Skandiabanken
Periodic information on capital adequacy and liquidity risk
– Pillar III 31 December 2011

skandia
bank & försäkring

Contents

Capital adequacy analysis and liquidity risk – Skandiabanken financial company group

Capital adequacy analysis and liquidity risk – Skandiabanken financial company group

1. Information on the parent company and the financial company group

Skandiabanken Aktiebolag (publ) (reg. no. 516401-9738), with domicile in Stockholm, Sweden, was established on 1 June 1994 and is a wholly owned subsidiary of Skandia Insurance Company Ltd (publ) ("Skandia" – reg. no. 502017-3083). Old Mutual plc (reg. no. 3591559), with domicile in London, UK, owns 100% (100%) of the shares in Skandia Insurance Company Ltd (publ).

Skandiabanken conducts business in Sweden and Norway. Operations are broken down into the operating segments Sweden banking, Norway banking (which is conducted via a branch located in Bergen, Norway), and Sweden mutual funds. In Sweden and Norway, Skandiabanken conducts banking business in the retail market and offers lending to individuals primarily in the form of home mortgages, personal loans, lines of credit and credit card credits, custody account lending and deposits. In addition to the lending and deposit activities, the bank offers services for trading in equities and mutual funds.

In 2011 the Sweden service operations segment was divested. The segment included insourced units from the parent company Skandia. Services provided by this segment were further invoiced to Skandia and Skandia Liv after the Swedish banking operations were charged with their share of the unit's costs.

During the third quarter of 2011, roughly half of the employees in the services segment were either transferred through their employment to the parent company Skandia or to the Sweden banking segment. The units that were transferred to the parent company Skandia pertain to customer service, market and administrative functions related to insurance activities. The units transferred to the Swedish banking segment pertain to customer service and market functions related to banking. The remainder of the services segment pertain to advisory activities, which were returned to the parent company Skandia on 1 January 2012.

Table 1: Consolidation of the financial company group in accordance with the capital adequacy rules

31/12/2011

Subsidiary	Registered number	Domicile/country	Share of ownership	Book value	Method of consolidation
Skandia Fonder AB	556317-2310	Stockholm, Sweden	100%	41	Acquisition method

In accordance with the capital adequacy rules, all subsidiaries are fully consolidated in accordance with the acquisition method.

On 1 February 2011 the minority owned (51%) subsidiary Svenska Lärarfonder was sold. The book value of the shares was SEK 3.1 million.

2. Capital adequacy

2.1 Comments on capital adequacy outcome at 31 Dec 2011 compared with 31 Dec 2010

The capital ratio increased compared with at 31 December 2010 to 14.31% (14.18%), mainly on account of the fact that comprehensive income for the period was verified by the company's auditors and was thereby included in the capital base. The capital base strengthened by SEK 148 million, and the capital requirement for risk-weighted assets increased by only SEK 64 million (3%), despite increased exposure to credit risk by SEK 8.7 billion (13%).

Risk-weighted exposures amounted to SEK 27,631 million (26,830). The change pertained mainly to increased exposure to credit risks during the second half of 2011. By risk-weighted exposures in meant the assessed value of an exposure to credit risk, currency risk and operational risk. By exposure is meant items on and off the balance sheet. According to the regulations, the definition of risk-weighted exposures does not apply for currency risk and operational risk; instead, the capital requirement for these risks is determined explicitly. To illustrate the calculation the capital requirement, these risks have been converted to risk-weighted exposures.

Risk-weighted exposures for credit risk increased by SEK 362 million. Lower lending to the retail market and home mortgages by SEK 571 million resulted in a decrease in risk-weighted assets by SEK 79 million. Exposures pertaining to the liquidity buffer increased by SEK 9.1 billion and entailed an increase in risk-weighted assets by SEK 139 million. Other risk-weighted credit exposures increased by SEK 302 million. The last-mentioned item includes fund settlement receivables and derivatives, among other things. The capital requirement for currency risk decreased by SEK 2 million, and the capital requirement for operational risk increased by SEK 37 million. The minority-owned subsidiary Svenska Lärarfonder was sold on 1 February 2011. The impact of this sale on risk-weighted assets and minority interests was SEK 6 million each.

