading Portfolios of the other subsidiaries are immune to market risk. Trading in derivatives, which are brokered on behalf of customers, calls for risk to be centralised at, and managed by, MPSC.

The market risks in the trading book of both the Parent Company and the other Group entities (which are relevant as independent market risk taking centres), are monitored in terms of Value-at-Risk (VaR) for operational purposes. The Group's Finance and Liquidity Committee is responsible for directing and coordinating the overall process of managing the Group's proprietary finance thereby ensuring that the management strategies of the various business units are consistent.

The Group's Trading Book is subject to daily monitoring and reporting by the Risk Management Area of the Parent Company on the basis of proprietary systems. VaR for management purposes is calculated separately from the operating units, using the internal risk measurement model implemented by the Risk Management function in keeping with international best practices. However, the Group uses the standardised methodology in the area of market risks solely for reporting purposes.

Operating limits to trading activities, which are established by the Board of Directors of the Parent Company, are expressed by level of delegated authority in terms of VaR, which is diversified by risk factors and portfolios, monthly and annual stop losses and Stress. Furthermore, the trading book's credit risk, in addition to being included in VaR computations and in the respective limits for the credit spread risk component, is also subject to specific operating limits for issuer and bond concentration risk which specify maximum notional amounts by type of guarantor and rating class.

VaR is calculated with a 99% confidence interval and a holding period of 1 business day. The Group adopts the method of historical simulation with daily full revaluation of all basic positions, out of 500 historical entries of risk factors (lookback period) with daily scrolling. The VaR calculated in this manner takes account of all diversification effects of risk factors, portfolios and types of instruments traded. It is not necessary to assume, a priori, any functional form in the distribution of asset returns, and the correlations of different financial instruments are implicitly captured by the VaR model on the basis of the combined time trend of risk factors.

From the point of view of methodological adjustment, in the last quarter of 2014 the commodity risk factor was introduced in the internal management model: this completes the representation of risk in the Group's financial portfolios.

The management reporting flow on market risks is periodically transmitted to the Risk Committee, the Group's Top Management and the Board of Directors of the Parent Company in a Risk Management Report, which keeps Executive Management and governing bodies up to date on the overall risk profile of the Group.

The macro-categories of risk factors covered by the Internal Market Risk Model are IR, EQ, CO, FX and CS as described below:

- IR: interest rates on all relevant curves, inflation curves and related volatilities;
- EQ: share prices, indexes, baskets and relative volatilities;;
- CO: commodity prices, indexes and baskets;
- FX: exchange rates and related volatilities;
- CS: credit spread levels.

VaR (or diversified or net VaR) is calculated and broken down daily for internal management purposes, even with respect to other dimensions of analysis:

- organisational/management analysis of portfolios,
- analysis by financial instrument,
- analysis by risk family.

It is then possible to assess VaR along each combination of these dimensions in order to facilitate highly detailed analyses of events characterising the portfolios.

In particular, with reference to risk factors the following are identified: Interest Rate VaR (IR VaR), Equity VaR (EQ VaR), Commodity VaR (CO VaR), Forex VaR (FX VaR) and Credit Spread VaR (CS VaR). The algebraic sum of these items gives the so-called Gross VaR (or non-diversified VaR), which, when compared with diversified VaR, makes it possible to quantify the benefit of diversifying risk factors resulting from holding portfolios on asset class and risk factor allocations which are not perfectly correlated. This information can also be analysed along all the dimensions referenced above.

The model enables the production of diversified VaR metrics for the entire Group in order to get an integrated overview of all the effects of diversification that can be generated among the various banks on account of the specific joint positioning of the various business units.

Moreover, scenario and stress-test analyses are regularly conducted on various risk factors with different degrees of granularity across the entire tree structure of the Group's portfolios and for all categories of instruments analysed.

Stress tests are used to assess the bank's capacity to absorb large potential losses in extreme market situations, so as to identify the measures necessary to reduce the risk profile and preserve assets.

Stress tests are developed on the basis of discretionary and trend-based scenarios. Trend-based scenarios are defined on the basis of previously-registered real situations of market disruption. Such scenarios are identified based on a time frame in which risk factors were subjected to stress. No particular assumptions are required with regard to the correlation among risk factors since trend-based data for the stress period identified has been measured.

Stress tests based upon discretionary scenarios assume extreme changes occurring to certain market parameters (interest rates, exchange rates, stock indices, credit spreads and volatility) and measure the corresponding impact on the value of portfolios, regardless of their actual occurrence in the past. Simple discretionary scenarios are currently being developed (variation of a single risk factor) as are multiple ones (variation of several risk factors simultaneously). Simple discretionary scenarios are calibrated to independently deal with one category of risk factors at a time, assuming shocks do not spread to the other factors. Multiple discretionary scenarios, on the other hand, aim to assess the impact of global shocks that simultaneously affect all types of risk factors.

It should be noted that the VaR methodology described above is, for operational purposes, also applied to the portion of the Banking Book consisting of financial instruments that are similar to trading instruments (eg. AFS bonds/Equity instruments).

The Group has implemented a backtesting procedure compliant with current regulations governing Market Risk as part of its own risk management system.

Backtesting refers to a series of tests conducted on VaR model results against day-to-day changes in the trading book value, with a view to assessing the model's forecasting capacity as regards the accuracy of risk metrics generated. If the model is robust, by periodically comparing the estimated daily VaR against daily trading losses from the previous day, the result should be that actual losses greater than the VaR occur with a frequency consistent with that defined by the confidence level.

Based on applicable regulatory provisions, the Risk Management Area considered it appropriate to apply the theoretical and actual backtesting methods and integrate these into the Group's management reporting system.

The first type of test **(theoretical backtesting)** has a stronger statistical significance in reference to measuring the accuracy of the VaR model ("uncontaminated test").

The second type of test **(actual backtesting)** meets the need for verifying the VaR model's forecasting reliability in reference to actual Bank operations (daily trading P&L) less the effect of any interest accrued between trading days t-1 and t on the securities and less the effect of fees and commissions.

These "clean" P&L results (the "actual P&L") are compared with the previous trading day VaR. If the losses are greater than those forecast by the model an "exception" is recorded.

Each bank of the MPS Group which is relevant as a *market risk-taking centre* contributes to the generation of interest rate risk and price risk in the overall Trading Book.

With reference specifically to the Parent Company, the Finance, Treasury & Capital Management Area (FTCMA) within the

CFO division is the Business Area in charge of trading. The Global Markets Division carries out trading activities for MPSCS.

The FTCMA manages a proprietary portfolio which takes trading positions on interest rates and credit. In general, interest rate positions are taken by purchasing or selling bonds, and by creating positions in listed derivatives (futures) and OTCs (IRS, swaptions). Trading is carried out exclusively on the Bank's own behalf, with objectives of absolute return, in compliance with the delegated limits of monthly and yearly VaR and Stop Loss.

In particular, the FTCMA operates in the short-term portion of the main interest rate curves, mostly through bonds and listed derivatives.

With regard to credit risk in the trading book, the equity positions are generally managed through the purchase or sale of bonds issued by companies or by creating synthetic positions in derivatives. The activity is oriented to achieving a long or short position on individual issuers, or a long or short exposure on specific commodities. The activity is carried out solely on the Bank's own behalf with objectives of absolute return and in compliance with other specific issuer and concentration risk limits approved by the Board of Directors.

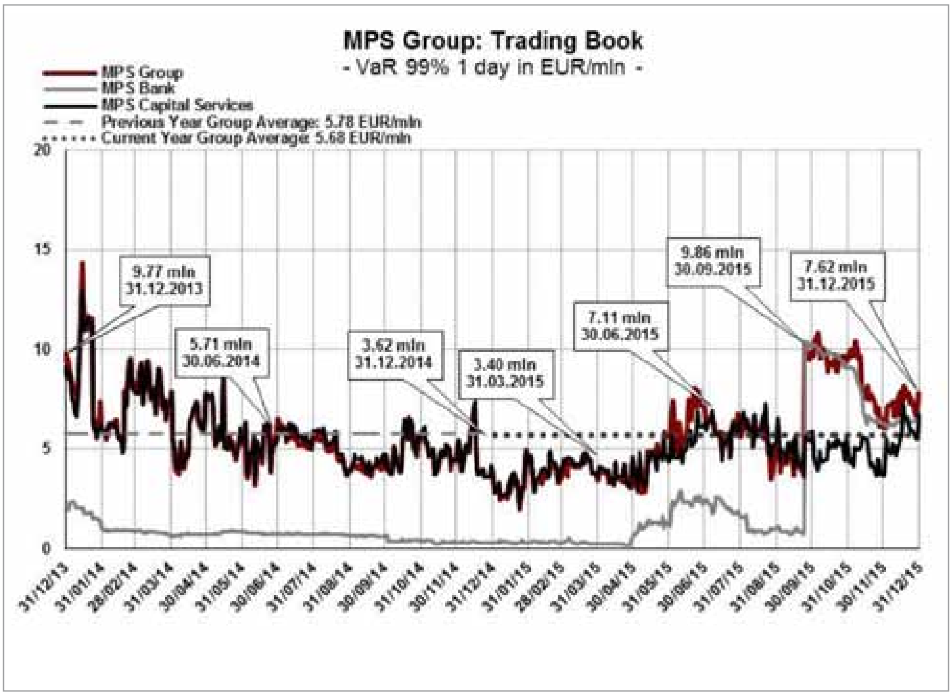
The Business Area in charge of the Parent Bank's trading activity with respect to price risk is the FTCMA which manages a proprietary portfolio and takes trading positions on equities, Stock Exchange indexes and commodities. In general, positions on equity securities are taken both through the purchase/sale of equities and through the positions created in listed derivatives (e.g. futures) and OTC (e.g. options). Trading is carried out exclusively on the Bank's own behalf, with objectives of absolute return, in compliance with the delegated limits of monthly and yearly VaR and Stop Loss. Similarly, the Global Markets Division carries out trading activities for MPSCS. For further information, please refer to the **Notes to the Consolidated Financial Statements**, *Part E – Information on risks and hedging policies – Section 2.1 – Interest Rate Risk and Price Risk – Regulatory Trading Book.*

During 2015, market risks in the Group's Regulatory Trading Book in terms of VaR showed an increasing trend in volatility although on average they remained at around the same levels as the previous year. Until the end of September 2015, VaR trends were primarily impacted by the subsidiary MPS Capital Services in relation to trading and policy structuring and hedging activities. VaR increased at the end of September due to transactions resulting from the early unwinding of the "Alexandria" transaction by the Parent Company, resulting in the acquisition, from the counterparty Nomura, of a portfolio composed primarily of BTPs via an asset swap with medium/long financial term, totalling around EUR 2.64 bn.

A part of the portfolio, held for sale starting from October, was classified as Held for

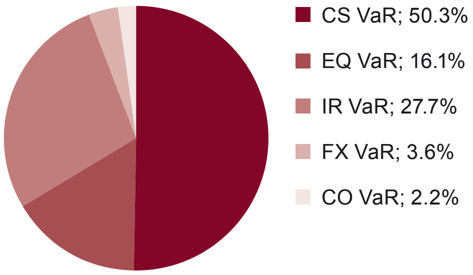
Trading, consequently causing an increase in the Group's VaR in the last quarter as well as in the weight of the Parent Company with respect to the overall risk measurement. In any event, the Group's VaR then decreased, reaching EUR 7.62 mln as at 31 December 2015.

A breakdown of VaR by risk factors as at 31 December 2015 shows that approx. 50.3% of the Group's portfolio was allocated to risk factors such as Credit Spread (CS VaR), 16.1% was absorbed by equity risk factors (EQ VaR), 27.7% was absorbed by interest rate risk factors (IR VaR), 3.6% by foreign exchange risk factors (FX VaR) and the remaining 2.2% by commodity risk factors (CO VaR). With regard to legal entities, the Group's market risks are equally distributed between MPSCS (50.7%) and the Parent Company (49.3%).

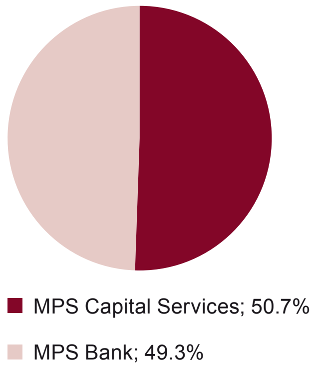


VaR breakdown

MPS Group: Trading Book
VaR by Risk Factor as at 31/12/2015



MPS Group: Trading Book
VaR by Bank as at 31/12/2015



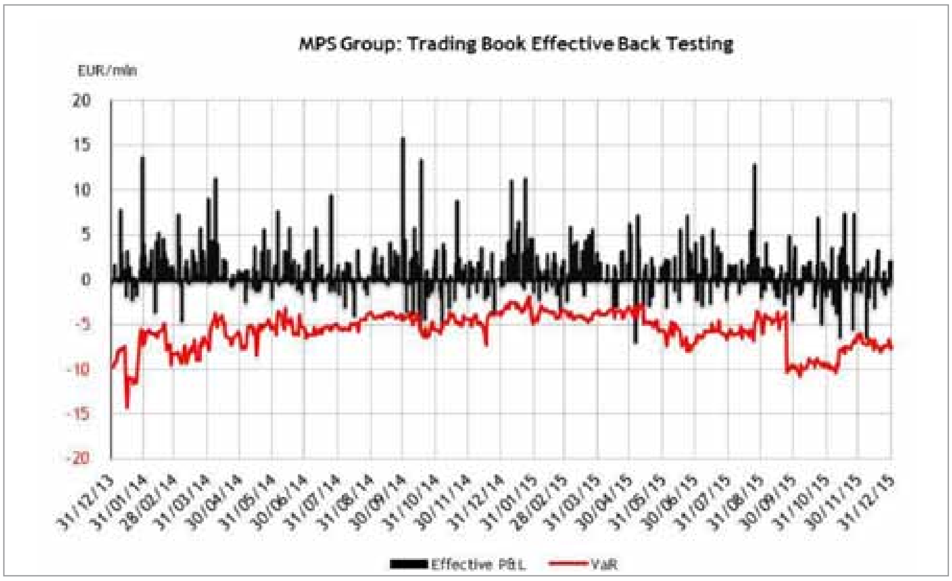
Group VaR

In 2015, the Group's VaR in the Regulatory Trading Book ranged between a low of EUR 1.94 mln recorded on 23 January 2015 and a high of EUR 10.80 mln on 5 October 2015 with an average value registered of EUR 5.68 mln. VaR in the Regulatory Trading Book as at 31 12 2015 amounted to EUR 7.62 mln.

