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The Bancassurance Model:

Analysis of the Intesa – Generali case

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Academic Year 2016 / 2017

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Introduction

At the beginning of 2017, in Italy, there was an attempt to merge two giants of their own respective sectors, the banking and the insurance ones. The subjects involved were respectively Banca Intesa Sanpaolo and Assicurazioni Generali, where the first was interested in acquiring the second. This fact made me think about how can two different sectors like these come together into a unique entity.

The first chapter of this thesis is about mergers and acquisitions in general. I start by describing what they are and the possible reasons behind a takeover. The main objective is to create value, and we will see how this can be done. Subsequently, I focused on hostile mergers and acquisitions, since the attempt of takeover considered here was likely to be a hostile one. In this part, I describe the process of a takeover and analyse the pros and cons of acquiring a target hostilely. The analysis also explores the main defensive tactics that a target can implement to avoid a hostile takeover. Moreover, I go through some of the most relevant agency problems that can interfere in the decision-making process of the top management.

The second chapter is a description and analysis of the bancassurance model. It starts with a definition and introduction of the model, followed by the history of regulation in Europe and in the United States of America. I then go through the various types of structures that the bancassurance model can take: contractual agreement, joint venture, merger and acquisition. In the end, I also go through the distribution of insurance products, underlying the difference that exists between life and non-life insurance.

Once the topic has been introduced, the next step is the empirical analysis of the model. In order to understand if it is a valuable and profitable model, I have read and brought to you the results of various academic researches and papers. The analysis is based on econometric models that try to understand the relationship between different variables and value creation in bancassurance mergers. The variables analysed include: economies of scale, economies of scope, profitability, governance and geographic diversification. I describe which variables affect value post-merger and to what extent, positively or negatively. The chapter concludes with an analysis of the possible risks and returns of a bancassurance merger. From this, I can deduct if the bancassurance model is risky to be implemented and if there are possibilities of value extraction from a bancassurance merger.

The third and last chapter focuses on the case Intesa Sanpaolo – Assicurazioni Generali. I start by describing the structure, activities and the history of the two companies involved. I then illustrate what happened and what could have been other possible scenarios of the deal. In addition, I discuss what other defensive options would have been available to Assicurazioni Generali to defend itself from a possible hostile takeover. At this point, it is important to understand the rationale of the deal, why was Intesa interested in acquiring Generali? How could the two companies fit together?

Once the situation is clearly pictured, it is possible to match the results of the empirical analysis with the case. Here, I investigate if, from a theoretical point of view, the bancassurance model would have had the fundamentals to work successfully. I have taken all the statistically significant variables found in chapter two, and compared them with the case. Finally, I discuss the facts about the withdrawal and the possible reasons behind such decision, commenting Intesa's last press release on the case.

Chapter 1 – Mergers and Acquisitions

1.1 Definition and rationale behind M&As

First, we must define what do we mean by mergers and acquisitions, commonly called M&A transactions. The two terms are closely linked and for this reason are put together. As a matter of fact, both in case of a merger and that of an acquisition there is a buyer (acquirer) which purchases the stocks or assets of a seller (target). We can enclose this procedure under the umbrella term: *takeover*.[1]

Transactions can be: all-cash, stock for stock, or cash and stock. In the first case, the acquirer purchases the majority or totality of the target firm using only cash. This, opposed to the stock for stock transaction, is a taxable event. The equity value is simply the cash offer price per share times the target's outstanding shares. In the second case, acquirer and target firm exchange their shares, based on the offer price per share divided by the acquirer's share price. This ratio can be fixed or floating. The fixed exchange ratio sets the number of shares received by the acquirer and lets the offer price fluctuate with the acquirer's share price. On the other hand, the floating exchange rate, sets the offer price and lets the number of shares fluctuate with the acquirer's share price. At last, cash and stock transactions are a mix of the first two types of transactions. The target is paid with a fixed amount of cash plus a stock portion, which can be calculated with a fixed or floating exchange ratio.[2]

Damodaran (2008) classifies takeovers in five different ways. When a target firm ceases to exist, and becomes part of the acquiring firm, we call this a *merger*. *Consolidation*, instead, is when a new firm is created from the takeover and both parties receive stocks in the new firm. On the other hand, there are *tender offers*. These are when the acquirer communicates an offer price to the target's stockholders, which usually leads to a hostile takeover. Still, target entity continues to exist as long as there are stockholders who refuse the tender offer. Acquirer can also perform an *asset purchase*, where the assets are transferred to the buyer and the target gets eventually liquidated. Finally, a *buyout* is when a

[1] Berk J., De Marzo P., Corporate Finance (third edition) – ch. 28, p. 931, Pearson, 2014
[2] Rosenbaum J., Pearl J., Investment banking: valuation, leveraged buyouts, and mergers & acquisitions – ch. 1, Wiley, 2009

group of investors acquire the target (usually through a tender offer) which then becomes a privately-owned business. Usually, buyouts tend to be made using a high portion of debt, which allows the buyer to leverage the transaction. These are called Leveraged Buyouts (LBOs); their objective is to repay debt through the future cash flows of the target.

Now that we have understood *what* are we talking about, we must understand *why* a firm would want to pursue a takeover. The main scope, just as in any other project or investment, is *value creation*. It is in fact for this reason that, usually, target firms are paid at premium over their market price. This concept is called acquisition premium. In other words, the difference between the acquisition price and the market price of a target firm. Obviously, the acquirer believes that the value created from the takeover will be greater than the premium paid. It is estimated that, on average, out of all US deals between 1980 and 2005, the acquisition premium was 43% of the target's premerger price.[3]

So, how is it possible to create value greater than the sum of the parts? The answer is *synergy*. Literally, it is when two or more entities work together for the same scope and produce a greater output than they would have produced by their own. We can further distinguish between operating and financial synergies.

Speaking of operating synergies, Jensen and Ruback (1983) state that economies of scale bring about a potential saving in terms of production and distribution costs. In other words, a product has a fixed cost per unit, if the number of units produced increase, then this fixed per unit cost decreases and we obtain economies of scale.

On the other hand, the clearest example of financial synergy is increased debt capacity. Once a merger is completed, the resulting cash flows and earnings become more predictable. Therefore, the new entity will find easier access to credit than the two separate entities.[4] Nevertheless, Modigliani and Miller (1958) argue that the value of a firm is not affected by synergy or by its capital structure. Since the value of a company is, in theory, the sum of the NPVs (Net Present Values) of its projects and where the latter are calculated independently. Therefore, they conclude that a takeover does not affect the value of a firm.

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[3] Eckbo B. E., Handbook of Corporate Finance: Empirical Corporate Finance, Vol. 2 – Ch. 15, pp. 291–430, Elsevier, North-Holland, 2008

[4] Damodaran A., Acquisitions and Takeovers, Published in Handbook of finance - Investment Management and Financial Management, p.11, Hoboken, Wiley, 2008

Which means that synergy is not considered. However, the M-M model assumes perfect capital markets, which in the real world are very difficult (if not impossible) to find. For example, the increased debt capacity mentioned above would be useless if firms could easily access credit notwithstanding their capital structure.

Now the question is: how do we extract value from a takeover to achieve synergy? *Diversification* is beneficial to firms that wish to reduce their idiosyncratic risk. Just like investors diversify their portfolios, companies can acquire targets that operate in different sectors to spread the risk. However, Salter and Weinhold (1978) state that investors do not need a highly-diversified company, since they can easily diversify their portfolio. In fact, a diversified portfolio is much less costly to build than a diversified company. Nonetheless, Jaffe et al. (2002) write that a proper diversification can increase value more than the sum of the parts. This is made possible by the financial synergy created which, because of a reduced risk of corporate default, leads to an increase in debt capacity and thus an increase in value.

Another reason to pursue a takeover is *expertise*. A firm who is willing to attract qualified workers will find it easier to acquire an already functioning unit rather than searching for them in the labour market. Let's take, for example, "Facebook". Mark Zuckerberg said in an interview [5] that he doesn't buy companies "for the company", he buys them "to get excellent people". He believes that the secret for a successful takeover is to buy "great companies with great founders".

Leigh and North (1978) see takeovers as a rapid way to enter new markets and spread the *geographic reach* of a company. For a company to exploit existing human resources and networks of a foreign firm is usually simpler and more effective than creating ex-novo a subsidiary overseas. Moreover, they allow companies to gain *market power* and thus, higher profits and barriers to entry. However, as firms gain market power, the degree of competition decreases and the deadweight loss in terms of efficiency increases. For this reason, antitrust agencies intervene if they believe that competition is threatened by a takeover.

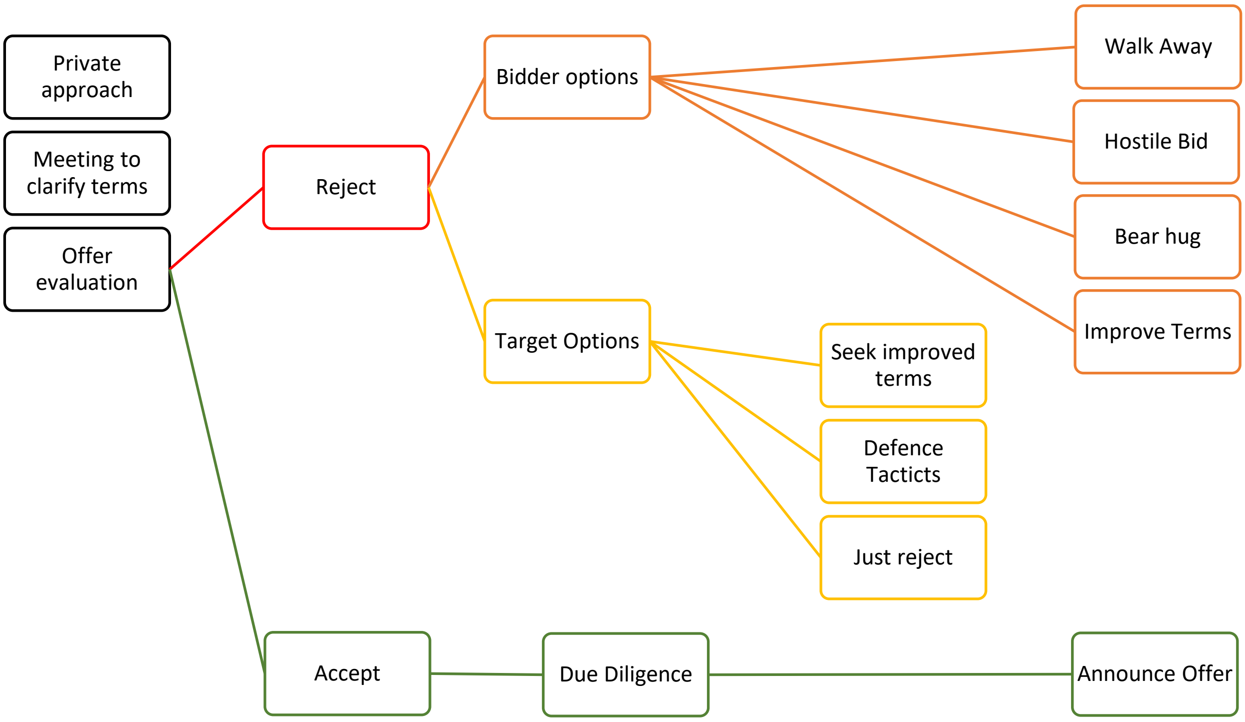
[5] Huffington Post, Mark Zuckerberg: 'We Buy Companies To Get Excellent People', 25 May 2011, Nathaniel C. Hindman

Efficiency is a very debated concept in economics. How can we define efficiency? Vilfredo Pareto defined his view of efficiency (optimality) as an economic situation in which resources are perfectly allocated and one party's situation cannot be improved to the detriment of the other party. In case of a takeover, this means that the management of the parent company believes that the target is not allocating its resources efficiently and thinks that under their control it will do so. It can also mean that there can be some cost synergies by cutting redundant departments.

Still, takeovers not always end well. Stallworthy and Kharbanda (1988) discovered that around one third of takeovers are sold within five years. The main reasoning is because of the clash of corporate cultures.

1.2 Hostile takeovers

Let us continue with a more in-depth description of the process of a takeover. It all starts with a private approach to the target board of directors. Subsequently, if the first impressions were good, there is a meeting which serves to clarify terms and conditions of the eventual takeover. Such as the deal structure, the type of financing and the future goals for the business. Once this is done, the board must evaluate the offer with the help of an



advisor. In case of acceptance, before a binding contract is made, both parties must perform a due diligence analysis. Namely, it is the care that a reasonable person would take before entering into an agreement or a financial transaction with another party. It is an investigation to check if the counterparty has its "papers in order". Due diligence is a risk management device and it can be done broadly or narrowly. In the first case, it is costlier but less risky. In the sense that the investigation is focused on analysing in depth the target to understand if it is an optimal target, so to have less surprises once the deal is done. On the other hand, narrow scope due diligence simply focuses on accounting and legal issues to close the deal. Which is faster and cheaper, but can reserve surprises in the future and thus it is riskier.[6] At last, the target's board of directors agrees and negotiates with the buyer a sales and purchase agreement. It is a legally binding contract which contains information on the price, closing

[6] Bruner R. F., Applied Mergers and Acquisitions, chapter 8, Wiley Finance, 2004

conditions, break-up fees, execution provisions, covenants and other key details on the deal. This contract is then submitted to shareholders for approval.[7]

However, takeovers are not always friendly. When the management of the target does not want the deal to happen, the bidder can either walk away or improve the terms of the deal and start again the entire process. Another option is to go public (bear hug). This consists in offering the target a consistently higher per share price than the actual value of shares. In this case, management will be forced to accept such an offer, since its objective is to maximize shareholder value. It is similar to a hostile takeover, since the target's management does not have many choices to escape from this situation.

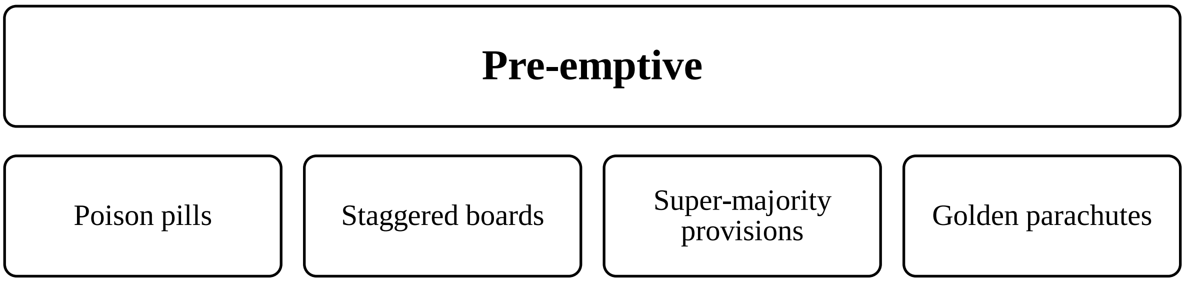
Speaking of which, if the bidder wants the deal to happen even without the consensus of the management, he must gain control of the target in alternative ways, bypassing it. Hostile takeovers are possible only for publicly traded companies. A way to acquire hostilely a target is through a tender offer. As mentioned previously, it consists in buying stocks at a fixed price, overvalued with respect to the market. Alternatively, the bidder can buy shares on the open market. It can either do this through the free-float shares or passing through another company which has a consistent stake in the target. However, if it results too costly, the acquirer can start a "proxy fight" with shareholders and convince them to replace existing management with one that is in favour of the takeover.

