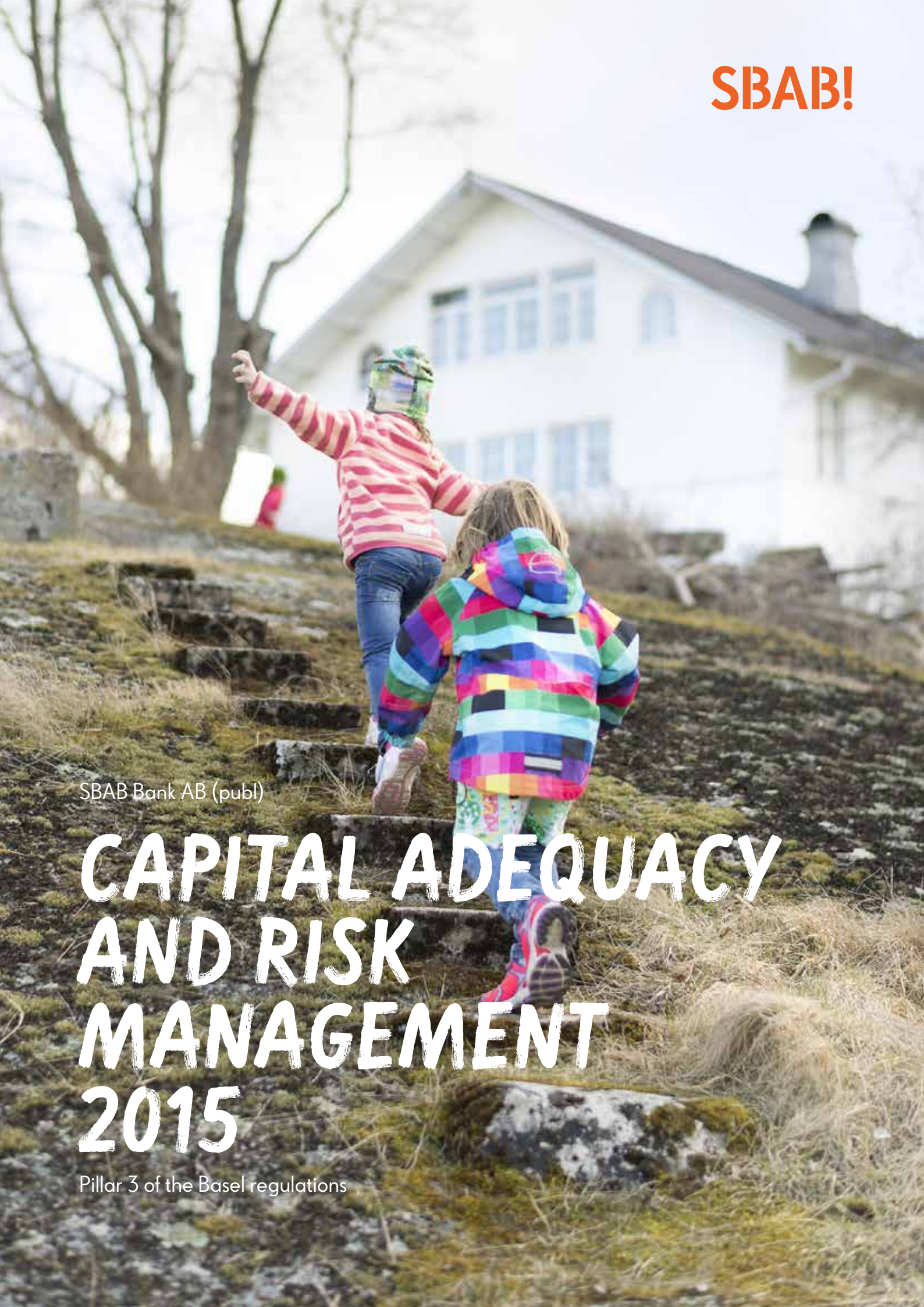

SBAB Bank AB (publ)

CAPITAL ADEQUACY AND RISK MANAGEMENT 2015

Pillar 3 of the Basel regulations

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GLOSSARY

CHAPTER
4 RISK MANAGEMENT AND RISK ORGANISATION

Asset and Liability Committee (ALCO)
Body that handles matters relating to risk and capital planning, which are then addressed by Executive Management and the Board of Directors.

The European Parliament and Council's directive on authority to conduct operations in credit institutions and on the supervision of credit institutions and securities companies 2013/36/EU – CRD IV
Common European regulations on risk management and capital adequacy.

The European Parliament and Council's recommendation on supervisory requirements for credit institutions and securities companies No. 575/2013 – CRR
Common European regulations on risk management and capital adequacy.

Internal capital adequacy assessment process (ICAAP)
Process according to Article 73 of CRD IV for calculating the combined capital requirements taking into account all risks, risk weight floors for residential mortgages and stress tests.

CHAPTER
5 CAPITAL ADEQUACY

Perpetual subordinated debentures
Perpetual subordinated debentures have a maturity that is essentially unlimited, but they can be repurchased if a licence is obtained from the Swedish Financial Supervisory Authority.

Internal ratings-based approach (IRB method)
The IRB approach is used to calculate the company's statutory capital requirement for credit risk. The foundation IRB approach entails that the institution is only to estimate the parameter PD. In the advanced IRB approach, the institution is to estimate, in addition to PD, one or several of the parameters CCF, LGD and M (maturity).

Own funds
Own funds consist primarily of equity and subordinated debentures and act as a buffer against unexpected losses

Capital requirements under Pillar 1
Refers to the minimum amount of capital that the company is to have in accordance with CRR and CRD IV, the Special Supervision of Credit Institutions and Investment Firms Act (2014:968), the Capital Buffers Act (2014:966) and the Swedish Financial Supervisory Authority's regulations (FFFS 2014:12). These provisions also include transitional regulations deriving from Basel I.

Total capital ratio
Own funds divided by the risk exposure amount.

Common Equity Tier 1 capital
Tier 1 capital less additional Tier 1 instruments. Consists primarily of equity.

Minimum capital requirement
The lowest amount that the company is permitted to have as own funds.

Additional Tier 1 instruments
Additional Tier 1 instruments generally comprise perpetual subordinated debentures that meet the requirements in Article 52 of the CRR. According to the transitional regulations, older additional Tier 1 instruments may also be included in Tier 1 capital.

Tier 1 capital
Tier 1 capital mainly comprises equity and additional Tier 1 instruments.

Risk exposure amount in accordance with Basel I
All balance-sheet and off-balance sheet assets are weighted according to risk. Under the regulations of Basel I, this is performed on a standardised basis. Assets are divided into categories based on risk, whereby they are multiplied by a number of pre-established risk weightings, primarily 0 percent, 20 percent, 50 percent and 100 percent of the nominal amount.

Risk exposure amount in accordance with Basel III
The regulations of Basel III permit the use of the IRB approach, within the framework of Pillar 1, to establish risk exposure amounts for balance-sheet and off-balance sheet exposures based on SBAB's own models for credit risk, market risk and operational risk. The risk weightings of other exposures are determined on a standardised basis, in appropriate cases based on the counterparty's rating.

Tier 2 instruments
Subordinated debentures that meet the requirements in Article 63 of the CRR may be included in own funds. According to the transitional regulations, older Tier 2 instruments may also be included in own funds. If the remaining maturity is less than five years, a deduction will be made based on the remaining number of days.

CHAPTER
6 INTERNAL MODEL FOR CALCULATING CAPITAL REQUIREMENTS

Economic capital
Economic capital is based on models in which SBAB assesses quantifiable risks. This constitutes an important component in, for example, pricing, financial control and the amount of own funds.

Exposure At Default (EAD)
Exposure at time of default. To calculate the EAD for off-balance sheet exposures, the unutilised amount is multiplied by a credit conversion factor (CCF).

Capital requirements under Pillar 2
Are based on economic capital which, in combination with capital based on stress tests and capital for further risk, comprises the company's assessment of the appropriate size of risk capital. In accordance with Pillar 2, the capital requirement may not be less than the capital standardised per risk type in accordance with Pillar 1.

Value at Risk (VaR)
Measure of the maximum expected loss at a given level of security and over a defined time period

CHAPTER
9 CREDIT RISK IN LENDING OPERATIONS

Expected Loss (EL)
The calculated expected loss must be covered by earnings from operating activities, while unexpected losses must be covered by the company's equity. EL is arrived at by calculating the risk associated with each individual loan using a statistical model based on a long time period. EL is measured through the formula EL = PD*LGD*EAD.

Off-balance sheet item
Commitment, pledged collateral or similar item that is not recognised in the balance sheet because it is unlikely that it will be necessary to realise or utilise it, or because, due to its extent, it cannot be calculated with sufficient reliability. Off-balance sheet items may also comprise potential commitments, meaning it is uncertain whether the commitment exists.

Credit Conversion Factor (CCF)
Percentage of an off-balance sheet item that is utilised at the time of a possible future default.

Loan to Value (LTV)
Extent of a loan in relation to the value of pledged collateral, meaning the loan-to-value ratio.

Loss Given Default (LGD)
Share of loss in the event of default.

Probability of Default (PD)
Probability of default of a customer or counterparty within a year.

CHAPTER
10 FUNDING

Euro Medium Term Covered Note Programme (EMTCN)
International funding programme for issuance of covered bonds

Euro Medium Term Note Programme (EMTN)
International funding programme for medium and long-term non-secured senior funding.

Credit Support Annexe (CSA)
Supplement to the ISDA Master Agreement that regulates the provision of collateral in connection with a derivative transaction.

Global Master Repurchase Agreement (GMRA)
International standardised agreement for repurchases

CHAPTER
11 CREDIT RISK IN THE FUNDING OPERATIONS

International Swap and Derivatives Association (ISDA) Master Agreement
Framework agreement that regulates the rights and obligations between the parties to a derivative transaction, primarily the netting of debt in the event of bankruptcy.

CHAPTER
13 LIQUIDITY RISK

Liquidity Coverage Ratio (LCR)
Liquidity risk measurement that measures the relationship between liquid assets and a 30-day net cash outflow in a stressed scenario.

Survival horizon
Measurement of the number of days over which liquidity needs can be met in a stressed scenario without access to new liquidity.

Net Stable Funding Ratio (NSFR)
Liquidity risk measurement of a structural nature, which indicates the stability of the Group's funding in relation to assets.

1 INTRODUCTION

In this report, SBAB discloses information on capital adequacy and risk management based on the European Parliament and Council's recommendation on supervisory requirements for credit institutions and securities companies No. 575/2013 and the Swedish Financial Supervisory Authority's recommendation (FFFS 2014:12) on regulatory requirements and capital buffers. This report pertains to the consolidated situation and the conditions prevailing on 31 December 2015, unless otherwise specified. For periodic information, please refer to the interim reports.

SBAB Bank AB (publ) is owned by the Swedish state. Its operations, which consist principally of deposit operations and residential mortgage lending to private individuals, tenant-owner associations and property companies in Sweden, are characterised by a low level of risk. The Common Equity Tier 1 capital ratio decreased to 28.6 percent in 2015, mainly due to increased growth in the lending portfolio. The loan loss level is low (0.01 percent).

The credit risk in SBAB's operations rose over the year as a consequence of increased lending. Over the year, the credit rules have been made more stringent for new lending, including a decision by SBAB to reduce the amortisation period for residential mortgages with a loan-to-value ratio in excess of 70 percent from 15 to 7.5 years and to limit the debt ratio[1] to 6 for new loans, with the purpose of ensuring that the good credit quality of the lending portfolio remains.

Liquidity risk decreased as a consequence of extended funding, increased deposits from the public and a larger liquidity reserve. Over the year, market risk declined due to the liquidity portfolio largely being transferred from the trading book to the banking book.

New common regulations on supervisory requirements for credit institutions were adopted by the EU and have been applied since 1 January 2014. The regulations serve to increase the stability of the international banking sector and include capital adequacy and major exposures, requirements regarding liquidity coverage and debt/equity ratio, as well as an opportunity for the authorities to introduce capital buffers that can be used to mitigate systemic risk and economic fluctuations. The changes entail increased capital requirements and demand increased quality of capital compared with the current regulations. Within the framework of these regulations, Swedish authorities have announced additional national capital requirements regarding the financing of housing.

The pace of regulatory change has remained high and during the year, the EBA and the Basel Committee presented additional proposals for changes, aimed at increasing transparency and making credit institutions more resilient to disruptions in the market. Proposals have been submitted regarding new common reporting rules and a new standardised method that involves an increased requirement for Common Equity Tier 1 capital.

SBAB is well capitalised, and to retain a strong capital position, SBAB's Board of Directors has adopted a new policy for capital. The Common Equity Tier 1 capital ratio shall exceed the internally assessed Common Equity Tier 1 capital requirement by 1.5 percent of the risk exposure amount, and the total capital ratio shall exceed the internally assessed own funds requirement by 1.5 percent of the risk exposure amount. By means of a strong capital position and good risk management, SBAB meets the supervisory rules adopted by the EU.

SBAB has entered into an agreement to acquire 71 percent of Booli Technologies AB. The purpose of the acquisition is to strengthen SBAB's position as an institution focused on housing, thereby increasing competitiveness within housing financing. The acquisition will only have a marginal effect on SBAB's capital position.

In this document, the collective risk in the business is divided into:

- Credit risk – the counterparty is unable to fulfil its payment obligations
- Concentration risk – Exposures concentrated to certain counterparties, regions or industries
- Market risk – The risk of loss or reduced future income due to market fluctuations
- Liquidity risk – The risk that the company is unable to meet its payment obligations on the date of maturity without the related cost increasing significantly
- Operational risk – The risk of losses due to inappropriate or unsuccessful processes, human error, faulty systems or external events, including legal risk
- Business risk – The risk of declining earnings due to deteriorating competitive conditions or an incorrect strategy or decision.

[1] Income in relation to loans.

2 THE BOARD'S STATEMENT ON RISK MANAGEMENT AND A BRIEF RISK DECLARATION

The Board of Directors of SBAB Bank AB (publ) supports the risk management described in this document and considers that it meets the requirements that may be posed on it in relation to SBAB's risk profile and adopted short-term and long-term strategic, capital and financial plans. For all risk categories, SBAB's risk profile is in line with or lower than the risk appetite adopted by the Board of Directors.

TABLE 1. **SBAB'S RISK APPETITE AND RISK PROFILE**

	RISK APPETITE		RISK PROFILE		
Risk category	**Classification**	**Level**	**Limit utilisation**	**Risk level**	**Proportion of economic capital**
Credit risk in lending operations	Wanted risk	Medium	Medium	Low	68%
Credit risk in treasury operations	Necessary risk	Low	Low	Low	4%
Market risk	Necessary risk	Low	Medium	Low	19%
Operational risk	Unwanted risk	Low	High	Low	6%
Business risk	Necessary risk	Low	Low	Low	3%
Liquidity risk	Necessary risk	Low	Medium	Low	265 days[1)]

[1)] Survival horizon – For further information, please see Note 2 in SBAB's Annual Report 2015.

SBAB classifies risks as wanted, necessary and unwanted:

- Wanted risks comprise those directly related to the business concept
- Necessary risks are those arising from activities that are regarded as a direct prerequisite for being able to implement the business concept efficiently and competitively, whereby a certain level of risk is accepted to achieve these positive effects for the operations that are directly within the business concept
- Unwanted risks are those that may well be unavoidable in terms of exposure, but which for various reasons are deemed to be damaging enough to warrant their minimisation, although this could entail significant costs.

Credit risk is central to SBAB's business model and it is considered to be the predominant risk in SBAB's operations, which is apparent as it constitutes a major part of the economic capital. Credit risk directly related to SBAB's business operations qualifies as a wanted risk, while credit risk related to liquidity placements or in the form of counterparty risk has been classified as necessary risk that are acceptable, but where the level of risk should be limited.

Market risk and its components are primarily considered a necessary risk for SBAB. Within SBAB, market risk should be kept at a low level and not be a predominant risk.

Operational risk in SBAB is defined as an unwanted risk, which means that both expected and unexpected losses shall be kept at low levels and primarily be covered by the current earnings capacity. SBAB shall strive actively to minimise operational risk, as it is considered as a cost.

SBAB defines business risk as a necessary risk. Changes in the form of new products or new markets may only constitute a small part of SBAB's activities and must be implemented at such a pace that SBAB does not substantially jeopardise its profit level and with great probability avoids pressure on its capital base.

Liquidity risk is defined by SBAB as a necessary risk and shall be maintained at such a level that SBAB can manage a period of acute liquidity crisis without dependency on the capital market. Liquidity risk is not managed by capital provisions but by maintaining a liquidity buffer. The survival horizon measures how many days SBAB can manage without access to capital market funding.

3 CONSOLIDATED SITUATION

The consolidated situation includes SBAB Bank AB (publ) and the Swedish Covered Bond Corporation (SCBC). The Swedish Covered Bond Corporation issues covered bonds in the Swedish and international capital markets.

TABLE 2. **COMPANIES INCLUDED IN THE CONSOLIDATED SITUATION**

Company	Corp. reg. number	Ownership share	Consolidation method used in the accounts	Consolidation method used for capital adequacy
SBAB Bank AB (publ)	556253-7513	Parent Company	–	–
AB Sveriges Säkerställda Obligationer (publ) (Swedish Covered Bond Corporation – SCBC)	556645-9755	100%	Acquisition method	Acquisition method

SBAB's principal activity is to provide mortgage loans for residential properties and tenant-owner rights located in Sweden against collateral in the form of mortgage deeds and units in tenant-owner associations and, to a limited extent, to finance commercial properties and provide unsecured loans. The Parent Company also offers the option of savings accounts.

Information about the Board of Directors, the recruitment policy, the diversity policy and the risk committee is included in the Corporate Governance Report in SBAB's Annual Report. For information about related parties, please refer to Note 39 of SBAB's Annual Report.

The Swedish Covered Bond Corporation (hereinafter referred to as SCBC) does not conduct any proprietary new lending operations. Instead, it acquires loans from the Parent Company on a regular basis or as needed. The purpose of securing credits is for them to be included, in full or in part, in the cover pool that comprises collateral for holders of SCBC's covered bonds, which are issued in Swedish and international capital markets. SCBC's operations are conducted by SBAB employees through an outsourcing agreement.

SBAB's sales activities are conducted in two channels: Retail and Corporate Clients & Tenant-owner Associations. Retail focuses on lending to private individuals and deposits from private individuals and companies. Retail also includes the sales channel Collaboration, which manages partnerships with external actors. Corporate Clients and Tenant-owner Associations is active in the property market through lending to property companies, property funds and tenant-owner associations. SBAB's funding is managed by the Treasury, within the Accounting & Finance department.

SBAB has entered into an agreement to acquire 71 percent of Booli Technologies AB (556733-0567), the Parent Company of the Booli Group. The Booli Group also comprises the subsidiaries HittaMäklare Sverige AB (556698-3895) and Booli Development AB (556764-2367).

FIGURE 1. **SIMPLIFIED BALANCE SHEET FOR SBAB**

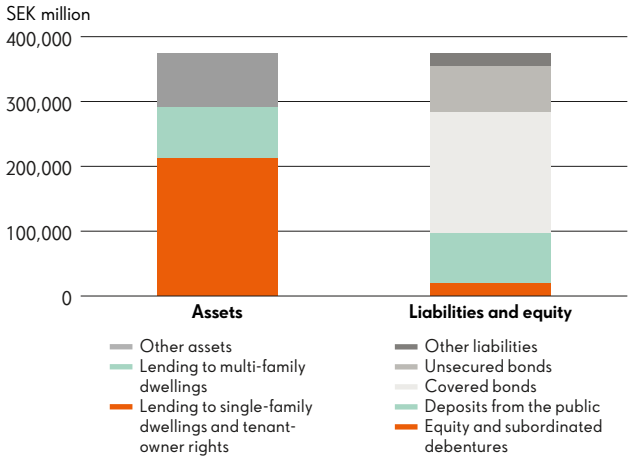
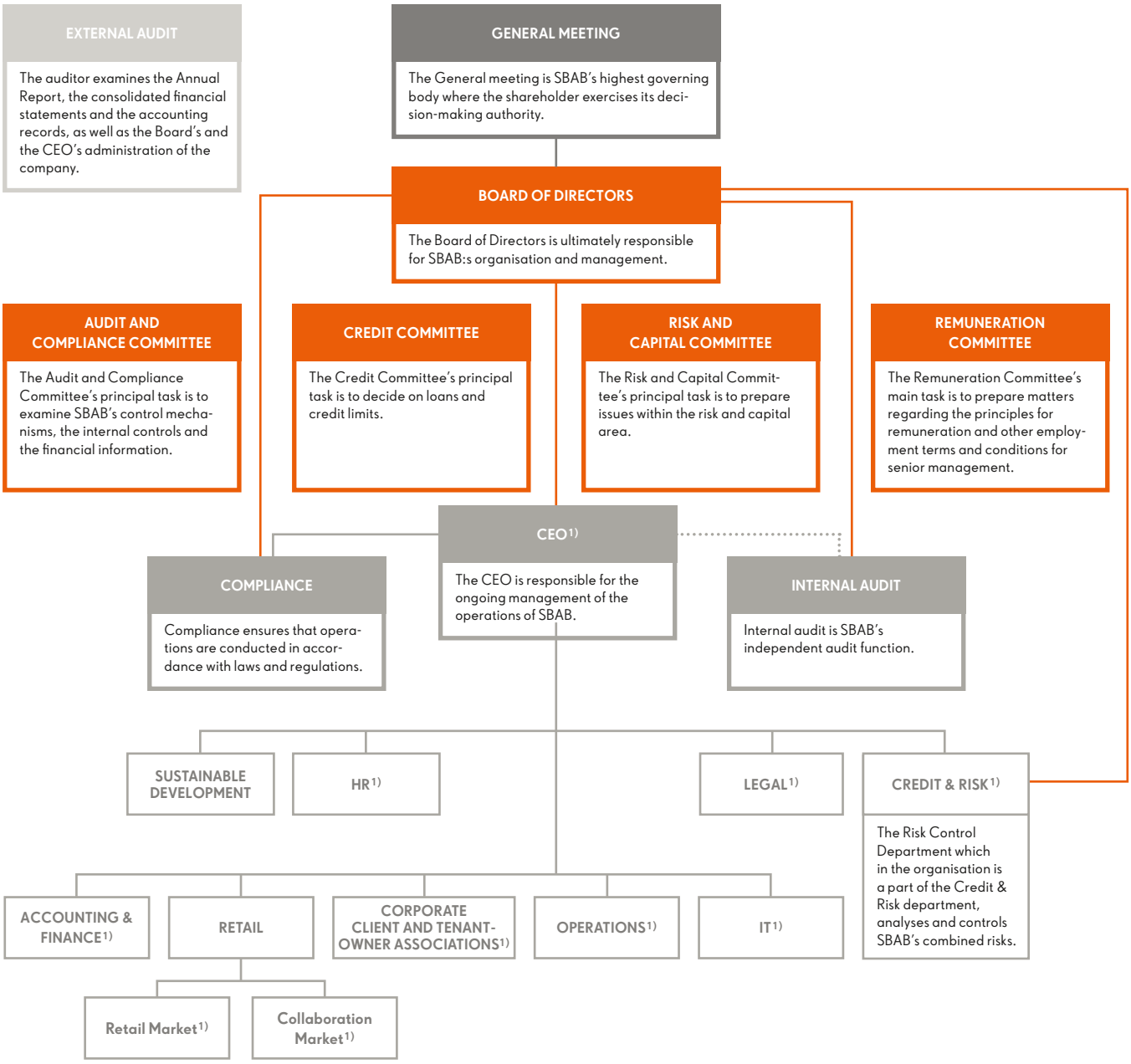


FIGURE 2. **SBAB'S ORGANISATION**

OVERVIEW, 31 DECEMBER 2015



1) Included in corporate management. The head of Retail Market is also the Head of Communication & Business Development.

