
BANCA

S I S T E M A
SPECIALTY FINANCE

MARKET UPDATE

29 & 30 November 2017

Agenda

I. Late Payment Interests

II. Asset Quality

Annexes

I. Late Payment Interests

EU Directive 7/2011

[...] “To protect European businesses, in particular SMEs, against late payment and to improve their competitiveness, Directive 2011/7/EU on combating late payment in commercial transactions was adopted on 16 February 2011 and was due to be integrated into national law by EU countries by 16 March 2013 at the latest. This Directive puts in place strict measures which, when properly implemented by EU countries, will contribute significantly to employment, growth and an improvement in the liquidity of businesses”.

Main provisions of the Directive

- Public authorities **have to pay for the goods and services that they procure within 30 days or, in very exceptional circumstances, within 60 days**
- Automatic entitlement to interest for late payment and €40 minimum as compensation for recovery costs
- **Statutory interest of at least 8% above the European Central Bank’s reference rate (“LPI”)**
- EU countries may continue maintaining or bringing into force laws and regulations which are more favorable to the creditor than the provisions of the Directive



On 26 August 2016, EU Commission adopted a [Report](#) on the implementation of the Directive. The results of the study, as well as further research, fed into this Report, that has been submitted to the European Parliament and to the Council. **The Report assesses the effectiveness, efficiency, coherence, relevance and EU added value of the Directive.**

Accounting framework (GAAP)

- **IAS 39:** Interest income accrued at amortised cost, utilising IRR over an estimated collection period
- **IAS 8:** Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors. An estimate may need revision if changes occur in the circumstances on which the estimate was based or as a result of new information or more experience



Expected cash flows from LPI have to be included in amortised cost to the extent of information available at each reporting date to assess recoverable amount and collection date

Regulatory framework

Document of Bank of Italy/ Consob/ Ivass n. 7 of November 9, 2016 on the accounting treatment of Late Payment Interests pursuant to Legislative Decree 231/2002:

- **LPI are due by law:**
 - without any legal action to be initiated;
 - from the day following the terms of contractual payment.
- **For the purpose of verifying the existence of the ability to reliably estimate LPI on P&L, are necessary:**
 1. the availability of a business model and an organizational structure, dedicated to LPI collection;
 2. the existence of statistically "robust" sample, such as to allow a sufficiently reliable estimate of both % of Collection and time of the Collection.

