Nordea



Capital adequacy and risk management report (pillar 3) Nordea 2008

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1. Introduction

This is Nordea's second report on capital adequacy and risk management in accordance with the legal disclosure requirements in EU's Capital Requirements Directive (CRD). The report presents the capital position and how the size and composition of the capital base is related to the risks as measured in risk weighted amounts (RWA). CRD is based on the Basel II framework, see appendix section 12.1 for a general description of the three pillars in the framework. Nordea follows the Swedish Capital adequacy and large exposure act (2006:1371) and the Swedish Financial Supervisory Authority's regulation and general guidelines regarding public disclosure of information concerning capital adequacy and risk management (FFFS 2007:5), which are based on the CRD.

This report constitutes the comprehensive disclosure on risks and capital as well as risk management and capital management. In a summarised form, the main disclosure on exposures as well as on risk, liquidity and capital management are also presented in Nordea's annual report.

In the capital adequacy and risk management report for 2008, Nordea increases the transparency on relevant risk factors inherent in the operations, how these are managed and mitigated and the effect on the capital adequacy for the Nordea Group. The report has been developed with the ambition to meet the pillar 3 requirements as well as to meet the increased need of transparency in the financial market. The enhanced disclosure is developed to be aligned with the recommendations issued in 2008 by the Financial Stability Forum, Committee of European Bank Supervisors (CEBS) and European Banking Federation (EBF).

The report follows the structure below:

- Highlights of 2008.
- Description of the Group structure and overall risk and capital management.
- Credit risk, including description of credit process, exposure, RWA and RWA calculations and loan losses.
 Market risk.
- Operational risk.
- Off halance including
- Off balance, including risk in derivatives and securitisation.
- Liquidity risk and Structural Interest Income Risk (SIIR).
- Internal Capital Adequacy Assessment Process (ICAAP).
- Capital base components.
- Capital adequacy conclusions.

The pillar 3 disclosure is made for the Nordea Group and for the subgroups Nordea Bank Denmark Group, Nordea Bank Finland Group and Nordea Bank Norway Group as well as Nordea Bank Polska S.A. The report for the Nordea Group and the reports for the sub-groups are presented on www.nordea.com and the key data on capital adequacy is presented in the annual report of respective legal entity.

The full pillar 3 disclosure is made annually and the periodic information is published quarterly, included in the quarterly report for the entity. The format, frequency and content of the disclosures follow, to as large extent as possible with regards to the local legislation, a common setup in Nordea. Group Corporate Centre within Nordea has stated the common principles in a policy and instructions for disclosing information on capital adequacy in the Nordea Group.

2. Highlights of 2008

2008 has been a challenging and extreme year in the global financial market. The financial turmoil continued throughout the year and deepened in the fall due to failures of some of the largest investment banks in the world. Uncertainty and risks have increased significantly both in the financial markets and about the macroeconomic development.

During 2008, stability programmes have been launched by the governments in the Nordic region with the purpose to ensure liquidity and improve the overall stability of the financial system. Nordea has chosen to participate in the stability programme in Denmark by end of 2008. For further details about the stability plans in the Nordic area, see section 12.2 in the appendix.

During the turbulent 2008 risk management strategies and models have been tested under very severe and challenging market conditions. It is therefore satisfying that Nordea despite challenging market conditions is reporting a solid result, including only minor negative effects from the turmoil in financial markets. Nordea's well segmented culture of cost, risk and capital management has proved to be working well. Active risk management and control measures have been taken during the year to ensure a well balanced risk taking. During the year specifically activities have been enforced to control liquidity, credit and costs as well as increased internal focus on the RWA at all levels in the organisation. The process for capital management is well established and the ICAAP was done for the second time and sent to the Nordic financial supervisory authorities in June 2008.

Nordea continues to roll out the Internal Rating Based approach (IRB) for its credit portfolios under the CRD (the new Basel II regime). In December 2008, the IRB approval was received for the retail portfolio, with start from 31 of December 2008. The Retail IRB approval reduces the capital requirement with 14%.

The overall purpose of the capital policy is to maintain capital at levels that are adequate from the perspective of regulators, funding, rating agencies and to optimise shareholder value in light of the external requirements. In February 2009, Nordea revised its capital policy and capital targets. The revised capital policy for Nordea Group states that over a business cycle, the target for the Tier 1 ratio is 9% and the target for the Capital ratio is 11.5%.

Nordea announced measures to strengthen the Group's core tier 1 capital by EUR 3bn. The Board of Directors of Nordea has resolved to increase Nordea's share capital through an underwritten discounted issue of new ordinary shares with pre-emptive rights for existing shareholders of approx. EUR 2.5bn net and secondly by proposing to reduce the dividend payment to 19% of the net profit for 2008, to be decided by the 2009 Annual General Meeting, which will increase core tier 1 capital by approx. EUR 0.5bn. The rights offering is subject to shareholder approval at an Extraordinary General Meeting to be held on 12 March 2009.

3. Risk and capital management

In this chapter, the consolidation principles for the capital base are described as well as the principles for management and control of risk and capital. For information about the organisational structure, please see the Annual report.

3.1 The Financial Group in the capital adequacy context

The information given in this report refers to the Financial Group of Nordea Bank AB (publ), with corporate registration number 516406-0120. Nordea is supervised on different levels and subject to ensure sufficient capital on all entities and subgroups. The Financial Conglomerate is the formalised definition of the consolidation of both bank and insurance. The capital situation is similar when consolidating the Financial Conglomerate as is for the Financial Group. In this report, most focus is on the Financial Group due to the pillar 3 legislation but risks in the insurance part is also mentioned.

The financial statements are published quarterly and the consolidated financial statements include the accounts of the parent company Nordea Bank AB (publ) including subsidiaries according to International Accounting Standard (IAS) 27. In the Financial Group, the insurance operations are not consolidated. According to the requirements in the CRD, insurance subsidiaries and associated undertakings with financial operations are instead deducted from the capital base in the capital adequacy reporting (e g credit institutions or insurance companies where Nordea own 10% or more of the capital). Table 1 below includes information of what undertakings that have been consolidated and deducted from the capital base.

Table 1 Specification over group undertakings consolidated/deducted from the capital base, 31 Dec 2008

	Number of shares	Book value EURm	Voting power of holding %	Domicile	Consolidation method
Group undertakings included in the capital base					
Nordea Bank Finland Plc	1,030,800,000	5,948	100	Helsinki	purchase method
Nordea Finance Finland Ltd			100	Espoo	purchase method
Nordea Bank Danmark A/S	50,000,000	3,503	100	Copenhagen	purchase method
Nordea Finans Danmark A/S			100	Höje-Taastrup	purchase method
Nordea Kredit Realkreditaktieselskab			100	Copenhagen	purchase method
Nordea Bank Norge ASA	551,358,576	2,402	100	Oslo	purchase method
Norgeskreditt AS			100	Oslo	purchase method
Nordea Finans Norge AS			100	Oslo	purchase method
Christiania Forsikring AS			100	Oslo	purchase method
Nordea Bank Polska S.A.	45,038,791	262	99	Gdynia	purchase method
OOO Promyshlennaya Companiya				2	•
Vestcon (Orgresbank)	749,991,704	649	100	Moscow	purchase method
JSB Orgresbank			91	Moscow	purchase method
Nordea Hypotek AB (publ)	100,000	1,714	100	Stockholm	purchase method
Nordea Fonder AB	15,000	679	100	Stockholm	purchase method
Nordea Bank S.A.	999,999	323	100	Luxembourg	purchase method
Nordea Finans Sverige AB (publ)	1,000,000	77	100	Stockholm	purchase method
Nordea Fondene Norge Holding AS	1,200	29	100	Oslo	purchase method
Nordea Investment Management AB	12,600	64	100	Stockholm	purchase method
Nordic Baltic Holding (NBH) AB	1,000	9	100	Stockholm	purchase method
Nordea Life Holding AB	1,000	201	100	Stockholm	purchase method
Other companies		6			- purchase method
Total included in the capital base		15,866			

cont. Table	1 Specification over grou	p undertakings consolidated	/deducted from the capita	I base, 31 Dec 2008
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	Number of shares	Book value EURm	Voting power of holding %	Domicile	Consolidation method
Group undertakings deducted from the capital base					
Nordea Life Holding AB, including debts from	1 000	1 050	100	0. 11 1	
parent company	1,000	1,059	100	Stockholm	
Total group undertakings deducted from the capita	l base	1,059			
Over 10 % investments in credit institutions deducted from the capital base					
Eksportfinans ASA		112	23	Oslo	
Luottokunta		41	24	Helsinki	
NF Fleet Oy		0	20	Espoo	
LR Realkredit A/S		1	39	Copenhagen	
KIFU-AX II A/S		2	26	Copenhagen	
KFU-AX II A/S		2	34	Copenhagen	
Axel IKU Invest A/S		1	33	Billund	
Nordea Thematic funds of Funds KS		12	25	Copenhagen	
INN KAP 2		1	15	Copenhagen	
Symbion Capital I		1	25	Copenhagen	
Other		1			
Total investments in credit institutions deducted from the capital base		174			

3.2 Risk, liquidity and capital management

Risk, liquidity and capital management are key success factors in the financial services industry. Exposure to risk is inherent in providing financial services, and Nordea assumes a variety of risks in its ordinary business activities, the most significant being credit risk related to loans and receivables. Maintaining risk awareness in the organisation is a key component of Nordea's business strategies. Nordea has clearly defined risk, liquidity and capital management frameworks, including policies and instructions for different risk types and for the capital structure.

3.2.1 Management principles and control

Board of Directors

The Board of Directors has the ultimate responsibility for limiting and monitoring the Group's risk exposure. The Board of Directors also has the ultimate responsibility for setting the targets for the capital ratios. Risk is measured and reported according to common principles and policies approved by the Board of Directors. The Board of Directors decides on policies for credit, market, liquidity, operational risk management and the ICAAP. All policies are reviewed at least annually.

In the credit instructions, the Board of Directors decides on powers-to-act for credit committees at different levels within the customer areas. Authorisations may also vary depending on the internal rating of customers. The Board of Directors also decides on the limits for market and liquidity risk in the Group.

Board Credit Committee

The Board Credit Committee monitors the development of the credit portfolio including industry and major customer exposures. The Board Credit Committee confirms industry policies approved by the Executive Credit Committee (ECC).

CEO and GEM

The Chief Executive Officer (CEO) has overall responsibility for developing and maintaining effective principles for risk, liquidity and capital management as well as internal principles and control in Nordea.

The CEO in Group Executive Management (GEM) decides on the targets for the Group's risk management regarding SIIR and, in accordance with the scope of resolutions adopted by the Board of Directors, allocates the market and liquidity risk limits to risk taking units such as Group Treasury and Markets. The setting of limits is guided by Nordea's business strategies, which are reviewed at least annually. The heads of the units allocate the respective limits within the unit and may introduce more detailed limits and other risk mitigating techniques such as stop loss rules.

The CEO and GEM regularly review reports on risk exposures and have established the following committees for risk, liquidity and capital management:

• The Asset and Liability Committee (ALCO), chaired by the Chief Financial Officer (CFO), prepares issues of major importance concerning the Group's financial operations, financial risks as well as capital management for decision by the CEO in GEM.

- Capital Planning Forum (CPF), chaired by the CFO, monitors the development of internal and regulatory capital requirements, the capital base, and decides also upon capital planning activities within the Group.
- The Risk Committee, chaired by the Chief Risk Officer (CRO), monitors developments of risks on an aggregated level.
- The ECC and Group Credit Committee (GCC), chaired by the CRO, decide on major credit risk limits and industry policies for the Group. Credit risk limits are granted as individual limits for customers or consolidated customer groups and as industry limits for certain defined industries.

The CRO has the authority, when deemed necessary, to issue supplementary guidelines and limits.

CRO and CFO

In figure 1 below, the governance structure of risk and capital management in Nordea is illustrated.

Within the Group, two units, Group Credit and Risk Control and Group Corporate Centre, are responsible for risk, capital, liquidity and balance sheet management.

Group Credit and Risk Control is responsible for the risk management framework, consisting of policies, instructions and guidelines for the whole Group. Group Corporate Centre is responsible for the capital management framework including required capital as well as the capital base. Group Treasury, within Group Corporate Centre, is responsible for SIIR and liquidity risk.

The CRO is head of Group Credit and Risk Control and the CFO is head of Group Corporate Centre.

The CRO is responsible for the Group's credit, market and operational risk management framework. This includes the development, validation and monitoring of the rating and scoring systems, as well as the credit policy and strategy, the credit instructions, the guidelines to the

Figure 1 Risk, Liquidity and Capital Management governance structure



(Head: CRO)

Group Corporate Centre Group Credit and Risk Control (Head: CFO) Liquidity management framework Risk management framework Capital management framework Monitoring and reporting Balance sheet management framework

credit instructions as well as the credit decision process and the credit control processes.

The CFO is responsible for the capital planning process, which includes capital adequacy reporting, Economic Capital (EC) and parameter estimation used for the calculation of RWA and for liquidity and balance sheet management.

Each customer area and product area is primarily responsible for managing the risks arising from its operations. This responsibility entails identification, control and reporting, while Group Credit and Risk Control consolidates and monitors the risks on Group level and relevant sub levels.

3.2.2 Monitoring and reporting

The control environment in Nordea is based on the principles of separation of duties and strict independence of organisational units. Monitoring and reporting of risk is conducted on a daily basis for market and liquidity risk, on a monthly and quarterly basis for credit risk and on a quarterly basis for operational risk.

Risk reporting is regularly made to GEM and to the Board of Directors. The Board of Directors in each legal entity reviews internal risk reporting covering market, credit and liquidity risk per legal entity. Within the credit risk reporting, different portfolio analyses such as credit migration, current Probability of Default (PD) and stress testing are included.

The internal capital reporting includes all types of risks and is reported regularly to the Risk Committee, ALCO, CPF, GEM and Board of Directors.

Group Internal Audit makes an independent evaluation of the processes regarding risk and capital management in accordance with the annual audit plan.

3.2.3 Different risk types

There are different risk types which are described more in detail below in accordance with how they are structured within CRD.

Risk in pillar 1

In pillar 1, which forms the base for the capital requirement, three risk types are covered: credit risk, market risk and operational risk.

- Credit risk is the risk of loss if counterparts fail to fulfil their agreed obligations and that the pledged collateral does not cover the claims. The credit risk arises mainly from various forms of lending but also from guarantees and documentary credits, such as letters of credit. Furthermore, credit risk includes counterparty risk which is the risk that a counterpart in a foreign exchange (FX), interest rate, commodity, equity or credit derivative contract defaults prior to maturity of the contract and Nordea at that time has a claim on the counterpart. The measurement of credit risk is based on the parameters; PD, Loss Given Default (LGD) and Credit Conversion Factors (CCF).
- Market risk is the risk of loss in the market value of portfolios and financial instruments, also known as market price risk, as a result of movements in financial market variables. The market price risk exposure relates primarily to interest rates and equity prices and to a lesser degree to FX rates and commodity prices. For all other activities, the basic principle is that market risk is eliminated by matching assets, liabilities and off-balance sheet items.

• Operational risk is defined as the risk of direct or indirect loss, or damaged reputation resulting from inadequate or failed internal processes, from people and systems, or from external events. Legal and compliance risk as well as crime risk, project risk and process risk, including IT risk, constitute the main sub-categories to operational risk.

Risk in pillar 2

In pillar 2 other risk types are measured and assessed. These are managed and measured although they are not included in the calculation of the minimum capital requirements. In the calculation of EC most of the pillar 2 risk is included as well as risk in the life insurance operations. Examples of pillar 2 risk types are liquidity risk, business risk, interest rate risk in the non-trading book and concentration risk:

- Liquidity risk is the risk of being able to meet liquidity commitments only at increased cost or, ultimately, being unable to meet obligations as they fall due. The liquidity risk management focuses on both short-term liquidity risk and long-term structural liquidity risk. The liquidity risk management includes a business continuity plan and stress testing for liquidity management. In order to measure the exposure, a number of liquidity risk measures have been developed.
- Business risk represents the earnings volatility inherent in all business due to the uncertainty of revenues and costs due to changes in the economic and competitive environment. Business risk in the EC framework is calculated based on the observed volatility in historical profit and loss that is attributed to business risk.

- Interest rate risk in the non-trading book consists of exposures deriving from the balance sheet (mainly lending to public and deposits from public) and from hedging the equity capital of the Group. The interest rate risk inherent in the non-trading book is measured in several ways on a daily basis and in accordance with the financial supervisory authorities' requirements. The market risk in investment portfolios includes equity, interest rate, private equity, hedge fund and FX risk and is included as market risk in the EC framework.
- Pension risk is included in market risk EC and includes equity, interest rate and FX risk in Nordea sponsored defined pension plans.
- Real estate risk consists of exposure to owned and leased properties and is included in the market risk EC.
- Concentration risk is the credit risk related to the degree of diversification in the credit portfolio, i e the risk inherent in doing business with large customers or not being equally exposed across industries and regions. The concentration risk is measured by comparing the output from a credit risk portfolio model with the risk weight functions used in calculating RWA. The concentration risk is included in the EC framework.

4. Credit risk

Credit risk is the largest risk comprising approximately 90% of the total RWA. The information in this chapter is disclosed in several dimensions aiming to give an in depth view of the distribution of the credit portfolio in different exposure classes, geography, industries, risk weights etc.

In appendix 12.2 the definition of exposure classes and calculation principles of credit risk RWA in pillar 1 can be found.

4.1 Credit process

4.1.1 Roles and responsibilities in credit risk management

Group Credit and Risk Control is responsible for the credit risk management framework, consisting of policies, instructions and guidelines for the Group.

Each customer area and product area is primarily responsible for managing the credit risks in its operations, while Group Credit and Risk Control consolidates and monitors the credit risks on both Group level and sublevels.

Within the powers-to act granted by the Board of Directors, credit risk limits are approved by decision-making authorities on different levels in the organisation (see figure 2).

The responsibility for a credit exposure lies with a customer responsible unit. Customers are assigned a rating or scoring in accordance with the framework for quantification of credit risk.

4.1.2 Credit risk identification

Credit risk is defined as the risk of loss if counterparts fail to fulfil their agreed obligations and that the pledged collateral does not cover the claims.

The credit risks stem mainly from various forms of lending to the public (corporate and household customers), but also from guarantees and documentary credits, such as letters of credit. The credit risk from guarantees and documentary credits arises from the potential claims on customers, for which Nordea has issued guarantees or documentary credits. Furthermore, credit risk may also include counterparty credit risk, transfer risk and settlement risk.

Counterparty risk is the risk that the counterpart in an FX, interest, commodity, equity or credit derivatives contract defaults prior to maturity of the contract and that the bank at that time has a claim on the counterpart.

Settlement risk is the risk of losing the principal on a financial contract, due to a counterpart's default during the settlement process. Further information about counterparty risk and settlement risk is available in section 7.2 in this report.

Transfer risk is a credit risk attributable to the transfer of money from a country where a borrower is domiciled, and is affected by changes in the economic and political situation of the countries concerned.

Risks in specific industries are followed by industry monitoring groups and managed through industry policies, which establish requirements and limits on the overall industry exposure. Corporate customers' environmental risks are taken into account in the overall risk assessment through the so-called Environmental Risk Assessment Tool. This tool is currently being extended to also include assessment of social and political risk.

For larger project finance transactions, the bank has adopted the Equator Principles, which is a financial industry benchmark for determining, assessing and managing social and environmental risk in project financing. The Equator Principles are based on the policies and guidelines of the World Bank and International Finance Corporation.

4.1.3 Decisions and monitoring of credit risk

The decisions regarding credit risk limits for customers and customer groups are made by the relevant credit decision authorities on different levels within the Group.

The responsibility for credit risk lies with the customer responsible unit, which on an ongoing basis assesses customers' ability to fulfil their obligations and identifying deviations from agreed conditions and weaknesses in the customers' performance.

In addition to building strong customer relationships and understanding each customer's financial position, monitoring of credit risk is based on all available information from internal systems, such as late payments data, behavioural scoring migration and macroeconomic circumstances.

If new information indicates the need, the customer responsible unit must reassess the rating and assess whether the exposure is impaired if the customer's repayment ability is threatened.

If it is considered unlikely that the customer will be able to repay its debt obligations, for example the principal, interest, or fees, and the situation cannot be satisfactorily

Figure 2 Credit decision-making structure



remedied, then the exposure is regarded as defaulted. Exposures that have been past due more than 90 days are automatically regarded as defaulted.

If credit weaknesses are identified in relation to a customer exposure, that exposure is assigned special attention in terms of review of the risk. In addition to the continuous monitoring, an action plan is established outlining how to minimise a potential credit loss. If necessary, a special team is set up to support the customer responsible unit.

4.1.3.1 Collateral policy and documentation

Local instructions emphasise that national practice and routines are timely and prudent in order to ensure that collateral items are controlled by the bank and that the loan and pledge agreement as well as the collateral is legally enforceable. Thus the bank holds the right to liquidate collateral in event of the obligor's financial distress and the bank can claim and control cash proceeds from a liquidation process.

To a large extent national standard loan and pledge agreements are used, ensuring legal enforceability.

4.1.3.2 Types of collateral commonly accepted

The following collateral types are most common in Nordea: • Residential real estate, commercial real estate and land

- which are situated in Nordea's core markets.
- Other physical assets such as machinery, equipment, vehicles, vessels, aircrafts and trains.
- Inventory, receivables (trade debtors) and assets pledged under floating charge.
- Financial collateral such as listed shares, listed bonds and other specific securities.
- Deposits.
- Guarantees and letters of support.
- Insurance policies (capital assurance with surrender value).

For each type, more specific instructions are added to the general valuation principle. A specific maximum collateral ratio is set for each type. Restrictions for acceptance refer in general to assessment of the collateral value rather than the use of the collateral for credit risk mitigation as such. In the RWA calculations, the collateral must fulfil certain eligible criteria.

4.1.3.3 The credit decision process and handling of collateral Credit risk measures are part of the approval in the credit decision process. Each corporate and institutions customer is reviewed at least annually in the annual review process. Each credit exposure is reviewed at least annually in the annual review of the customer. Furthermore, for some customers who have been assessed to have a high risk of default, an even more detailed review takes place in order to ensure an actual valuation and legal enforceability of collateral. Business and credit strategies towards the customer or customer group are also reviewed in detail.

4.1.4 Rating and scoring

The common element of both rating and scoring is the ability to classify and rank customers according to their default risk. They are used as integrated parts of the risk management and decision-making process, including:

- The credit approval process.
- Calculation of RWA.
- Calculation of EC and Expected Loss (EL).
- Monitoring and reporting of credit risk.
- Performance measurement using the Economic Profit framework.

While the rating is used for corporate customers, institution counterparts as well as sovereigns ¹), scoring is used for households as well as small business customers.

