BANCO BPM

GROUP

Consolidated 2021 Annual Report

Consolidated 2021
Annual Report

This document is a courtesy translation into English, for the convenience of international readers, of the non-official consolidated financial statements of Banco BPM Group in PDF format; this PDF document, prepared in Italian language, is a courtesy copy which is not compliant with the provisions of the Commission Delegated Regulation (EU) 2019/815 (European Single Electronic Format – ESEF) but consistent with the official annual consolidated financial Statements prepared in compliance with the Directive 2004/109/EC (so-called Transparency Directive) in Italian language and published in the new format (ESEF) within the legal deadlines.

In case of any discrepancies or doubts between the English and the Italian versions of the Report, the Italian version prevails.

Banco BPM S.p.A.

Registered office: Piazza F. Meda, 4 - 20121 Milan, Italy
Administrative headquarters: Piazza Nogara, 2 - 37121 Verona, Italy
Fully paid up share capital as at 31 December 2021: Euro 7,100,000,000.00
Tax Code and Milan Companies' Register Enrolment No.: 09722490969
A company representing Banco BPM VAT Group, VAT no. 10537050964
Member of the Interbank Deposit Guarantee Fund and the National Guarantee Fund
Parent Company of Banco BPM Banking Group
Enrolled in the Bank of Italy Register of Banks and the Register of Banking Groups

OFFICERS, DIRECTORS AND INDEPENDENT AUDITORS AS AT 31 DECEMBER 2021

Board of Directors

Chairman	Massimo Tononi
Deputy Chairman	Mauro Paoloni
Chief Executive Officer	Giuseppe Castagna
Directors	Mario Anolli
	Maurizio Comoli
	Nadine Farida Faruque
	Carlo Frascarolo
	Alberto Manenti
	Marina Mantelli
	Giulio Pedrollo
	Eugenio Rossetti
	Manuela Soffientini
	Luigia Tauro
	Costanza Torricelli
	Giovanna Zanotti

Board of Statutory Auditors

Chairman	Marcello Priori
Standing Auditors	Maurizio Lauri
	Silvia Muzi
	Alfonso Sonato
	Nadia Valenti
Alternate Auditors	Francesca Culasso
	Gabriele Camillo Erba
	Wilmo Carlo Ferrari

General Management

Joint General Manager	Domenico De Angelis
Joint General Manager	Salvatore Poloni

Manager responsible for preparing the Company's financial reports

Gianpietro Val

Independent Auditors

PricewaterhouseCoopers S.p.A.

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NOTICE OF CALL OF ORDINARY AND EXTRAORDINARY SHAREHOLDERS' MEETING

Pursuant to Articles 12 and 13 of the Articles of Association, the ordinary and extraordinary Shareholders' Meeting of Banco BPM S.p.A. is hereby convened on single call on **Thursday, 7 April 2022, at 10:30 am, in Novara, at Banco BPM, Via Negroni no. 12,** to discuss and resolve on the following

AGENDA

Ordinary meeting

1) Approval of the financial statements as at 31 December 2021 of Banco BPM S.p.A. as well as of the companies incorporated in parent company Bipielle Real Estate S.p.A. and Release S.p.A., accompanied by the reports of the Board of Directors, the Board of Statutory Auditors and the Independent Auditors. Presentation of the consolidated financial statements of the Banco BPM Group.
2) Resolutions on the allocation and distribution of profits.
3) Supplementation, upon the motivated proposal of the Board of Statutory Auditors, of the compensation due to auditing company PricewaterhouseCoopers S.p.A., which has been entrusted with performing the statutory audit of the accounts for the 2017-2025 period. Pertinent and consequent resolutions.
4) Report on the remuneration policy and on compensation paid of the Banco BPM Group 2022 (section I and section II).

   4.1 Approval of the remuneration policy (section I) pursuant to the legislative provisions in force. Pertinent and consequent resolutions.

   4.2 Approval of the report on compensation paid in 2021 (section II) pursuant to legislative provisions in force. Pertinent and consequent resolutions.
5) Approval, within the remuneration policy, of the criteria for calculating any amounts to be granted in the event of early termination of employment or early departure from office of all personnel, including the limits set on said amounts. Pertinent and consequent resolutions.
6) Compensation Plans based on shares of Banco BPM S.p.A.:
   6.1 Approval of the *short-term incentive plan* (2022). Pertinent and consequent resolutions.
   6.2 Approval of the *long-term incentive plan* (2022-2024) and the raising of the levels of achievement of the performance objectives of the *long-term incentive plan* (2021-2023), in line with the most challenging 2023 objectives of the Strategic Plan. Pertinent and consequent resolutions.
7) Request for authorisation to purchase and dispose of own shares for the Banco BPM S.p.A. stock award plans. Relevant and consequent resolutions.

Extraordinary meeting

1) Proposal to amend Articles 12.1., 12.2., 20.1.2., 20.1.4., 20.1.6., 20.1.7., 20.3.1., 20.3.5., 20.4.2., 20.5.2., 20.6.1., 20.11.2., 23.5.1., 24.1., 24.2.2., 24.4.1, 33.1., 33.2., 33.3., 33.4., 33.5., 34.2., 34.3., 34.8., 35.2.,

35.3., 35.4., 35.8., 35.9., 35.10., 35.11., 35.12., 35.13., 36.7., 36.9., and 41.1. of the Articles of Association of Banco BPM S.p.A.

Please note that - considering the Covid-19 (coronavirus) epidemiological emergency - pursuant to what is set forth in article 106 " Rules concerning the shareholders' meetings of companies and entities" of Decree Law no. 18 of 17 March 2020 (so called "Cura Italia"), converted into Law no. 27 of 24 April 2020 and lastly amended by Law no. 15 of 25 February 2022 which converted **Decree Law no. 228 of 30 December 2021** into law, participation in the Shareholders' Meeting and the voting right shall be exercised by those entitled exclusively through the proxy designated pursuant to article 135-undecies of Italian Legislative Decree no. 58 of 24 February 1998 as subsequently amended ("TUF") according to what is specified below, therefore without the physical participation in the meeting of any other party entitled to vote.
Directors, statutory auditors, the meeting secretary, representatives of the Independent Auditors and the designated proxy shall take part in the meeting in compliance with the containment measures established by law, including, if applicable, using remote connection systems, in compliance with applicable legislative provisions in force.

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Please find below all necessary information in compliance with article 125-*bis* of the TUF.

PARTICIPATION IN THE SHAREHOLDERS' MEETING

All shareholders with voting rights, for whom within the third trading day prior to the date of the Shareholders' Meeting, i.e., **by 4 April 2022, the Company has duly received the authorised intermediary's notification certifying that they are entitled to participate in the Shareholders' Meeting and to exercise their voting rights,** are entitled to participate in the Shareholders' Meeting exclusively through the designated proxy (the "Designated Proxy"), according to what is set forth below.

In compliance with article 83-*sexies* of the TUF and article 42 of the Joint Order on post-trading issued by Consob and the Bank of Italy on 13 August 2018 ("Joint Order"), the authorised intermediary's notification to the Company shall be based on the records at the end of the accounting day of the seventh trading day prior to the date of the Shareholders' Meeting (**29 March 2022** – "record date").

