Capital and Risk Management (Pillar III) Report

Nordea Bank Danmark Group 2013

Nordea Bank Danmark hereby presents its capital position and how the size and composition of the capital base is related to the risks as measured in Risk-Weighted Assets (RWA). The national capital adequacy legislation is based on Directive 2006/48/EC of the European Parliament and of the Council , commonly referred to as the Capital Requirements Directive (the CRD) , which is in turn based on the Basel II framework issued by the Basel Committee on Banking Supervision (BCBS).

The Nordea Bank Danmark Group follows the Danish Financial business act 948 and the Danish Financial Supervisory Authority's regulation 1399Executive order on capital adequacy and 915 Executive order on Capital Base, which are based on the CRD.

This Pillar III disclosure constitutes a comprehensive disclosure on risks, risk management and capital management. In a summarised form, the disclosure is also presented in Nordea Bank Danmark's Annual Report 2013.

The Pillar III 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. These reports are presented on www.nordea.com and the key data on capital adequacy is also presented in the annual report of each legal entity.

The full Pillar III 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 local legislation, a common set-up in Nordea. Nordea has stated the common principles in a policy and instruction for disclosing information on capital adequacy in the Nordea Group.

In this report, Nordea Bank Danmark Group is defined as Nordea Bank Danmark and Nordea Group is defined as Nordea.

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1. Highlights of 2013

Nordea Bank Danmark continued to show a solid risk position and credit quality as well as further improved its capital ratios in 2013. This was reflected by a core tier 1 capital ratio excluding transition rules which increased to 14.0%, a lower loan loss ratio of 45bp, and stable overall effects from migration.

The Nordic economies have continued to perform well compared to the rest of Europe, although with differences within the region. Despite that the growth outlook for the Nordic economies has deteriorated somewhat lately, the growth outlook for Denmark is positive.

Nordea Bank Danmark is confident and well-prepared for the future, due to stable profitability, solid quality in its well-diversified credit portfolio, a strong capital position and a diversified funding base.

Continued solid credit quality and strong risk management

Overall credit quality remained solid in 2013. Net loan losses remained on an elevated level compared to Nordea Bank Danmark's historical average, however the loan loss ratio decreased to 45bp (70bp). The improved loan loss ratios reflect the ongoing economic recovery in Denmark.

Nordea Bank Danmark's market risk-taking activities are well-diversified and oriented towards the Nordic and European markets. The total consolidated market risk VaR (mainly interest rate risk) in 2013 decreased to an average of EUR 12m (EUR 26m).

Capital ratios already at strong levels

The core tier 1 capital ratio excluding transition rules, increased by 1.9 %-points during 2013, to reach 14.0% The capital ratio excluding transition rules ended at 20.5% (18.2%).

Strong funding name maintained

Nordea Bank Danmark remains a strong name in the funding market, with maintained high activity also in the long-term funding market. The average size of the liquidity buffer was EUR 22.2bn (EUR 24.1bn).

CRD IV and CRR – new regulations for capital and liquidity risk

In Nordea Bank Danmark, there is a strong focus on capital, liquidity and risk management and the bank is well-prepared to meet the new regulatory environment, further described in Chapter 11.

2. Governance of risk and capital management

Management of risk, liquidity and capital are key success factors in the financial services industry. The maintaining of risk awareness in the organisation is incorporated in the business strategies. Nordea has defined clear risk, liquidity and capital management frameworks, including policies and instructions for different risk types, capital adequacy and capital structure.

2.1 The Financial Group Nordea Bank Danmark in the capital adequacy context

The information given in this report refers to Nordea Bank Danmark A/S, with corporate registration number 13522197.

The financial statements are published semi-annually and the consolidated financial statements include the accounts of the parent company Nordea Bank Danmark A/S including subsidiaries according to International Accounting Standard (IAS) 27. In the Financial Group, the insurance operations are not consolidated, which is a difference to the treatment for accounting purposes. 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). End 2013 Nordea Bank Danmark included no insurance entities. However, with references to act 705 "Bekendtgørelsen om finansiel virksomhed and by requirements by the Danish Financial Supervisory Authority, holdings in LR Realkredit A/S (Nordea Bank Danmark holds 39% of voting power) are included in RWA and capital base with a proportional part. Tables and figures with specification of exposures, RWA and capital requirement related to LR Kredit are not included in this report if not stated. This is valid only in Nordea Bank Danmark and is not included in the capital requirements of Nordea Group. Table 2.1 at the end of this chapter discloses the undertakings that have been consolidated and deducted from the capital base.

2.2 Risk and capital management

2.2.1 *Risk and capital management principles and control*

Risk and capital management in the Nordea Group is governed by principles and procedures stated in charters, policies, guidelines and instructions in effect throughout the organisation. All legal entities are subject to the same internal control and risk management environment via Nordea's business structure. Each business area is responsible for managing the risks in its operations, which includes identification, control, mitigating actions and reporting. Group Risk Management consolidates and monitors risk on Group level.

Nordea monitors aggregated risks via specific committees, as well as through reporting to Group Executive Management (GEM) and the Group Board of Directors and the local bank boards. More specifically, Nordea's risks and capital are monitored by the Risk Committee and the Asset and Liability Committee (ALCO).

2.2.1.1 Board of Directors and Board Risk Committee

The Board of Directors has the ultimate responsibility for limiting and monitoring the Group's risk exposure as well as for setting targets for the capital ratios and risk appetite. Risk is measured and reported according to common principles and policies approved by the Board of Directors, which also decides on policies for credit risk, counterparty credit risk, market risk, liquidity risk, business risk, life insurance risk and operational risk management as well as the internal capital adequacy assessment process (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 business areas. These authorisations vary for different decision-making levels, mainly in terms of size of limits but also dependent on the internal rating of customers. The Board of Directors furthermore decides on the limits for market and liquidity risk in Nordea.

The Board Risk Committee assists the Board of Directors in fulfilling its oversight responsibilities concerning management and control of risk, risk frameworks as well as controls and processes associated with the Group's operations.

2.2.1.2 *Responsibility of CEO and GEM*

The Chief Executive Officer (CEO) has the overall responsibility for developing and maintaining effective risk, liquidity and capital management principles and control of the bank and the Group.

The CEO and GEM regularly review reports on risk exposure and have established a number of committees for risk, liquidity and capital management.

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

The Risk Committee, chaired by the Chief Risk Officer (CRO), oversees the management and control of the Group's risks on an aggregate level and evaluates the sufficiency of the risk frameworks, controls and processes associated with these risks. Furthermore, the Risk Committee decides, within the scope of resolutions adopted by the Board of Directors, the allocation of market risk limits as well as liquidity risk limits to the risk-taking units Nordea Markets and Group Treasury respectively. 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 Risk Committee has established sub-committees for its work and decision-making within specific risk areas.

The Group Executive Management Credit Committee (GEM CC) and Executive Credit Committee (ECC) are chaired by the CRO, while the Group Credit Committee Retail Banking (GCCR) and the Group Credit Committee Wholesale Banking (GCCW) are chaired by the Chief Credit Officer (CCO). These credit committees 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.

2.2.1.3 *Responsibility of Group Risk Management and Group Corporate Centre*

Figure 2.1 illustrates Nordea's governance structure of risk, liquidity and capital management.

Figure 2.1 Governance of risk, liquidity and capital management

Within the Group, two units – Group Risk Management and Group Corporate Centre, are responsible for risk, capital, liquidity and balance sheet management. Group Risk Management, headed by the CRO, is responsible for the risk management framework and processes. Group Corporate Centre, headed by the CFO,

is responsible for the capital policy, the composition of the capital base, the capital adequacy framework (including the IRB framework) and for management of liquidity risk.

Each Business Area and Group function is primarily responsible for managing the risks in its operations within the applicable limits and framework, including identification, control and reporting.

Nordea Bank Danmark has appointed a Chief Risk Officer (CRO). The CRO reports to the Executive Management of Nordea Bank Danmark and is responsible for the overall risk management coordination in Nordea Bank Danmark.

The risk management functions of Nordea Bank Danmark are represented by independent risk management units which are responsible for risk management in individual areas. The interaction between the individual risk management units and the CRO includes credit risk, counterparty credit risk, market risk, liquidity risk and operational risk. The risk function comprises Group Credit Risk, Group Credit Control, Group Market & Counterparty Credit Risk, Group Treasury and Group Operational Risk & Compliance.

Nordea Bank Danmark has appointed a Country Risk and Compliance Officer (Country RCO) as of January 2014. The Country RCO will be responsible for the overall operational risk, compliance and AML coordination in Nordea Bank Danmark and will report to the Executive Management of Nordea Bank Danmark.

2.2.2 *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 the consequences of the risks. Management of risk 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.

The control environment is, among other things, based on the principles of segregation of duties and independence. Monitoring and reporting of risk is conducted on a daily basis for market, counterparty credit and liquidity risk and on a monthly and quarterly basis for credit and operational risk. Risk appetite reporting is presented quarterly to the Risk Committee, GEM, the Board Risk Committee and the Board of Directors.

Detailed risk information, covering all risks as well as capital adequacy for the consolidated group is regularly reported to the Risk Committee, GEM and the Board of Directors. In addition, the Board of Directors in Nordea Bank Danmark receives risk reporting which covers market, credit and liquidity risk in Nordea Bank Danmark. Nordea's internal capital requirement includes all types of risks and is regularly reported to ALCO.

Group Internal Audit independently evaluates the processes regarding risk and capital management in accordance with the annual audit plan.

Table 2.1 Specification over undertakings consolidated/deducted from Nordea Bank Danmark, 31 December 2013

	Number of shares	Book value EURm	Voting power of holding %	Domicile	Consolidation method
Group undertakings included in the Nordea Bank Danmark Group					
Nordea Finans Danmark A/S	20,006	193	100	Høje-Taastrup	purchase method
Nordea Kredit Realkreditaktieselskab	17,172,500	2,346	100	Copenhagen	purchase method
Fionia Asset Company A/S	148,742,586	1,172	100	Copenhagen	purchase method
Nordea Finance Ltd	2	0	100	London	purchase method
Structured Finance Servicer A/S	2	1	100	Copenhagen	purchase method
NJK 1 ApS	34,562,926	36	100	Copenhagen	purchase method
Other companies		1			
Total included in the Nordea Bank Danmark Group					
Over 10% investments in credit institutions deducted from the capital base					
None					
Total investments in credit institutions deducted from the capital base					

3. Capital position

Nordea Bank Danmark strengthened its capital position during 2013 in terms of decreased RWA and an increased capital base. The core tier 1 capital ratio excluding transition rules increased to 14.0% compared to 12.1% at the end of 2012. The capital ratio increased to 20.5% compared to 18.2% at the end of 2012.

3.1 Capital adequacy assessment

Banks need to keep sufficient capital to cover all risks taken over a foreseeable future. Therefore, Nordea Bank Danmark strives to be efficient in its use of capital through active management of the balance sheet with respect to different asset, liability and risk categories. Nordea Bank Danmark's goal is to enhance returns to shareholders while maintaining a prudent risk and return relationship. Strong capital and RWA management supports the strategic visions. In addition, it provides protection against unexpected losses that arise as a result of risks taken.

The internal capital adequacy assessment process (ICAAP) is established to determine internal capital requirements that reflect the risks and to assess capital adequacy.

3.2 Regulatory capital requirements and RWA

The regulatory capital requirements that Nordea Bank Danmark fell under on the balance date for this report, 31 December 2013, are based on the consolidated version of the Capital Requirements Directive (CRD); EU Directive 2006/48/EC (including 2009/111/EC and 2010/76/EU). In Danish legislation capital requirements are defined in Danish Financial business act 948 and the Danish Financial Supervisory Authority's regulation: 1399 Executive order on capital adequacy and 915 Executive order on capital base. The capital adequacy figures presented in this report follow the CRD definitions.

Table 3.1 presents an overview of capital requirements and RWA as of end 2013, split by risk type and with comparison to previous year. Of the RWA, credit risk accounts for approximately 86%, while operational risk accounts for 12% and market risk 2%. The table also includes information about the approach used for calculation of the RWA. Out of the RWA for credit risk, 84% of the exposure has been calculated with the IRB approach and 16% with the standardised approach (see table 4.2).

3.2.1 *Current capital base*

As shown in Table 3.2, the capital base as of end 2013 was EUR 7.1bn, of which EUR 4.8bn represented core tier 1 capital. Tier 1 and tier 2 capital net of deductions was EUR 4.8bn and EUR 2.3bn respectively. See chapter 10 for further details regarding the capital base.

3.3 Capital ratios

To quantify the degree of capital coverage, different ratios based on different capital base items are used. These ratios include, but are not limited to:

- The core tier 1 capital ratio: calculated by dividing core tier 1 capital with RWA.
- The tier 1 capital ratio: calculated by dividing tier 1 capital with RWA.
- The capital ratio: calculated by dividing the capital base with RWA.

Nordea Bank Danmark's core tier 1 capital ratio and tier 1 capital ratio excluding transition rules was 14.0% at the end of 2013, representing a 190bp improvement since 2012. Improved capital ratios were achieved through profit generation and decreased RWA, mainly for credit risk. The capital ratio excluding transition rules was 20.5% (18.2%).

The core tier 1 capital ratio and tier 1 capital ratio including transition rules was 9.3% (8.4%) the capital ratio including transition rules were 13.7% (12.6%) respectively.

Table 3.2 shows the key capital adequacy figures of Nordea Bank Danmark, both including and excluding transition rules.

Table 3.1 Capital requirements and RWA

	31 December 2013		31 December 2012	
EURm	Capital requirement	RWA	Capital requirement	RWA
Credit risk	**2,374**	**29,675**	**2,526**	**31,579**
IRB	2,203	27,532	2,357	29,467
- of which institution	46	570	45	562
- of which corporate	1,429	17,859	1,470	18,375
- of which retail	706	8,828	803	10,032
- of which mortgage	347	4,336	391	4,889
- of which other retail	344	4,306	390	4,873
- of which SME	15	186	22	271
- of which other	22	276	40	499
Standardised	171	2,143	169	2,112
- of which sovereign	4	52	5	63
- of which institution	11	143	11	141
- of which corporate	5	68	5	67
- of which retail	51	642	43	532
- of which other[1]	99	1,238	105	1,309
Market risk	**69**	**863**	**153**	**1,910**
- of which trading book, Internal approach	40	505	60	754
- of which trading book, Standardised approach	29	358	92	1,156
- of which banking book, Standardised approach				
Operational risk	**322**	**4,024**	**325**	**4,062**
Standardised	322	4,024	325	4,062
Sub total	**2,765**	**34,562**	**3,004**	**37,551**
Additional capital requirement due to transition rules	1,383	17,293	1,329	16,608
Total	**4,148**	**51,855**	**4,333**	**54,159**

1) Includes associated company LR Kredit with EUR 63m (EUR 54m) in capital requirements, of which EUR 18m (EUR 18m) is market risk

Table 3.2 Key capital adequacy figures

EURm	31 December 2013	31 December 2012
RWA including transition rules	51,856	54,159
RWA excluding transition rules	34,563	37,551
Capital requirement including transition rules	4,148	4,333
Core tier 1 capital	4,835	4,558
Tier 1 capital	4,835	4,558
Capital base	7,091	6,816
Capital ratios excluding transition rules		
Core tier 1 capital ratio (%)	14.0%	12.1%
Tier 1 capital ratio (%)	14.0%	12.1%
Capital ratio (%)	20.5%	18.2%
Capital adequacy quotient (Capital base/Capital requirement)	2.6	2.3
Capital ratios including transition rules		
Core tier 1 capital ratio (%)	9.3%	8.4%
Tier 1 capital ratio (%)	9.3%	8.4%
Capital ratio (%)	13.7%	12.6%
Capital adequacy quotient (Capital base/Capital requirement)	1.7	1.6

4. Credit risk

The overall credit quality in Nordea Bank Danmark's portfolio improved in 2013. Net loan losses remained on an elevated level however decreased to 45bp (70bp) during the year as the Danish economy continued to recover.

4.1 Management, governance and measurement of credit risk

Credit risk is defined as the risk of loss if customers fail to fulfil their agreed obligations and the pledged collateral does not cover existing claims. The credit risks stem mainly from various forms of lending, but also from issued guarantees and documentary credits, such as letters of credit. Furthermore, credit risk may also include counterparty credit risk, transfer risk and settlement risk.

4.1.1 *Management of credit risk*

For monitoring the distribution of a portfolio, improving risk management and defining a common strategy, there are specific industry credit policies and principles in place. The concentration risk in specific industries is followed by industry monitoring groups. Industry credit policies are established for industries where at least two of the following criteria are fulfilled:

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

Nordea currently has industry credit policies in place for the following industries:

- Shipping, Oil and Offshore
- Energy
- Leveraged buy-out (LBO)
- Financial Institutions
- Commercial Real Estate

Industry credit principles apply to:

- Forest
- Telecom
- Aircraft
- Hedge Funds

All industry credit policies are approved by the Executive Credit Committee and confirmed annually by the Board Risk Committee. The Industry Credit Principles are approved by Group Credit Committee Wholesale (GCCW) and confirmed by the Executive Credit Committee (ECC).

Decisions regarding credit risk limits for customers and customer groups are made by the relevant decision-making bodies on different levels within the Group. The responsibility for credit risk lies within 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 his/her debt obligations in full and the situation cannot be satisfactorily remedied, the customer must be tested for impairment. See section 4.9.1 for more details on impairment.

If credit weakness is identified in relation to a customer exposure, the exposure is assigned special attention in terms of more frequent reviewing of the risk. In addition to continuous monitoring, an action plan is established outlining how to minimise the potential credit loss. If necessary, a special work-out team is set

up to support the customer responsible unit. Nordea has a project organisation for handling work-out credits for corporate customers and individual work-out teams including relevant specialists are established for larger work-out cases. The 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 also assessed and the actions related to handling of work-out customers are reviewed and followed up.

