Eksportfinans

Pillar III Report 2012

Contents

1. INTRODUCTION

1.1 Background

The Pillar III report contains information on risk, risk management and capital adequacy in accordance with the capital adequacy regulation, Basel II. The document describes the company's capital requirements based on the applied methods for market risk, credit risk and operational risk (Pillar I) as well as information on internal processes regarding the company's assessment of capital (Pillar II).

A more detailed description of Eksportfinans' can be found in the annual report and the 20-F filing with the Securities and Exchange Commission ("SEC").

Summary

- Eksportfinans has estimated Pillar I capital for credit risk and market risk with the standard method and the capital for operational risk based on the basic indicator approach. The capital requirement under Pillar I is estimated to be approximately NOK 1.7 billion.

- Additional capital for market, credit and operational risk as well as business / strategic risk and concentration risk, is NOK 1 billion, to cover risk based capital requirements (Pillar II).

- In addition, The company requires NOK 2.9 billion in capital to meet EU regulations regarding large exposures. Eksportfinans' total capital requirement is, therefore, NOK 5.6 billion.

1.2 Overview of risk and capital management in Eksportfinans

Risk and capital are managed through a framework of principles, organizational structures as well as measurement and monitoring processes that are closely aligned with the activities of the business areas. Particular focus on liquidity risk, business risk and operational risk is important going forward.

- The management team provides overall risk and capital management supervision. The Board regularly monitors the risk and capital profile, which it revises at a minimum on an annual basis.

- Eksportfinans manages market, credit, operational, business, liquidity, strategic and reputation risk as well as capital according to policies and guidelines present throughout the organization.

Risk management supports the company's strategy and ensures that the company complies with external guidelines and regulations. Eksportfinans' risk profile is conservative. In order to achieve this, the company has estimated a required risk-based capital of NOK 2.7 billion. In addition the company has a capital buffer of NOK 2.9 billion to meet EU regulations regarding large exposures. The company will cover the risk-based capital requirement with core capital, while the NOK 2.9 billion large exposure capital add-on, may also consist of total capital.

In future total capital assessment processes the need for additional capital due to large single exposures may be reduced. Future external influences such as market turbulence, new regulation or idiosyncratic risk could also affect the level of capital requirements.

1.3 Structure of the Pillar III disclosure

The report includes information on risk, risk management and capital adequacy in accordance with the capital adequacy regulation, Basel II.

The minimum capital requirement for Pillar I is calculated using a combination of the different methods shown in table 1.

Table 1 *– Pillar I capital calculation methods*

Credit Risk	MARKET RISK	OPERATIONAL RISK
Standard method Foundation IRB-method*) Advanced IRB-method*)	Standard method Internal methods*)	Basic indicator approach Standardised approach AMA method*) **)

*) Needs special approval from financial authorities, **) AMA=advanced measurement approach

Eksportfinans calculates minimum capital under Pillar I using the standard methods for credit risk and market risk and the basic indicator approach for operational risk.

In the company's risk assessment under Pillar II financial revenue projections have been taken into account. Expected financial results are then adjusted with the impact from an adverse scenario for market, credit, operational and business/strategic risk. These risk categories are significant for the company.

This Pillar III report is structured as follows:

- Chapter 2 (Risk and capital management) describes Eksportfinans' overall risk and capital management procedures. The chapter also demonstrates how the company calculates its capital requirements, capital objectives and actual capitalization.

- Chapter 3 (Capital and capital adequacy) provides information on terms and conditions that apply to the items included in Eksportfinans capital base. The chapter also gives a capital adequacy analysis as well as information on compliance with large exposure regulations.

- Chapter 4 (ICAAP and economic capital) describes Eksportfinans' internal capital adequacy assessment process and the methods that apply to the items included in Eksportfinans' capital base.

- Chapter 5 (assessment of capital requirements) covers how Eksportfinans identifies and analyzes credit risk, market risk, operational risk, and business/strategic risk. For all key risk categories, the chapter describes risk management, risk control and capital requirements.

2. RISK AND CAPITAL MANAGEMENT

2.1 Objective

Overall risk management includes principles for managing, monitoring, controlling and reporting total and business unit risk.