4 RISK MANAGEMENT AND RISK ORGANISATION

SBAB's risk taking is low and is kept at a level commensurate with financial targets for return, scope of own funds and target rating. The lending operations mainly generate credit risk, while the most significant risks in the funding operations consist of interest rate risk and liquidity risk.

4.1 General rules for risk management

- Risk management within SBAB should consist of effective management and monitoring of all of the risks in the operations
- Risk management must support the operations, maintaining a high level of quality to ensure control of all risks, safeguard SBAB's survival and be in line with SBAB's rating targets. Furthermore, risk management aims to limit volatility in SBAB's financial position
- The ability to assess, manage and price risks while simultaneously maintaining sufficient liquidity to meet unforeseen events is of fundamental significance for long-term profitability and stability. The aim of the strategy adopted for the lending operations, with respect to management and pricing, is to consider the risks that arise in the operations and the capital needed to cover these risks. This entails that an on-going discussion should be maintained regarding the risks generated in the operations and the capital required to counter those risks
- SBAB shall have an organisation that identifies, measures, governs, reports and maintains control of the risks that SBAB is or may become exposed to. There shall be satisfactory internal control and a functioning and effective risk management system
- SBAB shall have knowledge and awareness of any risks to which the bank may be exposed. SBAB shall be able to estimate the size of the risks to which the bank is and may become exposed
- There shall be an independent function for risk control, which has the skills and authority required
- All SBAB employees shall be responsible for managing the company's risks, as part of their regular work. SBAB shall continuously inform and train its employees on the company's risk management framework.

4.2 Risk strategy

SBAB's operations are to be conducted such that risks are suited to SBAB's capacity to bear risk. Risk-bearing capacity primarily refers to the capacity to manage unexpected and expected losses by means of own funds or on-going earnings capacity and, secondly, the capacity to minimise unwanted risks by means of appropriate functions, strategies, processes, procedures, internal rules, limits and controls. Certain risks cannot be quantified and compared with the risk-bearing capacity. In such cases, the cost of mitigating the risk should be weighed up against the desired level of risk and the change in the level of risk achieved through a particular measure.

SBAB should only deliberately expose itself to risks directly attributable or necessary to SBAB's business operations. Such risks primarily encompass credit risk, liquidity risk, market risk, business risk and operational risk.

In addition to limiting the exposure to different types of risk, the risks to SBAB from using different types of financial instruments shall also be limited. In its treasury operations, SBAB shall mainly use derivatives for hedging purposes. Since the risk profile of a derivative transaction may differ from that of the hedged exposure, an analysis must always be performed to ensure that the overall risk is understood. This is especially important in the use of new financial instruments that must be approved in SBAB's process for new financial instruments prior to the transaction.

SBAB shall have a documented process for the approval of new or significantly altered products, services, markets, processes and IT-systems as well as major operational and organisational changes.

SBAB's risk strategy involves managing and evaluating risks that the operations are or may be exposed to, through:

- Clear and documented internal procedures and control system
- An appropriate and lucid organisational structure with clearly defined and documented powers
- Current and documented decision-making procedures that clearly state the reporting structure
- Risk evaluation methods and system support that are adapted to the operations' requirements, complexity and size
- Sufficient resources and skills to achieve the desirable quality in both business and control activities
- Regular incident reporting by the operations according to a documented process
- Documented and communicated contingency and continuity plans
- Clear instructions on internal capital adequacy assessments, credit risk, operational risk, liquidity risk and market risk, which are updated annually and adopted by the CEO or, if required, by the Board of Directors.

All risks that are significant to SBAB shall be limited by the Board of Directors and be commensurate with the pre-determined risk appetite.

4.3 Risk appetite

The level of risk taking within SBAB shall be low. This is achieved by ensuring that total risk level is kept at a level compatible with short- and long-term strategic plans, capital plans and financial plans.

An important part of SBAB's business model entails risks being relatively low and predictable, making it possible to maintain a large volume of business in relation to own funds. This does not mean that each individual credit exposure has low risk, but rather that the total lending portfolio consists largely of low-risk exposures and that their internal risk effect is such that SBAB's total risk is limited. The basis for SBAB's appetite for various types of risk is that each risk should fit within a well-defined area of SBAB's risk-bearing capacity. The total risk exposure may not exceed the total risk-bearing capacity. The scope of the risk that is accepted must be clearly linked to how important the relevant risk is to SBAB's business model and the positive effects expected to be achieved in the form of expected income, cost savings or reduction of other risks.

As a rule, each business decision changes SBAB's exposure to various risk types. Accordingly, SBAB's risk control models should be designed to reflect the risk appetite and such that each business decision is based on a healthy balance between the estimated impact on earnings and changes in risk exposure.

Based on the chosen strategy, on-going earnings and the size of own funds, the Board of Directors of the Parent Company establishes the risk that SBAB is prepared to take and makes decisions regarding risk appetite targets. These targets are based on the three main categories of financial solvency, liquidity risk and compliance. The category, financial solvency, encompasses the risks for which SBAB must retain capital, while liquidity risk encompasses the risks impacting SBAB's prerequisites for successful financing and cash management. Compliance, the third main category, encompasses the regulations and ethical standards with which SBAB must comply to be able to pursue its operations. Each category is broken down into subgroups with established limits for which the outcome is followed up on and reported monthly to the CEO and the Board of Directors.

SBAB's goals for the three risk appetite categories:

- In the first category, solvency, work is conducted to monitor that SBAB maintains sufficient capital to conduct an operation in accordance with the adopted strategy and that credit risk, market risk, operational risk, concentration risk and risk of earnings volatility are kept within the levels approved by the Board of Directors and that minimum levels are maintained with regard to capital ratios
- In the second category, liquidity risk, work is conducted to monitor that liquidity meets approved minimum levels so that SBAB is able to cope with periods of strained liquidity in the market. It also includes ensuring that the SCBC's cover pool has a sufficient level of collateral to maintain a AAA rating in a stressed scenario
- Regulatory compliance is essential in maintaining confidence in SBAB's operations. Even rules that are not legally binding, but that reflect a market practice or ethical guidelines, affect SBAB's approach to employees and customers. The risk appetite measure for the third category, compliance, is not quantifiable in the same way as the other categories – solvency and liquidity – but is summarised in a more preventive qualitative objective.

SBAB shall continuously, and at least annually, reassess the balance between risks and risk-bearing capacity or the costs to minimise risk. The reassessment includes limits and calibration levels and should be performed prior to the commencement of business planning, the internal capital adequacy assessment process (ICAAP) and capital planning. The processes for business planning, ICAAP and capital planning should then include a clear and documented link to risk appetite.

4.4 Limits for capital ratios and targets for return

Each year, the Board of Directors considers capital requirements in relation to the risks to which SBAB is exposed. This occurs through a decision on limits for capital ratios and targets for return.

Based on the chosen business strategy, rating targets and capital planning, in December 2015, the Board of Directors decided to change the internal limit for the Common Equity Tier 1 capital ratio from 22 percent, calculated according to CRR, to be equal to the internally calculated capital requirement. At the same time, new target levels were adopted for the Common Equity Tier 1 capital ratio and the total capital ratio. SBAB targets a Common Equity Tier 1 capital ratio exceeding the internally assessed Common Equity Tier 1 capital requirement by 1.5 percent of the risk exposure amount. The total capital ratio shall exceed the internally assessed own funds requirement by 1.5 percent of the risk exposure amount.

At the same time, the internal limit for capital under the transitional rules from Basel 1 was changed. Previously, the total capital ratio was required to amount to 9.5 percent, calculated according to the transitional regulations for CRR/CRD IV. Own funds are now required to exceed the amount defined by the minimum requirements and a capital planning buffer. The target for own funds is to exceed the minimum requirements and a capital planning buffer plus an additional 10 percent of the minimum requirements.

Internal capital requirements shall be calculated including the risk weight floor applicable at any given time, cover all risks quantified by SBAB within the framework of internal capital assessment and encompass all buffer requirements to which SBAB is subject.

Outcomes are reported to the CEO and Board on a monthly basis. More in-depth reporting of the current capital position in relation to established targets is performed quarterly. The CRO is responsible for this reporting.

TABLE 3. **LIMITS FOR CAPITAL RATIOS AND TARGETS FOR RETURN**

	OBJECTIVES		OUTCOME		DIFFERENCE	
	2015	**2014**	**2015**	**2014**	**2015**	**2014**
Return on equity (owner's return requirement)[1)]	10.0%	10.0%	10.2%	12.1%	0.2%	2.1%
Common Equity Tier 1 capital ratio according to CRR/CRD IV	24.2%	22.0%	28.6%	29.8%	4.4%	7.8%
Total capital ratio	34.4%	–	49.3%	–	14.9%	–
Total capital/total capital ratio according to transitional rules	SEK 15.2 billion	≥9.5%	SEK 18.9 billion	10.8%	SEK 3.7 billion	1.3%

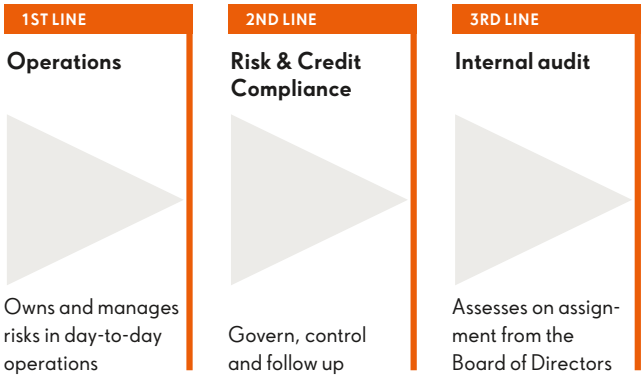
[1)] Net profit/loss for the year divided by average equity.

4.5 The three lines of defence

To define the division of responsibilities between the business operations, Risk Control and Compliance, as well as Internal Audit, SBAB applies the division of roles and responsibilities resulting from the principle of the three lines of defence:

- The first line of defence refers to the day-to-day management of risks performed by the business operations that incur and own the risks
- The second line of defence refers to the risk control and compliance functions. Risk Control is to ensure that risk awareness and acceptance are sufficient to be able to manage risks on a daily basis. Risk Control shall also have a supportive role and work to ensure that the business operations have the procedures, systems and tools required to maintain the daily management of risks, thereby ensuring that the business operations comply with applicable laws and regulations in the sphere of responsibility of risk control. Compliance shall verify that the business operations adhere to laws and regulations and shall support the business operations within its area of responsibility
- The third line of defence refers to the internal audit, which shall review and regularly assess whether the company's organisation, governance processes, IT systems, models and procedures are appropriate and efficient, and whether the company's internal controls are appropriate and efficient. The internal audit shall also review and regularly assess the company's risk management based its adopted risk strategy and risk appetite.

FIGURE 3. **THE THREE LINES OF DEFENCE**



4.6 Risk organisation

The Board of Directors bears the overarching responsibility for the company's total risk exposure and determines the risk policy, capital policy and risk appetite. It is the Board's responsibility to ensure that operations can be conducted with good internal control so that SBAB's ability to meet its obligations is not compromised. When the Board determines the business strategy, it shall take into account the risks that SBAB is and may be exposed to as well as the capital required to cover SBAB's risks.

The Board of Directors or its committees shall approve all significant methods, models and processes used in the risk management. (For more information regarding the Board of Directors' committees, see the Corporate Governance Report in SBAB's Annual Report.) The Board and CEO should have a good overall comprehension of these and a detailed understanding of the content of the risk reports submitted to them. The CRO (Chief Risk Officer) is responsible for the Board and CEO receiving on-going training in risk-related issues and for ensuring that new members are trained within two months of commencing their appointments.

The CEO is responsible for on-going administration in accordance with the strategies, guidelines and governance documents set out by the Board of Directors. The CEO shall ensure that the methods, models and processes forming part of the internal measurement and control of identified risks functions as intended and are approved by the Board of Directors. The CEO also ensures, on an on-going basis, that the reporting to the Board of Directors by each unit, including the Risk Control function, is conducted in accordance with the relevant instructions to the Board.

Risk Control, which is an independent central organisation, is responsible for the identification, quantification, analysis and reporting of all risks. The CRO is responsible for Risk Control. The CRO is directly subordinate to the CEO and reports directly to the CEO and Board of Directors of SBAB.

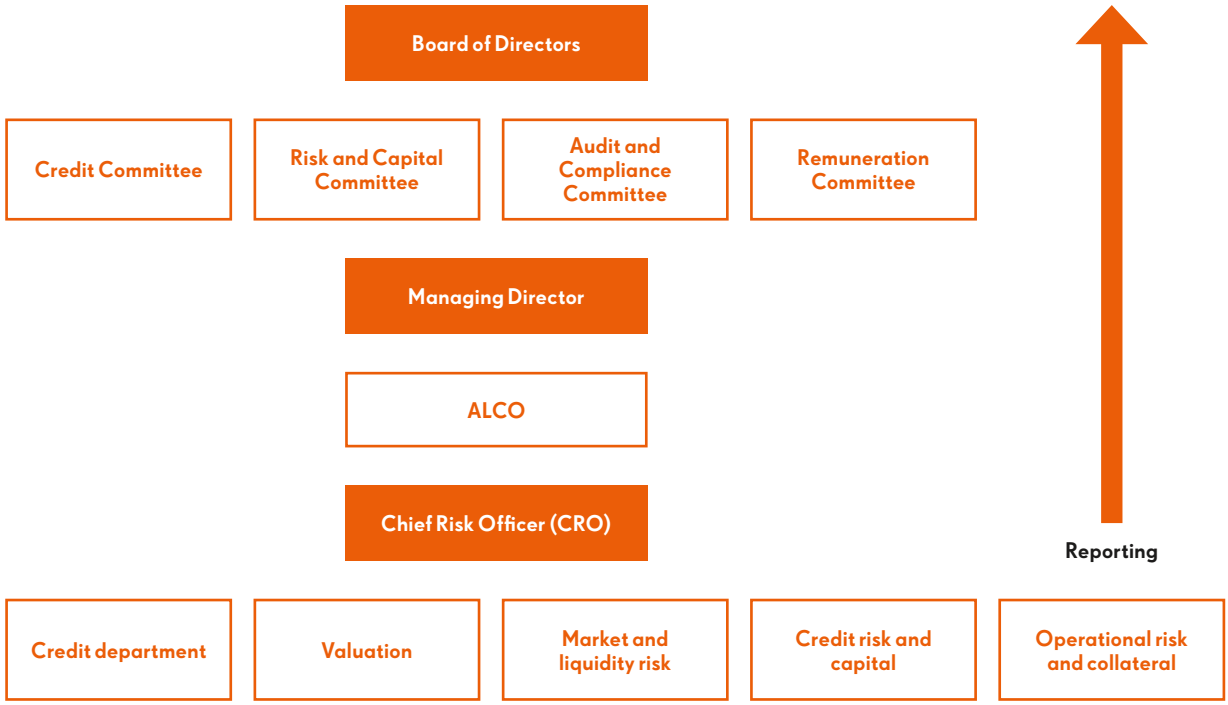
Among other matters, Risk Control is responsible for:

- At an overarching level, developing risk-taking strategies and for ensuring that SBAB's strategies for risk-taking are implemented in accordance with the Board of Directors' intentions, and that policies, instructions and processes facilitate relevant follow-up
- Identifying, measuring, analysing and reporting risk exposure to the Board of Directors and CEO;
- Providing the Board of Directors and the CEO with a tangible and comprehensive overview of all risks in the institution;
- Participating in the production of the institution's risk strategy and in all material risk management decisions;
- Having sufficient authority to influence strategic risk management decisions and being able to contact the Board of Directors directly;
- The design, implementation, reliability and follow-up of SBAB's risk classification system and for the economic capital model.

A monthly report on the overall risk situation and capital adequacy ratio is presented by Risk Control to the Board, the CEO and Executive Management. The Board of Directors and the CEO are also provided with a more in-depth description of risks on a quarterly basis. In addition, a daily report on current risk levels in relation to granted limits is presented to the CEO, CFO and CRO. SBAB's Board and Executive Management are thereby provided with a relevant overview of the Group's risk exposure on a continuous basis.

Those who own the risks, i.e. the business operations, shall, without delay, inform Risk Control of occurrences of material events that could entail a heightened risk.

FIGURE 4. **REPORTING OF RISK**



5 CAPITAL ADEQUACY

The rules for capital adequacy are stated in CRR and CRD IV. In part, the rules serve to make institutions more resilient to new crises, in part to raise confidence in the institutions' ability to manage new crises. The institutions shall prove to rating agencies and the investors who purchase securities from banks, as well as new and existing customers, that they have an adequate capital situation.

5.1 Capital requirements

The size of SBAB's capital requirement depends on laws and regulations, the company's internal assessment based on approved strategies, the assessments of investors and rating agencies and the evaluations made by the owner, the Board of Directors and Executive Management.

Capital in accordance with Pillar 1 refers to the minimum amount of capital that the company is to have in accordance with CRR and CRD IV, the EU's technical standards and delegated acts, the Special Supervision of Credit Institutions and Investment Firms Act (2014:968), the Capital Buffers Act (2014:966) and the Swedish Financial Supervisory Authority's regulations (FFFS 2014:12). CCR also includes transitional regulations entailing that the capital requirement be at least 80 percent of the capital requirements under Basel I. At 31 December 2015, the total capital ratio was 49.3 percent and the Common Equity Tier 1 capital ratio was 28.6 percent.

5.2 Capital requirements and buffers

The rules in CRR and CRD IV entail, among other things, requirements for a minimum level of own funds and controls on capital requirements. According to the requirements, the bank must have a Common Equity Tier I capital ratio of at least 4.5 percent, a Tier 1 capital ratio of at least 6 percent and a total capital ratio at least equal to 8 percent of the total risk-weighted exposure amount for credit risk, market risk and operational risk. In addition, the bank must maintain Common Equity Tier I capital to meet the combined buffer requirement, which in Sweden is the sum of a capital conservation buffer of 2.5 percent of risk exposure amount, a countercyclical buffer of up to 2.5 percent and buffers for systemic risk of up to 5 percent.

The Swedish Financial Supervisory Authority has decided that, in addition to the capital conservation buffer of 2.5 percent, a countercyclical buffer of 1 percent shall be applied for Swedish exposures effective from 13 September 2015 and of 1.5 percent from 27 June 2016. The Swedish Financial Supervisory Authority has also decided to recognise countercyclical buffer values of up to 2.5 percent set by the proper authority in another EEA country, which means that Norwegian exposures are subject to a countercyclical buffer of 1 percent. Furthermore, banks considered systemically important are subject to an additional capital requirement of 5 percent to be covered by Common Equity Tier 1 capital. The four largest banks in Sweden are currently considered systemically important: Handelsbanken, Nordea, SEB and Swedbank. In addition, Sweden has introduced a risk weight floor that has been raised from 15 percent to 25 percent for residential mortgages to Swedish households.

SBAB has taken these regulations into account in its capital planning and meets the requirements with a margin. Buffer values are presented in Table 9, Capital requirements and risk exposure amounts.

In November 2014, the Swedish Financial Supervisory Authority announced that an amortisation requirement would be introduced for new residential mortgages. According to this requirement, new residential mortgages were to be amortised by 2 percent of the initial loan until a loan to value ratio of 70 percent was reached, and thereafter by 1 percent down to a loan-to-value ratio of 50 percent. The requirement was not introduced in 2015, but a new proposal with a similar content was presented on 18 December 2015. For the Swedish Financial Supervisory Authority's proposal to enter into force, it is required that the legislative change and authorisation proposed by the Swedish Government is adopted by the Swedish Riksdag (parliament). The Swedish Government must further authorise the Swedish Financial Supervisory Authority to determine the details of the regulation. As an amortisation requirement may have far-reaching impact on individual households, the regulations must also be approved by the Swedish Government before entering into force.