The environmental risks of corporate customers are taken into account in the overall risk assessment through the Environmental Risk Assessment Tool (ERAT). Social and political risks are taken into account by the Social and Political Risk Assessment Tool (SPRAT). A project to develop the Environmental Social Governance (ESG) risk assessment tools and processes is on-going. The aim is to move towards a risk based approach to identify and focus our efforts on potential higher risk cases. For larger project finance transactions, Nordea has adopted the Equator Principles, a financial industry benchmark for determining, assessing and managing social and environmental risk in project financing. The Equator Principles are based on the policies and guidelines of the World Bank and International Finance Corporation.

4.1.1.1 Credit risk mitigation and collateral policy

Credit risk mitigation is a fundamental part of the credit decision process. In every credit decision and review, the valuation of collaterals as well as the adequacy of covenants and other risk mitigation measures are considered.

Pledging of collaterals is the main credit risk mitigation method. Local instructions emphasise that practice and routines are timely and prudent in order to ensure that collateral items are controlled by Nordea and that loans and pledge agreements as well as collaterals are legally enforceable. Nordea is therefore entitled to liquidate collateral in the event of the obligor's default and can claim and control cash proceeds from a liquidation process.

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

The following collateral types are most common in Nordea Bank Danmark:

- Residential real estate, commercial real estate and land situated in Denmark
- Other tangible assets such as vehicles- and vessels
- Financial collateral such as listed shares, listed bonds and other specific securities
- Deposits
- Guarantees

For each type of collateral, more specific instructions are added to the general valuation principle. A specific maximum collateral ratio is set for each collateral type. In the calculation of RWA, the collateral must fulfil certain eligibility criteria.

For large exposures, syndication of loans is the primary tool for managing concentration risk, while credit risk mitigation by the use of credit default swaps is applied to a very limited extent.

Covenants in credit agreements serve as a complement to both secured and unsecured exposures. All exposures of substantial size and complexity include appropriate covenants. Financial covenants are designed to highlight early warning signs and are closely monitored.

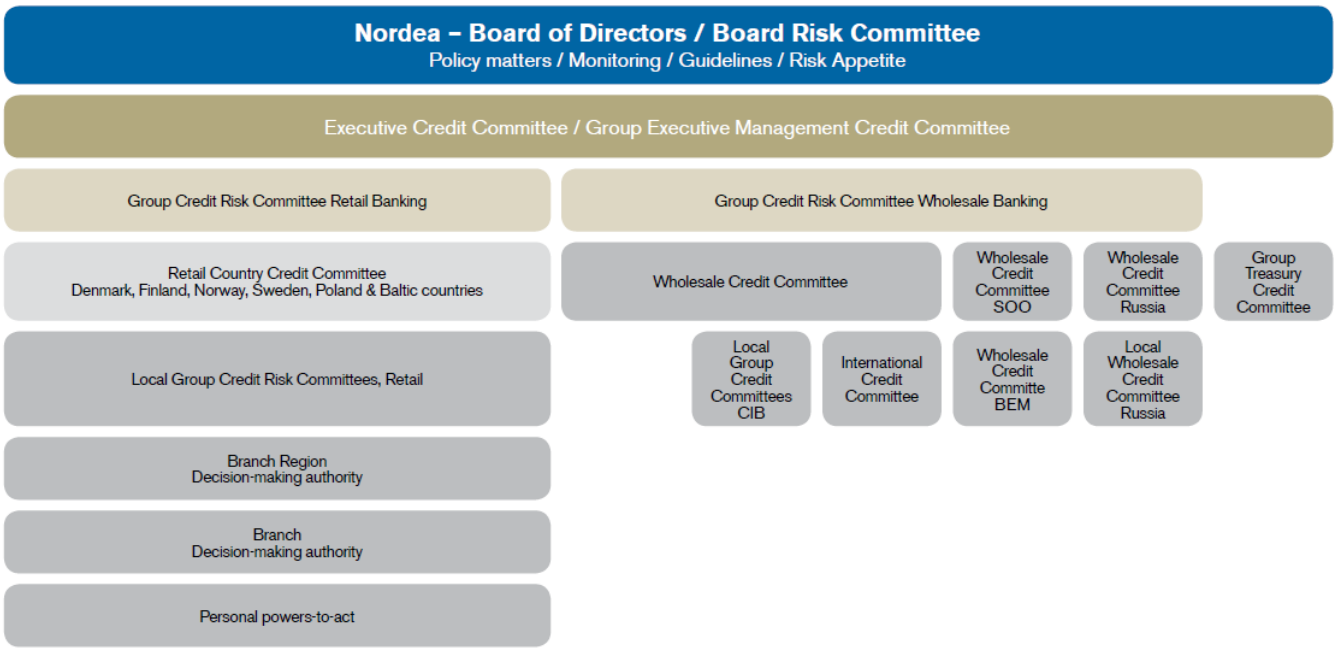
4.1.2 ***Governance of credit risk***

Group Risk Management is responsible for the credit process framework and the credit risk management framework, consisting of policies, instructions and guidelines for the Group. Group Risk Management is also responsible for controlling and monitoring the quality of the credit portfolio and the credit process, and for ensuring that all incurred losses are covered by adequate allowances. Each division/unit is primarily responsible for managing the credit risks in its operations within the applicable framework and limits, including identification, control and reporting.

Within the powers-to-act granted by the Group Board of Directors, credit risk limits are approved by credit decision-making bodies on different levels in the organisation. The rating and exposure of the customer determine at what level the decision will be made (see Figure 4.1). Group Executive Management Credit

Committee decides on proposals for the largest exposures and proposals related to major principle issues. Responsibility for the credit risk lies within the customer responsible unit. Customers are assigned a rating or risk grade in accordance with the framework for quantification of credit risk. The Board of Directors in Nordea Bank Danmark makes the final credit decision concerning Nordea Bank Danmark.

Figure 4.1 Credit risk decision making structure for main operations



4.1.3 *Measurement of credit risk*

Credit risk is measured, monitored and segmented in several dimensions. On-balance sheet lending constitutes the major part of the credit portfolio and the basis for impaired loans and loan losses. Credit risk in lending is measured and presented as the principle amount of on-balance sheet claims, i.e. loans to credit institutions and the public as well as off-balance sheet potential claims on customers and counterparts net after allowances. Credit risk exposure also includes counterparty credit risk such as risk related to derivative contracts and securities financing. Nordea's loan portfolio is broken down by segment, industry and geography.

One way of assessing credit quality is through analysis of the distribution across rating grades for rated corporate customers and institutions, as well as the distribution across risk grades for scored retail customers.

4.2 Link between credit risk exposure and balance sheet

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 is shown in appendix 12.2 and 12.3.

Original exposure is the exposure before taking into account substitution effects stemming from credit risk mitigation, credit conversion factors (CCFs) for off-balance exposure and allowances within the standardised approach. In this report, however, exposure is defined as exposure at default (EAD) for IRB exposure and exposure value for standardised exposure unless otherwise stated. Credit risk exposure presented in this report, in accordance with the CRD, is divided into exposure classes, where each exposure class is divided into exposure types as follows:

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

Items presented in the Annual Report are divided as follows (in accordance with the accounting standards):

- On-balance sheet items (e.g. loans to central banks and credit institutions, loans to the public, reversed repurchase agreements, positive fair value for derivatives and interest-bearing securities)
- Off-balance sheet items (e.g. guarantees and unutilised lines of credit)

Table 4.1 shows the link between the CRD credit risk exposure and items presented in the Annual Report.

Table 4.1 Specification of on-balance sheet and off-balance sheet items for Nordea Bank Danmark, 31 December 2013

EURm **On-balance sheet items**	Balance sheet (accounting)	Items related to market risk	Repos, derivatives, securities lending	Other	Original Exposure	Adjustments[1]	Exposure
Cash and balances with central banks	11,243				11,243		11,243
Treasury bills, other interest-bearing securities and pledged instruments	10,497	-2,238			8,259		8,259
Loans to credit institutions	1,545		-541		1,004		1,004
Loans to the public	80,552			1,461	82,013	-10	82,003
Derivatives	111		-111		0		0
Intangible assets	371			-371	0		0
Other assets and prepaid expenses	6,442	-3,450		-1,861	1,131		1,131
Total	**110,761**	**-5,688**	**-652**	**-771**	**103,650**	**-10**	**103,640**

Off-balance sheet items in the Annual Report	Off-bal. sheet (accounting)	Life insurance operations	Included in derivatives & sec fin	Included in CRD off-bal.
Contingent liabilities	3,710			3,710
Commitments	23,486			23,486
Total	**27,196**			**27,196**

Off-balance items in CRD	Included in CRD off-bal. (from AR)	Included in CRD (not in AR)[2]	Original Exposure	CCF%	Exposure
Credit facilities & checking accounts	22,749		22,749	29%	6,600
Loan commitments	735		735	49%	363
Guarantees	3,312		3,312	72%	2,384
Other (leasing and documentary credits)	400		400	7%	27
Total	**27,196**		**27,196**		**9,374**

Derivatives and securities financing	Original Exposure	Adjustments	Exposure
Derivatives	84		84
Securities Financing Transactions & Long Settlement Transactions	66		66
Total credit risk (CRD definition)	**130,996**		**113,164**

1 The on-balance exposures can have a lower EAD than original exposure 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) Off-balance exposures included in the CRD but not included in the Annual Report (AR), such as exposures related to undrawn credit facilities which are unconditionally cancellable.

4.2.1 *On-balance sheet items*

The following items have been excluded from the balance sheet, when calculating on-balance exposure in accordance with the CRD:

- Market risk related items in the trading book, such as certain interest-bearing securities and pledged instruments.
- 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).
- Other, mainly allowances, intangible assets and deferred tax assets.

4.2.2 *Off-balance sheet items*

The following off-balance sheet items specified in the Annual Report are excluded when off-balance exposure is calculated in accordance with the CRD:

- Assets pledged as security for own liabilities and Other assets pledged (apart from leasing). These transactions are reported as securities financing (i.e. a separate exposure type).
- Derivatives

4.2.3 *Derivatives and securities financing*

Derivatives can be both on-balance (i.e. positive fair value) and off-balance (i.e. nominal amounts) in accordance with accounting standards. However, in the CRD, the derivatives and securities financing are reported as separate exposure types. Also, repurchase agreements and securities lending/borrowing transactions are in the balance sheet calculated based on nominal value. In the CRD calculations these exposure types are determined net of collateral.

4.3 Credit risk approach

Nordea Bank Danmark is approved by the Danish FSA to use the IRB approach for the main part of the credit portfolio.

Nordea Bank Danmark and Nordea Kredit Realkreditaktieselskab are approved to use the Advanced IRB approach for the corporate exposure class from January 2014. On the balance date of this report however, the Foundation IRB method was used for corporate and institution exposure classes. The IRB approach is used for the exposure class Retail.

Nordea Finans in Denmark is approved to use the Foundation IRB approach for the corporate and institution exposure classes.

Other legal entities, mainly small units, and exposure classes are reported according to the standardised approach, however Nordea aims to continue the roll-out of the IRB approaches in the forthcoming years. Acquisitions of new portfolios are treated under the standardised approach until approved for the IRB approach by the supervisory authorities.

4.4 Capital requirement for credit risk

This section includes an overview of the credit risk portfolio distribution. For more detailed information on the principles for RWA calculations under the IRB and standardised approaches see appendix 12.2 and 12.3.

Table 4.2 shows original exposure, exposure, average risk weight, RWA and the capital requirements, distributed by exposure class. The IRB exposure classes contain the portfolios for which Nordea Bank Danmark has been approved to use IRB methods. The standardised approach is currently used for the remaining portfolios, such as Nordea Finance Retail. Some exposure classes have been merged in the table due to insignificant exposure.

Table 4.2 Capital requirements for credit risk, split by exposure class, 31 December 2013

EURm	Original exposure	Exposure	Average risk weight	RWA	Capital requirement
IRB exposure classes					
Institutions	6,584	6,304	9%	570	46
Corporate	52,679	37,383	48%	17,859	1,429
Retail	52,060	51,147	17%	8,828	706
- of which mortgage	38,344	38,234	11%	4,336	347
- of which other retail	13,017	12,294	35%	4,306	344
- of which SME	699	620	30%	186	15
Other non-credit obligation assets	276	276	100%	276	22
Total IRB approach	**111,599**	**95,111**	**29%**	**27,532**	**2,203**
Standardised exposure classes					
Central government and central banks	13,999	13,885	0%	52	4
Regional governments and local authorities	2,213	1,367	0%		
Institutions	704	694	21%	143	11
Corporates	123	68	100%	68	5
Retail	1,171	856	75%	642	51
Exposures secured by real estate					
Other[1]	1,187	1,183	57%	675	54
Total standardised approach	**19,397**	**18,053**	**9%**	**1,581**	**126**
Total	**130,996**	**113,164**	**26%**	**29,113**	**2,329**

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

4.5 Credit risk exposure

4.5.1 *Exposure by exposure class and exposure type*

Table 4.3 shows exposures split by exposure class and exposure type. The average quarterly exposure in 2013, split by exposure type and exposure class is presented in Table 4.4.

Table 4.3 Exposure split by exposure class and exposure type, 31 December 2013

EURm	On-balance sheet items	Off-balance sheet items	Securities financing	Derivatives	Total
IRB exposure classes					
Institutions	6,182	116		6	6,304
Corporates	31,835	5,548			37,383
Retail	47,743	3,405			51,147
- of which mortgage	37,885	349			38,234
- of which other retail	9,486	2,808			12,294
- of which SME	372	248			620
Other non-credit obligation assets	276				276
Total IRB approach	**86,036**	**9,068**		**6**	**95,111**
Standardised exposure classes					
Central governments and central banks	13,748	137			13,885
Regional governments and local authorities	1,281	86			1,367
Institutions	539	11	66	78	694
Corporates	14	55			68
Retail	839	17			856
Exposures secured by real estate					
Other[1]	1,183				1,183
Total standardised approach	**17,604**	**305**	**66**	**78**	**18,053**
Total exposure	**103,640**	**9,374**	**66**	**84**	**113,164**

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

Table 4.4 Average quarterly exposure during 2013, split by exposure class and exposure type

EURm	On-balance sheet items	Off-balance sheet items	Securities financing	Derivatives	Total
IRB exposure classes					
Institutions	6,510	122		8	6,640
Corporates	32,364	5,289			37,652
Retail	47,832	3,511		0	51,343
- of which mortgage	37,429	280			37,710
- of which other retail	10,002	2,982			12,984
- of which SME	400	249		0	649
Other non-credit obligation assets	359				359
Total IRB approach	**87,065**	**8,921**		**8**	**95,994**
Standardised exposure classes					
Central governments and central banks	11,815	156			11,971
Regional governments and local authorities	1,179	62			1,241
Institutions	390	9	16	177	592
Corporates	14	55			69
Retail	759	16			776
Exposures secured by real estate					
Other[1]	1,167	0			1,167
Total standardised approach	**15,325**	**298**	**16**	**177**	**15,817**
Total exposure	**102,390**	**9,219**	**16**	**185**	**111,811**

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

4.5.2 *Exposure by geography*

Table 4.5 splits exposure by geography, based on where the exposure is booked.

Table 4.5 Exposure split by exposure class and geography, 31 December 2013

EURm	Nordic countries	- of which Denmark	- of which Finland	- of which Norway	- of which Sweden	Baltic countries	Poland	Russia	Other[2]	Total
IRB exposure classes										
Institution	6,304	6,304								6,304
Corporate	37,383	37,383								37,383
Retail	51,147	51,147								51,147
- of which mortgage	38,234	38,234								38,234
- of which other retail	12,294	12,294								12,294
- of which SME	620	620								620
Other non-credit obligation assets	276	276								276
Total IRB approach	**95,111**	**95,111**								**95,111**
Standardised exposure classes										
Central governments and central banks	13,885	13,885								13,885
Regional governments and local authorities	1,367	1,367								1,367
Institution	694	694								694
Corporate	68	68								68
Retail	856	856								856
Exposures secured by real estates										
Other[1]	1,183	1,183								1,183
Total standardised approach	**18,053**	**18,053**								**18,053**
Total exposure	**113,164**	**113,164**								**113,164**

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.
2) Includes International Units

4.5.3 *Exposure by industry*

In Table 4.6 the total exposure is split by industry and by the main exposure classes. The industry breakdown mainly follows the Global Industries Classification Standard (GICS) and is based on NACE codes (statistical classification codes of economic activities in the European community).

Table 4.6 Exposure split by industry group and by main exposure class, 31 December 2013

	IRB approach				Standardised approach		
EURm	Institutions	Corporates	Retail	Other	Central governments and central banks	Regional governments and local authorities	Other [1]
Retail mortgage			38,234				
Other retail			12,294				856
Central and local governments					3,110	1,367	
Banks	5,102				10,776		720
Industry group							
Construction and engineering		488	54				0
Consumer durables (cars, appliances, etc.)		314	8				0
Consumer staples (food, agriculture etc.)		7,633	65				
Energy (oil, gas, etc.)		15	0				
Health care and pharmaceuticals		291	22				1
Industrial capital goods		656	5				
Industrial commercial services		4,702	76				111
IT software, hardware and services		293	13				3
Media and leisure		516	30				0
Metals and mining materials		22	0				
Other financial institutions	1,202	3,203	23				260
Other materials (chemical, building materials, etc.)		626	9				0
Other, public and organisations		3,269	75	276			850
Paper and forest materials		248	3				0
Real estate management and investment		7,752	106				0
Retail trade		3,911	107				0
Shipping and offshore		869	1				
Telecommunication equipment		2	0				
Telecommunication operators		181	1				
Transportation		553	17				0
Utilities (distribution and production)		1,840	6				
Total exposure	**6,304**	**37,383**	**51,147**	**276**	**13,885**	**1,367**	**2,801**

1) Administrative bodies and non-commercial undertakings, multilateral developments banks, standardised institutions, standardised corporates, standardised retail, standardised exposures secured by real estate, past due items, short term claims, covered bonds and other items.

