UBI Banca

EQUITA GROUP

Company report

Buy (maintained)

19 March 2020 – 5:30 PM

MARKET PRICE: ***EUR2.12*** *TARGET PRICE:* ***EUR2.57 (from EUR3.37)***

Investment Banking

Data

Shares Outstanding (m):	45.5
Market Cap. (EURm):	96.4
Enterprise Value (EURm):	NA
Free Float (%):	37.0%
Av. Daily Trad. Vol. (m):	0.03
Main Shareholder:	Management 53.9%
Reuters/Bloomberg:	EQUI.MI EQUI IM
52-Week Range (EUR)	1.9 3.2

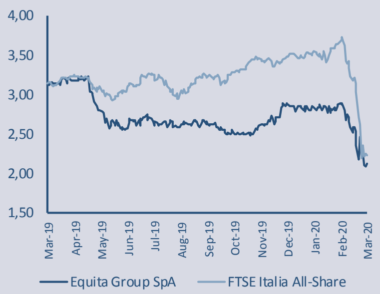
Source: FactSet, UBI Banca estimates

Performance

	1m	3m	12m
Absolute	-26.4%	-26.4%	-32.5%
Rel. to FTSE IT	+12.8%	+9.1%	-3.0%

Source: FactSet

Graph area Absolute/Relative 12 M



Source: FactSet

Massimo Vecchio
Senior Analyst
massimiliano.vecchio@ubibanca.it
Tel. +39 02 62753016

Dario Fasani
Analyst
dario.fasani@ubibanca.it
Tel. +39 02 62753014

www.ubibanca.com/equity-research

Solid 4Q/dividend, but 2020 is an unknown

Equita reported a very strong 4Q19 with net profit almost doubling YoY thanks to a +80% YoY in revenues that was able to bring the FY19 top line almost in line with 2018, something thought to be anattainable only 6 months ago. IB revenues doubling and EUR3.7 million performance fees in AAM were the main drivers of the surprise vs. our estimates. EUR0,19 dividend, in line with guidance, was not to give for granted in the current scenario. However, in this turmoil, 4Q19 is already history and investors will be looking at leverage/cash flow generation, flexibility of costs structures and revenues diversification. Equita is well positioned in terms of capital (TCR at 26% in 2019 and more than EUR40 million of reserves) and the variable part of the employees compensation is a buffer in order to manage the cost/income ratio. Dependancy on Italy and stock liquidity instead plays against Equita. In our base case scenario (which assumes a V-shape recovery in 2H20) we are reducing our 2020-21 estimates by 21.1% but reiterating our positive stance supported by the capital strength coupled with the recent price fall. The stock seems to be pricing already our worst case scenario, a prolongued recession, which we see as a valuation floor.

> **V-shape recovery scenario (our base case).** It is based on previous experiences (SARS/MERS/Swine fever) when market falls were followed by a V-shape rebound and assumes that by the end of 2Q20 the infection is over (like for the Swine flu). In this scenario we expect Equita EPS to go down 15% in 2020 and back to growth in 2021. This is based on traded countervalues down 20% in the remaining 9 months of 2020, cost cutting of EUR2.8 million and some capital preservation (a EUR0,01 dividend decline vs. the 2019 levels).

> **Prolongued recession scenario (our worst case).** This scenario assumes that the infection would last longer and/or that real economy issues will impact financial markets health. This scenario, similar to the 2008-09 crisis, may stiil see a short-term rebound (as in 2010) but followed by a couple of years of slow but steady decline. Traded volumes should decline significantly, IB revenues would be hit hard and AAM would see outflows and no performance fees. We would expect Equita EPS to go down 26% in 2020 and than stabilize. This is based on traded countervalues down 40% in the remaining 9 months of 2020, cost cutting of EUR4.5 million and significant capital preservation.

