Capital and risk management (pillar 3)

Nordea 2009

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1. Introduction

Nordea hereby presents its capital and risk management report 2009, which serves two main purposes:
- To provide a full and comprehensive disclosure of the risks and risk management
- To fulfill the legal disclosure requirements

Capital adequacy and capital management disclosure
Nordea presents its capital position and how the size and composition of the capital base is related to the risks as measured in Risk Weighted Amounts (RWA). The national capital adequacy legislations are based on the European Union's (EU) Capital Requirements Directive (CRD), which in turn is based on the Basel II framework issued by the Basel Committee on Banking Supervision. A general description of the three pillars in the Basel II framework is available in the appendix, section 14.2. This disclosure follows the Swedish Capital adequacy and large exposure act (2006:1371) and the Swedish Financial Supervisory Authority's (Swedish FSA) regulation and general guidelines regarding public disclosure of information concerning capital adequacy and risk management (FFFS 2007:5), which are based on the CRD.

Full and comprehensive risk and risk management disclosure
This report constitutes the comprehensive disclosure on risks, risk management and capital management. In a summarised form, the main disclosure on exposure as well as on risk, liquidity and capital management are also presented in Nordea Group's Annual Report 2009.

With this capital and risk management report, Nordea further increases the transparency on relevant risk factors inherent in the operations, how these are managed and mitigated and the effect on the capital adequacy. 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 report 2009 follows the structure below:
- Highlights of 2009
- Governance of risk and capital management
- Capital position
- Credit risk
- Market risk
- Operational risk
- Securitisation and credit derivatives
- Liquidity risk and structural interest income risk (SIIR)
- Risk and capital in the life operations
- Internal Capital Adequacy Assessment Process (ICAAP)
- Capital base components
- New regulations

The pillar 3 disclosure is made for the Nordea Group and for the subgroups Nordea Bank Danmark Group, Nordea Bank Finland Group and Nordea Bank Norge 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 also 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 has stated the common principles in a policy and instructions for disclosing information on capital adequacy in the Nordea Group.

2. Highlights of 2009

2009 has been another challenging and extreme year in the global financial market. The financial crisis continued from the year before and was during the first half of year deepened by the macroeconomic downturn, globally and in the Nordic countries. Uncertainty and risks have been significant both in the financial markets and about the macroeconomic development.

Nordea has presented a strong result in 2009 despite the financial crisis. Nordea is confident and well prepared for the future due to strong profitability, high quality in the credit portfolio, strong capital base and a diversified funding base.

Strong risk management and stable risk development

Credit risk management has remained in focus. The impairment and net loan losses have continued to stabilise. In 2009, the credit exposure increased, which stem to a large extent from the retail and central government/central banks segments. Loan losses amounted to EUR 1,486m (EUR 466m), giving a loan loss ratio of 54 basis points[1] (19 basis points). The development is in line with the expectations of the slowdown in the economy and Nordea works actively to monitor the development of the portfolio giving special attention to weak performing customers.

Nordea's market risk activities are well diversified and oriented towards liquid Nordic and European markets. The Group's market risk is to a large extent driven by interest rate risk. Exposure to assets of an illiquid nature has been limited.

Also in the funding and liquidity risk area, Nordea maintained its position as one of the strongest names in the funding market. Nordea, supported by its well recognised name and strong rating, has had access to all relevant financial markets and has been able to actively use all its funding programmes. Approximately EUR 27bn was issued in long-term debt during 2009, excluding Danish covered bonds.

Capital management well established – strengthened core capital

In order to remain among the strongest banks in the European peer group, Nordea strengthened its core capital in a rights issue and with a reduced dividend payout in the beginning of 2009. The core tier 1 capital ratio, excluding transition rules, was at the end of 2009 10.3% (8.5%). During 2009, Nordea has performed several internal stress tests in order to evaluate the effects of a worsened economic downturn as well as potential effects for certain identified high risk areas. Also, in 2009, the financial supervisors and central banks have performed several stress tests of the Nordea Group and its peers. The results clearly show that the Nordea Group is well capitalised and Nordea's ability to assess a sufficient capital need. In accordance with the 2009 ICAAP and Supervisory Review and Evaluation Process (SREP), the regulators agreed that Nordea was adequately capitalised given its risk profile and portfolio.

New regulations for capital and liquidity risk

Following the financial crisis, the revision and extension of the regulatory frameworks is characterising the banking industry. There is a strong focus on risk and capital management within the organisation and to meet new regulatory demands. Nordea is well prepared for new capital and liquidity regulations.

1) Excluding a one-off provision of EUR 47m concerning a contested legal claim.

3. Governance of risk 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. The maintaining of risk awareness in the organisation is incorporated in the 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.

3.1 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 described in a separate section.

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 includes information on undertakings that have been consolidated and deducted from the capital base.

3.2 Risk and capital management

3.2.1 Risk and capital 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. The targets are documented in the Group's capital policy. 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. These authorisations vary for different decision-making levels, mainly in terms of size of limits, and are also dependent 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 exposure. 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 risk, liquidity and capital management principles and control.

The CEO in Group Executive Management (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 market risk limits and liquidity risk limits to the risktaking units Group Treasury and Markets. The limits are set in accordance with the business strategies and 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 exposure 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 the required (internal and regulatory) capital and 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 to issue supplementary guidelines and limits, where it is deemed necessary.

Table 1 Specification over group undertakings consolidated/deducted from the Nordea Financial Group, 31 December 2009

	Number of shares	Book value EURm	Voting power of holding	Domicile	Consolidation method
Group undertakings included in the Nordea Financial Group					
Nordea Bank Finland Plc	1,030,800,000	5,951	100%	Helsinki	purchase method
Nordea Finance Finland Ltd			100%	Espoo	purchase method
Nordea Bank Danmark A/S	50,000,000	3,505	100%	Copenhagen	purchase method
Nordea Finans Danmark A/S				Copenhagen	purchase method
Nordea Kredit Realkreditaktieselskab				Copenhagen	purchase method
Fionia Bank A/S			100%	Odense	purchase method
Nordea Bank Norge ASA	551,358,576	2,403	100%	Oslo	purchase method
Nordea Eiendomskreditt AS			100%	Oslo	purchase method
Nordea Finans Norge AS			100%	Oslo	purchase method
Christiania Forsikring AS			100%	Oslo	purchase method
PRIVATmegleren AS			67%	Oslo	purchase method
Nordea Bank Polska S.A.	45,081,403	262	99%	Gdynia	purchase method
OOO Promyshlennaya Companiya Vestcon (Orgresbank)	4,601,942,680	658	100%	Moscow	purchase method
OJSC Nordea Bank			93%	Moscow	purchase method
Nordea Hypotek AB (publ)	100,000	1,898	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	301	100%	Stockholm	purchase method
Other companies		6			purchase method
Total included in the capital base		**16,165**			
Group undertakings deducted from the capital base					
Nordea Life Holding AB, including debts from parent company	1,000	1,177	100%	Stockholm	
Total group undertakings deducted from the capital base		**1,177**			
Over 10 % investments in credit institutions deducted from the capital base					
Eksportfinans ASA		119	23%	Oslo	
Luottokunta		42	24%	Helsinki	
NF Fleet Oy		1	20%	Espoo	
LR Realkredit A/S		12	39%	Copenhagen	
KIFU-AX II A/S		2	28%	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		0	15%	Copenhagen	
Symbion Capital I		1	25%	Copenhagen	
Norges Investor III AS		1	16%	Copenhagen	
Other		3			
Total investments in credit institutions deducted from the capital base		**196**			

CRO and CFO
In figure 1 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 are 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, for the development, validation and monitoring of the rating and scoring systems, for the credit policy and strategy, the credit instructions, the guidelines to the credit instructions as well as the credit decision process and the credit control processes. The CFO is responsible for the capital planning process including capital adequacy reporting, economic capital 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 in its operations, including identification, control and reporting, while Group Credit and Risk Control consolidates and monitors the risks on Group level and on other organisational levels.

Figure 1 Governance of Risk, Liquidity and Capital Management

3.2.2 Monitoring and reporting

The "Policy for Internal Control and Risk Management in the Nordea Group" states that the management of risks includes all activities aiming at identifying, measuring, assessing, monitoring and controlling risks as well as measures to limit and mitigate consequences of the risks. Management of risks is proactive, emphasising training and risk awareness. The Nordea Group maintains a high standard of risk management by means of applying available techniques and methodology to its own needs in a cost-efficient way.

The control environment is based on the principles for segregation of duties and independence. Monitoring and reporting of risk is conducted on a daily basis for market and liquidity risk, on a monthly or 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 receives internal risk reporting which covers 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 Factor (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, equity prices and credit spreads, and less to FX rates and commodity prices.
- 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 economic capital 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:

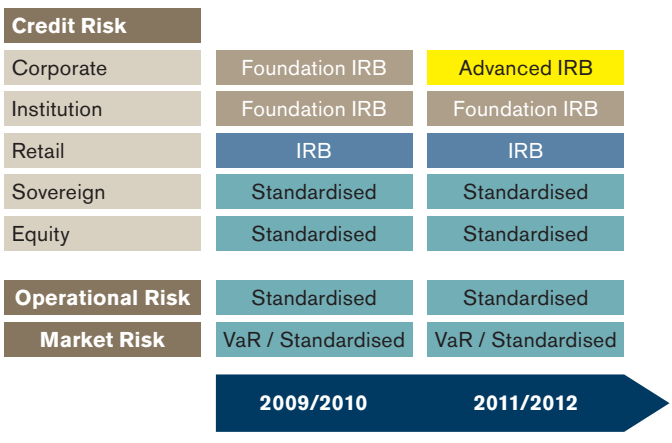
- Liquidity risk is the risk of being able to meet liquidity commitments only at increased cost or, ultimately, being unable to meet obligations as they fall due. The liquidity risk management focuses on both short-term liquidity risk and long-term structural liquidity risk. The liquidity risk management 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 economic capital 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 exposure deriving from the balance sheet (mainly lending to public and deposits from public), from hedging the equity capital of the Group and from Group Treasury's investment and liquidity portfolios. 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 economic capital framework.
- Pension risk is included in market risk economic capital and includes equity, interest rate and FX risk in Nordea sponsored defined pension plans.
- Life insurance risk is the impact from changes in mortality rates, longevity rates and disability rates.
- 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 economic capital framework.

3.3 Roll-out plan

In June 2007, Nordea received approval by the financial supervisory authorities to use the Foundation Internal Rating Based (FIRB) approach for corporate and institution exposure classes in Denmark, Finland, Norway and Sweden. In December 2008 Nordea was approved of using the Internal Rating Based (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. 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 approaches used in the RWA calculations roll-out plan is displayed in figure 2.

Figure 2 Roll-out plan 2010–2012



4. Capital position

In the beginning of 2009, Nordea strengthened its core capital in a rights issue and with a reduced dividend payout, which in total amounted to EUR 3bn. The increased core equity has placed Nordea among the best in terms of capital strength. At the end of 2009, the capital ratios were well above the current regulatory requirements and Nordea's capital policy. Nordea is well prepared for the future, with its high quality in the capital base and sustainable business model. Nordea has demonstrated a prudent and sustainable approach to risk and capital management, which has resulted in a strong capital position among peers.

4.1 Capital management and governance

Nordea strives to attain efficient use of capital 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. Strong capital management supports Nordea's strategic visions and, in addition, provides resistance against unexpected losses that arise as a result of the risks taken within the Group.

The ICAAP, see chapter 11, is put in place to determine internal capital requirement that reflects the risks of Nordea and to assess the adequacy of Nordea's capital. The internal capital requirement combines regulatory capital and capital calculated by internal models in a so called "pillar 1 plus pillar 2" approach, where the pillar 1 capital requirement forms the base. The capital policy is designed with consideration given to the internal capital requirements.

Nordea's risk and capital governance structure is built on strict definition of roles and responsibilities originating from the Board of Directors, GEM and in particular the roles of the CFO and CRO.

The Board of Directors decides ultimately on the targets for capital ratios and the capital policy. The CEO in GEM decides on the overall framework of capital management.

Nordea's ability to meet targets and to maintain minimum capital requirements is followed at least quarterly by Group Risk Modelling in Group Corporate Centre and is reported to the Board of Directors, ALCO and CPF. The CPF, headed by the CFO is the forum responsible for coordinating capital planning activities within the Group, including regulatory and internal capital as well as the capital base. Additionally, the CPF reviews the future capital requirements in the assessment of annual dividends, share re-purchases, 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 not only the capital situation in the Nordea Group but also 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.

4.2 Financial conglomerate

The capital requirements valid for financial conglomerates are stated in Swedish Law (Act 2006:531). The Swedish FSA has defined Nordea as a financial conglomerate. This means that the capital position from the banking sector and the insurance sector is assessed. Institutions and insurance companies, which are defined as conglomerates, are required to hold a capital base that at all times are equal or above the aggregated capital requirements.

The capital base per 31 December 2009 for the financial conglomerate was EUR 24.5bn (EUR 21.5bn) while the aggregated capital requirement were EUR 16.5bn (EUR 18.1bn), resulting in excess capital of EUR 8.0bn (EUR 3.4bn).

4.3 Regulatory capital requirement

In table 2, an overview of the capital requirements and the RWA as of December 2009 divided on the different risk types is presented in comparison with previous year. The credit risk comprises approximate 90% of the risk, while operational risk accounts for 8% of the capital requirements and market risk comprises 3% of the capital requirements.

The table also includes information about the approach used for calculation of the capital requirements. Out of the total capital requirements for credit risk, 79% of the exposure has been calculated with the IRB approach and 21% with the standardised approach.

The RWA for credit risk, market risk and operational risk are adjusted with EUR 20.1bn due to the transition rules. In 2009, the capital requirements could not be lower than 80% of the capital requirements calculated under Basel I regulations. The transition rules have been prolonged, at least for 2010 and 2011, and the capital requirement is not allowed to be below 80% of the capital requirement calculated under Basel I regulations.

The RWA excluding transition rules increased slightly with 1.9% during the year to EUR 171.7bn while the RWA including transition rules decreased with 10% due to changes in the regulatory floor level from 90% to 80%. The increase in RWA excluding transition rules is due to changes in credit quality and stronger Swedish/Norwegian krona counteracted by decreased exposure and high attention to improve processes and data sourcing. In figure 3 the different drivers behind the development of RWA are disclosed.

4.4 Capital ratios

The controlled growth in RWA has been supported by the growth in the capital base which has lead to improved capital ratios during the year. The main contribution in the capital base was the rights offering of EUR 2.5bn and the reduced 2008 dividend to strengthen core capital position, which in total summarised to EUR 3bn.

The transition rules create a need to manage the bank using a variety of capital measurements and capital ratios. Table 3 shows that the regulatory transition rules comprise

Table 2 Capital requirements and RWA

	2009		2008	
EURm	Capital requirement	RWA	Capital requirement	RWA
Credit risk	**12,250**	**153,123**	**12,060**	**150,746**
IRB	9,655	120,692	9,537	119,207
– of which corporate	7,060	88,249	6,909	86,358
– of which institution	821	10,263	1,016	12,699
– of which retail	1,673	20,912	1,465	18,313
– of which other	101	1,269	147	1,837
Standardised	2 595	32 431	2 523	31 539
- of which sovereign	70	871	75	940
- of which retail	711	8 887	630	7 875
- of which other	1 814	22 673	1 818	22 724
Market risk	**431**	**5,386**	**474**	**5,930**
– of which trading book, VaR	107	1,335	137	1,715
– of which trading book, non-VaR	267	3,342	270	3,372
– of which FX, non-VaR	57	710	67	843
– of which commodity risk				
Operational risk	**1,057**	**13,215**	**952**	**11,896**
Standardised	1,057	13,215	952	11,896
Sub total (excluding transition rules)	**13,738**	**171,724**	**13,486**	**168,572**
Adjustment for transition rules				
Additional capital requirement according to transition rules	1,611	20,134	3,577	44,709
Total (including transition rules)	**15,348**	**191,858**	**17,062**	**213,281**

a floor on Nordea's capital requirement when compared to Basel II (pillar 1) minimum requirements.

The rights issue increased the capital ratios with approximately 150bps. At the end of 2009, the core tier 1 excluding transition rules ended at 10.3% (8.5%) while corresponding tier 1 ratio was 11.4% (9.3%) and the capital ratio excluding transition rules was 13.4% (12.1%). The tier 1 ratio including transition rules was 10.2% (7.4%) and the capital ratio including transition rules was 11.9% (9.5%).

The development of different capital ratios per quarter are disclosed in table 3. In the figure 4 the development of the core tier 1 ratios and tier 1 ratios are illustrated.

There are many different drivers of the ratios, while the main RWA drivers mentioned are credit quality, FX changes and growth. The highest impact on the capital base has been the rights issue, the profit generation and buy back of subordinated debt. The impact in terms of basis points is disclosed in figure 5. The mismatch between the currency distribution of credit risk RWA and the currency composition of the tier 1 capital implies that capital ratios are affected by changes in the FX rates.

As can be seen in table 4 the capital ratios are well above the targets set in the capital policy. The purpose of the capital policy is to maintain capital at levels that are adequate from the perspective of regulators, funding and rating agencies and to optimise shareholder value in light of the external requirements. The capital policy stipulates the minimum and target levels for certain defined ratios; capital ratio and tier 1 ratio. Once regulatory definitions of capital quality are finalised, Nordea will review the impact on existing capital policy.

The Nordea Group needs to keep sufficient available capital to cover all risks taken (required capital) over a foreseeable future. The capital position is managed through the ICAAP.

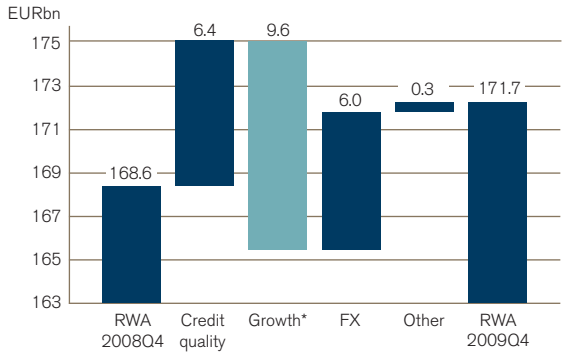
Table 3 Key capital adequacy figures

EURbn	Q4 2009	Q3 2009	Q2 2009	Q1 2009	Q4 2008
RWA including transition rules	191.9	191.7	192.2	188.1	213.3
RWA Basel II (pillar 1) excluding transition rules	171.7	168.6	170.4	171.0	168.6
Regulatory capital requirement including transition rules	15.3	15.3	15.4	15.0	17.1
Capital base	22.9	23.7	22.5	19.4	20.3
Tier 1 capital	19.6	20.2	19.0	16.1	15.8
Core tier 1 capital	17.8	18.0	17.6	14.6	14.3
Tier 1 ratio including transition rules (%)	10.2%	10.5%	9.9%	8.5%	7.4%
Tier 1 ratio excluding transition rules (%)	11.4%	12.0%	11.2%	9.4%	9.3%
Core tier 1 ratio including transition rules (%)	9.3%	9.4%	9.2%	7.8%	6.7%
Core tier 1 ratio excluding transition rules (%)	10.3%	10.7%	10.3%	8.5%	8.5%
Capital ratio including transition rules (%)	11.9%	12.4%	11.7%	10.3%	9.5%
Capital ratio excluding transition rules (%)	13.4%	14.1%	13.2%	11.4%	12.1%
Capital adequacy quotient (Capital base /Regulatory capital requirement excluding transition rules)	1.7	1.8	1.7	1.4	1.5
Capital adequacy quotient (Capital base /Regulatory capital requirement including transition rules)	1.5	1.5	1.5	1.3	1.2

Table 4 Actual vs Target (excl. transition rules)

%	31 December 2009	Policy (Target)
Tier 1 ratio	11.4	9.0
Total capital ratio	13.4	11.5

Figure 3 Drivers behind the development of RWA excluding transition rules



* Including activities related to improved processes and data sourcing

Figure 4 Capital adequacy ratios

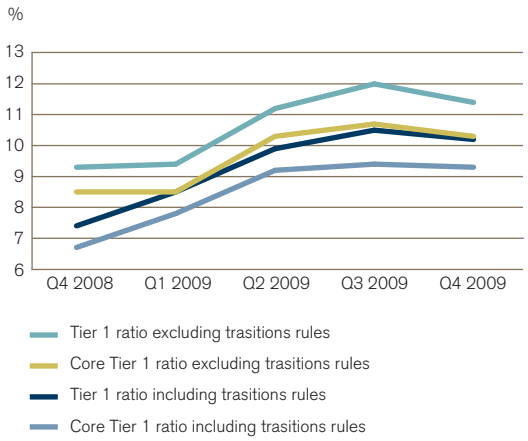
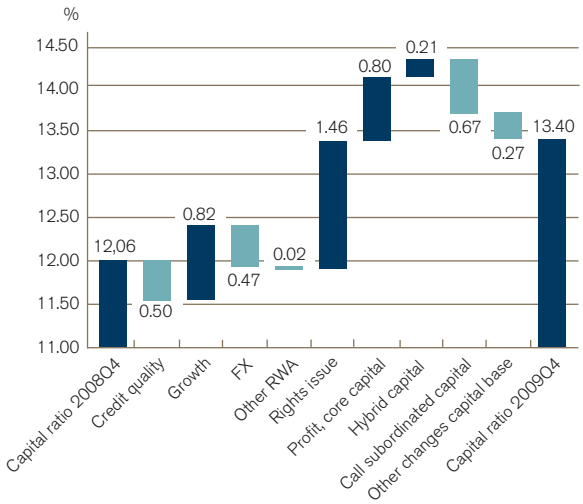


Figure 5 Development of capital ratio (excluding transition rules)



5. Credit risk

Credit risk is the largest risk comprising approximately 90% of the total RWA, of which household mortgage loans and corporate loans are the key components. Nordea has a well diversified credit portfolio, both from an industry and geographical perspective. Total exposure increased by 5% during 2009 mainly due to an increase to retail and central governments/central banks, which have a relatively low risk weight. The credit risk RWA increased with 2% and the average risk weight of the total portfolio has decreased to 38% (39%). The loan loss ratio is in line with the outlook and was 54 basis points in 2009. Credit quality stabilised during the autumn of 2009, supported by the economic recovery in Nordea's home markets. Nordea works actively to monitor the development of the portfolio giving special attention to poorly performing customers.

5.1 Identification of credit risk

5.1.1 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 authority granted by the Board of Directors, credit risk limits are approved by decision-making authorities on different levels in the organisation (see figure 6). 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.

5.1.2 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 stems mainly from various forms of lending, and 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 5.2.7 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. See section 5.4.3 for further information about transfer risk.

Concentration risk in specific industries is followed by industry monitoring groups and managed through specific industry credit policies which are established for industries where at least two of the following criteria are fulfilled:

- Significant weight in the Nordea portfolio
- High cyclicality and/or volatility of the industry
- Special skills and knowledge required

There is usually a cap set for the Group's total exposure in such an industry. All industry credit policies are approved by the Executive Credit Committees and confirmed annually by the Board Credit Committee.

Corporate customers' environmental risks are taken into account in the overall risk assessment through the so-called Environmental Risk Assessment Tool (ERAT). Social and political risks are taken into account by the so-called Social and Political Risk Assessment Tool (SPRAT). SPRAT is used as part of the corporate lending process, in parallel to the ERAT. 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.

5.1.3 Decisions and monitoring of credit risk

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 continuously assesses customers' ability to fulfil their obligations and identifies 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 about the customer and macroeconomic factors. Information such as late payments data, behavioural scoring and rating migration are important parameters in the internal monitoring process. If new information indicates the need, the customer responsible unit must reassess the rating and assess whether 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 remedied, the customer must be tested for impairment.

In case 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. Nordea has a project organisation for handling work-out corporate customers. Individual deal-teams including relevant specialists are established for larger work-out cases. Credit organisation and other specialist units support customer responsible units in handling smaller work out customers. The follow-up of individual work-out cases is part of the quarterly risk review process. In this process the impairment of individual customers and customer groups is assessed and the actions related to handling of work-out customers are reviewed and followed up.

5.1.4 Credit risk appetite

Nordea has defined its credit risk appetite as an expected loan loss level of 25 basis points over the cycle. Net loan losses over the past years show an average not exceeding this level.

5.1.5 Credit risk mitigation and collateral policy

All credit risk mitigations are an inherent part of the credit decision process. In every credit decision and review the valuation of collateral is considered as well as the adequacy of covenants and other risk mitigations.

