
Møre Boligkreditt

# Report from the Board of Directors

**OPERATIONS IN 2017**

Møre Boligkreditt AS is a wholly owned subsidiary of Sparebanken Møre, a regional Norwegian savings bank operating in the county of Møre og Romsdal. Møre Boligkreditt AS is licensed to operate as a mortgage company and to issue covered bonds, and is located at Sparebanken Møre's headquarter in Keiser Wilhelmsgate 29 – 33, in the city of Ålesund. Møre Boligkreditt AS is Sparebanken Møre's most important source of long term market funding and an important part of the parent bank's funding strategy.

During 2017, Møre Boligkreditt AS' net growth in acquired loans from Sparebanken Møre was NOK 1 352 million, and the company's lending portfolio amounted to NOK 21 162 million at year-end 2017. Mortgages in the company's cover pool are secured by residential properties, all at the time of acquisition within 75 per cent of the property's estimated value.

In 2017 Møre Boligkreditt AS issued one new floating rate bond loan of EUR 250 million, and also drew a total of NOK 1 000 million on two existing NOK denominated floating rate bond loans. Furthermore two NOK denominated bond loans with total outstanding NOK 2 250 million, and one SEK denominated bond loan with outstanding SEK 700 million, matured in 2017 and was fully paid in. Net growth in outstanding bond loans in 2017 was NOK 558 million, and total outstanding covered bond loan volume issued by Møre Boligkreditt AS amounts to NOK 18 823 million.

**RATING OF THE COMPANY'S ISSUES OF COVERED BONDS**

The rating agency Moody's has given all covered bonds issued by Møre Boligkreditt AS an Aaa- rating.

**THE MORTGAGE COMPANY'S ANNUAL FINANCIAL STATEMENTS**

The financial statements of Møre Boligkreditt AS show a profit before tax of NOK 213 million, compared with NOK 208 million in 2016. Interest income amounted to NOK 530 million, compared with NOK 502 million in 2016, while interest expenses totaled NOK 269 million, compared with NOK 260 million in 2016. Total operating costs amounted to NOK 38 million, compared with NOK 33 million in 2016.

Møre Boligkreditt AS had no losses and allocated no provisions for individual impairment in 2017. The company decreased provisions for collective impairment in 2017 with NOK 3 million. The amount allocated for collective impairment was NOK 2 million by year end 2017. Profit after tax amounted to NOK 165 million, compared with NOK 156 million in 2016. Taxes amounted to NOK 48 million, compared with NOK 52 million in 2016. Total assets at the end of 2017 amounted to NOK 21 748 million compared with NOK 20 972 million at the end of 2016. Loans and receivables from customers amounted to NOK 21 162 million, compared with NOK 19 810 million at the end of 2016.

The company's substitute assets included in the cover pool amounted to NOK 85 million, compared with NOK 743 million as at 31 December 2016. Over-collateralisation, calculated as the value of the coverpool relative to the value of outstanding covered bond loan debt was 13.3 per cent as at 31 December 2017, compared with 12.4 per cent as at 31 December 2016.

Møre Boligkreditt AS' liquidity portfolio consisting of Liquidity Coverage Ratio (LCR) eligible assets amounted to NOK 60 million.

It is the opinion of the Board of Directors that the presented financial statements provide correct and adequate information about the company's operations and status as at 31 December 2017.

**CAPITAL STRENGTH**

Paid in equity and retained earnings amounted to NOK 1 667 million, compared to NOK 1 509 million as at 31 December 2016. Risk weighted assets amounted to NOK 8 936 million as at 31 December 2017, compared to NOK 8 722 million last year. Net equity and subordinated loan capital amounted to NOK 1 476 million, compared to NOK 1 313 million as at 31 December 2016. This corresponds to a capital adequacy/core capital ratio of 16.5 per cent as at 31 December 2017, compared to 15.1 per cent last year. Møre Boligkreditt AS uses internal rating based (IRB) models to calculate capital requirements for credit risk.

**EFFECT OF TRANSITION TO IFRS 9**

The company's equity will be charged with NOK 15 million after tax as a consequence of increased impairments due to implementation of IFRS 9.

The implementation of IFRS 9 will have no effect on Møre Boligkreditt AS' common equity tier 1 capital as expected loss according to the capital adequacy requirements already exceeds the company's calculated ECL according to IFRS 9.

Further information is given in Note 1.13.

**RISKS**
Møre Boligkreditt AS is subject to a number of acts, regulations, recommendations and regulatory provisions. These regulations largely stipulate restrictions concerning the scope of the company's various risk exposures.

The Board and the Managing Director of Møre Boligkreditt AS are responsible for ensuring that proper risk management is established, and that such risk management is adequate and complies with current laws and regulations. Operational risk management in Møre Boligkreditt AS is maintained by Sparebanken Møre according to a service agreement concluded between Møre Boligkreditt AS and Sparebanken Møre.

Risk management emphasizes identifying, measuring and managing the company's risk elements in a manner that ensures that Møre Boligkreditt AS complies with the professional credit regulations and keeps the various risks at a low level.

**CREDIT RISK**
Credit risk is defined as the risk of losses associated with customers or other counterparties being unable to fulfill their obligations at the agreed time and pursuant to written agreements, and that the received collateral is not covering outstanding claims.

The credit risk strategy adopted by the company defines which loans can be acquired by the company. The strategy stipulates criteria for both borrowers and the collateral for the loans that can be acquired. At year-end 2017 , the mortgages in the cover pool had an average loan-to-value ratio of 58 per cent, calculated as mortgage amount relative to the value of the property used as collateral. The Board regards the quality of the loan portfolio as very good and the credit risk as low.

**MARKET RISK**
Market risk is the risk that will arise due to the mortgage company holding or assuming positions in lending and financial instruments in which the values over time will be affected by changes in market prices. Møre Boligkreditt AS must, pursuant to laws and regulations, have very low market risk and Board approved restrictions concerning its maximum exposure to market risk. The company utilizes financial derivatives to keep this type of risk at a low level. A specific market strategy has been adopted for Møre Boligkreditt AS which establishes the limits for this type of risk. The company's positions in fixed interest and foreign currencies are hedged with financial derivatives. The Board considers the overall market risk as low.

**LIQUIDITY RISK**
Liquidity risk is the risk that Møre Boligkreditt AS will be unable to fulfill its obligations without substantial extra costs being incurred in the form of decline in asset values, forced sales or more expensive funding. The company has adopted a liquidity risk strategy and established limits for long-term funding and short-term liquidity risk limits. Bonds issued by Møre Boligkreditt AS have a soft bullet structure in which the company has the opportunity to extend the term of its borrowing by up to 12 months. Møre Boligkreditt AS reports LCR of 295 per cent by year-end 2017 . The Board regards the company's liquidity risk as low.