> **Stock discounting the worst. BUY reiterated, TP to EUR2.57.** In our base case scenario, at current peers' multiples, the stock fair value is EUR2.57 (our new TP). In our worst case scenario the fair value is EUR2.18. We may therefore say that the current share price implies a prolongued recession that contamines the financial markets. While it is difficult draw conclusions, the prolongued recession seems a too harsh scenario and, after the fall, we don't suggest to sell the stock. We therefore reiterate the Buy.

Financials EURm (ex. treasury shares)

	2019A	2020E	2021E	2022E
Revenues	58,3	53,5	55,3	58,5
Profit Before Taxes	13,7	11,7	13,2	14,2
Net Income	9,5	8,1	9,1	9,8
Net Income Adjusted	9,5	8,1	9,1	9,8
BVPS (EUR)	1,76	1,75	1,77	1,80
EPS (EUR)	0,21	0,18	0,20	0,22
DPS (EUR)	0,19	0,18	0,19	0,20

Source: Company data, UBI Banca estimates

Ratios (ex treasury shs), priced on 18-03-20

	2019A*	2020E	2021E	2022E
P/E (x)	13,4	11,9	10,5	9,8
P/BV (x)	1,6	1,2	1,2	1,2
TCR (%)	25,8%	26,3%	26,1%	25,7%
CET1 ratio (%)	25,8%	26,3%	26,1%	25,7%
Dividend yield (%)	6,7%	8,5%	9,0%	9,4%
Payout ratio (%)	90,5%	101,0%	94,5%	92,7%
Net Inc./Sales (%)	16,4%	15,1%	16,5%	16,8%

*Source: Company data, UBI Banca est. *Based on 2019 avg*

Key Financials

(EURm)	2019A	2020E	2021E	2022E
Revenues	58,3	53,5	55,3	58,5
Profit Before Taxes	13,7	11,7	13,2	14,2
Net profit	9,5	8,1	9,1	9,8
Net Profit - Adjusted	9,5	8,1	9,1	9,8
Shareholders' Equity	80,1	79,6	80,5	81,7
RWA	220,9	219,7	227,6	237,7

Source: Company data, UBI Banca estimates

Key Profitability Drivers

(%)	2019A	2020E	2021E	2022E
RoE	11,9%	10,2%	11,3%	12,0%
RoTE	17,2%	14,4%	16,2%	17,2%
Cost/Income	76,4%	78,1%	76,1%	75,7%
Comp/Revenues	46,5%	45,5%	44,4%	45,2%

Source: Company data, UBI Banca estimates

Key Valuation Ratios

(x)	2019A*	2020E	2021E	2022E
P/E (x)	13,4	11,9	10,5	9,8
P/E Adjusted (x)	13,4	11,9	10,5	9,8
P/BV (x)	1,6	1,2	1,2	1,2
P/TBV (x)	2,0	1,5	1,5	1,5
Dividend Yield (%)	6,7%	8,5%	9,0%	9,4%
RoE/CoE (x)	1,59	1,36	1,51	1,60

Source: Company data, UBI Banca estimates ** Based on 2019 average price*

Growth Rates

(%)	2019A	2020E	2021E	2022E
Revenues	-2,4%	-8,3%	3,3%	5,7%
Profit Before Taxes	-11,9%	-14,6%	12,7%	7,3%
Net Income	-13,5%	-15,1%	12,7%	7,3%
Net Income Adjusted	-20,1%	-15,1%	12,7%	7,3%

Source: Company data, UBI Banca estimates

Recent developments

> **4Q19 was 55% above our estimates**. Revenues surprised and were 40% above our estimates with the bulk of the surprise coming from IB and AAM while Global markets were broadly aligned. The IB surprise came despite the overall market volumes were down (M&A -27%, ECM -32% and DCM -4%) with deals spread across all three markets. AAM benefited from EUR3.7 million performance fees, which we never include in our estimates, which are eventually booked in 4Q. Even net of that, and adjusting for the SPAC m-t-m, revenues would have doubled YoY. Global market revenues were stable YoY as the net effect of different trends: retail volumes up, institutional we believe slightly down, client driven up and directional trading down. The usual tight control on costs (comp/revenues at 46% in FY2019 and average fixed compensation at EUR119K) translated into EUR1.4 million surprise at net income level which managed to grow 60.9% YoY.

