Eksportfinans

Pillar III Report 2013

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1 INTRODUCTION

1.1 Background

The Pillar III report contains information about 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 own assessment of capital (Pillar II). The time of implementation of new regulations, CRD IV (Capital Requirement Directive) in Norway, is not yet decided, but Eksportfinans is prepared to gradually implement the new regulations from third quarter 2014. As a result of implementing these new regulations, the calculated capital requirement increases significantly even though Eksportfinans' balance is reduced considerably through 2013.

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

Summary.

- Eksportfinans has estimated Pillar I capital for credit risk and market risk based on 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 2.5 billion

- Additional capital for market, operational risk, business / strategic risk and concentration risk of NOK 0.8 billion, to cover risk based capital requirements (Pillar II).

- In addition, The Company requires NOK 2.2 billion in capital to meet EU regulations regarding large exposures. Eksportfinans' total capital requirement is 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, and performs a revision of the profile at least annually.

- Eksportfinans manages market, credit, operational, business, liquidity, strategic and reputational risk as well as capital in a coordinated manner.

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 3.3 billion. In addition the company has a capital buffer of NOK 2.2 billion to meet EU regulations regarding large exposures.
In future total capital assessment processes the need for capitalisation due to large single exposures may be reduced. Thus said, future external effects such as market turbulence, new regulations or idiosyncratic risk will affect the level of future capital requirements.

1.3 Structure of the Pillar III disclosure

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

The minimum capital requirement for Pillar I may be calculated using the different methods shown in Table 1.

Table 1 *– Pillar I capital calculation methods*

CREDIT RISK	MARKET RISK	OPERATIONAL RISK
Standard method	Standard method	Basic indicator approach
Foundation IRB-method*)	Internal methods*)	Standardized approach
Advanced IRB-method*)		AMA method*) **)

*) Need 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 own risk assessment under Pillar II it has implemented its current financial revenue projections. Expected financial results were then adjusted in accordance with qualified impact assessments from an adverse scenario for market, credit, operational and business/strategic risk. These risk categories are identified as 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 formulates its capital requirement, capital objective and actual capitalisation.

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

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

- Chapter 5 (own assessment of capital requirements) contains information about how Eksportfinans identifies and analyses credit risk, market risk, operational risk, and business/strategic risk. For all important risk categories, the chapter describes risk management, risk control and capital requirements.

2 RISK AND CAPITAL MANAGEMENT

2.2 Objective

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

2.3 Organizational setup, roles and responsibilities

Risk management and control is performed by The Board, the audit committee, the risk 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.

Committee	Tasks	Members
The Board	- External reporting of financing accounts and risk information. - External reporting according to Basel II (this Pillar III document).	Five external members, where three are from owner banks in addition to one member elected by and among the employees.
The audit committee	- Preparing the board's monitoring of reporting of financial accounts. Monitoring the internal audit.	Three external members, including two from owner banks
The risk committee	- Assist the board in assessing different types of risk, internal control systems and processes.	Three 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 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 and amortization - Suggesting liquidity actions for the ALCO committee	Members from the departments Funding & Lending, Risk Management and Accounting & Financial Control
Asset /liability commitee (ALCO)	- 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 departments Liquidity Placements & Internal Bank, the Accounting & Financial control and Risk Management
Credit commitee	- Make decisions in credit limit cases that are not directly covered by general mandates	CEO, operating responsible for the particular case and directors for the departments Risk Management, Accounting & Financial Control, Lending and Legal & Compliance
New product approval forum	- Forum gathering to discuss approval or not for potential new products. There is a clear definition as to when this forum has to meet.	Members from the departments Risk Management, Accounting & Financial Control, IT and Back Office, 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 on the status and quality of the established internal control.

- When there is a change in existing products or new products are being introduced, the CEO should ensure that risk assessments, internal control and documentation exist before the change is implemented. 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
- Approve credit risks within set limits
- Monitor all exposures
- Timely, frequent and independent controls
- Report according to internal control guidelines on the practice of controls, weaknesses and risk assessments
- Report on loss events

The Risk Management department

The Risk Management department monitors the company's overall risk management, 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 to 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 about the risk management process, routines, instructions, mandates and risk/compliance models relevant for their department.