MPS Group: Trading Book
VaR 99% 1 day in EUR/mln

	VaR	Data
End of Period	7.62	31/12/2015
Min	1.94	23/01/2015
Max	10.80	05/10/2015
Average	5.68	

The following chart shows the Effective Backtesting data of the internal model for Market Risk, related to the Supervisory Trading Portfolio of the group.



The backtesting shows two exceptions during the second quarter of 2015 on the Group trading book, details of which are as follows:

- 14 April 2015: negative day for the market (negative shift in the market parameters, amplified by the exposure in equity options on the S&P MIB index and interest rate future options on CBOT US 6%) with a significant effect on the portfolio of subsidiary MPS Capital Services;

- 05 May 2015: negative day for the market (negative shift in the market parameters, particularly due to expansion of the Italy credit spread) with a significant impact on the portfolio of subsidiary MPS Capital Services. The Montepaschi Group adopts the standardised approach for calculating market risk capital requirements, as summaried in table 4.4.

8. Exposure to interest rate risk on positions not included in the trading book

The Banking Book or Banking Portfolio consists of all exposures not falling within the Trading Book and, in accordance with international best practices, it refers to all of the Bank's commercial operations relating to the transformation of maturities with respect to balance-sheet assets and liabilities, Treasury, foreign branches, and hedging derivatives of reference. The definition of the scope of the Banking Book and the ALM centralisation process are set out in a resolution by the Board of Directors of the Parent Company in compliance with the framework described in the regulatory provisions (Bank of Italy Circ. 285). The framework sets the rules for the centralisation of Asset & Liability Management under the Parent Company's Finance, Treasury and Capital Management Area (FTCMA) and the definition and monitoring of operating limits for interest rate risk in the Group's Banking Book.

The Banking Book also includes bond receivables held for investment purposes, classified as either AFS or L&R. The same ALM rate risk metrics of measurement used for other accounts were also applied to this aggregate.

The operational and strategic choices for the Banking Book, adopted by the Finance and Liquidity Committee and monitored by the Risk Committee of the Parent Company, are based first and foremost on exposure to interest rate risk for a variation in the economic value of the assets and liabilities of the banking book by applying a parallel shift of 25bp, 100bp and 200bp, the latter in accordance with the requirements set out in the "second pillar" of Basel.

The risk measurements of the retail banks of the Montepaschi Group are calculated by using, among other things, a model for the valuation of demand items or core deposits, whose characteristics of stability and partial insensitivity to variations in interest rates are described in systems with a statistical/predictive model *(replicating portfolio)*, which takes into consideration a significant historical series of customer behaviours in the past.

In addition, the Montepaschi Group's ALM model includes within rate risk measurements, a behavioural model which takes into account the aspect of mortgage advance repayment *(prepayment risk)*.

The Montepaschi Group is committed to the continual updating of risk measurement methodologies by gradually fine-tuning estimation models so as to include all major factors that progressively modify the interest rate risk profile of the banking book.

In the course of 2013, the Group continued to carefully and constantly monitor its risk profile characteristics particularly in the light of existing contractual options and operating practices adopted, all of which make the risk profile more dependent on market performance, interest rates and their volatility.

The Group adopts a rate risk governance and management system which, in accordance with the provisions of the Supervisory authority, avails itself of:

- a quantitative model, which provides the basis for calculation of risk indicators for the interest rate risk exposure of the Group and Group companies/entities;
- risk monitoring processes, aimed at the ongoing verification of compliance with the operational limits assigned to the Group overall and to the individual business units;
- risk control and management processes, geared toward bringing about adequate initiatives for optimising the risk profile and activating any necessary corrective actions.

As part of the above system, the Parent Company has opted to centralise the responsibility for defining the policies aimed at managing the Group's Banking Book and controlling its related interest rate risk.

Tab. 8 – Exposure to interest rate risk in the Banking Book

Shift (+/-)	"Effect on Economic Value (values in €/mln)"		"Effect on Net Interest Income (values in €/mln)"	
	dec-15	dec-14	dec-15	dec-14
Eur +200bp	-707.19	-1,412.24	164.53	65.64
Usd +200bp	-2.97	-5.20	3.46	8.05
Other +200bp	-1.09	1.30	0.70	1.51
Total +200bp	**-711.25**	**-1,416.14**	**168.69**	**75.20**
Eur -200bp	436.44	724.69	-4.79	-14.40
Usd -200bp	37.23	40.92	2.05	-0.92
Other -200bp	2.13	1.54	0.81	0.03
Total -200bp	**475.80**	**767.15**	**-1.92**	**-15.28**

The amount of economic value at risk is, in any case, below the level considered as a critical threshold by current regulations.

The measure of sensitivity of net interest income refers to a parallel and instantaneous shock in the rate curve of +/-200 basis points.

The gapping period is 12 months. The simulation model for net interest income sensitivity includes and assesses the mismatch generated by the trading book (via replication of the loan on the banking book).

It shows how the measure of sensitivity to net interest income only expresses the effect of interest rate changes on the items under analysis. Assumptions regarding future trends in assets and liabilities are thus excluded and, therefore, cannot be considered as a predictor of level of net interest.

The sensitivity of the Montepaschi Group, at the end of 2015, suggests a profile of exposure to rate hike risk. With a shift of +200 bp in the interest rate curve, total sensitivity of the economic value stands at -711.25 Eur/mln, a decrease compared to the end of 2014.

Risk is almost entirely allocated to exposures denominated in Euros. For further information, please refer to the **Notes to the Consolidated Financial Statements**, *Part E – Information on risks and hedging policies – Section 2.1 – Interest Rate Risk and Price Risk – Banking Book*.

9. Exposures in equities not included in the trading book

Exposures in equity instruments are held by the Group for strategic purposes (group investments, associates and joint ventures), institutional purposes (investments in trade associations, local entities and institutions), purposes functional to the bank's business and the development of commercial business and financial investment purposes (limited to the investments associated with the merchant banking business of MPS Capital Services). Other investments exist, which are no longer considered as strategic and that are being sold, as well as investments in companies in liquidation.

Equity exposures included in the Banking book are classified for balance sheet purposes under available-for-sale financial assets and equity investments.

Measurements and accounting criteria

Assets available for sale

Classification criteria

This category includes non-derivative financial assets which are not classified as loans, financial assets designated at fair value through profit and loss or financial assets held to maturity. In particular, this category also comprises strategic equity investments which are not managed for trading purposes and cannot be defined as controlling interest, investment in an associate and joint control, and bonds which are not subject to trading. Such investments may be transferred for any reason, such as need for liquidity or variations in interest rates, exchange rates, or stock price.

Recognition criteria

Financial assets represented by debt or equity securities are initially booked at the settlement date, whereas receivables are initially booked as of the disbursement date. On initial recognition, the assets are reported at their fair value which normally corresponds to the price paid, inclusive of transaction costs or income directly attributable to the instrument. if recognition occurs as a result of reclassification from assets held to maturity, the value at which the assets are booked is represented by the fair value as of the date of transfer. In the case of debt instruments, any difference between the initial value and the value of repayment is posted to P&L and spread out over the life of the debt instrument in accordance with the method of amortised cost.

Measurement criteria

After initial recognition, financial assets available for sale are measured at fair value, with interest being recognised in the income statement as resulting from the application of the amortised cost and with appropriation to a specific net equity reserve of the gains or losses arising from changes in fair value net of the related tax effect, except losses due to impairment. Foreign exchange fluctuations in relation to non-monetary (equity) instruments are posted to the specific net equity reserve, whereas changes in monetary instruments (loans/receivables and debt instruments) are allocated to profit and loss. Equities, for which it is not possible to determine a reliable fair value, are maintained at cost, adjusted for any impairment losses. Financial assets available for sale are reviewed for objective evidence of impairment at each balance sheet and interim reporting date. Indicators of a likely impairment are, for instance, significant financial difficulty of the issuer, non-fulfilment or defaults in payments of interest or principal , the possibility that the borrower is declared bankrupt or submitted to other forms of insolvency proceedings, the disappearance of an active market for the assets. In particular, as far as equity instruments that have a quoted market price in an active market are concerned, a market price as at the date of the financial statements lower than the original purchasing cost of at least 30% or a market value lower than the cost lasting more than 12 months are considered an objective evidence of value reduction. If further reductions take place in subsequent financial years, these are charged directly to the profit and loss statement. With regard to debt securities, regardless of whether or not these are listed on active markets, any impairment loss is recognised in the profit and loss statement strictly in relation to the issuer's ability to fulfil its obligations and therefore make the necessary payments and repay capital at maturity. Therefore, it needs to be established whether there are indications of a loss event which could have a negative impact on estimated future cash flows. Where there are no actual losses, no loss is recognised on the stock, and any capital loss is recognised in the negative net equity reserve. Any writedowns recognised as a result of the impairment test are booked to the profit and loss statement as an operating expense. If the reasons for impairment cease to exist, following an event which occurred after recognition of impairment, writebacks are recognised in equity in the case of equity instruments, and through profit and loss in the case of debt securities.

Derecognition criteria

Financial assets are derecognised from the balance sheet when the contractual rights to the cash flows derived from the assets expire or when the financial asset is sold and virtually all of the risks and rewards in relation thereto are transferred. Securities received within the scope of a transaction that contractually provides for subsequent sale are not recognised in the financial statements, and securities delivered within the scope of a transaction that contractually provides for subsequent repurchase are not derecognised from the financial statements. Securities received within the scope of a transaction that contractually provides for subsequent sale are not recognised in the financial statements, and securities delivered within the scope of a transaction that contractually provides for subsequent repurchase are not derecognised from the financial statements. Consequently, in the case of securities acquired with an agreement for resale, the amount paid is recognised in the financial statements as loans to customers or banks, while in the case of securities transferred with an agreement for repurchase, the liability is shown under deposits from customers or deposits from banks.

Criteria for reporting of income and expenses

Upon disposal, or exchange with other financial instruments or measurement of a loss of value following impairment testing, the fair value results accrued to the reserve for assets available for sale are reversed to profit and loss under:

- account "100 - Gains/losses on purchase/ disposal of: b) financial assets available for sale", in the case of disposal;
- account "130 - Net impairment losses/ reversals" on: b) financial assets available for sale", in the case of recognition of impairment.

If the reasons for impairment cease to exist, following an event which occurred after the impairment was recognised, the impairment loss is appropriately reversed: through profit and loss in the case of loans or debt securities, and through net equity in the case of equity instruments.

Equity investments

Classification criteria

The Group considers as associates, that is subject to significant influence, the companies of which it holds at least 20 per cent of the voting rights (including potential voting rights) and in which it has the power to participate in determining the financial and operating policies. Similarly, companies are considered associates also when the Group – despite a lower percentage of voting rights– has the power of participating in the determination of the financial and operating policies of the investee on account of specific legal agreements such as, for example, the participation in important committees of the investee as well as the presence of vetoing rights on significant decisions.

The Group considers jointly controlled those companies with respect to which the following circumstances occur simultaneously:

- a written agreement is in place providing for participation in the management of the investee's business through the presence in the latter's Board of Directors;
- none of the parties to the agreement holds exclusive control of the investee;
- the decisions on key activities are made unanimously by the identified parties (each has an implicit or explicit veto power on key decisions).

Recognition criteria

The account includes equity investments held in associates and in joint ventures: these investments are initially recognised at purchase cost.

Revenue recognition and measurement criteria

In consideration of the above, this item broadly contains the valuation of equity investments using the equity method; this method provides for initial recognition of the investment at cost and its subsequent adjustment on the basis of the share of the investee's profits and losses made after the date of purchase. The pro-rata amount of the profit/loss for the period of the investee is posted to item 240 "Gains/losses on investments" in the consolidated profit and loss statement.

If evidence of impairment indicates that there may have been a loss in value of an equity investment, then the recoverable value of the investment (which is the higher of the fair value, less costs to sell, and the value in use) should be estimated. The value in use is the present value of the future cash flows expected to be derived from the investment, including those arising from its final disposal. Should the recoverable value be less than its carrying value, the difference is recognised in profit or loss under account "240 - Gains (losses) on equity investments". Should the reasons for impairment no longer apply as a result of an event occurring after the impairment was recognised, reversals of impairment losses are credited to the same account in profit and loss.

Derecognition criteria

Investments are derecognised from the balance sheet when the contractual rights to the cash flows derived from the assets expire or when the financial asset is sold and virtually all of the risks and rewards in relation thereto are transferred. If a company is committed to a plan to sell a subsidiary that involves loss of control over said subsidiary, all the subsidiary's assets and liabilities should be reclassified as assets held for sale, regardless of whether the company will retain a non-controlling interest after the sale.

Quantitative information

The table illustrates exposures in capital instruments broken down by the respective accounting portfolio. The values refer to Group accounting exposures included in the Banking Book and do not include exposures in equity investemnts (shareholding) which are deducted for the calculation of Own Funds. The item "financial assets available for sale" refers to equity investments whose shareholdings are lower than the controlling or associate interests.

