RISK AND CAPITAL MANAGEMENT

Disclosure of financial information according to Pillar 3 2023

SpareBank SR-BANK

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THE CRO'S SUMMARY OF THE YEAR


Frode Bø, CRO

The geopolitical unrest has continued to escalate throughout 2023, with no immediate signs of an end to the invasion war in Ukraine. There is also concern that the conflict between Hamas and Israel could spread to other countries in the Middle East. At the same time, China and the USA are in intense competition to develop the most advanced and sought-after products in artificial intelligence (AI), with both countries aiming for dominance in the digital development going forward. The USA faces a crucial presidential election, which could impact the global security situation.

These conditions contribute to an increase in geopolitical risk, with a higher likelihood of escalation of existing conflicts. Considering this, SpareBank 1 SR-Bank in 2023 has strongly focused on scenario analyses to better understand the depth and breadth of various situations where there is great uncertainty. The goal of the work is to implement risk-reducing measures as early as possible before the risk arises.

Based on various scenarios and potential outcomes, SpareBank 1 SR-Bank has conducted several financial and operational stress tests. The financial stress tests are designed to identify potential financial weaknesses early, ensure the implementation of risk-reducing measures, and prevent the group from violating regulatory requirements given extremely serious outcomes as much as possible. Operational stress tests aim to ensure stable and sound operation of SpareBank 1 SR-Bank under a variety of critical potential events that could be triggered by geopolitical uncertainty.

The bank's crisis management regulations (BRRD) lay the foundation for and require preparedness and preventive measures. The group has worked systematically with this topic throughout the year and has prepared a guide that describes the operational process when using the crisis management measure of internal capitalization.

Given the uncertain macroeconomic picture, SpareBank 1 SR-Bank has close monitoring of credit exposures. Beyond ongoing monitoring of the portfolio through various portfolio management and early warning systems, there has been a lot of focus on the consequences of increased geopolitical unrest in the work of the current year. The corporate market divisions have conducted several stress tests at the customer level to identify customers who need close follow-up and contribute to the customers receiving good financial advice in challenging times.

A specific review of the corporate market portfolio has been carried out to identify commitments that could potentially face liquidity challenges because of a more challenging macroeconomic picture. In this context, there has also been a significant focus on ongoing monitoring of the development in applications for deferral of payments both in the corporate market and the consumer market. Over many years, systematic work has been carried out in the corporate market divisions, which is reflected in a generally positive development in portfolio quality, concentration risk, risk pricing and profitability. The development of defaults is closely monitored, and there has been some increased default within the corporate market, especially within the SMB segment. In the consumer market, defaults are still at historically low levels. The risk of money laundering has received a more prominent place in credit assessments, and the internal requirements for thorough AML assessments in the ongoing lending are tightened. There are also tightened requirements in lending to ESG assessments, well aided by a more sophisticated framework for identifying this type of risk.

The operational risk picture in 2023 has been characterized by geopolitical unrest, with war in Ukraine and in Gaza as drivers for an elevated threat picture regarding cyber risk. However, the attack methods used by threat actors are techniques that SpareBank 1 SR-Bank has worked systematically to prevent over several years. The group is therefore considered to be well prepared for, and equipped for, any attacks. Cyber risk is still expected to dominate the group's operational risk picture in the coming years and requires continuous work with relevant measures in the group and towards central suppliers. Upcoming regulations from the EU in the ICT area, DORA and NIS2, are expected to strengthen the resilience in the financial industry and with associated actors.

A clear increase in fraud cases is observed and experienced, and the anti-fraud area has experienced a high pressure of cases. The work with anti-fraud has been intensified during 2023.

The planned merger with SpareBank 1 Sørøst-Norge will affect the group's operational activities and associated operational risk picture. In the time leading up to the merger, thorough risk assessments and preparations will be made to ensure a good execution of the merger itself.

Sustainability, and especially climate risk, is still a high priority. In this regard, the group has recently adopted the first climate adaptation plans, and emission reduction targets have been set for four of the most important industries in the loan portfolio; shipping, oil/gas, agriculture, and commercial buildings. The Framework for Sustainable Financing was updated in 2023 by including the taxonomy rules for green buildings built after 2020. This framework, which constitutes the rules for defining loans as either green or sustainability-linked, is a central tool in connection with the group's objectives for green and sustainable financing towards 2030.

The group uses a common SpareBank 1 risk framework for assessing sustainability risk. The ESG framework is used in connection with credit approval and renewal of corporate customers with a consolidated exposure over 10 million kroner. It contains evaluation criteria for several specific industries, and it includes inherent risk per industry. The ESG scoring is based on questions within the four sub-themes physical climate risk (E), transition risk (E), social conditions (S) and ownership and corporate governance (G) and gives a sub-score per sub-theme and a total score. If a customer gets a particularly low ESG score, there is a requirement that the customer advisor should prepare an action plan for improvement together with the customer. The aim of the scoring is to assess the customer's sustainability risk, as well as to assist the customer advisor in the dialogue with the customer about sustainability. The group's overall ambition for sustainability is to be the customer's ally in the transition. Therefore, integrating sustainability into customer dialogue in a good way is an important success criterion. The experiences so far are good, and the scoring gives a good ranking of the customers.

Data capture, quality assurance, storage, and further dissemination of ESG risk data for internal purposes and for external reporting will be a major challenge that will be solved in an alliance project in collaboration with SpareBank 1 Utvikling. The project, which started in the fall of 2022, has developed into a department in SpareBank 1 Utvikling that is responsible for ESG data. SpareBank 1 SR-Bank contributes with the rental of resources to this department.

As a large bank in Norway, the group has extensive disclosure obligations within the ESG area. For 2023, this means a significant expansion of the pillar 3 reporting requirement compared to the more limited reporting obligation following the EU taxonomy for green financing. SpareBank 1 SR-Bank carries out its first reporting of both pillar 3 ESG and EU taxonomy for 2023.

There is a continuous development of internal control and operational risk management in the group. Operational risk management is an integrated part of all business and involves all employees. Facilitating good risk assessments and conducting training in this area is an important part of risk management's work. The group conducts regular measurements of the risk culture, the last of which was in 2023. The results show that there is a good risk culture, where values, frames and expectations are well known and adhered to, and with a high-risk awareness in the organization. This is reflected in the ongoing risk management in the group, with good compliance related to registration and handling of significant changes through the group's PoPS process (change in products, organization, processes, and systems), registration of unwanted events and improvement measures, and to capture and escalate potential risks, so that risk-reducing measures can be established. There is active work to facilitate and strengthen this independent risk management in the organization, where each manager and employee takes responsibility for and manages potential risks related to their tasks and areas of responsibility, supported by uniform methods, systems, and processes. At the same time, systematic work is being done in the second line of defence with mapping, monitoring, and management of the overall risk picture.

SpareBank 1 SR-Bank has established good processes to ensure compliance with applicable regulatory requirements and the group's guidelines. In 2023, particular attention has been paid to compliance with anti-money laundering and sanctions regulations, requirements for outsourcing and supplier follow-up, data protection regulations, MiFiDII and the EU's new directive on sustainability reporting (CSRD). Furthermore, the compliance function has participated in several projects and initiatives related to upcoming regulations and the use of new technology, including the DORA regulations and the implementation of AI technology in the group.

RISK STATEMENT FROM THE BOARD OF DIRECTORS

The Board of Directors of SpareBank 1 SR-Bank is continuously updated about the group's risk development through regular reports and established notification routines. Each year, the board evaluates and establishes the group's risk appetite, along with other relevant risk frameworks. These frameworks include, but are not limited to, credit, market, liquidity, and operational risk. The Board considers the group's risk management to be good and well adapted to the group's risk appetite and business strategy. During 2023, there have been no breaches of the overall adopted risk profile.

SpareBank 1 SR-Bank is a forward-looking relationship bank that is present in the communities where people and businesses meet. The group has offices spread from Bergen in the west to Oslo in the east and is an aggressive financial group with national distribution. As Norway's second-largest Norwegian-owned bank, the group contributes to economic growth, value creation, and profitability for customers, society, and our owners. The group's head office is in Stavanger, and including subsidiaries, SpareBank 1 SR-Bank has about 1,500 employees. At the end of 2023, SpareBank 1 SR-Bank had about 390,000 personal customers and around 34,000 business customers.