2.2 Organizational setup, roles and responsibilities

Risk management and control is performed by The Board, The Board's audit committee, the control committee, the management team as well as operational units. The table below gives an overview of the structure, role and members of the different committees as of December 31, 2012.

Committee	Tasks	Members
The Board	- External reporting of financing accounts and risk information - External reporting according to Basel II (this Pillar III document)	Seven external members, where three are from owner banks in addition to one member elected by and among the employees
The Board's audit committee	- Preparing the board's monitoring of reporting of financial accounts - Monitoring risk, internal control systems and the internal audit.	Four external members, including two from owner banks
The control committee	- Ensuring operations in compliance with rules and regulations from the Norwegian FSA	Three external members and one external deputy member
Asset/liability management (ALM) group	- Discussing the company's liquidity in light of market expectations, including stress scenarios as well as projections for loan payments Suggesting liquidity actions for the ALCO committee	Members from the funding & lending, risk management and the accounting & financial control departments
ALCO committee	- Making decisions in asset/liability management questions	All members of the company's management team
Investment commitee	- Overseeing development and strategy for the liquidity reserve portfolio within limits set forth by The Board	Members from the liquidity placements & internal bank, the accounting & financial control and risk management departments
Credit commitee	- Makes decisions in credit risk cases that are not directly covered by general mandates	CEO, operating entity responsible for the particular case and directors from the risk management, accounting & financial control, funding, lending and legal & compliance departments
New product approval forum	- Forum gathering to discuss potential new products. There is a clear definition as to when this forum should meet.	Members from the risk management, accounting & financial control, funding and lending, IT departments in addition to the unit suggesting the new product

The company's CEO is required to ensure the following:

- Establishment of a strong risk management function from guidelines given by the Board.

- Risk management is adequately documented, conducted and monitored.

- Reporting to The Board complies with rules, regulations, decisions and principles set forth in The Board's risk guidelines.

- The internal audit function reports at least annually to the Board of Directors on the status and quality of established internal controls.

- When there is a change in existing products or new products are being introduced, the CEO should ensure that risk assessment, internal control and documentation are in place prior to the implementation of the change. The Board shall be informed of significant changes in the company's quality assurance process.

The responsibilities of the Management Team include:

- Risk management according to set guidelines.
- Approval of credit risks within set limits.
- Monitoring of all exposures.
- Timely, frequent and independent controls.
- Reporting according to internal control guidelines on the practice of controls, weaknesses and risk assessments.
- Reporting of loss events.

The risk management department

The risk management department monitors the company's overall risk, including overseeing market and credit risk against set limits. The department is also responsible for calculating fair values used in official financial reporting (according to IFRS). The risk management department is also responsible for asset/liability management (ALM).

The risk management department must ensure that:

- Relevant risk management systems are established, followed up and maintained in accordance with relevant regulations, rules and routines.

- The risk management process is in accordance with regulations and guidelines set by the Board and that these seek to be best practice.

- The company's risk status and development is in accordance with the company's strategy.

All employees

- Should have sufficient knowledge on the risk management processes, routines, instructions, mandates and risk/compliance models relevant for their department.

- Have responsibility for communicating significant breaches in the risk management process to senior managers.

Internal audit

The internal auditor:

- Reports to the Board and the management group in accordance with an approved audit plan.

- Gives objective suggestions to the Board and the management team regarding risk management, development of and compliance with controls, established routines, procedures and guidelines.

- Analyzes significant risk categories and risk adjusted capital requirements annually.

- Shall have sufficient competence and experience, methodology and tools to be able to assess whether all significant risk areas are covered by the company's risk management.

2.3 Risk management and control

Risk management

Eksportfinans' loan and investment portfolios have exposures in several different markets. This requires identification, aggregation and management of the total risk in a prudent manner.

The risk management process in Eksportfinans is based on the following elements:

- Control environment
- Risk identification
- Risk analysis
- Guidelines and routines
- Risk strategy
- Control actions
- Reporting
- Monitoring

Control environment

The control environment includes company organization, management team guidelines, management style as well as the integrity of all employees. Eksportfinans puts emphasis on the following principles:

- Values and ethical guidelines: The company's ethical guidelines shall underpin the company's strategy and be known in all parts of the organization.