A rating is an estimate that exclusively reflects the quantification of the repayment capacity of the customer, i e the risk of customer default. The rating scale in Nordea consists of 18 grades from 6+ to 1– for non-defaulted customers and 3 grades from 0+ to 0– for defaulted customers. The repayment capacity of each rating grade is quantified by a one year PD.

Rating grades 4– and higher are comparable to investment grade as defined by external rating agencies such as Moody's and Standard & Poor (S&P). Rating grades 2+ and lower are considered as weak or critical, and require special attention. In table 2, the mapping from the internal rating scale to the S&P's rating scale, using condensed scales, is shown.

Table 2 Indicative mapping between internalrating and Standard & Poor's

Rat	ing
Internal	Standard & Poor's
6+, 6, 6-	AAA to AA
5+, 5, 5-	А
4+,4,4-	BBB
3+, 3, 3-	BB
2+, 2, 2-	В
1+, 1, 1-	CCC to C
0+, 0, 0-	D

The mapping of the internal ratings to the S&P's rating scale is based on a predefined set of criteria, such as comparison of default and risk definitions. The mapping does not intend to indicate a fixed relationship between Nordea's internal rating grades and S&P's rating grades since the rating approaches differ. On a customer level the mapping does not always hold and, moreover, the mapping may change over time.

Ratings are assigned in conjunction with credit proposals and the annual review of the customers, and approved by the credit committees. However, a customer is downgraded as soon as new information indicates a deterioration in the customer's repayment capacity. The consistency and transparency of the ratings are ensured by the use of rating models.

¹⁾ Sovereigns include central governments, central banks, regional governments, local authorities and other public sector entities

A rating model is a set of specified and distinct criteria which, given a set of customer characteristics, produces a rating that ranks the customer based on its repayment capacity. Rating models are based on the principle that it is possible to derive a prediction of future customer performance from the default history of past customers on the basis of their characteristics. In order to better reflect the risk of customers in industries with highly distinctive characteristics, Nordea has decided upon a differentiation of rating models. Aside from a general corporate model used to rate the majority of industries, a number of specific models have been developed for specific segments, such as shipping and real estate management, taking into account the unique characteristics of these segments. Moreover, in each model the development methodology may vary. These methods range from purely statistical models based on internal data to expert-based models. In general however, all rating models are based on an overall framework, in which financial and quantitative factors are combined with qualitative factors.

Scoring models are pure statistical methods used to predict the probability of customer default. The models are used in the household segment as well as for small corporate customers. Nordea utilises bespoke behavioural scoring models developed on internal data to support both the credit approval process, e g automatic approvals or decision support, as well as the risk management process, where "early warnings" can be issued for high risk customers and monitoring of portfolio risk levels can be closely monitored. As a supplement to the behavioural scoring models Nordea also utilises commercial credit bureau information in the credit process.

4.2 Exposures versus lending

The credit process is essential in verifying that lending is given to solid counterparts. In IFRS the term lending is used, whereas exposures are used in the CRD. For several reasons the principles for how these terms are used differs. In both disclosures the items booked in the balance sheet on and off balance are included but presented in different ways. The main differences will be outlined in this section clarifying and highlighting the bridge between the information presented in the balance sheet in the Annual report and this report. A detailed definition of exposure classes used in the capital adequacy calculations can be found in appendix 12.3.

Tables presented in this chapter, containing exposure, are presented as Exposure At Default (EAD) or original exposure. EAD is the exposure after applying credit conversion factors (CCF) and original exposure before applying CCF. See chapter 7 for further information about off balance, where this is further explained. The figures presented are aggregated from transaction level in EUR. The tables are presented in EURm, which can lead to small rounding discrepancies in the tables. The numbers for 2007 have not been restated following the financial supervisory authority approval of Retail IRB end of December 2008.

4.2.1 Differences as regards to classification of exposure The main differences and the effect on comparisons

between the exposures are presented below.

• The exposure distributions by industry and by geography are in this report presented for the entire credit portfolio, whereas in the financial reporting, these distributions are presented for loans and receivables to the public (lending), being the main part of the on balance sheet exposure.

- Treasury bills and interest-bearing securities are in this report partly included in the capital requirements for market risk, whereas in the financial reporting, these are included in the credit risk exposure.
- Reversed repurchase agreements are in this report included as a separate exposure type, whereas in the financial reporting, these are included in the on balance sheet item loans and receivables to the public (corporate/institutions) or as off balance.
- In the financial reporting loans and receivables to the public (corporate) consist of the on balance sheet exposure in the Corporate exposure class as well as smaller part of the Retail exposure class (non-rated SMEs).
- Equity holdings related to insurance operations are included in the annual report, but excluded in this report since the insurance operations are deducted from the capital base based on the fact that insurance companies are subject to specific solvency regulations.
- Intangible assets and deferred taxes are deducted from the capital base and are therefore not included in the RWA calculations. In the financial reporting these items are included in the balance sheet.

The credit risk exposures presented in this report are distributed by exposure class, where each exposure class is distributed into the following different exposure types:

- On balance sheet items.
- Off balance sheet items (e g guarantees and unutilised amounts of credit facilities).
- Securities financing (e g reversed repurchase agreements).
- Derivative contracts.

In the annual report, the credit risk exposure includes:

- On balance sheet items: loans and receivables to credit institutions and loans and receivables to the public (e g reversed repurchase agreements).
- Off balance sheet items (e g guarantees and unutilised amounts of credit facilities).
- Counterparty risk in derivative contracts.
- Credit risk in treasury bills and interest-bearing securities.

Table 3 Link between balance sheet and CapitalAdequacy, 31 Dec 2008, EURm

Loans and receivables to credit institutions	18,686
Loans and receivables to the public	251,265
Cash and balances with central banks	3,152
Other assets and prepaid expenses	10,805
Interest bearing securities, treasury bills	
and pledged instruments	17,033
Other	2,036
On-balance sheet exposure (Banking book)	302,977
Items related to capital requirements for market risk	34,766
 of which treasury bills and other eligible bills 	2,099
- of which loans and receivables to credit institutions	53
 of which loans and receivables to the public 	442
 of which interest-bearing securities 	23,460
- of which other	8,712
Derivatives	86,838
Repos	16,246
Life insurance operations ¹)	31,590
Other ²⁾	1,657
Total assets balance sheet	474,074

¹⁾ Intragroup exposures in the Life operations are treated as external

from a credit risk perspective.

2) Other includes adjustments of provisions, deferred taxes and intangible assets.

In table 3, the link between the balance sheet and the capital adequacy is presented, as regards to on balance items. It can be concluded that the on balance sheet exposure in this report equals 302,977 (original exposure) and consists mainly of loans and receivables but also of interest bearing securities in the banking book. The other assets in the balance sheet are not included in the on balance sheet items part of the credit exposure but treated differently depending on type of asset. The counterparty risk from derivatives and repos are included in the credit exposure, while assets related to the trading book are included in market risk RWA calculations. Life insurance operations are excluded.

4.3 Development of exposure

Throughout this chapter, the credit risk exposure is presented based on definitions and approaches used in the calculation of capital requirement. In June 2007, Nordea received approval by the financial supervisory authorities





Table 4 Exposure classes split by exposure type

to use FIRB approach for corporate and institution exposure classes in Denmark, Finland, Norway and Sweden. In December 2008 Nordea was approved of using the IRB approach for the Retail exposure class in Denmark, Finland, Norway and Sweden (with the exception for the finance companies in all countries that were not applied for). The standardised approach is used for the remaining portfolios, such as foreign branches and subsidiaries in Luxembourg, Russia and Poland.

Nordea aims to continue the roll-out of the IRB approaches. The main focus is the development of advanced IRB for corporate customers in the Nordic area, including internal estimates of LGD and CCF. Roll-out of the IRB approach for the Finance company in Finland is planned to 2009.

The standardised approach will continue to be used for smaller portfolios and new portfolios for which approved internal models are not yet in place. An overview of the roll-out plan is displayed below in figure 3.

4.3.1 Exposure type by exposure class

In table 4, the exposures as of 31 December 2007 and 31 December 2008 are split by exposure classes and exposure types. For more detailed information about off balance and derivatives, see chapter 7. The table is split between exposure classes subject to the IRB approach and exposure classes subject to the standardised approach. The shift from the standardised approach to the IRB approach can be seen when comparing exposures in 2008 with 2007. As of 31 December 2008, the IRB approaching is used for 83% of the total credit exposure compared to 52% in 31 December 2007. The retail portfolio comprises 36% of the total credit risk exposure in the IRB exposure class.

It can be concluded that the main part of the exposure is within the corporate and retail portfolios. Out of the total retail portfolio approximately 92% of the exposures relate to the approved IRB retail portfolio. The parts remaining in standardised approach are the foreign branches, subsidiar-

Dorivativo

	On balance	Off balance	Securities	(counter-	Total
31 Dec 2008, EURm	sheet items	sheet items	financing	party risk)	EAD
IRB exposure classes					
Institutions	26,208	2,211	147	20,577	49,143
Corporate	107,690	31,873	54	12,398	152,015
Retail	105,994	9,960		91	116,045
 of which mortgage 	84,677	1,559			86,236
 of which other retail 	18,038	7,544		67	25,649
- of which SME	3,278	857		24	4,160
Other non-credit obligation assets	1,838				1,838
Total IRB approach	241,730	44,044	201	33,067	319,042
Standardised exposure classes					
Central governments and central banks	19,650	366	400	543	20,959
Regional governments and local authorities	6,615	335		474	7,425
Institution	3,913	169		542	4,624
Corporate	18,194	2,678		88	20,960
Retail	9,467	272			9,739
Exposures secured by real estates	534	23			558
Other ¹⁾	2,192	5		13	2,210
Total standardised approach	60,565	3,850	400	1,661	66,475
Total EAD	302.295	47.893	601	34,727	385.517

¹⁾ Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items, short-term claims, covered bonds, and other items.

cont. Table 4 Exposure classes split by exposure type

				Derivatives	
	On balance	Off balance	Securities	(counter-	Total
31 Dec 2007, EURm	sheet items	sheet items	financing	party risk)	EAD
IRB exposure classes					
Institutions	21,344	2,466	600	17,182	41 <i>,</i> 591
Corporate	97,966	31,877	313	3,939	134,095
Other non-credit obligation assets	827				827
Total IRB approach	120,136	34,343	913	21,121	176,513
Standardised exposure classes					
Central governments and central banks	16,288	88	12	442	16,831
Regional governments and local authorities	7,266	274		144	7,684
Institution	575	366	2	553	1,497
Corporate	13,684	2,387	13	259	16,343
Retail	24,362	824		34	25,220
Exposures secured by real estates	85,989	40			86,030
Other ¹⁾	1,747	16		10	1,773
Total standardised approach	149,913	3,995	27	1,443	155,378
Basel I reporting entities					7,101
Total EAD	270,049	38,338	940	22,564	338,993

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items, short-term claims, covered bonds, and other items.

ies in Poland, Luxemburg and Russia and the retail exposures in the finance companies as well as exposures towards sovereigns. Approximately 42% of the exposure class IRB Institutions relate to counterparty credit risk exposures stemming from derivatives.

The exposure class Corporate calculated according to the IRB approach include off balance sheet exposures which comprise 21% of the total exposure.

The total credit risk exposure (IRB and Standardised) has increased with 14% compared to previous year. The increase is mainly related to exposure class corporate following Nordea's organic growth strategy. The main changes are within on balance and derivatives items, whereas the off balance sheet exposures are relatively unchanged.

During 2008 the business in the New European Markets has increased due to opening of new branches and a selective organic growth strategy. This has an impact on the increase in standardised corporate. More information regarding the development in New European Market can be found in 4.3.2.

In table 5, the average exposure during 2008 is presented. The retail exposures are presented as standardised approach since the IRB approach was approved late December 2008.

Table 5 Exposure classes split by exposure type, Average exposure during 2008

20,267	2,581	599	19,238	42,686
106,811	32,775	324	7,049	146,959
1,724				1,724
128,802	35,357	923	26,287	191,369
17,502	247	100	496	18,344
7,141	317		262	7,720
2,915	117		605	3,637
17,809	2,907	2	219	20,937
28,617	4,103		63	32,783
88,346	453			88,798
1,947	4		17	1,968
164,277	8,148	102	1,661	174,188
293,079	43,504	1,025	27,949	365,557
	sheet items 20,267 106,811 1,724 128,802 17,502 7,141 2,915 17,809 28,617 88,346 1,947 164,277 293,079	sheet items sheet items 20,267 2,581 106,811 32,775 1,724 35,357 1 32,775 1,724 35,357 1 117,502 2,915 117 17,809 2,907 28,617 4,103 88,346 453 1,947 4 164,277 8,148 293,079 43,504	sheet items sheet items financing 20,267 2,581 599 106,811 32,775 324 1,724	sheet items sheet items financing party risk) 20,267 2,581 599 19,238 106,811 32,775 324 7,049 1,724

¹⁾ Retail is presented in the standardised approach since the approval was achieved in late December. The average exposure is calculated on quarterly data.

2) Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items, short-term claims, covered bonds, and other items.

The average exposure during 2008 is lower than the exposure at year end 2008 due mainly to that the exposures to corporate and retail customers have gradually increased during the year. The IRB corporate portfolio has had a steady growth during the three first quarters (8% based on original exposure). In the last quarter the growth has been lower as a consequence of the financial turmoil as well as the FX rate fluctuations in EUR/NOK and EUR/SEK.

Retail mortgage exposure has increased gradually over the year, but at a slowing growth rate.

Exposure to central government and central banks has increased stemming mainly from Sweden where Nordea

has increased exposure to central bank and other state banks. The increased exposure in standardised corporate is related to the growth in New European Markets. The increase was mainly during the first three quarters in 2008.

Nordea has not securitised assets as defined in CRD from its ordinary lending portfolio (banking book), therefore no exposure are defined and classified in the securitisation exposure class. For details about Nordea's activities in the securitisation area, see chapter 7.

4.3.2 Exposure by geography

In table 6, exposures as of end December 2007 and 2008 are split by main geographical areas, based on where the credit

Table 6 Exposure split by geography and exposure classes

31 Dec 2008, EURm	countries	Denmark	Finland	Norway	Sweden	countries	Poland	Russia	OtherT	otal EAD
IRB exposure classes										
Institutions	49,144	8,090	26,003	4,171	10,880					49,144
Corporate	152,015	37,461	44,579	32,132	37,843					152,015
Retail	116,045	41,582	28,326	18,866	27,271					116,045
Other non-credit obligation assets	s 1,838	650	518	142	528					1,838
Total IRB approach	319,042	87,783	99,426	55,311	76,522					319,042
Standardised exposure classes										
Central governments and central banks	19,877	3,924	7,446	1,459	7,048	698	74	11	299	20,959
Regional governments and local authorities	7,336	694	2,001	408	4,233	87			1	7,424
Institution	620	601	1	2	16	892	416	63	2,633	4,624
Corporate	244	46	99	31	68	5,211	1,226	4,052	10,229	20,962
Retail	5,513	918	3,026	714	855	2,528	1,537	1	160	9,739
Exposures secured by real estates	90	90					329		324	558
Other ¹⁾	1,571	627	250	269	425	93	87	360	98	2,209
Total standardised approach	35,251	6,900	12,823	2,883	12,645	9,509	3,484	4,487	13,744	66,475
Total EAD	354,293	94,683	112,249	58,194	89,167	9,509	3,484	4,487	13,744	385,517

	Nordic	- of which	- of which	- of which	- of which	Baltic				
31 Dec 2007, EURm	countries	Denmark	Finland	Norway	Sweden	countries	Poland	Russia	OtherT	otal EAD
IRB exposure classes										
Institutions	41,590	8,819	21,436	4,047	7,288					41,590
Corporate	134,096	32,536	33,344	30,845	37,371					134,096
Other non-credit obligation assets	s 827	166	227	114	320					827
Total IRB approach	176,513	41,521	55,007	35,006	44,979					176,513
Standardised exposure classes										
Central governments and central banks	16,488	4,660	7,977	1,912	1,939	334			10	16,832
Regional governments and local authorities	7,637	336	2,143	218	4,940	47				7,684
Institution	37	1	1	2	33	880			580	1,497
Corporate	2,282	855	848	244	335	4,071	52		9 <i>,</i> 938	16,343
Retail	23,169	8,553	7,682	3,014	3,920	2,034				25,221
Exposures secured by real estates	86,030	26,614	18,761	16,749	23,906					86,030
Other ¹⁾	1,667	523	343	250	551	105				1,772
Total standardised approach	137,310	41,542	37,755	22,389	35,624	7,471	52		10,546	155,379
Basel I reporting entities							2,743	1,748	2,610	7,101
Total EAD	313,823	83,063	92,762	57,395	80,603	7,471	2,795	1,748	13,156	338,993

¹⁾ Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items, short-term claims, covered bonds, and other items.

risk is referable. The main markets for Nordea are the Nordic countries and the New European Market (Estonia, Latvia, Lithuania, Poland and Russia) together with New York branch, London branch and Luxembourg.

The exposure in Finland represents 29% of the total exposure in the Group while Denmark represents 25%, Sweden 23% and Norway 15%. The main reason for the large relative share in Finland relates to business activities in Markets and Trade finance being centralised to Finland.

During 2008, the corporate exposure in Finland increased with 34%, mainly due to increase in the counterparty risk in derivatives. Also, the relatively large exposure amount in the exposure class Institutions in Finland is explained by the fact that the main part of the Group's counterparty credit risk derivative exposures are booked in Finland. Overall, the exposures to institutions fluctuate much during the year, following the ordinary pattern for short lending in the interbank market.

Exposures in the New European Markets, are increasingly in accordance with the strategic plans. The sharp slowdown in the GDP-growth in the Baltic countries has also led to a slowing lending growth during 2008. The increased corporate exposure in New European market is both related to new local customers as well as to Nordic customers.

4.3.3 Exposure by industry

In table 7 the total exposure as of 31 December 2008 is split by important industries and by the main exposure classes.

The main exposures in the IRB corporate portfolio relate to industrial commercial services and real estate management and investment. These industries comprise approximately 34% of the total exposure in the portfolio. In the industrial commercial services 53% of the exposures are concentrated to 100 customers.

In the retail portfolio the main exposures are within retail mortgage and other personal consumer lending. The SME exposure is mainly related to retail trade, real estate management and industrial commercial services.

4.3.4 Equity holdings

In the exposure class "Other items", Nordea's equity holdings outside the trading book are included. Investments in companies where Nordea holds over 10% of the capital are

Table 7 Exposure split by industry group, 31 Dec 2008

]	Internal ratin	g based appı	oach	Standardised approach		L	
ELID	La stitustica (2	n C	Other on-credit bligation	Central governments and	Regional government and local	Oth1)	
EURM	Institution C	Lorporate	Retail	assets	central banks	authorities	Other 1)	
Retail mortgage			86,236				558	
Other retail			25,649			= (25	9,739	
governments					5,944	7,425		
Banks	27,362		1		15,015		51	
Construction and engineering		3,307	428				536	
Consumer durables (cars, appliances etc)		3,610	64				555	
Consumer staples		12,697	252				814	
(food, agriculture etc)								
Energy (oil, gas etc)		3,303	1				572	
Health care and pharmaceuticals		1,731	123				321	
Industrial capital goods		5,916	40				339	
Industrial commercial services		19,442	686				452	
IT software, hardware and services		1,268	75				172	
Media and leisure		2,603	282				214	
Metals and mining materials		694	7				53	
Paper and forest materials		3,136	34				362	
Real estate management and investment		31,948	893				1,633	
Retail trade		9,308	587				1,291	
Shipping and offshore		9,258	6				3,675	
Telecommunication equipment		803	3				68	
Telecommunication operators		2,778	4				61	
Transportation		3,014	184				654	
Utilities (distribution and production)		6,998	15				467	
Other financial companies Other materials (chemical, building materials etc)	21,782	10,381 5,399	27 104				726 1,268	
Other		14,420	344	1,838			13,514	
Total EAD ¹⁾ Administrative bodies and non-commercial una corporate, past due items, short term claims of	49,143 dertakings, multilateral	152,015 developments ba er items.	116,045 nks, standardised	1,838 institution, stand	20,959 ardised	7,425	38,093	

deducted from the capital base (see table 1) and hence not included in the "other items".

In table 8, Nordea's equity holdings outside the trading book are grouped based on the intention of the holding. In the investment portfolio, holdings in private equity funds are included with EUR 186m. All equities in the table are booked at fair value. The evidence of published price quotations in an active market is the best evidence of fair value and when they exist they are used to measure the value of financial assets and financial liabilities. For equities with no published price quotations, internal valuation techniques are used to establish fair value. The table below shows to what extent published price quotations are used.

4.4 Calculation of RWA

The risk weight and EAD calculations in Nordea differ between approaches but also depending on the exposure classes within IRB approach. In table 9, the exposure, EAD, average risk weight expressed as percentages, RWA and capital requirement, are distributed by exposure class, which serves as the basis for the reporting of capital requirements to the authorities. In this report the IRB exposure classes that Nordea has been approved for are presented. The retail portfolio is divided in three sub-segments; mortgage (credit risk exposures to private individuals, pledged by real estate), other retail (exposures to private individuals, except mortgage) and SME (exposures to small and medium sized enterprises, including loans secured by real estate collateral).

For the remaining portfolios the standardised approach exposure classes are used. Some exposure classes have been merged in the table, due to low exposures in these exposure classes.

The main reason for the reduction in the average risk weight is the introduction of the IRB approach for retail exposures, which has lowered the risk weight from an average of 47% in 2007 to an average risk weight of 39% for the portfolio.

The main increase, as mentioned earlier, is seen in the corporate exposure class. The average risk weight of the corporate exposures is however stable showing a growth in high rated customer groups.

The following sections describe the principles for calculating RWA with the IRB and the standardised approach respectively.

D 1' 1

Table 8 Equity holding outside trading book, 31 Dec 2008

EURm	Book value	Fair value	Unrealized gains loss	gains/losses period YTD	Capital requirement
Investment portfolio ¹⁾	375	375	-103	120	30
Other ²⁾	65	65	-13	7	5
Total	440	440	-116	127	35
¹⁾ of which listed equity holdings.	121				
²⁾ of which listed equity holdings.	43				

Table 9 Capital requirement for credit risk

	Original	1	Average risk		Capital
31 Dec 2008, EURm	exposure	EAD	weight	RWA	requirement
IRB exposure classes					
Institutions	52,401	49,143	26%	12,699	1,016
Corporate	214,072	152,015	57%	86,358	6,909
Retail	120,390	116,045	16%	18,313	1,465
 of which mortgage 	86,788	86,236	10%	8,925	714
 of which other retail 	28,981	25,649	31%	8,065	645
– of which SME	4,621	4,160	32%	1,323	106
Other non-credit obligation assets	2,226	1,838	100%	1,837	147
Total IRB approach	389,088	319,042	37%	119,208	9,537
Standardised exposure classes					
Central government and central banks	19,752	20,959	4%	840	67
Regional governments and local authorities	9,126	7,425	1%	100	8
Institution	4,310	4,624	20%	903	72
Corporate	30,402	20,960	99%	20,719	1,658
Retail	13,864	9,739	77%	7,469	598
Exposures secured by real estates	564	558	73%	406	33
Other ¹⁾	2,327	2,210	50%	1,099	88
Total standardised approach	80,346	66,476	47%	31,538	2,523
Total	469,434	385,517	39%	150,746	12,060

¹⁾ Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items, short term claims,

covered bonds, and other items.

