

# Report of the Board of Directors

## First half 2013

*(Consolidated figures. Figures in parentheses refer to the same period of 2012 unless otherwise stated)*

- Profit before tax: NOK 782m (661m)
- Net profit: NOK 606m (510m)
- Return on equity: 11.9 per cent (11.7 per cent)
- 12-month growth in lending: 8.4 per cent (10.6 per cent), in deposits: 7.3 per cent (12.0 per cent)
- Loan losses: NOK 38m (25m)
- Common equity tier 1 (CET1) ratio: 10.3 per cent (9.5 per cent)
- Earnings per EC: NOK 2.99 (2.63)

## Second quarter 2013

- Profit before tax: NOK 391m (328m)
- Net profit: NOK 285m (238m)
- Return on equity: 11.1 per cent (10.7 per cent)
- Loan losses: NOK 21m (17m)
- Earnings per EC: NOK 1.43 (1.22)

## Good result for first half 2013

### Highlights:

- Profit growth of NOK 96m compared with same period 2012
- Strong profit trend in core business
- Increased lending margins
- Reduced cost growth
- Low loan losses
- Strong financial position and ample funding
- High growth in lending to retail market, low growth in lending to corporate market

In the first half of 2013 SpareBank 1 SMN achieved a pre-tax profit of NOK 782m (661m). Net profit was NOK 606m (510m) and return on equity was 11.9 per cent (11.7 per cent).

Pre-tax profit for the second quarter in isolation was NOK 391m (328m). Return on equity in the quarter was 11.1 per cent (10.7 per cent).

Overall operating income in the first half-year came to NOK 1,459m (1,244m), an increase of NOK 215m compared with the first half of 2012. Both net interest income and commission income rose compared with the first half of 2012, largely as a result of higher lending margins.

Return on financial investments was NOK 211m (238m), of which the income from owner interests was NOK 137m (151m).

Group operating expenses came to NOK 850m in the first half of 2013 (795m), NOK 55m higher than in the first half of 2012.

Loan losses were NOK 38m (loss of 25m), corresponding to 0.07 per cent (0.05 per cent) of total lending.

On a 12-month basis lending growth was 8.4 per cent (10.6 per cent) and deposit growth was 7.3 per cent (12.0 per cent) in the first half of 2013. Total lending growth in the first half-year was 3.9 per cent (5.6 per cent) and total deposit growth was in the same period was 5.8 per cent (7.6 per cent).

The common equity tier 1 ratio at 30 June 2013 was 10.3 per cent (9.5 per cent). On 22 March 2013 the Ministry of Finance published a proposal for new capital requirements, a timetable for implementation as well as various alternatives for new home mortgage loan weights. Future requirements on CET1 capital will depend on the economic situation and whether the bank concerned is considered systemically critical. SpareBank 1 SMN plans to increase the CET1 ratio to 14.5 per cent by 1 July 2016. The capital plan and underlying assumptions are further described in the section on financial strength.

At the half-year mark the Bank's ECC was priced at NOK 46.50 (34.80 at end-2012). A cash dividend of NOK 1.50 per ECC was paid out for the year 2012 in the second quarter.

In the first half-year earnings per EC were NOK 2.99. The book value per EC at 30 June 2013 was NOK 51.66.

### Increased net interest income

Net interest income in the first half-year came to NOK 746m (720m). Net interest income strengthened substantially in the second quarter due to interest rate increases on loans to both retail and corporate customers. Margins on loans transferred to SpareBank 1 Boligkreditt and SpareBank 1 Næringskreditt are recognised as commission income, not as interest income. Margins on loans transferred to these two mortgage companies improved substantially compared with the first half of 2012 due to repricing, and commissions totalled NOK 188m (74m).

Lending margins rose as a result of increased capital requirements for Norwegian banks, bringing higher costs of equity capital.