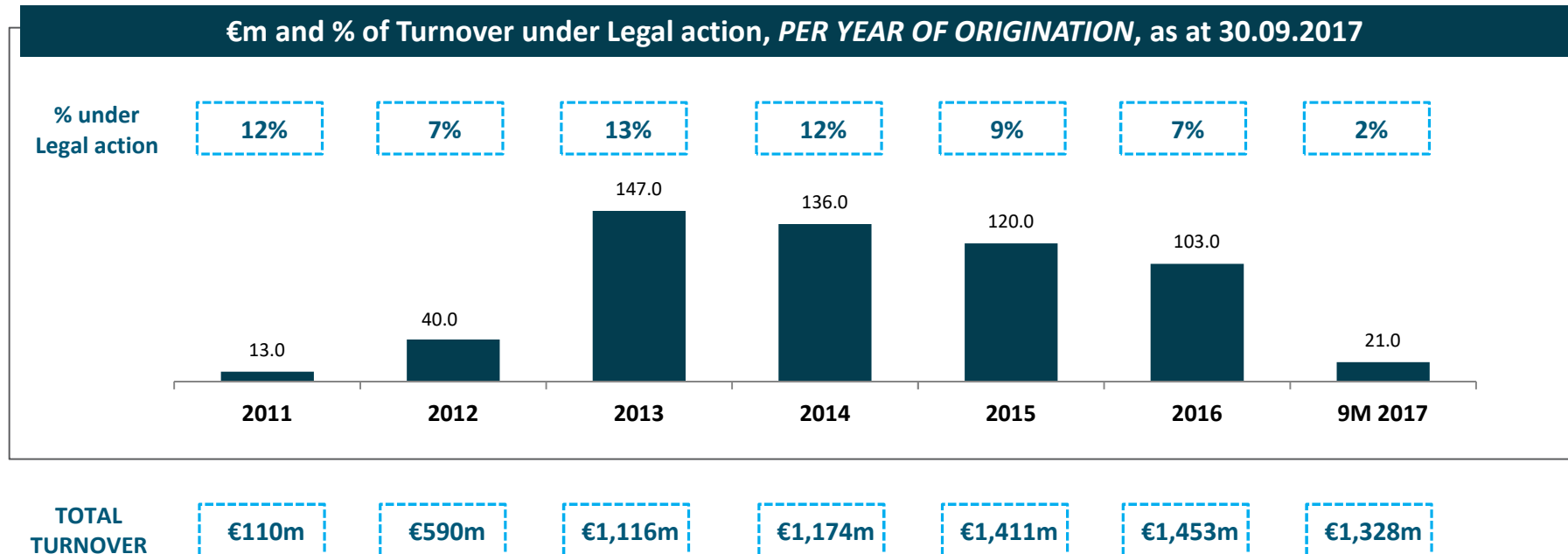


Accrual of LPI goes to P&L

Outstanding under Legal action

Following the evolution of the business in the few years since the inception of Banca Sistema, factoring Outstanding under Legal Action has increased in 2016 reaching at the end of Q3 2017 €348m (€214m as at 30.09.2016), equals to c. 28% of overall factoring Outstanding

Banca Sistema has not changed its commercial model and strategy during the last few years (“start Legal action when needed”), as you can see from the chart below, that show the % of the factoring Turnover of each period, as at 30.09.2017, that was under Legal Action...



...Banca Sistema estimates, in the following months, an increase of the 2015, 2016 and 9M 2017 Turnover's percentage under Legal action

LPI recovery

LPI collection on closed legal actions as at 31.08.2017

| | # Injunction | Average Recovery |
|-----------------------|--------------|------------------|
| <i>Healthcare</i> | 1,968 | 86.4% |
| <i>Non-Healthcare</i> | 202 | 83.3% |
| Total | 2,170 | 86.1% |

Each Injunction includes often more than one invoice

Despite Banca Sistema historical lower exposure to Healthcare segment, # Injunction of Healthcare include Beta Stepstones database

Note: LPI referred in the document are those related to Legal actions.

BST LPI Accrual Model (1/2)

As recently updated, the policy of the accrual is based on the following main features:

| | No legal action | | | | Legal action | | | |
|------------------------------|-----------------|-----------|-----|-----------|--------------|-----------|-----|-----------|
| | Performing | Past dues | UTP | Bad loans | Performing | Past dues | UTP | Bad loans |
| State Central Administration | NO | NO | NO | NO | YES | YES | NO | NO |
| ASL <i>Healthcare</i> | NO | NO | NO | NO | YES | YES | NO | NO |
| Public Sector Organizations | NO | NO | NO | NO | YES | YES | NO | NO |
| Local Entities | NO | NO | NO | NO | YES | YES | NO | NO |
| Corporate | NO | NO | NO | NO | NO | NO | NO | NO |

Including public consortium even though controlled by PAs

1. LPI recovery evidence: First level of breakdown by Healthcare and Non-Healthcare and second level of breakdown by geographic area (“PSI statistical approach”)
2. % of accrual based on the application of a high probability statistical concept, selecting a percentile of the recovery output
3. Internal collection policy addressing minimum level of LPI acceptance in case of out of court agreements
4. Quarterly back testing of the LPI recovery

BST LPI Accrual Model (2/2)

Positions under Legal action
As at 30.09.2017

| | # Injunction | €/m |
|----------------|-----------------|------------|
| Healthcare | 1,127 | 56 |
| Non-Healthcare | 2,294 | 292 |
| Total | 3,421 | 348 |



Perimeter relevant for the accrual

| | # Injunction | €/m |
|----------------|-----------------|------------|
| Healthcare | 1,114 | 50 |
| Non-Healthcare | 2,146 | 234 |
| Total | 3,260 | 284 |



