Group Risk Report 2012

AKTIESELSKABET
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Contents

Overall risk management

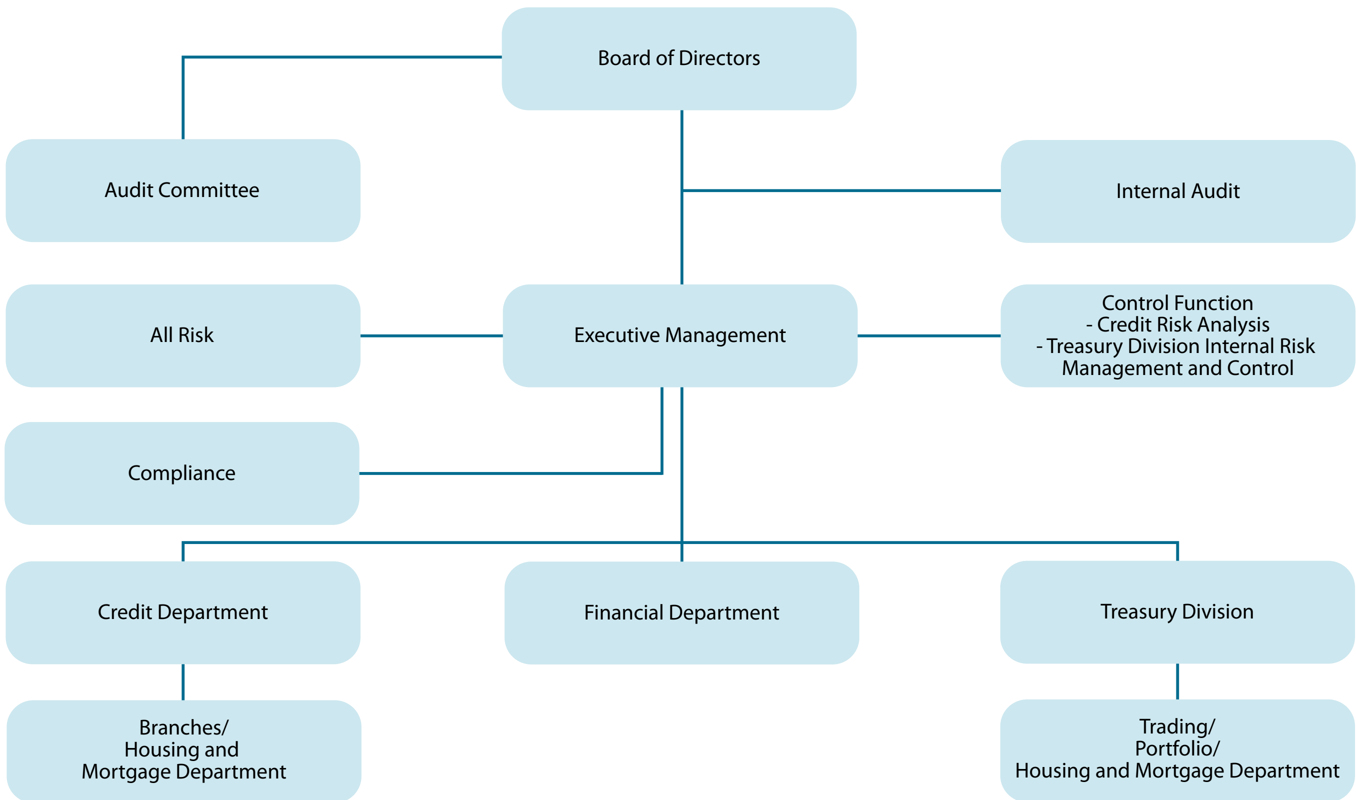
The aim of the Group Risk Report is to provide an insight into the internal risk management of Arbejdernes Landsbank on the basis of the Group's method of reviewing and managing risks, as well as the underlying risk organisation. Arbejdernes Landsbank wants to ensure that the Group remains a strong financial unit for the owners of the Bank as well as its customers, and accordingly, it is important that the Bank is aware of and controls the various risks to which the Group is exposed.

The basis for overall risk management at Arbejdernes Landsbank is:

- Written instructions from the Board of Directors, including "Instructions for segregation of responsibilities between the Board of Directors and the Executive Management of Aktieselskabet Arbejdernes Landsbank" (*Instruks for arbejdsfordelingen mellem bestyrelsen og direktionen i Aktieselskabet Arbejdernes Landsbank*) with the associated "Instructions for reporting to the Board of Directors of Aktieselskabet Arbejdernes Landsbank" (*Instruks for rapportering til bestyrelsen i Aktieselskabet Arbejdernes Landsbank*),
- An Audit Committee established by the Board of Directors which assesses whether the company's internal control system, and its internal audit, risk and security systems are working effectively,
- Meetings of the Executive Management and of the Board of Directors, where instructions on specific corporate decisions are specified, and other risks affecting the Bank are assessed, and
- Meetings of the Balance-sheet and Risk Management Committee at which risk aspects are discussed as well as
- the frequent reports on results, business areas, financial ratios and relevant risk targets.

Since 2011, the Bank has had a function under the Financial Department which is responsible for risk management. The function aims at ensuring that the Bank management receive relevant risk information about all the Bank's

Figure 1. Organisation chart for risk management



business activities. This function is to ensure that reporting is carried out consistently, promptly and frequently.

The Bank systematically reports on risks for relevant business activities in order to be able to act in the event of changes in business developments, if required, and to ensure that the risks accepted are in accordance with resolutions adopted.

Risk management of core business activities, such as Credit and Holdings/Liquidity is carried out in close dialogue with the units in which banking operations are managed. The Bank's credit risk analysis function regularly follows up on guarantees, loans and credits in the Bank's branches, prepares risk analyses, and develops and maintains credit monitoring tools. Internal Risk Management and Control under the auspices of the Bank's Treasury Division (LIFI) performs regular monitoring of the Bank's compliance with section 152 of the Danish Financial Business Act, which stipulates a number of requirements for the Bank's liquidity, including stress tests. In addition, monitoring is to ensure compliance with instructions and guidelines covering counterparty and market risks. The Board of Directors receives monthly and quarterly reports on the extent of risks accepted for the period. Internal Risk Management and Control, and the credit risk analysis function refer directly to the Executive Management of the Bank, but also to the head of All Risk with regard to the routine risk reporting.

The Credit Department ensures compliance with the credit strategy as well as the credit policy and coordinates branch contact as well as credit advisory services for processing individual cases.

The Treasury Division ensures compliance with the investment strategy and coordinates branch contact and advisory services on complicated business transactions.

Operational risk is rooted in the individual business units and aims at ensuring procedures and measures are carried out immediately after ascertaining events which may trigger or have triggered operational risks. The Bank has systems to collect risk events of an operational nature which, other than reporting for managerial purposes, are used for continuous improvement of procedures and contingency plans.

The Bank's Financial Department follows up the operating financial developments arising from business decisions.

The funding of Arbejdernes Landsbank is primarily from deposits, which remain larger than the banks lending. In order to satisfy the banks objective for excess coverage of the liquidity requirement mentioned in the Danish Financial Business Act, Bank funding is supplemented by liquidity from domestic and foreign cooperation partners.

If exposures in new areas are under consideration, the nature and scope of these are discussed at the daily meetings of the Executive Management before a recommendation is made to the Board of Directors, either to enter into specific business or to adjust previously completed instructions.

Every endeavour is made to maintain up-to-date IT systems in order to be able to support risk management and quantify the size of risks to which the Group is exposed at any time.

Assessment of the effects of the total Group risks is carried out at least once a year in connection with preparation of proposals for the Board of Directors of the Bank on the annual budget, solvency need as well as stipulation of the level of adequate capital base.

Credit risk on loans to customers

Credit risk is the risk that a counterparty is wholly or partly unable to, or fails to make payments. The risk covers the entire spectrum, from a customer being unable to pay on time, to a customer ultimately being declared bankrupt. For each loan, the Bank must consider a customer's ability to meet his or her liabilities. The Bank enters into loan agreements with customers with the ability and willingness to make payments.

Credit risk is the largest risk item in the Bank's risk statement and amounted to 70% of the Bank's solvency requirement at the end of 2012 (69% at the end of 2011). The Bank has allocated the most funds to this item in order to meet unforeseen losses. Overall, the credit risks of the Bank have increased as a result of the current economic situation, and this is recognised in the Bank's solvency need. However, the quality of the loans is still deemed to be satisfactory, partly due to the large spread within the portfolio. The following is a description of the Bank's practice in the credit area and the composition of the loan portfolio.

Strategies and procedures to manage customer credit risks

The Bank provides all types of advice on loans, credits and guarantees for private customers, associations as well as small and medium-sized Danish enterprises. Today the Bank has a large private customer base and with "Vision 2015" it wants to instigate sustainable growth, particularly within the corporate customer area. In order to provide the best advice, it is a matter of course that the Bank has good insight into the overall financial situation of its customers. Insight into customers' finances is also necessary to enable assessment of the risks in the individual exposure.

The Bank's practice with regard to the Credit Department follows the guidelines in the Bank's credit policy and credit strategy to measure, manage and report credit risks. The credit strategy functions as a link between the Bank's credit policy and procedures and internal control and provides in-depth treatment of individual areas within the Bank's credit policy approach to customer exposures, sectors and portfolio composition. Approval by the Bank of a loan or credit is given on the basis of an assessment of the customer's financial ability and willingness to manage the repayment terms of the loan/credit. Approval of a loan is limited by authorities documented in authorisation instructions for individual employees for the respective lending areas. Authorisation to grant loans is built on a hierarchical framework so that larger exposures are always approved by the Credit Department and/or the Bank management.

Since 2010 the Bank has been using its own internally developed rating model to support the assessment of the risk of the individual customer exposure. The rating classes are objective credit rating classes and these are used as a control tool in regular monitoring of exposures. The rating is used as an indication of the extent to which the Bank wishes to expand its exposures with the relevant customer. The rating is based on point intervals where customers are awarded points on the basis of customer data and repayment behaviour. The rating classes are compatible with the credit rating categories of the Danish Financial Supervisory Authority (Danish FSA). Ratings classes are from 1-10, where rating 1 is the best and rating 10 is the poorest.

- Rating classes 1-3 are customers with exposures of good credit quality
- Rating class 4 are customers with exposures of normal credit quality
- Rating classes 5-8 are customers with exposures that require stricter monitoring, and where customers should only to a very limited extent be allowed to take up more loans
- Rating classes 9-10 are customers with poor credit rating. These customers are partly written down

Regardless of the customer's rating class, each credit decision, whether it is a new loan or a reassessment of an existing loan, will always be based on the Bank's overall assessment of the customer. Accordingly, individual credit ratings will always consist of an objective and a subjective part. The basis for the decision depends on the type, scope and complexity of the loan.

The risk environment

- Changed write-down regulations and new EU requirements for extra capital for banks entail stricter requirements for capital and earnings.
- The American housing market is picking up, and China and Brazil are again making steps to stimulate their economies. This can provide hope for a fledgling positive effect for the Danish economy, in which house prices around the large cities have increased slightly since Q2 in 2012.