Future rules in IFRS 9 will regulate a new method used for credit risk provisions. SBAB is working on devising a model for this. It is still to early to express a view on the impact this will have on the size of the provision, and therefore also on own funds.

TABLE 4. **GEOGRAPHIC DISTRIBUTION OF CREDIT RISK EXPOSURES FOR THE CALCULATION OF THE COUNTERCYCLICAL BUFFER**

	CREDIT EXPOSURES		EXPOSURES IN THE TRADING BOOK		SECURITISED EXPOSURES		CAPITAL REQUIREMENTS					
Countercyclical buffer by country, SEK million	**Exposure amount of credit risk exposures reported using the standard method**	**Exposure amount of credit risk exposures reported applying IRB**	**Long and short positions in the trading book reported using the standardised method**	**Exposures in the trading book reported applying IRB**	**Exposure amounts for exposures reported using the standardised method**	**Exposure amounts for exposures reported applying IRB**	**of which credit exposures**	**of which, exposures in the trading book**	**of which, securitised exposures**	**Total**	**Weights capital requirements**	**Level capital conservation buffer**
Sweden	31,924	306,049	12,747	–	–	–	2,447	20	–	2,467	98.09%	1.00%
Norway	464	–	3,302	–	–	–	4	22	–	26	1.04%	1.00%
Other	852	–	11,173	–	–	–	7	15	–	22	0.87%	–
Total	32,240	306,049	27,222	–	–	–	2,458	57	–	2,515	100.00%	

TABLE 5. **INSTITUTION-SPECIFIC COUNTERCYCLICAL BUFFER**

SEK million	
Total risk exposure amount	38,244
Institution-specific countercyclical buffer	0.99%
Institution-specific countercyclical buffer requirements	379

5.3 Own funds

SBAB's own funds comprise equity as well as additional Tier 1 instruments and Tier 2 capital consisting of subordinated debentures. SBAB's own funds amounted to SEK 18,867 million as per 31 December 2015. Over the year, the Common Equity Tier 1 capital was affected by the fact that net profit/loss for the period was added and the estimated dividend in accordance with SBAB's dividend policy was deducted. However, with respect to future capital requirements and the uncertainty regarding these, the Board of Directors proposes that no dividend be paid. The surplus has been verified by the Company's auditors, in accordance with Article 26, item 2, of the CRR.

According to Article 35 of the CRR, the institution shall, except in the case of the items referred to in Article 33, not make adjustments to remove from own funds unrealised gains or losses on assets or liabilities measured at fair value. According to this Article, SEK 264 million have been added to Common Equity Tier 1 capital.

According to Article 33, item 1, of the CRR, the part of the fair value reserves related to gains or losses on cash flow hedges of financial instruments that are not valued at fair value, including projected cash flows, shall not be included in own funds. The Common Equity Tier 1 capital has been adjusted down for SEK 236 million in cash flow hedges.

Changes in fair value that depend on the institution's own credit standing and that are related to derivative instruments have affected the Common Equity Tier 1 capital negatively by SEK 25 million, in accordance with Article 33, item b.

With reference to Articles 34 and 105 of the CRR, SEK 67 million has been deducted due to the requirements for prudent valuation.

A deduction of SEK 46 million for intangible assets and a deduction of SEK 83 million for net provisions were made, in accordance with Article 36.

No risk exposures have been deducted from own funds.

Older subordinated debt that does not meet the requirements of CRR may be included in the calculation of Tier 1 capital if certain conditions are present according to the transitional regulations of the CRR and the Swedish Financial Supervisory Authority has given its consent. SBAB has secured such permission for two debenture loans for a total nominal value of SEK 1,000 million recognised as core capital of SEK 994 million. Both loans have incentives to redeem (step-up). In addition, SBAB reports two debenture loans with a nominal value SEK 1,500 million (see Table 7) as Tier 1 capital.

TABLE 6. **CAPITAL ADEQUACY**

	CONSOLIDATED SITUATION		PARENT COMPANY		SCBC	
SEK million	**2015**	**2014**	**2015**	**2014**	**2015**	**2014**
Common Equity Tier 1 capital	10,926	10,199	7,459	8,066	13,906	12,700
Tier 1 capital	13,420	12,594	9,953	10,461	13,906	12,700
Total capital	18,867	15,307	15,400	13,174	13,906	12,700
Without transitional regulations						
Risk exposure amount	38,244	34,247	33,295	20,363	16,151	17,565
Common Equity Tier 1 capital ratio	28.6%	29.8%	22.4%	28.4%	86.1%	72.3%
Excess[1)] Common Equity Tier 1 capital	9,205	8,658	5,961	6,790	13,179	11,909
Tier 1 capital ratio	35.1%	36.8%	29.9%	36.9%	86.1%	72.3%
Excess[1)] Tier 1 capital	11,125	10,539	7,955	8,760	12,937	11,646
Total capital ratio	49.3%	44.7%	46.3%	46.4%	86.1%	72.3%
Excess[1)] total capital	15,807	12,567	12,737	10,905	12,614	11,295
With transitional regulations						
Own funds	18,950	15,392	15,449	13,223	13,940	12,736
Risk exposure amount	165,830	142,975	50,414	29,938	115,555	113,258
Total capital ratio	11.4%	10.8%	30.6%	44.2%	12.1%	11.2%

[1)] Surplus of capital has been calculated based on the minimum capital requirements (without buffer requirements).

5.3.1 Subordinated debentures

The subordinated debentures are subordinate to the Parent Company's other liabilities, and the subordinated debentures included in Tier 1 capital are subordinate to other subordinated debentures. For a specification of the own funds and the terms and conditions for debenture loans in accordance with Commission Implementing Regulation (EU) No 1423/2013, please refer to information under "Risk management" at sbab.se. The complete terms and conditions of the debenture loans are also specified at sbab.se.

TABLE 7. **DEBENTURE LOANS, SEK million**

ISIN	**Currency**	**Nominal amount**	**Outstanding nominal amount**	**First possible date for redemption**	**Interest rate,**	**Interest rate after first possible date for redemption**	**Maturity date**	**Taken up in the capital base as additional Tier 1 instruments**	**Taken up in the capital base as Tier 2 instruments**
XS0259220266	SEK	700	700	30 June 2016	5.22%	3m stibor+1.93%	Perpetual	694	–
XS0259219920	SEK	300	300	30 June 2016	3m stibor+0.93%	3m stibor+1.93%	Perpetual	300	–
XS0619201378	SEK	1,000	1,000	20 April 2016	6.123%	3m stibor+2.4%	20 April 2021	–	1,000
XS0854751186	SEK	800	800	16 November 2017	3m stibor+2.65%	3m stibor+2.65%	16 November 2022	–	800
XS0854751004	SEK	200	200	16 November 2017	4.18%	3m stibor+2.65%	16 November 2022	–	200
XS1202975386	SEK	400	400	16 March 2020	3.82%	3m stibor+3.25%	Perpetual	400	–
XS1202987985	SEK	1,100	1,100	16 March 2020	3m stibor+3.25%	3m stibor+3.25%	Perpetual	1,100	–
XS1245415812	SEK	1,000	1,000	11 June 2020	3m stibor+1.30%	3m stibor+1.30%	11 June 2025	–	1,000
XS1317715842	SEK	600	600	10 November 2020	2.25%	3m stibor+1.90%	10 November 2025	–	597
XS1317716147	SEK	1,850	1,850	10 November 2020	3m stibor+1.90%	3m stibor+1.90%	10 November 2025	–	1,850
Total		**7,950**	**7,950**					**2,494**	**5,447**

There are no on-going or foreseen material obstacles or legal barriers to a rapid transfer of funds from own funds other than what is stipulated in the terms and conditions governing subordinated debentures (see Note 32 in SBAB's Annual Report for 2015) or what generally applies under the Companies Act (2005:551).

The starting capital required for the Parent Company in accordance with the Act on Banking and Financing Activities (2004:297) totalled SEK 45.9 million. The corresponding capital requirement for SCBC amounted to SEK 47.0 million.

Disclosure of own funds during a transitional period

Disclosures in accordance with Article 5 of Commission Implementing Regulation (EU) No 1423/2013. No amounts are subject to the provisions preceding Regulation (EU) No 575/2013 ("CRR") or the prescribed residual amount according to Regulation (EU) No 575/2013.

TABLE 8. **OWN FUNDS, CONSOLIDATED SITUATION**

GROUP, SEK million	**Amount as per 31 December 2015**	**Amount as per 31 December 2014**
Common Equity Tier 1 instruments: Instruments and reserves		
Capital instruments and the related share premium reserves	1,958	1,958
Retained earnings	8,464	7,710
Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses under the applicable accounting standards)	264	76
Independently reviewed interim profits net of any foreseeable charge or dividend	697	754
Common Equity Tier 1 capital before regulatory adjustments	**11,383**	**10,498**
Common Equity Tier 1 capital: Regulatory adjustments		
Additional value adjustments (negative amount)	–67	–70
Intangible assets (net after deduction for associated tax liability) (negative amount)	–46	–43
Fair value reserves to gain or losses on cash flow hedges	–236	–100
Negative amounts resulting from the calculation of expected loss amounts	–83	–84
Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	–25	–2
Total regulatory adjustments to the Common Equity Tier 1 capital	**–457**	**–299**
Common Equity Tier 1 capital	**10,926**	**10,199**
Additional Tier 1 capital: Instruments		
Capital instruments and the related share premium accounts	1,500	–
of which classified as liabilities under applicable accounting standards	*1,500*	–
Amount of qualifying items referred to in Article 484(4) and the related share premium accounts subject to phase out from AT1 capital	994	2,395
Additional Tier 1 capital before regulatory adjustments	**2,494**	**2,395**
Additional Tier 1 instruments: Regulatory adjustments		
Total regulatory adjustments to Additional Tier 1 capital	–	**–**
Additional Tier 1 capital	**2,494**	**2,395**
Tier 1 capital (Tier 1 capital = Common Equity Tier 1 capital + additional Tier 1 capital)	**13,420**	**12,594**
Tier 2 capital: Instruments and provisions		
Capital instruments and the related share premium reserves	5,447	2,599
Amount for qualifying items referred to in Article 484(5) and the related share premium accounts subject to phase out from Tier 2 capital	–	114
Tier 2 capital before regulatory adjustments	**5,447**	**2,713**
Tier 2 capital: Regulatory adjustments		
Total regulatory adjustments to Tier 2 capital	–	**–**
Tier 2 capital	**5,447**	**2,713**
Total capital (total capital = Tier 1 capital + Tier 2 capital)	**18,867**	**15,307**
Total risk-weighted assets	**38,244**	**34,247**
Capital ratios and buffers		
Common Equity Tier 1 capital (as a percentage of risk exposure amount), %	28.6	29.8
Tier 1 capital (as a percentage of the risk exposure amount), %	35.1	36.8
Total capital (as a percentage of risk exposure amount), %	49.3	44.7
Institution specific buffer requirement (common equity Tier 1 capital requirement in accordance with Article 92(1)(a) plus capital conservation buffer and countercyclical capital buffer requirements, plus systemic risk buffer, plus the systemically important institution buffer (G-SII buffer and O-SII buffer) expressed as a percentage of risk exposure amount, %	8.0	7.0
of which, capital conservation buffer requirement, %	*2.5*	*2.5*
of which, countercyclical buffer requirement, %	*1.0*	–
of which, systemic risk buffer requirement, %	–	–
of which, G-SII buffer and O-SII buffer, %	–	–
Common Equity Tier 1 capital, available to meet buffers (as a percentage of risk exposure amount), %	24.1	25.3
Capital instruments subject to phase-out arrangements (only applicable between 1 January 2013 and 1 January 2022)		
Current cap on additional Tier 1 instruments subject to phase-out arrangements	2,096	2,395
Amount excluded from additional Tier 1 instruments due to cap (excess over cap after after redemptions and maturities)	–	599
Current ceiling for Tier 2 instruments subject to phase-out arrangements	910	1,040

5.4 Capital requirements

When calculating capital requirements, each exposure is allocated to an exposure class, either using the standardised approach or the IRB approach. Table 9 shows the individual risk exposure amounts distributed by exposure class. A significant difference in the calculation of capital requirements with and without transitional regulations involves the treatment of tenant-owner rights. In accordance with Basel III, tenant-owner rights are equated with residential properties and risk-weighted according to the standard method at 35 percent if the loan-to-value ratio limit has been met. According to the transitional regulations, however, lending against collateral in tenant-owner rights is equated with unsecured lending and risk-weighted at 100 percent, as opposed to loans secured by mortgage deeds on residential property that are risk-weighted at 50. This means that, according to the transitional regulations, lending against collateral in tenant-owner rights is equated with unsecured lending, which is questionable even during a transitional period, given the considerable difference in risk weights and capital requirements between the regulations. If the actual risk is calculated according to IRB models, lending for tenant-owner rights has a low risk. SBAB's lending portfolio consists 33 percent of lending for tenant-owner rights.

Over the year, the capital requirement for credit risk increased due to the larger lending portfolio, while the capital requirement for market risk declined due to the liquidity portfolio largely being transferred from the trading book to the banking book.

No credit risk reducing measures have been applied for credit exposures where the standardised approach has been used.

TABLE 9. **CAPITAL REQUIREMENTS AND RISK EXPOSURE AMOUNTS, CONSOLIDATED SITUATION**

GROUP, SEK million	Capital requirements 31 December 2015	Risk exposure amount 31 December 2015	Capital requirements 31 December 2014	Risk exposure amount 31 December 2014
Credit risk recognised in accordance with IRB approach				
Exposure to corporates	864	10,795	558	6,975
Retail exposures	1,128	14,103	1,028	12,851
of which, exposures to small and medium-sized companies	*130*	*1,628*	*139*	*1,737*
of which, exposures to tenant-owner rights, single-family dwellings and holiday homes	*998*	*12,475*	*889*	*11,114*
Total exposure recognised in accordance with IRB approach	**1,992**	**24,898**	**1,586**	**19,826**
Credit risk recognised in accordance with standardised approach				
Exposures to central governments and central banks	0	0	0	0
Exposures to regional governments or local authorities	0	0	0	0
Exposures to institutions [1)]	122	1,526	111	1,388
of which, derivatives listed in CRR, Annex II	*120*	*1,505*	*103*	*1,291*
of which, repos	*1*	*14*	*7*	*85*
Exposure to corporates	1	15	146	1,829
Retail exposures	168	2,106	143	1,783
Exposures in default	1	7	1	10
Exposures in the form of covered bonds	237	2,957	59	744
Exposures to institutions and corporates with a short-term credit assessment	1	15	7	86
Exposures in the form of shares or units in collective investment undertakings (CIUs)	–	–	20	253
Other items	58	730	86	1,070
Total exposures recognised in accordance with standardised approach	**588**	**7,356**	**573**	**7,163**
Market risk	**149**	**1,856**	**337**	**4,210**
of which, position risk	*105*	*1,314*	*279*	*3,491*
of which, currency risk	*44*	*542*	*58*	*719*
Operational risk	**239**	**2,989**	**164**	**2,047**
Credit Value Adjustment risk	**92**	**1,145**	**80**	**1,001**
Total minimum capital requirement and risk exposure amount	**3,060**	**38,244**	**2,740**	**34,247**
Capital requirements for capital conservation buffer	**956**		**856**	
Capital requirements for countercyclical buffer	**379**		**–**	
Total capital requirements	**4,395**		**3,596**	

[1)] The risk weighted exposure amount for counterparty risk according to Article 92, item 3f, of CRR amounts to SEK 1,519 million (1,376).

TABLE 10. **EXPOSURE AND CAPITAL REQUIREMENTS IN OTHER OPERATIONS BASED ON THE BALANCE SHEET**

Balance sheet, SEK million	Assets according to the balance sheet	Exposure before CCF	Exposure after CCF	of which, counterparty exposures	REA before SME	REA after SME	Capital requirements
Cash and balances at central banks	0	0	0	–	0	0	0
Chargeable treasury bills and other eligible bills	14,312	4,127	4,127	4,127	0	0	0
Lending to credit institutions	3,456	128	128	69	29	29	2
Lending to the public	296,981	297,411	297,395	–	27,184	24,963	1,997
Change in value of interest-rate-hedged items in portfolio hedges	549	549	549	–	550	549	44
Bonds and other interest-bearing securities	49,714	33,439	33,439	33,439	2,903	2,903	232
Derivative instruments	7,192	3,394	3,394	3,394	1,505	1,505	120
Intangible fixed assets	56	56	56	–	–	–	–
Property, plant and equipment	20	20	20	–	20	20	2
Other assets	1,246	847	847	–	50	50	4
Prepaid expenses and accrued income	1,026	589	589	–	68	68	5
Total	**374,552**	**340,560**	**340,544**	**41,029**	**32,309**	**30,087**	**2,407**
Memorandum items	47,949	47,949	13,242	–	2,171	2,167	173
Total	**422,501**	**388,509**	**353,786**	**41,029**	**34,480**	**32,254**	**2,580**

TABLE 11. **EXPOSURE AMOUNTS BEFORE AND AFTER CREDIT RISK MITIGATION, PER CREDIT QUALITY STEP**

Credit quality step	Exposure amount before credit risk mitigation	Exposure amount after credit risk mitigation
1	40,275	40,275
2	2,263	2,263
3	13	13
4	–	–
5	–	–
6	–	–
Total	**42,551**	**42,551**

5.5 Securitised assets

SBAB has no loans that are securitised and neither has it participated in the securitisation of any other institution. SBAB has no due exposures in respect of securitisation, re-securitisation and no securitised rolling exposures.

5.6 Rating

For cases in which external ratings are used, the lowest rating from Moody's or Standard & Poor's is selected. External rating is used for the exposure classes exposures to central governments or central banks, regional governments or local authorities, institutions, institutions and corporates with a short-term credit assessment, and exposures in the form of covered bonds. The association of the external rating provided by credit rating agencies with the credit quality steps prescribed in the CRR complies with the standard association published by EBA.

6 INTERNAL MODEL FOR CALCULATING CAPITAL REQUIREMENTS

The internal capital adequacy assessment is to ensure that SBAB has sufficient capital to deal with any financial problems that arise. The Board of Directors and executive management are responsible for the internal capital evaluation. In relation to strategic decisions, business planning and changes in the operating environment, SBAB conducts an assessment of how the capital requirement has changed based on risk. SBAB uses an economic capital model as the basis for its assessment of the company's capital requirement within the framework of the internal capital evaluation process (ICAAP).

6.1 Internal capital assessment, Pillar 2 of the Basel regulations

The business conducted by SBAB affects the size of the risk taken by the company, which in turn impacts the size of the capital required. The size of the capital in turn affects the price of individual transactions for customers. The better the risk can be assessed by SBAB, the better the assessment of the size of the capital requirement that is utilised in the individual transaction. The risk-adjusted return can also be assessed for the company when the capital requirement for the individual transaction can be calculated.

Pillar 2 of the Basel III regulations imposes the requirement that the banks' management and assessment of risks must be satisfactory to ensure that the banks can fulfil their obligations. In order to fulfil this requirement, the banks must have methods that enable them to continuously evaluate and uphold capital in an amount, type and distribution sufficient to cover the risks to which they are or will become exposed. This is called the internal capital adequacy assessment process (ICAAP).

SBAB's assessment of the capital requirement in accordance with Pillar 2 is based on economic capital. In combination with capital requirements based on stress tests and capital for further risk, this comprises SBAB's assessment of the appropriate size of risk capital. The capital requirement for any type of risk may not be less than the capital ratio stipulated in Pillar 1. In such a case, the capital requirement in Pillar 2 is adjusted.

Economic capital is based on SBAB's own relatively advanced models in which quantifiable risks are summarised as a single entity. Economic capital is also an important component in pricing and financial control.

When determining the size of the capital requirement, assessments of investors and rating agencies regarding the company's capital requirements compared with the capital held by the company are also taken into account. The views of rating agencies are reflected in SBAB's rating, which directly impacts the company's funding cost.

The quality and utilisation of risk information are essential to SBAB's long-term competitiveness in the market. The purpose of the internal capital adequacy assessment process is to ensure that the company identifies, measures, secures and manages the risks to which SBAB is exposed and that SBAB has own funds that are compatible with the selected risk tolerance. The process is revised annually to capture changes in the operating environment that continuously affect the company's performance.

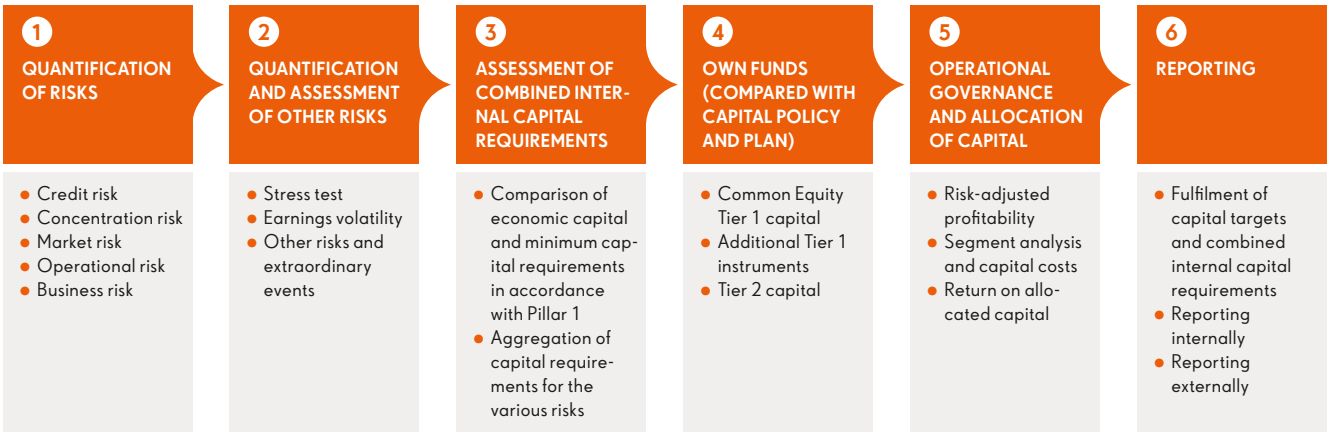
6.2 Process for internal calculation of capital requirements

As part of SBAB's process for establishing internally calculated capital requirements, the risks generated in the operations are identified initially. Risk Control is responsible for the quantification of all risks. Various models are used depending on the risk to be measured. The model for economic capital is used to calculate capital requirements for the quantifiable risks.