By the end of the first half of 2013, home mortgage loans worth NOK 29.4bn (26.2bn) had been sold to SpareBank 1 Boligkreditt. Sales of loans to SpareBank 1 Næringskreditt started in 2012, and as of 30 June 2013 NOK 611m had been sold to this company.

From 2013 onwards banks are required to pay a levy to the Banks' Guarantee Fund. For SpareBank 1 SMN the levy for the first half-year comes to NOK 26m, and for the full year 2013 to NOK 52m.

### Increased commission income

Commission income and other operating income rose by NOK 190m, or 36 per cent, to total NOK 713m in the first half of 2013 (524m). The increase is mainly due to growth in income from SpareBank 1 Boligkreditt resulting from higher margins on home mortgage loans. In addition, a positive trend was seen above all in income from payment services, accountancy services and guarantee commissions.

	30 Jun 2013	30 Jun 2012	Change
<b>Commission income, NOKm</b>			
Payment transfers	107	94	13

Savings	21	21	0
Insurance	60	59	1
SpareBank 1 Boligkreditt and Næringskreditt	188	75	113
Guarantee commission	30	14	16
Real estate agency	174	166	7
Accountancy services	73	52	21
Active management	6	5	1
Income from new head office	22	17	5
Other commissions	32	22	11
<b>Total</b>	<b>713</b>	<b>524</b>	<b>190</b>

### Positive return on financial investments

Overall return on financial investments (excluding the Bank's share of the profit/loss of affiliates and joint ventures) was NOK 74m (87m).

Net gains (incl. dividends of NOK 31m) on the Group's share portfolios totalled NOK 26m in the first half of 2013 (net loss of 10m).

Total gains on bonds and derivatives in the first half-year came to NOK 5m (38m). Gains on bonds and financial instruments at SpareBank 1 SMN Markets amounted to NOK 42m (59m).

	30 Jun 2013	30 Jun 2012
<b>Capital gains/dividends, shares</b>		
Capital gains/dividends, shares	26	-10
Bonds and derivatives	5	38
SpareBank 1 SMN Markets	42	59
<b>Net return on financial investments</b>	<b>74</b>	<b>87</b>
SpareBank 1 Gruppen	79	60
SpareBank 1 Boligkreditt	13	25
SpareBank 1 Næringskreditt	3	5
BN Bank ASA	43	27
Other jointly controlled companies	0	34
<b>Income from investment in related companies</b>	<b>137</b>	<b>151</b>
<b>Total</b>	<b>211</b>	<b>238</b>

### SpareBank 1 Gruppen

SpareBank 1 Gruppen's post-tax profit for the first half of 2013 was NOK 402m (263m). The main contributors were SpareBank 1 Livsforsikring (life insurer) and SpareBank 1 Skadeforsikring (non-life insurer), although the latter's result in the second quarter was weakened as a result of natural damage. The value of shares at SpareBank 1 SMN Markets was written down by NOK 122m in the second quarter (see *separate section below*).

SpareBank 1 SMN's share of the profit was NOK 79m (60m).

### Strengthened owner focus at SpareBank 1 Markets

SpareBank 1 Markets, whose main shareholder was previously SpareBank 1 Gruppen, is to acquire a new ownership structure. This involves SpareBank 1 Gruppen's disposal of its holding in the company. SpareBank 1 Markets will henceforth be owned directly by SpareBank 1 SMN (24 per cent), SpareBank 1 Nord Norge (24 per cent), SpareBanken Hedmark (15 per cent), Samspar (24 per cent), Norwegian Confederation of Trade Unions (12 per cent) and employees (2 per cent).

Stronger collaboration will be put in place between the banks and SpareBank 1 Markets. This will include integration of the owner banks' corporate finance and stockbroking units with corresponding areas in

SpareBank 1 Markets. In addition, the banks' business volumes will be internalised to a greater degree. This, together with other measures, will promote profitability for SpareBank 1 Markets and the banks alike.