Nevertheless, we have still to understand why would the target's management refuse a takeover offer, if they are paid a premium to sell. First, the premium can be considered not sufficient and therefore the offer price is too low to accept an offer. If we are speaking of a stock for stock transaction, target may believe that buyer's share price is overvalued and thus, that the actual offer price is lower than the one proposed. Ultimately, if the rationale behind the takeover are efficiency gains, managers may take defensive measures to keep their jobs. As a matter of fact, we have seen that in case of an "efficiency-guided" takeover, redundant departments are cut and inefficient management is substituted with the acquirer's one.

So, if a target is not willing to continue the deal under certain conditions it can seek for improved terms, so that the bidder has to restart all over the acquisition process. If,

[7] Bruner R. F., Applied Mergers and Acquisitions, chapter 29, Wiley Finance, 2004

instead, it simply does not want the deal to happen it can just reject and walk away. However, we said that the bidder can try to acquire the target even if the target disagrees. To defend itself from a hostile takeover, the target can take defensive measures. These can be pre-emptive, so to avoid being targeted, or reactive, which are taken once the company is already targeted. Let us go through some of the pre-emptive measures.



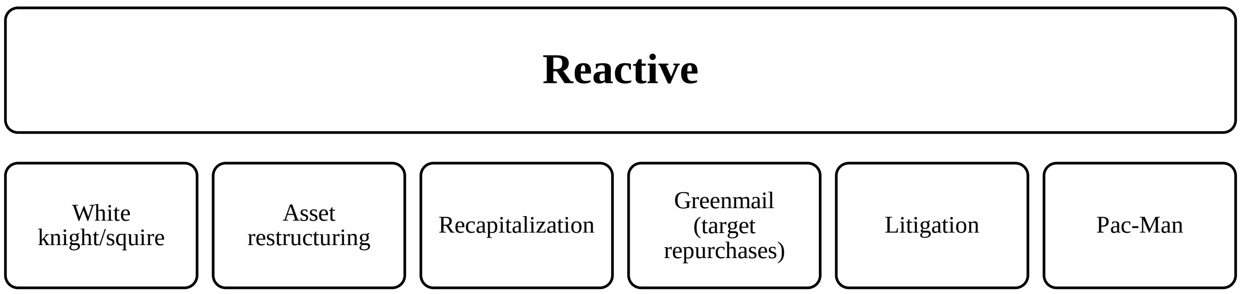
Poison pills are rights offerings to target shareholders to buy shares at a highly-discounted price. The acquirer is explicitly excluded. The name comes from the fact that when a spy gets caught, to avoid revealing relevant secrets, he should swallow a poison pill. As a matter of fact, Malatesta and Walkling (1988) proved that a firm's stock price and financial performance decrease after adopting a poison pill.

However, a poison pill may not be enough to prevent a hostile takeover. The acquirer can have its trusty directors be elected by the target shareholders and complete in this way the deal. Anti-takeover amendments, also called shark repellents, are changes made to the company's charter to avoid being taken over. *Staggered boards* present a solution to this eventuality. Directors are held in charge for a predetermined amount of time and elections can change only a third of them. In this way, even if the acquirer manages to win the elections he will control only a minority of the target's board. The process will therefore become too long and costly to complete and the acquirer will be deterred from proceeding with the takeover. In combination with poison pills, a staggered board is one of the most effective ways to avoid a hostile takeover.[8]

[8] Berk J., De Marzo P., Corporate Finance (third edition), pp. 945-948, Pearson, 2014

Another type of anti-takeover amendment are the *super-majority provisions*. These are charter provisions that require an extremely high amount of voting shares to approve a takeover, usually above 80%.[9] They can apply to all mergers or at board discretion. However, Ruback (1987) argues that this is a "mild takeover defence", as it does not affect the cost of the acquisition. The bidder can offer the same price per share, only that it must do it for the entire firm, rather than for just part of it.

Golden parachutes are abnormal bonuses guaranteed to senior managers in case of a takeover and a subsequent layoff of the senior management. Narayanan and Sundaram (1998) found out that companies announcing a golden parachute policy see their stock prices rise and that this policy creates value. This because it helps to avoid management entrenchment in a takeover.



Other than pre-emptive measures, targets can react to a hostile takeover even once it has started. The *white knight* is a friendly company that acquires the target at premium with respect to the hostile bidder. Moreover, incumbent managers agree with the acquirer to maintain their positions. Similarly, the *white squire* is a friendly company that acquires a relevant block of voting shares without exercising their voting rights.

Asset restructuring is another effective reactive method. The target will buy assets that are undesirable for the bidder or that can create antitrust/regulatory problems. The target may also divest into desirable assets for the bidder, so that the interest in its company will decrease. *Recapitalization* is a change in the target's capital structure to reduce the

[9] Ruback R. S., An overview of takeover defences, Published in Mergers and Acquisitions, p. 57, University of Chicago press, 1987

attractiveness of the firm. The target can issue debt to increase dividends or repurchase stock. This will increase the firm's leverage to unacceptable levels for the bidder, since it will be the target to gain tax shield benefits from the leverage and not the bidder. Other than this, deals like LBOs are not possible if the firm is already highly indebted.

Target repurchases (*Greenmail*) are used as a takeover defence when the target buys back its shares from the bidder at a premium. In exchange, the acquirer is asked not to bid-over for a given amount of time.

Litigation is one of the most common reactive measures to take against a hostile takeover. The target can accuse the bidder of fraud or of violating antitrust regulations for example. In this way the takeover gets delayed, allowing for different players to make their bids. Furthermore, the acquiring company can raise the offer price so that the target drops the suit and avoids legal expenses. [10]

The *Pac-Man* defensive strategy responds to the hostile bid with a counter bid on the acquiring company. This strategy is very costly as it requires a large amount of cash, that can come from debt issues or cash reserves. Sometimes, it is not necessary to make a huge counter bid. In Italy, there is a law concerning public companies called "Legge Draghi 1998". If company A has more than 2% of company B, then company B cannot acquire more than that amount in company A. In case of non-compliance, voting rights of the exceeding shares are suspended. Moreover, the exceeding shares must be sold within a year, if not, the company loses its voting rights on the totality of the shares. To overcome these issues, company B must make an offer for the acquisition of at least 60% of the target (company A).[11]

Let us now analyse some of the pros and cons of a hostile takeover with respect to a friendly one. First, in a friendly takeover, the target will help the bidder perform an accurate due diligence, therefore, making it less costly and more reliable than that of a hostile takeover. Given that no counterbid is expected and there will be full cooperation of the management, the premium and the overall costs of a friendly takeover will be less. On the other hand, hostile takeovers have the great advantage of acquiring a target company even

[10] Ruback R. S., An overview of takeover defences, Published in Mergers and Acquisitions, pp. 61-64, University of Chicago press, 1987
[11] Testo Unico della Finanza, Decreto legislativo 24 feb. 1998, n. 58, art. 121

against its wills. Moreover, the management control of an enlarged group, created from a friendly takeover, can be compromised, whilst in hostile takeovers there is a complete renewal of management that can avoid these kinds of problems.

As a matter of fact, empirical evidence[12] shows that targets of hostile takeovers are usually firms that underperform because of the incumbent management. For this reason, we speak about the value of control. The latter can be extracted only if the inefficient incumbent management is replaced with a new management. Obviously, this will be easier through a hostile takeover rather than a friendly one, since incumbent management will not leave their positions so easily. Thus, efficiency gains are an important rationale behind hostile takeovers.

[12] Damodaran A., Acquisitions and Takeovers, Published in Handbook of finance - Investment Management and Financial Management, pp. 13-14, Hoboken, Wiley, 2008

1.3 The agency motive

So, we have seen the rationale behind friendly and hostile takeovers. However, we have not seen why sometimes the reasons behind some mergers and acquisitions do not seem so clear. Jensen and Meckling (1976) describe companies as a set of contractual relations between owners (shareholders) and agents (managers), all of whom are rational, wealth-seeking individuals which act in their own interests. This is called the "principal-agent problem". There exist numerous examples of agency problems. We will now go through some of them that can occur when a takeover decision is made.

Managers can invest in specific companies or assets that operate in their own sector (*entrenching investments*), so that the company depends on their specific capacities. Berkovitch and Narayanan (1993) believe that managers can use this dependency to defeat possible rivals that would have been better than them in managing the firm. Entrenching investments happen more frequently if the company is abundant of cash and has low investment opportunities.

Empire building occurs when managers want to expand the company solely for their fame or compensation and not to create shareholder value.[13] The bigger the firm, the bigger the managers' visibility. Along with entrenching investments, it represents a situation of overinvestment.

Politics interference is found in strategically important firms. As a matter of fact, companies that operate in sectors like telecommunication, transport, finance, assurance, healthcare and others, will receive pressure by politics in their decisions. We will further discuss in depth how have these interferences affected Intesa's top management decision making process. These agency problems are in all senses costs, and they decrease the value for shareholders.

To solve agency problems, there must be found a way that matches principals' and agents' interests. Managers' remuneration should be linked to their performance, so that they are incentivized to bring value to the company. However, in many cases it is difficult to measure the value added.

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[13] Allen F., Brealy R. A., Myers S. C., Principles of corporate finance, pp. 291-292, McGraw-Hill, Irwin: New York, 2011

Speaking of incentive compensation, Piesse et. al. (2013) explain another way to link principals' and agents' interests: these are stock options. Managers are given call options to buy stocks of the company at a predetermined price. Therefore, if the company's stock performs well, both shareholders and managers can earn a profit.

Monitoring serves to control agents and check that their decisions are taken to maximize shareholders' value. Stoughton and Zechner (1998) believe that the more concentrated the shareholders are, the easier it is to monitor. When there are just a few big investors their interests coincide more easily than a vast base of shareholders and, therefore, monitoring activities are also less costly. Moreover, if there are many small shareholders, "free-riding" problems can show up. In other words, each shareholder will think that the other one is performing monitoring and, in the end, no one or just a few will perform it. Less efficient monitoring, implies more asymmetry of information, where the agent can act in its own interests without the principal knowing. This is called moral hazard, it can happen when an agent does not enter into a contract in good faith and, ex-post, provides misleading information on its activities to the principal.[14]

[14] Berk J., De Marzo P., Corporate Finance (third edition) - ch. 16, p. 562, Pearson, 2014

Chapter 2 – The Bancassurance model

2.1 The model

A general definition of the bancassurance model concerns banks that manufacture and/or distribute insurance products. This phenomenon is spread across the world, however, at different levels. The development of the bancassurance industry within different countries depends on various factors. The most important one, which will be discussed later on, is the regulatory environment in which the model has to develop. Intuitively, if bancassurance is prohibited in one country, its presence in the financial system will be zero.

Another reason are diversities in the structure of pension and tax systems. For example, in France life insurance products are favoured by banks given their tax incentives and similarity to banking products.

One more crucial success factor for the bancassurance model in a given country is the extent to which banks are relevant within a financial system. In countries where the stock market commands, such as United States and the UK, bancassurance will struggle to penetrate the financial system.

Finally, the development of the insurance market influences the extent to which bancassurance is used to distribute insurance products. Recall the concept of geographic reach as a rationale behind takeovers, explained in the first chapter. In fact, insurers will join forces with local banks to sell their products, as this represents a cheaper way of market penetration with respect to creating *ex-novo* a subsidiary.[15]

Bancassurance brings about mutual benefits for customers and banks. On the one hand, it simplifies client's lives, given that they can shop for multiple products at the same place. On the other hand, banks gain loyalty from their customers, which implies long term benefits. The bank has to offer the most types of products possible to cover the majority of customers' lives in order to maintain this loyalty.

[15] Benoist G., Bancassurance: The new challenges, The Geneva papers on risk and insurance, issues and practice, vol. 27, no. 3, pp. 297-298, Palgrave Macmillan Journals, 2002

2.2 Regulation and structure

Daniel (1995) divides the history of bancassurance in three different periods. Before 1980, banks sold closely linked insurance products. Afterwards, they started to sell also savings insurance products. Since the nineties, there has been an expansion towards more traditional insurance products. Regulation has played a significant role in the expansion of the bancassurance model.

As a matter of fact, in Europe, it was the "Second banking coordination directive" (1989, effective in 1993) to boost bancassurance activities and enter the third phase of the industry's history. It allowed financial institutions to freely operate across the European Union. This increased competition amongst universal banks[16] brought them to offer an increasing amount and types of products.

The United States suffered from a strict regulation of the banking sector known as the Glass-Stegall act of 1933, to overcome the great depression started in 1929. The main issue was the separation between commercial and investment banks. Moreover, the 1956 Bank Holding Company act, prohibited bank holding companies to engage in non-banking activities, like insurance underwritings. These two acts were ended by the Gramm-Leach-Bliley Act (also known as Financial Services Modernization Act, 1999) which basically legalized the bancassurance model, allowing the formation of financial holding companies that can operate in a wide range of sectors. Bancassurance is typically a European model: however, thanks to deregulation, it has started to spread also in the US.[17]

The model can vary depending on the level of integration between the bank and the insurance structure. Benoist (2002) provides different examples of bancassurance structures. These are: contractual agreements, joint ventures and mergers and acquisitions. Distribution (contractual) agreements concern the bank recommending its clients to an insurer. In case of a non-exclusive agreement, the bank sells insurance products both of the linked insurance company and of others, basically acting like a broker. On the other hand, a limited distribution agreement consists in a bilateral agreement regarding a limited number of products; those that are not included in the agreement can be contracted with other partners.

[16] Banks which offer a wide variety of financial services, from commercial to investment ones.
[17] Fields L. P., Fraser D. R., Kolari J. W., Bidder returns in Bancassurance mergers: Is there evidence of synergy?, , p. 3648, Journal of banking & finance 31, 2007

The exclusive distribution agreement allows the bank to sell exclusively insurance products of its partner through its channels.[18] These may seem a cheaper solution to a takeover; nevertheless, it requires consistent investment in logistics, information technologies and administrative expenses even to build commercial ties.