4.5.3.1 Specification of exposure against central governments and central banks

Nordea applies the standardised approach for exposure to central governments and central banks. In this approach, the rating from an eligible rating agency is converted to a credit quality step (the mapping is defined by the financial supervisory authorities). Each credit quality step corresponds to a fixed risk weight. Nordea uses Standard & Poor's as eligible rating agency. Table 4.7 presents the central government and central bank exposure distributed by credit quality steps.

Table 4.7 Exposures to central governments and central banks, distributed by credit quality step, 31 December 2013

Credit quality step	Standard & Poor's rating	Risk weight	Exposure (EURm)
1	AAA to AA-	0%	13,833
2	A+ to A-	20%	
3	BBB+ to BBB-	50%	
4 to 6 or blank	BB+ and below, or without rating	100 - 150%	52
Total			**13,885**

4.5.4 *Specification of off-balance exposure*

For the RWA calculation, off-balance amount are converted to on-balance equivalents through the application of a CCF between 0% and 100%. The main categories within off-balance sheet items are guarantees, credit commitments and unutilised lines of credit. Credit commitments and unutilised lines of credit constitute external commitments that have not been utilised. The CCF is set depending on the calculation approach, product type and whether the commitments are unconditionally cancellable or not.

For the IRB retail portfolio an internal CCF model is used. The model is built on a product based approach. There are three explanatory variables that determine which CCF value an IRB retail off-balance exposure will receive: customer type, product type and country in which the reporting is made. The CCF is based on internal estimates of the expected total exposure at the time of default. Table 4.8 shows the weighted average CCF for the IRB retail exposure.

Table 4.8 Average credit conversion factors and off-balance exposure split by IRB exposure class, 31 December 2013

EURm	Exposure after substitution effects	Exposure	CCF
Retail	4,302	3,405	79%
- of which mortgage	458	349	76%
- of which other retail	3,524	2,808	80%
- of which SME	320	248	78%

4.5.5 *Counterparty credit risk*

Counterparty credit risk is the risk that Nordea's counterpart in an FX, interest, equity, credit or commodity 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), which means the terms connected to the specific contract are individually defined and agreed on 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. Group Treasury also uses interest rate swaps and other derivatives in its hedging activities of the assets and liability mismatches in the balance sheet. Furthermore, Nordea may, within clearly defined restrictions, use derivatives to take open positions in its operations. Derivatives affect counterparty credit 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.

4.5.5.1 Pillar I method for counterparty credit risk

The mark-to-market method, also called the current exposure method (CEM), is used to calculate the exposure for counterparty credit risk in accordance with the credit risk framework in the CRD, i.e. the sum of current exposure (replacement cost) and potential future exposure. The potential future exposure is an estimate reflecting possible changes in the future market value of the individual contract during the

remaining life of the contract and is measured as the notional principal amount multiplied by the add-on factor. The size of the add-on factor depends on the contract's underlying asset and time to maturity.

Table 4.9 shows the CCR exposures as well as RWA split by exposure class.

Table 4.9 Counterparty credit risk by exposures by exposure class, 31 December 2013

EURm	Exposure	RWA
IRB exposure classes		
Institution	6	1
Corporate		
Retail		
Total IRB approach	**6**	**1**
Standardised exposure classes		
Central government and central banks		
Other	78	16
Total standardised approach	**78**	**16**
Total exposure	**84**	**17**

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

4.5.5.2 Counterparty credit risk for internal credit limit purposes

Counterparty credit risk for internal credit limit purposes is, for Nordea Bank Danmark's OTC derivatives exposure, calculated using a simulation model, based on a stressed calibration. Model parameters are based on data from a specific three-year period, including a one-year period identified to have the most significant increase in credit spreads in recent times. Thereby general wrong-way risk is taken into account in counterparty credit risk management.

On traded OTC contracts, Nordea Bank Danmark 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.

4.5.5.3 Mitigation of counterparty credit risk exposure

To reduce the exposure towards single counterparties, risk mitigation techniques are used. The most common is the use of closeout netting agreements, which allows 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.

Table 4.10 shows counterparty credit risk mitigated through closeout netting and collateral agreements.

Table 4.10 Mitigation of counterparty credit risk exposure, 31 December 2013

EURm	Current exposure (gross)	Reduction from closeout netting agreements	Reduction from held collateral	Current exposure (net)
Total	**10**	**6**		**3**

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

4.5.5.4 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.

4.5.6 *Other items*

In the exposure class Other items, Nordea's equity holdings in the banking book are included. Investments in companies in which Nordea Bank Danmark holds over 10% of the capital are deducted from the capital base (see Table 2.1) and are hence not included in Other items. For more information about equity holdings in the banking book see section 5.7.

4.6 Rating and scoring

4.6.1 *Rating and scoring definition*

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

- The credit approval process
- Calculation of RWA
- Calculation of EC and expected loss (EL)
- Monitoring and reporting of credit risk
- Performance measurement using the economic profit (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 reflects only the risk of customer default. The rating scale in Nordea consists of 18 grades; from 6+ to 1– for non-defaulted customers and three grades from 0+ to 0– for defaulted customers. The default risk of each rating grade is quantified by a one-year PD. Rating grades 4– and better are comparable to investment grade as defined by 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.

Table 4.11 shows the mapping from the internal rating scale to the S&P's rating scale.

Table 4.11 Indicative mapping between internal ratings and the S&P rating scale

Rating

Internal	Standard & Poor's
6+, 6, 6-	AAA to AA-
5+, 5, 5-	A+ to A-
4+, 4, 4-	BBB+ to BBB-
3+, 3, 3-	BB+ to BB-
2+, 2, 2-,1+	B+ to B-
1, 1-	CCC
0+, 0, 0-	D

The mapping of the internal ratings to 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.

Ratings are assigned in conjunction with credit proposals and the annual review of the customers, and are approved by the credit committees. However, a customer is down-graded 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 different rating models for different customer types to better reflect the risk. Rating models have therefore been developed for several general as well as specific segments, such as real estate management and shipping. Different methods ranging from statistical to purely expert-based, depending on the segment in question, have been used when developing the rating models. The models are largely based on an overall framework, in which financial factors are combined with qualitative factors as well as customer factors.

Models used in the household segment and for the SME retail segment are based on scoring, which is a statistical technique used to predict the probability of customer default. The models are based on internal data and takes account specific characteristics as well as behavioural information of the customer. The models 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 scoring models, credit bureau information is used in the credit process. The scoring models are used to predict PDs, in order to calculate the economic capital and RWA for customers. The risk grade scale used for scored customers in order to represent the scores consists of 18 grades, named A+ to F– for non-defaulted customers and three grades from 0+ to 0– for defaulted customers.

Nordea has established an internal validation process in accordance with the CRD requirements with the aim to ensure and improve 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 models' ability to distinguish default risk on a relative basis, and cardinal accuracy, i.e. the ability to predict default levels.

The Parameters, Scoring and Rating Models Validation subcommittee, a sub-committee to the Asset and Liability committee and the Risk Committee, is responsible for the approval of the annual rating and scoring model validations, as well as approval of proposals concerning the credit risk model validation framework.

4.6.2 *Point-In-Time vs. Through-The-Cycle*

A point-in-time (PIT) rating system uses all currently available obligor-specific and aggregate information to assign obligors to risk buckets. All obligors within a risk grade share roughly the same unstressed PD, and an obligor's rating is expected to change rapidly as its economic prospects change. A through-the-cycle (TTC) rating system uses static and dynamic obligor characteristics but tends not to adjust ratings in response to

changes in macroeconomic conditions. The distribution of ratings across obligors will not change significantly over the business cycle, and an obligor's rating is expected to change only when its own dynamic characteristics change.

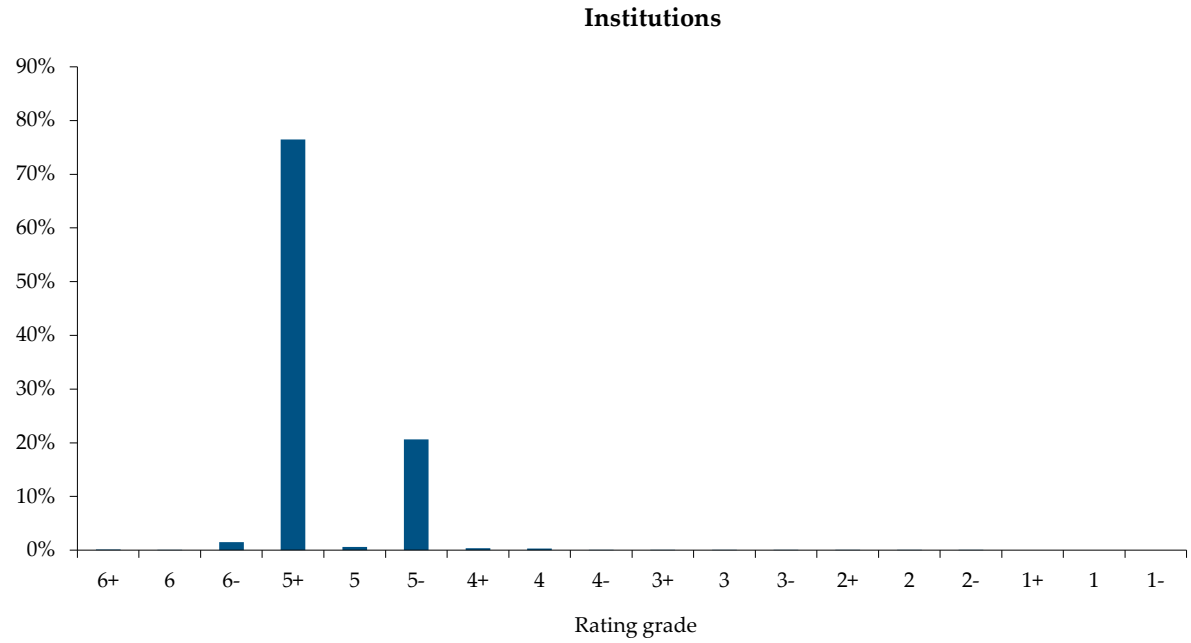
The rating models Nordea uses for exposure classes corporate and institution exhibits characteristics of both TTC and PIT rating philosophies. For the retail portfolio, Nordea currently employs a set of scoring models which are close to PIT.

4.6.3 *Rating and scoring distribution*

4.6.3.1 Rating distribution of the IRB institution portfolio

Figure 4.2 shows the rating grade distribution of the IRB institution portfolio. In December 2013, 100% (100%) of the institution exposure was found in the rating grades 4 and higher.

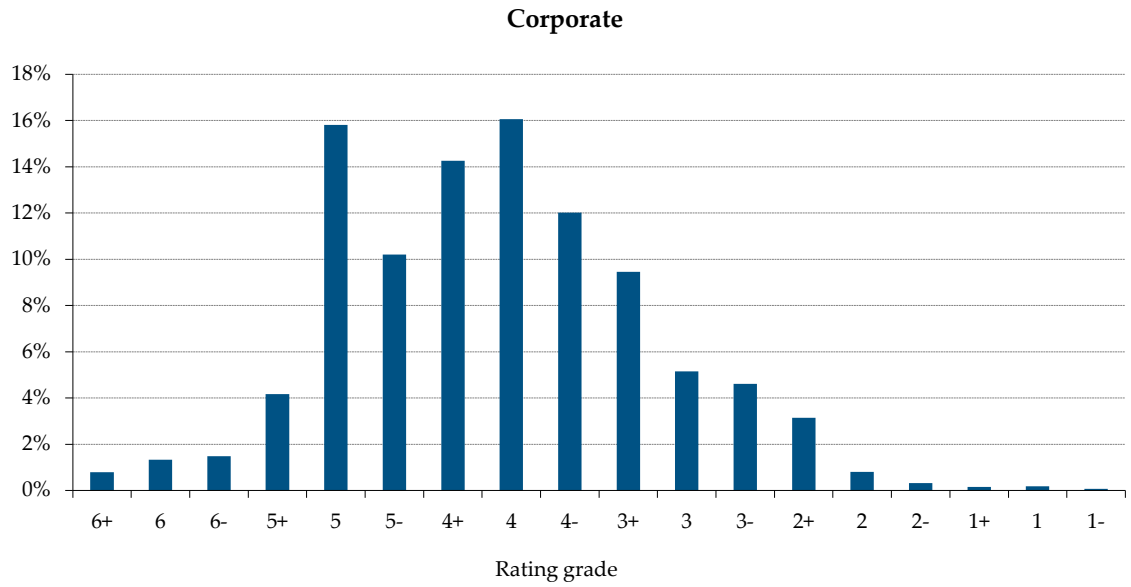
Figure 4.2 Exposure distributed by rating grade, IRB institution



4.6.3.2 Rating distribution of the IRB corporate portfolio

Figure 4.3 shows the rating grade distribution of the IRB corporate portfolio. In December 2013, 76% (75%) of the IRB corporate exposure was found in the rating grades 4- and above.

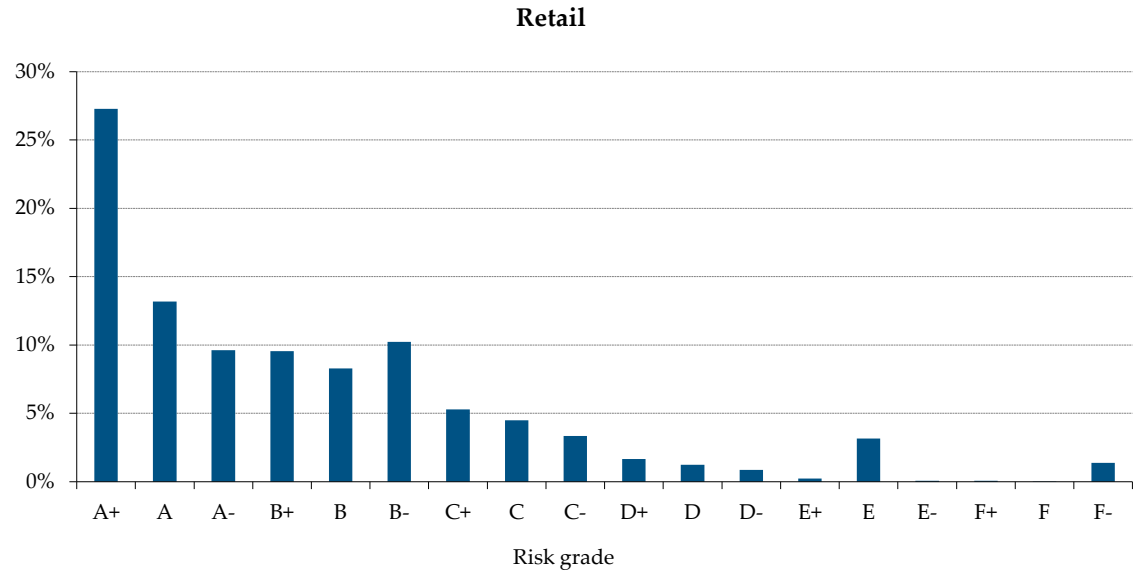
Figure 4.3 Exposure distributed by rating grade, IRB corporate



4.6.3.3 *Scoring distribution of the IRB retail portfolio*

Figure 4.4 shows the risk grade distribution of the IRB retail portfolio. As of end 2013, approximately 91% (90%) of the retail exposure was found in the risk grades C- and above.

Figure 4.4 Exposure distributed by rating grade, IRB retail



4.6.4 *Rating and scoring migration*

The rating and scoring distribution changes mainly due to three factors:

- Changes in rating/scoring for existing customers (pure migration).
- Different rating/scoring distribution of new customers and customers leaving Nordea, compared to the rating distribution of existing customers during the comparison period.
- Increased or decreased exposure per rating/scoring to existing customers.

Rating migration is affected by macroeconomic development, industry sector developments, changes in business opportunities and changes in the financial situation of customers and other company related factors.

Risk grade migration is affected by macroeconomic development and the customers' repayment capacity among other things.

4.7 Collateral

4.7.1 *Loss Given Default*

Table 4.12 shows the exposure secured by eligible collateral, guarantees and credit derivatives, split by exposure class.

Table 4.12 Exposure secured by collaterals, guarantees and credit derivatives, split by exposure class, 31 December 2013

EURm	Original exposure	Exposure	- of which secured by guarantees and credit derivatives	- of which secured by collateral	Average weighted LGD
IRB exposure classes					
Institution	6,584	6,304	44	2	14%
Corporate	52,679	37,383	806	15,784	40%
Retail	52,060	51,147	265	38,549	20%
- of which mortgage	38,344	38,234		38,047	14%
- of which other retail	13,017	12,294	128	288	38%
- of which SME	699	620	137	214	21%
Other non-credit obligation assets	276	276			n.a.
Total IRB approach	**111,599**	**95,111**	**1,115**	**54,335**	
Standardised exposure classes					
Central government and central banks	13,999	13,885	334		
Regional governments and local authorities	2,213	1,367			
Institution	704	694			
Corporate	123	68			
Retail	1,171	856			
Exposures secured by real estates					
Other [1]	1,187	1,183			
Total standardised approach	**19,397**	**18,053**	**334**		

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.

4.7.1.1 Guarantees and credit derivatives

The guarantees used as credit risk mitigation are to a large extent 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 IRB approach for credit risk. All central governments, regional governments and institutions are eligible as well as some multinational development banks and international organisations. Guarantees issued by corporate entities can only be taken into account if their rating corresponds to A– (S&P's rating scale) or better.

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

4.7.1.2 Collateral distribution

Table 4.13 presents the distribution of collateral used in the capital adequacy calculation process. The table shows real estate to have the major share of eligible collateral items in relative terms.