Anyone whose shareholding has been recorded after the above date will not be entitled to attend and vote at the Shareholders' Meeting through the designated proxy.

The right to attend and vote at the meeting shall still be valid in the event that the notifications have reached the Company after the deadline of 4 April 2022, provided they are received before the opening of the meeting.

Shareholders - whose shares are already deposited in a custody and administration account with the Parent Company Banco BPM S.p.A. or with Banca Aletti & C. S.p.A., and as such have already been dematerialised - must in any case, under article 42 of the Joint Order, give specific instructions **by 4 April 2022** that the notification be issued, and obtain an immediate copy thereof, to be used as an admission ticket to the Shareholders' Meeting.

For Shareholders whose shares are deposited with other authorised intermediaries, note that, pursuant to the above-mentioned article 42 of the Joint Order, the notification instructions must still be submitted **no later than 4 April 2022**, making sure to obtain a copy of the notification.

ASSIGNMENT OF PROXY AND/OR SUB-PROXY TO THE DESIGNATED PROXY

Pursuant to article 106, paragraph 4 of the "Cura Italia" Decree, those entitled to vote who wish to participate in the Shareholders' Meeting will need to either:

(i) grant proxy - free of charge (except for transmission expenses) - to Computershare S.p.A. - Via Nizza 262/73, 10126, Turin - in its capacity as "Designated Proxy" pursuant to article 135-undecies of the TUF, with voting instructions on all or some of the proposed resolutions on the items on the agenda.

In this regard, to facilitate sending the proxy and the voting instructions, in the section of the Banco BPM website dedicated to this Shareholders' Meeting, www.gruppo.bancobpm.it "Corporate Governance - Shareholders' Meeting", it will be possible to complete and transmit online via a guided procedure the dedicated form prepared by Computershare, **until 12:00 p.m. on 6 April 2022.**

Shareholders are advised to make use of the online procedure.

Instead of the online procedure, the form downloadable from the same website may also be used and transmitted by **5 April 2022** to the addresses and with the methods specified on such form.

The proxy to the Designated Proxy, with voting instructions, along with an ID - and if the delegating party is a legal entity, a document proving the powers for issuing the proxy - must be transmitted to Computershare S.p.A. at the certified email address bancobpm@pecserviziotitoli.it or via fax to no. 011/0923202, provided the delegating party, even if a legal entity, uses its own certified email account or, lacking this, its own ordinary email account.

The original proxy, voting instructions and a copy of the correlated documentation must be sent to Computershare S.p.A. (Ref. "Banco BPM S.p.A. Shareholders' Meeting Proxy"), Via Nizza 262/73, 10126, Turin.

The proxy shall be valid exclusively for the proposals for which voting instructions have been given. The proxy and the voting instructions be revoked by the above deadline;

(ii) be represented by Computershare S.p.A., Designated Proxy pursuant to article 135-*novies* of the TUF in derogation of article 135-*undecies*, paragraph 4 of the TUF, via proxy and/or sub-proxy, with voting instructions on all or some of the proposed resolutions concerning the items on the agenda, with the possibility to that end to use the proxy/sub-proxy form available on the Banco BPM website www.gruppo.bancobpm.it (Corporate Governance - Shareholders' Meeting section) and to send it to Computershare S.p.A., by the deadline specified on the form itself, at the certified email address bancobpm@pecserviziotitoli.it or via fax to no. 011/0923202, provided the delegating party, even if a legal entity, uses its own certified email account or, lacking this, its own ordinary email account.

The Designated Proxy will be available to provide clarifications or information at 011/0923200.

The participation in the Shareholders' Meeting and the exercise of the right to vote by those entitled to vote will take place exclusively through the Designated Representative, who must be given voting instructions on all or some of the proposed resolutions concerning the agenda items; in consideration of the deadline for the submission of any individual resolution proposals referred to below, the proxy forms will be available, in the manner indicated above, starting on **24 March 2022**.

There is no electronic voting or voting by correspondence.

ADDITIONS TO THE AGENDA AND PRESENTATION OF NEW RESOLUTION PROPOSALS

Shareholders who even jointly represent no less than 1/40 of the share capital may ask, **by 17 March 2022** (within ten days of the publication of this notice calling the shareholders' meeting), to make additions to the list of items on the Meeting's agenda (with the exception of matters to be resolved by the Shareholders' Meeting, under the law, based on a proposal by the Board of Directors or based on a project or report submitted by the latter, other than those specified in article 125-*ter*, paragraph 1, TUF), specifying in the request the additional subject matters they propose, pursuant to art. 13.3 of the Articles of Association, or proposing additional resolutions on items already on the agenda, in compliance with article 126-*bis* of the TUF.

The written request must be sent to the Company by certified email to the certified email address soci@pec.bancobpmspa.it or by registered mail (Affari Societari di Gruppo, Piazza Filippo Meda, 4 - 20121 Milan).

The entitlement to exercise the right (including ownership of the minimum portion of the share capital specified above) is attested by filing a copy of the notification issued by the authorised intermediary under article 43 of the Joint Order.

Shareholders requesting the addition to the agenda or proposing new resolutions on subject matters already on the agenda shall prepare a report explaining the reasons for the proposed resolutions on new subject matters they are submitting for discussion or the reason for the additional resolution proposals on matters already on the agenda. The report shall be sent to the Board of Directors by the final deadline for the presentation of the request for additions, as described above. The Board of Directors shall make the report available to the public, together with any additional assessment, when it publishes the notice of the additions to the agenda or presents the new proposed resolutions, along the procedures prescribed by current regulations.

Any additions to the agenda or the proposal of additional resolutions on items already on the agenda shall be disclosed using the same procedure prescribed for the publication of the notice calling the meeting, at least fifteen days prior to the date scheduled for the Shareholders' Meeting (23 March 2022).

SUBMISSION OF INDIVIDUAL RESOLUTION PROPOSALS

As participation in the Shareholders' Meeting is permitted exclusively through the Designated Proxy, the shareholders entitled, **even if not holding the portion of the share capital specified in the previous paragraph, which intend to make individual resolution proposals on the items on the agenda, must submit them by 23 March 2022** via electronic communication to the certified email address soci@pec.bancobpmspa.it.

Each resolution proposal must specify the agenda topic to which it refers and indicate the specific proposed resolution. Entitlement to make proposals must be certified by the communication set forth in article 83-sexies of the TUF provided by the intermediary for participation in the Shareholders' Meeting and exercising the voting right, along with a copy of a valid ID (for natural persons) or the documentation attesting to the relative powers (for legal entities).

Such proposals, when pertinent to items on the agenda, shall be published by 24 March 2022 on the Company's website in order to allow those entitled to vote to knowledgeably express themselves also taking into account such new proposals and enable the Designated Proxy to receive any voting instructions on them.

RIGHT TO ASK QUESTIONS ON ITEMS ON THE AGENDA

Shareholders with voting rights may ask questions on items on the agenda only before the Shareholders' Meeting, by sending them no later than the end of the seventh trading day prior to the date of the Shareholders' Meeting on single call (i.e., by 29 March 2022) by certified email to the address soci@pec.bancobpmspa.it.