**OPERATIONAL RISK**
Operational risk is the risk of losses due to inadequate or failing internal processes, human error, system failures or external events. Møre Boligkreditt AS has entered into a management agreement with Sparebanken Møre. The services covered by this agreement include administration, production, IT operations, and financial and risk management. Although the operational risk of Møre Boligkreditt AS is dependent of Sparebanken Møre's ability to manage this type of risk, Møre Boligkreditt AS independently bear risk associated with errors in the deliveries and services provided by Sparebanken Møre.

The evaluation of the management and control of operational risk is also afforded considerable space in the Group's annual ICAAP. The operational and established yearly internal control report, both within Sparebanken Møre and by the Managing Director of Møre Boligkreditt AS, is an important tool for reducing operational risk. The internal control reports will help identifying any operational risk, and enable action to be taken. The Board regards the company's operational risk as low.

**CORPORATE GOVERNANCE STATEMENT**
Møre Boligkreditt AS complies with the latest Norwegian Code of Practice for Corporate Governance. Møre Boligkreditt AS was established as part of Sparebanken Møre's long-term funding strategy with the purpose of funding the bank through issuing covered bonds. Møre Boligkreditt AS helps ensure that the Sparebanken Møre Group properly manages its assets, as well as providing additional assurance that goals and strategies are achieved and realized.

The Board ensures that risk management and internal control are adequate and systematic, and that they have been established in compliance with the law and regulations, articles of association, ethical guidelines, instructions, and external and internal guidelines. The Board shall lay down principles and guidelines for risk management and internal control for the various levels of activity pursuant to the company's risk bearing capacity, and assure themselves that the strategies and guidelines are being followed. The Board shall systematically and regularly assess the strategies and guidelines for risk management.

In order to ensure that Møre Boligkreditt AS' risk management and internal control are carried out satisfactorily, the Board continuously receives various types of reports throughout the year from Sparebanken Møre's control bodies, as well as from internal and external auditors. The Board actively participates in the annual implementation of the long-term strategic plan. The Board revises and approves all the company's general risk management documents at least once a year. Every year in the 4th quarter, the Managing Director of Møre Boligkreditt AS reports on the structure and efficiency of the company's internal control.

The overall responsibility for ensuring that principles of accounting and financial control are identified, monitored and evaluated is outsourced to the Finance Department and the Risk Management department in Sparebanken Møre. The responsibility for the preparation of financial statements, and the reporting of these to the Managing Director in Møre Boligkreditt AS, is assigned to the Finance department in the parent bank.

The Board of Directors (the Board) and the Chairman of the Board is elected by the General Meeting, and shall consist of four to six members elected for a period of two years. After one year, at least half of the elected members shall step down, based on the drawing of lots, while the remainder shall step down after one more year. Board members can be re-elected.

The Chairman of the Board in Møre Boligkreditt AS shall, by the end of October and in consultation with the Managing Director, set out a proposed annual plan for the Board's work for the coming year and the main items on the agendas of board meetings for the next calendar. Each year, the Board evaluates its own methods and professional competence to see if improvements can be made.

The Chairman of the Board shall ensure that the Board of Directors convenes at least once every quarter and otherwise as often as is called for by the nature of the company's activities, or when requested by a board member. A valid Board resolution is passed by at least three board members voting in favor of the resolution. The annual General Meeting shall be held each year before the end of June.

The company's paid-in equity of NOK 1 500 000 000 consist of 1 060 000 shares of NOK 1 250 fully paid in, together with a share premium of NOK 175 000 000. With the consent of the Financial Supervisory Authority of Norway, the General Meeting may raise additional share capital, subordinated loan capital and guarantee capital.

**INTERNAL CONTROL**

The Managing Director of Møre Boligkreditt AS is responsible for establishing proper risk management and internal control based on the guidelines decided by the Board, making sure that these are adhered to, and providing the Board with information about developments within the various areas. The Managing Director reports on structure and efficiency of the company's internal control in the fourth quarter every year.

Møre Boligkreditt AS bases its internal control on an overall risk management process. This is set out in various documents included in the company's Risk Policy. The Board has decided upon guidelines for establishing proper risk management and internal control, and ensures that risk management and internal control in Møre Boligkreditt AS are adequate and systematic, and that the processes have been established in compliance with the law and regulations, articles of association, instructions, and external and internal guidelines. The Board systematically and regularly assesses the strategies and guidelines for risk management.

In the financial reports, written procedures relating to critical areas within the company, as well as the level of achievement of both the company's financial goals, and the qualitative goals relating to risk managing are presented. This ensures a close and accurate monitoring of the financial reporting and increases the possibility of early risk detection. The Managing Director of Møre Boligkreditt AS has the primary responsibility for managing risk associated with the company's operational and financial reporting, which is the foundation for satisfactory quality in the financial reporting.

The internal control and risk assessment of the financial reporting is one of the areas of focus in the Managing Director's annual confirmation on the quality of, and the compliance with internal controls. The Internal Auditor has an important role in the monitoring of internal controls related to financial reporting. The financial statements provide additional information about the risk management and internal control of Møre Boligkreditt AS.

**PROFIT DISTRIBUTION POLICY**

Møre Boligkreditt AS' profit distribution policy states the following: "The company shall make a maximum payment from the profit generated in the fiscal year, either in the form of a dividend or as a group contribution. Such payments, however, shall not conflict with the requirement for liquidity and financial strength of the company, and shall in any case abide by what is considered good and prudent business and accounting practice."

**GENERAL MEETING AND COMPANY BOARD**

The General Meeting is the supreme body of Møre Boligkreditt AS. The General Meeting of Møre Boligkreditt AS consists of the Board of Directors of Sparebanken Møre, Sparebanken Møre being the sole owner of the company. All board members of Sparebanken Møre are independent of the bank's day-to-day management and important business connections.

The Board shall consist of four to six members elected for a period of two years.

In electing the members of the Board, the goal is to meet the need for continuity and independence, as well as ensuring a balanced composition of the Board.

The Board's responsibilities and tasks are set forth in a separate document which is discussed and revised by the Board regularly. The document contains the dividing of responsibilities and tasks between the Board and the Managing Director of the company. Each year, the Board evaluates its own methods and professional competence.

**GOING CONCERN ASSUMPTION**

The Board is of the opinion that the prerequisites for the going concern assumption exist, and the Board confirms that the 2017 annual financial statements is prepared on the basis of the going concern assumption.

**EMPLOYEES**

Møre Boligkreditt AS had no employees at year-end 2017. One man-year from Sparebanken Møre is dedicated full time to the mortgage company. Furthermore, a number of services are outsourced to Sparebanken Møre, regulated by a specific agreement between the mortgage company and the bank.

No special work environment measures have been implemented in Møre Boligkreditt AS.

**EQUAL OPPORTUNITIES**

The Sparebanken Møre Group strives for gender-neutral employment – and wage policy. The Board and management in Sparebanken Møre systematically and actively work to promote equality. The Board of Møre Boligkreditt AS consists of two men and three women.

**POLLUTION OF THE EXTERNAL ENVIRONMENT**

The activities of Møre Boligkreditt AS do not pollute the external environment.