Table 4.13 Distribution of collateral, 31 December 2013

Financial collateral	1%
Receivables	0%
Residential real estate	71%
Commercial real estate	26%
Other physical collateral	2%

4.7.1.3 Valuation principles of collateral

A conservative approach with long-term market values taking volatility into account is used as valuation principle for collaterals when defining the maximum collateral ratio. Valuation and hence eligibility of collaterals 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 time frame.
- 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.
- Forced sale principle: assessment of market value or the collateral value must reflect that realisation of collaterals in a distressed situation is initiated by Nordea.
- 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.

4.8 Estimation and validation of credit risk parameters

Nordea has established an internal process, aimed at ensuring and improving the performance of models, procedures and systems and at ensuring the accuracy of the parameters.

The PD, LGD and CCF parameters are validated 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 frequency (ADF).

The PD estimation, and hence the validation, takes into account that the rating models used for corporate and institution customers have 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 4.14 shows expected loss, actual gross loss and net loss for the last three years.

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

Table 4.14 Expected loss vs. gross loss and net loss

	Retail household					
EURm	Mortgage	Other	Corporate[1]	Institution	Government	**Total**
2013						
EL	-18	-60	-59	-2	0	**-139**
Gross loss	-80	-204	-448			**-732**
Net loss	-47	-95	-228			**-370**
2012						
EL	-22	-40	-80	-2	0	**-144**
Gross loss	-86	-284	-602			**-972**
Net loss	-62	-161	-357			**-580**
2011						
EL	-28	-47	-95	-2	0	**-172**
Gross loss	-47	-206	-544			**-797**
Net loss	-38	-144	-246			**-429**

1) Includes SME retail.

4.9 Impaired loans and loan losses

In the tables 4.15-4.18 impaired loans, loan losses and allowances are distributed and stated according to International Financial Reporting Standard (IFRS) as in the Annual Report which differs somewhat from CRD.

4.9.1 *Definition and methodology of impairment*

Weak and impaired exposure is closely and continuously monitored and reviewed at least quarterly in terms of current performance, business outlook, future debt service capacity and the possible need for provisions. A need for provisioning is recognised if there is objective evidence, based on loss events or observable data, that there is an impact on the customer's future cash flow to the extent that full repayment is unlikely, collaterals taken into account. Exposures with provision are considered impaired. The size of the provision is equal to the estimated loss, which is the difference between the book value of the outstanding exposure and the discounted value of the future cash flow, including the value of pledged collaterals. Impaired exposure can be either performing or non-performing. Exposures that are past due more than 90 days is 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 as impaired. Collective impairment is based on the migration of rated and scored customers in the credit portfolio. The assessment of collective impairment relates to both up- and downgrades of customers, as well as new customers entering and those leaving the portfolio. Moreover, customers going to and from default affect 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 a group of loans represent an interim step pending the identification of impairment losses for an individual customer.

Table 4.15 Loans and receivables, impaired loans, allowances and provisioning ratios, split by customer type, 31 December 2013

EURm	Loans after allowances	Impaired loans before allowances	Impaired loans in % of loans and receivables	Allowances for collectively assessed loans	Specific allowances	Total provisioning ratio
To central banks and credit institutions	**10,662**	**0**	**0.00**	**0**	**0**	
- of which central banks	9,117	0	0.00	0	0	
- of which credit institutions	1,545	0	0.00	0	0	0%
To the public	**80,552**	**3,677**	**4.57**	**142**	**1,318**	**40%**
- of which corporate	38,274	2,462	6.43	116	848	39%
Construction and engineering	1,156	135	11.68	2	37	29%
Consumer durables (cars, appliances, etc.)	329	39	11.87	1	51	135%
Consumer staples (food, agriculture, etc.)	8,059	779	9.66	29	213	31%
Energy (oil, gas, etc.)	4	0	0.00	0	0	
Financial institutions	569	17	2.90	0	4	27%
Health care and pharmaceuticals	365	6	1.64	2	3	76%
Industrial capital goods	5,788	246	4.26	5	64	28%
Industrial commercial services, etc.	754	29	3.88	1	9	35%
IT software, hardware and services	902	61	6.75	1	27	46%
Media and leisure	23	1	4.88	0	0	36%
Metals and mining materials	3,157	214	6.77	1	95	45%
Other materials (chemical, building materials, etc.)	544	59	10.78	2	18	33%
Other, public and organisations	1,535	96	6.23	1	49	53%
Paper and forest materials	357	5	1.38	1	1	42%
Real estate management and investment	8,057	389	4.82	30	111	36%
Retail trade	3,765	179	4.77	18	73	51%
Shipping and offshore	661	166	25.07	18	76	57%
Telecommunication equipment	4	0	0.70	0	0	60%
Telecommunication operators	57	1	0.89	0	0	81%
Transportation	666	35	5.27	2	12	40%
Utilities (distribution and production)	1,523	7	0.44	1	4	71%
- of which household	40,564	1,216	3.00	26	470	41%
Mortgage financing	28,851	591	2.05	10	56	11%
Consumer financing	11,713	625	5.34	17	415	69%
- of which public sector	1,715	0	0.00	0	0	
Total loans in the banking operations	**91,215**	**3,677**	**4.03**	**142**	**1,318**	**40%**
Lending in the life insurance operations						
Total including life insurance operations	**91,215**	**3,677**	**4.03**	**142**	**1,318**	**40%**

Table 4.16 Loans to the public, impaired loans, allowances and provisioning ratios, split by geography, 31 December 2013

EURm	Loans after allowances	Impaired loans before allowances	Impaired loans in % of loans	Allowances for collectively assessed loans	Specific allowances	Total provisioning ratio
Nordic countries	77,621	3,659	4.71	142	1,301	39%
- of which Denmark	77,144	3,627	4.70	142	1,270	39%
- of which Finland	118	0	0.00	0	0	
- of which Norway	86	1	0.91	0	1	100%
- of which Sweden	273	31	11.41	0	31	98%
Estonia	16	2	14.40	0	2	100%
Latvia	19	0	1.59	0	0	97%
Lithuania	21	1	3.42	0	1	100%
Poland	145	0	0.00	0	0	
Russia	4	0	0.00	0	0	
EU countries other	1,139	6	0.56	0	6	93%
USA	105	0	0.29	0	0	73%
Asia	298	1	0.22	0	0	100%
Latin America	108	6	5.78	0	6	100%
OECD other	203	1	0.37	0	1	100%
Non-OECD other	874	1	0.06	0	0	100%
Total	**80,552**	**3,677**	**4.57**	**142**	**1,318**	**40%**

Table 4.17 Reconciliation of allowance accounts for impaired loans, 2013

	Group			Parent company		
Loans and receivables, EURm	Ind. assessed	Coll. assessed	Total	Ind. assessed	Coll. assessed	Total
Opening balance at 1 Jan 2013	**-1,284**	**-113**	**-1,397**	**-1,100**	**-76**	**-1,176**
Provisions	-574	-93	-667	-455	-83	-538
Reversals	255	63	318	199	49	248
Changes through the income statement	**-319**	**-30**	**-349**	**-256**	**-33**	**-290**
Allowances used to cover write-offs	280	0	280	210	0	210
Currency translations differences	5	0	5	5	0	5
Closing balance at 31 Dec 2013	**-1,318**	**-142**	**-1,461**	**-1,141**	**-110**	**-1,251**

Table 4.18 Loan losses, 2013
EURm

Loan losses divided by class, net	
Loans and receivables to credit institutions	0
- of which write-offs and provisions	0
- of which reversals and recoveries	0
Loans and receivables to the public	-379
- of which write-offs and provisions	-719
- of which reversals and recoveries	340
Off-balance sheet items	18
- of which write-offs and provisions	-5
- of which reversals and recoveries	22
Total	**-361**
Specification of loan losses	
Changes of allowance accounts in the balance sheet	-331
- of which loans and receivables	-349
- of which off-balance sheet items	18
Changes directly recognised in the income statement	-30
- of which realised loan losses	-52
- of which realised recoveries	22
Total	**-361**

5. Market risk

The market risk taking activities of Nordea Bank Danmark are primarily focused on the Nordic and European markets. The total consolidated market risk for Nordea Bank Danmark, measured by VaR, was EUR 12m on average in 2013, compared to EUR 26m in 2012. The total market risk, measured by VaR, is primarily driven by interest rate risk.

5.1 Management, governance and measurement of market risk

Market risk is defined as the risk of value loss in Nordea's holdings and transactions as a result of changes in market rates and parameters that affect the market value, for example changes to interest rates, credit spreads, FX rates, equity prices, commodity prices and option volatilities.

5.1.1 *Management of market risk*

Nordea Markets and Group Treasury are the key contributors to market risk in the Nordea Group. Nordea Markets is responsible for the customer-driven trading activities, whereas Group Treasury is responsible for funding activities, asset and liability management, liquidity portfolios, pledge/collateral portfolios and investments for Nordea's own account. For all other banking activities, the basic principle is that market risks are transferred to Group Treasury where the risks are managed.

5.1.1.1 Structural market risks

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 structural interest income risk (SIIR).

5.1.2 *Governance of market risk*

Group Risk Management has the operational responsibility for the development and maintenance of the group-wide market risk framework. The framework defines common management principles and policies for the market risk management in the Nordea Group. These principles and policies are approved by the Group Board of Directors and have been endorsed by the Board of Directors in Nordea Bank Danmark. The same reporting and control processes are applied for market risk exposures in both the trading and banking books, on a Nordea Group level as well as in Nordea Bank Danmark.

Transparency in the risk management process is central to maintaining risk awareness and a sound risk culture throughout the organisation. This transparency is achieved through:

- A comprehensive Group-wide policy framework, in which responsibilities and objectives are explicitly outlined and in which the risk appetite is clearly defined.
- Clearly defined risk mandates, in terms of limits and restrictions on which instruments may be traded.
- A framework for approval of traded financial instruments and valuation methods that require an elaborate analysis and documentation of the instruments' features and risk factors.
- Proactive information sharing between trading and risk control.
- Timely reporting to senior management on market risk development. The Group CRO receives reporting on the Group's consolidated market risk daily, whereas GEM, the Board of Directors and associated risk committees receive reports on a monthly basis. The Board of Directors in Nordea Bank Danmark receives a report of Nordea Bank Danmark's consolidated market risk quarterly.

5.1.3 *Measurement of market risk*

As there is no single risk measure that captures all aspects of market risk, Nordea uses several risk measures including Value-at-Risk (VaR), stressed VaR, stress testing, scenario simulation and other non-statistical risk measures such as basis point values, net open positions and option key figures.

5.1.3.1 Value-at-Risk

Nordea calculates VaR using historical simulation. This means that the current portfolio is revaluated using the daily changes in market prices and parameters observed during the last 500 trading days, thus generating a distribution of 499 returns based on empirical data. From this distribution, the expected shortfall method is used to calculate a VaR figure, meaning that the VaR figure is based on the average of the worst outcomes from the distribution. The 1-day VaR figure is subsequently scaled to a 10-day figure. The 10-day VaR figure is used to limit and measure market risk at all levels both in the trading book and in the banking book.

Separate VaR figures are calculated for interest rate, credit spread, foreign exchange rate and equity risks. The total VaR includes all these risk categories and allows for diversification among them. The VaR figures include both linear positions and options. The model has been calibrated to generate a 99% VaR figure. This means that the 10-day VaR figure can be interpreted as the loss that will be exceeded in one of hundred 10-day trading periods.

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. While historical simulation has the advantage of not being dependent on a specific assumption regarding the distribution of returns, it should be noted that the historical observations of the market variables that are used as input, may not give an adequate description of the behaviour of these variables in the future. The choice of the time period used is also important. While using a longer time period may enhance the model's predictive properties and lead to reduced cyclicality, using a shorter time period increases the model's responsiveness to sudden changes in the volatility of financial markets. The choice of using the last 500 days of historical data has thus been made with the aim to strike a balance between the pros and cons from using longer or shorter time series in the calculation of VaR.

5.1.3.2 Stressed VaR

Stressed VaR is calculated using a similar methodology as the ordinary VaR measure. However, whereas the ordinary VaR model is based on data from the last 500 days, stressed VaR is based on a specific 250 day period with considerable stress in financial markets. Since the relevant period with stressed markets will depend on the positions currently held in the portfolio, the level of the stressed VaR in relation to the ordinary VaR is monitored continuously. Further analysis may be conducted if deemed necessary, which may lead to a change of the period. The specific period to be used is evaluated at least once every year.

5.1.3.3 Stress testing

Stress tests are used to estimate the possible losses that may occur under extreme market conditions. The main types of stress tests include:

1. 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.
2. Sensitivity tests, where rates, prices, and/or volatilities are shifted markedly to emphasize exposure to situations where historical correlations 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.
3. Reversed stress tests. These assess and try to identify the type of events that could lead to losses equal to or greater than a pre-defined level.

Subjective stress tests and sensitivity tests are conducted periodically for the consolidated risk across the banking book and trading book. Reversed stress tests are conducted quarterly for the trading book.

While these stress tests measure the risk over a shorter time horizon, market risk is also a part of Nordea's comprehensive firm-wide ICAAP stress test, which measures the risk over a three-year horizon. For further information on group-wide stress tests, see chapter 9.

5.2 Consolidated market risk for Nordea Bank Danmark

The consolidated market risk for Nordea Bank Danmark presented in Table 5.1 includes both the trading book and the banking book. Total VaR was EUR 16m at the end of 2013 (EUR 17m at the end of 2012). The main contributor to total VaR was interest rate risk, with the largest part of the interest rate sensitivity stemming from interest rate positions in DKK, USD and EUR.

Table 5.1 Consolidated market risk figures for Nordea Bank Danmark, 31 December 2013

EURm	Measure	31 Dec 2013	2013 high	2013 low	2013 avg	31 Dec 2012
Total risk	VaR	16.2	23.4	6.8	12.4	17.2
- Interest rate risk	VaR	16.4	22.6	3.1	10.5	14.2
- Equity risk	VaR	1.5	12.9	1.3	4.5	11.5
- Foreign exchange risk	VaR	1.2	1.9	0.7	1.0	0.7
Diversification effect		16%	42%	12%	24%	35%

5.3 Market risk for the trading book

The market risk for the trading book in Nordea Bank Danmark is presented in Table 5.2. Total VaR was EUR 5m at the end of 2013 (EUR 15m at the end of 2012). The main contributor to total VaR was interest rate risk, with the largest part of the interest rate sensitivity stemming from interest rate positions in DKK and EUR.

Table 5.2 Market risk (VaR) figures in the trading book, 31 December 2013

EURm	Measure	31 Dec 2013	2013 high	2013 low	2013 avg	31 Dec 2012
Total risk	VaR	4.8	14.9	1.4	3.5	15.0
- Interest rate risk	VaR	5.0	14.8	0.2	2.1	15.8
- Equity risk	VaR	1.7	4.8	1.1	2.2	3.7
- Foreign exchange risk	VaR	0.5	2.0	0.5	1.1	1.1
Diversification effect		32%	56%	9%	38%	27%
Total stressed VaR	sVaR	9.0	16.7	2.9	6.3	17.0

5.4 Capital requirements for market risk in the trading book (Pillar I)

Market risk in the CRD context contains two categories: general risk and specific risk. General risk is related to changes in overall market prices and specific risk is related to price changes for specific issuers. When calculating the capital requirements for market risk using the internal model approach, general risk is based on VaR and stressed VaR.

Nordea Bank Danmark uses the internal model approach to calculate the market risk capital requirements for the predominant part of the trading book. However, for specific interest rate risk, specific equity risk and commodity risk the market risk capital requirements are calculated using the standardised approach. The use of the internal model approach in Nordea Bank Danmark is shown in Table 5.3.

In addition to positions in the trading book, market risk capital requirements also cover FX risk in the banking book through the standardised approach.

By the end of 2013, RWA and the capital requirements for market risk in the trading book were EUR 963m (EUR 1,911m) and EUR 77m (EUR 153m), respectively. The decomposition of the current figures is presented in Table 5.4. RWA was significantly reduced during the year as a consequence of reduced risk levels in the trading book (mainly interest rate risk)

Table 5.3 Methods for calculating capital requirements

	Interest rate risk		Equity risk		
	General	Specific	General	Specific	FX risk
Nordea Bank Danmark	IA	SA	IA	SA	IA

IA: internal model approach, SA: Standardised approach

Table 5.4 RWA and capital requirements for market risk, 31 December 2013

	Trading book, IA		Trading book, SA		Banking book, SA		Total	
EURm	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement	RWA	Capital requirement
Interest rate risk[1]	143	11	50	4			194	15
Equity risk	77	6	305	24			382	31
Foreign exchange risk	47	4					47	4
Commodity risk			3				3	
Diversification effect	-93	-7					-93	-7
Stressed VaR	331	26					331	26
Total	**505**	**40**	**358**	**28**	**100**	**0**	**863**	**69**

1) Interest rate risk in column IA only includes general interest rate risk while column SA includes both general and specific interest rate risk

5.4.1 *Backtesting*

Backtesting of the VaR models is conducted on a daily basis in accordance with the guidelines laid out by the Basel Committee on Banking Supervision (BCBS). Backtests are conducted using both hypothetical profit/loss and actual profit/loss (hypothetical profit/loss is the profit/loss that would have been realised if the positions in the portfolio had been held constant during the following trading day). The profit/loss is in the backtest compared to one-day VaR figures.

5.5 Interest rate risk in the banking book

Monitoring of the interest rate risk in the banking book is done daily by measuring and monitoring VaR on the banking book and by controlling interest rate sensitivities, which measure the immediate effects of interest rate changes on the economic values of assets, liabilities and off-balance sheet items. As of end 2013, the interest rate VaR in the banking book of Nordea Bank Danmark was EUR 20m (EUR 8m at the end of 2012). Table 5.5 shows the net effect on economic value of a parallel shift in rates of up to 200 basis points.