The results are reviewed and analysed. SBAB uses stress tests to assess the possible impact of the recession on the capital requirement.

In addition to economic capital, capital buffers are reserved for capital requirements caused by profit volatility and stress tests, which are all included in the internal capital requirement. The results are reviewed and analysed, in the short and long term, in relation to capital planning and forecasts. The combined results of the internal capital assessment are reported to the Board of Directors and the CEO. Finally, the Board of Directors adopts the process and results of the company's internal capital assessment.

FIGURE 5. **PROCESS FOR INTERNAL CAPITAL EVALUATION**



6.3 Economic capital

The capital requirements for credit risk, market risk and operational risk are quantified in SBAB's model for economic capital. The calculation of capital requirements for credit risk is largely based on the results of the Group's IRB models. Economic capital is defined as the amount of capital needed to ensure solvency over a one-year period, given a predetermined confidence interval. The confidence interval is chosen to reflect the company's target rating. In SBAB's case, the level of confidence is 99.97 percent, which corresponds to the long-term AA- target rating (according to Standard & Poor's ratings scale).

Capital requirements for operational risk are calculated using standards based on operating income while market risk is calculated using Value at Risk (VaR) models. In addition to comprising an assessment of the combined capital requirement to counter the risks in the company's operations, the economic capital is used to monitor profitability in the company's operations, for economic control and for strategic considerations.

Economic capital comprises most of the capital that, according to SBAB's assessment, is required to cover unexpected losses during the coming year. Expected losses must be covered by earnings from operating activities. As shown in Table 13, credit risk is the dominant risk in SBAB's operations.

6.3.1 Concentration risk

Concentration risk arises when exposures are concentrated to certain types of borrowers, regions or industries. SBAB Bank is considered to be exposed to credit-risk related concentration risk in its lending and finance operations. The full capital requirement for concentration risk is included in the economic capital for credit risk.

SBAB calculates the concentration risk divided into single-name concentration, industry concentration and geographic concentration. SBAB:s method for single-name concentration is based on a method developed by Gordy & Lutkebohmert (2007) while industry and sector concentration are based on a method based on the Herfindahl index.

Upon calculation at 31 December 2015, the internally calculated capital requirement for concentration risk amounted to SEK 562 million, of which SEK 521 million pertained to credit risk in the lending operations and SEK 41 million to credit risk in the funding operations. Concentration risk related to finance operations increased SEK 16 million while concentration risk related to lending operations increased by SEK 200 million compared with the preceding year-end.

6.4 Stress tests

Capital planning is founded on a basic scenario that reflects the most probable operational development in accordance with internal forecasts. Complementing this, stress tests and scenario analyses are performed, whereby the development of the loan portfolio and capital requirements during a serious but not implausible uneconomic downturn is evaluated. When performing the tests, events and economic conditions that could give rise to an unfavourable impact on the institution's loan-portfolio exposures and that are not reflected in the anticipated scenario are also taken into account.

FIGURE 6. **SCHEMATIC PROCESS FOR CALCULATING ECONOMIC CAPITAL**

6.4.1 Stress test methods

SBAB uses a number of statistical models to forecast credit risk. The common factor for the models is that they are built around one or more explanatory variables that are specifically adapted to the kind of exposure and risk dimension (PD or LGD) for which the model is intended to be used. A change in one or more of these explanatory variables results in a change in the forecast credit risk. This in turn affects the risk class to which an exposure is allocated. In the stress tests, this relationship is utilised by simulating changes in the underlying model variables. The starting point for this simulation is a macroeconomic scenario. The starting point for this simulation is an assumed macroeconomic scenario In the stress test, a scenario that expresses an unfavourable economic trend will result in a migration towards worse risk classes, which in turn entails higher economic capital, higher risk exposure amounts and larger anticipated losses (PD*LGD*EAD). A scenario that reflects an economic recovery will consequently result in the opposite effect. A simplified illustration of the process is provided in Figure 6 on page 18.

The stress test is conducted for the portfolio at that specific time. Then, this portfolio is subjected to stress over a three-year time horizon, taking the planned volume development within different portfolio segments into account. The macroeconomic scenario that forms the basis of the stress test is also assumed to have a direct effect in SBAB's risk models. This means that the model variables are expected to change without any time shift.

The components included in SBAB's model for stress tests comprise:

- Determination of a macroeconomic scenario for the stress test
- Translation of the macroeconomic scenario to model variables
- Assumptions regarding new sales and loan redemption
- Calculation of expected losses and capital requirements
- Calculation of profit and own funds.

In addition to loan losses and capital requirements related to credit risk, the stress tests also simulate the effect of a deterioration in SBAB's credit ratings and the effect of a decline in property prices on SBAB's scope for funding by means of covered bonds. These are expected to lead to increased funding costs, resulting in weaker net interest income, lower earnings and consequently also reduced own funds. Finally, realised losses related to operational risks are also brought out by applying a fraud scenario independent from the macro scenarios, thus leading to further deterioration in earnings and deceased own funds.

TABLE 12. **THE FOLLOWING PARAMETERS ARE SUBJECTED TO STRESS IN THE CURRENT AND NEXT THREE YEARS**

Demand	Prices	Interest rates
GDP growth (real)	Consumer prices	Residential mortgages, 3 month
Disposable household income (nominal)	Single-family home prices	STIBOR, 3 month
Employment	Prices of tenant owners' rights	Government bond rate, 10 year
Unemployment	Residential property prices	STIBOR-Treasury discount not
		Housing bonds-Government bonds, 5 year
		Government bonds Sweden–Germany, 10 year

6.4.2 Macroeconomic scenario

The stress tests can be used in a number of conceivable approaches and methods. In general, these involve an assumption regarding a future scenario, either hypothetical or based on historical outcome. The stress tests presented in the current ICAAP are based on a hypothetical scenario whereby the development of the parameters is based on a subjective interpretation of economic theory and empirical analysis. The scenario describes a sharp economic decline.

For a number of variables in the models, there is a natural connection between the value the variable is expected to take on and the development of one or more of the macroeconomic parameters. In these cases, the variable value could consequently be recalculated directly based on the change in the underlying macro-parameters.

In general, all model variables are expected to be affected to some extent, except the variables that are not deemed to be correlated to economic conditions.

Since a macroeconomic scenario cannot be directly translated to the effect that it has on certain PD variables, historical correlations are used instead. Examples of such model variables are the number of reminders and claims. For these variables, the effect has instead been estimated based on the historical correlation in relation to the residential mortgage interest rate.

LGD is subjected to stress according to the same methodology as PD. Since SBAB's LGD models are built around the loan-to-value ratio, changes in the market value of property have a direct impact on LGD.

Finally, the macro scenario is combined with a simulated deterioration in SBAB's credit rating by two rating levels.

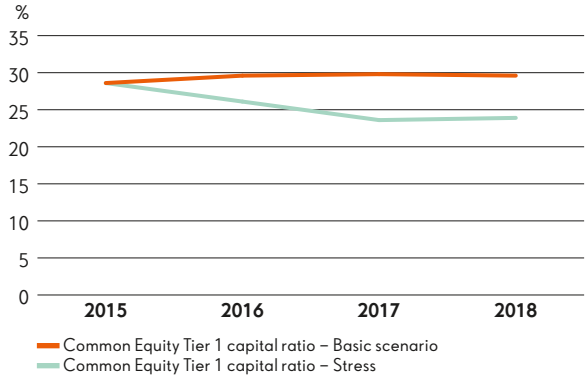
Scenario

- External shocks have a heavy impact on the Swedish economy hard, internal imbalances and problems reinforce these effects, resulting in recession and problems in the banking system. Typically, this kind of scenario occurs approximately every 25th year.
- Declining growth and financial unease in China and other growth countries, combined with unease surrounding escalated conflicts in the Middle East, major refugee migrations and renewed uncertainty surrounding cooperation on the euro are leading to the prices of oil and other commodities falling sharply and the international financial markets being impacted by a "flight to quality". International demand is declining rapidly and Swedish households are rapidly tightening their belts while international confidence in the central government's financing and the banks' financial strength is being eroded due to an uncertain parliamentary position and imbalances in the housing and mortgage markets. The Swedish krona as weakening, helping maintain inflation at around 0 percent.
- The GDP decline will be about the same as during the recent financial crisis in 2008/09, although the process is more protracted. Employment and income levels are falling. The economy will not stabilise until during 2018.
- The central government's finances are deteriorating rapidly and the parliamentary situation is helping erode the credibility of economic policy, causing a sharp rise in risk premiums. The banking system is under pressure. Although the Riksbank is attempting to stimulate the economy, it is not succeeding, since risk premiums are rising sharply. On the whole, housing prices will fall by 30 percent before stabilising in 2018.

6.4.3 Results of stress tests

To evaluate the effect of the stress test, the change is calculated in SBAB's capital adequacy ratios resulting from increased capital requirements, reduced own funds and greater loan losses. In the stress scenario characterised by a severe recession, both the capital requirement and expected losses would increase significantly, albeit from very low levels. At the same time, net interest income would deteriorate relative to the basic scenario as a result of increased funding expenses. As a result of the simulation of a difficult but not unlikely scenario, SBAB's Common Equity Tier 1 capital ratio would weaken according to the below.

FIGURE 7. **COMMON EQUITY TIER 1 CAPITAL RATIO IN A STRESSED SCENARIO**



To counteract the weakening of SBAB's Common Equity Tier 1 capital ratio, a provision of SEK 2,370 million is made as a buffer, which is the additional Common Equity Tier 1 capital required to maintain an unchanged Common Equity Tier 1 capital ratio relative to the basic scenario. However, most of SBAB's credit exposures are covered by the risk weight floor for Swedish mortgages and, consequently, the capital requirements will not increase due to a reasonable increase in risk in the loan portfolio. Excluding the increase in the capital requirements for Swedish mortgages, a provision of SEK 640 million has been made as a buffer.

6.5 Capital requirement due to earnings volatility

Due to the structure of the accounting regulations, whereby different parts of the balance sheet are measured differently, valuation effects arise that affect operating profit and thereby the capital base without constituting a real market risk.

Basis swaps not included in a hedging relation are to be measured at fair value while the loans to which the basis swaps are linked are not fully measured at market value in case there is no hedge accounting. This means that the basis risk on basis swaps that are not subject to hedge accounting lack counter-items in profit and loss.

This has the effect that operating profit, and thereby the capital base, varies in a manner that does match the actual risk to which the portfolio is exposed. To simulate how much this can conceivably affect the own funds, a simplified value at risk (VaR) model has been used. The model is based on a holding period of one year and a confidence level of 99.97 percent. The capital requirement for earnings volatility is estimated to SEK 228 million at per 31 December 2015.

6.6 Risk weightings for residential mortgages and a standardised assessment of Pillar 2 risks

In September 2014, the Swedish Financial Supervisory Authority decided to raise the risk weight floor for Swedish residential mortgages to 25 percent from the previous 15 percent. The floor is applied as a supervisory practice in internal capital adequacy assessment under Pillar 2 and consequently does not affect the capital ratios reported under Pillar 1. SBAB has already allocated more capital to the residential mortgage portfolio than that demanded under the minimum requirements of Pillar 1, since its economic capital for credit risk has exceeded the minimum capital requirements under Pillar 1.

In addition to the risk weight floor, the Swedish Financial Supervisory Authority has introduced standardised methods to assess risks that are not included in Pillar 1 within the framework for supervision within Pillar 2. It is expected that methods for interest-rate risk within the banking book, credit risk and pension risk were adopted in 2015.

According to the Swedish Supervisory Authority's supervisory practices, it is expected that SBAB will cover a certain part of its capital requirement for Pillar 2 risks with Common Equity Tier 1 capital. Pillar 2 risks shall as a general rule be covered according to the same capital distribution as the requirement for capital 1, including static buffer requirements (capital conservation buffer, systemic risk buffer and O-SII buffer). For SBAB, this means that 67 percent of the capital requirement for Pillar 2 risks should be covered with Common Equity Tier 1 capital.

SBAB's internally calculated capital requirements without and with consideration for the risk weight floor for Swedish residential mortgages are stated below. SBAB's internally assessed capital requirement corresponds to a Common Equity Tier I capital ratio of 22.7 percent and a total capital ratio of 32.9 percent. According to the targets set out in SBAB's capital policy, these levels should, under normal conditions, be exceeded by at least 1.5 percent of the risk exposure amount. Accordingly, the Common Equity Tier I capital ratio should amount to at least 24.2 percent and the total capital ratio to at least 34.4 percent as per 31 December 2015.

TABLE 13. **INTERNALLY CALCULATED CAPITAL REQUIREMENTS PER RISK TYPE**

		EXCLUSIVE OF THE RISK WEIGH FLOOR		INCLUSIVE OF THE RISK WEIGHT FLOOR
SEK million		**Pillar 1**	**Internally assessed capital requirements**	**Internally assessed capital requirements**
Pillar 1	Credit & CVA risk[1)]	2,672	2,672	2,672
	Market risk	149	149	149
	Operational risk	239	239	239
Pillar 2	Credit risk		1,101	
	Market risk		1,006	1,006
	Operational risk		111	111
	Risk-weight floor		0	6,175
	Concentration risk		562	562
	State risk		67	67
	Pension risk		21	21
	Earnings volatility		228	228
Buffers	Capital conservation buffer	956	956	956
	Capital planning buffer, supplement[2)]		1,414	–
	Countercyclical buffer	379	379	379
		4,395	**8,905**	**12,565**

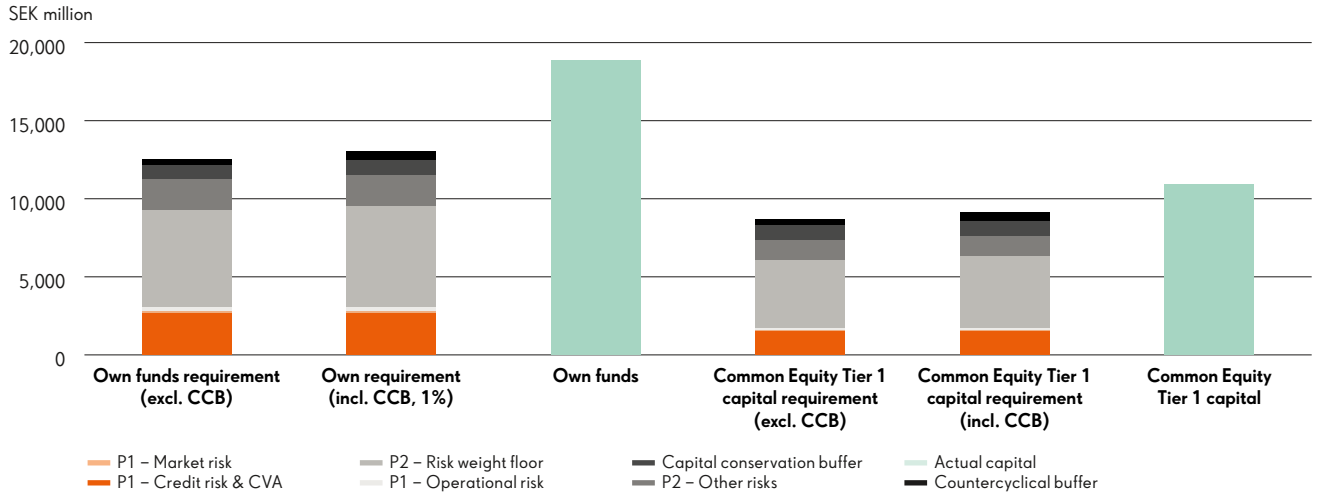
[1)] In internal capital requirement without consideration for the risk weight floor, additional credit risks in Pillar 2 consists of SBAB's estimated capital requirement in economic capital. As the additional capital requirement for the risk weight floor is larger that the additional capital requirement according to economic capital, only the risk weight floor is included in internal capital requirement with consideration for the risk weight floor.

[2)] The higher of the stress test buffer and capital planning buffer are included in internal capital requirements. With consideration for the risk weight floor, the stress test buffer is calculated without consideration for risk migration in the residential mortgage portfolios, so the required buffer is smaller.

According to its supervision and evaluation process, the Swedish Financial Supervisory Authority's assessed SBAB's Common Equity Tier I capital to correspond to a Common Equity Tier I capital ratio of 20.4 percent, corresponding to total capital ratio requirement of 30.6 percent.

The requirements for a countercyclical buffer for Swedish exposures will be increased from the current 1 percent to 1.5 percent as of June 2016. The effect of this is illustrated in figure 8 below.

FIGURE 8. **INTERNAL CAPITAL REQUIREMENTS TAKING THE INCREASED REQUIREMENTS FOR A COUNTERCYCLICAL BUFFER (CCB) INTO ACCOUNT**



7 LEVERAGE RATIO

According to the Basel 3 agreement, the bank must have a leverage ratio of 3 percent effective from 2018. In a decision made in January 2015, the Basel Committee confirmed that the minimum level will be 3 percent. However, changes may be made to the definition during 2016.

The leverage ratio is a measure of solvency. Compared with the capital adequacy requirement, assets are not weighted but rather the same amount of capital is required, regardless of what risk is associated with the assets. The leverage ratio is calculated as Common Equity Tier I capital divided by the total exposure amount. According to current reporting practices, SBAB's leverage ratio amounted to 3.15 percent as of December 2015 and 2.91 percent calculated as an average over three months.

8 RISK IN THE REMUNERATION SYSTEM

SBAB is to have a remuneration system that is both compatible with and promotes effective risk management and does not encourage undue risk-taking. Remuneration is to promote SBAB's long-term interests. Further information on remuneration systems is available in Note 8 of SBAB's annual report and on the website sbab.se.

The Annual General Meeting decides on the overall principles for remuneration and other employment benefits for senior executives (members of SBAB's executive management). The Board of Directors decides on:

- Remuneration policy and risk analysis regarding remuneration systems
- Remuneration and other employment benefits for Executive Management and the heads of the control functions (the CRO and the heads of Internal Audit and Compliance).
- Follow up on the application of SBAB's control documents regarding remuneration issues.

The Board has appointed a Remuneration Committee. Members of the Remuneration Committee and the number of meetings can be found in the Corporate Governance Report in SBAB's Annual Report at sbab.se.

The principal task of the Remuneration Committee is to prepare motions regarding principles for remuneration and other employment terms and conditions for senior executives for resolution by the Board. The Remuneration Committee also prepares matters pertaining to SBAB's remuneration system ahead of Board decisions. The Remuneration Committee follows up remuneration structures and remuneration levels within SBAB. The Board of Directors decides on the mission description for the Remuneration Committee. The meetings of the Remuneration Committee are reported back to the Board of Directors through the minutes prepared from the Remuneration Committee's meetings. The Board of Directors is to annually evaluate and follow up how SBAB has complied with the principles for the remuneration of senior executives that have been decided on by the Annual General Meeting and the remuneration structures and remuneration levels, including bonuses, in SBAB.

SBAB has had no variable remuneration in recent years and there are no funds retained regarding personnel subject to specific terms.

9 CREDIT RISK IN LENDING OPERATIONS

SBAB conducts customer-oriented credit operations in which guiding principles such as professionalism, simplicity and quality create the conditions for favourable profitability and long-term customer relations. This means that the credit operations are to be characterised by high credit quality, efficient decision-making processes, respect for and understanding of the customer's situation, straightforward conduct, language and procedures, balanced risk-taking in the portfolio and in each individual transaction, and risk-based pricing.

9.1 Credit risk management

SBAB shall have documented risk management regarding credit risk with a clear division of responsibilities. The credit risk management shall support the business operations, ensure SBAB's survival and be in line with SBAB's rating targets. SBAB's credit operations shall be characterised by low risk taking. Business-related risks shall be viewed in relation to arisen earnings. Credit risk shall be considered in business decisions and constitute a component in the pricing of products and services.

SBAB's Board and Executive Management shall be actively involved in the design of the institution's risk management system and the follow-up of credit risks. The Board of Directors or its committees shall approve all significant methods, models and processes related to credit risk.

The reporting structure shall be designed so that the Board of the Parent Company and the Executive Management receives reports on all material risks, including credit risk. There shall be procedures for managing and acting, based on the information provided in the reports.

9.2 Credit risk in the lending portfolio

Credit risk is the single largest risk in SBAB and accounts for 84 percent of the risk exposure amount according to Pillar 1. Credit risk is defined as the risk of loss due to the customer's inability to pay interest and make loan repayments or otherwise fulfil the loan agreement. Credit risk arises in conjunction with loans and loan promises, and also in connection with impairment of the value of pledged assets entailing that these no longer cover the Group's receivables.

In the approval of a new loan, the credit checked first by the business area and then, in some cases, by the credit department. Credit risk is then monitored through portfolio management by Risk Control, which is also responsible for analysing credit risk. Each business operation deals with the practical management of credit risk.

Credit risk in lending operations is restricted by limits determined for the customer or customer group. The credit risk is also managed through a credit-granting process, whereby the ability of potential borrowers to make their interest payments and pay amortisation is analysed. For example, new retail loans are granted only to borrowers who are expected to be able to pay interest and amortisation in an interest-rate situation that significantly exceeds today's levels. Furthermore, risk classification based on the IRB approach is used in the analysis of the credit risk for new and existing customers in the loan portfolios. Large exposures, meaning those amounting to 10 percent or more of the capital base, are managed based on the credit directives and external regulations. All exposures exceeding 2 percent of the capital base are identified and analysed for the purpose of deciding whether they fall within the framework of large exposures in relation to a group of customers with internal association.