The applicants must deliver to the Company – through their intermediaries – the notifications certifying their entitlement to exercise this right; in the event that they have instructed their intermediaries to issue the notification to attend the Shareholders' Meeting, it will be sufficient to specify the notification reference numbers or at least the name of the intermediary in the application.

Questions received prior to the Shareholders' Meeting shall be answered, at the latest, at least two trading days prior to the date of the Shareholders' Meeting, via publication on the Company's website.

The Company may provide a comprehensive answer to questions covering the same content. No response will be provided if the information requested is already available in "FAQ" format in the dedicated section of the Company's website or if the response has already been published in the same section.

SHARE CAPITAL INFORMATION

The share capital subscribed and paid in by the Company at the date of this notice totals Euro 7,100,000,000.00 subdivided into no. 1,515,182,126 shares with no nominal value. As of the date of this notice, the Company owns no. 8,152,151 treasury shares.

DOCUMENTATION

The Directors' explanatory reports on each of the items on the agenda, including resolution proposals, together with all the other documentation to be published before the Shareholders' Meeting, shall be made available to the public at the registered office of Banco BPM S.p.A. and at Borsa Italiana S.p.A., and also published on the Bank's website (www.gruppo.bancobpm.it, "*Corporate Governance – Shareholders' Meeting*" section), as well as on the website of the authorised central storage mechanism www.emarketstorage.com, in compliance with the terms and procedures under the law.

Shareholders are entitled to receive a copy of the documentation once it has been duly filed by sending a request to Banco BPM S.p.A. at the certified email address soci@pec.bancobpmspa.it.

The Bank has also prepared (i) the Corporate governance and shareholding structure report pursuant to article 123-*bis* of Italian Legislative Decree no. 58/1998; (ii) the Consolidated non-financial statement in compliance with Italian Legislative Decree no. 254/2016 and Consob Resolution no. 20267 of 18 January 2018. The documents shall be made available to the public at the registered office of Banco BPM S.p.A. and at Borsa Italiana S.p.A., and also published on the Bank's website (www.gruppo.bancobpm.it, "*Corporate Governance*" section), as well as on the website of the authorised central storage mechanism www.emarketstorage.com, in compliance with the terms and procedures under the law.

This notice to convene – prepared interalia pursuant to article 84 of Consob Regulation no. 11971/99 and following amendments (Issuers Regulation) – shall be published in compliance with articles 125-*bis* of the TUF and 13.4 of the Articles of Association, in the daily newspapers “***Il Sole 24 Ore***“ and ***"MF,***" as well as with the other methods described above.

To receive additional information on the procedure to attend the Shareholders' Meeting, please contact Banco BPM S.p.A. (Affari Societari di Gruppo, Piazza Filippo Meda no. 4 – 20121 Milan) by sending a request to the certified email address soci@pec.bancobpmspa.it.

In compliance with Privacy regulations (EU Regulation 2016/679 of the European Parliament and of the Council of 27 April 2016), the Data Controller is Banco BPM S.p.A.. For full disclosure on data processing with respect to the exercise of rights related to the Shareholders' Meeting, please visit the website www.gruppo.bancobpm.it, “*Corporate Governance* – Shareholders’ Meeting” section.

Lastly, the Bank reserves the right to add to and/or amend the content of this notice if necessary as a result of the evolution of the Covid-19 emergency situation.

Milan-Verona, 1° March 2022

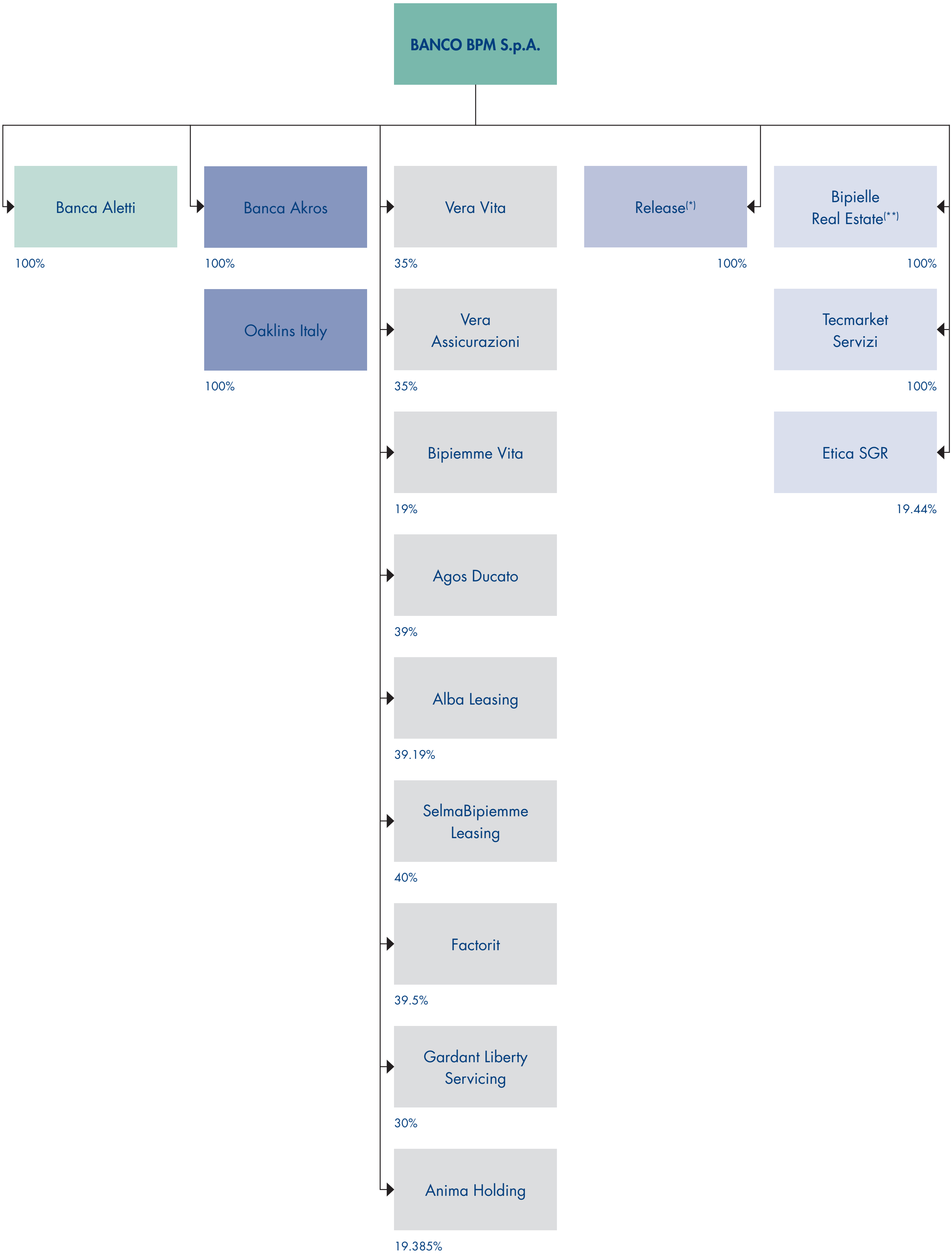
On behalf of the BOARD OF DIRECTORS

The Chairman

(Mr Massimo Tononi)