- Social responsibility: The policy covers a broad range of social responsibility considerations and comprises ethical guidelines, environment-friendly measures in the company, environmental and social requirements for projects financed by the company, required anti-corruptions measures in projects financed by the company and reporting requirements. As part of the company’s environmental requirements Eksportfinans is obliged to adhere to the OECD Common Approaches on the Environment and Officially Supported Export Credits, which also gives specific direction on how the requirements should be implemented in the company’s lending operations. In addition, The Board has decided upon an environmental poster which provides guidelines for practical application of environmental considerations in the company’s activities. As a result of these efforts, Eksportfinans is not aware of violations of human or social rights, or breaches of environmental requirements, in any of its projects or operations in 2012 or historically.

- Structure of control and management: A clearly understandable and independent control and management structure is emphasized. The company is Sarbanes Oxley (SOX) compliant, which implies extensive use of routine descriptions, control evidence and clarity regarding operational risk concerning publically available financial statements. The SOX framework also makes auditing, end-of-month processes and reporting more transparent. There are also established internal forums for assessment and approval of new products, asset/liability mix as well as credit cases in addition to the external control environments.

Risk identification

The Board and the management team have assessed the company's overall risk and have set limits for accepted risk exposure. The company has country and single counterparty limits, based mainly on long term credit ratings from Fitch, Moody's and Standard & Poor's.

Risk identification shall be conducted annually, at a minimum, or when required by special situations or events, and cover all significant risks which the company faces. The following processes are to be adhered to at all times:

- The Board and the management team are responsible for identifying strategic risks as part of the ICAAP and strategy process, and for incorporating these risks in future planning.

- Identify key corporate process risks, and present them in an annual internal control report and an annual risk workshop. All members of the management team assess and prepare a written summary of the risk level in their respective department.

- A dedicated new product approval forum is responsible for assessing and advising the management team regarding approval of new products or changes in existing products, or routines for investments or lending.

- An asset liability committee (ALCO) meets monthly to review and discuss the current view of the company's assets and liabilities. The committee analyzes perceived changes in prepayment rates and requests from borrowers on amortization plans as well as changes in expected maturities for liabilities with different early termination options.

- An investment committee reviews the strategy and development of the liquidity reserve and PHA portfolios relative to limits set by the Board.

Risk assessment

Assessment of changes in portfolios and regulations form the basis for the company's management of identified risk types. This includes:

- That all significant risks are quantified based on well known methods and procedures to measure risk combined with own assessments.

- That sensitivity- and stress tests for different scenarios are calculated.

- Ensuring that a qualified and structured assessment and documentation of implemented policies and controls is carried out.

- As part of the annual ICAAP process, losses from security investments and credit exposure from lending, are estimated. The company's capital target is to have capital sufficient to cover present and future credit risk under a number of scenarios.

- Management is responsible for adjusting and updating their area’s defined risk profiles to fit into the overall risk strategy of the company. The risk assessments should include an identified risk profile and a suggested risk limit.

Regulations, instructions and routines

The Board evaluates the company's risk policy and guidelines at least annually.

The Board decides guidelines for:

- Overall risk management
- ICAAP in Eksportfinans
- Credit risk
- Liquidity risk
- Market risk including
    - General interest rate risk
    - Currency risk
    - Credit spread risk
    - Basis risk
- Operational risk

- Lending activity
- Investment activity

Other instructions and mandates include:

- Instruction for control committees in financial institution
- Instruction for the Board of Directors in Eksportfinans ASA
- Instruction for the Chief Executive Officer in Eksportfinans ASA
- The CEO's mandate
- Instruction for internal audit in Eksportfinans ASA
- Mandate for the Board’s audit committee

2.4 Capital strategy, capital target and risk tolerance

Every year the Board has a strategy meeting discussing market developments, future focus areas and capital requirements. The capital strategy defines how capital will be managed to support the business areas.

The capital assessment in this Pillar III report is based on an expected balance sheet development for the period 2013-2015.

Pillar I (credit risk, market risk and operational risk) has a set of minimum requirements. The company performs an assessment process to determine the correct level of capital and to what extent these minimum requirements are sufficient. In the internal assessment of other key risks, both qualitative and quantitative methods are taken into account. Capital is also required for concentration risk, basis risk and strategic/business risk.