In connection with the change in owner structure, SpareBank 1 Gruppen has written down its holding in SpareBank 1 Markets by NOK 122m. SpareBank 1 SMN's portion of this write-down is NOK 23.8m.

### **SpareBank 1 Boligkreditt**

SpareBank 1 Boligkreditt was established by the banks participating in the SpareBank 1 Alliance to assure funding through the market for covered bonds. The banks sell their highest quality home mortgage loans to the company, thereby reducing funding costs and enhancing competitiveness.

The Bank's ownership interest in SpareBank 1 Boligkreditt is 18.4 per cent, and the Bank's share of that company's profit in the first half of 2013 was NOK 13m (25m). The Bank's ownership interest reflects the Bank's relative share of total home mortgage loans transferred to SpareBank 1 Boligkreditt by the end of 2012.

### **SpareBank 1 Næringskreditt**

The SpareBank 1 banks established SpareBank 1 Næringskreditt in the second quarter of 2009 along the same lines, and with the same administration, as SpareBank 1 Boligkreditt.

SpareBank 1 SMN's stake in the company is 33.8 per cent, and the Bank's share of the company's profit in the first half of 2013 was NOK 3m (5m). The Bank's ownership interest mainly reflects SpareBank 1 SMN's stake in BN Bank.

### **BN Bank**

SpareBank 1 SMN has a 33 per cent stake in BN Bank as of 30 June 2013. SpareBank 1 SMN's share of the profit of BN Bank in the first half-year was NOK 43m (27m), including amortisation effects. The amortisation effect increased the profit by NOK 4.8m (5.4m). BN Bank has repriced its loan portfolios in 2013 while reducing the rate of growth in lending to commercial property.

### **Other companies**

As of 30 June 2013 this includes figures for SpareBank 1 Kredittkort and SpareBank 1 Verdipapirservice, as well as companies established to handle corporate exposures taken over from other entities. Last year's figures also include SpareBank 1 SMN's profit shares in Bank 1 Oslo Akershus and Polaris Media.

### **Bank 1 Oslo Akershus**

At the start of the current year SpareBank 1 SMN signed an agreement to sell 475,594 shares to Sparebanken Hedmark. The sale, which was formally completed in the second quarter of 2013, reduced SpareBank 1 SMN's holding in Bank 1 Oslo Akershus to 4.78 per cent. Further, an option was taken on a further reduction of the Bank's holding in Bank 1 Oslo Akershus. The option must be exercised by 31 December 2015.

### **Polaris Media**

The Group's investment in Polaris Media is recognised at fair value. Goodwill in Polaris Media's balance sheet previously enabled a reduction in SpareBank 1 SMN's capital ratio. Reducing this holding strengthened the Bank's tier 1 capital by NOK 175m in the first quarter of 2013.

**Operating expenses**

Total expenses came to NOK 850m (795m) in the first half of 2013. Group expenses rose by NOK 55m or 6.9 per cent in the last 12 months.

Parent bank cost growth was NOK 18m or 3.1 per cent. This is in keeping with the parent bank's cost ambitions.

The Board of Directors has a tight focus on cost-reducing measures whose goal for 2013 is to bring down cost growth across the Group to below 3 per cent. The Board has decided on a reduction of at least 75 FTEs at the parent bank in the period to 2015. The number of permanent FTEs was reduced by 20 to 772 in the first half of 2013.

Overall cost growth among the subsidiaries was NOK 36m or 18.6 per cent. NOK 20m of the growth was at SpareBank 1 SMN Regnskap, relating in all essentials to an increased cost base due to acquisition of local accountancy firms.

Operating expenses measured 1.54 per cent (1.55 per cent) of average total assets. The Group's cost-income ratio was 51 per cent (54 per cent).

**Low losses and low defaults**

Loan losses came to NOK 38m (25m) in the first half of 2013.

Net losses of NOK 32m (loss of 23m) were recorded on the corporate customer portfolio in the first half of 2013, including losses at SpareBank 1 SMN Finans of NOK 6m (1m). A net loss of NOK 6m (2m) was recorded on the retail portfolio in the first half of 2013.