Tab. 9.1 – Exposures in equities not included in the trading book

Amounts as at 31.12.2015

Type of exposure / values	Book value		Fair value		Market value	Gains / losses realized		Gains / losses not realized and recognized in net assets	
	Level 1	Level 2/3	Level 1	Level 2/3	Level 1	Profits	Losses	Plus (+)	Minus (-)
A. Equity investments	11,873	818,383	13,305	X	13,305	126,292	-1,607	X	X
B. Financial assets available for sale	17,984	335,729	17,984	335,729	17,984	2,950	-17	38,886	-18,157

X = not attributable value
The item Equity Investments also includes the investment in Fabbrica Immobiliare classified under assets held for sale in the balance sheet in the amount of EUR 5.6 mln.
The item Financial Assets available for sale includes AFS investments classified under assets held for sale in the balance sheet in the amount of EUR 22.2 mln.

In addition to exposures in the equity instruments illustrated above, the Group also holds the portion of UCITs (EUR 123.8 mln) not intended for trading purposes and therefore included in assets available for sale for accounting purposes, as summarized in table 9.2.

Tab. 9.2 – Units of UCITs: breakdown by main category

Categories / Amounts	dec-2015	dec-2014
Equity	-	-
Bonds	-	-
Balanced	-	-
Hedge Funds	10,563	4,853
Private Equity	107,107	116,855
Real estate	5,335	1,553
Other	828	-
Total	**123,833**	**123,261**

The units of UCITs relate mostly to interests held by the Parent Company in private equity funds, whose purpose is to increase the value of the respective equity through mainly medium to long-term investments chiefly in the purchase and/or subscription of shares, units and securities in general representing the equity of target enterprises, exclusively in the best interest of the investors. The remaining portion of the Parent Company's UCITs portfolio consists of hedge funds, in particular side pocket, funds under liquidation and holdbacks on total redemptions as well as units of a closed-end real estate fund for qualified investors only, held by the subsidiary MPSCS.

Maximum exposure to the risk of loss was determined to be equal to book value for exposures to UCITs units other than the financial and credit derivatives for which reference is made to positive fair value plus the add-on (calculated also taking into account positions with a negative fair value). The standard approach is applied for calculating the capital requirements for these exposures.

10. Encumbered and unencumbered assets

Information on the Group's encumbered and unencumbered assets was prepared on the basis of guidelines and templates issued by the EBA on 27 June 2014 in accordance with the provisions of Part eight, Title II of EU Regulations (CRR 575/2013). To this end, an asset is considered as encumbered if it has been pledged or if it is subject to any form of arrangement to secure, collateralise or credit-enhance any on-balance-sheet or off-balance-sheet transaction from which it cannot be freely withdrawn. Assets pledged that are subject to any restrictions in withdrawal, such as assets that require prior approval before withdrawal or replacement by other assets, should be considered encumbered. Generally, the following types of contracts are considered encumbered:

a. secured financing transactions, including repurchase contracts and agreements, securities lending and other forms of secured lending;
b. collateral agreements, for instance, collateral placed for the market value of derivatives transactions;
c. financial guarantees that are collateralised;
d. collateral placed in clearing systems, with central counterparties (CCPs) and with other infrastructure institutions as a condition for access to service; this includes default funds and initial margins;
e. central bank facilities; pre-positioned assets should be considered unencumbered only if the central bank allows withdrawal of assets placed without prior approval;
f. underlying assets from securitisation structures, where the financial assets have not been derecognised from the institution's financial assets; assets that are underlying fully retained securities do not count as encumbered, unless these securities are pledged or collateralised in any way to secure a transaction;
g. assets in cover pools used for covered bond issuance; assets that are underlying covered bonds count as encumbered, except in certain situations where the institution holds the corresponding covered bonds as referred to in Article 33 of the CRR.

The table below reports the amount of encumbered and unencumbered assets by asset type in accordance with Template A of EBA Guidelines of 27/06/2014 and based on the median values of the quarterly data. The encumbered assets are: on-balance sheet assets that have been either pledged or transferred without derecognition or otherwise encumbered; collateral received that meets the conditions for recognition in the balance sheet of the transferee in accordance with the applicable accounting framework.

Tab. 10.1 – Assets

	Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
Assets	**56,325,364**		**119,956,505**	
of which: Equity instruments	*28,878*	*51,120*	*541,903*	*541,919*
of which: Debt securities	*19,850,930*	*20,053,215*	*9,019,950*	*8,893,996*
of which: Other assets	*1,130,115*		*21,092,359*	

As per Template B of the annex to the EBA Guidelines on the disclosure of encumbered and unencumbered assets of 27/06/2014, the table below shows the amount of encumbered and unencumbered collateral received that does not meet the conditions for recognition in the balance sheet of the transferee in accordance with the applicable accounting framework, typically guarantees for securities lending transactions or repo agreements (assets), including repurchased own issued securities.

Tab. 10.2 – Collateral received

	Fair value of encumbered collateral received or own debt securities issued	Fair value of collateral received or own debt securities issued available for encumbrance
Collateral received	**13,393,960**	**3,388,886**
of which: Equity instruments	*399,436*	*7,256*
of which: Debt securities	*12,944,214*	*3,381,630*
of which: Other collateral received	*50,310*	*-*
Own debt securities issued other than own covered bonds or ABSs	2,037,449	617,469

As per Template C of the annex to the EBA Guidelines on the disclosure of encumbered and unencumbered assets of 27/06/2014, the table below includes the total of the different sources of liabilities, of which the more significant for the MPS Group are repos (liaiblities), collateralized deposits other than repos and debt securities issued. The assets reported refer to both on- and off-balance sheet assets.

Tab. 10.3 – Encumbered assets / collateral received and associated liabilities

	Matching liabilities, contingent liabilities or securities lent	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered
Carrying amount of selected financial liabilities	52,980,613	62,657,933

The most quantitatively important item for the MPS Group in terms of encumbered assets is the funding through Repos (liabilities) on the institutional market and with customers.

11. Exposures to securitisation transactions

11.1 General information

The Group operates in the securitisation market both as an originator, through the issue of notes from originated securitisations, and as an investor through subscription of securities from third-party securitisations.

As at today, the Montepaschi Group has not sponsored any securitisation transactions.

Originated securitisations include:

- securitisation transactions structured with the aim of deriving economic advantages regarding the optimisation of the loan portfolio, the diversification of sources of funding and the reduction of the cost of funding and the alignment of the natural maturities of assets and liabilities (securitisation transactions in the strict sense);
- securitisations aimed at strengthening the available funding sources, through the conversion of the loans sold into securities that can be refinanced (self-securitisations). Self-securitisation transactions are part of the more general policy of strengthening the group's liquidity position and are not included in securitisations of a stricter sense since they do not transfer risk outside the Group.

For this reason, the numerical data concerning these transactions are not included in the tables under the quantitative section.

Securitizations in the strict sense of the term

In general this type of transaction involves the spin-off of a package of assets (generally loans) recognised in the balance sheet of Group Banks and its subsequent transfer to a Special Purpose Entity. The SPE, in turn, finances the purchase through the issue and placement of securities exclusively guaranteed by the assets received (ABS – Asset-Backed Securities). Resources raised in this way are returned to the Montepaschi Group (the seller), whereas commitments to subscribers are met using the cash flows generated by the loans sold. Following is an outline of the Group's main securitisation transactions (of the traditional type, as the Group has not engaged in any synthetic securitisations) originated in previous years and outstanding at 31 December 2015 - broken down into quality/type of underlying and vehicle company:

- securitisation of **performing loans**:
  - · Spoleto Mortgages Srl (2003, BP Spoleto);
  - · Siena Mortgages 10-7 Srl (2010, BMPS);
  - · Casaforte Srl (2010, BMPS);
  - · Siena Consumer (2013, Consum.it);
  - · Siena Consumer 2015 (2015, Consum.it);
  - · Siena PMI 2015 Srl (2015, BMPS).
- securitisation of **other assets**:

- Gonzaga Finance Srl (2000, BAM), closed on 16 February 2015.

Spoleto Mortgages Srl

Spoleto Mortgages Srl is a securitisation which was originated by Banca Popolare di Spoleto (BP Spoleto), a subsidiary of the Parent Company Banca MPS until 5 July 2013. As of this date, the shareholders' agreement with the co-operative company Spoleto-Credito e Servizi Società Cooperativa concerning the bank's shareholding (for a total of 22,972,924 ordinary shares) in Banca Popolare di Spoleto SpA was terminated with the latter being subsequently removed from the MPS Group's area of consolidation. Consequently, the securitisation Spoleto Mortgages Srl is no longer included among own securitisations but among third-party securitisations. The securitisation of Spoleto Mortgages Srl performing loans shows a residual debt of EUR 0.014 bn as at 31/10/2015 and on 25 November 2015 the vehicle company reimbursed 100% of the related senior notes and began reimbursement of the mezzanine notes.

In the course of 2010, in light of the European ABS market recovery and with a view to achieving economic benefits through reserves management, two additional securitisations were completed through the vehicles, Casaforte Srl and Siena Mortgages 10-7 Srl.

Siena Mortgages 10-7 S.r.l

This securitisation transaction was carried out on 30 September 2010. Its portfolio contained 34,971 BMPS performing, real estate backed loans for a total outstanding debt of approx. Euro 3.5 bn. The special-purpose vehicle Siena Mortgages 10–7 is 93% owned by Stichting Canova, a foundation incorporated under Dutch law, and the remaining part is owned by the Parent Company.

The vehicle structure ensures its independence. The remaining debt balance amounted to EUR 2.3 bn as at 31/12/2015.

On 22 November 2010, Siena Mortgages 10-7 financed purchasing of the portfolio by issuing Residential Mortgages Backed Floating Rate Securities in the following tranches:

Securities	Rating Fitch/ Moody's	Total consideration (€/mln)
A1 Senior	AAA/Aaa	595.00
A2 Senior	AAA/Aaa	400.00
A3 Senior	AAA/Aaa	1,666.90
B Mezzanine	NR /Caa1	817.60
C Junior	NR/NR	106.63

Classes A1 and A2 were placed with market investors, whereas the remaining classes of notes issued by the vehicle were initially underwritten by the Parent Company and a part of them (from Class 3) were sold on the market. The deal has not entailed the derecognition of the underlying assets from the balance sheet of the Parent Company (transferor), which has substantially retained all risks and rewards associated with the property of the assets sold.

Casaforte Srl

With a view to enhancing part of the Group's properties used in the business, the

Parent Company formalised an additional securitisation transaction for an amount of Euro 1.7 bn on 21 September 2010. The transaction was completed at the end of December in the same year with the transfer of receivables arising from a mortgage loan granted to the consortium company "Perimetro Gestione Proprietà Immobiliari", to vehicle Casaforte srl. As at 31/12/205, the total outstanding debt amounted to Euro 1,36 bn.

On 22 December, the vehicle Casaforte Srl (with share capital entirely held by Stichting Perimetro and registered offices in Amsterdam) issued asset backed securities (classes A, B and Z) in the following tranches:

Securities	Rating Fitch	Total consideration (€/mln)
A	A-	1,536.64
B	NR	130.00
Z	NR	3.00

Class B and Z notes are not offered to the public.

They were placed with professional and/or qualified investors. The securitisation-underlying assets were derecognised in their entirety from the balance sheet of the Parent Company, since all of the risks and rewards associated thereto were transferred to the vehicle in both form and substance.

The subsidiary MPS Capital Services holds Class A and B notes in its portfolio. At the end of December 2013, the MPS Group acquired control of 'Perimetro Gestione Proprietà Immobiliari' and 'Casaforte'. The acquisition of control was completed by way of a two-step purchase of 100% of Equity Instruments issued by Perimetro and Class Z notes issued by Casaforte for an approximate EUR 70 mln. The transactions are part of the activities planned for the restructuring of the 'Chianti Classico' trade, outlined in the Parent Company's Restructuring Plan and approved by the Board of Directors on 7 October 2013 and subsequently by the European Commission on 27 November 2013.

Siena Consumer Srl

This securitisation transaction was carried out in 2013 through the sale to the vehicle "Siena Consumer Srl" of a portfolio consisting of 200,542 personal loans, autoloans, and special-purpose loans originated by Consum.it S.p.A. of approximately EUR 1.5 bn. As at 31/12/2015, the remaining debt balance amounted to EUR 552.07mln (199,816 outstanding mortgages).

To finance the purchase of this portfolio, the Vehicle Company issued Residential Mortgage-Backed Securities (RMBSs, of which those in Class A were placed with institutional investors; the remaining classes were subscribed by the Originator.

Market placement of class A did not entail the derecognition of the underlying assets from the balance sheet of the Parent Company (transferor), which has substantially retained all risks and rewards associated with the property of the assets sold. Consequently, an offsetting entry for the cash flows arising from the disposal was posted on the liabilities side of the balance sheet.

As subordinated lender, upon occurrence of a Commingling Reserve Trigger (Rating MPS < BBB- for Fitch and BBB (low) for DBRS) the Parent Company may be required to pay to the vehicle the amount of the Commingling Reserve up to a maximum of EUR 188 mln. Moreover, ther Parent Company issued a guarantee in favour of the former subisidiary Consum.it S.p.A (now fully merged), to ensure its correct performance as servicer, for a maximum amount equal to the lesser between EUR 500 mln and the existing Class A notional amount (EUR 86.6 mln as at 31 December 2015). Finally, it should be noted that should the Originator exercise its early repayment option , the Parent Company will be required to pay the senior underwriters any additional costs resulting from that repayment.

For all the securitisation tranactions described above and for those entered into in the course of 2015 (described below), during the period under review the Parent Company and its subsidiaries did not provide any financial or other support without being obliged under the contract. There are no cases of financial or other support to a previously non-consolidated structured entity as a result of which the structured entity was controlled by the Group.

Moreover, the Group does not intend to provide financial or other support to consolidated securitisation vehicles, nor to assist entities in obtaining financial support.

