BANCA D'ITALIA
EUROSISTEMA

Address by the Governor

Ordinary General Meeting of Shareholders
Rome, 31 March 2022

128th FINANCIAL YEAR

2021

Financial Year 128th

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Ladies and Gentlemen,

Today's General Meeting of Shareholders is being held at a time of great uncertainty for the world economy, due to the turmoil of the last fifteen years caused first by the global financial crisis, quickly followed by the euro-area sovereign debt crisis, and then the pandemic we have faced over the last two years.

Serious geopolitical tensions now threaten peace in Europe and in the world at large.

The Russian invasion of Ukraine, aside from the suffering, violence and destruction it has already wrought, is sure to inflict deep societal and economic wounds. It is proving to be a dramatic disruption to the process of international economic and financial integration which, if not speedily resolved in a peaceful way, could have severe repercussions on Europe's energy supply, on inflation, on domestic demand and on international trade. And, not least, on the time line for achieving energy transition.

The Governing Council of the European Central Bank (ECB) is closely monitoring the evolving situation, aware of the problems in ensuring at such a difficult time that the financial market functions properly and monetary policy impulses are transmitted in an orderly fashion, and stands ready to implement the sanctions decided by the European Union and the international community.

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The composition of the Governing Board has changed as follows: after Daniele Franco's appointment as Minister of Economy and Finance and Luigi Federico Signorini was made Senior Deputy Governor, Paolo Angelini, previously Director General for Financial Supervision and Regulation, was appointed Deputy Governor on 15 April 2021.

After two years of being unable to attend in person, most of the Board of Directors is also here today, with some changes in its composition: the Shareholders elected Renata Codello in the Venice branch and

Salvatore Di Vitale in the Palermo branch in 2020, and Mirella Bompadre in the Bologna branch and Francesca Cozzani in the Genoa branch in 2021.

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The impact of the Eurosystem's monetary policy on the Bank of Italy's annual accounts

In 2021, the Governing Council of the ECB maintained a very accommodative monetary policy stance, confirming the package of extraordinary measures previously adopted to provide liquidity and to safeguard the smooth transmission of monetary policy throughout all the euro-area economies.

The Eurosystem continued to provide abundant liquidity to credit institutions through the third programme of targeted longer-term refinancing operations (TLTRO3) to support the flow of credit to households and firms. At the end of 2021, they had reached a volume of almost €2,200 billion (around €450 billion requested by Italian banks). The banking counterparties benefited from especially favourable financing conditions for all of 2021.

The net purchases under the pandemic emergency purchase programme (PEPP), which continued throughout 2021, end today. The reinvestment of principal payments from maturing securities will continue at least until the end of 2024.

The net purchases under the asset purchase programme (APP) continued through all of 2021 and in the first quarter of 2022 at a monthly pace of €20 billion. As decided at its 10 March meeting, net purchases will rise to €40 billion in April, will then be cut back to €30 billion in May and then go back to €20 billion in June. The calibration of net purchases for the third quarter will be guided by the evolving assessment of the medium-term inflation outlook. The principal payments from maturing securities will be reinvested for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

Any adjustments to the key ECB interest rates will take place some time after the end of the net purchases under the APP and will be gradual.

The monetary policy measures adopted by the Eurosystem to address the economic fallout of the pandemic – which I have already summarized – are reflected in the Annual Accounts submitted today for your approval.

Assets, which rose by €242 billion over the previous year, exceeded €1,500 billion, an unprecedented amount. In the last two years, the total balance sheet has expanded by 60 per cent, mainly due to the effect of securities purchased for monetary policy purposes and to the increase in longer-term refinancing operations.

The Bank's profitability has remained high, although it has fallen for the second straight year. As in the year before, the positive impact on income of the expansion in asset holdings was more than offset by the impact of lower yields. The gross profit, before tax and transfers to the general risk provision, nevertheless remains above €9 billion, €1 billion lower than last year; the net profit fell slightly, from €6.3 billion to €5.9 billion.

The balance sheet

At the end of 2021, the Bank of Italy's total assets amounted to €1,538 billion.

Assets continued to largely consist of securities purchased for monetary policy purposes, equal to €666 billion (of which almost €600 billion in Italian government securities), up €127 billion compared with the end of 2020. Refinancing operations equalled €453 billion, an increase of €79 billion, due exclusively to the higher amounts allotted through TLTRO3. Overall, monetary policy assets amounted to 73 per cent of the total balance sheet.

Foreign currency assets, amounting to €76 billion at the end of 2021, rose by €24 billion during the year, mainly owing to the recent allocation of special drawing rights by the International Monetary Fund, carried out to increase the funding available to handle the pandemic crisis, especially for the weakest economies. A liability with respect to the IMF was recorded for an amount equal to the SDRs allocated to Italy. The value of the gold reserves increased by about €5 billion, to stand at €127 billion. In line with Eurosystem accounting rules, this appreciation is recorded in the revaluation account on the liability side and does not contribute to the Bank's net profit. The value of the gold reserves increased further in the first quarter of 2022, exceeding €145 billion in March.

Investment assets other than those held for monetary policy purposes rose by €2 billion, to just over €150 billion; of these, 83 per cent are public sector securities, 13 per cent are equity and investment fund shares, and the remaining 4 per cent are other financial assets.