| % Accrual |
|------------|
| 61% |
| 31% |
| 38% |

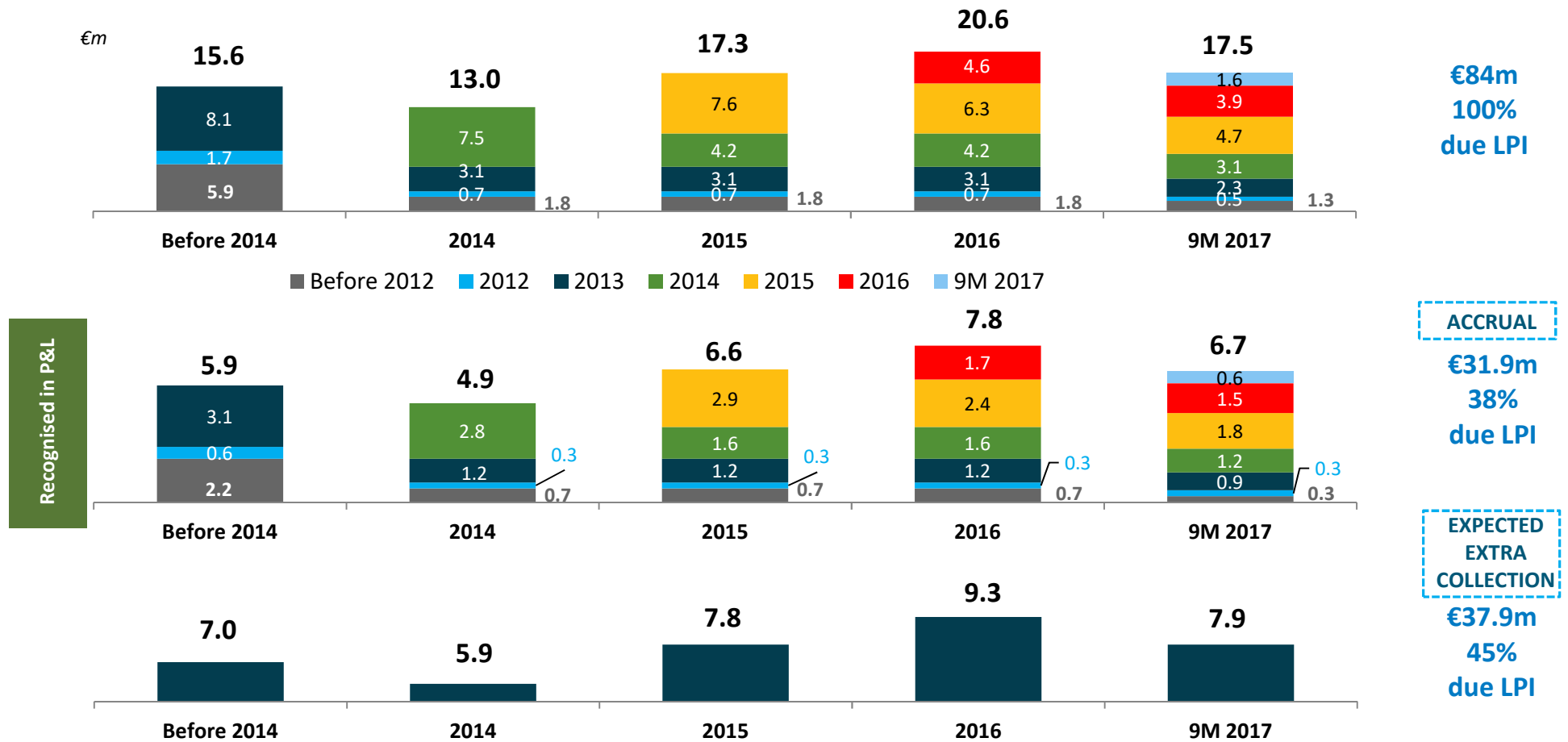
Note: LPI referred in the document are those related to Legal actions.

Due LPI as at 30.09.2017

As at 30.09.2017, Outstanding under Legal action, relevant for our Policy on LPI, reached €284m (out of €348m on Total) corresponding to total due LPI of €84m (based on EU Directive):

- on which we have taken on P&L an accrual of 38% on average;
- and on which we expect a collection rate of 83% (+45% extra collection vs accrual).

