RISK AND CAPITAL MANAGEMENT 2021

Disclosure of financial information
for SpareBank 1 SR-Bank Group

SpareBank 1 SR-BANK

Contents

INTRODUCTION

Risk and capital management in SpareBank 1 SR-Bank intend to create financial and strategic added value

Risk and capital management in SpareBank 1 SR-Bank should create financial and strategic added value through:

- A good risk culture
- A clear management and control structure that promotes independence
- A good understanding and management of the risks that drive earnings and losses
- Preventing single events damaging the group's financial position
- Pricing products and services based on underlying risk
- Effective raising and use of capital that reflects the chosen risk profile

This document has been prepared to provide the market with the best possible information on SpareBank 1 SR-Bank's risk and capital management. It is also intended to satisfy the stipulated requirements concerning the disclosure of risk information in accordance with the Norwegian Capital Requirements Regulations. This document is updated each year except for information on capital adequacy and the minimum regulatory capital requirements, which is updated quarterly. This information is updated in separate appendices. For information on the Group's remuneration scheme, see the separate report with accompanying tables in the Annual Report 2021.

SPAREBANK 1 SR-BANK ASA

SpareBank 1 SR-Bank ASA aspires to be the leading relationship bank in the group's market area. SpareBank 1 SR-Bank is a financial group for the whole of southern Norway that offers far more than banking services to customers.

SpareBank 1 SR-Bank has over several years developed into a large financial services group with subsidiaries and product companies that compliment the bank's service offering. The purpose is to give stimulus to growth and development in the market area where the group operates. The group assists customers in important decisions and investments – both in the lives of retail customers and the development of companies.

The group has an active role in society. It is natural based on the group's roots and long history as a savings bank. SpareBank 1 SR-Bank works actively to stimulate the creation of more jobs and for companies to grow vigorously. The group will be an ally for companies in the sustainability shift that will affect Norwegian companies in the future.

SpareBank 1 SR-Bank has a national distribution and has for several years had a position as the second largest Norwegian-owned bank. The group has offices in Rogaland, Vestland, Agder, Oslo and Viken.

The group's largest business areas are the traditional banking business with services aimed at the retail and corporate markets and customers in the public sector. The bank has over 350,000 customers, NOK 230 billion in loans and total assets of NOK 304 billion.

In 2021, group management spent time adjusting the existing group strategy. The strategy has been changed to ensure that the group is still well equipped for growth and development. The goal is stronger customer orientation throughout the organization, closer collaboration across the group and to promote sustainability as a business focus area.

An overview of the companies in the SpareBank 1 SR-Bank group is provided in the figure below.

Figure 1: Fully and partly owned companies in the SpareBank 1 SR-Bank group as of 31 December 2021

SPAREBANK 1 ALLIANCE

The SpareBank 1 Alliance is one of the largest providers of financial products and services in the Norwegian market.

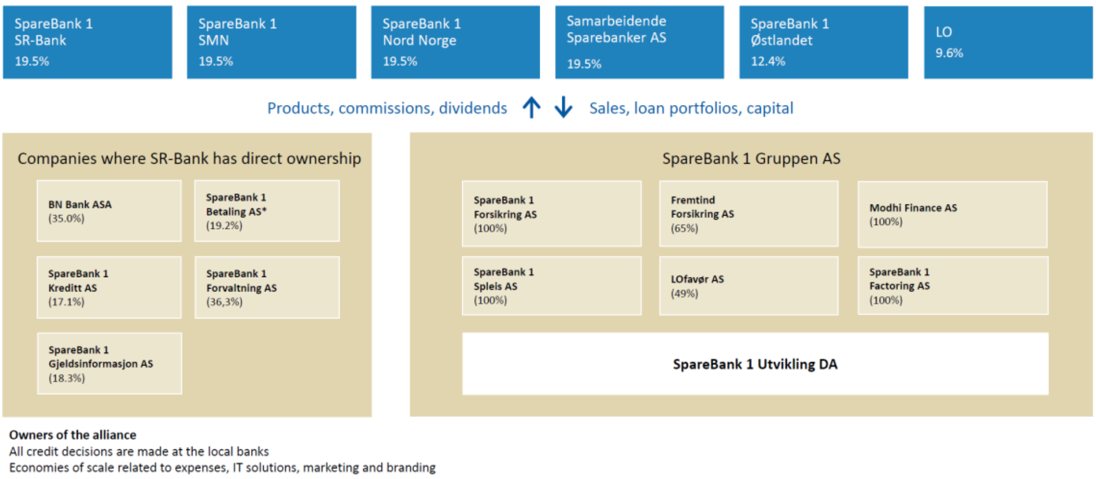
The SpareBank 1 Alliance's purpose is to acquire and provide competitive financial services and products and to exploit economies of scale in the form of lower costs and/or higher quality. The alliance also helps to secure the participating banks' value creation for the benefit of their own regions and the banks' owners.

The SpareBank 1 banks run the alliance through their ownership of, and participation in, SpareBank 1 Utvikling DA. The development and organisation of the product companies are organised through the banks' ownership of the holding company SpareBank 1 Gruppen AS.

SpareBank 1 Gruppen AS is owned by SpareBank 1 SR-Bank ASA (19.5%), SpareBank 1 Nord-Norge (19.5%), SpareBank 1 SMN (19.5%), SpareBank 1 Østlandet (12.4%), Samarbeidende Sparebanker AS (19.5% – owned by 11 savings banks in Southern Norway), and the Norwegian Confederation of Trade Unions (LO) and affiliated trade unions (9.6%).

The product companies in the SpareBank 1 Alliance are owned by the banks through the holding company SpareBank 1 Gruppen AS. The figure below summarises the ownership structure of the SpareBank 1 Alliance.

Figure 2: SpareBank 1 Alliance as of 31 December 2021



*Owns 23.1% in Vipps AS.

CAPITAL REQUIREMENTS

SpareBank 1 SR-Bank has significantly strengthened its capital adequacy over the past years.

Capital Adequacy Requirements

Financial supervisory authorities regulate financial institutions in order to ensure they assess and handle risk in an effective and sound manner and at the same time are solid and robust enough to withstand fluctuations and shocks in the economy. The capital adequacy Requirements are one way doing this.

The capital adequacy requirements build on three pillars:

- **Pillar 1**: Quantitative minimum requirements for primary capital.
- **Pillar 2**: Requirements for risk management and internal control, including requirements for internal processes for assessment of risk exposure and capital needs (ICAAP). Under Pillar 2 the supervisory authorities may impose requirements for additional capital if they find that the other requirements do not adequately capture the underlying risk in the institution.
- **Pillar 3**: Requirements for reporting and disclosing financial information. The intention of the pillar is to enable the market to assess the financial institution's risk and capital management.

Primary capital

According to the Norwegian Public Limited Liability Companies Act, all companies must always have equity commensurate with the risk and scope of the activities of the company. In Pillar 1, the Capital Requirements Regulations define minimum requirements for the following risk types: credit, market, and operational risk.

The different methods for calculating the minimum primary capital requirements in Pillar 1 are presented in the figure below.

[1] *The three methods available for calculating capital for operational risk will be replaced by a new standard method when final basel regulations enter into force in January 2022.*

Figure 3: Alternative methods for calculating the minimum primary capital requirements[1]

Credit risk	Market risk	Operational risk
Standard method	Standard method	Basic Indicator Approach
Basic IRB method*	Internal Measurement Approach*	Standardised Approach
Advanced IRB-method*		Advanced Measurement Approach*

* The methods require approval of the Financial Supervisory Authority of Norway

SpareBank 1 SR-Bank uses the standard method for calculating capital requirements for market risk and the standardised approach for operational risk. When calculating necessary requirements for capital on credit risk, SpareBank 1 SR-Bank has permission to use internal models for both the retail and the corporate market. This entails that internal models are used in calculating the risk parameters probability of default (PD), conversion factor (CF), used in determining exposure at default (EAD), and loss given default (LGD).

IRB system

The IRB system includes all the models, work and decision processes, control mechanisms, IT systems and internal guidelines used in the measurement and management of credit risk. SpareBank 1 SR-Bank’s objective with the IRB system is to provide a basis for sound risk management and ensure satisfactory capital adequacy according to the risk the group undertakes. The IRB system affects a substantial part of the group’s operations, and since its implementation the system has helped improve the quality of risk management in SpareBank 1 SR-Bank considerably.

The internal measurement methods used for internal risk management are reviewed in the chapter on risk and capital management in SpareBank 1 SR-Bank. Regulatory calculations of risk exposure and capital requirements are calculated using the same systems and models that are used for internal risk management, but with individual differences in models and model parameters. The effect of these differences is illustrated in table 32 in the appendix.

The table below shows the main methods used by SpareBank 1 SR-Bank when calculating the minimum primary capital requirements for credit, market and operational risk.

Table 1: SpareBank 1 SR-Bank's methods for calculating minimum regulatory capital requirements

Type of risk	Portfolio	Regulatory method
Credit risk	States – parent bank	Standard method
	Institutions – parent bank	Standard method
	Housing cooperatives, clubs and associations – parent bank	Standard method
	Enterprises – parent bank	Advanced IRB
	Mass market – parent bank	IRB - Mass market
	Leasing	Standard method*
	Consumer financing and secured car loans	Standard method
	SpareBank 1 SR-Investering AS – subsidiary	Standard method
	SpareBank 1 SR-Forvaltning AS – subsidiary	Standard method
	Mass market - SpareBank 1 Boligkreditt AS	IRB - Mass market
	Mass market - SR-Boligkreditt AS	IRB - Mass market
	Enterprises – SpareBank 1 Næringskreditt AS	Standard method
	Enterprises – BN Bank AS	Advanced IRB
	Mass market – BN Bank AS	IRB - Mass market
Market risk	Equity risk – parent bank	Standard method
	Debt risk – parent bank	Standard method
	Currency risk – parent bank	Standard method
	Subsidiaries and part-owned companies	Standard method
Operational risk	SpareBank 1 SR-Bank including subsidiaries	Standardised approach
	Other part-owned companies	Standard method

*The formerly wholly owned subsidiary SpareBank 1 SR-Finans AS was merged into the parent bank SpareBank 1 SR-Bank ASA in 2017. The merged portfolio is reported on a regulatory basis in accordance with the standard method, while internally using the IRB method. SpareBank 1 SR-Bank has applied the Financial Supervisory Authority for permission to use advanced IRB for the merged portfolio of leasing.

Combined buffer requirements

Basel III introduces requirements for combined buffer capital that exceed the minimum primary capital requirements. These are the capital conservation buffer, systemic risk buffer, countercyclical buffer and buffer for systemically important institutions.

Capital conservation buffer (2.5%): The requirement for a capital conservation buffer of 2.5 per cent of the bank's basis for calculation remains constant throughout all economic cycles. The purpose of this buffer is to ensure that banks build up capital in economic booms in order to prevent the capital falling below the minimum requirement in periods of recession.

Systemic risk buffer (4.5%): System risk is defined as the risk that financial instability will result in disruptions in the provision of financial services of a scope that could give significant negative effects for production and employment. The systemic risk buffer requirement increased from 3.0% to 4.5% with effect from 31 December 2020. Since this buffer requirement is directed at structural vulnerabilities and other systemic risks in the Norwegian economy, it will only apply to banks' exposures in Norway, unlike previous buffer requirements that apply to all operations.

Countercyclical buffer (0-2.5%): The Ministry of Finance sets the level of the countercyclical buffer based on Norges Bank's advice, and the size of the buffer depends on the economic situation. The objective of the countercyclical buffer is to make the institutions even more solid and resistant to lending losses in a future recession and to reduce the risk that banks will reinforce a potential recession by reducing their lending.