In June 2023, the Ministry of Finance decided that SpareBank 1 SR-Bank should be considered a systemically important institution. This will entail increased requirements for pure core capital coverage of 1.0 percentage points from 30.09.2024, as well as closer regulatory follow-up.

On October 26, 2023, the boards of SpareBank 1 SR-Bank ASA and SpareBank 1 Sørøst-Norge adopted a plan for merging and establishing SpareBank 1 Sør-Norge ASA. Subject to necessary permissions from the authorities, the date for the legal merger is set for October 1, 2024.

In October 2023, a successful issue of approximately 1 billion kroner was carried out. The issue was made to meet increased regulatory requirements, continue the bank's dividend policy, and contribute to further lending growth in 2024.

SR-Bank Markets was transferred to SpareBank 1 Markets AS with accounting effect from December 1, 2023. In connection with this transaction, SpareBank 1 SR-Bank ASA increased its ownership interest in SpareBank 1 Markets AS from 5.6 percent to 33.3 percent.

The Board annually determines the group's overall risk capacity and appetite in both normal business cycles and during severe economic downturns. This includes setting targets/frames for profitability, largest single loss, solidity, liquidity, credit quality, financial rating, and sustainability rating, among others. The group's actual and expected risk exposure, compared to the adopted risk appetite, is followed up quarterly by the risk committee and the board. Scenario analyses and stress tests are central tools in this work, so that the group is as well prepared as possible for severe economic downturns or other serious events.

Credit risk is managed through the framework for credit approval, commitment follow-up, and portfolio management. The group's credit strategy includes overarching credit strategic frameworks, designed to ensure a diversified portfolio and a satisfactory risk profile. The main focus in lending should be the customer's repayment capacity, and a weak or lacking repayment capacity should not be compensated by good security. The credit strategic frameworks set requirements and limitations related to the overall loss profile and portfolio quality. The group has a particular focus on concentration risk related to exposure to large single customers and single industries. To avoid unwanted concentration risk, the credit strategic frameworks set limitations related to exposure and risk profile at the portfolio level, as well as for different industries and single customers. These limitations come in addition to the frameworks that the rules for large engagements set. The credit professional guidelines set requirements that apply to all types of financing, except for engagements granted as part of the exercise of special credit security powers. In addition to the general credit professional guidelines, a set of more specific credit professional guidelines related to industries or segments that may involve a particular risk has been prepared.

The Board is responsible for the group's loans and credit approvals, but delegates within certain limits the credit powers to the CEO, who can further delegate these within his own powers. Emphasis should be placed on ensuring that customers' business is in accordance with applicable laws and regulations, and that the business has a long-term perspective. The group's sustainability policy is reflected in the general credit professional guidelines, including requirements that all financing must meet the group's guidelines related to environment, society, and corporate governance. The group also has guidelines that support the group's policy for anti-money laundering (AML). The group has IRB permission from the Financial Supervisory Authority and actively uses credit models for risk classification, risk pricing, capital calculations, and portfolio management.

Liquidity risk is managed through the group's overarching liquidity strategy which is reviewed and approved by the board at least annually. The liquidity management is based on conservative frameworks and reflects the group's moderate risk profile. It is the group's treasury department that is responsible for liquidity management, and the risk management department monitors and reports the utilization of frames according to the liquidity strategy. The group's loans are mainly financed with customer deposits and long-term securities debt. Liquidity risk is limited by distributing securities debt across different markets, sources of borrowing, instruments, and maturities.

Market risk is managed through the market risk strategy that defines the group's risk appetite. The strategy with accompanying specification of necessary risk frameworks, reporting lines, and powers is treated and approved by the board at least annually. Market risk in SpareBank 1 SR-Bank is primarily related to the group's long-term investments in securities. In addition, the group has a certain exposure to market risk from activities that support ordinary deposit and lending business. The group's market risk is measured and monitored based on conservative frameworks that are renewed and approved by the board at least annually. The size of the frameworks is determined based on stress tests and analyses of negative market movements. The group's exposure to market risk is moderate.

Operational risk is managed through the risk strategy that is annually determined by the board, as well as a separate policy for operational risk. The strategy contains the group's risk appetite, with frames for allowed risk exposure. The policy, which is also adopted by the board, provides guiding principles and requirements for identifying, assessing, managing, monitoring, and reporting operational risk, with associated allocation of roles and responsibilities. The group has a dynamic approach to managing operational risk and conducts regular analyses to uncover weaknesses and new or changed risks. Unwanted events that occur are registered and followed up systematically to extract learning effects and avoid repetition, and the board receives a quarterly report with an overview of registered events. Furthermore, all significant change initiatives go through a standardized risk assessment process to avoid introducing unwanted risk. Risk-reducing measures are considered and implemented continuously.

Climate risk is an integrated part of the group's risk management processes and SpareBank 1 SR-Bank identifies and assesses climate-related risks and opportunities that can affect customers, business areas, and operations at various levels. The group's loan portfolio undergoes annual stress tests and financial presentations. The largest climate risk exposure to SpareBank 1 SR-Bank lies in the corporate market portfolio including agriculture, so handling climate risk from this part of the business is prioritized. The group uses a common SpareBank 1 risk framework and scoring model for assessing sustainability risk (ESG score). The ESG framework is used in connection with credit approval and renewal of corporate customers with consolidated exposure over 10 million kroner. It contains evaluation criteria for several specific industries, and it includes inherent risk per industry.

Compliance risk is managed by practicing the group's framework for compliance as it appears from the group's policy for compliance. The framework should help ensure that the group does not incur public sanctions/fines or financial loss as a result of a lack of implementation and compliance with laws and regulations. The policy for compliance is adopted by the board and describes the main principles for responsibility and organization in connection with compliance with laws, regulations, internal guidelines, etc. The board has decided that the group should have a very low tolerance for compliance risk. This means that regulations should be interpreted with a conservative approach. SpareBank 1 SR-Bank is committed to having good processes to ensure compliance with applicable laws and regulations. Compliance should be an integrated part of management and decision-making processes. The group's strategies, policies, standards, and routines form the governing framework that should support that regulatory requirements and the group's self-defined requirements are complied with.

Key figures

Key figures	31.12.2023	31.12.2022
Return on equity	15,3 %	12,6 %
Rating	Aa3	A1
Common equity Tier 1 capital ratio	17,6 %	17,4 %
Leverage ratio	7,2 %	6,9 %
MREL (minimum requirement from 01.01.2024)	36,6 %	35,2 %
Deposit to loan ratio	54,8 %	58,5 %
LCR	207 %	176 %
NSFR	130 %	130 %
Impairment on loans retail market in % of lending	0,0 %	0,0 %
Impairment on loans corporate market in % of lending	-0,2 %	0,0 %
Share of the corporate market lending portfolio	39,9 %	39,4 %
Share of the retail lending portfolio	60,1 %	60,6 %
ESG (Position Green)	A	A

Stavanger, 7. March 2024

Dag Mejdell
(Chair of the Board)

Kate Henriksen

Trine Sæther Romuld

Jan Skogseth

Kjetil Skjæveland

Camilla AC Tepfers

Sally Lund-Antonsen

Kristian Kristensen

Benedicte Schilbred Fasmer
(Chief Executive Officer, CEO)

Frode Bø
(Executive vice president risk management, CRO)

1. ABOUT THIS REPORT

Risk and capital management in SpareBank 1 SR-Bank intend to create financial and strategic added value. This report contains information on risk management, risk measurement and capital adequacy.

Financial and strategic added value should be created 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

The Pillar 3 report, along with the associated Excel supplement, is designed to give the market insight into SpareBank 1 SR-Bank's risk and capital management practices. The report is prepared in accordance with the current capital adequacy regulations and meets the requirements for disclosing information about risk and capital management. The Pillar 3 report supplements the information found in the annual report, quarterly reports, and Factbook.