Eksportfinans calculates Pillar I capital for credit and market risk using the standard method. For operational risk the basic indicator approach is used. Much of the capital required is to offset credit risk. Since a large part of the loan portfolio is guaranteed by governments or by banks, this portfolio is considered to have a low risk profile. As described in chapter 3, the company assesses credit risk capital under Pillar I to sufficiently cover credit risk, while additional capital is required under Pillar II for market risk and operational risk as the Pillar I calculation methodologies do not cover all risks adequately.

Additional capital is required for business/strategic risk and concentration risk. In total these calculations determine a risk based capital requirement for the company. This capital requirement is covered by core capital and should be sufficient for expected future changes in regulations.

In a normal business situation the company would set a capital target higher than the required capital level to have a buffer. The capital target has had two objectives: ensuring the company's capital adequately supports the business strategy, and ensuring that capital at all times is above minimum levels set by the government - also in periods of adverse business development. The capital targets have previously been set from a total assessment based on the company's risk situation, regulatory requirements and expectations from the market and rating agencies.

In the ICAAP process for 2012, no capital target directly linked to Pillar I and II assessments has been set. This is due to the large exposure regulations which for a period going forward demands a higher capitalization than the risk based approach under Pillar I and Pillar II.

The total capital assessment process (Pillar I & II) aims to provide sufficient capital for large exposures taking conservative assumptions into account. Both core and non-core capital may be used to cover capital needs for large exposure regulations. The risk based capital requirement under Pillar I and II is to be covered by core capital only. In future total capital assessment processes the need for capitalization due to large single exposures may be reduced. External effects such as market turbulence, new regulations or idiosyncratic risk will also have an effect on the level of capital requirements.

As a part of the ICAAP process the company makes an assessment of a hypothetical three year scenario with a serious setback. According to the calculations Eksportfinans will have sufficient capital to handle a severe recession for three years without exceeding the risk-based capital allocated under Pillar II.

3. CAPITAL BASE AND CAPITAL ADEQUACY

Eksportfinans had a core capital ratio of 25 % and total capital ratio of 28% based on Basel II Pillar I methods at year end 2012.

Capital adequacy assessments (ICAAP) are conducted at least annually and Eksportfinans' capital strategy will be based on an assessment of the risk level in the organization supplemented by the effect of various stress scenarios.

Eksportfinans shall at all times comply with regulatory capital requirements.

Capital is intended as a buffer against risk which the company is exposed to from its business operations. Capital consists of equity capital and supplementary capital. The supplementary capital consists of capital contribution securities, subordinated debt and various adjustments.

3.1 Capital base

The tables below provide information on regulatory capital, including core capital and supplementary capital. All tables are linked to regulatory reporting and are based on figures as December 31, 2012.

Table 2 *– Specification of minimum capital requirements for different risk categories*

RISK CATEGORY	**Capital requirement** **NOK mill.**
Credit risk	1 377
Split into:	
o *Governments*	0
o *Local and regional authorities*	26
o *Government owned corporations*	0
o *Multilateral development banks*	0
o *Institutions*	1 149
o *Enterprises*	0
o *Security for property*	1
o *Other commitments*	30
o *Securitisation*	171
Market risk	127
Operational risk	197
Total minimum requirement for subordinated loan capital	**1 701**

Capital adequacy

The table below shows the development of capital adequacy during the past three years.

Table 3 *– Capital adequacy 2010 - 2012*

	2012 NOK mill.	2011 NOK mill.	2010 NOK mill.
Core capital	5 314	4 786	4 077
Additional capital	628	975	1 565
Total capital	5 942	5 761	5 642
Core capital in percent	25 %	16,10 %	12,70 %
Total capital in percent	28 %	19,40 %	17,60 %
Total risk-weighted assets (incl. "off-balance" elements, operational risk and trading portfolio)	21 243	29 661	31 985
Total	***157 406***	***213 929***	***225 254***

Table 4 gives an overview of the company's assets as of 31 December 2012, and the assets that are secured with guarantees, so that credit loss only occurs if both the borrower and the guarantor breach their obligations.