The granting of credit requires the provision of adequate collateral, which can be provided in the form of real property or a unit in a tenant-owner association. Adequate collateral usually means mortgage deeds in a property or a tenant-owner right of up to 75–85 percent of the market value. The 85 percent ratio applies provided that collateral can be obtained with first lien and that the customer has risk class R1–R4 for retail customers and C1–C3, and manually adjusted from C3–C4, for corporate customers (for the relation between risk class and rating, please refer to Table 15). In other cases, a loan to value ratio of 75 percent applies in general. SBAB also grants small unsecured loans to borrowers in the retail segment.

SBAB has decided to double the amortisation rate down to a loan-to-value ratio of 70 percent, meaning that the customer must pay off the portion that is above 70 percent over 7.5 years, rather than 15 years as previously. The requirement is risk-based, in that clients with a higher loan-to-value ratio must repay a larger amount than those with a lower loan-to-value ratio. Furthermore, SBAB has, in two stages, lowered the ceiling on the debt ratio for new loans. At the end of 2015, the limit was 6.0.

In case of lending to consumers, market values for collateral in the form of properties or rights of use shall generally be determined by the administrator, based on approved calculation models. If the market value cannot be determined using approved calculation models, it shall be determined by the person in charge of valuations or an approved external valuer.

Market values for collateral in the form of properties or rights of use in case of lending to tenant-owner associations and companies shall generally be determined by the person in charge of valuations. External valuations can form the basis of decisions upon approval by the person in charge of valuations. If an external valuation is carried out by an approved external valuer, the valuation does not require approval by the person in charge of valuations.

SBAB verifies the property value on a regular basis. For residential properties and tenant-owner rights, the property value is

verified at least every third year. For other properties, the value is verified at least every year. If there are major changes in economic factors that affect the property market, the value is verified more often.

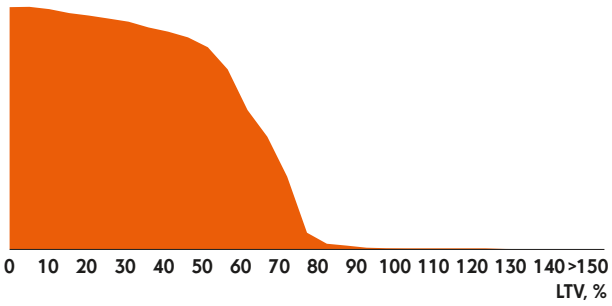
In addition to collateral in real property or a unit in a tenant-owner association, it is possible to grant credit against, for example, collateral in the form of a state credit guarantee, a municipal guarantee, securities, bank guarantees and deposits in a Swedish bank. To a limited extent, equities corresponding to up to 85 percent of the market value of the underlying property can be approved as collateral. SBAB does not hold any collateral that has been taken over to protect a receivable.

Lending to the public accounts for 79 percent of SBAB's overall assets. Figures 9 and 10 describe loan-to-value (LTV) for loans for which collateral consists of mortgage deeds on a unit in a tenant-owner association. Figure 9 shows corporate exposures and Figure 10 shows retail exposures[1]. The figures cover 97 percent of total lending to the public. Since 80 percent of lending has collateral in mortgage deeds or in units in tenant-owner associations, within 50 percent LTV and 97 percent within 75 percent LTV, while 93 percent of borrowers are categorised in risk classes 1–4, the credit quality is viewed as being very favourable (see the table under Figures 9 and 10).

FIGURES 9 AND 10. **LOAN-TO-VALUE (LTV) FOR CORPORATE AND RETAIL EXPOSURES**

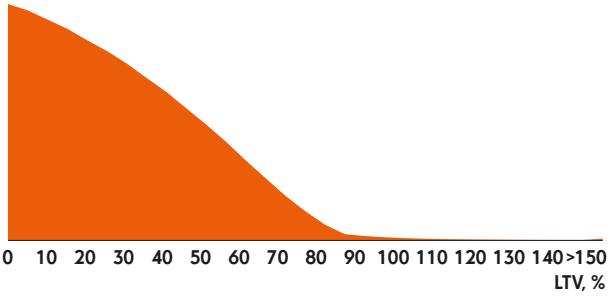
EXPOSURES TO CORPORATES

Lending volume



RETAIL EXPOSURES

Lending volume



Segment, %	Below 50%	Below 75%	Below 100%	Exposure weighted average LTV
Exposures to corporates	75.7	98.9	99.8	66.0
Retail exposures	80.3	97.2	99.6	59.6
Total	**79.9**	**97.4**	**99.6**	**60.2**

[1] "Retail loans" refers to all lending to the public pertaining to single-family homes, holiday homes and tenant-owner rights, as well as unsecured loans to private individuals and loans to tenant-owner associations with a turnover of less than EUR 50 million. "Loans to corporates" refers to loans to other legal entities and to other loans to private individuals.

9.3 Risk classification system

SBAB applies the IRB approach for retail loans and lending to tenant-owner associations and the foundation IRB approach (FIRB approach) for Corporate loans. These commitments comprise 98 percent of lending to the public. For other types of exposures, including unsecured loans, the standardised approach is used for measurement of credit risk.

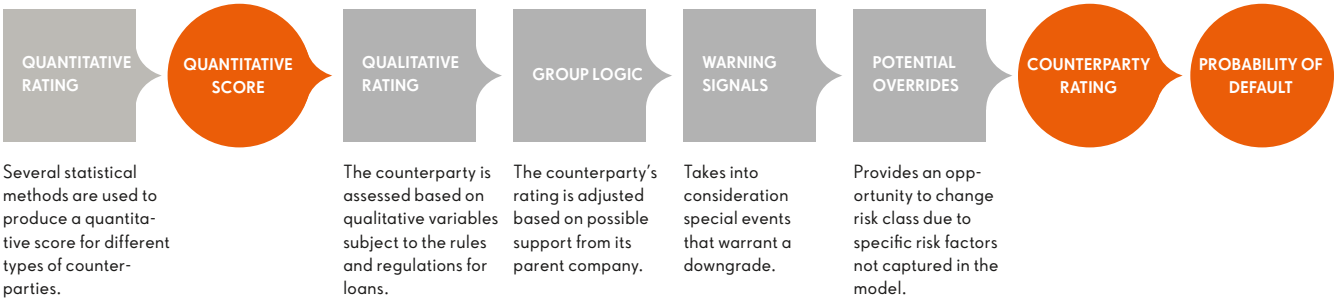
The IRB approach has been used since 2007 used for assessing credit risk where a mortgage deed or a tenant-owner right is used as collateral. In 2013, permission was received to include housing associations with a turnover of less than EUR 50 million in the Retail exposures class, for which SBAB holds an IRB permit. In 2015, SBAB also received permission to use the IRB approach for excess exposures that are not fully covered by mortgage deeds, property financing using other collateral than directly pledged mortgage deeds and letters of credit. Previously, the standardised approach was used for these exposures.

In credit risk models, an assessment is made of the probability of default[2] and share of loss, as well as the proportion of loan commitments utilised in the event of default. On the basis of these parameters, together with exposure at default (EAD), customers can be ranked according to credit risk and the expected and unexpected loss can be estimated. After assessment, the exposure is referred to one of eight risk classes for corporate and retail loans, of which the eighth class comprises customers in default. The trend for customers in high-risk classes is monitored thoroughly and, when necessary, exposure is managed actively by credit monitoring personnel.

The IRB models are used throughout SBAB's operations for tasks such as granting of credit, pricing, portfolio analysis and performance monitoring per business area. All deviations from the quantitatively calculated risk class are analysed. The models produced are validated annually by Risk Control and, whenever required, they are recalibrated. The validations carried out for 2015 did not result in any changes to models. A major challenge in the validation process has been that the number of defaults and losses has been very low.

For those customer segments within corporate exposures for which current financial statements are available, the quantitative assessment process is supplemented with a systematic qualitative assessment in accordance with SBAB's rules and regulations, based on a number of questions (see Figure 11). For other customer segments involving corporate lending, credit analysts add their assessment of risk class and an explanatory statement to the supporting material for assessment of risk class in the decision-processing system.

FIGURE 11. **INTERNAL RISK CLASSIFICATION METHOD FOR CORPORATE CLIENTS**



[2] An exposure is regarded as in default if the receivable is more than 60 days past due (for receivables exceeding SEK 1,000) or if the assessment has been made that the customer will probably not be able to pay agreed interest amounts or cover repayments of the principal.

9.4 Risk classification method

In conjunction with capital adequacy and risk classification, exposures are categorised in exposure classes. The IRB approach is applied for corporate exposures with collateral in real property, while in the case of retail exposures, the advanced IRB approach, with collateral in residential property or a unit in a tenant owner association, is applied. Loans to tenant-owner associations with a turnover of less than EUR 50 million and 100 percent collateral in residential property are reported in the retail exposure class. For central government, institutional, corporate and other exposures for which collateral other than a mortgage deed or a unit in tenant-owner associations has been received, the standardised approach is applied. The portion of loans for which a municipality or the Swedish National Housing Credit Guarantee Board (currently a part of the Swedish Board of Housing Building and Planning) has issued a guarantee is referred to central government and municipal exposures and is recognised in accordance with the standardised approach. Table 9, capital requirements and risk exposure amounts, shows the distribution of capital requirements by exposure classes and risk exposure amounts.

With regard to exposures that are assessed using the IRB approach, SBAB has opted to use a scoring method for risk classification of counterparties in the PD dimension. The data on which the scoring models are based was obtained from both internal and external sources. Internal data consists of customer information, loan information, default outcomes and internal payment records. Data obtained externally includes financial accounts, external payment records, property data and macroeconomic data.

SBAB's PD models for corporate exposures and exposures to tenant-owner associations are based on data originating in December 1996. PD models for exposures to private individuals are based on data from September 2001 and onwards. In preparing PD estimates, data from the financial crisis of the 1990s and onwards are also used. Table 14 shows the distinction between retail exposures and corporate exposures.

For off-balance sheet retail exposures, which primarily consist of retain residential mortgage commitments to private individuals, SBAB uses in-house estimates of the credit conversion factor (CCF). In the CFF calculation, a scoring model is used to estimate the probability that the exposure will end up on SBAB's balance sheet. The model builds primarily on how far the particular loan case has progressed in SBAB's credit approval system. The estimated probability is used to allocate each exposure to eight CCF risk classes. The CCF estimate, including the safety margin, is calculated as the 99-percentile of the average approval frequencies per monthly observation point in the particular CFF classes.

TABLE 14. **LOAN PORTFOLIOS AND EXPOSURE CLASSES FOR WHICH THE IRB METHOD IS APPLIED**

Portfolio	Property	Exposure class	PD-model
Corporate	Private properties		
	Tenant-owner associations (turnover ≥ EUR 50 million)	Corporate exposures	Corporate
	Commercial properties		
Retail	Single-family dwellings and holiday homes		
	Tenant-owner rights	Retail exposures	Retail
	Tenant-owner associations (turnover < EUR 50 million)		

9.5 The link between external and internal ratings

SBAB's risk classes are not directly comparable to the ratings used by external credit rating agencies. The credit rating agencies' ratings do not correspond to a direct classification of the counterparties' probability of default in the same way that the bank's risk classification does. The credit rating agencies also consider, to a varying degree, the seriousness of the losses that may be caused by default, whereas SBAB captures this in the LGD dimension.

The time horizon on which the credit rating is based is not always the same for credit rating agencies as for SBAB. Accordingly, it is difficult to translate internal risk classes to external ratings unequivocally and consistently. However, by analysing the historic proportion of default in SBAB's risk classes compared to the proportion of default in Standard & Poor's rating classes, it is possible to obtain a reasonably correct comparative table. Table 15 presents the external rating classes that best correspond to the historic proportion of default in each of SBAB's risk classes.

TABLE 15. **RELATIONSHIP BETWEEN INTERNAL AND EXTERNAL RATING**

Risk class	Standard & Poor's rating
C1	AAA–A
C2	A
C3	A–BBB
C4	BBB-BB
C5	BB
C6	BB–C
C7	B–C

Risk class	Standard & Poor's rating
C/R1	AAA–AA
R2	AA–A
R3	A
R4	A–BBB
R5	BBB–BB
R6	BB
R7	BB–C

9.6 Exposure amounts by exposure class

In contrast to other tables in this section, Table 16 shows all credit-risk exposures both in and outside the lending portfolio. Without taking credit risk protection into account, the total amount for all credit risk exposures was SEK 388,509 million.

Credit risk protection used for IRB exposures consist of government and municipal guarantees. Loans backed by collateral in the form of a unit in a tenant-owner association or mortgage deeds account for the entire amount for IRB exposures. Residential properties that constitute collateral are first valued at the lending occasion and subsequently at least every third year. Commercial properties are measured annually. Credit risk protection is not used for exposures reported in accordance with the standardised approach.

Although SBAB has also obtained credit-loss guarantees of SEK 206 SEK million from business partners, these are not used when calculating capital adequacy ratios. In addition, the Parent Company and SCBC have jointly taken up credit insurance with Genworth Financial Mortgage Insurance Limited (Genworth), which is also not used when calculating capital adequacy. The credit insurance covers that part of the principal that exceeds 85 percent of the value of collateral pledged. The insured principal amounted to SEK 138 million at 31 December 2015. The insurance policy has been cancelled effective 1 January 2009 and cannot be utilised for new loans. However, the policy continues to apply as before for loans that were covered by the insurance from the start. Genworth has a rating of BB- (Standard & Poor's).

Corporate exposures comprised only 11 percent of total exposures in the loan portfolio for which the IRB approach is used, but due to the higher average risk weighting, the exposures account for 43 percent of the total capital requirement according to Pillar 1 when the IRB approach is applied.

The average exposure amount for the corresponding loan portfolio, calculated on the basis of the exposure amount in the lending portfolios at the end of each month in the past year, was SEK 277,413 million, of which 89 percent comprised retail exposures. Loan promises and other credit-related commitments totalled SEK 47,949 million which, after the credit conversion factor was taken into account, amounted to SEK 13,242 million.

Risk exposure amounts for credit exposures amounted to SEK 32,254 million, of which SEK 24,898 million was recognised in accordance with the IRB approach and SEK 7,356 million according to the standardised approach. The average risk weighting for exposures recognised in accordance with the IRB approach was 8.1 percent, while the weighting for exposures recognised in accordance with the standardised approach was 15.4 percent. Exposure-weighted average PD per counterparty for IRB exposures amounted to 0.39 percent for corporate exposures and 0.64 percent for retail exposures. Exposure-weighted average LGD for corporate exposures was 36.7 percent and exposure- weighted LGD for retail exposures was 10.0 percent. The exposure-weighted amount for LGD is controlled by the limitation rule, which entails a lowest total level for LGD of 10 percent for retail exposures covered by the advanced IRB approach, for which collateral consists of a tenant-owner right, a mortgage in a residential property or the site leasehold on such a property.

TABLE 16. **EXPOSURE AMOUNTS BY EXPOSURE CLASS FOR CREDIT RISK EXPOSURES**

SEK million	Exposure before credit risk protection	Securities that reduce capital requirements in the form of guarantees and financial securities and the effect on credits reported according to the standardised approach.	Exposure within the line before the conversion factor	Exposure after conversion factor[1)]	Exposure within the line after the conversion factor	Exposure amounts covered by credit risk protection in the form of properties	Average exposure amounts for exposures in the lending portfolio[2)]	REA	Capital requirements	Average risk weight	Individual provision	Collective provisions with deduction for guarantees	Expected loss	Exposure-weighted average PD	Exposure-weighted average LGD
Credit risk recognised in accordance with IRB approach	0	0	0	0	0	0	0	0	0		–1	0	0	0	0
Exposure to corporates	36,029	–265	3,523	34,836	2,596	34,836	28,482	10,795	864	31.0%	18	1	50	0.39%	36.7%
Retail exposures	305,509	–1,383	43,343	271,213	10,429	271,213	243,884	14,103	1,128	5.2%	58	122	231	0.64%	10.0%
of which, Single-family dwellings and holiday homes	*131,829*	*–161*	*16,235*	*119,421*	*3,989*	*119,421*	*110,263*	*6,643*	*531*	*5.6%*	*6*	*61*	*107*	*0.68%*	*10.77%*
of which, tenant-owner rights	*122,698*	*0*	*26,808*	*102,133*	*6,242*	*102,133*	*84,239*	*5,832*	*467*	*5.7%*	*26*	*53*	*93*	*0.70%*	*9.77%*
of which, tenant-owner associations	*50,982*	*–1,222*	*300*	*49,659*	*198*	*49,659*	*49,382*	*1,628*	*130*	*3.3%*	*25*	*8*	*31*	*0.44%*	*8.63%*
Total credit risk in accordance with IRB approach	**341,538**	**–1,648**	**46,866**	**306,049**	**13,025**	**306,049**	**272,366**	**24,898**	**1,992**	**8.1%**	**76**	**123**	**281**		
Credit risk in the lending portfolio recognised in accordance with standardised approach															
Exposures to central governments and central banks	5,001	144	–	5,145	–	–	174	0	0	0.0%	–	–			
Exposures to regional governments or local authorities	4,013	1,504	–	5,517	–	–	1,777	0	0	0.0%	–	–			
Exposures to multilateral development banks	336	–	–	336	–	–		0	0	0.0%	–	–			
Exposures to institutions	3,499	–	–	3,499	–	–	–	1,526	122	43.6%	–	–			
Exposure to corporates	15	–	–	15	–	–	523	15	1	100.0%	–	–			
Retail exposures	3,683	–	1,083	2,808	217	–	2,564	2,106	168	750%	–	9			
Defaulted exposures	12	–	0	5	0	–	9	7	1	121.5%	5	1			
Exposures in the form of covered bonds	29,567	–	–	29,567	–	–	–	2,957	237	10.0%	–	–			
Exposures to institutions and corporates with a short-term credit assessment	59	–	–	59	–	–	–	15	1	26.5%	–	–			
Other items	786	–	–	786	–	–	–	730	58	92.9%	–	–			
Total credit risk in accordance with standardised approach	**46,971**	**1,648**	**1,083**	**47,737**	**217**	**–**	**5,047**	**7,356**	**588**	**15.4%**	**5**	**10**			
Total	**388,509**	**0**	**47,949**	**353,786**	**13,242**	**306,049**	**277,413**	**32,254**	**2,580**	**9.1%**	**81**	**133**			

[1)] In exposures after inflows and outflows, adjustments have been made of amounts to be recognised and covered by capital in an exposure class other than the original one.
[2)] Off-balance sheet exposures have been excluded.

The information in this section is from 31 December 2015 but it differs from the information provided in the Annual Report 2015 as the exposure amounts, including accrued interest, are reported instead of the principal. Compared with the annual report, the tables detailing lending operations do not include a claim against Nasdaq/OMX of SEK 14.6 million that is outside the ordinary lending operations. When the term exposure is used in the following section of this chapter, it refers to exposure after outflows or inflows, i.e. exposure before credit risk with deductions for collateral, inflows and off-balance sheet exposure, unless stated otherwise. The tables may contain differences due to rounding off.

9.7 Exposure amounts by geographical region

SBAB's lending operations are concentrated to Sweden. There is some exposure to other countries in Western Europe, Canada and USA due to the funding of the Swedish lending operations.

SBAB's lending portfolio is mainly secured by housing in the Stockholm area (56 percent) and the Öresund region (19 percent). Only 1 percent of the underlying collateral derives from economically weak regions. Sweden is divided as follows:

- Greater Stockholm: Stockholm's labour market region according to Statistics Sweden (SCB) (2004);
- Greater Gothenburg: Gothenburg's labour market region according to SCB (2004);
- The Öresund region: Labour market regions in Malmö and Helsingborg according to SCB (2004);
- University and growth regions: Municipalities with universities and municipalities with especially buoyant growth according to analyses by SBAB;
- Weak regions[1)]: Municipalities with very weak or negative growth according to analyses by SBAB;
- Other regions[1)]: Municipalities that are not allocated to any other category.

TABLE 17. **EXPOSURE AMOUNT PER GEOGRAPHICAL AREA FOR CREDIT RISK EXPOSURES**

SEK million	Sweden	Denmark	Finland	France	Germany	Norway	United Kingdom	USA	Canada	Switzerland	Other countries	Total
Credit recognised in accordance with the IRB approach												
Exposure to corporates	32,241	–	–	–	–	–	–	–	–	–	–	32,241
Retail exposures	260,783	–	–	–	–	–	–	–	–	–	–	260,783
of which, exposures to small and medium-sized companies	*49,461*	–	–	–	–	–	–	–	–	–	–	*49,461*
of which, exposures to tenant-owner rights, single-family dwellings and holiday homes	*211,323*	–	–	–	–	–	–	–	–	–	–	*211,323*
Total exposures recognised in accordance with the IRB approach	**293,024**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**293,024**
Credit risk recognised in accordance with standardised approach												
Exposures to central governments and central banks	5,077	–	68	–	–	–	–	–	–	–	–	5,145
Exposures to regional governments or local authorities	5,517	–	–	–	–	–	–	–	–	–	–	5,517
Exposures to multilateral development banks		–	–	–	–	–	–	–	–	–	336	336
Exposures to institutions	1,052	950	–	119	61	15	952	319	2	29	–	3,499
Exposure to corporates	15	–	–	–	–	–	–	–	–	–	–	15
Retail exposures	2,600	–	–	–	–	–	–	–	–	–	–	2,600
Defaulted exposures	12	–	–	–	–	–	–	–	–	–	–	12
Exposures in the form of covered bonds	28,251	477	–	–	–	464	–	–	375	–	–	29,567
Exposures to institutions and corporates with a short-term credit assessment	59	–	–	–	–	–	–	–	–	–	–	59
Other items	786	–	–	–	–	–	–	–	–	–	–	786
Total exposures recognised in accordance with standardised approach	**43,369**	**1,427**	**68**	**119**	**61**	**479**	**952**	**319**	**377**	**29**	**336**	**47,536**
Total	**336,393**	**1,427**	**68**	**119**	**61**	**479**	**952**	**319**	**377**	**29**	**336**	**340,560**

[1)] The analysis is based in part on statistics from SCB, such as short and long-term population growth, the proportion of the population older than 64 years, average income and the vacancy rate in public utility housing, and in part on the local knowledge of SBAB's analysts.