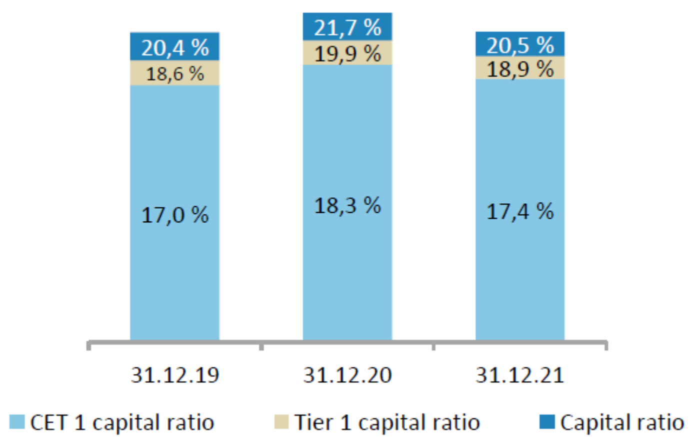
The capital buffer requirement was 2.5 percentage points at the end of 2019. As a result of the Covid-19 situation, the countercyclical buffer requirement was lowered by 1.5 percentage points to 1.0 percent with effect from March 2020. In June 2021, it was decided to increase the capital requirement for countercyclical capital buffer by 0.5 percentage points to 1.5 per cent with effect from 30 June 2022. In December 2021, it was decided to increase the countercyclical capital buffer further by 0.5 percentage points to 2.0 per cent, with effect from 31 December 2022.

Buffer for systemically important institutions (2.0%): Mortgage companies that are defined as systemically important by the Norwegian authorities will be subject to an extra buffer requirement of 2 per cent. In general, institutions with total assets of at least 10 per cent of mainland Norway's GDP, or at least a 5 per cent share of the market for loans, is defined as systemically important institutions. SpareBank 1 SR-Bank ASA is not defined as a systemically important financial institution.

Pillar 2 requirement (1.7%): The objective of the Pillar 2 requirement is to identify capital needs related to risks that are not entirely or at all covered by the capital requirements in Pillar 1. For SpareBank 1 SR-Bank, the Pillar 2 supplement is set to 1.7 per cent.

At year end 2021, the common equity tier 1 capital ratio of 15.2 per cent will be met with a good margin. SpareBank 1 SR-Bank ASA has an internal target of having core tier 1 capital adequacy of 16.7 per cent by the end of 2022. The group has maintained its original capital target to take into account the expectation of a gradual increase in the countercyclical capital buffer from 2022.

Figure 4: Capital Requirements



Actual capital adequacy

At year-end 2021, the Common Equity Tier 1 capital ratio was 17.4% (18.3%).

Common Equity Tier 1 capital ratio has been reduced by 0.9 percentage points in the last 12 months, of which 1.1 percentage points are due to provisions and payment of dividends of NOK 5.50 for the financial year 2019, and 0.6 percentage points are due to provisions and payment of dividends of NOK 3.10 for the financial year 2020. As a result of the outbreak of Covid-19 in March 2020, the general meeting in April 2020 decided to follow the board's recommendation not to pay dividends for 2019. Dividends for 2019 were therefore not paid until 19 March 2021. Dividend for 2020 was paid on October 13, 2021.

Leverage ratio

Unweighted tier 1 capital adequacy (leverage ratio) is a solidity indicator that supplements the risk-weighted minimum requirements. The minimum requirement for an unweighted tier 1 capital ratio is set at 3 per cent. In addition, all banks must have an unweighted tier 1 capital buffer of at least 2 per cent. In addition, systemically important banks must have an unweighted tier 1 capital adequacy buffer of at least 1 per cent.

The minimum requirement for unweighted tier 1 capital adequacy for SpareBank 1 SR-Bank is 5.0 per cent. At the end of 2021, SpareBank 1 SR-Bank has an unweighted tier 1 capital ratio of 7.1 per cent, and thus well above the minimum requirement.

RISK AND CAPITAL MANAGEMENT IN SPAREBANK 1 SR-BANK

The core purpose of the banking industry is to create value by assuming deliberate and acceptable risk. SpareBank 1 SR-Bank therefore invests significant resources in the further development of risk management systems and processes that are in line with leading international practice.

Overall risk exposure

SpareBank 1 SR-Bank is exposed to various types of risk, and the most important ones are:

- **Credit risk:** the risk of loss resulting from the customer's or counterparty's inability or unwillingness to fulfil their obligations
- **Liquidity risk:** the risk that the group is unable to refinance its debt or does not have the ability to fund increases in assets without significant additional costs
- **Market risk:** the risk of loss due to changes in observable market variables such as interest rates, foreign exchange rates and securities markets
- **Operational risk:** the risk of losses due to weak or inadequate internal processes or systems, human error or external incidents
- **Climate risk:** the risk of financial losses and financial instability as a result of physical climate change and society’s response to it
- **Owner risk:** the risk of SpareBank 1 SR-Bank suffering negative results from stakes in strategically owned companies or of the group having to inject fresh equity into these companies. Owned companies are defined as companies where SpareBank 1 SR-Bank has a significant stake and influence
- **Compliance risk:** the risk of the group incurring public sanctions/penalties or financial loss as a result of a failure to comply with legislation and regulations
- **Pension risk:** the risk of increases in future pension liabilities
- **Regulatory risk:** uncertainty about future regulations
- **Business risk:** the risk of a failure in earnings and access to capital because of lack of trust and reputation in the market, i.e. customers, counterparties, stock market and authorities
- **Reputation risk:** the risk of a failure in earnings and access to capital because of lack of trust and reputation in the market, i.e. customers, counterparties, stock market and authorities
- **Strategic risk:** the risk of losses resulting from the wrong strategic decisions
- **Concentration risk:** the risk of an accumulation of exposure to an individual customer, sector or geographical area arising

One of the ways in which the group’s risk is quantified is through the calculation of expected losses and risk-adjusted capital. Expected losses describe the amount that the group must expect statistically to lose during a 12-month period, while risk-adjusted capital describes how much capital the group believes it needs to cover the actual risk to which the group is exposed. Since it is impossible to fully protect against all losses, the group has stipulated that the risk-adjusted capital shall cover 99.9 per cent of potential unexpected losses.

The process of risk and capital management (ICAAP)

The purpose of the Policy for risk and capital management is to provide guidelines for the Group's overall attitudes and principles for risk and capital management, and to ensure that the Group has an efficient process for this. The policy shall furthermore ensure that the internal framework satisfies laws, regulations and best practices for good risk and capital management.

The process of risk and capital management in SpareBank 1 SR-Bank builds on the following main principles:

- The group’s risk and capital management framework must be documented and based on the best international practices
- The group must have a management and control structure that promotes prudent, independent management and control
- The risk and capital management shall form an integral part of the management and decision process in the group

- Risk and capital management in the group shall support the group's strategic development and achievement of objectives while ensuring financial stability and sound management of assets
- The group must have a good risk culture characterised by a high awareness of risk and capital management
- The board must approve the group's desired risk profile on at least an annual basis
- SpareBank 1 SR-Bank shall have a willingness to assume risk that provides a sufficient buffer in relation to the group's risk capability, and that no single events can seriously damage the group's financial position
- The risk identification process must be implemented regularly, look forwards, and cover all significant areas of risk
- Quantification of risk must be based on recognised methods and be sufficiently conservative to properly take account of any weaknesses in the model
- Thorough analyses must be carried out of the identified risks in order to understand the risks' effects on income, costs and losses
- Based on the risk analysis, effective management and control measures shall be established for the individual risks based on the risk analysis. Measures that reduce probability shall take precedence over measures that reduce consequences
- The group must prepare a minimum 5-year financial prognosis at least once a year, and this must as a minimum cover expected financial developments, as well as a period involving a serious financial setback. The serious financial setback must be severe, but realistic.
- Return on economic capital shall be one of the most important strategic result measurements for the internal control of SpareBank 1 SR-Bank. The credit-based framework for EAD in the bank's internal market divisions must be determined on the basis of risk-adjusted returns.
- The group must carry out comprehensive, periodic risk follow-up and reporting
- The group shall, insofar as it is possible, price activities and products in line with the underlying risk to ensure the right level of risk is assumed
- The group must draw up robust recovery plans so it can manage critical situations in the best possible way should they arise
- The group must have clear, unambiguous definitions of the various types of risk

To ensure an effective and suitable process, the framework is based on different elements that reflect the way the board and management manage SpareBank 1 SR-Bank. The main elements are described in the figure below.

Figure 5: Main elements in the risk and capital management process in SpareBank 1 SR-Bank

The group's strategic target

The framework for management and control is based on the group's current strategic target.

Defining the risk profile

The board must, at least once a year, adopt the group's risk profile. SpareBank 1 SR-Bank defines its risk profile by first calculating the group's *capacity* to bear risk and secondly calculating its *willingness* to assume risk. Capacity and willingness to bear risk are defined by the group's results, solidity, liquidity and credit quality, and are set for both a normal business cycle and for a serious economic downturn.

The capacity to bear risk describes the maximum risk exposure the group can bear before it is forced into an unwanted situation and needs to evaluate necessary recovery measures. The willingness to assume risk defines the group's maximum desired risk exposure from the perspective of its earnings and losses and given the defined risk capacity. The difference between the capacity and willingness to bear risk expresses the group's safety buffer in relation to ending up in a possible recovery situation. The willingness to assume risk should be significantly lower than the capacity to bear risk.

Risk identification and analysis

The process for risk identification is forward-looking and covers all the group's significant risk areas.

In areas where the effect of the established control and management measures is not considered satisfactory, improvement measures are implemented. Thorough analyses of the identified risks are conducted to understand their characteristics and the effect of established control and measurement measures.

Measures that reduce probability shall take precedence over measures that reduce consequences. Up-to-date documentation should be available for all the important parts of the group's business areas. This documentation should specify the control and management measures that have been established, levels of risk, and references to any instructions, authorities and specifications. An annual risk strategy is prepared each year based on these risk analysis. The strategy specifies acceptable levels of risk and targets for risk-adjusted returns.

Financial projections

Two financial projections are conducted, at least annually:

- Financial projection of expected financial development over the next five years
- Financial projection in a situation involving serious economic downturn over five years

Financial projection of expected financial development

The financial projection of expected financial development is based on SpareBank 1 SR-Bank's prognosis for the current period. This prognosis mirrors the group's strategic target, business plans, capital requirements and expected macroeconomic development over the coming years.

The purpose of the projection is to demonstrate how this will affect the group's financial development, including the return on equity, the funding situation and capital adequacy.

Financial projection of a serious economic downturn (stress test)

The purpose of the financial projection of a serious economic downturn is to:

- evaluate potential losses based on different economic scenarios
- evaluate the vulnerability of portfolios/activities
- increase the understanding of how a shock would affect the group's profitability, liquidity situation and capital adequacy
- evaluate potential losses based on different strategic possibilities
- identify weaknesses in the group's risk strategies and processes to help develop risk mitigation measures and prepare contingency plans

To assess the consequences of an economic downturn, SpareBank 1 SR-Bank largely focuses on those areas of the economy that affect financial development. These are primarily developments in credit demand, the stock market, the interest rate market, and credit risk. In addition to having an impact on the yield of the underlying assets, an economic downturn will also have an impact on customer savings habits.

Capital allocation

Risk-adjusted return is one of the most important strategic result measurements in SpareBank 1 SR-Bank. Risk-adjusted return is based on the calculation of risk-adjusted capital, which describes what level of capital the group must hold to cover an unexpected loss within a year. The calculation is made with a confidence level of 99.9 per cent.

This implies that capital is allocated to business areas in accordance with the calculated risk of the operation. Return on capital is continuously monitored.