**OTHER FACTORS**

As far as the Board is aware, no events have occurred after the end of the financial year 2017 of material importance to the position and result of Møre Boligkreditt AS.

**RESEARCH AND DEVELOPMENT**

Møre Boligkreditt AS has no research and development activities.

**CORPORATE SOCIAL RESPONSIBILITY**

For information on corporate social responsibility, Møre Boligkreditt AS being a wholly owned subsidiary of Sparebanken Møre, we refer to Sparebanken Møre Group's Annual Report.

**FUTURE PROSPECTS**

The oil related part of the Norwegian economy experienced a slowdown also in 2017. A strong household sector due to record low interest rates, low unemployment levels, together with a solid public sector have however kept the production levels high in several other sectors. The weak NOK is positive for the competitiveness of the export industry and the tourist industry. We will probably see the same development with selective growth also in the coming quarters.

The development of house prices, together with growth in debt, is the most important risk factors to Norwegian households. Important risk factors going forward are also the oil price development, macroeconomic growth in export markets and the NOK exchange rate. Should the Norwegian economy experience a negative development, monetary and fiscal policy can be moved in an even more expansive direction.

The combined activity of businesses located in Møre og Romsdal county remains high despite the decline in the petroleum related industries, and unemployment is declining. The registered unemployment rate in the county of Møre og Romsdal was 2.4 per cent in December 2017, which is the same unemployment level as the Norwegian national average. We expect unemployment in the county to stay around national average levels.

Retail lending growth in Sparebanken Møre Group was 7.2 per cent in 2017, but in line with signs of weaker national growth in household debt, we also expect to see the Sparebanken Møre Group retail lending growth rate slowing down somewhat in the coming quarters.

The Board believes that the reduction in unemployment, low interest rates and high disposable household income will contribute to further mortgage loan growth in Sparebanken Møre. This mortgage growth will position Møre Boligkreditt AS to acquire further mortgage loan portfolios from the parent bank, and further increase the volume of outstanding bond loans from Møre Boligkreditt AS.

**DISTRIBUTIONS**

Profit after tax amounted to NOK 165 million in 2017. The Board of Directors proposes to the annual General Meeting to pay out NOK 152 million as dividend and to allocate NOK 13 million to retained earnings.

Ålesund, 31 December 2017

5 February 2018

**THE BOARD OF DIRECTORS OF MØRE BOLIGKREDITT AS**

Kjetil Hauge
CHAIRMAN

Britt Iren Tøsse Aandal

Elisabeth Blomvik

Geir Tore Hjelle

Sandra Myhre Helseth

Ole Kjerstad
MANAGING DIRECTOR

# Statement of income

STATEMENT OF INCOME

| Amounts in NOK million | Notes | 2017 | 2016 |
|---|---|---|---|
| Interest income from: | | | |
| Loans to and receivables from credit institutions | 11 | 2 | 2 |
| Loans to and receivables from customers | | 525 | 494 |
| Certificates, bonds and other interest-bearing securities | | 3 | 6 |
| Interest income | 2 | 530 | 502 |
| Interest expenses in respect of: | | | |
| Loans from credit institutions | 11 | 17 | 18 |
| Debt securities | 9 10 11 | 252 | 242 |
| Interest expenses | 9 | 269 | 260 |
| Net interest income | 4 | 261 | 242 |
| Commission income | | 1 | 0 |
| Net change in value of securities and related derivatives | | -14 | 0 |
| Wages, salaries and general administration costs | | 3 | 2 |
| Other operating costs | 11 | 35 | 31 |
| Total operating costs | 12 | 38 | 33 |
| Profit before impairment on loans and taxes | | 210 | 209 |
| Impairment on loans | 3 5 | -3 | 1 |
| Pre tax profit | | 213 | 208 |
| Taxes | 13 | 48 | 52 |
| Profit after tax | | 165 | 156 |
| Proposed distribution: | | | |
| Proposed dividends | | 152 | 156 |
| Retained earnings | | 13 | 0 |
| Total | | 165 | 156 |

STATEMENT OF COMPREHENSIVE INCOME

| Amounts in NOK million | 2017 | 2016 |
|---|---|---|
| Profit after tax | 165 | 156 |
| Other comprehensive income | 0 | 0 |
| Total comprehensive income after tax | 165 | 156 |

# Statement of financial position

Assets

| Amounts in NOK million | Notes | 31.12.2017 | 31.12.2016 |
|---|---|---|---|
| Loans to and receivables from credit institutions | 4 6 8 10 11 | 85 | 271 |
| Loans to and receivables from customers | 2 3 4 5 6 8 10 | 21 162 | 19 810 |
| Certificates and bonds | 4 6 8 10 | 60 | 522 |
| Financial derivatives | 4 7 8 9 | 439 | 368 |
| Deferred tax asset | | 2 | 0 |
| Total assets | | 21 748 | 20 972 |

Liabilities and equity

| Amounts in NOK million | Notes | 31.12.2017 | 31.12.2016 |
|---|---|---|---|
| Loans from credit institutions | 4 6 8 11 | 1 202 | 1 141 |
| Debt securities issued | 4 6 8 10 11 | 18 823 | 18 265 |
| Financial derivatives | 4 7 8 9 | 4 | 4 |
| Tax payable | | 52 | 54 |
| Total liabilities | | 20 081 | 19 463 |
| Share capital | 15 | 1 325 | 1 175 |
| Share premium | | 175 | 175 |
| Paid-in equity | | 1 500 | 1 350 |
| Retained earnings | | 167 | 159 |
| Total equity | 14 | 1 667 | 1 509 |
| Total liabilities and equity | | 21 748 | 20 972 |

Ålesund, 31 December 2017

5 February 2018

**THE BOARD OF DIRECTORS OF MØRE BOLIGKREDITT AS**

Kjetil Hauge
CHAIRMAN

Britt Iren Tøsse Aandal

Elisabeth Blomvik

Geir Tore Hjelle

Sandra Myhre Helseth

Ole Kjerstad
MANAGING DIRECTOR

# Statement of changes in equity

**31.12.2017**

| Amounts in NOK million | Notes | Total equity | Share capital | Share premium | Retained earnings |
|---|---|---|---|---|---|
| Equity as at 31 December 2016 | | 1 509 | 1 175 | 175 | 159 |
| Total comprehensive income for the period | | 165 | | | 165 |
| Issue of share capital | | 150 | 150 | | |
| Dividends | | -156 | | | -156 |
| Equity as at 31 December 2017 | 14 15 | 1 667 | 1 325 | 175 | 167 |

The share capital consists of 1 060 000 shares at NOK 1 250, a total of NOK 1 325 million. All shares are owned by Sparebanken Møre. The issue of share capital of NOK 150 million was fully paid on 27 February 2017, approved by the Norwegian FSA 20 March 2017, and registered in the Norwegian Register of Business Enterprises 4 April 2017.

Proposed dividend as of 31 December amounts to NOK 152 million.