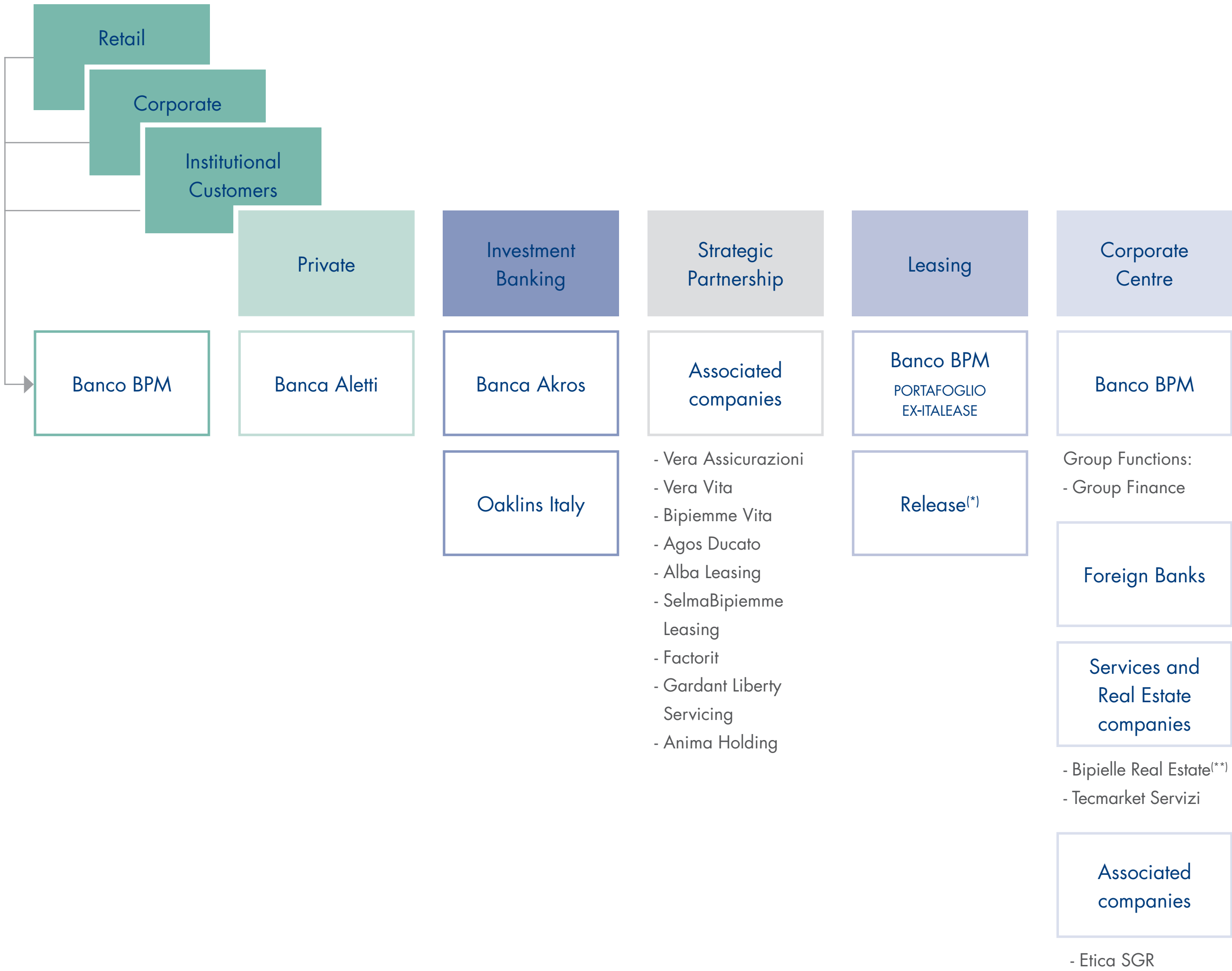
Reports on operations and consolidated
financial statements for the year

GROUP STRUCTURE: MAIN COMPANIES



(*) Company incorporated into the Parent Company on 21 February 2022.
(**) Company incorporated into the Parent Company on 1 January 2022.

GROUP STRUCTURE: BUSINESS LINES



(*) Company incorporated into the Parent Company on 21 February 2022.
(**) Company incorporated into the Parent Company on 1 January 2022.

GROUP TERRITORIAL NETWORK

N° BRANCHES

NORTH	1,155
CENTRE	218
SOUTH AND ISLANDS	135
TOTAL	1,508

Banco BPM Group Branches in Italy	Number
Banco BPM	1,452
Banca Aletti	55
Banca Akros	1
Total	**1,508**

Presence abroad

The Group's foreign operations include a subsidiary company, Banca Aletti Suisse, and Representative Offices in China (Hong Kong) and India (Mumbai).

Group financial highlights and economic ratios

Highlights

The highlights and main ratios of the Group, calculated based on the reclassified financial statements, are presented below. The underlying calculations for these are illustrated in the "Results" section of this Report.

(millions of euro)	2021	2020	Change
Income statement figures			
Financial margin	2,273.6	2,113.4	7.6%
Net fee and commission income	1,911.2	1,663.8	14.9%
Operating income	4,510.7	4,151.8	8.6%
Operating expenses	(2,515.8)	(2,430.1)	3.5%
Profit (loss) from operations	1,995.0	1,721.8	15.9%
Profit (loss) before tax from continuing operations	921.0	306.1	200.9%
Profit (loss) after tax from continuing operations	667.2	292.6	128.0%
Parent Company's profit (loss) for the year	569.1	20.9	not sign.

(millions of euro)	31/12/2021	31/12/2020	Change
Balance sheet figures			
Total assets	200,489.2	183,685.2	9.1%
Loans to customers (net)	109,383.4	109,335.0	0.0%
Financial assets and hedging derivatives	36,326.4	41,175.6	(11.8%)
Group shareholders' equity	13,095.0	12,225.2	7.1%
Customers' financial assets			
Direct funding	120,213.0	116,936.7	2.8%
Direct funding without repurchase agreements with certificates	123,168.0	120,141.1	2.5%
Indirect funding	102,187.9	94,807.3	7.8%
Indirect funding without protected capital certificates	99,067.3	91,575.9	8.2%
- Asset management	65,347.9	59,599.2	9.6%
- Mutual funds and SICAVs	45,762.8	40,797.6	12.2%
- Securities and fund management	4,135.1	3,945.2	4.8%
- Insurance policies	15,449.9	14,856.4	4.0%
- Administered assets	36,840.1	35,208.1	4.6%
- Administered assets without protected capital certificates	33,719.4	31,976.7	5.5%
Information on the organisation			
Average number of employees and other staff (*)	19,949	20,776	
Number of bank branches	1,508	1,808	

(*) Weighted average calculated on a monthly basis in terms of full-time equivalent resources. Does not include the Directors and Statutory Auditors of Group Companies.

The following table shows several alternative performance measures (APM) identified by directors to facilitate the understanding of the economic and financial performance of Banco BPM Group's operations. The APMs are not envisaged in IAS/IFRS and, although they are calculated based on financial statements data, they are not subject to a full or limited audit.

The aforementioned measures are based on the guidelines of the European Securities and Markets Authority (ESMA) of 5 October 2015 (ESMA/2015/1415), incorporated in CONSOB communication no. 0092543 of 3 December 2015.