Pledging of collateral is the main credit risk mitigation technique. In corporate exposure, the main collateral types are real estate mortgages, floating charges and leasing objects. Collateral coverage is higher for exposure to financially weaker customers than for those which are financially strong.

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.

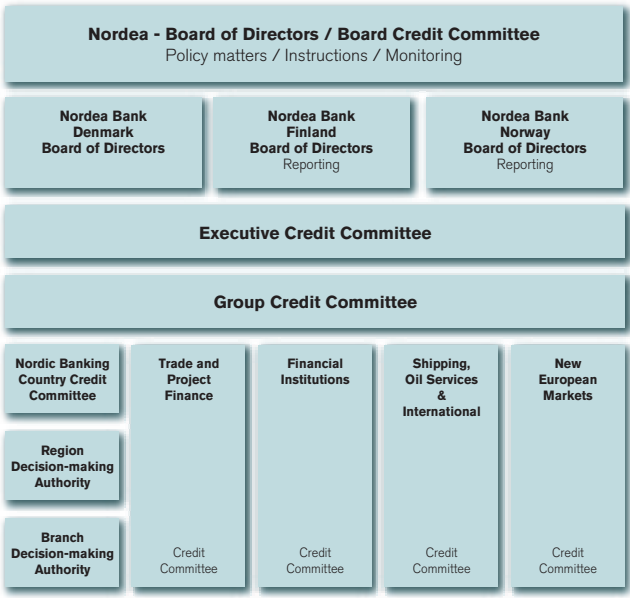
The following collateral types are most common in Nordea:

- Residential real estate, commercial real estate and land situated in Nordea's home markets.
- Other tangible 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 eligibility criteria.

Regarding large exposure, syndication of loans is the primary tool for managing concentration risk while credit risk mitigation by the use of credit default swaps has been done to a limited extent.

Figure 6 Credit decision-making structure



Covenants in credit agreements do not substitute collateral but may be of great help as a complement to both secured and unsecured exposure. All exposure of substantial size and complexity includes appropriate covenants. Financial covenants are designed to react on early warning signs and are followed up carefully.

5.1.6 Definition and methodology of impairment

Weak and impaired exposure is 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 being the difference between the book value and the discounted value of the future cash flow, including the value of pledged collateral. Impaired exposure can be either performing or non-performing. Impaired exposure is treated as in default when determining default probability. Exposure that is past due more than 90 days is automatically regarded as in default, and reported as non-performing and impaired or not impaired depending on the deemed loss potential. In addition to individual impairment testing of all individually significant customers, collective impairment testing is performed for groups of customers not identified individually to be impaired. Collective impairment is based on the migration of rated and scored customers in the credit portfolio. The assessment of collective impairment reacts to up and down-ratings of customers as well as new customers and customers leaving the portfolio. Also customers going to and from default effect the calculation. Collective impairment is assessed quarterly for each legal unit.

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 portfolio, including ensuring that all incurred losses are covered by adequate allowances.

5.1.7 Link between credit risk exposure and balance sheet in annual report

Credit risk can be measured, monitored and segmented in different ways. The loan portfolio is the major part of the credit portfolio and the basis for impaired loans and loan losses. This section discloses the link between the loan portfolio as defined in accordance with accounting standards and exposure as defined in accordance with the CRD.

The main differences are outlined in this section to illustrate the link between the different reporting methods. A detailed definition of exposure classes used in the capital adequacy calculations can be found in appendix 14.3.

In this report, tables containing exposure are presented as Exposure At Default (EAD) for IRB exposure and Exposure value for standardised exposure if nothing else is stated. It is based on the exposure amount on which the RWA is calculated. This amount differs from the original exposure, which is the exposure before taking into account substitution effects stemming from credit risk mitigation and credit conversion factors for off-balance exposure.

Credit risk exposure presented in this report, in accordance with the CRD, is distributed by exposure class, where each exposure class is divided 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)
- Derivatives

Items presented in the annual report, in accordance to the accounting standards, are divided into the following types:

- On-balance-sheet items (loans to credit institutions and loans to the public, including reversed repurchase agreements)
- Off-balance-sheet items (e.g. guarantees and unutilised amounts of credit facilities)
- Derivatives (positive fair value)
- Treasury bills and interest-bearing securities

Table 5 shows the link between the CRD credit risk exposure and items presented in the annual report.

5.1.7.1 On-balance items

As can be seen in table 5, the following items have been excluded from the balance sheet, when calculating on-balance exposure in accordance with CRD:

- Market-risk-related items in the trading book, such as certain interest-bearing securities and treasury bills
- Repos, derivatives and securities lending. These transactions are either included in the calculation of market risk in the trading book or reported as separate exposure types (Derivatives or Securities financing)
- Life insurance assets, due to solvency regulation
- Other, mainly intangible assets and deferred tax. These items are adjusted for when calculating the capital base

5.1.7.2 Off-balance items

The following items are excluded from the off-balance sheet, in accordance with accounting rules, when calculating the off-balance exposure in accordance with CRD:

- Life insurance exposure, due to solvency regulation
- Assets pledged as security for own liabilities and other assets pledged (as long as it is not leasing). These transactions are reported as a separate exposure type, Securities financing.
- Derivatives and other commitments. These transactions are reported as a separate exposure type, Derivatives.

5.1.7.3 Securities financing and derivatives

It should be noted that derivatives are both included on-balance (i.e. positive fair value without netting) and off-balance (i.e. nominal amounts) in accordance to accounting standards. The calculation method used in the CRD is based on the sum of current exposure and potential future exposure. Also, repurchase agreements and securities lending/borrowing transactions are in the balance sheet calculated based upon nominal value. The exposure in the CRD calculations is determined net of the collateral value.

5.2 Capital requirement for credit risk

5.2.1 Development of exposure and RWA

The information in this chapter aims to give an overview as well as an in-depth description of the distribution of the credit risk portfolio. For more detailed information of the principles for RWA calculations, under the IRB and standardised approaches, see appendix 14.4.

In table 6, the original exposure, the exposure, the average risk weight expressed as percentages, RWA and capital requirement, are distributed by exposure class. The IRB exposure classes contain the portfolios for which Nordea has been approved.

The retail portfolio is divided in three sub-segments; mortgage (credit risk exposure to private individuals, pledged by real estate), other retail (exposure to private individuals, except mortgage) and SME (exposure to small and medium-sized enterprises, including loans secured by real estate collateral).

For the remaining portfolios the standardised approach exposure classes are used. The exposure in Poland, Russia, Luxembourg and foreign branches (e.g. Baltic countries, New York, London), as well as the finance companies in the Nordic countries, are calculated according to the standardised approach. Furthermore acquisitions of new portfolios are treated according to the standardised approach until approval has been given to include them by the financial supervisory authorities.

Some exposure classes have been merged in the table, due to low exposure in these exposure classes.

The total exposure has increased 5% and the composition has changed during 2009. The IRB institution portfolio decreased by 8% and comprised 11% (13%) of the total exposure at year end. The IRB corporate portfolio decreased mainly due to reduced counterparty credit risk exposure and comprised 36% (39%) of the total exposure at year end. The IRB retail portfolio increased and comprised in 32% (30%) of the total exposure at year end, which mainly stems from retail mortgages. The remaining exposure in IRB and standardised comprises 21% (18%) of the total exposure. The exposure to central government and central banks increased and composed at year end 9% of the total exposure (5%).

The total credit risk RWA has only increased by 2%, due to the change of exposure composition towards segments with lower risk weights. Retail exposure with an average risk weight of 16% has increased, while the corporate exposure with an average risk weight of 61% has decreased. In total the average risk weight under the IRB approach has remained unchanged.

The average risk weight was reduced from 47% to 39% in 2009 for the standardised exposure classes. This is mainly due to the increase in the exposure towards central governments and central banks, where the majority of the exposure has 0% risk weight. Also, corporate exposure has decreased slightly whereas retail exposure has increased under the standardised approach.

Table 5 Specification of on-balance and off-balance items for Nordea Group, 31 December 2009

EURm On-balance	Balance sheet (accounting)	Items related to market risk	Repos, derivatives, securities lending	Life insurance operations	Other	Original exposure	Credit Conversion Factor %	Exposure[1]
On-balance items								
Cash and balances with central banks	11,500			–89		11,411	100%	11,411
Treasury bills, other interest-bearing securities and pledged instruments	80,339	–25,903		–23,014		31,422	100%	31,422
Loans to credit institutions [2]	18,555		–6,142		13	12,426	100%	12,426
Loans to the public [3]	282,411		–18,418	–310	–173	263,510	100%	262,584
Derivatives	75,422		–75,402	–20		0		0
Intangible assets	2,947			–336	–2,611	0		0
Other assets and prepaid expenses	36,370	–12,929	–3	–13,984	–1,085	8,369	100%	8,369
Total	**507,544**	**–38,832**	**–99,965**	**–37,753**	**–3,856**	**327,138**		**326,212**

Off-balance	Balance sheet (accounting)	Life insurance operations	Excluded in CRD	Included in CRD
Off-balance items in balance sheet				
Assets pledged as security for own liabilities	121,052	4,438	116,614	
Other assets pledged	6,635	1	6,634	
Contingent liabilities	22,267	205		22,062
Commitments	79,797	890		78,907
Total	**229,751**	**5,534**	**123,248**	**100,969**

	Included in CRD OffBal (from balance sheet)	Not balance sheet, incl in CRD [4]	Original exposure	Credit Conversion Factor %	Exposure
Off-balance items in CRD					
Credit facilities	41,634	32,381	74,015	33%	24,354
Checking accounts	23,498		23,498	22%	5,083
Loan commitments	13,655	1,415	15,070	44%	6,686
Guarantees	19,871		19,871	67%	13,347
Other (leasing and documentary credits)	2,311		2,311	41%	952
Total	**100,969**	**33,796**	**134,765**		**50,422**

Derivatives and Securities Financing	Original exposure	Credit Conversion Factor %	Exposure
Derivatives	28,792	100%	28,792
Securities Financing Transactions & Long Settlement Transactions	519	100%	519
Total credit risk (CRD definition)	**491,214**		**405,945**

1) The on-balance exposures have a CCF of 100% but can still have lower EAD due to provisions in the standardised approach, financial collateral in the standardised approach and residual value for leasing in the IRB approach, that are deducted from the original exposure when calculating EAD.

2) Corresponding figure before allowances EUR 18,593m

3) Corresponding figure before allowances EUR 284,529m

4) There are also off-balance exposures that are included under the capital adequacy regulation but not included in the annual report. Such exposure relates to undrawn credit facilities which are unconditionally cancellable.

Table 6 Capital requirement for credit risk, 31 December 2009

EURm	Original exposure	Exposure	Average risk weight	RWA	Capital requirement
IRB exposure classes					
Institution	50,345	45,416	23%	10,263	821
Corporate	207,214	145,376	61%	88,249	7,060
Retail	135,231	130,751	16%	20,912	1,673
– of which mortgage	100,704	100,144	11%	10,661	853
– of which other retail	30,497	27,007	33%	8,860	709
– of which SME	4,030	3,600	39%	1,391	111
Other non-credit obligation assets	1,712	1,269	100%	1,269	102
Total IRB approach	**394,501**	**322,813**	**37%**	**120,692**	**9,655**
Standardised exposure classes					
Central government and central banks	32,148	35,236	2%	786	63
Regional governments and local authorities	9,703	7,625	1%	85	7
Institution	4,452	4,159	24%	1,014	81
Corporate	28,196	19,646	98%	19,266	1,541
Retail	16,419	11,025	75%	8,269	661
Exposures secured by real estates	1,162	1,114	56%	618	49
Other[1]	4,633	4,328	55%	2,393	191
Total standardised approach	**96,713**	**83,133**	**39%**	**32,431**	**2,595**
Total	**491,214**	**405,945**	**38%**	**153,123**	**12,250**

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 in exposure.

Capital requirement for credit risk, 31 December 2008

EURm	Original exposure	Exposure	Average risk weight	RWA	Capital requirement
IRB exposure classes					
Institution	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. Associated companies not included in exposure.

5.2.1.1 FX effect on exposure and RWA

In the four Nordic countries the impact of changes in the exchange rates relates mainly to SEK and NOK since Nordea reports in EUR. During 2009 changes in SEK/EUR and NOK/EUR, especially in the first three quarters, have increased the exposure by EUR 14.2bn which has had an impact on RWA by EUR 6.0bn.

5.2.2 Exposure type by exposure class

In table 7, the exposure is split by exposure classes and exposure types.

As of 31 December 2009, the IRB approach is applicable for 79% (83%) of the total credit risk exposure. The main part of the exposure is within the IRB corporate and IRB retail portfolio.

During 2009, the counterparty credit risk in derivatives decreased, mainly in the corporate exposure class. The remaining exposure types are largely stable.

The average exposure in 2009 is presented in table 8.

5.2.3 Exposure by geography

In table 9, exposure is split by geographical areas, based on where the credit risk is referable. The home markets for Nordea are the Nordic countries and the New European Markets (Baltic countries, Poland and Russia).

Nordea is geographically well diversified as no market account for more than 30% of the exposure. The IRB retail exposure has shown a stable growth in all Nordic countries during 2009.

The exposure in Finland represents 27% of the total exposure in the Group while Denmark 24%, Sweden 25% and Norway 17%. The main reason for the large relative share in Finland relates to derivative exposure in Markets and Trade Finance being centralised to Finland.

In the Nordic countries, the exposure increased except in Finland. The IRB corporate exposure in Finland has decreased by 20% mainly due to the reduction in counterparty credit risk. Overall, the exposure to institutions fluctuated much during the year mainly due to interbank market activities with short maturity.

The total exposure in New European Markets was stable during the year, but the exposure has increased in Poland and decreased in the Baltic countries and Russia.

Table 7 Exposure classes split by exposure type, 31 December 2009

EURm	On-balance sheet items	Off-balance sheet items	Securities financing	Derivatives	Total
IRB exposure classes					
Institution	22,663	2,298	141	20,314	45,416
Corporate	106,516	32,335	49	6,476	145,376
Retail	119,477	11,227	0	47	130,751
– of which mortgage	97,406	2,738			100,144
– of which other retail	19,266	7,716		24	27,007
– of which SME	2,805	772	0	23	3,600
Other non-credit obligation assets	1,269				1,269
Total IRB approach	**249,925**	**45,860**	**190**	**26,838**	**322,813**
Standardised exposure classes					
Central governments and central banks	33,377	496	310	1,054	35,236
Regional governments and local authorities	6,674	419		532	7,625
Institution	3,676	189	14	281	4,159
Corporate	16,414	3,170	4	57	19,646
Retail	10,771	252	1	1	11,025
Exposures secured by real estates	1,095	19			1,114
Other[1]	4,280	17		30	4,328
Total standardised approach	**76,287**	**4,562**	**329**	**1,954**	**83,133**
Total exposure	**326,213**	**50,422**	**519**	**28,792**	**405,945**

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 in exposure.

Exposure classes split by exposure type, 31 December 2008

EURm	On-balance sheet items	Off-balance sheet items	Securities financing	Derivatives	Total
IRB exposure classes					
Institution	26,208	2,211	147	20,577	49,143
Corporate	107,690	31,873	54	12,398	152,015
Retail	105,994	9,960	0	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	0	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		0	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 exposure	**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.Associated companies not included in exposure.

Table 8 Exposure classes split by exposure type, average[1] exposure during 2009

Average exposure

EURm	On-balance sheet items	Off-balance sheet items	Securities financing	Derivatives	Total
IRB exposure classes					
Institution	23,309	2,210	166	19,340	45,024
Corporate	108,445	31,765	142	7,583	147,935
Retail	114,325	10,564	0	67	124,957
– of which mortgage	93,065	2,160			95,225
– of which other retail	18,410	7,599		44	26,052
– of which SME	2,851	805	0	24	3,680
Other non-credit obligation assets	1,224				1,224
Total IRB approach	**247,303**	**44,540**	**307**	**26,990**	**319,140**
Standardised exposure classes					
Central governments and central banks	22,533	477	330	789	24,129
Regional governments and local authorities	6,541	369		532	7,441
Institution	3,938	170	3	588	4,699
Corporate	17,643	3,207	1	73	20,925
Retail	9,800	268	0	0	10,068
Exposures secured by real estates	1,102	22			1,124
Other[2]	3,328	9		20	3,357
Total standardised approach	**64,884**	**4,522**	**335**	**2,003**	**71,743**
Total exposure	**312,187**	**49,062**	**642**	**28,993**	**390,884**

1) Quarterly average
2) Administrative bodies and non-commercial undertakings, multilateral developments banks, past due items, short-term claims, covered bonds, and other items. Associated companies not included in exposure.

Table 9 Exposure split by geography and exposure classes, 31 December 2009

EURm	Nordic countries	of which Denmark	of which Finland	of which Norway	of which Sweden	Baltic countries	Poland	Russia	Other	Total
IRB exposure classes										
Institution	45,416	4,526	24,571	3,286	13,033					45,416
Corporate	145,376	38,473	35,492	33,591	37,821					145,376
Retail	130,751	44,714	29,702	23,654	32,681					130,751
– of which mortgage	100,144	33,012	22,118	17,963	27,052					100,144
– of which other retail	27,007	10,883	6,670	5,296	4,157					27,007
– of which SME	3,600	819	914	395	1,472					3,600
Other non-credit obligation assets	1,269	279	254	162	574					1,269
Total IRB approach	**322,813**	**87,991**	**90,019**	**60,693**	**84,109**					**322,813**
Standardised exposure classes										
Central governments and central banks	31,662	5,658	12,217	5,015	8,772	968	872	123	1,610	35,236
Regional governments and local authorities	7,009	902	1,498	255	4,354	97			519	7,625
Institution	1,022	540	441	2	38	276	289	289	2,283	4,159
Corporate	1,208	211	783	51	163	4,104	1,562	3,228	9,544	19,646
Retail	5,863	984	3,051	834	995	2,621	2,157	215	169	11,025
Exposures secured by real estates	581	171	410		0		183		350	1,114
Other[1]	3,478	1,201	280	277	1,719	277	93	142	336	4,328
Total standardised approach	**50,823**	**9,668**	**18,679**	**6,435**	**16,040**	**8,343**	**5,157**	**3,997**	**14,813**	**83,133**
Total exposure	**373,635**	**97,659**	**108,699**	**67,128**	**100,150**	**8,343**	**5,157**	**3,997**	**14,813**	**405,945**

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 in exposure.

Exposure split by geography and exposure classes, 31 December 2008

EURm	Nordic countries	of which Denmark	of which Finland	of which Norway	of which Sweden	Baltic countries	Poland	Russia	Other	Total
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
– of which mortgage	86,236	28,934	20,713	14,220	22,370					86,236
– of which other retail	25,649	11,805	6,155	4,213	3,476					25,649
– of which SME	4,160	844	1,458	434	1,425					4,160
Other non-credit obligation assets	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					144		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 exposure	**354,293**	**94,683**	**112,249**	**58,194**	**89,167**	**9,509**	**3,484**	**4,487**	**13,744**	**385,517**

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 in exposure.

5.2.4 Exposure and RWA distributed per legal entity

Figure 7 shows the exposure and RWA distributed by legal entity. Intra-group exposure within the Nordea Group has been excluded.

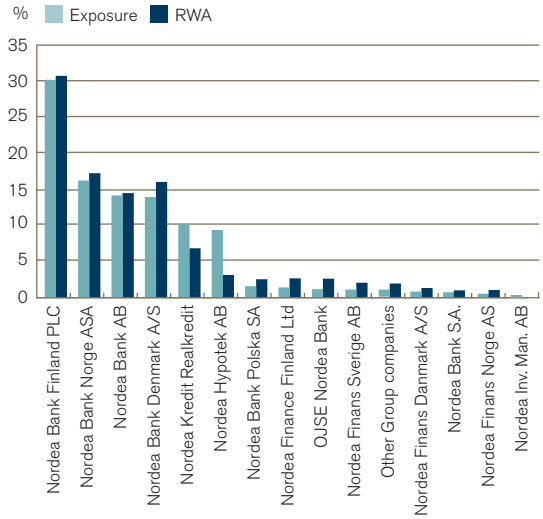
A substantial part of the exposure and RWA relates to Nordea Bank Finland Plc. This is attributable to that the Baltic countries and a majority of other branches are being included, as well as derivative transactions in Markets and off-balance exposure that are mainly booked in Nordea Bank Finland Plc.

The mortgage companies Nordea Kredit Realkreditaktieselskab A/S and Nordea Hypotek AB have a lower portion of RWA compared to exposure resulting from a major part of exposure being secured by real estate collateral.

The four main banks in the Nordic countries (excluding the Baltic countries) comprise some 70% of the total credit risk exposure and RWA. Poland and Russia together comprise 2% of the credit risk exposure and 5% of RWA. The Baltic countries, included in Nordea Bank Finland Plc, comprise 2% of exposure and 5% of RWA.

During 2009 Nordea signed share purchase agreements concerning the acquisitions of for example Fionia Bank.

Figure 7 Exposure and RWA distribution per legal entity



5.2.5 Exposure by industry

In table 10 the total exposure is split by industries and by the main exposure classes. The industry breakdown follows the Global Industries Classification Standard (GICS) and is based on NACE codes (i.e. statistical classification of economic activities in the European community).

The IRB corporate portfolio is well diversified between industries. The real estate sector in this portfolio is the largest sector, and is the only sector that accounts for more than 5% of the total exposure of EUR 406bn. During the year, the largest increases are within the real estate sector and the consumer durables sector.

Table 11 shows the exposure in the IRB corporate portfolio distributed both by industry and geography. This illustrates Nordea's good diversification of the corporate portfolio and cross-border business model.

Table 10 Exposure split by industry sector, 31 December 2009

	Internal rating based approach				Standardised approach			
EURm	Institution	Corporate	Retail	Other non-credit obligation assets	Central governments and central banks	Regional government and local authorities	Other[1]	Total
Retail mortgage			100,144				1,114	101,259
Other retail			27,007				11,025	38,031
Central and local governments					17,837	7,625		25,462
Banks	28,496				17,399		1,844	47,739
Industry sector								
– Construction and engineering		4,252	444				434	5,130
– Consumer durables (cars, appliances etc)		5,594	55				427	6,076
– Consumer staples (food, agriculture etc)		11,560	240				840	12,639
– Energy (oil, gas etc)		3,102	1				579	3,683
– Health care and pharmaceuticals		2,087	132				297	2,516
– Industrial capital goods		4,387	24				179	4,590
– Industrial commercial services		15,204	650				311	16,165
– IT software, hardware and services		1,408	86				278	1,772
– Media and leisure		2,561	291				244	3,096
– Metals and mining materials		888	7				72	967
– Paper and forest materials		3,444	33				80	3,558
– Real estate management and investment		34,461	472				1,445	36,378
– Retail trade		10,552	632				758	11,942
– Shipping and offshore		8,053	6				3,434	11,493
– Telecommunication equipment		374	1				36	412
– Telecommunication operators		2,583	3				158	2,744
– Transportation		3,383	164				463	4,010
– Utilities (distribution and production)		5,792	15				617	6,424
– Other financial institutions	16,920	10,140	53				335	27,448
– Other materials (chemical, building materials etc)		6,882	107				539	7,528
– Other		8,669	184	1,269			14,762	24,884
Total exposure	**45,416**	**145,376**	**130,751**	**1,269**	**35,236**	**7,625**	**40,271**	**405,945**

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, standardised institution, standardised corporate, past due items, short term claims, covered bonds and other items. Associated companies not included in exposure.