**31.12.2016**

| Amounts in NOK million | Notes | Total equity | Share capital | Share premium | Retained earnings |
|---|---|---|---|---|---|
| Equity as at 31 December 2015 | | 1 329 | 975 | 175 | 179 |
| Total comprehensive income for the period | | 156 | | | 156 |
| Issue of share capital | | 200 | 200 | | |
| Dividends | | -176 | | | -176 |
| Equity as at 31 December 2016 | 14 15 | 1 509 | 1 175 | 175 | 159 |

The share capital consisted of 940 000 shares at NOK 1 250, a total of NOK 1 175 million. All shares were owned by Sparebanken Møre. Dividend as of 31 December 2016 amounted to NOK 156 million.

# Statement of cash flow

| Amounts in NOK million | Notes | 2017 | 2016 |
|---|---|---|---|
| **Cash flow from operating activities** | | | |
| Interest, commission and fees received | | 527 | 496 |
| Interest, commission and fees paid | | -14 | -19 |
| Operating expenses paid | | -38 | -33 |
| Income taxes paid | | -51 | -63 |
| Payment for acquiring loans from the Parent Bank | | -5 108 | -7 838 |
| Payment related to instalment loans and credit lines to customers | | 3 759 | 4 934 |
| Net cash flow from operating activities | 4 12 | -925 | -2 523 |
| | | | |
| **Cash flow from investing activities** | | | |
| Received interest, commission and fees related to certificates, bonds and other securities | | 3 | 6 |
| Proceeds from the sale and settlement of certificates, bonds and other securities | | 1 170 | 114 |
| Purchases of certificates, bonds and other securities | | -707 | -231 |
| Changes in other assets | | -14 | -3 |
| Net cash flow from investing activities | 4 8 10 | 452 | -114 |
| | | | |
| **Cash flow from financing activities** | | | |
| Paid interest, commission and fees related to issued bonds | | -252 | -242 |
| Net change in loans from credit institutions | | 61 | 171 |
| Proceeds from covered bond issuance | | 3 350 | 3 494 |
| Redemption of issued covered bonds | | -2 883 | -828 |
| Dividend paid | | -156 | -176 |
| Changes in other debt | | 17 | 4 |
| Issue of share capital | | 150 | 200 |
| Net cash flow from financing activities | 10 15 | 287 | 2 623 |
| | | | |
| Net change in cash and cash equivalents | | -186 | -14 |
| Cash balance at 01.01 | | 271 | 285 |
| Cash balance at 31.12 | 6 | 85 | 271 |

The cash flow statement shows cash payments received and made, and cash equivalents throughout the year. The statement has been prepared according to the direct method. The cash flows are classified as operating activites, investing activites or financing activites. Financial position line items have been adjusted for the impact of foreign exchange rate changes. Cash and cash equivalents are defined as loans to and receivables from credit institutions with no agreed period of notice. Loans and receivables from credit institutions are entirely to Sparebanken Møre.

# Note 1

## ACCOUNTING POLICIES

**1.1 Main policies**

Møre Boligkreditt AS (the company) is part of the Sparebanken Møre Group. The company's Head Office is located at Keiser Wilhelmsgt. 29/33, P.O.Box 121 Sentrum, 6001 Ålesund, Norway.

The company`s financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS), which have been issued by the International Accounting Standards Board, and approved by the EU as at 31 December 2017.

**Changes in accounting policies and presentation**
There were no material changes to the accounting policies in 2017.

**New or revised standards applicable for 2017**
The mortgage company has not implemented any new or revised standards/interpretations in 2017.

**Approved IFRSs and IFRICs with future effective dates**
Standards and interpretations that are issued up to the date of issuance of the financial statements, but not yet effective are disclosed below. The company's intention is to adopt the relevant new and amended standards and interpretations when they become effective, subject to EU approval before the financial statements are issued.

• IFRS 9 Financial Instruments will replace IAS 39 as of 1 January 2018. Please see note 1.13 for information and specifications regarding the effects of the implementation.

The following approved IFRSs with future effective dates are expected not to be relevant for the company, thus have no impact on the financial statements of the company:

• IFRS 15 Revenues from Contracts with Customers

• IFRS 16 Leases

**1.2 Revenue recognition**
Interest income is recognised as income using the effective interest rate method, including loan related fees and charges.

**1.3 Currency**
All amounts in the financial statements and notes are stated in NOK million, unless otherwise specified. The company's functional currency and presentation currency is Norwegian kroner (NOK). Cash items in foreign currencies are converted into NOK at the exchange rates at the reporting date. Changes in value for such items due to exchange rates differences between the transaction date and the reporting date are recognised in the income statement. Income statement items are converted using the exchange rate at the time of the transaction.

**1.4 Recognition and derecognition of financial assets and liabilities**
Financial assets and financial liabilities are recognized in the statement of financial position when the company becomes a party to the contractual provisions of the instruments. All financial instruments are measured initially at fair value plus transaction costs, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss. Fair value at initial recognition is normally equal to the transaction price.

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire, or the company transfers the financial asset in such a way that substantially all of the potential for risk and rewards of ownership of the asset is transferred. A financial liability is derecognised when the financial liability is discharged, cancelled or expired.

### 1.5 Financial instruments

#### 1.5.1 Classification

The company's financial instruments are classified at initial recognition based on type of instrument and their purpose. Møre Boligkreditt AS has the following categories of financial instruments:

• Financial assets held for trading. This category includes derivatives, including derivatives designated as hedging instruments.

• Financial assets designated as at fair value through profit or loss. This category includes the company's holding of covered bonds.

• Loans and receivables (at amortised cost). The category includes loans and receivables from customers and receivables from the parent bank.

• Other financial liabilities. This category includes securities-related debt recorded in the statement of financial position at amortised cost.

#### 1.5.2 Measurement

**Measurement at amortised cost**
Financial instruments at amortised cost include loans to and receivables from credit institutions, loans to and receivables from customers, loans from credit institutions and debt securities issued. These are recognised at fair value at initial recognition, with the addition of establishment fees and other commissions. Loans are subsequently measured at amortised cost by applying the effective interest rate method. The effective rate of interest is the rate which exactly discounts estimated, future cash flows over the loan's expected life to the carrying amount of the financial instrument as shown in the statement of financial position. In this process all cash flows are estimated, and all contract-related terms and conditions relating to the loan are taken into consideration. Fees and commissions are amortised over the life of the loans as an integral part of the instruments effective interest rate.