Evaluation and measures

The abovementioned financial projections provide the executive management team and the board with sufficient understanding of the risk to make proper strategic choices and at the same time ensure that the group has an acceptable risk profile. Based on the analysis, SpareBank 1 SR-Bank develops capital plans to achieve a long-term and effective capital management and ensure that the group's capital adequacy is acceptable, given the risk exposure and strategic targets.

SpareBank 1 SR-Bank has also prepared recovery plans to the extent possible be able to handle emergencies if they nevertheless arise. The recovery plans cover:

- Capital adequacy
- Liquidity risk
- Operational risk

Reporting and follow-up

SpareBank 1 SR-Bank's overall risk exposure and risk trends are reported to the executive management team and the board in periodic risk reports.

The Risk Management Department performs general risk monitoring and reporting, and the department is independent of the different business units in the group; the department reports directly to the chief executive.

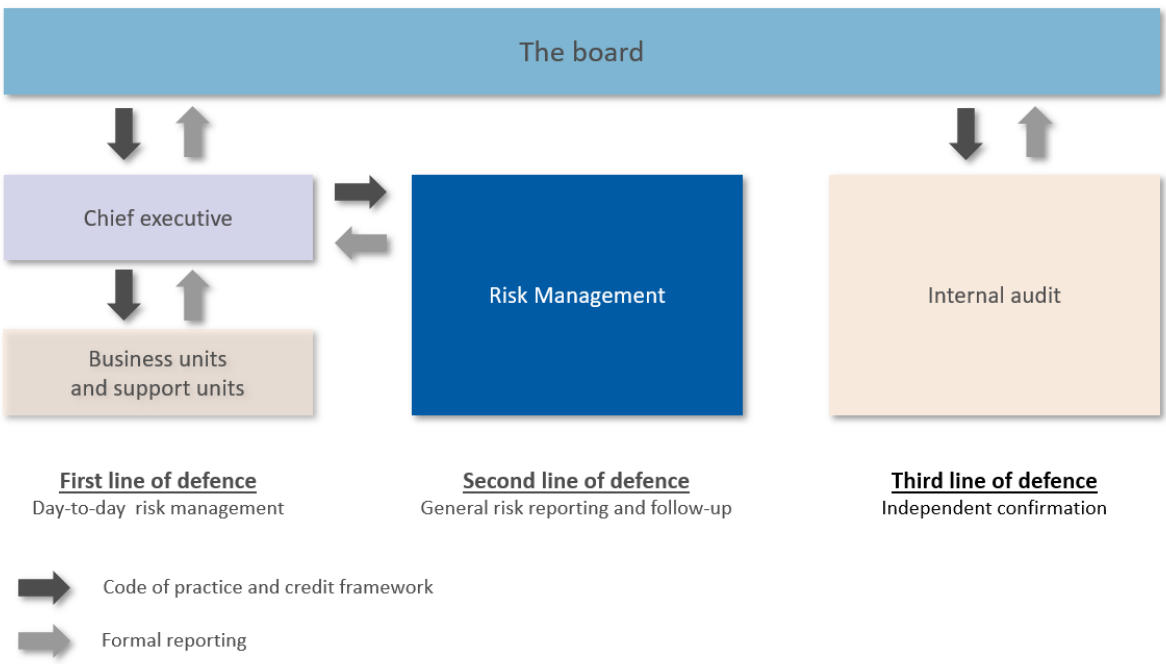
All managers are responsible for the day-to-day risk management within their area of responsibility and must continuously ensure that the risk exposure is within the limits set by the board or chief executive.

Organisation

SpareBank 1 SR-Bank values independence in management and control, and the responsibility is divided between different roles in the organisation. Through the general assembly, the shareholders execute the highest authority in SpareBank 1 SR-Bank.

The group values a control and management structure that encourages targeted and independent management and control.

Figure 6: The organisation of risk and capital management



The Board of SpareBank 1 SR-Bank is responsible for approving a sound risk profile, return targets, overall framework for risk and capital management including the IRB system and risk models in general. The Board is also responsible for approving risk limits and authorizations as well as the ICAAP (Internal Adequacy Assessment Process) with associated assessment of sound solvency and liquidity in relation to the Group's risk profile and regulatory requirements.

The board shall ensure that the framework for risk and capital management is sufficiently communicated and implemented throughout the group. The board shall further ensure that the framework is followed up with sufficient authority and resources.

The chief executive (CEO) is responsible for the overall risk management. This means that the CEO is responsible for implementing the framework for risk and capital management in the group. The CEO is also responsible for ensuring that the group has a risk exposure at all times that is within the group's chosen risk profile and in accordance with the risk strategies.

Managers of the business and support areas and employees are responsible for the day-to-day risk management within their area of responsibility. They must at all times ensure that the risk management and risk exposure are in accordance with the framework and that the risk exposure is within the given framework.

The risk management department is organised independently of the business units and reports directly to the CEO. The Chief Risk Officer also has the opportunity, in individual cases, to report directly to the Board if extraordinary situations should require so. The department is responsible for the further development of the framework for risk and capital management. The department is also responsible for independent follow-up that the risk exposure is in accordance with risk appetite and risk strategies. The department also prepares proposals for risk profiles and risk strategies that ensure financial robustness and an efficient use of the group's equity. The department must have sufficient breadth and depth in competence and capacity.

The internal audit is responsible for systematically evaluating and reviewing the effectiveness and appropriateness of the group's control and management structure, framework for risk and capital management, internal control and compliance. The internal audit is risk-based and evaluates on a rolling basis both the frameworks for the mentioned topics and compliance with these. The internal audit must be independent and have sufficient competence and capacity. The internal audit reports to the board.

Committees:

*The risk committe*e shall generally follow up the Group's risk exposure and framework for risk and capital management. The risk committee shall have the authority to investigate all activities and matters relating to the group's overall risk and may obtain information from any employee. All the Group's employees and shop stewards shall provide the information and assistance that the risk committee may request. The risk committee can implement any investigations it finds necessary to cover its tasks, including obtaining external advice and assistance.

The risk committee answers to the board of SpareBank 1 SR-Bank for the execution of its tasks. The individual member has no special external responsibility in his role as a member of the risk committee. The board's responsibility and the individual board member's responsibility are not reduced because of the risk committee's activities.

The Risk and Compliance Committee is an advisory body for the Chief Risk Officer and the Chief Compliance Officer, respectively, in matters within their own area of responsibility. The committee's mandate is to follow up the group's risk management and compliance status and recommend overall measures, propose risk strategic frameworks within the various risk areas and follow up capital allocation principles in the various risk areas and business units.

The Validation Committee is an advisory body on matters related to the IRB system and recommends to the Chief Risk Officer. The committee's mandate is to consider the validation of the risk models and risk management systems as well as to assess and possibly recommend changes or needs for new risk models and risk management systems. The committee shall also follow up regulatory matters related to the risk models and risk management systems.

The *Balance Committee* in SpareBank 1 SR-Bank provides advice on the operative management of the bank's balance sheet within the limits set by the board. The committee's main focus is monitoring and control of the factors that directly and/or indirectly affect the bank's funding capacity.

The credit committees are responsible for making independent recommendations to authority holders. When making their recommendations, the credit committees evaluate loan and credit applications based on the current credit strategy, credit policy guidelines, loan granting regulations, and credit review routines. The credit committees attach special importance to the identification of risk in relation to individual applications and carry out an independent assessment of credit risk, which clarifies the consequences for the bank of the various risks.

Risk culture

Risk culture means values and attitudes that are expressed through risk awareness, actions and ability for organisational learning. A good risk culture constitutes the foundation of good risk management and is a prerequisite for the full benefit of professional policies, procedures and models.

In cooperation with the University of Stavanger, the Group has therefore developed a framework that is used to carry out regular group-wide evaluations of risk culture. A Risk Culture survey was conducted in 2021 and shows good risk culture through and through all departments. The results of the measurements provide good discussions in the group and increased awareness and insight into themes that are not usually discussed directly. The fact that such measurements are conducted is therefore considered to make an important contribution to creating a sound risk culture in the organisation.

CREDIT RISK

Credit risk is the risk of loss resulting from the customers or counterparty's inability or unwillingness to fulfil his obligations.

About credit risk

SpareBank 1 SR-Bank is primarily exposed to credit risk through its loan portfolios in the retail and corporate markets. The group is also exposed to credit risk through the liquidity portfolio. This portfolio mainly consists of low risk commercial paper and bonds that qualify for loans from Norges Bank.

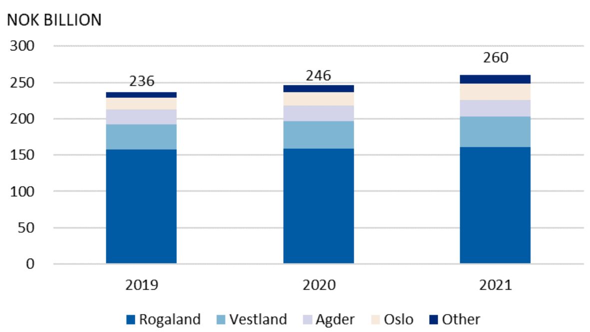
Development in credit risk

In describing credit risk in this paragraph, the following terms are used:

- Probability of default (PD) – the probability for default in a twelve-month period based on a long-term outcome[2]
- Exposure at default (EAD) – a calculated size that contains actual exposure and expected exposure for allocated, but not drawn limits at the time of default

SpareBank 1 SR-Bank has Southern Norway as its primary geographic market area, with the largest presence in Rogaland, Agder and Vestland as well as Oslo and Viken. The figure below shows the exposure by geographical area as of December the last three years for performing customers in SpareBank 1 SR-Bank. The exposure is shown for the parent bank and includes portfolios transferred to credit institutions.

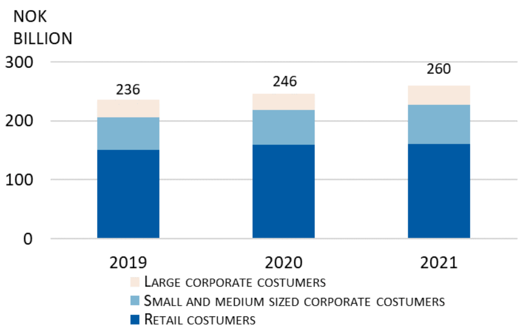
Figure 7: Exposure (EAD) by geographic market areas



Rogaland is the group's largest market area, and the exposure as of December 2021 is about NOK 161 billion. This represents 62 per cent of SpareBank 1 SR-Bank's total loan exposure. The exposure in Vestland, Agder and Oslo amounted to NOK 42, 23 and 23 billion, respectively, in 2021.

SpareBank 1 SR-Bank's loan exposure consists of a well-diversified portfolio with both retail and corporate customers. The figure below shows the development in the loan portfolio over the last three years.

Figure 8: Exposure by customer segment

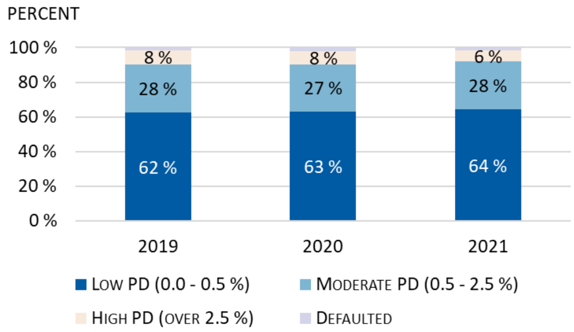


The largest share of the loan exposure in SpareBank 1 SR-Bank is aimed at retail customers, and loans are mainly financed by mortgages on real estate. Exposure to retail customers has increased from NOK 160 to 161 billion in 2021. 97 per cent of loan exposure in the retail market consists of loans that are smaller than NOK 10 million. Exposure to small and medium sized corporate customers has increased from NOK 58 to 67 billion in 2021. Credit exposure to large corporate customers has increased from NOK 28 to 32 billion in 2021. Large corporate customers are defined as single customers with exposure (EAD) larger than NOK 250 million.