- The tax packages have provided the majority of Danes with better financial flexibility, and the release of early-retirement pension contributions has increased liquidity. The extra money has mainly been placed as deposits in banks and/or used to repay debt. Consequently, companies with solid financial resources will be strengthened whilst those without solid financial resources will have even more difficulties.
- The prospects of continued slow growth and slightly increasing unemployment have a negative impact. These factors are making private households as well as enterprises cut down on consumption. Although house prices around the large cities seem to have improved slightly, recent years' strong falls have eroded equity in property, and households' excessive spending can no longer be refinanced. Many households are technically insolvent and with the expiry of the interest-only loans for many households as well as banks' stricter requirements for disposable income, the financial flexibility of many households will be reduced considerably in the years to come.
- Even though the variable interest rate is historically low, even a modest increase in this would be a threat to the financial stability of households. Increasing interest rates could influence the ability to repay loans, and thereby give rise to several defaults in the loan portfolio.

In 2012, the number of bankruptcies in Denmark were on a par with 2011 and is expected to remain unchanged in 2013. Even incipient economic progress in 2013 will hardly affect the trend in bankruptcies, which typically reacts with some delay. The number of compulsory sales increased slightly in 2012 compared with 2011, but remains at a low level in relation to the general socio-economic situation, and this is due to the low level of interest rates. The number of compulsory sales is expected to remain stable in 2013. The prospect of slightly increasing unemployment and continued uncertainty regarding the housing market are pulling developments in a negative direction, whereas the continued low level of interest rates is helping keep down the number of compulsory sales. Unemployment has been somewhat stable since 2010, and has not increased significantly in 2012, but is expected to increase slightly in 2013.

Increasing unemployment is a direct threat to the ability of private borrowers to repay their loans and an indirect threat to individual companies' ability to pay because, all else being equal, demand will drop off. In contrast, historically low interest rates and several tax packages are giving a large number of private customers better financial flexibility.

The Bank expects the negative socio-economic development to continue affecting the credit quality of our loan portfolio negatively, but not quite as seriously as in 2012.

The Bank's total exposure, expressed as gross loans and guarantees, as presented in the 2012 Financial Statements, has increased by about DKK 1 bn. compared with the end of 2011.

Table 1
The Bank's loans and guarantees before and after write-downs broken down by main customer segments

	Private 2012 DKK '000	Corporate 2012 DKK '000	Total, Bank 2012 DKK '000	Total, Bank 2011 DKK '000
Loans and guarantees				
Loans before write-downs	11,266,180	7,498,133	18,764,313	17,800,660
Guarantees before write-downs	924,787	1,131,949	2,056,736	2,016,353
Total loans and guarantees before write-downs, etc.	*12,190,967*	*8,630,082*	*20,821,049*	*19,817,013*
Individual write-downs on loans	446,871	582,264	1,029,135	799,650
Group write-downs on loans	34,854	13,153	48,007	52,892
Individual provisions for guarantees	590	3,960	4,550	5,566
Group provisions for guarantees	1,038	3,641	4,679	4,259
Total loans and guarantees after write-downs, etc.	*11,707,614*	*8,027,064*	*19,734,678*	*18,954,646*

Note: The figures are excluding loans to credit institutions. The breakdown into the "Private" and "Corporate" customer segments is based on the Bank's internal customer groupings. "Corporate" is including associations.

Among other things, this is due to increased activity in/and loans to the Bank's subsidiary, AL Finans A/S, and actual growth in loans by the Bank. Net loans and guarantees at the end of 2012 have also increased as a consequence of the increased gross exposure. However, this increase has been limited by the increased write-downs and provisions in 2012, see table 1.

The Bank's portfolio has been organised in the main segments "Private" and "Corporate" and the breakdown follows the Bank's own criteria. Total gross loans and guarantees continue to be assessed as having satisfactory credit quality with a sound risk-spread in which 69% of gross loans and guarantees are in rating classes 1-4, which is at par with the end of 2011. Therefore, the total portfolio has only been slightly affected by the negative general economic development, see tables 2 and 3.

Historically, the Bank's private portfolio has been relatively large compared with its corporate portfolio. At the end of 2012 the private portfolio accounted for 59% of the total loan volume. Viewed separately, the private as well as the corporate portfolio have a solid risk spread, in which 66% and 72% of gross loans and guarantees are in rating class 1-4, see tables 2 and 3.

Table 2
The Bank's loans and guarantees broken down by main customer segments and rating classes

	Private 2012 DKK '000	Corporate 2012 DKK '000	Total 2012 DKK '000
Rating			
1	325,822	1,141,117	1,466,939
2	707,016	1,219,148	1,926,164
3	1,793,894	974,612	2,768,506
4	5,217,967	2,897,842	8,115,809
5	1,996,717	380,213	2,376,930
6	939,165	265,024	1,204,189
7	358,135	175,704	533,839
8	94,029	324,948	418,977
9	485,955	1,072,626	1,558,581
10	272,267	178,848	451,115
Total	*12,190,967*	*8,630,082*	*20,821,049*

Note: The calculation is based on gross loans and guarantees. The break-down into the "Private" and "Corporate" customer segments is based on the Bank's internal customer groupings. The figures are excluding loans to credit institutions.

The Bank's loan portfolio is further described below, whereas write-downs and provisions are described in "write-downs and provisions analysed by loans and guarantees", see page 21.

Table 3
The Bank's loans and guarantees broken down by main customer segments and rating classes

	Private 2011 DKK '000	Corporate 2011 DKK '000	Total 2011 DKK '000
Rating			
1	62,771	999,509	1,062,280
2	742,833	801,441	1,544,274
3	1,836,780	821,330	2,658,110
4	4,967,644	2,958,878	7,926,521
5	2,047,539	709,279	2,756,817
6	1,042,972	328,289	1,371,260
7	384,201	261,851	646,051
8	143,356	7,368	150,724
9	418,423	843,460	1,261,883
10	247,101	191,991	439,092
Total	*11,893,619*	*7,923,394*	*19,817,013*

Note: The calculation is based on gross loans and guarantees. The break-down into the "Private" and "Corporate" customer segments is based on the Bank's internal customer groupings. The figures are excluding loans to credit institutions.

Largest customer credit risks

The Bank focuses on avoiding concentrations of risk, and Group credit policy is to minimise the risk of large single exposures.

The financial ratio "Sum of large exposures", i.e. the sum of section 145 exposures after deductions, greater than or equal to 10% of the capital base, is calculated at 92.2% of the capital base at the end of 2012 at group level, including loans to credit institutions. This corresponds to an overall exposure totalling DKK 3.4 bn. which is at a par with the end of 2011.

The sum of large exposures excl. credit institutions, which individually exceed 10% of the Bank's capital base, was reduced to 35.3% in 2012, broken down by four exposures.

Based on a risk perspective, this is an improvement compared to the end of 2011, when the sum of large exposures excl. credit institutions accounted for 54%.

These exposures are in the intervals 10-18% of the Group's capital base, and have been established after a thorough evaluation of whether there is acceptable risk and collateralisation.

For more information on credit institutions, see "Credit risk on credit institutions" on page 20.

Sum of large exposures

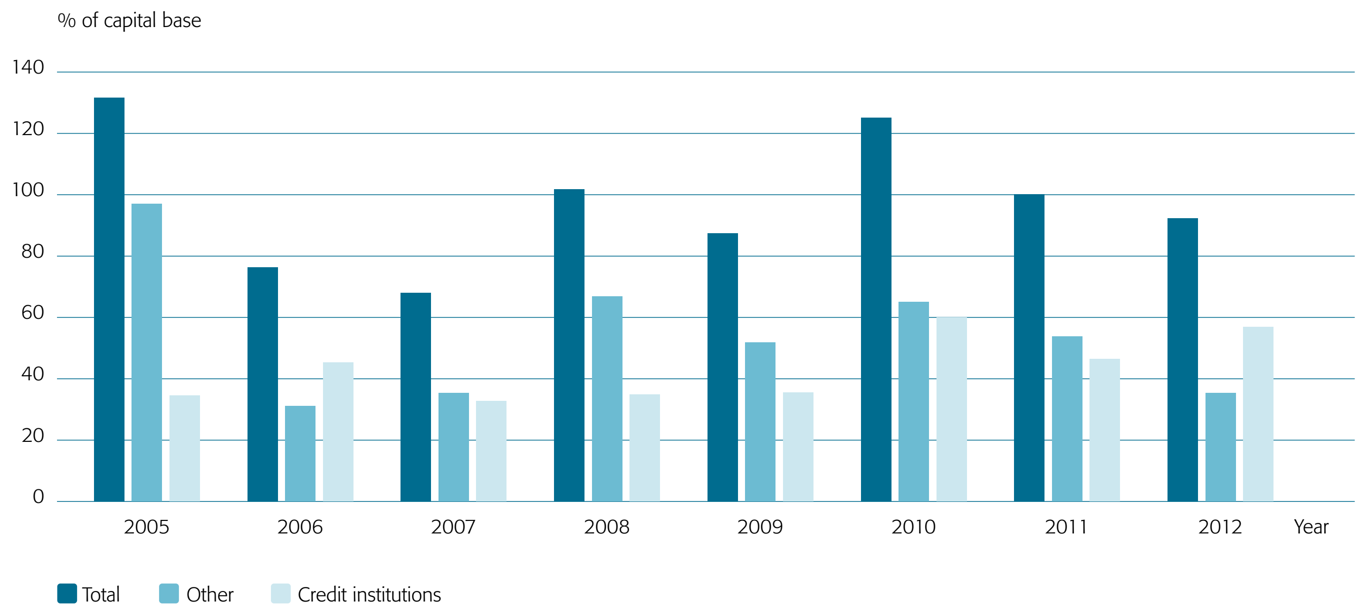
The Bank tries to keep exposures after deductions of 10% or more of the Bank's capital base at a low level. The Bank's current and previous large loans have primarily been loans to credit institutions, see figure 2.

Exposures over DKK 10 mill.

Main customer exposures over DKK 10 mill., excl. credit institutions and loans to the Bank's subsidiaries, account for 26% of total gross loans and guarantees at the end of 2012. Lending is broken down by 110 main customers. Main customer exposures of more than DKK 100 mill. account for the largest share, amounting to 17% of the Bank's total loan portfolio, see table 4. Impairment of main customer exposures of more than DKK 10 mill. is mainly a result of individual write-downs on already known risks. Arrears are mainly limited to main customers with exposures of less than DKK 50 mill. Arrears on exposures between DKK 10 mill. and DKK 50 mill. account for a total of 31% of the Bank's overall arrears at the end of 2012. This is an improvement of five percentage points compared to the end of 2011. The breakdown on gross loans and guarantees, write-downs and arrears on main customer exposures of more than DKK 10 mill. is shown in table 4.

The Bank's large exposures are focused in the sectors "Finance and Insurance", "Real Property" and "Other Corporate", see table 5. It should be noted that the Bank's exposure to large cooperative housing associations is included in the category "Real Property". A total of 65% of the loan portfolio on main customer exposures of more than DKK 10 mill. belongs to single customers in rating classes 1-4 and credit quality is therefore generally considered good, see table 5.

Figure 2
Development in the financial ratio "Sum of large exposures"



Note: The figures are calculated on the basis of reported values of section 145 exposures greater than or equal to 10% of the capital base after deduction and follow all relevant legislation.