> **Dividend proposed is EUR0.19 per share, in line with the EUR0.18/0.20 guidance**. The overall dividend amounts to EUR8.6 million and could have been in the high-end of the guidance but, we believe, the current market turmoil pushed management to stay a little bit more cautious. Considering the EUR2,12 price the dividend proposed implies a 9% yield.

Figure 1 - 4Q19 and FY19 results

(EURm)	4Q18A	4Q19A	YoY chg.	4Q19E	A/E change	FY18A	FY19A	YoY chg.
Global Markets	7,1	7,1	-1,0%	7,8	-10,1%	30,0	31,5	5,1%
Inv Banking	3,7	7,8	112,1%	4,7	64,0%	26,1	18,2	-30,4%
AAM	0,5	5,5	976,4%	1,9	188,2%	3,7	8,6	133,6%
Net Revenues	**11,3**	**20,4**	**80,1%**	**14,5**	**40,4%**	**59,8**	**58,3**	**-2,4%**
Personnel Costs	4,6	9,7		6,8		27,4	27,1	
Administrative expenses	3,9	5,0		4,1		16,8	17,5	
Profit before Taxes	2,8	5,6	98,4%	3,6	54,4%	15,6	13,7	-11,9%
Group Net profit	**1,90**	**3,93**	**107,0%**	**2,52**	**56,4%**	**11,03**	**9,54**	**-13,5%**
margin %	16,8%	19,3%		17,3%		18,4%	16,4%	
Group Net profit Adj.	2,42	3,93	62,2%	2,52	56,4%	11,95	9,54	-20,1%
margin %	21,4%	19,3%		17,3%		20,0%	16,4%	
Group Net Equity	**80,1**	**80,1**	**0,0%**	**73,8**	**8,5%**	**80,1**	**80,1**	**0,0%**

Source: Company data, UBI Banca estimates

Financial Projections

> **Scenario-playing could help in such turbulent times.** Comparing it with past infections (SARS, MERS, Swine flu, seasonal flu, Ebola, Spanish flu and bird flue) it seems that COVID-19 sits in the middle in terms of mortality rates (SARS and MERS the worst) and number of total cases (seasonal flue and Swine flue the worst). However, the reality of it is that data on COVID-19 are not yet clear. We believe that this low visibility is what is impacting markets the most. The infection that impacted the most, in terms of GDP, was the swine flu with US GDP declining for two quarters in a row (-4.4% and -0.6% followed by a +1.5%). The one that impacted the most the stock market was MERS (-12% decline for the S&P from peaks). In terms of stock market reaction we are past that point with the S&P 500 down almost 40% from peaks. The market is pricing a shock in between a temporary sanitary risk and a financial crisis (close to 2009 when the S&P 500 wasdown almost 80%). We therefore worked out two scenarios: the worst case one that assumes a prolongued recession and our base case where the GDP impact is strong in 1Q20 and 2Q20 and than is followed by a rebound in 3Q20 and a normalization in 4Q20 ending the entire year in negative territory. This to help investor traveling the EPS and fair value assumptions on the stock.