Table 4 *– Specification of risk weighted assets as per December 31, 2012*

ASSET TYPE	Book	RISK WEIGHT	BOOK VALUE	RISK WEIGHT	GUARANTEE	REMARKS
Loans	87 918	0 %	33 440	-	31 398	Guarantees from GIEK
					2 042	Guarantees from other Government
		20%	52 679	10 536	43 588	Guarantees from banks
		20%	1 602	320		Direct to or guarantees from municipalities
		35%	35	12		
		50%	50	25		
		100%	112	112		
Securities	41 785		11 580	2 141		Securitisation
			30 205	1 574		Trading portfolio
Financial derivatives and Cash Collaterals	16 329			1 664		
Other	11 375			2 243		10 bln. deposits
Off-balance transaction				152		
Operational risk				2 465		
Currency risk				-		
TOTAL	**157 406**			**21 243**		
Total risik-weighted assets / Total assets				13,5 %		

3.2 Capital requirement process

Eksportfinans has calculated Pillar I capital for credit risk and market risk using the standard method and used the basic indicator approach for operational risk. Total capital requirements are deducted using a three step procedure:

- Minimum capital requirements are calculated for credit risk and market risk by using standard method, and for operational risk using the basic indicator. Pillar I capital requirements are estimated to NOK 1.7 billion.

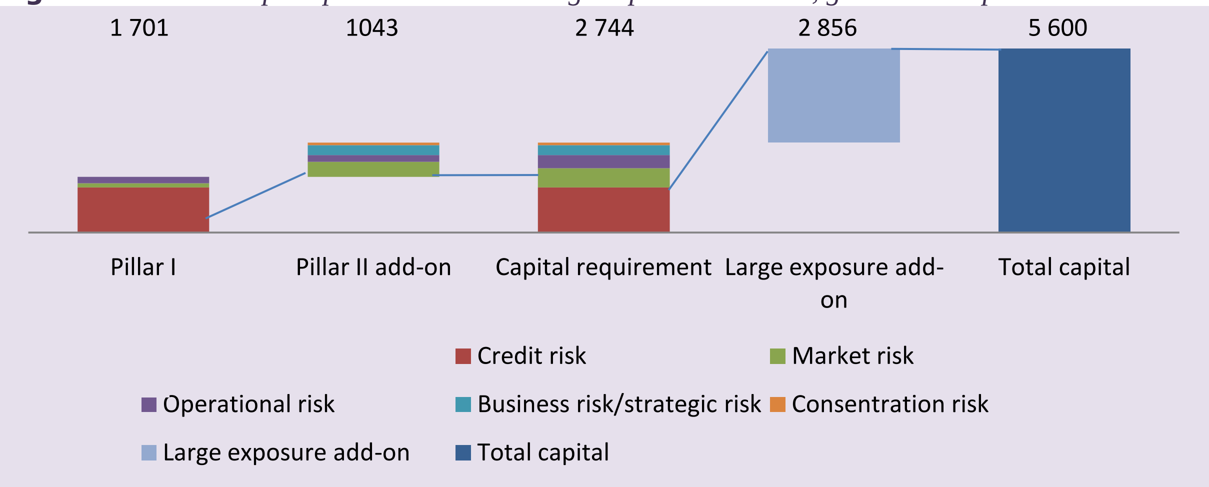
- In addition to the minimum capital requirement the company annually performs an internal adequacy assessment process, ICAAP, to ensure the level of capital is sufficient. Both qualitative and quantitative methods are adopted to identify key risks. This is the Pillar II assessment which covers the consequences of significant negative events. The estimated additional capital requirements are also tested against an adverse three year scenario. In this analysis another NOK 1 billion of capital is required for credit risks (concentration risk towards single names and sectors), market risk (credit spread risk, currency risk and basis spread risk), operational risk and business risk.

- Finally, an additional assessment of capital to comply with external rules and regulations is conducted. To adhere to CRD large exposures regulations the company currently holds another NOK 2.9 billion in capital in addition to the risk based capital requirement of 2.7 billion NOK.

Hence the company's risk based capital requirement is NOK 2.7 billion which the company will cover through core capital. The total capital requirement is NOK 5.6 billion which may also be covered by additional capital.

The below figure summarizes the steps in the capitalization process.