Self-Securitisations

These transactions involve the transfer of a portfolio of loans originated by Group Banks to a Special Purpose Entity which, in turn, finances the purchase through the issue of Residential Mortgage- Backed Floating Rate Notes (also known as Residential Mortgage-Backed Securities or RMBS). All Residential Mortgage Backed Securities (RMBS) issued are underwritten by the Parent Company. Although the Group's full underwriting did not generate any direct cash flows from the market, it still provided the Group with securities that could be used for ECB refinancing and repo transactions, thereby improving the MPS's safety margin against the MPS Group's liquidity risk position. In fact, self-securitisations allow for liquidity requirements to be covered by optimising the amount of assets readily available. Securities that can be allocated with an AAA rating (eligible assets) represent the Group's main core for covering short-term obligations using instruments that can be readily liquidated. Within this logic, from 2007 to 2011 five self-securitisation transactions were carried out on performing loans for a total amount of Euro 20.1 bn and two self-securitisation transactions were carried out using the portfolio of loans to small and medium businesses issued by MPS Capital Services Banca per le Imprese Spa (MPS CS) and the Leasing portfolio of the subsidiary MPS Leasing & Factoring, for a total EUR 5.4 bn.

The two latter transactions were redeemed in 2014. Here follows a list of the self-securitisations as at 31 December 2015, which show a remaining debt of approximately EUR 6.7 bn:

- Self-securitisations of performing loans (mortgages):
  · Siena Mortgages 07 -5 Srl (2007);
  · Siena Mortgages 07 -5/Bis Srl (2008);
  · Siena Mortgages 09 -6 (2009);
  · Siena Mortgages 09 -6/Bis Srl (2009).

The first two transactions, involving performing residential mortgage loans were carried out in December 2007 (Euro 5.2 bn) and march 2008 (Euro 3.4 bn) for an overall amount of Euro 8.6 bn, through the vehicle, Siena mortgages 07-5 Srl.

In 2009, two new transactions were added (Euro 4.4 bn as at February 2009 and Euro 4.1 bn as at June 2009), involving performing loans for a total of approx. Euro 8.5 bn through the vehicle, Siena mortgages 09 – 6 Srl. These transactions have generated eligible assets for a total amount of Euro 4.9 bn at 31/12/2015.

Self-securitisations do not contribute to the numerical data reported in the following tables of the quantitative disclosure, because - as was explained above - they do not constitute securitisations in the strict sense of the term.

Securitisation transactions completed in 2015

In 2015, two new securitisation transactions were entered into and the covered bonds issuance programme continued to be implemented.

Siena Consumer 2015 Srl

On 27 February 2015, the former subsidiary Consum.it S.p.A., now absorbed into the Parent Company, carried out a second securitisation transaction with the disposal of a portfolio of 198,371 personal, auto and special purpose loans, all disbursed by Consum.it S.p.A. As at 31 December 2015, the remaining debt balance amounted to EUR 1,036.7 mln (nr. 198,251 outstanding loans).

The transaction was carried out in order to optimise the Group's liquidity profile.

To finance the purchase of this portfolio the Vehicle issued various classes of ABS securities, of which those in the Senior Class were placed with an institutional investor; the remaining mezzanine and junior classes were subscribed by the Bank.

The securities do not carry a rating.

The disposal of classes A did not entail the derecognition of the underlying assets from the balance sheet of the Parent Company, which has substantially retained all risks and rewards associated with the ownership of the assets sold; therefore, a liability was recognized under the Vehicle as an offsetting item to the liquidity received from the sale.

Siena PMI 2015 Srl

In order to optimise the Group's liquidity profile, il 6 agosto 2015 è stata lanciata una cartolarizzazione di crediti verso piccole e medie imprese originati da BMPS.

On 26 June 2015, BMPS transferred to the vehicle company "Siena PMI 2015 Srl", a portfolio of performing, unsecured or mortgage loans disbursed to Italian, SMEs, consisting of 24,683 mortgages totaling € 3,002.7 mln. As at 31 December 2015, the remaining debt balance amounted to EUR 2,605.1 mln (23,777 outstanding loans).

To fund the acquisition of the portfolio, the Vehicle issued ABS securities on 6 August 2015. In the senior tranche, Senior classes A1A and A1B were placed with institutional investors, while classes A2A and A2B were placed with the European Investment Bank. The remaining classes of notes issued were repurchased by the Bank (transferor).

The Senior and Mezzanine classes were rated by Moody's and DBRS.

The new did not entail the derecognition of the underlying assets from the balance sheet of the Parent Company, which has substantially retained all risks and rewards associated with the ownership of the assets sold; therefore, a liability was recognized under the Vehicle as an offsetting item to the liquidity received from the sale.

Third-party securitizations

The Group allocates a part of its capital to stock market investments, with the objective to:

- attain a risk-adjusted return that is significantly higher than the cost of allocated capital so as to create value for the shareholders;
- diversify risks with respect to other risks that are typical of its business;
- maintain in-depth and up-to-date knowledge of financial market trends which additionally and inevitably condition the domestic markets in which the Group mainly operates.

Activities are overseen by the Finance, Treasury and Capital Management Area and are carried out within a broad and varied range of potential financial market areas so as to draw maximum benefit from risk diversification and reduced exposure to individual sectors: from investment activities in the government bonds, securities and forex markets to activities in the corporate bond and credit derivative markets.

Third-party securitisations are compliant with the above-mentioned process of diversification and with the support of a specialised desk within the subsidiary, Mps Capital Services. The investment process starts with the analyses carried out by the traders in a bottom-up logic and is included in the overall monitoring of portfolio risks. As with all operations in securities markets, these investments are subject to risk limits set by the Board of Directors that are monitored daily by the Business Control Units and Risk Management; Stop loss, risk and nominal limits are defined for maximum exposure for major issuer categories broken down by rating.

Methods for calculating risk weighted exposures

To calculate capital adequacy for credit risk relating to securitisation transactions included in the Banking Book, the MPS Group applies the standardised approach and the AIRB approach.

The standardized approach is also used to calculate the capital requirement for market risk (specific risk) relating to securitised exposures included in the Trading Book for Regulatory purposes.

Under the standardized approach, risk-weighted exposure is calculated by applying a 'weight' depending on the ratings assigned by an External Credit Assessment Institution (ECAI) to the securitised exposures (in the banking book and trading book). The ECAIs used by the group for positions in short-term rated securitisations and securitisations other than those with a short-term rating, include:

- *Fitch Rating Ltd,*
- *Moody's Investors Service Ltd,*
- *Standard & Poor's Rating Services,*
- *DBRS.*

Under the AIRB approach, the Supervisory Formula Approach (SFA) is adopted for Tranched Cover transactions.

Below is a list of the securitisations along with the agencies that provide their ratings.

Type[a]	Rating agencies
PERFORMING LOANS	
SPOLETO MORTGAGES (BP SPOLETO)	Moody's Investors Service Ltd Standard & Poor's Rating Services
SIENA MORTGAGES 10-7 (BMPS)	Fitch Rating Ltd Moody's Investors Service Ltd
CASAFORTE (BMPS)	Fitch Rating Ltd Moody's Investors Service Ltd
SIENA CONSUMER (CONSUM.IT)	N.R. N.R.
SIENA CONSUMER 2015 (CONSUM.IT)	N.R. N.R.
SIENA PMI 2015 Srl (CONSUM.IT)	Moody's Investors Service Ltd DBRS Rating Ltd
OTHER ASSETS	
GONZAGA FINANCE (BAM)	Moody's Investors Service Ltd Standard & Poor's Rating Services

(a) Originator in brackets.

Accounting policies

The accounting of securitisation transactions completed prior to the first-time adoption (FTA) of international accounting standards is not reported in the financial statements inasmuch as the Group has made use of the optional exemption provided for by IFRS 1, which permits not re-posting financial assets/liabilities sold or derecognised prior to 1 January 2004. Therefore, loans underlying the transactions prior to the first-time-adoption of international accounting standards have been derecognised from the transferor's balance sheet. The relative junior securities underwritten have been classified among receivables. For transactions completed subsequent to the first-time-adoption of international accounting standards, where receivables were sold to vehicle companies and in which - even with formal transfer of legal ownership of the receivables - control over the cash flows deriving therefrom and most risks and rewards are maintained, the loans that are the object of the transaction are not eliminated from the transferor's balance sheet. In this case, a payable is posted with the vehicle company net of the securities issued by the company and repurchased by the seller. The profit and loss statement also reflects the same accounting criteria. related junior notes underwritten were classified among receivables. Thus, for the purposes of calculating capital absorption, the loans are maintained in the Group's weighted assets as if they had never been sold. The only exception among securitisations completed after F.T.A. (first-time adoption) and outstanding as at 31.12.2015 is Casaforte Srl, the underlying receivables of which were removed in their entirety from the Parent Company's balance sheet since the risks and rewards connected thereto were transferred to the vehicle company in both form and substance. From an accounting standpoint, self-securitisations do not entail the derecognition of underlying assets.

Control System and Top Management Reporting

The securitisation management process is supported by a specific internal procedure which assigns roles and responsibilities to the various organisational units involved in the individual phases of the process.

The Parent Company's ALM & Capital Management function establishes general practices and coordinates activities in relation to securitisation transactions. The Montepaschi Group set up a specific unit within the Parent Company's Specialised Processes and Services Area, responsible for determining the rules and criteria for the management of performing securitisations. More specifically, the Special-purpose Loans and Securitisations Service within this area sets the operational guidelines while looking after aspects and obligations associated with servicing activities.

The trend of the transactions is steadily monitored through the periodical (monthly and quarterly) recording of remaining principal repayment flows, default and bad debt positions generated by these securitisations.

In coordination with other originator Banks in the Group, the Special-Purpose Loans and Securitisations Service prepares summary reports on portfolios sold ("total reports"). In addition, as part of critical situation management, the ALM & Capital Management Service, notifies cases that may pose potential risks for noteholders to the relevant functions in the organisation.

In its capacity as third-level control body, the internal audit area uses sampling procedures to periodically validate:

- whether the degree of recoverability of loans sold is accurate and, as a result, whether the fair value of securities issued is appropriate;
- whether line checks assigned to the various units have been carried out and roles and responsibilities properly identified;
- it also verifies the compliance of reporting/accounting procedures with current regulations in collaboration with other units, as necessary;
- the existence of any conflicts of interest with respect to noteholders; and compliance, on a sampling basis, with the obligations of law 197/91, as amended.

Non-performing securitisations, on the other hand, are managed by the Debt Collection Area, while all activities connected with the securitisation of loans originated by other subsidiaries (in particular Mps Leasing&Factoring) are managed by the subsidiaries themselves.

Risk-hedging policies

With regard to monitoring procedures for risks inherent in own securitisations , the Bank uses the control tools already in place for portfolio risks. Pursuant to the provisions set out in the Supervisory Instructions Issued by the Bank of Italy on this subject, the Bank makes sure that the overall transactions are managed in compliance with the law and the prospectuses.

When transactions are structured, it is the responsibility of the ALM & Capital Management Service, in collaboration with the Arranger and liaising with the asset-holding unit, the Quality Control function and Risk Management, to submit to the approval of the Finance Committee the definition of the hedging strategy as well as the potential recourse to a back-to-back swap as a way to hedge against the risks of fluctuations in the interest rates of securitised assets.

With regard to procedures aimed at monitoring the risks of third party securitisations, the Bank uses the control tools and internal models implemented for the measurement and management of market risks in line with the qualitative and quantitative requirements set out by the regulatory authorities. In detail, the BoD-defined limits of the following are monitored: Stop loss, Value at risk (Var) and nominal limits of maximum exposure by issuer's product categories, broken down by rating classes. Finally, the appropriateness and quality of the market settings applied to Front Office and market risk management are monitored, as are the frequency and quality of upgrades.

Traditional securitisations and self-securitisations originated by the Group are also relevant for liquidity risk monitoring and management. Securitisations have been used by the Group in recent years primarily with a view to 'certificate' commercial assets, using hem for ECB refinancing transactions and collateralised securities lending. In order to maximise the efficiency and economic advantageousness of these transactions, some of the structuring roles required are generally carried out by the *originator bank* itself. In particular, the roles that are particularly relevant for the purpose of liquidity management include the following:

- Servicer: the originating entity, which manages the cash flows and usually maintains a direct relationship with its own customers, avoiding disclosure of the list of debtors sold to a third party entrusted with the collection of payments for -and daily management of- the portfolio in question;
- Account Bank**:** the entity that acts as a custodian of the securitisation liquidity, i.e. the depository bank for the collections that the servicer deposits on a daily basis;
- Swap counterparty**:** the direct counterparty for vehicles' interest rate risk hedging swaps.

To fulfil the above roles, the entity is required to comply with specific credit market requirements for the entire period in which the transaction is in place. To maintain the rating of its transactions, if the creditworthiness of the *originator* is downgraded to a rating below the minimum levels set out by the Rating Agencies, the originator will be required to put in place remedies which may expose it to liquidity risk. On a case by case basis it may, in particular, be necessary to collateralize or secure the credit exposure arising from the role itself or replace it with a third institution. Consequently, a downgrade has significant repercussions on the originating banks in terms of liquidity risk, due both to higher collateral required to maintain the typical roles of these transactions in place and the cost for outsourcing part of these roles.

More specifically:

- in order to maintain the role of Servicer, if the bank's rating is downgraded to below the levels set out by the rating agencies, it will be required to fund a reserve, known as the **commingling** reserve which, should a default occur, will provide hedging against the risk that the amounts collected on behalf of the vehicle and not yet credited to the vehicle's accounts may fall into the funds available for the general body of creditors of the bankrupt bank;
- for the role of Account Bank, Rating Agencies may require a third bank to be entrusted with the custody of the vehicles' financial assets, thus generating strong liquidity losses;
- for the role of Swap Counterparty, if credit scoring is below a certain level, Agencies may require either replacement of (or a guarantee from) the counterparty or specific collateralization. Externalisation or derivative guarantee may instead be imposed by the agencies if creditworthiness is below a certain limit threshold.