This report is updated annually. Information about capital adequacy and minimum requirements for eligible capital is updated quarterly in separate appendices. For information about the group's remuneration scheme, please refer to the annual report and the separate executive pay report.

To ensure that financial institutions assess and manage risk in an effective and good way and that they are solid and robust towards fluctuations and shocks in the economy, financial institutions are regulated by financial authorities, including requirements for capital adequacy. The capital adequacy regulations are based on three pillars:

Pillar 1: Quantitative minimum requirements for eligible capital and description of the calculation methods for risk-weighted volume and what counts as capital.

Pillar 2: Requirements for risk management and internal control, including requirements for internal processes for assessing risk exposure and capital needs (ICAAP). Under Pillar 2, supervisory authorities can require additional capital if they believe that other capital requirements do not adequately capture the underlying risk in an institution.

Pillar 3: Requirements for reporting and disclosure of financial information. Pillar 3 is designed to enable the market to assess a financial institution's risk and capital management.

The report has been reviewed by the Board of Directors of SpareBank 1 SR-Bank. This report is not subject to external audit.

2. 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.

2.1 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 because 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.

Reputational 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.

Model risk: the risk of loss, underestimation of capital needs and/or erroneous decisions because of errors in the development, implementation or application of models.

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.

2.2 The Internal Capital Adequacy Assessment Process (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. Furthermore, the policy shall 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 shall be documented and based on best international practices.
- The group shall 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.
- Risk and capital management shall support the group's strategic development and achievement of objectives while ensuring financial stability and sound management of assets.

- The group shall 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 risk appetite that provides a sufficient buffer in relation to the group's risk capability and ensure that no single events can seriously damage the group's financial position.
- The risk identification process must be implemented regularly, forward-looking 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 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. Measures that reduce probability shall be prioritized 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 based on risk-adjusted returns.
- The group must carry out comprehensive, periodic risk follow-up and reporting.
- The group shall, as far 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 1: 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 adopt the group's risk profile at least annually. SpareBank 1 SR-Bank defines its risk profile by calculating the group's risk capacity and then determining the group's risk appetite. 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 risk capacity 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 bear risk describes the maximum desired risk exposure from an earnings and loss perspective, given the defined risk capacity. The difference between risk capacity and risk appetite expresses the group's desired safety buffer.

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 this risk analysis. The strategy specifies acceptable levels of risk, and targets for risk-adjusted returns.

Financial projections

Various financial projections are made annually:

- Financial projection of expected financial development over the next five years.
- Financial projection of severe economic setbacks based on various scenarios, which include for example:
    - Climate
    - Political instability
    - Building of financial bubbles

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.

Risk reporting to the board

The table below shows the regular reports on risk and compliance to the board.

Table 1: Regular reports on risk and compliance

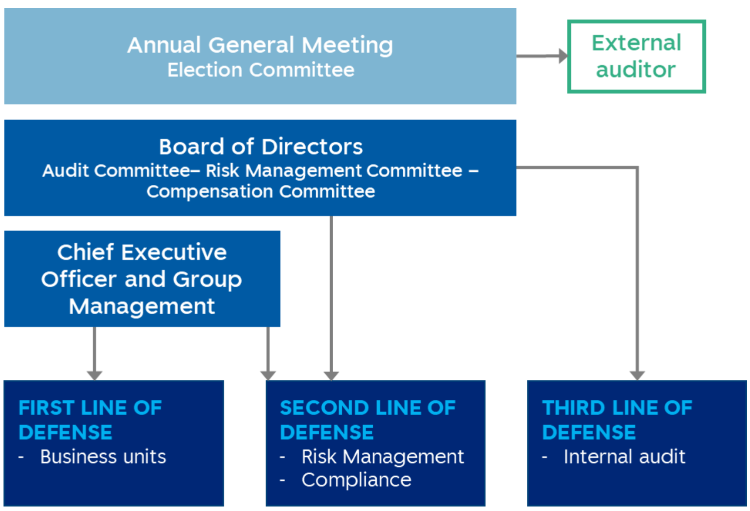
Frequency	Report
Monthly	**Liquidity and market risk:** The monthly report is the second line assessment of the risk profile within liquidity and market risk. The monthly report provides a status on key metrics with analyses and comments.
Quarterly	**Risk report:** The risk report is the second-line assessment of the risk picture. The risk report provides an overview of the risk situation, with analyses and comments.
Quarterly	**Compliance report:** Compliance prepares a report on the status and development of the compliance situation. The reporting is Compliance's independent assessment and shall provide a clear overall picture of SpareBank 1 SR-Bank's compliance risk.
Quarterly	**Undesired incidents:** The quarterly undesired incidents report provides an overview of the development in registered incidents as well as the financial consequences of these. Significant events are highlighted together with a description of the consequences and follow-up.
Annual	**ICAAP report:** The ICAAP report contains a detailed description of SpareBank 1 SR-Bank's process for self-evaluation of the risk and capital situation. SpareBank 1 SR-Bank's process for self-evaluation of the liquidity situation ILAAP (Internal Liquidity Adequacy Assessment Process) describes and assesses the liquidity situation for the entire group.
Annual	**Validation report:** The validation officer prepares an annual validation report which forms the basis for the board of SpareBank 1 SR-Bank to decide whether the risk management system (IRB system) is well integrated in the organization and whether it calculates the risk level and capital requirements in a satisfactory manner.
Annual	**Recovery plan:** The recovery plan is an important part of SpareBank 1 SR-Bank's preparedness. An important part of the recovery plan is a description of various identified measures that can improve SpareBank 1 SR-Bank's capital coverage and liquidity situation in an imagined crisis. The plan is revised annually. The status of defined recovery indicators is reported to the board every quarter.

2.3 Roles and responsibilities

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 2: Governing bodies of SpareBank 1 SR-Bank



The Board of SpareBank 1 SR-Bank is responsible for approving the group's risk profile, framework for risk and capital management, and ensure that the group is sufficiently capitalized in accordance with regulatory requirements and chosen risk profile. The Board should further ensure that the group's risk profile and risk framework for risk and capital management are adequately communicated and implemented in the group, and that it 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 risk exposure at all times 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 led by the Chief Risk Officer (CRO), who reports directly to the CEO. The department is organized independently of the business units. The CRO has the option to report directly to the Board if extraordinary situations should indicate it. The department is responsible for further development of the framework for risk and capital management so that it works effectively and as intended. The department is also responsible for independent follow-up of risk exposure in accordance with risk appetite and risk strategy. The department should also prepare proposals for risk profile and risk strategies that ensure financial robustness and efficient use of the group's equity. The department should 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 Committee 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 representatives 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 their 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 committee held six meetings during 2023.

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 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 providing an independent recommendation to the mandate holder. The Credit Committees assess loan and credit applications in accordance with the current credit strategy, credit policy, authorization regulations, and credit processing routines.

2.4 Risk culture

Risk culture means values and attitudes that are expressed through risk awareness, actions, and ability for organizational learning. A good risk culture forms the foundation of good risk management and is a prerequisite for getting full benefit from policies, routines, and models.

In collaboration with the University of Stavanger, SpareBank 1 SR-Bank has developed a framework used to conduct regular group-wide evaluations of risk culture. The survey is conducted every other year and was last conducted in 2023. The results show that the risk culture in the organization is good. The results from the measurements lead to good discussions in the group, increased awareness, and insight into topics that are usually not discussed as directly. The fact that such measurements are conducted is therefore considered in itself to constitute an important contribution to a good risk culture.

3. CAPITAL REQUIREMENTS

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

3.1 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.

There are in principle two different approaches for calculating the minimum requirement for responsible capital according to the capital adequacy regulations. One approach is based on template rules, while the other is based on the use of internal models. When using internal models, the regulatory minimum requirement for capital is based on the banks' internal risk assessments. This makes the statutory minimum requirement for capital coverage more risk-sensitive, so that the capital requirement matches to a greater extent the risk in the underlying portfolios or activities.

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

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).

3.2 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.