Table 4
Gross loans and guarantees, write-downs and arrears analysed by section 145 exposures of more than DKK 10 mill.

	Gross loans and guarantees DKK '000	Write-downs on loans DKK '000	Arrears DKK '000	Number of section 145 customers
Section 145 exposure intervals, end-2012				
DKK 10 - 25 mill.	652,268	113,230	12,183	55
DKK 25 - 50 mill.	820,096	135,282	15,781	29
DKK 50 - 100 mill.	431,235	2,895	71	9
> DKK 100 mill.	3,438,509	307,818	653	17
Total	*5,342,108*	*559,225*	*28,688*	*110*

Note: Write-downs include the sum of individual and group write-downs and provisions. Arrears are calculated as in the notes to the financial statements on page 55. The figures are excluding loans to credit insitutions and loans to the Bank's subsidiary companies.

Table 5
Section 145 exposures of more than DKK 10 mill. analysed by sectors and rating classes

	Rating 1-4 DKK '000	Rating 5-8 DKK '000	Rating 9-10 DKK '000	Total DKK '000
Sector breakdown, end-2012				
Public authorities	21,681	41,943	13,036	76,660
Corporate				
Agriculture, hunting, forestry and fisheries	0	31,909	0	31,909
Industry and extraction of raw materials	129,360	2,741	2,856	134,957
Energy supply	0	1	2	3
Building and construction	127,644	142,213	55,073	324,930
Trade	244,678	20,473	23,156	288,307
Transport, hotels and restaurants	173,778	107,858	23,354	304,990
Information and communication	4,000	0	6,741	10,741
Financing and insurance	903,597	102,781	170,728	1,177,106
Real property	512,693	212,773	762,578	1,488,044
Other corporate	1,291,686	33,430	61,843	1,386,959
Total corporate	*3,387,436*	*654,179*	*1,106,331*	*5,147,946*
Private	64,326	2,412	50,764	117,502
Total	*3,473,443*	*698,534*	*1,170,131*	*5,342,108*

Note: The calculation is based on gross loans and guarantees. The sector breakdown is in accordance with section 93 of the Danish Executive Order on Financial Reports for Credit Institutions and Investment Firms, etc. and is allocated to single customers included in section 145 exposures > DKK 10 mill. CPR-customers (Civil Registration System) with sector code are classified under the sectors for "Corporate", and therefore the table is not comparable to the Bank's internal customer grouping into "Private" and "Corporate". The figures are excluding loans to credit institutions and excluding loans to the Bank's subsidiary companies.

Customer credit risks broken down by segment

The overall credit risk is managed in accordance with policies and frameworks adopted and stipulated by the Bank's Board of Directors and Executive Management. The Bank's Credit Department establishes procedures and internal controls, as well as authorisation guidelines on implementation of policies and frameworks for risk and collateralisation in day-to-day credit management.

Credit authorisation is delegated so that most decisions regarding private customers can be made by the individual branches. Large and particularly complicated credit relations are dealt with in close cooperation with the Credit Department.

Figure 3 below shows the Bank's exposure on significant customer segments, measured as gross loans and guarantees at the end of 2012. The Bank is characterised by holding a lower share of "Corporate customers", a higher share of "Private customers with cooperative property" and a higher share of "Associations etc." than comparative banks. The breakdown of the portfolio is largely unchanged compared with the end of 2011.

Private customers

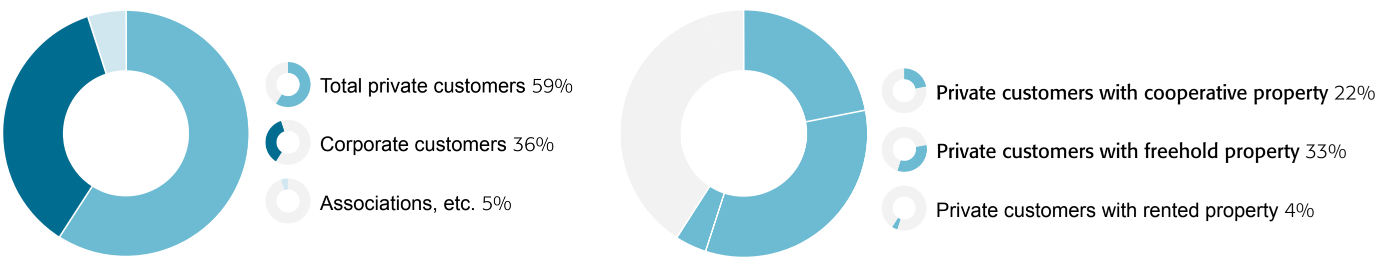
The exposures to "Private" are characterised by a considerably wider spread as well as significant collateral, see tables 6 and 7. This means that individual losses can be considered insignificant unless there is a large number of simultaneous losses, such as in the event of a serious recession in the entire economy.

Creditworthiness of private households is assessed on the basis of the customer's rating and an individual assessment of the customer's general financial situation, job situation, age, etc. The assessment is based on the customer's pay slips, annual tax returns, account behaviour, budgets and knowledge about the customer, which all provide an overall view of the customer's financial situation.

In view of unemployment developments, in future the Bank will continue focusing on e.g. private customers who despite tax cuts and low interest rates still have problems paying off their debt, and customers who will not be able to satisfy their repayment obligations in the event of interest-rate rises. Furthermore, focus is on the private customers with loans on which the non-repayment period will soon expire.

The exposure to the Bank's private customers is further broken down by customer segments, depending on the debtor's status on the housing market, see tables 6 and 8. Each of the three customer segments, "Customers with freehold property", "Customers with cooperative property" and "Customers with rented property" are managed according to separate guidelines as the terms of the loans,

Figure 3
The Bank's loan portfolio broken down by customer segment measured by gross loans and guarantees at the end of 2012



Note: The breakdown on the main segments "Private" and "Corporate" is based on the Bank's internal customer groupings, and accordingly "Corporate" is broken down as "Corporate customers" and "Associations, etc.". Public authorities are included in the group "Corporate customers".

Table 6

Gross loans and guarantees, net loans and guarantees, collateral, unsecured part and arrears analysed by the private customer segments “Freehold property”, “Cooperative property” and “Rented property”

	Freehold property DKK ‘000	Cooperative property DKK ‘000	Rented property DKK ‘000	Total DKK ‘000
End-2012				
Gross loans and guarantees (before write-downs, etc.)	6,836,098	4,470,401	884,468	12,190,967
Net loans and guarantees (after write-downs, etc.)	6,470,416	4,410,307	826,891	11,707,614
Collateral	2,707,749	3,655,244	168,397	6,531,390
Unsecured part (%)	58%	17%	80%	44%
Arrears	32,030	7,374	3,919	43,323
Arrears in % of total arrears	36%	8%	4%	48%
Total loan rate	33%	22%	4%	59%

Note: Write-downs include individual and group write-downs and provisions. Arrears are calculated as in the notes to the financial statements on page 55.

Table 7

Net loans and guarantees for the private customer segment broken down by exposure intervals and rating classes

	Rating 1-4 DKK '000	Rating 5-8 DKK '000	Rating 9-10 DKK '000	Total DKK '000
Exposure intervals, end-2012				
DKK 0 - DKK 500,000	2,843,398	1,467,094	91,943	4,402,435
DKK 500,000 - 2,000,000	4,530,226	1,655,319	153,372	6,338,917
DKK 2,000,000 - DKK 4,000,000	447,158	157,534	32,300	636,992
DKK 4,000,000 - DKK 10,000,000	158,118	79,849	22,834	260,801
DKK 10,000,000 - DKK 25,000,000	58,797	0	9,672	68,469
> DKK 25,000,000	0	0	0	0
Total	***8,037,697***	***3,359,796***	***310,121***	***11,707,614***

Note: The calculation is based on net loans and guarantees.

Table 8

Gross loans and guarantees analysed by the private customer segments “Freehold property”, “Cooperative property” and “Rented property” and rating classes

	Rating 1-4 DKK '000	Rating 5-8 DKK '000	Rating 9-10 DKK '000	Total DKK '000
Private customer segments, end-2012				
Freehold property	4,586,507	1,692,038	557,553	6,836,098
Cooperative property	3,192,504	1,152,563	125,334	4,470,401
Rented property	265,688	543,445	75,335	884,468
Total	***8,044,699***	***3,388,046***	***758,222***	***12,190,967***

Note: The calculation is based on gross loans and guarantees.

behaviour and risks in the segments are different. The segments "Freehold property" and "Cooperative property" account for 55% of the Bank's overall loans at the end of 2012. The Bank's collateral for the private segment mainly consists of mortgages in real property; however, despite previous years' negative trends on housing markets and more cautious valuation by the Bank, the unsecured part in the private segment is still at a satisfactory level.

Breakdown on the three private customer segments by gross loans and guarantees, net loans and guarantees, collateral, unsecured part and arrears is shown in table 6.

A. Customers with freehold property

Exposures to private customers owning freehold property amounted to 33% of the loan portfolio measured by gross loans and guarantees at the end of 2012, see figure 3. Equity in freehold property has fallen as a result of previous years' falling freehold property prices, and a more cautious assessment by the Bank has increased the unsecured part. The unsecured part is still at a satisfactory level.

The number of weakly financed or technically insolvent home owners, who cannot sustain a significant drop in income, is limited to owners who have not been on the housing market for very long in the parts of the market where prices have fallen the most and/or owners who are highly geared, possibly due to excessive consumption. There is only a relatively modest proportion of this type of customer because of the good spread in the portfolio of customers owning freehold property as well as the low interest rate. Further to this, losses typically only occur when customers are forced to sell properties.

The Bank provides loans against collateral in the financed asset. In this connection, please note that generally the Bank does not get involved in speculation based on mortgaging real property.

Cessation of the non-repayment period for interest-only loans, significantly increasing unemployment for a long period and/or a long-term interest-rate increase are assessed to be the largest risks in this segment, as a large number of the customers have floating-rate loans. However, a large proportion of the floating-rate loans has an interest ceiling. The significantly falling and now historically low interest rates are expected to compensate for any income drops in this customer segment. Repayment discipline for customers with freehold property was more or less unchanged in 2012 compared to 2011. Seen in the light of the general socio-economic development, this is attributable to continued low interest rates, tax cuts as well as the repayment of early-retirement pension contributions. The credit quality of this segment is considered good and this is underpinned by the fact that 67% of gross loans and guarantees in the freehold property segment were in rating classes 1-4 at the end of 2012, see table 8.

B. Customers with cooperative property

Exposures to private customers with cooperative property are due to a legislative amendment in 2005 which makes it possible to take out a mortgage in cooperative property. The Bank's focus on this area meant that the share increased to 22% of the total portfolio, measured as gross loans and guarantees, see figure 3. This percentage of the total portfolio is comparable with the end of 2011, but given that the Bank saw overall growth in loans in 2012, in real terms there has been continued growth in loans in the cooperative property segment. The Bank's expectations for 2013 are continued growth in the housing area, including in the cooperative property segment.

