UniCredit

Dear Shareholders,

As you may have seen, the Proxy Advisors have published, in these days, a recommendation to vote "AGAINST" on a few Remuneration items.

We were disappointed to see this outcome, not least because it is apparent that some elements have not been fully taken into consideration in making this recommendation and some of the points used to substantiate the opposition are inaccurate.

Hence, we are taking the opportunity with this letter to present our view on the matter.

1. **Proxy advisors recommend an AGAINST vote on the Remuneration policy because of**
   a. **the 30% increase fixed pay increase in favour of the CEO (ISS +GL)**
   b. **the introduction of a discount on the share conversion price of equity awards that could lead to an excessive increase in the CEO total pay (ISS + GL)**
   c. **the failure to change the termination payments policy in response to 2021 shareholder's criticism (ISS)**

a) the 30% increase fixed pay increase in favour of the CEO

We understand the attention on the review of the CEO package. However, the Board believes that this is warranted not only to make sure we have a properly operating incentive system, but also given we have exceeded the original UniCredit Unlocked ambitions, with a stepped-up run rate across our three levers, and with the bank delivering a return on tangible equity up 60% and net profit up 85% vs the average of 2017-19.

The bank is structurally improved, demonstrated in its delivery of an historic eight consecutive quarters of year-over-year growth and exceptional per-share value creation, creating an impressive track record. This positive performance translated into strong returns for shareholders, with TSR the best of the peer group in the period 2021-22, as an outcome of our distribution strategy as well as share price performance.

Reading the Proxy Advisors' report, we feel that there might be confusion on what is really the content that is up for voting and hence we want to clarify this, as the Italian context may not be always extensively known.

The increased quantum of fixed salary is the one element of this proposal that is an act of the Board and is not voted on at the AGM since it is resolved in line with the target pay policy already approved in 2022. As such, the resolution to vote down the proposal will not impact the salary decision. The salary review could, in principle, have been disclosed only in the context of the remuneration report of 2024 (that is up for a consultative vote only) – but the Board decided to be clear on the course of action as well as on the rationales that accompany it, for the sake of having a constructive and transparent relationship with its shareholders' base.

Therefore, investors' focus should not be on the fixed salary, but instead on the new components designed to reflect investors' feedback from last year. These include but are not limited to: the reduction of variable target compensation in order to keep overall target compensation flat year on year; the new floor and ceiling which drive a steeper payoff curve, the adjustments to the increase in the equity component to 100% of variable pay, the increased shareholding requirement, and the new stretch targets. All to drive long term alignment with shareholders.

To vote down this proposal will force the policy to reflect the old KPIs (those that were in existence in 2022) while not affecting the new level of fixed compensation. This would mean that the CEO overall renumeration at target would increase as opposed to remaining flat, that the payoff curve would be much

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less demanding that the one proposed, and that the proposed adjustments to the KPIs that reflect last year's feedback from shareholders cannot be put into place. Furthermore, it would force the split of variable to revert to the 20 / 80 cash-share split rather than the best-in-class proposal of 100% of equity for all variable compensation, which ensures alignment with shareholders. The increase of minimum shareholding requirements from €5 million to €9.75 million (i.e. the minimum level of shares the CEO must hold for the whole duration of your employment) would also be eliminated.

In contrast our newly proposed structure is meritocratic, rewarding continued success with clear shareholder alignment, but in equal measure, it is punitive if the leadership does not deliver. It is an enhanced structure that fixes the flaw of the hiring package within the EU ratio limit between variable and fixed remuneration and reflects specific feedback from investors.

The impact of these changes on the pay benchmarking versus the European peer group we adopt for all compensation decisions is moderate, and we remain within the third quartile of the market. At this time of war for talent, our organisation cannot afford to have an incentive system for the CEO which is not aligned with the philosophy we apply to the rest of the organisation.

We are also not making these changes in a vacuum. This is alongside the steps we are taking to create a safe, inclusive, and fair workplace amid global macroeconomic uncertainty. We have launched several initiatives to support employees facing high inflation (€80 million in 4Q22), to close the gender pay gap (€100 million over three years), and to reward adequately our people's performance (c. €250 million of variable remuneration increase since 2020, with c. 75% going to the non-executive population), as widely disclosed in our Remuneration Policy.

While financial success is just one piece of the puzzle, it is this which will enable us to fulfil our other, more fundamental roles as the engines of social progress. It will let us support the communities we serve, offering assistance both financial and otherwise, as we have done recently with initiatives such as UniCredit per l' Italia, and empower our Foundation to do more philanthropic work. The longer the sustained success and subsequent financial performance is, the greater the social impact the bank can achieve.

b) <u>the introduction of a discount on the share conversion price of equity awards that could lead to an excessive increase in the CEO total pay</u>

As repeatedly reinforced in our remuneration policy we believe in meritocracy and alignment to shareholders' interest. As such, we believe that any instrument should be properly priced, in a manner that is aligned to the performance (good and bad) that investors experience during a certain period of time.