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

Table 2: 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
	Corporates– parent bank	Advanced IRB
	Retail – 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
	Retail - SR-Boligkreditt AS	IRB - Mass market
	Corporates – SpareBank 1 Næringskreditt AS	Standard method
	Corporates – BN Bank AS	Advanced IRB
	Retail – 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 former wholly owned subsidiary SpareBank 1 SR-Finans AS was merged into the parent bank SpareBank 1 SR-Bank ASA from January 1, 2017. The merged portfolio of leasing is reported regulatorily using the standard method, while internally the IRB method is used. SpareBank 1 SR-Bank has applied for and received permission from the Financial Supervisory Authority to use advanced IRB for the merged portfolio of leasing. The implementation of IRB on this part of the portfolio will be carried out during the implementation of revised IRB models for companies.

3.3 Combined buffer requirements

In Basel III, combined buffer requirements were introduced in addition to the minimum requirement for regulatory capital. These include the conservation buffer, systemic risk buffer, countercyclical buffer, and buffer for systemically important financial institutions.

Capital conservation buffer (2.5%): The requirement for a conservation buffer of 2.5 percent of the bank's calculation basis remains constant throughout all economic cycles. The purpose of the conservation buffer is to ensure that banks build capital in boom times to prevent the capital from falling below the minimum requirement in periods of economic downturn.

Systemic risk buffer (4.5%): Systemic risk can be defined as a risk that financial instability causes disruptions in the provision of financial services to an extent that can have significant negative effects on production and employment. The systemic risk buffer requirement increased from 3.0 percent to 4.5 percent with effect from December 31, 2020. Since this buffer requirement targets structural vulnerabilities and other systemic risks in the Norwegian economy, it should only apply to the banks' exposures in Norway, as opposed to previous buffer requirements that apply to all activities. As of December 31, 2023, the actual rate is 4.46 percent for SpareBank 1 SR-Bank.

Countercyclical buffer (0,0-2,5%): In Norway, a countercyclical capital buffer in the range of 0 - 2.5 percentage points in the form of common equity is required. The purpose of the countercyclical capital buffer is to make banks more resilient and robust against loan losses. In December, Norges Bank decided to keep the countercyclical buffer requirement for banks unchanged at 2.5 percent.

Buffer for systemically important institutions (1.0 - 2.0 percent): Credit institutions defined as systemically important by Norwegian authorities will be subject to an additional buffer requirement of two percent. Institutions with assets under management of at least 10 percent of mainland Norway's GDP, or a share of the lending market of at least five percent, are defined as systemically important. SpareBank 1 SR-Bank ASA is defined as a systemically important financial institution with a specific buffer requirement of 1 percent, effective from September 30, 2024.

Pillar 2 requirement (1.6 per cent): The Pillar 2 addition is an institution-specific addition aimed at ensuring that Norwegian banks have sufficient capital to cover the risks associated with their operations beyond those included in the regulatory minimum requirement. In December 2023, the Financial Supervisory Authority granted the group an individual Pillar 2 addition of 1.6 percent and a temporary Pillar 2 addition of 0.5 percent, until applications for model changes are processed. The requirements from the Financial Supervisory Authority were unchanged from the previous SREP6 process. The main rule that the Pillar 2 requirement should be covered by 100 percent common equity was changed to 56.25 percent. Additionally, the Financial Supervisory Authority expects the group to have a capital requirement margin of 1.25 percent.

3.4 Actual capital adequacy

Common equity tier 1 capital coverage was 17.61 percent, while total capital coverage was 21.58 percent as of December 31, 2023. This exceeds the capital coverage requirement of 20.81 percent. The total requirement for common equity tier 1 capital coverage for SpareBank 1 SR-Bank ASA was 16.39 percent as of December 31, 2023.

3.5 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. SpareBank 1 SR-Bank had an unweighted tier 1 capital ratio of 7.2 per cent at the end of 2023, and thus well above the minimum requirement.

4.CREDIT RISK

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

4.1 About credit risk

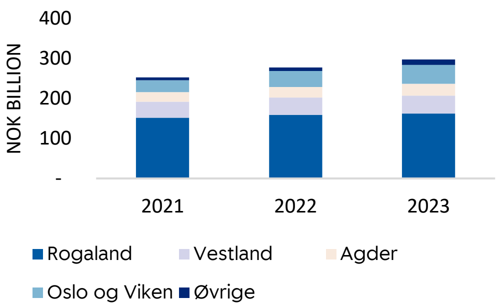
SpareBank 1 SR-Bank is primarily exposed to credit risk through its loan portfolios in the retail and corporate markets. The group is also exposed to credit risk through the liquidity portfolio. This portfolio mainly consists of low-risk commercial paper and bonds that qualify for loans from The Central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

4.2 Development in credit risk

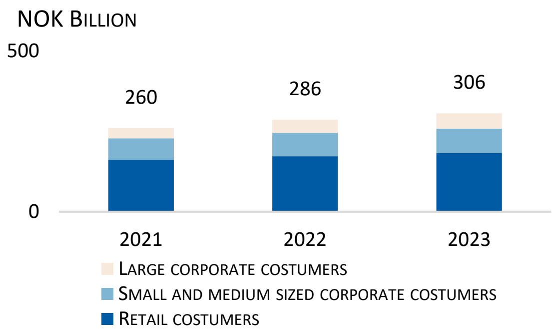
SpareBank 1 SR-Bank has Southern Norway as its primary geographic market area, with the largest presence in Rogaland, Agder and Vestland as well as Oslo and Viken. The figure below shows the exposure by geographical area as of December the last three years for customers in SpareBank 1 SR-Bank. The exposure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

Figure 5: Exposure (EAD) by geographic market areas



Rogaland is the group's largest market area, and the exposure as of December 2023 is NOK 162 billion. This represents 54 percent of SpareBank 1 SR-Bank's total loan exposure. The exposure in Vestland, Agder and Oslo/Viken amounted to respectively 45, 30 and 47 billion in 2023. The 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 6: Exposure by customer segment

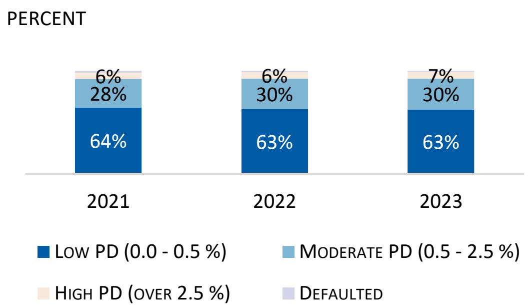


The largest share of the loan exposure in SpareBank 1 SR-Bank is aimed at retail customers, and loans are mainly financed by mortgages on real estate. Exposure to retail customers has increased from NOK 173 to 182 billion in 2023. 95 per cent of loan exposure in the retail market consists of loans that are smaller than NOK 10 million. Exposure to small and medium sized corporate customers has increased from NOK 72 to 76 billion in 2023. Credit exposure to large corporate customers has increased from NOK 41 to 48 billion in 2023. 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. The share of loan exposure on customers with a probability of default (PD) lower than 0.5 per cent constitutes 63 per cent of the total loan portfolio in 2023. These are customers risk classified in default classes A, B or C. The share of the loan exposure with moderate PD was 30 per cent. These customers are risk classified in the default classes D, E or F.

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

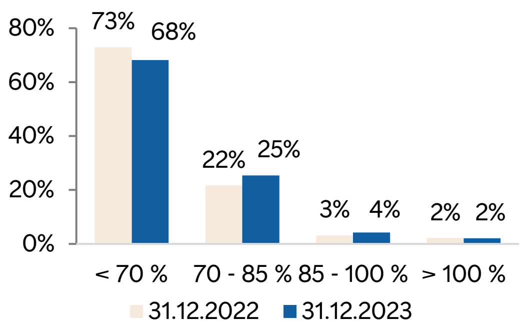
Figure 7: Loan portfolio by probability of default (PD)[3]



SpareBank 1 SR-Bank has a significant focus on monitoring exposures with PD (Probability of Default) higher than 2.5 percent. As of December 2023, 7 percent of the loan exposure is towards customers with PD higher than 2.5 percent. These customers are classified into default classes G, H, and I. The exposure to defaulted customers constitutes 1.1 percent of the total loan exposure in the corporate and retail markets as of December 2023. The portfolio composition is based on a clearly defined strategy where growth and risk profile are managed through specific credit strategic frameworks for concentration risk, among other factors.