2.2 Minimum capital requirement – Pillar I

Table 2: Capital adequacy analysis

SEK million

Capital adequacy measures	31/12/2011	31/12/2010
Total capital ratio [1]	14,31%	14,18%
Tier 1 capital ratio [2]	9,95%	9,71%
Capital adequacy quotient [3]	1,79	1,77
Capital base [4]		
Equity according to balance sheet at 31 December	2,806	2,641
Proposed dividend	-	-
Minority interest	-	6
Tier 1 capital, gross [4.1]	**2,806**	**2,647**
Less: intangible assets	-3	-7
Less: deferred tax assets	-35	-34
Unrealised result of available-for-sale financial assets, fixed-income securities	-20	-2
Tier 1 capital, net	**2,748**	**2,604**
Unrealised gain from available-for-sale financial assets, equities	4	-
Perpetual subordinated debt [4.2]	900	900
Fixed-term subordinated debt [4.3]	300	300
Total tier 2 capital	**1,204**	**1,200**
Capital base	**3,952**	**3,804**
Risk-weighted exposures/basis for calculating capital requirement [5]		
Credit risk according to standardised approach	23,585	23,223
Currency risk	134	156
Operational risk according to basic indicator approach	3,,911	3,451
Total risk-weighted exposures	**27,630**	**26,830**
Capital requirement [6]		
Credit risk according to standardised approach	1,887	1,858
Currency risk	10	12
Operational risk according to basic indicator approach	313	276
Total minimum capital requirement	**2,210**	**2,146**

For a description of quantitative concepts, see appendix 1, Description of quantitative information for tables in point 2, Minimum capital requirement.

Table 3: Exposures to credit risk per exposure class

SEK million

		31 December 2011			31 December 2010		
		Exposures	Risk-weighted assets	Capital requirement	Exposures	Risk-weighted assets	Capital requirement
	Footnotes	7	5	5	7	5	5
1	Exposures to governments and central banks	4,331	-	-	2,726	197	16
2	Exposures to local governments and comparable associations and authorities	3,165	97	8	399	80	6
3	Exposures to administrative bodies, non-commercial undertakings and religious communities	-	-	-	-	-	-
4	Exposures to multilateral development banks	-	-	-	-	-	-
5	Exposures to international organisations	-	-	-	-	-	-
6	Exposures to institutions	5,937	1,172	94	5,361	1,056	84
7	Exposures to corporates	919	758	61	901	690	55
8	Retail exposures	3,242	2,431	195	3,162	2,371	190
9	Exposures secured by real estate	49,177	17,919	1,433	49,821	18,059	1 445
10	Non-performing loans [8]	26	26	2	22	22	2
11	High-risk items	-	-	-	-	-	-
12	Exposures in the form of covered bonds	9,881	988	79	5,627	563	45
13	Securitisation positions	-	-	-	-	-	-
14	Exposures to CIUs	53	53	4	60	60	5
15	Other items	145	141	11	138	125	10
	Total credit risks	**76,876**	**23,585**	**1,887**	**68,217**	**23,223**	**1,858**

For a description of quantitative concepts, see appendix 1, Description of quantitative information for tables in point 2, Minimum capital requirement.

3. Liquidity risks

Liquidity risk is the risk that the bank cannot meet its liquidity obligations without a substantially elevated cost for obtaining means of payment.

Management

Skandiabanken offers lending to individuals, which is funded mainly by deposits from individuals. Most of the deposit surplus, i.e., the difference between deposits and lending, is invested in a high quality liquidity buffer, see tables 5-7, and this liquidity buffer must be sufficiently large to ensure readily available liquidity in the event of a stressed scenario.