Exposure split by industry sector, 31 December 2008

	Internal rating based approach				Standardised approach			
EURm	Institution	Corporate	Retail	Other non-credit obligation assets	Central governments and central banks	Regional government and local authorities	Other[1]	Total
Retail mortgage			86,236				558	86,794
Other retail			25,649				9,739	35,388
Central and local governments					5,944	7,425		13,369
Banks	27,362		1		15,015		51	42,429
Industry sector								
– Construction and engineering		3,307	428				536	4,271
– Consumer durables (cars, appliances etc)		3,610	64				555	4,229
– Consumer staples (food, agriculture etc)		12,697	252				814	13,763
– Energy (oil, gas etc)		3,303	1				572	3,876
– Health care and pharmaceuticals		1,731	123				321	2,176
– Industrial capital goods		5,916	40				339	6,295
– Industrial commercial services		19,442	686				452	20,580
– IT software, hardware and services		1,268	75				172	1,515
– Media and leisure		2,603	282				214	3,099
– Metals and mining materials		694	7				53	754
– Paper and forest materials		3,136	34				362	3,532
– Real estate management and investment		31,948	893				1,633	34,474
– Retail trade		9,308	587				1,291	11,186
– Shipping and offshore		9,258	6				3,675	12,939
– Telecommunication equipment		803	3				68	874
– Telecommunication operators		2,778	4				61	2,843
– Transportation		3,014	184				654	3,853
– Utilities (distribution and production)		6,998	15				467	7,479
– Other financial institutions	21,782	10,381	27				726	32,915
– Other materials (chemical, building materials etc)		5,399	104				1,268	6,771
– Other		14,420	344	1,838			13,514	30,116
Total exposure	**49,143**	**152,015**	**116,045**	**1,838**	**20,959**	**7,425**	**38,093**	**385,518**

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, standardised institution, standardised corporate, past due items, short term claims, covered bonds and other items. Associated companies not included in exposure.

Table 11 IRB corporate exposure split by industry and geography, 31 December 2009

EURm	Denmark	Finland	Norway	Sweden	Total
Construction and engineering	606	1,435	1,455	756	4,252
Consumer durables (cars, appliances etc)	685	1,054	1,567	2,288	5,594
Consumer staples (food, agriculture etc)	7,204	1,980	1,478	898	11,560
Energy (oil, gas etc)	5	667	1,421	1,010	3,102
Health care and pharmaceuticals	818	399	176	694	2,087
Industrial capital goods	899	2,406	109	973	4,387
Industrial commercial services	3,527	2,715	5,853	3,107	15,204
IT software, hardware and services	465	525	145	273	1,408
Media and leisure	741	646	566	607	2,561
Metals and mining materials	20	435	159	274	888
Paper and forest materials	164	1,536	38	1,707	3,444
Real estate management and investment	5,331	6,430	9,114	13,585	34,461
Retail trade	3,798	2,749	1,407	2,598	10,552
Shipping and offshore	1,406	1,362	4,653	632	8,053
Telecommunication equipment	11	362	1	1	374
Telecommunication operators	441	816	241	1,085	2,583
Transportation	736	850	539	1,258	3,383
Utilities (distribution and production)	1,259	2,768	1,034	731	5,792
Other financial institutions	3,194	2,621	1,010	3,315	10,140
Other materials (chemical, building materials etc)	1,234	2,782	887	1,979	6,882
Other	5,929	954	1,738	48	8,669
Total exposure	**38,473**	**35,492**	**33,591**	**37,821**	**145,376**

5.2.5.1 Specification of exposure against central government and central banks

Nordea applies the standardised approach for exposure against central government and central banks. In this approach, the external rating from an eligible rating agency is converted to the credit quality step (the mapping is defined by the financial supervisory authorities), which corresponds to a fixed risk weight. Nordea uses Standard & Poor's as eligible rating agency. In table 12, the central government and central banks exposure distributed by the credit quality steps is available.

The main part (96%) of the exposure towards central governments and central banks is within the highest credit quality step, resulting in no RWA. For this exposure only insignificant amounts relate to central governments and central banks outside the OECD. The exposure towards central governments and central banks has increased in 2009 by 68% due to increased exposure mainly in bonds and deposits in central banks.

Table 12 Exposure to central governments and central banks

EURm Standard & Poor's rating	Credit quality step	Risk weight	31 December 2009 Exposure	31 December 2008 Exposure
AAA to AA–	1	0%	33,868	19,230
A+ to A–	2	20%	552	1,108
BBB+ to BBB–	3	50%	280	6
BB+ and below, or without rating	4 to 6 or blank	100-150%	536	616
Total			**35,236**	**20,959**

5.2.6 Specification of off-balance exposure

The distribution of the off-balance exposure is specified in table 13. The off-balance exposure is presented as original exposure (excluding the application of CCF).

Table 13 Original exposure off-balance split by exposure class

EURm	31 December 2009	31 December 2008
IRB exposure classes		
Institution	5,322	4,855
Corporate	89,843	90,102
Retail	14,786	13,401
– of which mortgage	3,298	2,110
– of which other retail	10,329	10,000
– of which SME	1,158	1,290
Other non-credit obligation assets	0	
Total IRB approach	**109,951**	**108,357**
Standardised exposure classes		
Central government and central banks	1,346	1,213
Regional governments and local authorities	5,374	4,881
Institution	1,200	727
Corporate	11,318	11,824
Retail	5,417	4,097
Exposures secured by real estates	67	29
Other	92	
Total standardised approach	**24,815**	**22,771**
Total	**134,766**	**131,129**

The total off-balance volume increased by 3% during 2009. 75% of the off-balance sheet items stem from the corporate exposure class, which was stable during the year.

The largest part of the increase in off-balance exposure stems from the retail segment. The increase in retail IRB stems mainly from increasing housing loan commitments in Sweden and Norway

The overall capital requirement split by exposure type is available in table 14, where the exposure for derivatives stems from counterparty risk. The information in the table includes exposure from both the IRB and standardised exposure classes. The main categories within off-balance items are guarantees, credit commitments and unutilised portion of approved credit facilities.

Table 14 Exposure, RWA and capital requirements split by exposure type, 31 December 2009

EURm	On-balance sheet items[1]	Off-balance sheet items	Derivatives	Total
Original exposure	327,657	134,766	28,792	491,214
EAD	326,732	50,422	28,792	405,945
RWA	118,094	25,631	9,398	153,123
Capital requirement	9,448	2,051	752	12,250
Average risk weight	36%	51%	33%	38%

1) On-balance sheet items include securities financing.

Exposure, RWA and capital requirements split by exposure type, 31 December 2008

EURm	On-balance sheet items[1]	Off-balance sheet items	Derivatives	Total
Original 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	9,274	1,916	870	12,060
Average risk weight	38%	50%	31%	39%

1) On-balance sheet items include securities financing.

Off-balance items have a smaller effect on RWA than on-balance items. At the end of 2009, only 23% of the total credit risk RWA stem from off-balance items and derivatives, which is similar to last year (23%). RWA for off-balance items was 19% of the original exposure, while RWA for on-balance including securities financing was 36% of the original exposure.

The exposure class IRB corporate has the largest portion of off-balance exposure which comprises 43% of the total original exposure, but a large part is revocable credit facilities.

An off-balance exposure amount does not contain the same risk as an on-balance exposure amount. The off-balance amount can be reduced to a value that carries the risk of a corresponding on-balance amount. This is done with a CCF, which is a percentage value (i.e. 0-100%) that is multiplied with the committed undrawn off-balance amount. For the off balance items, the nominal value of a guarantee is applied with a CCF for calculating the exposure. The CCF factor is for instance 50% or 100% depending of the type of guarantee, i.e. lowering the risk weights compared with the same exposure on-balance. Credit commitments and unutilised amounts are part of the external commitments that has not been utilised. This amount forms the calculation base depending on approach, product type and whether the utilised amounts are unconditionally cancellable or not.

The internal CCF model used for retail IRB is built on a product based approach. There are three explanatory variables that 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 CCF is based on own estimates on expected total exposure at the time of default.

Table 15 shows the weighted average CCF for the IRB exposure.

The decrease on average CCF for exposure class institutions stems from lower volumes in documentary credits and guarantees carrying 50% CCF. The total increase in average CCF in exposure class retail IRB stems from an increasing share of housing loan commitments carrying 100% CCF.

Table 15 Credit conversion factor and exposure split by IRB exposure class, 31 December 2009

EURm	Exposure after substitution effects[1]	Exposure	CCF
Institution	5,572	2,298	41%
Corporate	89,333	32,335	36%
Retail	14,783	11,227	76%
– of which mortgage	3,298	2,738	83%
– of which other retail	10,329	7,716	75%
– of which SME	1,156	772	67%

1) Exposure after substitution effects is the exposure after taking credit risk mitigation techniques into account as guarantees and credit derivatives

Credit conversion factor and exposure split by IRB exposure class, 31 December 2008

EURm	Exposure after substitution effects[1]	Exposure	CCF
Institution	5,072	2,211	44%
Corporate	89,537	31,873	36%
Retail	13,401	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%

1) Exposure after substitution effects is the exposure after taking credit risk mitigation techniques into account as guarantees and credit derivatives

5.2.7 Counterparty credit risk

Counterparty credit risk is the risk that Nordea's counterpart in a FX, interest, 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 credit risk can also exist in repurchasing agreements and other securities financing transactions.

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 traded over the counter (OTC), i.e. the terms connected to the specific contract are agreed upon on individual terms with the counterpart.

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.

Counterparty credit risk is subject to credit limits like other credit exposure and is treated accordingly.

5.2.7.1 Pillar 1 method for counterparty risk

Nordea uses the marked-to-market method to calculate the exposure for counterparty credit 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 exposure 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 16, the exposure as well as the RWA and capital requirement split on the exposure classes is available. As stated above, exposure equals the sum of current exposure and potential future exposure and as of December 2009 the potential future exposure is the major part of the exposure.

Table 16 Counterparty risk split by exposure class[1]

	31 December 2009		31 December 2008	
EURm	Exposure	RWA	Exposure	RWA
IRB exposure classes				
Institution	20,314	5,232	20,792	4,799
Corporate	6,476	3,867	12,400	5,778
Retail	47	24		
Total IRB approach	**26,838**	**9,124**	**33,193**	**10,576**
Standardised exposure classes				
Central government and central banks	1,054	14	543	1
Other	900	260	992	293
Total standardised approach	**1,954**	**275**	**1,535**	**294**
Total exposure	**28,792**	**9,398**	**34,727**	**10,870**

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

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

In table 17, the current exposure and potential future exposure are presented for different type of customers.As of December 2009, the current net exposure was EUR 6,392m and the potential future exposure was EUR 24,508m in the internal counterparty risk framework. The drop in the current exposure by almost 50% since December 2008 is mainly due to decreasing interest rates throughout 2009 and the slightly higher potential future exposure indicates an increase in the business volumes.

For internal capital purposes (economic capital 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, which are adjustments to the counterparty credit risk exposure done by including an estimate of the cost of hedging the specific counterparty credit risk. This cost of hedging is either based directly on market prices or on a theoretical calculation based on the credit rating of the counterparty.

5.2.7.3 Mitigation of counterparty risk exposure
To reduce the exposure towards single counterparties, risk mitigation techniques are widely used in Nordea. The most common is the use of closeout netting agreements, which allow Nordea 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 counterparties by an increasing use of financial collateral agreements, where collateral on daily basis is placed or received to cover the current exposure. The collateral is largely cash (EUR, USD, DKK, SEK and NOK), as well as government bonds and to a lesser extent mortgage bonds are accepted.

In table 18, information of how the counterparty risk exposure is reduced with risk mitigation techniques is available.

Table 17 Counterparty credit risk, current and potential future exposure

	December 31, 2009			December 31, 2008		
EURm	Current exposure	Potential future exposure	Total credit risk	Current exposure	Potential future exposure	Total credit risk
Public entities	596	2,180	2,466	1,754	1,302	2,727
Institution	1,933	15,304	16,223	4,291	14,454	13,010
Corporate	3,863	7,024	9,918	6,157	7,146	12,150
Total	**6,392**	**24,508**	**28,608**	**12,202**	**22,902**	**27,887**

Table 18 Mitigation of counterparty risk exposure due to closeout netting and collateral agreements, 31 December 2009 & 2008

	31 December 2009				31 December 2008			
EURm	Current Exposure (gross)	Reduction from closeout netting agreements	Reduction from held collateral	Current Exposure (net)	Current Exposure (gross)	Reduction from closeout netting agreements	Reduction from held collateral	Current Exposure (net)
Total	**77,030**	**67,201**	**3,437**	**6,392**	**82,203**	**66,364**	**3,637**	**12,202**

As of December 2009 Nordea had 703 financial collateral agreements. The effects of closeout netting and collateral agreements are considerable, as 92% of the current exposure (gross) was eliminated by the use of these risk mitigation techniques.

Nordea's financial collateral agreements do not normally 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 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 net current exposure account for around 18% (20%) of the total current exposure, and consists of a mix of financial institutions, public and corporate counterparties.

5.2.7.4 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.

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

In table 19, the equity holdings outside the trading book are grouped based on the inten-tion of the holding. In the investment portfolio, holdings in private equity funds are included in the amount of EUR 184m. 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. Table 19 shows to what extent published price quotations are used.

Table 19 Equity holdings outside the trading book, 31 December 2009

EURm	Book value	Fair value	Unrealised gains/losses	Realised gains/losses	Capital requirement
Investment portfolio[1]	557	557	43	1	45
Other[2]	47	47	17	–2	4
Total	**604**	**604**	**60**	**–1**	**49**

1) Of which listed equity holdings, 149
2) Of which listed equity holdings, 30

5.3 Rating, collateral and maturity distribution

The parameters PD, LGD and maturity are central as part of calculating the RWA. In this section the components are described with respect to development of rating distribution and migration, LGD development and maturity distribution. The final section analyses how these parameters are estimated and validated.

5.3.1 Rating and scoring

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

- The credit approval process
- Calculation of Risk Weighted Assets (RWA)
- Calculation of economic capital and Expected Loss (EL)
- Monitoring and reporting of credit risk
- Performance measurement using the Economic Profit (EP) framework
- Collective impairment assessment

While rating is used for corporate and institution exposure, scoring is used for retail exposure.

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 better are comparable to investment grade as defined by external rating agencies such as Moody's and Standard & Poor's (S&P). Rating grades 2+ and lower are considered as weak or critical, and require special attention.

The risk grade master scale used for scored customers in the Retail portfolio consists of 18 grades, named A+ to F-.

In table 20, the mapping from the internal rating scale to the S&P's rating scale, using condensed scales, is shown.

Table 20 Indicative mapping between internal rating and Standard & Poor's

Rating

Internal	Standard & Poor's
6+, 6, 6–	AAA to AA
5+, 5, 5–	A
4+, 4, 4–	BBB
3+, 3, 3–	BB
2+, 2, 2–	B
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 need for it. The consistency and transparency of the ratings are ensured by the use of rating models. A rating model is a set of specified and distinct rating criteria which, given a set of customer characteristics, produces a rating. It is based on the predictability of customers' future performance based on their characteristics.

Nordea has decided upon a differentiation of rating models to better reflect the risk involved for customers with different characteristics. Hence, rating models have been developed for a number of general as well as specific segments, e.g. real estate management and shipping. Different methods ranging from purely statistical, using internal data to expertbased methods, depending of the segment in question, have been used when developing the rating models. The models are in general based on an overall framework, in which financial and quantitative factors are combined with qualitative factors.

Scoring models are pure statistical methods to predict the probability of customer default. The models are used in the household segment as well as for small corporate customers. Bespoke behavioural scoring models, developed on internal data, are used to support both the credit approval process, e.g. automatic approvals or decision support, and the risk management process, e.g. "early warning" for high risk customers and monitoring of portfolio risk levels. As a supplement to the behavioural scoring models also bureau information is used in the credit process. The internal behaviour scoring models are used to identify the PDs, in order to calculate the economic capital and RWA for customers. During 2009, the scorecards have been adjusted in order to improve the risk differentiation.

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

The rating and scoring models are validated annually and the validation includes both a quantitative and a qualitative validation. The quantitative validation includes statistical tests of the models' discriminatory power, i.e. the ability to distinguish default risk on a relative basis, and cardinal accuracy, i.e. the ability to predict default levels.

In tables 21 to 24, the exposure is distributed over the internal rating scale for the exposure in the IRB exposure classes. The PD and the average risk weight are weighted based on exposure. 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 8, figure 9 and figure 11.

5.3.2 Rating distribution

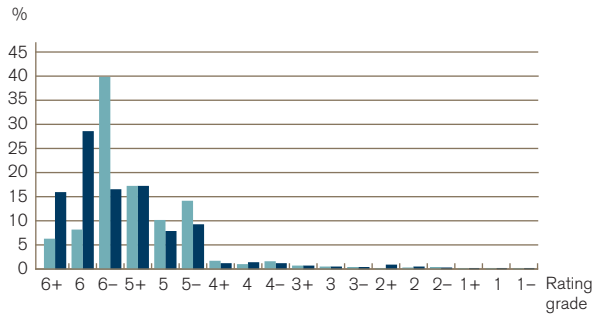
5.3.2.1 Institution rating
In December 2009, approximately 99% (98%) of the institution exposure is found in the nine highest rating grades, 4– and higher.

Table 21 Exposure towards IRB Institution, distributed by rating grade[1]

	31 December 2009 Institution			31 December 2008 Institution		
EURm Rating	PD scale	Exposure	Average risk weight	PD scale	Exposure	Average risk weight
6+	0.03%	2,758	14%	0.03%	7,671	15%
6	0.03%	3,626	13%	0.03%	13,847	16%
6–	0.05%	17,950	13%	0.05%	7,947	20%
5+	0.07%	7,695	18%	0.07%	8,323	24%
5	0.10%	4,493	28%	0.10%	3,745	31%
5–	0.16%	6,332	38%	0.16%	4,413	37%
4+	0.24%	698	49%	0.24%	471	50%
4	0.35%	357	53%	0.35%	583	60%
4–	0.53%	611	73%	0.53%	484	76%
3+	0.81%	207	91%	0.81%	253	91%
3	1.18%	119	104%	1.18%	143	104%
3–	2.01%	94	122%	2.01%	83	122%
2+	3.63%	21	128%	3.63%	355	124%
2	6.16%	24	150%	6.16%	138	164%
2–	9.86%	83	198%	9.86%	56	187%
1+	14.79%	14	234%	14.79%	9	234%
1	20.71%	7	254%	20.71%	12	254%
1–	26.93%	17	263%	26.93%	1	263%
	0.13%[2]	**45,104**	**23%**	**0.14%[2]**	**48,532**	**26%**

1) Exposure includes rated customers.
2) Exposure weighted PD.

Figure 8 Exposure distributed by rating grade, IRB Institution



As can be seen in table 21 the exposure in 2009 has decreased in rating grades 6 and 6+. This is mainly due to fluctuating exposure and downratings. The exposure to institution fluctuates over time to a higher extent than for instance retail and corporate exposure. The average PD of the institution portfolio improved even though the majority of the migrated exposure migrated downwards. This is because the exposure in the rating grades 2 and 2+ has decreased during 2009 and the weight of this exposure in the average PD was relatively large in 2008. More information about the migration can be found in section 5.3.4. Table 21 shows that the average risk weight has been reduced from 26% to 23%, despite negative migration. The average risk weights have been positively affected by process improvements.

5.3.2.2 Corporate rating

In December 2009, approximately 67% (73%) of the corporate exposure is found in the nine highest rating grades, 4– and above.

Many industries have encountered challenges in 2009 and this in turn affected the ratings in Nordea. The credit quality of the corporate exposure was reduced during 2009 due to migration of existing customers, which has increased the average PD from 0.72% to 0.87%. This in turn has affected the average risk weight which has increased from 57% to 61%.

Table 22 Exposure towards IRB Corporate, distributed by rating grade[1]

	31 December 2009 Corporate			31 December 2008 Corporate		
EURm Rating	PD scale	Exposure	Average risk weight	PD scale	Exposure	Average risk weight
6+	0.03%	1,711	14%	0.03%	1,946	12%
6	0.03%	3,647	17%	0.03%	4,438	15%
6-	0.05%	2,676	15%	0.05%	5,075	19%
5+	0.07%	6,389	23%	0.07%	8,855	24%
5	0.10%	9,690	29%	0.10%	12,290	29%
5-	0.16%	12,417	37%	0.16%	16,079	37%
4+	0.24%	16,333	45%	0.24%	17,851	45%
4	0.35%	21,181	56%	0.35%	23,643	56%
4-	0.53%	20,286	66%	0.53%	18,865	66%
3+	0.81%	16,594	79%	0.81%	14,205	77%
3	1.18%	12,263	88%	1.18%	10,982	89%
3-	2.01%	10,690	101%	2.01%	9,513	98%
2+	3.63%	3,641	122%	3.63%	2,260	119%
2	6.16%	1,970	133%	6.16%	1,406	142%
2-	9.86%	1,039	163%	9.86%	635	160%
1+	14.79%	297	162%	14.79%	232	172%
1	20.71%	216	200%	20.71%	308	227%
1-	26.93%	123	211%	26.93%	100	247%
	0.87%[2]	141,161	61%	0.72%[2]	148,684	57%

1) Exposure includes rated customers.
2) Exposure weighted PD.

Figure 9 Exposure distributed by rating grade, IRB Corporate

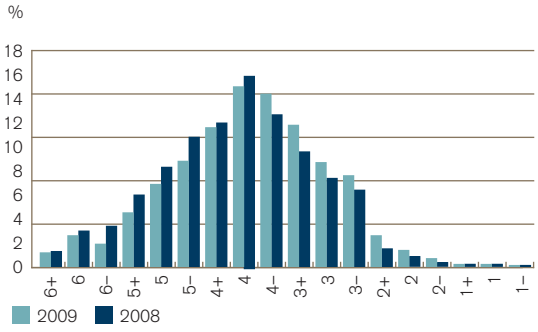
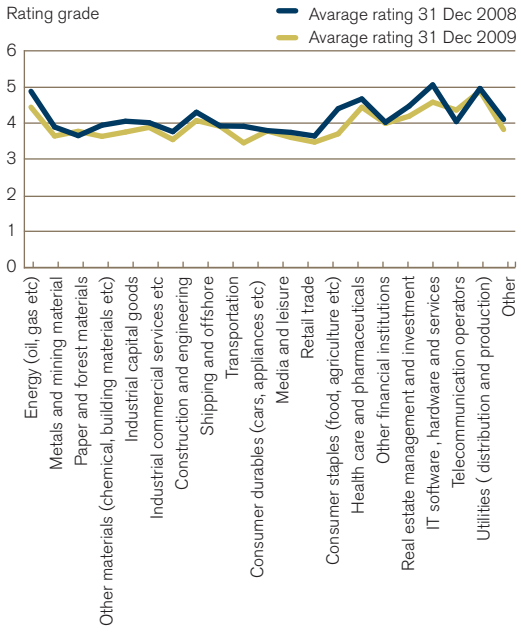


Figure 10 Development of average rating per industry, IRB corporate



The average rating per industry has shown a downward trend in 2009. At the end of 2009 the average rating was 3.94 compared to 4.10 in 2008. The industries that have decreased the average rating the most are energy, consumer durables, health care and pharmaceuticals and telecommunication equipment. In 2009, the sectors real estate management and investment, media and leisure, transportation and utilities have remained largely un-changed. The downgrade in ratings took place mainly in the first 6 months of the year.

5.3.2.3 Retail scoring

At the end of 2009, approximately 86% (86%) of the retail exposure is found in the nine highest risk grades, C- and above. In the sub-exposure class retail mortgage approximately 91% of the customers have the highest rating grades. For retail other and retail SME the corresponding figures are 74% and 52%.

The scoring distribution for the retail portfolio was relatively stable in 2009. Improvements can be seen in the highest risk grade, A+, but it can also be seen that risk grade E has a relative increase. Altogether, the new scoring distribution has increased the average PD from 0.89% to 0.93%.

Table 23 Exposure towards IRB Retail, distributed by risk grade[1]

	31 December 2009 Retail			31 December 2008 Retail		
EURm Risk grade	PD scale	Exposure	Average risk weight	PD scale	Exposure	Average risk weight
A+	0.08%	34,771	3%	0.08%	28,364	3%
A	0.11%	15,136	5%	0.11%	14,041	5%
A–	0.16%	11,572	7%	0.16%	10,606	7%
B+	0.22%	11,264	9%	0.22%	11,404	9%
B	0.31%	10,729	11%	0.31%	9,298	11%
B–	0.43%	8,948	14%	0.43%	8,582	14%
C+	0.60%	6,736	18%	0.60%	6,931	19%
C	0.84%	7,224	22%	0.84%	5,270	23%
C–	1.17%	4,665	28%	1.17%	4,047	28%
D+	1.64%	4,391	35%	1.64%	4,474	34%
D	2.30%	3,205	38%	2.30%	2,933	39%
D–	3.20%	3,191	44%	3.20%	2,573	45%
E+	4.47%	1,940	50%	4.47%	2,833	51%
E	6.30%	2,764	52%	6.30%	862	53%
E–	8.79%	585	57%	8.79%	492	59%
F+	12.28%	421	66%	12.28%	715	61%
F	17.19%	321	80%	17.19%	183	78%
F–	24.04%	879	87%	24.04%	741	90%
	0.93%[2]	**128,742**	**16%**	**0.89%[2]**	**114,349**	**16%**

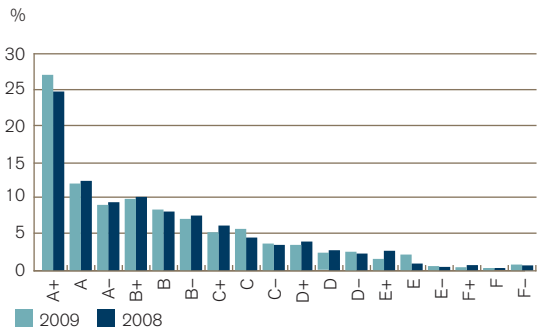
1) Exposure includes scored customers.
2) Exposure weighted PD.