Table 9 Capital requirement for credit risk

	Original		Average risk		Capital
31 Dec 2007, EURm	exposure	EAD	weight	RWA	requirement
IRB exposure classes					
Institutions	44,328	41,591	22%	9,302	744
Corporate	197,800	134,095	55%	73,736	5 <i>,</i> 899
Other non-credit obligation assets	1,186	827	100%	827	66
Total IRB approach	243,314	176,513	48%	83,865	6,709
Standardised exposure classes					
Central government and central banks	17,670	16,831	1%	188	15
Regional governments and local authorities	9,113	7,684	1%	55	4
Institution	1,698	1,497	30%	452	36
Corporate	22,417	16,343	100%	16,343	1,307
Retail	38,432	25,220	75%	18,916	1,513
Exposures secured by real estates	87,680	86,030	35%	30,498	2,440
Other ¹⁾	1,862	1,773	50%	890	71
Total standardised approach	178,871	155,378	43%	67,342	5,387
Basel I reporting entities	7,101			5,745	460
Total	429,286	331,892	47%	156,952	12,556

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items,

short term claims, covered bonds, and other items. Associated companies not included.

4.4.1 Calculation of RWA with the IRB approach

The FIRB approach is used for calculating the minimum capital requirements for exposures to institutions and corporate customers. Credit risk is measured using sophisticated formulas for calculating RWA. Input parameters are Nordea's internal estimate of PDs and inputs fixed by the financial authorities supervisory for LGD, EAD and maturity.

Internal estimates of PD, LGD and EAD are used for the IRB approach for retail exposures, which in turn are based on internal historical loss data.

4.4.1.1 Probability of default (PD)

PD means the likelihood of default of a counterpart. The PD represents the long-term average of yearly default rates. The internal credit risk classification models (rating models for corporate customers and institutions and scoring models for retail customers) provide an estimation of the repayment capacity of a counterpart. The internal risk classification scale consists of 18 grades for non-defaulted customers and 3 grades for defaulted customers. All customers with the same risk classification are expected to have the same repayment capacity; independent of the customers' industry, size, etc.

Table 10 Exposure towards Institutions, distributed by rating grade 1)

EURm		31 Dec 2008 Institutions	3		31 Dec 2007 Institutions	7
Rating	PD scale	EAD	Average risk weight	PD scale	EAD	Average risk weight
6+	0.03%	7,671	15%	0.03%	6,426	13%
6	0.03%	13,847	16%	0.03%	19,031	16%
6–	0.05%	7,947	20%	0.05%	6,174	18%
5+	0.07%	8,323	24%	0.07%	4,238	25%
5	0.10%	3,745	31%	0.10%	2,100	31%
5–	0.16%	4,413	37%	0.14%	1,413	37%
4+	0.24%	471	50%	0.20%	509	45%
4	0.35%	583	60%	0.32%	179	60%
4–	0.53%	484	76%	0.54%	474	76%
3+	0.81%	253	91%	0.85%	186	92%
3	1.18%	143	104%	1.31%	143	106%
3–	2.01%	83	122%	2.04%	128	121%
2+	3.63%	355	124%	3.39%	60	139%
2	6.16%	138	164%	5.21%	182	161%
2–	9.86%	56	187%	8.29%	24	154%
1+	14.79%	9	234%	12.43%	16	221%
1	20.71%	12	254%	17.74%	5	246%
1–	26.93%	1	263%	26.85%	2	263%
	0.14% ²⁾	48,532	26%	0.11% ²⁾	41,291	22%

¹⁾ Exposure includes rated perforing customers.

2) Exposure weighted PD.

Rating distribution

In tables 10 to 12, the exposure is distributed over the internal risk classification scale for the exposures in the IRB exposure classes. The PD and the average risk weight are weighted based on EAD. The risk weight is a function of PD and the lower the PD is, the lower the risk weight. The exposure distributions on the rating scale are illustrated in figure 4 to 6.

Institutions

In December 2008, approximately 98% of the exposures to institutions are found in the nine highest rating grades. The exposure to institution fluctuates over time and has mainly a maturity of less than 3 months. The exposures towards the institutions fluctuate relatively much compared with other exposure classes. This is due to that inter bank lending has relatively short maturity.

As can be seen in table 10 the relative exposure distribution in 2008 has decreased in rating grade 6. This is due to mainly two reasons. Firstly the exposures towards other institutions fluctuate which in turn affects the relative distribution when comparing two periods. Secondly there are many institutions that have received a lower rating in the internal process and are affected by migration. More information about the migration can be found in the migration chapter below.

Corporate

In December 2008, approximately 73% of the exposures to corporate customers are found in the nine highest rating grades.

As part of the estimation and validation, the limit from which counterparts were classified as belonging to the exposure class corporate was increased from 100,000 EUR

Figure 4 Exposure distributed by rating grades, IRB Institutions



Figure 5 Exposure distributed by rating grades, IRB Corporate



Table 11 Exposure towards Corporate, distributed by rating grade 1)

EURm		31 Dec 2008 Corporate			31 Dec 2007 Corporate	
Rating	PD scale	EAD	Average risk weight	PD scale	EAD	Average risk weight
6+	0.03%	1 946	12%	0.03%	2 610	14%
6	0.03%	4 438	15%	0.03%	2,010	15%
6-	0.05%	5.075	19%	0.05%	3 873	13%
5+	0.07%	8.855	24%	0.07%	7,532	20%
5	0.10%	12,290	29%	0.10%	10.509	29%
5-	0.16%	16.079	37%	0.14%	14,184	35%
4+	0.24%	17.851	45%	0.20%	19,392	41%
4	0.35%	23,643	56%	0.32%	20,721	53%
4–	0.53%	18,865	66%	0.54%	16,740	67%
3+	0.81%	14,205	77%	0.85%	13,656	80%
3	1.18%	10,982	89%	1.31%	10,621	93%
3–	2.01%	9,513	98%	2.04%	7,209	101%
2+	3.63%	2,260	119%	3.39%	1,046	113%
2	6.16%	1,406	142%	5.21%	814	131%
2–	9.86%	635	160%	8.29%	462	146%
1+	14.79%	232	172%	12.43%	164	174%
1	20.71%	308	227%	17.74%	77	202%
1–	26.93%	100	247%	26.85%	43	220%
	0.72% ²⁾	148,684	57%	0.61% ²⁾	131,947	55%

1) Exposure includes rated performing customers.

²⁾ Exposure weighted PD.

Table 12 Exposure towards Retail,distributed by risk grade 1)

EURm		Retail	
Risk grade	PD scale	EAD	Average risk weight
A+	0.08%	28,364	3%
А	0.11%	14,041	5%
A–	0.16%	10,606	7%
B+	0.22%	11,404	9%
В	0.31%	9,298	11%
В-	0.43%	8,582	14%
C+	0.60%	6,931	19%
С	0.84%	5,270	23%
C-	1.17%	4,047	28%
D+	1.64%	4,474	34%
D	2.30%	2,933	39%
D-	3.20%	2,573	45%
E+	4.47%	2,833	51%
Е	6.30%	862	53%
E-	8.79%	492	59%
F+	12.28%	715	61%
F	17.19%	183	78%
F-	24.04%	741	90%
	0.89% ²⁾	114,349	16%

¹⁾ Exposure includes scored performing customers.

2) Exposure weighted PD.

Figure 6 Exposure distributed by risk grades, IRB Retail, 2008



Figure 7a Institution rating migration, EAD that have been up or down graded during 2008



to 250 000 EUR in beginning of 2008. As a consequence of the validation, the PD scale was updated. The table shows that growth has been achieved without reducing the requirements on solid credit quality, i.e. the growth is seen in the better rating grades. The development of the average risk weight is affected by the changes in PD, rating migration, LGD and other parameters. The graphs show the relative distribution of rating 2008 compared with 2007. The average risk weight is affected by not only PD. The collateral and size of the counterpart etc are other factors that need to be taken into account when analysing the changes.

The figures shows the relative distribution in 2008 compared with 2007.

Retail

The risk grade master scale used for scored customers in the Retail portfolio consists of 18 grades, named A+ to F–. In December 2008, approximately 86% of the exposures to Retail customers are found in the nine highest rating grades. In the sub-exposure class retail mortgage approximately 90% of the customers are in the nine highest rating grades. For retail other and retail SME the corresponding figures are 74% and 69%.

Migration

The rating/scoring distribution changes over time intervals mainly due to three factors:

- 1. The rating distribution for new customers and customers leaving the bank differs from the rating distribution of the old and remaining customers.
- 2. Increased or decreased exposures to existing customers.
- 3. Changes in rating/scoring for existing customers (migration). Migration is for instance affected by macroeconomic development, industry sector developments, changes in business opportunities and development in financial statements of the customers and other company related factors. Scoring migration is affected by amongst other macroeconomic development and timely payments.

The figures 7 and 8 below show the rating migration for institutions and corporate customers during 2008, comparing the rating in beginning of the year with year end rating. The migration is done only for customers that existed at year end 2007. The migration in terms of number of customers as well as EAD is shown.

The institution portfolio is volatile in terms of exposure volume. Out of the total EAD in the institution portfolio approximately 41% have migrated up or down during

Figure 7b Institution rating migration, number of counterparts that have been up or down graded during 2008



2008. This corresponds to approximately 22% number of counterparts.

Out of the total EAD in the corporate portfolio approximately 39% have migrated up or down during 2008. This corresponds to approximately 32% in customers. The effect on the RWA due to this rating migration was 4.5% RWA increase for the corporate portfolio. The RWA increase due to rating migration reflects the impact of pro-cyclicality in the pillar 1 capital requirement calculations of the IRB approaches.

4.4.1.2 EAD

EAD is an estimate of how much of an exposure will be drawn within the period one year prior to default. For on balance sheet items, EAD is normally the same as the booked value, such as the market value or utilisation. An off balance product, such as a credit facility, does not contain the same risk as an on balance exposure, since it is rarely fully utilised at the time of the customer's default. A Credit Conversion Factor (CCF) is multiplied to the off balance amount to estimate how much of the exposure will be drawn at default. In the FIRB approach the CCFs are fixed by financial supervisory authorities.

The CCF model used for the Retail IRB approach is built on a product based approach. There are three explanatory variables that determine which CCF value an off balance exposure will receive. These variables determine which CCF value an off balance exposure will receive. The three variables are: customer type, product type/CCF pool and country in which the reporting is made. The table below shows the weighted average CCF for the IRB retail portfolio. The CCF is based on own estimates on expected total exposure at the time of default. More information regarding the off balance sheet exposure can be found in chapter 7.

Table 13 Credit Conversion Factor, 31 Dec 2008

Original	Exposure	EAD	CCF
Retail	13,400	9,960	74%
 of which mortgage 	2,110	1,559	74%
 of which other retail 	10,000	7,544	75%
 of which SME 	1,290	857	66%

4.4.1.3 LGD

LGD is measured taking into account the collateral type, the counterparty's balance sheet components, and the presence of any structural support. LGD measures the expected

Figure 8a Corporate rating migration, EAD that have been up or down graded during 2008



realised loss given the default of a customer. The regulatory capital requirement is dependent on LGD.

For the FIRB institution and corporate exposure classes the LGD values are fixed by financial supervisory authorities. When setting the LGD to fixed levels the CRD has taken into account downturn in the economy.

The LGD value in the retail IRB approach is based on internal estimates. LGD estimates are based on the experience and practices in Nordea as well as the external environment in which the bank operates. Nordea uses LGD estimates that are appropriate for an economic downturn if those are more conservative than the long-run average. The LGD pools are based on collateral types. These codes are mapped to LGD pools depending on country and customer type (household or SME).

Credit risk mitigation

RWA and exposures are reduced by the recognition of credit risk mitigation techniques. Only certain types of collateral and some issuers of guarantees are eligible to reduce the capital requirement purposes. Furthermore the collateral management process and the terms in the collateral agreements have to fulfil the minimum requirements (such as procedures for monitoring of market values, insurance and legal certainty) in the capital adequacy regulations. Collateral items and guarantees which can reduce the capital requirement are called eligible collateral. The eligibility requirements are explicitly mentioned in the CRD for physical exposures in FIRB, which are currently used for corporate and institution exposures. Financial supervisory authorities may permit the use of other physical collateral only if two specific requirements are met in addition to the general minimum requirements listed further down in the document. The first requirement is that there is a liquid market and the second that there are established market prices.

The reduction of the capital requirements is calculated in four ways, depending of the type of credit risk mitigation technique:

- 1. Adjusted exposure amount
 - The comprehensive method for financial collateral such as cash, bonds and stocks. The exposure amount is adjusted with regards to the financial collateral. The size of the adjustment depends on the volatility of the collateral and the type of exposure. Nordea uses volatility adjustments specified by the financial supervisory authorities (supervisory haircuts).

Figure 8b Corporate rating migration, number of counterparts that have been up or down graded during 2008



2. Adjusted PD (substitution of PD)

The substitution method is used for guarantees, which implies that the PD for the customer is substituted. This means that the credit risk in respect of the customer is substituted by the credit risk of the guarantor and the risk thereby reduced. Hence, an exposure fully guaranteed will be assigned the same capital requirement as if the loan was initially granted to the guarantor rather than the customer. The PD value of exposures is adjusted if the capital requirement for both the customer and the guarantor is calculated according to the IRB approach.

3. Adjusted LGD

The LGD value is reduced if the exposures in the IRB approach (i e to large corporate and institutions) is fully collateralised with real estates (commercial and residential), other physical collateral or receivables. The size of the LGD adjustment is stipulated by the CRD in the FIRB approach. The LGD value in the retail IRB approach is based on internal estimates.

Table 14 Exposure secured by collaterals, guarantees and credit derivatives

31 Dec 2008, EURm	Original Exposure	EAD	– of which secured by guarantees and credit derivatives	– of which secured by collateral
IRB exposure classes	1			
Institutions	52,401	49,143	728	2,123
Corporate	214,072	152,015	4,523	41,504
Retail	120,390	116,045	2,132	89,033
 of which mortgage 	86,788	86,236		86,155
- of which other retail	28,981	25,649	1,878	550
- of which SME	4,621	4,160	254	2,327
Other non-credit obligation assets	2,226	1,838		
Total IRB approach	389,088	319,042	7,382	132,659
Standardised exposure classes				
Central government and central banks	19,752	20,959	27	1
Regional governments and local authorities	9,126	7,425		
Institution	4,310	4,624		30
Corporate	30,402	20,960	554	20
Retail	13,864	9,739	193	3
Exposures secured by real estates	564	558		558
Other ¹⁾	2,327	2,210		
Total standardised approach	80,346	66,476	774	612

Basel I reporting entities	7,101			
Total standardised approach	178,872	155,378	963	86,077
Other ¹⁾	1,862	1,773		
Exposures secured by real estates	87,680	86,030		86,030
Retail	38,432	25,220	934	45
Corporate	22,417	16,343	2	2
Institution	1,698	1,497		
Regional governments and local authorities	9,113	7,684		
Central government and central banks	17,671	16,831	27	
Standardised exposure classes				
Total IRB approach	243,314	176,514	5,110	40,330
Other non-credit obligation assets	1,186	827		
Corporate	197,800	134,095	4,971	37,761
Institutions	44,328	41,591	139	2,569
IRB exposure classes				
31 Dec 2007, EURm	Original Exposure	EAD	secured by guarantees and credit derivatives	– of which secured by collateral
			- of which	

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items, short term claims, covered bonds, and other items.

4. Adjusted risk weight

Netting agreements are mainly used for transactions in derivatives in the trading book. The exposure value is adjusted so that the capital requirements for credit risk reflect only the net position of derivative contracts with positive and negative values under the netting agreement. Netting across product categories is not used.

Nordea uses a wide variety of risk mitigation techniques in several different markets which contribute to risk diversification and credit protection. The different credit risk mitigation techniques such as collateral, guarantees, netting agreements and covenants are used to reduce the credit risk. All credit mitigation activities are not recognised for capital adequacy purposes since they are not defined as eligible, i e covenants. Loan documentations and similar agreements can include covenants such as financial ratios that the debtor has to comply with. Receivables with an original maturity of more than one year are not eligible for capital adequacy purposes. Another example is assets that could not be sold in a liquid market. Such assets could be pledged but are not assigned any value in the credit process, nor in the regulatory capital calculations.

In table 14, the exposure per exposure class secured by eligible collateral, guarantees and credit derivatives are available. The table present a split between exposure classes subject to the IRB approach and exposure classes subject to the standardised approach. In 2008, approximately 35% (38% in 2007) of EAD was secured by eligible collateral. The decline is due to that the exposures in Poland, Luxemburg and Russia were in 2007 reported under Basel I and in 2008 Standardised approach. In the IRB corporate portfolio 27% (28%) of EAD is secured by collateral. In the Standardised approach only exposures secured by real estate and financial collateral are regarded as eligible collateral.

Guarantees and credit derivatives

The guarantees used as credit risk mitigation are largely issued by central and regional governments in the Nordic countries. Banks and insurance companies are also important guarantors of credit risk.

Only eligible providers of guarantees and credit derivatives can be recognised in the standardised and FIRB approach for credit risk. All central governments, regional governments and institutions are eligible. Some multinational development banks and international organisations are also eligible. Guarantees issued by corporate entities can only be taken into account if their rating corresponds to A- (S&P's rating scale) or better. Out of the guarantors, central governments and municipalities within the Nordic countries comprise approximately 86%. The exposures that are guaranteed by these guarantors receive a 0% risk weight. Approximately 5% of the main guarantors are institutions, where 99% of these exposures have a guarantor with a rating of 5 or higher. The remaining guarantors are corporate.

Credit derivatives are only used as credit risk protection to a very limited extent since the credit portfolio is considered to be well diversified.

Collateral distribution

In table 15, the distribution of collateral used in the capital adequacy calculation process is presented. The table shows that real estate is the major part of the eligible collateral items.

Real estate is commonly used as collateral for credit risk mitigation purposes. There is no major concentration of real estate collateral to any region within the Nordic and Baltic countries. Other physical collateral consist mainly of ships.

Table 15 Collateral distribution

	31 Dec 2008	31 Dec 2007
Other Physical Collateral	6.1%	4.5%
Receivables	0.8%	2.2%
Residential Real Estate	72.5%	75.7%
Commercial Real Estate	17.8%	15.1%
Financial Collateral	2.8%	2.5%

Valuation principles of collateral

A conservative approach with long-term market values and taking volatility into account is used as valuation principle for collateral when defining the maximum collateral ratio.

Valuation and hence eligibility is based on the following principles:

- Market value is assessed; markets must be liquid, public prices must be available and the collateral is expected to be liquidated within a reasonable timeframe.
- A reduction of the collateral value is to be considered if the type, location or character (such as deterioration and obsolescence) of the asset indicates uncertainty regarding the sustainability of the market value. Assessment of the collateral value also reflects the experienced volatility of market values in the past.
- Forced sale principle; assessment of market value or the collateral value must reflect that realisation of a collateral in a distressed situation is initiated by the bank.
- No collateral value is to be assigned if a pledge is not legally enforceable and/or if the underlying asset is not adequately insured against damage.

A common way to analyse the value of the collateral is to measure the loan to value (LTV) ratio, i e the exposure divided by market value. At the end of 2008, 91% of the mortgage portfolio had a LTV ratio below 80%.

Table 16 Loan-to-value distribution

Mortgage exposure on households and SME

Total	87.3	100
>90%	3.9	4
80–90%	4.8	5
70-80%	23.1	27
50–70%	26.0	30
<50%	29.5	34
EURbn	31 Dec 2008	%

Average weighted LGD

As of December 31 2008, the average exposure weighted LGD for the corporate and institution portfolio were 42% and 43% respectively. In the FIRB approach the LGD estimates are pre-defined in the legislation. For instance, exposures fully secured by real estate collateral are assigned an LGD of 30–35% depending on national regulations. Exposures fully secured by other physical collateral are assigned an LGD of 40%. The LGD value for unsecured senior exposures is 45%.

The LGDs for the retail portfolio are based on a internal model, and are divided in pools of collateral and is based on historical loss data. In table 17 below, the exposure weighted LGD is shown for the retail portfolio.

Table 17 Exposure weighted LGD, 31 Dec 2008

	LGD%
Retail	19%
 of which mortgage 	14%
 of which other retail 	33%
- of which SME	25%

4.4.1.4 Maturity

For exposures calculated with the FIRB approach, the maturity is set to standard values in the RWA calculation formula based on the estimates set by the financial supervisory authorities. The maturity parameter used is set to 2.5 years for the exposure types on balance, off balance and derivatives. For securities financing the maturity parameter is 0.5 years.

Exposures in IRB split by maturity, defined as remaining maturity, are presented in table 18.

Nordea's exposures to institutions are mainly within the short maturity below 1 year as part of the liquidity management. The corporate exposure below 1 year equals 43% of the exposure and includes a large portion of revocable off balance sheet items. The corporate exposure above 5 years includes mainly on balance sheet items. 69% of the retail exposure is above 5 years.

Table 18 IRB exposures split by maturity, 31 Dec 2008,Original exposure

EURm	Institutions	Corporate	Retail
<1 year	34,841	104,643	32,688
<1–3 years	7,893	22,455	1,739
<3–5 years	1,564	21,289	2,396
> 5 years	8,103	65,686	80,567
Total	52,401	214,073	120,390

4.4.1.5 Estimation and validation of parameters

Nordea has established an internal process in accordance with the legal requirements with the purpose of ensuring and improving the performance of models, procedures and systems and to ensure the accuracy of the parameters.

The PDs are validated semi annually, while the LGD and CCF parameters are validated at least annually. The validation includes both a quantitative and a qualitative validation. The quantitative validation includes statistical tests to ensure that the estimates are still valid when new data is added. Triggers have been defined for all tests.

In table 19 the EL is compared to the actual gross and net losses. The EL has been calculated using the definition from the EC framework, in which defaulted exposures receive 0% EL. The average EL ratio used in the economic profit framework, calculated as EL divided by EAD, was 17 basis points as of end of 2008 (16 basis points as of end of 2007) excluding the sovereign and institution exposure classes. Nordea has the ambition to use the same parameters in internal calculations of EC and EL as in regulatory capital calculations. Therefore, the average EL ratio has been recalibrated as a consequence of the IRB Retail approval to be 22 basis points as of end of 2008. The model change will going forward affect the calculation of riskadjusted profit for 2009 and 2008.

