SBAB Bank AB (publ)

Capital adequacy and risk management 2014

Basel Regulations, Pillar 3

SBAB!

Contents

Glossary

Chapter 1. Introduction

Directive 2013/36/EU of the European Parliament and of the Council on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms – CRD IV | Common European regulations on risk management and capital adequacy.
Regulation (EU) no 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms – CRR | common European regulations on risk management and capital adequacy.

Chapter 3. Consolidated situation

Asset and Liability Committee (ALCO) | Body that prepares matters relating to risk and capital planning, which are then addressed by Executive Management or the Board of Directors.
Internal capital adequacy assessment process (ICAAP) | Process according to Article 73 of CRD IV for calculating the combined capital requirements with consideration for 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 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 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 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 of own funds that the company is permitted to have.
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.
Residential Mortgage-Backed Securities (RMBS) | Securities with collateral in the form of residential mortgage portfolios.
Risk-weighted assets 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%, 20%, 50% and 100% of the nominal amount.
Risk exposure amounts 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 assessment of necessary 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 in accordance with Pillar 2 | This is based on the 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) | Statistic measure of the maximum expected loss at a given level of security and over a defined time period.

Chapter 8. Credit risk in the 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 over a long-term period in a statistic model. 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 expected to be utilised at the time of a possible future default.
Loan to Value (LTV) | Loan to value rate, i.e. the size of a loan in relation to the value of pledged collateral.
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 9. 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.

Chapter 10. Credit risk in the treasury operations

Credit Support Annex (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.
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 12. Liquidity risk

Liquidity Coverage Ratio (LCR) | Liquidity risk measurement that measures the relationship between liquid reserves and a 30-day net outflow in a stressed scenario.
Survival horizon | A measurement of how many days liquidity needs can be met without access to new wholesale funding in a stressed scenario.
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 presents information about capital adequacy and risk management based on CRR/CRD IV and the Swedish Financial Supervisory Authority's Regulatory Code (FFFS 2014:12). This report pertains to conditions prevailing on 31 December 2014, unless otherwise specified. This report and the corresponding but more limited periodic information on capital adequacy and liquidity reserves and tables in accordance with Commission Implementing Regulation (EU) No 1423/2013, as well as information on the remuneration system, are published on SBAB's website, sbab.se.

SBAB is owned by the Swedish state. Its operations, which consist principally of retail residential mortgage lending in Sweden, are characterized by a low level of risk. SBAB is well capitalized and complies with the rules on capital adequacy by a comfortable margin. The Common Equity Tier 1 capital ratio rose to 29.8% in 2014. The loan loss ratio is low (-0.01%) and the net cost for loan losses for the year shows a positive result.

The credit risk in SBAB's operations declined over the year through a reduction in the corporate portfolio and a divestment of all RMBSs. Liquidity risk also decreased as a consequence of extended funding, increased deposits from the public and a larger liquidity portfolio.

In December 2014, the Board of Directors raised the internal limit of the Common Equity Tier 1 capital ratio from 18% to 22%, calculated according to CRR. As of previously, the total capital ratio shall amount to 9.5%, calculated according to the transitional regulations for CRR/CRD IV.

New common regulations on supervisory requirements for credit institutions have been adopted by the EU. They have been applied since 1 January 2014 and are to be fully implemented by 2019. 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 buffers that authorities can use 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 requirements regarding the mortgages to households. By means of a strong capital position and good risk management, SBAB meets the requirements in CRR/CRD IV.

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

- Credit risk – The risk that 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.

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 the lending operations	Wanted risk	Medium	Medium	Low	73%
Credit risk in the treasury operations	Necessary risk	Low	Low	Low	4%
Market risk	Necessary risk	Low	Medium	Low	13%
Operational risk	Unwanted risk	Low	Low	Low	6%
Business risk	Necessary risk	Low	Low	Low	4%
Liquidity risk	Necessary risk	Low	Medium	Low	234 days[1)]

[1)] Survival horizon

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 own funds.

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 (SCBC) issues covered bonds in the Swedish and international capital markets.

Table 2. Companies included in the consolidated situation

Company	Corporate identity number	Ownership share	Consolidation method used in the accounts	Consolidation method 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 customers the opportunity to open 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.

In the light of the Board of Directors' decision to discontinue the investment in extended banking operations, a resolution was passed to wind up the sales of fund units that had begun in 2013.

Figure 1. Simplified balance sheet for SBAB

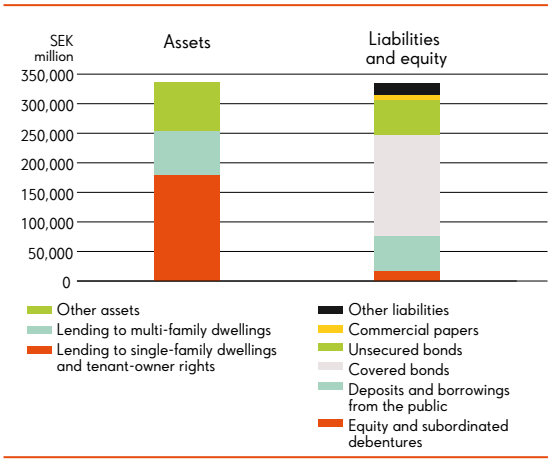
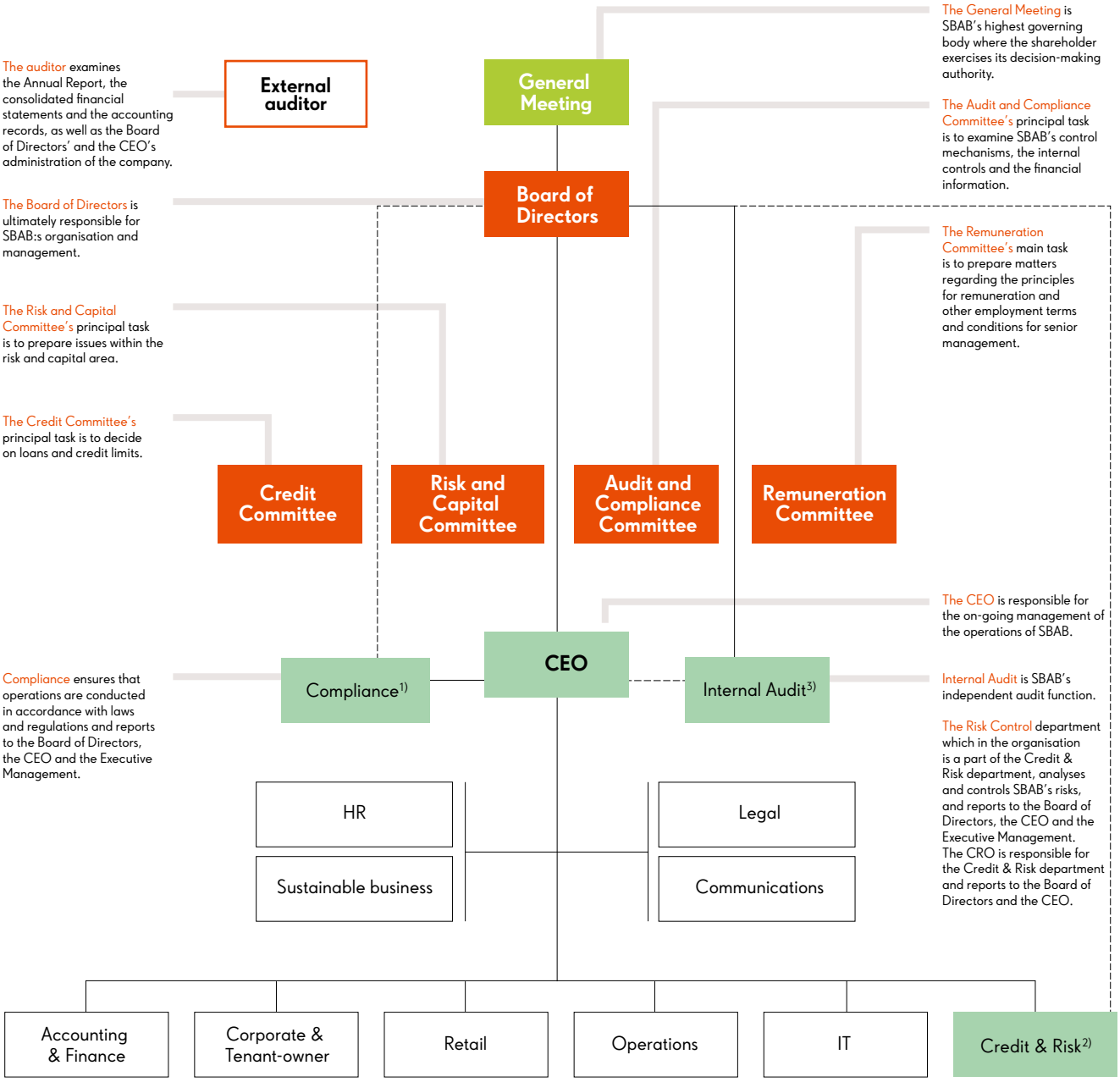


Figure 2. SBAB's organisation

Overview, 31 December 2014



[1)] In addition to reporting to the CEO, Compliance reports to the Board of Directors.
[2)] SBAB's function for independent risk management within the Credit and Risk Department reports to the Board of Directors in addition to the CEO.
[3)] The internal auditor reports to the Board of Directors and the Board's Audit and Compliance Committee.

In addition to the CEO, the following positions are included in SBAB's Executive Management: The heads of IT, economics & finance (CFO), HR, legal, credit & risk
(CRO), retail, corporate and tenant-owner associations and communications.

4. Risk management and risk organisation

SBAB's risk taking is low and is kept at a level commensurate with financial targets for return, adequacy 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 an on-going discussion 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 shall have 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 desirable 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 use derivatives mainly 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 clear 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, 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 small 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 acceptable risk must be clearly linked to how important the prevailing risk is to SBAB's business model and the positive effects anticipated to be achieved in the form of expected revenues, cost savings or reductions in other risk.

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. This measure also includes ensuring that the SCBC's covered pool has a sufficient level of collateral to maintain an 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.

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.

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.

Table 3. Limits for capital ratios and targets for return

	Limit		Outcome		Difference	
	2014	2013	2014	2013	2014	2013
Return on equity (owner's return requirement)[1)]	10.0%	10.0%	12.1%	9.5%	+2.1%	-0.5%
Common Equity Tier 1 capital ratio according to CRR/CRD	22.0%	–	29.8%	–	+7.8%	–
Total capital ratio with transitional regulations	≥ 9.5%	≥ 9.5%	10.8%	10.5%	+1.3%	+1.0%

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

Based on the chosen business strategy, rating targets and capital planning, the Board of Directors has adopted the targets described in Table 3 in accordance with CRR/CRD IV and the transitional regulations.