A clearly defined framework that sets limitations on what is financed, and under which conditions, helps to ensure that the portfolio remains robust.

[2] Long term outcome through a full loss cycle of 25 years

Figure 9: Loan portfolio by probability of default (PD)[3]



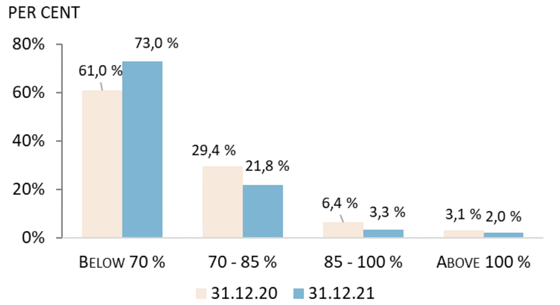
The share of loan exposure on customers with a probability of default (PD) lower than 0.5 per cent constitutes 64 per cent of the total loan portfolio in 2021. These are customers risk classified in default classes A, B or C. The share of the loan exposure with moderate PD was 28 per cent. These customers are risk classified in the default classes D, E or F.

SpareBank 1 SR-Bank has a considerable focus on following up commitments with PD higher than 2.5 per cent. As of December 2021, 6 per cent of the loan exposure to customers with PD is higher than 2.5 per cent. These customers are risk classified in default classes G, H and I. The exposure to non-performing customers amounts to 1,6 per cent of total lending exposure in the corporate market and the retail market as of December 2021.

The composition of the portfolio is based on a clearly defined strategy in which the growth and risk profile are managed, for example, through special credit strategy limits for concentration risk. The concentration risk has been significantly reduced in the last few years in line with the risk strategy guidelines set by the board. In particular, there has been a heavy focus on reducing the proportion of commitments with the potential to produce significant losses.

The figure below illustrates the development of the loan-to-value ratio in the retail market portfolio from 2020 to 2021. The calculation of loan-to-value ratio is based on the collateral's market value and is shown as total-distributed loan-to-value ratio. In the case of total-distributed loan-to-value ratio, the entire relevant loan is allocated to one and the same interval.

Figure 10: Loan-to-value ratio (LTV) retail market portfolio - total distributed (including portfolio transferred to SpareBank 1 Boligkreditt AS and SR-Boligkreditt AS)



The market values of housing in SpareBank 1 SR-Bank's market area have developed positively over the past year. This means that the proportion of loans within 70 per cent of assessed collateral values has increased through 2021. The proportion of loans with a loan-to-value ratio lower than 85 per cent 94.8 per cent at the end of 2021, compared to 90.5 per cent the year before.

Managing credit risk

There is currently extensive work with the bank's overall framework for risk and capital management, including the IRB system and risk models in general. This is done to comply with new requirements and guidelines from EBA which enter into force on 01.01.2022. The changes are subject to application.

The overall credit strategy establishes that the group shall have a moderate risk profile. The credit risk is managed through limitations for granting credit, follow-up of commitments and portfolio management.

Credit risk management is based on the following main principles:

- The Group shall be among the leading in Norway in managing credit risk
- Particular emphasis should be placed on ensuring that the customers' activities comply with applicable laws and regulations, and that the business has a long-term perspective
- The main focus of credit granting should be the customer's ability of debt servicing, and weak / lacking service capacity should not be compensated with good security
- The risk that arises from concentrating the lending activity against a single customer,

[3] For retail customers, there are different requirements for a long-term outcome for probability of default (PD), internal and regulatory. The figure shows the loan portfolio with internal PD estimates

industry or segment should be limited to avoid single events being able to seriously harm the Group's financial position

Credit culture

SpareBank 1 SR-Bank is one of the leading players in Norway within managing credit risk. This is achieved through local knowledge about the customer, the use of robust credit models and credit analyses, and by stipulating clear requirements concerning the employees' qualifications and attitudes where the ability to recognise risk and willingness to learn from experience is emphasised.

In credit appraisals, special importance is attached to whether the customer's activities comply with current laws and regulations, whether the customer's activities have a long-term perspective, and whether the customer has both the necessary ability to pay and robust equity given the nature of their activities. The process of granting credit involves a clear division of responsibilities where cooperation should ensure the best possible basis for making decisions, but where actual decisions about credit are made on an individual basis.

The ability to comply with our own guidelines and in this way avoid financing commitments that conflict with these is especially important. There is, therefore, a heavy focus on ensuring the credit staff's active use of, and compliance with, a framework for managing credit risk is in line with best practice in this area. Compliance is also specifically monitored by independent representatives of the corporate risk management team, both through ongoing participation in the various credit committees and through independent reporting from the work of the credit committees.

Credit strategy

The group's primary market areas for risk exposure are Rogaland, the Agder counties and Hordaland. The general credit strategy stipulates that the group shall have a moderate risk profile where no single event shall be capable of seriously harming the group's financial position.

The group's credit strategy consists of general credit strategy limits for ensuring a diversified portfolio and a satisfactory risk profile. This limits the probability of default, expected losses, risk-adjusted capital and how high the total loan exposure can be in the corporate market. Portfolios that have been, or are going to be, transferred from SpareBank 1 SR-Bank to the mortgage companies, SpareBank 1 Boligkreditt AS and SR-Boligkreditt AS, are included in the abovementioned credit strategic framework.

There are also specific limits for the corporate market for the maximum share of risk-adjusted capital for individual sectors, the group of major customers, and maximum exposure to high risk customers, respectively. Specific limits have also been established to limit the maximum loss from a single customer. A single customer in this context includes commitments with one or more counterparties, when specific influence or financial links between the companies imply that financial difficulties in one of the companies is likely to result in payment difficulties for one or more others. The framework has been established to secure a diversified portfolio within the corporate market.

The credit strategic framework has been established by the board and any breaches from it must, therefore, be presented to the board for approval. The Risk Management Department reports on the development of the strategic credit framework to the board every quarter.

Credit political guidelines

The group's credit policy guidelines stipulate minimum requirements that apply to all types of financing, except commitments granted as part of the exercise of special credit hedging authorities. In addition to the general credit policy guidelines, a set of more specific credit policy guidelines related to sectors or segments that can entail a special risk have been prepared. The credit policy guidelines are revised at least once a year and are approved by the chief executive and reported to the board.

Credit authority regulations

The board is responsible for the group's granting of loans and credit, but delegates the responsibility to the chief executive, within certain limits. The chief executive then delegates these responsibilities within his own authority. Delegated credit authority is linked to a commitment's probability of default and collateral value. The authorities are personal. This means that the credit committees do not have decision-making authority but make recommendations to the authority holder. If there are no recommendations from credit committee, the authorisation limits will be halved. In general, the authorities are ample if a commitment's expected loss and probability of default indicate a low risk, but they will be restricted progressively with increasing risk. The credit authority rules are reviewed annually, and changes are approved by the chief executive and reported to the board. However, this does not apply to changes in the chief executive's credit authority as this is approved by the board.

Credit review routines

The credit review routines regulate in detail all factors related to the granting of credit by the group and follow-up of commitments. The credit granting process provides a more detailed description of the customer and the purpose of the loan application, in addition to evaluations of the following:

- Owners and management
- Structure of financing
- Compliance with credit strategy and credit policy
- Whether the customer will have adequate earnings to service the current obligations, interest and instalments
- For how long and in what manner the customer can cover their current obligations, interest and instalments if their earnings fail
- Collateral and overall assessment of risk

Measuring credit risk

Continuous commitment and portfolio monitoring is carried out on existing commitments. The credit risk is followed up in general by means of the group's portfolio management systems, systems for early notification of key development trends (early warning) and systems for monitoring the quality of the actual credit granting process.

Portfolio management

SpareBank 1 SR-Bank's risk exposure is monitored via a general portfolio management system. The portfolio management system contains information on the risk at both the aggregate and detailed levels. This makes it possible to conduct efficient monitoring and management of the risk performance of the portfolio. All portfolio information is updated monthly, including updates of the customers' probability of default. The development of risk in the portfolios is followed up with special emphasis on the development of the risk classification (migration), expected losses, risk-adjusted capital and risk-adjusted return. Risk-adjusted capital reflects the actual risk exposure better than what the traditional focus on lending volume does.

Early warning

The group's *early warning* system makes it possible to continuously monitor customers' key risk drivers and acts as an important indicator of potential negative developments in default rates. Its purpose is to detect key trends in development at an early stage.

Some examples of risk drivers are:

- Short-term and repeated default
- Development in limit utilisation
- Development in number of instalment postponements
- Official announcements

Credit process surveillance

The group's systems for monitoring the credit approval process make it possible to monitor credit quality and the risk-adjusted return on new commitments continuously. The system can compare quality across departments, and enables early action if, for instance, a department's credit practice is developing in an undesired direction.

Risk classification system

The group utilises credit models for risk classification, risk pricing and portfolio management. The risk classification system is based on the risk parameters as shown in the figure below:

Figure 11: The risk classification system in SpareBank 1 SR-Bank

Probability of default (PD)	The customers are classified in default classes based on the probability of default over a 12-month period, based on a long-term outcome
Exposure at default (EAD)	This is an estimate that indicates the group's exposure to a customer at default
Loss given default (LGD)	This is an estimate of how much the group can potentially lose if the costumer defaults on his obligations
Expected loss (EL)	Describes the loss the group can statistically expect to lose on the loan portfolio during a 12-month period (long-term outcome) in a normal business cycle
Risk-adjusted capital (UL)	Describes how much capital the group needs to reserve as a buffer for future unexpected losses
Risk group	The customer is assigned a risk group based on the risk-adjusted capital on the commitment
Risk pricing	SpareBank 1 SR-Bank is committed to finding the proper price for each risk, and has developed a pricing model that calculates a price given the commitment's risk

1) Probability of default (PD)

Customers are classified in default classes based on the probability of default over a twelve-month period, based on a long-term outcome through a full loss cycle[4].

SpareBank 1 SR-Bank defines default in line with guidelines[5] from the European Banking Authority (EBA) and Regulations on capital requirements and national adaptation of CRR / CRD IV § 7.

The probability of default is calculated based on historical series of data for financial key figures related to earnings and deterioration, as well as based on non-financial criteria such as conduct and age. Nine default classes (A – I) are used to classify the customers according to the probability of default. The group has two additional default classes (J and K) for customers with defaulted and/or written-down commitments.

SpareBank 1 SR-Bank focuses on stable and predictable credit granting and capitalisation over time, and the group therefore develops the models for calculating the probability of default based on a 'Through the Cycle' approach. This also corresponds with the approach behind the rating methods in the most renowned rating companies.

Besides predicting the long-term outcomes of probability of default regardless of the economic situation, the models must also manage to rate the customers based on risk (from the lowest probability of default to the highest probability of default) based on the current economic situation. This is important for predicting which customers may experience problems in the next twelve months. To achieve this, the model must also include variables that identify changes in the economic cycles.

SpareBank 1 SR-Bank calculates the long-term outcome for probability of default based on a full loss cycle lasting about twenty-five years, which consist of four periods with a normal economic situation and one period with a sharp economic downturn. Our own, representative historic default data is used as the data basis for the calculation.

Definitions of the individual default classes are shown in the table below. The table also shows the correlation between classification in the largest external ratings agencies and the classification used in SpareBank 1 SR-Bank.

[4] Long term outcome through a full loss cycle, consisting of four periods with normal business cycle and one period with an economic downturn

[5] EBA-GL-2016-07 and EBA-GL-2018-06.