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

Internal audit

The internal auditor:

- Reports to The Board and The Managing team in accordance with the 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.

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

- Should 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.

2.4 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 company’s risk management process 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 organisation, 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-corruption 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 directions 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 2013 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. Further exist 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 The Board has set limits for accepted risk exposure.

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

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

- The management team are responsible to 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.

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

Risk assessments

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

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

- Sensitivity- and stress tests for different scenarios are performed

- 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 sufficient capital to cover for present and future credit risk under a number of scenarios.

- Management is responsible for adjusting and updating the risk profiles defeined for the different areas to fit into the overall risk strategy of the company. The risk assessments should include an identified risk profile and a suggested risk acceptance.

Regulations, instructions and routines

The Board is to evaluate 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:

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

2.5 Capitalisation strategy, capital target and risk tolerence

Every year The Board has a strategy meeting to discuss market developments, future focus areas and capital requirements. The capital strategy defines how the capital management supports the business areas.

The capital assessment in this Pillar III is based on an expected balance sheet development for the period 2014-2016.

Pillar I (credit risk, market risk and operational risk) has a set of minimum requirements. The company performs an assessment process to determine the 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 and banks, this portfolio is considered to have a low 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 to be covered by core capital and must be sufficient for expected future changes in regulations.

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 capital due to large single exposures may be reduced. External effects such as market turbulence, new regulations or idiosyncratic risk will affect the level of future 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 36,8 % and total capital ratio of 38,1% based on Basel II Pillar I methods at year end 2013.

Internal Capital Adequacy Assessment Processes (ICAAP) are conducted at least annually and Eksportfinans' capital strategy will be based on an assessment of the risk level in the organisation 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 of 31. December 2013.

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

RISK CATEGORY	**Capital requirement** **NOK mln.**
Credit risk	946
Split into:	
o *Governments*	0
o *Local and regional authorities*	24
o *Government owned corporations*	0
o *Multilateral development banks*	0
o *Institusjoner*	799
o *Enterprises*	0
o *Security for property*	1
o *Other commitments*	12
o *Securitisation*	110
Market risk	182
Operational risk	185
Total minimum capital requirement	**1 313**

Capital adequacy

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

***Table 3** – Capital adequacy 2011 - 2013*

	2013 I NOK mill	2012 I NOK mill	2011 I NOK mill
Core capital	6 040	5 314	4 786
Additional capital	220	628	975
Total capital	6 260	5 942	5 761
Core capital in percent	37 %	25 %	16,10 %
Total capital in percent	38 %	28 %	19,40 %
Total risk-weighted assets (incl. ”off-balance” elements, operational risk and trading portfolio)	16 416	21 243	29 661
Total balance	***100 793***	***157 406***	***213 929***

Table 4 gives an overview of the company’s assets as of 31 December 2013, 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 balance as per December 31st 2013*

ASSET TYPE	BOOK VALUE	RISK WEIGHT	BOOK VALUE	RWA	GUARANTEE	REMARKS
Loans	59 042	0 %	17 949	-	17 949	Guarantees from GIEK and Government
		20%	39 516	7 903	33 493	Guarantees from banks
		20%	1 468	294		Direct to or guarantees from municipalities
		35%	37	13		
		50%	45	23		
		100%	27	27		
Securities	26 462		7 619	1 374		Securitization
			18 843	1 913		Trading portfolio
Financial derivatives and Cash Collateral	8 427			737		
Other	6 862			1 432		6 bill. deposits
Off-balance transactions				23		
Operational risk				2 315		
Currency risk				362		
TOTAL	**100 793**			**16 416**		
Total risik-weighted assets / Total assets				16,3 %		

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 requirement is deducted using a three step procedure:

- Minimum capital requirements are calculated using the methods described above. This defines a minimum capital requirement of NOK 2.5 billion.