Table 5.5 Interest rate sensitivities for the banking book, instantaneous interest rate movements, 31 December 2013

EURm	+200bp	+100bp	+50bp	-50bp	-100bp	-200bp
DKK	-42.3	-21.2	-10.6	10.6	21.2	42.3
USD	5.4	2.7	1.4	-1.4	-2.7	-5.4
EUR	3.0	1.5	0.8	-0.8	-1.5	-3.0
Total	**-36.2**	**-18.1**	**-9.0**	**9.0**	**18.1**	**36.2**

The totals are netted and include currencies not specified.

5.6 Structural Interest Income Risk

Structural Interest Income Risk (SIIR) is the amount Nordea's accumulated net interest income would change during the next 12 months if all interest rates were to change by one percentage point. SIIR reflects the mismatch in the balance sheet items and the off-balance sheet items when the interest rate repricing 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 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.

5.6.1 *SIIR measurement methods*

Nordea's SIIR is measured through dynamic simulations by calculating several net interest income scenarios and comparing the difference between these scenarios. Several interest rate scenarios are applied, but the basic measures for SIIR are the two scenarios (increasing rates and decreasing rates). These scenarios measure the effect on Nordea's net interest income for a 12 month period of a one percentage point increase, respectively decrease, in all interest rates (note that Table 5.6 below also covers repricing gaps over 12 months). The balance sheet is assumed to be constant over time, however main elements of the customer behaviour and Nordea's decision-making process concerning Nordea's own rates are however taken into account.

5.6.2 *SIIR analysis*

At the end of the year, the SIIR for increasing market rates in Nordea Bank Danmark was EUR 212m (EUR 166m) and the SIIR for decreasing market rates was EUR –78m (EUR –42m). These figures imply that net interest income would increase if interest rates rise and decrease if interest rates fell.

Table 5.6 Repricing gap analysis, scenario of a one percentage point increase in all rates, 31 December 2013

		Interest rate fixing period							
EURm	Group balance sheet	Within 3 months	3-6 months	6-12 months	1-2 years	2-5 years	>5 years	Non-repricing	Total
Interest-bearing assets	103,837	50,420	4,447	5,683	6,791	16,028	20,406	64	103,837
Non-interest bearing assets	6,924	0	0	0	0	0	0	6,924	6,924
Total assets	**110,761**	**50,420**	**4,447**	**5,683**	**6,791**	**16,028**	**20,406**	**6,987**	**110,761**
Interest-bearing liabilities	100,297	35,603	4,850	6,023	9,488	10,337	12,930	21,065	100,297
Non-interest bearing liabilities	10,464	0	0	0	0	0	0	10,464	10,464
Total liabilities and equity	**110,761**	**35,603**	**4,850**	**6,023**	**9,488**	**10,337**	**12,930**	**31,530**	**110,761**
Off-balance sheet items, net		**11,924**	**-3,273**	**-1,895**	**-710**	**-4,657**	**-1,390**	**0**	
Exposure		**26,741**	**-3,676**	**-2,234**	**-3,408**	**1,033**	**6,086**	**-24,543**	
Cumulative exposure			**23,065**	**20,831**	**17,423**	**18,456**	**24,542**	**-1**	

SIIR impact of increasing interest rates for the year 2014				
Impact[1]	234	-17	-6	
Cumulative SIIR impact		217	212	

1) Impact is calcated based on +100bps change on exposure

5.7 Equity risk in the banking book

In Table 5.7, the equity holdings in the banking book are grouped based on the intention of the holding. All equities in the table are carried at fair value. The portfolio of illiquid alternative investments is included with a fair value of EUR 470m (EUR 556m), of which private equity funds EUR 255m, hedge funds EUR 117m and credit funds EUR 97m. All three types of investments are spread over a number of funds in Nordea Bank Danmark.

Table 5.7 Equity holdings in the banking book, 31 December 2013

EURm	Book value	Fair value	Unrealised gains/losses[3]	Realised gains/losses[3]	Capital requirement
Investment portfolio[1]	497	497	48	27	40
Other[2]	43	43	-2	1	3
Total	**540**	**540**	**46**	**28**	**43**
1) Of which listed equity holdings	6				
2) Of which listed equity holdings	48				
3) Result for 2013					

5.8 Determination of fair value of financial instruments

Fair value is defined in IFRS 13 as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is the existence of published price quotations in an active market and when such prices exist they are used for the assignment of fair value. Published price quotations are predominantly used to establish fair value for items disclosed under the following balance sheet items:

- Treasury bills
- Interest-bearing securities
- Shares
- 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. These are designed to apply observable market prices and rates as input whenever possible, but can also make use of unobservable model parameters. Nordea uses valuation techniques to establish fair value for OTC derivatives and for securities and shares for which quoted prices in an active market are not available.

The calculation of fair value using valuation techniques is supplemented by a portfolio adjustment for uncertainties associated with the model assumptions and uncertainties associated with the portfolio's counterparty credit risk and liquidity risk.

If non-observable data has a significant impact on the valuation, the instrument cannot be recognised initially at fair value and any upfront gains are therefore deferred and amortised 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 Risk Management and all models are reviewed on a regular basis.

The valuation framework is a joint responsibility between the Group CFO and the Group CRO. The Group Valuation Committee, a sub-committee to the Risk Committee consisting of senior management representatives from Group Finance, Group Risk Management and the control organisations in the business divisions, serves as an oversight committee and supports the CFO and CRO on different issues in relation to the framework, including standards for valuation and processes for valuation and valuation control.

5.8.1 *Compliance with requirements applicable to exposure in the trading book*

The CRD outlines requirements for systems and controls. These systems and controls must be of sufficient quality to provide prudent and reliable valuation estimates. Nordea complies in all material aspects with these requirements. Overall valuation principles and processes are governed by the valuation policy which is developed and maintained by the Group Valuation Committee. The product control organisations in the individual business units are responsible for performing valuation controls in accordance with 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 set-up for valuation adjustments is designed to be compliant with the requirements in IFRS 13. Requirements in the CRD that are not supported by IFRS 13 are therefore not implemented. Nordea incorporates counterparty credit risk in OTC derivatives, bid/ask spreads and where judged relevant, also model risk.

6. Operational risk

Operational risk is inherent in all activities performed by Nordea Bank Danmark. Nordea Bank Danmark is included in the Nordea Group's processes for operational risk management.

6.1 Management, governance and measurement of operational risk

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 Nordea.

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.

6.1.1 *Management 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.

An important part of operational and compliance risk management is protecting the Group from being used for the purpose of money laundering and terrorist financing. Therefore the Group has strict processes concerning customer identification and verification, customer acceptance, monitoring of customer relations, record keeping, detection and reporting of suspicious activities and transactions and employee training to ensure adequate awareness.

Operational risks are managed based on common principles established for the Group. A common operating model and key processes are set forth in the Nordea Operational Risk Policy.

6.1.2 *Governance of operational risk*

Group 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 as well as educational and training activities are important components when managing operational risks.

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

The key principle for the management of operational risks in Nordea is the three lines of defence where the first line of defence is represented by the business organisation. Group Operational Risk and Compliance represents the second line of defence and has defined a common set of standards (Group Directives, processes and reporting) in order to manage operational risks. The network of risk and compliance officers (RCOs) ensures the implementation and roll-out of the common standards by advising the business organisation on how to manage operational and compliance risks and by monitoring and reporting on them. The RCOs work together with the business but is part of second line of defence. Group Internal Audit, representing the third line of defence, provides assurance to the Board of Directors on the risk management, control and governance processes.

A new operating model for operational risk management was established in 2013 and ensures both the independence of the risk and compliance officers and strengthens the cooperation between first and second line of defence. An Operational Risk and Compliance Committee, a sub-committee to the Group's Risk Committee, has been established and the main duties of the committee is to prepare proposals for the Risk Committee on framework, planning and policies and to approve activity plans and various risk assessments. The committee is chaired by the Chief Operational Risk Officer.

Improvements of anti-money laundering processes and routines have been a focus area since 2012 and in 2013 a Group-wide AML programme was established with a programme management office responsible for reporting on progress within the various AML related projects and initiatives across the Group.

A Group-wide BCM programme was also established during 2013 in order to improve the current BCM framework and it will run for three years. The programme includes several work streams, including a review of the existing operating model and governance structure, creation and verification of a Business Impact Analysis model and process, development of crisis management framework and improvement of governing policies.

Nordea uses external risk transfer in the form of insurance, including re-insurance, to cover certain aspects of crime risk and professional liability, including the liability of directors and officers. The Nordea Group furthermore uses insurance for travel, property and general liability purposes.

6.1.3 *Measurement of operational risk*

6.1.3.1 Key processes

Risk and control self-assessment

The risk and control self-assessment (RCSA) process puts focus on identifying key risks as well as ensuring fulfilment of requirements specified in Group directives.

The RCSA process is executed in the operational and compliance risk system where an operational risk library is used. The risk library is used for several processes which enables comparison of data across the processes. The division management assesses the risks in the risk library and estimate which risks are relevant for their organisation. The risks are identified both through top-down division management involvement and through bottom-up analysis of result from control questions as well as existing information from processes, e.g. incident reporting, scenario analysis quality and risk analyses, and product approvals. Upon identification of the risks, the estimated impact of risk materialisation is assessed and the mitigating actions are identified. The mitigating actions related to the most critical risks are followed up in the Group's risk appetite reporting. Mitigating actions to critical risks in Denmark are followed up separately in the local Danish risk appetite reporting.

The purpose of the RCSA is to identify, assess and prioritise operational risks as well as plan mitigating actions for prioritised risks and it provides for an overview of the overall risk picture. The results are used as input to the annual Operational and compliance risk map. Furthermore, the purpose of the control assessment part of the control assessment part of the RCSA is to verify whether Nordea adequately fulfils minimum legal requirements as specified in the Nordea Group Directives as well as to ensure a sufficient level of internal control in the Group. The time period (end of April – beginning of September) for answering aims at providing time for actions to be taken by the business to correct substandard matters, making the process an active tool for improvement rather than merely a status report.

Incident reporting

Incidents and security weaknesses are dealt with immediately in order to minimise damage. Upon detection of an incident, handling of the incident has first priority. The unit manager is responsible for the proper handling, documentation and reporting of the incidents and any quality deficiencies in the unit.

Incident reporting is a Group-wide process which is performed in the operational and compliance risk system by the risk and compliance officer in order to ensure consistent quality in the process. Nordea's operational risk library is used for categorising all incidents and the taxonomy reflects the Operational Riskdata eXchange Association's (ORX) reporting requirements. Nordea joined ORX in 2010 and since Q2 2011, Nordea delivers risk loss data on a quarterly basis to ORX.

The threshold levels for incidents are EUR 1,000 for minor incidents and EUR 20,000 for major incidents. Incidents with no direct financial loss are reported if there is a reputational, regulatory, process or other impact to it. Aggregated incident information is included in regular risk reports to the Risk Committee, GEM, the Board Risk Committee and the Board of Directors, and key observations are included in the Operational and compliance risk map and the semi-annual compliance report.

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.

Business continuity management covers the broad scope from the procedures for handling incidents in the organisation via escalation procedures to crisis management on Nordea Group level. As most service chains are supported by IT applications, disaster recovery plans for technical infrastructure and IT systems constitute the core of the business continuity management in Nordea.

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 programmes or projects, significant changes to organisations, processes, systems and procedures. Conducting a QRA is mandatory as part of the product approval process.

The Group-wide Scenario Analysis process aims to put focus on extreme operational risks. The objective of the process is to challenge and extend the Group's present understanding of its operational risk landscape as well as evaluate the potential financial impact of certain risks. The process has been run since 2012 and Nordea aims to further integrate this process in the existing RCSA process.

The two awareness programmes, one targeting senior management and one group-wide, which were introduced in 2011 will continue during 2014 with updated existing modules as well as launch of new topics. Modules about preventing bribery and corruption and AML, counter-terrorist financing and sanctions risk management has been run during 2013 and they were both part of the Group-wide programme Both programmes were mandatory and aimed to set the tone at the top and to increase the awareness of operational and compliance risk-related threats and challenges throughout the organisation. The next module which is about Operational Risk, will be launched in early 2014.

6.1.3.2 Key reports

Operational and compliance risk map

The results from RCSA process and the identification of top risks represent the main input to the Operational and compliance risk map. In the first part of the report, the Group's overall risk picture is illustrated in a dashboard including the RCSA results from scenario analysis process and Group loss data as well as an assessment of the development of each risk category in the Group's operational risk library. . The second part of the report supplies a risk overview for each of the business areas in the Group with a business area specific dashboard together with more detailed information on individual risks. The report is used as input to the Group's annual planning process in order to ensure adequate resource allocation to the planned mitigating actions. Mitigating actions are followed up on a quarterly basis within the risk appetite framework with detailed descriptions of the current development status. The Operational and compliance risk map is submitted to the Risk Committee, GEM, the Board Risk Committee and the Board of Directors on an annual basis. A local Operational and compliance risk map is submitted to Board of Directors of Nordea Bank Danmark.

Semi-annual compliance report

Semi-annual reporting on operational and compliance risks is done based on input from risk and compliance officers in the business. The risk and compliance officers are asked to make their own reflections on the division's future challenges, improvements and his/her own ability to work independently. Reporting also contains specific, ad hoc themes, focusing on areas that are relevant at current. The semi-annual Nordea Group compliance report is based on the risk and compliance officers' reports as well as Group Risk Managements's own observations and analysis of key compliance risks, incident reporting and other relevant data. Local compliance report is sent to the Board of Directors or Nordea Bank Danmark.

6.2 Capital requirements for operational risk

The capital requirements 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. Nordea Bank Danmark's capital requirements for operational risk for 2013 amounts to EUR 322m (EUR 325m). The capital requirements for operational risk are updated yearly.

7. Securitisation and credit derivatives

Nordea's role in securitisation has been limited to that of being a sponsor of various schemes together with some limited trading on credit derivatives as described below. Nordea has not participated in securitisation as originator and hence has not transferred loans or their risk outside of Nordea.

7.1 Introduction to securitisation and credit derivatives trading

The CRD defines securitisation as a scheme where the credit risk of underlying exposures is converted into marketable securities so that payments from these securities depend on the performance of the underlying exposures and a subordination scheme exists for determining how losses are distributed among investors to these securities. In a traditional securitisation, the ownership of these assets is transferred to a special purpose entity (SPE), which in turn issues securities backed by these assets. In synthetic securitisation, ownership of these assets does not change, however the credit risk is still transferred to the investor through the use of credit derivatives.

Banks have different roles in securitisations. First, they can act as originators by having assets they have originated themselves as underlying exposures. Second, they can act as sponsors in which role they establish and manage securitisations of assets from third party entities. Third, in their credit trading activity they can themselves invest in these types of marketable securities or create these exposures in credit derivatives markets.

Nordea has to date not acted as originator in securitisations. However, Nordea has sponsored various securitisation schemes which are described in the following section. Nordea is also acting as an intermediary in the credit derivatives market, especially in Nordic names. In addition to becoming exposed to the credit risk of a single entity, credit derivatives trading often involves buying and selling protection for collateralised debt obligation (CDO) tranches. These can be characterised as credit risk related financial products, the risk of which depends on the risk of a portfolio of single entities ('a reference portfolio') as well as the subordination. Subordination defines the level of defaults in the reference portfolio after which further defaults will create a credit loss for the investor in the CDO tranche. Because hedging CDO tranches always involves a view on how the correlation between the credit risk of single names evolves it has been customary to talk about correlation trading in this context. The market risk created by Nordea's correlation trading is described in further detail in section 7.3.

7.2 Traditional securitisations where Nordea acts as sponsor

Nordea sponsors a limited number of SPEs. These SPEs have been established to facilitate or secure customer transactions, either to enable investments in structured credit products, or with the purpose of supporting trade receivable or account payable securitisation for Nordea corporate customers. At year-end 2013, Nordea is sponsoring the SPEs presented in Table 7.1.

The decision to sponsor these SPEs has been made by senior management. The SPEs are monitored centrally to ensure appropriate purpose and governance. Nordea's role in these transactions has included acting as arranger, account bank, swap/FX counterparty, administrator, calculation agent and/or CP dealer.

In accordance with IFRS, Nordea does not consolidate SPEs' assets and liabilities beyond its control. In determining whether Nordea controls an SPE or not, Nordea makes judgements about risks and rewards from the SPE and assesses its ability to make operational decisions for the SPE. Nordea consolidates all SPEs where it retains 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 nor rewards on these assets and liabilities.

The SPEs in Table 7.1 are not consolidated for capital adequacy purposes. Instead, loans and loan commitments to the SPEs are included in the banking book and capital requirements are calculated in accordance with the rules described in chapter 4. Bonds and notes issued by the SPE and held by Nordea as well as credit derivative transactions between Nordea and the SPE are reported in the trading book. Nordea has been approved to calculate the general and specific market risk of these transactions under the VaR

model. The counterparty credit risk of credit derivative transactions is calculated in accordance with the current exposure method. More information on the different SPEs can be found in the sections following.

Table 7.1 Special purpose entities where Nordea is the sponsor, 31 December 2013

EURm		Duration	Accounting treatment	Book	Nordea's investment[1]	Total assets
Viking ABCP Conduit	Receivables Securitisation	< 5 years	Consolidated	Banking	512	536
Total					**512**	**536**

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

7.2.1 *Entities issuing structured credit products*

Nordea gives investors an opportunity to invest in different types of structured credit products, such as structured Credit-Linked Notes (CLN) and Collateralised Mortgage Obligations (CMO).