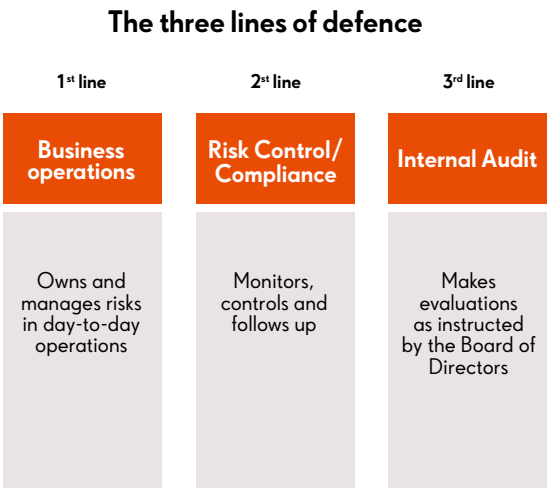
The outcome is reported to the CEO and Board of Directors on a monthly basis. More in-depth reporting of the current capital position in relation to established targets is performed quarterly. The CRO is responsible for this reporting.

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 pertains to the Internal Audit, which regularly performs independent checks of the management of and systems for internal controls.

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. The Board of Directors are responsible for ensuring that the operations can be conducted with generally accepted internal control, so that SBAB's ability to meet its obligations is not jeopardised. When the Board of Directors 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 of Directors 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 of Directors and CEO receiving on-going training in risk-related matters 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 adopted 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 of Directors.

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.

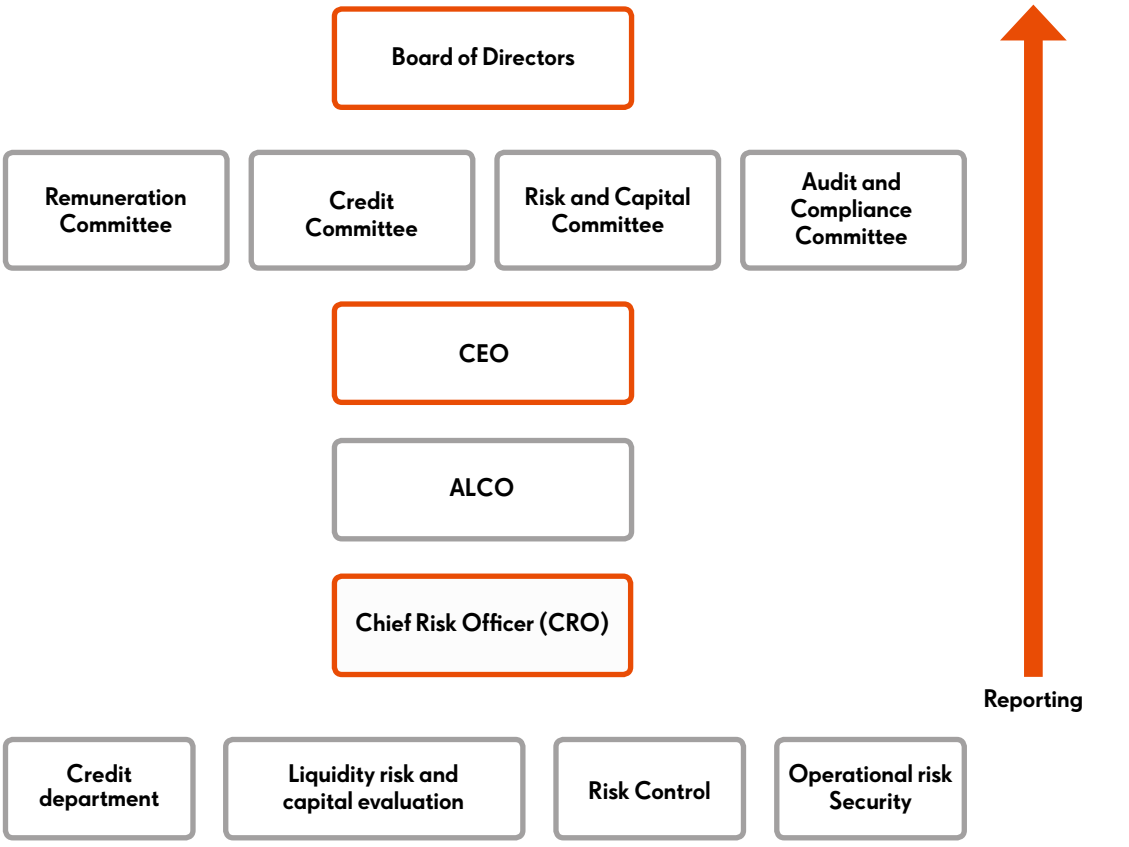
Among other matters, Risk Control is responsible for:

- 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 of Directors, 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 from on current risk levels in relation to granted limits is presented to the CEO, CFO and CRO. SBAB's Board of Directors 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

As of 2014, new rules on capital adequacy apply. The purpose of the new rules is in part to make institutions more resilient to new crises, in part to raise confidence in the institutions' ability to manage new crises. Additionally, rating agencies and the investors who purchase securities from banks, as well as new and existing customers, must be confident that the capital situation is sufficient.

5.1 Capital requirements according to the new regulations

The new regulations entail, among other things, requirements for increased own funds and higher capital requirements. SBAB has taken this into account in its capital planning and meets the requirements according to the new rules.

In addition to the new regulations, the Swedish Financial Supervisory Authority has increased the national risk-weight floor from 15% to 25% for residential mortgages to Swedish households. Banks that are considered systemic will be subject to additional capital requirements. The four largest banks in Sweden are currently considered systemically important: Handelsbanken, Nordea, SEB and Swedbank. The requirement for additional capital could eventually encompass more banks.

In November 2014, the Swedish Financial Supervisory Authority announced that an amortisation requirement will be introduced for new residential mortgages. According to the proposal, new residential mortgages must be amortised by 2% of the initial loan per year until a loan to value ratio of 70% is reached, and thereafter by 1% per year down to a loan to value ratio of 50%. It is difficult to assess the effect of these measures, intended to restrain the market for residential mortgages, and developments are carefully monitored.

5.2 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 requirements 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). CRR further contains transitional regulations entailing that the capital requirement must be at least 80% of the capital requirements under Basel I. The total capital ratio amounted to 44.7% at per 31 December 2014 and the Common Equity Tier 1 capital ratio amounted to 29.8%.

Table 4. Capital adequacy

	Consolidated situation		Parent Company		SCBC	
SEK million	**2014**	**2013[1)]**	**2014**	**2013[1)]**	**2014**	**2013[1)]**
Common Equity Tier 1 capital	10,199	9,583	8,066	8,268	12,700	11,318
Tier 1 capital	12,594	12,577	10,461	11,262	12,700	11,318
Total capital	15,307	14,644	13,174	13,368	12,700	11,318
Without transitional regulations						
Risk exposure amount	34,247	41,149	28,363	23,417	17,565	19,263
Common Equity Tier 1 capital ratio	29.8%	23.3%	28.4%	35.3%	72.3%	58.8%
Excess Common Equity Tier 1 capital	8,658	7,732	6,790	7,215	11,909	10,451
Tier 1 capital ratio	36.8%	30.6%	36.9%	48.1%	72.3%	58.8%
Excess Tier 1 capital	10,539	10,108	8,760	9,857	11,646	10,162
Total capital ratio	44.7%	35.6%	46.4%	57.1%	72.3%	58.8%
Excess total capital	12,567	11,352	10,905	11,495	11,295	9,777
With transitional rules						
Own funds	15,392	14,644	13,223	13,368	12,736	11,318
Risk exposure amount	142,975	139,600	29,938	32,507	113,258	107,089
Total capital ratio	10.8%	10.5%	44.2%	41.1%	11.2%	10.6%

[1)] According to the earlier regulations (Basel II)

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 15,307 million as per 31 December 2014. 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 was deducted. The surplus has been verified by the Company's auditors, in accordance with Article 26, item 2, of the CRR.

According to the transitional regulations to Article 35 of the CRR, unrealised gains shall not be recognised in 2014, except for unrealised gains according to Article 33 of the CRR. SEK 76 million was 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 for SEK -100 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 with SEK -2 million, in accordance with Article 33, item b.

With reference to Articles 34 and 105 of the CRR, SEK 70 million has been deducted due to the requirements for prudent valuation.

A deduction of SEK 43 million for intangible assets and a deduction of SEK 85 million for net provisions were made, in accordance with Article 36.

No risk exposures have been deducted from own funds.

As a step in the adaptation to Basel III, FriSpar Bolån AB, which was 51% owned by SBAB, was liquidated in 2014. As a result, SBAB no longer has any minority interests as of 31 December 2014. Subordinated debt 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 permission. SBAB has obtained such permission for three debenture loans with a nominal value of SEK 3,000 million (Subordinated debenture SEK 1, 2 and 3 in Table 5), of which SEK 2,395 million has been included in Tier 1 capital, according to the transitional regulations. The difference has been recognised as Tier 2 capital. A nominal amount of SEK 1,000 million has an incentive to redeem (step-up).

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 the document under "Risk management" at sbab.se. The complete terms and conditions of the debenture loans are also specified at sbab.se.

Table 5. Debenture loans (million)

Loan designation	Currency	Nominal amount	Outstanding nominal amount	First possible date for redemption	Interest rate, 31 December 2013	Interest rate after first possible date for redemption	Maturity date	Recognised in own funds as Common Equity Tier 1 instruments (SEK million)	Recognised at in own funds (SEK million)
JPY 1	JPY	10,000	10,000	–	5.23%	5.23%	16 November 2015	–	114
Subordinated debenture SEK 1	SEK	700	700	30 June 2016	5.22%	3 m stibor+1.93%	Perpetual	555	139
Subordinated debenture SEK 2	SEK	300	300	30 June 2016	3 m stibor+0.93%	3 m stibor+1.93%	Perpetual	240	60
Subordinated debenture SEK 3	SEK	2,000	2,000	8 June 2015	7.16%	3 m stibor+4,50%	Perpetual	1,600	400
Subordinated debenture SEK 4	SEK	1,000	1,000	20 April 2016	6.123%	3 m stibor+2,4%	20 April 2021	–	1,000
Subordinated debenture SEK 5	SEK	800	800	16 November 2017	3 m stibor+2.65%	3 m stibor+2.65%	16 November 2022	–	800
Subordinated debenture SEK 6	SEK	200	200	16 November 2017	4.18%	3 m stibor+2.65%	16 November 2022	–	200
Total		**15,000**	**15,000**					**2,395**	**2,713**

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 2014) or what generally applies under the Companies Act (2005:551).