In line with the guidance contained in the update of the document "ESMA32_51_370 – Question and answer – ESMA Guidelines on Alternative Performance Measures (APMS)", published on 17 April 2020, no changes have been made to the APMs to take into account the effects of the Covid-19 crisis.

In this regard, it should be noted that for each APM, evidence of the calculation formula has been provided and the figures used can be inferred from the information contained in the table above and/or in the reclassified financial statements provided in the "Results" section of this Report.

Financial and economic ratios and other Group figures

	31/12/2021	31/12/2020
Alternative performance measures		
Profitability ratios (%)		
Return on equity (ROE) [1]	4.54%	0.17%
Return on assets (ROA) [2]	0.28%	0.01%
Financial margin / Operating income	50.40%	50.90%
Net fee and commission income / Operating income	42.37%	40.07%
Operating expenses / Operating income	55.77%	58.53%
Operational productivity figures (thousands of euro)		
Loans to customers (net) per employee [3]	5,483.1	5,262.7
Operating income per employee [3]	226.1	199.8
Operating expenses per employee [3]	126.1	117.0
Credit risk ratios (%)		
Net bad loans / Loans to customers (net)	0.83%	1.34%
Net unlikely to pay / Loans to customers (net)	2.11%	2.55%
Net bad loans / Shareholders' equity	6.92%	11.96%
Other ratios		
Financial assets and hedging derivatives / Total assets	18.12%	22.42%
Total derivatives / Total assets	1.06%	1.45%
- trading derivatives / total assets	1.00%	1.41%
- hedging derivatives / total assets	0.06%	0.04%
Net trading derivatives [4] / Total assets	-0.02%	0.21%
Net loans / Direct funding	90.99%	93.50%
Regulatory capitalisation and liquidity ratios		
Common equity tier 1 ratio (CET1 capital ratio) [5]	14.68%	14.63%
Tier 1 capital ratio [5]	16.52%	15.85%
Total capital ratio [5]	19.59%	18.75%
Liquidity Coverage Ratio (LCR)	209%	191%
Leverage ratio	5.92%	5.66%
Banco BPM stock		
Number of outstanding shares	1,515,182,126	1,515,182,126
Official closing prices of the stock		
- Final	2.640	1.808
- Maximum	3.040	2.456
- Minimum	1.781	1.043
- Average	2.542	1.538
Basic EPS	0.375	0.014
Diluted EPS	0.375	0.014

(1) Calculated as the ratio of net profit (loss) for the year to shareholders' equity excluding the profit (loss) for the year.
(2) Calculated as the ratio of profit (loss) for the year to total assets.
(3) Arithmetic average calculated on a monthly basis in terms of full-time equivalent resources, as shown in the previous table. Does not include the Directors and Statutory Auditors of Group Companies.
(4) The aggregate of net trading derivatives corresponds to the mismatch, in absolute terms, between the derivatives included under the Balance Sheet item 20 a) of assets, "Financial assets at fair value through profit and loss - held for trading", and item 20 of liabilities, "Financial liabilities held for trading".
(5) Ratios calculated including the profit (loss) for the year and deducting the amount of the dividend and other allocations.

Group report on operations

ECONOMIC SCENARIO

The evolution of the pandemic

The pandemic's impact on economic activity subsided considerably over the course of 2021, however, Covid-19 directly and indirectly conditioned global recovery, and in particular, that of the EU. Up until the summer, vaccination campaigns continued to improve the underlying situation with the spread of the Delta variant, which was accompanied by a less marked increase in deaths in areas with high vaccination rates. From September, cases gradually fell until they were under the levels recorded at the beginning of July. Mobility continued to resume everywhere, returning to pre-pandemic levels. However, the vaccinations campaigns in areas in which they were at the most advanced stages (USA, United Kingdom and Eurozone) started to slow down, while accelerating significantly in Japan; instead, low-income countries continue to lag far behind. In the last quarter of 2021, the rapid spread of the Omicron variant brought back growing uncertainty, representing a potential obstacle to economic recovery. The wave of new cases in the major industrialised countries triggered fears that restriction would be reintroduced. At the end of November, according to "Our World in Data", 54.2% of the world population had received at least one dose of the vaccination against Covid-19, a percentage that falls to 5.8% in low-income countries.

The international scenario

In 2021, the global economy emerged from the recession provoked by the pandemic. The strong rebound after the collapse in 2020, initially driven by manufacturing, then extended to services, seemingly making a return to previous development trends: in several of the major advanced economies, GDP reached levels that were even higher than those of 2019, particularly in the USA and China, while in others, including Italy, this milestone will be achieved in 2022. In just five quarters, a deep recession was followed by a very fast recovery, with an unprecedented V-shaped economic rebound. However, the rapidity of growth risks causing more damaging effects in the medium-long term than world economy could indirectly inherit from the pandemic: the increase in income inequality, widespread interruptions of supply chains, which started in 2020 and extended into 2021, as well as a healthy recovery of consumer price trends, especially in the advanced economies, facilitated by the unprecedented increase of money supply.
Following the 2.9% collapse in 2020, preliminary results indicate a 5.9% growth of world GDP in 2021 (IMF estimates), thanks to the substantial recovery of domestic demand, especially the services component, and of international trade. Towards the end of the year, a certain inconsistency of the paths towards economic recovery was noted in the industrialised countries, with better performance in Europe than in the United States and China. In fact, the aggregate figure conceals a differentiated scenario, both between the advanced market economies and between emerging countries, which essentially reflects their different vaccination rates.
In this context, the pace of international trade increased considerably, especially in the first half of 2021, despite various obstacles to the full reactivation of value chains and a fall in trade with China in the second half of the year. Average annual growth is estimated to be +8.6% (Source Prometeia in constant USD 2000) against -5.2% in 2020.
Looking more in detail at the individual major economies, in the United States, after a brilliant start at the beginning of the year, also driven by the "Stimulus and Relief Package 4" measures from the end of 2020, in the third quarter, GDP recorded a marked deceleration (GDP of Q3 +2.3% annualised from +6.7% in Q2), mostly due to the slowdown in consumption and in non-residential fixed investments. In the last quarter of 2021, growth picked up pace: +6.9% annualised, driven by the recovery of consumption, +3.3%, but above all by the sustained momentum of gross private investments, +32.0%, also thanks to the component of intellectual property products, +10.6%. Lastly, towards the end of the year, we draw attention to the lack of approval of the "Build Back Better Plan" - the examination of which has been postponed to 2022 - which contains both the measures envisaged by the American Job Plan (to support the world of production) and by the American Family Plan (to support households). Average growth for 2021 stood at +5.7%. The strong recovery had a positive impact on the labour market: unemployment fell to 3.9% in December (6.7% at the end of 2020), while non-agricultural jobs rose by around 6.5 million over 12 months. Despite this, job openings continued to be particularly high: 10.9 million in December 2021 against 6.6 million twelve months earlier, a mismatch that represents one of the significant constraints to aggregated supply. This phenomenon, through pressure on average hourly pay (+4.7% yoy at December 2021), also has a strong influence