Covered Bond Transactions

The MPS Group currently has two Covered Bond programmes for a total of Euro 30 bn. In the course of 2010, the Montepaschi Group launched a first programme for the issuance of Covered Bonds for an amount of Euro 10 bn with a view to improving the mid-long term financial profile.

In light of the developments in the financial markets, the programme should be considered as part of a wider strategy, aimed at:

- curbing the costs of funding: covered bonds are widely preferred, inasmuch as they are issued directly by the bank and their repayment is guaranteed by a segregated pool of assets (in this case, residential mortgage loans); in the event of issuer bankruptcy, covered bond holders enjoy a right of recourse on a portfolio of segregated high-quality assets and are, therefore, willing to accept a lower yield than the one offered by similar uncovered bonds;
- diversifying the bank's funding sources on the international market too;
- lengthening its average debt maturity profile.

On 26 June 2015, the meeting of covered bond holders approved the proposed amendments to the Programme which made it possible to:

- amend the Programme, to obtain a rating from DBRS (in addition to Moody's and Fitch) for the covered bonds issued and to be issued as part of the Programme;
- activate, if specific cases of default take place pursuant to the Programme, a "conditional pass through" type mechanism for the repayment of the bonds issued.

With a view to improving the efficiency and stability of the Group's counterbalancing capacity, in 2012 a second issuance programme was authorised for a maximum of Euro 20 bn. The covered bonds were not explicitly rated when launched but, in the course of 2013, were assigned a rating (A) by the agency DBRS. The second programme is not intended for the market but for transactions eligible as collateral in refinancing transactions through the European Central Bank.

These transactions are structured into the following stages:

a) the Parent Company, or other Group Company, transfers, without recourse, a pool of assets having certain characteristics to the vehicle, MPS Covered Bond S.r.l. and MPS Covered Bond 2 S.r.l, thus forming a segregated *Cover Pool*;
b) the Transferor grants a subordinated loan to the vehicle, for the purpose of financing payment of the assets' purchase price by the vehicle;
c) the Parent Company issues covered bonds secured by an autonomous, irrevocable and unconditional first demand guarantee issued by the vehicle for the only benefit of the bond-holding investors and senior debtors involved in the transaction; the guarantee involves limited recourse to the assets of the Cover Pool owned by the vehicle (guarantor).

The structure of the deal is such that the Parent Company is the transferor (a), lender (b) and issuer (c) in the transaction.

In order to allow the transferee to meet the obligations of the collateral pledged, the Parent Company uses appropriate Asset & Liability Management techniques to secure a trend of substantial balance between the maturities of cash flows arising from the assets sold and maturities of payments due in relation with the covered bonds issued and other costs of the transaction. The programmes, in both cases, were structured in compliance with applicable rules and regulations which authorise the issuance of covered bonds only if the transferring and issuing banks meet certain capital requirements.

The structure of the debt issuance programmes of the Parent Company (transferor and servicer) is subject to stringent regulatory requirements and calls for continuous actions by the Specialised Credit Processes and Services Area; Finance, Treasury & Capital Management and Risk Management Areas, as well as supervision by an external auditor (Deloitte & Touche) as asset monitors. In particular, these actions include:

- assessment of capital requirements mandated by Supervisory Instructions when it comes to covered bond issuance programmes;

- assessment of the quality and integrity of assets transferred with regard, in particular, to the estimated value of properties, both residential and non-residential, on which a mortgage in relation with the asset-backed loans is placed; this assessment may result in repurchases, integrations and additional transfers of supplemental assets;
- assessment of an appropriate ratio being maintained between bonds issued and assets transferred as collateral (Cover Pool -mortgage and residential assets; commercial assets for the second programme);
- assessment of transfer limits and integration practices;
- assessment on whether risks are effectively and adequately hedged by derivative contracts in relation to the transaction.

In the course of 2013, the mitigation strategy for interest rate risk on the first Programme was restructured in order to minimise the Vehicle's exposure to market counterparties. In particular, the newly-defined strategy aims to only cover the Vehicle's net exposure to interest rate risk, as opposed to the nominal amount.

At the same time, in December 2013, the outsourcing of three Covered Bond Swaps outstanding with market counterparties was carried out. This was followed in 2014 with the further outsourcing of 3 Covered Bond Swaps for a total of € 2 bn.

The paragraphs below provide information on the nature of the risks associated with the interest in the MPS Covered Bond S.r.l. vehicle, whose assets are pledged as collateral of bond issues of the Parent Company partly placed with the market.

In particular, the terms of the agreements that could require the Group to provide financial support to the vehicle MPS Covered Bond S.r.l. are as follows:

- the Parent Company undertakes, in accordance with the programme's terms, to ensure compliance over time with the regulatory and contractual tests determined according to the methodologies set by the rating agencies from time to time;
- if the Parent Company's rating decreases below "BBB(low)" (DBRS), "BBB-" (Fitch) and "Baa3" (Moody's), the repayment of each subordinated loan will be delayed by 6 months after the original expiry;
- in accordance with the Master Definition Agreement, the Parent Company shall allocate and change the amount of the variable liquidity reserve according to criteria agreed upon with the rating agencies.

During the period under review the Parent Company and its subsidiaries did not provid any financial or other support without being obliged under the contract.

There are no cases of financial or other support to a previously non-consolidated structured entity as a result of which the structured entity was controlled by the Group.

The Group does not intend to provide

financial or other support to the vehicle, nor to assist the entity in obtaining financial support.

Description of individual issuances

In order to support the issuances of Covered Bonds in the first programme, the Parent Company transferred a portfolio of approximately 170 thousand mortgages for a total value of Euro 17.3 bn, consisting in performing residential mortgages in real estate and building secured by 1st mortgages and with all instalments regularly paid as at the date of valuation of the portfolio.

2015 saw the disposal of a portfolio of 15,080 performing mortgages granted to natural persons residing in Italy meeting the identified selection criteria, substantially comparable to those used for previous disposals, for an amount of approximately EUR 1,529 mln.

Details are reported in the table below:

Date of sale	Portfolio	Loans number	Amount (€/bln)
21/05/10	Loans BMPS	36,711	4.4
19/11/10	Loans BMPS	19,058	2.4
25/02/11	Loans BMPS	40,627	3.9
25/05/11	Loans BMPS (ex BAV)	26,804	2.3
16/09/11	Loans BMPS	27,973	2.3
14/06/13	Loans BMPS	4,259	0.4
18/09/15	Loans BMPS	15,080	1.5
Total		**170,512**	**17.3**

In the Covered Bond, it is MPS and not the vehicle that directly issues the bonds.

As part of its first issuance programme, the Parent Company completed a total of 21 issuances, twelve of which had not yet matured or been repaid early for a total, as at 31 December 2015, of EUR 8,570 mln, of which EUR 6,200 mln were placed on the market, while EUR 2,370 mln were repurchased by the Bank.

The remaining debt balance on the portfolio as at 31 December 2015 amounted to EUR 11,909.4 mln for 140,526 mortgages.

In 2015 two notes were issued for a total of EUR 1,750 mln, fully placed on the market:

Issuer Date	Legal Maturity	Interest Rate	Amount (€/bln)
28/10/15	jan-22	1.25%	0.75
26/11/15	nov-25	2.13%	1
Total			**1.75**

As part of the second Programme, the Parent Company sold a portfolio of approximately 101 thousand mortgages for a total of around € 14.6 bn to support 17 issuances (of which 6 matured or redeemed), which were not intended for the market but repurchased by the Bank and used as collateral for refinancing transactions in the Eurosystem, for a total as at 31 December 2015 of EUR 6,300 mln.

The portfolio sold consists of real estate-backed, residential and commercial mortgage loans, receivables from -or guaranteed by- the Public administration and securities issued as part of securitisations consisting in these same types of loans and receivables.

On 16 October 2015, a portolio containing 5,671 residential and commercial mortage loans was sold for € 977.5 mln. Details are reported in the table below:

Date of sale	Portfolio	Loans number	Amount (€/bln)
27/04/12	Residential Mortgages	27,047	2.38
22/06/12	Residential and commercial Mortgages	13,993	2.48
24/08/12	Residential and commercial Mortgages	17,353	1.40
21/09/12	Residential and commercial Mortgages	9,870	2.47
15/02/13	Residential and commercial Mortgages	9,033	1.29
21/06/13	Residential and commercial Mortgages	12,771	2.15
29/03/14	Residential and commercial Mortgages	5,645	1.46
16/10/15	Residential and commercial Mortgages	5,671	0.98
Total		**101,383**	**14.6**

Management of the new Covered Bond Programme follows the proven processes and controls already adopted for management of the covered bonds Programme established in 2010.

The covered bonds issued as part of the second programme amount to seventeen, 11 of which have not yet matured or been reimbursed early. They were not intended for the market but repurchased by the bank and used as collateral for refinancing transactions in the Eurosystem for a total EUR 6,300 mln as at 31 December 2015.

The following issuances were carried out in 2015:

Issuer Date	Legal Maturity	Interest Rate	Amount €/bln)
04/02/15	apr-18	Adjustable Euribor 3m+1.0%	0.8
06/05/15	jul-18	Adjustable Euribor 3m+1.0%	0.3
Total			**1.1**

From an accounting viewpoint, both covered bond transactions did not involve the derecognition of assets sold and consequent recognition in the balance sheet of swaps connected with the transaction. It should be noted that:

- transferred loans continue to be reported in the Parent Company's balance sheet inasmuch as the Parent Company retains the risks and rewards of ownership of the loans transferred;
- the loan disbursed by the Parent to the Vehicle is not classified as a separate item in the balance sheet, since it is offset with the amount due to the Vehicle in which the initial transfer price was recognised. The loan, therefore, is not subject to credit risk assessment, because this risk is entirely reflected in the assessment of transferred loans, which continue to be reported in the Parent Company's balance sheet;
- loans are subject to movements based on own events (figures and assessment);
- instalments collected by the Parent (which also acts as a servicer) are reallocated daily to the Vehicle's "collection account" and accounted for by the Parent as follows:
  - collection of principal from borrower is recognised as an offsetting entry to the reduction in the loan to the borrower;
  - reallocation of principal to the Vehicle is recognised as an offsetting entry to the recognition of a loan to the Vehicle; this loan is paid off upon repayment of the subordinated loan;
  - interest received by borrower is recognized as an offsetting entry to account 10 "Interest income: loans to customers" (interest on loans continues to be recognised on an accrual basis);
  - reallocation of interest to the Vehicle is

recognised as an offsetting entry to the recognition of a loan to the Vehicle;
- this loan is paid off upon collection of the receive leg of the Cover Pool Swap.

- the Vehicle “MPS Covered Bond S.r.l.” is invested in by the Parent Company for a control stake of 90%, recognised under account 100 “Equity investments” and included in the Group’s consolidated financial statements under the comprehensive approach;
- the vehicle “MPS Covered Bond 2 S.r.l.” is invested in by the Parent company for a control stake of 90%, recognised under Account 100 “Equity investments” and included in the Group’s consolidated financial statements under the comprehensive approach;
- bonds issued are posted to Account 30 “debt securities in issue” on the liabilities side, and related interest expense is recognized on an accrual basis.

The following tables report the Group’s overall exposures in securitisations.

11.2 Quantitative disclosure

Tab. 11.2.1 – Exposures securitised by the MPS Group

Type of Assets/Exposures securitised	Exposure net	Exposure of which impaired	Losses for the period
RMBS	**6,311,105**	**42,583**	**-**
Non-performing loans	-	-	-
	-	-	-
Mortgages	6,311,105	42,583	-
Mantegna Finance II (BAM - repurchase 5/8/2013)	-	-	-
Casaforte Srl (Banca MPS)	1,366,636	-	-
Siena Mortgages 10 -7 (Banca MPS)	2,339,332	42,583	
Siena PMI 2015 Srl	*2,605,137*		
ABS	**1,583,007**	**108,590**	**-**
Consumer Credit	1,583,007	108,590	-
Siena Consumer (Consum.it merged on 1 June 2015)	*590,974*	*38,902*	-
Siena Consumer 2015 (Consum.it merged on 1 June 2015)	*992,033*	*69,688*	
CDO	**-**	**-**	**-**
Bonds and credit derivatives	-	-	-
Gonzaga Finance (BAM)	-	-	-
Total as at 31/12/2015	**7,894,112**	**151,173**	**-**
Total as at 31/12/2014	**4,911,908**	**50,438**	**-**

Reported below are the assets underlying the securitizations originated by the Bank, included in the Banking Book and Trading Book. These securitizations involve total derecognition of underlying assets from an accounting viewpoint, with the exception of Siena Mortgages 10 – 7, Siena PMI 2015 Srl, Siena Consumer and Siena Consumer 2015.
The Group has not issued any synthetic securitizations so far.

The following tables report the Group's overall exposures in on- and off-balance sheet securitisations broken down by banking and Trading book and by type of securities.
The tables refer to exposures used for prudential supervisory reporting purposes and include securitised exposures that are not recognised for the purpose of capital requirement calculation. In this latter case, capital requirements are calculated having regard to the securitised assets and not to the corresponding exposure.

Tab. 11.2.2 – Total Securitised Exposures by type of Securities(*) (On and Off-Balance sheet)

	Securitisations		Total
	own	of third parties	
1. Balance-sheet exposures	**1,041,687**	**70,804**	**1,112,491**
Banking book	**2,821**	**3,914**	**6,734**
CLO	2,821	3	2,824
CDO	-	3,910	3,910
Regulatory Trading book	**1,038,867**	**66,890**	**1,105,757**
ABS	-	65,823	65,823
CLO	967,936	1,067	969,003
CDO	70,931	-	70,931
2. Off-balance-sheet exposures	-	-	-
Total as at 31/12/2015	**1,041,687**	**70,804**	**1,112,491**
Total as at 31/12/2014	**843,044**	**99,484**	**942,528**

(*) Asset types are defined in the Glossary.