In example the Kalmar Structured Finance A/S (Kalmar) was established to allow customers to invest in structured products in the global credit markets. Nordea sells protection in the credit derivative market by entering into a portfolio CDO. At the same time, Nordea purchases protection under similar terms from Kalmar which issues CLNs to investors. In this process the investors end up bearing the credit risk of the underlying portfolio. In case of credit losses in the underlying portfolio the collateral given by the investors in connection with the CLN is reduced. The total notional outstanding CLNs in this category were reduced to zero (EUR 23m) at end of 2013.

7.2.2 *Securitisations of customer assets*

The Viking ABCP Conduit (Viking) was established with the purpose of supporting trade receivable or accounts payable securitisations to core Nordic customers. The SPEs purchase trade receivables (the only asset class purchased) and fund the purchases either by issuing commercial paper via the established asset-backed commercial paper programme or by drawing on the liquidity facilities. Nordea has provided liquidity facilities of maximum EUR 1,646m at year end 2013 (EUR 1,691m) out of which EUR 1,369m (EUR 1,230m) had been utilised. Nordea Bank Danmark has provided liquidity facilities of maximum EUR 593m at year end 2013 (EUR 593m) out of which EUR 512m (EUR 488m) were utilised.

Nordea's risks are limited to its holding of CPs issued by Viking and to the drawings under the liquidity facilities provided by Nordea to the SPEs. First loss protection is provided by the originators of the assets and/or from additional external credit enhancement such as the purchase of credit protection from a credit insurance policy, depending on the nature of the SPE and the quality of the purchased assets. When deciding if Nordea should arrange a new transaction, and in providing the liquidity facilities, Nordea uses the same approach as if it was to provide liquidity directly to the underlying customer.

There was no outstanding commercial paper issue at year end 2012 or 2013. The liquidity facility results in an RWA of EUR 665m (EUR 614m), which is included within the credit risk framework of Nordea's banking book. The RWA for Nordea Bank Danmark for the liquidity facility was EUR 176m (EUR 191m).

7.3 Credit derivatives trading

Nordea acts as an intermediary in the credit derivatives market, especially in Nordic names. Nordea also uses credit derivatives to hedge positions in corporate bonds and synthetic CDOs.

When Nordea sells protection in a CDO transaction, it carries the risk of losses in the reference portfolio if a credit event occurs. When Nordea buys protection in a CDO transaction, any losses in the reference portfolio triggered by a credit event are then carried by the seller of protection.

Credit derivatives transactions create counterparty credit risk in similar manner to other derivative transactions. Counterparties in these transactions are typically subject to a financial collateral agreement, where the exposure is covered daily by collateral placements.

The CDO valuations are subject to fair value adjustments for model risk. These fair value adjustments are recognised in the income statement. The credit derivative portfolio is part of Nordea Bank Finland Plc.

8. Liquidity risk and funding

During 2013, Nordea Bank Danmark continued to benefit from its focus on prudent liquidity risk management, in terms of maintaining a diversified and strong funding base. Nordea had access to all relevant financial markets and was able to actively use all of its funding programmes.

8.1 Management, governance and measurement of liquidity 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.

8.1.1 *Management of liquidity risk*

Nordea's liquidity management and strategy is based on policy statements resulting in various 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 ensure market access. A 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 programmes are both short-term (US commercial paper, European commercial paper, commercial paper, Certificates of Deposits) and long-term (covered bonds, European medium-term notes, medium term notes) and cover a range of currencies.

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 testing framework also includes survival horizon metrics (see below), which represents a combined liquidity risk scenario (idiosyncratic and market-wide stress).

8.1.2 *Governance of liquidity risk*

Group Treasury is responsible for pursuing the Nordea's liquidity strategy, managing the liquidity in Nordea and for compliance with the group-wide limits set by the Board of Directors and the Risk Committee. Furthermore, Group Treasury develops the liquidity risk management frameworks, which consist of policies, instructions and guidelines for the Group as well as the principles for pricing liquidity risk.

8.1.3 *Measurement of liquidity risk*

The liquidity risk management focuses on both short-term liquidity risk and long-term structural 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 30 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. The buffer minimum level is set by the Board of Directors. The liquidity buffer consists of central bank eligible high-grade liquid securities held by Group Treasury that can be readily sold or used as collateral in funding operations.

During 2011, the Survival horizon metric was introduced. The metric is composed of a liquidity buffer and funding gap risk cash flows, and includes expected behavioural cash flows from contingent liquidity drivers. Survival horizon defines the short-term liquidity risk appetite of the Group and expresses the excess liquidity after a 30-day period without access to market funding. The Board of Directors has set a limit for minimum survival without access to market funding during 30 days.

The structural liquidity risk of Nordea is measured and limited by the Board of Directors through the net balance of stable funding (NBSF), 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 of more than 12 months, as well as shareholders' equity, while stable assets primarily comprise retail loans, other loans with a remaining term to maturity longer than 12 months and committed facilities. The CEO in GEM has set as a target that the NBSF should be positive, which means that stable assets must be funded by stable liabilities.

8.2 Liquidity risk and funding analysis

The short-term liquidity risk remained at moderate levels throughout 2013. The average funding gap risk, i.e. the average expected need for raising liquidity in the course of the next 30 days, was EUR +0.8bn (EUR +1.1bn). Nordea Bank Danmark's liquidity buffer range was EUR 18.5 – 27.2bn (EUR 20.8 – 31.2bn) throughout 2013 with an average buffer size of EUR 22.2bn (EUR 24.1bn). Nordea Bank Danmark's liquidity buffer is highly liquid, consisting of only central bank eligible securities held by Group Treasury. Survival horizon was in the range of EUR 15.5 – 26.7bn (EUR 11.3 – 24.8bn) throughout 2013 with an average of EUR 22.8bn (EUR 17.8bn). The target of maintaining a positive NBSF was comfortably achieved throughout 2013, with a yearly average NBSF of EUR 14.4bn (EUR 13.3bn).

9. ICAAP and internal capital requirement

The internal capital adequacy assessment process aims to ensure that the bank keeps sufficient available capital to cover all risks taken over a foreseeable future, including during periods of stress. The level of capital needs to be adequate from an internal perspective as well as from the perspective of regulators, as well as market participants. Note that this chapter does not present the individual solvency need for Nordea Bank Danmark and its legal entities. The individual solvency need is disclosed quarterly in a separate document and can be found at www.nordea.dk or on Nordea's Investor Relations webpage at www.nordea.com/IR.

9.1 ICAAP

The purpose of the Internal Capital Adequacy Assessment Process (ICAAP) is to review the management, mitigation and measurement of material risks within the business environment in order to assess the adequacy of capitalisation and to determine an internal capital requirement reflecting the risks of the institution.

The ICAAP is a continuous process which increases awareness of Nordea's capital requirements and exposure to material risks throughout the organisation, both in the business area and legal entity dimensions. Stress tests are important drivers of risk awareness, looking at capital and risk from a firm-wide perspective on a regular basis and on an ad hoc basis for 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.

The capital ratios and capital forecasts for Nordea Bank Danmark and its legal entities are regularly monitored by Group Corporate Center. The current capital situation and forecasts are reported to the Asset and Liability Committee (ALCO), Risk Committee, GEM and the Board of Directors. On an annual basis the capital requirements and adequacy are thoroughly reviewed and documented in Nordea Bank Danmark's ICAAP report, which ultimately is decided and signed off by the Nordea Bank Danmark's Board of Directors.

9.1.1 *Capital planning and capital policy*

The capital planning process is intended to ensure that the Nordea Group and its legal entities have sufficient capital to meet minimum regulatory requirements, support its credit rating, growth and strategic options. The process includes a forecast of the capital development (e.g. the Pillar I and Pillar II capital requirements), the available capital (e.g. core tier 1, tier 1 and tier 2 capital) as well as the impact of new regulations. 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 considers forecasts of the state of the economy to reflect the future impact of credit risk migration on the capital situation of Nordea Bank Danmark Group. An active capital planning process ensures that Nordea is prepared to make necessary capital arrangements regardless the state of the economy and the introduction of new capital adequacy regulations.

The ALCO is responsible for evaluating and deciding on capitalisation and prepares proposals for decision by the CEO in GEM when needed.

9.1.2 *Conclusion of ICAAP and SREP*

Nordea's capital levels continue to be adequate to support the risks taken, both from an internal perspective as well as from the perspective of supervisors. Heading into 2014, Nordea Bank Danmark will continue to closely follow the development of the new capital requirement regime as well as maintain its open dialogue with the Danish FSA.

9.2 Internal capital requirements

Nordea Bank Danmark bases its internal capital requirements under the ICAAP on its internally identified risks, which consists of both Pillar I and Pillar II risks. In effect, the internal capital requirement is a combination of risks defined by the CRD and risks defined by quantitative models under Pillar II.
The following risk types are included under Pillar II:

- Business risk is the earnings volatility inherent in all business due to changes in the economic and competitive environment. Business risk is calculated based on the observed volatility in historical profit and loss that is attributed to business risk.
- Interest rate risk in the banking book consists of exposures deriving from the balance sheet (mainly lending to public and deposits from public) and from Group Treasury's investment and liquidity portfolios. The interest rate risk is measured in several ways on a daily basis and in accordance with the financial supervisory authorities' requirements.
- Pension risk is included in the market risk framework and includes equity risk, interest rate risk and FX risk in the Nordea-sponsored defined benefit pension plans.
- Real estate risk consists of exposure to owned and leased properties and is included in the market risk framework.
- Concentration risk is the credit risk related to the degree of diversification in the credit portfolio and includes both single name concentration risk and sector/geography concentration risk.

Liquidity risk is a Pillar II risk, however it is not included in the capital framework, instead it is mitigated through active management of liquidity. Liquidity risk is the risk of being able to meet liquidity commitments only at increased costs, 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. In addition to calculating risk capital for its various risk types, Nordea Bank Danmark conducts a comprehensive capital adequacy stress test to analyse the effects of a series of global and local shock scenarios. The results of the stress tests are considered in Nordea Bank Danmark's internal capital requirements as buffers for economic stress.

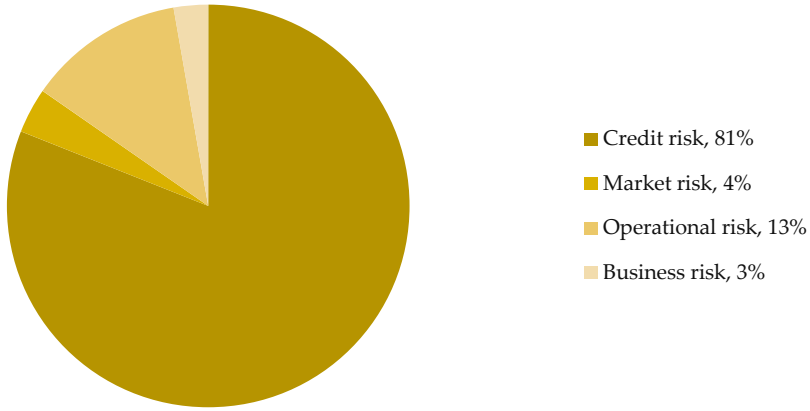
By considering the stress test results in the assessment of internal capital requirements, the pro-cyclical effects inherent in the risk-adjusted capital calculations of the economic capital and IRB approaches are addressed. Regulatory buffers are introduced with the implementation of CRD IV. This might lead to higher capitalisation requirements than what is determined in the internal capital requirement. Should the regulatory capital requirement come to exceed the internal capital requirement, additional capital will be held to meet regulatory requirements with a margin.

9.2.1 *Economic capital (EC)*

EC is input in the EP framework which is calculated as risk adjusted profit less cost of equity. EP drives and supports the operational decision making process in Nordea to support performance management and shareholder value creation.
Nordea's Economic Capital model is based on the same risk components as the ICAAP. Pillar II closes the gap between regulatory capital and EC by improving the risk sensitivity of regulatory capital measurement.
EC was during 2013 further aligned to core tier 1 capitalisation requirements anticipated in forthcoming regulation. For 2014, additional capital items will be introduced in the EC to reduce the gap between legal equity and allocated capital.

As of end 2013 the total EC for Nordea Bank Danmark equalled EUR 4.5bn (EUR 4.9bn as of 2012, restated). Figure 9.1 shows the economic capital distributed by risk type. Notably, credit risk accounts for 81% of total EC. Total EC decreased from last year by 0.3bn.

Figure 9.1 EC distributed by risk type



9.2.2 *Stress testing governance and framework*

Stress testing governance and framework are important due to the vital role of capital for Nordea's management and profitability. Thus an adequate governance structure is required for the stress testing process. Key responsibilities include Group Executive Management (GEM) and the legal entity boards engagement in the internal assessment of capital (ICAAP) stress testing. In addition, the Executive Management of Group Risk Management (GREM) and the Asset and Liability Committee/Risk Committee review in details the stress test performed and potential implications for future capital.

Capital adequacy stress testing is carried out annually during the first quarter, using end-of-year data. Ad hoc stress testing may be carried out throughout the year when necessary. In order to determine the adequacy of capital for the Nordea Group throughout the scenarios, Key financial targets , which are stated in Nordea's capital policy, are also considered. As long as the capital policy is fulfilled during the scenarios, the adequacy of existing capital can be supported.

The key measure for determining the stress test impact is the core tier 1 ratio and how it develops during the scenarios. The stress test capital impact is defined as the percentage drop in core tier 1 ratio in the most stressed year. The impact is then analysed in relation to capital policy, regulatory buffers and internal capital requirements.

9.2.2.1 Stress tests performed

During 2013, Nordea Bank Danmark performed internal stress tests in order to evaluate general effects of an economic downturn as well as effects for specifically identified segments or high risk areas. In addition to the internal stress tests, the Nordea Group and Nordea Bank Danmark were subject to stress tests and capital review exercises performed by financial supervisors and central banks.

As part of the ICAAP and the capital planning process, firm-wide stress tests are used as an important risk management tool in order to determine how severe unexpected changes in the business and macro environment will affect the capital need. The stress tests reveal how the capital need varies during a stress scenario, where the income statements, balance sheet, regulatory capital requirements, EC and capital ratios are impacted.

In addition to the firm-wide stress tests which cover all risks defined in the EC framework, Nordea Bank Danmark performs ad hoc stress test and sensitivity analysis of various risk parameters and risk factors on a need-by-need basis. The Nordea Group has also carried out reverse stress tests of various recovery environments in relation to the development of the recovery and resolution plan.

Nordea Bank Danmark continuously refines its stress testing methodologies and practises to ensure a forward-looking element.

The general stress test process is divided into the following three steps:

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

Each of these steps is described in further in the sections following.

9.2.2.2 Scenario development and translation

The annual ICAAP stress test is based on three-year macroeconomic scenarios for each Nordic and Baltic country and the scenarios are designed to replicate shocks that are particularly relevant for the existing portfolio. Stress scenarios are designed by experts within the Nordea Economic Research division. Nordea also uses its rolling financial forecast for complementary assumptions of the base case. The difference between the stressed scenarios and the base case scenario is used to determine the stress effect and the additional capital need.

While the annual stress test is based on comprehensive macroeconomic 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 macroeconomic 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 on risk drivers 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 9.1.

Table 9.1 Parameters in the annual stress test

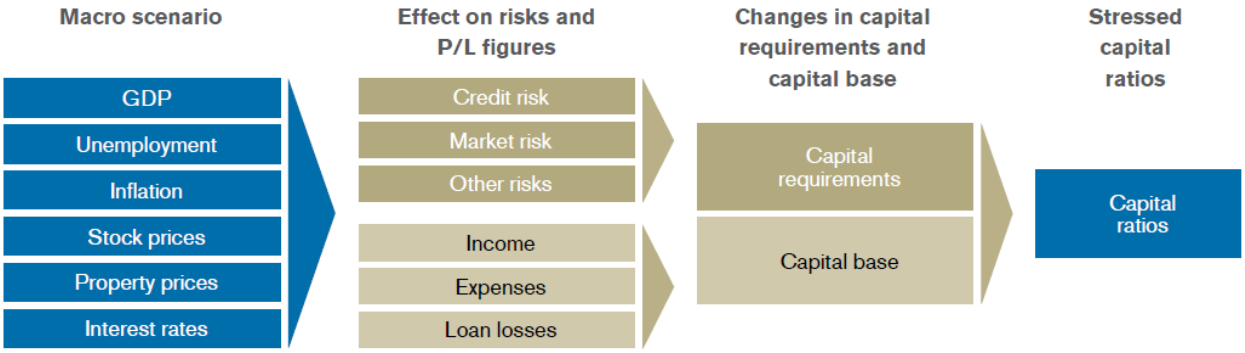
Parameter	Impact
Volumes	Lending volumes are dependent on lending growth specified in the scenario and on inflow to default and loss provisions. Deposit volumes are given directly by the RFF.
Margins	Corporate lending margins are country and rating specific and therefore sensitive to rating migrations. Retail margins are country specific and split by mortgage lending and other lending. Defaulted (but performing) customers are assigned a lower margin. Deposit margins are given by the RFF.
Net interest income	Net interest income figures are adjusted according to the change in volume and margins for deposits and lending, as well as increased funding cost (see below).
Funding cost	Changes in funding costs are derived from the assumption of Nordea being down-rated. The increased funding cost, due to a lower rating, reduces net interest income.
Net fee and commission income	Net fee and commission income is calculated according to product mix. Commission income is assumed to follow market movements and is adjusted according to changes in the stock index, whereas other items are adjusted according to changes in GDP.
Operating expenses	Operating expenses are assumed to be constant except for variable salary expenses, which are adjusted according to changes in net profit the previous year.
Loan losses	Loan losses are calculated based on a bottom-up, EL-based model. The EL-calculations are carried out on stressed rating distributions, stressed point in time PD curves and stressed LGD values (see below). The model covers both collective and specific provisions. The loan loss model consists of two components that cover losses related to (i) a general macroeconomic scenario and (ii) industry specific and idiosyncratic loss events.
P/L effect of Operational- and Market Risk	Stressed losses related to operational risk and market risk are calculated using assumed loss distributions and correlations between the risk types.
Rating/Scoring migration	For corporate customers, rating migrations are calculated on customer level based on stressing their financial statements for each year and scenario. For retail and bank customers, rating/scoring migrations are calculated based on central macro-economic variables per year and scenario.
Probability of default	Stressed PD values are calculated on customer level based on the stressed rating/scoring migrations (see above). For loan loss calculations point in time PDs are used. The point in time PDs are dependent on the severity of the macroeconomic scenario. In addition the PDs contain an add-on factor to reflect industry specific and idiosyncratic risk.
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.
Risk weighted assets (RWA)	Credit risk RWA is calculated on customer/exposure level based on stressed PDs and LGDs. RWA is also dependent on changes in volumes (EAD) which are a function of lending growth and inflow to default.