on inflation. Consumer prices, measured by the CPI, accelerated substantially in the period: +7.0% in December 2021, compared to +1.4% twelve months earlier.
In China, after a first half of significant recovery, encouraged by the generalised reopening of production activities and by the positive trend in social credit (total social financing), although at a slower rate, from the third quarter, economic activity (GDP +0.2%, +1.2% in the previous three months) suffered from problems in the real estate sector, which represents around one third of China's GDP, weighed down by the significant financial difficulties of the real estate giant, Evergrande, which then went into default. This episode, which had limited financial contagion, was accompanied by a greater weakness of infrastructure investments with respect to the past, and by a tightening of the legislative framework, with a view to slowing down the excess lending to the private sector at a time in which the prices of energy products were rising and new lockdown measures related to the resumption of local cases were being implemented. Overall, China's GDP for 2021 is expected to increase by +8.1%, against a rate of inflation, which recovered in December: +1.5% against +2.3% in November (+0.2% in December 2020).
In the first half of the year, the Japanese economy suffered from an extension of its state of emergency (and of the relative distancing measures), decided by the authorities of the country's largest prefectures given the rise in the number of infectious cases. The recovery of consumption and of investment took place mainly in the second quarter (GDP +1.9% annualised), thanks to activities relating to the Olympics, as well as to corporate spending and investment fuelled by the rapid global economic recovery. However, it was dampened again by the spread of the Delta variant in the summer: GDP in the third quarter was -3.6% annualised. The Japanese manufacturing system, one of the main beneficiaries of the shift of the axis of global growth towards China, also suffered from the slowdown of its large Asian trading partner in the second half of the year, and growth for 2021 overall was +1.6% (against -4.8% in 2020). The new Government, in office from October and headed by Prime Minister Fumio Kishida, launched a package of stimulus measures in November worth USD 490 billion, aimed at increasing the momentum of growth, weakened by the pandemic.
Of the emerging economies, the acceleration of prices interrupted the recovery most abruptly in Russia and Brazil, where consumer price inflation reached 8.1% and 10.7% respectively in October. Nevertheless, both central banks increased interest rates numerous times during the year. The growth rate of producer prices towards the end of the year stabilised in both cases, against some relocations of supply. Estimates indicate for 2021 a growth in Russia's GDP of +3.2%, while the growth of Brazil's GDP was 4.9%.
International inflation recorded an abrupt acceleration during the year, +4.5% against +3.4% in 2020 (Source Prometeia), driven both by the sudden recovery in global demand, and, especially in the second half of the year, by the widespread increase in the prices of commodities and energy. Spot prices for oil exceeded 80 dollars a barrel (both Brent and WTI). The impact on inflation was exacerbated by the widespread difficulties along global supply chains, for example the shortage of semiconductors, which substantially affected the automotive industry, and the staggering increase in the cost of sea freight. At May 2021, the Baltic Dry Index had risen by +670% with respect to 12 months earlier. Expectations for inflation in the medium-term reached 3% in the United States.

The situation in Europe and Italy

Last year, on a par with the other major industrialised countries, the EU's economy was characterised by a decided recovery, which enabled it to make up a significant share of the GDP lost in 2020. After a difficult start to the year, heavily conditioned by the various restrictions still in place, towards the spring, economic activity took off. In fact, in the first quarter, the average GDP of the EMU fell (-0.2% against the previous quarter), particularly in Germany (-1.8% qoq), in the wake of weak domestic consumption. However, in the following months, as the restrictions were relaxed and the critical phase of the health emergency was overcome, the economy entered into a period of robust expansion, driven by domestic demand and in particular by spending on services and tourism. The recovery of consumption was encouraged by the exceptional tax policy measures adopted in all EU countries, to mitigate the effects of the crisis on households and businesses, as well as by the savings accumulated during the pandemic. The confidence of economic operators, of households in particular, rose rapidly, also thanks to the launch of the vaccination campaigns, which accelerated the economic recovery. In the winter months, the GDP should have settled at the levels reached in the third quarter. Various factors contributed to this slowdown, particularly the new wave of cases, which had a devastating effect on the Eurozone and many other countries, especially the USA, following the emergence of the Omicron variant of the virus.
During the year, the institutions of the European Union continued to implement extraordinary initiatives to relaunch growth: the ECB maintained the Pandemic Emergency Purchase Programme (PEPP) unchanged until the end of the year, and the EU finalised the European relaunch plan, known as Next Generation EU (NGEU). The NGEU Plan, approved in July 2020 and ratified at the end of May 2021, makes 800 billion available to Member States to invest

in the economic recovery of the EU, aimed at repairing the economic and social damage caused by the pandemic. The measures contemplated by plan, financed through fundraising in the capital market from 2021 to 2026, include roughly 390 billion in subsidies and around 360 billion in loans to be repaid over a medium-long term time horizon. More specifically, in the third quarter, the last reported figure, the GDP of the Eurozone rose by 2.2% qoq (+2.2% in the previous quarter), and +3.9% against the corresponding quarter of the previous year (+14.4% in Q2 of 2021). The most dynamic component was household consumption (+4.1 qoq) which contributed over 2 percentage points to GDP. Instead, the performance of net exports was more modest, contributing only 0.3 points to GDP in the quarter in question. By contrast, the Eurozone average for gross fixed investment fell by 0.9% against the previous quarter, thus deducting 0.3% from GDP. To a certain extent, this performance reflects the persistent weakness of investment in means of transport, which fell by 8.6% in the period (-5.1% in the second quarter, and -6.2% in the first) which, on the production side, suffers particularly from problems with the global supply chains cited earlier. For the fourth quarter, the preliminary flash estimate, communicated by Eurostat, indicates a fairly modest growth of GDP in the Eurozone compared to the previous quarter, +0.3% qoq, which brings the increase for the whole of 2021 to +5.2%. In this economic framework, the Eurozone has also seen an abrupt and violent increase in inflation, after many years of moderate price trends. The main reason for this inversion of the trend is the substantial increase in the prices of energy commodities, especially natural gas. In December, the yoy increase of consumer prices reached 5%, compared to -0.3% twelve months earlier, with an average annual figure that settled at around 2.6%.
The performance of the Italian economy reflects this context of strong world recovery. Some aspects of Italy's recovery have far surpassed those of their Eurozone partners. The emergence of the second wave of Coronavirus at the end of 2020, pushed the Government to introduce a new system of restrictions for the Regions, based on colours. Despite the new limits imposed on the circulation of people and of certain businesses, particularly the restaurant and tourism industries, the change in GDP in the first quarter was positive (+0.3% qoq), unlike the average figure for the EMU. The fall in household consumption, in the wake of the above-cited limitations, was in fact more than offset by the robust increase in gross fixed investment and in stock. From the spring onwards, encouraged by receding cases and by the gradual relaxing of restrictions, the recovery gained even more momentum, marking a further two consecutive quarters with growth that was appreciably higher than the Eurozone average. The abundant measures that the government has kept deployed and strengthened to combat the effects of the restrictions have obviously provided robust support to the economy. In the first quarter, the establishment of the Draghi government contributed to reinforcing the expectations of economic operators and favoured a reduction in the BTP-Bund spread. Furthermore, in late April, the government submitted its "National Recovery and Resilience Plan (NRRP)" to the EU Council, which was then approved in mid-July.
More specifically, the qoq change in Italian GDP in the second quarter stood at 2.7% (17.1% yoy), sustained by the consistent increase in household consumption (+5% qoq).[1] The performance of the third quarter, the latest for which final figures are available, confirmed the positive trend enjoyed by Italy's economy, pushing up growth forecasts for the whole year. For the second consecutive quarter, the market services sector recovered considerably, alongside the growth of the industrial sector. Household consumption rose by 3.0% against the previous period, encouraged by a recover of consumer confidence, which led the relative index to return to pre-pandemic levels in the summer. Gross fixed investment also rose (+1.6%), albeit at a slightly slower pace than the first half. Investment in machinery and equipment contributed significantly to this trend, with an increase of 4.5%, while that in housing, following the achievements of the previous quarters, set the pace (+0.4%). The contribution of net exports was positive (0.5%), marking a further increase compared to the first half of the year.
Following the third quarter, which recorded +2.6% qoq (+3.8% yoy), in the fourth quarter, the economic recovery levelled out, due to the effects of the spread of the new Omicron variant of the virus, which has proven to be highly infectious and has provoked another huge wave of cases. However, the widespread implementation of vaccination campaigns contributed to lightening the health emergency, reducing the need for hospitalisation. The success of the vaccination campaigns, the solicitous launch of the administration of third doses, together with the introduction of the so-called green pass, enabled the Government to limit the introduction of distancing measures to tackle the new health crisis. Nevertheless, in the last few weeks of the year, the surge in the number of cases, with the consequent rise in the number of people in quarantine, contributed to greater consumer caution. Based on ISTAT's preliminary estimates, the change in GDP for the last quarter in question stood at +0.6% qoq (+6.4% yoy), enabling the year to close with a growth, for the whole of 2021, of 6.6%, one percentage point more than the Eurozone average.
Part of the merit for this dynamism should be attributed to the manufacturing segment which, despite the difficulties relating to the supply chains and tension over production prices, demonstrated unexpected resilience in certain aspects, given the performance of the past 15 years. Indeed, in the third quarter, Italian industrial production