Table 2: Definition of default classes and the correlation between classification in SpareBank 1 SR-Bank and in the largest external rating agencies

Default class	Lower limit for default	Upper limit for default	Rating scale Moody's	Rating scale Standard & Poor and Fitch
A	0.00%	0.10%	AAA - A-	Aaa - A3
B	0.10%	0.25%	BBB+ - BBB	Baa1 - Baa2
C	0.25%	0.50%	BBB-	Baa3
D	0.50%	0.75%	BB+	Ba1
E	0.75%	1.25%	BB	Ba2
F	1.25%	2.50%	BB-	Ba3
G	2.50%	5.00%	B+	B1
H	5.00%	10.00%	B	B2
I	10.00%	40.00%	B- - CCC/C	B3 - Caa3/C

2) Exposure at default (EAD)

Exposure at default (EAD) is defined as the exposure the bank has to a customer at the time of default. The conversion factor (CF) defines the extent the unutilised credit limit is expected to be drawn on upon default. Unutilised credit in this regard is defined as the remaining disposable limit one year prior to default.

For allocated, but not drawn upon limits for corporate market customers there is a drawing of 100 per cent (1). Granted, but not drawn upon limits for retail market customers have a conversion factor of 1, i.e. 100 per cent drawing upon default is assumed. For the corporate market, approved but not drawn upon facilities are multiplied by a conversion factor that varies between 60-90 per cent, depending on the customer's probability of default. The conversion factor for guarantees is a parameter set by the authorities and is set at 1 for loan guarantees and 0.5 for and other guarantees.

3) Loss given default

Loss given default describes how much the group could potentially lose if the customer defaults on their obligations. The model presents estimates that predict the degree of loss in an economic downturn. The valuation takes in account the value of underlying securities, the degree of recovery of unsecured loans, the degree of recovery before realisation and the costs the group has in recovering defaulted commitments.

Seven classes are used (1–7) for classifying commitments in relation to loss given default.

Definitions of these classes are illustrated in the table below.

Table 3: Definition of loss given default (collateral class)

LGD class	LGD interval
1	Until 10%
2	<10%, 20%]
3	<20%, 30%]
4	<30%, 40%]
5	<40%, 50%]
6	<50%, 60%]
7	Over 60%

4) Expected loss (EL)

Expected loss describes the loss the group can statistically expect to experience on the loan portfolio during a twelve-month period, based on a long-term outcome through a full loss cycle. Expected losses are calculated based on the probability of default, exposure at default and loss given default.

5) Risk-adjusted capital (UL)

There are many factors that affect the group's losses on loans and credits. The expected loss is based on uncertain magnitudes, where the uncertainty is largely related to the characteristics of the commitments. On well-secured loans, the uncertainty is limited, while the uncertainty is relatively large with less well-secured loans and with customers with an unstable ability to fulfil their obligations.

To take account of this uncertainty, a value for unexpected loss, or risk-adjusted capital, (UL) is calculated on all commitments. In this regard, SpareBank 1 SR-Bank uses the reference model for unexpected loss as set out in the Capital Requirements Regulations. The sum of unexpected losses for all commitments provides an estimate of how much the group could lose more than the expected loss.

Risk-adjusted capital describes how much capital the group believes it needs to cover the actual risk that the group has assumed. As it is impossible to fully protect against all losses, the group has stipulated that the risk-adjusted capital must cover all possible unexpected losses based on a stipulated confidence level of 99.9 per cent.

A commitment is risk classified in a risk group from lowest to highest risk, depending on the risk-adjusted capital. The risk groups are defined as shown in the table below.

Table 4: Definition of risk groups

	RISK-ADJUSTED CAPITAL (UL)% OF EAD	
RISK GROUP	**Lower limit**	**Upper limit**
LOWEST	0.0%	1.6%
LOW	1.6%	4.0%
MEDIUM	4.0%	8.0%
HIGH	8.0%	12.0%
HIGHEST	12.0%	99.99%

6) Risk pricing –RARORAC (Risk Adjusted Return on Risk Adjusted Capital)

SpareBank 1 SR-Bank focuses on pricing risk correctly. This means that high risk commitments are priced higher than low risk commitments. The general level of risk pricing will, however, also depend on the group's general return targets and an assessment of the competition situation. SpareBank 1 SR-Bank therefore uses models that calculate the correct risk price that should be taken into consideration when pricing the expected losses and return on risk-adjusted capital. The risk pricing model uses the same main components as in the groups risk classification system as the basis. The model is based on a standard risk adjusted return on risk adjusted capital (RARORAC) model for measuring risk-adjusted return.

The pricing model is primarily used for granting and renewing credit, as well as calculating the customer's price and measuring and monitoring profitability.

Collateral and other risk mitigation measures

SpareBank 1 SR-Bank uses collateral to reduce the credit risk in each commitment. For corporations, different types of conditions and terms are also specified in most credit agreements. Use of terms gives the bank assurance that the company keeps proper levels of liquidity and equity, or that the company complies with applicable laws and regulations related to its services.

In the retail market, the collateral is primarily real estate (housing). Several different types of collateral are accepted in the corporate market. This is shown in the table below.

Table 5: Main types of collateral

Type of collateral	**Retail market**	**Corporate market**
Real property	X	X
Land	X	X
Securities	X	X
Guarantees	X	X
Machinery and plant		X
Vessels		X
Motor vehicles/construction machines		X
Inventories		X
Agricultural chattels		X
Trade receivables		X
Deposits	X	X

The group establishes the realisation value of posted collateral based on statistical data over time, as well as expert evaluations in cases where the statistical date is insufficient. The realisation value is set to give a conservative evaluation that reflects presumed realisation value in an economic downturn.

Monetary claims in the form of deposit accounts with credit institutions may be pledged for the benefit of the credit institution. In consumer relations such pledge must be established by a written contract, and the pledge may only cover deposits that are in a unique account created in connection with the agreement.

In the retail market the market value of real estate is stipulated either by utilising the purchase price according to the contract, a broker valuation/appraisal or value estimates from Eiendomsverdi (applies only to residential properties. Eiendomsverdi is an information and analysis tool that provides access to an estimated market value for properties in Norway. Value estimates from Eiendomsverdi may be utilised in accordance with internal procedures if the property is located in a well-functioning residential market and if there is little uncertainty with regard to the value estimate. The realisation value on real estate is established based on the market value of the property and reduces this value by a reduction factor that depends on the type of property. In the retail market, assets other than real property are used as collateral to a limited extent.

In the corporate market, the value of commercial properties is calculated using the yield method, where the value is the present value of the expected cash flow to the property. Yield reflects the return an investor can demand when investing in a property and is affected by factors such as the property's location and nature, duration of the lease, tenants' solidity, regulatory risks, and the anticipated long-term, risk-free interest rate. The realisation value of the collateral is determined based on the market value, which is reduced by a factor that varies with the property's characteristics.

The reduction factors for all types of collateral are set based on the fall in value that must be expected in a sharp economic downturn.

Validation

The group continuously develops and tests the risk management system and the credit granting process to ensure that it is of high quality over time. The work is summarised in an annual validation report that provides a basis for the board of SpareBank 1 SR-Bank to determine whether the risk management system (IRB system) is well integrated within the organisation and whether it calculates the level of risk and capital requirements satisfactorily.

The IRB system is described in the chapter on capital requirements.

The aim of the validation process is to ensure that:

- The IRB system is customised to the portfolios on which it is used
- The assumptions the IRB system builds on are reasonable
- The IRB system measures what it is meant to measure
- The IRB system is well integrated in the organisation, and that it is a central part of the risk management and decision making in the bank
- SpareBank 1 SR-Bank complies with regulatory requirements

The validation process can be divided into four main areas:

Quantitative validation: Quantitative validation is intended to ensure that the estimates used for the probability of default, exposure at default and loss given default are always of adequately good quality.

Qualitative validation: The quantitative validation is supplemented by more qualitative assessments in the form of meetings with the bank's own expert group and with customer advisers. Using qualitative measuring methods ensures all processes, control mechanisms, and routines are fully validated, and it also contributes valuable input in relation to further developing the current models. Qualitative validation also provides supplementary information in those cases where the capture of statistical data is limited.

Application: Verification should show whether the system for managing and measuring credit risk is well integrated in the organisation, and if it represents a key part of the group's risk management and decision-making.

Compliance with regulatory capital requirements: The review is intended to ensure that SpareBank 1 SR-Bank complies with regulatory capital requirements.

The table below shows the models used by SpareBank 1 SR-Bank in the regulatory IRB reporting, as of end 2021.

Table 6: Risk models used in regulatory reporting, 2021

Commitment category	Segment	PD model	EAD model	LGD model
Mass Market (Retail Market) Housing	Mortgage customers with internal history of behaviour	RM score card A	CF = 1	LGD RM
Mass Market (Retail Market) Other	Other retail customers with internal history of behaviour	RM score card B	CF = 1	LGD RM
Businesses (Corporate Market)	Companies that have delivered public accounting	CM sector 1-7	EAD CM	LGD CM
	Companies that do not provide public accounting	Stencil core	EAD CM	LGD CM
	Newly established companies	Stencil score	EAD CM	LGD CM

In 2021, SpareBank 1 SR-Bank has developed and applied to the Norwegian FSA for permission to implement revised IRB models that are in accordance with new regulatory requirements from the European Banking Authority (EBA). At the same time, the bank has developed a new framework for validation that ensures compliance with new requirements from EBA in this area. The new regulatory requirements for the IRB system are valid from 2022.

In the validation, the different models are assessed based on four criteria: data quality, ranking ability, level and stability in the estimates.

Data quality

The models used for estimating probability of default (PD), exposure at default (EAD), and loss given default (LGD) were developed based on data from the period 1994-2012 from the banks in the SpareBank 1 Alliance.

The data is subject to thorough, continuous quality assurance and an annual validation process is conducted to ensure that it is representative of the current portfolio in SpareBank 1 SR-Bank. Validating the data also shows that it complies with the requirements concerning data that are stipulated in the Capital Requirements Regulations. Proper safety margins have been established where deemed necessary due to the uncertainty in the data.

Discrimination power

The model's ability to rank the customers is primarily measured by means of the area under curve (AUC) method.

The discrimination power of the model that estimates the customers' PD expresses the model's ability to rank the customers from the highest actual PD to the lowest PD.

The discrimination power of the model that estimates EAD will show the degree to which the model manages to rank the customers from those with the highest conversion factor (CF) to the lowest CF. Validation of the model for corporate customers is conducted annually. Exposure on retail market customers has a fixed conversion factor of one for all customers.

The discrimination power of the model for calculating LGD is validated by analysing estimated and actual losses in the various LGD classes, measured by median, unweighted and weighted average.

The extent to which the model can differentiate between customers with the highest expected losses (EL) and the lowest EL in relation to geographic exposure is also validated.

Level

Estimated PD shall predict long-term outcome through a full loss cycle. This means that the level of default will be overestimated in booms and normal economic situations, while in periods of serious recession the level of defaults will be underestimated. An assessment is made of whether the difference between actual level of default and estimated level of default is justifiable, given the economic situation. Stress tests are conducted to show that the economic properties of the model satisfy the requirements of the Capital Requirements Regulations.

For CF and LGD, the Capital Requirements Regulations assume that model estimates can predict the framework utilisation (CF) and losses in the event of serious economic downturns. This means that the conversion factor and loss estimates must always be higher than observed values in normal economic situations. Each element in the LGD model, including recovery, the reduction factors used for collateral values, proportion of unsecured exposure recovered, and unsecured exposure and recovery costs, undergoes validation.

The level of expected loss (EL) is assessed against the level of actual costs recognised in the accounts, both on an overall level and by geographic area. As with the estimated PD, EL should predict long-term outcome through a full business cycle.

Furthermore, stress tests are conducted on all parameters to validate that the complies with the Capital Requirements Regulations.