TABLE 18. **EXPOSURE AMOUNT PER GEOGRAPHICAL AREA FOR THE LENDING OPERATIONS**

SEK million	Greater Stockholm	Greater Gothenburg	Öresund region	University and growth regions	Weak regions	Other regions	Total
Credit risk recognised in accordance with IRB approach							
Exposure to corporates	13,860	2,578	6,465	5,523	817	2,998	32,241
Retail exposures	151,396	22,304	48,215	21,606	3,230	14,033	260,784
Total exposure recognised in accordance with IRB approach	**165,256**	**24,882**	**54,680**	**27,129**	**4,047**	**17,031**	**293,025**
Standardised exposures							
Exposures to central governments and central banks	28	5	24	41	16	30	144
Exposures to regional governments or local authorities	394	140	96	302	171	408	1,511
Exposure to corporates	0	0	0	0	0	0	0
Retail exposures	1,433	259	341	303	73	191	2,600
Defaulted exposures	9	1	1	1	0	0	12
Total exposures recognised in accordance with standardised approach	**1,864**	**405**	**462**	**647**	**260**	**629**	**4,267**
Total	**167,120**	**25,287**	**55,142**	**27,776**	**4,307**	**17,660**	**297,292**

9.8 Exposure amounts by next stipulated term of expiry

A large proportion (62 percent) of credit risk exposures have less than one year remaining until maturity.[1)] The proportion with a remaining term of between one and five years accounts for 36 percent of the outstanding exposure. The inflows from exposures assessed according to the IRB method has been divided into government exposures and municipal exposures in the table. Exposures in other items where the duration cannot be calculated have been placed in the interval less than a year to provide a better overview.

TABLE 19. **EXPOSURE AMOUNTS DISTRIBUTED ACCORDING TO REMAINING MATURITY FOR CREDIT RISK EXPOSURES**

SEK million	< 1 year	1–5 years	> 5 years	Total
Credit risk recognised in accordance with IRB approach				
Exposure to corporates	7,760	24,113	368	32,241
Retail exposures	197,222	59,720	3,841	260,783
Total exposure recognised in accordance with IRB approach	**204,982**	**83,833**	**4,209**	**293,024**
Credit risk recognised in accordance with standardised approach				
Exposures to governments and central banks	938	4,207	0	5,145
Exposures to regional governments or local authorities	1,823	3,576	118	5,517
Exposures to multilateral development banks	–	336	–	336
Exposures to institutions	940	2,153	406	3,499
Exposure to corporates	15	–	–	15
Retail exposures	2,600	–	–	2,600
Defaulted exposures	12	–	–	12
Exposures in the form of covered bonds	421	28,157	989	29,567
Exposures to institutions and corporates with a short-term credit assessment	59	–	–	59
Other items	786	–	–	786
Total exposures recognised in accordance with standardised approach	**7,594**	**38,429**	**1,513**	**47,536**
Total	**212,576**	**122,262**	**5,722**	**340,560**

[1)] For credit risk exposures in the lending portfolio, the next stipulated date of expiry has been used. The stipulated date of expiry is defined as the day for establishing the conditions that are to apply for loans during the forthcoming contractual period. The terms must be supported by the stipulations of the original loan agreement.

9.9 Exposure amounts by type of property

In the distribution of the lending portfolio by type of property, lending for single-family dwellings, holiday homes, tenant-owner rights and tenant-owner associations accounts for 89 percent of the total lending portfolio.

TABLE 20. **EXPOSURE AMOUNTS BY TYPE OF PROPERTY FOR CREDIT RISK EXPOSURES IN THE LENDING OPERATIONS**

SEK million	Single-family dwellings and holiday homes	Tenant-owner	Tenant-owner associations	Private multi-family dwellings	Municipal multi-family dwellings	Commercial properties	Unsecured	Total
Credit risk recognised in accordance with IRB approach								
Exposure to corporates	13	–	1,780	25,846	284	4,318	–	32,241
of which, exposures to small and medium-sized companies	*13*	–	–	*11,929*	*212*	*1,457*	–	*13,611*
Retail exposures	115,433	95,890	49,461	–	–	–	–	260,784
Total exposure recognised in accordance with IRB approach	**115,446**	**95,890**	**51,241**	**25,846**	**284**	**4,318**	**–**	**293,025**
Credit risk recognised in accordance with standardised approach								
Exposures to central governments and central banks	22	–	115	7	–	–	–	144
Exposures to regional governments or local authorities	140	–	1,111	71	188	2	–	1,512
Exposure to corporates	–	–	–	–	–	–	–	–
of which, exposures to small and medium-sized companies	–	–	–	–	–	–	–	–
Retail exposures	200	360	–	–	–	–	2,040	2,600
Defaulted exposures	1	0	–	–	–	–	10	11
Total exposures recognised in accordance with standardised approach	**363**	**360**	**1,226**	**78**	**188**	**2**	**2,050**	**4,267**
Total	**115,809**	**96,250**	**52,467**	**25,924**	**472**	**4,320**	**2,050**	**297,292**

9.10 Past due exposures and exposures subject to impairment requirements

Past due exposures refer to total claims where any part is more than five days past due. SBAB has elected to use this method so that the result of the analysis is not distorted when payments are delayed because the payment date coincided with a public holiday. Exposures subject to impairment requirements refer to doubtful exposures whereby individual provisions have been posted for commitments relating to corporate loans or retail loans, meaning that in SBAB's assessment, future payments are exposed to risk and the collateral does not cover the amount of the claim. The selection used for provisions comprises all corporate customers where there is objective evidence of impairment and individual private customers where special reasons for impairment exist. All exposures in risk class C8 are reviewed monthly and assessed for risk. The size of the individual provision is assessed by comparing the agreed payment flow from the customer with the expected future payment capacity, whereby an analysis of the property's cash flow is included as an important parameter in combination with a valuation of the underlying collateral. Customers in risk class R8 are covered by the individual provision, in special cases after individual assessment. The individual and collective provisions, with deductions for guarantees, amounted to 43 percent of the exposure amount for past due exposures.

The collective provision is intended to cover losses for events that have occurred but that have not yet had effect on the individual level in the form of payment difficulties or been otherwise identified in an individual review of commitments. The collective provision consists of customers in risk classes C6–C8 and R5–R8. All individually reserved loans are automatically excluded. Other customers in risk class C8 are included in the collective reserve but with a risk of loss of SEK 0. The risk of loss is estimated at SEK 0 as SBAB has assessed these individually and there is no need for them to be included in the collective provision.

All provisions have been assessed to constitute specific risks based on Article 1, item 5, of EBA's regulatory technical standards regarding specific and general risk regarding Article 110(4) of the CRR.

TABLE 21. **EXPOSURES WITH PAST DUE AMOUNTS AND PROVISIONS**

				SPECIFIC RISK		
SEK million	**Total exposure amount in the lending portfolio**	**Exposure amounts for past due receivables[1)]**	**Exposure amounts for exposures with individual provisions**	**Individual provision**	**Collective provisions with deduction for guarantees**	**Total exposure amount in the lending portfolio after deduction for provisions**
Single-family dwellings and holiday homes	115,809	304	19	6	62	115,741
Tenant-owner rights	96,251	158	90	27	53	96,171
Tenant-owner associations	52,467	18	27	25	8	52,434
Private multi-family dwellings	25,924	–	30	18	0	25,906
Municipal multi-family dwellings	471	–	–	–	–	471
Commercial properties	4,320	–	–	–	–	4,320
Unsecured	2,050	13	5	5	10	2,035
Total	**297,292**	**493**	**171**	**81**	**133**	**297,078**

1) For past due receivables, amounts past-due by five days or less are not taken into consideration to ensure that the analysis is not distorted by payments delayed because the payment date is a holiday.

TABLE 22. **GEOGRAPHICAL DISTRIBUTION OF EXPOSURES WITH PAST DUE AMOUNTS AND PROVISIONS**

				SPECIFIC RISK		
SEK million	**Total exposure amount in the lending portfolio**	**Exposure amounts for past due receivables[1)]**	**Exposure amounts for exposures with individual provisions**	**Individual provision**	**Collective provisions with deduction for guarantees**	**Total exposure amount in the lending portfolio after deduction for provisions**
Greater Stockholm	167,120	234	120	41	68	167,011
Greater Gothenburg	25,287	35	17	15	10	25,262
Öresund region	55,142	136	17	11	24	55,107
University and growth regions	27,776	44	2	1	9	27,766
Weak regions	4,307	16	14	12	6	4,289
Other regions	17,660	28	1	1	16	17,643
Total	**297,292**	**493**	**171**	**81**	**133**	**297,078**

1) For past due receivables, amounts past-due by five days or less are not taken into consideration to ensure that the analysis is not distorted by payments delayed because the payment date is a holiday.

TABLE 23. **EXPOSURES WITH PAST DUE AMOUNTS AND PROVISIONS PER EXPOSURE CLASS**

				SPECIFIC RISK		
SEK million	**Total exposure amount in the lending portfolio**	**Exposure amounts for past due receivables[1)]**	**Exposure amounts for exposures with individual provisions**	**Individual provision**	**Collective provisions with deduction for guarantees**	**Total exposure amount in the lending portfolio after deduction for provisions**
Credit risk recognised in accordance with IRB approach						
Exposure to corporates	32,241	–	30	18	1	32,222
Retail exposures	260,783	472	136	58	122	260,603
of which, Single-family dwellings and holiday homes	*115,433*	*300*	*19*	*6*	*61*	*115,366*
of which, tenant-owner rights	*95,890*	*153*	*90*	*27*	*53*	*95,810*
of which, tenant-owner associations	*49,460*	*19*	*27*	*25*	*8*	*49,427*
Total exposure recognised in accordance with IRB approach	**293,024**	**472**	**166**	**76**	**123**	**292,825**
Credit risk recognised in accordance with standardised approach						
Exposures to central governments and central banks	144	1	–	–	–	144
Exposures to regional governments or local authorities	1,512	1	–	–	–	1,512
Exposure to corporates	–	–	–	–	–	–
Retail exposures	2,600	14	–	–	9	2,591
Defaulted exposures	12	5	5	5	1	6
Total exposures recognised in accordance with standardised approach	**4,268**	**21**	**5**	**5**	**10**	**4,253**
Total	**297,292**	**493**	**171**	**81**	**133**	**297,078**

1) For past due receivables, amounts past-due by five days or less are not taken into consideration to ensure that the analysis is not distorted by payments delayed because the payment date is a holiday.

9.11 Reconciliation of change in specific credit risk adjustments for loans with provisions

SBAB only has specific credit risk adjustments and no general credit risk adjustments. These emanate from the individual and collective provisions.

TABLE 24. **CHANGE IN PROVISION FOR PROBABLE LOAN LOSSES**

SEK million	Individual provision for individually measured receivables	Individual provision for collectively measured receivables	Collective provision
Provision at the beginning of the year	–21	–15	–206
Individual provision for the year	–22	–24	–
Reversed from previous provisions	–	–	–
Individual provision utilised for confirmed losses	–	1	–
Allocation to/redemption of collective provisions	–	–	34
Provision at the end of the year	–43	–38	–172

9.12 Exposures per risk class in the PD dimension

The quality of the portfolio is favourable. A total of 99 percent of corporate exposures and 92 percent of retail exposures in the balance sheet derive from the four best risk classes (up to C4) (corporate exposures) and up to R4 (retail exposures).

FIGURE 12. **IRB CORPORATE – EXPOSURE BY RISK CLASS**

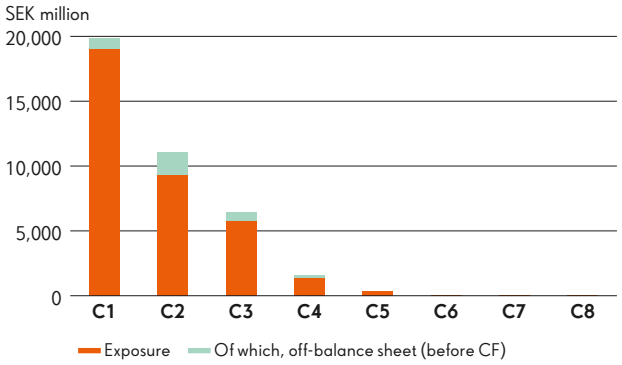


FIGURE 13. **IRB HOUSEHOLD – EXPOSURE BY RISK CLASS**

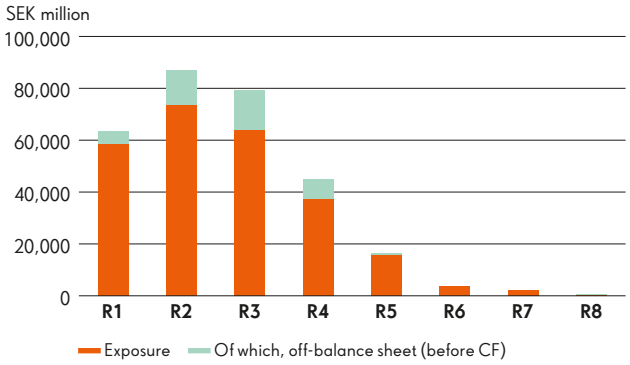


FIGURE 14. **IRB HOUSEHOLD – TENANT-OWNER RIGHTS – EXPOSURE BY RISK CLASS**

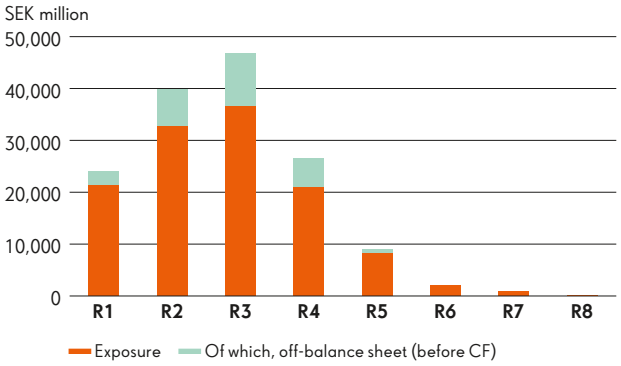


FIGURE 15. **IRB HOUSEHOLD – SINGLE-FAMILY DWELLINGS/ HOLIDAY HOMES – EXPOSURE BY RISK CLASS**

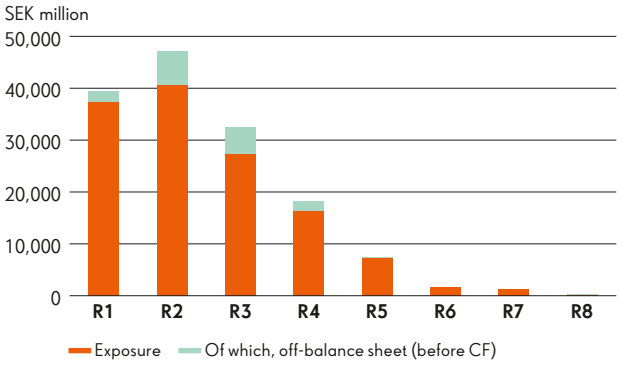
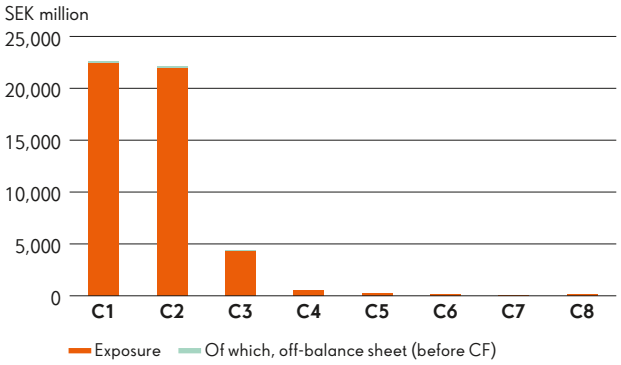


FIGURE 16. **IRB TENANT-OWNER ASSOCIATIONS – EXPOSURE BY RISK CLASS**



9.13 Realised outcome in the PD and LGD dimensions

Table 25 shows the PD and LGD estimate as of 31 December 2014 and the outcome for 2015. The estimated outcome for the retail exposures is somewhat above the actual outcome, which indicates that, in the prevailing economic conditions, the PD models overestimate the risk of default. The estimated outcome for corporate exposures is also somewhat above the actual outcome. However, as there are so few outcomes, it is not possible to draw any conclusions based on the result. The exposure-weighted amount for LGD is controlled by the above-mentioned limitation rule, which entails that the lowest total level for LGD is 10 percent for exposures covered by the advanced IRB approach and where collateral comprises a unit in tenant-owner associations, a mortgage in a residential property or the site leasehold on such a property.

TABLE 25. **REALISED OUTCOME IN THE PD AND LGD DIMENSIONS**

Exposure class	PD estimates	Realised outcome[1)]	LGD estimates	Realised outcome[2)]
Exposure to corporates	0.5%	0.2%		
Retail exposures	0.7%	0.3%	10%[3)]	1.1%[3)]

[1)] An exposure is considered to be in default if the claim is more than 60 days past due or if the assessment has been made that the customer will probably not pay the agreed interest or amortisation.
[2)] Realised outcome has been calculated on loans in default where the default was concluded during the year.
[3)] The results are exposure-weighted.

9.14 Comparison of expected loss and outcome

During the comparison period, it can be seen that the expected loss (EL), in accordance with the internal rating, decreased for both corporate and retail exposures. For corporate exposures, the difference is explained mainly by lower volumes. For retail exposures, EL has fallen slightly, partly due to reduced risk for retail exposures. The relatively small confirmed losses emerging during the year were due, in part, to lenders not managing their interest payments and amortisations and, in part, because the value of pledged collateral was less than the value of SBAB's receivables.

TABLE 26. **COMPARISON OF EXPECTED LOSS BETWEEN OUTCOME AND MODEL, AND PROVISION FOR LOANS REPORTED ACCORDING TO IRB[1)]**

Exposure class, SEK million	EL, IRB/IRB basic 31 Dec 2014	EL, IRB/IRB basic 31 Dec 2013	EL, IRB/IRB advanced 31 Dec 2014	EL, IRB/IRB advanced 31 Dec 2013	Realised outcome2015	Realised outcome 2014	Total provisions, including guarantees 31 Dec 2015	Total provisions, including guarantees 31 Dec 2014
Exposure to corporates	44	62	–	–	–	–	19	24
Retail exposures	–	–	215	237	13	27	179	154
of which, Single-family dwellings and holiday homes	–	–	*113*	*129*	*9*	*23*	*179*	*79*
of which, tenant-owner rights	–	–	*69*	*78*	*3*	*4*	*80*	*64*
of which, tenant-owner associations	–	–	*33*	*30*	*1*	–	*32*	*11*
Total	**44**	**62**	**215**	**237**	**13**	**27**	**198**	**178**

[1)] Expected loss (EL) has been calculated for the loan receivables that existed at the end of 2013 and 2014, respectively.
In Table 18, the expected loss is compared with the actual outcome for confirmed loan losses during the outcome years of 2014 and 2015, respectively.

10 FINANCING

SBAB is primarily financed through funding in the capital and money markets. Since 2007 and increasingly, funding also comes from deposits from the public. Funding takes place, in part, through the Parent Company SBAB Bank AB (publ) and, in part, through SCBC, with funding in SCBC occurring through the issuance of covered bonds. SBAB use Swedish and international funding programmes, mainly in public markets but occasionally supplemented by private placements. Funding is mainly targeted at major institutional investors. International funding is primarily aimed at European investors, but SBAB also attracts investors in the US, Japan and other parts of Asia, highlighting a well diversified investor base.

10.1 Medium and long term funding

Senior unsecured funding

SBAB has a regular programme for medium and long term funding, the Euro Medium Term Note Programme (EMTN programme), which is used both for Swedish and international funding. The EMTN programme has a framework limit of EUR 13 billion. The programme grants investors the right to demand premature repayment of a bond should the Swedish Government no longer have the right to exercise at least 51 percent of the voting rights for the shares in the company. This right is subject to the condition that the Swedish Government has not previously guaranteed SBAB's obligations under the bonds, in which case the right to premature repayment expires. In all other cases, the terms of the EMTN programme match market practice for similar programmes and entitle investors to premature repayment of the bonds if, for example, SBAB fails to pay the interest or capital amount on time, breaks other terms of the programme (with consideration given to certain healing periods) or if SBAB is placed in bankruptcy or liquidation. Under the EMTN programme, SBAB can choose between various types of interest rate structures, including floating and fixed rates, and issue bonds in several currencies and denominations. Under the EMTN programme, SBAB can issue both non subordinated and dated subordinated debt, which may qualify as Tier 2 capital on approval by Finansinspektionen (Swedish financial supervisory authority).

Based on the EMTN programme, SBAB has also drawn up a stand alone prospectus under which perpetual subordinated debt intended to qualify as additional Tier 1 instruments has been issued. SBAB has a Japanese Shelf Registration in place, under which SBAB has the potential to issue bonds on the Japanese market. Like the EMTN programme, the bondholder is entitled to premature repayment of a bond if the Swedish Government ceases to exercise at least 51 percent of the voting rights for shares in the company. This right is subject to the condition that the Swedish government has not previously guaranteed SBAB's obligations under the bonds, in which case the right to premature repayment expires.