Figure 2: *Pillar I capital plus Pillar II and large exposure add-ons, gives total capital*



In chapter 5 the significant risk categories for the company are defined and discussed. The management and control of each risk is evaluated.

3.3 Large exposures

Limits for large exposures decrease the potential loss an institution can experience from a single counterparty due to unforeseen events. Until 31/12/2012, the company had a temporary exemption from the large exposure provision in the EU’s capital requirement directive. From 01/01 2013 Eksportfinans has had to adhere to the large exposure provisions in the EU’s capital requirement directive, with an exemption from the Norwegian FSA (Finanstilsynet) for five outstanding loans until the exposure is expected to be below regulatory limits for each of the five outstanding loans. A large exposure is defined as an exposure that is more than

10% of a company's total capital. The largest exposure rule sets maximum limits for exposure to a single counterparty to 25% of the total capital.

To ensure that the company has adequate capital in a distressed financial situation, Chapter 4 below discusses the robustness of capital in a three-year adverse scenario.

3.4 Effect on capital from 'leverage ratio' regulations

In addition to risk-based and rule-based capital adequacy requirements, Basel III introduces a minimum equity requirement in relation to total assets, regardless of the risk weighting of assets; "leverage ratio". Eksportfinans expects to comply with the leverage ratio requirement by a large margin when these rules are implemented.

3.5 Effect on capital from new OTC derivatives regulation

The European Union is introducing the European Market Infrastructure Regulation (EMIR) to enhance the efficiency and the robustness of the derivatives marked. In the U.S., new rules will be implemented through the Frank Dodd reform. The company uses derivatives extensively to hedge exposure, and the rules only apply to new transactions. The new rules are expected to produce higher margin requirements for both cleared and non-cleared transactions. Eksportfinans expects that the new rules will have a limited impact, but there is still some uncertainty about the expected market effects.

4. ICAAP AND ECONOMIC CAPITAL

4.1 International capital adequacy assessment process (ICAAP)

According to Pillar II of the Basel II framework, institutions are required to use their own process of self-assessment of capital requirements and capital (internal capital adequacy assessment, ICAAP). This requires an overall and total risk estimation and evaluation. From this, capital requirements, including robustness of a three-year adverse scenario is determined. In the ICAAP document, Eksportfinans analyzes and assesses this information which is approved by the Board and submitted to the Norwegian FSA, "Finanstilsynet".

Calculation of capital under Pillars I and II are made using different methodologies. Eksportfinans analyzes all material risk categories for the company and calculates capital requirements per risk category. For those categories with regulatory minimum capital requirements (market risk, credit risk and operational risk), Pillar II calculations are compared to the minimum requirements. If Pillar II assesses a higher capital requirement than Pillar I, then the difference is added as the Pillar II add-on. Pillar 2 assessments provide additional capital for credit, market, operational and business risk as shown in the figure below. Liquidity risk is controlled through active management and frequent asset / liability management group meetings where liquidity under different stress conditions is analyzed. The company does not calculate capital for liquidity risk.

Regulatory capital	**Add-on capital (Pillar II ICAAP assessments)**	**Risk management**
Credit risk	Credit risk (concentration)	Liquidity risk
Market risk	Market risk (currency risk, spread risk and basis risk)	
Operational risk	Operational risk	
	Business risk	

5. ASSESSMENT OF CAPITAL REQIREMENT

5.1 Credit risk

Eksportfinans' credit risk is the risk of loss due to defaults on loans with guarantees where both the debtor and the guarantor default, defaults on loan contracts for direct loans, and defaults of interest and principal payments on investments.

The company's portfolios consist of guarantors and counterparties with high credit ratings. Loans are generally guaranteed by Governments entities or banks. Eksportfinans is exposed to credit risks through loans to the export industry/guarantors, towards issuers of securities and counterparties in swap agreements.

Capital for credit risk is calculated from the Basel II standardized approach in Pillar I. Eksportfinans is exposed to financial institutions through direct exposure, derivate transactions, guarantee exposure and exposures from investments in the liquidity reserve portfolio.

The company's credit exposure related to counterparties in derivative agreements is governed by master agreements developed by ISDA (International Swaps and Derivatives Associations). The exposure is mitigated by regulated agreements for exchange of collateral, known as Credit Support Annexes / CSA agreements. Eksportfinans only accepts cash as collateral under the CSA agreements.