Table 4: Deposit-to-loan ratio

%	31/12/2011	31/12/2010
Deposit-to-loan ratio, retail market incl. home mortgages	131	119

Investments are made in bonds and money market instruments, which are intended to be used as collateral for accounts with central banks, against which all clearing is conducted and where collateral is required from the first krona – even for temporary negative intraday balances.

Liquidity management for the Swedish and Norwegian operations is co-ordinated, but the liquidity portfolios are segregated. Liquidity in the Norwegian branch is invested in Norwegian kronor, and liquidity in Sweden is invested in Swedish kronor. Where needed, liquidity can be transferred from a country with a surplus to a country with a deficit, or investments can be made in the country in which the surplus has arisen.

Liquidity buffer – outcome 31 December 2011 compared with 31 December 2010

Surplus liquidity makes up Skandiabanken's liquidity buffer, see table 7. The total liquidity buffer consists of assets at the disposal of the Treasury function and includes balances with and lending to central banks and governments, short-term lending to credit institutions and liquid, fixed-income securities that can be realised at short notice and converted to cash after deducting collateral for borrowings from the Central Bank of Sweden. No part of the liquidity buffer has been used as collateral for loans. The total liquidity buffer shall always amount to at least 20% of deposits from the general public, in accordance with the internal limits set by the Board of Directors. Limits have been set for the respective issuers in accordance with the Board's instructions. The investment portfolio is judged to have good credit quality, and no impaired loans exist. In addition to surplus liquidity are granted credit facilities.

In rules and regulations that took effect on 31 December 2010, the Financial Supervisory Authority adopted a stricter definition of the liquidity buffer, which in table 5 below is called "Liquidity buffer according to the Financial Supervisory Authority's guidelines". The new, stricter definition puts additional demands which entail that fixed-income securities shall be eligible as collateral with central banks and that only intraday loans to banks may be included. For further information, see table 5.

Stress tests are performed daily to ensure that Skandiabanken has routines, processes and a contingency funding plan for conditions that deviate from normal circumstances. Additional stress tests of short-term preparedness to pay within the next thirty days are conducted monthly. The outcomes of the stress tests are taken into account in the contingency funding plans that are based on various crisis situations. The plan covers the division of responsibility as well as instructions for dealing with a potential liquidity deficit. In addition to the stress tests, monthly analysis and follow-up are conducted of the structural funding need during unfavourable circumstances.

Table 5: Liquidity buffer according to the Financial Supervisory Authority's guidelines

SEK million

		31/12/2011				31/12/2010			
		SEK	NOK	EUR	Total	SEK	NOK	EUR	Total
1	Cash and balances with, and lending to central banks and governments	986	2,354	5	3,345	1,000	483	3	1,486
2	Lending to other banks, intraday loans	-	-	-	-	107	-	-	107
3	Securities issued or guaranteed by sovereigns, central banks or multilateral development banks	898	30	-	928	1,200	-	-	1,200
4	Securities issued or guaranteed by municipalities or other public sector entities	1,495	1,176	-	2,671	-	304	-	304
5	Covered bonds issued by other banks or institutions	4,589	5,033	-	9,622	3,801	1,858	-	5,659
6	Covered bonds issued by own bank or related unit	-	-	-	-	-	-	-	-
7	Securities issued by non-financial corporates	-	-	-	-	-	-	-	-
8	Securities issued by financial corporates, excl. covered bonds	-	2,642	-	2,642	290	3,099	-	3,389
9	All other securities	-	-	-	-	-	-	-	-
	Total liquidity buffer according to Financial Supervisory Authority definition [1]	**7,968**	**11,235**	**5**	**19,208**	**6,398**	**5,744**	**3**	**12,145**

[1] The liquidity buffer is presented in accordance with the Swedish Bankers' Association's presentation format. The liquidity buffer consists of assets at the disposal of the Treasury function. The assets are eligible as collateral with central banks and are not claimed as collateral. The holdings are carried at current market value and receive a risk weight of 0-20% in accordance with the capital adequacy rules and the standardised approach for credit risk.