In recent years, the Bank of Italy has incorporated environmental, social and governance (ESG) profiles into its investment decisions, in line with its long-term investor profile, mindful of society and the environment and of safeguarding against the financial and reputational risks associated with sustainability factors. The Bank's sustainable investment policy is set out in the Responsible Investment Charter, published in 2021. It sets out the Bank's vision of sustainability and includes the principles and the reference criteria underlying the sustainable management of its financial investments and currency reserves, outlining the precise commitments for a model of sustainable economic growth.

On the liability side, the deposits of credit institutions rose by €107 billion to €406 billion, four times more than immediately prior to the pandemic, due to the enormous injection of liquidity by the Eurosystem. The Bank of Italy's negative balance on the TARGET2 European payment system rose by €74 billion, reaching €590 billion, mainly owing to investments in foreign securities by residents and to sizeable net redemptions of Treasury bonds in the fourth quarter. In December, it was also affected by the drop in resident banks' net funding abroad. The liability fell in the first quarter of 2022, averaging €575 billion in March.

The total value of banknotes in circulation, which are allocated within the Eurosystem according to the ECB capital key, increased by €17 billion, arriving at a total of €241 billion at year-end.

Profitability, risks and organizational measures

The gross profit for 2021, before tax and transfers to the general risk provision, was equal to €9.2 billion, €1 billion lower than in 2020.

Some €0.5 billion of the decline is attributable to net interest income. Specifically, the decrease was caused by higher interest expense on longer-time refinancing operations and the decline in yields on securities denominated in euros and in foreign currency; this was partially offset by higher interest income on securities held for monetary policy purposes, driven by the increase in such holdings. Some €0.8 billion of this decrease is also due to the net result from financial operations, which had benefited in 2020 from significant gains realized thanks to the sale of equity instruments and fund shares.

In order to continue with the strengthening of the Bank's financial buffers, given the continuous and sizeable growth in the size of its balance sheet and its overall risk exposure, transfers to the provision for general risks amounted to €2 billion (€2.5 billion in 2020). Taxes for the year amount to about €1.2 billion, just under the €1.4 billion posted in 2020.

Operating expenses are broadly stable. While the extraordinary charitable donations linked to the pandemic emergency and the severance payments during the year have decreased, the provision for pensions and severance payments and expenditure on property maintenance have increased.

In 2021, the Bank of Italy again promptly adapted the organization of work based on the course of the pandemic and made ample use of remote working to cope with the emergency.

The project launched in 2020 to define a new work organization model led to the signing of an agreement with the trade unions in December 2021 to introduce a new hybrid work model, in which on-site working will be appropriately integrated with remote working. The new system, which will be fully operational from 1 April, is a strategic opportunity for the Bank to transform its organization. By means of an extensive use of technology and by streamlining processes, the model ensures high-quality services for the public, guarantees protection against risks, and reduces the Bank's costs and its ecological footprint, thereby encouraging a better work-life balance for its employees.

From an organizational point of view, there has been a reform of the Directorate General for Planning, Organization and Accounting that – by making the best use of functional interdependencies and an integrated management of data bases – will make it possible to enhance the Bank's management control and the monitoring of its quality and efficiency.

Additional initiatives are under way to strengthen the role of the Bank's centre for innovation (Milano Hub) in encouraging the adoption of digital technologies by Italy's financial market. There have also been interventions designed to improve the organizational safeguards to combat the counterfeiting of banknotes and cyber threats. The treasury services that the Bank's branches formerly performed on behalf of the government were transferred to the head office, thereby further rationalizing work processes. This reform, which was made possible by the progress made in recent years in digitalizing procedures, will foster the overall efficiency of the system.

As usual, further information on the activities of the Bank and on the organizational and management measures implemented in 2021 is available in the Report on Operations and Activities of the Bank of Italy, which will be published in May, on the occasion of the presentation of the Annual Report. More information on the Bank's commitment to the issue of environmental sustainability is in the annual Environment Report, available on the Bank's website and updated every year. In addition, the first report on sustainable investment and climate-related risk will be published in the next few months, containing the results achieved and the methodologies applied.

Proposal for the allocation of the net profit

Dear Shareholders,

Pursuant to Article 38 of the Statute, acting on a proposal of the Governing Board and after hearing the opinion of the Board of Auditors, I present for your approval the Board of Directors' proposal for the allocation of the net profit.

Under the current dividend policy, the amount paid to the Shareholders is kept within a range of €340 million to €380 million, provided that the net profit is sufficient and without prejudice to the Bank's capital adequacy. The difference between the upper limit of the range and the dividend paid to the shareholders may be allocated to the special item for stabilizing dividends, until such item reaches a maximum amount of €450 million.

Accordingly, from the net profit of €5.945 million, we propose allocating €340 million as a dividend to the shareholders, equal to 4.5 per cent of the capital, the same amount allocated in each of the last few years. As already noted during the Extraordinary Meeting of the Shareholders, there are no shares exceeding the 5 per cent threshold for which the corresponding dividend is allocated to the Bank's statutory reserves; therefore, the sum allocated is paid fully to the Shareholders.

We therefore propose allocating €40 million to the special item for stabilizing dividends, which would then amount to €240 million.

As a result, the remaining profit for the State would be equal to €5,565 million which, in addition to taxes for the year amounting to €1,236 million, would bring the total amount allocated to the State to around €6,801 billion. Over the last five years, the total amount allocated to the State comes to €28.5 billion, in addition to taxes amounting to €6.3 billion.

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