**Measurement at fair value**
Møre Boligkreditt AS has covered bonds and financial derivatives (interest rate swaps and currency swaps) measured at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Furthermore, the fair value measurements are categorized into the following three levels based on the inputs used to measure fair value:

- Financial instruments traded in an active market
For financial instruments traded in an active market, quoted price obtained from either an exchange, a broker or a pricing agency is used to measure fair value. None of the financial instruments of the company are quoted in an active market

- Financial instruments not traded in an active market
For financial instruments that are not traded in active markets various valuation techniques are used to measure fair value. These measurements are divided into two types based on the inputs used in the measurement:

1) Measurement based on observable market data:

• Recently observed transactions in the same instrument between informed, willing and unrelated parties

• Instruments traded in an active market, which are substantially similar to the instruments that are valued

2) Measurement based on other than observable market data:

• Estimated cash flows

• Other valuation techniques where material parameters are not based on observable market data

**Impairment**
Møre Boligkreditt AS assesses whether there is objective evidence that the financial assets have been exposed to loss events that have negative effects on future cash flows. A financial asset or group of financial assets are impaired if there is objective evidence that one or more loss events have occurred after initial recognition of the asset or assets. See note 3 for further description. Impairment of loans is recognised in the income statement.

**Individual assessment**
An impairment loss is recognised for a loan on an individual basis if there is objective evidence that impairment exists when they are assessed individually. Examples of objective evidence of impairment that may be observed for assets on individual basis are:

a) Significant financial problems in the case of the borrower in question

b) Default of payment or other significant breaches of contract. A loan or other asset is considered to be in default if the borrower fails to pay when due, or overdrawn amounts are not repaid, within a maximum of 90 days past due limit

c) Amendments to terms or conditions as a result of the borrower's financial difficulties, such as deferment of payment or new credit to make the borrower able to pay an instalment, or amendments to interest rate terms

d) It becomes probable that the debtor will enter into debt negotiations or other financial restructuring, or that the debtor's assets are subject to bankruptcy proceedings

**Collective assessment**
Assets for which no objective evidence of impairment is observed on an individual instrument basis are grouped based on similar credit risk characteristics and assessed on a collective basis. Collective impairments are recognised for sub-groups of loans when there is observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of loans since the initial recognition, while the decrease cannot yet be identified with the individual financial assets in the group.

The collective assessment is based on risk classification and loss experience for the group in question.

Objective evidence of loss events for groups of loans include:

a) Negative changes in the payment status for the borrowers in the group

b) Negative changes in national or regional economic conditions that have occurred at the reporting date that have not been fully taken into account in the group's risk classification system

An impairment is reversed if the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised. If objective evidence of impairment is identified, impairment is calculated as the difference between the assets' carrying amount and the present value of estimated future cash flows discounted using the effective interest rate. The effective interest rate used to calculate the impairment is the effective interest rate applicable to the loan before objective evidence of impairment was identified. The effective interest rate is accordingly not adjusted to reflect changes in the loan's credit risk or other amendments to terms. Impairment reduces the assets' carrying amount and is recognised in the income statement as "Impairment on loans". Interest income calculated using the effective interest method based on carrying amounts net of impairment, is included in "Net interest income".

**1.5.3 Hedge accounting**
The company applies fair value hedge accounting and hedges interest rate risk and foreign exchange rate risk on debt securities issued with fixed interest rate or foreign currency denomination. Hedge accounting requires a clear, direct and proven correlation between changes in fair value or of the hedged item arising from the hedged risk and changes in fair value of the financial derivative (hedging instrument).

At the origination of the hedge, the relationship between the hedging instrument and the hedged item is documented. In addition the objectives and the strategy for the hedging transaction are documented. Changes in fair value related to the hedged risk of the hedged item and the hedging instrument are evaluated periodically to ensure sufficient hedge effectiveness. Hedging instruments are carried at fair value and are recorded under "Net change in value of securities and related derivatives".

For the hedged item, changes in fair value due to the hedged risk are recognised as an adjustment to the carrying value of the debt securities, and are recorded under "Net change in value of securities and related derivatives".

**1.6 Presentation in the statement of financial position and income statement**

**Lending**
Lending is presented in the statement of financial position, depending on the counterparty, either as "Loans to and receivables from credit institutions" or "Loans to and receivables from customers". Interest income is recognised in the lines "Interest income from: Loans to and receivables from credit institutions and Loans to and receivables from customers" using the effective interest rate method. Impairments are recognised in "Impairment on loans".

**Certificates and bonds**
The holding of covered bonds measured at fair value is presented in the balance sheet as "Certificates and bonds". The interest income is included in "Certificates, bonds and other interest-bearing securities" and fair value changes in "Net change in value of securities and related derivatives".

**Liabilities to financial institutions**
Liabilities to financial institutions are recognised in the statement of financial position as "Loans from credit institutions". Interest expenses on liabilities are included in "Interest expenses in respect of loans from credit institutions" based on the effective interest rate method.

**Debt securities issued**
Debt securities issued include issued bonds. Interest expenses on the financial instruments are included in "Interest expenses in respect of debt securities" based on the effective interest rate method.

### 1.7 Tax

Tax cost consists of payable tax for the income year, any tax payable for previous years, and any changes in deferred tax. Deferred tax is calculated on the temporary differences in accordance with IAS 12 Income Taxes. A temporary difference is the difference between the carrying amount of an asset or liability and the taxable value of that asset or liability. Tax increasing and tax reducing temporary differences that are reversed or could be reversed in the same period are offset and the net amount recognised. Deferred tax assets are recognised in the statement of financial position to the extent that it is likely they will be able to be utilised against future taxable income. Deferred tax (tax assets) is recognised at its nominal value and reported on a separate line on the statement of financial position.

### 1.8 Provisions, contingent assets and contingent liabilities

A provision is only recognised when an obligation exists (legal or constructive) as a result of a previous event, and it is likely that an outflow of resources embodying economic benefits will be required to fulfil the obligation, and a reliable estimate of the amount of the obligation can be made. Provisions are recognised at the amount that expresses the best estimate of the expenditure required to fulfil the existing obligation. If material the time value of money is taken into account when calculating the size of the provision. Contingent assets or contingent liabilities are not recognised.

### 1.9 Events occurring after the reporting period

New information about conditions that existed at the end of the reporting period is taken into account in the annual financial statements. Events after the reporting date that do not affect the mortgage company's position at that date, but will affect the mortgage company's financial position in the future, are disclosed if they are material.

### 1.10 Statement of cash flow

The cash flow analysis is prepared on the basis of the direct method with cash flows attributable to operational, investment and financing activities. Cash flows from operational activities are net receipts and payments from lending activities, and payments generated from costs associated with operational activities. Cash flows from investing activities are purchases or sales of bonds and other securities. Cash flows from other securities transactions, issuing and repaying securities issued, and equity are defined as financing activities.

### 1.11 Equity

The equity consists of paid-in share capital, share premium and retained earnings. Møre Boligkreditt AS recognises proposed dividends and group contributions as retained earnings until approved by the company's general meeting. Transaction costs associated with an equity transaction are recognized directly against Equity.

### 1.12 Use of estimates in the preparation of the annual financial statements
In the preparation of the financial statements, management makes estimates and assumptions that affect the financial statements and the reported amounts of assets and liabilities, income and costs. The assessments are based on historical experience and assumptions deemed to be reasonable and sensible by the management. There is a risk that the actual outcomes will deviate from the estimated outcomes.