Note that the EL will vary over time as a consequence of that the rating and the collateral coverage distributions change with the business cycle. This manifests that Nordea's rating models are neither entirely through the cycle nor entirely point in time. The implication is that the EL calculated at the top of the business cycle will not represent the EL over a full business cycle and that migration will not explain the full variation in actual losses. It is expected that the average long term net loss will match the average EL over time. The fact that net losses includes reversals and recoveries from previous years limits the use of the figure as an indicator of the model's performance looking at only one year of data. Also for the gross loss figure a much longer times series than 1 year is required since the EL is reflecting business cycle adjusted long term averages in the case of PD and expected downturn levels for the LGD and CCF.

4.4.2 Calculation of RWA with the standardised approach

Approximately 17% of Nordea's credit exposure is calculated with the standardised approach. The standardised measures credit risk pursuant to fixed risk weight and is the least sophisticated capital calculations. The application of risk weight in standardised is given by financial supervisory authorities and is based on the exposure classes to which the exposure is assigned. Some exposure classes are derived from the type of counterparty while others are based on the asset type, product type, collateral type or exposure size. The EAD of an on balance sheet exposure in the standardised is measured net of value adjustments such as provisions. Off balance sheet exposures are converted into EAD using CCF set by the financial supervisory authorities. Derivative contracts and securities financing has an EAD that is the same as the exposure.

In calculating RWA with the standardised approach, external rating may be used as an alternative to use the fixed risk weight. The external ratings must come from eligible external credit assessment institutions. More information regarding the risk weight of the exposures under the standardised approach can be found in appendix 12.3.

Exposure against central government and central banks Nordea uses S&P's as eligible rating agency. The external rating is converted to the credit quality step (the mapping is defined by the financial supervisory authorities), which corresponds to a fixed risk weight. In table 20, the central government and central banks exposures distributed by the credit quality steps is available. The exposure in the table is based on original exposure It can be concluded that the main part of the exposure towards central governments and central banks is within the highest credit quality step, which results in no RWA for these exposures.

Exposure against remaining standardised exposures The exposures in Poland, Russia, Luxemburg and foreign branches are calculated accordingly to the standardised approach. Furthermore acquisitions of new portfolios are treated as standardised until approval has been given to include them by the financial supervisory authorities. Retail exposures in the finance companies have not been applied to use advanced models. These will be applied for in near future starting with Nordea Finance Finland in 2009.

4.5 Information about impaired loans and loan losses

4.5.1 Information about definition and methods of impaired loans

The responsibility for credit risk lies with the customer responsible unit, which on a continuing basis assesses the customers' ability to fulfil their obligations and identifies deviations from agreed conditions and potential weaknesses in customer's performance.

Based on credit monitoring reports, the customer responsible unit must also assess whether it is an indication of that the customer's repayment ability is threatened.

If it is considered unlikely that the customer will be able to repay its debt obligations (principal, interest or fees) in full, and the situation cannot be satisfactorily remedied, the exposure is regarded as default. Exposures that have been past due more than 90 days are automatically

	Retail				
EURm	Household	Corporate ¹⁾	Institutions	Government	Total
2008					
EL	-115	-325	-8		-449
Gross loss	-216	-635	-38		-890
Net loss	-103	-330	-32		-466
2007					
EL	-110	-270			-381
Gross loss	-126	-333	-15		-473
Net loss	-28	61	27		60

Table 19 EL vs Gross loss and net loss

1) Corporate segment in this table includes SME Retail.

Table 20 Exposures to central governments and central banks

Total			19,752	17,670
BB+ and below, or without rating	4 to 6 or blank	100-150%	746	192
BBB+ to BBB-	3	50%	6	10
A+ to A-	2	20%	1,043	446
AAA to AA-	1	0%	17,957	17,022
Standard & Poor's rating, EURm	Credit quality step	Risk weight	31 Dec 2008 Original Exposure	31 Dec 2007 Original Exposure

regarded as in default, and reported as impaired and nonperforming.

If credit weakness is identified in relation to a customer exposure, such exposure is assigned special attention in terms of review of the risk. In addition to continuous monitoring, an action plan is established outlining how to minimise a potential credit loss. If necessary, a special team is set up to support the customer responsible unit.

In the process to identify indication of impairment, Nordea is pursues a continuous process to review the financial status of the credit exposures. Weak and impaired exposures are closely and continuously monitored and reviewed at least on a quarterly basis in terms of current performance, business outlook, future debt service capacity and the possible need for provisions.

An exposure is impaired, and a provision is recognised, if there is objective evidence, based on loss events or observable data, that there is impact on the customer's future cash flow to the extent that full repayment is unlikely, collateral included. The size of the provision is equal to the estimated loss considering the discounted value of the future cash flow and the value of pledged collateral. Impaired exposures can be either performing or non-performing. Impaired exposures are treated as in default when determining default probability.

In addition to individual impairment testing of all individually significant customers, collective impairment testing must be performed for groups of customers not considered found to be impaired on individual level.

The rationale for this two step procedure with both individual and collective assessment is to ensure that all incurred losses are accounted for up to and including each balance sheet day. Impairment losses recognised for group of loans represent an interim step pending the identification of impairment losses for an individual customer.

An independent credit control organisation has been established with the overall responsibility to control and monitor the quality in the credit port-folio, including ensuring that all incurred losses are covered by adequate allowances.

4.5.2 Disclosure of exposures, impaired loans and loan losses

In the tables 21-22 impaired loans, loan losses and allowances are distributed and stated according to IFRS as in the annual report. The tables in this section follow the segmentation used in the annual report.

In table 21, impaired loans to corporate customers are distributed by industry.

Table 21 Loans and receivables, impaired loans and allowances, by customer type

						loans ar	idually ii id receiva	mpaired	
		A	Allowances			Gross	u recerri	ao reo grooo	
	Loans and	1	for collec-		i	mpaired		in % of	
	receivables	– of which	tively	in %		loans	Specific	impaired	
21 Dec 2008 ELID	before	not	assessed	of not	Cross	of loans	allow-	loans	
	anowances	impaired	Ioans	impaired	Gross	and rec.	ances	gross	
lo credit institutions	23,926	23,893	3	0.01	33	0.14	20	61	
- of which banks	22,572	22,539	3	0.01	33	0.15	20	61	
- of which other credit institutions	1,355	1,355	0	0.00	0	0.00	0	0	
lo the public	266,247	264,056	405	0.15	2,191	0.82	742	34	
- of which corporate	152,613	151,005	320	0.21	1,608	1.05	582	36	
Energy (oil, gas etc)	2,816	2,816	1	0.04	1	0.02	0	46	
Metals and mining materials	1,752	1,750	1	0.06	2	0.14	1	29	
Paper and forest materials	2,292	2,274	1	0.04	19	0.82	5	27	
Other materials (building materials etc)	5,452	5,283	27	0.52	169	3.10	48	28	
Industrial capital goods	3,272	3,254	2	0.06	18	0.56	6	35	
Industrial commercial services etc	15,570	15,427	11	0.07	143	0.92	77	54	
Construction and civil engineering	3,749	3,613	31	0.85	136	3.62	46	34	
Shipping and offshore	11,301	11,242	1	0.01	59	0.52	5	9	
Transportation	4,049	3,995	10	0.25	53	1.32	22	42	
Consumer durables (cars, appliances etc	2,795	2,626	4	0.17	168	6.03	38	23	
Media and leisure	3,200	3,129	3	0.09	71	2.23	26	36	
Retail trade	11,115	10,898	14	0.13	217	1.95	81	37	
Consumer staples (food, agriculture etc)	13,054	12,917	50	0.39	136	1.04	60	44	
Health care and pharmaceuticals	1,613	1,574	1	0.07	39	2.40	6	16	
Financial institutions	16,498	16,442	2	0.01	56	0.34	15	26	
Real estate management	35 <i>,</i> 695	35,489	119	0.34	206	0.58	76	37	
IT software, hardware and services	1,498	1,476	1	0.06	21	1.43	8	37	
Telecommunication equipment	633	599	0	0.01	33	5.28	10	29	
Telecommunication operators	1,689	1,688	3	0.20	2	0.09	0	25	
Utilities (distribution and production)	4,024	4,022	2	0.05	3	0.07	0	16	
Other, public and organisations	10,548	10,493	35	0.33	55	0.52	51	93	
 of which household 	108,845	108,266	85	0.08	579	0.53	158	27	
 mortgage financing 	84,019	83,837	32	0.04	182	0.22	13	7	
 consumer financing 	24,826	24,429	53	0.22	397	1.60	145	37	
 of which public sector 	4,789	4,784	0	0.00	5	0.10	2	32	
Total credit risk exposure in the banking									
operations	290,173	287,949	408	0.14	2,224	0.77	762	34	
Lending in the life insurance operations	120	120	0	0,00	0	0,00	0	0	
Total credit risk exposure including life insurance operations	290,293	288,069	408	0.14	2,224	0.77	762	34	

Provisions for off-balance sheet items for 2008 totaled EUR 54m for credit institutions, while EUR 45.7m was related to lending to the public.

cont. Table 21 Loans and receivables, impaired loans and allowances, by customer type

						Indiv loans an	idually ii d receiva	mpaired	
		Δ	llowances			Gross	iu recerve	10100 81000	
	Loans and	1	for collec-		i	mpaired		in % of	
	receivables	– of which	tively	in %		loans	Specific	impaired	
21 Dec 2007 EUP	before	not	assessed	of not	Cross	of loans	allow-	loans	
	anowances		104115	inipaneu	GIUSS		ances	gross	
To credit institutions	24,272	24,264	2	0.01	8	0.03	8	100	
- of which banks	23,750	23,743	2	0.01	8	0.03	8	100	
 of which other credit institutions 	522	522	0	0.00	0	0.00	0	0	
To the public	245,629	244,204	352	0.14	1,425	0.58	595	42	
 of which corporate 	134,076	133,047	294	0.22	1,029	0.77	461	45	
Energy (oil. gas. etc.)	1,449	1,447	0	0.00	1	0.08	0	3	
Metals and mining materials	793	790	0	0.00	3	0.34	1	23	
Paper and forest materials	1,955	1,914	0	0.00	40	2.07	26	65	
Other materials (building materials. etc.)	3,627	3,517	19	0.52	109	3.01	39	36	
Industrial capital goods	3,209	3,172	7	0.21	37	1.16	13	36	
Industrial commercial services. etc.	15,482	15,354	11	0.07	128	0.83	68	53	
Construction and civil engineering	3,269	3,222	8	0.26	47	1.43	17	37	
Shipping and offshore	7,583	7,579	0	0.00	4	0.05	2	51	
Transportation	3,870	3,810	7	0.18	60	1.54	18	30	
Consumer durables (cars. appliances. etc.) 2,845	2,785	6	0.23	60	2.11	31	52	
Media and leisure	3,130	3,067	2	0.06	63	2.00	24	38	
Retail trade	10,254	10,121	4	0.03	132	1.29	60	45	
Consumer staples (food. agriculture. etc.)	11,350	11,251	30	0.27	100	0.88	53	53	
Health care and pharmaceuticals	1,779	1,767	2	0.11	13	0.71	5	42	
Financial institutions	12,246	12,213	0	0.00	33	0.27	6	20	
Real estate management	36,898	36,809	98	0.26	89	0.24	34	38	
IT software. hardware and services	1,314	1,300	0	0.00	14	1.09	6	39	
Telecommunication equipment	654	617	0	0.00	37	5.66	13	34	
Telecommunication operators	1,062	1,061	0	0.00	1	0.11	0	24	
Utilities (distribution and production)	3,311	3,308	0	0.00	3	0.09	1	40	
Other	7,998	7,943	100	1.25	56	0.70	43	77	
- of which household	107,258	106,864	58	0.05	394	0.37	133	34	
Mortgage financing	82,929	82,832	23	0.03	97	0.12	12	13	
Consumer financing	24,329	24,032	35	0.14	297	1.22	120	41	
- of which public sector	4,296	4,294	0	0.01	2	0.04	1	70	
Total credit risk exposure in the banking operations	269,901	268,469	354	0.13	1,432	0.53	603	42	
Lending in the life insurance operations	0	0							
Total credit risk exposure including life insurance operations	269,901	268,469	354	0.13	1,432	0.53	603	42	
		D 26 6	411111111111111						

Provisions for off-balance sheet items in 2007 totaled EUR 36m for credit institutions, while EUR 19m was related to lending to the public.

Impaired loans, gross, have increased to EUR 2,224m from EUR 1,432m, during 2008, which is a result of the current downturn and worsened economic conditions for many customers, especially during the last quarter of 2008. Allowances for individually assessed loans increased to EUR 762m from EUR 603m. The ratio of allowances to cover impaired loans, gross, was 34% (42%). Allowances for collectively assessed exposures were EUR 408m (EUR 354m). Provisions for off-balance items have increased to EUR 100m (EUR 54m). The main increases in impaired loans were in the sectors "Real estate management", "Consumer durables", "Construction and civil engineering" and "Retail trade".

In table 22, impaired loans are distributed by geography. The main increases in impaired loans by borrower domicile were in the Baltic Countries, Russia, Norway and Denmark.

Table 22 Loans and receivables, impaired loans and allowances, by geography $^{\rm 1)}$

					Individually impaired loans and receivables gros			mpaired ables gross	5
		1	Allowances						
	Loans and		for collec-					in % of	
	receivables	– of which	tively	in %		Gross	Specific	impaired	
21 D 2000 EUD	before	not	assessed	of not	C	in % of	allow-	loans	
31 Dec 2008, EURm	allowances	impaired	loans	impaired	Gross	lending	ances	gross	
Nordic countries	230,342	228,419	262	0.11	1,923	0.83	677	35	
 of which Denmark 	73,184	72,560	81	0.11	624	0.85	309	49	
 of which Finland 	51,683	50,887	74	0.15	796	1.54	211	27	
 of which Norway 	41,744	41,493	61	0.15	251	0.60	83	33	
 of which Sweden 	63,731	63,480	46	0.07	251	0.39	74	29	
Estonia	2,632	2,588	35	1.35	44	1.68	2	5	
Latvia	3,231	3,167	55	1.74	64	1.99	10	16	
Lithuania	2,561	2,527	15	0.71	34	1.33	18	52	
Poland	3,379	3,341	7	0.21	38	1.12	18	46	
Russia	3 <i>,</i> 558	3,541	16	0.47	17	0.49	7	40	
EU countries other	10,704	10,673	0	0.00	32	0.30	7	20	
USA	1,797	1,762	0	0.00	35	1.94	0	1	
Asia	2,656	2,655	6	0.23	1	0.02	1	80	
Latin America	2,769	2,769	0	0.01	0	0.00	0	0	
OECD other	1,203	1,199	2	0.17	4	0.31	3	80	
Non-OECD other	1,416	1,415	2	0.17	0	0.01	0	98	
Total	266,247	264,056	405	0.15	2,191	0.82	742	34	

Individually impaired loans and receivables gross

31 Dec 2007, EURm	Loans and receivables before allowances	– of which not impaired	Allowances for collec- tively assessed loans	in % of not impaired	Gross	in % of gross	Specific allow- ances	in % of impaired loans gross	
Nordic countries	219,117	217,775	261	0.12	1,342	0.61	553	41	
 of which Denmark 	65,578	65,139	68	0.10	439	0.67	220	50	
 of which Finland 	47,962	47,380	78	0.16	582	1.21	176	30	
 of which Norway 	42,950	42,833	70	0.16	117	0.27	57	49	
- of which Sweden	62,626	62,422	45	0.07	204	0.33	100	49	
Estonia	2,033	2,023	25	1.24	10	0.48	0	2	
Latvia	2,391	2,381	44	1.83	10	0.42	1	7	
Lithuania	1,632	1,624	12	0.76	8	0.49	7	87	
Poland	2,341	2,301	2	0.07	40	1.70	24	60	
Russia	1,612	1,611	8	0.50	1	0.06	1	100	
EU countries other	8,940	8,932	0	0.00	8	0.09	7	87	
USA	1,917	1,916	0	0.00	1	0.05	1	100	
Asia	1,421	1,418	0	0.00	3	0.24	0	0	
Latin America	1,722	1,722	0	0.00	1	0.06	0	0	
OECD other	923	923	0	0.00	0	0.01	0	0	
Non-OECD other	1,579	1,579	1	0.08	0	0.00	0	0	
Total	245,629	244,205	352	0.14	1,424	0.58	595	42	

1) On balance sheet items excluding credit institutions

Table 23 shows the specification of the loan losses according to the income statement in the annual report, as well the changes in the allowance accounts in the balance sheet. which EUR 330m (EUR –88m) relates to corporate customers and EUR 103m (EUR 28m) to household customers.

The net loan losses in the income statement from credit risk impairments were in 2008 EUR 466m (EUR –60m), of

The main loan losses were in the corporate sectors "Retail Trade" and "Construction and civil engineering" as well as household "Consumer financing".

Table 23 Loan losses, 2008

EURm	New provisions and write-offs	Reversals and recoveries	Net loan losses	Loan loss ratio bps
To credit institutions	-38	6	-32	-13
To the public	-852	418	-433	-18
 of which corporate 	-635	305	-330	-25
Energy (oil, gas, etc.)	0	0	0	-2
Metals and mining materials	0	0	0	-5
Paper and forest materials	-15	15	0	-
Other materials (building materials, etc.)	-46	11	-36	-100
Industrial capital goods	-6	10	4	_
Industrial commercial services, etc.	-60	28	-32	-21
Construction and civil				
engineering	-66	11	-55	-170
Shipping and offshore	-12	1	-11	-15
Transportation	-18	6	-13	-33
Consumer durables				
(cars, appliances, etc.)	-37	16	-21	-76
Media and leisure	-12	5	-7	-21
Retail trade	-76	20	-56	-55
Consumer staples (food, agriculture, etc.)	-46	23	-23	-21
Health care and pharmaceuticals	-1	4	3	-
Financial institutions	-12	4	-9	-7
Real estate	-64	19	-45	-12
IT software, hardware and services	-6	3	-2	-18
Telecommunication equipment	-10	12	2	-
Telecommunication operators	0	1	1	-
Utilities (distribution and production)	-3	0	-3	_9
Other	_144	117	-27	-34
 of which household 	-216	113	-103	-10
Total	-890	424	-466	-17

Table 24 shows the changes in the allowance accounts in the balance sheet.

Table 24 Reconciliation of allowance accounts for impaired loans

EURm	Individually assessed	Collectively assessed	Total
Opening balance, 1 Jan 2008	-603	-354	-957
Provisions	-555	-188	-743
Reversals	229	123	352
Allowances used to cover write-offs	129	0	129
Reclassification	4	0	4
Currency translation differen	ices 34	11	45
Closing balance, 31 Dec 2008	-762	-408	-1,170

Table 25 shows past due split for corporate and house-hold customers.

Table 25 Past due loans, excl. impaired loans, 31 Dec 2008

EURm	Corporate customers	Household customers
6–30 days	671	673
31–60 days	422	369
61–90 days	227	102
>90 days	266	179
Total	1,586	1,323
Past due not impaired/ loans and receivables	1.05%	1.22%

5. Market risk

In this chapter, the management of market risk is described. Market risk is the risk of a loss in the market value of portfolios and financial instruments as a result of movements in financial market variables.

The customer-driven trading activity of Nordea Markets and the investment and liquidity portfolios of Group Treasury are the key contributors to market risk in Nordea. For all other banking activities, the basic principle is that market risks are eliminated by matching assets, liabilities and off balance sheet items. This is achieved by transactions in Group Treasury.

Furthermore, market risk on Nordea's account arises from the investment of policy-holders' money with guaranteed minimum yields in Life and Pensions, and Nordea sponsored defined benefit pension plans for employees.

Structural FX risk arises primarily from investments in subsidiaries and associated enterprises denominated in foreign currencies. The general principle is to hedge this by matched funding, although exceptions from this principle may be made in markets where matched funding is impossible to obtain, or can only be obtained at an excessive cost. Nordea Bank AB's holding of JSB Orgresbank (Russia) is partly financed in Euro. A 1% decrease in the Russian rouble's exchange rate towards the Euro will cause a decrease in Nordea's equity capital of approximately EUR 6m.

Payments made to parent companies from subsidiaries as dividends are exchanged to the functional currency of the parent company. Furthermore, earnings and cost streams generated in foreign currencies or from foreign branches generate an FX exposure, which for the individual Nordea companies is handled in each company's FX position.

In addition to the immediate change in the market value of Nordea's assets and liabilities from a change in financial market variables, a change in interest rates could also affect the net interest income of Nordea over time. In Nordea this is seen as structural interest income risk (SIIR) and is described in Chapter 8.

5.1 Reporting and control process

A Nordea Group wide framework establishes common management principles and standards for the market risk management. This implies that the same reporting and control processes are applied for the market risk exposures in Nordea Markets (the Trading Book) and Group Treasury. Moreover the same Value-at-Risk model (VaR model) is used to measure and manage the consolidated risk and the risk divided into Trading Book and Banking Book risk.

However, certain risk exposures have special characteristics and are monitored and limited separately. For example, this is the case for commodity risk, structured equity options and fund linked derivatives in Markets and private equity funds and investments in hedge funds in Group Treasury, which are measured using scenario simulation. The scenarios are based on the sensitivity to changes in the underlying prices and, where relevant, their volatility. These risk figures are limited and monitored in the daily reporting and control process, but not included in the VaR numbers. CDOs and CDSs are included in the VaR figures through their sensitivities to changes in credit spreads, in analogy with corporate bonds. In addition, jump-to-default exposures and correlation risk are limited and monitored in the daily control process. See section 7.2 for more specific information about CDOs and CDSs.

The market risk on Nordea's account due to minimum yield guarantees in Life and Pensions is measured, controlled and limited separately. It is measured as the loss sensitivity for two standard market scenarios, which represent normal and stressed market conditions, respectively.

Also the market risk in the Nordea sponsored defined benefit pension plans for employees is measured and analysed separately.

