

Note 4 - Capital adequacy

SpareBank 1 SMN utilises the Internal Rating Based Approach (IRB) for credit risk. Use of IRB imposes wide-ranging requirements on the bank's organisational set-up, competence, risk models and risk management systems. As from 31 March 2015 the bank has received permission to apply the Advanced IRB Approach to those corporate portfolios that were previously reported under the Basic Indicator Approach.

As of 31 March 2018 the capital conservation buffer requirement is 2.5 per cent, the systemic risk requirement is 3.0 per cent and the Norwegian countercyclical buffer is 2.0 per cent. These requirements are additional to the requirement of 4.5 per cent CET1 capital, so that the overall minimum requirement on CET1 capital is 12.0 per cent. In addition the financial supervisory authority has set a Pillar 2 requirement of 2.1 per cent for SpareBank 1 SMN. The total minimum requirement on CET1 capital is accordingly 14.1 per cent.

Historical figures are restated due to an error found in the treatment of the share of the fund for unrealised gains from related companies. This reduces the reported common equity tier 1 (CET1) capital. A correction for the fourth quarter of 2017 is also made to repurchase agreements and collaterals related to the calculation of capital charges for the transitional arrangement (Basel 1 floor), entailing an increase in risk weighted assets compared to the originally reported figure. The CET1 capital ratio is accordingly revised from 14.9 per cent to 14.6 per cent as at 31 December 2017.

The countercyclical buffer increased from 1.5 per cent to 2.0 per cent with effect from 31 December 2017.

Countercyclical buffer is calculated using differentiated rates. For exposures in other countries the countercyclical buffer rate set by the authorities in the country concerned is applied. If that country has not set a rate, the same rate as for exposures in Norway is applied unless the Ministry of Finance sets another rate. For the first quarter of 2018 the parent bank is below the capital deduction threshold such that the Norwegian rate is applied to all relevant exposures. For the group, the risk-weighted countercyclical capital buffer is 2.0 per cent.

Parts of the group's hybrid capital and subordinated debt were issued under earlier rules. This will be subject to a write-down of 50 per cent in 2017 and 60 per cent in 2018. As at 31 March 2018 the bank held hybrid capital worth NOK 450 million subject to write-down. For subordinated debt the figure was NOK 659 million.

| Parent Bank | | | | Group | | |
|--|---------------|---------------|---|---------------|---------------|---------------|
| 31 Dec 2017 | 31 Mar 2017 | 31 Mar 2018 | (NOKm) | 31 Mar 2018 | 31 Mar 2017 | 31 Dec 2017 |
| 15,372 | 13,837 | 15,118 | Total book equity | 17,365 | 16,269 | 17,510 |
| -950 | -941 | -1,264 | Additional Tier 1 capital instruments included in total equity | -1,306 | -1,208 | -993 |
| -522 | -475 | -520 | Deferred taxes, goodwill and other intangible assets | -1,040 | -853 | -984 |
| - | - | - | Part of reserve for unrealised gains, associated companies | - | - | - |
| -893 | - | - | Deduction for allocated dividends and gifts | - | - | -893 |
| - | - | - | Non-controlling interests recognised in other equity capital | -572 | -443 | -565 |
| - | - | - | Non-controlling interests eligible for inclusion in CET1 capital | 341 | 223 | 324 |
| - | -279 | -341 | Net profit | -466 | -358 | - |
| - | 100 | 108 | Year-to-date profit included in core capital (50 per cent pre tax of group profit in 2018) | 233 | 179 | - |
| -30 | -30 | -28 | Value adjustments due to requirements for prudent valuation | -45 | -48 | -41 |
| -350 | -186 | -326 | Positive value of adjusted expected loss under IRB Approach | -313 | -247 | -333 |
| - | - | - | Cash flow hedge reserve | 3 | 8 | 7 |
| - | - | - | Deduction for common equity Tier 1 capital in significant investments in financial institutions | -222 | -188 | -212 |
| 12,627 | 12,026 | 12,748 | Total common equity Tier one | 13,976 | 13,332 | 13,820 |
| 950 | 950 | 876 | Additional Tier 1 capital instruments | 1,353 | 1,358 | 1,427 |
| 459 | 459 | 367 | Additional Tier 1 capital instruments covered by transitional provisions | 367 | 459 | 459 |
| 14,036 | 13,435 | 13,991 | Total core capital | 15,697 | 15,149 | 15,707 |
| Supplementary capital in excess of core capital | | | | | | |
| 1,000 | 1,000 | 1,000 | Subordinated capital | 1,621 | 1,710 | 1,615 |
| 561 | 561 | 449 | Subordinated capital covered by transitional provisions | 449 | 561 | 561 |
| -254 | -237 | -248 | Deduction for significant investments in financial institutions | -248 | -237 | -254 |
| 1,307 | 1,324 | 1,201 | Total supplementary capital | 1,822 | 2,034 | 1,922 |
| 15,343 | 14,758 | 15,192 | Net subordinated capital | 17,518 | 17,183 | 17,629 |