[1] The preliminary figures illustrated in this paragraph are consistent with the forecasts and the scenarios used in the valuation processes implemented by the Group.

returned to pre-Covid levels, marking an exception with respect to its main Eurozone partners: in December, yoy growth was 4.4%.
The recovery led to an appreciable improvement in the labour market. In fact, employment rose during the year with a rate of employment that rose by 1.9%. The rate of employment as at December 2021 stood at 9.0% (9.8% as at December 2020). The use of pay integration instruments - CIG (temporary redundancy fund) and solidarity funds - remained high, although to a lesser extent than in 2020.
At the same time, inflation reared its head in Italy as well for the same reasons as the Eurozone. In December, consumer prices for the whole community (NIC index) rose by 3.9% yoy. On average, in 2021, inflation was +1.9% (-0.2% in the previous year). The increase in consumer prices, net of energy ones, was +0.7%, the same change as in 2020, confirming the significant impact that energy prices have on inflationary trends, also in Italy.
The liveliness of the economic scenario contributed to substantially containing the budget deficit with respect to the forecasts of the Economic and Financial Document (DEF) in April. In September, the net debt of the public administrations recorded a yoy increase of 9.4% against an initial forecast for 2021 of 11.8% (final figure for 2020 was 9.6%). According to several estimates, the final figure could be around 1% lower. This improvement is the result of a significant increase in tax revenue, which at the end of October recorded a 12% increase yoy. By virtue of these trends, and of the robust increase in nominal growth, the debt/GDP ratio should fall, following the maxi-increase in 2020: the update note of the DEF in September envisaged a reduction of over 2 percentage points, from 155.6% to 153.5%.

Monetary policy and the financial markets

At the beginning of 2021, the financial markets were still highly impacted by news concerning the evolution of the pandemic and vaccination campaigns. After a positive start, the half-year period recorded greater volatility due to the discovery of new virus variants and the accumulation of delays in vaccine deliveries, which were combined with uncertainty as regards the timing of the fiscal stimulus in the United States.
The continuation of the pandemic with the development of the third wave indeed required governments to renew their income support measures, which initially should have expired in 2021.
From mid-February, there was a strong increase in inflationary expectations in Europe and especially in the United States, which translated into a sudden increase in nominal and real rates, in the presence of actual inflation which continued to hover at low levels. The rate of inflation in the United States accelerated between February and June (to 5.3%) and between September and November, closing the year at 7.1%. The price jump in certain sectors (e.g. energy, used cars), sustained the general index, but this increase is likely to be temporary in part, considering the base effect and post-crisis return of consumer preferences in the past few months. In Europe, price trends were more contained, despite the growing pressure of the energy sector linked to the dependence on supplies from Russia: the HICP index (Harmonised Index of Consumer Prices) closed the year at 5%.
The steepening of the curves in the USA further harmed the investment grade bond classes, while the high yield sector showed greater stability, as the good outlooks for an economic recovery continued to support demand for new issues which offered still appealing returns in absolute terms. The progress made in the vaccination campaigns were taken as a positive sign for the strengthening of the US dollar and the British pound.
The figures and expectations for inflation together with the presumed or actual responses of the central banks, were the main drivers in 2021.
For Italy, the new high-profile and highly European-oriented government which took office, guided by former ECB President Mario Draghi, contributed to the good performance of the Italian sovereign market. Also strengthened expectations regarding inflation, which translated into a considerable sell-off on government bonds of core countries (starting with the United States), stimulated the over-performance of peripheral countries (particularly Italy) in terms of credit risk.
The Government bond market in Europe recorded modest fluctuations of spreads in the first six months of the year, against a rise in the yields of the 10-year German bond, which reached a maximum of -0.1% in May and October; as regards Italy, the BTP/Bund spread rose from 110 bps to 132 bps at the end of the year, a level close to the maximum of the period during two times of tension: at the time of the fall of the Conte bis Government in January, and the announcement by the ECB of the end of the Pandemic Emergency Purchase Programme (PEPP) in March 2022. Following the establishment of the Draghi Government, market performance almost exclusively reflected the expectations regarding the evolution of ECB monetary policy, rather than the political affairs of the new government, apart from started a more marked expansion towards the end of the year in view of the Presidential elections.
Western stock markets were sustained up until September by optimism relating to the vaccination campaigns and by excellent macroeconomic data: an early end to the pandemic appeared certain, around 6 months ahead of Europe.