The market for cooperative housing is less transparent than that for freehold housing. Therefore, as at 1 November 2012 the Danish Association of Chartered Estate Agents introduced new regulations for what the description and particulars of sale for a cooperative property must contain with a view to helping potential buyers of cooperative property when they are to navigate in the cooperative property market. However, there are still significantly differing price-setting practices among cooperative housing associations, which is why changes in prices continue to be difficult to assess. The drop in prices seen from 2008-2012 has lagged behind that seen for owner-occupied flats and houses. The portfolio of loans for cooperative property at Arbejdernes Landsbank is deemed to be relatively resilient and less sensitive than the freehold property segment, despite its concentration in the Greater Copenhagen region. This is because of individual assessments of the individual cooperative housing associations in the Bank's portfolio. In general, this involves the Bank choosing more cautious valuation principles when setting the maximum statutory value of a cooperative share. The disproportionate weight of loans in older housing stock further reduces risk compared with, e.g. loans for new building and freehold properties.

In order to reduce the risk on this segment, the Bank has developed special business procedures and tools to assess the financial situation of private borrowers as well as the financial situation of the underlying cooperative housing associations. The valuation is tested using comparisons with the prices of similar cooperative housing in the same area. Furthermore, valuations are compared with prices per square meter of freehold property in the same area and similarly gross/net payments are compared with comparable freehold residences. In connection with the valuation of cooperative housing, there is a requirement that both prices per square meter and gross/net payments are as a minimum 20% less than comparable freehold residences.

Repayment discipline for 2012 improved slightly compared with 2011. The cooperative property segment has the lowest arrears percentage measured in relation to the segment's share of lending, see table 6. Arrears in this segment account for just 8% of the Bank's overall arrears and just 0.2% of the overall loans for cooperative property. In 2012 the cooperative property segment saw slightly falling market values and consequent slight increases in the unsecured part. The credit quality of the cooperative property segment continues to be assessed as good, which is also reflected in the rating, where 71% of gross loans and guarantees in the segment are in rating classes 1-4 at the end of 2012, see table 8. This is an improvement compared with the end of 2011, where 68% of gross loans and guarantees in the segment were in rating classes 1-4.

C. Customers with rented property

Exposures to private customers with rented property amounted to 4% measured by gross loans and guarantees at the end of 2012 are therefore relatively less significant than for the freehold property and cooperative property segments.

Clearly this segment has not experienced the same drop in wealth as the freehold property market, but neither has it benefited from the massive increases in the value of freehold housing in previous years. Typically, loans to this segment are not as large as for the two other groups, and therefore interest-rate sensitivity is generally not as pronounced. Repayment discipline improved in 2012 and the arrears percentage measured in relation to the segment's gross loans and guarantees has improved. Uncertainty remains regarding the extent to which a rise in unemployment in 2013 will affect this segment. The credit quality in the segment is less good; 70 per cent of gross loans and guarantees at the end of 2012 are in rating classes 5-10, see table 8.

Corporate customers

Exposure to corporate customers is limited in comparison with banks of a similar size.

In "Vision 2015", the Bank's strategy is to create sustainable growth within the corporate customer area. The corporate segment accounts for 36% of total gross loans and guarantees at the end of 2012, see figure 3, and this is an

Table 9
Gross loans and guarantees, net loans and guarantees, collateral, unsecured part and arrears analysed by corporate customer segments "Corporate" and " Associations"

	Corporate DKK '000	**Associations** DKK '000	**Total** DKK '000
End-2012			
Gross loans and guarantees (before write-downs, etc.)	7,516,729	1,113,353	8,630,082
Net loans and guarantees (after write-downs, etc.)	6,967,199	1,059,865	8,027,064
Collateral	1,286,246	434,641	1,720,887
Unsecured part (%)	82%	59%	79%
Arrears	24,568	21,117	45,685
Arrears in % of total arrears	28%	24%	52%
Total loan rate	36%	5%	41%

Note: Write-downs include individual and group write-downs and provisions. Arrears are calculated as in the notes to the financial statements on page 55. The figures are excluding loans to credit institutions.

improvement of two percentage points compared with the end of 2011, mainly in rating groups 1-4, see tables 2, 3, 10 and 11. Apart from a few larger corporate exposures, the segment is characterised by a large number of small and medium-sized, primarily owner-managed, enterprises. There is also a good spread between sectors, see sector breakdown at Group level in table 19.

According to "Vision 2015", the Bank's strategy is to increase lending to smaller and medium-sized enterprises; primarily owner-managed enterprises. The Bank's policy is that a significant part of corporate exposures must be covered by collateral in the assets of the company, possibly supplemented with personal guarantees from the business owner. Growth in loans in the corporate segment has contributed positively to this, as the overall unsecured part has dropped despite more cautious valuations and assessments of unsecured amounts. Several years ago, the Bank decided to limit lending to enterprises which are dependent upon changes in the property market, and the Bank's policy is not to engage in financing projects with no advance guarantees of the necessary operating income to service the total indebtedness. The Bank wishes only to participate in financing business which the Bank understands and is able to manage in relation to advisory services, and where the risk profile matches the Bank's credit policy. As a general rule, the Bank's policy is also not to lend to fisheries and agriculture, as well as sectors and enterprises with which the Bank does not want to be compared in terms of ethics and politics.

Creditworthiness is assessed on the basis of a review of an enterprise's ability to manage its debt commitments. The basis for approval includes the rating and strength profile of the enterprise. The basis for processing and managing corporate customer exposures is described in the internal business procedures. Typically the assessment is based on the Bank's philosophy, financial statements, budgets, business plans and insights into the business owner's private financial situation. The Bank's credit policy prepares the ground for corporate exposures to also be based on full customer relationships, including exposures of the Bank to the owner personally. This is done in order to provide the best possible advice, but also to maintain best overall financial insight into the Bank's exposures with customers.

Repayment discipline in the corporate segment has improved since the end of 2011. Arrears in the segment account for 28% of the Bank's total arrears, which is an improvement of six percentage points and considerably below the lending share of the segment of 36%, see table 9. This is primarily attributable to the fact that the Bank's smaller corporate customers are not as affected by the negative societal developments, as has been the case in previous years.

Continued decreasing demand is still assessed to be the largest risk in this segment, as failing sales will typically lead to liquidity pressure on the enterprise, which is intensified by customers' increasing difficulties to pay. The credit rating continues to be good; at the end of 2012, 72% of the segment's gross loans and guarantees are in rating classes 1-4, see tables 10 and 11.

Table 10
Net loans and guarantees for the corporate customer segment analysed by exposure intervals and rating classes

	Rating 1-4 DKK '000	**Rating 5-8** DKK '000	**Rating 9-10** DKK '000	**Total** DKK '000
Exposure intervals, end- 2012				
DKK 0 - DKK 500,000	49,206	132,424	9,727	191,357
DKK 500,000 - DKK 2,000,000	166,945	203,061	20,324	390,330
DKK 2,000,000 - DKK 4,000,000	200,310	97,021	19,440	316,771
DKK 4,000,000 - DKK 10,000,000	235,384	127,176	39,405	401,965
DKK 10,000,000 - DKK 25,000,000	396,526	231,779	50,562	678,867
> DKK 25,000,000	5,175,484	346,585	525,705	6,047,774
Total	*6,223,855*	*1,138,046*	*665,163*	*8,027,064*

Note: The calculation is based on net loans and guarantees. The figures are excluding loans to credit institutions.

Associations etc.

As a result of its basic philosophy and historical foundation, the Bank has a certain exposure to associations, including trade unions and charitable housing companies. Therefore, the Bank has specialist experience in credit assessment of these segments. The Bank has worked regularly on strengthening cooperation with associations and has come significantly closer to decision-makers in the associations. The basis for approval includes the individual association's foundation and articles of association, its assets and collateral, as well as its operations and management.

The exposure to associations accounted for 5% of total gross loans and guarantees at the end of 2012, see figure 3. Generally, it is a small but not insignificant part of the portfolio of costumer loans characterised by a relatively good spread. Repayment discipline in the associations segment worsened in 2012, and arrears in this segment accounted for 24% of the Bank's total arrears. Moreover, the unsecured part increased to 59%. The worsening of the situation is mainly attributable to the Bank's lending to cooperative housing associations, where there has been a degree of deterioration. The credit rating of the portfolio continues to be good; 71% of the segment's gross loans and guarantees are in rating classes 1-4, see tables 10 and 11.

Table 11

Gross loans and guarantees analysed by the corporate segments "Corporate" and "Associations" and rating classes

	Rating 1-4 DKK '000	**Rating 5-8** DKK '000	**Rating 9-10** DKK '000	**Total** DKK '000
Corporate customer segment, end-2012				
Corporate	5,442,827	896,066	1,177,836	7,516,729
Associations	789,893	249,822	73,638	1,113,353
Total	*6,232,720*	*1,145,888*	*1,251,474*	*8,630,082*

Note: The calculation is based on gross loans and guarantees. The figures are excluding loans to credit institutions.

Systems for risk reporting, measurement and monitoring

The basis for credit assessment is reassessed at least once a year, provided the exposure is more than a specific limit. In practice the basis is often updated more frequently, for example in connection with ongoing contact with customers.

Each quarter, the Board of Directors reviews the developments in the loan portfolio, providing a brief summary of the most significant risks and focus areas as well as a report describing developments in the most recent quarters. The report includes detailed break-downs of balances, general levels of overdraft, 90-day overdrafts, lending segments, sectors, migration between rating classes, etc. In addition, each month the Board of Directors reviews the developments in the Bank's monthly balance sheet and loans granted over a certain amount.

The quality of the overall portfolio is also assessed during the annual review of assets by the Credit Department, and during the subsequent presentation of the review to the Board of Directors and the Bank's internal and external auditors.

Customers with objective evidence of impairment (OEI) are mainly selected mechanically on the basis of selected criteria and the customer's rating class. All these customers are reviewed at least quarterly by their branch advisors in order to prepare action plans and make calculations/assessments of any need for write-downs. The Credit Department subsequently reviews the work of the branches.

Repayment discipline is monitored continuously using lists of overdrawn accounts, which are processed by advisors every day. Overdrafts of more than DKK 50,000 or DKK 10,000 and with a term of more than 90 days are assessed weekly by the branch manager and sent to the Bank's Credit Department. Using samples and lists of accounts in arrears, the Bank's Credit Department checks whether branches' action plans and follow-ups are adequate.

The Credit Department carries out ongoing credit reviews, where branches undergo an extraordinary review of their credit-weak customers and a physical review of the contents of their customer files. There is a fixed rotation arrangement, so that all branches are reviewed within a period of 3-4 years, and more often if prompted by statistical analyses.

Finally, credit monitoring is supported by ad hoc analyses on the basis of developments in the portfolio as well as fixed exercises such as calculations of quarterly solvency needs and quarterly assessments of the need for individual and group write-downs.

Loans in arrears

The Bank's net loans in arrears are focused on arrears with short duration, mainly in the private customer segment, see table 12.

Table 12
Loans in arrears analysed by age of the arrears and loan segment

	Freehold property DKK '000	Cooperative property DKK '000	Rented property DKK '000	Corporate DKK '000	Associations DKK '000	Total DKK '000
Days in arrears, end-2012						
1 - 30 days	527,767	440,852	56,186	441,406	62,384	1,528,595
31 - 60 days	37,828	24,622	5,292	20,017	173	87,932
61 - 90 days	20,866	11,804	3,731	227	5	36,633
91+ days	37,360	8,352	2,691	20,147	30,162	98,712
Total	*623,821*	*485,630*	*67,900*	*481,797*	*92,724*	*1,751,872*

Note: The calculation is based on the loans balance on customers in arrears, presented in the notes to the financial statements on page 55. The figures are excluding loans to credit institutions, but excluding the Bank's loans to subsidiary companies.