Transparency in all elements of the risk management process is central to maintaining risk awareness and a sound risk culture throughout the organisation. In Nordea this transparency is achieved by:

- Senior management taking an active role in the process. The CRO receives reporting on the Group's consolidated market risk every day; GEM receives reports on a monthly basis, and the Board of Directors on a quarterly basis:
- Defining clear risk mandates (at departmental, desk and individual levels), in terms of limits and restrictions on which instruments may be traded. Adherence to limits is crucial, and should a limit be breached, the decisionmaking body would be informed immediately.
- Having a comprehensive policy framework, in which responsibilities and objectives are explicitly outlined. Policies are decided by the Board of Directors, and are complemented by instructions issued by the CRO.
- Having detailed business procedures that clearly state how policies and guidelines are implemented.
- Having proactive information sharing between trading and risk control.
- Having risk models that make risk figures easily decomposable.
- Having a framework for approval of traded financial instruments and methods for the valuation of these that requires an elaborate analysis and documentation of the instruments' features and risk factors.
- Having a "business intelligence" type risk IT system that allows all traders and controllers to easily monitor and analyse their risk figures.
- Having tools that allow the calculation of VaR figures on the positions that a trader, desk or department has during the day.

5.2 Market risk appetite

The Board of Directors has formulated market risk appetites for both the investment and liquidity portfolios in Group Treasury and the trading activities in Nordea Markets. For Group Treasury, the Board of Directors has set the maximum level of risk so as not lead to an accumulated loss in earnings in excess of EUR 250m at any time in a financial year. The compliance with the risk appetite is ensured by market risk limits and stop-loss rules. The risk appetite was increased in 2008 in order to facilitate unchanged business activity in an environment of increased volatility. For trading activities, the risk appetite and the market risk limits are set in relation to the earnings these activities generate.

5.3 Measurement methods

As there is no single risk measure that captures all aspects of market risk, Nordea on a daily basis uses several risk measures including VaR models, stress testing, Jump-to-Default exposure, scenario simulation and other non-statistical risk measures such as basis point values, net open positions and option key figures.

5.3.1 Value-at-Risk

Nordea's universal VaR model is a 10-day, 99% confidence model, which uses the expected shortfall approach (sometimes referred to as tVaR, for tail-VaR) and is based on historical simulation on up to two years' historical changes in market prices and rates. This implies that Nordea's historical simulation VaR model uses the average of a number of the most adverse simulation results as an estimate of VaR. The sample of historical market changes in the model is updated daily. The "square root of ten" rule is applied to scale 1-day VaR figures to 10-day figures. The model is used to limit and measure market risk at all levels both for the Trading Book and in Banking Book.

VaR is used by Nordea to measure interest rate, FX, equity and credit spread risks. A VaR measure across these risk categories, allowing for diversification among them, is also used. The VaR figures include both linear positions and options.

With the chosen characteristics of Nordea's VaR model, the VaR-figures can be interpreted as the loss that will only be exceeded in one of hundred 10-day trading periods. However, it is important to note that, while every effort is made to make the VaR-model as realistic as possible all VaR-models are based on assumptions and approximations that have significant effect on the risk figures produced. Also, it should be noted that the historical observations of the market variables that are used as input, may not give an adequate description of their behaviour in the future. In particular the historical values may fail to reflect the potential for extreme market moves.

In the summer of 2007 the volatility in the financial markets increased markedly, and in the spring of 2008, Nordea's backtesting indicated a need for making the model more responsive to changes in market volatility. As a result, in June 2008, the model was adjusted by reducing the lookback period, to one year, and the number of the most adverse simulation results in the estimate of the VaR (i.e. further out in the left-hand tail of the distribution of historical simulation outcomes). The adjustment entailed immediate increases in the VaR figures of between 20% and 40%.

5.3.2 Stress testing

Stress tests are used to estimate the possible losses that may occur under extreme market conditions.

Stress tests are conducted daily for the consolidated risk across Banking book and Trading book, for the consolidated Trading book as well as for the market risk in the legal entities Nordea Bank Norge ASA, Nordea Bank Danmark A/S and Nordea Bank Finland Plc. The main types of stress tests include:

- 1. Historical stress tests, which include selected historical episodes, and are calculated by exposing the current portfolio to the most unfavourable developments in financial markets since 1993.
- 2. Subjective stress tests, where the portfolios are exposed to scenarios for financial developments that are deemed particularly relevant at a particular time. The scenarios are inspired by the financial, the macroeconomic or geopolitical situation, or the current composition of the portfolio.
- 3. Sensitivity tests are conducted on interest rates, and include tests where rates, spreads and/or volatilities are shifted markedly. The sensitivities are measured both gross and net; the gross figures shedding light on exposure to situations where normal relationships between financial variables fail to hold. Another sensitivity measure used is the potential loss stemming from a sudden default of an issuer of a bond or the underlying in a credit default swap.

While these stress tests measure the risk over a shorter time horizon, market risk is also a part of Nordea's comprehensive ICAAP stress testing, which measures the risk over a three year horizon. For further information see Chapter 9.

5.4 Consolidated market risk for the Nordea Group The volatile developments in the financial markets and the fact that the model is now more responsive to changes in market volatility, has effected that the market risk in the Nordea Group as measured by the total VaR was higher (EUR 85.8m) at the end of 2008 than at the end of 2007 (EUR 58.9m), although underlying exposures in most cases were unchanged or had even decreased. The consolidated market risk figures are presented in table 26.

Other drivers for change for the consolidated VaR figures over 2008 have been the sale of Nordea's holding in the OMX Group, reducing equity VaR, and the extension of the credit spread VaR model to include Group Treasury, increasing this figure.

Table 26 Consolidated market risk figures, 31 Dec 2008

EURm	Measure	31 Dec 2008	2008 high	2008 low	2008 average	31 Dec 2007
Total Risk	VaR	85.8	123.4	43.4	73.0	58.9
 Interest Rate Risk 	VaR	74.4	123.1	38.8	72.8	57.2
 Equity Risk 	VaR	31.1	45.5	2.6	16.7	32.9
 Credit Spread Risk 	VaR	29.7	36.1	8.3	20.3	4.8
– Foreign Exchange Risk	VaR	17.2	22.7	2.1	6.5	3.4
Diversification effect		44%				41%
Structured Equity Option Risk	Simulation	12.0	29.3	11.2	21.0	25.9
Commodity Risk	Simulation	4.1	11.0	3.6	6.5	8.2

5.5 Regulatory capital for market risk in the Trading Book (pillar 1)

Nordea uses both the Internal Models Approach (VaR) and the Standardised Approach to capture the market risk capital requirement in the Trading Book. Market risk in the CRD context contains two types of risk measures: general risk and specific risk. General risk is risk related to changes in the overall market prices while specific risk is related to price changes for the specific issuer. In addition to the positions in the Trading Book, regulatory capital for market risk covers FX risk in the Banking Book through the standard approach.

The capital requirement for market risk at the end of 2007 and 2008 is presented in table 27. As seen the largest contribution to the non-VaR capital requirement is interest rate risk and equity risk. More precisely, the non-VaR contribution is mainly related to specific interest rate risk on Danish mortgage bonds and specific equity risk in the trading book in Nordea Bank Danmark A/S.

The main part of the market risk RWA is related to business in Nordea Markets. Market risk RWA increased from EUR 3.6bn to EUR 5.9bn between Q4 2007 and Q4 2008. The increase is mainly related to increased VaR contribution to the Group's market risk RWA which increased from EUR 0.5bn to EUR 1.7bn during the year as a result of both increased average VaR and an increased multiplier. In Q4 2008 the FX risk outside the trading book is above 2% of the capital base and therefore also included in the total market risk RWA.

The following section describes the principles for calculating RWA with the Internal Models Approach and the Standardised Approach respectively. Table 28 presents the methods in use for calculation of capital requirements.

5.5.1 Internal model approach (VaR)

Nordea uses the VaR model to calculate capital requirements for the predominant part of the Trading Book. In 2008, the financial supervisory authorities extended the approval to also cover exposures on standard equity

Table 27 Capital requirements for market risk

	Tradi	Trading book, VaR		Trading book, non-VaR		nking book, non-VaR	Total	
31 Dec 2008, EURm	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement
Interest rate risk	2,068	164	2,654	213	0	0	4,722	377
Equity risk	171	14	668	53	0	0	839	67
Foreign exchange risk	520	42	0	0	843	67	1,363	109
Commodity risk	0	0	50	4	0	0	50	4
Diversification effect	-1,044	-83	0	0	0	0	-1,044	-83
Total	1,715	137	3,372	270	843	67	5,930	474

	Tradi	, Trading book, VaR		ding book, 10n-VaR	Ban	Banking book, non-VaR		Total	
31 Dec 2007, EURm	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement	
Interest rate risk	665	53	2,656	213			3,321	266	
Equity risk	183	15	305	24			488	39	
Foreign exchange risk	103	8			01)	01)	103	8	
Commodity risk			66	5			66	5	
Diversification effect	-424	-34					-424	-34	
Total	527	42	3,027	242	0	0	3,554	284	

¹⁾ FX risk in the banking book (25 EURm) is less than 2% of the capital base and therefore excluded from the market risk capital.

Table 28 Methods for calculating capital requirements

	Interes	st rate risk	Eq	Equity risk		
	General	Specific	General	Specific	General	
Nordea Group	IM	IM	IM	IM	IM	
Nordea Bank Danmark	IM	Standard	IM	Standard	IM	
Nordea Bank Finland	IM	IM	IM	IM	IM	
Nordea Bank Norge	IM	Standard	IM	Standard	IM	
Orgresbank	Standard	Standard	Standard	Standard	Standard	

IM:internal model approach, Standard: Standardised approach

options. Consequently, the methods used for calculating capital requirements for market risk for the Group's legal entities are:

General interest risk is measured by the Interest Rate VaR, while specific interest rate risk is measured through Credit Spread VaR.

5.5.2 Backtesting of the VaR-model

Back testing is conducted daily in accordance with the guidelines laid out by the Basel Committee on Banking Supervision.

For interest rate risk, separate tests of general and specific risk are carried out. For the Trading Books of the legal entities, hypothetical (simulated) profit/loss (p/l) is used in the test for capture of general risk, while at consolidated Trading Book level 1-day VaR is held against both hypothetical and actual p/l. In the test for capture of specific risk, 1-day VaR is also held against both actual and hypothetical p/l for the consolidated credit trading desk.

For equity risk, a joint test of general and specific risk is conducted. For the Trading Books of the four legal entities, hypothetical p/l is used, while at global Trading Book level, 1-day VaR is held against both hypothetical and actual p/l.

Total 1-day VaR (comprising all risk categories) is also held against both hypothetical and actual p/l.

As stated above, in June 2008 an adjustment to the VaR model was made, however, since then the volatility in the markets has increased even further, and the number of backtest exceptions has consequently remained high.

5.5.3 VaR in the Trading book

Table 29 shows VaR in the trading book. The increase in VaR levels that was the result of the continued extreme volatility in financial markets and adjustment to the VaRmodel is as apparent for the Trading book as it is for the Group's consolidated risk

5.5.4 Standardised approach

Not all positions are covered by the approved VaR model, instead these have to be calculated following the standardised approach. Capital requirement for these positions is calculated according to the CRD. Figure 9 Backtesting, one-day VaR and actual profit/loss for the trading book



The main part of the standardised approach contribution to market risk required capital is specific interest rate risk on Danish mortgage bonds. In the standardised approach specific interest rate risk is calculated trough a maturity based method with different risk capital charge factors depending on category and time to maturity.

The current approved equity risk VaR model does not capture the risk on structured equity options, for which instead the standardised approach is used. In the standardised approach equity positions receives a capital charge factor depending on the position's quality and liquidity.

FX risk outside the Trading Book is not covered by the VaR model and is also calculated through the standardised approach.

5.5.5 Compliance with requirements applicable to exposures in the Trading Book

Annex VII, Part B of the European Parliament and Council Directive 2006/49/EG of 14 June 2006 on the capital requirements for investment firms and credit institutions outlines the requirements for systems and controls to provide prudent and reliable valuation estimates. Nordea complies in all material aspects with these requirements. Overall valuation principles are governed by policies and

Table 29 Consolidated market risk figures for the trading book, 31 Dec 2008

EURm	Measure	31 Dec 2008	2008 high	2008 low	2008 average	31 Dec 2007
Total Risk	VaR	32.6	46.7	14.8	26.7	15.6
 Interest Rate Risk 	VaR	20.8	42.3	10.3	23.0	14.2
– Equity Risk	VaR	2.3	13.2	1.3	3.4	4.4
- Credit Spread Risk	VaR	12.2	18.5	6.1	11.0	4.7
– Foreign Exchange Risk	VaR	15.6	17.3	1.6	5.7	3.4
Diversification effect		36%				44%
Structured Equity Option Risk	Simulation	12.0	29.3	11.2	21.0	25.9
Commodity Risk	Simulation	4.1	11.0	3.6	6.5	8.2

instructions applicable for the Nordea Group and independent Group staffs are responsible for the overall valuation process. The local risk control organisations in the individual business units are responsible for performing valuation controls in accordance to the policies and instructions applicable for the Nordea Group. The quality control framework is assessed by relevant Group functions as well as by Group Internal Audit on an ongoing basis.

The set-up for valuation adjustments in Nordea is designed to be compliant with the requirements in IAS 39. Requirements in the annex not supported by IAS 39 are therefore not implemented. Nordea incorporates counterparty risk in Over The Counter (OTC) derivatives, bid/ask spreads and where judged relevant, also model risk.

For a description of how fair values of financial traded instruments are determined in Nordea, see Note 1, section 10 to the 2008 Annual Report. Disclosure of assets and liabilities at fair value can be found in Note 48 of the Annual Report.

A description of critical judgements related to the determination of fair value can be found in Note 1, section 4 to the same report.

5.6 Interest rate risk in the Banking Book

Monitoring of the interest rate risk in the Banking Book is done daily by controlling interest rate sensitivities which measure the immediate effects of interest rate changes on the fair values of assets, liabilities and off-balance sheet items. Table 30 shows the net effect on fair value of a 200 basis points parallel shift increase in rates, by currency, with positions as of 31 December 2008.

Furthermore Nordea regularly measures the structural interest income risk (SIIR), which is the amount Nordea's accumulated net interest income would change during the next 12 months if all interest rates change by one percentage point. See chapter 8 for further details.

Table 30 Interest rate sensitivities for Nordea Group non-trading book 31 December 2008, instantaneous interest rate movements, EURm

	+200 bp	+100 bp	+50 bp	–50 bp	–100 bp	–200 bp
CHF	-3.3	-1.7	-0.8	0.8	1.7	3.3
DKK	-101.2	-50.6	-25.3	25.3	50.6	101.2
EUR	-79.1	-40.5	-21.0	24.3	49.2	96.1
GBP	-5.4	-2.7	-1.4	1.5	3.0	5.2
NOK	-15.1	-7.6	-3.8	3.8	7.6	15.1
SEK	-109.0	-54.5	-27.2	27.2	54.5	109.0
USD	-11.2	-6.1	-3.3	4.4	9.1	14.4
Total	-325.2	-164.0	-83.0	87.6	176.1	345.2

The totals are netted and include currencies not specified.

6. Operational risk

In this chapter, the management of operational risk is described.

6.1 Report and control process

Operational risk is defined as the risk of direct or indirect loss, or damaged reputation resulting from inadequate or failed internal processes, from people and systems, or from external events. Compliance risk is defined as the risk of business not being conducted according to legal and regulatory requirements, market standards and business ethics, thereby jeopardising customers' best interest, other stakeholders trust and increasing the risk of regulatory sanctions, financial loss or damage to the reputation and confidence in the Group. Operational risk also includes "Legal Risk", which means the risk that the Group suffers damage due to a deficient or incorrect legal assessment.

Operational risks are inherent in all activities within the organisation, in outsourced activities and in all interaction with external parties.

Solid internal control and quality management, consisting of a risk management framework, leadership and skilled personnel, is the key to successful operational risk management.

An annual report on the quality of Internal Control in the Group is submitted to the Board, incorporating all main issues on financial and operational risks.

Each Division in Nordea is primarily responsible for managing its own operational risks. Group Credit and Risk Control develops and maintains a framework for identifying, assessing, mitigating, monitoring, controlling and reporting operational risks and supports the line organisation in implementing the framework.

Information security, physical security, crime prevention and educational and training activities are important components when managing operational risks. To cover this broad scope, the Group security and the Group compliance functions are included in Group Credit and Risk Control, and close cooperation is maintained with Group IT and Group Legal, in order to raise the risk awareness throughout the organisation.

The main processes for managing operational risks are ongoing monitoring through risk self-assessment and the documenting, registering and following up activities related to incidents and quality deficiencies. The analysis of operational risk-related events, potential risk indicators and other early-warning signals are in focus when developing the processes.

Special emphasis is put on quality and risk analysis in change management and product development.

The mitigating techniques consist of continuous improvement initiatives and business continuity plans together with crisis management preparedness and a broad insurance cover for handling major incidents. Mitigation efforts target reliability and continuity in the value chains rather than focusing on single units in the organisation.

The techniques and processes for managing operational risks are structured around the risk sources as described in the definition of operational risk. This approach improves the comparability of risk profiles in different areas and functions and globally throughout the organisation. It also complement the Group's the focus on limiting and mitigating measures in relation to the sources, rather than the symptoms.

6.2 Capital requirements for operational risk The capital requirement for operational risk is in Nordea calculated according to the Standardised Approach, in which all of the institution's activities are divided into eight standardised business lines and a defined beta coefficient is multiplied by the average of the gross income for each business line. The capital requirement for operational risk amounts to EUR 952m (EUR 878m in 2007). The capital requirement for operational risk is updated on a yearly basis.

7. Off balance items including derivatives and securitisation

In this chapter, Nordea discloses information about off balance with focus on derivatives, Special Purpose Entities (SPEs) and securitisations.

7.1 General disclosure of off balance

Off balance sheet items are divided into two different exposure types in accordance with calculation of credit risk RWA in the CRD:

1. Off balance sheet items:

- Main categories of off balance sheet items are guarantees, credit commitments and unutilised portion of approved credit facilities. Off balance sheet items in this report include also revocable exposures in accordance with the CRD, which are not included in the accounting.
- 2. Derivatives:

Financial instruments that derive their value from underlying interest rates, currencies, equities, credit spreads or commodity prices. Derivatives do not only result in counterparty risk measured within the credit risk RWA but also affect the market risk RWA (see section 7.2 below).

For the different off balance exposure types mentioned above, there are different possible values for the calculation base. For the off balance items, the nominal value of the guarantee is applied with a CCF for calculating the EAD. The CCF factor is for instance 50% or 100% depending of the type of guarantee, i e lowering the risk weight compared with the same exposure on balance. Credit commitments and unutilised amounts are the part of the external commitment that has not been utilised. This amount forms the calculation base for which a CCF is used for calculating the EAD. The CCF factor, ranging from 0 to 100% is multiplied with the calculation base depending of approach, product type and whether the unutilised amounts are unconditionally cancellable or not.

The overall capital requirements split by exposure type are available in table 31, where the exposure for derivatives stem from counterparty risk. The information in the table include exposures both from the IRB and SA exposure classes.

Table 31 Exposure, RWA and capital requirementsby exposure type

Or 31 Dec 2008 EURm	n balance sheet items ¹⁾	Off balance sheet items	Deriv- atives	Total
Exposure	303,578	131,129	34,727	469,434
EAD	302,896	47,893	34,727	385,517
RWA	115,931	23,944	10,870	150,746
Capital requirement	t 9,274	1,916	870	12,060
Average risk weight	t 38%	50%	31%	39%

31 Dec 2007 EURm	On balance sheet items ¹⁾	Off balance sheet items	Deriv- atives	Total ²⁾
Exposure	271,685	127,937	22,564	422,185
EAD	270,989	38,338	22,564	331,892
RWA	126,009	20,111	5,087	151,207
Capital requirement	10,081	1,609	407	12,097
Average risk weight	46%	52%	23%	46%

¹⁾ On-balance sheet items includes securities financing.

2) Excludes Basel 1 reporting entities.

It can be concluded that although off balance items have large exposure amounts, the effect on RWA is smaller than on balance items. At the end of December 2008, 23% of the total RWA in Nordea stem from off balance sheet items and derivatives, which is similar to last year (17% in 2007). At the end of 2008, the RWA for off balance sheet items was 18% of the original exposure, while the RWA for on balance sheet items was 38% of the original exposure. The CCF is set to 0% for 50% of the off balance sheet exposure, due to that they are revocable. The exposure class Corporate in FIRB has the largest portion of off balance sheet exposures which comprises 42% of the total exposures, but a large part is revocable credit facilities.

In table 32, the off balance exposures are distributed by type of item. Out of the total off balance sheet items, 45% relate to credit facilities.

Table 32 Off balance distribution, 31 Dec 2008

EURm	EAD	Share %	RWA	Share %
Credit facilities	21,779	45	11 <i>,</i> 507	48
Checking accounts	5,569	12	2,267	9
Loan commitments	6,099	13	2,528	11
Guarantees	13,488	28	7,110	30
Other	958	2	533	2
Total	47,893		23,944	

7.2 Risk in derivatives

Derivative contracts are financial instruments, such as futures, forwards, swaps or options that derive their value from underlying interest rates, currencies, equities, credit spreads or commodity prices. The derivative contracts are often OTC-traded, i e the terms connected to the specific contract are agreed upon on individual terms with the counterpart.

7.2.1 General information about derivatives

Nordea enters into derivative contracts based on customer demand, both directly and in order to hedge positions that arise through such activities. Nordea, through Group Treasury also uses interest rate swaps and other derivatives in its hedging activities of the assets and liabilities on the balance sheet. Furthermore, Nordea may, within clearly defined restrictions, use derivatives to take open positions in its operations. Derivatives affect counterparty risk and market risk as well as operational risk.

7.2.1.1 Specific information about credit derivatives transactions

Nordea acts as an active intermediary in the credit derivatives market, especially in Nordic based names. Nordea is also using credit derivatives to hedge positions in corporate bonds and collateralised debt obligations (CDOs). Typical derivative products are single name credit default swaps and synthetic CDOs. Credit derivatives are only used to a very limited extent to mitigate the risk in Nordea's lending credit portfolio.

When Nordea sells protection in a CDO transaction, Nordea carries the risk of losses in the reference portfolio on the occurrence of a credit event. When Nordea buys protection in a CDO transaction, any losses in the reference portfolio, in which Nordea has not necessarily invested, triggered by a credit event is then carried by the seller of protection.

Credit derivatives transactions create counterparty risk equal to other derivative transactions. As it is Nordea's policy to enter into bilateral, cross product closeout netting agreements with the counterparts, it is not possible to quantify the counterparty risk exposure arising from credit derivatives transactions isolated. Counterparts from which Nordea buys protection are typically subject to a financial collateral agreement, thus the exposure is on daily basis covered by collateral placements.

Table 33 and table 34 lists the total outstanding volumes of credit default swaps and CDOs at the end of 2008, split into bought and sold positions. To illustrate the business volume, the figures are provided on gross level, meaning no netting has been considered between bought and sold contracts in the same underlying name. The risk positions are subject to various types of market risk limits, including VaR, and the CDO valuations are subject to fair value adjustments for model risk. These fair value adjustments are recognised in the income statement. In the Nordea Group, the credit derivative portfolio is referable to Nordea Bank Finland Plc.