The figure below shows the development of the loan-to-value ratio in the retail portfolio from 2022 to 2023. The calculation of the loan-to-value ratio is based on the market value of the collateral and is presented as the total distributed loan-to-value ratio. With the total distributed loan-to-value ratio, the entire relevant loan is assigned to one and the same interval.

Figure 8: Loan-to-value ratio (LTV) – total distributed



4.3 Managing credit risk

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, 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 among the leading players in Norway in credit risk management. This has been achieved through local knowledge of the customer and the use of robust credit models and credit analysis. Furthermore, clear requirements are set for the employees' competence and attitudes, where the ability to recognize risk and the willingness to learn from experience are emphasized. In credit assessments, particular emphasis is placed on ensuring that customers' businesses comply with applicable laws and regulations, that customers' businesses have a long-term perspective, and that customers have both the necessary repayment ability and robust equity considering the nature of the business. The credit granting process is characterized by clear responsibilities where collaboration ensures the best possible basis for decision-making, but where the credit decision itself is made individually.

The ability to adhere to its own guidelines and thus avoid financing engagements that contradict these guidelines is given significant importance. Therefore, there is a strong focus on credit employees' active use and compliance with a framework for credit risk management that aligns with best practices in the field. Compliance is also specifically monitored by independent representatives from the group's risk management environment, both through ongoing participation in various credit committees and through independent reporting from the work of the credit committees.

[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

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 company 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 policy 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 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 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

4.4 Measurement of 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.

4.5 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 table below:

Table 3: The risk classification system in SpareBank 1 SR-Bank

Risk classification	Short description
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 customer 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.

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

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

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.

Table 4: 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	Ratingscale Standard & Poor's	Ratingscale Moody's
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

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.

Loss given default – LGD

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 5: definition of LGD (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 %

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.

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 6: 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 %

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 price 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.

4.6 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 7: 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 of the IRB system

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. Independent validation is carried out by the department "Model risk and external risk reporting," which is organized independently of the units responsible for model development and the establishment and renewal of loans. 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. Validation findings and any recommendations for improvement are presented by the Executive Vise President Risk Management (CRO). The IRB system is described in the chapter on capital requirements.

The aim of the validation process is to ensure that:

- The IRB parameters are based on relevant data of sufficient quality
- The assumptions on which the IRB system is based are reasonable
- Weaknesses and limitations in the models or the use of models are identified, assessed and followed up where possible
- The IRB system is well integrated into the organisation, and that it forms a central part of the banks risk management and decision making

The validation process can be divided into the following main areas:

Data validation: Control of data quality, possible breaks in data series or missing data in the estimation basis and later in model follow-up.

Qualitative validation: Assessment of the models and model implementation, providing an overall assessment of the IRB system. The assessments include the models' ability to measure relevant risk, the models' conceptual reasonableness and model limitations, internal anchoring, documentation, and implementation.

Quantitative validation: Verification of the models' data representativeness, ranking ability, calibration targets, calibration to the calibration targets, and stability. Includes assessments at the calibration segment level and significant sub-portfolios, as well as default class and risk drivers.

Application: The review should be able to demonstrate that the IRB system is well integrated into the organisation and that it forms a central part of the bank's risk management and decision-making.

Compliance with regulatory capital requirements: The review should ensure that the bank meets regulatory capital requirements.

The table below shows models used in the regulatory IRB reporting in SpareBank 1 SR-Bank at the end of 2023:

Table 8: Risk models used in regulatory reporting 2023

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 2022, new guidelines from the EBA in the IRB area came into effect. The bank has in recent years worked to update the IRB models and validation framework in line with the new guidelines.

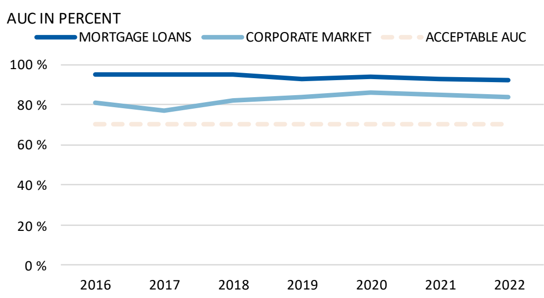
4.7 Comparison of risk parameters and actual outcome

This section presents an extract of the validation results for the PD, EAD and LGD models in SpareBank 1 SR-Bank for the IRB portfolio. As a result of the fact that validation results for 2023 had not been processed by the board at the reporting time for publication under Pillar 3, results up to and including validation year 2022 are reproduced.

PD models

The figure below shows the PD models' ranking ability for mortgages and the corporate market respectively in the period 2016-2022. The generic PD model for mortgages has very high and stable ranking ability, which means that the model has a very good ability to rank customers from those with the highest to those with the lowest actual probability of default. Validation on various segments also shows high ranking ability. The generic PD model for corporate market customers has a high and stable ranking ability for the total portfolio.

Figure 9: Discrimination power, PD models

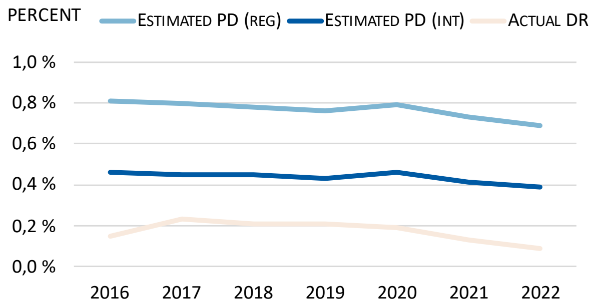


When validating different sub-portfolios, the ranking ability may be somewhat lower. This applies to larger customers and certain industry types. For this reason, separate PD models have been developed for these segments which are currently only used in the internal portfolio management.

Current capital adequacy regulations require that the estimated probability of default (PD) must predict long-term outcomes through a full loss cycle. This means that the default estimates must be relatively stable over time, also through a business cycle. The figure below shows the average unweighted estimated probability of default (PD) internally and regulatory compared to the average actual default in the years 2016-2022.

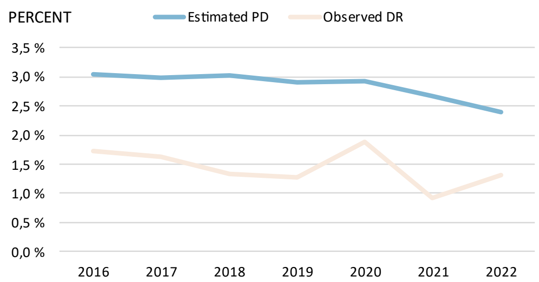
Regulatory PD is calculated in line with Finanstilsynet's methodology for calculating long-term outcomes, with fixed levels for, among other things, defaults in a severe recession. Internal PD is estimated using the bank's best estimates for default through a full loss cycle and reflects to a greater extent the underlying risk in the portfolio. Use of the internal estimates provides more risk-sensitive risk weights and contributes to increased motivation for good risk management.

Figure 10: 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 internal and regulatory estimated default (PD) throughout the period. In regulatory terms, there is – in accordance with current regulations – a significant overestimation of the level of default. For companies, there is consistency in the calibration of internal and regulatory default levels, and the figure below indicates the average unweighted estimated and actual default for the corporate market.

Figure 11: Comparison of unweighted estimated PD and actual DR – corporate market



As the figure shows, the estimated probability of default (PD) is higher than actual default (DR) throughout the period. The PD level is considered to be in line with the model's desired cyclical characteristics.

All customers with credit exposure in SpareBank 1 SR-Bank are risk-classified at least annually when accounting or balance sheet data is updated. In addition, customers are scored monthly based on information on internal and external behaviour. The figures below show annual migration for mortgage customers and the corporate market, respectively. Migration refers to the proportion of customers who change their default class during a 12-month period.