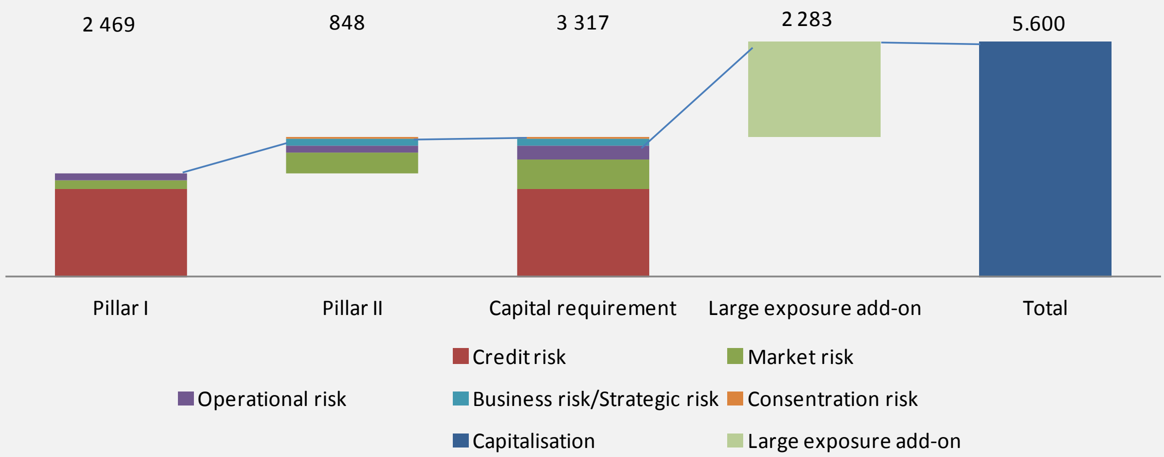
- In addition to the minimum capital requirement the company annually performs an Internal Capital Adequacy Assessment Process, ICAAP, to ensure the level of capital is sufficient. To identify key risks, both qualitative and quantitative methods are adopted. ThThe document on hand is the Pillar II assessment 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, NOK 0.8 billion of capital is required to cover 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 meet the EU's CRD large exposures regulations, the company currently holds another NOK 2.3 billion in capital in addition to the risk based capital requirement of NOK 3.3 billion.

Hence the company's risk based capital requirement is NOK 3.3 billion which the company will cover through core capital, while total capitalization is NOK 5.6 billion which also may 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 capitalization*



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

3.3 Large exposures

Limits for large exposures decreases the potential loss an institution can experience from a single counterparty due to unforeseen events. Since 01/01/2013 Eksportfinans is obliged to meet the large exposure provisions in the EU's Capital Requirement Directive. Eksportfinans is granted exemption by 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. As of 31/12/2013, only one remaining outstanding loan needs exemption.

3.4 New regulation for capital and liquidity risk

The Capital Requirement Directive IV (CRD IV) will be implemented in Norway through the EEA agreement. The final time schedule for implementing the new regulations is not yet decided. However, Eksportfinans is prepared to implement the new framework starting gradually from the third quarter 2014. In the capital assessment for 2014 the impact of new regulations is included in the calculations. The capital required in Pillar I has increased even though the balance is reduced. The main reason is that due to the new regulations bank exposure will require more capital. In addition a capital charge for credit valuation adjustment (CVA) for derivative credit risk is introduced.

"Leverage ratio":

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, the so-called "leverage ratio". Eksportfinans expects to comply with the leverage ratio requirement by a large margin when these rules are implemented.

Effect on capital from new OTC derivatives regulation:

European Market Infrastructure Regulation (EMIR) will be introduced to enhance the efficiency and the robustness of the derivatives marked. 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 the new rules will have only a limited impact, but there is still some uncertainty about the expected markets 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 analyses and assesses this information which is approved by the Board and submitted to the Norwegian FSA, "Finanstilsynet".