Table 6: Other liquidity buffer

SEK million

		31/12/2011				31/12/2010			
		SEK	NOK	EUR	Total	SEK	NOK	EUR	Total
1	Cash and balances with, and lending to central banks and governments	-	-	-	-	-	-	-	-
2	Lending to other banks, intraday loans	-	-	-	-	-	-	-	-
3	Securities issued or guaranteed by sovereigns, central banks or multilateral development banks	-	-	-	-	-	-	-	-
4	Securities issued or guaranteed by municipalities or other public sector entities	-	483	-	483	-	152	-	152
5	Covered bonds issued by other banks or institutions		230	-	230	-	225	-	225
6	Covered bonds issued by own bank or related unit	-	-	-	-	-	-	-	-
7	Securities issued by non-financial corporates	200	-	-	200	200	93	-	293
8	Securities issued by financial corporates, excl. covered bonds	1,740	1,102	-	2,842	679	1,403	-	2,082
9	All other securities	-	-	-	-				
	Total other liquidity buffer [2]	**1,940**	**1,815**	**-**	**3,755**	**879**	**1,873**	**-**	**2,752**

[2] The other liquidity buffer is at the disposal of the Treasury function and pertains to fixed-income securities that are not eligible as collateral with central banks and which thus do not meet the Financial Supervisory Authority's requirements for assets that qualify to be included in the liquidity buffer. The holdings are carried at current fair value and receive a risk weight of 0-20% in accordance with the capital adequacy rules and the standardised approach for credit risk.

Table 7: Total liquidity buffer

SEK million

		31/12/2011				31/12/2010			
		SEK	NOK	EUR	Total	SEK	NOK	EUR	Total
1	Cash and balances with, and lending to central banks and governments	986	2,354	5	3,345	1,000	483	3	1,486
2	Lending to other banks, intraday loans	-	-	-	-	107	-	-	107
3	Securities issued or guaranteed by sovereigns, central banks or multilateral development banks	898	30	-	928	1,200	-	-	1,200
4	Securities issued or guaranteed by municipalities or other public sector entities	1,495	1,659	-	3,154	-	456	-	456
5	Covered bonds issued by other banks or institutions	4,589	5,263	-	9,852	3,801	2,083	-	5,884
6	Covered bonds issued by own bank or related unit	-	-	-	-	-	-	-	-
7	Securities issued by non-financial corporates	200	-	-	200	200	93	-	293
8	Securities issued by financial corporates, excl. covered bonds	1,740	3,744	-	5,484	968	4,503	-	5,471
9	All other securities	-	-	-	-				
	Total liquidity buffer	**9,908**	**13,050**	**5**	**22,963**	**7,276**	**7,618**	**3**	**14,897**
	Of which, eligible (pledgeable) assets	7,968	11,235	5	19,208	6,398	5,744	3	12,145
	Of which, pledged assets	2,036	3,545	-	5,581	1,645	1,313	-	2,958

Credit facilities	SEK	NOK	EUR	Total	SEK	NOK	EUR	NOK
Own credit facilities granted	400	-	-	400	400	-	-	400

4. Applied rules and regulations

Swedish law and the Financial Supervisory Authority's rules and regulations on capital adequacy and large exposures are based on the EU Capital Requirements Directive (CRD), and are based on three pillars:

Pillar I – Minimum capital requirement

Calculations of minimum capital requirement are performed in accordance with the Capital Adequacy and Large Exposures Act (*Lagen (2006:1371) om kapitaltäckning och stora exponeringar*) and the Financial Supervisory Authority's regulations and general guidelines on capital adequacy and large exposures (FFFS 2007:1).

Skandiabanken uses the standardised approach in calculating credit risk. This entails that 15 exposure classes with several different risk weightings are used in the respective classes. For further information, see appendix 2. The capital requirement for currency risks covers all items on and off the balance sheet at current fair value and translated to Swedish kronor at the exchange rate in effect on the balance sheet date. Eight per cent of the total net position in foreign currency is calculated to make up the capital requirement. The capital requirement for operational risks is calculated using the basic indicator approach, which entails that the capital requirement consists of 15% of average operating income for the last three financial years. Skandiabanken has received permission from the Financial Supervisory Authority to calculate the capital requirement for market risks in accordance with the rules for credit risk.