Table 24 Exposure towards IRB Retail sub-exposure classes, distributed by risk grade[1]

EURm	31 December 2009 Retail				31 December 2008 Retail			
Risk grade	PD scale	Retail mortgage	Other Retail	SME	PD scale	Retail mortgage	Other Retail	SME
A+	0.08%	30,588	3,735	448	0.08%	24,428	3,126	810
A	0.11%	12,683	2,381	73	0.11%	11,762	2,221	58
A–	0.16%	9,677	1,834	61	0.16%	8,609	1,893	105
B+	0.22%	9,244	1,948	73	0.22%	9,024	2,230	150
B	0.31%	8,339	2,270	119	0.31%	6,890	2,135	273
B–	0.43%	6,849	1,967	133	0.43%	6,434	1,857	291
C+	0.60%	4,908	1,727	101	0.60%	4,678	2,036	216
C	0.84%	5,354	1,714	156	0.84%	3,532	1,501	238
C–	1.17%	2,882	1,178	605	1.17%	2,433	1,007	607
D+	1.64%	2,601	1,418	371	1.64%	2,657	1,553	265
D	2.30%	1,957	925	323	2.30%	1,572	1,150	210
D–	3.20%	2,060	785	346	3.20%	1,466	842	264
E+	4.47%	1,086	678	176	4.47%	1,450	1,199	184
E	6.30%	664	1,915	185	6.30%	388	402	72
E–	8.79%	130	370	85	8.79%	138	255	99
F+	12.28%	202	181	39	12.28%	162	508	45
F	17.19%	173	103	46	17.19%	93	63	26
F–	24.04%	506	319	54	24.04%	443	256	42
		99,901	**25,447**	**3,395**		**86,161**	**24,234**	**3,954**

1) Exposure includes scored customers.

Figure 11 Exposure distributed by risk grade, IRB Retail



5.3.3 Point-In-Time vs Through-The-Cycle

In a Point-In-Time (PIT) process, an internal rating reflects an assessment of the borrower's current condition and/or most likely future condition over the course of the chosen time horizon. The internal rating changes as the borrower's condition changes over the course of the credit/business cycle. A Through-The-Cycle (TTC) process requires assessment of the borrower's risk under a longer period of time. In this case, a borrower's rating would tend to stay the same over the course of the credit/business cycle.

The creditworthiness indicated by a purely TTC risk classification system would correspond to the long term average credit risk, which manifests itself in no migration between rating grades. A purely PIT risk classification system, on the other hand, would only represent the credit risk at the point when the risk assessment was made which leads to higher migration compared to a TTC system.

Nordea currently employs a hybrid risk classification system that is neither purely TTC nor purely PIT. The PD estimates for the risk grades remain fairly stable over time, but migration between risk grades is expected which affects the average PDs and hence RWA.

Nordea's rating system (used in the exposure classes corporate and institution) is balanced between PIT and TTC. The main factors influencing the rating produced by the models are the financial factors supplemented with qualitative factors into a total risk assessment. The financial factors are based on the last audited financial statements and will therefore vary as the overall business conditions fluctuate. Adjustments and overrides in ratings can be made when the financial factors do not reflect the future repayment capacity. The qualitative factors are based on the subjective view of the expert with respect to management, industry outlook, products etc. The qualitative factors are seen as more forward looking, but assess the risk of a borrower based on the current state and not on a worst-case scenario. Therefore, the qualitative factors can be seen as more long term.

Nordea's scoring models (used in the exposure class retail) are assessed to be relatively close to PIT. The scorecards, or score models, are built to reflect the latest available information and a new score is calculated each month.

This will guarantee that the score models give a score reflecting a customer's monthly performance status and behaviour. The model is, however not fully PIT due to that there are some elements that have a lag and do not meet the requirements for 100% PIT.

Nordea's internal data is used when determining estimates of PD. However, the time series used are representing a relatively recent period and the observed values are adjusted in order to represent long term average estimates. For PDs this adjustment is called Margin of Conservatism and represents an adjustment for the number of observations as well as an adjustment to the long-term default frequency observed in Nordea's markets.

5.3.4 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 exposure 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 among other macroeconomic development and timely payments.

Figures 12 to 14 show the rating/scoring migration for institution, corporate and retail customers during 2009, comparing the development from the beginning of the year with year-end. The migration is based on customers existing at year-end 2008 and 2009. The mi-gration is shown both in terms of number of customers and exposure. The RWA increase due to rating/scoring migration reflects the impact of pro-cyclicality in the pillar 1 capital requirement calculations of the IRB approaches.

The institution portfolio is volatile in terms of exposure volume. Out of the total exposure in the institution portfolio approximately 48% has migrated up or down during 2009. This corresponds to approximately 27% of the number of counterparts. Most of the migration downwards can be seen in the top rating grades. A downgrading in these by one rating grade does not have a significant impact on RWA due to the low risk weights.

Out of the total exposure in the corporate portfolio approximately 50% has migrated either up or down in 2009. This corresponds to approximately 36% of customers.

Out of the total exposure in the retail portfolio approximately 48% has migrated up or down during 2009. This corresponds to approximately 50% of the customers.

The impact of the migration on credit risk RWA was 6.9% for 2009. This calculation does not take into account the rating distribution of lost/new counterparts as well as counterparts that have defaulted.

5.3.5 Loss Given Default

In table 25, the exposure per exposure class secured by eligible collateral, guarantees and credit derivatives is shown. The table presents a split between exposure classes subject to the IRB approach and exposure classes subject to the standardised approach. In 2009, approximately 37% (35%) of total exposure was secured by eligible collateral. In the IRB portfolios 47% (42%) of the exposure was secured by eligible collateral.

The increase in relative share of collateralised exposure comes mainly from exposure classes corporate and retail in IRB approach. In both exposure classes the main source of increase is larger shares of the exposure collateralised by residential real estate and commercial real estate, and smaller shares of unsecured exposure.

In the FIRB approach the LGD estimates are predefined in the legislation. For instance, exposure fully secured by real estate collateral is assigned an LGD of 30-35% depending on national regulations. Exposure fully secured by other physical collateral is assigned an LGD of 40%. The LGD value for unsecured senior exposure is 45%. The LGDs for the retail portfolio are based on an internal model, and divided in pools of collateral and based on historical loss data.

Figure 12a Institution rating migration, exposure that has been up or downgraded during 2009

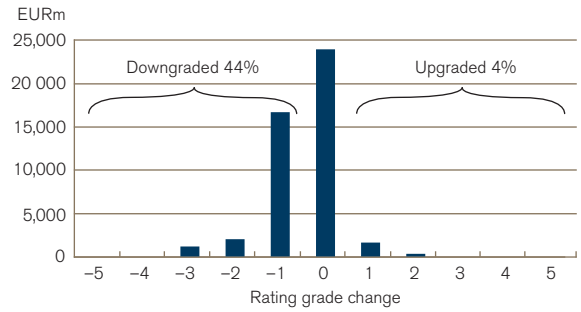


Figure 12b Institution rating migration, number of counterparts that have been up or downgraded during 2009

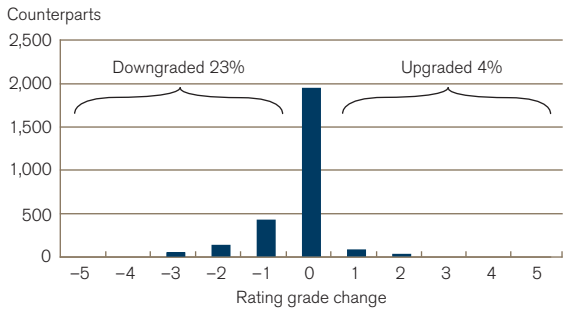


Figure 13a Corporate rating migration, exposure that has been up or downgraded during 2009

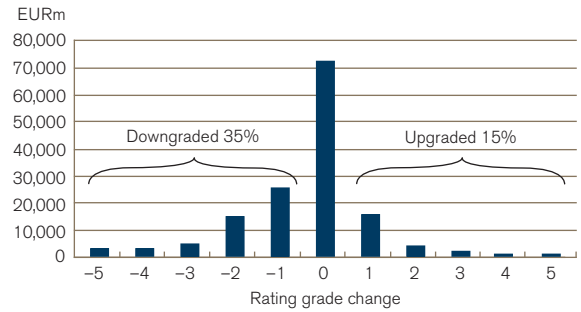


Figure 13b Corporate rating migration, number of counterparts that have been up or downgraded during 2009

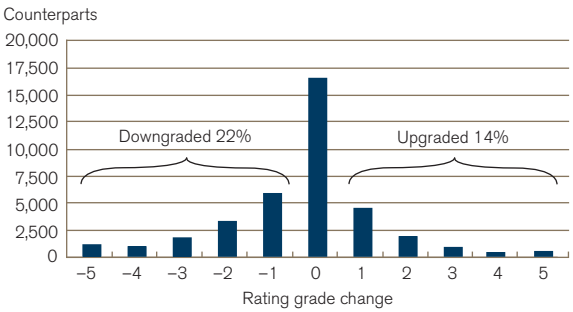


Figure 14a Retail risk grade migration, exposure that has been up or downgraded during 2009

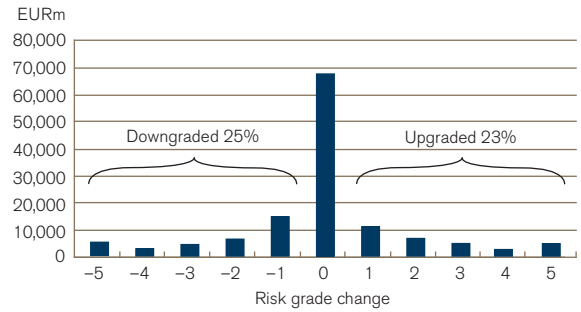


Figure 14b Retail risk grade migration, number of counterparts that have been up or downgraded during 2009

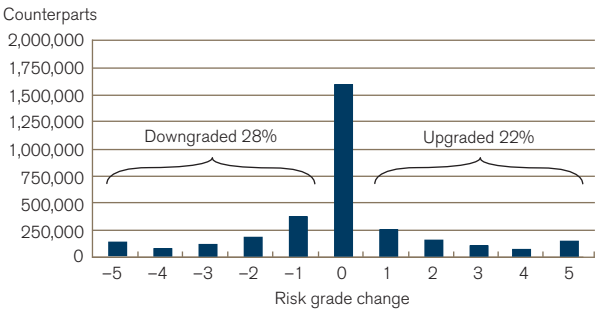


Table 25 Exposure secured by collaterals, guarantees and credit derivatives, 31 December 2009

EURm	Original exposure	Exposure	of which secured by guarantees and credit derivatives	of which secured by collateral	Average weighted LGD
IRB exposure classes					
Institution	50,345	45,416	2,342	2,667	34.1%
Corporate	207,214	145,376	5,125	45,933	41.4%
Retail	135,231	130,751	2,584	102,189	18.9%
– of which mortgage	100,704	100,144		99,065	14.5%
– of which other retail	30,497	27,007	2,282	781	34.6%
– of which SME	4,030	3,600	302	2,343	24.7%
Other non-credit obligation assets	1,712	1,269			n.a.
Total IRB approach	**394,501**	**322,813**	**10,052**	**150,789**	
Standardised exposure classes					
Central government and central banks	32,148	35,236	28	0	
Regional governments and local authorities	9,703	7,625	0		
Institution	4,452	4,159	1		
Corporate	28,196	19,646	777	38	
Retail	16,419	11,025	97		
Exposures secured by real estates	1,162	1,114		1,114	
Other[1]	4,633	4,328	2	0	
Total standardised approach	**96,713**	**83,133**	**905**	**1,153**	

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, standardised institution, standardised corporate, past due items, short term claims, covered bonds and other items. Associated companies not included in exposure.

Exposure secured by collaterals, guarantees and credit derivatives, 31 December 2008

EURm	Original exposure	Exposure	of which secured by guarantees and credit derivatives	of which secured by collateral	Average weighted LGD
IRB exposure classes					
Institution	52,401	49,143	728	2,123	43.2%
Corporate	214,072	152,015	4,523	41,504	41.7%
Retail	120,390	116,045	2,132	89,033	19.0%
– of which mortgage	86,788	86,236		86,155	14.4%
– of which other retail	28,981	25,649	1,878	550	33.5%
– of which SME	4,621	4,160	254	2,327	24.7%
Other non-credit obligation assets	2,226	1,838			n.a.
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**	

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, standardised institution, standardised corporate, past due items, short term claims, covered bonds and other items. Associated companies not included in exposure.

Average LGD in exposure class institution decreased to 34% (43%), which is mainly related to process improvements.

Average LGD in exposure class corporate decreased mainly due to increased shares of the exposure collateralised by commercial real estates and residential real estates, and decreased share of unsecured exposure. Average LGD in retail is slightly down compared to 2008, stemming mainly from an increased share of the exposure collateralised by residential real estate.

5.3.5.1 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 76%. The exposure that is guaranteed by these guarantors receives an average risk weight of 0%. 7% of the guarantors are IRB institutions, of which 95% have a rating of 5- or higher. IRB corporate accounts for 3% of the guarantors, where 100% have a guarantor with a rating of 5- or higher. The remaining 14% of the guarantors are within the standardised institution and corporate portfolios.

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

5.3.5.2 Collateral distribution

In table 26, 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 26 Collateral distribution

	31 Dec 2009	31 Dec 2008
Other Physical Collateral	6.0%	6.1%
Receivables	1.0%	0.8%
Residential Real Estate	72.9%	72.5%
Commercial Real Estate	17.6%	17.8%
Financial Collateral	2.5%	2.8%

5.3.5.3 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 previously experienced volatility of market values.
- Forced sale principle: assessment of market value or the collateral value must reflect that realisation of 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. In table 27, the retail mortgage exposures are distributed continuously by LTV range up to the top LTV bucket based on the LTV ratio. 3.4% of the total mortgage retail exposures are distributed to the LTV ratio-buckets above 80% by end of 2009. This is an increase in comparison to 2008 (1.9%), mainly due to a decrease of market values in Denmark.

Table 27 Loan-to-value distribution[1], Retail mortgage exposure

EURbn	31 Dec 2009	%
<50%	74.2	76
50–70%	15.8	16
70–80%	4.0	4
80–90%	2.0	2
>90%	1.3	1
Total	**97.4**	**100**

EURbn	31 Dec 2008	%
<50%	67.2	79
50–70%	13.0	15
70–80%	2.9	3
80–90%	1.0	1
>90%	0.7	1
Total	**84.7**	**100**

1) The exposure is continously distributed by LTV buckets. For example, an exposure of 540 with a LTV of 54% is distributed 500 to the <50% bucket and 40 to the 50-70% bucket. 2008 figures are restated due to change of method.

5.3.6 Maturity

Exposure in the IRB exposure classes is divided by maturity, defined as remaining maturity, is presented in table 28.

Table 28 IRB exposure split by maturity, 31 December 2009

EURm	Institution	Corporate	Retail
< 1 year	29,775	47,756	44,884
1-3 years	7,402	19,405	1,468
3-5 years	1,488	19,930	2,445
> 5 years	6,752	58,285	81,954
Total exposure	**45,416**	**145,376**	**130,751**

IRB exposure split by maturity, 31 December 2008

EURm	Institution	Corporate	Retail
< 1 year	34,433	53,833	40,173
1-3 years	7,640	18,616	1,648
3-5 years	1,536	19,008	2,268
> 5 years	5,534	60,559	71,955
Total exposure	**49,143**	**152,015**	**116,045**

5.3.7 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.

The estimation process is linked to the validation since the estimates used for the PD scale are based on Nordea's Actual Default Frequencies (ADF). Any suggested changes to the PD scale is processed through appropriate channels such as the Risk Committee and subsequently decided by GEM.

The PD estimation, and hence the validation, takes into account that the rating models used for corporate and institution customers has a higher degree of TTC than the scoring models used for retail customers. The PD estimates are based on the long-term default experience and adjusted by adding a Margin of Conservatism between the average PD and the average ADF. This add-on consists of two parts, one that compensates for statistical uncertainty whereas the other constitutes a business cycle adjustment of the rating and scoring models.

Table 29 shows, from the validation, the average PD based on Nordea's current PD scale and weighted with the number of customers for each exposure class. The average PD is based on the period 2003 – 2008 for the corporate and institution portfolios and 2005 – 2008 for the retail portfolio. Table 29 also shows the average ADF, calculated as the customer weighted default frequency for the period 2004 -2009 for the corporate and institution portfolios and 2006 – 2009 for the retail portfolio.

Table 29 Obligor weighted PD vs. ADF, 2009

	Average PD	Average ADF
Retail	1.26%	1.10%
Corporate & Institutions	1.35%	1.12%

Table 30 shows estimated and realised LGD for IRB exposure. The estimated LGD is higher than the realised LGD mainly due to the fact that the estimated LGD includes a downturn add-on.

Table 30 Estimated vs. realised LGD, 2009

	LGD	
	Estimated[1] %	Realised average %
Retail	18.73%	12.10%

1) Defaulted customers are not included.

In table 31, the EL is compared to the actual gross and net losses. EL has been calculated using the definition from the economic capital framework, in which defaulted exposure receive 0% EL and where Nordea has internal LGD and CCF estimates for corporate and institution exposure. Figures represent the full year outcome. For 2009, the EL ratio used for calculating risk-adjusted profit was on average 25 basis points, excluding the sovereign and institution exposure classes.

Table 31 EL vs. gross loss and net loss

	Retail Household[1]					
EURm	Mortgage	Other	Corporate[1]	Institution	Government	**Total**
2009						
EL	–81	–198	–451	–21	–3	**–754**
Gross loss	–108	–236	–1,479	–19	0	**–1,842**
Net loss	–97	–148	–1,262	21	0	**–1,486**
2008[2]						
EL	–77	–190	–390	–48	–3	**–706**
Gross loss	–20	–196	–635	–38	0	**–890**
Net loss	–17	–86	–330	–32	0	**–466**
2007[2]						
EL	–68	–190	–324	0	0	**–582**
Gross loss	–7	–119	–333	–15	0	**–473**
Net loss	–4	–25	61	27	0	**60**

1) SME Retail is included in the corporate segment
2) Figures are restated due to changes in economic capital framework as of 1st of January 2009

Note that the EL will vary over time due to changes in the rating and the collateral coverage distributions, but it is expected that the average long term net loss will be in line with average EL disregarding the fact that EL includes extra margins for statistical uncertainty and, in the case of LGD, a downturn add-on.

5.4 Loan portfolio, impaired loans and loan losses

5.4.1 Loan portfolio

Nordea's total loans have increased by 7% to EUR 282bn during 2009 (EUR 265bn) and was mainly due to a large increase in the household portfolio. The portion of total lending to corporate customers was 54% (57%) and to household customers 44% (41%). The portfolio is geographically well diversified as no market accounts for more than 30% of total lending. Lending in the Baltic countries constitutes 3% and the shipping industry 4% of the Group's total lending. Lending to companies owned by private equity funds constitutes 3% of lending, of which 99% are senior loans. Some weakening has been seen in credit quality in 2009, mainly in the corporate credit portfolio. The total effect from rating migration on RWA was an increase by approx. 6.9% in 2009.

For breakdown of the loan portfolio by geography see Annual report

5.4.1.1 Lending to corporate customers

Loans to corporate customers increased 1% to EUR 154bn (EUR 152bn), supported by FX effects. Real estate, consumer durables and construction were the sectors that increased the most in 2009. Three industries account for more than 5% of total lending. Real estate remains the largest sector in the lending portfolio, at EUR 37.2bn (EUR 35.5bn).

The distribution of loans to corporate by size of loans shows a high degree of diversification where approximately 62% of the corporate volume represents loans up to EUR 50m per customer.

The real estate portfolio predominantly is comprised of relatively large and financially strong companies, with 69% (74%) of the lending in rating grades 4– and higher. There is a higher level of collateral coverage for the real estate portfolio than for other corporate customers. Slightly more than 38% of lending to the real estate industry (EUR 14.2bn) is to companies in Sweden and close to half is to companies with mainly residential real estate.

Decreased investments on exploration and production coupled with oversupply in certain segments, resulted in lower earnings for many offshore and oil services companies in 2009. Nordea's exposure to the shipping, offshore and oil services industries is well diversified with an average rating of 4- (4+). However, proactive risk management will remain high on the agenda in 2010 as developments within the shipping industry remain uncertain.

The loans to shipping and offshore decreased 8% to EUR 10.4bn (EUR 11.4bn). Reflecting Nordea's global customer strategy, there is an even distribution between Nordic and non-Nordic customers.

Table 32 Loans to corporate customers, split by size of loan

	31 Dec 2009		31 Dec 2008	
EURbn	Loans	%	Loans	%
0-10	58.9	38.4	57.3	37.8
10-50	35.9	23.4	35.2	23.2
50-100	18.3	11.9	18.2	12.0
100-250	17.7	11.5	20.8	13.7
250-500	11.4	7.4	11.2	7.4
500-	11.2	7.3	9.0	5.9
Total	**153.5**	**100%**	**151.7**	**100%**

Table 33 Real estate management industry, loans and total exposure, split by country

	31 Dec 2009		31 Dec 2008	
EURbn	Loans	%	Loans	%
Denmark	5.6	15.1	4.8	13.5
Finland	6.5	17.6	7.1	20.0
Norway	8.7	23.4	7.7	21.7
Sweden	14.2	38.3	13.5	38.2
Baltic countries	1.3	3.5	1.2	3.4
Poland	0.2	0.6	0.2	0.6
Russia	0.4	1.0	0.4	1.2
Other	0.2	0.6	0.5	1.4
Total	**37.2**	**100%**	**35.5**	**100%**

Table 34 Shipping and offshore industry, loans

	31 Dec 2009		31 Dec 2008	
EURbn	Loans	%	Loans	%
Bulk carriers	1.6	15	1.6	14
Product tankers	1.1	11	1.3	11
Crude tankers	1.0	9	1.1	9
Chemical tankers	0.7	7	1.0	9
Gas tankers	0.7	7	0.7	6
Other Shipping	2.6	25	2.1	18
Offshore and Oil Services	2.7	26	3.6	32
Total exposure	**10.4**	**100%**	**11.4**	**100%**

5.4.1.2 Lending to household customers

In 2009, mortgage loans increased by 15% to EUR 96.6bn and consumer loans increased by 8% to EUR 26.5bn. The portion of mortgage loans out of total household loans was 78% (77%), of which the Nordic market accounts for 98%.

5.4.2 Impaired loans

In tables 35-38 impaired loans, loan losses and allowances are distributed and stated according to International Financial Reporting Standard (IFRS) as in the annual report which is not exactly the same as in CRD. In table 35, impaired loans to corporate customers are distributed by industry.