10.1.1 Secured funding

The subsidiary SCBC has three funding programmes for issuing covered bonds: a Swedish covered bond programme with no fixed limit, an international Euro Medium Term Covered Note Programme (EMTCN programme) with a limit of EUR 10 billion and an Australian Covered Bond Issuance Programme with a limit of AUD 4 billion. The terms of these programmes for the issuance of covered bonds are in line with market practice for similar programmes and entail, for example, that investors are not entitled to premature repayment of the bonds. The terms also stipulate that SCBC can choose between various types of interest rate structures, including floating and fixed rates, and issue bonds through these three programmes in several currencies and denominations. The EMTCN programme also allows SCBC to issue bonds with a soft bullet structure, which, where appropriate, entitles the issuer to postpone the maturity of the bond according to the issuer's terms.

10.2 Short term funding SBAB manages its short term funding primarily through two commercial paper programmes:

- A Swedish commercial paper programme with a limit of SEK 25 billion;
- A European commercial paper programme with a limit of EUR 3 billion.

The terms of these commercial paper programmes match market practice for similar programmes and include limited opportunities for an investor to demand premature repayment. SBAB may issue commercial papers in the international market in a variety of currencies through the European programmes, while the Swedish programme is mainly used for SEK. The commercial papers mainly comprises "discount paper," meaning that it does not have floating or fixed coupon rates, but is issued in an amount that is more/less than the nominal amount, and when it falls due, the nominal amount is repaid.

10.3 Encumbered and unencumbered assets

As a part of SBAB's operations, residential mortgages are transferred to the subsidiary SCBC. These residential mortgages can include credits pledged against mortgages in real estate intended for residential purposes, against tenant owner rights or credits that otherwise qualify for inclusion in the cover pool of covered bonds. SBAB's receivable relating to the residential

mortgages that have been transferred to and purchased by SCBC may be repaid (wholly or in part) to SBAB at the same time as covered bonds are issued by SCBC. SBAB's receivable relating to these transfers and other receivables (unless they have arisen as a result of a derivative contract connected to the cover pool) are subordinated receivables without priority in case SCBC is declared bankrupt or liquidated.
The structural image in Figure 17 gives an overview of the transactions that may occur between SCBC and SBAB in connection with the issuance of covered bonds and related derivative contracts.

Derivative contracts may be used to ensure a good balance regarding currencies, interest rates and fixed interest periods in the cover pool. By entering into interest rate swap contracts with SBAB or external counterparties regarding the assets registered in the cover pool, SCBC has the ability to convert interest payments received by SCBC in SEK regarding certain assets that are registered in the cover pool to variable payments connected to 3 month STIBOR. In the same manner, SCBC may enter into currency swap contracts to hedge currency risks arising from funding in foreign currencies or potential assets in foreign currencies that are registered in the cover pool.

The companies in the SBAB Group also have the possibility of entering into derivatives transactions that do not need to be recorded in the cover pool. Derivative contracts may be entered between the companies in the SBAB Group or with external counterparties. For all counterparties documentation exists in the form of ISDA Master Agreements. In most cases, an agreement is supplemented by a Credit Support Annex (CSA). The Parent Company and SCBC may also enter repo transactions with certain counterparties, these transactions are governed through so called Global Master Repurchase Agreements (GMRA). The collateral transferred between counterparties under CSA and GMRA agreements is, in all instances, in the form of cash.

As of 31 December 2015, assets in the cover pool consisted mainly of loans to the public in the form of loans against mortgage of immovable property intended for residential or against pledged tenant owner rights. The cover pool may also include substitute collateral, and it is consequently possible to include derivatives or securities in the cover pool.

FIGURE 17. **MORTGAGE STRUCTURE BETWEEN DIFFERENT GROUP COMPANIES**

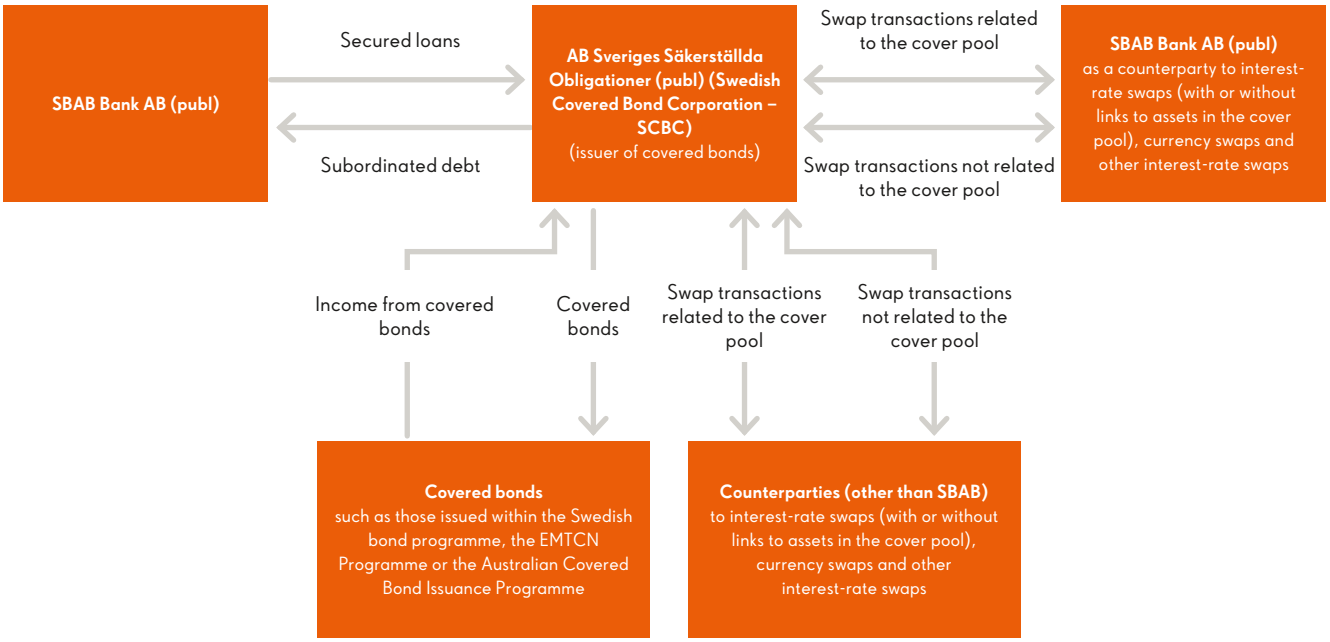
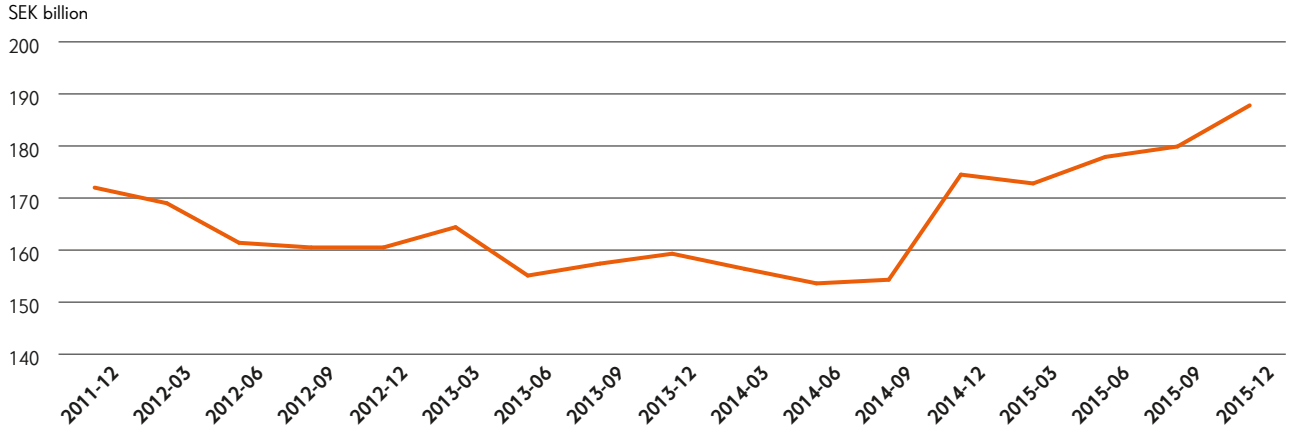


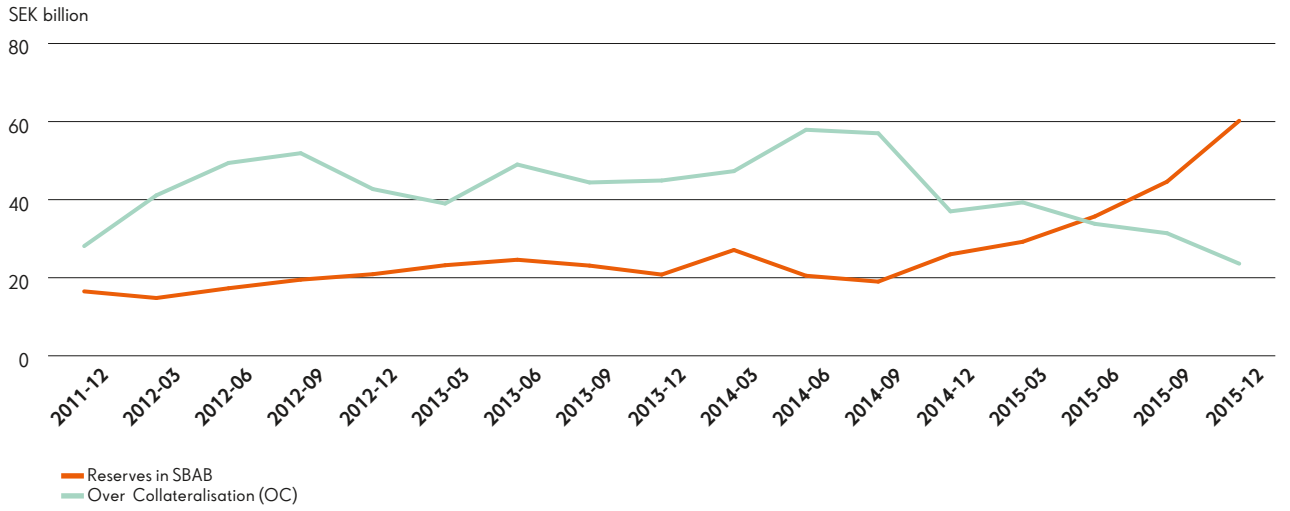
FIGURE 18. **VOLUME MORTGAGED ASSETS 2011–2015**



According to the Covered Bonds (Issuance) Act (2003:1223), the value of the assets in the cover pool shall always exceed the value of bonds issued with the mortgaged assets as collateral (referred to as over collateralisation, "OC"). The unutilised scope in the last four year period is described in Figure 19, "Unutilised scope 2012–2015". As of 31 December 2015, SCBC had set as a minimum requirement that the OC level should meet 6 percent, which is the level required by Moody's to maintain the Aaa rating. As of 31 December 2015, this level equals a volume of SEK 11.1 billion, corresponding to 28.8 percent of the unencumbered assets in SCBC and 5.8 percent of the unencumbered assets in the SBAB Group.

As of 31 December 2015, SBAB had assets (reserves) corresponding to SEK 60.2 billion that may constitute covered assets in SCBC. Reserves in SBAB over the past four year period are shown in Figure 19, "Reserves in SBAB 2012–2015".

FIGURE 19. **OVER COLLATERALISATION AND RESERVES IN SBAB 2011–2015**



Of the assets included in Table 27, "Information on mortgaged asset" below under "Unencumbered assets", with the amount recognised in the item "Other assets", SBAB has reported any items that are not available for mortgaging or other security arrangements in the regular operations. Such assets include deferred tax assets, property, plant and equipment, intangible fixed assets and certain other assets that are not mortgaged, pledged as collateral or used as security in the regular operations.

TABLE 27. **MORTGAGED ASSETS**

Assets, SEK million	Mortgaged assets, book value	Mortgaged assets, fair value	Unencumbered assets, book value	Unencumbered assets, fair value
Assets of the reporting institution	184,824		154,161	
Equity instruments	–	–	–	–
Interest bearing securities	–	–	64,027	64,021
Other assets	184,824		90,135	

TABLE 28. **COLLATERAL RECEIVED**

SEK million	Mortgaged collateral received or own interest bearing securities in issue, fair value	Mortgaged collateral or own interest bearing securities in issue that can be mortgaged, fair value
Collateral received by the reporting institution	3,266	1,535
Equity instruments	–	–
Interest bearing securities	1,535	1,535
Other security received	1,731	–
Own interest bearing securities in issue, except own covered bonds or asset backed securities	**–**	**–**

TABLE 29. **MORTGAGED ASSETS/COLLATERAL RECEIVED AND ENSUING DEBT**

SEK million	Matching debt, contingent liabilities and securities lent	Mortgaged assets, collateral received and own interest bearing securities in issue except covered bonds and asset backed securities
Certain financial liabilities, book value	184,824	184,824

10.4 Funding strategy

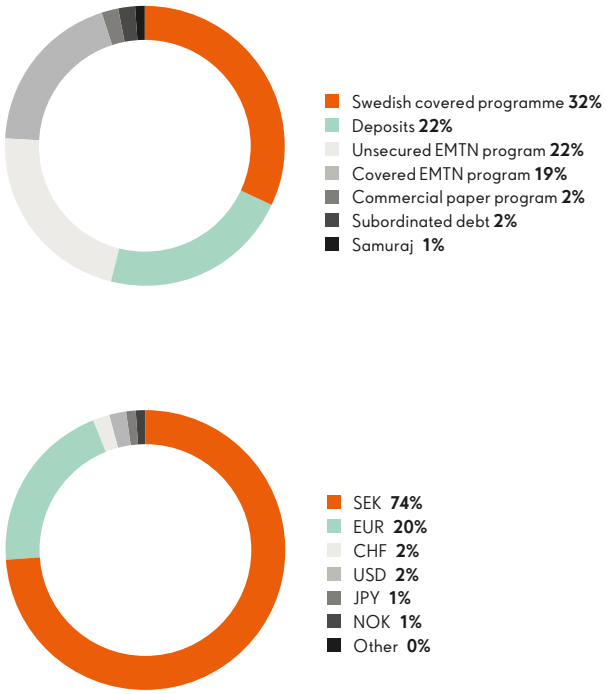
The size of the funding portfolio is adjusted based on the volume of the outstanding loans and the composition of the assets, taking into consideration such factors as liquidity risk and based on the company's risk appetite. Funding is also continuously adapted to meet the new liquidity rules included in Basel III and the requirements imposed by rating agencies and investors. Funding must be well diversified. The portfolio must have an effective distribution between secured and unsecured funding and strive for an even distributions of debt maturity dates, i.e. avoiding periods with large concentrations of maturities. The funding portfolio must also comprise funding in several currencies with a balanced and diversified investor base. Since the company's lending is conducted exclusively in SEK, consequently the majority of the funding is allocated against SEK. The second largest currency for funding is EUR. The Group has been a regular issuer in the EUR market for many years. Funding is to take place through several leading banks and through public transactions and private placements. Interest rate risk and currency risk associated with funding are managed through the use of derivatives, primarily interest rate swaps and currency swaps.

SBAB's lending is funded mainly by deposits from the public and through the financial capital markets in the form of commercial papers and bonds. Long term funding is mainly achieved through covered bonds.

Short term funding under SBAB's commercial paper programme must be adjusted to market conditions and needs, but always constitute at most a limited share of the total funding portfolio. SBAB's loan assets should be used effectively by acting as collateral in case of secured funding. The funding mix between SCBC and the Parent Company must be well balanced, taking into account the companies' risk appetite, ratings and total long term funding cost.

SBAB and SCBC must have an active market presence, with favourable and frequent relations with investors in each investor segment.

FIGURE 20. **FUNDING SOURCES AND DISTRIBUTION BY CURRENCY FOR DEPOSITS AND FUNDING**



11 CREDIT RISK IN TREASURY

In Treasury, credit risk arises, in part, in the form of counterparty credit risks for the derivative contracts entered into by SBAB to manage its financial risks and, in part, as a result of investments in the liquidity portfolio and investment of surplus liquidity

In accordance with the credit directive adopted by the Board of Directors, the credit risk limit is established by SBAB's Credit Committee for all counterparties in treasury operations (meaning debtors and financial counterparties), with the exception of the Swedish government and companies included in the SBAB Group, for which no limits are placed on exposure. The exposure amount for the counterparty credit risk is generally calculated on the basis of market value and observes the standard set in the Bank's agreements on netting of derivative contracts.

The credit risk limit may be established for a period of no longer than one year, following which a new assessment must be conducted. Decisions on the credit risk limit that are taken by the Credit Committee must be reported to the Parent Company's Board of Directors at the following Board meeting.

11.1 Counterparty credit risk

Counterparty credit risk is the risk that SBAB's financial counterparties cannot meet their commitments to the completed derivatives and repo agreements, and such risk consists primarily of exposures to major banks. Exposure is primarily covered through collateral agreements in which the counterparty provides collateral in an effort to reduce exposure.

To limit the potential counterparty credit risk associated with derivative transactions involving non standardised derivative instruments that are not cleared by clearing organisations approved by the competent authority (in accordance with Regulation (EU) No 648/2012), a framework agreement must have been concluded with the counterparty. This ISDA Master Agreement, or similar agreements, has in most cases been supplemented with associated collateral agreements, known as Credit Support Annexes (CSAs). The ISDA Master Agreement entails, inter alia, that netting is regulated in the event of bankruptcy. A CSA means that the parties have agreed in advance to transfer collateral if the exposure exceeds a certain "threshold amount". The threshold amount and the minimum amount to be transferred to or from the counterparty can vary depending on the parties' ratings. Tables 30 and 31 provide an overview of the distribution of the market value of individual derivative instrument transactions by rating and maturities.

To limit the counterparty credit risk associated with repo transactions, GMRAs (Global Master Repurchase Agreements) are used. These agreements control aspects such as the transfer of collateral to or from the counterparty.

Reconciliation with the counterparty are to be conducted daily or weekly with each derivatives counterparty with whom a collateral agreement has been signed, and collateral is moved over to even out exposure. Wherever applicable, the posted and received collateral takes the form of cash under a transfer of title, which entitles the party that receives the collateral to use it in its operations. In certain cases, the threshold amount and the minimum transfer amount are regulated by agreements concluded by the Parent Company and SCBC regarding the parties' rating; the worse the rating held by a party, the lower are these amounts. A decline in SBAB's rating would, as of 31 December 2015, not result in the need for extra collateral to any external counterparty[1)].

11.2 Credit quality in the liquidity portfolio

The SBAB Group's liquidity portfolio primarily comprises liquid, interest bearing securities with a high rating and is intended to reduce the Group's liquidity risk. Holdings in securities are limited by asset class and by country, respectively, and have the highest possible rating upon acquisition. Moreover, the securities holder is an integral part of the overall credit risk utilisation for each issuer.

Covered bond holdings are risk weighted in relation to their credit quality step according to CRR. As at 31 December 2015, all of SBAB's covered bond holdings were assigned credit quality step one, which means a risk weight of 10 percent. The holdings in the portfolio are long term and at 31 December 2015, the market value amounted to SEK 64.8 billion with an average maturity of 2.7 years. At the same date, 95 percent of the portfolio's value had a rating of Aaa from Moody's or AAA from Standard & Poor's. The various asset classes in the portfolio are securities issued by or guaranteed by central governments, securities issued by supranational agencies, securities issued by public sector entities and European covered bonds. Liquidity portfolio holdings are either classified as "Held for trading" (HFT), "Available for sale assets" (AFS) or "Hold to maturity" (HTM).

Securities measured at fair value through profit or loss:

- Securities issued by central governments, SEK 10.3 billion;
- Securities guaranteed by central governments, SEK 2.9 billion;
- Securities issued by supranational and sovereign agencies (SSAs), SEK 1.6 billion
- Securities issued by public sector entities, SEK 3.0 billion;
- European covered bonds, SEK 8.9 billion.

[1)] In case of a decline in SBAB's rating, the Parent Company would need to provide collateral of SEK 1.62 billion to SCBC.

Available for sale assets:

- Securities issued by central governments, SEK 4.2 billion;
- Securities issued by supranational and sovereign agencies (SSAs), SEK 0.2 billion
- Securities issued by public sector entities, SEK 0.5 billion;
- European covered bonds, SEK 23.8 billion.

Investments held to maturity:

- Securities issued by supranational and sovereign agencies (SSAs), SEK 0.1 billion
- Securities issued by public sector entities, SEK 3.5 billion;
- European covered bonds, SEK 5.8 billion.

All securities are recognised above at their market value, regardless of how they have been classified in the accounts. Credit risk assessment is conducted on the basis of assessed future cash flows and the market value of the collateral.

TABLE 30. **DERIVATIVE INSTRUMENTS FOR THE SBAB GROUP**

SEK million	Total nominal value	Positive market values	Negative market values
< 1 year, interest rate related	58,709	651	–392
> 1 year, interest rate related	172,531	3,746	–1,809
< 1 year, currency related	36,134	1,426	–1,457
> 1 year, currency related	54,672	1,369	–1,536
Total	**322,047**	**7,192**	**–5,194**

TABLE 31. **DERIVATIVE INSTRUMENTS DISTRIBUTED BY RATING FOR THE SBAB GROUP**

SEK million	Net market value	Positive market values	Negative market values
AA–	284	1,912	–1,628
A+	904	1,387	–483
A	562	2,182	–1,619
A–	175	189	–14
BBB+	822	1,342	–520
BBB	–650	20	–670
BBB–	–99	160	–260
Total	**1,998**	**7,193**	**–5,194**
Collateral			**2,176**
Nettings gains			**4,587**

TABLE 32. **DERIVATIVE INSTRUMENTS FOR THE SBAB GROUP**

SEK million	
Positive gross market value of contracts	7,192
– Nettings gains	–3,035
= Current offset credit exposure	4,157
– Collateral held	–3,683
= Net credit exposure to derivatives	474

12 MARKET RISK

Market risk is the risk of loss or reduced future income due to market fluctuations.