The financial assets and liabilities of the company are allocated to different categories according to IAS 39 by the management. Normally this process requires limited judgment.

In the opinion of the management, the most important areas which involve critical estimates and assumptions are as follows:

**Impairment on loans**
The company examines the lending portfolio at least every quarter. Loans are reviewed individually and deemed to be impaired when there is objective evidence of impairment, at the latest when the commitment have been in default for more than 90 days. Similarly, groups of loans are assessed collectively for impairment on a quarterly basis. When examining the lending portfolio to assess whether loans or groups of loans are impaired, management relies on approximation and prior experience.

**Fair value assessments**
For financial instruments which are not traded in active markets, various methods are applied in order to ascertain fair value. Further information and a description of the techniques used, is stated above. Financial instruments not traded in an active market are measured based on in-house judgments and assumptions with regards to current market conditions, or valuations from other market participants.

### 1.13 The effect of implementation of IFRS 9 at 01.01.2018

IFRS 9 Financial Instruments will replace IAS 39 as of 1 January 2018. IFRS 9 introduces a business oriented model for classification and measurement of financial instruments, an expected loss model for impairments and a new accounting regulation for hedge accounting.

For Møre Boligkreditt AS the transition to IFRS 9 will impact the company's accounting for basisswap spreads as these will be charged to OCI as of 1.1.2018 as part of the new hedge accounting model where the cost of hedging can be charged to OCI in certain circumstances. In addition IFRS 9 fundamentally changes the loan loss impairment methodology. The standard replaces IAS 39's incurred loss approach with a forward looking expected credit loss (ECL) approach.

The measurement of impairment losses both under IFRS 9 and IAS 39 across all categories of financial assets requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Sparebanken Møre Group has developed an ECL-model based on the Group's IRB parameters.

The ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL model that are considered accounting judgements and estimates include:

- The internal credit grading model, which assigns PDs to the individual grades
- The criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a lifetime ECL basis and the qualitative assessment
- Development of ECL models, including the various formulas and the choice of inputs
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models

As a consequence of low levels of PDs and low LTVs almost the entire portfolio in Møre Boligkreditt AS is assigned to stage 1 in the ECL-model, thus loss is calculated according to 12 months ECL for the major part of the company's portfolio.

The following tables set out the impact of adopting IFRS 9 on the statement of financial position, and retained earnings including the effect of replacing IAS 39's incurred credit loss calculations with IFRS 9's ECLs.

The following table shows a reconciliation between the carrying amounts under IAS 39 to the balances reported under IFRS 9 as of 1 January 2018.

| | IAS 39 measurement | | | IFRS 9 | |
|---|---|---|---|---|---|
| | Category | Amount | Remeasurement | Amount | Category |
| Amounts in NOK million | | **31.12.2017** | ECL | **01.01.2018** | |
| **Financial assets** | | | | | |
| Loans to and receivables from credit institutions | L & R - AC | 85 | | 85 | AC |
| Loans to and receivables from customers | L & R - AC | 21 162 | -20 | 21 142 | AC |
| Certificates and bonds | FVPL | 60 | | 60 | FVPL |
| Financial derivatives | FVPL | 439 | | 439 | FVPL |

The following table reconciles the aggregate opening loan loss provision allowances under IAS 39 to the ECL allowances under IFRS 9.

| Amounts in NOK million | **Loan loss provision under IAS 39 as at 31 December 2017** | **Remeasurement** | **ECLs under IFRS 9 at 1 January 2018** |
|---|---|---|---|
| Impairment allowance for: | | | |
| Loans and receivables per IAS 39/financial assets at amortised cost under IFRS 9 | 2 | 20 | 22 |
| | 2 | 20 | 22 |

The ECL model's calculation of expected loss for Møre Boligkreditt AS at 1.1.2018 results in increased impairments of NOK 20 million.

The impact of transition to IFRS 9 on retained earnings is, as follows:

| Amounts in NOK million | **Retained earnings** |
|---|---|
| **Retained earnings** | |
| Closing balance under IAS 39 (31 December 2017) | 167 |
| Recognition of IFRS 9 ECLs | -20 |
| Deferred tax in relation to the above | 5 |
| Opening balance under IFRS 9 (1 January 2018) | 152 |
| Total change in equity due to adopting IFRS 9 | -15 |

The company's equity will be charged with NOK 15 million after tax as a consequence of the implementation of IFRS 9.

The implementation of IFRS 9 will have no effect on Møre Boligkreditt AS' common equity tier 1 capital as expected loss according to the capital adequacy requirements already exceeds the company's calculated ECL according to IFRS 9.

# Note 2

## OPERATING SEGMENTS

Møre Boligkreditt AS' business mainly comprises operations within the retail banking market. Møre Boligkreditt AS has only one operating segment. The following tables contain details of loans to customers by sector, business activity and geographical area.

| (MNOK) | Loans | |
|---|---|---|
| **Broken down according to sectors** | **31.12.2017** | **31.12.2016** |
| Agriculture and forestry | 3 | 1 |
| Fisheries | 6 | 2 |
| Manufacturing industries | 6 | 11 |
| Building and construction | 26 | 25 |
| Wholesale and retail trade, hotels | 5 | 8 |
| Property management | 215 | 246 |
| Transport and private/public services | 119 | 73 |
| Public entities | 0 | 0 |
| Activities abroad | 0 | 0 |
| Miscellaneous | 0 | 0 |
| Total corporate/public entities | 380 | 366 |
| Retail customers | 20 759 | 19 426 |
| Accrued interest income | 25 | 23 |
| Loans, nominal amount | 21 164 | 19 815 |
| Collective impairment | -2 | -5 |
| Loans to and receivables from customers | 21 162 | 19 810 |

**Geographical spesification**

| | Møre og Romsdal | | Remaining parts of Norway | | Foreign countries | | Total | |
|---|---|---|---|---|---|---|---|---|
| | **2017** | **2016** | **2017** | **2016** | **2017** | **2016** | **2017** | **2016** |
| Loans, nominal amount | 16 471 | 15 476 | 4 673 | 4 316 | 20 | 23 | 21 164 | 19 815 |
| In percentage | 77,8 | 78,1 | 22,1 | 21,8 | 0,1 | 0,1 | 100,0 | 100,0 |
| Interest income | 404 | 381 | 125 | 120 | 1 | 1 | 530 | 502 |
| In percentage | 76,3 | 77,3 | 23,5 | 22,5 | 0,2 | 0,2 | 100,0 | 100,0 |

# Note 3

## IMPAIRMENT, LOSSES AND NON-PERFORMANCE

Møre Boligkreditt AS reviews its loan portfolio continuously. If there is objective evidence that a loan is impaired, the impairment loss is calculated quarterly as the difference between the carrying value of the loan and the estimated present value of future cash flows. Loans and loan commitments are assessed to see whether or not objective evidence exists that a loss event has occurred at the reporting date that have a negative impact on future cash flows. Examples of such objective evidence are significant financial problems at the borrower, payment defaults, significant breaches of contract, amendments to terms as a result of the borrower's financial difficulties, bankruptcy, etc.