Individually assessed loan impairment write-downs in the first half of 2013 totalled NOK 153m (166m).

Total problem loans (defaulted and doubtful) came to NOK 559m (537m), or 0.51 per cent (0.53 per cent) of gross outstanding loans as of end-June 2013.

Defaults in excess of 90 days totalled NOK 413m (338m). Defaults measured 0.38 per cent (0.34 per cent) of gross lending. Defaults on the corporate portfolio totalled NOK 277m (207m) and on the retail portfolio NOK 136m (131m). Individually assessed write-downs on defaulted exposures came to NOK 89m (99m) or 22 per cent (29 per cent).

Other doubtful exposures totalled NOK 146m (199m), breaking down to NOK 131m (187m) on the corporate market and NOK 15m (12m) on the retail market. Other doubtful exposures measure 0.13 per cent (0.20 per cent) of gross lending. Individually assessed write-downs on these exposures totalled NOK 64m (67m) or 44 per cent (34 per cent).

**Collectively assessed impairment write-downs**

Collective assessment of impairment write-downs is based on two factors:

- events that have affected the Bank's portfolio (causing migration between risk categories)
- events that have not yet affected the portfolio since the Bank's credit risk models do not capture the effects rapidly enough (e.g. significant changes in macroeconomic factors)

In the first half of 2013 no basis was found for any change in collectively assessed impairment write-downs in the Group. The aggregate volume of such write-downs is accordingly NOK 295m (290m).

### Total assets of NOK 113.2bn

The Group's assets totalled NOK 113.2bn as of mid-2013 (107.8bn), having risen by NOK 5.4bn or 5 per cent in the last 12 months. The increase is ascribable to increased lending and increased liquidity reserves.

As of mid-2013 home mortgage loans worth 29.4bn (26.2bn) had in addition been transferred to SpareBank 1 Boligkreditt and commercial loans worth NOK 611m to SpareBank 1 Næringskreditt. These loans do not figure as lending in the Bank's balance sheet. The comments covering lending growth do however include loans sold to SpareBank 1 Boligkreditt and SpareBank 1 Næringskreditt.

### Reduced growth in lending to the corporate market and demand for mortgages remains high.

In the last 12 months, total outstanding loans rose by NOK 8.4bn (9.6bn) or 8.4 per cent (10.6 per cent) to reach NOK 109bn (including SpareBank 1 Boligkreditt) by mid-year. Growth in the first half in isolation was 3.9 per cent (5.6 per cent).

Lending to retail customers rose by NOK 8.1bn (5.6bn) or 14.0 per cent (10.8 per cent) to reach NOK 65.8bn in the last 12 months. Growth in the first half-year in isolation was 5.2 per cent (4.9 per cent).

Growth in 12-month lending to corporates in the last 12 months was NOK 0.3bn (4.0bn) or 0.7 per cent (10.2 per cent). Overall loans to corporates came to NOK 43.1bn as of mid-2013. Growth in lending to corporates in the first half-year was 1.9 per cent (6.5 per cent).

Lending to retail customers accounted for 60 per cent (57 per cent) of ordinary loans to customers as of mid-2013.

Total customer deposits rose by NOK 3.8bn (5.5bn) in the last 12 months to NOK 55.3bn as of mid-2013. This corresponds to a growth of 7.3 per cent (12.0 per cent). Growth in deposits in the first half of 2013 was 5.8 per cent (7.6 per cent).

Retail customer deposits rose in the same period by NOK 2.0bn (1.8bn) or 8.7 per cent (8.6 per cent) to reach NOK 24.4bn, while deposits from corporates rose by NOK 1.8bn (3.7bn) or 6.2 per cent (14.8 per cent) to reach NOK 30.9bn. In the first half-year deposit growth at Retail Market and Corporate Market was, respectively, 9.5 per cent (7.5 per cent) and 3.0 per cent (7.6 per cent).