Stability in the estimates

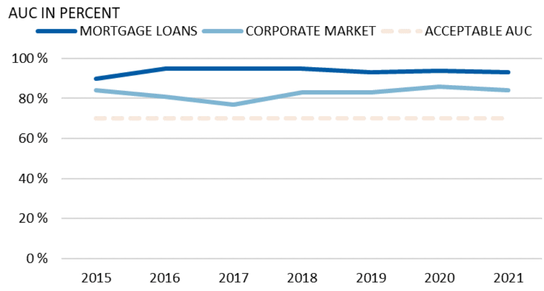
Every risk parameter is validated to establish their stability over time, independent of the economic situation. In validating the PD model, the validation is conducted by analysing migration over a twelve-month period, and over time.

Comparison of risk parameters and actual outcome

In this paragraph, an outtake of the validation results for the PD, EAD and LGD models for the IRB portfolio in SpareBank 1 SR-Bank is presented.

PD models

Figure 12: Discrimination power, PD models



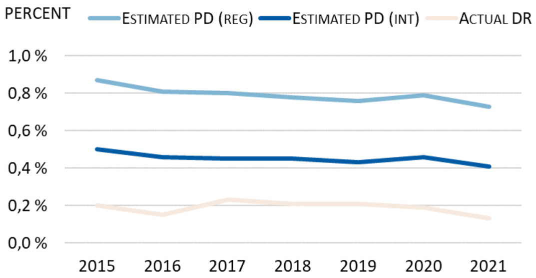
The PD model on mortgage loans has a very high and stable ranking ability, which means that the model can rank the customers from the ones with highest to lowest actual probability of default. Validation on different segments also demonstrates its good ranking ability. The PD model for corporate customers has a high and stable ranking ability for the portfolio, while its ranking ability may be somewhat lower for validation in different sub-portfolios. This applies to larger customers and certain types of sector. Therefore specific PD models have been developed for these segments.

In 2014, the Norwegian FSA passed a new methodology for regulatory calculation of probability of default (PD) and loss given default (LGD) for mortgage loans. The new methodology for calculating the probability of default includes four periods of a normal business cycle and one period with an economic downturn. The level of default in the economic downturn must be fixed ad 3.5 per cent each year, regardless of the underlying portfolio quality and loss history. Furthermore, a safety margin is attributed to the PD estimates to prevent a level of PD below 0.2 per cent. SpareBank 1 SR-Bank has taken the regulation into account and implemented new, regulatory levels for PD and LGD.

However, SpareBank 1 SR-Bank finds that the new methodology for regulatory calculation of probability of default in an economic downturn significantly overestimates the risk in the underlying portfolio. This entails an overestimation of the PD through a full loss cycle. Internally, SpareBank 1 SR-Bank uses lower PD estimates that reflect the underlying risk in the portfolio to a greater degree. Using the internal estimates provides more risk sensitive risk weightings and better encourages sound risk management.

Probability of default (PD) should predict a long-term outcome through a full loss cycle. This means that the PD estimates must be relatively stable over time, as well as through a business cycle. The figure below shows the average estimated unweighted probability of default (PD), both internally and regulatory, compared with the average actual default rate in the years 2015-2021.

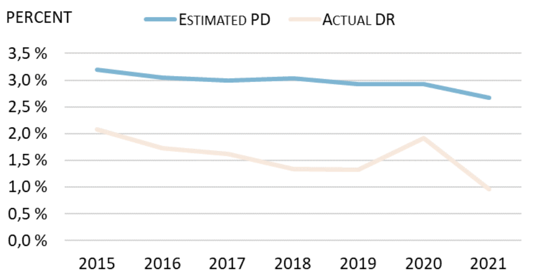
Figure 13: Comparison of unweighted estimated PD with actual DR – mortgage loans (regulatory and internal)



Actual default (DR) has been stably low. The default is significantly lower than both internally and regulatory estimated default (PD) throughout the period. Regulatory, there is - in accordance with current regulations - a significant overestimation of the default level.

For corporations, the internal and regulatory calibrations are consistent with each other. The figure below shows the average unweighted estimated and actual default rate for the corporate portfolio.

Figure 14: Comparison of unweighted estimated PD and actual DR – corporate market



As the figure shows, estimated probability of default (PD) is significantly higher than actual default (DR) over the entire period. The PD-level is in line with the desired cyclical properties of the model.

Every customer with a credit exposure in SpareBank 1 SR-Bank is risk classified at least annually by updating accounting or tax assessment data. Furthermore, the customers are scored monthly, based on information on internal and external behaviour. The figures below show the annual migration of the retail and corporate customers, respectively. Migration is the proportion of customers who change default class during a twelve-month period.

Figure 15: Annual migration – mortgage loans

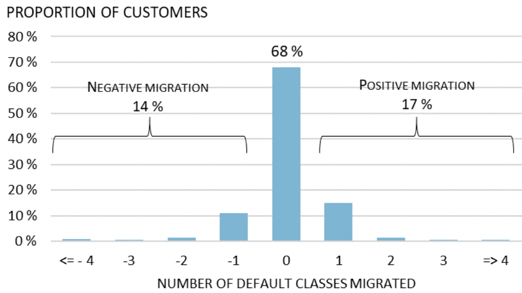
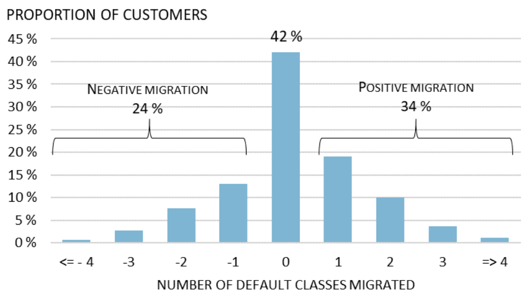


Figure 16: Annual migration – corporate market

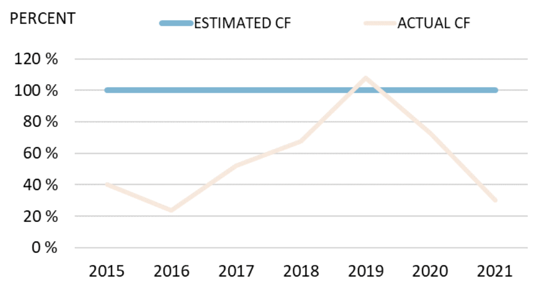


Stability in the PD estimates is an indicator of a model's cyclical properties. The proportion of stable customers in 2021 was 68 per cent for mortgage loans and 42 per cent for the corporate market.

EAD models

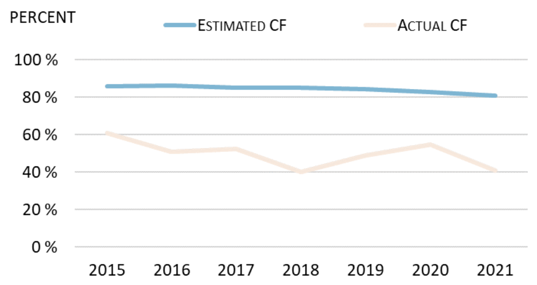
Validation is made as to whether the model estimates can predict the utilisation of limits (CF) by a serious downturn. This means that there should be a sufficient margin between estimated and observed values in normal economic conditions. The graphs below show comparisons of conversion factor for the period 2015-2021.

Figure 17: Comparison of estimated and actual conversion factor (CF) – mortgage loans (limit loans)



For all the mortgage loan customers with credit loans, the conversion factor is a fixed parameter. The average actual conversion factor is 59 per cent during the period, and significantly lower than the set parameter of 100 per cent.

Figure 18: Comparison of estimated and actual conversion factor (CF) – corporate market



A separate model has been developed for the corporate market that estimates conversion factors based on risk classification and type of commitment. Average estimated conversion factor is 84 per cent, and higher than average actual conversion factor at 50 per cent.

LGD models

Regulatory calculation of loss given default (LGD) for mortgage loans entails a minimum LGD of 20 per cent, regardless of the underlying quality in the portfolio or historic losses. Internally, SpareBank 1 SR-Bank's own estimates for degree of loss based on internal data with empirical evidence and that is representative of the bank's portfolio are used.

For the corporate market, the internal and regulatory estimates for LGD are consistent with each other. The figures below show the comparison of estimated and actual loss rate on defaulted customers, both in the retail and corporate markets. The loss rate is measured in per cent and weighted relative to the exposure (EAD) on the defaulted commitments.

Validation of LGD for 2021 was still being prepared at the time of publication. The figures below therefore show the estimated and actual loss ratio for the period 2015-2020.

Figure 19: Comparison of estimated and actual weighted LGD for defaulted loans – mortgage loans (internal and regulatory)

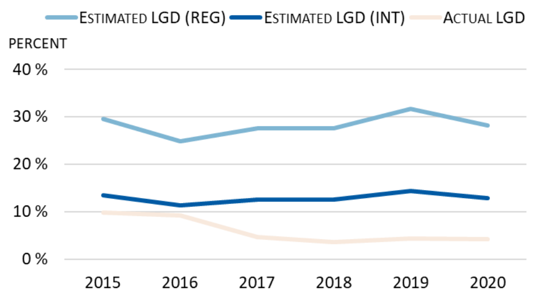
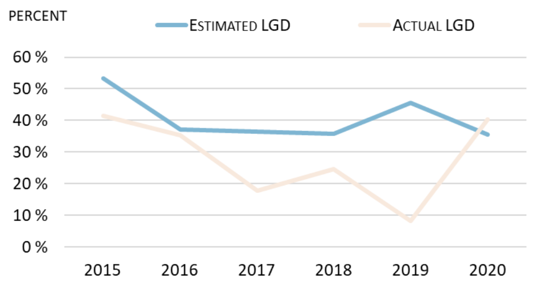


Figure 20: Comparison of estimated an actual weighted LGD for defaulted loans – corporate market



The figures show that actual loss rate is lower than estimated loss rate, for both mortgage loans and the corporate market. Few defaults mean the loss rate of a single customer has the potential to have a large impact on the actual loss rate. This is especially seen in cases with corporate customers.

Default and impairment

SpareBank 1 SR-Bank continuously evaluates the quality of the credit portfolio, both on an overall level and on a customer level. Customers in default in the form of an overdraft or arrears are monitored and followed up at an early stage. This ensures that any necessary measures are implemented quickly.

Close follow-up of customers and preventive work are important tools for maintaining a good risk profile in the Group's loan portfolio to reduce future write-downs.

Under IFRS 9, the Group's loans and financial liabilities are grouped into three groups; Stage 1, Stage 2, and Stage 3, where Stage 3 is used for loans with a significant increase in credit risk since being granted and have objective evidence of a loss on the balance sheet date. For these loans and financial liabilities, provision shall be made for the expected loss over the lifetime.

Table 7: Expected credit loss on segments and stages (amounts in NOK million)

2021 (According to IFRS 9)			
Rogaland	94	172	654
Agder	20	46	48
Vestland	33	68	265
Oslo/Viken	28	48	90
Øvrige	18	17	120
Sum	**193**	**351**	**1.177**

2020 (According to IFRS 9)	**Stage 1**	**Stage 2**	**Stage 3**
Rogaland	153	172	1.196
Agder	30	45	58
Vestland	51	64	202
Oslo/Viken	37	33	9
Øvrige	27	43	95
Sum	**298**	**357**	**1.560**

The total expected credit loss at the end of 2021 was NOK 1,721 million, of which NOK 920 million in Rogaland. Shipping and other transport was the industry with the most expected credit loss in Stage 3 with NOK 691 million. For a complete overview per industry see attachment (excel) sheet tab 12.

MARKET RISK

Market risk is a collective term that comprises the risk of loss due to changes in market prices. Securities risk, currency risk, interest rate risk, spread risk, risk associated with own holdings and/or use of equity in syndicates, as well as guarantees for the full subscription of offerings are included in market risk.

About market risk

Risk strategy

Market risk in SpareBank 1 SR-Bank primarily relates to the group's investments in securities, including equities and bonds. Furthermore, the group is somewhat exposed to market risk through trading activities in interest rate and currency markets, as well as from activities that underpin ordinary funding and lending activities. The group's exposure to market risk is deemed moderate.