Table 35 Loans, impaired loans and allowances, split by customer type, 31 December 2009

EURm	Loans before allowances	Impaired loans before allowances	Impaired loans in % of loans	Allowances for collectively assessed loans	Specific allowances	Provisioning ratio
To credit institutions	**18,593**	**35**	**0.19**	**–3**	**–35**	**107%**
– of which banks	16,716	35	0.21	–3	–35	107%
– of which other credit institutions	1,877					
To the public[1]	**284,529**	**4,067**	**1.43**	**–822**	**–1,296**	**52%**
– of which corporate	155,144	2,901	1.87	–585	–1,057	57%
Energy (oil, gas, etc.)	3,005	0	0.01	–5	0	
Metals and mining materials	1,242	6	0.47	–10	–3	221%
Paper and forest materials	2,243	17	0.76	–9	–9	104%
Other materials (building materials, etc,)	5,351	248	4.63	–29	–119	60%
Industrial capital goods	2,329	126	5.40	–20	–42	49%
Industrial commercial services, etc.	15,059	200	1.32	–40	–82	61%
Construction and civil engineering	4,576	202	4.41	–35	–85	59%
Shipping and offshore	10,474	239	2.28	–53	–44	41%
Transportation	4,519	88	1.95	–15	–25	45%
Consumer durables (cars, appliances, etc.)	4,410	215	4.88	–17	–75	43%
Media and leisure	3,066	94	3.07	–7	–27	36%
Retail trade	10,737	298	2.78	–46	–151	66%
Consumer staples (food, agriculture, etc.)	12,366	247	2.00	–93	–56	61%
Health care and pharmaceuticals	2,073	17	0.81	–3	–4	42%
Financial institutions	16,818	81	0.48	–14	–41	68%
Real estate management	37,435	501	1.34	–127	–134	52%
IT software, hardware and services	1,561	58	3.72	–12	–18	51%
Telecommunication equipment	140	11	8.21	0	–13	110%
Telecommunication operators	1,706	103	6.05	–7	–27	33%
Utilities (distribution and production)	3,923	16	0.41	–6	–2	51%
Other	12,111	134	1.11	–37	–100	102%
– of which household	**123,571**	**1,166**	**0.94**	**–238**	**–239**	**41%**
Mortgage financing	96,785	503	0.52	–143	–27	34%
Consumer financing	26,786	664	2.48	–95	–212	46%
– of which public sector	**5,814**	**0**	**0.01**	**0**	**0**	**70%**
Total loans in the banking operations	**303,122**	**4,102**	**1.35**	**–825**	**–1,331**	**53%**
Loans in the life insurance operations	309					
Total loans including life insurance operations	**303,431**	**4,102**	**1.35**	**–825**	**–1,331**	**53%**

Provisions for off-balance sheet items for 2009 were EUR 19m for credit institutions and EUR 217m related to lending to the public.
1) Corresponding loans figure after allowances EUR 282,411m.

cont. Loans, impaired loans and allowances, split by customer type, 31 December 2008

EURm	Loans before allowances	Impaired loans before allowances	Impaired loans in % of loans	Allowances for collectively assessed loans	Specific allowances	Provisioning ratio
To credit institutions	**23,926**	**33**	**0.14**	**–3**	**–20**	**70%**
– of which banks	22,572	33	0.15	–3	–20	70%
– of which other credit institutions	1,355					
To the public[1]	**266,247**	**2,191**	**0.82**	**–405**	**–742**	**52%**
– of which corporate	152,613	1,608	1.05	–320	–582	56%
Energy (oil, gas, etc.)	2,816	1	0.02	–1	0	253%
Metals and mining materials	1,752	2	0.14	–1	–1	71%
Paper and forest materials	2,292	19	0.82	–1	–5	31%
Other materials (building materials, etc,)	5,452	169	3.10	–27	–48	45%
Industrial capital goods	3,272	18	0.56	–2	–6	45%
Industrial commercial services, etc.	15,570	143	0.92	–11	–77	61%
Construction and civil engineering	3,749	136	3.62	–31	–46	57%
Shipping and offshore	11,301	59	0.52	–1	–5	10%
Transportation	4,049	53	1.32	–10	–22	60%
Consumer durables (cars, appliances, etc.)	2,795	168	6.03	–4	–38	25%
Media and leisure	3,200	71	2.23	–3	–26	40%
Retail trade	11,115	217	1.95	–14	–81	44%
Consumer staples (food, agriculture, etc.)	13,054	136	1.04	–50	–60	81%
Health care and pharmaceuticals	1,613	39	2.40	–1	–6	19%
Financial institutions	16,497	56	0.34	–2	–15	30%
Real estate management	35,695	206	0.58	–119	–76	95%
IT software, hardware and services	1,498	21	1.43	–1	–8	41%
Telecommunication equipment	633	33	5.28	0	–10	29%
Telecommunication operators	1,689	2	0.09	–3	0	253%
Utilities (distribution and production)	4,024	3	0.07	–2	0	88%
Other	10,548	55	0.52	–35	–51	155%
– of which household	**108,845**	**579**	**0.53**	**–85**	**–158**	**42%**
Mortgage financing	84,019	182	0.22	–32	–13	25%
Consumer financing	24,826	397	1.60	–53	–145	50%
– of which public sector	**4,789**	**5**	**0.10**	**0**	**–2**	**35%**
Total loans in the banking operations	**290,173**	**2,224**	**0.77**	**–408**	**–762**	**53%**
Loans in the life insurance operations	120					
Total loans including life insurance operations	**290,293**	**2,224**	**0.77**	**–408**	**–762**	**53%**

Provisions for off-balance sheet items for 2008 were EUR 54m for credit institutions, while EUR 45.7m was related to lending to the public.
1) Corresponding loans figure after allowances EUR 265,100m.

Impaired loans, gross, increased 84% to EUR 4,102m (EUR 2,224m) in 2009 as result of the current downturn and worsened economic conditions for many customers. 54% of impaired loans gross are performing loans and 46% are non-performing loans. Allowances for individually assessed loans increased to EUR 1,331m (EUR 762m). Allowances for collectively assessed loans increased to EUR 825m (EUR 408m). The ratio of total allowances to cover impaired loans, gross, was 53% (53%). The sectors with the largest increases in impaired loans were real estate, consumer staples and industrial capital goods. Provisions for off-balance items have increased to EUR 236m (EUR 100m).

In table 36, impaired loans are distributed by geography and industry. The increase in impaired loans was mainly related to Denmark.

Table 36 Impaired loans gross and allowances split by country and industry, 31 December 2009

EURm	Nordea	Denmark	Finland	Norway	Sweden	Baltic	Poland	Russia	Allow-ances	Provision-ing ratio
Energy (oil, gas etc)	0			0					5	
Metals and mining materials	6	0	2	0	0	0		4	13	221%
Paper and forest materials	17	7	5	2	2	1	0		18	104%
Other materials (building materials etc.)	248	17	69	5	125	28	4	0	148	60%
Industrial capital goods	126	47	66	1	7	2	0	1	62	49%
Industrial commercial services, etc.	200	59	100	23	9	7	0		122	61%
Construction and engineering	202	84	17	37	5	50	5	4	120	59%
Shipping and offshore	239	3	43	192	0	0			97	41%
Transportation	88	17	40	4	20	5	1		40	45%
Consumer durables (cars, appliances etc)	215	84	73	4	49	4	1		92	43%
Media and leisure	94	21	45	6	13	8	0		34	36%
Retail trade	298	130	83	9	49	16	3	8	197	66%
Consumer staples (food, agriculture, etc.)	247	164	38	6	8	18	3	9	149	61%
Health care and pharmaceuticals	17	7	7	1	2		0		7	42%
Financial institutions	81	58	8	10	1	3	0		55	68%
Real estate	501	136	65	117	49	134	0		261	52%
IT software, hardware and services	58	18	35	0	4	0	0	0	30	51%
Telecommunication equipment	11	0	4			7	0		13	110%
Telecommunication operators	103	1	0	102	0		0		34	33%
Utilities (distribution and productions)	16	1	1	1	1	12			8	51%
Other, public and organisations	134	92	3	0	0	38	2		137	102%
Corporate	**2,901**	**948**	**705**	**522**	**346**	**334**	**20**	**27**	**1,642**	**57%**
Household mortgages	503	8	248	52	3	177	12	4	170	34%
Household consumer	664	256	289	68	15	24	2	10	307	46%
Public sector	0						0		0	70%
Total impaired loans	**4,067**	**1,212**	**1,242**	**641**	**364**	**535**	**34**	**40**		
Allowances	**2,118**	**760**	**420**	**330**	**227**	**319**	**19**	**36**	**2,118**	**100%**
Provisioning ratio	**52%**	**63%**	**34%**	**52%**	**63%**	**60%**	**55%**	**89%**		

Table does not include credit institutions

Table 37 Reconciliation of allowance accounts for impaired loans, 2009

EURm	Individually assessed	Collectively assessed	Total
Opening balance, 1 Jan 2009	–762	–408	–1,170
Provisions	–971	–495	–1,466
Reversals	152	89	241
Changes through the income statement			**-1 224**
Allowances used to cover write-offs	278		278
Reclassification			
Currency translation differences	–28	–11	–39
Closing balance, 31 Dec 2009	**–1,331**	**–825**	**–2,156**

5.4.3 Loan losses

Table 38 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. Loan losses were EUR 1,486m in 2009 compared to EUR 466m last year. This corresponded to a loan loss ratio, excluding the provision concerning the contested legal claim related to the debt/restructuring liquidation of Swiss Air Group, of 54 basis points. These included 4 basis points of provisions related to the Danish guarantee scheme.

EUR 1,262m (EUR 330m) relates to corporate customers and EUR 245m (EUR 103m) relates to household customers. The main losses were in the corporate sectors retail trade, real estate, other materials and shipping as well as household consumer financing. The loan loss ratio in Nordic Banking was 52 basis points (21 basis points) and in IIB 66 basis points (31 basis points). Net loan losses as well as impaired loans continue to stem from a large number of smaller and medium-sized exposures rather than from a few large exposures. In the Baltic countries, the loan loss ratio was 259 basis points (72 basis points). Individual net loan losses amounted to 40 basis points[2] (16 basis points) and collective provisions net amounted to 14 basis points (3 basis points).

Table 38 Loan losses, 2009

EURm	New provisions and write-offs	Reversals and recoveries	Net loan losses	Loan loss ratio bps
To credit institutions	**–19**	**40**	**21**	
– of which banks	–19	40	21	
– of which other financial institutions				
To the public	**–1,823**	**316**	**–1,506**	**57**
– of which corporate	–1,479	217	–1,262	83
Energy (oil, gas, etc.)	–5	1	–4	13
Metals and mining materials	–13	1	–12	66
Paper and forest materials	–5	5	1	
Other materials (building materials, etc,)	–127	7	–120	223
Industrial capital goods	–46	4	–42	128
Industrial commercial services, etc.	–107	13	–94	61
Construction and civil engineering	–87	37	–49	134
Shipping and offshore	–109	9	–100	89
Transportation	–24	12	–12	29
Consumer durables (cars, appliances, etc.)	–80	12	–68	247
Media and leisure	–23	6	–17	53
Retail trade	–183	23	–160	145
Consumer staples (food, agriculture, etc.)	–91	21	–70	54
Health care and pharmaceuticals	–6	2	–4	25
Financial institutions	–57	4	–52	32
Real estate management	–173	16	–157	44
IT software, hardware and services	–19	7	–12	82
Telecommunication equipment	–5	0	–5	79
Telecommunication operators	–33	3	–29	175
Utilities (distribution and production)	–3	0	–3	7
Other	–283	31	–252	241
– of which household	**–344**	**99**	**–245**	**23**
Mortgage financing	–108	11	–97	12
Consumer financing	–236	88	–148	60
– of which public sector	**0**	**0**	**0**	**0**
Total	**–1,842**	**357**	**–1,486**	**51**

Loan losses corresponded to 54 basis points[2] in 2009 (19 basis points) and 53 basis points in H2 2009 which can be seen in figure 15. Over a cycle loan losses of 25 basis points of total loans are expected which also is the measure of the credit risk appetite. As can be seen in table 38 the loan loss ratio is 51 basis points when lending to the public as well as lending to credit institutions is included.

2) Excluding the provision concerning the legal claim, contested by Nordea, related to the debt restructuring liquidation of Swiss Air Group.

Table 39 Past due loans, not impaired, 31 December 2009

EURm	Corporate customers	Household customers
6–30 days	835	582
31–60 days	239	281
61–90 days	84	259
>90 days	369	307
Total	**1,528**	**1,430**
Past due not loans, not impaired, in %	1.00%	1.16%

Past due loans, not impaired, 31 December 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 loans, not impaired, in %	1.05%	1.22%

Table 39 shows past due loans not impaired split by corporate and household customers. Past due loans were for corporate customers end 2009 EUR 1,528m (EUR 1,586m) and for household customers EUR 1,430m (EUR 1,323m). The decrease in past due loans for corporate customers is partly due to an increase in impaired loans.

Figure 15 Annualised net loan losses

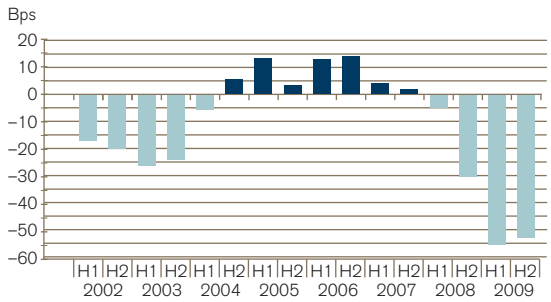


Table 40 Transfer risk exposure

EURm	31 Dec 2009	31 Dec 2008
Asia	1,504	1,512
Eastern Europe and CIS	179	277
Latin America	612	662
Middle East	470	691
Africa	182	175
Total	**2,947**	**3,316**

To recognise the risk related to lending to developing countries, Nordea carries transfer risk allowance and provisions for non-investment grade rated countries. The transfer risk exposure is dominated by a few countries and is primarily short-term and trade-related. China (EUR 644m) and Brazil (EUR 409m) are the countries contributing the highest to transfer risk, reflecting the countries importance for Nordea's Nordic corporate customers. The total transfer risk allowance and provisions at the end of 2009 was 27m, down from 2008 (EUR 58m).

6. Market risk

Nordea's market risk taking activities are well diversified and oriented towards liquid Nordic and European markets. The Group's market risk is to a large extent driven by interest rate risk, and exposure to assets of an illiquid nature is limited.

Value-at-Risk models performed well during 2009 with backtests showing no exceptions.

6.1 Overall description

The customer-driven trading activity of Nordea Markets and the investment and liquidity portfolios of Group Treasury are the key contributors to market risk. 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 policyholders' 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 OJSC Nordea Bank (Russia) is financed in Euro. A 1% decrease in the Russian rouble's exchange rate towards the Euro will cause a decrease in 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 over time. In Nordea this is seen as SIIR (structural interest income risk) and is described in chapter 9.

6.2 Reporting and control process

A 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 exposure 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. Collateralised Debt Obligations (CDOs) and Credit Default Swaps (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 exposure and correlation risk are subject to limits and monitored in the daily control process. See chapter 8 for more specific information about CDOs. 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. 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 decision-making 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.

6.3 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 such as not to 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. For trading activities, the risk appetite and the market risk limits are set in relation to the earnings these activities generate.

6.4 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.

6.4.1 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 the banking book.

VaR is used 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.

6.4.2 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 11.

6.5 Consolidated market risk for the Nordea Group

The consolidated risk for Nordea presented in table 41 includes both the trading book and the banking book. The risk for the trading book only, which forms the predominant part of the basis for the calculation of the minimum capital requirements presented in table 42, is specified in table 44.

The total VaR was EUR 114m (EUR 86m) at the end of 2009 demonstrating a considerable diversification effect between interest rate, equity, credit spread and foreign exchange risk, as the total VaR is lower than the sum of the risk in the four categories.

The total interest rate VaR ended 2009 at EUR 111m (EUR 74m). The total gross sensitivity to a 1 percentage point parallel shift, which measures the development in the market value of Nordea's interest rate sensitive positions if all interest rates were to move adversely, was EUR 375m at the end of 2009 (EUR 212m). The largest part of Nordea's interest rate sensitivity stemmed from interest rate positions in Danish Kroner and Euro, with positions in Norwegian Kroner, US Dollars, Swedish Kronor and Pound sterling also contributing significantly.

At the end of 2009, Nordea's equity VaR stood at EUR 38m (EUR 31m), and structured equity option risk was EUR 17m (EUR12m).

Credit spread VaR ended 2009 at EUR 24m (EUR 30m). Credit spread risk is to a large extent concentrated on Nordic financials.

Table 41 Market risk

Consolidated market risk figures for Nordea Group as of 31 December 2009

EURm	Measure	31 Dec 2009	2009 high	2009 low	2009 avg	31 Dec 2008
Total risk	VaR	114.1	136.4	48.1	87.1	85.8
– Interest rate risk	VaR	111.5	140.2	39.8	82.1	74.4
– Equity risk	VaR	37.5	52.5	6.4	27.2	31.1
– Credit spread risk	VaR	23.8	48.0	23.0	35.1	29.7
– Foreign exchange risk	VaR	18.8	33.9	7.5	21.2	17.2
Diversification effect		41%	63%	29%	48%	44%
Structured equity option risk	Simulation	16.8	24.1	8.8	14.6	12.0
Commodity risk	Simulation	8.9	9.9	1.4	4.4	4.1

The foreign exchange VaR was EUR 19m (EUR 17m) at year-end. The largest foreign exchange exposure is to Danish Kroner.

Nordea's exposure to commodity risk, primarily pulp and paper, is solely related to customer-driven activities. The risk was EUR 9m at the end of 2009 (EUR 4m).

The net asset value of investments in hedge funds was EUR 197m at year-end (EUR 99m), and the fair value of investments in private equity funds was EUR 184m (EUR 143m). Both types of investments are spread over a number of funds.

Market risk associated with the mismatch between policyholders' assets and liabilities in Nordea Life and Pension is analysed separately. The scenario for normal market conditions shows a risk of EUR 9m at the end of 2009 (EUR 59m). The market risk from the internal pension plans is also measured separately.

6.6 Capital requirement 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 standardised approach.

The capital requirement for market risk at the end of 2008 and 2009 is presented in table 42. As seen in the table, 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 Finland Plc. The main part of the market risk RWA is related to business in Nordea Markets. Market risk RWA decreased from EUR 5.9bn to EUR 5.4bn between Q4 2008 and Q4 2009. The decrease is mainly related to decreased VaR contribution to the Group's market risk RWA which decreased from EUR 1.7bn to EUR 1.3bn during the year as a result of both decreased average VaR and a decreased multiplier.

The VaR figures for the trading book that are one part of the basis for table 42 are presented in table 44.

Table 42 Capital requirements for market risk, 31 December 2009

	Trading book, VaR		Trading book, non–VaR		Banking book, non–VaR		Total	
EURm	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement
Interest rate risk[1]	1,529	123	2,268	181			3,797	304
Equity risk	124	10	938	75			1,062	85
Foreign exchange risk	502	40			710	57	1,212	97
Commodity risk			135	11			135	11
Diversification effect	–820	–66					–820	–66
Total	**1,335**	**107**	**3,342**	**267**	**710**	**57**	**5,386**	**431**

1) Interest rate risk in column Trading book VaR includes both general and specific interest rate risk which is elsewhere referred to as interest rate VaR and credit spread VaR

Capital requirements for market risk, 31 December 2008

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

1) Interest rate risk in column Trading book VaR includes both general and specific interest rate risk which is elsewhere referred to as interest rate VaR and credit spread VaR

The following section describes the principles for calculating RWA with the Internal Models Approach and the Standardised Approach respectively. Table 43 presents the methods in use for calculation of capital requirements.

6.6.1 Internal model approach (VaR)

Nordea uses the VaR model to calculate capital requirements for the predominant part of the trading book.

The methods used for calculating capital requirements for market risk for the Group's legal entities are:

Table 43 Methods for calculating capital requirements

EURm	Interest rate risk General	Interest rate risk Specific	Equity risk General	Equity risk Specific	FX risk 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
OJSC Nordea Bank (Russia)	Standard	Standard	Standard	Standard	Standard

IM: Internal model approach, Standard: Standardised approach

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

6.6.2 Backtesting of the VaR-model

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

The Basel multiplier deciding backtest for Nordea's consolidated trading book is holding the 1-day VaR figures against actual profit/loss. As can be seen from figure 16, there were no backtest exceptions in 2009.

6.6.3 VaR in the trading book

Table 44 shows VaR in the trading book.

6.6.4 Standardised approach

The minimum capital requirement for the positions not covered by the VaR model is calculated according to the standardised approach.

The main part of this contribution to market risk required capital is the 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.

Figure 16 Backtest of VaR for the trading book: Profit/loss (actual, excluding commisions) against one-day VaR

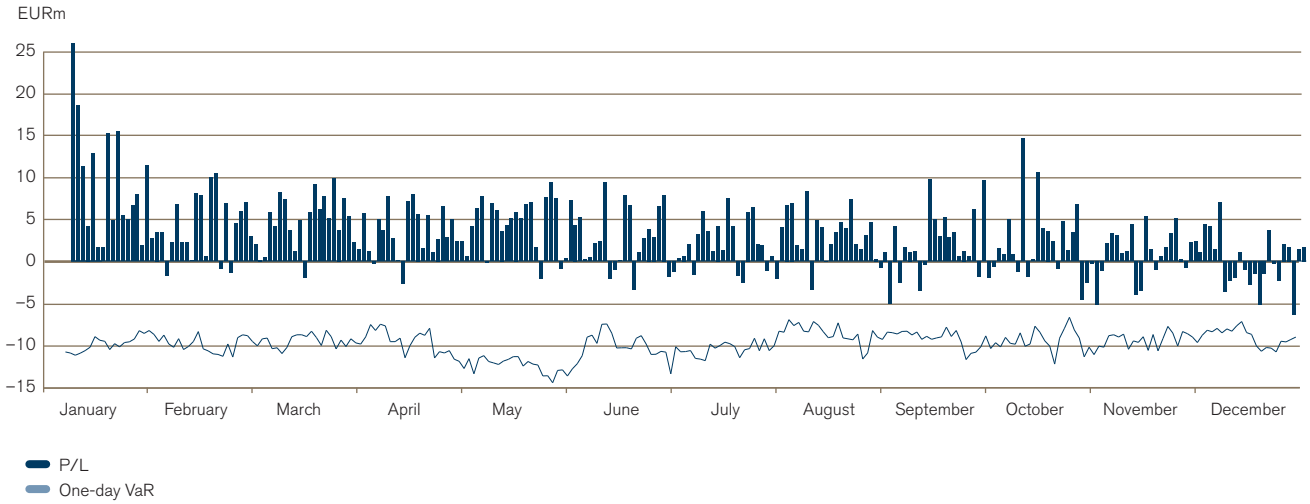


Table 44 Market risk, trading book

Consolidated market risk figures for the trading book ofNordea Group as of 31 December 2009

EURm	Measure	31 Dec 2009	2009 high	2009 low	2009 avg	31 Dec 2008
Total risk	VaR	28.3	45.6	20.8	30.7	32.6
– Interest rate risk	VaR	18.9	44.0	11.1	24.3	20.8
– Equity risk	VaR	3.7	5.6	1.0	2.5	2.3
– Credit spread risk	VaR	13.8	23.5	9.2	14.2	12.2
– Foreign exchange risk	VaR	14.3	25.6	5.0	14.3	15.6
Diversification effect		44%	57%	25%	44%	36%
Structured equity option risk	Simulation	16.8	24.1	8.8	14.6	12.0
Commodity risk	Simulation	8.9	9.9	1.4	4.4	4.1

6.7 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 45 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 2009.

Furthermore, Nordea regularly measures the 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 9 for further details.

Table 45 Interest rate sensitivities for Nordea Group non-trading book 31 December 2009, instantaneous interest rate movements

EURm	+200 bp	+100 bp	+50 bp	–50 bp	–100 bp	–200 bp
DKK	–211.3	–105.6	–52.8	52.8	105.6	211.3
EUR	–333.5	–167.2	–83.4	81.4	161.5	318.6
GBP	–2.0	–1.3	–0.7	1.4	2.5	4.2
NOK	–70.5	–35.2	–17.6	17.6	35.2	70.5
SEK	–70.0	–32.8	–16.5	14.2	27.8	70.0
USD	–64.4	–32.2	–16.0	16.2	32.6	65.3
Total	**–749.9**	**–373.4**	**–186.6**	**183.1**	**364.3**	**738.1**

The totals are netted and include currencies not specified. In accordance with an analysis of account holder behaviour, a portion of non-maturing deposit accounts are assumed to be fixed term. For the majority of products, convexity is ignored.

6.8 Determination of fair value of financial instruments

Financial assets and liabilities classified as financial assets/liabilities at fair value through profit or loss and derivative instruments are recorded at fair value on the balance sheet with changes in fair value recognised in the income statement in the item "Net gains/losses on items at fair value".

Fair value is defined by IAS 32 and IAS 39 as the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The existence of published price quotations in an active market is the best evidence of fair value and when they exist they are used to measure financial assets and financial liabilities. Nordea is predominantly using published price quotations to establish fair value for items disclosed under the following balance sheet items:

- Treasury bills.
- Interest-bearing securities.
- Shares.
- Derivatives (listed derivatives).
- Debt securities in issue (issued mortgage bonds in Nordea Kredit Realkreditaktieselskab).