### Investment products

The overall customer portfolio of off-balance sheet investment products totalled NOK 4.6bn (4.3bn) as of mid-2013, up 6 per cent over the last 12 months. The increase is largely related to changes in the value of underlying securities.

<b>Saving products, customer portfolio, NOKm</b>	<b>30 Jun 2013</b>	<b>30 Jun 2012</b>	<b>Change</b>
Equity funds	2,839	2,462	377
Pension products	573	1,055	-482
Active management	1,027	989	38
Energy fund management	111	170	-59
<b>Total</b>	<b>4,550</b>	<b>4,676</b>	<b>-126</b>



**Insurance products**

The Bank's insurance portfolio grew by 8 per cent in the last 12 months, and the premium volume totalled NOK 1,053m as of 30 June 2013 (968m). Non-life insurance rose by 5 per cent, personal insurance by 7 per cent and the occupational pension segment by 28 per cent.

<b>Insurance, premium volume, NOKm</b>	<b>30 Jun 2013</b>	<b>30 Jun 2012</b>	<b>Change</b>
Non-life insurance	690	656	34
Personal insurance	188	175	13
Occupational pensions	175	137	38
<b>Total</b>	<b>1,053</b>	<b>968</b>	<b>85</b>

**Offices (Retail Market and SMBs)**

As from 2013 the retail market business and the SMB segment comprise a unit in its own right. SMBs were previously a part of the corporate business. Retail Market and SMBs are each commented on separately. The SMB segment consists of corporate customers with an exposure size of +/- NOK 8m and agricultural customers. Owing to the reorganisation, historical data for the SMB segment are not recreated and no comparison is made with last year's figures. Return on equity in the first half-year for the retail business and SMB segment in total was 31.8 per cent with 31.9 per cent (16.2 per cent) reported by the retail business and 31.5 per cent by the SMB segment. Return for Retail Market is calculated using existing risk weights on home mortgage loans. Risk weights on home mortgage loans are expected to increase considerably.

**Retail Market**

Operating income – and return on equity – have risen substantially owing to increased margins on home mortgage loans, both on the Bank's own books and on home mortgages transferred to SpareBank 1 Boligkreditt, and totalled NOK 601m (464m) in the first half of 2013. Net interest income came to NOK 291m (259m) and commission income to NOK 310m (205m).

The lending margin in the first half of 2013 was 2.37 per cent (1.70 per cent), while the deposit margin was -0.31 per cent (0.25 per cent) (measured against three-month Nibor).

In the last 12 months, lending to retail customers rose by 14.0 per cent (11.7 per cent) and deposits from the same segment by 8.7 per cent (10.8 per cent).

Lending to retail borrowers generally carries low risk, as reflected in continued very low losses. Losses and defaults are expected to remain low. The loan portfolio is secured on residential properties, and the trend in house prices has been satisfactory throughout the market area.

**SMB segment**

Operating income totalled NOK 179m, comprising net interest income of NOK 140m and commission income of NOK 39m.

The lending margin measured against three-month Nibor in the first half-year was 3.32 per cent and the deposit margin was -0.22 per cent.

SMB customers have loan capital totalling NOK 8.8bn and deposit capital totalling NOK 8.6bn. Growth in loans and deposits respectively in the first half of 2013 was 3.7 per cent and 1.3 per cent.



## Group customers

In connection with the reorganisation of the Bank as from 2013, SMB customers have been separated out from the previous Corporate Market Division and the segment has changed name to Group Customers.

Group customers are mainly customers with exposure sizes in excess of NOK 8m. Given the organisation changes, historical data on group customers are incomplete.

Return on equity for group customers was 10.0 per cent in the first half-year. For the entire corporate market business (SMBs and Group Customers), return on equity in the first half of 2012 was 13.8 per cent.