Pillar II – Rules for the supervisory authorities' overall capital assessment and Internal Capital Adequacy Assessment Process (ICAAP)

Skandiabanken's strategy is always to have a total capital ratio of higher than 10.5% including the internal capital requirement. According to the statutory minimal capital requirement, the capital base in relation to the risk-weighted amount of exposure shall be no less than 8%. For choice of method, see "Minimum capital requirement" above. In addition to the statutory minimum capital requirement, banks are expected to maintain a higher capital base, which is addressed under Pillar II, "Capital assessment and risk management". Skandiabanken's total capital requirement is taken into consideration in the Internal Capital Adequacy Assessment Process (ICAAP). This entails that Skandiabanken holds additional capital – referred to above as internal capital – for other significant risks in addition to above-mentioned risks, i.e., credit risks, currency risks and operational risks. The ICAAP also takes into account Skandiabanken's future business plans. A capital buffer is held in addition to the capital requirement for identified risks and with continued expansion taken into account. The EU directive's stipulations have been included in the Banking and Finance Business Act (*Lagen (2004:297) om Bank- och finansieringsrörelse*). The Financial Supervisory Authority reviews and evaluates risk management and performs controls to ensure that sufficient capital is held for the significant risks that Skandiabanken is exposed to.

Pillar III – Disclosures of capital adequacy and risk management

Information is to be provided yearly in accordance with the Financial Supervisory Authority's regulations and general guidelines regarding public disclosure of information concerning capital adequacy and risk management (FFFS 2007:5), called Pillar III. Complete information is disclosed yearly and not later than in connection with publication of the annual report on Skandiabanken's website. This yearly, complete information also includes disclosure of information on remuneration.

Periodic information on capital adequacy is provided on Skandiabanken's website for the periods ended 31 March, 30 June, 30 September and 31 December.

Appendix 1

Description of quantitative information on the tables in point 2 "Minimum capital requirement"

[1]Total capital ratio
The capital base in relation to the risk-weighted amount of exposure; shall amount to at least 8%.

[2]Tier I capital ratio
Tier I capital in relation to the risk-weighted amount of exposure; shall amount to at least 4%.

[3] Capital adequacy quotient
By capital adequacy quotient is meant capital base in relation to the total minimum capital requirement.

[4] The capital base is allocated between primary (Tier 1) capital and supplementary (Tier 2) capital. Tier 1 capital shall amount to at least 50% of the sum of tier 1 and tier 2 capital. Tier 2 capital refers to perpetual and fixed-term subordinated debt. Fixed-term subordinated debt may not exceed 50% of tier 1 capital

[4.1]Tier 1 capital, gross, refers to equity as per the balance sheet at 31 December including minority interests and the appropriation of profits proposed by the Board, which is reported in equity. Profit for the period is included when verified by the external auditors.

[4.2]Perpetual subordinated debt
According to the terms of agreement, the rate of interest is determined in relation to the interest base, Stibor +1.25%. The loan has subordinated terms of payment and runs with no collateral pledged. Repayment of the debt is only possible in case the issuer is declared bankrupt or has entered into liquidation, or, after having obtained permission from the Financial Supervisory Authority.

[4.3]Fixed-term subordinated debt
According to the terms of agreement, the rate of interest is determined in relation to the interest base, Stibor +1.00%. The loan has subordinated terms of payment and runs with no collateral.

On 10 December 2018 an amount of SEK 200 million will fall due, and SEK 100 million will fall due on 16 December 2019. In cases where the remaining term is less than five years, the amount that may be included in the capital base shall amount to a maximum of 20% of the notional value for each remaining year.