If objective evidence of impairment exists, the impairment is estimated as the difference between the carrying amount and the present value of future cash flows. Estimates of future cash flows also take into account takeovers and sales of associated collateral, including expenses associated with such takeovers and sales.

When all collateral has been realised and there is no doubt that the mortgage company will not receive further payments relating to the loan, the impairment will be reversed and the actual loss will be booked. Nonetheless, the claim against the customer will remain and be followed up, unless a debt forgiveness agreement is reached with the customer.

Assets for which no objective evidence of impairment is observed on an individual instrument basis are grouped based on similar credit risk characteristics and assessed on a collective basis. Collective impairments are recognised for sub-groups of loans or loan commitments when there is observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of loans or loan commitments since the initial recognition, while the decrease cannot yet be identified with the individual financial assets in the group.

The Sparebanken Møre Group has developed its own collective impairment model and calculations are conducted each month based on input from the risk classification system, data warehouse, and assessments of macroeconomic factors. Changes to risk classification, negative developments in collateral values, and registered macroeconomic events that affect future estimated cash flows are taken into account in the model. The Group's model for collective impairment is tailored to Møre Boligkreditt AS' assumptions and operations.

No objective evidence of loss events requiring impairment on an individual loan or loan commitment basis was observed at the reporting date. The company has no loans in arrear above 90 days at year-end. The collective impairment model on this date indicates a decrease in collective impairments for the mortgage company's portfolio of NOK 3 million. Total impairment amounts to NOK 2 million as at 31 December 2017 .

# Note 4

## RISK MANAGEMENT

**Strategy**

The Sparebanken Møre Group`s, and thereby Møre Boligkreditt AS', long-term strategic development and goal achievement are supported by high quality risk- and capital management. The overall purpose of risk management and -control is to ensure that goals are achieved, to ensure internal and external reporting of high quality, and to make sure that the Group operates in accordance with relevant laws, rules, regulations and internal guidelines.

Risk-taking is a fundamental aspect of banking operations, which is why risk management is a central area in the day-to-day operations as well as in the Board of Directors' ongoing focus. Sparebanken Møre's Board of Directors has agreed overall guidelines for management and control throughout the Group. The Board of Directors of Møre Boligkreditt AS has agreed a separate risk policy for the company.

Møre Boligkreditt AS shall have a low risk profile and revenue generation shall be a product of customer related activities related to the company`s operations and purpose, not a product of financial risk-taking. In addition, the company has introduced separate policies for each significant risk area: credit risk, market risk, funding risk and counterparty risk. The risk strategies are adopted by the Board of Directors and revised at least once a year or when special circumstances should warrant it. The approved risk policies operationalize the business strategy set forth in the company's overall strategic plan. The company has established a follow-up and control structure which shall ensure that the overall framework of the strategic plan is adhered to at all times.

**Reporting**

Møre Boligkreditt AS focuses on correct, complete and timely reporting of the risk and capital situation. Based on this, a number of different types of periodic reporting have been established that are intended for the Group's Board. The most important reports during the year are as follows**:**

ICAAP (Internal Capital Adequacy Assessment Process) is carried out and reported at least once a year. Møre Boligkreditt AS is included in the assessments of overall ICAAP for the Sparebanken Møre Group, and the Managing Director of Møre Boligkreditt AS is involved in the process. The process is led by the department for Risk Management in Sparebanken Møre. Specific guidelines have been prepared for ICAAP in Sparebanken Møre. ICAAP is reviewed by the bank's management team and the Board of Directors.

Møre Boligkreditt AS' internal liquidity adequacy assessment process (ILAAP) is included in the company's Internal Capital Adequacy Assessment Process (ICAAP).

A performance management report is prepared every month. The report presents the status and performance of the most important aspects of goal achievement at Møre Boligkreditt AS. The report is an integral part of the reporting to the Board of Directors.

A risk report is prepared every quarter. This is a key element of Møre Boligkreditt AS' continuous monitoring of its risk position. The risk report is reviewed by the Board of Directors in quarterly board meetings.

Each quarter, a liquidity forecast with a 5-year horizon is prepared, contributing to a continuous control of the liquidity situation and the refinancing needs of the mortgage company.

Internal control reports are produced every year. In the report an assessment is made of whether or not the internal control is adequate in relation to the risk tolerance. This includes an assessment and comments on internal control work performed, a review of all important risk areas, an assessment of compliance with external and internal regulations, and suggestions for and planned improvement measures. The internal control report is discussed by the Board of Directors. Møre Boligkreditt AS` internal control report is consolidated in the Group`s total internal control reporting.

Reports from external and internal auditors are reviewed by the Board of Directors, as well as the Audit Committee of Sparebanken Møre.

A reporting portal has been established in the Sparebanken Møre Group, and customer relationship employees have access to reports which show the position and development in the credit risk in his or her portfolio. The portal has a hierarchical structure, allowing managers in Sparebanken Møre and Møre Boligkreditt AS to monitor performance within their area of responsibility. The reports are also used to analyse customers, portfolios and different industrial, commercial and other sectors.

Finance and accounting reports are prepared monthly (and include calculations of collective impairment, as well as quarterly loss reviews of portfolios with a focus on the need for individual impairment). The reports are reviewed by the Board of Directors.

**Capital management**
Møre Boligkreditt AS acquires mortgages from Sparebanken Møre of which minimum 80 per cent are funded through the issue of covered bonds. The funding of the mortgage company in excess of issues of covered bonds is done by equity and established credit facility in the Parent Bank.

**Capital adequacy rules and regulations**
The EU's capital adequacy directive`s purpose is to strengthen the stability in the financial system through more risk-sensitive capital requirements, better risk management and control, more stringent supervision and more information provided for the market. The capital adequacy directive is based on three pillars:

• Pilar I – Minimum requirement for equity and related capital

• Pilar II – Assessment of aggregate capital requirements and regulatory follow-up (ICAAP)

• Pilar III – Publication of information

Møre Boligkreditt AS applies the IRB Approach when calculating capital adequacy for credit risk, the Standard Approach for market risk, and the base method for operational risk. Møre Boligkreditt AS' Board of Directors ensures that plans for the capitalization of the Company are in place, both during economic downturns and periods of strong economic expansion. Capital assessments (ICAAP) are done every year, and the company's capital strategy is based on the risk in the company's operations, having taken into consideration different stress scenarios.

**Risk exposure and strategic risk management**
Møre Boligkreditt AS is exposed to several different types of risk. The most important risk groups are:

• Credit risk: This is the company's most significant risk area. Credit risk is defined as the risk of loss due to customers or other counterparts being unable to meet their obligations at the agreed time in accordance with the written agreements, or that collateral held is not covering the outstanding claims. Included in the credit risk is also concentration risk, defined as the risk of loss resulting from the concentration of large individual clients, specific industries, geographical areas, collateral with the same risk characteristics, counterparties in interbank operations or trading in financial derivatives.