The risk strategy and the associated specification of the necessary risk limits, reporting procedures and authorities must be reviewed and approved by the group's board at least once a year.

Authorities, guidelines and routines

The limits set by the board relating to SpareBank 1 SR-Bank Markets and Treasury are delegated by the chief executive to named people.

SpareBank 1 SR-Bank Markets' guidelines and routines are well described in Guiden, the bank's system for process and routine descriptions. Guiden continuously updates the processing steps and routines so that the last valid version is always available. Compliance with the routines by the people involved in managing and controlling market risk is satisfactory.

The group's market risk is measured and monitored based on fixed limits. The responsibility for continuous position reconciliation and measurement of the group's market risk exposure lies with the middle office in SpareBank 1 SR-Bank Markets. The risk manager for market and funding risk is responsible for maintaining continuous control of risk measurements and independent risk reporting, both internally and externally.

Market risk, including spread risk for bonds and securities

Price risk is the risk of losses that arise following changes in the value of the group’s commercial paper, bonds and equity instruments. The risk associated with a fall in value for the bond portfolios, including both systematic and unsystematic, is quantified by calculations based on the Financial Supervisory Authority of Norway's stress test model for insurance companies. The method is generally based on Solvency II (the QIS5 specifications).

The liquidity portfolio's total holding amounts to NOK 55,9 billion[6]. The portfolio in SpareBank 1 SR-Bank Markets amounts to NOK 0.2 billion[7]. The table below provides an overview of exposure by asset class.

Table 8: Fair value of the bond portfolio (NOK million)

Sub-portfolio	4th Qtr. 2021	3rd Qtr. 2021	2nd Qtr. 2021	1st Qtr. 2021
Treasury	**55.886**	**52.677**	**50.757**	**48.341**
Norwegian government	1.024	0	0	4.230
Foreign guarantees	30.947	28.383	27.336	24.262
OMF/Covered Bond	23.915	24.294	23.421	19.849
SR-Bank Markets	**162**	**210**	**265**	**298**
Norwegian bank/finance	22	35	52	63
Industry/other	140	175	213	235

Risk-adjusted capital associated with other market risk is measured and followed-up in accordance with the Value-at-Risk (VaR) principle. The VaR model covers the group's interest rate and currency risk, as well as the securities risk associated with the

[6] Of which NOK 8.3 billion is measured at amortized cost and is therefore not exposed to market risk.

[7] Includes hybrid capital (fund bonds) classified as equity

group's investments in equities, units and other equity investments.

Market risk is reported under credit and counterparty risk in accordance with the standard method.

Bond portfolio

Risk profile and portfolio performance

The group has two different portfolios consisting of bonds and commercial paper – the liquidity portfolio and trading portfolio, respectively. The respective portfolios are governed by separate management mandates.

Liquidity portfolio (managed by Treasury)

The liquidity portfolio consists of interest-bearing securities that either satisfies the requirements for depositing with Norges Bank, the LCR regulations or uncommitted credit facilities, as well as exposure on companies within the SpareBank 1 alliance. The size of the portfolio will always depend on the group's balance sheet and thereby the need for liquid assets. At the end of 2021, the value of the combined liquidity portfolio totals NOK 55.9 billion.

In accordance with the group's internal guidelines, securities that do not satisfy internal requirements entail a credit risk governed by special processing rules.

Trading portfolio (managed by SpareBank 1 SR-Bank Markets)

The trading portfolio consists of financially oriented investments in interest-bearing securities[8]. The current limit for such investments is NOK 1 billion. All investments in the trading portfolio that do not satisfy the criteria for uncommitted credit lines stipulated by the board of directors shall be subject to ordinary credit processing. At the end of 2021 the trading portfolio includes investments in 16 companies valued at NOK 162 million.

The trading portfolio does not have any structured bonds (CDOs, etc.) or other types of financial instruments.

The tables below provide a summary of SpareBank 1 SR-Bank's exposure to bonds in the different portfolios:

Table 9: Securities exposure, bonds and securities

Risk classes for bonds and commercial paper – total

Risk category	Rating	Market value NOK million	Total %
Very low risk	AAA, AA+, AA and AA-	55.886	99,2 %
Low risk	A+, A and A-	0	0,0 %
Moderate risk	BBB+, BBB and BBB-	289	0,5 %
High risk	BB+, BB and BB-	88	0,2 %
Very high risk	B+ and lower	61	0,1 %
Total		**39,987**	**100,0 %**

Risk classes – Treasury

Risk category	Rating	Market value NOK million	Treasury %
Very low risk	AAA, AA+, AA and AA-	55.886	99,5 %
Low risk	A+, A and A-	0	0,0 %
Moderate risk	BBB+, BBB and BBB-	275	0,5 %
High risk	BB+, BB and BB-	0	0 %
Very high risk	B+ and lower	0	0 %
Total		**56.161**	**100,0 %**

Risk classes – SpareBank 1 SR-Bank Markets

Risk category	Rating	Market value NOK mill	Trading %
Very low risk	AAA, AA+, AA and AA-	0	0 %
Low risk	A+, A and A-	0	0 %
Moderate risk	BBB+, BBB and BBB-	13	8,2 %
High risk	BB+, BB and BB-	88	54,0 %
Very high risk	B+ and lower	61	37,9 %
Total		**162**	**100,0 %**

[8] Includes hybrid capital (mutual fund bonds), classified as equity

Interest rate risk

Interest rate risk arises because the group's assets and liabilities can be subject to different fixed rate periods. Interest rate instrument trading must always comply with the adopted limits and authorities. The group's limits define quantitative targets for the maximum potential loss. The commercial risk is quantified and monitored continuously.

The group's general limits for interest rate risk define the maximum loss from a 1 percentage point change in interest rates. The maximum loss following a 1 percentage change in interest rates totals NOK 85 million with NOK 35 million of the total balance in SpareBank 1 SR-Bank Markets and NOK 50 million of the total balance in Treasury.

The total currency position cannot exceed the interest rate risk limit in NOK.

Table 10: Sub-limits within the different maturity bonds

Maturity bond	Limit SR-Bank Markets	Treasury limit
0 – 3 months	NOK 20 million	NOK 50 million
3 – 6 months	NOK 20 million	NOK 50 million
6 – 9 months	NOK 10 million	NOK 50 million
9 months – 1 year	NOK 10 million	NOK 50 million
1 year – 18 months	NOK 10 million	NOK 20 million
18 – 24 months	NOK 15 million	NOK 15 million
Each year (1-10)	NOK 30 million	NOK 15 million
10 years or more	NOK 30 million	NOK 10 million

The table below shows the total interest rate risk by the end of the last four quarters.

Table 11: Effect on earnings of a positive parallel shift in the yield curve of one percentage point (NOK million)

Interest rate risk	0-6 months	6-12 months	1-5 years	> 5 years	Total
4th Qtr. 2021	4	0	0	0	**4**
3rd Qtr. 2021	-7	0	1	0	**-6**
2nd Qtr. 2021	-22	-0	1	0	**-21**
1st Qtr. 2021	-16	-0	1	-0	**-15**

Foreign exchange risk

Currency rate risk is the risk of loss due to fluctuations in foreign exchange rates. The group measures currency risk of net positions in the different currencies in which the group is exposed. The group has prepared limits for the net exposure to each individual currency, and limits for the aggregate net currency exposure. The overnight price risk for spot trading in foreign currencies shall not exceed NOK 100 million for each individual currency, and NOK 225 million in aggregate.

The table below shows the net foreign currency exposure including financial derivatives at the end of the last four quarters.

Table 12: Foreign currency exposure including financial derivatives (NOK million)

Currency	4th Qtr. 2021	3rd Qtr. 2021	2nd Qtr. 2021	1st Qtr. 2021
EUR	30	42	40	25
USD	35	8	4	13
CHF	1	0	-0	2
GBP	0	0	1	1
SEK	-4	0	1	2
Other	12	17	19	15

Securities risk, shares[9]

Shares, units and other equity interests are classified within the categories of fair value and available for sale. Securities that can be measured reliably and are reported internally at fair value are classified as fair value through profit and loss. Other shares are classified as available for sale.

The table below provides a summary of the group's shareholdings at the end of the last four quarters.

Table 13: The group's share portfolio at fair value at the end of the year (NOK million)

Balance sheet classification	4th Qtr. 2021	3rd Qtr. 2021	2nd Qtr. 2021	1st Qtr. 2021
Shares, units etc.	797	753	827	894

[9] Does not include hybrid capital (mutual fund bonds) classified as equity

OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events[10].

Management of operational risk

SpareBank 1 SR-Bank aims to have a good balance between trust and control that ensures efficiency, while not exposing the Group to unnecessary operational risk. This is to be achieved through a good risk culture in the organisation, continuous learning from undesired incidents and the development of leading methods for identifying and quantifying risk.

Risk strategy and limits on operational risk exposure are set annually and approved by the board. The individual managers are responsible of ensuring that the unit they lead is subject to adequate management and control, and that operational risk is managed in accordance with the strategy and exposure limits defined for SpareBank 1 SR-Bank. The Risk Management Department is responsible for supporting and challenging the risk owners, and for ensuring that the group has a good framework for the identification, reporting and follow-up of operational risk.

Measuring operational risk

SpareBank 1 SR-Bank calculates and maintains regulatory capital for operational risk according to the standardized approach. This method is considered to give an insufficient indication of actual exposure to operational risk as it is solely based on historical revenues and does not consider company-specific factors and established controls. Therefore, in order to gain insight into what drives operational risk in the Group, separate operational risk surveys are carried out in which process owners and professional experts are involved to identify potential risks with associated probabilities and consequences.

The Group has devoted considerable effort to developing advanced methods for identifying and assessing operational risk. In recent years, regular mapping and updating of the risk exposure has identified new operational risks with considerable potential for losses. At the same time, targeted risk mitigation measures have been implemented and kept the overall potential loss at a stable level. This has been achieved through better control measures in combination with insurance schemes.

Development in operational risk

The pace of change in the industry has been increasing for several years, which entails the risk that more and more frequent changes may introduce unintended operational risks. The Group has focused on the rate of change as a significant risk driver and has professionalized its routines and developed tailor-made system-support to record, assess and approve all significant changes in products, processes and systems. More than 100 changes have undergone standardized risk assessment and approval during 2021. Such proactive risk management is considered a key measure to avoid the Group being exposed to unintended new risks through individual or continuous weaknesses in products, systems and processes.

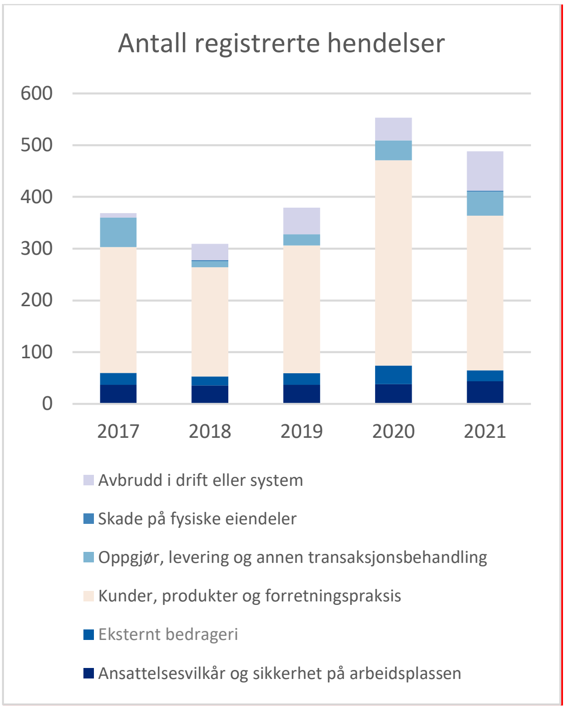
Undesired incidents

Recording and learning from undesired incidents is considered an important tool for capturing and realizing potential for risk reduction. For several years, the Group has focused on building culture and system support for incident reporting. 490 unwanted incidents were recorded in 2021, several of which have resulted in measures to reduce the risk of similar and more serious incidents in the future.