> **Prolonged recession scenario: our worst case.** We assumed: a) traded volumes on the equities, fixed income and derivatives market down 15% YoY (after the 2019 decline) for both 2020 and 2021. This is the combined effect of positive volumes in 2020 due to the sell-off (although local brokers tipically intercept only a part of those huge flows) but with lower prices per share. Proprietary trading should decline while client-driven trading to remain positive; b) IB revenues to decline 10% each year in 2020 and 2021 due to the decline in IPO fees and the halt that the M&A market reports in moment of high volatility. Minorities take-out and capital increases could partially compensate for that once the volatility stabilizes; c) some outflows in the AAM (with the notable exception of private debt), asset decline due to performances and no performance fees. Management would balance by freezing any hiring, reducing the variable compensation and optimize the cost base so to manage the total cost/income. To preserve capital, but also taking into account to the solid capital ratios, the dividend could be reduced and touch a bottom of EUR0.15 in 2020 and than stable in 2021. All in all, the 2020 EPS could be in the EUR0.15 and EUR0.16 in 2021.

> **V-Shape rebound: our base case.** We assumed: a) traded volumes on the equities, fixed income and derivatives market down 20% YoY in the remaining 9 months of 2020 as the combined effect of flat to +10% volumes growth and 20/30% price declines. This, coupled with the +30% Borsa Italiana reported in Jan/Feb 2020 should imply an overall flat traded countervalue in 2020 (which comes after a 11% decline in 2019 and a 24% decline in 2018) for both 2020 and 2021. Our expectations of flat/slightly positive volumes in 2020 has to due with the sell-off (although local brokers tipically intercept only a part of those huge flows). Last but not least, our estimates incorporates also the retail hub, which tipically is less volatile (which, in current conditions, means more resilient). Proprietary trading should decline while client-driven trading should remain positive; b) IB revenues to decline 10% in 2020 and back to growth (5%) in 2021 due to the decline in IPO fees and the halt that the M&A market reports in moment of high volatility. Minorities take-out and capital increases could partially compensate for that once the volatility stabilizes. In our talks with the company, management stressed that the pipeline is of good quality (i.e. M&A driven and less financials market related); c) no outflows in the AAM (with the

notable exception of private debt that should continue to raise and deploy), asset decline due to performances and no performance fees. Management would balance by freezing any hiring, reducing the variable compensation and optimize the cost base so to manage the total cost/income. To preserve capital, but also taking into account to the solid capital ratios, the dividend could be reduced and touch a bottom of EUR0.18 in 2020 and than back to EUR0.19 in 2021 and EUR0.20 in 2022. All in all, the 2020 EPS could be in the EUR0.18 and EUR0.20 in 2021 and EUR0.22 in 2022.

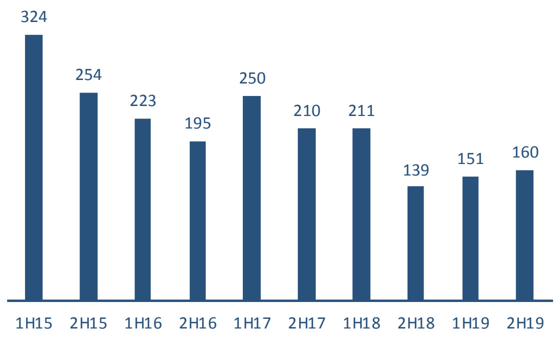
> **Our new 2020-21 estimates: 21.1% cut.** The V-shape recovery scenario is the base for our new 2020-21 estimates. In this report we are also introducing our 2022 estimates. In the outlook statement management points out that, YTD, revenues and profits are up in all divisions (with the exception of directional proprietary trading) and this is coherent with the traded countervalues disclosed by Borsa Italiana for Jan/Feb. While management says it is not in the position to assess the precise impact of the COVID-19 on its business, it stresses that the company is fully operational and mentions the cost-flexibility on which Equita business model is based.