Figure 12: Annual migration – mortgage loans

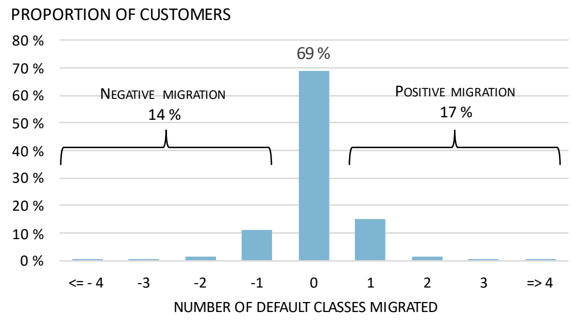
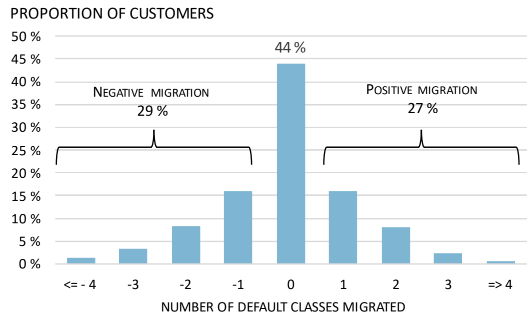


Figure 13: Annual migration – corporate market

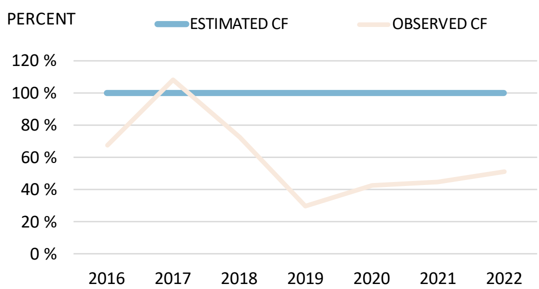


The stability of the default estimates is an indicator of the model's cyclical characteristics. The proportion of stable customers in 2022 was 69 per cent for mortgages and 44 per cent for the business market.

EAD models

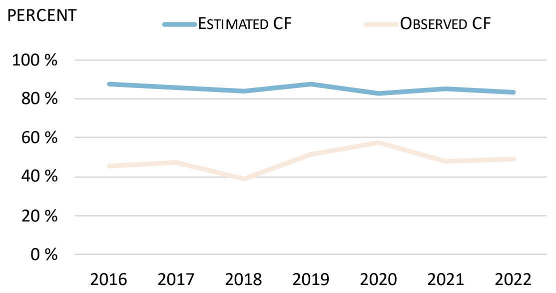
A validation is carried out of whether the model estimates can predict the utilization of limits (CF) in the event of a serious economic setback ("downturn"). This means that there must be a sufficient margin between estimated and observed values in normal business conditions. The graphs below show comparisons of the conversion factor for the period 2016-2022.

Figure 14: Comparison of estimated and actual conversion factor (CF) – mortgage loans (limit loans)



For all home loan customers with a framework loan, the conversion factor is a fixed parameter. The average observed conversion factor is 60 per cent in the period, and significantly lower than the set parameter of 100 per cent. The high observed KF in 2017 is due to the fact that small amounts have relatively large effects measured in percentage in periods with a low number of defaults.

Figure 15: comparison of estimated and actual conversion factor (CF) – corporate market



For the corporate market, a separate model has been developed which estimates the conversion factor based on risk classification and engagement type. The average estimated conversion factor is 85 percent, and higher than the average observed conversion factor of 48 percent.

LGD models

Regulatory calculation of loss ratio (LGD) for mortgages dictates that the minimum estimated LGD must be 20 per cent, regardless of underlying portfolio quality and loss history. Internally, own estimates are used for loss ratio which are based on internal data with empirical coverage, and which are representative of the bank's portfolio.

For the corporate market, there is full agreement between internal and regulatory estimates for LGD. The figures below show estimated and observed unweighted loss ratio for resolved default cases in the period 2016-2022 Both estimated and observed loss ratio are measured for defaulted customers, and the estimates are normally higher than the overall portfolio including healthy customers.

Figure 16: Comparison of estimated and actual weighted LGD for defaulted loans – mortgage loans (internal and regulatory)

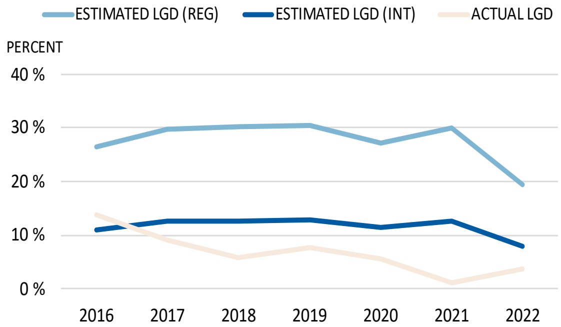
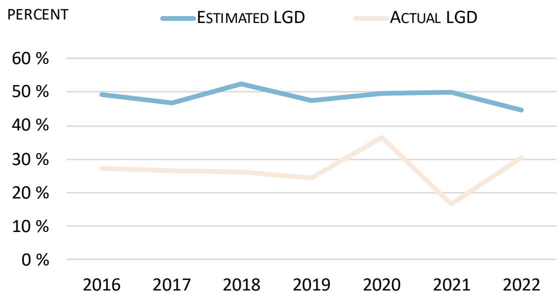


Figure 17: Comparison of estimated an actual weighted LGD for defaulted loans – corporate market



The figures above show that the observed loss rate is lower than the estimated loss rate over time, both for mortgages and the corporate market.

In 2020, a small increase in the observed loss rate for the corporate market is observed. This is related to the recession that has affected certain industries within the large customer segment in offshore and oil-related business after the drop in oil prices that started in 2014 and the corona pandemic in 2020.

In the larger and more complex cases, recovery time is somewhat longer than normal, and it must be expected that the observed loss rate will be corrected as cases are clarified. Analyses carried out indicate that the loss estimates are sufficiently conservative to cover losses also for the cases that have not been settled.

4.8 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 2 is used for loans with a significant increase in credit risk since being granted and Stage 3 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 9: Expected credit loss on segments and stages (amounts in NOK million)

2023 (IFRS 9)	**Stage 1**	**Stage 2**	**Stage 3**
Rogaland	89	166	449
Agder	28	50	31
Vestland	40	64	17
Oslo/Viken	51	82	44
Other	25	63	45
Sum	**233**	**425**	**586**
2022 (IFRS 9)	**Trinn 1**	**Trinn 2**	**Trinn 3**
Rogaland	121	155	598
Agder	27	32	49
Vestland	45	52	298
Oslo/Viken	65	59	15
Other	30	20	118
Sum	**288**	**318**	**1.079**

5. COUNTERPARTY RISK

Counterparty risk is a form of credit risk that arises from trading in financial instruments, for example derivatives or lending with collateral in securities. Derivatives are most often traded Over the Counter (OTC), i.e., by individual contracts between two counterparties. Counterparty risk is risk linked to the counterparty's ability to fulfil the agreed obligations in the contract and differs from other credit risk in that the exposure usually depends on market risk factors such as interest rates, exchange rates, commodity prices or share prices.

5.1 About counterparty risk

SpareBank 1 SR-Bank enters into derivative transactions to hedge currency and interest rate risks that arise in connection with ordinary banking operations, including in connection with borrowing and lending operations. In addition, derivative transactions are entered into in connection with customers' demand for hedging instruments and to hedge own positions that arise in connection with customer trades.

Customers use derivatives to hedge against unfavourable movements in exchange rates and interest rates. The exposure to the bank is therefore basically risk-reducing for the customer. If a customer is to trade in currency and/or interest instruments, a separate limit must be granted to cover the bank's counterparty risk. The framework is granted in accordance with normal credit processing, i.e. in accordance with the bank's ordinary authorization regulations.