Tab. 11.2.3 – Own securitised exposures by type of securities and underlying assets – Banking Book

	Junior	Mezzanine	Senior	Total
CLO	**2,821**	**-**	**-**	**2,821**
Mortgages	2,821	-	-	2,821
Total as at 31/12/2015	**2,821**	**-**	**-**	**2,821**
Total as at 31/12/2014	**6,915**	**-**	**-**	**6,915**

The shown exposures are not included in the calculation of prudential requirements reported in Tables 11.2.8 and 11.2.9.
Since this is an own securitisation with derecognition of underlying assets, please note that "Receivables" includes the assets acquired by the Originator Banca MPS and therefore included in the exposures in the related regulatory portfolios reported in table 5.2.2.

Tab. 11.2.4 – Third-party securitised exposures by type of securities and underlying assets – Banking Book

	Junior	Mezzanine	Senior	Total
CDO	**3,910**	**-**	**-**	**3,910**
Bond	3,910	-		3,910
CLO	**-**	**3**	**-**	**3**
Public Sector Loans	-	3	-	3
Total as at 31/12/2015	**3,910**	**3**	**-**	**3,914**
Total as at 31/12/2014	**-**	**-**	**49,994**	**49,994**

Tab. 11.2.5 – Own securitised exposures by type of Securities and underlying assets – Trading Book

	Junior	Mezzanine	Senior	Total
CBO	**-**	**-**	**70,931**	**70,931**
Bond	-	-	70,931	70,931
CLO	**-**	**135,323**	**832,612**	**967,936**
Commercial mortgages	-	135,323	832,612	967,936
Total as at 31/12/2015	**-**	**135,323**	**903,544**	**1,038,867**
Total as at 31/12/2014	**-**	**115,482**	**720,647**	**836,129**

The shown exposures are not included in the calculation of prudential requirements reported in Tables 11.2.10 and 11.2.11.

Tab. 11.2.6 – Third-party securitised exposures by type of Securities and underlying assets – Trading Book

	Junior	Mezzanine	Senior	Total
ABS	**-**	**-**	**65,823**	**65,823**
Commercial mortgages	-	-	725	725
Residential mortgages	-	-	25,816	25,816
Consumer loans	-	-	39,281	39,281
CLO	**-**	**1,067**	**-**	**1,067**
Public Sector Loans		1,067	-	1,067
Total as at 31/12/2015	**-**	**1,067**	**65,823**	**66,890**
Total as at 31/12/2014	**766**	**2,588**	**25,461**	**49,490**

Tab. 11.2.7 – Total securitised exposures by Banking/Trading and related capital requirements (standard approach)

Type	Exposure	Requirement
Banking Book	13,778	4,099
↳ *of which Standardised Approach*	*3,914*	*3,910*
↳ *of which Airb Approach*	*9,865*	*189*
Regulatory Trading Book	66,890	3,211
Total as at 31/12/2015	**80,668**	**7,310**
Total as at 31/12/2014	**103,578**	**17,779**

The tables refer to securitised exposures (own and third-party securitisations), broken down by Banking or Trading book subject to the standard approach and related capital requirements. The tables do not include exposures whose requirements are calculated on the basis of their underlying assets. The risk weighting factors provided for by regulations are applied in this latter case and such exposures are included in the regulatory portfolios of Table 5.2.2 Exposures in own and third-party securitisations and re-securitisations are not credit risk mitigated through CRM techniques such as those included in Table 5.5.1 and 5.2.2. The exposures broken down by Banking or Trading book, type of securitisation and weight band are reported in the tables below.

Tab. 11.2.8 – Securitised exposures by risk weight bands – Banking Book

Type	Risk weight band							Total
	0%	20%	50%	100%	225%	650% 1250%	1250% No Rating	
Own Securitisations	-	-	-	-	-	-	-	-
Third-party Securitisations	3	-	-	-	-	-	3,910	3,914
Re-securitisation	-	-	-	-	-	-	-	-
Total as at 31/12/2015	**3**	**-**	**-**	**-**	**-**	**-**	**3,910**	**3,914**
Total as at 31/12/2014	**-**	**-**	**-**	**-**	**49,994**	**-**	**4,094**	**54,088**

The table above details the securitised exposures by risk weight bands and type of transactions. The amounts shown, in line with prudential regulations, relate to own and third-party securitised exposures included in the banking book. Therefore, they do not include the securitised exposures included in the regulatory trading book, detailed in the following tab. 11.2.10. Moreover, as far as own securitisations are concerned, in compliance with supervisory regulations, the table does not include securitised exposures:
a) that refer to transactions that are not recognised as securitisations for prudential supervisory purposes, since, among other reasons, they do not entail the actual transfer of credit risk;
b) whose overall risk-weighted value to the same securitisation exceeds the risk-weighted value of underlying securitised assets, calculated as if they had not been securitised (cap test).
Both in the case of a) and b), capital requirements are calculated in relation to securitised assets and not to the corresponding exposures securitised. Moreover, in this case, securitized assets are classified in their original regulatory classes (exposures secured by real estate, etc.) and are therefore excluded from "Securitisations".

Tab. 11.2.9 – Capital requirements of securitised exposures by risk weight bands – Banking Book

Type	Risk weight band 0%	20%	50%	100%	225%	650% 1250%	1250% No Rating	Total
Own Securitisations	-	-	-	-	-	-	-	-
Third-party Securitisations	-	-	-	-	-	-	3,910	3,910
Re-securitisation	-	-	-	-	-	-	-	-
Total as at 31/12/2015	**-**	**-**	**-**	**-**	**-**	**-**	**3,910**	**3,910**
Total as at 31/12/2014	**-**	**-**	**-**	**-**	**8,999**	**-**	**4,094**	**13,093**

Tab. 11.2.10 – Securitised exposures by risk weight bands – Trading Book

Type	Risk weight band 20%	50%	100%	225%	350%	650% 1250%	1250% No Rating	Total
Risk weight band						-	-	-
Cartolarizzazioni di Terzi	47,307	2,375	16,141	-	-	1,067	-	66,890
Re-securitisation	-	-	-	-	-	-	-	-
Total as at 31/12/2015	**47,307**	**2,375**	**16,141**	**-**	**-**	**1,067**	**-**	**66,890**
Total as at 31/12/2014	**23,459**	**22,677**	**-**	**-**	**-**	**3,354**	**-**	**49,490**

The table above details the exposures securitised by risk weight bands and by type of transactions.
The amounts shown relate to own and third-party securitised exposures included in the regulatory trading book.

Tab. 11.2.11 – Capital requirements of securitised exposures by risk weight bands – Trading Book

Type	Risk weight band 20%	50%	100%	225%	350%	650% 1250%	1250% No Rating	Total
Own Securitisations	-	-	-	-	-	-	-	-
Third-party Securitisations	757	95	1,291	-	-	1,067	-	3,211
Re-securitisation	-	-	-	-	-	-	-	-
Total as at 31/12/2015	**757**	**95**	**1,291**	**-**	**-**	**1,067**	**-**	**3,211**
Total as at 31/12/2014	**375**	**907**	**-**	**-**	**-**	**3,354**	**-**	**4,636**

12. Operational Risk

12.1 Operational Risk: general disclosure

The Montepaschi Group has implemented an integrated risk management system on the basis of a governance model which involves all the companies of the Montepaschi Group included in the scope of application. The approach defines the standards, methods and instruments that make it possible to measure risk exposure and the effects of mitigation by business area.

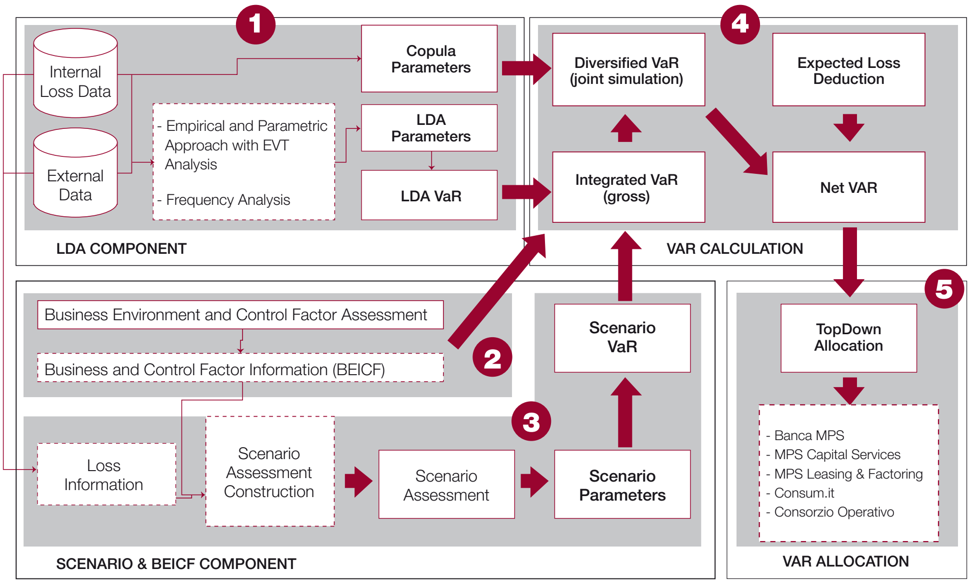
The Montepaschi Group was authorized by the Bank of Italy on 12 June 2008 to use the internal advanced measurement approach (AMA) for the calculation of capital requirements for operational risks. The advanced model officially started operating on 1 January 2008. The first consolidated regulatory reporting on the basis of the model was prepared in relation to the results as at 30 June 2008.

All the domestic banking and financial components are incorporated in the scope of advanced measurement approach (AMA). For remaining components and foreign companies, the foundation model has been adopted.

Today's internal model coverage in terms of total banking income exceeds 95%. The advanced approach adopted by the Montepaschi Group is designed so as to homogeneously combine all the main qualitative and quantitative information (or data) sources (mixed LDA-Scenario model). The quantitative loss Distribution Approach component is based on the statistical collection, analysis and modelling of internal and external historical loss data (Italian Database of Operational Losses, DIPO). The model includes calculation in relation to the 7 categories of events established by Basel 2 used as risk classes, with the adoption of Extreme Value Theory techniques. The estimated frequency of occurrence is based exclusively on internal data.

The qualitative component focuses on the evaluation of the risk profile of each unit and is based on the identification of relevant scenarios. In this framework, the companies are involved in process and risk identification, risk evaluation by process managers, identification of possible mitigation plans, discussion (in scenario-sharing sessions) of priorities and technical-economic feasibility of mitigation actions with the H.O. units.

Despite having insurance coverage to mitigate operational risk, the MPS Group does not use insurance for the mitigation of risk in the calculation of capital requirements since this has not yet been authorized by the supervisor.



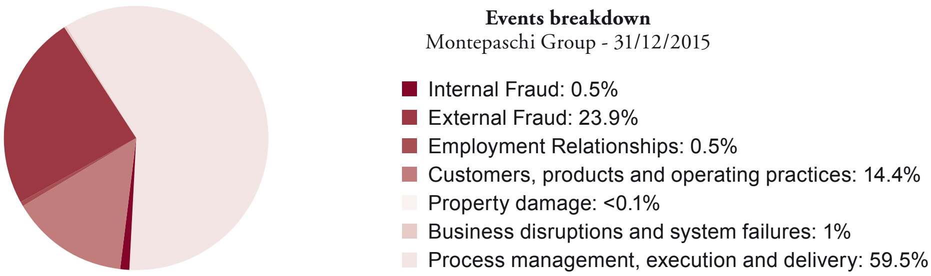
Finally, the percentage breakdown of events and operational losses recorded in 2015 is reported, divided into the following risk classes:

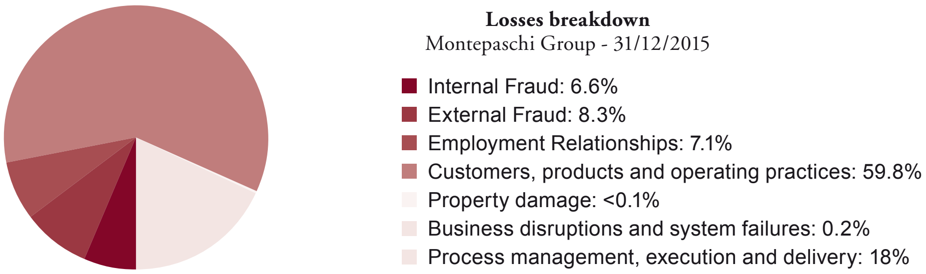
- Internal fraud: losses arising from unauthorised activities, fraud, embezzlement or violation of laws, regulations or corporate directives that involve at least one internal resource of the Group;
- External fraud: losses due to fraud, embezzlement or violation of laws by subjects external to the Group;
- Employment relationships and Occupational safety: losses arising from actions in breach of employment, occupational health and safety laws and agreements, payment of compensation for personal injury or episodes of discrimination or failure to apply equal treatment;
- Customers, products and operating practices: losses arising from non-fulfilment of professional obligations with customers or from the nature and characteristics of the product or service provided;
- Property damage: losses arising from external events, including natural disasters, acts of terrorism or vandalism;
- Business disruptions and system failures: losses due to business disruption or system failures or interruption;
- Process management, execution and delivery: losses arising from operational and process management shortfalls, as well from transactions with business counterparties, vendors and suppliers.