Table 33 Credit default swaps, 31 Dec 2008

EURm	Total gross notional sold	Total gross notional bought
Single name CDS: Investment grade	18,399	18,335
Single name CDS: Non-Investment grade	7,364	7,629
Multi name CDS indices	20,082	19,416
Total	45,845	45,380

Table 34 Collateralised Debt

Obligations (CDO) - Exposure (excluding NLP)

Bought protection	Sold protection
4,390	3,909
2,883	2,883
1,507 ²⁾	1,026 ³⁾
277	207
337	143
893	676
	Bought protection 4,390 2,883 1,507 ²⁾ 277 337 893

 $^{1)}\,\mathrm{Net}$ exposure disregards exposure where bought and sold tranches are completely

identical in terms of reference pool attachment, detachment, maturity and currency. $^{2)}$ Of which investment grade EUR 1,503m and sub investment grade EUR 4m.

³⁾ Of which investment grade EUR 1,026m.

Except for a negligible part of the Multi name CDS indices (bought), all the CDS contracts are referable to the trading book.

7.2.2 Counterparty risk

Counterparty risk is the risk that Nordea's counterpart in a FX, interest rate, commodity, equity or credit derivative contract defaults prior to maturity of the contract and that Nordea at that time has a claim on the counterpart. Counterparty risk in Nordea is subject to credit limits like other credit exposures and is treated accordingly. Counterparty risk arises mainly in the trading book, but also in the banking book due to hedging of external funding.

7.2.2.1 Pillar 1 method for counterparty risk

Nordea uses the mark-to-market method to calculate the EAD for counterparty risk in accordance with the credit risk framework in CRD, i e the sum of current exposure (replacement cost) and potential future exposure. The potential future exposure is an estimate, which reflects possible changes in the market value of the individual contract during the remaining lifetime, and is measured as the notional principal amount multiplied by a risk weight. The size of the risk weight depends on the contract's remaining lifetime and the underlying asset. Netting of potential future exposures on contracts within the same legally enforceable netting agreement is done as a function of the gross potential future exposure of all the contracts and the quotient between the net current exposure and the gross current exposure. In table 35, the EAD as well as the RWA and capital requirement split on the exposure classes are available. As stated above, EAD equals the sum of current exposure and potential future exposure and as of December 2008 the potential future exposure is the major part of the EAD. It can be concluded that the RWA has increased considerably during 2008, mainly due to increased RWA against corporate customers.

7.2.2.2 Internal measurement of counterparty risk

Counterparty risk for internal credit limit purposes are calculated using a similar method to the pillar 1 method, but somewhat different risk weight and netting principles for calculation of the potential future exposure are applied.

In table 36, the current exposure and potential future exposure are presented for different type of customers.

As of December 2008, the current net exposure was EUR 12,202m and the potential future exposure was EUR 22,902 in the internal counterparty risk framework. It can be concluded that especially the current exposure has increased considerable during the year, which is due to the large movements in the financial markets, especially for various FX rates, interest rates and credit spreads.

For internal capital purposes (EC framework), the significant part of the counterparty risk exposure is calculated using a method referred to as Expected Positive Exposure. For the remaining part of the exposure, the method is similar to the method used for internal credit risk limits.

On traded OTC contracts, Nordea performs fair value adjustments to the counterparty risk exposures on portfolio level, which means that the market value of the contracts is adjusted to account for credit risk.

7.2.2.3 Mitigation of counterparty risk exposure

To reduce the exposure towards single counterparts, risk mitigation techniques are widely used in Nordea. The most common is the use of closeout netting agreements, which allow the bank to net positive and negative replacement values of contracts under the agreement in the event of default of the counterparty. In addition, Nordea also mitigates the exposure towards large banks, hedge funds and institutional counterparts by an increasing use of financial collateral agreements, where collateral on regular – typically daily – basis is placed or received to cover the current exposure. The collateral is largely cash (EUR, USD, DKK, SEK and NOK), but also government bonds and to a lesser extent mortgage bonds are accepted.

In table 37, information of how the counterparty risk exposure is reduced with risk mitigation techniques are available.

Table 35 Counterparty risk exposures 1), Pillar 1 method

		2008		31 Dec 2007		
EURm	EAD	RWA	Capital requirement	EAD	RWA	Capital requirement
Central government and central banks	543	1	0	442	3	0
Institutions	20,792	4,799	384	17,182	2,997	240
Corporate	12,400	5,778	462	3,939	1,618	129
Other	992	293	23	1,001	469	38
Total	34,727	10,870	870	22,564	5,087	407

1) Exposures are after closeout netting and collateral agreements and only include derivatives.

Table 36 Counterparty risk exposures, Internal method

EURm		31 Dec 2008		31 Dec 2007		
	Current exposure	Potential exposure future	Total credit risk	Current exposure	Potential exposure future	Total credit risk
Public entities	1,754	1,302	2,727	310	1,136	1,136
Institutions	4,291	14,454	13,010	2,201	14,734	14,738
Corporate	6,157	7,146	12,150	864	6,119	5,351
Total	12,202	22,902	27,887	3,375	21,989	21,225

Table 37 Mitigation of counterparty risk exposure due to closeout netting and collateral agreements

	31 Dec 2008				31 Dec 2007			
FUR	Current Exposure	Reduction from closeout netting	Reduction from held	Current	Current Exposure	Reduction from closeout netting	Reduction from held	Current Exposure
EUKIII	(gross)	agreements	conateral	Exposure (net)	(gross)	agreements	conateral	(net)
Total	82,203	66,364	3,637	12,202	29,800	23,979	2,446	3,375

As of December 2008 Nordea had 479 financial collateral agreements. The effects of closeout netting and collateral agreements are considerable, as 85% of the current exposure (gross) was eliminated by the use of these risk mitigation techniques.

Nordea's financial collateral agreements do typically not contain any trigger dependent features, for example rating triggers. For a few agreements the minimum exposure level for further posting of collateral will be lowered in case of a downgrading. Separate credit guidelines are in place for handling of the financial collateral agreements.

Finally, Nordea also uses a risk mitigation technique based upon a condition in some of the long-term derivative contracts, which gives Nordea the option to terminate a contract at a specific time or upon the occurrence of specified credit related events.

The 10 largest counterparties measured on current exposure (net) account for around 20% (2007: 33%) of Nordea's total current exposure, and consists of a mix of financial institutions, public and corporate counterparties.

7.2.3 Settlement risk

Settlement risk is a type of credit risk arising during the process of settling a contract or execution of a payment.

The risk amount is the principal of the transaction, and a loss could occur if a counterpart were to default after Nordea has given irrevocable instructions for a transfer of a principal amount or security, but before receipt of the corresponding payment or security has been finally confirmed.

The settlement risk on individual counterparts is restricted by settlement risk limits. Each counterpart is assessed in the credit process and clearing agents, correspondent banks and custodians are selected with a view of minimising settlement risk.

Nordea is a shareholder of, and participant in, the global FX clearing system CLS (Continuous Linked Settlement), which eliminates the settlement risk of FX trades in those currencies and with those counterparts that are eligible for CLS-clearing. As a result, Nordea's settlement risk exposure against major trading counterparts has decreased considerably in recent years.

7.2.4 Market risk

For all categories of derivatives, it applies that the market risk stemming from the derivative contracts is an integral part of Nordea's general setup for managing market risk. A prime purpose of derivatives is to hedge market risk from on balance sheet items. Therefore, when measuring Nordea's market risk, no distinction is made between risk from onbalance sheet items and derivatives. The RWA for market risk therefore contains risk stemming from derivatives, including credit derivatives. See chapter 5 for further description of Nordea market risk models and capital requirement for market risk in Nordea.

7.3 Special Purpose Entities and securitisations7.3.1 Consolidation of Special Purpose Entities

A special purpose entity (SPE) is an entity created to accomplish a narrow and well-defined objective. Examples are entities created to effect leases, research and development activities or securitisations of financial assets. The legal form of a SPE may be a corporation, trust, partnership or unincorporated entity. SPEs are often created with legal arrangements setting limits on the decision-making powers of their governing board, trustee or management over the SPE's operations.

The sponsor (or entity on whose behalf the SPE was created) often transfers assets to the SPE and obtains the right to use assets held by the SPE. The sponsor can perform services for the SPE, while other parties may provide capital to fund the SPE. A SPE can in substance be controlled by an entity engaged in transactions with the SPE.

In accordance with IFRS Nordea does not consolidate SPEs' assets and liabilities beyond its control. In order to determine whether Nordea controls a SPE or not, Nordea has to make judgements about risks and rewards and assesses the ability to make operational decisions for the SPE in question. Factors included in the assessment are whether the activities of the SPE are being in substance conducted on Nordea's behalf or if Nordea has in substance the decision making powers, the rights to obtain the majority of the benefits or the majority of the residual- or ownership risks. Nordea consolidates all SPEs where Nordea has retained the majority of the risks and rewards. For the SPEs that are not consolidated the rationale is that Nordea does not have any significant risks or rewards on these assets and liabilities.

At year end 2008, Nordea is the sponsor of the following SPEs presented in table 38.

		Duration	Accounting treatment	Nordea's investment ¹⁾	Total assets
CMO Denmark A/S	Collateralised Mortgage Obligation	>5 years	Consolidated	12	33
Kalmar Structured Finance A/S	Credit Linked Note	>5 years	Consolidated	25	142
Mermaid Repackaging Plc	Credit Linked Note	4 years	Not consolidated	34	71
Viking ABCP Conduit	Factoring	<1 year	Consolidated	733	801
Kirkas Northern Lights Ltd	Collateralised Mortgage Obligation	>5 years	Consolidated	8,096	8,096
Total				8,900	9,143

Table 38 Special Purpose Entities

1) Includes all assets towards SPEs (such as bonds, subordinated loans and drawn credit facilities).

Nordea offers a secondary market in notes issued by some of these SPEs and occasionally buys back financial instruments from the external counterparts. More information on the different SPEs can be found below.

7.3.2 Entities issuing structured credit products

Nordea gives investors an opportunity to invest in different types of structured credit products such as CDO and Collateralised Mortgage Obligations (CMO). These have previously been offered through the three SPEs described below but are currently mainly offered through Nordea Bank Finland and thereby included on balance in the Group.

Collateralised Mortgage Obligations Denmark A/S (CMO Denmark A/S) was established with the purpose to issue CMOs in order to meet specific customer preferences in terms of credit risk, interest rate risk, prepayment risk, maturity etc. The SPE purchased a pool of mortgage bonds and reallocated the risks through tranching a similar bond issue (CMOs). At year end 2008 the total notional of outstanding bonds was EUR 33m available to investors. Nordea holds bonds issued by CMO Denmark A/S as part of offering a secondary market for the bonds. The investment amounted to EUR 12m as of year end 2008. Nordea includes the bond holdings with CMO Denmark A/S in its capital requirement calculation. The RWA and capital requirement of these positions are included within the market risk framework of Nordea's trading book, see chapter 5 for further information.

Kalmar Structured Finance A/S was established to allow customers to invest in structured products in the global credit markets. The SPE enters into Credit Default Swaps (CDS) and hereby acquires a credit risk on an underlying portfolio of names (like corporate names) and at the same time the SPE issues Credit Linked Notes (CLN) with a similar credit risk that reflect the terms in the CDS. Nordea is the counterpart in the derivative transactions. The total notional of outstanding CLNs in this category was EUR 142m at year end 2008. Nordea holds CLNs issued by the SPE as part of offering a secondary market for the notes. The investment amounted to EUR 25m at year end 2008. Nordea includes the CLN holdings and derivative positions with the SPEs in the capital requirement calculations. The RWA and capital requirement of these positions are included within the market risk framework of Nordeas trading book, see chapter 5 for further information.

Mermaid Repackaging Plc was established to allow customers to invest in structured products in the global credit markets. The SPE issues Credit Linked Notes (CLN) to investors and invests the funds received in Floating Rate Notes and credit derivatives. Nordea does not supply any liquidity to the SPE or participate in any derivative transactions. The total notional of CLN issuance in this category was EUR 71m year end 2008. Nordea holds CLNs issued by Mermaid at year end 2008 and the investment amounts to EUR 34m. Nordea includes the CLN holdings and derivative positions with the SPEs in the capital requirement calculations. The RWA and capital requirement of these positions are included within the market risk framework of Nordea trading book, see chapter 5 for further information.

7.3.3 Other SPEs

The Viking ABCP Conduit (Viking) has been established with the purpose of supporting trade receivable or accounts payable securitisations to core Nordic customers. The SPEs purchase trade receivables from the approved sellers and fund the purchases either by issuing Commercial Papers (CP) via the established Asset Backed Commercial Papers programme or by drawing the funds on the liquidity facilities available. Nordea has provided liquidity facilities of maximum EUR 1,122m and at year end 2008, EUR 733m were utilised. There is no outstanding CP issue at year end 2008. These SPEs are consolidated as they are closely linked to the activities within Nordea. Also, Nordea is exposed to credit risk through the liquidity facility. The RWA and capital requirement of assets in Viking are included within the market risk framework of Nordeas trading book, see chapter 5 for further information.

Kirkas Northern Lights Ltd (Kirkas) has been established during 2008. Assets have been sold from Nordea's ordinary lending portfolio to Kirkas. Kirkas has used the assets as collateral for bonds issued. The total notional of bonds and subordinated loans was EUR 8,096m at year end 2008, which are held in full by Nordea. Nordea still holds the majority of the residual- and ownership risks in the SPE, why the SPE is consolidated into the Nordea Group. Capital requirement is calculated based on the lending portfolio as if the transaction had not been performed due to that there has been no transfer of risk.

7.3.4 Investments in securitisations

According to the CRD, banks have securitisation positions whenever exposed to transactions where payments depend on the performance of an underlying pool of exposures and where a subordination structure ("tranche structure") exists for determination of losses from the same pool.

In a traditional securitisation, assets are transferred to a SPE, which in turn issues securities backed by these assets. In synthetic securitisation, assets are not physically transferred but by using credit derivatives it is possible to synthetically create a situation similar to a physical transfer. Nordea has no investments in securitisations in the banking book, according to the CRD definition of securitisation.

During 2008, in response to the financial turmoil, the Financial Stability Forum recommended enhanced transparency in selected exposures related to securitisation. As described in chapter 7.2, Nordea acts as an intermediary in the credit derivative market and, amongst other products, also trade in CDOs. These exposures, synthetic securitisations, are included in Nordea's trading book.

8. Liquidity management

8.1 Liquidity risk

8.1.1 Management principles and control

The Board of Directors of Nordea has the ultimate responsibility for Asset and Liability Management of the Group ie limiting and monitoring the Group's structural risk exposures.

Risks in Nordea are measured and reported according to common principles and policies approved by the Board. The Board of Directors also decides on policies for liquidity risk management. These policies are reviewed at least annually.

The CEO in GEM decides on the targets for the Group's risk management regarding SIIR, as well as, within the scope of resolutions adopted by the Board of Directors, the allocation of the liquidity risk limits.

The ALCO, chaired by the CFO, prepares issues of major importance concerning the Group's financial operations and financial risks for decision by CEO in GEM.

Group Treasury operationalises the targets and limits and develops the liquidity risk and SIIR management frameworks, which consists of policies, instructions and guidelines for the whole Group.

8.1.2 Liquidity risk management

Liquidity risk is the risk of being able to meet liquidity commitments only at increased cost or, ultimately, being unable to meet obligations as they fall due.

Nordea's liquidity management is based on policy statements resulting in different liquidity risk measures, limits and organisational procedures.

Policy statements stipulate that Nordea's liquidity management reflects a conservative attitude towards liquidity risk. Nordea strives to diversify the Group's sources of funding and seeks to establish and maintain relationships with investors in order to manage the market access.

Broad and diversified funding structure is reflected by the strong presence in the Group's four domestic markets in the form of a strong and stable retail customer base and the variety of funding programmes.

Funding programs are both short-term (US Commercial Papers, European Commercial Papers, Commercial Papers, Certificates of Deposits) and long-term (Swedish and Danish Covered bonds, European Medium Term Notes, Medium Term Notes) in diverse currencies. However, foreign exchange risk is covered. In table 39, the funding sources are presented. As of the end of 2008, the total volume of short-term programs was EUR 44bn with the average maturity of 0.2 years and the total volume of the long-term programs is EUR 65bn with the average maturity of 9.0 years. Special focus is given for the composition of the investor base in the terms of geographical range and rating sensitivity.

Nordea publishes adequate information on the liquidity situation of the Group to remain trustworthy at all times.

Nordea's liquidity risk management includes stress testing and a business continuity plan for liquidity management. Stress testing is defined as the evaluation of potential effects on a bank's liquidity situation under a set of exceptional but plausible events. The stress test should identify events or influences that could affect the funding need or the funding price and seek to quantify the potential effects. The purpose of stress tests is to supplement the normal liquidity risk measurement and confirm that the business continuity plan is adequate in stressful events, and that the business continuity plan properly describes procedures to handle a liquidity crisis with minimal damage to Nordea. Nordea stress scenarios are based on assessment of the particular events for which Nordea is presumed to be most vulnerable to taking into account the current business structure and environment. Stress tests focus on the other hand on increased funding need and on the other hand on increased funding price.

Group Treasury is responsible for managing the liquidity in Nordea and for compliance with the group wide limits from the Boards of Directors, CEO in GEM and ALCO.

Table 39 Funding sources, 31 Dec 2008

T · 1 ·1·, ,	Interest	Average	FUD
Liability type	rate base	maturity	EUKM
Deposits by credit institutions			
 Shorter than 3 months 	Euribor etc	0.1	49,341
 Longer than 3 months 	Euribor etc	0.8	2,591
Deposits and borrowings from the public			
 Deposits on demand 	Administra	tive 0.0	107,393
 Other deposits 	Euribor etc	0.4	41,198
Debt securities in issue			
 Certificates of deposits 	Euribor etc	0.2	33,666
– Commercial papers	Euribor etc	0.2	10,440
- Mortgage covered	Fixed rate,	J 11.2	40 504
	market base	a 11.5	49,504
- Other bond loans	market base	ed 1.8	15,378
Derivatives	á	Not applicable	85,538
Other non-interest-bearing items	á	Not	23,774
Subordinated debentures			
 Dated subordinated 	Fixed rate,		
debenture loans	market base	d 6,4	6,268
 Undated and other 	Fixed rate,		
subordinated	market	Not	
debenture loans	based a	applicable	1,942
Eit		Not	17 002
Equity	č	аррисавіе	17,803
Total (total liabilities and equit	y)		444,836
Liabilities to policyholders		Not	29 238
Total (total liabilities and equi	(h)	rricubic	
including Life insurance opera	ations		474,074

8.1.3 Liquidity risk measurement methods

The liquidity risk management focuses on both short-term liquidity risk and long-term structural liquidity risk. In order to measure the exposure on both horizons, a number of liquidity risk measures have been developed covering all material sources of liquidity risk.

In order to manage short-term funding positions, Nordea measures the funding gap risk, which expresses the expected maximum accumulated need for raising liquidity in the course of the next 14 days. Cash flows from both on-balance sheet and off-balance sheet items are included. Funding gap risk is measured and limited for each currency and as a total figure for all currencies combined. The total figure for all currencies combined is limited by the Board of Directors.

To ensure funding in situations where Nordea is in urgent need of cash and the normal funding sources do not suffice, Nordea holds a liquidity buffer. Limit is set by the Board of Directors for the minimum size of the liquidity buffer. The liquidity buffer is set to ensure a total positive cash flow defined by the funding risk measurement and consists of high-grade liquid securities that can be sold or used as collateral in funding operations.

The structural liquidity risk of Nordea is measured and limited by the Board of Directors through the net balance of stable funding, which is defined as the difference between stable liabilities and stable assets. These liabilities primarily comprise retail deposits, bank deposits and bonds with a remaining term to maturity longer than 6 months, and shareholders' equity, while stable assets primarily comprise retail loans, other loans with a remaining term to maturity longer than 6 months and committed facilities. ALCO has set as a target that the net balance of stable funding should be positive, which means that stable assets must be funded by stable liabilities.

8.1.4 Liquidity risk analysis

The short-term liquidity risk has been held at moderate levels throughout 2008. The average funding gap risk, ie the average expected need for raising liquidity in the course of the next 14 days, has been EUR –8.7bn (EUR –4.8bn).

Nordea's liquidity buffer has been in the range EUR 20.1– 40.2bn (EUR 12.5–28.3bn) throughout 2008 with an average of EUR 27.1bn (EUR 19.4bn). Nordea considers this a high level and it reflects the Group's conservative attitude towards liquidity risk in general and towards unexpected liquidity events in particular. Nordea's liquidity buffer is highly liquid consisting of 94% of central bank eligible securities at the end of 2008.

The aim of always maintaining a positive net balance of stable funding has been comfortably achieved throughout 2008. The yearly average for the net balance of stable funding was EUR 8.0bn (EUR 9.8bn). The net balance of stable funding is shown in table 40.

8.2 Structural Interest Income Risk

Structural Interest Income Risk (SIIR) is the amount Nordea's accumulated net interest income would change during the next 12 months if all interest rates change by one percentage point.

SIIR reflects the mismatch in the balance sheet items and the off-balance- sheet items when the interest rate re-pricing periods, volumes or reference rates of assets, liabilities and derivatives do not correspond exactly. Nordea's SIIR management is based on policy statements resulting in different SIIR measures, targets and organisational procedures.

Policy statements focus on optimising financial structure, balanced risk taking and reliable earnings growth, identification of all significant sources of SIIR, measurement under stressful market conditions and adequate public information.

Group Treasury has the responsibility for the operational management of SIIR and for complying with Group wide targets.

8.2.1 SIIR measurement methods

The basic measures for SIIR are the two re-pricing gaps measuring the effect on Nordea's net interest income for a 12 months period of a one percentage point increase, respectively decrease, in all interest rates. The SIIR is presented in table 41. The re-pricing gaps are calculated under the assumption that no new market transactions are made during the period.

Main elements of the customer behaviour and Nordea's decision-making process concerning Nordea's own rates are, however, taken into account.

For example in a low interest rate environment, when rates are decreasing further, the total decrease of rates cannot be applied to non-maturity deposits since rates cannot be negative.

Similarly in an increasing rate environment Nordea may choose not to increase interest rates on all customer deposits correspondingly.

8.2.2 SIIR analysis

At the end of the year, the SIIR for decreasing market rates was EUR –218m (EUR –267m) and the SIIR for increasing rates was EUR 55m (EUR 235m). These figures imply that net interest income would decrease if interest rates fall and increase if interest rates rise.