Distribution of LPI, PER YEAR OF TURNOVER ORIGINATION, as at 30.09.2017

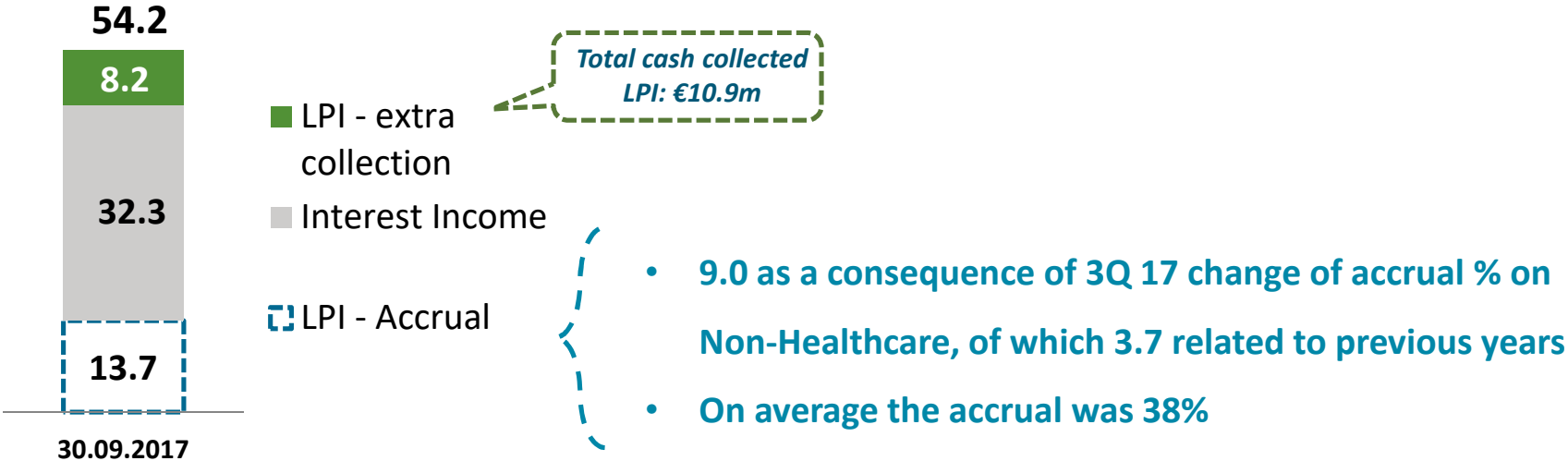


Note: LPI referred in the document are those related to Legal actions.

Factoring – 9M 2017 Interest Income

Factoring Interest Income (representing 82% of Group Interest Income)




€m



Note: LPI referred in the document are those related to Legal actions.

LPI evolution (1/3)

LPI stock as at 30.09.2017 might change for the following reasons:

1. *Cash collection of LPI*  *extra collection on P&L*
2. *Time effect on the LPI stock when the perimeter under Legal action does not change* 
3. *Increase of the perimeter under Legal action*  *new accrual*
4. *Deterioration/Improvement of the obligor classification (for example when a Municipalities is in “Distressed” and the exposure is classified as bad loans, in this case, based on our Policy we cannot rely on due LPI, even though the legal action will follow its course)*

On P&L:
 $Accrual \% * (8\% + ECB\ rate) * Time * OS$

Following slides are illustrative examples and do not represent estimates, but show the potential change of the LPI stock:

a) in case of an increase of Outstanding under Legal action, as a consequence new procedures and no collection of LPI on the Outstanding under legal action at 30.09.2017

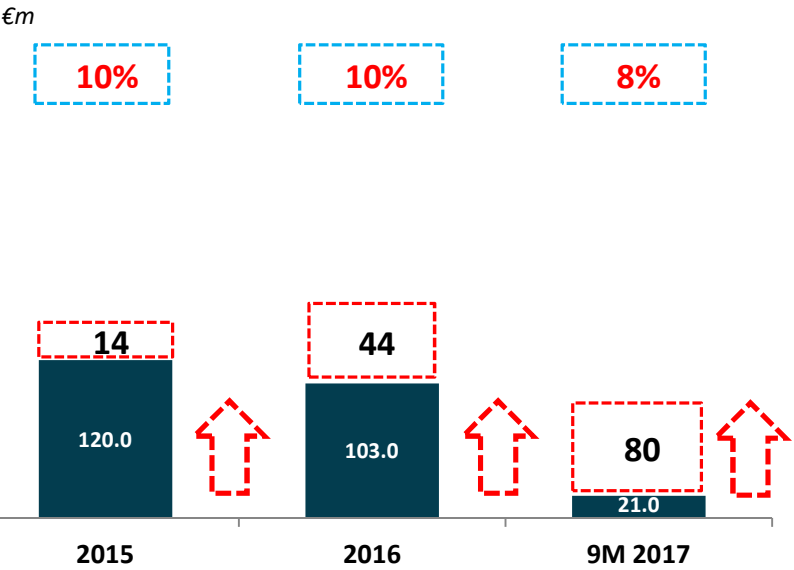
(Increase of 1 Year time of the LPI stock)

a) sensitivity on the LPI accrual % of the model (50% vs 38%)