The starting capital required for the Parent Company in accordance with the Banking and Financing Business Act (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

Table 6. Own funds

SEK million	31 Dec 2014	31 December 2013[1)]
Common Equity Tier 1 capital: Instruments and reserves		
Capital instruments and associated share premium accounts	1,958	1,958
Retained earnings	7,710	6,873
Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses according to applicable accounting standards)	76	n/a
Minority interests (amount that qualifies for inclusion in consolidated Common Equity Tier 1 capital)	–	100
Interim profit/loss after deduction of foreseeable costs and dividends, verified by persons in an independent position	754	873
Common Equity Tier 1 capital before regulatory adjustments	**10,498**	**9,804**
Common Equity Tier 1 capital: regulatory adjustments		
Additional value adjustments (negative amount)	-70	-18
Intangible assets (net after deduction for associated tax liabilities) (negative amount)	-43	-165
Deferred tax assets dependent on future profitability, except those arising from temporary differences (net after deductions for associated tax liabilities, provided the conditions in Article 38(3) are met) (negative amount)	0	0
Reserves in fair value related to profit or loss on cash flow hedging	-100	–
Negative amounts following the calculation of expected loss amounts	-84	-38
Gains or losses on liabilities valued at fair value that result from changes in the own credit standing of the institution	-2	n/a
Total regulatory adjustments to the Common Equity Tier 1 capital	**-299**	**-221**
Common Equity Tier 1 capital	**10,199**	**9,583**
Additional Tier 1 instruments: Instruments		
Capital instruments and associated share premium accounts	–	2,994
Amount for qualified items referred to in Article 484(4) and associated share premium reserves included in the phase-out from the additional Tier 1 instruments	2,395	n/a
Additional Tier 1 instruments before regulatory adjustments	**2,395**	**2,994**
Additional Tier 1 instruments: Regulatory adjustments		
Total regulatory adjustments of additional Tier 1 instruments	–	**n/a**
Additional Tier 1 instruments	**2,395**	**2,994**
Tier 1 capital (Tier 1 capital = Common Equity Tier 1 capital + additional Tier 1 instruments)	**12,594**	**12,577**
Tier 2 capital: instruments and allocations		
Capital instruments and associated share premium accounts	2,599	2,123
Amount for qualified items referred to in Article 484(5) and associated share premium reserves that are phased out from Tier 2 capital	114	n/a
Negative amounts following the calculation of expected loss amounts	–	-56
Tier 2 capital before regulatory adjustments	**2,713**	**2,067**
Tier 2 capital. Regulatory adjustments		
Total regulatory adjustments of Tier 2 capital	**–**	**n/a**
Tier 2 capital	**2,713**	**2,067**
Total capital (total capital = Tier 1 capital + Tier 2 capital)	**15,307**	**14,644**
Total risk-weighted assets	**34,247**	**41,149**
Capital ratios and buffers		
Common Equity Tier 1 capital (as a percentage of the risk-weighted exposure amount)	29.8%	23.3%
Tier 1 capital (as a percentage of the risk-weighted exposure amount)	36.8%	30.6%
Total capital (as a percentage of the risk-weighted exposure amount)	**44.7%**	**35.6%**
Institution-specific buffer requirements (common equity Tier 1 capital requirement according to Article 92(1)(a) plus capital conservation buffer requirement and countercyclical capital buffer, plus systemic risk buffer, plus buffer for systemic institutions (G-SII buffer and O-SII buffer) expressed as a percentage of the risk-weighted exposure amount	2.5%	n/a
Of which, capital conservation buffer requirement	2.5%	n/a
Of which, countercyclical buffer requirement	–	n/a
Of which, systemic risk buffer requirement	–	n/a
Of which, G-SII buffer and O-SII buffer	–	n/a
Common Equity Tier 1 capital, available for use as a buffer (as a percentage of the risk-weighted exposure amount)	–	n/a
Capital instruments that are subject to phase-out arrangements (only applicable between 1 January 2013 and 1 January 2022)		
Current ceiling for additional Tier 1 instruments that are subject to phase-out arrangements	2,395	n/a
Amount excluded from additional Tier 1 instruments due to the ceiling (amounts that exceed the ceiling after redemption and maturity)	599	n/a
Current ceiling for Tier 2 instruments that are subject to phase-out arrangements	1,040	n/a

[1)] According to the earlier regulations (Basel II)

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 7 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% if the loan-to-value ratio condition 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%, 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 28% of lending for tenant-owner rights.

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

Table 7. Capital requirements

	31 December 2014		31 December 2013[1]	
SEK million	**Capital requirements**	**Risk exposure amount**	**Capital requirements**	**Risk exposure amount**
Credit risk recognised in accordance with IRB approach				
Exposure to corporates	558	6,975	736	9,199
Retail exposures	1,028	12,851	1,124	14,051
– of which, exposures to small and medium-sized companies	*139*	*1,737*	*211*	*2,638*
– of which, exposures to tenant-owner rights, single-family dwellings and holiday homes	*889*	*11,114*	*913*	*11,413*
Items representing positions in securitisation	–	–	270	3,380
Total exposure recognised in accordance with IRB approach	**1,586**	**19,826**	**2,130**	**26,630**
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[2]	111	1,388	397	4,965
– of which, derivatives listed in CRR, Annex II	*103*	*1,291*	*88*	*1,106*
– of which, repos	*7*	*85*	*241*	*3,011*
Exposure to corporates	146	1,829	196	2,454
Retail exposures	143	1,783	99	1,231
Defaulted exposures	1	10	1	11
Exposures in the form of covered bonds	59	744	–	–
Exposures to institutions and corporates with a short-term credit assessment	7	86	–	–
Exposures in the form of shares or units in collective investment undertakings (funds)	20	253	17	217
Other items	86	1,070	10	127
Total exposure in accordance with the standardised approach	**573**	**7,163**	**720**	**9,005**
Market risk	**337**	**4,210**	**287**	**3,591**
– of which, position risk	*279*	*3,491*	*287*	*3,591*
– of which, currency risk	*58*	*719*	–	–
Operational risk	**164**	**2,047**	**154**	**1,923**
Credit rating risk	**80**	**1,001**	**–**	**–**
Total minimum capital requirement and risk exposure amount	**2,740**	**34,247**	**3,291**	**41,149**
Applicable capital buffer (capital conservation buffer)	**856**	–	–	–
Total capital requirement (including capital conservation buffer)	**3,596**			

[1] According to the earlier regulations (Basel II).
[2] The risk weighted exposure amount for counterparty risk according to Article 92, item 3f, of CRR amounts to SEK 1,376 million.

5.5 Securitised assets

SBAB previously held securitised assets in the form of RMBS. Securitised assets with a carrying amount of SEK 2,278 million were divested during the year, which impacted the operating profit/loss negatively by SEK 62.4 million.

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.

Table 8. Exposure amounts before and after credit risk mitigation, per credit quality step (SEK million)

Credit quality step	Exposure amount before credit risk mitigation	Exposure amount after credit risk mitigation
1	22,659	22,659
2	1,789	1,789
3	248	248
4	–	–
5	–	–
6	–	–
Total	**24,697**	**24,697**

5.7 Buffers

SBAB reports capital conservation buffers in the table showing capital requirements. As of 13 September 2015, Sweden announced the introduction of a countercyclical buffer. The buffer value shall be determined each quarter by the Swedish Financial Supervisory Authority. As per 31 December 2014, the value was 1%. Sweden has also chosen to implement a systemic risk buffer in 2015, amounting to 5% of the risk-weighted assets of the four major banks.

6. Internal model for calculating capital requirements

The internal capital adequacy assessment process 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 adequacy assessment. 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 adequacy assessment process (ICAAP).

6.1 Internal capital adequacy assessment according to the Basel Regulations, Pillar 2

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 required for the 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 based on stress tests and capital for further risk, this comprises SBAB's assessment of the appropriate size of risk capital. The capital requirement in accordance with Pillar 2 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 risk capital, 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 commensurate to 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 initially identified. 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 a 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. Internal capital adequacy assessment process

1. Quantification of risks	2. Quantification and assessment of other risks (capital buffers)	3. Assessment of combined internal capital requirements	4. Own funds (compared with capital policy and plan)	5. Operational governance Allocation of capital	6. Reporting
• Credit risk • Concentration risk • Market risk • Operational risk	• Stress test • Earnings volatility • Other risks and extraordinary events	• Comparison of economic capital and minimum capital requirements in accordance with Pillar 1 • Aggregation of capital requirements for the various risks	• Common Equity Tier 1 capital • Additional Tier 1 instruments • Tier 2 capital	• Risk-adjusted profitability • Segment analysis and capital costs • Return on allocated capital	• Fulfilment of capital targets and combined internal capital requirements • Reporting internally • Reporting externally

6.3 Economic capital

The capital requirements for credit risk, market risk, operational risk and business 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%, 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 as well as 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 10, 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 entire capital requirement for concentration risk is included in the economic capital framework for credit risk.

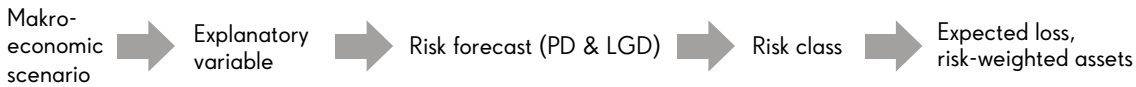
SBAB calculates the concentration risk divided into single-name concentration, industry concentration and sector concentration (geographic concentration). SBAB:s method for single-name concentration is based on a method developed by Gordy & Lütkebohmert (2007) while industry and sector concentration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

Upon calculation at 31 December 2014, the internally calculated capital requirement for concentration risk amounted to SEK 346 million, of which SEK 322 million pertained to credit risk in the lending operations and SEK 25 million to credit risk in the funding operations. Concentration risk related to finance operations increased SEK 7 million while concentration risk related to lending operations declined SEK 82 million compared with the preceding year-end.

6.4 Stress tests

Capital planning is founded on a base 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 economic downturn are 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 most likely scenario are also taken into account.

Figure 6. Schematic process for the calculation of loan losses and capital requirements under stress



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 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 above.

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 lag.

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 volume development;
- 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.

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

Scenario

External shocks have a heavy impact on the Swedish economy. 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.

Escalated conflicts in Ukraine and the Middle East are leading to substantial geopolitical unease, the prices of oil and other commodities are falling sharply and the international financial markets are 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. The Swedish krona is 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 late 2016.

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 20-25 percent before stabilising in 2016.

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.

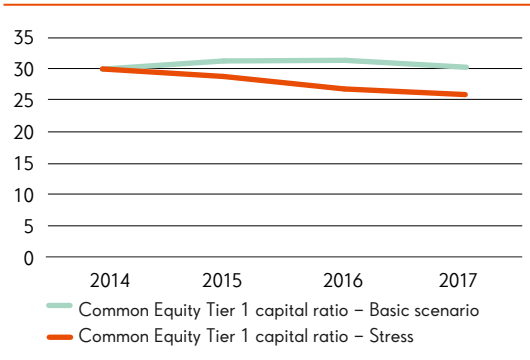
Table 9. The following parameters are subjected to stress in the current and next three years

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 note
		Housing bonds – Government bonds, 5 year
		Government bonds Sweden-Germany, 10 year

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 higher 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 base 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. To counteract the weakening of SBAB's Common Equity Tier 1 capital ratio, a provision of SEK 1,541 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 base scenario.

Figure 7. Common Equity Tier 1 capital ratio in stress scenario



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 own funds without constituting a real market risk. This primarily affects basis swap spreads and mortgage and government bond spreads in SBAB's liquidity portfolio, which largely comprises SBAB's liquidity reserve.