Table 13
Loans in arrears broken down by sectors and age of arrears

	1 - 30 days DKK '000	31 - 60 days DKK '000	61 - 90 days DKK '000	91+ days DKK '000	Total DKK '000
Sector breakdown, end-2012					
Public authorities	999	166	0	0	1,165
Corporate					
Agriculture, hunting, forestry and fisheries	3,710	6	55	265	4,036
Industry and extraction of raw materials	18,772	303	381	125	19,581
Energy supply	0	1	2	3	6
Building and construction	45,300	3,088	896	254	49,538
Trade	167,289	6,747	2,714	18,427	195,177
Transport, hotels and restaurants	34,266	3,355	1,126	1,910	40,657
Information and communication	15,328	222	1,673	8,741	25,964
Financing and insurance	129,017	10,092	0	5,030	144,139
Real property	74,551	0	0	30,600	105,151
Other corporate	162,177	2,830	331	7,126	172,464
Total corporate	*650,410*	*26,644*	*7,178*	*72,481*	*756,713*
Private	877,186	61,122	29,455	26,231	993,994
Total	*1,528,595*	*87,932*	*36,633*	*98,712*	*1,751,872*

Note: The calculation is based on the loans balance on customers in arrears, presented in the notes to the financial statements on page 55. CPR-customers (Civil Registration System) with a sector code are grouped under the sectors for "Corporate". The figures are excluding loans to credit institutions.

In terms of the sector breakdown for corporate customers, loans in arrears are mainly broken down by the sectors "Other corporate", "Real property", "Financing and insurance" and "Trade". Loans in arrears of more than 90 days are mainly related to a few overdrafts on individual large exposures. Loans in arrears totalled 9% of the Bank's total net loans at the end of 2012. Of this, loans more than 90 days in arrears accounted for 0.5%, see table 13.

The Bank has "early warning" lists, which are to reduce the number of customers with 90-day overdrafts. The Bank has an objective to reduce the level by finding lasting solutions to possible problems, collaboratively with the customer, rather than temporary solutions. This approach is expected to ensure that the number of customers on which the Bank will lose money is reduced in the long term. Arrears on loans of more than 90 days have increased compared to the end of 2011, and are largely concentrated on the sector "Trade", see table 13.

Policies to hedge and reduce customer risks

The Bank uses its possibilities to reduce risk by generally securing collateral in the items that it finances. The value of the collateral is calculated according to a prudence principle. This implies that, for reasons of prudence, some assets are calculated at a reduced value or the value 0, and

Table 14
The Bank's collateral for private customers

	Freehold property	Cooperative property	Rented property	Total 2012	Total 2011
	DKK '000	DKK '000	DKK '000	DKK '000	DKK '000
Collateral for private customers, end-2012					
Net loans and guarantees					
Properties	2,338,744	3,630,504	51,543	6,020,791	6,448,148
Securities, bonds, cash deposits, etc.	96,420	3,260	11,338	111,018	190,622
Cars	197,842	15,652	93,806	307,300	338,318
Warrents and guarantees	11,172	0	2,281	13,453	740
Other collateral	63,571	5,828	9,429	78,828	303,348
Total	***2,707,749***	***3,655,244***	***168,397***	***6,531,390***	***7,281,176***

Note: Calculated mortgaging values on collateral deposited according to the Bank's procedures.

Table 15
The Bank's collateral for corporate customers

	Corporate	Associations	Total 2012	Total 2011
	DKK '000	DKK '000	DKK '000	DKK '000
Collateral for corporate customers, end-2012				
Net loans and guarantees				
Properties	1,038,875	217,624	1,256,499	1,129,315
Securities, bonds, cash deposits, etc.	151,429	190,520	341,949	573,235
Cars	23,482	0	23,482	33,322
Warrants and guarantees	2,951	356	3,307	500
Other collateral	69,509	26,141	95,650	108,152
Total	***1,286,246***	***434,641***	***1,720,887***	***1,844,524***

Note: Calculated mortgaging values on collateral deposited according to the Bank's procedures.

therefore the real collateral value is significantly higher than the value calculated in tables 14 and 15.

An assessment of the value of the collateral is a significant factor in determining the Bank's risks. All large exposures are regularly reassessed and at least once a year on the basis of the customer's financial statements/accounts, budgets, business plan, etc. If the developments in objective indicators are assessed to warrant write-downs of the value of the exposures, write-downs are made according to regulations laid down for this purpose. Calculations of mortgaging values are based on the Bank's procedure for this. When assessing payment rows of exposures, collateral is calculated at estimated fair values.

- As far as possible, loans for private customers are hedged using different forms of collateral. This is usually by taking a registered mortgage deed in freehold and cooperative property. Moreover cars etc. are used as collateral.
- Loans to corporate customers in owner-managed (limited) companies (A/S and ApS) as a rule require full or part personal guarantees, supplemented by various forms of collateral.
- Loans to associations are frequently granted in return for collateral in the form of guarantees from members to pay fees, members accepting joint and several liability, or real collateral.

Furthermore, the Bank makes regular assessments of the value of the collateral calculated as the expected net proceeds on realisation. In each case of default, the Bank assesses whether compulsory realisation of collateral will best serve the Bank in relation to minimising the Bank's risk of losses. The economic cycle and market conditions for realisation of assets may vary considerably. Therefore, sometimes the Bank takes over assets which the Bank has set as collateral.

Broken down by types of collateral for private customers with freehold or cooperative property, properties make up the largest part of total collateral, see table 14 below.

The Bank does not use instruments such as credit default swaps or other types of insurance to hedge its risks on loans to customers.

Development of credit portfolio tools

Tools to measure and assess the Bank's credit risks are constantly being developed and improved. In recent years, the Bank's rating model has become an integrated part of credit management. The rating is an essential parametre in the selection of customers with objective evidence of impairment (OEI), and this rating is also an important part of both the Bank's model for solvency need and its model for group write-downs.

The Bank regularly focuses on improving data quality, as wrong or inadequate information may provide an incorrect basis for decision-making and possibly a misleading rating.

The Bank's branch management has further access to a number of quarterly and monthly reports which are to contribute to providing branch management with a better insight into the loan portfolio risk and thus enable them to identify any action areas.

Furthermore, the Bank is represented in projects with Bankernes EDB Central (BEC), including projects on management and monitoring of credit risks. Therefore, in 2012 the Bank implemented BEC's risk reporting tool and utilised the tool in selected areas. At the beginning of 2013, the tool will be further integrated, as the branches will have access to it as well. Moreover, the BEC is working on a cross-sectoral risk management tool to be used in sections 70/71 reporting.

Furthermore, in 2012 the Bank's Board of Directors was introduced to an automatically calculated credit barometer which measures credit quality objectively. The credit barometer can also be used as a benchmark for the individual solvency need.

Activities in AL Finans A/S

The activities of the subsidiary company, AL Finans A/S, are spread over three business areas

1. Car loans
2. Finance and operating leases, primarily automobiles
3. Factoring

AL Finans has no automatic rating or scoring systems to assess credit risks, but it has great experience within all the product-specific business activities.

Quarterly manual reviews are carried out of all customers with signs of weakness based on segments analysed by product. Once a year an active review is carried out in which credit risk is assessed for large exposures, and write-downs are made to the extent that there is objective evidence of impairment (OIE). The majority of all loans have collateral in the form of the underlying asset, for which there are public catalogues to assess the asset value.

Furthermore, as in 2011, for 98% of the car loans portfolio an initial payment of 20% or more has been made, see table 16. Automobiles are relatively easily valued and sold. Due to the current market imbalance, there will be an increased risk that assets will no longer cover the unpaid balance in the future. A total of 95% of the Bank's financed assets are automobiles, of which unsecured loans account for less than 1%. The credit quality is considered high and group write-downs on customers in arrears have fallen from 2009 to 2012.

Table 16
Breakdown of repayment percentage on car loans

	2012		2011	
	DKK '000	%	DKK '000	%
Repayment percentages on car loans				
0 - 9 %	23,781	2	26,250	2
10 - 19 %	8,131	1	7,943	1
20 - 29 %	1,095,433	76	790,962	76
30 - 39 %	180,919	13	132,980	13
40 - 99 %	107,086	8	80,312	8
Total	*1,415,350*	*100*	*1,038,447*	*100*

The risk on car loans and leasing is mainly related to whether the value of underlying assets can be realised at the values estimated when establishing the respective customer relationship, see the high collateral coverage in tables 17 and 18. One of the material risk factors in AL Finans A/S is therefore declining realisation values on cars in particular.

In 2012, prices of used small cars were pushed down by low prices for new small cars, while the situation was opposite for large cars. Overall prices for AL Finans are considered to be fairly stable. The current level of trading is considered realistic for the next half year. However, used car segments, in which AL Finans is exposed, may see further price reductions. This will mean risk for AL Finans on cars returned after leasing (operating agreements) and on cars returned after defaults on both leasing and loan payments. A change in the registration fee may also affect AL Finans and have immediate and negative consequences regardless of whether there is a long "transitional period".

In recent years, the number of cars returned has been falling, whilst the average loss per unit has been more or less stable. Car prices have stabilised and a large part of the portfolio has been replaced in recent years and is thus geared for new current prices. The level of returned cars as well as for average losses in 2013 is expected to be the same as in 2012.

There are two levels of repayment obligations in factoring. Debtor level is the first level, and if a debtor is unable to pay, then client level is the next level. In addition, claims are typically mortgaged by 80%, which in normal circumstances provides good cover for repayment obligations. Furthermore, a number of exposures have been hedged through guarantee insurance companies. Hedging amounts to about DKK 164 mill., corresponding to about 27% of outstanding debtor balances. Furthermore, the Bank has taken out crime insurance, which insures the entire Group against major losses due to fraud.

The exposures are broken down by the respective business activities in tables 17 and 18.

Table 17
Loans before write-downs and breakdown of collateral in the private portfolio in AL Finans

	2012			2011		
	Balance DKK '000	**Collateral** DKK '000	**Number of customers**	**Balance** DKK '000	**Collateral** DKK '000	**Number of customers**
Business activities, Private						
Car loans (debt instruments)	170,209	126,224	1,485	180,651	133,453	1,683
Car loans (purchase contracts)	1,182,638	1,146,311	11,286	945,518	935,421	9,104
Financial leasing	1,877	1,689	15	2,419	2,177	15
Operational leasing	5,802	5,222	43	4,108	3,702	32
Total	*1,360,526*	*1,279,446*	*12,829*	*1,132,696*	*1,074,753*	*10,834*

Note: Calculated mortgaging values of deposited collateral are according to the procedures for AL Finans. Note that in 2012 the principle in the breakdown in "Private" and "Corporate" has changed in AL Finans. The breakdown is now based on the Bank's internal customer groupings, and on the basis of this, the comparative figures for 2011 have changed.