Because of the EU banking regulation (that prohibits the distribution as well as the accrual and ex-post payment of dividends for unvested shares during their deferral period) the symmetry between shares traded on the market and the ones granted to executives under incentive schemes is altered. As can be easily proven by referring to any asset-pricing model or the direct observation of the relevant market, the price of a dividend-bearing asset is intrinsically different to any "zero-coupon" version of the same underlying.

As such, through this proposal we are simply aligning the value of the equity awards eventually granted under a remuneration scheme to their proper market-value (by always using public, market data like the futures on dividends). This is a tried and tested mechanism, already adopted by around 50% of our peers (both on the international and domestic markets), who use similar methodologies to convert their equity awards, based notably on these proxy advisors' support of their policies.

Once this is fixed, the ultimate value of equity awards for any executive depends on the evolution of the actual share price on the market, as required by regulation as well as explicit investors' demand. Clearly, whilst an executive will be granted shares whose value will have increased if the bank has performed well during the period that their compensation award is related to, if the bank does not perform well in a given year, the executive, just like shareholders, will be negatively impacted as the value of the shares awarded

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will be lower. Furthermore, in case the bank underperforms the long-term sustainable conditions, the number of shares will be further decreased. This is true alignment with shareholders.

Glass Lewis was also contesting the fact that not enough transparency was given on the actual calculation and possible impact on the share count of the new measure. As the share conversion price will be determined based on the market share price and futures on dividends up to the AGM date, it is factually impossible to disclose those details when the materials are published (ie one month before AGM, when those parameters are going to be determined).

c) the failure to change the termination payments policy in response to 2021 shareholder's criticism

Given the amount of time spent with the proxy advisor to explain the specific focus that we have included in the remuneration report on the matter, it is disappointing that the details of this element have remained misunderstood.

Our Termination policy must be evaluated within the Italian regulatory framework and within the context of Italian labor law, which has a clear protective approach. All banking executives are in fact bound to a national agreement which also includes severance clauses that are significantly higher than our policy (up to 41 months of total compensation plus up to 12 months of fixed for non-compete agreements) coupled by proper deferral and malus/claw back clauses according to Bank of Italy requirements.

UniCredit's policy's limit of 24 months of total compensation is all-inclusive, embedding the contractual notice, calculated severance amount and possible non-competition agreement. These details must be factored in, in order to properly compare our policy in the market on a *like-for-like* basis, as some of those elements are dictated by the above-mentioned national contract and not all peers present an all-inclusive policy. The example ISS uses, is inaccurate because on a *like-for-like* basis the severance arrangements for Intesa Sanpaolo's Chief Executive would arrive to above 14 million euros, as per our calculations.

The 15 million euros max limit is a theoretical cap and not a guaranteed severance arrangement. UniCredit termination payments policy (available on our website) and severance calculations are based on a specific formula considering tenure, actual performance achieved over time and other specific factors (as per board judgement) that determine the payable amount.

We have further clarified in the 2023 remuneration report our approach to the termination policy, especially in the context of Italian law, and our different, more comprehensive approach versus other players in the domestic market. Despite this and our explanations directly to ISS (via a letter in March 2022 and our engagement with ISS in both February and March 2023), ISS has chosen to compare our policy again inaccurately with a peer without acknowledging the differences. Furthermore, the policy is unchanged since we approved it for the last time in 2021, notably with ISS' support on the resolution.

To show responsiveness and attention to Shareholders' inputs, and despite the legal difficulties from the existence of specific national contract which are binding on this matter, no change was applied to the existing Termination payments policy (which means that, for the CEO, the two years general limit could potentially be unapplicable)

2. **Proxy advisors recommends an AGAINST vote on the 2023 incentive system because of**
    - **d. the above-mentioned introduction of the Dividend Adjusted Market Price, (ISS +GL)**
    - **e. The existence of a compensatory mechanism according to which the over-achievement of one or more goals can offset the potential underperformance of other objectives (ISS)**
    - **f. The long-term objectives attached to the plan may prove undemanding with a significant qualitative component left to board discretion (ISS)**

Further to the points mentioned above on the dividend discount, we would note the following

d. KPIs compensation within the scorecard

In the uncertain and volatile markets in which the bank needs to operate, the achievement of certain ambitions may depend on heterogenous factors that are not attributable to a proper performance review of the bank or any of its executives.