As at 31 December 2015, operational losses and the number of events were significantly down compared to December 2014. The types of event with the greatest impact on the income statement remain attributable to non-fulfilment of professional obligations with customers" (under "Customers, products and operating practices":

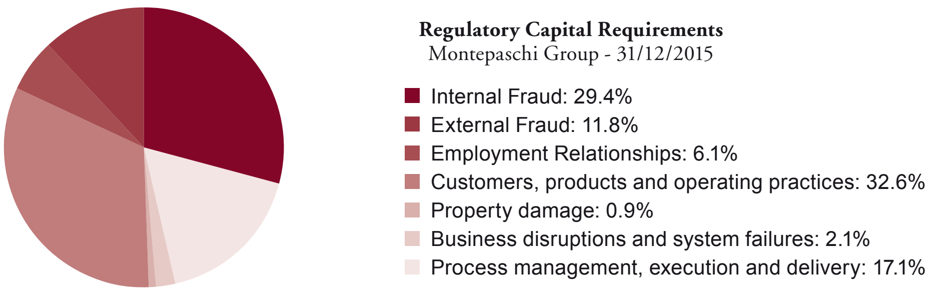
approximately 60% of total) and operational and process management shortfalls (under "Process management, execution and delivery", which accounts for 18% of total). With regard to "non-fulfilment of professional obligations with customers", risk events are mainly associated with claims (legal actions and complaints) due to the application of compound interest.

For further information, please refer to the **Notes to the Consoldiated Financial Statements** - *Part E – Information on risks and hedging policies – Section 4 – Operating Risks*.





The graph below shows the breakdown of regulatory requirements by class of risk:



The Regulatory Requirements as at 31 December 2015 were essentially stable compared to December 2014.

The breakdown of operational losses clearly differs from the breakdown of capital in that the latter is calculated using a 5-year time series and is mainly weighted by the unexpected loss component.

12.2 Operational Risk: use of advanced measurement methods

Tab. 12 – Capital requirements for Operational Risk

Requirements by Approach	dec-2015	dec-2014
Foundation Approach	18,507	20,212
Standardised Approach	-	-
Adavanced Measurement Approach	684,387	688,055
Total Operational Risk	**702,894**	**708,267**

Statement of the Chief Executive Officer pursuant to art. 435, e) and f) of Regulation (EU) no. 575/2013 of 26-06-2013

By mandate of the Board of Directors of Banca Monte dei Paschi di Siena S.p.A and pursuant to art. 435, e) and f) of Regulation (EU) no. 575/2013 of 26-06-2013, the Chief Executive Officer, Fabrizio Viola, declares that:

a) The risk management systems put in place by the Parent Company and described in the d document "Pillar 3 Disclosure: update as at 31 December 2015" are in line with the Banking institution's profile and strategy;

b) The section, "Executive Summary", of the same document provides a summary description of the Montepaschi Group's overall risk profile in relation to the company strategy adopted.

Siena, 25 February 2015

Fabrizio Viola

Chief Executive Officer

Declaration of the Financial Reporting Officer

Pursuant to para. 2, article 154-bis of the Consolidated Law on Banking, the Financial Reporting Officer, Mr. Arturo Betunio, declares that the accounting information contained in this document corresponds to the underlying documentary evidence and accounting records.

Siena, 25 February 2016

Arturo Betunio
Financial Reporting Officer

List of Tables

Glossary

ABS (Asset Backed Securities): Financial Securities whose coupon yield and redemption are guaranteed by a pool of assets (collateral) of the issuer (usually a Special Purpose Vehicle), exclusively intended to ensure satisfaction of the rights attached to said financial securities. Typically, thy are broken down into RMBS and CMBS.

AFS (Available For Sale): IAS category used to classify the assets available for sale.

AIRB (Advanced Internal Rating Based): advanced internal models used to calculate capital requirements for credit and counterparty risk within the Basel 2 and Basel 3international framework. They differ from the FIRB models since with the AIRB approach, the banks uses its own internal estimates for all inputs. See also PD, LGD, EAD.

ALM (Asset & Liability Management): the set of risk management models and techniques applied to the Banking Book for the purpose of measuring interest rate risk and liquidity risk.
See also Banking Book, Interest Rate Sensitivity, Shift Sensitivity, Economic Value Approach.

AMA (Advanced Measurement Appro-ach): advanced internal models used to calculate capital requirements for operational risk within the Basel 2 and Basel 3 international framework. The approach involves the measurement of capital requirements by the bank through calculation models based on operational loss data and other valuation elements the bank collects and processes.

AT1 (Additional Tier 1): Additional Tier 1 Capital consists of equity instruments other than ordinary shares (calculated in CET1) that meet the conditions for inclusion in Tier 1 capital net of deductions of class 1 items. The latter mainly relate to instruments held in financial entities with significant investments and not to cross-shareholdings.

Banking Book: in accordance with International best practices, the term “banking book” refers to all of the non-trading operations of the Bank in relation to the transformation of maturities with respect to balance-sheet assets and liabilities, Treasury, foreign branches and hedging derivatives. The interest rate, liquidity and forex risk of the Banking Book are typically measured trough Asset & Liability Management (ALM) models. See Regulatory Banking Book.

Basel 1: the regulations relating to the application of Minimum Capital Requirements issued by the Basel Committee in 1988.

Basel 2: the regulations relating to the application of the New Capital Accord issued by the Basel Committee in 2006.

Basel 3: a set of reforms that has been introduced by the Basel Committee as of 2010 to strengthen regulations concerning capital and liquidity and thereby increase the resilience of the banking sector. The reforms are aimed at increasing the banking system’s capacity to absorb shocks arising from financial and economic stress, whatever their origin, and reduce the risk of contagion from the financial sector to the real economy. Implemented within the Community by the “CRR”, Regulation (EU) No 575/2013 and “CRD IV”, Directive 2013/36/EU.

BCU: Business Control Unit. Local, first-level risk management functions, located within the areas / business units (BUs).

BP (basis point): one hundredth of a percentage point, ie. 1bp = 0.01% = 0.0001.

BU: Business Unit.

Capital Requirements: the sum of capital, calculated according to supervisory regulations, destined to cover the single risks of the First Pillar in compliance with the supervisory framework.

Overall Internal Capital: (or Overall Absorbed Capital) is the minimum amount of capital resources required to cover economic losses resulting from unforeseen events caused by the simultaneous exposure to different types of risk. In addition to Pillar 1 regulatory requirements for Credit and Counterparty Risk (which already include those relating to Issuer Risk in the Banking Book, Equity Investment Risk and Real Estate Risk) and for Operational Risk, internal operational models relating to Market Risk, Interest Rate Risk in the Banking Book, Concentration Risk and Strategic Risk are also added. Overall Internal Capital is calculated without considering inter-risk diversification and includes the input from each individual risk.

CCF: Credit Conversion Factor.

CDS (Credit Default Swap): An agreement whereby, upon payment of a premium, one party transfers to another party the credit risk attached

to a loan or security, in the event of a loan default by the debtor.
CDO (Collateralized Debt Obligation): Securities issued based on differentiated risk classes with various tranches following the securitisation of a portfolio of debt instruments embedding a credit risk. Typically characterised by financial leverage.

ABS CDO: CDOs whose underlying asset portfolio primarily consists of Asset-Backed Securities.

Corporate customers: customer segment consisting of medium- and large-sized companies (mid corporate, large corporate).

Retail customers: customer segment primarily consisting of consumers, professionals, shop-keepers and artisans.

CMBS: Commercial Mortgage Backed Securities.

Prudential Ratios: Regulatory ratios which relate different types of capital to risk-weighted assets (RWAs). *See also* CET1 capital ratio, Tier 1 Capital Ratio, Total Capital Ratio.

Common Equity Tier 1 (CET1) Capital Ratio: **t**he ratio between CET1 and total RWA.

Confidence level: level of probability linked to a risk measurements (e.g. VaR).

Counterparty Risk: Counterparty risk is the risk that the counterparty in a specific financial transaction is in default prior to settlement. Counterparty Risk is associated with certain, specifically-identified types of transactions, which: 1) generate an exposure that is equal to their positive fair value; 2) have a market value which evolves over time depending on underlying market variables; 3) generate an exchange of payments or an exchange of financial instruments or goods against payment. The categories of transactions subject to counterparty risk are:
credit and financial derivative instruments traded Over the Counter (OTC);
Securities Financing Transactions (SFT);
Long Settlement Transactions (LST).

Covered bond: Special bank bond that, in addition to the guarantee of the issuing bank, is also backed by a portfolio of mortgage loans or ther high-quality loans sold to a special purpose vehicle.

CRD IV (Capital Requirements Directive IV): Directive 2013/36/EU of the European Parliament and of the Council of the 26 June 2013, on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

CRR (Capital Requirements Regulation): Regulation (EU) No 575/2013 of the European Parliament and of the Council of the 26 June 2013, on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.

Credit derivatives: Derivative contracts for the transfer of credit risks. These products allow investors to perform arbitrage and/or hedging on the credit market, , to acquire credit exposures of varying maturities and intensities, to modify the risk profile of a portfolio and to separate credit risks from other market risks.

Credit Risk: the risk that a debtor may default on his obligations, either at maturity or subsequently. Credit Risk is associated with an unexpected change in creditworthiness of a responsable party – towards whom there is an exposure – which generates a corresponding unexpected change in the value of the credit position.

CRM (Credit Risk Mitigation): set of credit risk mitigation techniques recognised for supervisory purposes (e.g., compensation of accounts in balance sheet, personal guarantees, credit derivatives, financial collaterals), for which the following eligibility requirements apply - legal, economic and organisational - for the purpose of reducing risk.

Cure Rate: the rate with which impaired loan positions return to performing status.

Default, credit exposures: these include nonperforming loans, watchlist loans, restructured loans and past-due.

Default status: state of insolvency or delinquency of a debtor. Declared inability to honour one's debt and/or make the relevant interest payments.

Deferred Tax Assets (DTA): the amounts of income taxes payable in future periods in respect of taxable temporary differences between the carrying amount of an asset or liability and its tax base.

Deferred Tax Assets (DTA) that rely on future profitability: deferred tax assets, the future value of which may be realised in the event the institution generates taxable profit in the future. They are divided between DTAs arising from temporary differences and DTAs not arising from temporary differences (eg. Tax losses).

Delta EL: *see* Surplus of expected loss value over the value of net provisions.

DIPO: Database Italiano Perdite Operative. The Italian Database of Operational Losses. Database used for operational risk.

Diversification: benefit arising from the simultaneous holding of financial instruments which depend upon risk factors not perfectly matched. In the case of VaR, this corresponds to the correlation
effect among risk factors on the overall VaR value.

EAD: *see* Exposure-at-Default.

ECA: Export Credit Agency.

ECAI (External Credit Assessment Institution): External Credit Assessment Institution (Rating Agencies).

Economic Capital: the capital needed to deal with any loss in value generated by unexpected changes in conditions, internal or external, as a consequence of risk. It is calculated on the basis of risk measurement models developed by the Risk Management area. In general, it is obtained on the basis of a consistent transformation in terms of holding period and confidence interval of VaR measurements calculated for individual risk factors and appropriately diversified. The confidence interval is a function of the bank's objective rating. The Economic Capital is the internal estimation of capital needed to deal with risk that is the necessary operational equivalent of Capital Requirements (Regulatory Capital).

Economic Value approach: measure of the changes in the Banking Book overall net current value (defined as the difference between the current value of assets, the current value of liabilities and the value of hedging derivatives) in the presence of different alternative interest rate scenarios. The focus is placed on the changes in the net current economic value of the Bank and takes account of all maturities of assets, liabilities and off-balance-sheet items existing at the time of each valuation. It is typically measured with shift sensitivity assumptions. See also AL M, Banking Book, Interest Rate Sensitivity, Shift Sensitivity.

Expected Loss (EL): the total amount of net losses which, on average, the bank can expect (estimate) to incur in the 12 month period following the date of reference on the total amount of performing loans in the portfolio upon measurement. Estimated ex-ante as the "cost of doing business", it ought to be directly included, in terms of spread, in the pricing conditions applied to the customer and covered using an appropriate accounting provision policy.
It is defined as the product of the probability of default (PD) and loss given default (LGD):
EL = PD x LGD
The Expected Loss amount is defined as the product between EL and Exposure at Default (EAD):
EL amount = EL x EAD

Exposure at Default (EAD): estimated future value of an exposure upon default of a client. EAD, for the purposes of calculating capital requirements, includes both the cash exposure and the expected usage of the endorsment exposure.
Value required in the advanced model for credit risk measurement (AIRB - "Advanced Internal Rating Base Approach") as set out by Basel framework.

Fair Value (FV): the amount at which an asset could be bought or sold or a liability incurred or settled, in an arm's length transaction between willing, independent parties.

FIRB (Foundation Internal Rating Based): the internal models used to calculate capital requirements for credit and counterparty risk within the international Basel 2 Accord. It differs from the AIR B approaches because, in this case, only the PD parameters are estimated by the bank.

Grandfathering: Provision to safeguard capital adequacy, whereby an old rule continues to apply to some existing situations while a new rule will apply to all future situations.

HFT (Held For Trading): IAS category used to classify trading assets and liabilities.

Holding period (hp): forward-looking length of time for which a position is held.

IAS/IFRS: the International Accounting Standards are issued by the International Accounting Standards Board (IASB). The standards issued after July 2002 are called IFRS (International Financial Reporting Standards).

ICAAP (Internal Capital Adequacy Assessment Process): it is the "Second Pillar" of Basel framework. Banks are required to adopt processes and instruments for determining the level of internal capital needed to cover any type of risk, including risks different from those covered by the total capital requirement (“First Pillar”), when assessing current and future exposure, taking into account business strategies and developments in the economic and business environment.

ILAAP (Internal Liquidity Adequacy Assessment Process): is the internal process for assessing the overall liquidity profile of an institution. The equivalent ICAAP for liquidity risk within SREP.

IMA (Internal Models Approach): method of VaR internal models for the calculation of capital requirements for market risk.

Impairment: when referred to a financial asset, a situation of impairment is identified when the book value of an asset exceeds its estimated recoverable amount.

Risk Adjusted Indicators: see Risk Adjusted Performance Measurement.