Banks and insurers can come together in a Joint Venture and create a company *ex-novo*. However, it is very complicated to structure a well-balanced equity contribution and power distribution between the two entities.

Integrated operation systems, known as mergers and acquisitions, are another way of approaching a bancassurance model. Both banks and insurers are financial intermediaries that collect savings from individuals to then reinvest them in capital markets. In fact, there could easily be synergy gains arising from economies of scope. Below you will find a table comparing the advantages of the three methods mentioned above, both for banks and for insurers.

[18] Bolovan C., Clipici E., Bancassurance – Main insurance distribution and sale channel in Europe, Scientific Bulletin – Economic Sciences, Volume 11/ Special Issue, 2012

Table 1 – Comparison of the bancassurance structures

Advantages for banks	*Contractual*	*Joint-Venture*	*M & A*	*Advantages for insurers*	*Contractual*	*Joint-Venture*	*M & A*
Additional and stable source of incomes, reducing their dependence on the interest margin	X	X	X	Access to the bank's client database, usually more consistent	X	X	X
Expanding potential client portfolio	X	X	X	Reducing dependence on agents/brokers	X	X	X
Diversifying the range of products and services as a manner of increasing clients' loyalty		X	X	Sharing certain categories of services with the bank		X	X
Reducing the capital requirement (compared to the undertaken risks) at the same level of incomes	X			Increased efficiency in the development of new products in partnership with the bank		X	X
Continuity of the activity by providing integrated services tailored to consumer lifecycle		X	X	Quick access to new markets without being necessary to have a an own (distribution) network	X	X	X
Access to the funds of the life insurers, including for reasons of a fiscal nature		X	X	Obtaining capital to increase solvency and to develop the business		X	X

Source: Wong, C., Cheung, L., Bancassurance developments in Asia - shifting into a higher gear, in „Sigma" no. 7/2002, Swiss Re, p. 3-38

An alternative method is internal development. An example is Crédit Agricole's Predica (life insurance) and Pacifica (non-life insurance). There are also examples of Insurance companies which start to sell banking products to their clients. These are Banca Generali, launched by Assicurazioni Generali, and ING Direct, the online banking system offered by the Dutch ING Group. However, in these cases we speak about assurfinance (or assurbanking). Here, it is the insurance company that sells saving products, exploiting their networks.

The reasonings behind assurfinance are basically the same that bring banks to enter into the bancassurance market. First of all, it is widely understood that client relationship is increasingly important. Having a banking network allows insurers to maintain a constant contact with their clients and to gather useful information about them.

Assurfinance also allows insurers to enlarge their client base through a diversification of their distribution networks. Moreover, by offering multiple products, insurers will increase the profitability of their sales channels and enhance client loyalty. Lastly, assurfinance brings about an increased number of clients (economies of scale) that help insurance companies to compete in the international market.[19]

[19] Benoist G., Bancassurance: The new challenges, The Geneva papers on risk and insurance, issues and practice, vol. 27, no. 3, pp. 299-300, Palgrave Macmillan Journals, 2002

2.3 Distribution

According to Bergendahl (1995), the distribution of insurance products by banks can be divided into two ways: pure and mixed bundling. Pure bundling links two products so that they cannot be sold separately. For example, customer credits can be offered with life insurance contracts as a pure bundle.

The other cross-selling technique is mixed bundling. Intuitively, it differs from pure bundling in that the client can buy both banking and insurance services together or separately. Banks have to be able to identify those customers that are willing to attach insurance services to their banking products to efficiently cross-sell. However, savings deposits are easily replaceable by insurance contracts. Moreover, also life insurance products can be seen as substitutes of many investment products sold by banks. Thus, this is a double-edged sword, since the risk of cannibalization between banking and insurance products is high.

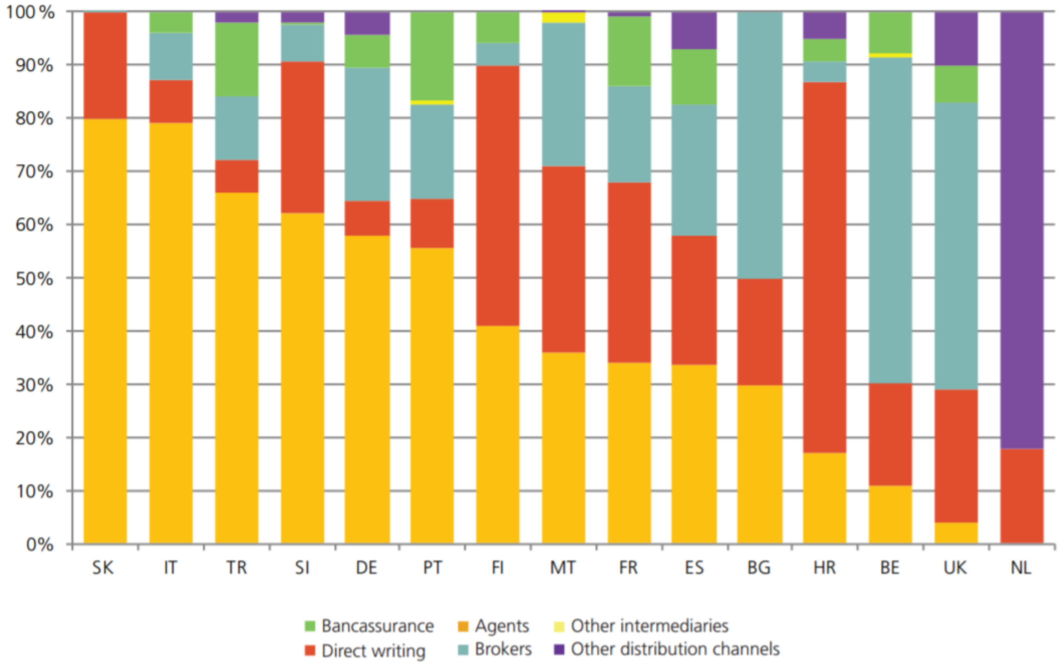
Nicholson (1990) found that, with respect to premiums, branch-based distribution costs are lower than the conventional salesforce model. This is true when banks manage to avoid spending extra money on training and are able to exploit their selling channels. To do so, they must sell fairly straight-forward and standardized insurance products, such as life insurance products.

Speaking of which, these kinds of contracts are largely preferred to non-life insurance contracts by banks. The main difference is that life insurance products are long term and do not require frequent contacts with the clients, that would result costly and time consuming. On the other hand, non-life insurance products require frequent contacts with the clients, leading to high training costs and use of time. This risks to hamper economies of scope.[20]

Below we can find a comparison of distribution channels in the European Union for life and non-life insurance products, which confirms what just said. Where GWP stands for Gross Written Premium.

[20] Bergendahl G., The profitability of bancassurance for European banks, p.20, International Journal of Bank Marketing, Vol. 13, 1995

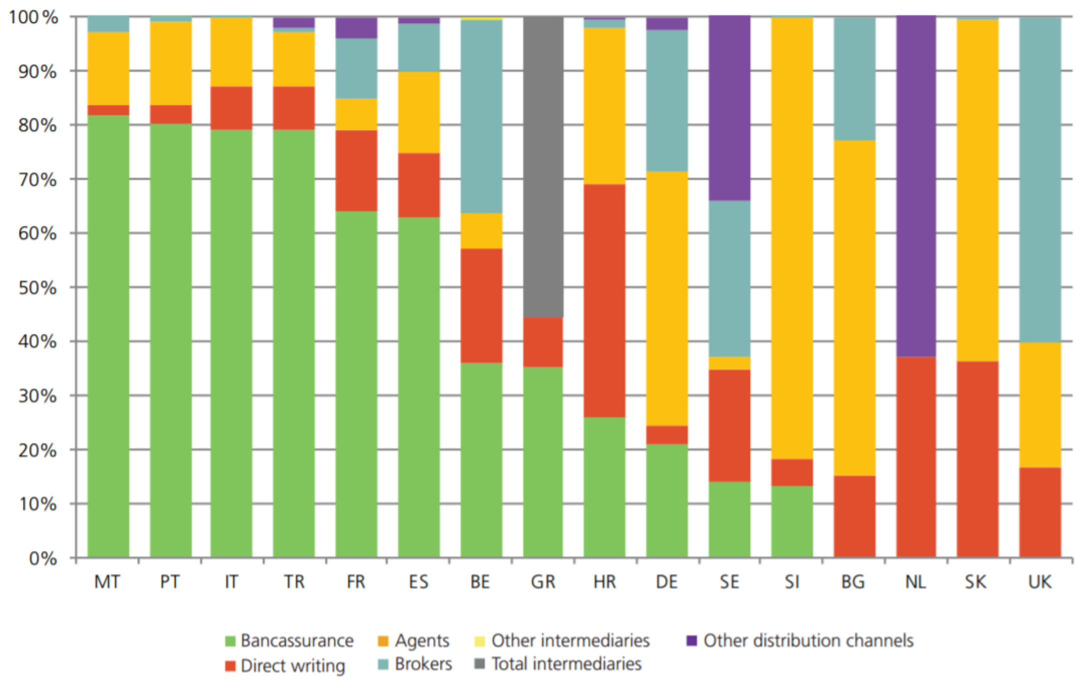
Graph 1 – Non-life distribution channels by country (%GWP)



Source: Insurance Europe, European Insurance – Key facts, August 2016, Brussels

For what concerns the non-life insurance sector, bancassurance is certainly not the predominant distribution channel. Agents are the main distribution channel for non-life insurance products.

Graph 2 – Life distribution channels by country (%GWP)



Source: Insurance Europe, European Insurance – Key facts, August 2016, Brussels

For what concerns life insurance, the first thing that we notice is the clear difference in the use of the bancassurance channel to distribute it with respect to non-life products. In case of life insurance, bancassurance is a predominant distribution channel in Malta, Portugal, Italy, Turkey, France and Spain. On the contrary, we see that in Bulgaria, Netherland, Slovakia and Unite Kingdom there is no use of bancassurance to distribute life insurance products. This depends on the differences between countries that we listed at the beginning of the chapter. As a matter of fact, we said that the UK was not well-suited to the bancassurance model, given its strong reliance on the stock market.

2.4 Empirical analysis

2.4.1 Economies of scale, scope and profitability

Throughout this chapter we will perform an analysis mainly based on the empirical results obtained by Fields et al. (2007) regarding the bancassurance model. The initial sample of their work are all the US and non-US takeovers between banks and insurance companies that took place between January 1997 and December 2002. Criteria to be included in the final sample are: a publicly traded bidder, no controlling interest of the bidder in the target before the announcement, merger results in the bidder owning a controlling interest in the target, and merger completion confirmed by press release or Securities Data Company (SDC).

These are some interesting insights regarding our sample. We can immediately see the predominance of friendly deals within the bancassurance context. Moreover, in most of the cases the bidders were banks and the deal involved a stock transaction.

Table 2 – Deal characteristics

Percentage of friendly deals	96.90%
Percentage of deals involving stock	75.19%
Percentage of bank bidders	81.40%

Source: L. P. Fields, D. R. Fraser, J. W. Kolari, Bidders returns in bancassurance mergers: is there evidence of synergy?, p. 3652, Journal of banking & finance 31, 2007

The basic rationale behind the bancassurance model is that banks can earn additional profits by selling insurance products and insurers can increase their client base by exploiting banks' sale channels, without incurring in additional sales forces costs. In other words, economies of scope. This concept suggests that the average total cost of production decreases with the increase of products offered. In order to create synergy, companies must share resources that can be used for distinct types of products without additional costs. Economies of scope are divided in: revenue, expense and profit (net income).

Nevertheless, also economies of scale play a significant role in value creation. The more products are sold, the less their unit cost will be. The target's size relative to the bidder is used as a proxy of economies of scale. As a matter of fact, Chen and Tan (2011) state that the larger the size of the target with respect to the bidder, the more synergy is created.

Another factor that affects value creation in a bancassurance merger is profitability. This is measured by "return on assets" (ROA). We presume bidders with a high profitability will invest wisely and are good in managing their assets. So why shouldn't they be able to manage wisely also the target's assets? Therefore, ROA can be considered as a proxy to assess the bidder's management quality. Furthermore, also the target's profitability is important to verify, since it is easier to implement an already functioning business into the new firm, rather than starting from scratch.

An additional variable that affects the bidders' abnormal returns is its size. Chen et al. (2009) believe that larger banks have greater experience in managing diverse operations, and thus, are more able to perform successful bancassurance operations. Furthermore, having a large client base, they can easily reach many potential buyers of insurance products at a low cost of promotion. Nevertheless, do not forget of the empire building problem mentioned in the first chapter. Managers of big firms are more likely to incur in acquisitions that could easily be avoided or even overpay for the target.

So, we spoke about profitability, size and economies of scale / scope. Below you will find a useful analysis of the correlation between these factors and the announcement period abnormal returns in takeovers of public targets. The objective is to check which variables are statistically significant, in which way (positive or negative) and to what extent. Abnormal returns are used as a measure of value creation. If there is a positive (and statistically significant) correlation between a variable and abnormal returns, it means that that variable contributed to the synergic effect of value creation.

Table 3 – Correlation between abnormal returns and synergy measures

Variable	N	Correlation coefficient
Financial and synergy measures		
Bidder market value	46	0.2783*
Bidder ROA	44	0.4651***
Target ROA	44	0.2631*
Economies of scale – Total assets[a]	40	0.3304**
Economies of scale – Market value[b]	32	−0.1317
Economies of scope – Revenue[c]	36	0.3172*
Economies of scope – Expenses[d]	25	−0.1909
Economies of scope – Net income[e]	36	0.0235

[a] Target total assets (year −1) divided by bidder total assets (year −1).
[b] Target market value (year −1) divided by bidder market value (year −1).
[c] ((Combined firm revenues from year +1) – (bidder revenues from year −1 + target revenues from year −1))/ combined firm revenues from year +1.
[d] ((Combined firm expenses from year +1) – (bidder expenses from year −1 + target expenses from year −1))/ combined firm expenses from year +1.
[e] ((Combined firm net income from year +1) – bidder new income from year −1 + target net income from year −1)/combined firm net income from year +1.

***, **, * denote significance at the 1%, 5%, 10%, respectively

Source: L. P. Fields, D. R. Fraser, J. W. Kolari, Bidders returns in bancassurance mergers: is there evidence of synergy?, p. 3657, Journal of banking & finance 31, 2007

Table 3 confirms what just said above. There exists a positive and statistically significant correlation of the bidder's size and profitability with respect to abnormal returns. We can also notice that the statistical significance of profitability is 1%, which means an accuracy of 99% and its correlation coefficient is 0.4651, the highest of all the variables tested; whereas the target's profitability proxy, has a correlation coefficient of 0.2631 at a significance level of 10%. This means that both bidder's and target's profitability are positively correlated with abnormal returns and thus, create value. However, it is of crucial importance that in a bancassurance merger the bidder has a strong ROA, mainly because in the post-merger, it will be the bidder that will take control of the new entity.