In order to minimize the counterparty risk towards bank counterparties, bilateral netting agreements, so-called ISDA agreements, are entered into. Such agreements make it possible to offset all positive and negative market values associated with derivative contracts entered into same counterparty. Bilateral agreements on the exchange of cash collateral, so-called CSA supplements, are also entered into with bank counterparties. The latter means that the market value of all derivative contracts entered into between SpareBank 1 SR-Bank, and the counterparty is settled daily, and counterparty risk will therefore be largely eliminated. The EMIR regulations also mean that a significant part of derivative transactions, including the lion's share of interest rate derivatives with bank counterparties, are offset via so-called clearing centers (CCP). SpareBank 1 SR-Bank is not a direct member of a central counterparty but is associated with other clearing members in connection with the clearing of derivatives.

The capital requirement for counterparty risk is calculated according to the standard method (SA-CCR). There are small changes in EAD the last year. The basis for calculating counterparty risk amounted to NOK 1.4 billion at the turn of the year, which was up from NOK 1.3 billion at the end of 2022. The basis for calculating counterparty risk as of 31 December 2023 is 1.0 per cent of the group's total basis for calculation.

6.MARKET RISK

Market risk is a collective term that encompasses the risk of loss as a result of changes in market prices, including the risk of loss resulting from changes in observable market variables, such as interest rates, exchange rates and securities markets.

6.1 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 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 are delegated by the chief executive to named people. Guidelines and routines are well described. 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 SB1 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.

6.2 Market risk, including spread risk bonds and certificates

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 Treasury's bond portfolio, is quantified by calculations based on the Financial Supervisory Authority of Norway's stress test model.

The liquidity portfolio's total holding amounts to NOK 57.7 billion[6]. All fixed interest rate exposure is hedged. Details of exposure and portfolio development is presented in the Group's Factbook and Pillar 3-attachement.

[6] NOK 9.0 billion of which is measured at amortized cost and is therefore not exposed to market risk.

Risk-adjusted capital associated with other market risks is measured and followed up according to the Value at Risk principle (VaR). The VaR model covers the group's interest rate risk, as well as the securities risk associated with the group's investments in shares, shares and other equity interests. Market risk is reported under credit and counterparty risk in accordance with the standard method.

6.3 Bond portfolio

Risk profile and portfolio performance

The group's liquidity portfolio consists of bonds and commercial.

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 2023, the value of the combined liquidity portfolio totals NOK 57.7 billion. The table below provides a summary of SpareBank 1 SR-Bank's exposure to bonds based on risk classification:

Table 11: Securities exposure, bonds and securities

Risk classes for bonds and commercial paper			
Risk category	**Rating**	**Market value NOK million**	**Total %**
Very low risk	AAA, AA+, AA og AA-	57.447	99,5 %
Low risk	A+, A og A-	0	0,0 %
Moderate risk	Not rated	272	0,5 %
High risk	Not rated	0	0,0 %
Very high risk	Not rated	0	0,01%
Total		**57.719**	**100,0 %**

6.4 Interest rate risk

Interest rate risk arises because the group can have different fixed interest periods on its assets and liabilities. Trading in fixed-income instruments must at all times take place within agreed limits and authorisations. The group's framework defines quantitative targets for the maximum potential loss in the event of a positive parallel shift in the yield curve of 2 percentage points. The framework for the group is a total of NOK 200 million with various sub-frames for specified maturity bands. Interest rate risk is quantified and monitored continuously. For loans and deposits with a fixed interest rate ("pt.-rente"), an expected interest rate fixation period is used depending on the interest rate shock scenario.

Table 12: Sub-limits within the different maturity bonds

Maturity bond	Treasury limit
0 – 3 months	NOK 200 mill.
3 – 6 months	NOK 100 mill.
6 – 9 months	NOK 100 mill.
9 months – 1 year	NOK 100 mill.
1 year – 18 months	NOK 40 mill.
18 – 24 months	NOK 30 mill.
Each year (1-10)	NOK 30 mill.
10 years or more	NOK 20 mill.

At the same time, the group has delegated an interest rate risk framework to SpareBank 1 Markets. The framework defines quantitative targets for the maximum potential loss in the event of a positive parallel shift in the yield curve of 2 percentage points, and the framework amounts to a total of NOK 70 million with various sub-frames for specified maturity bands. SpareBank 1 Markets is responsible for all gains and losses arising from use of the delegated interest rate risk framework, and the exposure associated with this framework is therefore not included in the table below.

Table 13: 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. 2023	11	15	5	0	**31**
3rd Qtr. 2023	-18	16	4	0	**2**
2nd Qtr. 2023	-33	22	4	-1	**-8**
1st Qtr. 2023	-40	15	4	0	**-21**

6.5 Foreign exchange risk

Exchange rate risk is the risk of loss due to changes in exchange rates. SpareBank 1 SR-Bank does not take currency risks that arise through ordinary banking operations and financing activities. All currency exposure is hedged.

At the same time, the group has delegated currency risk frameworks to SpareBank 1 Markets. The risk that can be taken is regulated by nominal limits for the maximum aggregated currency position and the maximum position in a single currency. The overnight rate risk for spot trading in currency must not exceed NOK 100 million net per individual currency and NOK 225 million aggregated. SpareBank 1 Markets is responsible for all gains and losses arising from use of the currency risk framework.

6.6 Securities risk, shares

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

Balance sheet classification	4th Qtr. 2023	3rd Qtr. 2023	2nd Qtr. 2023	1st Qtr. 2023
Shares, units etc.	680	809	790	777

7.OPERATIONAL RISK

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

7.1 Management of operational risk

The purpose of managing operational risk is primarily to protect the group's values, and values for which the group is responsible, but which are owned by other stakeholders. This applies to financial values, as well as other tangible and intangible values that can be affected by operational risk. Including reputation, information, people, relationships, integrity, nature and environment, ability to deliver and physical assets.

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, apparent prerequisites, clearly defined roles and responsibilities, and good process for managing operational risk.

Risk strategy and limits on operational risk exposure are set annually and approved by the board. The board also determines governing principles and frames in a policy for operational risk. The Risk Management Department is responsible for supporting and challenging the risk owners, and for ensuring that the group has a good framework for identification, reporting and mitigation of operational risk.

7.2 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, 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 and processes 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.

7.3 Development in operational risk

The finance sector has been evolving at ever increasing pace the last several years, introducing new and changed operational risks to the group. The group has therefore focused particularly on the rate of change as a significant risk driver and conducts thorough risk assessment for all significant changes in products, processes, systems, and activities. The assessments are conducted in a standardized process, securing the involvement of all interested parties, premise givers and decision makers. In total, more than a hundred change cases have been registered and processed during 2023. Such proactive risk management is a key measure to avoid the group being exposed to unintended new risks through individual or consistent weaknesses in products, systems, and routines.

7.4 Undesired incidents

Registration and learning of unwanted incidents are an important tool for capturing and realizing areas for improvement, as well as reducing risk. Over several years, the group has focused on building a good culture and good processes for incident reporting. There were 449 unwanted incidents registered in 2023, several of which have resulted in measures that lead to a real reduction in the risk of similar and more serious incidents in the future. The figure below shows the number of registered incidents in the years 2019 to 2023. The total loss from registered adverse incidents in 2023 amounted to NOK 5.37 million, compared to NOK 8.2 million in 2022.

Figure 18: Registered, undesired incidents by Basel categories

8. 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.

8.1 About liquidity risk

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

8.2 Management and measurement of liquidity risk

Liquidity risk is managed and measured using several measurement methods, as no single method can quantify this type of risk. The methods include frameworks for maximum refunding needs within different maturities, balance sheet ratios, survival targets in a normal situation assuming closed capital markets and the short-term liquidity target LCR. Furthermore, internal stress testing of the group's ability to survive is carried out under various scenarios, including a serious banking and market-specific crisis. The results of the stress tests form part of the information base for the group's liquidity strategy and recovery plan in the event of a liquidity crisis.

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 in SpareBank 1 SR-Bank is assessed as good. The group's liquidity target, LCR (liquidity coverage ratio), was 207 per cent, and the NSFR (net stable funding ratio) was 130 per cent at the end of 2023.

