

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. The EU capital adequacy framework (CRR/CRDIV) was incorporated into Norwegian law with effect from 31 December 2019. The Basel I floor was accordingly removed and an SME rebate introduced.

As of 30 June 2020 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 1.0 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 11.0 per cent. In addition the financial supervisory authority has set a Pillar 2 requirement of 1.9 per cent for SpareBank 1 SMN, however not below NOK 1,794 million in monetary terms. The total minimum requirement on CET1 capital is accordingly 12.9 per cent. The countercyclical capital buffer was reduced with immediate effect in March 2020 from 2.5 per cent to 1.0 per cent. The systemic risk buffer will rise to 4.5 per cent with effect from 31 December 2020.

The Supervisory Board adopted at its meeting on 26 March 2020 a revised proposal for application of the net profit for 2019 entailing an overall reduction of 303 NOK million compared with the original proposal of NOK 1,314 million for distribution as dividends and donations. Historical figures as at 31 December 2019 are not restated, but the effect of the above decision as at 31 December 2019 is shown in the table below.

The 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 half of 2020 the parent bank is below the capital deduction threshold such that the Norwegian rate is applied to all relevant exposures. For group the risk-weighted countercyclical capital buffer is 1.0 per cent.

The group's hybrid equity and subordinated debt issued under the old rules has now been redeemed such that as of the first half of 2020 the group has no holdings covered by the transitional provisions.

Parent Bank				Group		
31 Dec 2019	30 June 2019	30 June 2020	(NOKm)	30 June 2020	30 June 2019	31 Dec 2019
17,822	16,889	17,565	Total book equity	20,320	19,450	20,420
-1,250	-972	-1,213	Additional Tier 1 capital instruments included in total equity	-1,254	-1,013	-1,293
-512	-519	-501	Deferred taxes, goodwill and other intangible assets	-1,042	-1,105	-1,099
-1,314	-	-	Deduction for allocated dividends and gifts	-	-	-1,314
-	-	-	Non-controlling interests recognised in other equity capital	-768	-781	-761
-	-	-	Non-controlling interests eligible for inclusion in CET1 capital	401	447	438
-	-1,544	-835	Net profit	-1,008	-1,729	-
-	694	446	Year-to-date profit included in core capital (0 per cent (50 per cent) pre tax of group profit)	618	879	-
-33	-31	-51	Value adjustments due to requirements for prudent valuation	-62	-44	-45
-305	-290	-227	Positive value of adjusted expected loss under IRB Approach	-248	-309	-351
-	-	-	Cash flow hedge reserve	14	5	3
-185	-185	-187	Deduction for common equity Tier 1 capital in significant investments in financial institutions	-424	-175	-168
14,222	14,042	14,997	Common equity Tier 1 capital	16,547	15,625	15,830
1,250	1,000	1,250	Additional Tier 1 capital instruments	1,635	1,384	1,637
275	275	-	Additional Tier 1 capital instruments covered by transitional provisions	-	275	275
15,747	15,318	16,247	Tier 1 capital	18,182	17,284	17,742
			Supplementary capital in excess of core capital			
1,750	1,750	1,750	Subordinated capital	2,240	2,310	2,240
12	182	-	Subordinated capital covered by transitional provisions	-	182	12
-140	-141	-157	Deduction for significant investments in financial institutions	-157	-141	-140
1,623	1,791	1,593	Additional Tier 2 capital instruments	2,083	2,351	2,113
17,370	17,108	17,841	Total eligible capital	20,266	19,634	19,854

			Minimum requirements subordinated capital			
911	938	981	Specialised enterprises	1,166	1,094	1,101
1,139	1,156	1,042	Corporate	1,052	1,163	1,149
1,628	1,521	1,608	Mass market exposure, property	2,290	2,166	2,299
98	99	112	Other mass market	115	102	101
984	1,115	1,006	Equity investments	1	1	1
4,760	4,829	4,748	Total credit risk IRB	4,624	4,525	4,651
2	2	2	Central government	5	3	3
86	83	115	Covered bonds	159	136	132
419	412	597	Institutions	504	300	282
-	-	-	Local and regional authorities, state-owned enterprises	17	8	5
42	35	34	Corporate	251	237	239
22	38	18	Mass market	465	525	463
9	14	15	Exposures secured on real property	157	207	167
236	236	279	Equity positions	394	369	377
104	83	93	Other assets	150	167	151
918	902	1,152	Total credit risk standardised approach	2,102	1,952	1,818
31	34	43	Debt risk	44	35	34
-	-	-	Equity risk	10	14	15
-	-	-	Currency risk and risk exposure for settlement/delivery	1	3	3
407	387	407	Operational risk	720	656	720
29	28	53	Credit value adjustment (CVA)	193	122	115
-	-	-	Transitional arrangements	-	1,032	-
6,145	6,181	6,404	Minimum requirements subordinated capital	7,694	8,339	7,357
76,817	77,257	80,047	Risk weighted assets (RWA)	96,181	104,240	91,956
3,457	3,477	3,602	Minimum requirement on CET1 capital, 4.5 per cent	4,328	4,691	4,138
			Capital Buffers			
1,920	1,931	2,001	Capital conservation buffer, 2.5 per cent	2,405	2,606	2,299
2,305	2,318	2,401	Systemic risk buffer, 3.0 per cent	2,885	3,127	2,759
1,920	1,545	800	Countercyclical buffer, 1.0 per cent (2.5 and 2.0 per cent)	962	2,085	2,299
6,145	5,794	5,203	Total buffer requirements on CET1 capital	6,252	7,818	7,357
4,620	4,771	6,192	Available CET1 capital after buffer requirements	5,968	3,116	4,335
			Capital adequacy			
18.5 %	18.2 %	18.7 %	Common equity Tier 1 capital ratio	17.2 %	15.0 %	17.2 %
20.5 %	19.8 %	20.3 %	Tier 1 capital ratio	18.9 %	16.6 %	19.3 %
22.6 %	22.1 %	22.3 %	Capital ratio	21.1 %	18.8 %	21.6 %
			Leverage ratio			
161,905	156,091	183,256	Balance sheet items	255,493	223,781	230,048
6,830	6,824	8,084	Off-balance sheet items	8,944	8,343	7,897
-851	-840	-779	Regulatory adjustments	-1,603	-1,458	-1,503
167,885	162,075	190,562	Calculation basis for leverage ratio	262,834	230,667	236,441
15,747	15,318	16,247	Core capital	18,182	17,284	17,742
9.4 %	9.5 %	8.5 %	Leverage Ratio	6.9 %	7.5 %	7.5 %

Effect as at 31 December 2019 on the adopted application of net profit, as revised:

	31 Dec 2019	
	Parent Bank	Group
Common equity Tier 1 capital	14,525	16,133
Tier 1 capital	16,051	18,045
Total eligible capital	17,673	20,158
Common equity Tier 1 capital ratio	18.9 %	17.5 %
Tier 1 capital ratio	20.9 %	19.6 %
Capital ratio	23.0 %	21.9 %
Leverage Ratio	9.6 %	7.6 %