Table 40 Net balance of stable funding,31 Dec 2008

Stable liabilites and equity

Liability type	EURbn
Equity and Core liabilities	
Deposits and borrowings from the public	127.3
Equity	17.8
Structural funding	
Long-term deposits from credit institutions	1.3
Long CD and CP	2.5
Long-term bonds issued	43.2
Total stable liabilities and equity	192.0
Stable long-term assets	

Asset type	EURbn
Core assets	
Loans and receivables to the public	177.0
Long-term loans to credit institutions	5.7
Illiquid assets	1.6
Total stable long-term assets	184.3
Net balance of stable funding	7.8

Table 41 SIIR, Gap analysis, 31 Dec 2008

Re-pricing gap for increasing interest rates

EURm Interest Rate Fixing Period	Group balance sheet	Within 3 months	3–6 months	6–12 months	1–2 years	2–5 years	>5 years	Non Repricing	Total
Assets								1 0	
Interest bearing assets	351,451	246,780	19,326	10,296	9,045	9,169	31,797	25,037	351,451
Non interest bearing assets	122,624	0	0	0	0	0	0	122,624	122,624
Total assets	474,074	246,780	19,326	10,296	9,045	9,169	31,797	147,661	474,074
Liabilities and equity									
Interest bearing liabilities	317,721	233,138	19,760	10,344	11,919	14,773	25,830	1,957	317,721
Non interest bearing	156,353	0	0	0	0	0	0	156,353	156,353
Total liabilities and equity	474,074	233,138	19,760	10,344	11,919	14,773	25,830	158,310	474,074
Off-balance-sheet items, net		-6,060	-1,848	-870	4,538	4,539	-299		
Exposure	7,582	-2,283	-918	1,664	-1,065	5,669	-10,649		
Cumulative exposure		5,299	4,381	6,045	4,980	10,649	0		

9. ICAAP

Pillar 2 in the CRD, or the Supervisory Review Process (SRP), covers two main processes: the ICAAP and the Supervisory Review and Evaluation Process (SREP). This chapter describes the major components of these processes such as the EC framework, stress testing, and SREP.

9.1 Components of ICAAP

The purpose of the ICAAP is for each institution to review the management, mitigation and measurement of material risk to assess the adequacy of internal capital and to determine an internal capital requirement reflecting the risk appetite of the institution.

The internal capital requirements under the ICAAP are in Nordea based on the internal EC framework. In addition to calculating EC, Nordea conducts a comprehensive capital adequacy stress test process to analyse the effects of a series of global and local shock scenarios as part of the ICAAP. The results of stress testing are considered, along with potential management interventions, in internal capital requirement. Moreover, the internal capital requirement also takes less quantifiable components and third party requirements into consideration, both legally binding requirements and those arising from business decisions. By considering the stress test results in the assessment of internal capital requirements the pro-cyclicality effects inherent in the risk adjusted capital calculations of the EC and IRB approaches are addressed.

9.1.1 EC

Since 2001 Nordea has calculated internal capital requirements based on the EC frame-work. This covers the following major risk types: credit risk, market risk, operational risk, business risk and life insurance risk. Pillar 1 of the CRD closes the gap between regulatory capital and EC by improving the risk sensitivity of regulatory capital measurement, but still several differences remain, since EC covers both pillar 1 and pillar 2 risks. The primary differences between EC and the capital requirement according to CRD are:

- Confidence level:
 - The confidence level for all risk types is 99.97% in the EC framework, versus 99.9% in pillar 1 of CRD.
- Life insurance operations:
 - The EC framework includes risk in the life insurance operations of Nordea Life & Pensions (NLP), while this risk is not included in the pillar 1 of CRD (but instead deducted in the capital base). The life insurance business in Nordea generally consists of long-term contracts, having durations of more than 40 years. The two major risks in the life insurance business are life insurance risk and market risk. These risks have to a larger extent effects for policyholders and to a lesser extent effects on Nordea's own account. These risks are primarily controlled using actuarial methods, i.e. through tariffs, rules for acceptance of customers, reinsurance contracts, stress tests and provisions for risks. A continuous supervision of the appropriateness of the parameters in the risk models

is undertaken to ensure that changes in the underlying risks are properly taken into account.

- The market risk for Nordea's own account of life insurance operations arises from mismatches of the market risk exposure on assets and liabilities and is measured as a loss in operating income as a result of movements in financial market prices. The income model is primarily fee-based, contingent but not directly dependent on investment return. The market risk on separated equity capital investments for Nordea NLP is included in the Group's consolidated market risk measurement (see chapter 5). The market risk for NLP is not included in pillar 1 capital calculations, but included in the EC. The EC is included in the market risk capital.
- The life insurance risk is the risk of unexpected losses due to changes in mortality rates, longevity rates, disability rates and selection effects. Life insurance risk is not included in pillar 1 calculations, but included in the EC framework.
- Credit risk:
 - EC for credit risk includes maturity adjustments.
 - Exposures calculated using the Standardised Approach in pillar 1 according to CRD are calculated on the basis of internal models in the EC framework, though the models have not yet been approved by the financial supervisory authorities for use in the regulatory calculations.
 - Credit risk EC for corporate and institutions exposures is calculated using the internal estimates of LGD and EAD (i e using the Advanced IRB), rather than the regulatory values in the FIRB approach within pillar 1 of CRD.
 - Concentration risk is captured via the use of an internal credit risk portfolio model, which is not specifically accounted for in pillar 1 in CRD but accounted for in the EC framework. Credit concentration risk is the credit risk stemming from not having a perfectly diversified credit portfolio, i e the risk inherent in doing business with large customers or being overexposed in particular industries or regions. Through the use of a credit risk portfolio model which considers exposures by industry and geography, the concentration risk can be identified. Credit risk measures are based on the results of the portfolio model although the industry or region concentration impact is allocated pro rata over the entire portfolio. Additionally, the credit risk measures consider exposure to large customers by applying a single-name concentration addon in the EC frame-work.
- Market risk:
 - EC for market risk is calculated for the trading book, but also for market risk in the investment and funding portfolio and life insurance business (see second bullet point above), risk in sponsored defined benefit pension plans as well as real estate risk. The market risk associated with Nordea's long-term leases of its

own office buildings is measured using a framework based on the book value of the underlying assets. In pillar 1 of the CRD, only the trading book is included in the capital calculations for market risk.

- Business risk:
 - Business risk is not included in pillar 1 of CRD. The EC framework includes business risk to account for the residual volatility in historical profit and loss after adjustments for market, operational and credit risk. Business risk represents the earnings volatility inherent in all businesses due to the uncertainty of revenues and costs as a consequence of changes in the economic and competitive environment. The main risk drivers of business risk are size of the fixed cost base, business margin volatility, volatility in business volumes and cost volatility. In this context, indirect effects such as the net interest income (NII) effect (a consequence of the SIIR, strategic risk and liquidity risk are considered). The business risk measurement is based on historical volatility in profit and loss stemming from business risk, i.e. a "cleaned operating profit" where the contributions from other risk types are neglected (e.g. trading income, credit losses, effect of operational risk events).
- Operational risk:
 - Differences in operational risk are due to differences in the historical collection of gross income data, which is the most recent rolling four quarters in EC and a three year average in Pillar 1.
- Diversification effects:
 - Unlike pillar 1 in CRD, the EC framework accounts for group level diversification benefits in Nordea's varied operations.

The EC as of December 31 2008 amounted to EUR 12.8 bn. In figure 10 a comparison between Nordea's EC and capital calculated under pillar 1 in CRD is available. The approval of IRB Retail has reduced the differences between Nordea's EC and the pillar 1 capital requirement. The additional capital held for life operations, market risk, operational risk and business risk is offset by the higher parameters in pillar 1 for corporate and institutions, as well as the remaining portions of the portfolio measured using the standardised approach. Finally, Nordea's diversification adjustment reduces overall EC by 2.3 EURbn.

The figure 11 shows the EC in the dimensions customer area and risk type as of end of December 2008. Notably the credit risk accounts for 70% of the total EC. The diversification effect was 15.0% which reduced the total diversified EC, with EUR 2.3bn as compared to the total EC without diversification. In 2008 the EC increased with 18%. The increase is largely explained by increased credit risk, which to a high degree is accounted for by increased volumes.

Figure 10 Comparison of EC and pillar 1 regulatory capital requirement



Figure 11 EC distributed by customer area and risk type





9.1.2 Stress tests

As a part of the ICAAP stress tests are used as an important risk management tool in order to determine how severe unexpected changes in business and macro environment will effect the capital need. The stress test reveals how the capital need varies during a stress scenario, where impact on regulatory capital requirements, EC and capital ratios occurs.

Nordea conducts a comprehensive stress test annually, while ad-hoc stress tests, reverse stress tests and parameter sensitivity analyses for risk parameter are performed continuously. The stress test process is divided into the following three steps:

- Scenario development and translation.
- Calculation.
- Analysis and reporting.

9.1.2.1 Scenario development and translation

The annual stress test is based on three-year economic scenarios for each Nordic country and the scenarios are designed to replicate shocks that are particularly relevant for the existing portfolio. The development of stressed scenarios is performed by experts within Nordea Economic Research division in each Nordic country. In addition to the stress scenarios Nordea uses a rolling financial forecast as a base case and the difference between the stressed and the base case scenario will set the ground for the stress effect and the additional capital need.

While the annual stress test is based on complex macro economic scenarios which involve estimates of several macroeconomic factors, the ad-hoc stress tests are based on direct estimates on risk parameter changes or a few macro variables. This enables senior management to easily define scenarios and evaluate the effect of them in capital planning.

After a scenario is developed, the effects are translated and the risk and financial parameters are simulated. Advanced models in combination with expert judgment from business areas are used in order to determine the effect of the scenario.

As an example, in the annual stress test, the scenarios are translated to impact the parameters presented in table 42.

Table 42 Parameters in the annual stress test

Parameter	Impact
Volumes	Volumes from deposits and lending are adjusted according to each scenario by isolating the specific impact of each parameter.
Margins	The margins are adjusted according to the development of the credit spread and the maturity of the portfolio.
Net interest income	Net interest income figures are adjusted according to the change in volume and margins in deposits and lending.
Net fee and commission income	Net fee and commission income is adjusted for changes in fees and commissions from activities in Asset Management.
Funding cost	Changes in funding costs deriving from liquidity risk is incorporated and increases the cost of long-term and short-term funding and reduces the net interest income.
Loan losses	Loan losses are calculated using an expected loss/provisions-recoveries model or stated in the scenario as bps of lending for each segment and country.
Exposures	Exposures are adjusted with the volume and growth expectations as well as the loan losses.
Rating migration	Each year a new rating distribution is created for each portfolio. This includes stress testing of the financial statements for the majority of corporate customers which results in a new rating according to the rating model.
Probability of default	The PD values are stressed in order to reflect increases in defaults, simulating the existing process for defining probability of default.
Collateral values	The collateral coverage is stressed by moving parts of the exposure from secured to unsecured, resulting in an increase in average weighted LGD.

9.1.2.2 Calculation

The stressed figures and parameters from the scenario are used to calculate the effect on the regulatory capital requirements, EC and the financial statement. The regulatory capital is calculated for the credit risk, market risk and operational risk according to the CRD with regards to the IRB approaches used. The calculations for each risk type is aggregated into total capital requirement figures.

EC with the stressed parameters is calculated for credit risk, market risk, operational risk, business risk and life risk according to the EC framework. The calculation for each risk type is aggregated into total EC figures, including diversification effects.

Stressed figures for loan losses, net profit and dividend from the financial statements are used to calculate the effect on the capital base. The capital base is set in relation to the regulatory capital or EC in order to calculate the effect on capital ratios during a stress scenario.

9.1.2.3 Analysis and reporting

The first level of reporting is Nordea the Capital Planning Forum, which reviews the de-tails of the stress testing and implications on future capital. The finalised results are distributed to GEM and Board of Directors in the different legal entities in a manner that describes the implications of the stress tests on the adequacy of existing capital.

The results of the stress testing should support senior management's understanding of the implications of the current capital strategy given potential market shocks. Based on this information senior management is able to ensure that the Group holds enough capital against the risk of the stressed events, or similar events, occurring.

In 2008, the turbulence in the financial markets increased and in order to evaluate the effect of the market turmoil and the changes in macro economic forecasts Nordea actively works with stress tests as a part of the overall stress testing framework. The stress tests has a overall perspective for Nordea as a group while special focus areas are taken into account such as exposures against the Baltic's or the shipping industry which has been seen as high risk exposures in today's financial market situation. The stress tests are reproduced as soon as new forecasts is defined which will affect Nordea's portfolio such as changes in lending growth, rating, collateral coverage, loan losses and defaulted customers.

The outcome of the stress tests demonstrates how Nordea's loan loss and capital ratios will change during a stress scenario. The outcome is then analyzed in order to decide the capital need during a downturn period and ensure that Nordea is well capitalised.

9.1.3 Conclusion of ICAAP and SREP

Nordea's capital levels have been and continue to be adequate to support its risks from an internal perspective as well as from the vantage point of regulators. Heading into 2009, Nordea expects to continue to review the capital situation closely with regular ad-hoc stress testing providing a solid foundation for senior management decision making.

During the spring 2008, the regulators concluded that Nordea was adequately capitalized given its risk profile and portfolio based on the 2007 ICAAP. The 2008 ICAAP submission took place in mid 2008.

10. Capital base components

This chapter describes the conditions and major components of the capital base.

The calculation of capital base is done in accordance with the CRD and the Swedish legislation. The outcome must as a minimum correspond to the sum of the capital requirement for credit risks, market risks and operational risks and capital requirement related to transition rules. In the capital base for the Financial Group only capital contributed by subsidiaries or firms that are covered by the consolidated accounts are to be included.

Items included in the capital base should without restrictions or time constrains be available for the institution to cover risk and absorb potential losses. All amounts are included net of any tax charge. Generally, Nordea Group has the ability to transfer capital within its legal entities without material restrictions. International transfers of capital between legal entities are normally possible after approval by of the local regulator and are of importance when governing the capital position within the Group. The guarantee schemes introduced within EU has under certain circumstances limited the transferability to protect own countries' bank system before the functionality of cross border financial groups. The practical impact is at this time difficult to assess.

A summary of items included in the capital base is available in table 43.

The capital base (referred to as own funds in the CRD) is the sum of tier 1 capital and tier 2 capital after deductions

31 Dec 2008

31 Dec 2007

Table 43 Summary of items included in capital base EURm

Original own funds		
Paid up capital	2,600	2,597
Share premium		
Eligible capital	2,600	2,597
Reserves	12,157	11,060
Minority interests	11	10
Income (positive/negative) from current year	2,671	3,121
Eligible reserves	14,839	14,191
Tier 1 capital (before hybrid capital and deductions)	17,439	16,788
Hybrid capital loans subject to limits	1,447	1,409
Proposed/actual dividend	-519	-1,300
Deferred tax assets	-58	-185
Intangible assets	-2,193	-2,372
Deductions for investments in credtit institutions	-87	-80
IRB provisions excess (+) / shortfall (-)	-269	-30
Other items, net		
Deductions from original own funds	-3,126	-3,967
Tier 1 capital (net after deduction)	15,760	14,230
 of which hybrid capital 	1,447	1,409
Additional own funds		
Securities of indeterminate dur. and other instr.	690	664
Subordinate loan capital	5,407	5,406
Other additional own funds	0	5
Tier 2 capital (before deductions)	6,097	6,075
Deductions for investments in credtit institutions	-87	-80
IRB provisions excess (+) / shortfall (-)	-269	-30
Deductions from original additional own funds	-356	-110
Tier 2 capital (net after deductions)	5,741	5,965
Participations hold in insurance undert., reinsurance	-1,059	-1,535
Pension assets in excess of related liabilities	-116	0
Total own funds for solvency purposes (Capital base)	20,326	18,660

and less capital related to insurance companies. The two main components in the capital base are core equity in the balance sheet and subordinated debt. Below is a detailed description of the items included in the capital base.

The capital ratio is calculated by dividing the capital base with risk weighted assets while the quotient is calculated from the capital base in relation to the capital requirement.

10.1 Tier 1 capital

Tier 1 capital is defined as capital of the same or close to the character of eligible capital, eligible reserves and also a limited part (up to 30% of tier 1) instrument hybrid capital loans (perpetual loans).

10.1.1 Eligible capital

Paid up capital is equal to the share capital contributed by shareholders.

10.1.2 Eligible reserves

Eligible reserves consist primarily of retained earnings, other reserves, minority interest and income from current year. Retained earning are earnings from previous years reported via the income statement. Other reserves are related to the capital part of untaxed reserves, revaluation and translation reserves referred to acquisitions and associated companies under the equity method. The equity interests of minority shareholdings in companies that are fully consolidated in the financial companies group are also included. Positive income from current year is included as eligible capital after verification by the external auditors. However, negative income must always be included as a deduction. Repurchased own shares or own shares temporary included in trading portfolios, are deducted from eligible reserves.

10.1.3 Hybrid capital loans subject to limits

The requirements for including undated loans in tier 1 capital is restricted and repurchase can normally not take place until five years after the loan originally is issued. Hybrid capital loans, undated subordinated loans, may be repaid only by decision from Board of Directors in Nordea and with the permission of the Swedish Financial Supervisory Authority. Further, there are restrictions related to step up conditions, order of priority, interest payments under constraint conditions and the level of amount that can be part of the tier 1 capital. Previous years the limit for including hybrid capital in the tier 1 capital has been restricted to 15% but after decision by the Swedish financial supervisory authority and in effect from December 2008, the limit is changed to be 30% of the tier 1 capital after relevant deductions. If there are any surplus after applying the legal limit of 30%, exceeding amount can be transferred to tier 2 capital. For hybrid capital loans including step up conditions or other conditions that could give incentive to repurchase, the limit of 15% still apply.

Currently the hybrid capital loans included in the capital base of Nordea Group constitute 9.2% of the tier 1 capital, where of the loans with step up conditions together amounts to EUR 947m.

10.1.4 Deductions from Tier 1 capital

10.1.4.1 Proposed/actual dividend

In relation to income for the period, corresponding dividend should be deducted. The amount is deducted from the tier 1 capital and amounts to proposed distribution to shareholders by decision of the annual general meeting of shareholders.

10.1.4.2 Deferred tax assets

In accordance with local legal requirements deferred tax assets has been deducted from the tier 1 capital. Deducted amount is based on accounting standards relevant for the groups of institutions which constitute the capital base.

10.1.4.3 Intangible assets

The significant part of deducted intangible assets contains of goodwill. Other intangible assets relates to it software and development.

10.1.4.4 Deductions for investments in credit institutions The capital base should be deducted for equity holdings and some other certain types of contributions to institutions that are not part of the financial companies group (in Nordea foremost associated companies). 50% should be deducted from tier 1 capital and 50% should be deducted from tier 2 capital.

10.1.4.5 IRB provisions excess (+) / shortfall

The calculation of the capital base is in accordance with the CRD and the Swedish legislation. The differences between EL (EUR 1.5bn) and actual provision (EUR 1.0bn) made for the related exposures are adjusted for in the capital base. Note that this only relates to the IRB exposures. The negative difference (when the EL amount is larger than the provision amount) is included in the capital base as shortfall. According to the rules in the CRD, the shortfall amount shall be deducted from the capital base and be divided into both tier 1 capital and tier 2 capital. For the purpose of the CRD transitional rules calculations of the shortfall is under Swedish regulation deducted from the RWA to be neutralised in a Basel I perspective. A positive difference (provisions exceed EL) can be included in tier 2 capital with certain limitations (maximum 0,6 percentage of IRB RWA).

10.1.5 Changes in Tier 1 capital 2008–2007

The tier 1 capital has increased EUR 1.5bn and the main explanation is the retained earnings.

10.2 Tier 2 capital

The tier 2 capital is mainly related to subordinated debt with some specific deductions.

Tier 2 capital includes two different types of subordinated loan capital; perpetual loans and dated loans. The total tier 2 amount may not exceed tier 1 and dated tier 2 loans may not exceed half the amount of tier 1. The limits are set after deductions.

The basic principle for subordinated debt in the capital base is the order of priority in a default or bankruptcy situation. Under such conditions, the holder of the subordinated loan would be repaid after other creditors, but before

shareholders. The subordinated debt will to some extent prevent the institution to go into liquidation.

The amount possible to include in the tier 2 capital related to dated loans is reduced if the remaining maturity is less then five years. Outstanding amount in the specific issue is deducted by 20% for each year beyond five years.

As of end year 2008, Nordea holds EUR 5.4bn in dated subordinated debenture loans, EUR 0.7bn in undated subordinated debenture loans and EUR 1.5bn in hybrid capital loans (included as tier 1 capital).

10.2.1 Other additional funds

Other additional funds contains of adjustment to valuation differences in available for sale equities transferred to core additional own funds. Unrealised gains from equity holdings classified as available for sale securities can according to regulation only be included in tier 2 capital.

10.2.2 Deductions from Tier 2 capital

10.2.2.1 Deductions for investments in credit institutions The capital base should be deducted for equity holdings and some other certain types of contributions to institutions that are not part of the financial companies group (in Nordea foremost associated companies). 50% should be deducted from tier 1 capital and 50% should be deducted from tier 2 capital.

10.2.3 Participations hold in insurance undertakings

By a transitional rule in effect until year 2012, participations hold in insurance undertakings is deducted from the total capital base, meaning that the deduction should not affect the tier 1 capital. After year 2012, half of the amount should be deducted from tier 1 capital.

10.2.4 IRB provisions excess (+) / shortfall

The differences between EL and provision made for the related exposures are adjusted for in the capital base. The negative difference (when the EL amount is larger than the provision amount) is included in the capital base as shortfall. According to the rules in the CRD, the shortfall amount shall be deducted from the capital base and be divided into 50% in tier 1 capital and 50% in tier 2 capital.

10.2.5 Other deductions

Surplus net value of pension plans for employees should under certain circumstances be deducted from the sum of tier 1 and tier 2. At the end of 2008 the sum of the surplus values of the plans reached EUR 116m.

10.2.6 Changes in Tier 2 capital 2008

The main changes compared to year end 2007 refer to ordinary capital management and liquidity management and the deduction of the Nordea Life item. The decreased deduction for investments in NLP is explained by the change in the legal structure. Since 2008 the insurance companies are owned by the new NLP Holding AB in Sweden. The deduction is including both shares in the holding company and sub-ordinated loans. An additional capital injection of EUR 200m was conducted in the end of 2008 to strengthen the capital situation in the Life group. Note that this situation does not have any effect on the capital situation in Nordea as a financial conglomerate.

11. Capital adequacy conclusions

This chapter includes a summary of the capital management structure and detailed information of capital related ratios.

11.1 Capital management and governance

The efficient use of capital is achieved through active management of the balance sheet with respect to different asset-, liability- and risk categories. The goal is to enhance returns to the shareholder while maintaining a prudent risk and return relationship.

