Italy

Referendum: limited consequences for banks

- **Expectations of the referendum's outcome prevented the markets from over-reacting.**
- **Banking stocks fell mildly immediately following the referendum, but rebounded again until 8 December 2016.**
- **The referendum's outcome does not seem to have altered the chances of success of Monte dei Paschi di Siena's recovery plan.**
- **Sovereign yield spreads did not widen very much thanks to the ECB's ongoing intervention.**

On 4 December 2016, Italians voted massively against the constitutional reform to end Italy's perfect bicameralism. The markets largely anticipated this popular rejection of Matteo Renzi's policies, who handed in his resignation to Italy's president after the definitive 2017 budget was adopted.

After falling 0.21% on the day after the referendum, the Milan Stock Exchange reversed course and gained 4.15% on day two. The main banking stocks amplified these overall trends. UniCredit's share price fell 3.36% on 5 December, but regained 12.81% on 6 December, and continued to rise in the two days thereafter (+9.42% and +2.98%). The 9 December 2016 session appears to have ended the rally. The referendum's outcome does not seem to have significantly deteriorated expectations concerning the banking sector.

Monte dei Paschi di Siena (MPS) was slightly sanctioned. Its share price regained only 1.18% on 6 December after plunging 4.21% the previous day. Yet MPS shares continued to rebound over the next two days (+10.79% and +4.11%). Market expectations do not seem to have changed significantly concerning the chances of success of the bank's recovery plan. Between 28 November and 2 December, the plan managed to generate EUR 1 bn in additional equity. This was achieved through the voluntary conversion of bonds at nominal value into new shares with a maximum price set at EUR 24.90. The recovery plan also intends to raise an extra EUR 4 bn in new equity. This could include EUR 1 bn provided by one or more anchor investors. The bank still intends to sell off EUR 27.7 bn in securitised

Banking stocks are trending upwards

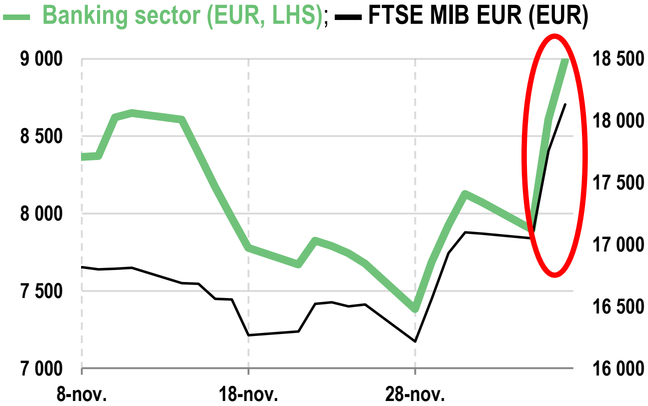

Chart Source: Macrobond

non-performing loans in the near future. The Italian government has already implemented structural reforms that should help the banks clean up their balance sheets. Remaining cautious, the Italian government might also be in negotiations with the European Commission and MPS concerning a preventative support. Even so, the bank requested additional time to carry through its recapitalisation plan from the ECB which rejected it.

Between 2 and 5 December 2016, the spreads on 10-year sovereign bond yields widened very slightly (from 172 basis points to 177 bp against the Bund), a limited move contained by the ECB's ongoing intervention. Volatility – a reflection of uncertainty – did not increase very much either. The market does not seem to be calling into question yet the future transition government's capacity to carry through structural reforms.

Although it is still worth being cautious, the referendum's outcome could have minor implications on the fate of Italian banks. In the days ahead, new factors will be released concerning the terms of the recovery plans and their chances of success.