Most of the assets in the liquidity portfolio are measured at market value in the balance sheet. The interest-rate swaps connected to these assets are also measured at market value. However, the funding that finances these assets is not to be measured at market value. Basis swaps are 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 and the credit spread on the assets lack counter-items in profit and loss.

This has the effect that operating profit, and thereby the own funds, varies in a manner that does not match the actual risk to which the portfolio is exposed. To simulate how much this can conceivably affect the own funds, a 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%. The capital requirement for earnings volatility is estimated at SEK 577 million as per 31 December 2014.

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% from the previous 15%. 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 intends to introduce 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 will be adopted in 2015. Until these methods have been adopted, there is some uncertainty how the Swedish Financial Supervisory Authority will assess the capital requirements for these risks.

SBAB's internally calculated capital requirements without and with consideration for the risk weight floor for Swedish residential mortgages are stated below.

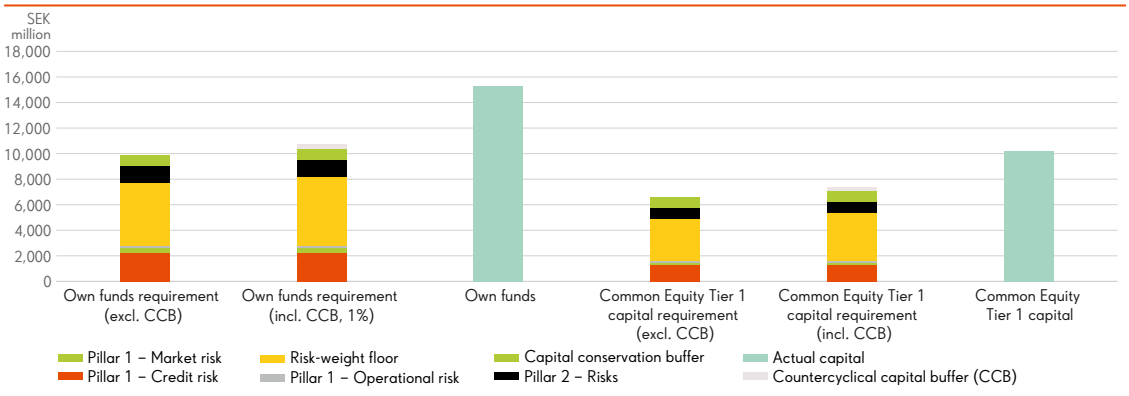
Table 10. Internally calculated capital requirements, by risk type

SEK million	Without risk weight floor			With risk weight floor for Swedish residential mortgages			
Risk category	Pillar 1	Economic capital and stress test	Internal capital requirements without risk weight floor	Pillar 1	Economic capital and stress test	Risk weight floor	Internal capital requirements with risk weight floor
Credit risk	2,239	3,243	3,243	2,239	3,243	7,189	7,189
Market risk	337	608	608	337	608		608
Operational risk	164	304	304	164	304		304
Concentration risk		346	346		346		346
Earnings volatility		577	577		577		577
Capital conservation buffer/ stress test buffer[1)]	856	1,541	1,541	856	570		856
Total	**3,596**	**6,620**	**6,620**	**3,596**	**5,648**	**7,189**	**9,881**

[1)] The higher 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 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 Pillar 1, including static buffer requirements (capital conservation buffer, systemic risk buffer and O-SII buffer). For SBAB, this means that 67% of the capital requirement for Pillar 2 risks should be covered with Common Equity Tier 1 capital.

Figure 8. Internal capital requirement, taking the risk-weight floor into account, by type of capital



7. Risk in remuneration systems

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 (the managers who are embers of SBAB's Executive Management). The Board of Directors decides on:

- Remuneration policy, underlying instruction 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).
- Measures to follow up the application of SBAB's control documents regarding remuneration issues.

The Board of Directors 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 issues regarding principles for remuneration and other employment terms and conditions for senior executives for resolution by the Board of Directors. The Remuneration Committee also prepares matters pertaining to SBAB's remuneration system ahead of Board of Directors 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.

In the past three years, SBAB has had no variable compensation. However, in the period 2009–2011, employees had the opportunity to receive variable remuneration. Since these year's incentive programmes, no funds are withheld regarding specially regulated personnel.

8. Credit risk in the 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.

8.1 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 generated earnings. Credit risk shall be considered in business decisions and constitute a component in the pricing of products and services.

SBAB's Board of Directors 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 taking actions, based on the information provided in the reports.

8.2 Credit risk in the lending portfolio

Credit risk is the single largest risk in SBAB and accounts for 79% of the risk-weighted assets 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 commitments, and also in connection with impairment of the value of pledged assets entailing that these no longer cover the Group's receivables.

Credit risk arising when granting new loans is first monitored by the business area, then 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 comfortably 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% or more of eligible capital, are managed based on the credit directives and external regulations. All exposures exceeding 2% of the eligible capital 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% of the market value. The 85% ratio applies provided that collateral can be obtained with first lien and that the customer has risk class R1–R5 for retail customers and C1–C3, and manually adjusted from C3–C4, for corporate customers (please refer to Table 12). In other cases, a loan to value ratio of 75% applies in general. SBAB also grants small unsecured loans to borrowers in the retail segment.

In case of lending to consumers, market values for collateral in the form of properties or units in a tenant-owner association 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.

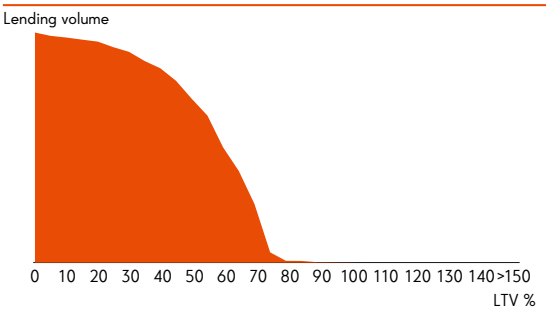
Market values for collateral in the form of properties or rights of use in case of lending to tenant-owner associations and companies shall generally be determined by the person in charge of valuations. External valuations can form the basis of decisions upon approval by the person in charge of valuations. 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.

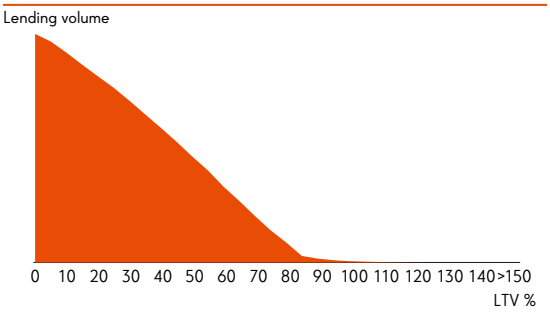
In addition to collateral in real property or a unit in a tenant-owner association, it is possible to grant credit against, for example, collateral in the form of a Government guarantee, a municipal guarantee, securities, bank guarantees and deposits in a Swedish bank. To a limited extent, equities corresponding to up to 85% 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 77% of SBAB's total assets. Figures 9 and 10 describe loan to value (LTV) for loans for which collateral consists of mortgage deeds or a unit in a tenant-owner association. Figure 9 shows corporate exposures and Figure 10 shows retail exposures[1]. The figures cover 98% of total lending to the public. Since 78% of lending has collateral in mortgage deeds or in units in tenant-owner association, within 50% of LTV and 96% within 75% of LTV, while 92% of borrowers are categorised in risk classes 1–4, the credit quality is viewed as being very favourable (for the link between risk category and rating, see Table 12).

Figures 9 and 10. "Loan to value" (LTV) for corporate and retail exposures respectively

Corporate market[1]



Retail[1]



Segment	Below 50%	Below 75%	Below 100%	Exposure-weighted average LTV
Exposures to corporates	76.6%	98.7%	99.9%	65.5%
Retail exposures	78.0%	96.0%	99.5%	62.2%
Total	**77.9%**	**96.3%**	**99.5%**	**62.5%**

[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.

8.3 Risk classification system

For each individual exposure to corporate or retail customers with tenant-owner rights or residential property as collateral, as is the case for 98% of SBAB's total lending, the credit risk is assessed using the Group's IRB models.

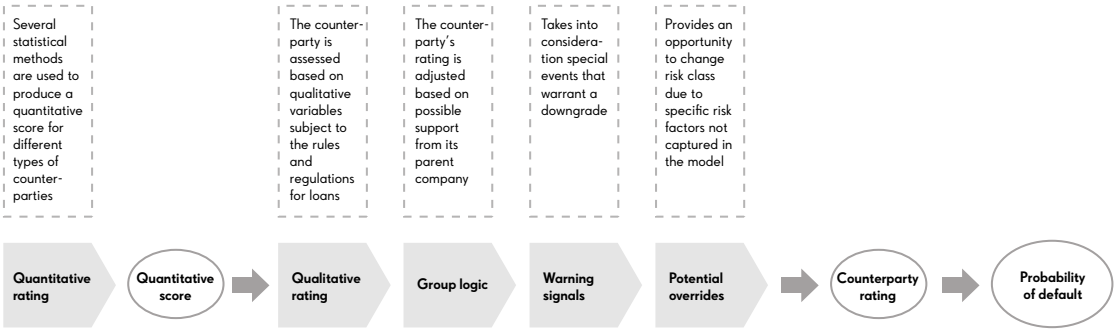
For other types of exposures, the standardised approach is used for measurement of credit risk.

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 in 2014 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 process 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.

8.4 Risk classification method

In conjunction with capital adequacy and risk classification, exposures are categorised in exposure classes.

The foundation 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% 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 7, capital requirements and risk-weighted assets, shows the distribution of capital requirements by exposure classes and risk-weighted assets.

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 collected since 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 11 shows the distinction between retail exposures and corporate exposures.

Table 11. 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) Commercial properties	Exposures to corporates	Corporate
Retail	Single-family dwellings and holiday homes Tenant-owner rights Tenant-owner associations (turnover < EUR 50 million)	Retail exposures	Retail

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 CCF 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 CCF classes.

- The internal ratings-based approach (IRB approach) is used to calculate risk-weighted exposure for credit risk if security is obtained in the form of real property or units in tenant-owner associations.
- The total exposure amount to the Swedish Government, the Riksbank, Swedish municipalities, exposures to institutions and exposures that due to their size and risk profile are less significant are calculated using the standardised approach for credit risks.

In 2014, SBAB applied for permission to use the existing IRB method for certain minor exposures for which the standardised approach is currently used, as well as a permanent permit to apply the standardised approach to exposures that, with regard to their risk profile and size, are of less significance, and which in 2014 were subject to a time-limited permit. In 2014, SBAB was granted a permanent permit to use the standardised approach to exposures of less significance, while the application to apply the IRB method to minor exposures was still being processed on 31 December 2014.

8.5 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. The table reflects the external rating classes that best correspond to the historic proportion of default in each of SBAB's risk classes.