LPI evolution (2/3)

A higher % of the 2015, 2016 and 9M 2017 Turnover to be classified as “Under Legal action” respectively to **10% (+1%)**, **10% (+3%)** and **8% (+6%)**

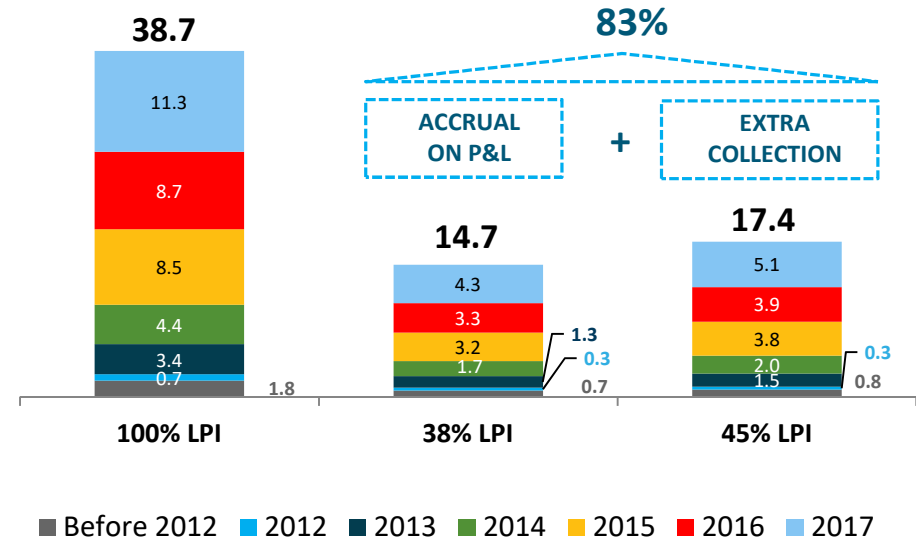
€m and % of Turnover under Legal Collection, PER YEAR OF ORIGINATION



TURNOVER **€1,411m** **€1,453m** **€1,328m**

Turnover/Outstading under legal action

LPI stock change, OF ONE YEAR, as a consequence of the time effect of the Outstanding under Legal action as at 30.09.2017 and a further increase of **€138m**