SBAB is characterised by low risk taking, with the Board determining the overall risk appetite and setting the limits for the risk measure Value at Risk (VaR). In addition to VaR, a number of supplementary risk based measurements set by the CEO of SBAB are also subject to limitation. Through daily reports, Risk Control checks compliance with current risk levels and limits. Market risk is followed up on the Group level as well as broken down to lower levels.

The general principle governing SBAB's exposure to market risk is that the level of risk taking should be low. Interest rate risk shall as a general principle be limited through direct funding or the use of derivatives. Currency risks are mitigated as funding in international currency must be hedged through currency swap contracts or invested in matching currencies.

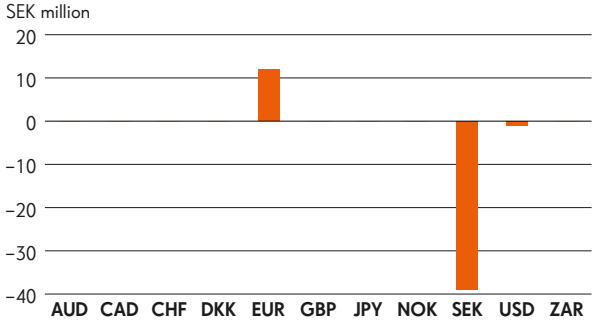
During 2015, SBAB reviewed its risk limits. As part of this review, the credit spread risk was reallocated from the earnings volatility framework to the market risk framework, and is therefore included in SBAB's VaR calculation of market risk. The reallocation does not affect SBAB's total risk attributable to market risk and earnings volatility.

12.1 Value at Risk

VaR is a comprehensive portfolio measurement expressing the potential loss that could occur given a certain level of probability and holding period. SBAB's model is a so called historical model and applies percentiles in historic market data from the past two years.

Limits for the day to day follow up of VaR are set at three levels: the market risk of SBAB, all market risks which Treasury is responsible for managing and the Trading portfolio. The limit for the market risk of the whole SBAB is based on the VaR measure included in the model for Economic Capital and applies a probability level of 99.97 percent and a holding period of one year, while the other two measures apply a probability level of 99 percent and a holding period of one day.

FIGURE 21. **INTEREST RATE RISK BY CURRENCY IN THE EVENT OF A PARALLEL SHIFT IN THE YIELD CURVE BY +1 PERCENTAGE POINT**



The interest rate risk totalled SEK –28.7 million as per 31 December 2015.

As of 31 December 2015, the exposure to the market risk of the whole SBAB was SEK 1,154 million (608), compared with the SEK 1,850 million (1,350) limit set by the Board of Directors. Exposure to market risks that Treasury is responsible for managing was SEK 36 million (7) compared with the limit of SEK 55 million (30). Exposure in the Trading portfolio was SEK 1.6 million (0) compared with the limit of SEK 12 million (12).

12.2 Supplementary risk measures

In addition to the overall VaR limits determined by the Board, the CEO has set a number of supplementary risk measurements for market risks to which SBAB is exposed. For interest rate risk, there are limits for parallel shifts, where the effect on the present value at a one percentage point shift in the yield curve by is measured, and curve risk, where the effect on the present value is measured in different scenarios, in which he short end of the yield curve is adjusted down (up) and the long end is adjusted up (down). Currency risk is controlled by measuring the effect of present value when currency exchange rates change and in the liquidity portfolio by controlling the matching of the principal in each currency. There are also limits for basis swap risk and earnings volatility from basis spreads.

Earnings volatility from basis spreads arise because the derivatives used to hedge funding are recognised at fair value while the underlying funding is reported as book value, in accordance with the accounting standards applied by SBAB. This causes effects to arise in operating profit/loss that do not correspond to the actual risk to which SBAB's portfolio is exposed to. The earnings volatility from basis spreads is expected to decrease in the future, as SBAB has applied hedge accounting through cash flow hedges since 2014, which means that earnings volatility will only be calculated for swap contracts that are not subject to cash flow hedges.

12.3 Interest-rate risk in other operations

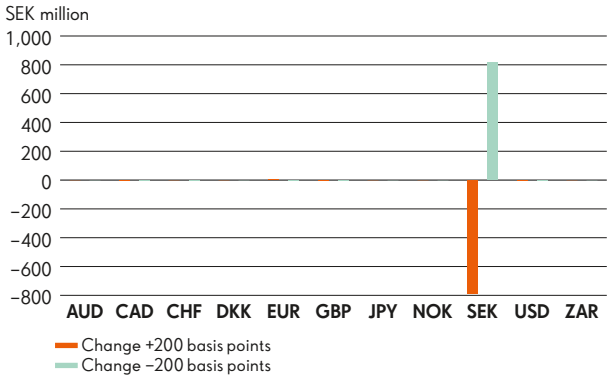
Interest rate risk in the banking book is measured and reported to the Swedish Financial Supervisory Authority in accordance with FFFS 2007:4.For the calculation of interest rate risk in other operations, a maturity of one day is assumed for funding that is not time limited. As per 31 December 2015, the effect on the present value was SEK –785 million (–803) at a parallel upward shift by 2 percentage points and SEK 809 million (841) at a parallel downward shift by 2 percentage points. The exposure distributed by currency is presented in Figure 22.

12.4 Risks in the Trading book

The Trading book consists of investments in SBAB's trading portfolio and the part of the liquidity portfolio that is classified as "held for trading". The liquidity portfolio is subject to a minimised interest rate risk. The risk in the liquidity portfolio primarily derives from credit risk. The trading portfolio gives SBAB a limited mandate to accept market risk by taking its own positions in the market. As of 31 December 2015, there was one open position in the trading portfolio.

Within SBAB, interest rate, currency, credit and liquidity risk in the trading book are managed as an integral part of the balance sheet together with the other operations. Credit risks in the form of issuer and counterparty risks in the trading book are governed by credit risk limits set by SBAB's Credit Committee.

FIGURE 22. **INTEREST RATE RISK IN OTHER OPERATIONS IN THE EVENT OF A PARALLEL SHIFT IN THE YIELD CURVE BY +–2 PERCENTAGE POINTS**



13 LIQUIDITY RISK

Liquidity risk is defined as the risk that SBAB will not be able to meet its payment obligations in conjunction with due dates without the related cost increasing significantly.

13.1 Liquidity strategy and liquidity risk management

The overall purpose of SBAB's liquidity strategy is to ensure SBAB's survival in terms of liquidity and that the company can effectively meet its payment obligations. Key features of the strategy are a proactive and continuous liquidity planning, active debt management and the size, content and management of SBAB's liquidity reserve. SBAB has long identified and allowed for the importance of well-functioning and proactive liquidity risk management. SBAB's liquidity risk management is described below.

Broad and diversified funding

Because SBAB has maintained an active presence in the international capital market since 1989, its brand is well established. Short-term, mid-term and long-term funding takes place on a global basis. Moreover, the SBAB Group has access to the covered bond market, both in Sweden and internationally, through SCBC.

Liquidity reserve

To ensure access to funds in times when the normal sources of funding do not function, SBAB has a liquidity portfolio. In calculating the reserve value of the securities in the liquidity portfolio, SBAB applies the valuation haircuts established by the Riksbank, in accordance with the Riksbank's Guidelines for Collateral Management in the Riksbank's regulatory framework for RIX and monetary policy instruments. The reserve value of the liquidity portfolio is referred to as the liquidity reserve. The portfolio comprises liquid securities with high ratings, with assets eligible for repos with the Riksbank or the European Central Bank (ECB) accounting for 100 percent of the portfolio value.

On 31 December 2015, SEK 62.1 billion of SBAB's liquidity reserve (reserve value at the Riksbank) comprised liquid securities. Moreover, unutilised capacity for the issuance of covered bonds constitutes a very liquid reserve.

SBAB publishes its liquidity reserve quarterly on the SBAB website, sbab.se, in accordance with FFFS 2010:7.

Liquid balance sheet

SBAB's assets consist primarily of lending against collateral in property and tenant-owner rights. SCBC was established in 2006 for the purpose of issuing covered bonds, which has also resulted in increased liquidity in SBAB's balance sheet.

SBAB's liquidity portfolio primarily comprises liquid, fixed income securities with a high rating and it is an integral part of the Group's liquidity risk management. Holdings in securities are limited by asset class and by country, respectively, and must have the highest rating upon acquisition. In addition to these collective limits, limits for individual issuers may also be set.

Continuous monitoring of liquidity risk

Active debt management, the liquidity of the balance sheet and the size of SBAB's liquidity reserves are key factors in SBAB's liquidity risk management. By viewing funding activities as a natural feature both of operations and strategic planning of liquidity risk, concentrations of excessively large funding maturities are avoided. Another important part of the ongoing liquidity risk management is the continuous monitoring and testing of the practical liquidity value of the liquidity portfolio in the secondary market.

Contingency plan

SBAB has a contingency plan for the management of liquidity crises. The contingency plan contains a clear delegation of responsibility for the personnel concerned, as well as instructions as to how the company can rectify potential liquidity deficits. The plan stipulates suitable actions to handle the implications of various types of crisis scenarios and contains definitions of events that cause and escalate the contingency plan. The contingency plan must be regularly tested and updated based, for example, on the results of stress tests.

13.2 Liquidity risk measurements – short-term liquidity risk

Since 1 January 2013, SBAB is subject to the Swedish Financial Supervisory Authority's Liquidity Coverage Ratio (LCR) requirements as defined in FFFS 2012:6. The Liquidity Coverage Ratio measures the amount of assets that can be converted to cash in relation to a stressed liquidity need during 30 days. The regulations stipulate that the institutions covered by them must, at every point in time, have a Liquidity Coverage Ratio amounting to at least 100 percent, both at the total level and for EUR and USD isolated.

On 31 December 2015, the liquidity coverage ratio, in accordance with the definition in FFFS 2012:6, was 232 percent at the consolidated level, and 1,544,051 percent and 233 percent, respectively, in EUR and USD. In 2015, SBAB's liquidity coverage ratio never fell below 171 percent.

On 1 October 2015, the European Commission's Delegated Regulation (EU) 2015/61 entered into force. According to the Regulation, all credit institutions shall meet an LCR of at least 60 percent, according to a new definition that differs somewhat from the definition used by the Swedish Financial Supervisory Authority. The requirement will be gradually increased by 10 percentage points per year-end, with the first increase occurring on 1 January 2016, until the requirement reaches 100 percent. Since SBAB is required to comply with the Swedish Financial Supervisory Authority's requirement of 100 percent, the introduction will not have any substantial effect on SBAB. As of 31 December 2015,

the LCR according to the EU's Delegated Regulation amounted to 251 percent at the consolidated level. Since this measure was introduced on 1 October 2015, it has never fallen below 211 percent.

Internally within the SBAB Group, the liquidity risk is measured and stress tested by totalling the maximum conceivable need for liquidity for every day in the coming period. This liquidity risk measure is referred to as the survival horizon. The calculations are based on a crisis scenario in which all loans are assumed to be extended on maturity, meaning that no liquidity is added through loan redemption, and where no funding is available. Deposits from the public are treated with a conservative assumption, whereby withdrawals from the portfolio are distributed over time on the basis of historical balance volatility. Accordingly, the maximum need for liquidity can be identified for every given future period, and the necessary liquidity reserve can be established. The survival horizon corresponds to the number of days for which the liquidity reserve covers the maximum outflow and, since 30 June 2015, it has been limited to a minimum of 180 days at any given time.

On 31 December 2015, the Group's survival horizon amounted to 265 days (234). In 2015, the survival horizon was never less than 189 days (105).

In addition to these measurements, the concentration of debt maturities in the next six months are also limited, so that the maximum debt maturity in a 30 day period does not exceed 60 percent of the size of the liquidity reserve.

TABLE 33. **LIQUIDITY COVERAGE RATIO**

SEK million	**Total**	**EUR**	**USD**
Liquidity coverage ratio	232%	1,544,051%	233%
Liquid assets	**59,285**	**12,213**	**3,723**
Assets weighted 100%	26,779	7,715	2,493
Assets weighted 85%	32,507	4,498	1,230
Cash outflows	**21,508**	**3**	**4,265**
Deposits from the public	11,285	0	0
Market funding	7,581	0	4,264
Other outflows	2,642	3	1
Cash inflows	**2,273**	**1,587**	**2,665**
Inflows from lending to the public	1,821	0	0
Other inflows	452	1,587	2,665

Liquidity Coverage Ratio = liquid assets/(cash outflow-cash inflow). The Liquidity Coverage Ratio is recognised according to the definitions and weights in FFFS 2012:6. The calculation takes into consideration that assets with 85 percent weight must not constitute more than 40 percent of the reserve, and that inflows must not exceed 75 percent of the outflow in each column.

13.3 Liquidity risk measurements – structural liquidity risk

Structural liquidity risk is the risk for more costly or shortage of funding opportunities as a result of differences in structure and maturity between lending and funding. SBAB aims to have a diversified funding.

To ensure that the funding is diversified and to limit dependence on capital markets, deposits shall constitute at least 18 percent of the lending. As of 31 December 2015, deposits amounted to 26 percent of the lending.

SBAB measures its structural liquidity risk mainly through a maturity-matching measure, which measures the relationship between the maturity of assets and liabilities from a liquidity perspective at various points in the future. This can be viewed as SBAB's internal variety of NSFR (see description below), in which the maturity, in terms of liquidity, on deposits and lending is estimated by means of SBAB's own statistical models, which are based on historical data on the behaviour of SBAB's customers. On 31 December 2015, the measure was 112 percent at the one-year point, compared with the limit of 90 percent. NFSR according to the Basel Committee definition was 115 percent.

In addition to this measure, structural liquidity risk is also measured by monitoring the extent to which SBAB can withstand a decline in house prices without the over colateralization (OC) level in the cover pool falling below the rating companies' requirements for AAA ratings and through the upcoming regulatory measurement NSFR.

13.4 New regulations for liquidity risk

In the wake of the financial crisis, a major international review and extensive efforts were launched to assess the regulations for the management of the liquidity risks of banks and credit institutions. The objective of the new regulations, parts of which are still being formulated, is to increase the resilience of banks to serious disruptions in the capital market and to achieve a more harmonised approach to liquidity risk at the international level. In order to set minimum levels for the liquidity of banks, the new regulations focus on two standard measurements called the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). The aim of NSFR is to indicate how stable the Group's funding is by comparing the maturities of the institutions' assets and liabilities.

In the EU, both measures are included in the new capital adequacy regulations that came into effect on 1 January 2014. The measurements should be reported to the EBA as soon as the regulations come into force, although there are still no quantita-

tive requirements for NSFR. The LCR requirement began to be phased in from 1 October 2015. The EU requirements refer to each company, but SBAB has entered into agreements regarding liquidity support between the Parent Company and SCBC and is therefore exempt from the requirements at the company level.

It is expected that the Basel Committee's definition of NFSR will be implemented in the EU, potentially with some deviations, and it is expected that the quantitative requirements will enter into force in 2018.

The EBA has developed five more measures of liquidity risk that are intended for comparison and supervisory purposes – no quantitative requirements are expected in connection with these. The reporting of these measures to the EBA is expected to start in 2016. The measures in question are:

- A maturity ladder showing maturities of assets and liabilities up to ten years into the future
- Concentration of counterbalancing capacity per issuer/counterparty, showing the bank's holdings of liquid assets or liquidity facilities to meet temporary declines in access to liquidity in the market
- Concentration of financing counterparties and products, showing the counterparties or financing products representing such a large percentage of the financing that losing them would affect the bank materially
- Prices for various financing maturities
- Extension of maturing financing during the reporting period.

13.5 Stress tests for liquidity risk

SBAB has a model for stress testing liquidity aimed at internal requirements for analytical and contingency management of liquidity risk. The stress tests have been designed in line with the Swedish Financial Supervisory Authority's stipulations on liquidity management, which impose general requirements on stress tests (FFFS 2010:7). The developed models analyse SBAB's capacity to meet the need for cash and cash equivalents in various market scenarios and to assess the effect of protracted stress SBAB's ability to finance its operations. The scenarios are designed on the basis of SBAB's specific risk profile and cover both company-specific and market-related scenarios that may render the financing of the operations difficult. The scenarios are divided into different stages that illustrate increasing levels of stress intensity to reflect how a crisis can continuously deteriorate.

The scenarios simulated by the stress tests include:

- The 2008/2009 financial crisis – stress in the funding operations, with funding programmes closing at various stages
- Rating-related stress, with gradually lower ratings for SBAB and SCBC
- Falling property market prices – various levels of falling prices, which increase LTV, thus lowering the share of funding that can be conducted via covered bonds
- Stress of liquidity in the liquidity reserve
- Sizeable fluctuations in interest and currency exchange rates, leading to larger amounts having to be secured through CSAs, which could thus impair liquidity.

The stress tests are under continuous development and the assumptions on which the various scenarios are based are assessed regularly. The stress tests are conducted and reported quarterly, with results assessed against SBAB's established risk appetite and used to adapt strategies and guidelines.

TABLE 34. **LIQUIDITY RESERVE**

		DISTRIBUTION BY CURRENCY			
Liquidity reserve, SEK million	**2015**	**SEK**	**EUR**	**USD**	**Other**
Cash and balances held at central banks	461	461	–	–	–
Balances at other banks	–	–	–	–	–
Securities issued or guaranteed by central governments central banks or multinational development banks	19,345	10,435	7,715	1,195	–
Securities issued or guaranteed by municipalities or non-governmental public sector entities	6,972	5,674	–	1,298	–
Covered bonds issued by others	38,504	31,575	5,292	1,447	190
Own covered bonds	–	–	–	–	–
Securities issued by non-financial companies	–	–	–	–	–
Securities issued by financial companies (excl. covered bonds)	–	–	–	–	–
Other securities	–	–	–	–	–
Total	**65,282**	**48,145**	**13,007**	**3,940**	**190**
Bank and loan facilities	–	–	–	–	–
Total	**65,282**	**48,145**	**13,007**	**3,940**	**190**
Distribution by currency, %		74	20	6	0

14 OPERATIONAL RISK

Operational risk means the risk of losses due to inappropriate or unsuccessful processes, human error, faulty systems or external events. The definition includes legal risk.

14.1 Risk management

Within SBAB, risk management consists of uniform measurement and reporting of operational risk. An analysis of risk levels in all operations is conducted on a regular basis and reported to the Board, the CEO and the Executive Management. The Operational Risk & Security functions within the Credit and Risk departments have overall responsibility for the methods and procedures used for identifying, governing, controlling and reporting on operational risk, including follow-up. The work on identifying and managing operational risk is conducted against a backdrop of SBAB's strict view of risk as well as its focus on cost efficiencies. SBAB strives for developing and improving the methods used for identifying and managing operational risk. This entails constant efforts to improve the bank's risk culture and procedures to manage operational risk and incidents effectively and pro-actively.

14.2 Self-evaluation

The self-evaluation process encompasses the identification of risks in all units, measurement of identified risks and management of material risks. The result of the self-evaluation is reported annually to the Board, the CEO and the Executive Management. The entire business uses a common method for self-evaluation of operational risk, and the method is further used to cover all key processes within the bank.

14.3 Incident management and reporting

SBAB has procedures and systems support intended to facilitate the reporting and follow-up of incidents The Operational Risk & Security function supports the operations in the reporting and analysis, to ensure that root causes are identified and suitable measures are implemented. Even incidents that have not caused direct damage or financial loss are reported, to promote proactive risk management.

14.4 Process for approving changes (GFF)

SBAB has a process for the approval of new or significantly altered products, services, markets, processes and IT-systems as well as major operational and organisational changes in SBAB. The purpose of GFF is the advance identification and management of risk related to change.

14.5 Security and contingency management

At SBAB, security involves protecting customers, individuals, information and physical assets. Information must be kept confidential and be reliable and accurate, and it must be made available to the appropriate people as and when needed. SBAB's security efforts include technical, organisational and administrative measures, and they are based on the international information security standard ISO/IEC 27002:5.

SBAB works in a pre-emptive manner to prevent security incidents that may affect the company's ability to operate. A crisis management organisation is responsible for crisis management and for Executive Management and communication in case of serious incidents, crises or disasters.

14.6 IT governance

The Operational Risk & Security function sets the requirements for the overall IT governance principles at SBAB in accordance with FFFS 2014:5. The overall goal is to create operative processes for measuring, evaluating and adapting IT in order to optimise resources. The purpose is to create value for SBAB, manage IT-related risk and create information to support decision-making and transparency for the Executive Management and the Board regarding IT.

14.7 Capital requirements for operational risks

SBAB uses the standardised approach to assess capital requirements for operational risk. This approach entails that the capital requirement is based on 12–18 percent of the average operating income of the business areas in the past three years. Capital requirements for operational risk are presented in Table 9, Capital requirements and risk exposure amount.

15 BUSINESS RISK

By business risk, SBAB means the risk of declining earnings due to harsher competition, inappropriate strategies or erroneous decisions.

SBAB defines business risk as a necessary risk. New business is usually relatively similar to the business SBAB already has. Changes in the form of new products or new markets may only constitute a small part of SBAB's activities and must be implemented at such a pace that SBAB does not substantially jeopardise its profit level and with great probability avoids pressure on its capital base.

As the accounting standards used by SBAB require that certain components of the portfolio are measured at market value while other components are recognised at their carrying amount, this has effects on the operating profit/loss, and consequently also on own funds, that do not correspond to the actual risk to which the portfolio is exposed. To limit such effects, earnings volatility shall be measured and limited. (See also Section 6.5 Capital requirement due to earnings volatility.)

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SBAB!

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