Interest Rate Sensitivity (Economic Value approach): measurement of the impact an unexpected shift (parallel or not) in the yield curves by maturity generates on the bank’s economic value. It is typically used to measure the interest rate risk of the Banking Book within the Asset & Liability Management (ALM) systems. The value is obtained from calculating the variation in the current value of the real and notional cash flows of sheet assets, liabilities and off-balance items existing at a certain date when there is a variation in the yield curve (eg. +25 bp) with respect to the values of the baseline.

Investment grade: issuers or issues with a rating between AAA and BBB-.

Issuer Risk: connected to the issuer’s official rating, this is the risk of decreasing portfolio value due to the unfavourable change in the issuer’s credit standing up to the extreme case of default, in the buying and selling of plain vanilla or credit structured bonds, ie. purchase/selling of protection through credit derivatives.

Junior tranche: in a securitisation transaction it is the lowest-ranking tranche of the securities issued (Equity tranche), being the fi rst to bear losses that may occur in the course of the recovery of the underlying assets.

LCR (Liquidity Coverage Ratio): Liquidity regulatory ratio. It aims to strengthen the short-term resilience of the liquidity profile of the bank. The calculation of the LCR is being defined by the EBA.

LDA (Loss Distribution Approach): model used to assess exposure to operational risk. It makes it possible to estimate the amount of expected and unexpected loss for any event/loss combination and any business line.

Leverage Ratio: indicator given by the ratio between Tier 1 and total assets introduced by Basel regulations with the objective to limit the growth of leverage in the banking sector and strengthen the risk-based requirements using a different measure based on balance sheet aggregates.

LGD (Loss-Given-Default): Tasso di perdita in caso di insolvenza (default) determinato come il rapporto tra la perdita subita su un’esposizione a causa del default di una controparte e l’importo residuo al momento del default. LGD is estimated in the form of a coefficient ranging from 0 to 1 (or in percentages) based on the following drivers: type of borrower, type of guarantee pledged, technical form of lending. This value is required within the framework of the Advanced Internal Ratings-Based Approach (AIRB) for credit risk under Basel framework. When conditioned on adverse macro-economic scenarios (or downturns), the LGD parameter is defined as “downturn LGD”.

Liquidity Risk: the risk that a company will be unable to meet its payment obligations due to its inability to liquidate assets or obtain adequate funding from the market (funding liquidity risk) or due to the difficulty/impossibility of rapidly converting financial assets into cash without negatively and significantly affecting their price due to inadequate market depth or temporary market disruptions (market liquidity risk).

L&R (Loans & Receivables): IAS category used to classify credit.

LST (Long Settlement Transactions): long settlement transactions (in which a counterparty commits to delivering (receiving) a security, commodity or foreign currency against receipt (delivery) of cash payment, other financial instruments or goods with settlement upon a pre-established contractual date, later than the one determined by market practice for these types of transaction, namely five days from the transaction stipulation date.

M (Maturity): the residual life of an exposure, calculated according to prudential requirements for credit risk. For banks authorised to use internal ratings, it is explicitly considered if the advanced approach is adopted, while it is predetermined by legislation if the FIR B approach is adopted.

Margin Sensitivity: measurement of the impact which an unexpected shift (parallel or not) in the yield curve by maturity generates on the Bank's estimated one year net interest income. It is typically used to measure interest rate risk in the banking book within Asset & Liability Management (ALM) systems along with Interest Rate Sensitivity.

Mark-to-market: valuation of a position at market value, usually from the trading book. For instruments officially traded on organised markets, it corresponds daily to the market closure price. For unlisted instruments, it results from the development and the application of specifically- developed pricing functions which determine the valuation starting from the market parameters relating to the respective risk factors. It is at the basis of the calculation of P&L in the trading book.

Mark-to-model: Valuation of financial instruments on the basis of internal valuation models since publicly observable market prices or comparable approaches are not available.

Market Risk: the risk of value loss on a financial instrument or a portfolio of financial instruments, resulting from an unfavourable and unexpected change in market risk factors (interest rates, share prices, exchange rates, price of goods, indices,…). A typical risk of the trading book.

Market Value Method (former Current Value method): supervisory method used to determine counterparty risk in derivatives and the capital requirement to cover it. The current value is calculated adding the replacement cost (or intrinsic value, determined on the basis of the "mark-to-market" value of the derivative, if positive) to the future credit exposure (approximating the time value of then derivative, i.e. the probability that, in the future, the intrinsic value will increase, if positive, or convert into a credit exposure if negative); the future credit exposure is determined for all contracts, independently of the positive value of the replacement cost, multiplying the nominal value of each derivative contract by coefficients differentiated by residual maturity and type of contract.

Mezzanine tranche: in a securitisation transaction, it is the tranche ranking between junior and senior tranche. As a rule, the mezzanine tranche is broken down into 2 or more tranches with different levels of risk, subordinated one to the other. They are typically characterised by an investment grade rating.

NFIs: New Financial Instruments, issued pursuant to art. 23-sexies of Legislative Decree no. 95 of 6 July 2012, containing "Urgent measures for reviewing public spending with unchanged services for citizens and measures to strengthen the capital of undertakings in the banking sector" converted, as amended, by law no. 135 of 7 August 2012, n.135 as subsequently amended.

NSFR (Net Stable Funding Ratio): Liquidity regulatory ratio. It is defined as the ratio between the available amount of stable funding and the required amount of stable funding. The time horizon considered for evaluating stable funding is one year. The calculation of the NSFR is being defined by the EBA.

Non performing: term generally referring to loans for which payments are overdue.

Operational Risk: the risk of incurring losses due to inadequacy or failure of processes, human resources or internal systems, or as a result of external events, including legal risk. These include, among other , loss deriving from fraud, human error, business disruption, system failure, breach of contract, natural disasters. Operational Risk includes legal risk while it does not include strategic or reputational risk (included in Pillar II of Basel).

Overall Capital Requirement (or Regulatory Capital): the sum of the capital requirements for the individual risk types (Credit, Counterparty, Market and Operational).

OTC: *see* OTC derivatives.

OTC Derivatives (Over the Counter): financial and credit derivatives traded over the counter (e.g.: swaps, forward rate agreements).

Own Funds: sum of Tier 1 (T1) and Tier 2 (T2) Capital.

Past due: *see* Default.

PD: *see* Probability of Default.

Performing: term generally referring to loans characterised by regular performance.

Regulatory Banking Book: comprises all positions that are not assigned to the Regulatory Trading Book; its definition is therefore 'residual' in nature, even though most of a retail bank's exposures are assigned to this portfolio; in general, the rules for determining the capital requirements for Credit Risk are applied to the Regulatory Banking Book. See also Banking Book.

Regulatory Trading Book: positions intentionally held for trading purposes and destined to be disposed of in the short term and/or assumed with the aim of benefitting, in the short term, from the differences between purchase and sale price, or other price or interest rate variations. It consists in a set of positions in financial instruments and commodities held for trading or to cover risk inherent in other constituent of the same portfolio. For eligibility to be included under the trading book prudential treatment, the financial instruments must be exempt from any clause which would limit their trade ability or, in alternative, fully covered. Furthermore, the positions must be frequently and accurately assessed. The trading book must be actively managed.

Private equity: activity aimed at the acquisition of equity investments and their subsequent sale to specific counterparties, without public offerings.

Preference shares: are innovative capital instruments that enjoy preferential rights in relation both to dividends (which may be cumulative or non-cumulative) and rights clearance and whose administrative rights are, as a rule, limited or subject to certain conditions of use.

Probability of Default (PD): the probability that a customer/counterparty will default within the space of 1 year. Each PD derives from an internal ratings system and thus falls within a specific range of values corresponding to those used by the official rating agencies (masterscale) so as to obtain standardised data processing between internal and external rating systems.

Profit & Loss (P&L): operational profit or loss indicator of the Trading book which expresses the difference in value of an instrument or a portfolio in a given timeframe, calculated on the basis of market values and directly validated/listed ("mark-to-market") or determined on the basis of internally-adopted pricing models ("mark-to-model").

RAPM: cfr. Risk Adjusted Performance Measurement.

Rating: the degree of risk of non-compliance regarding a specific debtor (counterparty or issuer rating) or a single loan (issuance rating). It is typically expressed through a qualitative assessment belonging to a calibration scale. If determined by a rating agency it becomes an "official" rating. If it is based upon internally-developed models it is called an "internal" rating. It expresses the likelihood of default or insolvency.

Risk: can be defined as an unexpected potential economic loss. Risk is an economic loss in the sense that, against the commercial initiatives undertaken, if risk emerges it always results in a loss of value in the books of the Bank. Risk is an unexpected loss and implies the need to set aside a corresponding sum of capital in order to guarantee the bank's stability and solvency over a long period. Risk is a potential loss in the sense that there may or may not be a certain confidence level (probability) in the future (forward looking) estimate and it is therefore an estimate, not a known value. Since risk is potential, it is always prospective or forward-looking. It is not the measurement of an economic effect that has already materialised.

Risk Adjusted Performance Measurement (RAPM): measurement of performance adjusted by risk. Method of measurement of profitability, which is defined as "risk adjusted" in that – on the one hand - it includes a new P&L negative component under Profit for the Year, that rises as the expected risk component increases (Expected Loss), and - on the other - replaces the "book value" capital used in the transaction with the Economic Capital.

Risk factor: the driver/variable which determines the variation in value of a financial instrument.

RMBS (Residential Mortgage Backed Securities): ABS backed by mortgages.

RWA (Risk Weighted Assets): it results from the application of certain risk weights to exposures as determined by supervisory regulations.

Securitisation Cap Test: the test undergone by all securitisation transactions recognised for prudential purposes, according to which the risk-RWAs of securitisation positions are compared with those of securitized exposures (calculated as though the latter were not securitised). If the RWAs of the former are greater than those of the latter (cap) then the latter are taken into consideration.

Scoring: a company's customer analysis system which consists in an indicator resulting from both an analysis of book data and an assessment of the performance forecast for the sector, on the basis of statistic-based methodologies.

Senior/Super Senior tranche: it represents the tranche with the highest credit enhancement, or rather the highest level of privilege in terms of priority of remuneration and reimbursement. It has a high rating and is higher than the mezzanine tranche.

Seniority: Level of subordination regarding the repayment of notes, generally broken down (in decreasing order) into SuperSenior, Senior, Mezzanine, Junior.

Servicer: in securitisation transactions it is the subject that - on the basis of a specific servicing contract - continues to manage the securitized loans or assets after they have been transferred to the special purpose vehicle responsible for issuing the securities.

Settlement Risk: the risk that arises in transactions on securities when, after expiry of a contract, the counterparty is in default with regard to delivery of securities or payment of amounts due.

SFT (Security Financing Transactions): repos and reverse repos on securities or commodities, securities or commodities lending or borrowing transactions and margin lending transactions.

Shift Sensitivity: measurement of the impact of an unexpected and parallel shift in the yield curve upon the bank's economic value. See ALM, Banking Book, Interest Rate Sensitivity, Economic Value Approach.

SMEs: Small and Medium Enterprises.

Speculative grade: issuers or issues with a rating below BBB-.

SPE/SPV (Special Purpose Entities o Special Purpose Vehicles): established in pursuit of specific objectives, mainly to isolate financial risk. The assets consist in a portfolio, the proceeds of which are used for the servicing of bond loans issued. Typically used in asset securitisation transactions.

SREP (Supervisory Review and Evaluation Process): a supervisory review and evaluation process put in place by the Regulatory Authority. It is composed of three main elements:

- a Risk Assessment System (RAS), which assesses the level of risk and control activities of credit institutions;
- a comprehensive review of the ICAAP and ILAAP processes;
- a methodology for quantifying capital and liquidity on the basis of risk assessment results.

Stress test: a set of quantitative and qualitative techniques used by banks to assess their vulnerability to exceptional, though plausible, events.

Surplus Expected Losses on Net Provisions ("Delta PA"): the difference between expected losses and overall net value adjustments, limited to the exposures subject to internal models for credit risk; it is a component of the Own Funds.

Consolidated Banking Act (CBA): Legislative Decree no. 385 of 1 September 1993 and subsequent amendments and additions.

T1 (Tier 1): Tier 1 capital. It is the sum of CET1 and AT1.

T2 (Tier 2): Tier 2 capital. It is mainly composed of computable subordinated liabilities computable and any excess value adjustments with respect to expected losses for exposures weighted according to the AIRB approach.

Tier 1 Capital Ratio: ratio between T1 and total RWAs.

Tier Total (see Own Funds, former Regulatory Capital): sum of Tier 1 (T1) and Tier 2 (T2) capital.

Total Capital Ratio: ratio between Tier Total (Own Funds) and total RWAs.

TTC (Through-the-cycle): a rating system which uses a long-term time series and better reflects the risks relating to a borrower's specific situation. The impact of macroeconomic trends on this kind of model are limited. A "Point-in-time" rating system uses a short-term or one year time series and not only reflects information regarding the individual borrower. It produces ratings that change on the basis of systemic factors. Most internal rating models estimated by banks do not perfectly correspond to one rating system or the other but fall somewhere between the two models. They are defined as "Hybrid".

UCITS: Undertakings for Collective Investments in Transferable Securities.

Value-at-Risk (VaR): probability measure of a portfolio's market risk. It is defined as the maximum potential loss in value of an asset or portfolio over a defined period *(holding period)* for a given *confidence interval* (with the *confidence level* expressing probability). As an example, with regard to the trading book, the VaR model estimates the maximum decrease (loss) that a portfolio is expected to incur with a specified probability (for ex. 99%), over a defined time horizon (for ex. 1 day). In this example, a 1 day VaR with a 99% confidence implies that there is only a 1% chance of the Bank losing more than the VaR amount in one single working day.

Volatility: measure of the exposure to fluctuations of a risk factor (e.g. rates, prices,

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