Table 12. The relationship between internal and external rating

Risk class	Standard & Poor's rating	Risk class	Standard & Poor's rating
C1	AAA-A	C/R1	AAA-AA
C2	A	R2	AA-A
C3	A-BBB	R3	A
C4	BBB-BB	R4	A-BBB
C5	BB	R5	BBB-BB
C6	BB-C	R6	BB
C7	B-C	R7	BB-C

8.6 Exposure amounts by exposure class

In contrast to other tables in this section, Table 13 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 321,468 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 valued 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 209 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% of the value of collateral pledged. The insured principal amounted to SEK 212 million at 31 December 2014. 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 9% 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 35% of the total capital requirement according to Pillar 1 where 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 253,533 million, of which 89% comprised retail exposures. Loan commitments and other credit-related commitments totalled SEK 36,479 million that, after the credit conversion factor was taken into account, amounted to SEK 9,601 million.

Risk-weighted assets for credit exposures amounted to SEK 26,989 million, of which SEK 19,826 million was recognised in accordance with the IRB approach and SEK 7,163 million according to the standardised approach. The average risk weighting for exposures recognised in accordance with the IRB approach was 7.5%, while the weighting for exposures recognised in accordance with the standardised approach was 26.5%. Exposure-weighted average PD per counterparty for IRB exposures amounted to 0.46% for corporate exposures and 0.71% for retail exposures. Exposure-weighted average LGD for corporate exposures was 35.6% and exposure- weighted LGD for retail exposures was 10.0%. The exposure-weighted amount for LGD is controlled by the limitation rule, which entails a lowest total level for LGD of 10% 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 13. Exposure amount per 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	Off-balance sheet exposure before CCF	Exposure after CCF[1]	Off-balance sheet exposure after CCF	Exposure covered by credit risk protection in the form of properties	Average value of exposures in lending portfolio[2]	RWA	Capital requirement	Average risk weight	Individual provisions	Collective provisions with deduction for guarantees	Expected loss	Exposure-weighted average PD	Exposure-weighted average LGD
Credit risk recognised in accordance with IRB approach															
Exposure to corporates	26,420	618	49	25,763	10	25,763	28,879	6,975	558	27.1%	18	6	44	0.46%	35.6%
Retail exposures	268,622	1,796	36,430	239,987	9,591	239,987	224,654	12,851	1,028	5.4%	18	136	218	0.71%	10.0%
– Of which, Single-family dwellings and holiday homes	*120,657*	*209*	*13,418*	*110,765*	*3,734*	*110,765*	*104,799*	*6,478*	*518*	*5.8%*	*2*	*78*	*114*	*0.83%*	*10.69%*
– Of which, tenant-owner rights	*96,464*	*–*	*22,441*	*79,468*	*5,446*	*79,468*	*70,503*	*4,636*	*371*	*5.8%*	*13*	*51*	*71*	*0.68%*	*10.30%*
– Of which, tenant-owner associations	*51,501*	*1,587*	*571*	*49,754*	*411*	*49,754*	*49,352*	*1,737*	*139*	*3.5%*	*3*	*7*	*33*	*0.49%*	*7.98%*
Total credit risk in accordance with IRB approach	**295,042**	**2,414**	**36,479**	**265,750**	**9,601**	**265,750**	**253,533**	**19,826**	**1,586**	**7.5%**	**36**	**142**	**262**		
Credit risk recognised in accordance with standardised approach															
Exposures to central governments and central banks	2,898	–	–	3,098	–	–	215	0	0	0.0%	–	–			
Exposures to regional governments or local authorities	1,187	–	–	3,401	–	–	2,622	0	0	0.0%	–	–			
Exposures to institutions	6,857	–	–	6,857	–	–	–	1,388	111	20.2%	–	–			
Exposure to corporates	2,902	–	1,797	2,003	899	–	1,260	1,829	146	91.3%	–	–			
Retail exposures	3,329	–	1,182	2,376	236	–	1,885	1,783	143	75.0%	–	7			
Exposures in default	8	–	–	8	–	–	13	10	1	134.1%	–	1			
Exposures in the form of covered bonds	7,443	–	–	7,443	–	–	–	744	59	10.0%	–	–			
Exposures to institutions and corporates with a short-term credit assessment	427	–	–	427	–	–	–	86	7	20.0%	–	–			
Exposures in the form of shares or units in collective investment undertakings (CIU)	253	–	–	253	–	–	–	253	20	100.1%	–	–			
Other items	1,122	–	–	1,122	–	–	–	1,070	86	95.4%	–	–			
Total credit risk in accordance with standardised approach	**26,426**	**–**	**2,979**	**26,988**	**1,135**	**–**	**5,995**	**7,163**	**573**	**26.5%**	**–**	**8**			
Total	**321,468**	**2,414**	**39,458**	**292,738**	**10,736**	**265,750**	**259,528**	**26,989**	**2,159**	**9.2%**	**36**	**150**			

[1] For 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 2014 but it differs from the information provided in the Annual Report 2014 as the exposure amounts, including accrued interest, are reported instead of the principal. When the term exposure is used in the following section of this chapter, it refers to exposure after outflows or inflows, i.e. with deductions for collateral and off-balance sheet exposure, unless stated otherwise. The tables may contain differences due to rounding off.

8.7 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.

Table 14. Exposure amount per geographical area for credit risk exposures

SEK million	Sweden	Denmark	France	Germany	Norway	United Kingdom	USA	Canada	Total
Credit risk recognised in accordance with IRB approach									
Exposure to corporates	25,753	–	–	–	–	–	–	–	25,753
Retail exposures	230,396	–	–	–	–	–	–	–	230,396
– of which, exposures to small and medium-sized companies	*49,342*	–	–	–	–	–	–	–	*49,342*
– of which, exposures to tenant-owner rights, single-family dwellings and holiday homes	*181,053*	–	–	–	–	–	–	–	*181,053*
Total exposure recognised in accordance with IRB approach	**256,149**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**256,149**
Credit risk recognised in accordance with standardised approach									
Exposures to central governments and central banks	3,098	–	–	–	–	–	–	–	3,098
Exposures to regional governments or local authorities	3,401	–	–	–	–	–	–	–	3,401
Exposures to institutions	4,732	630	199	81	18	1,044	151	2	6,857
Exposure to corporates	1,105	–	–	–	–	–	–	–	1,105
Retail exposures	2,147	–	–	–	–	–	–	–	2,147
Exposures in default	8	–	–	–	–	–	–	–	8
Exposures in the form of covered bonds	7,443	–	–	–	–	–	–	–	7,443
Exposures to institutions and corporates with a short-term credit assessment	427	–	–	–	–	–	–	–	427
Exposures in the form of shares or units in collective investment undertakings (CIU)	253	–	–	–	–	–	–	–	253
Other items	1,122	–	–	–	–	–	–	–	1,122
Total exposure in accordance with the standardised approach	**23,736**	**630**	**199**	**81**	**18**	**1,044**	**151**	**2**	**25,861**
Total	**279,885**	**630**	**199**	**81**	**18**	**1,044**	**151**	**2**	**282,010**

SBAB's lending portfolio is mainly secured by housing in the Stockholm area (52%) and the Öresund region (22%). Only 1% of the underlying collateral derives from economically weak regions (see Table 15). 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[3]: Municipalities with very weak or negative growth according to analyses by SBAB;
- Other regions[3]: Municipalities that are not allocated to any other category.

[3] 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 15. 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	11,543	2,471	4,575	3,977	235	2,952	25,753
Retail exposures	121,951	18,069	53,781	19,764	3,342	13,489	230,396
Total exposure recognised in accordance with IRB approach	**133,494**	**20,540**	**58,356**	**23,741**	**3,577**	**16,441**	**256,149**
Standardised exposures							
Exposures to central governments and central banks	38	15	27	50	28	42	200
Exposures to regional governments or local authorities	544	197	161	387	263	685	2,237
Exposure to corporates	840	38	7	194	0	3	1,082
Retail exposures	1,220	200	274	249	58	146	2,147
Exposures in default	4	0	2	1	0	1	8
Total exposure in accordance with the standardised approach	**2,646**	**450**	**471**	**881**	**349**	**877**	**5,674**
Total	**136,140**	**20,990**	**58,827**	**24,622**	**3,926**	**17,318**	**261,823**

8.8 Exposure amounts distributed by the next stipulated date of expiry

A large proportion (65%) of the credit risk exposures has a remaining maturity of less than a year.[1)] The proportion that has a remaining maturity of one to five years encompass 33% of the outstanding exposures (please see Table 16). 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 16. Exposure amounts distributed by 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	10,559	14,171	1,023	25,753
Retail exposures	163,834	63,318	3,244	230,396
Total exposure recognised in accordance with IRB approach	**174,393**	**77,489**	**4,267**	**256,149**
Credit risk recognised in accordance with the standardised approach				
Exposures to states and central banks	570	2,528	0	3,098
Exposures to regional governments or local authorities	1,466	1,706	229	3,401
Exposures to institutions	1,331	4,443	1,083	6,857
Exposure to corporates	510	591	4	1,105
Retail exposures	2,139	8	0	2,147
Exposures in default	8	0	0	8
Exposures in the form of covered bonds	1,668	5,775	0	7,443
Exposures to institutions and corporates with a short-term credit assessment	427	–	–	427
Exposures in the form of shares or units in collective investment undertakings (CIU)	253	–	–	253
Other items	1,122	–	–	1,122
Total exposure in accordance with the standardised approach	**9,494**	**15,051**	**1,316**	**25,861**
Total	**183,887**	**92,540**	**5,583**	**282,010**

[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.

8.9 Exposure amounts by type of property

In the distribution of the lending portfolio by type of property, lending for single-family dwellings, holiday homes and tenant-owner associations accounts for 90% of the total lending portfolio (see Table 17).

Table 17. Exposure amounts by type of property for credit risk exposures in the lending operations

SEK million	Single-family dwellings and holiday homes	Tenant-owner rights	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	18	3	1,115	20,896	100	3,620	–	25,752
– of which, exposures to small and medium-sized companies	*18*	*3*	*903*	*9,102*	*0*	*1,107*	–	*11,133*
Retail exposures	107,031	74,023	49,343	–	–	–	–	230,397
Total exposure recognised in accordance with IRB approach	**107,049**	**74,026**	**50,458**	**20,896**	**100**	**3,620**	**–**	**256,149**
Credit risk recognised in accordance with standardised approach								
Exposures to central governments and central banks	27	–	159	15	–	–	–	200
Exposures to regional governments or local authorities	182	–	1,459	74	507	15	–	2,237
Exposure to corporates	0	–	729	283	1	69	–	1,082
– of which, exposures to small and medium-sized companies	*0*	–	*729*	*275*	*1*	*69*	–	*1,074*
Retail exposures	178	276	–	–	–	–	1,694	2,147
Exposures in default	4	–	–	–	–	–	5	8
Total exposure in accordance with the standardised approach	**390**	**276**	**2,346**	**372**	**508**	**84**	**1,698**	**5,674**
Total	**107,439**	**74,302**	**52,804**	**21,268**	**608**	**3,704**	**1,698**	**261,823**

8.10 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 amounted to 25% of the total exposure amount for past due exposures (refer to Table 18).