Total operating income for Group Customers was NOK 397m in the first half of 2013. Net interest income was NOK 344m, while total commission income was NOK 53m including NOK 11m in income on forex and fixed-income business.

Lending and deposit margins for Group Customers were, respectively, 2.72 per cent and -0.62 per cent. Lending growth for Group Customers in the first half of 2013 was 0.9 per cent and deposit growth was 10.8 per cent. For corporates overall (Group customers and SMBs) the lending margin was 2.85 per cent (2.39 per cent) and the deposit margin was -0.49 per cent (0.05 per cent).

12-month growth for corporates overall (Group customers and SMBs) was 4.6 per cent (7.9 per cent) and deposit growth was 13.0 per cent (9.5 per cent).

## SpareBank 1 SMN Markets

SpareBank 1 Markets delivers a complete range of capital market products and services and is an integral part of SMN's parent bank operation.

SpareBank 1 Markets reported total income of NOK 56.3m (66.2m) in the first half of 2013.

Markets (NOKm)	30 Jun 2013	30 Jun 2012	Change
Currency trading	39.2	54.1	-14.9
Corporate	11.1	5.2	5.9
Securities, brokerage commission	15.4	8.8	6.6
SpareBank 1 Markets	-2.5	0.5	-3.0
Investments	-6.9	-2.4	-4.5
<b>Total income</b>	<b>56.3</b>	<b>66.2</b>	<b>-9.9</b>

*Of gross income of NOK 56.3m, NOK 11m is transferred to Group Customers and NOK 1m to SMBs. These amounts are Group Customers' and SMBs' share of income and fixed-income business derived from their own customers. NOK 2.2m of the corporate income refers to services sold to the parent bank.*

## Subsidiaries

The subsidiaries posted an aggregate pre-tax profit of NOK 100m (66m) in the first half of 2013.

Pre-tax profit, NOKm	30 Jun 2013	30 Jun 2012	Change
EiendomsMegler 1 Midt-Norge	41.5	41.9	-0.4
SpareBank 1 SMN Finans	29.1	30.3	-1.2
SpareBank 1 SMN Regnskap	12.1	8.6	3.5
Allegro Finans	-0.7	-1.3	0.6
SpareBank 1 SMN Invest	19.2	-1.7	20.9
Other	-1.0	-12.1	13.1
<b>Total</b>	<b>100.2</b>	<b>65.6</b>	<b>36.5</b>

*The above results show the companies' comprehensive income. The Bank's stake in Eiendomsmeidler 1 is 86.7 per cent, in SpareBank 1 SMN Finans 90.1 per cent and in Allegro 90.1 per cent. Its stake in the other companies is 100 per cent.*

**Eiendomsmeidler 1 Midt-Norge** leads the field in its catchment area with a market share of about 40 per cent. The company posted an excellent profit performance in 2012 and has also recorded a strong first half of 2013 with a pre-tax profit of NOK 41.5m (41.9m).

**SpareBank 1 SMN Finans** posted a first-half profit of NOK 29.1m (30.3m) in the first half-year. At quarter-end the company managed leases and car loan agreements worth a total of NOK 3.1bn of which leases account for NOK 1.8bn.

SpareBank 1 Nordvest and SpareBank 1 Søre Sunnmøre took over by agreement 9.9 per cent of the shares of SpareBank 1 SMN Finans in the fourth quarter 2012.

**SpareBank 1 SMN Regnskap** posted a pre-tax profit of NOK 12.1m (8.6m).

SpareBank 1 SMN Regnskap took over five accounting firms over the course of 2012 and aspires to continued strong growth. With a growth rate three times higher than the industry average, the company is market leader in Mid-Norway and among the leading accounting operations in Norway. It has in addition acquired a strategic owner position of 40 per cent in the accounting chain Consis. The company's alliance partner Sparebanken Hedmark owns the other 60 per cent.