Table 18
Loans before write-downs and breakdown of collateral in the corporate portfolio in AL Finans

	2012			2011		
	Balance DKK '000	**Collateral** DKK '000	**Number of customers**	**Balance** DKK '000	**Collateral** DKK '000	**Number of customers**
Business activities, Corporate						
Car loans (debt instruments)	13,003	11,882	78	13,508	11,644	113
Car loans (purchase contracts)	49,500	48,927	307	1,540	4,264	262
Financial leasing	359,745	323,770	1,056	360,232	324,883	1,024
Operational leasing	113,258	101,932	258	119,558	107,597	267
Factoring	612,131	612,131	186	448,136	448,136	200
Total	*1,147,637*	*1,098,642*	*1,885*	*942,974*	*896,524*	*1,866*

Note: Calculated mortgaging values of deposited collateral are according to the procedures for AL Finans. Note that in 2012 the principle in the breakdown in "Private" and "Corporate" has changed in AL Finans. The breakdown is now based on the Bank's internal customer groupings, and on the basis of this, the comparative figures for 2011 have been changed.

Credit risk on credit institutions

General conditions

The internal instructions on segregation of responsibilities ("*Instruks for arbejdsfordelingen mellem bestyrelsen og direktionen i A/S Arbejdernes Landsbank*") contain guidelines for managing counterparty risks as well as delegation of authority that the Executive Management may expose the Bank to credit risk on credit institutions and others.

In general the Bank adopts a tight practice for authorising exposures. In day-to-day trading, financial frameworks are only established with credit institutions known to the Bank. Authorisations of frameworks for Danish credit institutions are based on their most recent financial statements as well as the Bank's knowledge about the counterparty. Frameworks for foreign credit institutions are granted primarily to large first-class credit institutions. Authorisations of frameworks are also based on the same principles as mentioned above for Danish credit institutions.

Binding credit commitments

Arbejdernes Landsbank bases lending on business relationships, and as a point of departure credit is only granted to credit institutions having a natural cooperation potential with Arbejdernes Landsbank within other business areas.

In addition to obtaining knowledge about conditions relating to business counterparties, prior to entering into any commitment, the Bank carries out an analysis of the most recent interim financial statements, and the credit institution is interviewed on any issues arising. This analysis work is carried out by the Credit Department.

At least once a year, the Bank follows up all exposures and conducts a quality test for all exposures, often with a follow-up meeting with the counterparty. It is also routine practice that these credit institutions visit Arbejdernes Landsbank after publication of annual reports and provide more detailed information about developments.

Follow-up work is performed at management level in Arbejdernes Landsbank, and the Bank's Credit Department is involved in specific situations in order to complete a follow-up analysis of the previous decision base.

All those with contact to the credit institutions involved may have access to potentially market-sensitive information about the credit institution. These persons are primarily from the management group of the Bank and they are subject to more rigid internal regulations on transactions with the relevant credit institution using personal assets.

Ordinary undisclosed financial frameworks (credit lines)

This type of exposure with financial counterparties is mainly granted for trading, money market deposits and acquisition of bonds.

The exposures are granted on the basis of two main criteria:

A size criteria – whereby a credit line for credit institutions is measured according to objective criteria pursuant to internal instructions on segregation of responsibilities ("*Instruks for arbejdsfordelingen mellem bestyrelsen og direktionen i A/S Arbejdernes Landsbank*"). The size of a credit line is measured as both a specific percentage of Arbejdernes Landsbank's equity and as a percentage of the credit institution's equity.

A subjective assessment, whereby reviews of financial statements, market information, cooperation experience etc. are combined into a conclusion by the Bank's management.

Grants of credit lines to credit institutions are decided collaboratively between the head of the Credit Department and the Bank's Board of Directors and Executive Management.

Risk assessment

The risk on Danish credit institutions is assessed to be primarily on specific product receivables (share capital and capital base). As a starting point, the Bank's policy is not to provide loans in the form of capital base to credit institutions. On the basis of this, risk is assessed to be limited.

The Bank is exposed to credit institutions in other countries but the risk is assessed to be limited and capital provisions which the Bank deems necessary in a worst-case scenario have been made.

Write-downs and provisions on loans and guarantees

The Group's statement of impairment losses on receivables is pursuant to sections 51-54 of the Danish Executive Order on Financial Reports for Credit Institutions and Investment Firms, etc.

Write-downs and provisions and losses recognised in the income statement in 2012 amounted to DKK 286 mill. against DKK 217 mill. in 2011, see table 18 .

The calculations in tables 19 and 20 include credit institutions.

After this, Group accumulated write-downs and provisions amounted to DKK 1,121 mill. at the end of 2012 against DKK 894 mill. in 2011. Write-downs/provisions on the "Real Property" sector are related to individual large exposures of the Bank which are all monitored closely. The increase in write-downs and provisions is primarily due to the negative trends in the economic cycle as well as the Danish FSA's new regulations on write-downs which entered into force on 1 April 2012.

With expectations that the economic crisis will not affect the Bank's portfolio as much in 2013, the Bank expects the level of total write-downs and provisions to decrease considerably compared with 2012.

Table 19
Sector breakdown for impairment losses, including group write-downs and group provisions, at the end of 2012 (Group)

	Exposures DKK '000	Exposures which have been written down/provided DKK '000	Write-downs/ provisions DKK' 000	Write-downs/ provisions and losses recog-nised in 2012 DKK '000
Public authorities	96,563	21,998	10,738	-5,273
Corporate				
Agriculture, hunting, forestry and fisheries	63,333	14,211	1,016	-748
Industry and extraction of raw materials	693,510	181,317	9,488	-5,823
Energy supply	1,813	922	2	11
Building and construction	581,482	290,785	64,346	-1,547
Trade	1,097,853	476,160	67,616	-3,447
Transport, hotels and restaurants	592,005	299,541	49,867	-14,920
Information and communication	1,295,977	105,997	8,844	19,895
Financing and insurance	1,720,444	870,848	146,007	-36,812
Real property	1,493,121	1,163,839	281,635	-137,867
Other corporate	2,339,439	504,922	77,552	-4,552
Total corporate	***9,878,977***	***3,908,542***	***706,373***	***-185,810***
Private	11,998,654	4,799,913	403,602	-94,713
Total	***21,974,194***	***8,730,453***	***1,120,713***	***-285,796***

Note: CPR-customers (Civil Registration System) with a sector code are grouped under the sectors for Corporate.

Table 20
Changes in impairment losses on receivables (Group), 2012

	Individually written down, credit institution DKK '000	Individually written down loans and other items with credit risk DKK '000	Individually provided guarantees DKK '000	Group written down loans and other items with credit risk DKK '000	Group provided guarantees DKK '000
Accumulated write-downs/provisions brought forward	17,201	812,321	5,566	54,229	4,259
Write-downs/provisions carried forward	51	421,534	1,833	16,123	662
Reversal of write-downs	0	151,384	2,849	24,289	242
Other movements	0	19,835	0	2,518	0
Actual loss (written off) previously individually written down/ provided	0	56,654	0	0	0
Accumulated write-downs/provisions brought forward on loans and guarantee debtors	17,252	1,045,652	4,550	48,581	4,679
Actual loss (written off) not previously individually written down/provided	0	24,357	0	0	0
On previously written off claims	0	8,603	0	0	0

Note: The calculation is made according to note 13 in the financial statements.

Counterparty risk

Counterparty risk includes the Group's management of risks of losses on derivative financial instruments. Risks of losses on derivative financial instruments are included in the management of credit risk in both the authorisation process and in general exposure monitoring, see the relevant sections on this matter.

Table 21
Derivative financial instruments and spot transactions, end-2012

	Nominal value DKK '000	**Net market value** DKK '000	**Net market value** DKK '000	**Negative market value** DKK '000
Currency contracts				
Spot transactions, purchase	237,007	-564	52	616
Spot transactions, sale	252,398	-60	700	760
Forward transactions/Futures, purchase	314,048	-1,496	2	1,498
Forward transactions/Futures, sale	422,562	652	652	0
Options, acquired	199,885	702	702	0
Options, issued	30,879	0	0	0
Currency swaps	2,862,029	-35,359	0	35,359
Interest-rate contracts				
Spot transactions, purchase	369,833	21	95	74
Spot transactions, sale	392,872	-11	100	111
Forward transactions/Futures, purchase	663,328	1,182	1,263	81
Forward transactions/Futures, sale	7,748,487	-9,288	62	9,350
Options, issued	3,133,368	-6,218	0	6,218
Swaptions	0	0	0	0
Interest-rate swaps	4,297,753	-113,706	34,503	148,209
Share contracts				
Spot transactions, purchase	144,037	86	933	847
Spot transactions, sale	169,039	-534	488	1,022
Total	*21,237,525*	*-164,593*	*39,552*	*204,145*

The Bank does not apply netting in the statement of risks on items with counterparty risk.

Market risk

The Arbejdernes Landsbank Group regularly accepts various forms of market risk, primarily as interest-rate risk, share-price risk or currency risk, as well as securities-related credit risks in the form of investments in credit bonds.

Market risks arise partly as a result of servicing customers' needs and partly from the Bank's positions in financial instruments. The Bank utilises derivative financial instruments to manage and adjust market risks.

In general the Bank is prudent in the size of its exposure to market risk. The Bank puts high priority on managing business with market risk because of the increasing scope of its business in this area and the increasing complexity of a number of the products in recent years.

The current financial crisis has further underscored the need for active and tight management of this area.

Market risk covers positions, the market value of which depends on developments in the general levels of a number of market variables such as interest rates, share prices, and currency rates. Moreover, risks of a more specific nature on specific market securities are included, if these risks can be traded explicitly. The statement includes market risk on both balance-sheet items and non-balance-sheet items and calculations also include positions in the trading portfolio and business outside the trading portfolio which could have market risks.

Under normal market conditions, general market risks are determined by macroeconomics, national and international political conditions, etc., as well as actions by central banks, which are independent of the type of instrument and specific counterparties in a transaction.

Interest-rate risk is calculated on the basis of the modified duration and indicates the expected loss on positions with interest-rate risk in the event of a parallel change in the yield curve of 100 basis points. For convertible mortgage-credit bonds and bonds with an interest ceiling etc. correction factors issued by the Danish FSA and information obtained from leading market participants on modified duration are used. The calculations are made in the individual currencies and in duration intervals. The Bank's exposure is primarily in DKK interest.

Table 22
Group interest-rate risk at the end of the year

	2012 DKK '000	**2011** DKK '000
Broken down by modified duration (D)		
0 < D <= 3 mths.	15,454	14,888
3 < D <= 6 mths.	9,186	736
6 < D <= 9 mths.	2,590	4,362
9 < D <= 12 mths.	7,373	4,725
1 < D <= 2 years	54,088	34,519
2 < D <= 3.6 years	-98,687	-95,705
3.6 years < D	-24,960	44,458
Total	*-34,956*	*7,983*
Broken down by currency		
DKK	36,621	103,856
EUR	-76,264	-102,401
GBP	1,523	2,914
NOK	1,452	1,863
SEK	1,122	1,457
USD	610	213
Other currencies	-20	81
Total	*-34,956*	*7,983*

Interest-rate risk has been calculated for a change in interest rates of 100 basis points.

Share-price risk is the risk of losses as a result of changes in share prices. The share price risk covers the net position in shares as well as share-related instruments in the individual share or share index. The share-price risk is calculated as weighted positions across share instruments.