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 18. Exposures with past due amounts and provisions

SEK million	Total exposure amount in the lending portfolio	Exposure amounts for past due receivables[1)]	Exposure amounts for exposures with individual provisions	Specific risk		Total exposure amount in the lending portfolio after provisions
				Individual provisions	Collective provisions with deduction for guarantees	
Single-family dwellings and holiday homes	107,440	501	2	2	78	107,360
Tenant-owner rights	74,302	225	14	13	51	74,238
Tenant-owner associations	52,804	8	3	3	7	52,794
Private multi-family dwellings	21,268	1	30	18	6	21,244
Municipal multi-family dwellings	608	–	–	–	–	608
Commercial properties	3,704	–	–	–	–	3,704
Unsecured	1,698	11	–	–	8	1,690
Total	**261,824**	**746**	**49**	**36**	**150**	**261,638**

[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 19. Geographical distribution of exposures with past due amounts and provisions

SEK million	Total exposure amount in the lending portfolio	Exposure amounts for past due receivables[1)]	Exposure amounts for exposures with individual provisions	Specific risk		Total exposure amount in the lending portfolio after provisions
				Individual provisions	Collective provisions with deduction for guarantees	
Greater Stockholm	136,140	330	34	22	71	136,047
Greater Gothenburg	20,991	47	2	2	11	20,978
Öresund region	58,827	254	10	9	27	58,791
University and growth regions	24,623	36	1	1	12	24,610
Weak regions	3,926	19	2	2	10	3,914
Other regions	17,317	60	–	–	19	17,298
Total	**261,824**	**746**	**49**	**36**	**150**	**261,638**

[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 20. Exposures with past due amounts and provisions per exposure class

SEK million	Total exposure amount in the lending portfolio	Exposure amounts for past due receivables[1)]	Exposure amounts for exposures with individual provisions	Specific risk		Total exposure amount in the lending portfolio after provisions
				Individual provisions	Collective provisions with deduction for guarantees	
Credit risk recognised in accordance with IRB approach						
Exposure to corporates	25,753	1	30	18	6	25,729
Retail exposures	230,396	719	19	18	136	230,242
– Of which, Single-family dwellings and holiday homes	*107,032*	*494*	*2*	*2*	*78*	*106,952*
– Of which, tenant-owner rights	*74,022*	*218*	*14*	*13*	*51*	*73,958*
– Of which, tenant-owner associations	*49,343*	*7*	*3*	*3*	*8*	*49,332*
Total exposure recognised in accordance with IRB approach	**256,149**	**720**	**49**	**36**	**142**	**255,971**
Credit risk recognised in accordance with standardised approach						
Exposures to central governments and central banks	200	0	–	–	–	200
Exposures to regional governments or local authorities	2,237	1	–	–	–	2,237
Exposure to corporates	1,082	1	–	–	–	1,082
Retail exposures	2,148	16	–	–	7	2,141
Exposures in default	8	8	–	–	1	7
Total exposure in accordance with the standardised approach	**5,675**	**26**	**–**	**–**	**8**	**5,667**
Total	**261,824**	**746**	**49**	**36**	**150**	**261,638**

[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.

8.11 Reconciliation of changes in the specific credit risk adjustments for doubtful receivables

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

In June 2014, SBAB divested a portfolio of confirmed loan losses. The portfolio, comprising credits that were previously recognised as confirmed loan losses, included loans of SEK 84 million. The purchase price amounted to SEK 11.3 million and was recognised with SEK 10.6 million in the balance sheet after adjustment for payments received until the payment date.

Table 21. 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	-28	-19	-244
Individual provision for the year	0	-4	
Reversed from previous provisions	7	3	
Individual provision utilised for confirmed losses	–	5	
Allocation to/redemption of collective provisions			38
Provision at the end of the year	-21	-15	-206

8.12 Exposures per risk class in the PD dimension

The quality of the portfolio is favourable. A total of 98% of corporate exposures and 92% of retail exposures in the balance sheet derives from the four best risk classes C1–C4 (corporate exposures) and R1–R4 (retail exposures); see Figures 12–16.

Figure 12. IRB Corporate – exposure by risk class

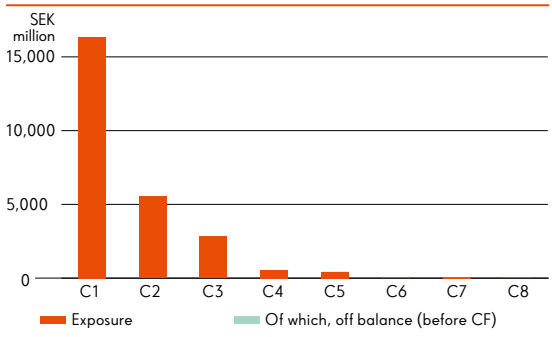


Figure 13. IRB Retail– exposure by risk class

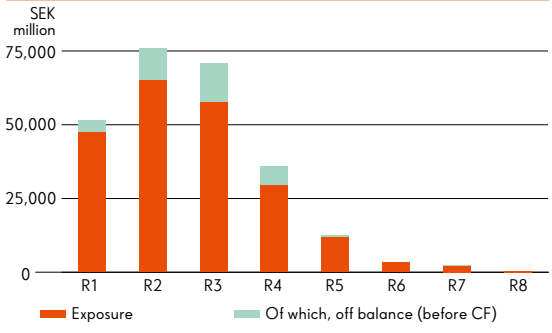


Figure 14. IRB Retail– Tenant-owner rights – exposure by risk class

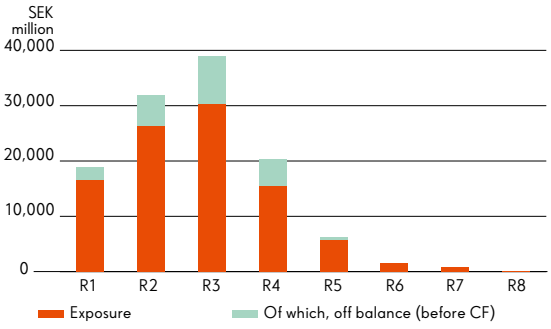


Figure 15. IRB Retail– single-family dwellings/holiday homes – exposure by risk class

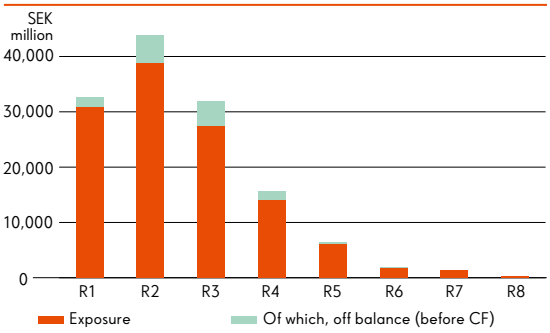
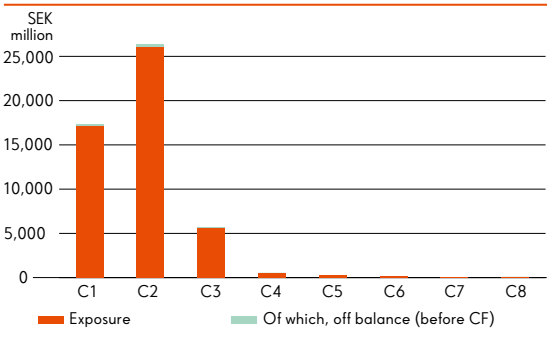


Figure 16. IRB Tenant-owner associations – exposure by risk class



8.13 Realised outcome in the PD and LGD dimensions

Table 22 shows the PD and LGD estimate as of 31 December 2013 and the outcome for 2014. The estimated outcome for the retail exposures is in line with the actual outcome, which indicates that, in the prevailing economic conditions, the PD models neither overestimate nor underestimate the risk of default. The estimated outcome for corporate exposures is considerably 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% for exposures covered by the advanced IRB approach and where collateral comprises a unit in a tenant-owner association, a mortgage in residential property or the site leasehold on such a property.

Table 22. Realised outcome in the PD and LGD dimensions

Exposure class	PD estimates	Realised outcome[1)]	LGD estimates	Realised outcome[2)]
Exposure to corporates	1.0%	0.1%		
Retail exposures	0.6%	0.5%	10.0%	3.1%[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.

8.14 Comparison of expected loss and outcome

During the comparison period (see Table 23), it can be seen that the expected loss (EL), in accordance with the internal risk rating, decreased for corporate loans and increased for retail loans. This difference is explained by the fact that in 2012, the group tenant-owner associations belonged to the group corporate exposures, with prescribed LGD values. Since 2013, tenant-owner associations are classified as retail exposures, which means that LGD is calculated according to internal models. Other groups within retail exposures report a reduction of EL. 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 23. Comparison of expected loss between outcome and model, and provision for loans reported according to IRB [1)]

SEK million	EL, IRB/IRB foundation 31 Dec 2013	EL, IRB/IRB foundation 31 Dec 2012	EL, IRB/IRB advanced 31 Dec 2013	EL, IRB/IRB advanced 31 Dec 2012	Realised outcome 2014	Realised outcome 2013	Total provisions, including guarantees 31 Dec 2014	Total provisions, including guarantees 31 Dec 2013
Exposure class								
Exposure to corporates	62	177	–	–	–	2	24	38
Retail exposures	–	–	237	223	27	31	154	187
Of which, Single-family dwellings and holiday homes	–	–	*129*	*139*	*23*	*17*	*79*	*100*
– Of which, tenant-owner rights	–	–	*78*	*84*	*4*	*14*	*64*	*75*
– Of which, tenant-owner associations	–	–	*30*	–	–	–	*11*	*12*
Total	**62**	**177**	**237**	**223**	**27**	**33**	**178**	**225**

[1)] Expected loss (EL) has been calculated for the loan receivables that existed at the end of 2012 and 2013, respectively.
In Table 18, the expected loss is compared with the actual outcome for confirmed loan losses during the outcome years of 2013 and 2014 respectively.

9. Funding

SBAB's operations are 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. The funding operations 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.

9.1 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% 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 enters into 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 terms of the EMTN programme, SBAB can issue both non-subordinated debt and dated subordinated debt, which with the Swedish Financial Supervisory Authority's permission can qualify as Tier 2 capital. SBAB also has a Japanese Shelf Registration in place, under which SBAB has the possibility to issue bonds in 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% 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.

9.1.1 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 rate notes, and issue bonds through these three programmes in several currencies and denominations.

9.2 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 less than the nominal amount, and when it falls due, the nominal amount is repaid.