The diagram below shows the number of recorded incidents in the years 2016 to 2021. The total loss from recorded undesirable incidents in 2021 amounted to NOK 440.000 compared to NOK 12.6 million in 2020

[10] Legal risk is included in operational risk, but not strategic risk and reputation risk, which are assessed separately.

Figure 21: Registered, undesired incidents by Basel categories



LIQUIDITY RISK

Liquidity risk is the risk that the group is unable to refinance its debt or is unable to finance an increase in assets.

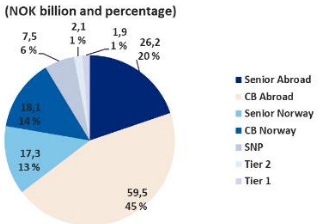
About liquidity risk

The bank's framework for managing liquidity risk shall reflect the bank's risk profile. Liquidity risk shall be low.

Management and measurement of liquidity risk

Liquidity risk is managed and measured by means of several measurement methods, as no method alone can be used to quantity this type of risk. The methods include limits for the maximum refunding need for various maturities, key balance sheet figures, survivability targets in a normal situation, assuming the capital markets are closed and the short-term liquidity measure LCR. Furthermore, internal stress tests are conducted to determine the bank's ability to survive under various scenarios, including a serious bank or market specific crisis. The results of the stress tests are included in the information on which the group's liquidity strategy and recovery plan for a liquidity crisis are based.

Figure 22: Composition of the group's securities borrowing as of 31 December 2021 (NOK billion and percent)



The liquidity reserve is NOK 57.9 billion, and the group has an additional NOK 22.7 billion representing mortgage loans ready to be utilised for covered bond funding. The liquidity situation for SpareBank 1 SR-Bank is satisfactory.

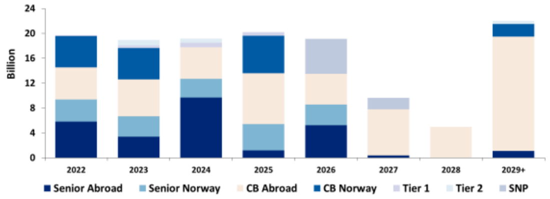
The liquidity buffer indicates a survival period of 37 months at the end of 2021 without access to external funding. During the next twelve months, debt corresponding to NOK 20.4 billion will be refinanced.

Deposits from customers is a central source of funding. For the group as a whole, the volume of deposits increased by NOK 8.4 billion (16.5 per cent) to 137.6 billion in 2021. The deposit coverage ratio is 59.8 per cent in 2021 compared to 53.9 per cent in 2020.

SR-Boligkreditt AS is a wholly owned subsidiary, established in the second quarter of 2015. The aim of the company is to buy mortgages from SpareBank 1 SR-Bank, which are financed by issuing covered bonds. Through SR-Boligkreditt AS, SpareBank 1 SR-Bank can diversify and optimise its funding. Mortgage loans transferred to SR-Boligkreditt AS amounted to NOK 89.6 billion by the end of 2021.

The figure below illustrates the maturity structure for the funding portfolio at the end of 2021.

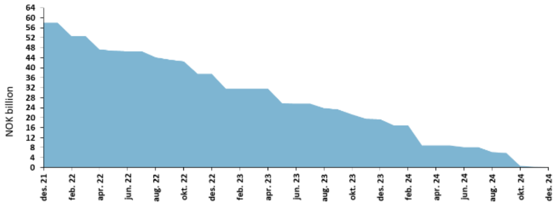
Figure 23: The funding portfolio's maturity structure as of 31 December 2021



The average remaining term to maturity in the portfolio of senior bond funding was 4.1 years[11] at the end of 2021.

A sensitivity analysis that measures the group's ability to survive in the event of closed capital markets is prepared monthly. The primary objective of the analysis is to measure whether the funding risk is in accordance with the definition of targets for liquidity management, which specify that SpareBank 1 SR-Bank must be able to survive for a minimum twelve months without external access to liquidity in a normal situation. The analysis is based on different scenarios. In the basis scenario, the growth in net funding needs is set at zero, i.e. the relationship between deposits and loans are kept constant.

Figure 24: Sensitivity analysis of the funding risk – basis scenario



As the basis scenario assumes that access to external funding is unavailable, new lending can only be funded by instalments from and the maturity of the existing loan portfolios. In such a situation, the group's liquidity buffer ensures the ability to survive until January 2025. The liquidity buffer consists of cash and very secure interest-bearing securities. The group's liquidity target, LCR (liquidity coverage ratio), was 168 per cent at the end of 2021.

[11] Based on «first call»

OWNER RISK

Owner risk is the risk that SpareBank 1 SR-Bank will incur a negative result from stakes in strategically owned companies and/or need to inject fresh capital into these companies. Owned companies are defined as companies in which SpareBank 1 SR-Bank has a significant stake and influence.

Management of ownership risk

SpareBank 1 SR-Bank heavily focuses on management and control in companies in which the bank has full or partial ownership. In companies that are part-owned, either through direct ownership by SpareBank 1 SR-Bank or indirectly through ownership of 19.5 per cent of SpareBank 1 Gruppen, SpareBank 1 SR-Bank, as the largest bank in the alliance, is represented as a board member in all companies of significant importance.

All follow-up of ownership interests is performed under the group's chief financial officer. All reporting from the individual companies and questions regarding capital increases etc. are reported here. A good supply of information is assured through active participation in the board of directors of several the part-owned companies, which safeguards SpareBank 1 SR-Bank's ownership interests. In cases of importance to SpareBank 1 SR-Bank's other operations, the individual board chairman/member will submit the matter for a plenary discussion by the group's executive management team.

The group's board stipulates risk limits and the allocation of equity to the individual companies annually. This is based on a framework for the assessment of risk.

About ownership risk

The ownership risk varies from company to company, depending on the company's operations and the inherent risk, as well as SpareBank 1 SR-Bank's stake. The figure below shows the Bank's wholly owned and partly owned companies as of 31 December 2021.

Figure 25: Wholly and partly owned companies as of 31 December 2021

BUSINESS RISK

Business risk is the risk of unexpected fluctuations in incomes and costs resulting from changes in external circumstances, such as the market situation or government regulation.

The group has developed a well-diversified income base over a long period of time, and this means that any reduction in the individual product groups or customer segments will not have significant consequences over time.

Over time, the group has developed cost-effective operations in combination with a continuous development of competence and expansion of the operations regarding the range of products and geography. SpareBank 1 SR-Bank has systematically focused on the value chain philosophy and development of products and services for several years.

REPUTATION RISK

Reputation risk is the risk of a failure in earnings and access to capital due to a lack of trust and damage to reputation in the market, i.e. in relation to customers, counterparties, stock markets and authorities.

The group has established an information department that is represented in the group's executive management team. Dedicated employees are responsible for handling all communications in social media, and information management is included in the group's contingency plan, which is distributed to all employees.

SpareBank 1 SR-Bank has also implemented an internal process for identifying and evaluating the group's overall reputation risk situation. A full review and survey of the reputation risks to which the group is exposed are conducted regularly and at least semi-annually. Changes in the risk situation are also registered.

Reputation risk is identified and sorted according to:

- Direct management cost (firefighting)
- Impact on departure of existing customers
- Impact on influx of new customers
- Potential for the Group's concessions may come under consideration and thus indirectly affect market value and financing capacity
- If certain events would result in revealing attitudes and actions that deviate significantly from the Group communicated values

The group continuously monitors its reputation, both through day-to-day media monitoring and evaluation, as well as continuously monitoring discussions in different social channels. The continuous day-to-day evaluations are carried out as objectively as possible. Members of the group's executive management team and other key personnel receive daily media reports.

STRATEGIC RISK

Strategic risk is the risk of loss due to failed strategic decisions.

SpareBank 1 SR-Bank annually conducts a strategy process that involves the board of directors, key personnel, departments and subsidiaries. The result of this process is a strategic presentation of goals for the following three years, with an associated business plan and plan of action. The business plan clearly shows the priorities the group has made for the period based on scenarios and the competition and market situation. The business plan and plan of action are more detailed for the next year.

The group’s executive management team conducts monthly and four-monthly evaluations of the group’s achievements and strategic direction. The evaluation also assesses relevant new initiatives and measures that must be implemented based on changes in assumptions or the market situation. Strategic work is therefore flexible in its approach and can safeguard both short-term and long-term goals.

CLIMATE RISK

Climate risk is the risk of financial losses and financial instability as a result of physical climate change and society’s response to it.

Climate risk is an integral part of the group’s risk management processes and SpareBank 1 SR-Bank identifies and assesses climate risks and opportunities that can affect customers, business areas and operations at various levels. The group conducts annual stress tests and financial simulations on its loan portfolio. SpareBank 1 SR-Bank’s greatest exposure to climate risk is in the corporate market portfolio, including agriculture, so climate managing the risk in this area has been made a priority. The group’s corporate market divisions have since 2019 used a separate risk assessment module for sustainability that is integrated into the credit process for all exposures over NOK 50 million. In 2021, SpareBank 1 SR-Bank started analysing CO2 emissions based on the methodology of the Partnership for Carbon Accounting Financials (PCAF).

COMPLIANCE RISK

Compliance risk is the risk that the group incurs public sanctions/penalties or financial loss due to failure to comply with legislation and regulations.

The compliance function at SpareBank 1 SR-Bank is an independent function that ensures that the laws, regulations, standards and recommendations that regulate our operations, and are laid down by government agencies or other institutions or associations, are implemented and complied with.

Compliance policy

The group's compliance policy is adopted by the board and describes the main principles for responsibility and organisation.

The group stresses the importance of good processes to ensure compliance with the current laws and regulations. Effective tools for achieving this include:

- Clear values that are clearly communicated and understood throughout the organisation.
- A process that detects, communicates, and implements changes in legislation and regulations.
- A process to monitor and report compliance with legislation and regulations.

Management of compliance risk

SpareBank 1 SR-Bank is managed through the compliance framework as set out in the Bank's compliance policy, which ensures that the Group does not incur public sanctions/fines or financial losses due to non-implementation and compliance with laws and regulations. The Group's compliance policy is adopted by the Board and describes the main principles of responsibility and organisation.

SpareBank 1 SR-Bank is committed to having good processes to ensure compliance with applicable laws and regulations. Focus areas are ongoing follow-up of compliance with applicable regulations and ensuring that the Group has the best adaptation to future regulatory changes.

The group's compliance function is performed by the Compliance Department, which is organised independently of the business units. The department bears overall responsibility for the framework, follow-up and reporting on compliance. Subsidiaries and the investment firm have designated compliance managers when this is required. The designated compliance manager for the group’s investment firm is responsible for ensuring that the bank’s activities relating to the provision of investment services always comply with the regulations for securities trading.

The group's managers have an operational responsibility for practical implementation and compliance with laws and regulations. All employees are responsible for ensuring that they comply and understand the laws and regulations on a day-to-day basis.

ABBREVIATIONS AND DEFINITIONS

An explanation of abbreviations used in Pillar 3 is given in the table below.

Abbreviation	Explanation
IRB	Internal Rating Based
PD	Probability of Default
DR	Default Rate
EAD	Exposure at Default
CF	Conversion Factor (proportion of unutilised credit facility which is expected to have been drawn upon default)
LGD	Loss Given Default
RM	Retail market
CM	Corporate Market

APPENDIX

Please see excel-sheet for attachments.