5.1.1 Management and monitoring

Eksportfinans applies credit ratings and analyses from the major rating agencies (Moody's, Standard & Poor and/or Fitch) to monitor the credit quality of all guarantors and credit counterparties in its portfolio of financial investments and in its derivatives portfolio. The risk management department monitors credit limits on a daily basis. Concentration risk and counterparty credit quality status are reported to The Management Team on a monthly basis.

The company uses various techniques to manage credit risk:

- The company has high requirements for counterparty credit quality. On the lending side, all loans are guaranteed by GIEK or other government entities, and/ or financial institutions with an acceptable rating. Credit losses from guaranteed export loans will only occur if both the borrower and guarantor fail to meet their obligations. A small portion of the balance sheet consists of unsecured loans to banks and municipalities.

- Legally binding standard ISDA agreements allow calculation of net derivatives exposure per counterparty. Special provisions in the ISDA agreements (CSA annexes) specify the transfer of collateral on a daily basis eliminating most of the counterparty credit exposure from Mark- to Market movement of swap contracts.

5.1.2 Portfolio information

As shown in the table below, the company's portfolio is of high credit quality. The average rating for loans rated by Moody's, Fitch or S&P is AA-.

Table 5 *– Aggregated credit exposure per rating class per end of 2012*

NOK mill.	Loans			Liquidity investments			Total
Rating	Unsecured	Guaranteed	Total loans	Liquidity reserve portfolio	PHA portfolio	Total liquidity holdings	
AAA	1.515	33,440	34.955	13.433	1.778	15.212	50.167
AA+/AA/AA-		5,325	5.325	7.510	913	8.422	13.748
A+/A/A-	3.934	33.228	37.162	7.003	3.465	10.467	47.629
BBB+/BBB/BBB-	143	3,793	3.935	(45)	3.029	2.984	6.919
BB+/BB/BB-		4	4		972	972	976
B+/B/B-			0		589	589	589
CCC+/C			0		125	125	125
No international rating	5.102	953	6.055	2.042	529	2.571	8.626
Total	**10.694**	**76.743**	**87.437**	**29.943**	**11.399**	**41.342**	**128.779**

Most of the loan portfolio is guaranteed either by GIEK or banks.

5.1.3 Capital requirements for credit risk

Eksportfinans utilizes the standard method for calculating capital for credit risk under Pillar I. The regulatory risk weights used for the portfolio are considered relatively conservative by the company. A high proportion of total loans are guaranteed by highly creditworthy counterparty banks (double default); credit risk is therefore assumed to be limited.

Based on the information above, the company's Pillar I calculation should provide robustness against actual credit risk also in an adverse scenario. The company does not apply additional capital for credit risk.

5.2 Market risk

Market risk is the risk of loss due to an adverse move in the market value of an asset, a liability or a derivative contract. For Eksportfinans the market value of the net positions will primarily depend on general interest rates, specific interest rates (credit spreads) and foreign exchange rates. The loss of derivative contracts could also significantly increase Eksportfinans' market risk.

5.2.1 Management and monitoring

The company applies various hedging strategies to manage interest rate risk, currency risk and other market-related risks in alignment with the company's limits.

Credit spread sensitivity is calculated per business area and reported monthly to the management team and the Board.

In addition to market information from trades, also quantitative measures are used in order to monitor Eksportfinans' market risk exposure. These include:

- Risk limits for foreign currency exposure.
- Limits for interest rate risk.
- "Stop loss" limits per security for the liquidity portfolio,. If these “stop loss” limits are exceeded, the investment committee will meet and recommend further action.
- Limits for credit spread sensitivity.

The PHA portfolio is guaranteed against all market risk through the portfolio hedge agreement with the owner banks (see annual report for a more detailed description of the PHA portfolio).

The company's system for management and control of market risk is regularly evaluated by internal and independent control functions. The external controls are most often performed by the company's auditor

5.2. Capital requirement for market risk

The company uses the standard method in calculation of minimum capital requirements. The company applies additional capital requirements for currency risk, credit spread risk and basis risk. This add-on assessment and calculation has also been tested against the adverse three year scenario. As a result of the negative scenario the company requires additional capital for credit spread-, currency-, and basis risk under market risk in Pillar II.