The Board of Directors decides ultimately on the targets for capital ratios in Nordea. The ability to meet targets and to maintain minimum capital requirements is reviewed regularly within the ALCO and the CPF. The CPF, headed by the CFO is the forum responsible for coordinating capital planning activities within the Group, including regulatory, internal and available capital. Additionally, the CPF and its members review forecasted capital requirements in the assessment of annual dividends, share repurchases, external and internal debt and capital injection decisions. The CPF considers information on key regulatory developments, market trends for subordinated debt and hybrid instruments and reviews the capital situation in the Nordea Group and in key legal entities. In the CPF the CFO decides, within the mandate given by the Board of Directors, on issuance of subordinated debt and hybrid capital instruments. Meetings are held at least quarterly or upon request by the CFO.

11.2 Capital policy

In 2008, Nordea's capital base and tier 1 capital exceeded the regulatory minimum requirements outlined in CRD. The overall purpose of the capital policy is to maintain capital at levels that are adequate from the perspective of regulators, funding, rating agencies and to optimise shareholder value in light of the external requirements. In February 2009, Nordea revised its capital policy and capital targets. The revised capital policy for Nordea Group states that over a business cycle, the target for the Tier 1 ratio is 9% and the target for the Capital ratio is 11.5%.

Nordea announced measures to strengthen the Group's core tier 1 capital by EUR 3bn. The Board of Directors of Nordea has resolved to increase Nordea's share capital through an underwritten discounted issue of new ordinary shares with pre-emptive rights for existing shareholders of approx. EUR 2.5bn net and secondly by proposing to reduce the dividend payment to 19% of the net profit for 2008, to be decided by the 2009 Annual General Meeting, which will

	2	2007		
EURm	Capital requirement	Basel II RWA	Capital requirement	Basel II RWA
Credit risk	12,060	150,746	12,556	156,952
IRB foundation	9,537	119,207	6,709	83,865
 of which corporate 	6,909	86,358	5,899	73,736
 of which institutions 	1,016	12,699	744	9,302
 of which retail 	1,465	18,313	na	na
- of which other	147	1,837	66	827
Standardised	2,523	31,539	5,387	67,342
 of which sovereign 	75	940	19	243
- of which other	2,448	30,599	5,368	67,099
Basel I reporting entities	na	na	460	5,745
Market risk	474	5,930	284	3,554
 of which trading book. VaR 	137	1,715	42	527
 of which trading book. non-VaR 	270	3,372	242	3,027
 of which FX. non-VaR 	67	843	0	0
 of which commodity risk 	0	0	0	0
Operational risk	952	11,896	878	10,976
Standardised	952	11,896	878	10,976
Sub total (excluding transition rules)	13,486	168,572	13,718	171,482
Adjustment for transition rules				
Additional capital requirement according to				
transition rules	3,577	44,709	2,649	33,103
Total (including transition rules)	17,062	213,281	16,367	204,585

Table 44 Capital requirements and RWA

increase core tier 1 capital by approx. EUR 0.5bn. The rights offering is subject to shareholder approval at an Extraordinary General Meeting to be held on 12 March 2009.

11.3 Regulatory capital requirement

In table 44, an overview of the capital requirements and the RWA as of December 2008 divided on the different risk types is presented. The credit risk comprises approximate 90% of the risk. Operational risk accounts for 7% of the capital requirements and market risk comprises 4% of the capital requirements. The low capital requirement for market risk is positively effected by the fact that the bank has received approval by the financial supervisory authorities to use the internal models approach for market risk. The FX risk in 2007 was below 2% of the capital base and therefore not included in the total market risk.

The table also includes information about the approach used for calculation of the capital requirements. Out of the total capital requirements for credit risk, 83% of the exposures have been calculated with the IRB approach, 17% with the standardised approach). Nordea Bank Polska S.A.,

Figure 12 RWA impact in 2008

Table 45 Key capital adequacy figures



Nordea Bank S.A. (Luxembourg) and JSB Orgres-bank (Russia) have in 2007 been reported in accordance with the previous regulatory framework, Basel I.

Furthermore in table 44, the capital requirements for credit risk, market risk and operational risk are adjusted with EUR 44.7m due to the transition rules (known as the capital floor). In 2008, the capital requirements could not be lower than 90% of the capital requirements calculated under Basel I regulations. The corresponding floor for 2009 is 80%. No floor limitations apply from 2010.

The main driver behind the changes in the RWA including transition rules relates to increased lending volumes and the approval to use IRB models for the Retail portfolio. Other impact on the RWA during the year have been rating migration and FX effects. In figure 12 the bridge between RWA Q4 2007 and RWA Q4 2008 is illustrated.

11.4 Capital ratios

The transition phase of Basel II creates a need to manage the bank using a variety of capital measurements and capital ratios. The table 45 shows that the regulatory transition rules comprise a floor on Nordea's capital requirement when compared to Basel II minimum requirements.

This difference will fluctuate through the transition period as the floor gradually decreases and Nordea receives approval for internal ratings based models for other portfolios. At present, this difference is EUR 44.7bn expressed as RWA and EUR 3.6bn expressed as regulatory capital requirement.

At the end of 2008 Nordea's tier 1 ratio excluding transition rules was 9.3% compared to 8.3% 2007. The increase relates to the approval from IRB Retail. The approval had the same impact on the capital ratios excluding transition rules which changed from 10.9% to 12.1%. Nordea's tier 1 ratio including transition rules was 7.4%, compared to 7.0% at the end of 2007. The capital ratio was 9.5% (including transition rules) at the end of 2008 and 9.1% 2007.

EURbn O4 2008 O3 2008 O2 2008 O1 2008 O4 2007 RWA including transition rules 213.3 218.2 214.3 201.4 204.6 RWA excluding transition rules 168.6 193.6 189.7 176.3 171.5 Regulatory capital requirement including transition rules 17.1 17.5 17.1 16.1 16.4 Regulatory capital requirement excluding transition rules 13.5 15.5 15.2 14.113.7 Capital base 20.3 20.5 19.9 18.8 18.7 15.8 Tier 1 capital 15.3 15.114.514.2 Core Tier 1 capital 14.3 13.8 13.5 13.1 12.8 7.0% 7.0% 7.0% Tier 1 ratio including transition rules 7.4% 7.2% Tier 1 ratio excluding transition rules 9.3% 7.9% 7.9% 8.3% 8.2% Core Tier 1 ratio including transition rules 6.7% 6.3% 6.3% 6.5% 6.3% Core Tier 1 ratio excluding transition rules 8.5% 7.1% 7.1% 7.5% 7.5% Capital ratio including transition rules 9.5% 9.4% 9.3% 9.4% 9.1% Capital ratio excluding transition rules 12.1% 10.6% 10.5%10.7% 10.9% Capital adequacy quotient (Capital base/Regulatory capital requirement excl transition rules) 1.5 1.3 1.3 1.3 1.4 Leverage ratio (Total assets/total equity) 26.6 24.7 25.0 23.1 22.7

In addition to regulatory requirements, Nordea has internal capital requirements based on the EC framework, which includes risks in Nordea's life insurance operations.

As such, the EC is compared to the capital base reversing the deduction for the life insurance operations.

The leverage ratio compares the total assets divided by total equity and is disclosed in table 45.

In the figures below, the development of tier 1 ratios and capital ratios are illustrated.

Figure 13 Capital adequacy ratios



11.5 Capital considerations for the future

The future regulation and subsequent capital requirements is expected to be influenced by the financial crises. To which extent the coming rules will change the prudential capital levels and management is unclear. Higher capital requirement will press the financial

market to assess the market operations.

The two EU directives, 2006/48 and 2006/49, in force to regulate the capital adequacy in Europe have been subject to an amendment process from 2007. In addition Basel Committee on Banking Supervision has also issued proposed new standards. Subsequently local laws are to be adjusted and the new rules will apply from 2009 or 2010 depending on the issue.

11.5.1 Own funds

Through a change in the local Swedish regulation the limit for tier 1 capital loans/hybrid capital was raised from 15 to 30% of the total tier 1 capital at the end of 2008. The other Nordic countries are expected to do the same with the purpose to open for new alternative capital sources for banks, to mitigate the financial turmoil.

11.5.2 Liquidity risk

Due to the prevailing financial turmoil there has been an increased focus on liquidity risk management practices by the banking industry, regulators and financial supervisory authorities. Nordea is also reviewing whether it can improve its own practices. Special focus will be given on liquidity stress test scenarios, effective collateral management and liquidity measures in general.

11.5.3 Large exposure

The lending on the interbank market will be subject to the same rules as other corporate lending with a few exceptions. Today most of the short term exposures are free from limitations. For Nordea this change might be interesting from an intragroup perspective as the inter bank rules currently apply cross border except in Sweden.

11.5.4 Market Risk

The Basel Committee announced further steps to strengthen the resilience of the banking system, among which was an extension of the Incremental Default Risk (IDRC) to capture risk from extraordinary events. The migration and default risk measure must be in place by 2010, while event and other risks may wait until 2011. The increased charge is expected to be more expensive in terms of required capital. It is very difficult to estimate the need for regulatory capital but it must be considered a given fact that the number will increase significantly in Nordea as for other banks.

11.5.5 Securitisation

The area of securitisation has been much in focus since the start of the crisis. The new rules and recommendations from other bodies will mean increased capital requirement and more transparency. This is only affecting Nordea marginally.

12. Appendix

12.1 General description of pillar 1, 2 and 3

The Basel II framework was an international initiative with the purpose to implement a more risk sensitive framework for the assessment of risk for the calculation of regulatory capital, i e the minimum capital that the institution must hold. The intention was also to align the actual assessment of risk within the institutions with the assessment of the regulatory capital by allowing use of internal models also for credit risk

From the beginning of 2007, the new CRD came into effect as the common frame-work for implementing the Basel II framework in EU. The CRD is built on three pillars:

- Pillar 1 requirements for the calculation of the RWAs and capital requirement.
- Pillar 2 rules for the (SRP), including the ICAAP.
- Pillar 3 rules for the disclosure of risk and capital management, including capital adequacy.

The CRD contains a detailed set of minimum requirements to assure the conceptual soundness and integrity of the internal assessment. In order to prevent large short-term effects on capital requirements, the regulators have introduced transitions rules (also known as capital floor) for all institutions implementing the new capital adequacy reporting. The transitional rules, in force 2007–2009, mark the lowest eligible capital base and relate directly to the capital requirements calculated under Basel I regulations. During 2007 the capital requirements should be no less than 95% of the capital requirements calculated under Basel I regulations. For 2008 and 2009 the amounts of capital requirements are allowed to be 90% and 80% respectively of the capital requirements calculated under Basel I regulations. Therefore, it can be concluded that the CRD will have a stepwise effect on the institutions through the transitional rules limiting the possible reduction of capital requirement. The full effect will occur after the transition rules period (January 2010).

12.1.1 Pillar 1

The new CRD is not changing the minimum required capital ratio of 8% compared to the previous regulation (Basel I). The changes are related to the definition and calculations of the RWA, which is the method used to measure the risk exposure of the reporting institution. The regulatory capital requirements are calculated using the following formula:

Minimum capital requirements = Capital base / RWA where, Minimum capital requirements ≥ 8% The RWAs are calculated by using more sophisticated and risk sensitive methods than previously. Credit risk and market risk are two essential risk types like in Basel I, while operational risk is introduced as a new risk type in the CRD. The table below identifies the approaches available for calculating RWA in each risk type in accordance with the CRD:

Table 46 Primary approaches in the CRD

Approaches for reporting capital requirements				
Credit Risk	Market Risk	Operational Risk		
(1) Standardised Approach	(1) Standardised Approach	(1) Basic Indicator Approach		
(2) Foundation Internal Rating Based Approach (FIRB)	(2) Internal Models Approach	(2) Standardised Approach		
(3) Advanced Internal Rating Based Approach (AIRB)		(3) Advanced Measurement Approach		

The standardised approach for calculating credit risk is close to the previous Basel I regulation, except an additional possibility to use external rating for the counterparts and wider use of financial collateral. The RWA is set by multiplying the exposure with a risk weight factor dependent on the external rating and exposure class.

Credit risk according to FIRB is based on the internal rating and PD for each counterpart and fixed estimates for LGD and CCF, while Advanced IRB is based on internal estimates for PD, LGD and CCF

Below is an overview of the key parameters used in calculation of RWA in Pillar I.

Figure 14 Key parameters in the RWA calculation



12.1.2 Pillar 2

Pillar 2, or the SRP, comprises two processes:

- the ICAAP and
- the (SREP).

The SRP is designed to ensure that institutions identify their material risk and allocate adequate capital, and employ sufficient management processes, to support such risk. The SRP also encourages institutions to develop and use better risk management techniques in monitoring and measuring risk in addition to the credit, market and operational risk in the CRD. The ICAAP allows banks to review their risk management policies and capital positions relative to the risk they undertake. In ICAAP, the institution ensures that it has sufficient available capital to meet regulatory and internal capital requirements, even during periods of economic or financial stress. The ICAAP includes all components of risk management, from daily risk management of material risk to the more strategic capital management of the entire Group and its legal entities. The SREP is the supervisor's review of the institution's capital management and an assessment of the institutes internal controls and governance.

Other risk types, which are not covered by the minimum capital requirements according to pillar 1, are typically liquidity risk, business risk, interest rate risk in the non-trading book and concentration risk. These are covered either by capital or risk management and mitigation processes under pillar 2.

12.1.3 Pillar 3

In the CRD it is also stipulated how and when institutions should disclose capital and risk management. The disclosure should follow the requirements according to the pillar 3. The main requirements are:

- Description of the Group structure and overall risk and capital management.
- Regulatory capital requirements and the capital base.
- Credit risk, including RWA calculations and loan losses.
- Market risk.
- Operational risk.

12.2 State schemes for finanical stability

State schemes for financial stability and amendments to these have been presented by the governments in the Nordic countries during the autumn 2008 and the beginning of 2009. Generally, Nordea welcomes the State schemes for financial stability and is currently evaluating the schemes and the amendments.

12.2.1 Denmark

In early October 2008, Danish Parliament agreed with banks to set up a guarantee scheme valid for two years, until the end of September 2010, which guarantees the claims of unsecured creditors, excluding covered bonds and subordinated debt, against losses in the participating banks.

Nordea decided for commercial reasons that Nordea Bank Danmark A/S would participate in the scheme. Nordea guarantees the payment of its portion of DKK 10bn to cover any losses under the guarantee scheme and will pay its portion of an annual guarantee commission of DKK 7.5bn annually for two years. If losses exceed these amounts, additional losses of up to DKK 10bn should also be covered by further guarantee commissions. The total payments for all participating banks are hence capped to DKK 35bn.

The scheme is expected to cost Nordea an annual commission expense of approx. EUR 180-200m, and possible additional expenses for the guarantee of at maximum approx. EUR 500m, which would be reported as loan losses.

In early 2009, Nordea benefitted from the Danish scheme by issuing a EUR 1.5bn senior bond in Denmark at the price of mid-swap +38 basis points.

A second Danish State scheme was launched in January 2009, aiming to ensure sufficient capital in the financial sector. The second scheme contains extended guarantees for banks' debt securities and deposits as well as a scheme for injections of tier 1 capital into participating and eligible banks.

This second scheme is open for participation until the end of June 2009. Nordea is evaluating whether or not to join the second scheme.

12.2.2 Finland

In Finland, a new regulation has been presented, which opens the possibility for the Finnish state to provide and invest in capital instruments and grant state guarantees to the refunding of Finnish banks up to a maximum value of EUR 50bn. A market-based fee will be charged for guarantees. Guarantees are granted until 30 April 2009, and limited to the amounts becoming due up to that date. At a later date, the Government will carry out a separate evaluation of the need to continue granting guarantees.

In February 2009, the Government will submit to Parliament a proposal for state capital investment in deposit-taking banks, in the form of subordinated loans, which can be considered as core capital.

Nordea has to date not joined the Finnish scheme.

12.2.3 Norway

In Norway, stabilising liquidity measures through the Norwegian Central Bank with a facility for banks, where government bonds are swapped for covered bonds have been conducted.

The Norwegian Government has also, in February 2009, announced a new stability plan that aims at providing adequate access to financing from banks to households and corporate at an amount of NOK 100bn. The stabilising liquidity measures have also been extended. During the fourth quarter 2008, Nordea participated in swap facilities under the present Norwegian scheme.

The government will establish a Government Bond Fund of NOK 50bn for the purpose of buying bonds issued by Norwegian corporate in the primary or second hand market. The Government Finance Fund of NOK 50bn can make investments in banks in the shape of hybrid bonds or preference capital, thus aimed improving the capital ratio.

Further details of the conditions will be developed in legislation and regulations to follow, and also in individual agreements with respective banks seeking capital injections under the plan.

During the fourth quarter, Nordea has participated in swap facilities under the present Norwegian scheme.

12.2.4 Sweden

The Swedish government, following the agreements made in the EU, introduced in late October a support system for the banking system with mainly four parts: short-term liquidity supply through activities by the National Debt Office and the Central Bank; a guarantee programme, a system for banks' middle-term funding planned to be running until the end of April 2009; a long-term solvency support system, a Stability fund; and assignment to the financial supervisory authority to examine that the support also benefits household and corporate customers. The amount of the deposit guarantee has also been increased to SEK 500,000.

The Swedish guarantee programme has been amended in late January 2009 and in early February, a capital injection programme for solid banks has been introduced, introducing availability for banks to issue new shares or hybrid loans on market terms to the State, as a participant on ordinary terms in a new shares issue. Changes are also proposed in the fee structure for issues of debt securities under the State guarantee, making fees deductible from the compulsory fee to the Stability fund.

12.3 Exposure classes for Credit risk

A diversified credit portfolio can be divided into the exposure classes defined by the CRD. The basis for calculation of the EAD in the RWA formula is the division of exposure classes. Nordea is approved to use the FIRB approach for the exposure classes: institution, corporate, Retail and other non-credit obligation assets. For the remaining exposure classes Nordea used the Standardised Approach in 2008. Following is a description of what exposures are included in the different exposure classes.

12.3.1 IRB exposure classes

Institutions exposures

Exposures to credit institutions and investment firms are classified as exposures to institutions. In addition, exposures to regional governments, local authorities and multilateral development banks are classified as exposures to institutions if they are not treated as exposures to sovereigns according to regulations issued by the authorities.

Corporate exposures

Exposures that are not assigned to any of the other exposure classes are classified as corporate exposures. The corporate exposure class contains exposures that are rated in accordance to Nordea's internal guidelines.

Retail exposures

Exposures to small and medium sized entities and to private individuals are included in the retail exposure class and defined in accordance to Nordea's internal guidelines for scoring.

Other non-credit obligation assets

Assets that do not require any performance from any counterparty are classified as non credit-obligation assets.

12.3.2 Standardised exposure classes

Central governments and central banks

Exposures to central governments and central banks are, subject to national discretion, treated with low risk if the counterparty is within European Economic Area (EEA) member states. Subject to national discretion, the risk weight of 0% is, for the majority of these exposures, applied in Nordea.

Regional governments and local authorities

Exposures to regional governments and local authorities are included in this exposure class. Exposures to regional governments and local authorities are treated as exposures to the central government in whose jurisdiction they are established, with the exception of Norway, where a risk weight of 20% is applied.

Institution exposures

Exposures to institutions are assigned a risk weight depending on the external rating, by an eligible rating agency, of the central government in the jurisdiction of the institution. In Poland, the risk weight of the exposure is determined according to the external rating of the institution. Specific rules also determine how to treat an exposure where no rating by an eligible rating agency exists. Therefore, the risk weights can differ from 0% to 150% for these exposures.

Corporate exposures

Exposures to corporate rated by eligible rating agency are assigned a risk weight from 20% to 150%. Exposures without external rating are assigned a risk weight of 100%.

Retail exposures

Retail exposures are assigned a risk weight of 75%.

Exposures secured by real estate

Exposures that are secured by mortgages on residential or commercial real estate are included in this exposure class. Exposures secured by mortgages on residential real estate are assigned a risk weight of 35%. The risk weight is only reduced for the part of the exposure that is fully secured. Exposures that are secured by commercial real estate are subject to national discretions and the regulations differ between the Nordic countries.

Other

- Exposures to administrative bodies and non-commercial undertakings (such as public sector entities) are, subject to decision by the local authority, assigned a risk weight of 0% to 100%.
- Exposures to named multilateral development banks are assigned a risk weight of 0%. Other multilateral development banks are assigned a risk weight according to the methods used for exposures to institutions.

- Exposures to named international organisations are assigned a risk weight of 0%. Other international organisations are assigned a risk weight of 100%.
- Past due items (items that are past due for more than 90 days). The unsecured part of any past due item are assigned a risk weight of 150% if value adjustments (allowances) are less than 20% and 100% if value adjustments (allowances) are no less than 20% of the unsecured part. The part of the past due items that are secured by residential real estate property are assigned a risk weight of 100% or 50% depending on the size of the value adjustment (above or below 20%) and national regulations.
- Short-term claims. Exposures reported as short-term claims receive a risk weight based on the short term external rating of the institution. Short-term exposures to institutions and corporate for which a short-term credit assessment by a nominated rating agency is available, are assigned a risk weight in accordance with a six step mapping scale made by the financial supervisory authorities. However, this exposure class is not used for exposures to institutions treated according to the central government risk weighted method.
- Other items
 - 1. Tangible assets, prepayments and accrued income where no counterpart can be determined, holdings of equity etc are assigned a risk weight of 100%.
 - 2. Cash are assigned a 0% risk weight.

List of abbreviations

ALCO	Asset and Liability Committee
CCF	Credit Conversion Factor
CDO	Collateralised Debt Obligation
CEBS	Committee of European Bank Supervisors
CDS	Credit Default Swaps
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CLN	Credit Linked Notes
СМО	Collateralised Mortgage Obligations
CPF	Capital Planning Forum
CRD	EU's Capital Requirements Directive
CRO	Chief Risk Officer
EBF	European Banking Federation
ECC	Executive Credit Committee
EEA	European Economic Area
EAD	Exposure at Default
EC	Economic Capital
EL	Expected Loss
EU	European Union
FFFS	Finansinspektionens Författningssamling (The Swedish FSA's directive)
FIRB	Foundation Internal Rating Based approach
FX	Foreign Exchange
GCC	Group Credit Committee
GEM	Group Executive Management
IAS	International Accounting Standard
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standard
IRB	Internal Rating Based approach
LGD	Loss Given Default
LTV	Loan to value
NLP	Nordea Life and Pensions
OTC	Over The Counter (derivatives)
PD	Probability of Default
RWA	Risk Weighted Amount
S&P	Standard & Poor's
SA	Standardised approach
SRP	Supervisory Review Process
SREP	Supervisory Review and Evaluation Process
SIIR	Structural Interest Income Risk
SME	Small and Medium-sized Enterprises
SPE	Special Purpose Entity
VaR	Value at Risk