The liquidity reserve indicates a survivability of 33 months at the end of 2023 without access to external financing. During the next 12 months, debt capital equivalent to NOK 22.3 billion will be refinanced.

Deposits from customers are a key source of funding. For the group, the deposit volume increased by NOK 0.9 billion (0.7 per cent) during the year and amounts to NOK 149.0 billion at the end of 2023. Deposit coverage is 54.8 per cent at the end of 2023 compared to 58.5 percent at the end of 2022.

SR-Boligkreditt AS is a wholly owned subsidiary that was established in the 2nd quarter of 2015. The company's purpose is to buy mortgages from SpareBank 1 SR-Bank and finance this by issuing covered bonds. Through SR-Boligkreditt AS, SpareBank 1 SR-Bank can diversify and optimize its funding. Mortgage loans transferred to SR-Boligkreditt AS amounted to NOK 100.3 billion at the end of 2023.

The figure below illustrates the maturity structure for the funding portfolio at the end of 2023:

Figure 20: The funding portfolio's maturity structure as of 31.12.2023

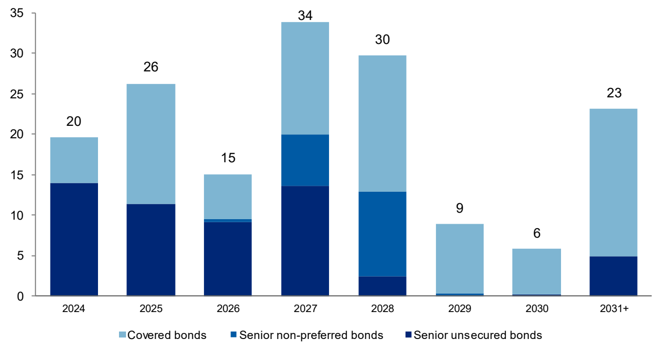
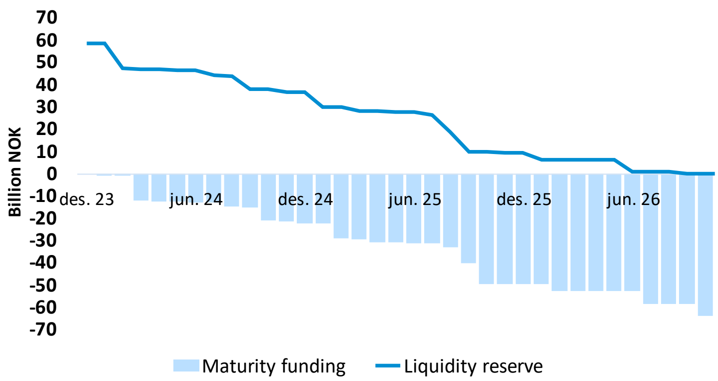


Figure 21: Sensitivity analysis of the funding risk – basis scenario



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 October 2026. The liquidity buffer consists of cash and very secure interest-bearing securities.

9. OWNERSHIP 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.

9.1 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 in several of 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.

9.2 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 companies in which the bank has direct and indirect ownership.

Figure 22: Partly owned companies as of 31 December 2023

10. 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.

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.

11. REPUTATIONAL 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.

SpareBank 1 SR-Bank has established a communication strategy to ensure that information is communicated internally and externally in a way that supports the company's values, goals, and vision.

The group has its own Communications department, which is represented in the group management through the People, Sustainability and Communication division. Dedicated responsible persons have been established to handle all communication on social media, and information management is included in the group's emergency plan which is distributed to all employees.

SpareBank 1 SR-Bank has also implemented an internal process for identifying and evaluating the group's reputational risk picture. A review and mapping of which reputational risks the group is exposed to is carried out regularly and at least annually, and whether there are any changes in the risk picture.

The reputational risks are identified and ranked based on assessment of:

- Direct management cost
- Impact on the departure of existing customers
- Influence on the access of new customers
- Potential for the group's licenses to come under review and thereby indirectly affect market value and financing ability
- 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.

12. STRATEGIC RISK

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

SpareBank 1 SR-Bank conducts an annual strategic process involving the board, management, key individuals, divisions, and subsidiaries. This work results in a strategic framework for the next three-year period with an associated business and action plan. The business plan clearly outlines the priorities the group has set for the period based on scenarios, competitive and market situations. The business and action plan is most detailed for the upcoming year.

The group management conducts both monthly and quarterly evaluations of the group's performance and strategic direction. The quarterly evaluation also assesses any new initiatives and measures that need to be implemented based on changes in assumptions or changes in the market situation. The strategic work is therefore flexible in its approach and can accommodate both short-term and long-term objectives.

13. 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-related risks and opportunities that may affect customers, business areas, and operations at various levels. The group's loan portfolio undergoes annual stress tests and financial projections. The largest climate risk exposure for SpareBank 1 SR-Bank lies in the corporate market portfolio, so the management of climate risk from this part of the business is prioritized. The group recently adopted its first climate transition plans and set emission reduction targets for four of the key industries in the loan portfolio: shipping, oil/gas, agriculture, and commercial real estate.

The framework for Sustainable Finance was updated in 2023 by incorporating the taxonomy rules for green buildings constructed after 2020. This framework, which constitutes the regulations for defining loans as either green or sustainable-linked, is a central tool in relation to the group's objectives for green and sustainable financing leading up to 2030. The group uses the common SpareBank 1 risk framework for assessing sustainability risk (ESG score). The ESG framework is used in connection with credit approval and renewal for corporate customers with consolidated exposure exceeding 10 million Norwegian kroner. It includes evaluation criteria for several specific industries and incorporates inherent industry-specific risks.

The ESG scoring is based on questions within the four sub-themes: physical climate risk (E), transition risk (E), social factors (S), and ownership and corporate governance (G), providing a sub-score for each sub-theme as well as a total score.

If a customer receives a particularly low ESG score, it is a requirement for the customer advisor to develop an improvement plan with the customer. The goal of the scoring is to assess the customer's sustainability risk and to assist the customer advisor in the dialogue with the customer about sustainability. The group's overall ambition in sustainability is to be the customer's ally in the transition. Therefore, effectively integrating sustainability into customer dialogue is an important success factor. The experiences so far have been positive, and the scoring shows a good ranking of the customers.

Capturing, ensuring the quality, storing, and disseminating ESG risk data for internal purposes and external reporting will be a major challenge, which will be addressed in an alliance project in collaboration with SpareBank 1 Utvikling. The project, which started in the fall of 2022, has evolved into a department in SpareBank 1 Utvikling responsible for ESG data. SpareBank 1 SR-Bank contributes by leasing resources to this department. As a major bank in Norway, the group has extensive disclosure obligations in the ESG area. For 2023, this means a significant expansion of the pillar 3 reporting requirement compared to the more limited reporting obligation following the EU taxonomy for green financing. In 2023, SpareBank 1 SR-Bank will carry out its first reporting of both pillar 3 ESG and the EU taxonomy.

14. 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.

14.1 Management of compliance risk

SpareBank 1 SR-Bank is managed through the framework for compliance that emerges from the bank's compliance policy, and which is to ensure that the group does not incur public sanctions/fines or financial loss as a result of a lack of implementation and compliance with laws and regulations.

Focus areas are ongoing follow-up of compliance with current regulations and ensuring that the group has the best adaptation to upcoming changes in regulations.

SpareBank 1 SR-Bank's compliance function is organized independently of the business units. The department has overall responsibility for the framework, follow-up and reporting within the compliance area. The executive vice president for compliance reports directly to the CEO and the board. The investment company and subsidiaries have their own compliance officers where this is required.

The managers in the group are operationally responsible for practical implementation and compliance with laws and regulations. All employees are responsible for ensuring that they comply with and understand the applicable laws and regulations on a daily basis.

15. 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
KF	Conversion Factor (proportion of unutilised credit facility which is expected to have been drawn upon default)
LGD	Loss Given Default
PM	Retail market
BM	Corporate Market

APPENDIX

Please see excel-sheet for attachments.