If quoted prices for a financial instrument fail to represent actual and regularly occurring market transactions or if quoted prices are not available, fair value is established by using an appropriate valuation technique. Valuation techniques can range from simple discounted cash flow analysis to complex option pricing models.

Valuation models are designed to apply observable market prices and rates as input whenever possible, but can also make use of unobservable model parameters. Nordea is predominantly using valuation techniques to establish fair value for items disclosed under the following balance sheet items:

- Treasury bills (when quoted prices in an active market are not available).
- Loans and receivables to the public (mortgage loans in the Danish subsidiary Nordea Kredit Realkreditaktieselskab).
- Interest-bearing securities (when quoted prices in an active market are not available).
- Shares (when quoted prices in an active market are not available).
- Derivatives (OTC-derivatives).

Fair value is calculated as the theoretical net present value of the individual contracts, based on independently sourced market parameters and assuming no risks and uncertainties. This calculation is supplemented by a portfolio adjustment. The portfolio adjustment covers uncertainties associated with the valuation techniques, model assumptions and unobservable parameters as well as the portfolio's counter party credit risk and liquidity risk. The portfolio adjustment for model risk comprises two components:

- Benchmarking of the model output (market values) against market information or against results from alternative models, where available.
- Sensitivity calculations where unobservable parameters are varied to take other reasonable values.

For financial instruments, where fair value is estimated by a valuation technique, it is investigated whether the variables used in the valuation model are fully based on data from observable markets. By data from observable markets, Nordea considers data that can be collected from generally available external sources and where this data is judged to represent realistic market prices. If non-observable data is used, the instrument cannot be recognised initially at the fair value estimated by the valuation technique and any up-front gains are thereby deferred and amortised through the income statement over the contractual life of the contract

The applied valuation models are consistent with accepted economic methodologies for pricing financial instruments, and incorporate the factors that market participants consider when setting a price.

New valuation models are subject to approval by Group Credit and Risk Control and all models are reviewed on a regular basis.

Table 46 shows fair value by valuation method as of 31 December 2009.

Table 46 Determination of fair value from quoted market prices or valuation techniques (Group, excluding Life & Pensions), 31 December 2009

EURm	Quoted prices in active markets for same instrument (Level 1)	Valuation technique using observable data (Level 2)	Valuation technique using non-observable data (Level 3)	Total
Assets				
Loans to credit institutions	37	6,044		**6,081**
Loans to the public		58,376		**58,376**
Debt securities	30,052	10,992	120	**41,164**
Shares	2,984	3	1,418	**4,404**
Derivatives	579	72,482	2,341	**75,402**
Other assets		3,390		**3,390**
Prepaid expenses and accrued income		397		**397**
Liabilities				
Deposits by credit institutions		24,128		**24,128**
Deposits and borrowings from the public		10,625		**10,625**
Debt securities in issue	29,422	6,147		**35,569**
Derivatives	529	70,167	2,285	**72,981**
Other liabilities	15	11,972		**11,987**
Accrued expenses and prepaid income		754		**754**

6.8.1 Group Valuation Committee

The Group Valuation Committee is a forum counting senior management representatives from Group Finance, Group Market Risk Management and from the different Business Division level Financial Control Organisations. The Committee constitutes an oversight committee that supports GEM in issues related to the valuation framework for traded financial instruments. Among its tasks, the Committee prepare proposals, for the Group CFO/ Group CRO on issues of major importance concerning the valuation framework, including governance structure, principles for model risk management, standards for valuation and model risk controls.

Also the Committee is responsible for monitoring the quality and reliability of performed valuations including the quality of valuation processes, the valuation control and model risk control procedures, based on input from GVC members representing individual Business Divisions.

Finally, the Committee receives reporting on standalone valuation adjustments made in the Business Divisions, based on critical judgement, and the Committee constitutes an escalation forum for reviewing and taking final decisions for any such adjustments of significance.

6.8.2 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 instructions 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. The quality control framework is assessed by relevant Group functions as well as by Group Internal Audit on an ongoing basis.

The setup for valuation adjustments 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 OTC derivatives, bid/ask spreads and where judged relevant, also model risk.

A description of critical judgements related to the determination of fair value can be found in Note 1, section 4 in the 2009 Annual Report.

7. Operational risk

Operational risk is inherent in all activities performed by Nordea. Risk management is proportional to the risks in question, and risk mitigation is designed based on the Group's risk appetite. During 2009 a redesigned risk management framework has been implemented in the Group, with enhanced focus on key risks as well as simplified reporting and structured follow-up procedures. This is expected to lead to better management information and added business value.

7.1 Overall description and definition of operational risk

The "Policy for Internal Control and Risk Management in the Nordea Group" states that the management of risks includes all activities aiming at identifying, measuring, assessing, monitoring and controlling risks as well as measures to limit and mitigate consequences of the risks. Management of risks is proactive, emphasising training and risk awareness. The Nordea Group maintains a high standard of risk management by means of applying available techniques and methodology to its own needs in a cost-efficient way.

Operational risk is 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. Operational risk includes compliance risk which means 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 is the risk that the Group suffers damage due to a deficient or incorrect legal assessment. Operational risk is inherent in all activities within the organisation, in outsourced activities and in all interactions with external parties.

7.2 Operational Risk Management and the operating model

Group Operational Risk Management is responsible for developing and maintaining the framework for managing operational and compliance risks, and for supporting the business organisation in their implementation of 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.

Managing operational risk is part of the management's responsibilities. In order to manage these risks a common set of standards and a sound risk management culture is aimed for with the objective to follow best practice regarding market conduct and ethical standards in all business activities.

The Group's network of risk and compliance officers ensures that operational and compliance risk within the Group is managed effectively in the business organisation, which represents the first line of defense. In order to manage these risks Group Operational Risk Management, representing the second line of defense, has defined a common set of standards (Group Directives, processes and reporting) and a sound risk management culture is aimed for with the objective to follow best practice regarding market conduct and ethical standards in all business activities. Group Internal Audit, representing the third line of defense, provides assurance to the Board of Directors on the risk management, control and governance processes.

7.3 Key processes

7.3.1 Risk self assessment

The risk self assessment process puts focus on the key risks, which are identified both through top-down division management involvement and bottom-up reuse of existing information from processes such as quality and risk analyses, product approvals etc. The risks are then scored, assessed and documented in a structured way, and subsequently presented in a risk map for prioritisation of them for mitigating activities. The key risks are prioritised and their mitigating activities are tracked together with the detailed information of the risk.

The divisions' key risks are also presented in a Group risk map. The timing of this process in synchronised with the annual planning process to be able to ensure adequate input to the Group's overall prioritisations.

7.3.2 Internal control

The internal control process aims at ensuring fulfillment of requirements specified in Group directives, reflecting both external and internal requirements on the business. The focus areas are addressed by the business organisation over an extended period of time, and the division result (score) will be commented on and signed off by the division manager, to be subsequently reported to Group Operational Risk Management. The extended time period for answering aims at providing time for actions to be taken by the business to correct substandard matters, thereby making the process an active tool for improvement rather than merely a status report. The results are subsequently aggregated in different dimensions and used as input to the CEO's annual report on internal control.

7.3.3 Other processes

Nordea has developed more task specific risk management processes in three key areas; product approvals, business continuity and ad-hoc changes.

The purpose of the product approval process is to ensure common requirements and documentation in respect of new products as well as material changes to existing products. Approved products are reported on a regular basis.

The business continuity management covers a broad scope ranging from procedures for handling incidents via escalation procedures, to crisis management on Group level. The most important factors governing the business continuity preparedness are the recovery requirements and prioritisations of products and services. As most of the value chains rely on IT applications, disaster recovery plans for technical infrastructure represent a key part of the business continuity planning.

The Quality and Risk Analysis (QRA) is used to analyse risk and quality aspects related to changes on case by case basis, for example new programs or projects, or significant changes to organisation, processes, systems and procedures. In principle, the product approval process described above constitutes a QRA.

7.4 Key reports

7.4.1 Annual report on internal control

The result and comments from the Internal Control process represent the main input. The reporting is provided once per year.

Group Operational Risk Management collects the signed off input from the Divisions, aggregates them to business area level and forwards them to the business area heads for comments. The comments from the business areas are then compiled and, together with comments from a Group perspective, forwarded to the CEO.

The CEO subsequently submits the annual report on internal control to the Group Board.

7.4.2 Semi annual report on operational risks

The semi annual report is the independent report from the risk organisation, and is based on input from risk and compliance officers in the business. The report also closely relates to the risk self assessment process as it requires the risk and compliance officers to comment on the key risks and their mitigating actions as identified in the risk self assessment process.

The report features standard, recurring subjects relating to operational risk and compliance for the risk and compliance officers to comment on, but may also contain specific, ad hoc themes focusing on currently relevant areas. Group Operational Risk Management adds own observations to the final Group report which is submitted to the Risk Committee, GEM, and the Board of Directors.

7.4.3 Incident reporting

The incident reporting reflects Basel II standards and ensures compliance with ORX (an international database for incidents) requirements.

The process of reporting incidents is divided into a two-tiered process, with one business specific part where business have the flexibility to adjust it to its specific needs, and one Group related part where the incidents are reported from the business to Group Operational Risk Management. Key aspects of the process include major and minor incidents being reported in the same way (albeit with different level of detail required), and both the identifier of the incident and the risk and compliance officer reporting different parts of the incident information to ensure consistent quality.

Aggregated incident reports are submitted to the every Risk Committee meeting, and key observations are included in the semi-annual report on operational risk.

7.5 Capital requirement for operational risk

The capital requirement for operational risk is calculated mainly 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 gross income for each business line. The basic indicator approach is used for some subsidiaries, such as the subsidiaries in Luxembourg, Russia and Poland. The capital requirement (end 2009) for operational risk amounts to EUR 1,057m (EUR 952m). The capital requirement for operational risk is updated on a yearly basis.

8. Securitisation and credit derivatives

Nordea has no exposure where capital requirement is calculated according to the current securitisation framework. In this chapter, Nordea's securitisation activities and related SPEs are described. These are included in the credit or market risk calculations.

Nordea is an active intermediary in the credit derivatives market for Nordic names, but activity levels in synthetic securitisations remain low.

8.1 Introduction

Banks might have positions that normally are defined as securitisation positions. A securitisation position occurs whenever Nordea is 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 Special Purpose Entity (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. Traditional securitisations where Nordea acts as sponsor for the SPE are described in further detail in section 8.2. Synthetic securitisations and other types of securitisations are described in section 8.3.

8.2 Traditional securitisations where Nordea acts as sponsor

Traditional securitisations where Nordea transfers assets to a SPE are consolidated in the Group accounts and are treated as any other subsidiary for capital adequacy purposes. The assets in the SPEs are included in the banking book and the capital requirement is calculated in accordance with the IRB approach described in chapter 5.

In addition to SPEs to which Nordea has transferred assets, Nordea has set up a limited number of SPEs where Nordea acts as sponsor for the SPE. These SPEs have either been set up for enabling investments in structured credit products or for acquiring assets from customers. At year end 2009, Nordea is the sponsor of the following SPEs presented in table 47.

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- and 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.

The SPEs in table 47 are not consolidated for capital adequacy purposes. Instead, loans and loan commitments to the SPEs are included in the banking book and capital requirement is calculated in accordance with the rules described in chapter 5, as these claims are not subordinated or part of the tranche structure of the SPE. Bonds and notes issued by the SPE and held by Nordea are reported in the trading book and capital requirement is calculated in accordance with the rules described in chapter 6. These bonds and notes are tranched but the capital requirement is calculated as for any other bonds and notes in the trading book in accordance with the current CRD rules. Derivatives with the SPEs are also included in the trading book, with the counterparty risk calculated in accordance with the rules in section 5.2.7. As the capital requirement for market risk is based on the total risk position, it is not meaningful to calculate separate RWAs for individual positions in the trading book. More information on the different SPEs can be found below.

8.2.1 Entities issuing structured credit products

Nordea gives investors an opportunity to invest in different types of structured credit products such as CDOs 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.

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 2009 the total notional of outstanding bonds was EUR 32m (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 13m (EUR 12m) as of year end 2009. 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 6 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 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

Table 47 Special Purpose Entities where Nordea is the sponsor

EURm			Accounting treatment	Book	Nordea's investment[1]	Total assets
CMO Denmark A/S	Collateralised Mortgage Obligation	>5 years	Consolidated	Trading	13	32
Kalmar Structured Finance A/S	Credit Linked Note	>5 years	Consolidated	Trading	34	144
Viking ABCP Conduit	Factoring	<1 year	Consolidated	Banking	478	529
Total					**525**	**705**

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

the derivative transactions. The total notional of outstanding CLNs in this category was EUR 144m (EUR 142m) at year end 2009. Nordea holds CLNs issued by the SPE as part of offering a secondary market for the notes. The investment amounted to EUR 34m (EUR 25m) at year end 2009. Nordea includes the CLN holdings and derivative positions with the SPEs in the capital requirement calculations. The RWA and capital requirement of the CLN holdings are included within the market risk framework of Nordea's trading book, see chapter 6 for further information. The counterparty risk in the derivatives translates to a RWA of EUR 1m, included within the credit risk framework of Nordea's banking 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. During 2009, Nordea terminated all outstanding claims on Mermaid and consequently no RWA is calculated for Mermaid as per 31 December 2009.

8.2.2 Securitisations of customer assets

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 955m and at year end 2009, EUR 478m (EUR 733m) were utilised. There is no outstanding CP issue at year end 2009. The credit facility results in an original exposure of EUR 663m and a RWA of EUR 335m, which is included within the credit risk framework of Nordea's banking book, see chapter 5 for further information.

8.3 Synthetic securitisations and other credit derivatives

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 CDOs. Typical derivative products are single name credit default swaps and synthetic CDOs.

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. Counterparties 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 48 and table 49 lists the total outstanding volumes of credit default swaps and CDOs at the end of 2009, 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 integrated in Nordea's consolidated market risk management and as such subject to:

- Limits, including VaR, jump-to-default and correlation risk
- The product and transaction approval process

Also 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 48 Credit default swaps, 31 December 2009

EURm	Total gross notional sold	Total gross notional bought
Single name CDS: Investment grade	15,302	15,059
Single name CDS: Non-Investment grade	7,804	7,715
Multi name CDS indices	11,856	12,590
Total	**34,962**	**35,364**

Table 49 Collateralised Debt Obligations (CDO) – Exposure (excl NLP)[1]

Notionals EURm	Bought protection	Sold protection
CDOs, gross	4,308	3,574
Hedged exposures	2,928	2,928
CDOs, net[2]	**1,380[3]**	**646[4]**
Of which:		
– Equity	259	285
– Mezzanine	237	204
– Senior	884	157

1) First-To-Default (FTD) swaps are not classified as CDOs and are therefore not included in the table. Net bought protection amounts to EUR 116m and net sold protection to EUR 105m. Both bought and sold protection are entirely investment grade.
2) Net exposure disregards exposure where bought and sold tranches are completely identical in terms of reference pool attachment, detachment, maturity and currency.
3) Of which investment grade EUR 1,380m and sub investment grade EUR 0m.
4) Of which investment grade EUR 646m and sub investment grade EUR 0m.

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

9. Liquidity risk and Structural Interest Income Risk

Nordea has during 2009 continued to benefit from its focus on prudent liquidity risk management, reflected by diversified and strong funding base. The Group, supported by its well recognised name and strong rating, has had access to all relevant financial markets and has been able to actively use all its funding programmes. Nordea issued approximately EUR 27bn in long-term debt during 2009 excluding Danish covered bonds

Extensive discussions on a new liquidity risk regulation are ongoing among regulators. Nordea is tightly participating the discussions on several forums and is well prepared for potential changes. Chapter 13 is discussing the new regulation in more detail.

9.1 Liquidity risk

9.1.1 Management principles and control

The Board of Directors of Nordea has the ultimate responsibility for Asset and Liability Management of the Group, i.e. limiting and monitoring the Group's structural risk exposure. Risks 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 as well as the principles for pricing the liquidity risk.

9.1.2 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 Paper programs in France and Sweden, Certificates of Deposits) and long-term (Swedish and Danish Covered bonds, European Medium Term Notes, Swedish Medium Term Notes and US Medium term notes) in diverse currencies. However, foreign exchange risk is covered. In table 50, the funding sources are presented. As of the end of 2009, the total utilised volume of short-term programs was EUR 53bn with the average maturity of 0.4 years and the total volume of the long-term programs is EUR 77bn with the average maturity of 7.8 years. During 2009 Nordea increased the proportion of long-term funding as the volume of long-term programs grew by EUR 12bn. The volume of short-term programs increased by EUR 9bn. Special focus is given for the composition of the investor base in the terms of geographical range and rating sensitivity. Nordea publishes periodically 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's 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. Nordea's stress tests cover both idiosyncratic and market wide scenarios, as well as the combination of these. Group Treasury is responsible for managing the liquidity and for compliance with the group-wide limits from the Boards of Directors, CEO in GEM and ALCO.

Table 50 Funding sources, 31 December 2009

Liability type	Interest rate base	Average maturity	EURm
Deposits by credit institutions			
– shorter than 3 months	Euribor etc	0.1	46,721
– longer than 3 months	Euribor etc	0.8	5,468
Deposits and borrowings from the public			
– Deposits on demand	Administrative	0.0	101,359
– Other deposits	Euribor etc	0.3	52,218
Debt securities in issue			
– Certificates of deposits	Euribor etc	0.4	40,636
– Commercial papers	Euribor etc	0.4	12,586
– Mortgage covered bond loans	Fixed rate, Market based	9.9	54,785
– Other bond loans	Fixed rate, Market based	2.7	22,512
Derivatives		n.a.	73,043
Other non-interest-bearing items		n.a.	34,779
Subordinated debentures			
– Dated subordinated debenture loans	Fixed rate, Market based	5.8	5,000
– Undated and other subordinated debenture loans	Fixed rate, Market based	n.a.	2,185
Equity			22,420
Total (total liabilities and equity)			**473,713**
Liabilities to policyholders			33,831
Total (total liabilities and equity) including Life insurance operations			**507,544**

9.1.3 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 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.

9.1.4 Liquidity risk analysis

The short-term liquidity risk has been held at moderate levels throughout 2009. The average funding gap risk, i.e. the average expected need for raising liquidity in the course of the next 14 days, has been EUR –9.4bn (EUR –8.7bn). Nordea's liquidity buffer has been in the range EUR 34.6– 59.3bn (EUR 20.1–40.2bn) throughout 2009 with an average of EUR 45.7bn (EUR 27.1bn). 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 96% of central bank eligible securities at the end of 2009. By utilising the liquidity buffer, Nordea is able to secure its funding requirements for more than one year without access to new market funding. The aim of always maintaining a positive net balance of stable funding has been comfortably achieved throughout 2009. The yearly average for the net balance of stable funding was EUR 16.9bn (EUR 8.0bn). The net balance of stable funding is shown in table 51.

Table 51 Net balance of stable funding, 31 December 2009

Stable liabilities and equity

Liability type	EURbn
Equity and Core Liabilities	
Deposits and borrowings from the public	125.4
Equity	22.4
Structural funding	
Long term deposits from credit institutions	6.9
Long CD and CP	1.9
Long term bonds issued	50.4
Other structural funding	3.9
Total stable liabilities	**210.9**

Stable long-term assets

Asset type	
Core assets	
Loans to the public	177.6
Long term loans to credit institutions	5.8
Illuiquid assets	5.0
Total stable long-term assets	**188.4**
Net balance of stable funding (NBSF)	**22.5**

9.2 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.

9.2.1 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 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.

9.2.2 SIIR analysis

At the end of the year, the SIIR for decreasing market rates was EUR –191m (EUR –218m) and the SIIR for increasing rates was EUR 148m (EUR 55m). These figures imply that net interest income would decrease if interest rates fall and increase if interest rates rise.

Table 52 Re-pricing gap analysis, 31 December 2009

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									
Interest bearing assets	392,722	283,649	18,277	13,076	11,352	9,188	22,145	35,033	392,722
Non interest bearing assets	114,822	0	0	0	0	0	0	114,822	114,822
Total assets	**507,544**	**283,649**	**18,277**	**13,076**	**11,352**	**9,188**	**22,145**	**149,856**	**507,544**
Liabilities and equity									
Interest bearing liabilities	343,470	251,699	13,871	17,085	15,114	24,163	18,218	3,320	343,470
Non interest bearing	164,074	0	0	0	0	0	0	164,074	164,074
Total liabilities and equity	**507,544**	**251,699**	**13,871**	**17,085**	**15,114**	**24,163**	**18,218**	**167,394**	**507,544**
Off-balance-sheet items, net		**–22,706**	**511**	**249**	**3,552**	**14,999**	**3,394**	**0**	
Exposure		**9,244**	**4,918**	**–3,759**	**–209**	**24**	**7,321**	**–17,539**	
Cumulative exposure			**14,162**	**10,402**	**10,193**	**10,218**	**17,539**	**0**	

10. Risk and Capital in the Life operation

The nature of life insurance leads Nordea Life and Pensions (NLP) to take risks that are quite different to those addressed in the bank. However, the largest risk in NLP is still the market risk. It is worth noting, that it is easier for a life and pensions company to quickly adjust the risk exposure by changing the asset allocation than it is to change risks in the credit portfolio in a bank.

2009 has been a turbulent year for life insurers throughout the world. The large reductions in equity prices during the spring have been followed by an enormous rush in the markets during the last three quarters. The impact of reduced interest rates has affected both asset values and liabilities. At the end of 2009, Nordea has managed to achieve an improved capital base, almost double the financial buffers and increased returns to a high stable level.

10.1 Risk and capital management principles and control

10.1.1 Legal structure

NLP is comprised of Nordea Life Holding AB and its subsidiaries and is 100% owned by Nordea Bank AB (publ).

The market risk for Nordea Bank AB's account is subject to a limit suggested by the CEO in GEM following a discussion in Nordea ALCO. The limit is set by the Board of Directors of Nordea Life Holding AB.

10.1.2 Internal risk governance

It is the responsibility of NLP Group Risk Management to formulate the risk management policy of NLP, consolidate the market risk, control limit utilisation and provide the market risk reporting to NLP Group management as well as country CEOs and CIOs.

NLP reports solvency levels and scenario-based P/L and financial buffer sensitivities on a weekly basis. Additionally, NLP reports the solvency levels, the scenarios-based P/L and financial buffer sensitivities to internal risk functions.

The market risk in the separated equity capital investment is measured daily according to the Nordea VaR methodology.

Solvency ratios for Nordea Life Holding AB are measured on a monthly basis and reported to the regulators. ALM issues are reported quarterly to the Group ALCO, while P/L risk and VaR of the separated equity capital are reported regularly to GEM and Group Board.

For local NLP entities, the local Board of Directors decide annually the risk limits for the P/L, solvency capital and financial buffers and in addition the investment strategy, the neutral asset allocation and deviations expressed as maximum and minimum boundaries. Nordea ALCO receives the investment strategy for recommendation before approval by the Boards.

It is the responsibility of the country-specific finance and control functions to monitor if regulatory requirements, risk limits and national asset allocation investment guidelines are within the specified national Boards' limits. If limits are exceeded, country and NLP Group CFO, CIO, CRO and CEO as well as the local Boards are informed.

10.2 Key risks in Nordea Life & Pensions

10.2.1 Market risk

The market price risk is the risk of loss in P/L as a result of movements in market rates and prices (e.g. interest and FX rates, equity and commodity prices, volatilities) that affect the value of Nordea's positions. For simplicity, in Nordea the term 'market risk' is used as a synonym for market price risk.

Market risks are measured according to two different approaches. The first is a scenario-based risk measure similar to the various traffic light methods use by the FSA's. The other approach is a VaR approach simulating the market risk in the separated equity capital investment.

10.2.2 Life insurance risk

Life insurance risk is the impact from changes in mortality rates, longevity rates and disability rates. The sensitivity on the financial accounts from these risks is shown in table 53.

10.2.3 Other risks

Other risks include insurance risk, credit risk and operational risk.

