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 Marc 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. The total minimum requirement on CET1 capital is accordingly 12.9 per cent.

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 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. 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 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 2020 both the parent bank and the group is below the capital deduction threshold such that the Norwegian rate is applied to all relevant exposures.

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

Parent Bank				Group		
31 Dec 2019	31 Mar 2019	31 Mar 2020	(NOKm)	31 Mar 2020	31 Mar 2019	31 Dec 2019
17,822	**16,103**	**16,866**	**Total book equity**	**19,600**	**18,673**	**20,420**
-1,250	-981	-1,227	Additional Tier 1 capital instruments included in total equity	-1,268	-1,023	-1,293
-512	-525	-507	Deferred taxes, goodwill and other intangible assets	-1,059	-1,073	-1,099
-1,314	-	-	Deduction for allocated dividends and gifts	-	-	-1,314
-	-	-	Non-controlling interests recognised in other equity capital	-760	-665	-761
-	-	-	Non-controlling interests eligible for inclusion in CET1 capital	398	392	438
-	-747	-106	Net profit	-290	-1,046	-
-	237	83	Year-to-date profit included in core capital (0 per cent (50 per cent) pre tax of group profit)	266	537	-
-33	-31	-50	Value adjustments due to requirements for prudent valuation	-62	-43	-45
-305	-284	-293	Positive value of adjusted expected loss under IRB Approach	-329	-303	-351
-	-	-	Cash flow hedge reserve	13	5	3
-185	-163	-185	Deduction for common equity Tier 1 capital in significant investments in financial institutions	-353	-333	-168
14,222	**13,609**	**14,582**	**Common equity Tier 1 capital**	**16,155**	**15,122**	**15,830**
1,250	1,000	1,250	Additional Tier 1 capital instruments	1,637	1,377	1,637
275	275	-	Additional Tier 1 capital instruments covered by transitional provisions	-	275	275
15,747	**14,884**	**15,832**	**Tier 1 capital**	**17,792**	**16,775**	**17,742**
			Supplementary capital in excess of core capital			
1,750	1,750	1,750	Subordinated capital	2,240	2,298	2,240
12	184	-0	Subordinated capital covered by transitional provisions	-0	184	12
-140	-142	-153	Deduction for significant investments in financial institutions	-153	-142	-140
1,623	**1,792**	**1,597**	**Additional Tier 2 capital instruments**	**2,087**	**2,340**	**2,113**
17,370	**16,676**	**17,429**	**Total eligible capital**	**19,879**	**19,115**	**19,854**

SpareBank 1 SMN

			Minimum requirements subordinated capital			
911	962	964	Specialised enterprises	1,153	1,106	1,101
1,139	1,155	1,269	Corporate	1,279	1,161	1,149
1,628	1,515	1,625	Mass market exposure, property	2,310	2,126	2,299
98	95	97	Other mass market	100	97	101
984	1,076	987	Equity investments	1	1	1
4,760	**4,802**	**4,942**	**Total credit risk IRB**	**4,842**	**4,491**	**4,651**
2	2	2	Central government	4	3	3
86	87	101	Covered bonds	152	135	132
419	387	567	Institutions	466	269	282
-	-	-	Local and regional authorities, state-owned enterprises	15	10	5
42	41	30	Corporate	227	251	239
22	73	17	Mass market	474	536	463
9	13	16	Exposures secured on real property	174	211	167
236	231	240	Equity positions	383	365	377
104	91	115	Other assets	150	169	151
918	**925**	**1,088**	**Total credit risk standardised approach**	**2,045**	**1,949**	**1,818**
31	43	47	Debt risk	48	45	34
-	-	-	Equity risk	7	12	15
-	-	-	Currency risk and risk exposure for settlement/delivery	3	3	3
407	387	407	Operational risk	720	654	720
29	28	98	Credit value adjustment risk (CVA)	240	118	115
-	-	-	Transitional arrangements	-	929	-
6,145	**6,186**	**6,583**	**Minimum requirements subordinated capital**	**7,907**	**8,200**	**7,357**
76,817	**77,327**	**82,282**	**Risk weighted assets (RWA)**	**98,832**	**102,495**	**91,956**
3,457	3,480	3,703	Minimum requirement on CET1 capital, 4.5 per cent	4,447	4,612	4,138
			Capital Buffers			
1,920	1,933	2,057	Capital conservation buffer, 2.5 per cent	2,471	2,562	2,299
2,305	2,320	2,468	Systemic rick buffer, 3.0 per cent	2,965	3,075	2,759
1,920	1,547	823	Countercyclical buffer, 1.0 per cent (2.5 and 2.0 per cent)	988	2,050	2,299
6,145	**5,800**	**5,348**	**Total buffer requirements on CET1 capital**	**6,424**	**7,687**	**7,357**
4,620	**4,330**	**5,531**	**Available CET1 capital after buffer requirements**	**5,284**	**2,823**	**4,335**
			Capital adequacy			
18.5 %	17.6 %	17.7 %	Common equity Tier 1 capital ratio	16.3 %	14.8 %	17.2 %
20.5 %	19.2 %	19.2 %	Tier 1 capital ratio	18.0 %	16.4 %	19.3 %
22.6 %	21.6 %	21.2 %	Capital ratio	20.1 %	18.6 %	21.6 %
			Leverage ratio			
161,905	156,292	177,198	Balance sheet items	249,366	221,200	230,048
6,830	6,834	7,719	Off-balance sheet items	8,702	8,262	7,897
-851	-840	-1,033	Regulatory adjustments	-1,820	-1,600	-1,503
167,885	162,287	183,884	Calculation basis for leverage ratio	256,248	227,862	236,441
15,747	14,884	15,832	Core capital	17,792	16,775	17,742
9.4 %	**9.2 %**	**8.6 %**	**Leverage Ratio**	**6.9 %**	**7.4 %**	**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 %