In collaboration with other SpareBank 1 banks, SpareBank 1 SMN Regnskap has launched a nationwide drive in the accounting business through SpareBank 1 Regnskapshuset. SpareBank 1 Regnskapshuset intends to be one of Norway's leading actors in the accounting industry. Together the SpareBank 1 banks will build up a national accounting enterprise built on regional ownership, strong links to the owner banks and closeness to the market.

**Allegro Finans** reported a pre-tax loss of NOK 0.7m (loss of 1.3m) in the first half-year. The company has a portfolio of some NOK 2.8bn under active management.

**Sparebanken SMN Invest's** mission is to invest in shares, mainly in regional businesses. The company posted a first-half net profit of NOK 19.2m (loss of 1.7m). The result is entirely related to value changes and realisation of losses or gains on the company's overall shareholding.

### **Satisfactory funding and ample liquidity**

The Bank has a conservative liquidity strategy. The strategy attaches importance to maintaining liquidity reserves that ensure the Bank's ability to survive for 12 months carrying on ordinary operations without need of fresh external funding.

The Bank has liquidity reserves of NOK 23bn and thus has the funding needed for 18 months of ordinary operations without fresh external finance.

The Bank's funding sources and products are amply diversified. At year-end the proportion of money market funding in excess of 1 year was 68 per cent (71 per cent).

SpareBank 1 Boligkreditt is the Bank's chief source of funding. As of 30 June 2013 loans totalling NOK 29.4bn had been transferred to SpareBank 1 Boligkreditt.

In the first quarter of 2013 SpareBank 1 SMN raised a five-year loan of EUR 500bn. The loan is spread across about 180 investors in Europe and Asia. The loan was raised in order for the bank to broaden its geographical spread of funding sources and thereby reduce its funding risk.

### Rating

SpareBank 1 SMN has a rating of A2 (stable) with Moody's and a rating of A- (stable outlook) with Fitch Ratings. The bank was downgraded by Moody's from A1 to A2 (under review) in December. In the first quarter of 2013 this was changed to A2 (stable).

### Financial strength

As of 31 March 2013 the CET1 capital ratio was 10.3 per cent (9.5 per cent). CET1 capital is tier 1 capital excluding hybrid capital.

The Group has shifted lending growth more over to the retail customer segment. Due to this transitional rules in the capital requirements regulations has resulted in growth in the regulatory need of capital.

Tier 1 capital adequacy is strengthened as a result of hybrid capital worth NOK 500m raised in June 2013.

Figures in NOKm	30 Jun 2013	30 Jun 2012
Tier 1 capital	8,882	7,592
Hybrid capital	1,625	1,130
<b>Subordinated loan</b>	<b>1,386</b>	<b>1,178</b>
<b>Capital base</b>	<b>11,894</b>	<b>9,900</b>
<b>Required subordinated debt</b>	<b>6,886</b>	<b>6,371</b>
<b>Risk weighted assets</b>	<b>86,079</b>	<b>79,635</b>
<b>Tier 1 capital ratio</b>	<b>10.3 %</b>	<b>9.5 %</b>
<b>Core capital ratio</b>	<b>12.2 %</b>	<b>11.0 %</b>
<b>Capital adequacy ratio</b>	<b>13.8 %</b>	<b>12.4 %</b>

On 22 March 2013 the Ministry of Finance published a proposal for new capital requirements, a timetable for implementation as well as various alternatives for home mortgage loan weights. All in all these proposals entail a tighter regime than was expected. Although there is uncertainty regarding several of the buffers, the Board of Directors of SpareBank 1 SMN has determined that planning must be on the assumption that all buffers must be in place by 1 July 2016. The objective is a CET1 capital ratio of 14.5 per cent by 1 July 2016.

The following measures will be put in place:

- Improved banking operation through improved efficiency and higher margins. Increased capital requirements for all banks provide a market basis for increased margins on lending
- A dividend policy as for 2012 with an effective payout of 25 – 35 per cent
- Moderate growth in the Bank's asset-intensive activities, including lending to the retail and corporate segments by the parent bank and BN Bank
- Sale of asset items not forming part of the core business
- Introduction of the advanced IRB approach at SpareBank 1 SMN and BN Bank

SpareBank 1 SMN currently has no plans with regard to equity capital issues.