Economies of scale are found to be significant only if the target's relative size is measured in terms of total assets, rather than market value. However, it is confirmed that economies of scale have a positive impact on abnormal returns.

Lastly, only revenue economies of scope are found to be statistically significant. This means that when the merged entity is able to create synergy, increasing its revenues more than the sum of the parts, the likelihood of obtaining abnormal returns rises.

2.4.2 Governance and geographic diversification

Fields et al. (2007) (1) found that there exists a relationship in bancassurance mergers between value added and governance characteristics of the bidder. High-quality corporate governance firms are expected to take better investment decisions than badly governed companies. Quality of corporate governance is assessed on three factors: ownership structure, executive compensation and board composition.

For what concerns the ownership structure, recall we spoke about linking managers' and shareholders' interests through managerial stockholdings. Stulz (1988) agrees with the fact that managerial ownership aligns interests with shareholders. However, up to a certain threshold. After this point, managerial entrenchment is larger than the benefits brought by this incentive scheme. There is no fixed percentage of share that causes managerial entrenchment. Nevertheless, for large firms, the threshold can be relatively low. Speaking of which, also block-holding affects the decision-making process of a firm. As already mentioned in the previous chapter, monitoring is crucial to check if managers' decisions maximize shareholders value. Large block-holders are able to perform this monitoring and thus, we expect these firm to make better takeovers than bidders with a fragmented ownership structure.

Another way of aligning shareholders' and managers' interests are executive compensation schemes. Incentive compensation could potentially reduce risk adverseness of managers and make them take beneficial investment decisions for shareholders. However, Erickson et al. (2004) provide evidence for executive compensation actually increasing the probability of agency problems. It could happen that stock performance based compensation induces managers to commit accounting frauds, in order to gain the bonuses. For this reason, the relation between executive compensation and the quality of corporate governance is unclear.

Board composition is the third and last factor considered to assess the quality of corporate governance. It is not clear whether it is better to have an independent board of directors or not. Theoretically, board independence can be used as an effective monitoring device. However, it appears that whilst this works for manufacturing firms, financial institutions could lose from having an independent board. In fact, Rangan et al. (1997)

demonstrated that there is a negative relationship between abnormal returns and board independence. This happens mainly because they believe that external members of the board are chosen because of their business expertise, rather than their target valuation abilities. Moreover, Yermack (1996) found out that relatively small boards of directors are associated with higher abnormal returns. After a bancassurance merger, board members tend to increase, implying a possible reduction in abnormal returns.

Fields et al. (2007) (1) performed a regression to understand the magnitude of the impact of these variables and if they are statistically significant. This table contains only US bidders with available governance data. As a matter of fact, they examined four different models to increase the reliability of the results, given the small size of the sample.

Table 4 – Ordinary Least Square (OLS) regression models for US bidders

Variable	Model 1	Model 2	Model 3	Model 4
Intercept	−0.0020	−0.0438	−0.0249	−0.0257**
Governance variables				
Number of directors (log)	0.0022			
Industry board dummy	−0.0040	−0.0037		
Percentage independent board	0.0002	0.0114	0.0024	
Unaffiliated block ownership	−0.0004	−0.0008	−0.0054	
Affiliated block ownership	−0.0007			
CEO ownership	−0.0020*	−0.0022**	−0.0024***	−0.0025***
Officer & director ownership	−0.0005			
CEO compensation (log)	−0.0030			
CEO incentive pay dummy	0.0083			
Control variables				
Bidder total assets (log)	−0.0000	−0.0000		
Bidder return on total assets	2.5047*	2.5287**	3.0265***	3.1257***
Postprobability of failure	0.2529	0.2419		
Public target dummy	0.0094	0.0123		
Stock payment dummy	0.0114	0.0104		
N	66	66	66	66
F-value	1.63	2.57**	5.28***	10.55***
p-value	0.1015	0.0145	0.0010	0.0001
Adjusted R^2	0.1202	0.1787	0.2086	0.2272

Notes: The dependent variable is the bidder 2-day abnormal returns calculated using a comparison period approach. The sample is composed only of U.S. bidders for which governance data are available.
Statistical significance: ***1%, **5%, and *10%.

Source: L. P. Fields, D. R. Fraser, J. W. Kolari, Is bancassurance a viable model for financial firms?, p. 790, The journal of risk and insurance, vol. 74, No. 4, 2007

The results show that most of the corporate governance variables are not statistically significant. Which means that their impact on value added is basically irrelevant. Nevertheless, we can observe that the "CEO ownership" variable is strongly statistically significant and has a negative impact on abnormal returns. In other words, some CEOs who own a high portion of a company's shares are likely to perform value reducing takeovers. Furthermore, the other variable that we can observe to be statistically significant, is the bidder's ROA. Its positive value confirms what we said previously. That is, that the market views positively an acquisition made by a bidder who already knows how to manage its own assets, since it is more likely that he will add value also for the target.

Within this study also a geographic diversification variable has been taken into consideration as a factor affecting the bidder's abnormal returns. It has been found a highly significant and positive relation between the two. Therefore, mergers that focus on the international market are seen better than domestic market deals. In that international takeovers enable domestic companies to easily access foreign markets and human resources. As a matter of fact, in the previous chapter we spoke about how the increase of geographic reach helps to create value for domestic firms.

Table 5 – Characteristics and number of mergers between banks and insurers

Panel A – Sample breakdown by year and by bidder and target type

Year	Number	Bank bidder	Public target	Bidder and target same country (both public)	Bidder and target same language (both public)
1997	11	6	7	4	4
1998	12	7	7	4	5
1999	26	20	12	6	9
2000	30	27	6	4	4
2001	22	19	9	4	5
2002	29	26	5	5	5
Total	129	105	46	27	32

Panel B – Sample breakdown by year and by bidder and target location

Year	Number	US bidders	US targets	EU bidders	EU targets
1997	11	3	2	6	5
1998	12	5	5	6	4
1999	26	10	10	11	6
2000	30	16	19	9	5
2001	22	14	14	6	3
2002	29	24	24	3	3
Total	129	72	74	41	26

Source: L. P. Fields, D. R. Fraser, J. W. Kolari, Is bancassurance a viable model for financial firms?, p. 3651, The journal of risk and insurance, vol. 74, No. 4, 2007

We can notice that 41% of public mergers and acquisitions involve counterparties from different countries. Moreover, the majority of public takeovers are between entities that speak the same language. Which can be both in the same country, or in another country where the same language is spoken. For example, UK and US, France and Belgium, Germany and Austria, etc. Other than simplifying communications, speaking the same language is a measure of cultural similarity.

2.4.3 Risk and returns

The bancassurance model can create value in terms of increased cash flow, risk reduction, or both together. Abnormal returns are a measure of value creation (or destruction) implied by these factors. We will now focus only on abnormal returns and see what are the consequences of a bancassurance merger. This analysis will tell us, in general, if bancassurance can be considered a profitable model.

Table 6 – Abnormal returns

Panel A: Event Study Results

Sample	N	Event Window	Abnormal Return	Number of Positive/Negative
Bank bidders	105	−1	0.08%	48/57
		0	0.29%*	55/50*
		−1.0	0.37%*	56/49*
Insurance company bidders	24	−1	0.38%*	15/9**
		0	0.25%	10/14
		−1.0	0.63%	10/14

**, * denote significance at the 5% and 10%, respectively

Source: L. P. Fields, D. R. Fraser, J. W. Kolari, Is bancassurance a viable model for financial firms?, p. 790, The journal of risk and insurance, vol. 74, No. 4, 2007

The event window indicates the days prior to the announcement: "-1.0" is a two-day figure (before and at the announcement). Bank bidders experience a positive and significant correlation between the merger and abnormal returns. Furthermore, the insurers abnormal returns are positively correlated with the announcement of a merger. However, they are significant only prior to one day. This is probably due to the low sample size.

Thus, we can conclude that the bancassurance model is a profitable and viable model. Nevertheless, this model does not account for the number and order of takeovers made by one single bidder. In their paper, Fields et al., found that while the first mergers experience a +0,20% abnormal returns, second mergers result in a +0,59% abnormal returns. Even if second takeovers have greater abnormal returns, they are not statistically different from the first ones. This concept is taken also from Chen and Tan (2011), where in a regression to understand the determinants of wealth, they have included a dummy variable[21] to account for "serial acquirers", where the latter is a bidder who performed at least three mergers during their sample period (1989-2004). The result is that this variable is a positive determinant of wealth (measured as Cumulative Abnormal Returns) and it is statistically significant at a 10% level.

Let us now see what happens in terms of risk in bancassurance mergers. Regulation across the world, has prohibited the formation of diversified financial firms until the nineties because regulators were afraid that a failure in the bancassurance model could spread more easily to the entire financial system, rather than keeping separate the entities. So, were the regulators right to think so? To reply to this question, we will analyse two different models and see the effects of mergers in the bancassurance sector on risk. Table 7 provides a risk shift analysis taken from Fields et al. (2007) (1).

[21] A binary variable that can only be 0 or 1. In this case, it is 1 if the bidder is a serial acquirer and 0 otherwise.

Table 7 –Changes in risk

Panel B: Risk Shift Analysis	N	Preacquisition	Postacquisition	Change
Bank bidder	105			
Variance		0.0206	0.0197	0.0009
Beta		0.668	0.708	0.0408
Probability of failure		0.048	0.041	−0.007
Insurance company bidders	24			
Variance		0.0224	0.0241	−0.0020
Beta		1.054	1.119	0.0657
Probability of failure		0.055	0.062	0.007

Source: L. P. Fields, D. R. Fraser, J. W. Kolari, Is bancassurance a viable model for financial firms?, p. 790, The journal of risk and insurance, vol. 74, No. 4, 2007

The variance is calculated on the basis of stock returns pre-, and post- acquisition. The period analysed is of 200 days and it starts 51 days before the merger announcement. The same is done for the beta and the risk of failure. The study demonstrates that there are no major changes in the perception of risk. Moreover, none of the results are statistically significant. This means that bancassurance mergers do not alter the bidder's systematic and total risk. Therefore, we can state that, according to this model, deregulation does not affect the stability of the financial system.

Let us now take a look also at Chen and Tan (2011) model. Their sample consists in 72 mergers, concerning only European banks as bidders. The period goes from 1989 to 2004. All the bidders owned more than 20% of the targets post-acquisition. We can observe the effect of a bancassurance merger on total relative risk and systematic risk. Let us first focus on total relative risk. Considering firm j and index k we can write the total relative risk as $TRR_{j,k} = \frac{Var(R_j)}{Var(RIndex_k)}$. Where $Var(R_j)$ is the return variance of the bank and $Var(RIndex_k)$ is the return variance of three market indices: world market, home market and home banking index. Pre-merger risk is calculated from 260 to 10 days before the announcement. Post-merger risk, instead, from 10 to 260 days after the announcement. Intuitively, the change in TRR is the difference between TRR before and after the announcement. Moreover, investigation has been further split into domestic and cross-border mergers. The t-statistic serves to understand the value of significance of the results. The star (*) represents the level of significance, if there are no stars it means that the result is not enough consistent to be taken as reliable.

Table 8 – Change in risk

	ΔTRR (world market index)			ΔTRR (home market index)			ΔTRR (home banking index)		
	Mean *t-Statistics*	Median	% Positive *t-Statistics*	Mean *t-Statistics*	Median	% Positive *t-Statistics*	Mean *t-Statistics*	Median	% Positive *t-Statistics*
Panel A: change in total risk									
Entire sample (72)	0.9307	−0.3102	45.83	0.1345	0.2274	55.56	0.142	0.1365	54.17
	0.7		*−0.7*	*0.59*		*0.94*	*0.7*		*0.7*
Domestic deals (41)	1.875	−0.4251	46.34	0.031	0.1785	56.10	0.1834	0.1213	51.22
	0.82		*−0.46*	*0.09*		*0.78*	*0.52*		*0.15*
Cross-border deals (31)	−0.318	−0.0259	45.16	0.2714	0.2956	54.84	0.0873	0.1590	58.06
	−0.66		*−0.53*	*1.06*		*0.53*	*1.01*		*0.9*
	Δβ (world market index)			**Δβ (home market index)**			**Δβ (home banking index)**		
	Mean *t-Statistics*	Median	% Positive *t-Statistics*	Mean *t-Statistics*	Median	% Positive *t-Statistics*	Mean *t-Statistics*	Median	% Positive *t-Statistics*
Panel B: change in systematic risk									
Entire sample (72)	−0.0260	0.0005	50.00	0.0685	0.0629	58.33	−0.0560	−0.0388	47.22
	−0.86		*0*	*1.67**		*1.42*	*−1.38*		*−0.47*
Domestic deals (41)	−0.0540	−0.0171	41.46	0.0691	0.0088	51.22	−0.1150	−0.0553	43.90
	−1.16		*−1.1*	*1.12*		*0.15*	*−2.07***		*−0.78*
Cross-border deals (31)	0.0105	0.0245	61.29	0.0678	0.0714	67.74	0.0212	0.0070	51.61
	0.31		*1.27*	*1.32*		*2.08***	*0.37*		*0.18*

Change in the acquiring bank's variance of daily stock return relative to the variance of three indices: world market index, acquirer home market index and acquirer home banking index. Change in beta coefficient of the acquirer's return after the merger compared to beforehand.

* Represent 10 percent significant levels.
** Represent 5 percent significant levels.

Source: Z. Chen, J. Tan, Does bancassurance add value for banks? – Evidence from mergers and acquisitions between European banks and insurance companies, p. 106, Research in international business and finance 25, 2011

The results do not show any significant change in terms of total risk. Thus, these results confirm what observed in the previous model, that the bidder's risk is not affected by a bancassurance merger. For what concerns cross-border deals, we would expect that, given geographic diversification, they would have led to a risk reduction. Nevertheless, it seems that risk increase and reduction effects offset each other. Whereas, in domestic mergers, given the fact that both companies operate in the same country and financial system, their stock returns are highly correlated. Therefore, no significant changes in terms of total risk are observed.

For what concerns systematic risk, measured by the change in beta, we do not see statistically significant results with respect to the world market index. However, for the entire sample, there is a positive correlation between bancassurance mergers and systematic risk, with respect to the home market index. Nevertheless, the change in beta in both domestic and cross-border mergers, considered independently, does not result statistically significant. Still, there is evidence that in cross-border mergers the majority (67,7%) of changes in beta are positive. Amihud et al. (2002) believe that this is because the market indexes are not very effective in capturing the bidder's systematic risk with respect to the banking industry. Thus, to remove this bias, the home banking index is added to the analysis. In fact, we see no significance in systematic risk changes. Except for domestic mergers, where the correlation is actually negative. Which means that in domestic mergers, beta (thus, systematic risk) decreases by 11% post-merger, with a 5% significance level. So, also according to this model, regulators do not have to worry that bancassurance mergers can cause financial system instability.