5.3 Operational risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes or systems, human error or external events in all the company's business areas.

5.3.1 Management and monitoring

Operational risk is inherent in all activities performed by Eksportfinans. Prudent management of operational risk is critical to maintain a low overall level of risk. Losses due to operational risk have historically been low in Eksportfinans.

Operational risk may arise in connection with for example legal risk, failure in internal processes, human error, data loss, embezzlement and fraud. These risks are reduced through increased focus on regulations concerning the use of information and communication technology, procedure manuals, training programs, ethical guidelines and a compliance function. The company's framework for managing and controlling operational risk is under risk management’s responsibility. The company also receives control and reporting from external parties such as external auditors, internal auditors, regulators and rating agencies. The management team will annually review the company's major risks in a risk workshop facilitated by the internal auditor.

Operational risks may also arise for example in connection with the trading and settlement of financial transactions. In addition, and the large volume and the number of derivatives that Eksportfinans has entered into is a significant source of operational risk. Adequate payments and settlement processes, as well as administration and termination of derivative contracts, are very important to avoid losses. A significant part of the company's framework and controls are therefore focused on this area, including procedures and independent control of transactions.

Eksportfinans has various contingency plans that will come into effect in certain scenarios. Contingency plans are made for liquidity, derivatives, and human resources.

5.3.2 Capital requirement for operational risk

Eksportfinans utilizes the basic indicator approach for calculating capital for operational risk under Pillar I. In a historical perspective, the Pillar 1 allocation is sufficient. Since capital is calculated from historical income without taking into account the current situation of Eksportfinans, additional capital is allocated for operational risk based on Pillar II assessments.

5.4 Business risk and strategic risk

Business and strategic risk are defined as the risk arising from incorrect strategic decisions, loss of reputation, reduced rating, or limitation in the company's business opportunities. Lower overall margins, the need for an unfavorable sale of assets or early termination of contracts could have a negative impact on financial results.

5.4.1 Management and monitoring

Eksportfinans current strategy is to actively manage the existing portfolio of loans, securities and other assets, liabilities and other commitments. In addition the company focuses on servicing borrowers and investors, and securing the organization with the necessary expertise to the best interest of the company and its stakeholders.

The company has guidelines for responsibility, including ethics, environmental responsibility and corruption. There are contingency plans for given scenarios, and an HR strategy which is frequently discussed in the management team.

For the management of the liquidity reserve, an ALCO committee (the management team) and an Investment Committee composed of leaders across the company are in effect. The investment committee reports to the management team, which has regular weekly meetings where strategic and operational topics are discussed.

5.4.2 Capital requirement for business- and strategic risk

Business and strategic risk are not risk categories in Pillar I. The company reserves capital for business- and strategic risk to be able to cover any loss due to business- and strategic risk.

5.5 Liquidity risk

Liquidity risk is defined as the ability of the company to meet all debt obligations.

5.5.1 Management and monitoring

Eksportfinans' main focus is to ensure sufficient funds to meet future payment obligations when they become due. Since Eksportfinans currently does not issue new funding, the liquidity portfolio has become the main instrument for securing liquidity. The liquidity portfolio consists of short maturity, very liquid and highly rated securities. The company manages liquidity risk both through matching maturities for assets and liabilities and through stress testing.

Different stress tests and scenario analyses are conducted regularly to ensure sufficient funds even under stressed conditions. The company manages liquidity risk against defined limits and has contingency plans if given limits are exceeded.

Eksportfinans has the following available liquidity buffers:

- A substantial liquidity portfolio with highly rated instruments with short maturities.
- Committed credit line of USD 2 billion with three of the owner banks.

5.5.2 Capital requirement for liquidity risk

Eksportfinans allocates no capital for liquidity risk. The company considers liquidity risk as a risk that is mainly conditioned by other types of risk since it is typically caused by credit losses. Liquidity risk may also occur in an economic downturn or financial crisis. The company focuses on conservative and professional liquidity management. Stressed scenarios have been implemented in Asset and Liability analyses. The result from scenarios indicates that the company has the ability to meet its obligations even under severe stress.