Table 53 Life insurance risk and market risks in the Life insurance operations

Sensitivites EURm	31 Dec 2009 Effect on policyholders	31 Dec 2009 Effect on Nordea's own account	31 Dec 2008 Effect on policyholders	31 Dec 2008 Effect on Nordea's own account
Mortality - increased living with 1 year	–124	–21	–94	–8
Mortality - decreased living with 1 year	126	23	81	7
Disability - 10% increase	–24	–4	–36	0
Disability - 10% decrease	24	4	35	0
50 bp increase in interest rates	–70	0	–183	–1
50 bp decrease in interest rates	–20	0	122	0
12% decrease in all shareprices	–217	–8	–103	–7
8% decrease in property value	–236	–6	–177	–29
8% loss on counterparts	–154	–10	–144	–6

10.3 Asset Liability Management (ALM)

The ALM aims at creating long-term value of NLP and at the same time optimise the rate of return to policyholder given a specific level of risk. The ALM square of NLP has been recognised as a mindset, meaning that the elements of value and risk given by the four corners (P/L, economic value & capital, legal requirements and market return) are taken into consideration when making management decisions or determine the ALM of NLP.

10.3.1 Guaranteed return

Due to strong sales in Unit Link policies (no guarantees) in 2009 the arithmetic average guarantee is reduced from 1.92% in 2008 to approximately 1.76% in 2009.

Table 54 Assets and liabilities, 31 December 2009

Assets	EURm
Investment properties	3,486
Shares	7,990
Alternative investments	2,377
Debt Securities - At fair value	18,707
Debt Securities - HtM	1,875
Deposits and treasury bills	4,660
Other assets	1,583
Total assets	**40,679**

Liabilities	EURm
Traditional provisions	21,166
Collective bonuspotential	1,434
Unit linked provisions	4,480
Investment contracts	6,178
Other insurance provisions	574
Other liabilities	5,134
Shareholders equity	836
Subordinated loans	878
Total liabilities	**40,679**

Table 55 Liabilities to policyholders divided in guarantee levels (technical interest rate)

31 Dec 2009 EURm	non	0 pct.	0 to 3 pct.	3 to 5 pct.	Over 5 pct.	Total liabilities
Technical provision	7,047	4,196	10,612	9,791	178	31,823

31 Dec 2008 EURm	non	0 pct.	0 to 3 pct.	3 to 5 pct.	Over 5 pct.	Total liabilities
Technical provision	4,351	4,091	9,823	9,496	160	27,919

Insurance claims provisions are EUR 395m in 2009 and EUR 362m in 2008

10.3.2 Investment return

Investment returns performance is only relevant for the traditional business because it is NLP that decides upon the asset allocation in both a strategic and tactical perspective.

Table 56 Investment return, traditional life insurance, 31 December 2009

EURm	Assets under management	Investment return
Interest bearing securities and deposits	19,513	6.7%
Shares	2,392	24.1%
Alternative investments	2,358	–2.3%
Investment property	3,401	3.6%
Total	27,664	6.4%

All figures are consolidated from the different life companies.

10.4 Market Consistent Embedded Value (MCEV)

The Market Consistent Embedded Value model (MCEV) is a stochastic dividend-stream model projecting the future developments in a large number of scenarios through Monte Carlo simulation. The model calculates the dividend stream to the shareholder in each scenario and derives the Economic Value (EV) for the shareholder in each scenario by finding the net present value of the dividend stream by discounting using relevant discount factors relevant for the specific scenario. Having run a large number of Monte Carlo simulations and knowing the EV in each scenario, the model draws up the probability distribution of EV for the company. The MCEV is defined as the average of this distribution and is calculated as the simple mean of the scenario-specific EVs.

The development of the MCEV during 2009 was largely impacted by changes in the expected financial-market outlook given the current low level of the interest rate curves and given the history of low equity return.

Table 57 MCEV development during 2009

	31 Dec 2009			31 Dec 2008		
EURm	Traditional	Unit Linked	Total	Traditional	Unit Linked	Total
Denmark	1,104	149	1,253	931	109	1,040
Finland	476	327	803	426	222	648
Norway	582	80	661	443	115	558
Poland	13	199	212	34	174	171
Sweden	–2	316	314	13	158	208
Total	**2,173**	**1,071**	**3,244**	**1,847**	**777**	**2,624**

Table 58 Financial buffers

	Financial buffers		% of guaranteed liabilities	
EURm	31 Dec 2009	31 Dec 2008	31 Dec 2009	31 Dec 2008
Denmark	448	157	3.4%	1.2%
Norway	127	32	3.1%	1.0%
Sweden	344	99	19.1%	6.0%
Finland	515	384	12.6%	8.7%
Total	**1,434**	**673**	**6.1%**	**3.0%**

10.5 Financial Buffers

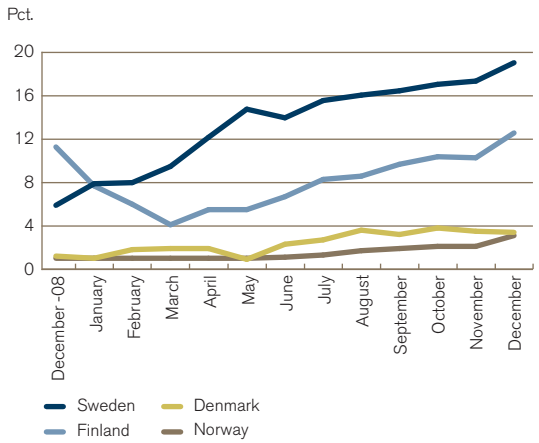
The level of financial buffers is crucial for the traditional life insurance business. The financial buffers express the policyholders' potential for bonus on top of the guaranteed benefit or yield. For the shareholders, the financial buffers are important due to the fact that they are a P/L protection against poor investment return, crediting and/or low return environments.

For NLP a moderate financial buffer level is almost equal to stabile P/L due to the mostly fee-based business models. However, at low financial buffer levels higher P/L volatility is expected.

10.5.1 Development of financial buffers

After reaching an all time low financial buffer levels by end March 2009 the situation has improved considerably, with buffers almost doubling compared to the beginning of 2009. The improvement comes from a robust investment return combined with a conservative crediting rate.

Figure 17 Financial buffers



11. ICAAP

The financial turmoil has increased the focus on banks' internal capital evaluation processes and their capability to asses the solvency need to cover losses and other cyclicality effects that arise in an economic downturn. In spring 2009, Nordea demonstrated the strength of its capital management by executing a successful rights issue. During 2009 financial supervisors and central banks have performed several stress tests of the Nordea Group and its peers. The result of the stress test clearly shows that the Nordea Group is well capitalised.

The regulators agreed that Nordea was adequately capitalised given its risk profile and portfolio, in accordance with the 2009 ICAAP and SREP process.

11.1 The process

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

The ICAAP is a continuous process within Nordea which contributes to increased awareness of Nordea's capital requirements and exposure to material risks throughout the organisation, in both the business area and legal entity dimensions. Stress tests are an important driver of the increased risk awareness, looking at capital and risk from a firm-wide perspective or, on an ad-hoc basis, on more specific areas or segments. The process includes a regular dialogue with Nordea's supervisors, rating agencies and other external stakeholders with respect to capital management, measurement and mitigation techniques used within Nordea.

The capital ratios and capital forecasts for the Nordea Group and its legal entities are followed up quarterly by Group Risk Modelling within Group Corporate Centre and are reported to the Capital Planning Forum and the Board of Directors, on group, subgroup as well as legal entity level. On an annual basis the ICAAP is thoroughly reviewed and documented and ultimately decided on by the Board of Directors.

11.1.1 Capital planning and Capital policy

The capital planning process includes a forecast of the development of the capital requirement, e.g. the pillar 1 capital requirement, and the available capital, e.g. measured as capital base, tier 1 or core tier 1 capital. The capital planning is based on key components of Nordea's rolling financial forecast, which includes lending volume growth by customer segment and country as well as forecasts of net profit including assumptions of future loan losses. The capital planning process also consider forecasts of the state of the economy, to reflect the future impact of credit risk migration on the capital situation of Nordea Group and its legal entities. An active capital planning process ensures that Nordea is prepared to make necessary capital arrangements regardless of the state of the economy.

Nordea's capital policy constitutes a major component of Nordea's ICAAP and as such has a key role in the capital planning. The capital policy is designed with consideration given to the internal capital requirements defined using a "pillar 1 plus pillar 2" approach. This methodology uses the pillar 1 capital requirements for credit risk, market risk and operational risk as outlined in the legislation as the starting point for its risk assessment. In the next step pillar 2 risks, risks not included in pillar 1, are considered using internal capital models to define the capital requirement. The capital policy states target capital ratios over a business cycle. The targets for tier 1 ratio and capital ratio are shown in table 59. The current capital position in relation to the capital policy is described in chapter 4.

Table 59 Nordea Group capital targets, 2009

	Target over the cycle
Tier 1 ratio	9,0%
Capital ratio	11,5%

Additional policies are in place reflecting Nordea's target capital allocation in terms of core tier 1, tier 1 hybrid instruments and tier 2 capital. The policies also define the internal process for combining the capital policy and capital planning to ensure that Nordea is adequately capitalised and that capital decisions are made in a timely manner.

The Capital Planning Forum is responsible for interpreting the capital plans of the Group and its legal entities and ensuring that each entity upholds its respective capital policies and/or minimum requirements.

11.2 Components of ICAAP

As described above, Nordea uses a "pillar 1 plus pillar 2" approach in determining its internal capital requirement. Therefore, a key component of Nordea's ICAAP is the pillar 1 capital requirement as shown in section 4.3. Nordea uses its economic capital framework to identify and assess risks that are not covered within pillar 1 of the CRD, so called pillar 2 risks, and as its primary tool for internal capital allocation considering all risk types. Another

important component of assessing capital adequacy is stress testing. Nordea stress tests both pillar 1 and pillar 2 risks and the stress tests are considered when determining Nordea's internal capital requirement. By considering the stress test results in the assessment of internal capital requirements the pro-cyclical effects inherent in the risk adjusted capital calculations of the economic capital and IRB approaches are addressed.

11.2.1 Economic capital

Since 2001, Nordea's economic capital framework has included the following major risk types:

- Credit risk
- Market risk
- Operational risk
- Business risk
- Life insurance risk.

Pillar 1 of the of the Basel II framework closes the gap between regulatory capital and economic capital by improving the risk sensitivity of regulatory capital measurement, but still several differences remain, since economic capital covers both pillar 1 and pillar 2 risks and economic capital also includes risks in the insurance business of the group. The primary differences between economic capital and the capital requirement according to the legislation are described in appendix 14.5.

As of end 2009 the total diversified economic capital equals EUR 14.1bn and Figure 18 shows the economic capital distributed by business area and risk type. Notably the credit risk accounts for 69% of the total economic capital. The diversification effect was 16%, reducing the total economic capital by EUR 2.6bn. During 2009, the EC increased with 10%, largely explained by changes in the economic capital framework as of 1st of January 2009 as well as by an increase in credit risk.

Changes to the economic capital framework

As a consequence of the financial turmoil, the focus has shifted towards building capital analysis on regulatory capital requirements rather than the result of internal capital models (economic capital). Due to the shift in focus and to ensure that each customer unit within Nordea is correctly charged for the actual capital consumption, Nordea has decided to further align the economic capital framework to the regulatory capital framework, with effect in the beginning of 2010.

This alignment provides a framework that links capital allocation to Nordea's internal capital requirement and targets, as described in Nordea's capital policy, and supports capital efficiency within the Group.

The alignment implies the following material changes to the economic capital framework for 2010:

- Credit risk – The calculation of economic capital for credit risk calculation in EC will in general be aligned to regulatory capital. This implies that the significant part of the corporate and institution exposure will be calculated according to the Foundation IRB approach, i.e. the internal estimates of LGD and CCF will be replaced by the regulatory values. However, in order to keep a risk differentiated measure within the economic capital framework, those corporate and institution portfolios not yet approved for Foundation IRB will be calculated as if they were approved. Moreover, an improved model for sector concentration risk will be used in the economic capital framework for 2010.
- Market risk – Economic capital for market risk will be based on the same VaR model and assumptions as used in the calculation for market risk in regulatory capital. The change results in a more conservative approach in the Expected Tails Loss technique.
- Operational risk – Economic capital for operational risk will be calculated in the same manner as the regulatory capital for operational risk. As a result of the alignment to regulatory capital the operational risk capital will be calculated on a yearly basis instead of a quarterly basis and calculated based on a three year average.

Figure 18 EC distributed by risk type

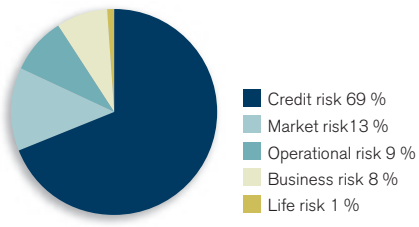
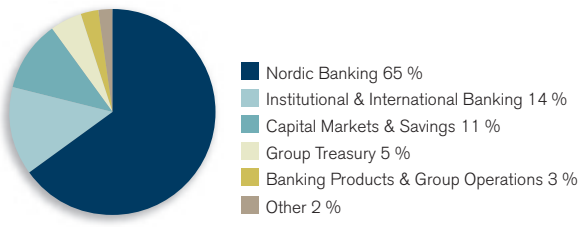


Figure 18 EC distributed by customer area



In total, the economic capital will increase because the internal estimates of credit risk parameters LGD and CCF are, on average, lower than the estimates used under the Foundation IRB approach.

11.2.2 Stress tests

The financial turmoil has increased the focus on stress tests and banks ability to mange a severe economic downturn, facing high levels of losses and other cyclicality effects.

During 2009 Nordea has performed several internal stress tests in order to evaluate general effects of an economic downturn as well as effects for specifically identified high risk areas. In addition to the internal stress tests, Nordea Group has been part of external stress tests performed by financial supervisors, central banks and equity analysts. The results clearly show that the Nordea Group is well capitalised and will manage periods of economic stress. This demonstrates the strength of Nordea's capital planning and its ability to asses a sufficient need of capital.

As a part of the ICAAP and the capital planning process, internal firm wide stress tests are used as an important risk management tool in order to determine how severe unexpected changes in business and macro environment will affect the capital need. The stress test reveals how the capital need varies during a stress scenario, where impact on financial statements, regulatory capital requirements, economic capital and capital ratios occur.

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

- Scenario development and translation
- Calculation
- Analysis and reporting

In addition to the firm wide stress tests which cover all risks defined in the economic capital framework, Nordea is performing several stand alone stress tests for each risk type such as market risk, liquidity risk as well as risks in the insurance business. See chapter 6, 9 and 10 for more details.

11.2.2.1 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 design of the stressed scenarios is performed by experts within Nordea Economic Research division in each Nordic country. In addition to the stress scenarios Nordea uses its 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 a complex macro economic scenario which involves estimates of several macroeconomic factors, the ad-hoc stress tests are based on direct estimates of risk parameter changes or based on 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 scenario is translated into an impact on the parameters listed in table 60.

Table 60 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

11.2.2.2 Calculation

The stressed figures and parameters from the scenario are used to calculate the effect on the regulatory capital requirements, economic capital and the financial statements. 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 are aggregated into total capital requirement figures.

Economic capital with the stressed parameters is calculated for credit risk, market risk, operational risk, business risk and life risk according to the economic capital framework. The calculation for each risk type is aggregated into total economic capital 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 components. The capital base is set in relation to the regulatory capital or economic capital in order to calculate the effect on capital ratios during a stress scenario.

11.2.2.3 Analysis and reporting

The first level of reporting in Nordea is the Capital Planning Forum, which reviews the details of the stress tests and implications on future capital need. The finalised results showing the implications of the stress tests on the adequacy of existing capital are distributed to GEM and the Board of Directors. A similar governance process is used for the sub groups and legal entities.

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 stressed or similar events occurring. Business area involvement in defining and assessing the stress tests is seen as important to increase the risk awareness throughout the organisation and the understanding of the relation between capital requirement and exposure to material risks.

During 2009 the turbulence in the financial markets has continued. In order to evaluate the effect of continued turbulence, Nordea actively works with stress tests as a part of the capital planning process. The stress tests generally take a firm-wide perspective, but special focus areas are addressed on an ad-hoc basis, e.g. exposure against the Baltic countries which has been seen as a high risk exposure in today's economic situation. The stress tests are reproduced as soon as new forecasts are defined which will affect Nordea's portfolio such as changes in lending growth, rating distribution, collateral coverage, loan losses and defaulted customers.

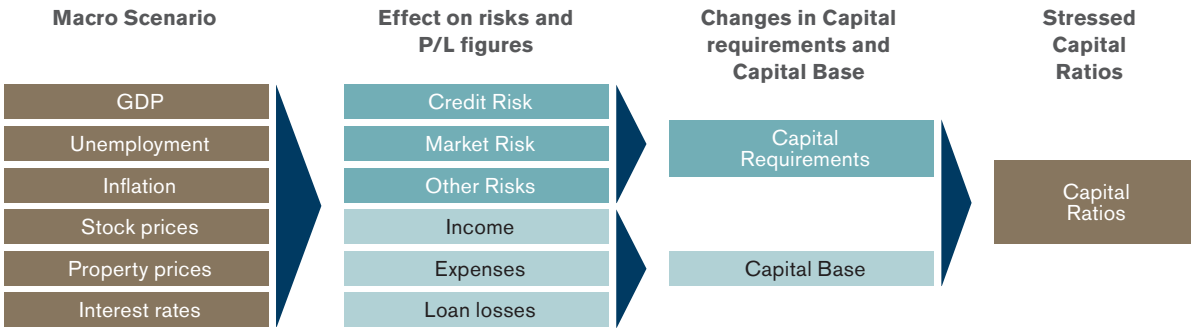
The outcome of the stress tests demonstrates how Nordea's loan loss and capital ratios will change during a stress scenario. The outcome is then analysed in order to decide the capital need during a downturn period and ensure that Nordea is well capitalised.

11.2.3 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 perspective of regulators and supervisors.

Heading into 2010, Nordea will review the capital situation closely and maintain its open dialogue with various supervisory authorities.

Figure 19 Calculation process



12. Capital base components

The quality of banks' capital bases has been very much in focus last years due to the global financial crisis. Nordea has during 2009 strengthened the capital base through the rights issue and the issuance of a USD-denominated hybrid capital loan. The increase in retained earnings during 2009 has also contributed to the positive development in the core tier 1 capital. Nordea distributed 19.4% of the net profit in 2008 to its shareholders and has deducted 43.5% of net profit in the capital base by end 2009, in accordance with the proposed dividend. Nordea can be considered as well capitalised and with a capital base of high quality. Currently, Nordea has only a limited portion of hybrids, 9.3% of tier 1 capital.

12.1 Capital base

The calculation of the capital base is done in accordance with the CRD and the Swedish legislation. The size of the capital base must as a minimum correspond to the sum of the capital requirement for credit risks, market risks and operational risks. Only capital contributed by companies within the financial group and by the consolidated accounts are included in the capital base (e.g. capital in the insurance companies are not included in the capital base of the financial group). Items included in the capital base should without restrictions or time constraints be available for the institution to cover risk and absorb potential losses. All amounts are included net of any tax charge.

The capital base has been affected positively by the rights issue during the first half of 2009 and also by the net profit for the year. As a result of the rights offering, the num-ber of ordinary shares increased to 4,030,167,751 shares and the share capital increase by EUR 1,430,059,524 to EUR 4,030,167,751. The total net proceeds of the rights offering amounts to about EUR 2.5bn, which affects the paid up capital and share premium items in the capital base. The impact on the capital ratios were approximately 1.5% as of December 31, 2009.

Profit for the year is included in the tier 1 capital and the proposed dividend are included as a separate item deducted within the tier 1 capital.

During the third quarter, Nordea Bank AB (publ) issued a USD-denominated tier 1 hybrid instrument of USD 1bn, priced at a coupon of 8.375% (which approximately corresponds to Euro Libor plus five percent). The impact on the capital ratios were approximately 0.9% as of December 31, 2009.

A summary of items included in the capital base is available in table 61.

The total capital base (referred to as own funds in the CRD) is the sum of tier 1 capital (called original own funds in the CRD) and tier 2 capital (called additional own funds in the CRD) after deductions 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. Different ratios are based on different capital base items, such as:

- The core tier 1 capital ratio is calculated by dividing the tier 1 capital less hybrid capital with risk weighted amounts.
- The tier 1 capital ratio is calculated by dividing the tier 1 capital with risk weighted amounts.
- The capital ratio is calculated by dividing the capital base with risk weighted amounts.
- The capital adequacy quotient is calculated from the capital base in relation to the capital requirement.

Below is a detailed description of the items included in the capital base.

12.2 Core tier 1 capital and tier 1 capital

Core tier 1 capital is defined as eligible capital including eligible reserves and net of regulatory required deductions done directly to the tier 1 capital. The capital recognised as core tier 1 capital, holds the ultimate characteristics for loss absorbance defined from a going concern basis and are the most subordinated claim in terms of liquidation.

The tier 1 capital is defined as capital of the same or close to the character of eligible capital and eligible reserves. The tier 1 capital can also include a limited part (up to 30% of tier 1) of hybrid capital loans (perpetual loans). Deductions mandatory for tier 1 capital will accordingly also be required as deduction in defined core tier 1 capital.

12.2.1 Eligible capital

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

12.2.2 Eligible reserves

Eligible reserves consist primarily of retained earnings, other reserves, minority interest and income from current year. Retained earnings 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.

Table 61 Summary of items included in capital base

EURm	31 December 2009	31 December 2008
Calculation of total capital base		
Original own funds		
Paid up capital	4,037	2,600
Share premium	1,065	
Eligible capital	**5,102**	**2,600**
Reserves	14,389	12,157
Minority interests	11	11
Income (positive/negative) from current year	2,313	2,671
Eligible reserves	**16,713**	**14,839**
Tier 1 capital (before hybrid capital and deductions)	**21,815**	**17,439**
Hybrid capital loans subject to limits	**1,811**	**1,447**
Proposed/actual dividend	–1,006	–519
Deferred tax assets	–122	–58
Intangible assets	–2,612	–2,193
Deductions for investments in credit institutions	–98	–87
IRB provisions shortfall (–)	–211	–269
Other items, net		
Deductions from original own funds	**–4,049**	**–3,126**
Tier 1 capital (net after deduction)	**19,577**	**15,760**
– of which hybrid capital	1,811	1,447
– of which core tier 1 capital	17,766	14,313
Additional own funds		
Securities of indeterminate dur. and other instr.	682	690
Subordinate loan capital	4,251	5,407
Other additional own funds		
Tier 2 capital (before deductions)	**4,933**	**6,097**
Deductions for investments in credit institutions	–98	–87
IRB provisions excess (+) / shortfall (–)	–211	–269
Deductions from original additional own funds	**–309**	**–356**
Tier 2 capital (net after deductions)	**4,624**	**5,741**
Participations hold in insurance undert., reinsurance	–1,177	–1,059
Pension assets in excess of related liabilities	–98	–116
Total own funds for solvency purposes	**22,926**	**20,326**

12.2.3 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 FSA 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 9.3% of the tier 1 capital, where of the loans with step up conditions together amounts to EUR 1,330m.

12.2.4 Deductions from tier 1 capital

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 the proposed dividend to shareholders by a decision of the annual general meeting of shareholders.

Deferred tax assets

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

Intangible assets

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

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.

IRB provisions shortfall

The calculation of the capital base is in accordance with the CRD and the Swedish legislation. The differences between EL (EUR 2.3bn) and actual provision (EUR 1.9bn) made for the related exposure are adjusted for in the capital base. Note that this only relates to the IRB exposure. 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 equally into both tier 1 capital and tier 2 capital. For the purpose of the CRD transition 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% of IRB RWA).

12.2.5 Changes in core tier 1 capital 2009-2008

The core tier 1 capital has increased about EUR 3.5bn and the main contribution is the rights issue, EUR 2.5bn and profit for the year EUR 1.4bn (excluding proposed dividend). There has also been a net increase is some deductions, EUR 0.8bn , affecting both core tier 1 and tier 1 capital, whereof dividend amounts to EUR 0.5bn of the increase. The increase deduction in intangible assets and deferred tax assets relates foremost to the acquisition of Fionia Bank during the autumn. The deduction from the shortfall has fallen during the period.

12.2.6 Change in hybrid capital loans 2009-2008

There has been a net increase in hybrid capital loans with an amount of EUR 0.4bn as per 31 December 2009. In September Nordea issued an USD nominated hybrid capital loan to an amount of USD 1.0bn (EUR 0.7bn). During the forth quarter hybrid capital loans to an amount of EUR 0.3bn were bought back. The amounts are to some extent also affected by revaluation impact. As of end year 2009, Nordea holds EUR 1.8bn in hybrid capital loans (included as tier 1 capital). Table 62 shows the booked outstanding amounts of hybrid capital loans included in the tier 1 capital.