Chapter 3 – Intesa Sanpaolo - Assicurazioni Generali

3.1 The acquirer: Intesa Sanpaolo

Intesa Sanpaolo is an Italian banking group born in 2007 from the merger of Sanpaolo IMI and Banca Intesa. Sanpaolo IMI was founded, in turn, in 1998 from a merger between the Istituto Bancario San Paolo di Torino and the Istituto Mobiliare Italiano (IMI). These two entities decided to merge because of their complementary nature. On the one hand, the first was a commercial bank focused on the retail industry. On the other hand, IMI was an investment bank, governed by public law, founded in 1931 to reconstruct the Italian industry following the great depression. The following years (2000-2002), Sanpaolo IMI acquires the Banco di Napoli. Moreover, it begins a process of integration with the Cardine Group (composed of seven north-eastern Italian banks) that will be completed in 2004. In January 2006, the asset management activities of the group converged into the subsidiary Eurizon Financial Group, which already comprehended the life-insurance company EurizonVita and Banca Fideuram, which operates in the private banking sector.[22]

Banca Intesa was born in 1998 with the merger between Cariplo and Banco Ambrosiano Veneto. Cariplo stands for Cassa di Risparmio delle Province Lombarde, it is a historical commercial bank born in the Lombardy region which then expanded its activities

[22] Group Intesa Sanpaolo website, About us

nationally and internationally. The Banco Ambrosiano Veneto was founded in 1989 thanks to the merger of two historical Veneto banks (Nuovo Banco Ambrosiano and Banca Cattolica del Veneto). In the early 90s, it started to perform acquisitions that allowed it to expand its commercial banking activities at a national level. In the meanwhile, it started to focus also on the investment banking sector. In order to maintain its position in the national and international markets, Banco Ambrosiano Veneto looked for a partner to join forces with, and found Cariplo. The merger then led to the creation of Banca Intesa. In 2001, Intesa merges with Comit (Banca Commerciale Italiana), one of the most relevant Italian banks of the early nineteen-hundreds. Until the 30s it has operated also as investment bank. In 1933, it was acquired by the IRI (Istituto per la Ricostruzione Industriale) and turned into a commercial bank three years later. After the second world war, Comit founded Mediobanca, one of the most important Italian investment bank nowadays.[23]

Intesa Sanpaolo is now the largest banking group in Italy and one of the major groups in Europe. It has approximately 20 million customers, of which more than a half (≈12.3 million) in Italy. Moreover, it counts almost six thousand branches, of which more than one thousand abroad mainly focused in the central-eastern European countries and Egypt.[24]

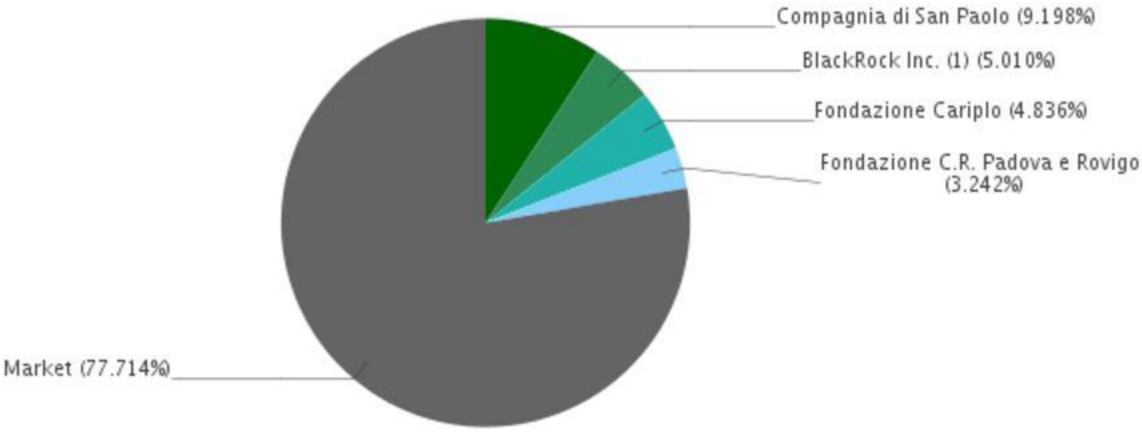
The group is divided in seven business units: banca dei territori, corporate and investment banking, international subsidiary banks, private banking, asset management, insurance and capital light bank. The *banca dei territori* division focuses on SMEs (Small and Medium Enterprises) and no-profit entities across the Italian territory, it also includes the Italian subsidiary banks. The *corporate and investment banking* division covers both national and international activities. Banca IMI performs capital markets and investment banking activities. To support cross-border activities of its clients, numerous branches, representative offices and subsidiaries abroad perform corporate banking activities. The *international subsidiary* division includes the subsidiaries that operate in the commercial banking sector abroad. The *private banking* division, which includes Fideuram, targets HNWI (High Net Worth Individuals) and private clients. The *asset management* division is managed by Eurizon. It serves the group's clients, commercial networks external to the group and institutional investors. The *insurance division* creates both pension and insurance products for the group's customers. It includes: Fideuram Vita (life insurance), Intesa

[23] *ibidem*
[24] *ibidem*

Sanpaolo Assicura (non-life insurance) and Intesa Sanpaolo Vita (life insurance). At last, the *capital light bank* division is set up to extract value from non-core activities. For example, it works out NPLs (Non-Performing Loans) or sells non-strategic equity stakes.[25]

Intesa Sanpaolo has a market capitalization of 48 billion euros[26], which makes it one of the biggest banks for capitalization amongst the eurozone. Its shareholder structure is shown in the graph below.

Graph 3 – Intesa Sanpaolo's shareholder structure



(1) Fund management. Shareholder owning aggregate investment equal to 5.106% as per form 120 B dated 4 July 2017.

Source: Group Intesa Sanpaolo website, Shareholder Base

We can immediately notice that almost 80 percent of the ownership is free-floating. In other words, a fragmented ownership. As we said in chapter 1, this could lead to difficulties in monitoring activities and thus, agency problems could arise.

[25] *ibidem*
[26] Source: Yahoo Finance, 22 August 2017

3.2 The target: Assicurazioni Generali

The group was founded in 1831 under the name of Assicurazioni Generali Austro-Italiche. Because of the 1848 insurrections, the company name becomes just “Assicurazioni Generali”. Later on, in 1860, also the imperial eagle on the logo will be substituted by the Lion of Saint Mark (still in use nowadays). One of the most notable acquisitions was that of INA Assitalia, in the year 2000. Generali became market leader in Europe for the life insurance sector. Moreover, in 2006, the group took over Toro Assicurazioni. This led Generali to a leadership position, in Italy, also for the non-life insurance sector.[27]

Generali has 55 million customers. Since its foundation, it pursued an internationalization strategy. Nowadays, up to 66% of the group’s premium income comes from abroad. Its main market is the European one, where it aims to become leader in the retail industry. Moreover, Generali has a strong position in Asia, mainly: China, India and Indonesia. It is also one of the largest foreign insurers in Latin America. Generali distributes its products around the world using a multichannel strategy. Its distribution channels are made of a proprietary sales network of agents and financial advisors, supported by brokers, bancassurance and direct channels.[28]

Generali is not only an insurance company. In 1998 the group founded Banca Generali, which now counts around 250 thousand customers, 52.1 billion euros of AUM (Asset Under Management) and 45 branches across Italy. Its distribution networks are divided by target customer: financial planners and private banking.[29] In 2006 Banca Generali has been listed on the Milan stock exchanged and it is controlled by Assicurazioni Generali, which detains 50.26% of the shares. Its market capitalization is of 3.3 billion euros.[30] Banca Generali controls the totality of: BG Fiduciaria, Generfid and BG Fund Management Luxemburg. The first two companies deal with the group’s wealth management services, whilst the third is Generali’s asset management product factory.[31]

[27] Generali website, Who we are
[28] *ibidem*
[29] Banca Generali website, About us
[30] Source: Yahoo Finance, 24 August 2017
[31] Banca Generali website, About us

Let us now analyse Generali's shareholders structure. From the diagram below, we can notice that retail shareholders are less than 30%. If we compare this number with Intesa's shares left to the market (77.8%), we see that it is much lower. This implies that a possible acquirer will find it more difficult and costlier to build up ownership, since there is less free-floating. Moreover, there is a strong presence of institutional investors.

Graph 4 – Assicurazioni Generali's shareholder structure

Source: Generali website, Ownership structure

Another notable aspect is the absence of shareholders' agreements. The objectives of shareholders' agreements are to protect the rights of shareholders and ensure that they are treated fairly. Moreover, they tend to eliminate internal conflict of interests between shareholders. Therefore, proxy fights would become more difficult given that the acquirer would have to deal with an entire block of shareholders that have their rights protected, rather than a diverse base of unprotected shareholders. As a matter of fact, shareholders' agreements can also include sections that define fair pricing of the shares. Furthermore, they can decide on which outside parties can enter the company and provide protection for minority shareholders. Therefore, the absence of such agreements is good news for an acquirer.

3.3 Facts

It is January 2017. Rumours start to appear on the press and on the medias at a national and international level. Italy's biggest bank, Intesa Sanpaolo, is seeking to acquire Italy's largest insurer, Assicurazioni Generali. The rumours are then confirmed from an official press release of Intesa Sanpaolo which says that they: "confirm, in line with the 2014-2017 business plan, their interest in industrial growth in the sectors of asset management, private banking and insurance in synergy with its banking networks, including through possible international partnerships". Reading these words, the first thing that comes to mind is Assicurazioni Generali. Recall that, other than being the leading Italian insurer, Generali has the control of Banca Generali, which operates in all the above-mentioned sectors. Moreover, Generali has a strong international presence, that could be used by Intesa to reinforce its position abroad. At the end of the note, it is specified that: "These opportunities, including possible industrial combinations with Assicurazioni Generali, are currently being examined by the Bank's management".[32]

Assicurazioni Generali activated their defensive strategy as soon as they acknowledged that there was an interest in their company. Generali bought 3.01% of Intesa Sanpaolo through an open-ended contract. In other words, Generali borrowed the shares and could have given them back in any occasion paying only the commissions.[33] As a matter of fact, Generali was not interested in these shares. It was, though, interested in protecting itself from a possible hostile takeover. Given the Italian law on cross-shareholdings, of which we spoke about in the first chapter, Intesa could not have bought more than that 3.01% of Generali without making an offer for at least 60% of the company. Another option could have been to buy a majority stake in Mediobanca, first shareholder of Generali, from Unicredit. Nevertheless, this defensive move allowed Generali to slow down, if not interrupt, Intesa's plans of stake building.

Still, Intesa Sanpaolo was not the only acquirer interested in buying Assicurazioni Generali. Also AXA (French) and Allianz (German) seemed interested in industrial combinations with Assicurazioni Generali. As a matter of fact, only the rumours of possible

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[32] Intesa Sanpaolo, News in the press regarding a possible M&A transaction with Assicurazioni Generali, Press release, 24 January 2017

[33] Il sole 24 ore, Generali prepara la risposta a Intesa, 25 January 2017, Laura Galvagni

foreign acquirers were enough for the government to raise the level of attention on the case. Matteo Renzi, the Italian prime minister at that time, started to probe possible Italian acquirers for Generali. The decision taken by Intesa Sanpaolo was not obviously taken by the government, however, they have put a significant pressure to protect Italian interests in such a strategic firm. Nevertheless, not even the government's objectives were aligned, since there was concern on what would the role of Allianz be in this deal.[34]

Whilst AXA had clarified that they had no intention to make a bid for Generali,[35] Allianz remained in silence and did not comment on the rumours. Given anti-trust issues both in Italy and in Germany, a total acquisition of Generali by Intesa and Allianz was seen as difficult. As a matter of fact, Intesa Sanpaolo, Assicurazioni Generali and Unicredit (first shareholder of Mediobanca) were all called by Consob (the Italian antitrust agency) to explain the situation.[36] Moreover, a total buyout of Generali would have implied a high complexity both regarding the deal structure and the integration strategies involved.

[34] La Stampa, L'entusiasmo di Renzi e la prudenza di Gentiloni: cosa pensa il governo delle nozze Intesa-Generali, 25 January 2017, Alessandro Barbera
[35] Reuters, AXA CEO says not interested in Generali -DPA, 25 January 2017, Reuters Staff
[36] La Stampa, La Consob convoca Generali, Intesa e Unicredit. Sanpaolo: "Possibili combinazioni industriali", 24 January 2017

3.4 Scenarios and other possible defensive strategies

So, at this point, what could have happened? Analysts[37] believed that the most plausible scenario could have been Allianz to buy Intesa's insurance business plus a part of Generali later on, while Intesa could have acquired a 5-6 billion euros stake (around 25%) in Generali. This explains Generali's defensive move, to prevent Intesa to begin a stake build up process. Allianz was interested in Generali's European subsidiaries, through which it could have gained geographical expansion and economies of scale. Under this scenario, both antitrust and political issues would have been satisfied. Nevertheless, Intesa would have had to let go one of the largest life insurance branches in Italy in exchange of a stake in Generali. Thus, a possible variation is that Intesa would have agreed with Allianz on a distribution agreement rather than a sale of the whole branch.

Intesa Sanpaolo has always stressed out that its primary interests are that of the shareholders. Therefore, every decision is made to create and distribute value to them. In light of this aspect, Carlo Messina (Intesa Sanpaolo's CEO) said that for any deal to happen there was the need of it to be capital neutral, without applying any capital arbitrage. This includes the Danish compromise, which allows banks to deduct a certain amount from the common equity tier 1 capital of holdings in an insurance company.[38] Moreover, he stated that the 3.4 billion euros dividends commitment for 2017 could not be touched by any kind of M&A deal.[39]

Starting from the fact that a capital neutral bid would be very difficult, there are a few ways to reduce the impact of an acquisition of Generali on Intesa's capital ratios. In a Societe Generale report,[40] it is calculated the effect of a paper deal (stock-for-stock transaction) involving a takeover of 100% of Assicurazioni Generali. They found out that this kind of transaction would not affect Intesa's capital ratios. Nevertheless, they assumed an adoption of the Danish Compromise, which Intesa clearly said that it was not intended to apply such methods.