9.2.2.3 *Calculation*

The stressed figures and parameters from the scenario are used to calculate the effects on the regulatory capital requirements, the EC 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.

Stressed figures for loan losses are calculated bottom-up, based on stressed rating migrations and collateral values. Stressed point-in-time PDs that are functions of the downturn scenario, are used in the calculation of loan losses. The loan loss calculation also covers idiosyncratic losses related to the exposure to single customers and industries. The loan loss model covers both specific and collective provisions. Together with net profit and dividend from the stressed 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 EC in order to calculate the effect on capital ratios during a stress scenario. Figure 9.2 shows the calculation process used in the stress test framework.

Figure 9.2 Calculation process



9.2.2.4 *Analysis and reporting*

The first level of reporting in Nordea is the ALCO and the Risk Committee, which review the details of the stress tests and implications on future capital need. The results, showing the implications of the stress tests on the adequacy of existing capital are distributed to the executive management and the Board of Directors.

The results of the stress tests 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 potential economic downturns and other stress events. Business area involvement in defining and assessing the stress tests is seen as important in order to increase the risk awareness throughout the organisation and the understanding of the relation between capital requirements and exposure to material risks.

The outcome of the stress tests demonstrates how Nordea Bank Danmark'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 to ensure that Nordea Bank Danmark is well capitalised.

10. Capital base

Nordea Bank Danmark's capital base improved further during 2013, due to profit generation. The core tier 1 capital ratio excluding transition rules, increased by 1.9 %-points to reach 14.0%. The capital ratio excluding transition rules ended at 20.5% (18.2%).

10.1 Capital base definition

Capital for regulatory purposes, the capital base, is determined in accordance with the CRD and the Danish legislation and is based on equity as reported under applicable accounting standards in the balance sheet.

Only capital contributed by companies within the financial group and by the consolidated accounts can be included in the capital base. Items included in the capital base should without restrictions or time constraints be available for the institution to cover risk and absorb potential losses.

The size of the capital base must as a minimum correspond to the sum of the capital requirements for credit, market and operational risks, in accordance with the pillar I requirements.

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

Tier 1 capital consists of both core tier 1 capital (paid-in shareholder capital and retained earnings) and other tier 1 (undated subordinated debt). The tier 2 capital consists mostly of dated/undated subordinated loans. For the moment Nordea Bank Danmark has no undated subordinated tier 1 capital loans. A summary of items included in the capital base is available in Table 10.1. Below is a detailed description of the items included in the capital base.

10.2 Core tier 1 capital and tier 1 capital

Core tier 1 capital is defined as eligible capital including eligible reserves, net of regulatory required deductions done directly to core tier 1 capital. The capital recognised as core tier 1 capital holds the ultimate characteristics for loss absorbance defined from a "going concern" perspective and are the most subordinated claim in the event of liquidation. The tier 1 capital is defined as core tier 1 capital and capital of the same or close to the character of eligible capital and eligible reserves. The tier 1 capital can include a limited part of subordinated capital loans (up to 50% of tier 1 dependent on the specific terms of the instruments).

10.2.1 *Eligible capital and eligible reserves*

Eligible capital is the share capital contributed by shareholders, including the share premium paid. 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 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 group are also included. Positive income from current year is included as eligible reserves after verification by the external auditors, however negative income must be deducted. Repurchased own shares or own shares temporary included in trading portfolios are deducted from eligible reserves.

10.2.2 *Tier 1 instruments subject to limits*

The inclusion of subordinated capital loans in tier 1 capital is restricted and repurchase can normally not take place until five years after original issuance. Undated subordinated loans may be repaid only upon decision by the Board of Directors in Nordea Bank Danmark and with the permission of the Danish FSA. Further, there are restrictions related to step-up conditions, order of priority andinterest payments under constraint conditions. Currently, the inclusion of undated subordinated capital loans as a component of tier 1 capital is limited by regulation to 50% net of relevant deductions.

Currently there are no subordinated capital loans issued by Nordea Bank Danmark or included in the capital base of Nordea Bank Danmark.

Table 10.1 Summary of items included in capital base, 31 December 2013

EURm	31 December 2013	31 December 2012
Tier 1 capital		
Paid-up capital	670	670
Share premium	0	0
Eligible capital	**670**	**670**
Reserves	4,291	4,089
Minority interests	170	170
Income from current year	491	203
Eligible reserves	**4,952**	**4,462**
Core tier 1 capital (before deductions)	**5,622**	**5,132**
Subordinated capital loans	**0**	**0**
Proposed/actual dividend	-235	0
Deferred tax assets	-11	-12
Intangible assets	-371	-392
Deductions for investments in credit institutions	0	0
IRB provisions shortfall (-)	-171	-170
Other items, net	0	0
Deductions	**-788**	**-574**
Tier 1 capital (net after deduction)	**4,835**	**4,558**
- of which subordinated capital	0	0
- of which core tier 1 capital (net of deductions)	**4,835**	**4,558**
Tier 2 capital		
Undated subordinated loans	0	0
Dated subordinated loans	2,425	2,425
Other additional own funds	3	3
Tier 2 capital (before deductions)	**2,428**	**2,428**
Deductions for investments in credit institutions	0	
IRB provisions shortfall (-)	-171	-170
Deductions	**-171**	**-170**
Tier 2 capital (net after deductions)	**2,256**	**2,258**
Capital base	**7,091**	**6,816**

10.2.3 *Deductions from tier 1 capital*

10.2.3.1 Proposed/actual dividend

In relation to income for the period, the corresponding dividend should be deducted. The amount deducted from tier 1 capital is based on the dividend proposed by the Board of Directors of Nordea Bank Danmark to be decided at the annual general meeting of Nordea Bank Danmark's shareholders.

10.2.3.2 Deferred tax assets

In accordance with local legal requirements deferred tax assets have been deducted from tier 1 capital. The deducted amount is calculated based on accounting standards relevant for the individual companies included in the finacial group.

10.2.3.3 Goodwill and other intangible assets

The significant part of deducted intangible assets contains goodwill and other intangible assets related to IT software and development.

10.2.3.4 Deductions for investments in credit institutions and financial institutions

The institutions should in its capital base deduct for equity holdings and some other types of contributions to institutions that are not consolidated into the financial group (in Nordea foremost associated companies). By end 2013 no holdings had to be deducted.

10.2.3.5 IRB provisions shortfall

In accordance with Danish legislation, the differences between actual IRB provision (EUR 1.5bn) made for the related exposure and expected loss (EUR 1.8bn) are adjusted for in the capital base. The negative difference (when the expected loss amount is larger than the provision amount) is defined as a shortfall. According to the CRD, the shortfall is to be deducted equally from tier 1 capital and tier 2 capital. A positive difference (provisions exceeding expected loss) can be included in tier 2 capital subject to certain limitations

10.3 Tier 2 capital

Tier 2 capital must be subordinated to depositors and general creditors of the bank. It cannot be secured or covered by a guarantee of the issuer or related entity or include any other arrangement that legally or economically enhances the seniority of the claim vis-à-vis depositors and other bank creditors.

10.3.1 *Tier 2 – Subordinated loans*

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

The basic principle for subordinated debt in the capital base is the order of priority in case of a default or bankruptcy situation. Under such conditions, the holder of the subordinated loan would be repaid after other creditors, but before shareholders. The share of outstanding loan amount possible to include in the tier 2 capital related to dated loans is reduced if the remaining maturity is less than three If the remaining maturity is less than three years but two years or more 25% shall be deducted. If the remaining maturity is less than two years but one year or more 50% shall be deducted and the last year 75% has to be deducted.

During 2013, Nordea has not issued new loans and and no loan has been called. Nordea thereby holds EUR 2,425 bn in dated subordinated loans.

10.3.2 *Other tier 2 capital*

Other additional funds contains revaluations appropriations according to Danish executive order on capital base §27 item 1 no 2.

10.3.3 *Deductions from tier 2 capital.*

10.3.3.1 Deductions for investments in credit institutions and financial institutions

The institutions should in its capital base deduct for equity holdings and some other types of contributions to institutions that are not consolidated into the financial group (in Nordea foremost associated companies). The regulation stipulates 50% to be deducted from tier 1 capital and 50% to be deducted from tier 2 capital.

10.3.3.2 IRB provisions excess (+) / shortfall

The differences between EL and provisions made for the related exposure are adjusted for in the tier 2 capital. See section 11.2.4 for further explanation.

11. New regulations

The final version of the Capital Requirement Directive IV (CRD IV) and Capital Requirement Regulation (CRR) for the European financial market was published in June 2013. The Directive will be implemented through national law within all EU member states during 2014, pending on national processes, while the Regulation will become applicable in all EU countries from 1 January 2014 directly through the European process.

11.1 Forthcoming regulatory framework

The changes for financial institutions in the regulatory area related to capital and risk are extensive. In addition to the CRD IV/CRR, other closely related regulations are also emerging. These include a new framework for dealing with bank failure (crisis management), a proposal for a Banking Union (including the already agreed single supervisory mechanism and the single resolution mechanism), a review regarding treatment of the trading book from the Basel Committee on Banking Supervision (Fundamental review of the Trading Book), a potential proposal regarding a structural reform primarily related to trading activities as well as changes to accounting regulation that will have an effect on capital and risk. Furthermore, data and reporting requirements for banks are expected to increase substantially.

11.2 Basel III and the CRD IV/CRR

In December 2010, the Basel Committee on Banking Supervision (BCBS) issued rules of new global regulatory standards on credit institutions capital adequacy, leverage and liquidity, collectively referred to as Basel III. These standards have now been transposed to European legislation through the CRD IV/CRR.

CRD IV/CRR include several key initiatives which change the current requirements that have been in effect since 2007. The regulation requires higher capitalisation levels and better quality of capital, better risk coverage, the introduction of a leverage ratio as a backstop to the risk based requirement, measures to promote the build-up of capital that can be drawn in periods of stress and the introduction of liquidity standards.

CRD IV/CRR will consist of a Directive and a Regulation:

- The Directive, CRD IV, covers areas such as authorisation of banks, principles for prudential supervision including Pillar II rules, corporate governance, capital buffers, sanctions and remuneration.
- The Regulation, CRR, contains detailed requirements covering own funds, capital requirements for credit risk, market risk and operational risk, large exposures, liquidity, leverage ratios, and disclosure requirements.

The CRR is intended to set a single rule book for all banks in the EU, avoiding diverging national rules. However, the on-going national implementation of the Directive and of the national options possible in the CRR shows that there will be differences between different countries.

The EBA, with its objective to play a leading role in the creation of the single rule book for the EU banking system, issues binding technical standards for banks. More than 100 binding technical standards are expected due to CRD IV/CRR, of which a large number were issued for consultation already during 2012 and 2013.

11.2.1 *Capital regulation*

11.2.1.1 Own funds

The CRR includes a revised definition of own funds, intending to increase the quality of capital, hence create better loss-absorbing capacity. Own funds is the sum of tier 1 capital and tier 2 capital. Tier 1 capital consists of common equity tier 1 capital (paid-in shareholder capital and retained earnings) and additional tier 1 (undated subordinated debt). Tier 2 capital consists predominantly of dated/undated subordinated loans. In common terms, tier 1 capital can absorb losses without an institution being required to close down it business activities, and tier 2 capital can absorb losses in the event of a winding-up and so provides a lesser degree of protection to depositors. The requirements for inclusion of instruments in common equity tier 1 (CET1) are stricter and the details have also been further regulated by technical standards from the EBA. Also, the CRR

applies deductions mainly to CET1 (under the previous framework, important deductions have been applied to other parts of own funds as well).

According to the CRR the changes should gradually be phased-in until 2024. However, the CRR also opens up for local regulators to phase in deductions faster. The required features of capital instruments to be eligible as additional tier 1 and tier 2 capital will also be stricter. For example, instruments with incentives to redeem (e.g. step-up clauses) will not be eligible. Instruments that do not contain the required features should be gradually phased-out until 2022. The regulation opens up for local regulators to phase out instruments that are not fully compliant faster.

11.2.1.2 Regulatory minimum capital requirements

CRR requires banks to comply with the following minimum capital ratios:

- Common equity tier 1 capital ratio of 4.5%
- Tier 1 capital ratio of 6%
- Capital ratio of 8%

The minimum CET1 capital ratio and the minimum tier 1 capital ratio should be gradually phased-in until 2015. Again, the framework opens up for faster implementation by national regulators.

11.2.1.3 Capital buffers

CRD IV introduces a number of capital buffer requirements. The capital buffers are expressed in relation to RWA and represent additional capital to be held on top of the minimum regulatory requirements. The levels and the phasing-in of the buffer requirements are subject to national discretion.
A mandatory capital conservation buffer of 2.5% to be met with CET1 will be established above regulatory minimum requirements. Further, a countercyclical capital buffer is implemented as an extension of the capital conservation buffer, which will be developed in national jurisdictions when excess credit growth is judged to be associated with a build-up of system wide risk. The countercyclical capital buffer should also be met with CET1 and the institution specific buffer will be in the range 0-2.5%. Supervisory authorities shall also require that globally systemically important institutions (G-SIIs) hold buffers of additionally 1-3.5% CET1. In addition, the CRD IV allows for a systemic risk buffer (SRB) to be added as well as a buffer for other systemically important institutions (O-SIIs). These buffers should be seen in conjunction with the other buffers and should also be met with CET1. The O-SII buffer can be set up to 2% and the SRB can be set up to 3% for a banks all exposures and up to 5% for a bank's domestic exposures. Breaching these buffer requirements will restrict banks' capital distribution, such as the payment of dividends.

11.2.2 ***Risk-weighted assets (RWA)***

RWA will mainly be affected by additional requirements related to counterparty credit risk, the introduction of an asset correlation factor for exposures towards financial institutions and a multiplication factor for exposures to SMEs. Several countries are also discussing the introduction of higher risk weights or other restrictions on mortgage lending.

For banks calculating RWA according to the IRB approach, a risk-weight floor was previously in place, stipulating that RWA should not be less than 80% of the RWA calculated under Basel I. This floor was expected to end December 2012 however, CRR extends these transition rules until 31 December 2017.

11.2.2.1 Counterparty credit risk

The largest change to the calculation of RWA relates to the changes made to the calculation of counterparty credit risk. The changes are mainly made in the introduction of a capital charge for credit valuation adjustment risk (CVA risk) and a capital charge for exposures to central counterparties (CCPs).

The CVA risk mirrors that the value of a financial instrument may not be realised due to the default of the counterparty. The basis of the capital charge is to hold capital against potential mark-to-market losses associated with deterioration in the creditworthiness of a counterparty. The capital charge can be determined according to two methods: the advanced and the standardised. The advanced method should be implemented if the bank has both IMM approval for counterparty credit risk and a specific interest rate VaR approval, hence Nordea is to use the advanced method for applicable portfolios.

Exposures to CCPs will be subject to a capital requirement. A CCP is an entity that interposes itself between counterparties to contracts traded in one or more financial markets, becoming the buyer to every seller and the seller to every buyer. The size of the capital requirement will depend on the type of exposure and whether the CCP is qualified or not.

11.2.2.2 Asset correlation factor

The CRR introduce an asset correlation factor of 1.25% when calculating RWA for exposures to large regulated financial entities that are subject to prudential supervision and whose assets are greater than or equal to EUR 70bn. Unregulated financial entities with relevant activities are also affected. The motivation for the introduction of an asset correlation factor is that correlation within these segments is substantial.

11.2.2.3 Risk weight for small and medium sized entities (SMEs)

In order to encourage lending to SMEs, the risk weights for SMEs will be reduced. The capital requirement for credit risk for exposures to SMEs shall be multiplied with the factor 0,7619. The definition includes exposures in both the standardised and IRB approaches in the exposure classes retail, corporate and secured by real estate. The annual turnover for the SME must be below EUR 50m and the total amount owed (for the group of connected clients) shall not exceed EUR 1.5m excluding claims secured by residential real estate

11.2.3 ***Leverage ratio***

The CRR introduce a non-risk based measure, the leverage ratio, in order to limit an excessive build-up of leverage on credit institutions' balance sheets and thus helps in containing the cyclicality of lending. The impact of the ratio will be monitored with an aim to migrate to a binding measure in 2018, based on appropriate review and calibration. The leverage ratio will be calculated as the tier 1 capital divided by the exposure (on-balance and off-balance sheet exposures, with adjustments for certain items such as derivatives and securities financing transactions).

In January 2014, the BCBS published the leverage ratio framework. The final version is more in line with CRR compared to the consultation paper that was issued during summer 2013.

11.2.4 ***Liquidity regulations***

The objective of the liquidity reform is to improve the banking sector's ability to absorb liquidity shocks arising from financial and economic stress, thus reducing the risk of spill-over from the financial sector to the real economy. In CRD IV/CRR two new quantitative liquidity standards have been introduced: liquidity coverage ratio (LCR) and net stable funding ratio (NSFR). LCR requires that a bank shall hold liquidity buffers which are adequate to face any possible imbalance between liquidity inflows and outflows under gravely stressed conditions over a period of 30 days. NSFR requires that a bank shall ensure that long term obligations are adequately met with a diversity of stable funding instruments under both normal and stressed conditions. CRD IV/CRR does not contain detailed rules for NSFR. BCBS published detailed proposals for NSFR in 2010 and changed proposals on 12 January 2014. According to the Basel proposals, a bank' Available Stable Funding (ASF) shall be at least equal to its Required Stable Funding (RSF). ASF and RSF are determined by pre-specified factors. Both LCR and NSFR will be subject to an observation period in CRD IV/CRR. After the observation period, LCR will be phased-in from January 2015 (60% in 2015, 70% in 2016, 80% in 2017, 100% in 2018) while NSFR might be introduced as a minimum standard by 2018.