The Bank is IRB(Internal Ratings-based), approved and uses the IRB foundation approach to compute capital charges for credit risk.

In June 2013 SpareBank 1 SMN applied to Finanstilsynet (Norway's FSA) for permission to use the advanced IRB approach to compute capital charges. Preparatory work on the application was done in conjunction with the other banks in the SpareBank 1 alliance.

### **The Bank's equity certificate (MING)**

The book value of the Bank's EC was NOK 51.66 as of 30 June 2013, and earnings per EC were NOK 2.99.

As of 30 June 2013 the price was NOK 46.50, and dividend of NOK 1.50 per EC was paid in 2013 for the year 2012.

The Price / Income ratio was 7.79, and the Price / Book ratio was 0.90 as of 30 June 2013.

### **Risk factors**

The credit quality of the Bank's loan portfolio is satisfactory, and loss and default levels are low.

The Bank expects the cyclical upturn to continue but to be somewhat weaker than previously assumed. This is on the expectation of moderate activity growth resulting from very weak international growth impulses. We expect continued low Norwegian unemployment which, combined with continued good income growth and low interest rates, suggests that the loss risk in the Bank's retail market portfolio will remain low. Credit demand from Norwegian households still outstrips wage growth and will in large measure be influenced by house price developments. The Bank assumes that a margin increase on home mortgage loans, resulting from higher capital requirements, could have a damping effect on house price developments. The Bank also expects moderate growth in mid-Norway's business sector ahead.

Increasing capital requirements combined with uncertainty particularly with regard to the Norwegian authorities' handling of the countercyclical buffer and possible continuation of the floor, suggests that Norwegian banks will adopt a more conservative credit policy towards the business sector.

The Bank's results are affected directly and indirectly by fluctuations in the securities markets. The indirect effect relates above all to the Bank's stake in SpareBank 1 Gruppen, where both the insurance business and asset management activities are affected by the fluctuations.

The Bank is also exposed to risk related to access to external funding. This is reflected in the Bank's conservative liquidity strategy (see the above section on funding and liquidity).

### **Outlook ahead**

The profit performance in the first half of 2013 was satisfactory, and it is particularly worthwhile to highlight the good trend in the core business. The Group's funding is robust. This is in keeping with the Directors' ambitions.

The Board of Directors has a keen focus on measures designed to strengthen the Bank's financial position so as to ensure that it attains a CET1 ratio of at least 14.5 per cent by 1 July 2016.

The Board has focus on the Group's cost trend and will continually assess further cost-reducing measures.

SpareBank 1 SMN has thus far not seen clear indications of the region's business sector being affected by the crisis in the euro area. The turbulence in international financial markets increases the uncertainties in the national and regional economies. However, business life in the Bank's market area shows continued growth

and sound profits, and the outlook for 2013 remains good. Unemployment is low, and there are few signs in the region's macroeconomy in isolation to suggest major changes in the risk picture for 2013 as a whole.

SpareBank 1 SMN has a conservative liquidity strategy and intends to be able to maintain normal operations for a minimum of 12 months without further access to external funding. The Board of Directors considers pressures in the funding market to be lighter in 2013 than in 2012.

The Board of Directors is satisfied with the Group's profit performance for the first half of 2013 and expects good results in the second half-year too.

Trondheim, 14. August  
The Board of Directors of SpareBank 1 SMN

Kjell Bordal  
(chair)

Bård Benum  
(deputy chair)

Paul E. Hjelm-Hansen

Aud Skrudland

Morten Loktu

Bente Karin Trana

Arnhild Holstad

Venche Johnsen  
(employee rep.)

Finn Haugan  
(Group CEO)