Figure 2 - Old vs. new estimates

	2018	2019		2020E			2021E		
(EURm)	**Actual**	**Actual**	**% diff.**	**Old**	**New**	**% diff.**	**Old**	**New**	**% diff.**
Revenues	59,8	58,3	-2,4%	57,6	53,5	-7,0%	61,7	55,3	-10,5%
Profit before taxes	15,6	13,7	-11,9%	14,8	11,7	-20,8%	16,9	13,2	-21,5%
Profit before taxes %	26,1%	23,6%		25,7%	21,9%		27,3%	23,9%	
Net profit	11,0	9,5	-13,4%	10,3	8,1	-21,3%	11,7	9,1	-22,1%
Net profit adjusted	12,0	9,5	-20,1%	10,3	8,1	-21,3%	11,7	9,1	-22,1%

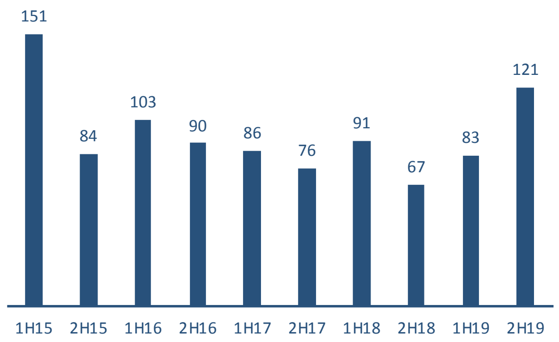
Source: UBI Banca estimates

Figure 3 - MTA traded volumes by semester (EURbn)



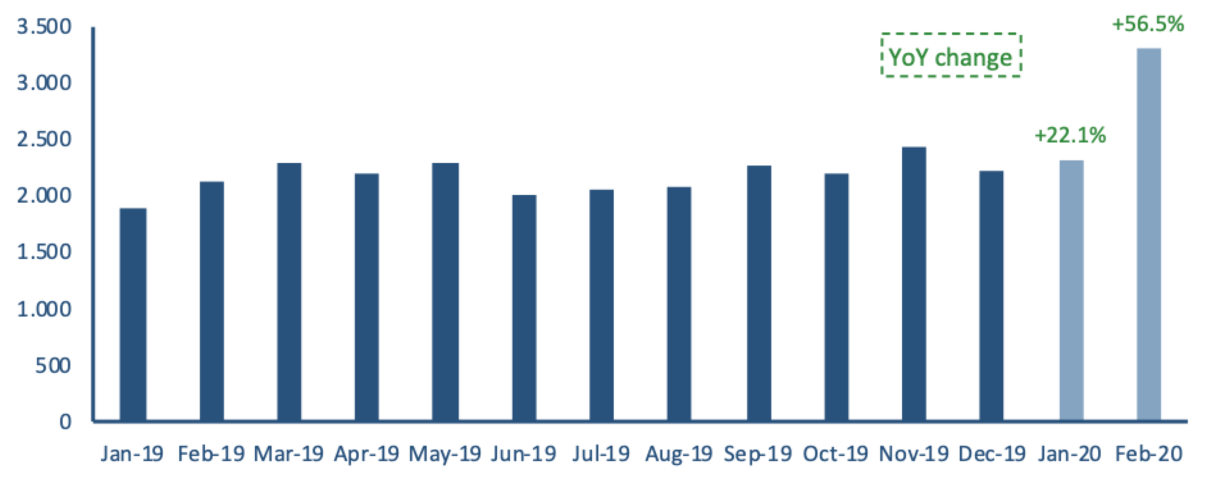
Source: Assosim

Figure 4 - Bond traded volumes by semester (EURbn)