Sensitivity to general changes in the share markets is concentrated in the relatively small part of share holdings held in the trading portfolio, and the holdings are spread over as many companies as possible so that a general fall in the stock markets of 10% would lead to a loss of DKK 23.5 mill. However, investment securities are more specifically affected by developments in the individual companies, which cannot be assumed to be influenced correspondingly by market fluctuations.

Currency risk reflects the Bank's risk of losses on positions in currency as a result of changes in currency exchange rates. The risk is calculated in part according to the Currency Indicator 2 method, and in part as a weighted sum of net positions in the individual currencies, by which the weighting takes into account volatility.

Securities-related credit risks reflect the Bank's risk of losses as a result of changes in market demands for returns on credit bonds not attributable to general changes in the market interest rate, but which reflect changes in the market's pricing of credit bonds compared with instruments with significantly less credit risk. The Bank's portfolio of bonds issued by banks and enterprises amounted to 41% of the bond portfolio at the end of 2012, primarily issued in EUR and DKK. A modest part of bonds issued by banks is subordinated capital.

Management of market risks
The Group's overall market risk is managed centrally by the Treasury Division.

The Bank ensures distinct segregation of responsibility in risk-taking at all levels of the Bank through setting maximum authorization frameworks for both the Executive Management and the management of the Treasury Division. On the basis of this, narrower frameworks are delegated to the individual authorising employees in the Treasury Division.

The individual risk areas are monitored continuously in relation to the frameworks set. Daily follow-up on this is via reports to the Executive Management and there are regular reports to the Board of Directors. The Internal Risk Management department monitors how much of the individual frameworks are used by the position takers and reports directly to the Executive Management.

The Bank's market risks are a result of customer trading or arise from the Bank's position-taking on the basis of tactical and strategic assessments of market developments. Risks can also arise from consideration of the scope of the Bank's other business, including transactions with interest-rate risk, but outside the trading portfolio.

In order to be able to deal with customers' trading activities, the Bank has a holding of securities which cancels out the differences between the size of customer trading and standard transactions on the professional market.

The market risk linked to this is kept within well defined limits both in total and on the individual securities ID. These limits are included in the frameworks set by the Board of Directors and they are continually monitored. Reports are made to the Executive Management in connection with breaches.

Tactical, short-term investments are managed by the Bank's trading function within relatively narrow limits which are continually monitored.

Strategic positions are decided by the Executive Management on the basis of an assessment of potential returns compared with the risk involved, and taking into account the Bank's overall appetite for risk, other risks of the Bank, as well as ongoing maintenance of a liquidity resource in the form of liquid assets.

In addition to daily calculations of the Bank's total market risks according to standard key figures, stress tests of the holdings are also performed occasionally.

Liquidity risk

Liquidity risk is the risk of losses resulting from the Bank having to pay more for the liquidity required to cover its payment obligations and to maintain normal liquidity reserves in a situation where the Bank itself or the sector as a whole is affected by extraordinary circumstances. Liquidity risk thus reflects a mismatch in the Bank's balance between maturity of its assets and liabilities, where the loan portfolio generally has a longer duration than deposits and other financial transactions.

Most of the Bank's liquidity risk is in Danish kroner (DKK), while the rest of the risk is concentrated in the major currencies.

The Bank generally has a very prudent liquidity policy. The Bank has an objective to have excess liquidity of 100% in relation to the 10% and 15% stipulated in section 152 of the Danish Financial Business Act. Liquidity is monitored daily and at the same time assessed in a long-term perspective in relation to business developments at the Bank and in the capital markets, as well as levels of deposits and loans. The Bank also has a policy that liquidity forecasts, which are prepared at least once a month, must demonstrate similar excess cover for at least three months ahead, and there must be excess cover of at least 75% 12 months ahead.

In addition to regular calculation of the excess liquidity cover, occasional stress tests of the Bank's liquidity in the long term are carried out in order to reveal the Bank's sensitivity to significant changes in its ongoing terms of funding.

The Bank's Board of Directors has adopted a Financial Resources Plan which defines efforts to be launched if liquidity deteriorates relative to the adopted liquidity strategy.

Interest-rate risk outside the trading portfolio

The Bank's interest-rate risk arises to a certain extent outside the trading portfolio in the form of fixed-interest loans or deposits for customers or variable interest loan products with built-in option elements. Interest-rate risk is calculated using the same principles as for interest-rate risk within the trading portfolio.

The Bank has no fixed-interest deposits with indefinite maturity. Some loans are provided with fixed interest-rate with the possibility of early redemption.

The interest-rate risk is part of the Treasury Division's calculations of the Group's overall interest-rate risk and it is managed within set limits. This primarily concerns risk in DKK of short duration. A few, major transactions are hedged seperately in terms of interest-rate risk.

Shares etc. outside the trading portfolio

In cooperation with other banks, Arbejdernes Landsbank has acquired holdings in a number of sector companies. The object of these companies is to support the Banks' business within mortgage credit, IT, money transmission services and investment associations. The holdings are not included in the trading portfolio, as participation in the sector companies is very important for the Bank's goal of being able to offer customers a broad range of financial services at competitive prices.

Table 23
Shares outside the trading portfolio:

	2012 DKK '000	**2011** DKK '000
Fair value carried forward	631,915	765,225
Realised capital gains in the income statement	2,716	126
Unrealised capital gains in the income statement	16,832	8,705
Net purchase	-80	33,942
Other disposals*)	0	-167,378
Total fair value brought forward **)	***651,383***	***631,915***

*) In 2011 the Bank invested additional capital in Bankernes EDB Central (BEC). The investment has meant that the equity interest exceeds 20% and that the BEC can be grouped as an associate.
**) of which 367.6 mill. amount to more than 10% in the given company. This amount has been deducted in the Group's capital base, and 50%, corresponding to DKK 183.8 mill., has been deducted from the core capital.

Holdings in sector companies are unlisted and are valued at fair value.

Operationel risk

Table 24
Operational risk is the risk of losses because of

Type	Description
Internal fraud	Losses due to acts of a type intended to defraud, misappropriate property or circumvent regulations, the law or Bank policy, and which involve at least one Bank employee.
External fraud	Losses due to acts of a type intended to defraud, misappropriate property or circumvent the law, by a third party.
Employment practices and workplace safety	Losses arising from acts inconsistent with employment, health or safety legislation. Payment of claims arising from personal injury or from discrimination events.
Clients, products, and business practice	Losses arising from an unintentional or negligent failure to meet a professional obligation to specific clients, or losses arising from the nature or design of a product.
Damage to physical assets	Losses arising from loss or damage to physical assets from natural disaster or other events.
Business disruption and systems failures	Losses arising from disruption of business or system failures.
Execution, delivery and process management	Losses from failed transaction processing or process management.

Note: As a rule, operational risk can be linked to specific individual events.

The organisation

In order to assist the management at the Bank with matters relating to operational risk, work in this area is based in the following departments:

- Legal Department with regard to compliance.
- IT Department with regard to following up IT security and emergency plans for transferring operations. In this connection, note that the majority of the Bank's IT development and operations have been outsourced to Bankernes EDB Central (BEC) in Roskilde and JN Data in Silkeborg and thus BEC and JN Data deal with the operational risk on development and operations.
- HR Department with regard to physical security relating to personnel and buildings.
- The individual business areas with regard to their own exposures.

Tasks

All operational losses exceeding DKK 5,000 are reported and assessed by the individual business areas.

Reports from the Internal Audit department are dealt with by the Board of Directors and the Executive Management in relation to operational risk, with special focus on relevant areas.

Reports from public inspection authorities are processed by the Board of Directors and Executive Management.

Reports are made to the Executive Management in the event of critical exposures from individual business areas when the management of a business area deems that reporting and follow up are necessary.

Management information is prepared in the form of descriptions of IT security, compliance and contingency plans.

On the basis of reports on current losses data from business areas, the IT Department calculates total operational risk every quarter.

Business risk

Business risk is defined as the risk of losses from changes in external conditions which influence banks, or incorrect assessments of the consequences of strategies adopted.

The risk becomes apparent in unexpected falls in revenues or unexpected rises in costs.

Examples of reasons are:

- Fierce price competition arising from a drop in business volume or falling revenues on the existing volume of business
- Increasing product-development costs to match new products from competitors
- Increasing marketing and communication costs arising from negative press coverage
- Incorrect estimates of revenues from new activities

The Group continually assesses this type of risk, and always when setting the solvency need.

Property risk

Property risk is defined as the risk of losses on the portfolio of properties, arising from a general drop in property prices.

A/S Arbejdernes Landsbank has a portfolio of its own owner-occupied properties of DKK 573 mill. and investment properties of DKK 55 mill.

The properties are primarily used for the operation of the Bank. In addition, parts of individual properties are rented out as dwellings or as professional offices.

The properties are widely located throughout Denmark, although on the basis of carrying amount there is an overweight in Greater Copenhagen.

Owner-occupied properties are measured annually at 31 December to "revalued amount" which is the fair value on the date of valuation.

Investment properties are measured at fair value according to the returns method.

Consolidation

A/S Arbejdernes Landsbank

Consolidation includes the subsidiary companies,

AL Finans A/S
Handels ApS Panoptikon,

which are both fully owned by A/S Arbejdernes Landsbank. There are no differences between the consolidation bases for accounting purposes, and consolidation is in accordance with part 12 of the Danish Financial Business Act.

The activities of subsidiary companies are based on funding from the parent company.

ALKA Forsikring A/S and Foreningen Bankernes EDB Central (BEC) are associates. These companies are not part of the consolidation.

Capital base

Table 25
Calculation of Group capital base

	2012 DKK '000	**2011** DKK '000
Share capital	300,000	300,000
Reserves	476,160	360,865
Retained earnings	2,627,460	2,310,154
Core capital	*3,403,620*	*2,971,019*
Proposed dividend	105,000	24,000
Intangible assets	11,897	10,992
Deferred tax assets	10,887	58,482
Core capital after primary deductions	*3,275,836*	*2,877,545*
Hybrid core capital	392,951	390,620
Core capital including hybrid core capital after primary deductions	*3,668,787*	*3,268,165*
50% of capital requirement in associates, operating insurance business *)	43,939	46,026
50% of equity investments > 10% in credit and financing companies **)	223,119	209,387
Core capital including hybrid capital after deductions	*3,401,729*	*3,012,752*
Subordinated debt	328,000	328,000
Revaluation reserves	203,593	186,241
Capital base before deductions	*3,933,322*	*3,526,993*
50% of capital requirement in associates, operating insurance business *)	43,939	46,026
50% of equity investments > 10% in credit and financing companies **)	223,119	209,387
Capital base	*3,666,264*	*3,271,580*

*) Deductions according to section 31(1), no. 10 of the Danish Executive Order on Calculation of Capital Base.
**) Deductions according to section 31(1), no. 12 of the Danish Executive Order on Calculation of Capital Base.

The Group capital composition mainly consists of core capital, of which the actual core capital after primary deductions accounts for 89%.

In 2011, the Bank issued hybrid core capital of DKK 400 mill., of which DKK 7 mill. continues to be in the Bank's own portfolio. The hybrid core capital meets the requirements laid down in sections 10-12 of the Danish Executive Order on Calculation of Capital Base.