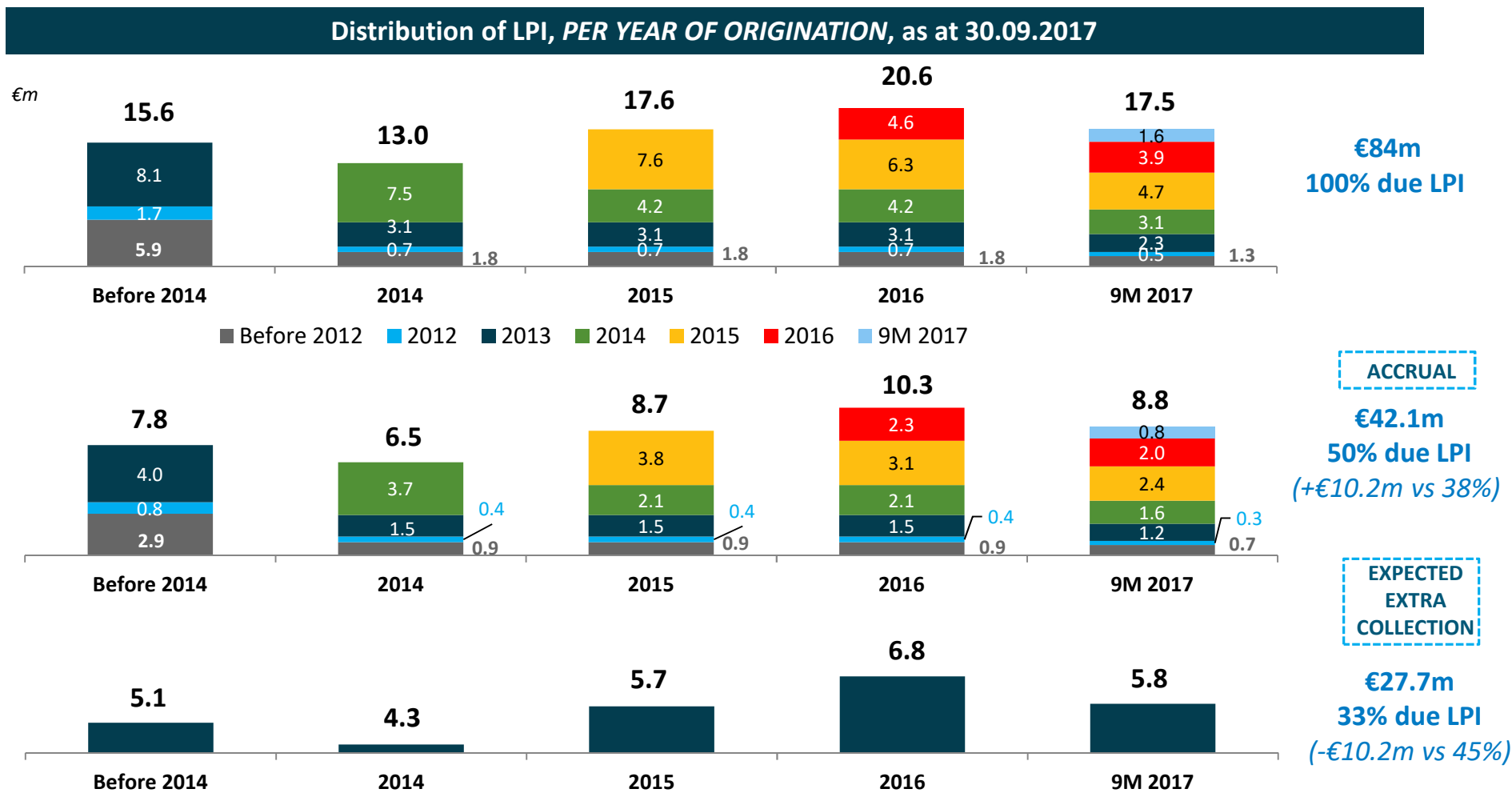


Note: LPI referred in the document are those related to Legal actions.

LPI evolution (3/3)

ILLUSTRATIVE
EXAMPLE

Sensitivity of a higher accrual for the model on LPI stock as at 30.09.2017



Note: LPI referred in the document are those related to Legal actions.

II. Asset Quality

Asset Quality – Factoring – as is vs to be (YE'20) (1/2)

As is – different regulatory rules due to different implied risk counterparties
Combined art. 178 E.U. C.R.R. No 575/2013 and Bankit circular letter No 272/2008

Bank of Italy's Circular 272/2008 considers specificities of Factoring products and Public Administrations exposures

| Non performing loans | | | |
|-----------------------|---------------------------|--|---|
| Regulatory segment | Bad Loans | UTP | Past dues |
| Public Administration | Distressed Local Entities | One by one evaluation | <p>Non recourse : No payment received during last 90 days, treshold of 5% exposures over 90 days, excluding disputes & law constrains</p> |
| Corporate | One by one evaluation | <ul style="list-style-type: none"> • «Concordati»; • One by one evaluation | <ul style="list-style-type: none"> • Non recourse: treshold of 5% exposures over 90 days excluding disputes & law constrains; a) Recourse: Funded exposure > nominal global exposure; b) at least an invoice > 90 days and non performing exposure > 5% of outstanding credit |

Asset Quality – Factoring – as is vs to be (YE'20) (2/2)

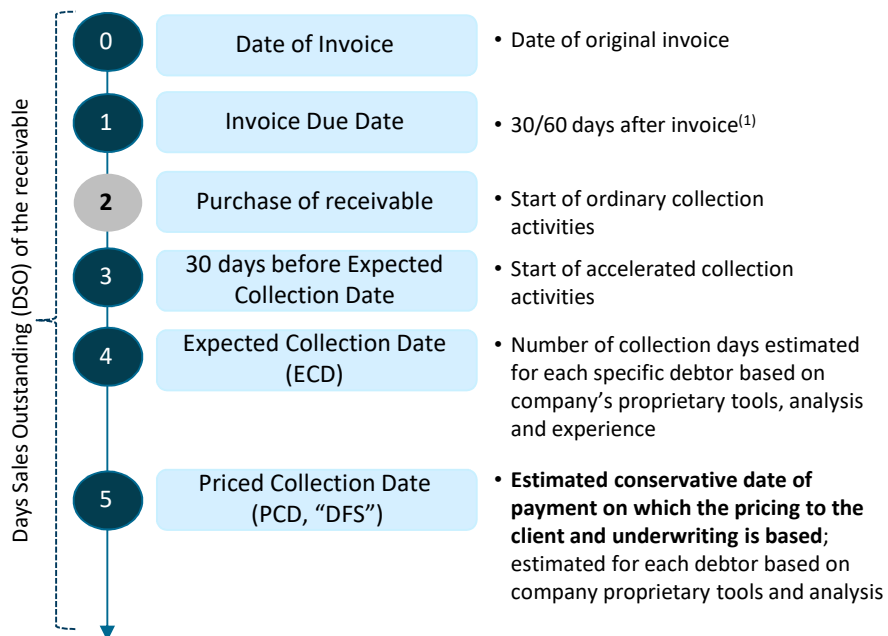
2021' EBA new rules on default (Past dues) – No relevant Impacts estimated