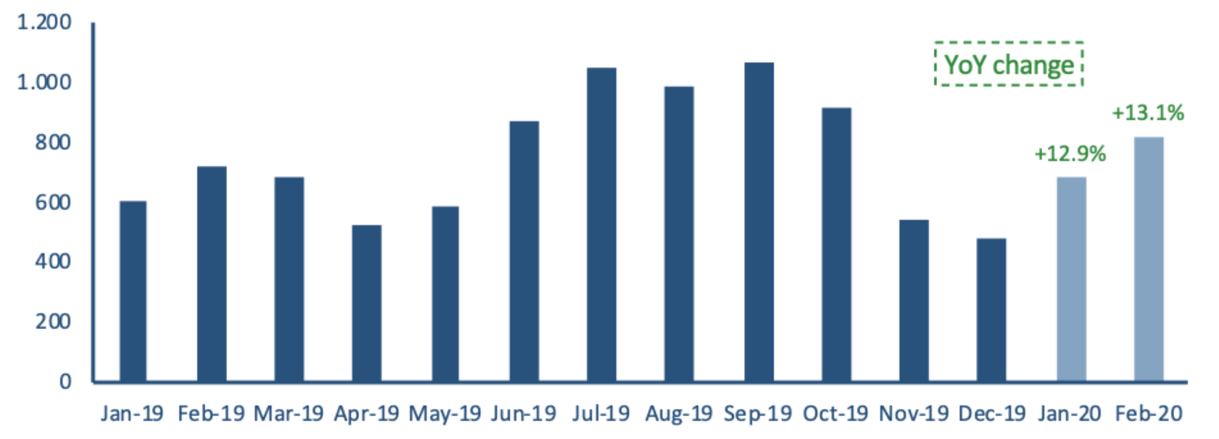
Source: Assosim

Figure 5 - Average daily trading volumes on MTA (EURm)



Source: Borsa Italiana

Figure 6 - Average daily trading volumes for fixed income (EURm)



Source: Borsa Italiana

Valuation

> **Revising the target price to EUR2.57 (from EUR3.37).** This is the result of a) the cut in estimates (-21.1% on average in 2020-21 at net income level); b) the substitution of the peer group valuation method with the DDM. Peers multiples in this moment reflect the price decline but not the (very likely) estimates cut. Temporarily we are replacing the peers group comparison with a DDM (EUR0.19, growing at 0.5% and with a CoE of 8.0%). A peer group comparison would have resulted in a EUR2.34 fair value and would have reduced the overall TP by 4% (considering it is weighted at 50%), therefore not massively. Still we believe that it is fair to take peers multiples with some cautiousness right now; c) the increase to 3.0% (from 2.5%) of the free-risk assumed in our models.

> **In the prolongued recession scenario the fair value would be close to the current share price.** With a 2020-21 EPS estimates which would be around 15-20% lower than our current estimates, and assuming peers multiples have already de-rated, the fair value would be around EUR2.18 in the worst case scenario.

> **Capital strength and flexible costs structure** vs. Italian exposure and stock liquidity. We have gone already through turbulent times in the past and we know that investors would look for solidity, no cash requirements, flexibility to adapt to changing scenarios, solid management teams and committed shareholders. Instead, investors would be wary of low revenues diversification (by country and by business) and small caps. Equita ranks very well in the majority of those features but we cannot hide that its revenues are significantly related to Italy and that it is a small cap. We believe this is already reflected in the share price and, after the recent fall, we see valuation as a protection to the downside. Furthermore, in the current market environment, Equita itself could take some opportunity with bolt-on M&A, which were probably prevented only some months ago. We therefore reiterate our Buy rating on the name.

Figure 7 - Valuation summary

(EUR)	New	Old	% difference
P/BV	2,72	3,13	-13%
DDM (new) or Peers (old)	2,55	3,60	-29%
Average	**2,57**	**3,37**	**-24%**

Source: Company data, UBI Banca estimates

Figure 8 - Peer based valuation

(EUR, x)	2020E
PE	10,9
Equita EPS	0,18
Equita fair value - A	1,94
Treasury shares - B	0,21
Equity co-invested - C	0,24
Pension liabilities - D	-0,05
Equita Equity Value (A+B+C-D)	**2,34**

Source: Company data, UBI Banca estimates

Figure 9 - Peer Group multiples (priced on 18 March 2020)