Calculation of capital under Pillar I and II are made using different methodologies. Eksportfinans analyses all material risk categories for the company and calculates capital requirements for every risk category. For 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 IIassessments 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 assets / liabilities meetings to analyze liquidity under different stress conditions. 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 REQUREMENT

5.1 Credit risk

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

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

Capital for credit risk is calculated with the Basel II standardized approach in Pillar I. Eksportfinans is exposed to financial institutions through direct exposure, guarantee exposure, derivative 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 the ISDA (International Swaps and derivatives Associations). The exposure is mitigated by regulated agreements for the exchange of collateral, known as Credit Support Annex (CSA agreements). In the CSA agreements, only cash is accepted as collateral.

5.1.1 Management and monitoring

Eksportfinans applies credit ratings and analyses from the major rating agencies (Moody's, Standard & Poor's and Fitch) to monitor the credit quality of all guarantors and credit counterparties. 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 governmental entities, and/ or financial institutions with an acceptable rating. Credit losses from guaranteed export loans will only occur if both the borrower and the highly rated guarantors 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 movements of swap contracts.

5.1.2 Portfolio information

As shown in the table below, the company has a portfolio of high credit quality.

Table 9 *– Aggregated credit exposure per rating class as per end of 2013*

(NOK mln)	Loans			Liquidity investments			Total
Rating	Unsecured	Guaranteed	Total loans	Liquidity reserve port.	PHA portfolio	Total liquidity holdings	
AAA	1.384	17.949	19.332	9.401	974	10.374	29.706
AA+/AA/AA-		3.460	3.460	4.329	576	4.905	8.365
A+/A/A-	4.035	25.832	29.868	3.772	1.085	4.857	34.724
BBB+/BBB/BBB-	628	3.378	4.006	-45	3.415	3.370	7.375
BB+/BB/BB-		1	1		304	304	305
B+/B/B-			-		1.030	1.030	1.030
CCC+/C			-		89	89	89
No international rating	1.453	415	1.867	1.126		1.126	2.993
Grand Total	**7.499**	**51.034**	**58.534**	**18.582**	**7.472**	**26.054**	**84.588**

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

5.1.3 Capital requirements for credit risk

Eksportfinans utilizes the standard method to calculate 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 the 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 derivate 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 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' exposure to market risk exposure. These include:

- Risk Limits for 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.
- The 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 external control functions. The external controls are most often performed by the company's auditor.

5.2.2 Capital requirement for market risk

The company uses the standard method for the calculation of minimum capital requirements. Additional capital requirements are applied 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 to cover market risk under 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 of 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 risk level. Losses due to operational risk have historically been low in Eksportfinans.

Operational risk may for example ariseout of legal risk, errors in accounting, data loss, embezzlement and fraud. These risks are reduced through increased focus on regulations concerning the use of information and communication technology (ICT Regulations), procedure manuals, training programs, ethical guidelines and a separate legal entity (compliance function). The company's framework for managing and controlling operational risk is the responsibility of the Risk Management team. The company is also audited and receives 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, and from the large volume and the number of derivatives which Eksportfinans has entered. Proper implementation of payments, and the correct settlement, 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 in the form of procedures and independent control of transactions.

Eksportfinans has various contingency plans that will take effect in the case of unexpected events. Contingency plans are made for liquidity, derivatives and for the overall organization.

5.3.2 Capital requirement for operational risk

Eksportfinans utilizes the basic indicator approach for calculating capital to cover operational risk under Pillar I. In a historical perspective, the Pillar I allocation is sufficient. Since capital is calculated from historical income without taking into account the current situation of Eksportfinans, we have allocated additional capital 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 wrong strategic decisions, loss of reputation , reduced rating, or limitation of 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, other main objectives are to service borrowers and investors and to secure the necessary expertise for the organization in 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 unexpected events in different areas, 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. 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 is not a risk category in Pillar I. The company reserves capital 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 analysis 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 lines in the amount of USD 1 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 mainly is 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 a conservative and professional liquidity management. Stressed scenarios have been implemented in Asset and Liability analyses. The results from scenarios indicate that the company has the ability to meet its obligations even under severe stress.