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[37] Societe Generale Report, 25 January 2017, Assicurazioni Generali: What could happen?
[38] Capital requirements regulation, Art. 36, 46, European Banking Authority, Regulation (EU) No 575/2013 of the European parliament and of the council of 26 June 2013
[39] Reuters, BRIEF-Intesa CEO says assessment on possible Generali move will take all time it needs, 3 February 2017, Reuters Staff
[40] Societe Generale Report, 30 January 2017, Intesa Sanpaolo: Good entry point, with or without Generali

Another scenario was possible. According to a Barclays research,[41] the less capital-absorbing strategy would have been to acquire and break-up Generali. In other words, to acquire the totality of the group and then to sell the non-core geographies. Recall that in Intesa's business plan for 2014-2017 there was the growth in asset management, private banking and insurance sectors as objective. Thus, intuitively, the best divisions for Intesa were Banca Generali and the life insurance division. Nevertheless, there is a huge executional risk on these kind of operations, given the uncertainty on the pricing and disposal of the divisions.

Other scenarios were unlikely to happen. For example, a white knight defensive strategy could have been made either by AXA or by Zurich, for their strategic fit with Generali. However, we said that AXA denied any kind of interest in Generali as soon as the rumours started to leak. For what concerns Zurich, its CEO Mario Greco was having a tough time with his cost cutting program, in that he will have to cut 1.5 billion dollars within 2019.[42] It is therefore unlikely for Zurich to invest in another company. Moreover, M. Greco is the former CEO of Generali. In January 2016, he stated that he was "unwilling to serve another term as CEO of the company at the expiry of his current mandate".[43] Consequently, it is probable that Zurich was not Generali's first choice as white knight.

Another defensive strategy that Generali could have used is asset restructuring. Generali already has assets that can create antitrust problems both for Intesa and for Allianz. Still, it could have divested in assets in which its acquirers were interested, for example its French branch, in which Allianz was looking forward to.

Moreover, Generali could have used the poison pill defence, becoming too large for Intesa or Allianz to takeover. Nevertheless, it is a very risky move and we said in chapter one that it has proved to be value destructive. Also, without a combination of staggered boards it may not be sufficient to avoid a hostile takeover.

[41] Barclays Equity Research, 9 February 2017, Intesa Sanpaolo: Potential bid plans and NPL strategies

[42] Bloomberg, Zurich Cuts Technology Spend as Greco Seeks $1.5 Billion Savings, 17 January 2017, Joe Mayes

[43] Assicurazioni Generali, press release statement, 26 January 2016

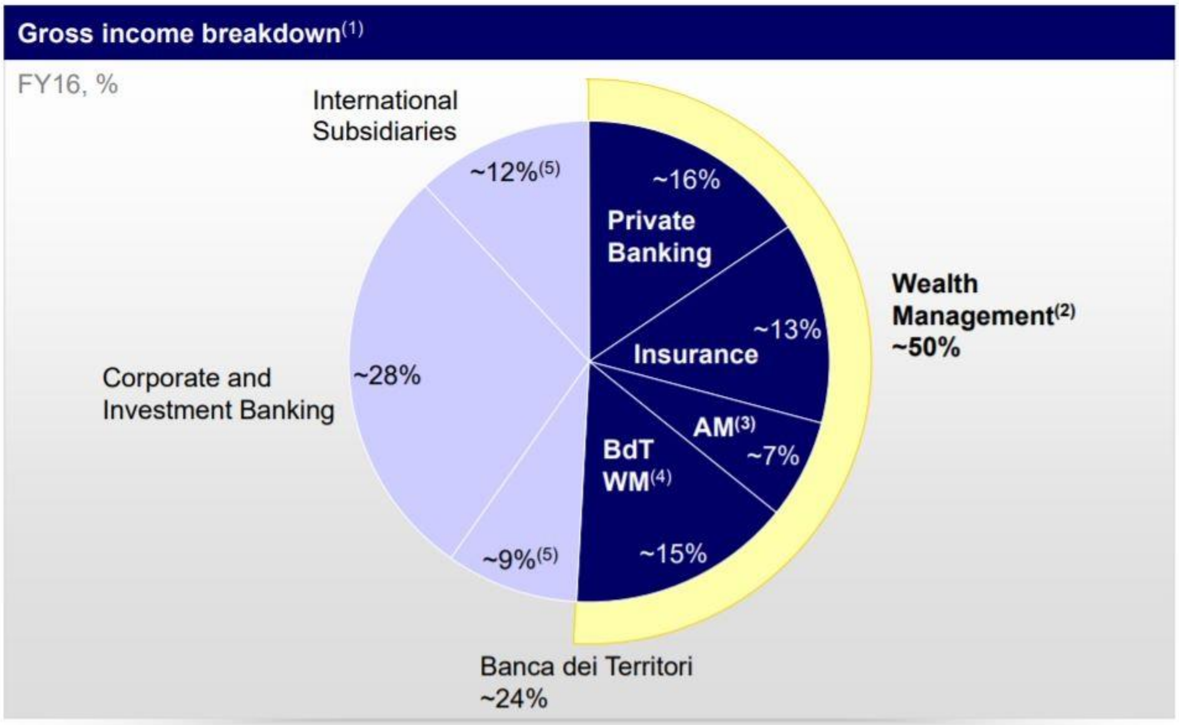
3.5 Rationale of the deal

There are many reasons for which Intesa Sanpaolo started to consider Generali as a possible target. First of all, we mentioned the fact that politics may have played a significant role, at least in the decision of taking in consideration a takeover of Generali. Keeping in mind that Generali has about 65 billion euros of Italian bonds,[44] it would have been a problem if its ownership had passed to a foreign company. Nevertheless, we have to notice that politics already tried to put pressure on Intesa's top management. During summer 2016, due to the problematic situation of Monte dei Paschi di Siena bank, Matteo Renzi knocked on the doors of Unicredit and Intesa to act as white knights and both refused.[45] It is therefore probable that, once more, politics pressures were not the decisive factor that brought Intesa to show an interest in Generali.

As previously written, the focus of the 2014-2017 business plan is to shift the core business from commercial banking to wealth management. The decision has been taken because, given the low growth and low interest rates, Intesa has to search for profitability in other sectors. Since there were no major changes in the macroeconomic scenario, it makes sense that Intesa is interested in Generali. The rationale is to diversify from commercial banking, in line with its strategic plans. Below we can find Intesa's gross income breakdown divided by sectors.

[44] Generali Group, 2017, First half results
[45] Financial Times, Italy races to gain private bailout for Monte Paschi, 26 July 2016, Rachel Sanderson

Graph 5 – Intesa Sanpaolo Gross Income Breakdown



(1) Excluding Corporate Centre
(2) Private Banking includes Fideuram, Intesa Sanpaolo Private Banking, Intesa Sanpaolo Private Bank (Suisse) and Sirefid; Insurance includes Fideuram Vita, Intesa Sanpaolo Assicura and Intesa Sanpaolo Vita; Asset Management includes Eurizon Capital; BdT WM includes ~€1.8bn revenues from WM products included in Banca dei Territori (applying a C/I of ~37%)
(3) Asset Management
(4) Banca dei Territori Wealth Management
(5) Excluding profit from disposal of Setefi and ISP Card
Note: figures may not add up exactly due to rounding differences

Source: Intesa Sanpaolo 2016 results, 3 February 2017

We can immediately notice that half of the pre-tax income comes from wealth management divisions. For what concerns life insurance, Intesa and Generali would have a combined market share of approximately 30% of the Italian market. This would make an eventual merged entity, the largest life insurer of Italy, followed by Poste Vita.[46] As already stressed above, antitrust issues in case of a merger between Intesa and Generali could arise.

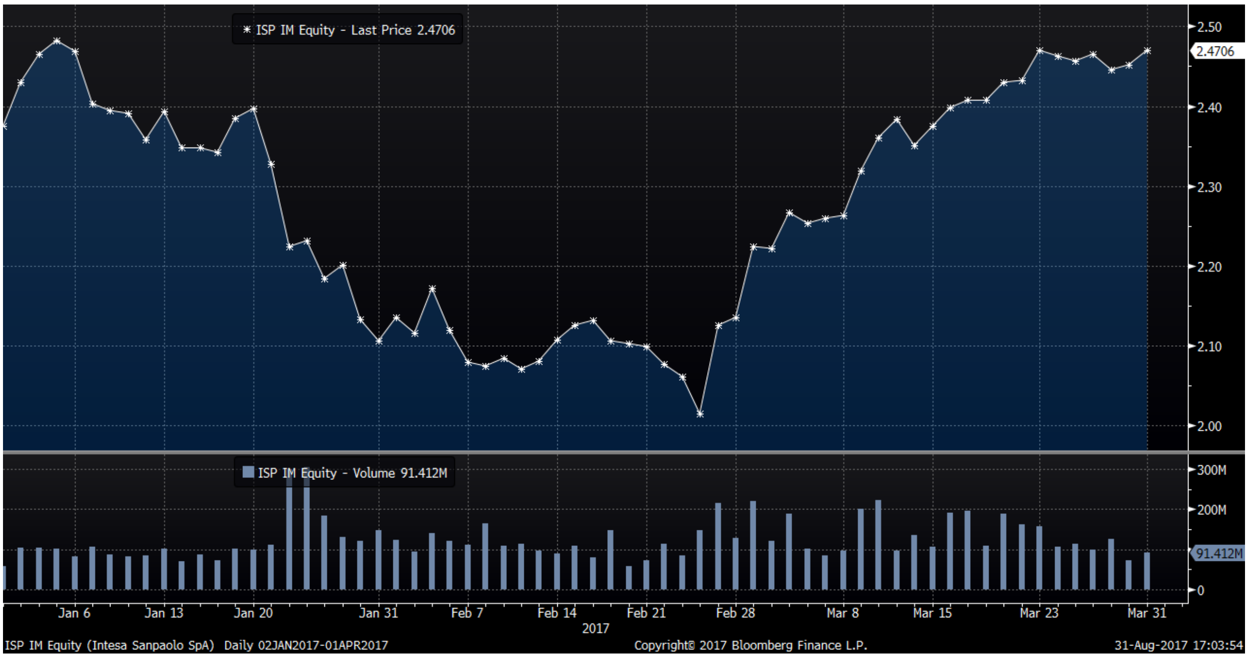
Another division in which Intesa could have been interested, is Banca Generali. Recall that Banca Generali operates both in the private banking and in the asset management sector. Thus, there could be potential synergy creations with Intesa's Banca Fideuram (private banking) and Eurizon capital (asset management).

[46] PWC publication, The Italian insurance market, 2015 figures, p. 4, September 2016

3.6 Would the bancassurance model have worked?

We have seen that there is a strategic fit between Intesa Sanpaolo and Assicurazioni Generali. This implies that there is a possibility of value creation through economies of scope. In other words, there are the fundamentals for a potential new merged entity to extract synergies by offering an increased number of products. Nevertheless, it seems that the market did not believe it this way and reacted negatively to the rumours of a merger. Below the market trend of the Intesa Sanpaolo's share price and volume of trade for the period of January – March 2017.

Graph 6 – Intesa Sanpaolo's share price trend



Source: Bloomberg

Notice how the share price suddenly dropped the 20^{th} of January, when rumours of a takeover started to leak out. A few days later, La Stampa, an important Italian newspaper, wrote the first article on the case[47] and the volumes of shares traded more than doubled. The

[47] La Stampa, Intesa Sanpaolo e Allianz interessate alle Generali, 22 January 2017, Francesco Spini

second slump happened after the official press release made by Intesa, which confirmed possible "industrial combinations" with Generali. The share continued to lose value, except for a few physiological peaks, until the 24th of February. This is the day when Intesa released another official press statement, where it ultimately renounced to acquire Generali. Later on, we will discuss the motivations. However, the remarkable point is the incredible recovery that the stock had the subsequent days and months.

Another reason for which investors' sentiment was not so positive, to use a euphemism, is that they were sceptical about the bancassurance model. One of the most striking cases of failure of the bancassurance model was that of the Dutch, ING Group. Its CEO, insisted that the model did not work because the banking and the insurance sectors have different dynamics and life-cycles, where the first is much quicker than the second. Moreover, he said that being also the people different, putting these two businesses together sets up the foundations for managerial conflicts.[48] Nevertheless, according to our empirical analysis, bancassurance can offer opportunities of value creation under certain circumstances.

So, let us come back to our case. We said that Intesa and Generali had the basis to create synergies through economies of scope. What about economies of scale? Recall that we measured economies of scale as the size of the target relative to the size of the acquirer. We also saw that the size was to be measured in terms of total assets, not of market capitalization. On the one hand, Intesa Sanpaolo's total assets accounted for 725,1 billion euros.[49] On the other hand, Assicurazioni Generali had 521,2 billion euros.[50] These numbers suggest us that there were the possibilities to extract value from economies of scale, as Generali's dimensions are significant with respect to Intesa Sanpaolo.

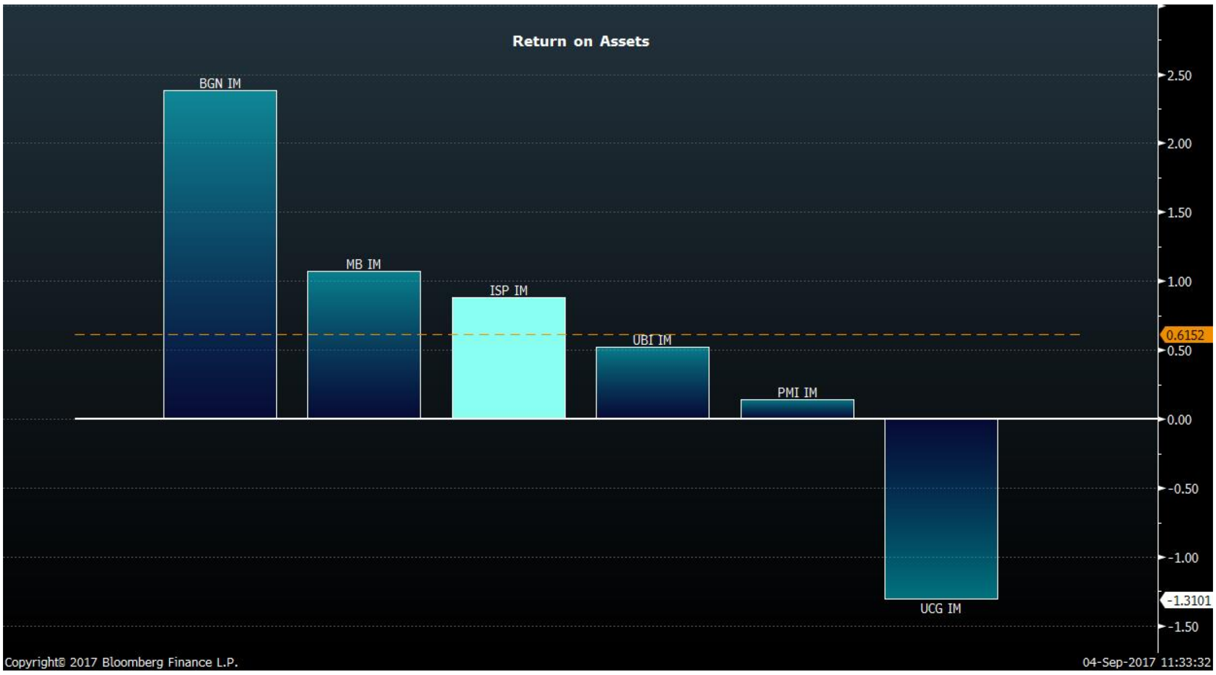
However, market value does count when we are looking at the bidder by its own. In our case, we said that Intesa Sanpaolo is one of the largest banks of the eurozone, with almost 50 billion euros of market capitalization. This infers, according to the model we analysed, that Intesa is an appropriate candidate for a successful implementation of the bancassurance

[48] Financial Times, Outgoing ING chairman attacks bancassurance model, 6 October 2013, Patrick Jenkins
[49] Intesa Sanpaolo, Annual report, 2016
[50] Assicurazioni Generali, Annual integrated report, 2016

model. In that it has already been able to manage correctly an empire, notwithstanding diversity across its operations.