Repayment of subordinated debt is only possible in cases where the issuer is declared bankrupt or has entered into liquidation, or, after having obtained permission from the Financial Supervisory Authority.

[5] By risk-weighted exposures is meant the assessed value of an exposure. By exposure is meant items on and off the balance sheet. Intra-group exposures are included, except for shares in subsidiaries and counterparties that are under supervision of the Financial Supervisory Authority.

According to the regulations, the definition of risk-weighted exposures does not apply for currency risk and operational risk; instead the capital requirement for these risks is determined explicitly. To illustrate the calculation, these risks have been converted to risk-weighted exposures.

[6] The capital requirement refers to 8% of risk-weighted exposures.

[7]By exposure is meant exposures on the balance sheet after deduction for loan losses and off-balance sheet undertakings.

[8]Non-performing loans refer to, in accordance with the Financial Supervisory Authority's regulations and general guideline regarding capital adequacy and large exposures (FFFS 2007:1), loans that are more than 90 days past due. This entails that, compared to applied definitions in the consolidated financial statements and disclosures, impaired loans are included in the concept of non-performing loans in the table above. Moreover, loans more than 60 days past due are stated as non-performing loans in other notes.

Appendix 2

Disclosures of credit risk – Pillar I

Method for calculating risk-weighted exposures to credit risk using the standardised approach

In accordance with Pillar I, exposures to credit risk include the following items less provisions for impaired loans
• Items on the balance sheet carried at net book value
• Items off the balance sheet carried at their notional value multiplied by an applicable conversion factor
• Counterparty risk in derivative contracts

The following exposures receive 0% in risk weight regardless of which exposure class they belong to
• Exposures deducted from the capital base
• Exposures pertaining to shareholdings in subsidiaries and other items that may be included in the issuing institution's capital base

Other exposures to group companies than shareholdings in subsidiaries receive a risk weight of 0% under the following circumstances
• The counterparty is an institution or financial holding company that is domiciled in Sweden and fully consolidated in the financial company group
• The counterparty has corresponding processes for risk assessment, risk measurement and control as the institution
• There are no prevailing or anticipated material or legal hindrances to the counterparty's ability to quickly transfer funds from the capital base or regulate liabilities to the institution.

For Skandiabanken, this means that exposures to the subsidiary Skandia Fonder AB receive a risk weight of 0%.

Calculation of risk-weighted amount for credit risk
Fifteen exposure classes are used in application of the standardised approach. The respective exposure classes can, within each class, have several different risk weights, which are set by the Financial Supervisory Authority. To determine which risk weight an exposure shall be assigned, an external credit rating is used. The Financial Supervisory Authority approves the credit rating agencies whose credit ratings may be used and specifies a number of credit quality steps and which credit ratings belong to the respective intervals.

Skandiabanken uses external ratings from Standard & Poor's, Moody's and Fitch. In cases where the counterparty has received two external credit ratings, the credit rating that leads to the highest risk weight is used. If an exposure has received more than two external credit ratings, the two credit ratings that provide the lowest risk weight shall be used. If these two differ, the one that provides the higher risk weight shall be used. When exposures pertain to a specific issue programme that has been assigned a credit rating, this credit rating shall be used.

Credit risk protection – collateral that reduces the capital requirement

Under certain circumstances, the capital requirement can be reduced when the bank receives collateral for the credit exposure. According to the rules, when applying the standardised approach, credit risk protection may be included if the form of collateral is acceptable and the bank meets certain handling requirements. The rules for collateral are broken down into guarantees, credit derivatives and financial collateral. The collateral that the bank uses to reduce the capital requirement pertains to guarantees.

The effect on the capital requirement of guarantees that may be included is that the debtor's risk weight is exchanged for the guarantee issuer's risk weight in calculating the risk-weighted exposure amount. In cases where there is a mismatch in the duration between the guaranteed exposure and the guarantee, the guarantee is not included if the original duration is less than one year or if the remaining duration is less than three months. In addition, guarantees longer than five years are not included.