Concerns regarding inflation, however, generated market volatility on several occasions, particularly in early May and October, despite the continuation of accommodating responses on the part of the central banks.
All of the world's major stock markets, with the striking exception of those linked to Chinese shares, closed the year with very positive performance, particularly technological securities, which however, in the second half of the year recorded a substantial slowdown.
The financial stock market sector (both European and Italian banks) recorded an average performance of 24% in the first half, closing the year at +34%. Instead, the performance of the insurance segment was visibly different, up 37% in Italy against +15% in Europe. The trend of the Asset Management segment in Italy was positive, with stock market performance estimated at 23.4%, on the basis of an index weighted by the capitalisation of listed issuers.
The average spread of credit default swaps (CDS) relating to European banking issuers did not record significant changes after the re-rating that took place in fall 2020 after the announcement of the first anti-Covid vaccines, closing the year at around 59 bps. CDSs marked similar performance for the two main Italian banks.
In the bond market, the European financial sector recorded a strong appreciation in relative terms with respect to the other sectors: the Iboxx BBB spread between the two segments fell to 7.2 bps over the year, closing at 14.6 bps, an exceptionally low level even for pre-Covid years. The spread between subordinated and senior securities (Itraxx 5Y) remained at low levels, around 50 bps, closing the year at 57 bps.
In Europe, the credit market continued to be supported by outlooks for an economic recovery, while in Italy it appeared to benefit primarily from outlooks for bank M&A transactions and expectations concerning the implementation of the Next Generation EU programme.
Although off and on, Covid was perceived by the financial markets as a problem being rapidly overcome: with investor attention primarily back on company accounts and the fundamentals, which were measured with respect to pre-Covid consensus levels.
The two main share and credit market corrections were made in September, when the difficulties of international logistics systems and the marked increase in energy commodity prices (oil, natural gas) raised concerns as to economic growth and substantiated the hypothesis that inflation might be less transitory than expected, and in the second half of November, following the reduction in purchases by the FED and the statements of central banks in Australia and Canada, in a month which culminated in a strong correction related to the announcement of the Omicron variant in South Africa.
Monetary policy took on an increasingly important role over the course of 2021: initially confirming, as in the case of the FED, or recalibrating and extending, as in the case of the ECB, the instruments set in motion in the previous 12 months; it then started to establish the timing and the intensity of a normalisation process, made more pressing by the rise in inflation, which quickly surpassed expectations, resulting in unprecedented price trends. However, no significant changes took place until June when for the first time, the FED hinted at a reduction in the monthly pace of its bond buying programme (compared to USD 120 billion), while projections on the policy rate level revealed that the majority of the Federal Reserve Board members expected two rate increases in the course of 2023. This resulted in a decisive change in inflationary expectations, the steepness of curves and medium-long term returns were also rapidly reflected by the European market.
The FED continued to adopt a cautious approach, even in August at Jackson Hole, where it was clarified that any possible reduction of monetary stimulus (known as tapering) would have been progressive and gradual, with schemes to support economic growth in the presence of inflation considered transitory. Only at the end of November, after the confirmation of Jerome Powell, did the Central Bank's tone appear more concerned about the price trends, echoing an issue that was gaining political importance.
At the beginning of November, US monetary policy took a decisive step, with the announcement of tapering, marking the start of monetary policy normalisation. The tapering will end in June 2022 to reduce the risk of a wage-price spiral, while the first intervention on FED Funds had been envisaged in May.
Looking now at Europe, it is important to remember how the mix of instruments set in motion by the European Central Bank has remained stable. Banking system liquidity was guaranteed by the third series of TLTRO which was subject to an important revision at the 10 December 2020 session, and was then implemented as of January 2021:

- introduction of three new auctions, all with a three-year duration, in June, September and December 2021;
- extension until June 2022 (from June 2021) of the collateral easing measures and the period in which it is possible to benefit from the discount of 50 additional bps on the cost of financing;
- raising of the maximum draw-down threshold to 55% of eligible loans.

It is important to add that the ECB adopted an ambitious programme for fighting against climate change, which calls for the inclusion of climate variables in the monetary policy framework with an extension of the level of analysis, modelling and disclosure. Climate variables will also be assessed as regards the banking sector risk assessment, collateral and the corporate sector purchase programme (CSPP).

At the end of March 2022, the Governing Council will suspend net asset purchases under the PEPP, the amount of which had been increased in December 2020 by 500 billion, bringing it to 1,875 billion, after having reduced the monthly amount from September. The Governing council also decided to extend the reinvestment horizon of the PEEP to the end of 2024, well beyond the end of purchases at the end of March. In any event, the future roll-off of the PEEP portfolio will be managed to avoid interference with the appropriate monetary policy orientation.

Domestic banking activity

Up until mid-2021, domestic banking activity benefited from the gradual improvement of the economic scenario. In the second half of the year, the stabilisation of growth caused a decisive slowdown in the increase of bank assets. With regard to non-financial companies, the slower trend was the result of both the huge amounts of available liquidity set aside during the pandemic and the recovery of cash flows due to the improvement in economic activity. These two factors also led to a lower demand for loans with state guarantees. Residual corporate demand was mostly driven by the need to renegotiate debt and, partly, by the recovery in fixed investment. Lastly, the trend was also influenced by the extension, albeit with limited changes, from 30 June to 31 December of the measures envisaged by the temporary framework of State aid, in particular the state guarantee on loans and a greater flexibility in insuring export credit.

As regards households, loans maintained a strong growth rate, reflecting the rise in mortgages for the purchase of a home, the demand for which was stimulated by prospects of an improvement in real estate prices and by the continuation of interest rates at record lows. This uptrend was facilitated by the increase in income, due to the improvement of the economic cycle and lower saving propensity. Instead, consumer credit recorded a substantially stable trend.

More specifically, according to ABI figures, total loans (private sector and the Public Administration) closed 2021 with an increase of 2.0%, while those of households and businesses were up by 2.6%. Looking more closely by type of borrower, according to Bank of Italy figures, loans to non-financial companies recorded a +1.6% yoy, marking a net slowdown against 2020 (+5.8%). The slowdown was widespread, affecting all sectors, but was more intense for manufacturing companies. Instead, loans to households rose +3.7%, compared to +1.6% in 2020.

Credit quality continued to improve, along the direction seen at the end of the first half, in several respects. Net bad loans (net of write-downs and provisions made) were down, according to ABI data, to 15.1 billion in December, compared to 20.9 billion twelve months earlier, with a reduction of over 27%, corresponding to -5.8 billion. The ratio of net bad loans to total loans, again at December, was 0.86% (compared to 1.21% twelve months earlier). The rate of default on total loans, based on the Bank of Italy’s figures, improved to 1.0%, on lower levels than those recorded prior to the Great Financial Crisis in 2008.

As regards funding, the funding streams originating from the ECB through auctions continued to substantially support the domestic banking system, which also benefited from the capital keys exemption regarding the purchase of Treasury bonds by the Central Bank. Total funding (deposits from resident customers and bank bonds), rose at the end of December by 5.6%, marking a slowdown with respect to the +8.0% recorded in 2020, against a fall in household saving propensity and an increase in the working capital of businesses as the economic recovery gained pace. Breaking down the aggregate figure, deposits continued to rise considerably: +6.9% compared to a year earlier. Instead, medium and long-term bond funding fell over the 12 month period by 4.4%.

The bank interest spread in November 2021, calculated as the difference between the average interest rate on loans and the average interest rate on total funding from households and non-financial companies, fell 11 bps to 169 bps, compared to 180 bps in December 2020. In the same month, the mark-up (calculated as the difference between the average rate on loans to households and non-financial companies and the 3-month Euribor rate) stood at 271 bps, recording the same decrease as the corresponding month of the previous year (-11 bps); while the mark-down (calculated as the difference between the 3-month Euribor rate and the rate on total funding) was substantially stable at 101 bps. Managed funds recorded a very positive trend: in December 2021, the assets of Italian and foreign open-ended funds amounted to 1,263.3 billion, up by +13.2% compared to the end of 2020. Net inflows of open-ended funds amounted to 64.7 billion from the beginning of the year.