Another key factor to the success of a bancassurance merger, but we could say of a merger in general, is profitability. This is valid both for the bidder and for the target, even if, with respect to value creation, the results we previously analysed showed a slightly greater correlation with the first rather than the second. Intesa Sanpaolo's ROA is 0.88. If we compare it with its peers (Graph 7), we can see that it lies above the average (orange line, 0.62). Moreover, I have included also Banca Generali in this profitability analysis, since Intesa has half of its gross income coming from wealth management, which is also Banca Generali's core business. Nevertheless, we are in a historical period of low interest rates and most of the other banks present in Graph 7 (included Intesa Sanpaolo) perform commercial banking activities that will drag their ROA down. In fact, we can notice how strong Banca Generali's profitability is (ROA 2.39) with respect to its peers. Banca Generali is not the target; however, it is a subsidiary controlled by the target and we saw that in case of a takeover it would have been one of the strongest factors of synergy.

<u>Graph 7 – Intesa Sanpaolo's and its peers' profitability</u>

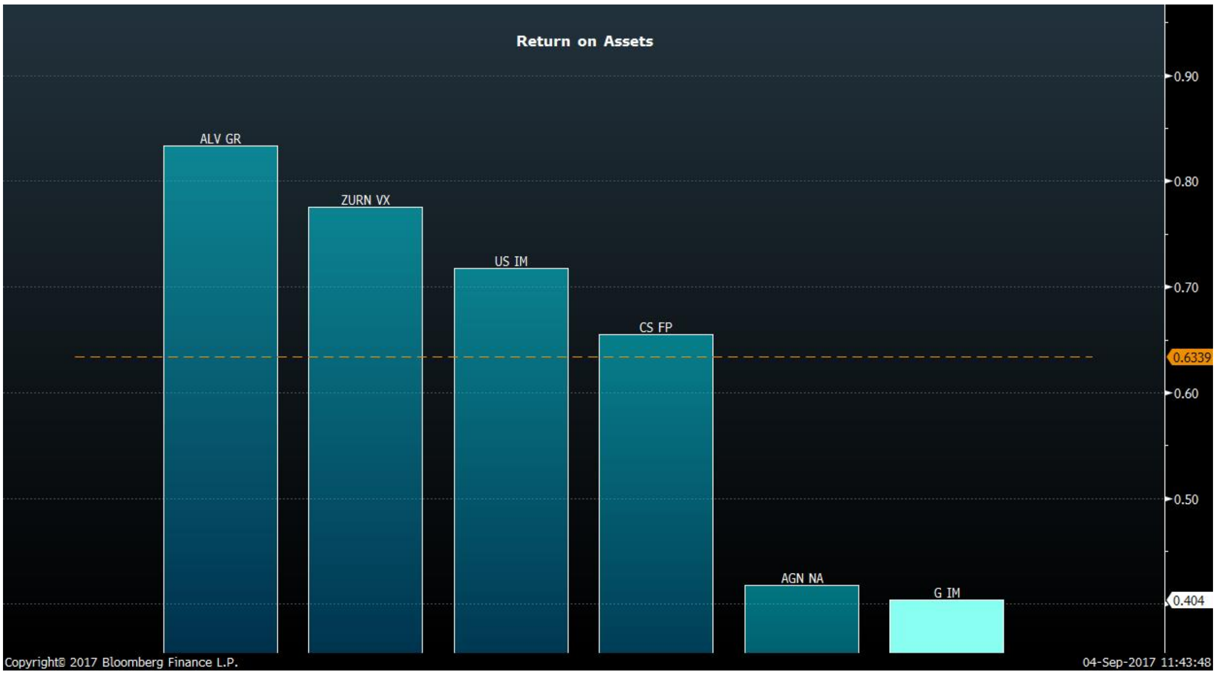


Source: Bloomberg. Starting from the left: Banca Generali, Mediobanca, Intesa Sanpaolo, UBI Banca, Banca Popolare di Milano, Unicredit

So, for what concerns the profitability analysis, the bidder has a good ROA with respect to the industry. Moreover, an important subsidiary of the target has a strong ROA. Now, we have to look also at the target by itself and see if it has a good profitability. In Graph 8, we compared the profitability of Assicurazioni Generali with its peers. It is important to notice that, in this case, the ROA of Assicurazioni Generali, 0.40, is much lower than the average of its peer companies, 0.63.

So, to sum up, from a profitability perspective, the deal has both positive and negative aspects. On one side, the bidder has an above average profitability and also Banca Generali, which is of crucial importance in the deal, has a strong ROA. On the other side, the target is not so strong on profitability. However, we said that it is more important to look at the profitability of the bidder. Moreover, the fact that Banca Generali has a high ROA could balance out the poor performance of Assicurazioni Generali.

<u>Graph 8 – Assicurazioni Generali's and its peers' profitability</u>



Source: Bloomberg. Starting from the left: Allianz, Zurich, Unipol Sai, AXA, Aegon, Assicurazioni Generali

Let us now pass to the governance and geographic diversification section. For what concerns the governance variables, we saw that the only statistically significant variable is CEO ownership. Specifically, we saw that if a CEO owns a significant block of a company, its contribution to value added in takeovers is negative. If we look at Intesa Sanpaolo's shareholder structure (Graph 3), we can see that there is no relevant ownership of the group's CEO, Carlo Messina. Thus, in this case, there are no governance variables that affect the results of a takeover.

From a geographic diversification point of view, the deal has different aspects to analyse. On the one hand, both Intesa Sanpaolo and Assicurazioni Generali are Italian companies. On the other hand, Generali is present in more than 60 countries across the world. Since they are both European companies, their focus is on the European market. However, Intesa could have exploited Generali's strong presence in China, India, Indonesia and Latin America. So, it is a domestic takeover. Still, there are many opportunities of growth in foreign markets. Being that international takeovers are preferred by investors, I believe that this aspect has a neutral effect on the success of the merger.

So, in the end, would the bancassurance model have worked? To answer this question, we have to look at the variables just analysed as a whole and see their impact on a bancassurance merger between Intesa and Generali. Below we can find a table that sums them up.

Table 9 – Variables of the bancassurance model

Variable	**Impact**
Economies of scope	Positive
Economies of scale	Positive
Bidder's size	Positive
Bidder's profitability	Positive
Target profitability	Negative
CEO ownership	Neutral
Geographic diversification	Neutral

Overall, according to the model that we are using as a proxy, it seems that there are the fundamentals for a successful takeover. The only negative aspect is the profitability of Assicurazioni Generali. However, this is balanced out by the good ROA of Banca Generali. Moreover, we said that the bidder's profitability counts more in the process of value creation and Intesa Sanpaolo has an above average ROA. Furthermore, Intesa Sanpaolo is a strong company with a significant market capitalization, which is another plus factor in a takeover. The synergy measures (economies of scale / scope) are both positive and thus, could have contributed in creating value post-merger.

For what concerns the governance measures, we found that the only statistically significant one is the CEO ownership. Here, we saw that there were no significant stakes owned by the CEO that could cause agency problems and interfere with the takeover process. At last, I ascribed to geographic diversification a neutral impact since we saw that international deals are preferred to domestic ones. In our case, we are talking of a domestic deal. Nevertheless, there are numerous subsidiaries across the world that would have been included in an eventual takeover.

3.7 The withdrawal

So, what happened in the end? The 24th of February Intesa Sanpaolo released a statement[51] in which it officially renounced on acquiring Generali. Specifically, it said that "…the management sees no opportunities that fulfil the criteria - in terms of creation and distribution of value for the Bank's shareholders in keeping with the objective of maintaining a leadership position in capital adequacy…". In other words, its focus remains on shareholders. After all, the objective of a good management is to maximize shareholder value. This means though, that the management of Intesa Sanpaolo did not see this deal as value creating. What reasons can there be behind this decision?

One of them is written in the sentence I quoted above. Intesa has a "leadership position" in capital ratios with respect to other banks and wants to maintain it. As a matter of fact, in this chapter, we mentioned the need of Intesa Sanpaolo to pursue a capital neutral deal, that would not affect its ambitious dividend plans. Apparently, the management did not find a deal structure that allowed these conditions to be respected.

I believe the main reason was the overall complexity of the deal. We just mentioned the capital neutral issue. Another problem were antitrust issues. As a matter of fact, remember that Consob called for a meeting all the players of a potential deal to explain the situation. A new merged entity would have become too big to avoid antitrust issues. Moreover, investors were clearly contrary to this deal to happen. This has been reflected in the poor stock performance of Intesa Sanpaolo during the period of management's assessment of the Generali case.

These factors brought Intesa Sanpaolo to withdraw from any kind of interest in Assicurazioni Generali. That notwithstanding, according to my analysis, I believe that a merger between Intesa and Generali had the theoretical fundamentals to work, given the fact that it had the right variables for the bancassurance model to create value.

However, closing this chapter meant opening another one. Intesa continued the press release saying that it will create value for shareholders organically and its new business plan

[51] Intesa Sanpaolo, The management of Intesa Sanpaolo completes the assessment of possible industrial combinations with Assicurazioni Generali and sees no opportunity fulfilling criteria set for the group's growth options, Press release, 24 February 2017

will be a continuity of the existing one. In particular, it aims at a further and significant growth in the wealth management division. Other than this, "a significant development of the non-life insurance business, raising the product penetration with the customer base to the same level as the life insurance business, through appropriate actions in synergy with the bank network". This basically confirms their will to develop internally their insurance division, thus, continuing to believe and invest in the bancassurance model, though, without Generali.

Furthermore, Intesa wants to boost cross-selling through the creation of the first Italian proximity bank, thanks also to the acquisition of Banca ITB (the tobacconists' bank) focused on instant banking. Another focus for the coming years is to significantly improve the asset quality through a reduction of Intesa's non-performing loans (NPL). These are the main objectives for the future years of Intesa Sanpaolo, which do not comprehend Assicurazioni Generali.

Conclusions

I began the thesis describing mergers and acquisitions, understanding the differences between friendly and hostile takeovers. It has emerged that, if possible, it is better to perform a friendly takeover, since the buyer is more likely to pay less for the acquisition and has more time to perform due diligence, other than getting helped by the target to do so. Nevertheless, there are cases in which the only way to perform an acquisition is through a hostile takeover. We also saw that the reason behind a takeover is to create value for shareholders.

Given that the case analysed involved a bank and an insurance company, I had to understand if this value creation was possible by merging companies of these two sectors. To do so, I looked at the bancassurance model. In particular, I performed an empirical analysis to understand if it is a viable and profitable model. The analysis led to the conclusion that, under certain circumstances the model can be profitable, it is therefore worth trying. Moreover, I found out that merging banks and insurers does not significantly affect neither total nor systematic risk.

In the last chapter, I have illustrated what happened between Intesa Sanpaolo and Assicurazioni Generali. I investigated which were the possible reasons behind such interest and analysed which could have been other probable scenarios. Subsequently, I compared the results of the empirical analysis to those of the case. I found out that, from a theoretical point of view, the bancassurance model could have worked successfully, since the two companies had the right characteristics to create value in a bancassurance merger. Nevertheless, in the end, Intesa Sanpaolo decided to withdraw itself from any kind of deal. The main reasons were the complexity of the deal, the will of Intesa to maintain its pay-out and capital ratios, and the negative sentiment of investors with respect to the deal.

At this point, there are two questions left to answer. The first is: can we say that Intesa was right to withdraw from the deal? Here, there is not an answer that is right or wrong. We can only say that, given Intesa's ambitious dividend plans and willingness to keep strong capital ratios, they did not have many alternatives. Nevertheless, we cannot assure that this has been the right path to take. In the sense that, since we saw that the two companies could have theoretically worked well together, it could have been better to conclude the takeover. This, however, would have meant letting go for a while the strict capital ratios and the generous dividend pay-out plan.

The other question to answer is: can Generali consider itself safe and sound from other attempts of takeover? In my opinion, no. The defensive measure Generali took, was specific to reject eventual attacks from Intesa Sanpaolo. As a matter of fact, Generali sold its stake in Intesa, once the deal was definitely over and there were no risks of hostile takeover. Generali's CEO confirmed that the significant ownership in Intesa Sanpaolo, was made exclusively to avoid possible stake-building and protect his shareholders.[52] However, Generali is still vulnerable to other potential attacks, since it has not pursued any other kind of pre-emptive defensive measure.

[52] Il sole 24 ore, Generali ha venduto il 3,04% del capitale di Intesa Sanpaolo, 30 May 2017

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Summary

The thesis is divided into three chapters: Mergers and Acquisitions, The Bancassurance model and Intesa Sanpaolo - Assicurazioni Generali. The first chapter introduces the theory behind mergers and acquisitions. The second chapter is a focus on the bancassurance model, including a review of academic papers and an empirical analysis of the model. At last, the theory will be applied to the practical case of Intesa Sanpaolo and Assicurazioni Generali.

Chapter one starts with a definition of mergers and acquisitions. At first it explains the difference between three types of transactions: all-cash, stock for stock and cash and stock. Then there is a classification of different types of takeovers. Once the definition of mergers and acquisitions is clear, the chapter goes on with the rationale behind them. The main scope, just as in any other project or investment, is value creation. For this reason, buyers usually pay an acquisition premium. The reason to pay a target more than its market price lies behind the concept of synergy. Here, a distinction in made between operating and financial synergies. Subsequently, the ways to achieve this synergy and thus, the rationale behind takeovers are examined. These are: diversification, acquisition of expertise, spread of geographic reach, market power increase and efficiency gains.

