

# Individual Solvency Need

Nordea Kredit Realkreditaktieselskab

30 September 2018



Nordea

## 1 Introduction

This report presents the individual solvency need (tilstrækkelig basiskapital og solvensbehov for pengeinstitutter) for Nordea Kredit Realkreditaktieselskab (Nordea Kredit). This report fulfils external disclosure requirements regarding the solvency need according to EU regulation No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms, and the Danish Financial Business Act (Lov om finansiel virksomhed jf. lovbekendtgørelse nr. 1140 af 26. September 2017) and Danish Executive Order no. 1353 (22 November 2016) "Bekendtgørelse om opgørelse af risikoeksponeringer, kapitalgrundlag og solvensbehov".

The individual solvency need is updated and published each quarter. Details about Nordea Kredit's risk profile and key exposures are available in the annually disclosed Capital and Risk Management (Pillar 3) report for Nordea Kredit, starting from 2016. Both reports are available on Nordea's Investor Relations website (nordea.com/ir) and links can be found on Nordea Kredit's website. Reference to the individual solvency need reporting is made in the annual report and the interim report for Nordea Kredit. The Internal Capital Adequacy Assessment Process (ICAAP) report for Nordea Kredit is produced at least annually. The reports are approved by the Board of Directors and presented to the Danish Financial Supervisory Authority (Dk-FSA).

All amounts are in DKK unless stated otherwise.

### 1.1 Main conclusions

#### ISN ratio excluding combined buffers

**14.8%**

Increased from 14.0% in Q2 2018

#### Total capital ratio

**32.6%**

Increased from 32.0% in Q2 2018

#### Capital situation

Nordea Kredit is well capitalised at end-Q3 2018 and has access to available capital from the parent company if necessary.

#### Stress Testing

Nordea Kredit conducts capital adequacy stress testing in collaboration with the Nordea Group to ensure that adequate capital is available in the event of, for instance, severe credit losses or changes in regulatory capital requirements. Stress testing is also made using Dk-FSA scenarios and methods.

#### Individual solvency need incl. combined buffers

**12.4bn**

Increased from 12.0bn in Q2 2018

#### Excess capital above individual solvency need incl. combined buffers

**10.2bn**

Decreased from 10.5bn in Q2 2018

#### Gældsbuffer

In addition to capital requirements Nordea Kredit has to meet a debt buffer requirement. The debt buffer is a way of implementing MREL in BRRD for mortgage institutions and is phased in, starting from 15 June 2016. As of 15 June 2018 the requirement is 1.6% of mortgage loans growing to 2.0% when fully implemented in 2020. The debt buffer requirement needs to be met by own funds instruments or unsecured senior debt not used to cover capital requirements.

## 2 Description of the individual solvency need

### Approach

Nordea Kredit uses a Pillar I plus Pillar II approach in calculating the individual solvency need. Each component and its capital requirement are shown graphically on page 3 in Figure 1, along with the Individual Solvency Need in Table 1, and the Own Funds and REA in Table 2.

This methodology uses the Pillar I capital requirements for credit risk, Credit Value Adjustment (CVA), market risk and operational risk as outlined in the Capital Requirements Regulation (CRR) as the starting point for its risk assessment. For each of these types, the risk is measured solely according to models and processes approved by the Dk-FSA for use in the calculation of legal capital requirements.

### Pillar II add-ons

In addition, Pillar II risks, i.e. risks not included in the CRR or not adequately covered, are considered – specifically concentration risk, interest rate risk in the banking book, operational risk, and earnings risk (prev. business risk).

### Temporary Pillar II add-ons

Also included in the Pillar II requirement are a number of temporary capital add-ons for changes pending internal approvals, approvals by FSAs or other add-ons of which some are related to the SREP. The Pillar II add-ons are reflecting the model deficiencies that are currently not captured in Pillar I.

An add-on reflects that the current average Actual Default Frequency (ADF) exceeds the Probability of Default (PD) used in the Pillar I capital requirements for the IRB corporate and institutions portfolio. The capital add-on is 11.5% of the credit risk Pillar I capital requirement for the IRB corporate and institutions portfolio.

### Pillar II add-ons due to SREP

Finally, some Pillar II add-ons reflect the increased requirements in the SREP which relate to corporate risk exposure adjustments, maturity floor adjustments and inadequate second line of defence and its involvement in the governance of the IRB system and modelling. Included is also an add-on for operational risk from inspections relating to IT and key processes. Part of the adjustments that are ongoing due to SREP 2015 is reversal of changes made in Pillar I REA. Before the changes are in effect, and are included in the relevant risk measure, these are reported as other risks in Pillar I.

### Management buffer

For Nordea Kredit the general management buffer is the difference between the measured Pillar I and Pillar II risks and the 14.8% individual solvency need.

A management buffer of 0.2% is included in Pillar II Other risks at end Q3 2018. The Dk-FSA benchmark model for earnings risk calculation results in no capital add-on at end Q3 2018.