Name	TIER	Price	Currency	Mkt Cap	P/Sales			P/E			P/BV			Div Yield		
				million	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
Piper Jaffray	I	31,6	USD	454	1,4 x	0,4 x	0,4 x	4,8	4,6	4,4	0,7 x	0,5 x	0,5 x	4,3%	4,7%	5,3%
Numis Corp	I	1,8	GBP	193	2,9 x	0,9 x		18,9	17,6		1,2 x	1,2 x		7,8%	7,2%	
Evli Pankki Oyj	I	7,1	EUR	170	3,3 x	2,2 x	2,1 x	9,9	10,5	8,5	2,1 x	2,1 x	2,0 x	9,3%	9,6%	11,3%
Moelis	II	22,0	USD	1.454	2,6 x	1,7 x	1,6 x	12,3	9,0	8,4	4,1 x	4,6 x	4,7 x	8,8%	12,5%	11,9%
Evercore	II	33,0	USD	1.342	1,4 x	0,7 x	0,7 x	4,7	4,3	4,1	1,6 x	1,3 x	1,0 x	6,3%	7,0%	7,7%
Houlihan Lokey	II	42,8	USD	2.781	2,7 x	2,4 x	2,3 x	14,9	13,9	13,1	3,1 x	2,8 x	2,4 x	2,7%	2,9%	3,1%
DeA Capital	II	1,0	EUR	263	5,5 x	3,7 x		21,0	24,1		0,6 x	0,6 x		12,1%	11,1%	
Tikehau Capital	II	17,5	EUR	2.385	7,1 x	5,4 x	4,1 x	13,3	14,0	9,5	0,7 x	0,8 x	0,7 x	3,6%	2,7%	4,1%
Azimut	II	11,0	EUR	1.603	3,0 x	1,7 x	1,6 x	4,9	6,9	6,5	2,0 x	1,8 x	1,7 x	10,0%	10,5%	11,0%
Average					**2,9 x**	**1,7 x**	**1,6 x**	**12,3 x**	**10,5 x**	**8,4 x**	**1,6 x**	**1,3 x**	**1,7 x**	**7,2%**	**7,6%**	**7,8%**
Equita Group		**2.1**	**EUR**	**128**	**2.2 x**	**1.8 x**	**1.7 x**	**13.4 x**	**11.9 x**	**10.5 x**	**1.6 x**	**1.2 x**	**1.2 x**	**6.7%**	**8.5%**	**9.0%**
Tier I					2,5 x	1,2 x	1,2 x	11,2 x	10,9 x	6,4 x	1,3 x	1,3 x	1,3 x	7,1%	7,1%	8,3%
Tier II					3,7 x	2,6 x	2,1 x	11,9 x	12,0 x	8,3 x	2,0 x	2,0 x	2,1 x	7,2%	7,8%	7,6%

Source: FactSet

Income Statement

(EURm)	2019A	2020E	2021E	2022E
Global Markets	31,5	30,9	30,9	30,9
Investment Banking	18,2	16,4	17,2	19,7
Alternative Asset Management	8,6	6,3	7,3	7,8
Net Revenues	58,3	53,5	55,3	58,5
Personnel Costs	27,1	24,4	24,5	26,4
Administrative Expenses	17,5	17,4	17,5	17,8
Profit Before Taxes	13,7	11,7	13,2	14,2
% on Net Revenues	23,6%	21,9%	23,9%	24,3%
Income Taxes	4,2	3,6	4,1	4,4
Group Net Profit	9,5	8,1	9,1	9,8
Non-recurring	0,0	0,0	0,0	0,0
Group Net Profit - Adjusted	9,5	8,1	9,1	9,8