The second part of chapter one focuses on hostile takeovers. There is an in-depth description of the whole process concerning the announcement of an official bid. In particular, what happens if the target rejects the initial offer. Both the target's and the buyer's options are examined. If the buyer walks away, then the process ends there. However, if the acquirer insists it wants to buy the target, there are some future combinations. To defend itself from a hostile bid, the target can put in place several defensive tactics. There is a distinction between pre-emptive and reactive strategies. On the one hand, for what concerns pre-emptive strategies, there is a focus on: poison pills, staggered boards, super-majority provisions and golden parachutes. On the other hand, the reactive defensive strategies analysed are: white knight / squire, asset restructuring, recapitalization, greenmail (target repurchases), litigation, pac-man.

The last part of the first chapter lists the agency problems that can occur in a takeover and examines how they can interfere in the decision-making process of the top management. The analysis focuses on: entrenching investments, empire building and politics interference. As a solution to these principal-agent problems, there is a discussion on incentive compensation and monitoring.

Having spoken about mergers and acquisitions, the second chapter begins with a general description of the bancassurance model, which is described as a situation in which banks manufacture and / or distribute insurance products. This part serves as an introduction to the model and lists the possible reasons behind the dissimilar penetration of the model in different countries. One of these reasons is regulation. In fact, the second part of the chapter clarifies the regulatory framework and history of the bancassurance model both in Europe and in the United States.

The chapter goes on with an explanation of the possible structures the bancassurance model can have. These are: contractual agreements, joint ventures and mergers and acquisitions. There are also a few examples of internal development. Moreover, a brief description of assurfinance is made. Basically, it is the same thing. However, in this case it is the insurance companies that sell saving products, exploiting their networks.

The next part focuses on the distribution of insurance products. When this is made by banks, it can be divided into two cross-selling techniques: pure and mixed bundling. Furthermore, the difference between non-life and life insurance products is stressed out. Whilst life insurance products are long term and do not require frequent contacts with the clients, non-life insurance products are the opposite. They require frequent contacts with the clients, leading to high training costs and use of time. This risks to hamper economies of scope. For this reason, the bancassurance model is a predominant distribution channel for life insurance products across several European countries. On the contrary, non-life insurance products are mainly distributed through other selling channels.

The last section of the second chapter contains an empirical analysis of the bancassurance model. It goes through the possible variables that can affect the model and its aim is to establish if the bancassurance model is a viable option of value creation. This part of the chapter is divided into three sub-sections:

1) Economies of scale, scope and profitability

2) Governance and geographic diversification

3) Risk and returns

The first sub-section serves to understand and introduce the model that will be used throughout the section. The variables examined are: bidder's size, profitability, economies of scale and of scope. The aim is to check which of these variables are statistically significant, in which way (positive or negative) and to what extent.

The results are that there exists a positive and statistically significant correlation of the bidder's size with respect to abnormal returns. Moreover, both bidder's and target's profitability are positively correlated with abnormal returns and thus, create value. However, it is of crucial importance that in a bancassurance merger the bidder has a strong ROA (measure of profitability used), mainly because in the post-merger, it will be the bidder that will take control of the new entity.

Economies of scale are found to be significant only if the target's relative size is measured in terms of total assets, rather than market value. However, it is confirmed that economies of scale have a positive impact on abnormal returns. Lastly, also revenue economies of scope are found to be statistically significant. This means that when the merged entity is able to create synergy, increasing its revenues more than the sum of the parts, the likelihood of obtaining abnormal returns rises.

The next sub-section starts with the governance variables. High-quality corporate governance firms are expected to take better investment decisions than badly governed companies. Quality of corporate governance is assessed on three factors: ownership structure, executive compensation and board composition. The results show that most of the corporate governance variables are not statistically significant. Which means that their impact on value added is basically irrelevant. Nevertheless, the "CEO ownership" variable is strongly statistically significant and has a negative impact on abnormal returns. This means that some CEOs who own a high portion of a company's shares are likely to perform value reducing takeovers.

Within this study also a geographic diversification variable has been taken into consideration as a factor affecting the bidder's abnormal returns. It has been found a highly significant and positive relation between the two. Therefore, mergers that focus on the international market are seen better than domestic market deals. In that international takeovers enable domestic companies to easily access foreign markets and human resources.

The last part of the chapter is on risks and returns of the bancassurance model. Value can be created in terms of increased cash flow, risk reduction, or both together. Abnormal returns are a measure of value creation (or destruction) implied by these factors. This analysis tells us, in general, if bancassurance can be considered a profitable model. Bank bidders experience a positive and significant correlation between the merger and abnormal returns. Furthermore, the insurers abnormal returns are positively correlated with the announcement of a merger. However, they are significant only prior to one day. This is probably due to the low sample size.

Thus, we can conclude that the bancassurance model is a profitable and viable model. Nevertheless, the model taken in consideration does not account for the number and order of takeovers made by one single bidder. It has been found that the second mergers, of the same bidders, experience a greater abnormal return than the first ones.

At this point, there is an exploration of risks in bancassurance mergers. Regulation across the world, has prohibited the formation of diversified financial firms until the nineties because regulators were afraid that a failure in the bancassurance model could spread more easily to the entire financial system, rather than keeping separate the entities. The model taken in consideration demonstrates that there are no major changes in the perception of risk. Moreover, none of the results are statistically significant. This means that bancassurance mergers do not alter the bidder's systematic and total risk. Therefore, we can state that deregulation does not affect the stability of the financial system.

In addition, another model is considered to see the effects of bancassurance mergers on risk. Here, a distinction is made between domestic and cross-border deals. All the bidders in this sample are European banks. The results confirm what observed in the previous model, that the bidder's risk is not affected by a bancassurance merger.

For what concerns cross-border deals, we would expect that, given geographic diversification, they would have led to a risk reduction. Nevertheless, it seems that risk increase and reduction effects offset each other. Whereas, in domestic mergers, given the fact that both companies operate in the same country and financial system, their stock returns are highly correlated. Therefore, no significant changes in terms of total risk are observed. So, also according to this model, regulators do not have to worry that bancassurance mergers can cause financial system instability.

At this point the thesis converges to its final chapter, the Intesa - Generali case. The first two chapters serve as an explanation of the framework and the theory necessary to well understand the case. The first two sub-sections of the last chapter introduce the companies involved. Then, there is a description of what happened.

Intesa Sanpaolo is an Italian banking group born in 2007 from the merger of Sanpaolo IMI and Banca Intesa. Intesa Sanpaolo is now the largest banking group in Italy and one of the major groups in Europe. It has approximately 20 million customers, of which more than a half (≈12.3 million) in Italy. Moreover, it counts almost six thousand branches, of which more than one thousand abroad mainly focused in the central-eastern European countries and Egypt. The group is divided in seven business units: banca dei territori, corporate and investment banking, international subsidiary banks, private banking, asset management, insurance and capital light bank.

Assicurazioni Generali was founded in 1831. It has 55 million customers. Since its foundation, it pursued an internationalization strategy. Nowadays, up to 66% of the group's premium income comes from abroad. Its main market is the European one, where it aims to become leader in the retail industry. Moreover, Generali has a strong position in Asia, mainly: China, India and Indonesia. It is also one of the largest foreign insurers in Latin America. Generali distributes its products around the world using a multichannel strategy. Its distribution channels are made of a proprietary sales network of agents and financial advisors, supported by brokers, bancassurance and direct channels.

Generali is not only an insurance company. In 1998 the group founded Banca Generali, which now counts around 250 thousand customers, 52.1 billion euros of AUM (Asset Under Management) and 45 branches across Italy. Its distribution networks are divided by target customer: financial planners and private banking. In 2006 Banca Generali has been listed on the Milan stock exchanged and it is controlled by Assicurazioni Generali, which detains 50.26% of the shares. Its market capitalization is of 3.3 billion euros. Banca Generali controls the totality of: BG Fiduciaria, Generfid and BG Fund Management Luxemburg. The first two companies deal with the group's wealth management services, whilst the third is Generali's asset management product factory.

It is January 2017. Rumours start to appear on the press and on the medias at a national and international level. Italy's biggest bank, Intesa Sanpaolo, is seeking to acquire Italy's largest insurer, Assicurazioni Generali. The rumours are then confirmed from an official press release of Intesa Sanpaolo. Assicurazioni Generali activated their defensive strategy as soon as they acknowledged that there was an interest in their company. Generali bought 3.01% of Intesa Sanpaolo through an open-ended contract. Given the Italian law on cross-shareholdings, Intesa could not have bought more than that 3.01% of Generali without making an offer for at least 60% of the company. Another option could have been to buy a majority stake in Mediobanca, first shareholder of Generali, from Unicredit. Nevertheless, this defensive move allowed Generali to slow down, if not interrupt, Intesa's plans of stake building.

Still, Intesa Sanpaolo was not the only acquirer interested in buying Assicurazioni Generali. Also AXA (French) and Allianz (German) seemed interested in industrial combinations with Assicurazioni Generali. As a matter of fact, only the rumours of possible foreign acquirers were enough for the government to raise the level of attention on the case.

Whilst AXA had clarified that they had no intention to make a bid for Generali, Allianz remained in silence and did not comment on the rumours. Given anti-trust issues both in Italy and in Germany, a total acquisition of Generali by Intesa and Allianz was seen as difficult. As a matter of fact, Intesa Sanpaolo, Assicurazioni Generali and Unicredit (first shareholder of Mediobanca) were all called by Consob (the Italian antitrust agency) to explain the situation. Moreover, a total buyout of Generali would have implied a high complexity both regarding the deal structure and the integration strategies involved.

The thesis then goes through alternative scenarios that could have developed. These are:

1) Allianz buys Intesa’s insurance business plus a part of Generali later on, while Intesa acquires a 5-6 billion euros stake, around 25%, in Generali (not possible because of Generali’s defensive move)
2) A paper deal (stock-for-stock transaction) involving a takeover of 100% of Assicurazioni Generali
3) Acquire the totality of Generali and then sell the non-core geographies (acquire and break-up strategy)

Other scenarios were unlikely to happen. Nevertheless, alternative defensive strategies have been taken in consideration. Such as: white knight, asset restructuring and poison pill.

At this point there is a focus on the rationale of the deal, why would Intesa be interested in acquiring Generali? Politics may have played a significant role, at least in the decision of taking in consideration a takeover of Generali. Keeping in mind that Generali has about 65 billion euros of Italian bonds, it would have been a problem if its ownership had passed to a foreign company. Nevertheless, it is explained that it was not the decisive factor that brought Intesa to show an interest in Generali.

Rather, the focus of the 2014-2017 business plan is to shift the core business from commercial banking to wealth management. For what concerns life insurance, Intesa and Generali would have a combined market share of approximately 30% of the Italian market. This would make an eventual merged entity, the largest life insurer of Italy, followed by Poste Vita. Moreover, there could be potential synergy creations between Banca Generali and Intesa’s Banca Fideuram (private banking) and Eurizon capital (asset management).

At this point, there is a match between the results of the empirical analysis and the Intesa - Generali case. To understand the overall effects of the variables on this case of bancassurance merger, I have built up a table that sums them up, including their impact on the deal.

Variable	Impact
Economies of scope	Positive
Economies of scale	Positive
Bidder’s size	Positive
Bidder’s profitability	Positive
Target profitability	Negative
CEO ownership	Neutral
Geographic diversification	Neutral

Overall, according to the model that we are using as a proxy, it seems that there are the fundamentals for a successful bancassurance merger. The only negative aspect is the profitability of Assicurazioni Generali. However, this is balanced out by the good ROA of Banca Generali. Moreover, the bidder’s profitability counts more in the process of value creation and Intesa Sanpaolo has an above average ROA. Furthermore, Intesa Sanpaolo is a strong company with a significant market capitalization, which is another plus factor in a takeover. The synergy measures (economies of scale / scope) are both positive and thus, could have contributed in creating value post-merger.

For what concerns the governance measures, the only statistically significant one is the CEO ownership. Here, we saw that there were no significant stakes owned by the CEO that could cause agency problems and interfere with the takeover process. At last, I ascribed to geographic diversification a neutral impact since we saw that international deals are preferred to domestic ones. In our case, we are talking of a domestic deal. Nevertheless, there are numerous subsidiaries across the world that would have been included in an eventual takeover.

So, what happened in the end? The 24th of February Intesa Sanpaolo released a statement in which it officially renounced on acquiring Generali. The thesis goes through the possible reasons behind this decision.

Intesa has a "leadership position" in capital ratios with respect to other banks and wants to maintain it. Apparently, the management did not find a deal structure that allowed these conditions to be respected.

I believe the main reason was the overall complexity of the deal. We just mentioned the capital neutral issue. Another problem were antitrust issues. A new merged entity would have become too big to avoid antitrust issues. Moreover, investors were clearly contrary to this deal to happen. This has been reflected in the poor stock performance of Intesa Sanpaolo during the period of management's assessment of the Generali case.

These factors brought Intesa Sanpaolo to withdraw from any kind of interest in Assicurazioni Generali. That notwithstanding, according to my analysis, I believe that a merger between Intesa and Generali had the theoretical fundamentals to work, given the fact that it had the right variables for the bancassurance model to create value.

However, closing this chapter meant opening another one. Intesa continued the press release saying that it will create value for shareholders organically and its new business plan will be a continuity of the existing one. In particular, it aims at a further and significant growth in the wealth management division. Other than this, "a significant development of the non-life insurance business, raising the product penetration with the customer base to the same level as the life insurance business, through appropriate actions in synergy with the bank network". This basically confirms their will to develop internally their insurance division, thus, continuing to believe and invest in the bancassurance model, though, without Generali.

Furthermore, Intesa wants to boost cross-selling through the creation of the first Italian proximity bank, thanks also to the acquisition of Banca ITB (the tobacconists' bank) focused on instant banking. Another focus for the coming years is to significantly improve the asset quality through a reduction of Intesa's non-performing loans (NPL). These are the main objectives for the future years of Intesa Sanpaolo, which do not comprehend Assicurazioni Generali.

At this point, there are two questions left to answer. The first is: can we say that Intesa was right to withdraw from the deal? Here, there is not an answer that is right or wrong. We can only say that, given Intesa's ambitious dividend plans and willingness to keep strong capital ratios, they did not have many alternatives. Nevertheless, we cannot assure that this has been the right path to take. In the sense that, since we saw that the two companies could have theoretically worked well together, it could have been better to conclude the takeover. This, however, would have meant letting go for a while the strict capital ratios and the generous dividend pay-out plan.

The other question to answer is: can Generali consider itself safe and sound from other attempts of takeover? In my opinion, no. The defensive measure Generali took, was specific to reject eventual attacks from Intesa Sanpaolo. As a matter of fact, Generali sold its stake in Intesa, once the deal was definitely over and there were no risks of hostile takeover. Generali's CEO confirmed that the significant ownership in Intesa Sanpaolo, was made exclusively to avoid possible stake-building and protect his shareholders. However, Generali is still vulnerable to other potential attacks, since it has not pursued any other kind of pre-emptive defensive measure.