9.3 Encumbered and unencumbered assets

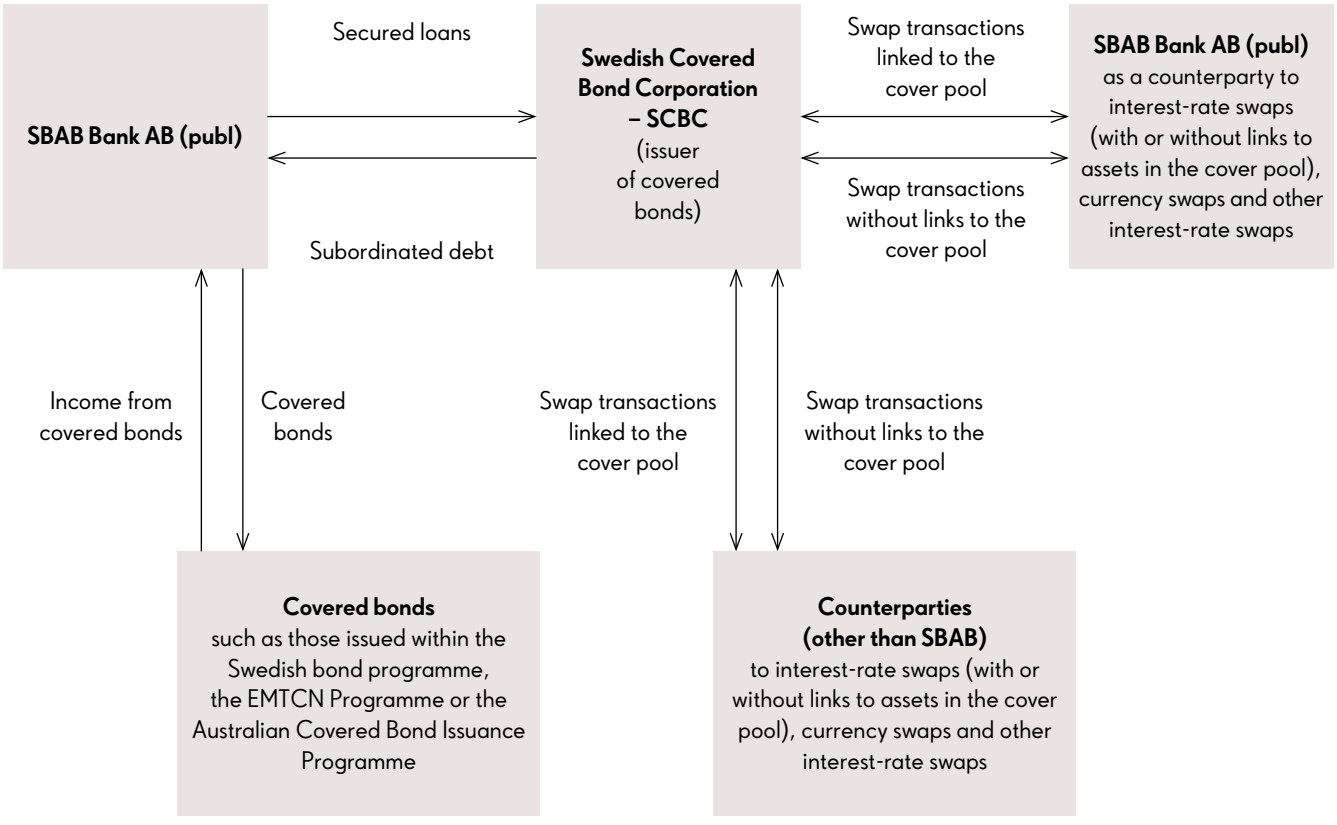
As a part of SBAB's operations, residential mortgages are transferred to the subsidiary SCBC. Such residential mortgages may loans provided against mortgages in real property intended for residential purposes or tenant-owner rights, and they are consequently included in the cover pool for covered bonds. 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.

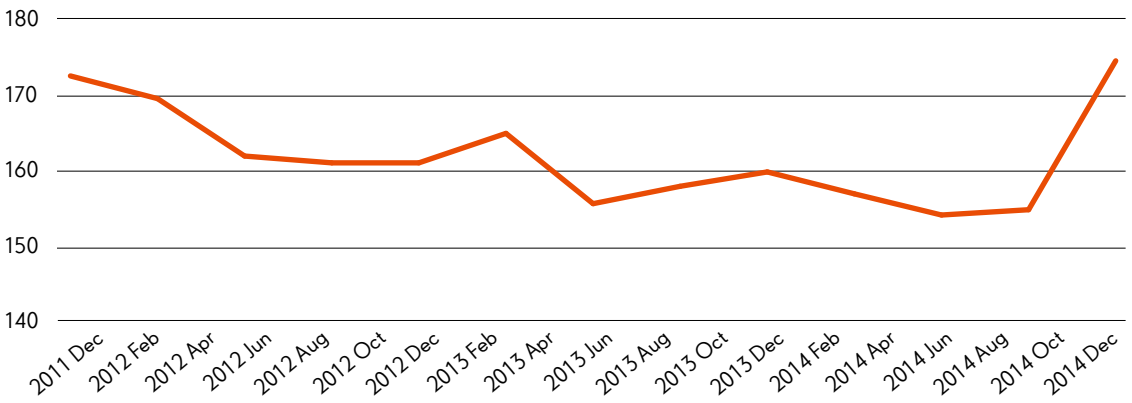
The companies in the SBAB Group also have the possibility of entering into derivatives transactions that do not need to be recorded in the cover pool. Derivative contracts may be entered between the companies in the SBAB Group or with external counterparties. For all counterparties documentation exists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

Figure 17. Mortgage structure between different Group companies



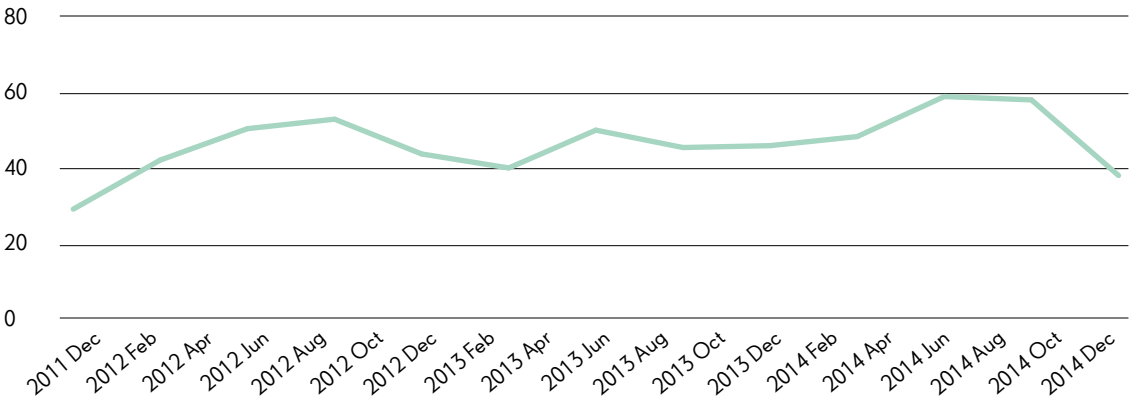
As per 31 December 2014, assets in the cover pool consisted mainly of loans to the public in the form of loans against mortgage of immovable property intended for residential use or against pledged tenant-owner rights. The cover pool may also include substitute collateral, and it is consequently possible to include derivatives or securities in the cover pool.

Figure 18. Volume of mortgaged assets 2011–2014



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 three-year period is described in Figure 19, "Unutilised scope 2011–2014. As per 31 December 2014, SCBC had set as a minimum requirement that the OC level should meet 9%, which is the level required by Moody's to maintain the Aaa-rating. As per 31 December 2014, this level equals a volume of SEK 15.4 billion, corresponding to 27.1% of the unencumbered assets in SCBC and 9.2% of the unencumbered assets in SBAB.

Figure 19. Unutilised scope 2011–2014



Of the assets included in Table 24, "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 24. Information on mortgaged assets

Assets, SEK million	Mortgaged assets, carrying amount	Mortgaged assets, fair value	Unencumbered assets, carrying amount	Unencumbered assets, fair value
Assets of the reporting institution	171,437		167,548	
Equity instruments	–	–	–	–
Interest-bearing securities	–	–	57,892	57,898
Other assets	171,437		109,656	

Table 25. 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	4,234	1,535
Equity instruments	–	–
Interest-bearing securities	1,535	1,535
Other security received	2,699	–
Own interest-bearing securities in issue, except own covered bonds or asset-backed securities	–	–

Table 26. 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, carrying amount	171,437	171,437

9.4 Funding strategy

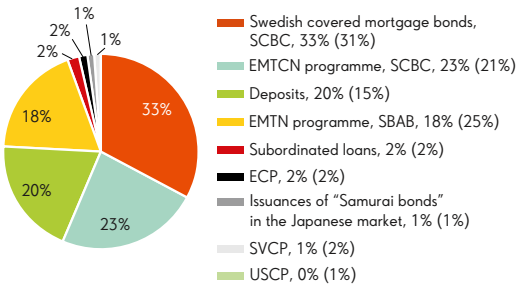
The size of the funding portfolio is adjusted based on the volume of the outstanding loans and the composition of the assets, taking into consideration such factors as liquidity risk and based on the company's risk appetite. Funding is also continuously adapted to meet the new liquidity rules included 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 with evenly distributed debt maturity dates, i.e. periods with large concentrations of debt maturities should be avoided. 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.

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. Secured funding is primarily utilised for protracted durations. 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.

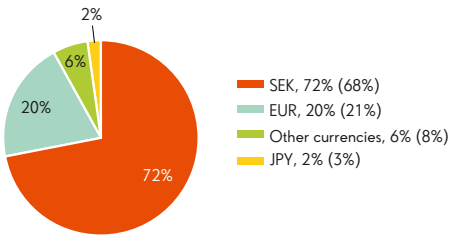
SBAB and SCBC must have an active market presence, with favourable and frequent relations with investors in each investor segment.

Figure 20. Funding sources and distribution by currency for deposits and funding

Issued securities (incl. subordinated loans) and deposits, Group. Debt outstanding at 31 December 2014: SEK 310 billion (296)



Currency distribution, issued securities (incl. subordinated loans) and deposits, Group. Debt outstanding at 31 December 2014: SEK 310 billion (296)



10. Credit risk in the treasury operations

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

In accordance with the credit directive adopted by the Board of Directors, credit risk limits are set by SBAB's Credit Committee for all counterparties in the 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 set. The exposure amount for 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.

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

10.1 Counterparty credit risk

Counterparty credit risk is the risk that SBAB's financial counterparties cannot meet their commitments pursuant to agreed derivatives and repo contracts, and such risk consists primarily of exposures to leading banks. Exposure is primarily secured by 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 a similar agreement, has in most cases been supplemented with an associated collateral agreement, known as Credit Support Annex (CSA). 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 transfer amount to or from the counterparty can vary depending on the parties' credit ratings. Tables 27 and 28 provide an overview of the distribution of the market value of individual derivative transactions by credit rating and maturity.

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

Reconciliation with the counterparty is conducted daily or weekly with each derivatives counterparty with whom a collateral agreement has been agreed, and collateral is transferred to even out exposure. Wherever applicable, the posted and received collateral takes the form of cash with a transfer of title, which entitles the party that receives the collateral to use the collateral 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' credit rating; the worse the credit rating held by a party, the lower are these amounts. A decline in SBAB's credit rating would, as per 31 December 2014, not result in the need for extra collateral to be posted to any external counterparty[1)].