| | | | | | | |
|---------------|---------------|---------------|---|---------------|---------------|---------------|
| | | | Minimum requirements subordinated capital | | | |
| 978 | 1,055 | 1,075 | Specialised enterprises | 1,200 | 1,186 | 1,107 |
| 1,098 | 1,087 | 1,058 | Corporate | 1,070 | 1,126 | 1,113 |
| 1,370 | 1,277 | 1,375 | Mass market exposure, property | 1,930 | 1,769 | 1,892 |
| 90 | 88 | 89 | Other mass market | 92 | 91 | 91 |
| 1,198 | 1,267 | 1,218 | Equity investments | 1 | 1 | 1 |
| 4,733 | 4,773 | 4,815 | Total credit risk IRB | 4,292 | 4,173 | 4,205 |
| 3 | 5 | 3 | Central government | 3 | 5 | 3 |
| 80 | 78 | 81 | Covered bonds | 142 | 134 | 146 |
| 429 | 452 | 406 | Institutions | 281 | 375 | 331 |
| 0 | 5 | - | Local and regional authorities, state-owned enterprises | 7 | 10 | 4 |
| 44 | 45 | 66 | Corporate | 256 | 149 | 245 |
| 1 | 0 | 1 | Mass market | 403 | 380 | 388 |
| 13 | 14 | 13 | Exposures secured on real property | 199 | 328 | 193 |
| 232 | 211 | 232 | Equity positions | 349 | 348 | 344 |
| 70 | 73 | 46 | Other assets | 150 | 163 | 166 |
| 872 | 885 | 848 | Total credit risk standardised approach | 1,791 | 1,891 | 1,820 |
| 16 | 34 | 23 | Debt risk | 25 | 35 | 18 |
| - | - | - | Equity risk | 14 | 15 | 22 |
| - | - | - | Currency risk and risk exposure for settlement/delivery | 4 | 1 | 1 |
| 341 | 341 | 370 | Operational risk | 575 | 510 | 510 |
| 52 | 56 | 52 | Credit value adjustment risk (CVA) | 119 | 119 | 117 |
| - | - | - | Transitional arrangements | 863 | 523 | 891 |
| 6,015 | 6,088 | 6,108 | Minimum requirements subordinated capital | 7,684 | 7,268 | 7,585 |
| 75,182 | 76,101 | 76,355 | Risk weighted assets (RWA) | 96,044 | 90,845 | 94,807 |
| 3,383 | 3,425 | 3,436 | Minimum requirement on CET1 capital, 4.5 per cent | 4,322 | 4,088 | 4,266 |
| | | | Capital Buffers | | | |
| 1,880 | 1,903 | 1,909 | Capital conservation buffer, 2.5 per cent | 2,401 | 2,271 | 2,337 |
| 2,255 | 2,283 | 2,291 | Systemic risk buffer, 3.0 per cent | 2,881 | 2,725 | 2,804 |
| 1,504 | 1,142 | 1,527 | Countercyclical buffer, 2.0 per (1.5 per cent) | 1,921 | 1,363 | 1,869 |
| 5,639 | 5,327 | 5,727 | Total buffer requirements on CET1 capital | 7,203 | 6,359 | 7,011 |
| 3,605 | 3,274 | 3,586 | Available CET1 capital after buffer requirements | 2,451 | 2,885 | 2,544 |
| | | | Capital adequacy | | | |
| 16.8 % | 15.8 % | 16.7 % | Common equity Tier one ratio | 14.6 % | 14.7 % | 14.6 % |
| 18.7 % | 17.7 % | 18.3 % | Core capital ratio | 16.3 % | 16.7 % | 16.6 % |
| 20.4 % | 19.4 % | 19.9 % | Capital adequacy ratio | 18.2 % | 18.9 % | 18.6 % |
| | | | Leverage ratio | | | |
| 145,821 | 137,192 | 143,334 | Balance sheet items | 207,831 | 199,551 | 210,764 |
| 7,112 | 7,402 | 7,418 | Off-balance sheet items | 9,530 | 9,292 | 9,295 |
| -902 | -691 | -1,341 | Regulatory adjustments | -2,113 | -1,346 | -1,580 |
| 152,032 | 143,903 | 149,410 | Calculation basis for leverage ratio | 215,248 | 207,497 | 218,479 |
| 14,036 | 13,435 | 13,991 | Core capital | 15,697 | 15,149 | 15,707 |
| 9.2 % | 9.3 % | 9.4 % | Leverage Ratio | 7.3 % | 7.3 % | 7.2 % |