Note 5 - Capital adequacy and capital management

SpareBank 1 SMN utilises the Internal Rating Based Approach (IRB) for credit risk. Use of IRB imposes wide-ranging requirements on the bank's organisational set-up, competence, risk models and risk management systems. As from 31 March 2015 the bank has received permission to apply the Advanced IRB Approach to those corporate portfolios that were previously reported under the Basic Indicator Approach.

As of 31 December 2017 the capital conservation buffer requirement is 2.5 per cent, the systemic risk requirement is 3.0 per cent and the Norwegian countercyclical buffer is 2.0 per cent. These requirements are additional to the requirement of 4.5 per cent CET1 capital, so that the overall minimum requirement on CET1 capital is 12.0 per cent. In addition the financial supervisory authority has set a Pillar 2 requirement of 2.1 per cent for SpareBank 1 SMN, effective as from the fourth quarter of 2016. The total minimum requirement on CET1 capital is accordingly 14.1 per cent.

The countercyclical buffer increased from 1.5 per cent to 2.0 per cent with effect from 31 December 2017.

SpareBank 1 SMN has in fourth quarter 2017 reclassified two additional Tier 1 capital bonds from liabilities to equity, and the comparable figures has been restated. For further details, see note 1.

As from the fourth quarter of 2016 differentiated rates came into force for the countercyclical buffer. For exposures in other countries the countercyclical buffer rate set by the authorities in the country concerned is applied. If that country has not set a rate, the same rate as for exposures in Norway is applied unless the Ministry of Finance sets another rate. For the fourth quarter of 2017 the parent bank is below the capital deduction threshold such that the Norwegian rate is applied to all relevant exposures. For the group, the risk-weighted countercyclical capital buffer is 2.0 per cent.

Parts of the group's hybrid capital and subordinated debt were issued under earlier rules. This will be subject to a write-down of 40 per cent in 2016 and 50 per cent in 2017. The write-down will increase by another 10 per cent per year thereafter. As at 31 Desember 2017 the bank held hybrid capital worth NOK 450 million subject to write-down. For subordinated debt the figure was NOK 659 million.

Parent Bank			Group	
31 Dec 2016	31 Dec 2017	(NOK million)	31 Dec 2017	31 Dec 2016
14,166	**15,372**	**Total book equity**	**17,510**	**16,253**
-950	-950	Additional Tier 1 capital instruments included in total equity	-993	-950
-470	-522	Deferred taxes, goodwill and other intangible assets	-984	-741
-	-	Part of reserve for unrealised gains, associated companies	117	117
-609	-893	Deduction for allocated dividends and gifts	-893	-609
-	-	Non-controlling interests recognised in other equity capital	-565	-425
-	-	Non-controlling interests eligible for inclusion in CET1 capital	324	220
-29	-30	Value adjustments due to requirements for prudent valuation	-41	-48
-190	-350	Positive value of adjusted expected loss under IRB Approach	-333	-248
-	-	Cash flow hedge reserve	7	-
-	-	Deduction for common equity Tier 1 capital in significant investments in financial institutions	-212	-337
11,917	**12,627**	**Total common equity Tier one**	**13,938**	**13,233**
950	950	Additional Tier 1 capital instruments	1,427	1,358
483	459	Additional Tier 1 capital instruments covered by transitional provisions	459	483
13,350	**14,036**	**Total core capital**	**15,824**	**15,073**
		Supplementary capital in excess of core capital		
1,000	1,000	Subordinated capital	1,615	1,698
673	561	Subordinated capital covered by transitional provisions	561	673
-256	-254	Deduction for significant investments in financial institutions	-254	-256
1,418	**1,307**	**Total supplementary capital**	**1,922**	**2,116**
14,768	**15,343**	**Net subordinated capital**	**17,746**	**17,189**

		Minimum requirements subordinated capital		
1,065	978	Specialised enterprises	1,107	1,206
1,064	1,098	Corporate	1,113	1,102
1,270	1,370	Mass market exposure, property	1,892	1,753
85	90	Other mass market	91	88
1,223	1,198	Equity investments	1	3
4,707	**4,733**	**Total credit risk IRB**	**4,205**	**4,153**
5	3	Central government	3	5
73	80	Covered bonds	146	130
426	429	Institutions	331	340
5	0	Local and regional authorities, state-owned enterprises	4	7
45	44	Corporate	245	253
0	1	Mass market	388	179
13	13	Exposures secured on real property	193	342
245	232	Equity positions	344	338
86	70	Other assets	166	178
898	**872**	**Total credit risk standardised approach**	**1,820**	**1,772**
35	16	Debt risk	18	36
-	-	Equity risk	22	5
-	-	Currency risk	1	1
334	341	Operational risk	510	479
51	52	Credit value adjustment risk (CVA)	117	84
-	-	Transitional arrangements	784	574
6,026	**6,015**	**Minimum requirements subordinated capital**	**7,478**	**7,103**
75,325	**75,182**	**Risk weighted assets (RWA)**	**93,474**	**88,786**
3,390	3,383	Minimum requirement on CET1 capital, 4.5 per cent	4,206	3,995
		Capital Buffers		
1,883	1,880	Capital conservation buffer, 2.5 per cent	2,337	2,220
2,260	2,255	Systemic rick buffer, 3.0 per cent	2,804	2,664
1,130	1,504	Countercyclical buffer, 2.0 per (1.5 per cent)	1,869	1,332
5,273	**5,639**	**Total buffer requirements on CET1 capital**	**7,011**	**6,215**
3,255	**3,605**	**Available CET1 capital after buffer requirements**	**2,721**	**3,022**
		Capital adequacy		
15.8 %	16.8 %	Common equity Tier one ratio	14.9 %	14.9 %
17.7 %	18.7 %	Core capital ratio	16.9 %	17.0 %
19.6 %	20.4 %	Capital adequacy ratio	19.0 %	19.4 %
		Leverage ratio		
133,514	145,821	Balance sheet items	210,764	194,324
8,234	7,112	Off-balance sheet items	9,295	10,068
-690	-902	Regulatory adjustments	-1,580	-1,388
141,058	152,032	Calculation basis for leverage ratio	218,479	203,005
13,350	14,036	Core capital	15,824	15,073
9.5 %	**9.2 %**	**Leverage Ratio**	**7.2 %**	**7.4 %**