Group deductions under "Equity investments > 10% in credit and financing companies" are primarily attributable to the Bank's ownership interest in LR Realkredit, which accounted for DKK 367.6 mill. of the total deduction at the end of 2012, of which 50% has been deducted from core capital.

Group deductions under "Percentage of capital requirement in associates operating insurance business" are attributable to the Bank's ownership interest in Alka Forsikring A/S, which at the end of 2012, amounted to DKK 87.9 mill., of which 50% has been deducted from core capital.

Group revaluation reserves of DKK 203.6 mill. are attributable to the Bank's owner-occupied properties.

The Bank's capital base received of DKK 328 mill. matures on 3 December 2018 and may be redeemed before maturity on 1 December 2015. According to existing rules on capital adequacy, capital base can be included in full in the Group's capital statement up to and including 2 December 2015. The percentage is then reduced by 25% per annum. However, a further reduction is expected in connection with the entry into force of the new Basel III rules.

Solvency need

Model

An individual solvency need for both the Group and the Bank is set by Arbejdernes Landsbank.

A model is used, in which the solvency need is built on the basis of 0%, after which capital is allocated for each risk area. The total capital need is obtained by adding the capital need for each risk area. Thus the model takes no account of correlations between the individual risk areas.

The model is based on own data and risk assessments as far as possible. However, the Bank's historical database is limited, and therefore external data and methods for calculating risks are used to a large extent. In several risk areas, risk calculations have been made for own and external data/methods. The highest calculated risk is used in these cases.

Solvency need is calculated as the total capital need as a percentage of the weighted items calculated according to the provisions of the Danish Executive Order on Capital Adequacy. Pursuant to the Executive Order on Capital Adequacy, the Bank calculates weighted items for both the Group and the Bank. The lowest calculated weighted items are used in the calculation of the solvency need.

This model was selected to ensure a high degree of prudence, clarity and transparency.

Adequate capital and solvency need

Bank and Group solvency need calculated according to section 124(4) of the Danish Financial Business Act is 9.1%. According to this provision, adequate capital base amounts to DKK 2,276.1 mill. Calculation of adequate capital base and solvency need can be broken down into the following categories:

Table 26
Adequate capital base and solvency need as of 31 December 2012

	DKK '000	%
Capital to cover credit risk	1,197,125	4.8
Capital to cover market risk	786,691	3.1
Capital to cover operational risk	232,758	0.9
Capital to cover other risks	59,607	0.2
Adequate capital base/solvency need	*2,276,181*	*9.1*
Weighted items	*25,068,460*	

Capital to cover credit risk

Capital to cover credit risk is calculated by stress testing the Group's loan and guarantee portfolio with the sector's historical worst-case loss rates broken down into sectors. In some situations higher loss rates are used, when the Group's historical data indicates a higher risk. The average loss rate applied is 2.9%. A separate assessment of loss risk is also provided on unutilised credit facilities, weak exposures, large exposures, receivables from credit institutions, concentration on collateral and sectors as well as geographic concentration.

Capital to cover market risk

Capital to cover market risk is calculated on the basis of stress factors for market risk issued by the Danish FSA for guidance. A separate assessment of loss risk is also provided on covered bonds, liquidity risk, counterparty risk, settlement risk and share and interest-rate risk outside the trading portfolio.

Capital to cover operational risk

Capital to cover operational risk is equivalent to the solvency need according to the base indicator of the Danish Executive Order on Capital Adequacy. The Group makes its own calculations of the operational risk, in part based on historical losses. These calculations show a significantly lower risk than the solvency requirement.

Capital to cover other risks

Capital to cover other risks includes assessments of capital requirements for growth, fluctuations in the level of earnings, strategic and reputation risks, concentration of customer segments and risk on own properties.

Process

Assessment of the solvency need is an integrated part of the Bank's routine budget process, in which the Board of Directors approves annually the Group budget and the solvency need. In addition, the budget and solvency need are adjusted and corrected every quarter, and this is also presented to the Board of Directors.

Preparation of the annual budget and solvency need as well as quarterly adjustment is a coordinated process in the Group with the Financial Department, including All Risk Reporting as the coordinating unit.

The 8+ model

At the end of 2012, the Danish FSA issued revised guidelines for calculating the solvency need. These guidelines are based on a calculation method according to the 8+ model. From Q1 of 2013, the Danish FSA will base its assessment of banks' solvency need according to this model. On this basis, the Bank has decided to change the calculation method to the 8+ model from Q1 of 2013. A preliminary calculation shows that the solvency need will increase by 0.1 - 0.2 percentage points as a consequences of this change.

Solvency requirement

The Group solvency ratio at the end of 2012 was 14.6 compared with 13.5 at the end of 2011.

The Group uses the following methods to calculate the solvency ratio:

- Standard method to calculate credit risk
- Standard method to calculate market risk
- Market value method to calculate counterparty risk
- Base indicator method to calculate operational risk
- Collateral in the form of securities in accordance with the extended method
- Collateral in the form of mortgages in real property and cash deposits with the Bank.

The solvency requirement according to pillar I (8% of weighted items) was DKK 2,009.7 mill. at the end of 2012 against DKK 1,942.3 mill. the previous year.

According to legislation, as a minimum the Group must have capital corresponding to the least of either the minimum statutory requirement of 8 per cent of risk-weighted items (solvency requirement), or the individual solvency need laid down by the Board of Directors. The Group has calculated its individual solvency need at 9.1%, and this is therefore the basis for requirements for the size of the Group capital.

Table 27
Solvency requirement according to pillar I (8%)

	Solvency requirement 31.12.2012 DKK '000	**Solvency requirement 31.12.2011** DKK '000	**Solvency requirement Average *) 2012** DKK '000
Items with credit risk etc.			
Exposures to credit institutions	50,675	31,937	40,344
Exposures to businesses, etc.	404,829	405,855	401,475
Exposures to retail customers	779,884	747,395	761,590
Exposures secured by mortgages in real property	56,433	57,769	56,543
Exposures in arrears	34,928	24,703	39,314
Exposures in other items	63,558	61,101	61,736
Group write-downs	-4,261	-4,679	-4,504
Total items with credit risk, etc.	***1,390,307***	***1,324,081***	***1,361,001***
Items with market risk			
Debt instruments, specific risk	235,487	188,334	217,739
Debt instruments, interest-rate risk	93,551	149,430	104,161
Position risk for shares	33,940	32,921	36,317
Position risk for collective investment associations	14,744	14,188	14,881
Currency risk	8,951	16,907	17,484
Other items	0	0	0
Total items with market risk	***386,673***	***401,780***	***390,582***
Operational risk	232,758	216,400	219,672
Total solvency requirement	***2,009,738***	***1,942,261***	***1,971,254***
Capital base for meeting the solvency requirement	3,666,264	3,271,580	3,376,142

*) The average is calculated on the basis of reports to the Danish FSA in the period from 31 December 2011 to 31 December 2012.

Exposure categories

Exposure categories calculated using the standard method for credit risk pursuant to section 9 of the Danish Executive Order on Capital Adequacy. Exposures are stated after individual write-downs and before taking account of the effects of credit reductions.

Table 28
Development and average for items with credit risk

	Average 2012 DKK '000	Status 31.12.2012 DKK '000	Status 30.09.2012 DKK '000	Status 30.06.2012 DKK '000	Status 31.03.2012 DKK '000	Status 31.12.2011 DKK '000
Exposures to central banks and central governments	355,524	379,714	372,814	708,422	169,051	147,619
Exposures to credit institutions	3,601,871	3,926,254	3,193,915	3,744,057	3,852,949	3,292,181
Exposures to businesses, etc.	6,944,162	7,223,764	6,595,527	6,904,274	6,933,789	7,063,458
Exposures to retail customers	16,018,767	16,171,424	16,198,986	16,157,221	15,671,782	15,894,424
Exposures secured by mortgages in real property	1,902,238	1,892,634	1,861,378	1,897,363	1,910,215	1,949,600
Exposures in arrears	393,501	375,884	378,104	325,417	638,200	249,900
Exposures in other items	1,109,597	1,170,777	1,084,566	1,093,922	1,104,647	1,094,072
Total balance-sheet items	*30,325,660*	*31,140,451*	*29,685,290*	*30,830,676*	*30,280,633*	*29,691,254*

Table 29
Balance-sheet items*) as of 31 December 2012, broken down by remaining term

	On demand DKK '000	0-3 months DKK '000	3 months - 1 year DKK '000	1 - 5 years DKK '000	Over 5 years DKK '000
Exposures to central banks and central governments	379,645	0	0	0	0
Exposures to credit institutions	857,146	832	1,330	18,195	173,000
Exposures to business, etc.	1,429,673	488,218	678,406	949,198	780,223
Exposures to retail customers	384,226	2,746,897	1,243,526	4,816,775	2,903,218
Exposures secured by mortgages in real property	120,493	96,843	280,669	591,065	772,245
Exposures in arrears	38,890	8,882	44,025	115,598	120,928
Exposures in other items	509,961	32,308	0	0	628,508
Total balance-sheet items	*3,720,034*	*3,373,980*	*2,247,956*	*6,490,831*	*5,378,122*

*) Balance-sheet items are defined according to the provisions of the Danish Executive Order on Capital Adequacy.

Table 30
Sector breakdown of exposure category as of 31 December 2012

	Central governments and central banks DKK '000	Institutions DKK '000	Enterprises DKK '000	Retail customers DKK '000	Mortgages in real property DKK '000	Arrears or overdrafts DKK '000	Other items DKK '000	Total DKK '000
Public authorities	13,079	0	88,541	42,630	8,150	0	0	152,400
Corporate								
Agriculture, hunting, forestry and fisheries	0	0	39,980	30,607	6,871	901	0	78,359
Industry and extraction of raw materials	0	0	353,771	379,347	45,314	731	0	779,163
Energy supply	0	0	0	4,424	0	0	0	4,424
Building and construction	0	0	380,168	319,201	59,661	12,246	0	771,276
Trade	0	0	490,383	665,933	49,653	51,978	0	1,257,947
Transport, hotels and restaurants	0	0	350,310	319,291	48,021	8,572	0	726,194
Information and communication	0	0	19,504	181,383	8,006	19,778	0	228,671
Financing and insurance	363,184	3,926,254	1,969,531	85,278	17,989	44,632	0	6,406,868
Real property	0	0	1,388,583	302,657	333,041	190,660	0	2,214,941
Other corporate	0	0	1,863,217	1,120,720	172,997	12,158	0	3,169,092
Total corporate	***363,184***	***3,926,254***	***6,855,447***	***3,408,841***	***741,553***	***341,656***	***0***	***15,636,935***
Private	3,451	0	279,776	12,719,952	1,142,931	34,227	0	14,180,337
Other items							1,170,777	1,170,777
Total	***379,714***	***3,926,254***	***7,223,764***	***16,171,423***	***1,892,634***	***375,883***	***1,170,777***	***31,140,449***

Table 31
Credit-risk reduction as of 31 December 2012

	Central governments and central banks DKK '000	Institutions DKK '000	Enterprises DKK '000	Retail customers DKK '000	Mortgages in real property DKK '000	Arrears or overdraft DKK '000	Other items DKK '000	Total DKK '000
Adjusted value of the collateral	0	2,138,477	346,674	127,382	90	22,985	0	2,635,608

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