10.2 Credit quality in the liquidity portfolio

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

Covered bonds are risk weighted in relation to their credit quality step according to CRR. As per 31 December 2014, all of SBAB's covered bond investments were assigned credit quality step one, which means a risk weight of 10%. The investments in the portfolio are long-term and as per 31 December 2014, the market value amounted to SEK 58.6 billion with an average maturity of 3 years. At the same date, 94% of the port-

[1)] In case of a decline in SBAB's rating, the Parent Company would need to provide collateral of SEK 1.87 billion to SCBC.

folio's value had a credit rating of Aaa from Moody's or AAA from Standard & Poor's. The various asset classes in the portfolio are securities issued or guaranteed by central governments, securities issued by supranationals and sovereign agencies, securities issued by public sector entities and European covered bonds. Liquidity portfolio investments are either classified as "Securities measured at fair value through profit or loss", "Available-for-sale financial assets" or "Investments held to maturity".

Securities measured at fair value through profit or loss:
- Securities issued by central governments, SEK 13.4 billion;
- Securities guaranteed by central governments, SEK 3.5 billion;
- Securities issued by supranationals and sovereign agencies, SEK 1.9 billion;
- Securities issued by public sector entities, SEK 5.1 billion;
- European covered bonds, SEK 23.7 billion.

Available-for-sale financial assets:
- Securities issued by central governments, SEK 2.4 billion;
- European covered bonds, SEK 3.6 billion.

Investments held to maturity:
- Securities issued by public sector entities, SEK 1.2 billion;
- European covered bonds, SEK 3.9 billion.

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

Table 27. Derivative instruments for the SBAB Group

SEK million	Total nominal value	Positive market values	Negative market values
< 1 year, interest-rate related	49,831	781	-586
> 1 year, interest-rate related	207,187	3,979	-5,049
< 1 year, currency related	28,063	894	-854
> 1 year, currency related	52,645	2,147	-2,614
Total	**337,726**	**7,800**	**-9,103**

Table 28. Derivative instruments distributed by rating for the SBAB Group

SEK million	Net market value	Positive market values	Negative market values
AA-	-69	2,929	-2,998
A+	1,255	2,341	-1,086
A	-519	790	-1,310
A-	419	1,657	-1,238
BBB+	969	1,544	-575
BBB	92	146	-54
Total	**2,147**	**9,408**	**-7,261**
Collateral			**1,794**
Nettings gains			**6,711**

Table 29. Derivative instruments for the SBAB Group

SEK million	
Positive gross market value of contracts	9,408
– Nettings gains	-4,392
= Current offset credit exposure	5,016
– Collateral held	-4,022
= Net credit exposure to derivatives	994

11. Market risk

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

SBAB is characterised by low risk-taking, with the Board of Directors 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 measures set by the CEO of SBAB are also subject to limitation. Through daily reports, Risk Control controls compliance with current risk levels and limits. Market risk is followed up at 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 minimised through direct funding or the use of derivatives. Foreign exchange risks are minimised as funding in foreign currency must be hedged by cross currency swaps or invested in matching currencies.

11.1 Value at Risk

VaR is a comprehensive portfolio measure 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 risk have been set at three levels: for the market risk of the entire SBAB Group portfolio, for all market risks that Treasury is responsible for managing and for the trading portfolio. The limit for market risk of the whole SBAB Group portfolio is based on the VaR measure included in the model for economic capital and applies a probability level of 99.97% and a holding period of one year, while the other two measures apply a probability level of 99% and a holding period of one day.

As per 31 December 2014, the exposure to the market risk of the whole SBAB portfolio amounted to SEK 608 million (661), compared with the SEK 1,350 million limit set by the Board of Directors. Exposure to market risks that Treasury is responsible for managing amounted to SEK 7 million (11) compared with the limit of SEK 30 million. Exposure in the trading portfolio amounted to SEK 0 million (0) compared with the limit of SEK 12 million.

11.2 Supplementary risk measures

In addition to the VaR limits determined by the Board of Directors, the CEO has set a number of supplementary risk measures 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 is measured, and curve risk, where the effect on the present value is measured in different scenarios, in which the short end of the yield curve is adjusted down (up) and the long end is adjusted up (down). Foreign exchange risk is controlled by measuring the effect on present value when foreign exchange rates change, and in the liquidity portfolio by controlling the matching of the principal amounts in each currency. There are also limits for basis-swap risk, credit spread risk and earnings volatility for basis spreads and credit spreads.

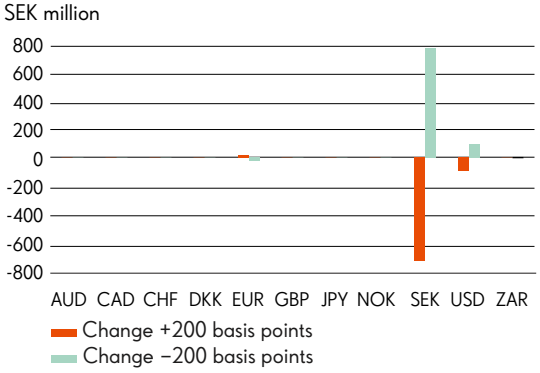
Earnings volatility for basis spreads arise because the derivatives used to hedge funding are recognised at fair value while the underlying funding is reported at the carrying amount, in accordance with the accounting standards applied by SBAB. This causes effects to arise in operating profit/loss that do not correspond to the actual risk to which SBAB's portfolio is exposed. The earnings volatility for basis spreads is expected to decrease going forward, 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.

Earnings volatility from credit spreads arise as investments in securities in the liquidity portfolio are hedged using derivatives or matched by funding with the same maturity. This means that only the underlying interest-rate risk is hedged and not the issuer-specific credit risk inherent in the securities.

11.3 Interest-rate risk in the banking book

Interest-rate risk in the banking book is measured and reported quarterly to the Swedish Financial Supervisory Authority in accordance with FFFS 2007:4. For the calculation of interest-rate risk in the banking book, a maturity of one day is assumed for non-maturity deposits. As per 31 December 2014, the effect on the present value was SEK -803 million at a parallel upward shift by 2 percentage points and SEK 841 million at a parallel downward shift by 2 percentage points. The exposure distributed by currency is presented in Figure 21.

Figure 21. Interest-rate risk in other operations in the event of a parallel shift in the yield curve by +/2 percentage points



11.4 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 "Financial assets valued at fair value through profit or loss." 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 take market risk by proprietary trading. As per 31 December 2014, there were no open positions 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 banking book. 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.

12. 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.

12.1 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 reserves. SBAB has long identified the importance of well-functioning and proactive liquidity risk management. SBAB's liquidity risk management is based on the following principles:

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 reserves

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 deductions 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 another central bank accounting for 97% of the portfolio value.

At 31 December 2014, SBAB's reserves comprised SEK 55.4 billion (reserve value at the Riksbank) in 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.

Table 30. Liquidity reserve

	December	Distribution by currency			
SEK million	**2014**	**SEK**	**EUR**	**USD**	**Other**
Cash and balances from central banks	–	–	–	–	–
Balances from other banks	–	–	–	–	–
Securities issued or guaranteed by central governments, central banks or multinational development banks	21,195	10,515	9,882	798	–
Securities issued or guaranteed by municipalities or non-governmental public sector entities	6,225	5,023	–	1,202	–
Covered bonds issued by others	31,174	24,724	4,894	1,345	211
Own covered bonds	–	–	–	–	–
Securities issued by non-financial companies	–	–	–	–	–
Securities issued by finance companies (excl. covered bonds)	–	–	–	–	–
Other securities	–	–	–	–	–
Total	**58,594**	**40,262**	**14,776**	**3,345**	**211**
Bank and loan facilities	–	–	–	–	–
Total	**58,594**	**40,262**	**14,776**	**3,345**	**211**
Distribution by currency		69%	25%	6%	0%

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 reserve primarily comprises liquid, interest-bearing securities with a high rating and is an integrated 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 on-going 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.

12.2 Liquidity-risk measurements – Short-term liquidity risk

Since 1 January 2013, SBAB is subject to the Swedish Financial Supervisory Authority Liquidity Coverage Ratio 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 pressed liquidity need. 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%, both at the total level and for EUR and USD isolated.

On 31 December 2014, the Liquidity Coverage Ratio, as defined in FFFS 2012:6, was 732% at the consolidated level, and 14751% and 349% in EUR and USD, respectively. In 2014, SBAB's liquidity coverage ratio never fell below 134%.

Internally within the SBAB Group, the liquidity risk is measured and stress tested by totalling the maximum conceivable need for liquidity for every day during the coming 365 days. 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 15 December 2014, it has been limited to a minimum of 120 days at any given time.

At 31 December 2014, the Group's survival horizon amounted to 234 days (142). In 2014, the survival horizon was never less than 105 days (57).

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% of the size of the liquidity reserve.

12.3 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 limit dependence on capital markets, deposits shall constitute at least 18% of the lending. As per 31 December 2014, deposits amounted to 23% of the lending.

SBAB mainly measures its structural liquidity risk primarily through a measure for maturity matching that 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 2014, the measure was 110% at the one-year point, compared with the limit of 90%.

In addition to this measure, structural liquidity risk is also measured through resistance to drops in house prices, which measures the extent to which SBAB can withstand a drop in house prices without the OC level in the cover pool falling below the rating companies'

requirements for Aaa ratings and through the upcoming regulatory measurement NSFR.

12.4 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 key ratios or standard measurements called the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). LCR aims to ensuring that an actor maintains unencumbered liquid assets that, if required, can be converted into cash and cash equivalents sufficient to meet its liquidity needs for a 30 day liquidity stress scenario. 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 are to be reported to the EBA as soon as the regulations come into effect, although no quantitative requirements will take immediate effect. The LCR requirement will be phased in from October 2015, when the minimum level will begin at 60%. Since SBAB is required to comply with the Swedish Financial Supervisory Authority's requirement of a Liquidity Coverage Ratio of 100%, the introduction will not have any substantial effect on SBAB. 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 expected to be exempt from the requirements at the company level.

The NSFR was reworked by the Basel Committee in 2014. 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 measures to the EBA is expected to start on 1 July 2015. 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.
- Rates for various financing maturities.
- Extension of maturing financing during the reporting period.

12.5 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 various stages that capture an increased degree of stress in order to show how a crisis can continuously worsen.

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 reduce 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.

13. 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.

13.1 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 of Directors, 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 proactively.

13.2 Self-evaluation

The self-evaluation process encompasses identification of risks in all units, measurement of identified risks and management of significant risks. The result of the self-evaluation is reported annually to the Board of Directors, 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.

13.3 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.

13.4 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.

13.5 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.

13.6 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 of Directors regarding IT.

13.7 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% of the average operating income of the business areas for the past three years. Capital requirements for operational risk are presented in Table 7, Capital requirements.

14. 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 own funds.

As the accounting standards used by SBAB require certain components of the portfolio being measured at market value while others are recognised at their carrying amount, this has effects on 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 6.5 Capital requirement due to earnings volatility.)

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