While the structure of the Incentive System effectively allows for the over-performance of certain KPIs to offset underperformance of other KPIs, the flexibility that the provision gives is clearly constrained and the following should be considered:

a. the "compensation" mechanism is only permitted in favour of KPIs whose achievement level is above the minimum threshold (e.g. for net revenues only if the result is above 17.1 bn eur)
b. any overachievement is weighted according to the single KPI's relevance in the scorecard and capped at 140 pts (e.g. for net revenues, weighting 20% in the scorecard, the max "compensation impact" is +4 points i.e. 20%*[140-120] pts)
c. the maximum 120 pts of the overall scorecard cannot be overcome in any case

We must also remember that the RemCo and the Board still retain unlimited downward discretion, so they are equipped with any lever to properly manage the outcome of the scorecard. Furthermore, the variable payments, which are fully granted in equity provide an additional layer of connection between remuneration and actual company performance.

e. Undemanding LT targets

The 2023 incentive system is based on the targets of the new guidance to the market, well above UniCredit Unlocked and previous run rate for all financial KPIs. Namely:

- Net Revenues: 18.5 bn eur at target (+12% vs UU, +17% vs avg 2017-2019), 19.9 bn eur at max (+20% vs UU, +26% vs avg 2017-2019)
- Cost/income: 48.3% at target (-5ppts vs UU, -8ppts vs avg 2017-2019), 45.9ppts at max (-7ppts vs UU, -10ppts vs avg 2017-2019)
- Costs: 9.7 bn eur at target (-0.9% vs UU, -7% vs avg 2017-2019), 9.5 bn eur at max (-1.2% vs UU, -9% vs avg 2017-2019)
- Net profit 5 bn at target (+31% vs UU, +77% vs avg 2017-2019), 5.5 bn eur at max (+45 vs UU, +94% vs avg 2017-2019)

Moreover, a tighter and steeper pay-curve is provided for each financial KPI, with minimum performance thresholds materially raised from the original 70% linear approach, before variable compensation becomes payable[1], whilst creating room to reward performance above targets

As per the shape of our incentive scheme, the LT goals come as a second performance gateway that can modify any award achieved under the short-term scorecard. The "double performance gate" is a structural difference to standalone LTI plans and includes the requirement to maintain a level of sustainability and value creation in the long run: without which, the awarded shares get reduced. In this vein the long-term targets on profitability above the cost of capital to testify our commitment to sustainable value creation. Specifically on long-term performance conditions:

- The reference target of RoTE has been increased from >7% to 11% i.e. +4ppts and above UniCredit Unlocked 2024 ambition of c. 10%
- The minimum RoTE threshold – ie the level at which bonus begins to be earned – has been raised from 2.3% to 5.5% i.e. +2.2ppts

[1] For example: Entry threshold for Net Revenues: from 11.4 bn eur in 2022 to 17.1 bn eur in 2023 (+50%), Cost/income: from 71.5% in 2022 to 50.7% in 2023 (-29%); Opex: from 12.7 bn eur in 2022 to 9.9 bn eur in 2023 (-22%); Organic capital generation: from 105 bps in 2022 to 120 bp in 2023 (-14%)

- The max upside level moves from 8.4% to 13% i.e +55% with a lower multiplier effect on pre-award (from +30% to +20%)

The weight of the non-financial objectives was reduced to 20% (from 30% in 2022) and it fully matches all commitments taken by the organization on the ESG and sustainability agenda. The fact that the timeframes did not match the time horizon of the incentive plan (that covers the period between 2024 and 2026, against current strategy targets ending in a variety of end points from 2024 to 2030) made it inevitable that the appraisal of this goal was centered on a qualitative basis, substantiated with KPIs and numbers coming from the application of the strategy, that we publicly committed to disclose on ex post basis.

We'd also like to remind that the element of discretion of the Board (unlimited downward and max +20% upward) is overarching and aims at making sure the outcomes of the incentive system are appropriate and reflective of the true demonstrated performance. This has been an element of the incentive system for multiple years, was always supported by ISS in their analysis of the past years and never flagged as a contentious point in the many meetings we had with them.

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We genuinely hope that this letter better clarifies the points raised by the proxy advisors and provides you with more information for your final voting decision. We have attentively listened to the concerns raised in the 2022 AGM season and believe that we have addressed them on a forward-looking basis.

This policy is the framework to support the execution of a significant improvement of the UniCredit Unlocked plan that all investors received extremely well upon its presentation, it ensures we can navigate challenging times, retain key people and always remain fully aligned to you as our shareholders.

We remain at your disposal should you wish to discuss the matter further in a dedicated call or please email us with any of your questions.

Sincerely,

Jeffrey Alan Hedberg
Chairman Remuneration Committee