### Combined buffers

The combined buffers consist of the Capital Conservation buffer (1.88%), the SIFI buffer (1.20%) and the Countercyclical buffer (0.01 %). The combined buffer requirements are not included in the ISN ratio calculated by Nordea Kredit, the combined buffer requirement is however included for information where applicable.

### Excess capital above requirements

At the end of Q3 2018 the own funds held by Nordea Kredit resulted in a capital buffer above the individual solvency need including the combined buffer requirements of DKK 10.2bn in total. This is a decrease in relation to Q2 2018. Disregarding the management buffer from the ISN, the capital excess would increase by DKK 139m.

### 3 Individual solvency need, own funds and REA

The components of the capital requirement are shown in figure 1. The individual solvency need, the own funds and the total risk exposure amounts for Nordea Kredit at end-Q3 2018 are presented in detail in tables 1 and 2 below.

Figure 1 Individual solvency need including combined buffers and actual capital for Nordea Kredit at end-Q3 2018

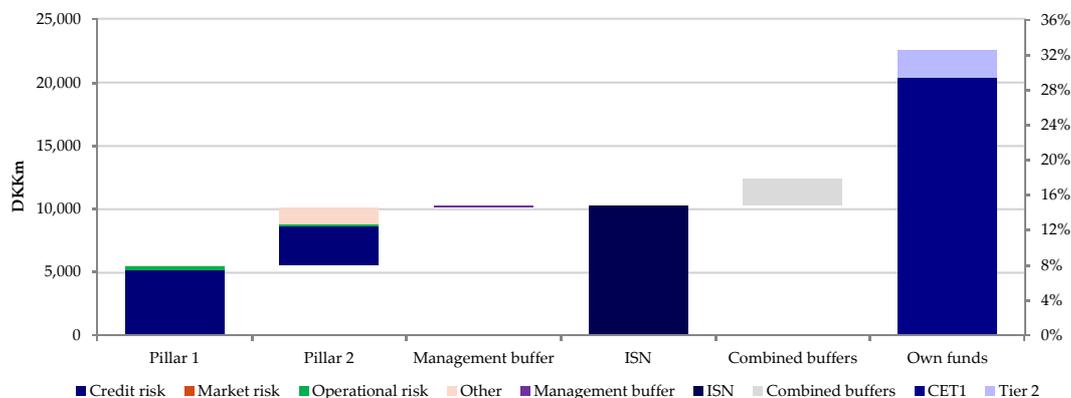


Table 1 Individual solvency need for Nordea Kredit at end-Q3 2018

| DKKm / pct.   | Solvency requirement | Pct. of REA  |   |
|---|----------------------|--------------|---|
| <b>Pillar I</b>   |                      |              |   |
| Credit risk   | 5,162                | 7.5%         |   |
| Market risk   | 0                    | 0.0%         |   |
| Operational risk  | 327                  | 0.5%         |   |
| Other   | 54                   | 0.1%         |   |
| <b>Total Pillar I</b>   | <b>5,543</b>         | <b>8.0%</b>  |   |
| <b>Pillar II</b>  |                      |              |   |
| Credit risk   | 3,072                | 4.4%         |   |
| Market risk   | 23                   | 0.0%         |   |
| Operational risk  | 131                  | 0.2%         |   |
| Other   | 1,486                | 2.1%         |   |
| - of which Management buffer  | 139                  | 0.2%         |   |
| <b>Total Pillar II</b>  | <b>4,712</b>         | <b>6.8%</b>  |   |
| <b>Individual solvency need</b>   | <b>10,255</b>        | <b>14.8%</b> |   |
| Combined capital buffer requirements  | 2,136                | 3.1%         |   |
| <b>Individual solvency need + combined buffers</b>                                  | <b>12,392</b>        | <b>17.9%</b> |   |
| Own funds   | 22,565               | 32.6%        |   |
| <b>Excess capital above individual solvency need + combined buffers</b>             | <b>10,173</b>        | <b>14.7%</b> |   |
| <b>Pillar II add-ons, not included or adequately covered in the CRR, consist of</b> |                      |              |   |
| Concentration risk  | x                    |              |   |
| IRR in the banking book   |                      | x            |   |
| Corporate and Bank ADF/PD adjustment  | x                    |              |   |
| Add-ons related to SREP   | x                    |              | x |

Table 2 Own funds excluding profit and total risk exposure amount for Nordea Kredit at end-Q3 2018

| DKKm / pct.                             | DKKm          | Pct. of REA  |
|---|---------------|--------------|
| <b>Own funds (net after deductions)</b> |               |              |
| Common Equity Tier 1 capital            | 20,365        | 29.4%        |
| Tier 1 capital                          | 20,365        | 29.4%        |
| <b>Total own funds</b>                  | <b>22,565</b> | <b>32.6%</b> |
| <b>REA</b>                              |               |              |
| Total Risk Exposure Amount              | 69,292        |              |