| Today | YE' 20 | Regulatory segment impacted | Impact |
|--|---|---|-------------------|
| 1. No default if incomplete procedures or credit freeze laws | 1. No default if incomplete procedures or credit freeze laws | All segments (Public Administration & Corporate) | NO |
| 2. Recognition of disclosed agreements | 2. Recognition of undisclosed agreements | | |
| 3. Threshold at 5%; | 3. Threshold at 500€ (absolute) and 1-2,5% (relative) | | |
| 4. Temporary waiver | 4. No waiver | Public Administration | YES (Negative) |
| 5. Recourse – Past due if: a) Funded exposure > nominal global exposure; b) at least an invoice > 90 days and non performing exposure > 5% of outstanding credit | 5. Recourse – The counting of days past due should start when the factoring account has a debit balance | Corporate | YES (Positive) |

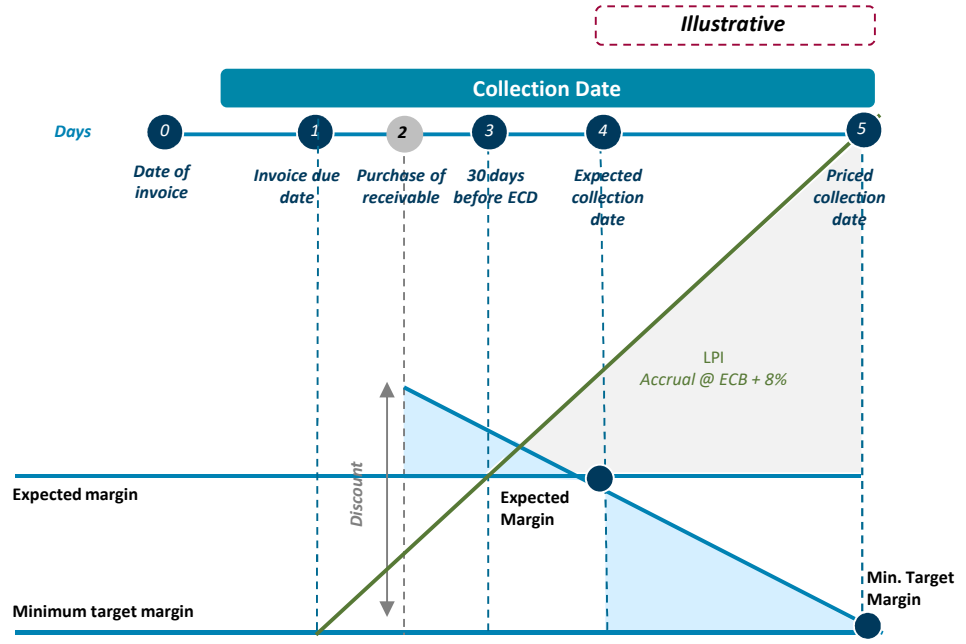
Annexes

Pricing and P&L

Receivables Factoring - Key Dates



Collection Dates and Contribution Margin Overview



Interest Margin – Illustrative

| | Priced collection date | Discount to face value | Min. target gross yield |
|------------------------------------|------------------------|----------------------------------|-------------------------|
| Client effective cost | 11 months | 5% | 5.8% |
| | Payment Date (ECD) | Months of anticipated collection | Actual gross yield |
| Banca Sistema gross interest yield | 7 months | 4 months | 9.0% |

Late Payment Interests:

- Try to collect without starting a legal action till 30 days before ECD
- From the start of the legal action we rely on due LPI at: 8% + ECB rate

Note: 1. 60 days for healthcare related receivables.

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