12.3 Additional own funds

The principal of tier 2 capital has turned from an additional capital base item to items with the function of absorbing losses on a "gone concern" basis, i.e. after the failure of a firm. The tier 2 capital must be subordinated to depositors and general creditors of the bank. It can not be secured or covered by a guarantee of the issuer or related entity or include other arrangement that legally or economically enhances the seniority of the claim vis-à-vis depositors and general bank creditors.

12.3.1 Tier 2 capital

The tier 2 capital is mainly related to subordinated debt and 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. Currently only one loan is subject to reduction. Outstanding amount in the specific issue is deducted by 20% for each year.

As of end year 2009, Nordea holds EUR 4.3bn in dated subordinated loans and EUR 0.7bn in undated subordinated loans.

Table 62 shows the booked outstanding amounts of hybrid capital loans included in the tier 1 capital and subordinate loans included in the tier 2 capital. Call date is where the issuer has the legal right buy back outstanding loan amounts according the terms of agreement. The loans and the principles for time-reductions follow Swedish legislation. The book value in the table can deviate from capital amounts used in the capital base due to swap arrangements and adjustments for maturities.

Table 62 Dated and undated loans

Dated loans

Issuer	Book value EURm	Start	Maturity	Call date	Coupon
Nordea Bank AB	19.5	05	Feb-15	Feb-10	Frn
Nordea Bank AB	58.4	05	Feb-15	Feb-10	Fixed Frn
Nordea Bank AB	750.0	05	May-15	May-10	Frn
Nordea Bank AB	264.7	05	Aug-15	Aug-10	Fixed Frn
Nordea Bank AB	352.9	05	Sep-15	Sep-10	4.625
Nordea Bank AB	68.2	05	Sep-15	Sep-10	Frn
Nordea Bank AB	68.1	06	Feb-16	Feb-11	Fixed Frn
Nordea Bank AB	500.0	06	Mar-16	Mar-11	Frn
Nordea Bank AB	194.7	06	Aug-16	Aug-11	Frn
Nordea Bank AB	349.6	05	Jun-16	Jun-11	Frn
Nordea Bank AB	244.7	06	Jun-16	Jun-11	Frn
Nordea Bank AB	500.0	04	Sep-16	Sep-11	4
Nordea Bank AB	97.4	06	Dec-16	Dec-11	Frn
Nordea Bank AB	97.4	06	Dec-16	Dec-11	Fixed Frn
Nordea Bank AB	558.5	02	Nov-12	n/a	5.25
Nordea Bank AB	497.9	08	Sep-18	Sep-13	Fixed Frn
Total Dat.loans	**4,621.9**		**Jan-16**		

Undated loans, tier 1

Issuer	Book value EURm	Start	Maturity	Call date	Coupon
Nordea Bank AB	500.0	04	n/a	n/a	Frn
Nordea Bank AB	419.5	05	n/a	Apr-15	Fixed
Nordea Bank AB	149.8	05	n/a	Mar-35	Fixed
Nordea Bank AB	74.9	05	n/a	Oct-35	Fixed
Nordea Bank AB	342.9	09	n/a	Mar-15	Fixed Frn
Nordea Bank AB	342.9	09	n/a	Mar-15	Fixed Frn
Total Und.tier 1	**1,830.0**				

Undated loans, tier 2

Issuer	Book value EURm	Start	Maturity	Call date	Coupon
Christiania Bank og Kreditkasse	138.9	86	n/a	n/a	Frn
Nordea Bank Finland Plc	337.2	02	n/a	Jul-14	6.25
Merita Bank Plc	75.1	99	n/a	Feb-29	4.51
Total Und.tier 2	**551.1**				
Grand Total	**7,003.0**				

12.3.2 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. Nordea has no significant holdings in this category and no impact in the tier 2 capital.

12.3.3 Deductions from tier 2 capital

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. (See section 3.1 for specification of associated companies)

IRB provisions excess (+) / shortfall (–)

The differences between EL and provision made for the related exposure are adjusted for in the tier 2 capital, see section 12.2.4 for further explanation.

12.3.4 Changes in tier 2 capital 2009

During the period, Nordea has bought back dated subordinated loans to an amount of EUR 1.1bn. There has not been any new issuance of tier 2 subordinated loans during 2009. The deduction from the shortfall has decreased during the period.

12.4 Deductions from the total capital base

Participations hold in insurance undertakings

By a transition rule in effect until end of 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. There has been a minor increase in the deducted amount following the holding in the insurance sector.

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 2009 the sum of the surplus values of the plans reached EUR 98m.

12.5 Changes in the capital base 2009

Figure 20 illustrates the main changes in the capital base during year 2009.

The significant increase relates to core tier 1 capital, while capital under tier 2 capital decreases over the year. The increase in deductions can foremost be referred to the acquisition of Fionia bank, in terms of goodwill and deferred tax assets.

12.6 Capital transferability and restrictions

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 during 2008 has under certain circumstances limited the transferability of capital with impact on cross border financial groups. There are no such restrictions directly affecting Nordea as per end of 2009.

12.7 Development of the capital base and the components

Figure 21 illustrates the increase in the capital base over a period of ten years and the developments of its main components; own funds, hybrid capital and tier 2 capital. Last year clearly points out the increase in core capital while there is a slight decease in the tier 2 capital.

Figure 20 Development of the capital base 2009

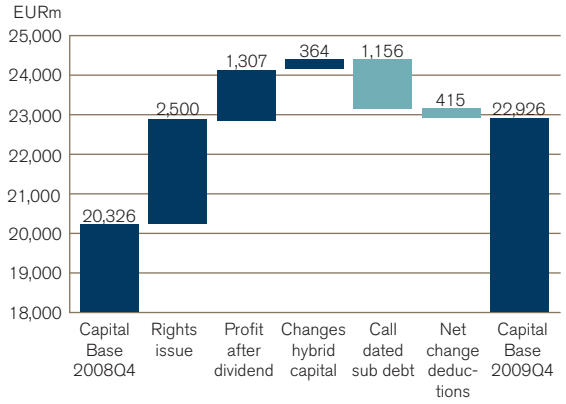
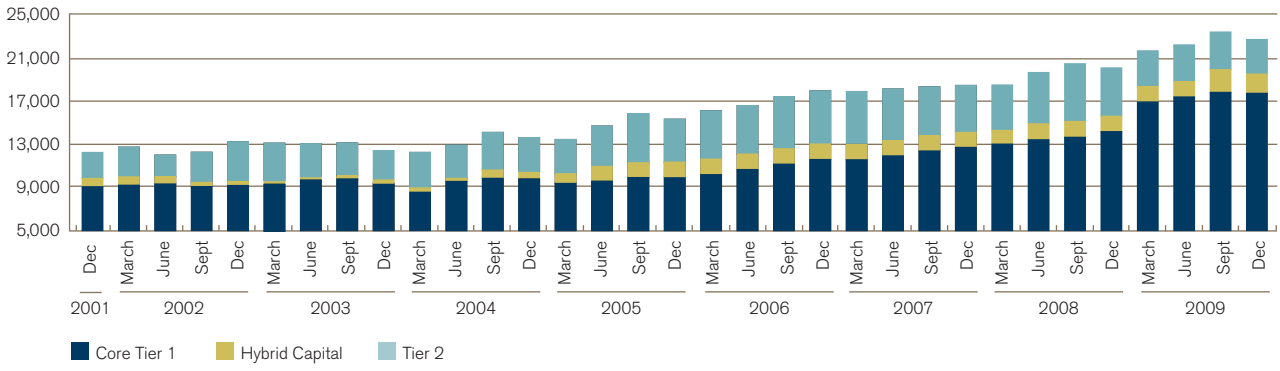


Figure 21 Development of the capital base



13. New regulations

Nordea is well prepared for new capital and liquidity regulations. There is a strong focus on capital management and liquidity risk management within the organisation in order to meet new regulatory demands. Nordea's rights issue in 2009 was done at the right timing, and holds a substantial margin for regulatory changes in the minimum requirements and capital base.

13.1 New capital regulations

Below follows a short description on key capital regulatory initiatives under implementation or under consideration:

Prolongation of transitional floors
The capital requirements will continue (at least to the end of 2011) to be limited to 80% of the requirements according to the old Basel I rules.

Large exposures, securitisation and hybrid capital
During 2009, some changes of capital adequacy legislation are already agreed upon, by BCBS but also on European level. In Europe, changes to the CRD have been agreed upon and are under implementation in national legislation which concern large exposure limits, capital requirements for securitisation positions and composition of the capital base. These changes are expected to be in effect from 2011.

Trading book, re-securitisation and remuneration
Changes to the trading book, re-securitisation and remuneration principles are in the final stage in the European decision process. The regulatory changes are expected to be in effect from 2011.

Other key capital regulations under consideration
In December 2009, BCBS published a proposal of a new regulatory regime (by some called "Basel III"), which is described in the consultative document "Strengthening the resilience of the banking sector". The proposal includes the following key initiatives:

1. Increased quality, consistency and transparency of the capital base. The main aspects of the proposal on quality of the capital are:
   - The predominant form of tier 1 capital must be common shares and retained earnings.
   - The regulatory adjustments should mainly be applied to the common equity component, which in the current framework have been applied partly or in full to tier 1, tier 2 or the total capital base.
   - All instruments included in Tier 1 will, among other things, need to be subordinated, have fully-discretionary non-cumulative dividends or coupons and have neither a maturity date nor an incentive to redeem.
   - Subordinated debt in tier 2 must have an original maturity of at least 5 years, and any calls must be approved by supervisors.
   - Tier 3 capital is abolished.
   - Separate explicit thresholds will be established for the common equity component of tier 1, total tier 1 and total capital. All thresholds are net of regulatory adjustments, but no new thresholds have been presented in the consultative document. It is stated that the total minimum capital requirement will be subject to revision in the second half of 2010 (currently 8% capital ratio), in order to achieve "an appropriate calibrated total level of capital.
2. The risk coverage is further strengthened. The draft proposal from BCBS includes the intention of increasing the capital requirement significantly for credit risk exposure to banks, insurance companies and other financial intermediaries. Furthermore, the capital requirement for counterparty credit risk in OTC derivatives, repos and some other securities financing transactions is suggested to be increased.
3. A leverage ratio is introduced as a supplementary measure. The leverage ratio should work as a "backstop", and be a supplementary measure to the risk based capital framework. The leverage ratio is proposed to start as a pillar 2 measure, but with a view to migrate to pillar 1 treatment based on appropriate review and calibration. The BCBS is considering several ways to calculate the leverage ratio and has not given any information on which backstop threshold that is most likely.
4. A series of measures are suggested to build up capital buffers in good times to make the framework more countercyclical. The BCBS are considering two alternative methods that aim to counteract the cyclicality in the minimum capital requirement for credit risk by adjusting the PD method. Also, the BCBS proposes to introduce constraints to banks that are below a certain capital target level. A buffer range is proposed to be established above the regulatory minimum capital requirement and capital distribution constraints will be imposed on the bank when their capital levels fall below the threshold. The main objective is to ensure that the banking sector builds up a capital buffer when it has earnings capacity and uses this buffer in periods of stress. The BCBS also supports International Accounting Standards Board's (IASB) initiative to account for credit losses at an earlier stage.

A comprehensive Quantitative Impact Study will be conducted by banks during the spring 2010 based on the draft proposal. The BCBS is expected to issue a fully calibrated and final comprehensive framework by end 2010, and has communicated that the aim is to implement the new regulatory regime by end 2012.

Solvency II
A new regulatory framework is also under implementation for the insurance sector, the Solvency II framework. In 2009 the Solvency II Framework Directive was approved by the EU Parliament and subsequently the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) has issued a number of Consultative Papers aiming at providing the FSA's in every country a set of advises for the implementation in local legislation. During 2010, a Quantitative Impact Study (QIS5) will be conducted throughout Europe. The implementation is expected to come into force in local legislations by end of 2012. Nordea has established a program to monitor the development in legislation and prepare and implement Solvency II by 2012.

13.1.1 Aggregated impact on Nordea's capital position

The proposed changes to the capital regulations can lead to an increase in the quality and quantity of capital for many banks, but the magnitude of the capital effects depends on the final calibration and implementation of the proposal. Nordea is well prepared for new capital regulations, with one of the strongest core tier 1 capital ratios in Europe and with a high portion of core equity in the capital base. Nordea will continue to proactively assess and manage the consequences during 2010.

13.2 New liquidity regulations

In the wake of the recent crisis regulators have focused on improving liquidity risk related standards. However, the regulators in general are still in the process of finalising the contents of regulations and the consequences for banking industry are still pending.

Already during 2008 BCBS and Committee of European Banking Supervisors (CEBS) published qualitative principles and guidelines on liquidity risk management. Publications cover among others issues; liquidity strategy, degree of risk tolerance, incorporation of liquidity costs, measurement and management process, segregation of duties, IT systems, funding strategy, intraday risk management, contingent liquidity, collateral management, conducting stress tests, contingency funding plan, liquidity buffers and public disclosure.

Above mentioned qualitative guidelines seem to be adapted by banking industry in general, Nordea included. As a consequence the general awareness of the inherited liquidity risks have improved within institutions.

In addition, CEBS has during 2009 initiated the process towards quantitative framework by publishing guidelines on liquidity buffers and liquidity identity card. Liquidity buffers paper sets out draft guidelines on the appropriate size and composition of liquidity buffers with a view to enhance banks' resilience to liquidity shocks. Bespoke buffers should be in place to enable credit institutions to withstand a liquidity stress for a period of at least one month without changing their business models. Liquidity identity card, in its part, aims at providing supervisors of European cross-border banking groups with a single prudential language to enable meaningful exchange of information, in particular within colleges of supervisors. Liquidity identity card introduces, in addition of liquidity buffer, also metrics like Long-term funding ratio and Core funding ratio. Long-term funding ratio compares long-term, stable funding with long-term assets. The ratio measures the extent to which core funding is used to finance longer-term, illiquid assets and contingencies. Core funding ratio is another type of long-term metrics and it measures the amount of stable or core liabilities as a percentage of total liabilities and equity. This ratio provides insight on the extent to which effective long-term funding is used, given the business model.

Further, BCBS issued at the end of 2009 a consultation paper called International framework for liquidity risk measurement, standards and monitoring. The document focuses on elevating the resilience of internationally active banks to liquidity stresses across the globe, as well as increasing international harmonisation of liquidity risk supervision. This quantitative document developed two internationally consistent regulatory standards i.e. Liquidity coverage ratio and Net stable funding ratio. These standards aim to set the minimum levels of liquidity for internationally active banks. Liquidity coverage ratio aims to ensure that a bank maintains an adequate level of unencumbered, high quality assets that can be converted into cash to meet its liquidity need for a 30-day time horizon under an acute liquidity stress scenario. Net stable funding ratio establishes a minimum acceptable amount of stable funding based on the liquidity characteristics of an institution's assets and activities over a one year horizon. To further strengthen and promote consistency in international liquidity risk supervision, BCBS has also developed a minimum set of monitoring tools to be used in the ongoing monitoring and in communicating this exposure among home and host supervisors.

However, above mentioned quantitative publications have not yet been able to create clear methodological standards or express the undisputed required level of liquidity, but the process has been started and is ongoing. This process should be finalised during 2010, where after it is possible to assess the consequences for banking industry. The consequences are dependent on both the underlying assumptions of metrics as well as required levels and the impact analysis is difficult without the knowledge of both parameters.

14. Appendix

14.1 Government guarantee scheme

The Nordic governments have established a number of measures in response to the global financial crisis. The measures were presented during the autumn 2008 and the beginning of 2009. Similar to many stability packages within EU, the measures include the following elements: implementation of a general framework for giving state support to ailing credit institutions, the creation of a stabilisation fund, a temporary guarantee program and a recapitalisation scheme. Nordea welcomes the actions taken by the Nordic governments to stabilise the markets.

Denmark

Nordea decided for commercial reasons that Nordea Bank Danmark A/S would participate in the Danish guarantee scheme launched in early October 2008. The scheme is valid for two years until end of September 2010 and guarantees the claims of unsecured senior creditors against losses in participating banks. The cost for the Danish guarantee scheme for Nordea during 2009 has been EUR 180m in annual commission expense and an additional EUR 116m reported as loan losses. Approximately the same cost is expected for 2010. Following the successful rights offering in April, Nordea has chosen not to apply for hybrid loans from the Danish state under the Act on State-Funded Capital Injections, i.e. Nordea does not participate in the second Danish scheme.

Finland

Nordea has to date not participated in the Finnish scheme.

Norway

During the fourth quarter 2008, Nordea participated in swap facilities under the Norwegian scheme.

Sweden

Nordea has not participated in the Swedish government's stability measures. However, in order to facilitate the Swedish State's subscription in Nordea's rights offering through the Recapitalisation scheme, Nordea has signed an agreement with the Swedish National Debt Office. The funding for the State's participation thus came from the Stabilisation Fund. The fund is to be built up with fees from banks and other credit institutions. The total stability fee for Nordea was EUR 20m during 2009 and approximately the same amount is expected for 2010.

14.2 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 framework 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 Supervisory Review Process (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 transition rules (also known as capital floor) for all institutions implementing the new capital adequacy reporting. The transition rules, in force 2007–2009 with prolongation at least to the end of 2011, mark the lowest eligible capital base and relate directly to the capital requirements calculated under Basel I regulations. During 2007 the capital requirement was no less than 95% of the capital requirement calculated under Basel I regulations. For 2008 and 2009, the amount of capital requirement was allowed to be 90% respectively 80% of the capital requirement calculated under Basel I regulations. The transition rules have been prolonged, at least for 2010 and 2011, and the capital requirement is not allowed to be below 80% of the capital requirement calculated under Basel I regulations.

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:

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 counterparties 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.

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.

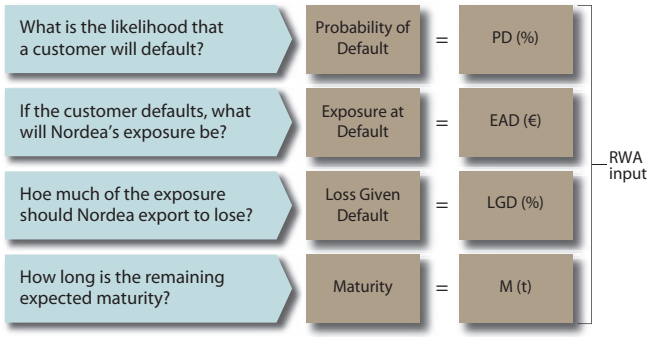
Pillar 3

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

14.3 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.



14.3.1 IRB exposure classes

Institution exposure
Exposure to credit institutions and investment firms is classified as exposure to institutions. In addition, exposure to regional governments, local authorities and multilateral development banks is classified as exposure to institutions if it is not treated as exposure to sovereigns[3] according to regulations issued by the authorities.

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

Retail exposure
Exposure to small and medium sized entities (with an exposure of less than EUR 250k) and to private individuals is 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.

14.3.2 Standardised exposure classes

Central governments and central banks
Exposure to central governments and central banks is, 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 this exposure, applied in Nordea.

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

Institution exposure
Exposure to institutions is 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 this exposure.

Corporate exposure
Exposure to corporate rated by eligible rating agency is assigned a risk weight from 20% to 150%. Exposure without external rating is assigned a risk weight of 100%.

Retail exposure
Retail exposure is assigned a risk weight of 75%.

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

Other
- Exposure to administrative bodies and non-commercial undertakings (such as public sector entities) subject to decision by the local authority, is assigned a risk weight of 0% to 100%.
- Exposure to named multilateral development banks is assigned a risk weight of 0%. Other multilateral development banks are assigned a risk weight according to the methods used for exposures to institutions.
- Exposure to named international organisations is 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. Exposure reported as short-term claims receives a risk weight based on the short term external rating of the institution. Short-term exposure to institutions and corporate for which a short-term credit assessment by a nominated rating agency is available, is 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 exposure 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.

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

14.4 Calculation of RWA

The calculation of exposure at default (EAD) in Nordea differs between approaches but also depending on the exposure classes within the IRB approach.

14.4.1 IRB approach

The FIRB approach is used for calculating the minimum capital requirements for exposure 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 input 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 exposure, which in turn is based on internal historical loss data.

14.4.1.1 Exposure at Default (EAD)

The EAD is an estimation of the total exposure to the customer at the time of default. For on-balance 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 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.

14.4.1.2 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.

14.4.1.3 Loss Given Default (LGD)

The LGD measures the economic loss that can be expected if a customer goes default. 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).

14.4.1.4 Credit risk mitigation

RWA and exposure 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 exposure in FIRB, which are currently used for corporate and institution exposure. Financial supervisory authorities may permit the use of other physical collaterals 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).
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 exposure 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 exposure 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.

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.

14.4.1.5 Maturity
For exposure 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.

14.4.2 Standardised approach
The parts remaining in the standardised approach are foreign branches, subsidiaries in Poland, Luxemburg and Russia and the retail exposure in the finance companies as well as exposure towards sovereigns. 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 class 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 exposure is converted into EAD using CCF set by the financial supervisory authorities. Derivative contracts and securities financing has an EAD that is the same amount 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.

14.5 Difference between economic capital and regulatory capitalrequirement
The differences between economic capital and the capital requirement according to CRD during 2009 are shown below, note that there will be changes in the economic capital framework for 2010 as described in chapter 11.

- 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 economic capital 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 the Group's investment in life insurance is deducted from 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 market risk and life insurance risk. These risks affect Nordea's policyholders to a larger extent than Nordea's own account. These risks are primarily controlled using asset allocation policies and 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. See chapter 10 for further information regarding life insurance.
  - 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 NLP is included in the Group's consolidated market risk measurement (see chapter 6). The market risk for NLP is not included in pillar 1 capital calculations, but included in the economic 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 economic capital framework.
  - A small amount of credit risk exists in the investment of own funds, though the risk level is very low by design.
  - Additionally, business risk and operational risk result in the life operations and the life operations are charged capital for these more general risks.

- Credit risk:
  - Economic capital for credit risk includes maturity adjustments.
  - Exposure calculated using the standardised approach in pillar 1 according to CRD is calculated on the basis of internal models in the economic capital framework, though the models have not yet been approved by the financial supervisory authorities for use in the regulatory calculations.
  - Credit risk economic capital for corporate and institutions exposure 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 economic capital 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 exposure 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 add-on in the economic capital framework.
- Market risk:
  - Economic capital 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 and FX risk outside the trading book are included in the capital calculations for market risk.
- Business risk:
  - Business risk is not included in pillar 1 of CRD. The economic capital 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 economic capital while operational risk in pillar 1 is based on calendar years.
- Diversification effects:
  - Unlike pillar 1 in CRD, the economic capital framework accounts for group level diversification benefits in Nordea's varied operations.

List of abbreviations

ADF	Actual Default Frequency
AIRB	Advanced Internal Rating Based approach
ALCO	Asset and Liability Committee
BCBS	Basel Committee on Banking Supervision
CCF	Credit Conversion Factor
CCR	Counterparty Credit Risk
CDO	Collateralised Debt Obligation
CEBS	Committee of European Bank Supervisors
CEIOPS	Committee of European Insurance and Occupational Pen-sions Supervisors
CEO	Chief Executive Officer
CDS	Credit Default Swap
CFO	Chief Financial Officer
CLN	Credit Linked Notes
CLS	Continuous Linked Settlement
CMO	Collateralised Mortgage Obligations
CP	Commercial Paper
CPF	Capital Planning Forum
CRD	EU's Capital Requirements Directive
CRO	Chief Risk Officer
ECC	Executive Credit Committee
EEA	European Economic Area
EAD	Exposure at Default
EL	Expected Loss
EP	Economic Profit
ERAT	Environmental Risk Assessment Tool
EU	European Union
EV	Economic Value
FSA	Financial Supervisory Authority
FFFS	Finansinspektionens Författningssamling (The Swedish FSA's directive)
FIRB	dFoundation 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
MCEV	Market Consistent Embedded Value model
NLP	Nordea Life and Pensions
OTC	Over The Counter (derivatives)
ORX	An international database for incidents
PD	Probability of Default
PIT	Point-in-Time
QIS	Quantitative Impact Study
QRA	Quality and Risk Analysis
RWA	Risk Weighted Amount
S&P	Standard & Poor's
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
SPRAT	Social and Political Risk Assessment Tool
TTC	Through-the-Cycle
VaR	Value at Risk