Source: Company data, UBI Banca estimates

Balance Sheet

(EURm)	2019A	2020E	2021E	2022E
Financial Assets at FV through P&L	59,1	61,3	63,6	66,0
Financial Assets at Amortised Cost	225,5	232,8	242,0	251,9
Equity Investments	1,5	1,5	1,5	1,5
Tangible Assets	0,6	0,6	0,6	0,6
Intangible Assets	15,0	15,0	15,0	15,0
Tax Assets	3,9	3,9	3,9	3,9
Other Assets	1,7	1,7	1,7	1,7
Total Assets	307,4	316,9	328,4	340,7
Financial Liabilities at Amort. Cost	194,0	203,7	213,9	224,6
Financial Liabilities Held for Trad.	8,1	8,4	8,8	9,2
Tax Liabilities	2,0	2,0	2,0	2,0
Other Liabilities	14,5	14,5	14,5	14,5
Employees' Termination Indemnities	2,4	2,4	2,4	2,4
Allowances for Risks and Charges	6,2	6,2	6,2	6,2
Equity	80,1	79,6	80,5	81,7
Total Liabilities and Equity	307,4	316,9	328,4	340,7

Source: Company data, UBI Banca estimates

Financial Ratios

(%)	2019A	2020E	2021E	2022E
TCR	25,8%	26,3%	26,1%	25,7%
CET1 ratio	25,8%	26,3%	26,1%	25,7%
RoE	11,9%	10,2%	11,3%	12,0%
RoTE	17,2%	14,4%	16,2%	17,2%
Cost/Income	76,4%	78,1%	76,1%	75,7%
Comp/Revenues	46,5%	45,5%	44,4%	45,2%
Payout	90,5%	101,0%	94,5%	92,7%

Source: Company data, UBI Banca estimates

Per Share Data

(EUR)	2019A	2020E	2021E	2022E
EPS - reported	0,21	0,18	0,20	0,22
EPS - adjusted	0,21	0,18	0,20	0,22
DPS	0,19	0,18	0,19	0,20
BVPS - ex-treasury	1,76	1,75	1,77	1,80
TBVPS - ex treasury	1,43	1,43	1,42	1,44

Source: Company data, UBI Banca estimates

Stock Market Ratios

(X)	2019A *	2020E	2021E	2022E
P/E	13,4	11,9	10,5	9,8
P/E Adjusted	13,4	11,9	10,5	9,8
P/BV	1,6	1,2	1,2	1,2
P/TBV	2,0	1,5	1,5	1,5
Dividend Yield (%)	6,7%	8,5%	9,0%	9,4%
RoE/CoE	1,6	1,4	1,5	1,6

Source: Company data, UBI Banca estimates ** Based on 2019 average price*

Growth rates

(%)	2019A	2020E	2021E	2022E
Revenues	-2,4%	-8,3%	3,3%	5,7%
Profit Before Taxes	-11,9%	-14,6%	12,7%	7,3%
Net Income	-13,5%	-15,1%	12,7%	7,3%
Net Income Adjusted	-20,1%	-15,1%	12,7%	7,3%

Source: Company data, UBI Banca estimates

Disclaimer

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Hold: if the target price is 15% below or 15% above the market price, over the next 12 months.

Sell: if the target price is 15% lower than the market price, over the next 12 months.

No Rating: the investment rating and target price have been suspended as there is not sufficient fundamental basis for determining an investment rating or target. The previous investment rating and target price, if any, are no longer in effect. Alternatively, No Rating is assigned in certain circumstances when UBI Banca is acting in any advisory capacity in a strategic transaction involving the Company.

Target price: the market price that the analyst believes that the share may reach within a one-year time horizon.

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Distribution of ratings

Equity rating dispersion in the past 12 months

Buy	***Hold***	***Sell***	***No Rating***
84.6%	*9.2%*	*3.1%*	*3.1%*

Proportion on issuers to which UBI Banca has supplied investment banking services relating to the last 12 months

Buy	***Hold***	***Sell***	***No Rating***
74.5%	*16.7%*	*100%*	*100%*

For further information regarding yearly and quarterly rating statistics and descriptions, please refer to www.ubibanca.com/equity-research.

Historical ratings and target prices

Date	Rating	Target Price (EUR)	Market Price (EUR)
9 May 2019	BUY	3.57	3.02
12 September 2019	BUY	3.50	2.68
18 November 2019	BUY	3.37	2.60