11.2.5 ***Reporting requirements***

The EBA has by mandate in the CRR developed Implementing Technical Standards related to supervisory reporting requirements. The harmonisation of the reporting is part of the intention in building the single rule book in Europe, with the particular aim of specifying uniform formats, frequencies and dates of prudential reporting as well as IT solutions to be applied by credit institutions and investment firms in the EU. The requirements cover capital adequacy ("Corep"), financial reporting ("Finrep") and liquidity. The new reporting requirements have required additional data gathering, extensive IT implementations and changes to reporting templates. The new Corep reporting will be mandatory when the CRR comes into force.

11.2.6 *Implementation of CRD IV/CRR Denmark*

As mentioned, CRD IV needs to be implemented into national laws and regulations before entering into force. The CRR will however enter into force at 1 January 2014 in all EU countries. Within CRR there are a number of national options that can be implemented into national legislation/regulation should the national authorities choose to do so and during the autumn and winter a number of consultations on national implementation of CRD IV/CRR has been issued.

In October, a political agreement was reached concerning the regulation of systemically important financial institutions and on the level of capital requirement. In November this was also submitted in a consultation from Finanstilsynet. The agreement states that the capital requirement for all banks will be the minimum 4.5% CET1, the capital conservation buffer of 2.5% CET1 and also the countercyclical capital buffer that are to be phased in from 2015 to 2019 and that can be set up to 2.5% CET1 from 2019. In addition to this, a buffer requirement for systemically important institutions will be phased in between 2015 to 2019. Based on the most recent financial statements, seven institutions have been identified of which Nordea Bank Danmark is one, and the buffer requirement for Nordea Bank Danmark is currently set to 2% CET1. In addition to this there is also a possible Pillar II requirement that is set on an individual basis. The new requirements are suggested to enter into force 31 March 2014.

In December Finanstilsynet also consulted on the national implementation of the CRD IV which suggests that the rules will enter into force from 31 March 2014.

11.3 Crisis management and Recovery and Resolution

During 2011, the FSB published "Key Attributes of Effective Resolution Regimes for Financial Institutions". The Bank Recovery and Resolution Directive (BRRD) is the EU implementation of the FSB guidelines, and were finally agreed upon in December 2013. The Banking Union regulation, parts of which is currently being drafted, implements the BRRD for the Eurozone (and potential opt-in) countries, and introduces single standards for resolution banks. On an overall level these regulations address how to maintain financial stability through reducing the systemic impact of failing financial institutions. A central political aim is to minimize the intrinsic public financial support to the banking system during large scale financial crises, while avoiding critical disruptions in the financial markets and infrastructures.

The BRRD outlines the tools and powers available to the relevant authorities in the EU, which are aimed at both preventing bank defaults, as well as handling banks in crises, while maintaining financial stability.

11.3.1 *Recovery and Resolution Plan*

In November every year, the FSB and the Basel Committee identifies global systemically important banks. The November 2013 report lists 29 institutions and Nordea was for the second time identified as the only institution in the Nordic region.

Global systemically important institutions are required to submit recovery plans aimed at establishing recovery planning processes to reduce the probability of default, while authorities are required to establish credible and operational resolution plans.

11.4 Banking union

In the early autumn of 2012, the EU Commission presented a proposal to move to a full banking union in the Euro zone. In December 2013 the Parliament and the Council ensured, by key legislation, that the European Central Bank (ECB) will be responsible for the supervision of banks in the framework of the Single Supervisory Mechanism (SSM). This is the first effective step in creating the banking union.
A banking union can be defined as a fully integrated bank regulatory and supervisory system within a federal structure. National supervisors will however continue to play an important role in preparing and implementing the ECB's decisions.

For increasing consistency and efficiency of supervisory practises the EBA will continue to develop the single rule book applicable to all 27 member states. It will also ensure that regular stress-tests are carried out to assess the resilience of European banks.

The SSM, as agreed by the Parliament and the Council, also establishes rules on the governance and responsibility of the ECB which should ensure a separation between its tasks as a supervisor and its monetary policy functions.

For banks active in several countries, both inside and outside the Eurozone, existing home/host supervisor coordination procedures will continue to exist as they do today.

11.5 Separation of trading activities

In February 2012, the EU Commission established a high-level expert group (HLEG) with the task to assess whether additional reforms on the structure of individual banks should be considered. The HLEG answer to the task was presented in a report in October 2012 and suggested mandatory separation of proprietary trading and other high-risk trading activities from the normal banking activities. The main purpose would be to separate certain particularly risky parts of financial activities from deposit taking activities within a banking group. The underlying objective is to make deposit taking banks safer and less connected to trading activities. Risky financial activities are defined as proprietary trading and all securities or derivatives incurred in the process of market-making as well as exposures towards hedge funds, private equity investments and structured investment vehicles.

During 2013 the Commission has been working on a legislative proposal and an impact study with the aim of presenting the proposal early 2014.

11.6 Trading book review

In October 2013, the BCBS published the second consultative document on a fundamental review of the trading book. The aim is to strengthen the resilience to markets risks due to observed weaknesses during the crisis. The review sets out a potential definition of the scope of the trading book and also proposes to strengthen the relationship between the standardised and internal model-based approaches.

11.7 Accounting standards

There are other regulations under consideration and implementation, which require close monitoring and assessment of the impact. New accounting rules and the proposal for a tax on financial transactions are two examples.

Nordea's accounting policies, which follow IFRS, are under significant change. Nordea's assessment is that the most important changes are related to Financial Instruments (IFRS 9), Insurance Contracts (IFRS 4) and Leasing (IAS 17), although other changes might/will also significantly impact Nordea. The finalisation dates and effective dates for these standards are still pending.

12. Appendix

12.1 General description of Pillar I, II and III

Capital adequacy is a measure of the financial strength of a bank, usually expressed as a ratio of capital to assets. There is now a worldwide capital adequacy standard (Basel II) drawn up by the Basel Committee on Banking Supervision. Within the EU, the capital adequacy requirements are outlined in the CRD III.

Over the years, amendments have been made to the first version of the CRD regulation. CRD II and CRD III were implemented at the end of 2010 and 2011and strengthened the large exposure regime, increased the quality of the capital base and added stricter securitisation regulation. The final version of the Capital Requirement Directive (CRD IV) and Capital Requirement Regulation (CRR), which was published in June 2013, require higher capitalisation levels and better quality of capital, better risk coverage, the introduction of a leverage ratio as a backstop to the risk based requirement, measures to promote the build-up of capital that can be drawn in periods of stress and the introduction of liquidity standards. The Directive will be implemented through national law within all EU countries during 2014, while the Regulation will become applicable in all EU countries from 1 January 2014.

The Basel II framework is built on three pillars:

- Pillar I – requirements for the calculation of RWA and capital requirements
- Pillar II – rules for the Supervisory Review Process (SRP), including the ICAAP
- Pillar III – rules for the disclosure on risk and capital management, including capital adequacy

12.1.1 *Pillar I*

Pillar I relates to the estimation, management and reporting of minimum capital requirements for credit risk, market risk, and operational risk. Banks can apply more or less sophisticated methods to calculate their RWA. More risk-sensitive models to estimate credit risk, market risk or operational risk require approval from the supervisory authorities.

There are three approaches for calculating capital requirements for credit risk in the CRD:

1. The standardised approach (SA), where calculation of credit risk is close to Basel I regulation, except an additional possibility to use external ratings for counterparties and a wider use of financial collateral. RWA is calculated by multiplying the exposure with a risk weight factor dependent on the external rating and exposure class.
2. The Foundation IRB (FIRB) calculation for credit risk is based on the internal rating and PD for each counterpart and fixed (supervisory) estimates for LGD, CCF and maturity.
3. The Advanced IRB (AIRB) calculations are based on internal estimates for PD, LGD, CCF and maturity. For the Retail IRB approach (RIRB), maturity is not included in the calculations.

Pillar I also encompasses the design, implementation, validation, oversight and performance of the credit risk classification systems.

12.1.2 *Pillar II*

Pillar II or the Supervisory Review Process (SRP), comprises two processes:

- the Internal Capital Adequacy Assessment Process (ICAAP); and
- the Supervisory Review and Evaluation Process (SREP).

The SRP is designed to ensure that institutions identify their material risks and allocate adequate capital, and employ sufficient management processes, to support the risks taken. The SRP also encourages institutions to develop and employ better risk management techniques in monitoring and measuring risk in addition to the credit risk, market risk and operational risk in the CRD. The ICAAP allows banks to review their risk management policies and capital positions relative to the risk they take. In the ICAAP, the institution ensures it has sufficient available capital to meet regulatory and internal capital requirements, also during periods of economic or financial stress. The ICAAP covers all components of risk management, from daily risk

management of material risk to the more strategic capital management of the Group and its legal entities. The SREP constitutes the supervisory review of the institutions' capital management and the assessment of their internal controls and governance.

Other risk types, which are not covered by the minimum capital requirements according to Pillar I, are typically liquidity risk, business risk, interest rate risk in the banking book, pension risk, real estate risk and concentration risk. These are covered either by capital or risk management and mitigation processes under Pillar II. In the calculation of economic capital (EC), Pillar II risks as well as risk in the life insurance operations are included. Liquidity risk is not included in the EC framework, but instead mitigated through the active management of liquidity. For further information on Pillar II, please see chapter 9.

12.1.3 *Pillar III*

The CRD also stipulates how and when institutions should make disclosures on capital and risk management. The disclosure should follow the requirements according to Pillar III. 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
- Liquidity risk
- Remuneration policy

12.2 IRB approach

Nordea is approved to use the IRB 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 2013. Following is a description of what exposures are included in the different exposure classes.

12.2.1 *IRB exposure classes*

12.2.1.1 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 unless it is treated as exposure to sovereigns according to regulations issued by the authorities.

12.2.1.2 Corporate exposure

Exposure that does not fall into any of the other exposure classes is classified as corporate exposure. The corporate exposure class contains exposure that is rated in accordance with Nordea's guidelines for rating.

12.2.1.3 Retail exposure

Exposure to SMEs (with an exposure of less than EUR 250k) and to private individuals are included in the retail exposure class and defined in accordance with Nordea's internal guidelines for scoring.

12.2.1.4 Other non-credit obligation assets

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

12.2.2 *Calculation of RWA in IRB approach*

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

The FIRB approach is used for calculating the minimum capital requirements for exposure to institutions and corporate customers. Input parameters are Nordea's internal estimate of PD while LGD, EAD and maturity are set by the supervisory authorities.

Internal estimates of PD, LGD and EAD are used in the retail IRB approach. Retail IRB risk parameters differ from the AIRB risk parameters in two respects; first, the asset correlation assumptions are different and second, the retail IRB risk weight functions do not include maturity adjustments.

12.2.2.1 Exposure at default (EAD)

The EAD is an estimate of the total exposure to the customer at the time of default. For on-balance sheet items, EAD is normally the same as the booked value, such as the market value or utilisation. For off-balance exposures, a CCF is multiplied with the amount to estimate how much of the exposure will be drawn at default.

12.2.2.2 Probability of default (PD)

PD means the likelihood of default of a counterpart and represents the long-term average of yearly default rates. The internal credit risk classification models provide an estimate of the repayment capacity of the counterpart. The internal risk classification scale consists of 18 grades for non-defaulted customers and three 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.

12.2.2.3 Loss given default (LGD)

The LGD measures the economic loss that can be expected if a customer defaults. The regulatory capital requirements are dependent on LGD.

For the FIRB institution and corporate exposure classes, LGD values are fixed by the supervisory authorities. The LGD values in the retail IRB approach are based on internal estimates. 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, country and customer type.

LGD values in the AIRB approach are calculated using similar internal calculations as for the retail IRB portfolio.

12.2.2.4 Credit risk mitigation

RWA and exposures are reduced by the application of credit risk mitigation techniques. Only certain types of collateral and some issuers of guarantees are eligible to reduce RWA and hence the capital requirement. 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 as well as insurance and legal certainty) stipulated in the capital adequacy regulations. Collateral items and guarantees which do fulfil the minimum capital requirements are defined as eligible collateral.

Nordea uses a wide variety of risk mitigation techniques in different markets which contribute to risk diversification and credit protection.

12.2.2.5 Maturity

For exposure calculated under the FIRB approach, maturity is set to standard values in the RWA calculation formula based on the estimates set by the financial supervisory authorities. The maturity parameter is set to 2.5 years for the exposure types on-balance sheet items, off-balance sheet items and derivatives. For securities financing the maturity parameter is set to 0.5 years. Under the RIRB approach, maturity is not included in the RWA calculation.

12.3 Standardised approach

12.3.1 *Standardised exposure classes*

12.3.1.1 Central governments and central banks

Exposure to central governments and central banks is treated as low risk if the counterparty is within the member states and/or has a high rating.

12.3.1.2 Regional governments and local authorities

Exposure to regional governments and local authorities is treated as exposure to the central government in whose jurisdiction they are established if there is no differences in risk weight between the government and the local authority (with the exception of Norway, where a risk weight of 20% is applied).

12.3.1.3 Institution exposure

Exposure to institutions is assigned a risk weight by an eligible rating agency depending on the credit quality steps of the central government in the jurisdiction (although risk weight cannot be lower than 20%). Specific rules determined how to treat an exposure where no rating exists. The rating cannot be lower than that of the central government in the jurisdiction of the institution.

12.3.1.4 Corporate exposure

Exposure to corporates rated by an eligible rating agency is assigned a risk weight between 20% and 150%. Exposure without rating agency rating is assigned a risk weight of 100%.

12.3.1.5 Retail exposure

Retail exposure is assigned a risk weight of 75%.

12.3.1.6 Exposure secured by real estate

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 regulation differs between the Nordic countries.

12.3.1.7 Other

Additional exposure classes exist within the standardised approach, such as:

- Exposure to public sector entities
- Exposure to multilateral development banks
- Exposure to named international organisations
- Exposures in default
- High risk exposures
- Equity exposures
- Past due items
- Short-term claims.

12.3.2 ***Calculation of RWA in the standardised approach***

The standardised approach remains in use for some portfolios. The standardised approach is the least sophisticated of the capital calculation approaches. The risk weights in the standardised approach are set by the supervisory authorities and are based on external rating and exposure class. Some exposure classes are derived from the type of counterparty while others are based on asset type, product type, collateral type or exposure size.

The EAD of an on-balance sheet exposure in the standardised approach is measured net of value adjustments such as provisions. Off-balance sheet exposure is converted into EAD using a CCF set by the FSAs. Derivative contracts and securities financing have an EAD that is the same amount as the exposure.

List of abbreviations

ADF	Actual Default Frequency
AIRB	Advanced Internal Ratings Based
ALCO	Asset and Liability Committee
AML	Anti-money laundering
BCBS	Basel Committee on Banking Supervision
BCM	Business Continuity Management
BEM	Banks and emerging markets
BRRD	Bank Recovery and Resolution Directive
CCF	Credit Conversion Factor
CCO	Chief Credit Officer
CCP	Central Counterparties
CCR	Counterparty credit risk
CDO	Collateralised Debt Obligation
CDS	Credit Default Swap
CEM	Current Exposure Method
CET1	Common equity tier 1
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CIB	Corporate and Institutional Banking
CLN	Credit-Linked Notes
CLS	Continuous Linked Settlement
CP	Commercial Paper
CRD	The EU's Capital Requirements Directive
CRM	Comprehensive Risk Measure
CRO	Chief Risk Officer
CRR	Capital Requirement Regulation
CVA	Credit Valuation Adjustment
EAD	Exposure at Default
EBA	European Banking Authority
EC	Economic capital
ECC	Executive Credit Committee
EL	Expected Loss
EP	Economic profit
ERAT	Environmental Risk Assessment Tool
FIRB	Foundation Internal Rating Based approach
FSA	Financial Supervisory Authority
FSB	Financial Stability Board
FX	Foreign exchange
G-SII	Global systemically important institutions
GCCR	Group Credit Committee Retail Banking
GCCW	Group Credit Committee Wholesale Banking
GDP	Gross Domestic Product
GEM	Group Executive Management
GEM CC	Group Executive Management Credit Committee
GICS	Global Industries Classification Standard
HLEG	High-level expert group
IAS	International Accounting Standard
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standard
IMM	Internal Model Method
IRB	Internal Rating Based approach
IRM	Incremental Risk Measure
LCR	Liquidity Coverage Ratio
LGD	Loss given default
NBSF	Net Balance of Stable Funding
NLP	Nordea Life & Pensions
NSFR	Net Stable Funding Ratio
O-SII	Other systemically important institutions
OTC	Over-the-counter
ORX	Operational Riskdata eXchange Association
P/L	Profit and Loss
PD	Probability of default
PIT	Point-in-time
QRA	Quality and Risk Analysis
RCSA	Risk and Control Self-Assessment
RWA	Risk-weighted assets
S&P	Standard & Poor's
SA	Standardised approach
SIIR	Structural Interest Income Risk
SME	Small and medium-sized enterprises
SOO	Shipping, oil and offshore
SPE	Special Purpose Entity
SPRAT	Social and Political Risk Assessment Tool
SREP	Supervisory Review and Evaluation Process
SRP	Supervisory Review Process
SSM	Single Supervisory Mechanism
TTC	Through-the-cycle
VaR	Value-at-Risk