Møre Boligkreditt AS' main credit risk is related to loans to customers with collateral in residential property and housing associations. Møre Boligkreditt AS acquires the loans from Sparebanken Møre, originally granted to customers by Sparebanken Møre, based on group policies and limits. At the time of the transfer of loan portfolios, only loans that qualifies as collateral for the issue of covered bonds, are accepted by Møre Boligkreditt AS. For all these mortgage loans, the value of the loan balance should not exceed 75 per cent of the total value of the property. The collateral value is monitored on an ongoing basis.

Møre Boligkreditt AS has adopted the credit risk policies as set by the Sparebanken Møre Group. The group manages and controls credit risk by setting limits on the amount of risk, and by monitoring exposures in relation to such limits. Collateral is taken to manage credit risk in the loan portfolios. According to the agreement relating to the transfer of loans between Sparebanken Møre and Møre Boligkreditt AS, the day-to-day monitoring of the loans are managed by Sparebanken Møre on behalf of Møre Boligkreditt AS. Sparebanken Møre`s risk classification system is based on the probability of default (PD), which estimates the likelihood of a customer defaulting on its contractual obligations.

See also the Group` s Pillar III document published on www.sbm.no.

• Market risk: The risk of loss due to changes in fair value of financial instruments as a result of fluctuations in market prices such as share prices, foreign exchange rates and interest rates.

Møre Boligkreditt AS minimizes currency risk through swap agreements with eligible counterparties.

The Board of Directors sets risk limits, positions are monitored on a daily basis, and quarterly exposure reports are prepared for the management and for The Board of Directors.

Fixed interest on the company's funding is managed through interest rate swaps with eligible counterparties.

• Liquidity risk: The risk that the company will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

The Board of Directors sets annual limits for the company's liquidity risk, which means preparing liquidity risk limits, contingency plans, forecasts, stress tests, routines for monitoring limit utilisation and compliance with guidelines, management reporting and monitoring of management and control systems.

In a stress scenario where the mortgage company faces difficulties in refinancing its covered bonds through normal funding sources, Møre Boligkreditt AS can rely on a revolving credit facility in Sparebanken Møre covering the mortgage company’s payment obligations for the next 12 months, and a 12 month soft-call (12 month extendable maturity) on covered bonds issued.

Møre Boligkreditt AS` liquidity situation at year-end is considered to be sound.

• Operational risk: The risk of losses due to inadequate or failing internal processes, human error, system failures, or external events. Møre Boligkreditt AS has a management agreement with Sparebanken Møre. The services covered by this include administration, production, IT operations, and financial and risk management. Although the operational risk of Møre Boligkreditt AS is dependent of Sparebanken Møre's ability to manage this type of risk, Møre Boligkreditt AS independently bear risk associated with errors in the deliveries and services provided by Sparebanken Møre.

The evaluation of the management and control of operational risk is also afforded substantial space in the group's annual ICAAP. The operational and established internal control system in the mortgage company is also an important tool for reducing operational risk with respect to both uncovering it and following it up.

The internal control system should be designed to ensure reasonable certainty with respect to attaining goals within the areas of strategic development, efficient operations, reliable reporting, and compliance with acts and regulations, including compliance with intragroup and company-specific guidelines and policies. A well-functioning internal control system should also ensure the mortgage company's risk exposure being within the adopted risk profile. Reports are submitted to the company's Board concerning operations and the risk situation throughout the year. The Managing Director submits an annual report to the Board containing an overall assessment of the risk situation and an assessment of whether the internal controls are functioning satisfactorily.

Møre Boligkreditt AS tries to take account of the interaction between the various risk areas by setting desired levels of exposure. Overall, it is the internal conditions, general conditions, customer base etc. in the Group that form the basis for setting the desired overall risk exposure.

Based on an evaluation of the risk profile, management and control, Møre Boligkreditt AS has set the following overall levels of risk exposure for the various risk areas:

• Credit risk: A low level of risk is accepted

• Market risk: A low level of risk is accepted

• Liquidity risk: A low level of risk is accepted

• Operational risk: The acceptable risk level is low to moderate

# Note 5

## CREDIT RISK

Credit risk represents the most significant area of risk and is defined as the risk of losses associated with customers being unable to fulfil their obligations at the agreed time and pursuant to written agreements, and the received collateral not covering outstanding claims. The company's credit risk strategy is revised and approved annually by the Board and sets forth the company's risk profile in the area of credit. Monthly portfolio management reports have been established to ensure that any deviations from the strategic goals set forth in the credit risk strategy are uncovered. The risk classification systems are used as decision support, monitoring and reporting. The risk parameters used in the classification systems are an integrated part of the credit process and ongoing risk monitoring, including the follow-up of credit strategies. Probability of default, PD, is used to measure quality.

The risk classification system is divided into ten risk classes where 1 represents the lowest and 10 the highest risk. The classification system is based on the probability of default which is an estimate of the likelihood of a counterparty defaulting on its contractual obligations within the next 12 months. In the table below, all loans to customers and undrawn commitments are presented according to risk level. The amounts are based on the nominal amounts before adjustments for impairment and accrued interest.

Loans for which payments are overdue with more than 90 days are considered non-performing and transferred to “Commitments in default”.

| Risk groups based on probability of default - 2017 | Loans | Credit facilities | Total |
|---|---|---|---|
| Low risk (0 % - < 0.5 %) | 20 082 | 1 210 | 21 292 |
| Medium risk (0.5 % - < 3 %) | 942 | 1 | 943 |
| High risk (3 % - <100 %) | 115 | 0 | 115 |
| Commitments in default | 0 | 0 | 0 |
| Total loans before individual and collective impairment | 21 139 | 1 211 | 22 350 |
| Accrued interest income | 25 | 0 | 25 |
| - Impairment (individual and collective impairment) | -2 | 0 | -2 |
| Loans to and receivables from customers 31.12.2017 | 21 162 | 1 211 | 22 373 |

| Risk groups based on probability of default - 2016 | Loans | Credit facilities | Total |
|---|---|---|---|
| Low risk (0 % - < 0.5 %) | 18 714 | 1 135 | 19 849 |
| Medium risk (0.5 % - < 3 %) | 931 | 10 | 941 |
| High risk (3 % - <100 %) | 147 | 0 | 147 |
| Commitments in default | 0 | 0 | 0 |
| Total loans before individual and collective impairment | 19 792 | 1 145 | 20 937 |
| Accrued interest income | 23 | 0 | 23 |
| - Impairment (individual and collective impairment) | -5 | 0 | -5 |
| Loans to and receivables from customers 31.12.2016 | 19 810 | 1 145 | 20 955 |

### Collateral

The company requires residential property as collateral to reduce the risk associated with customers' willingness and ability to serve their obligation. By the granting of loans there is an objective valuation of residential properties. Factors are also taken into account that may affect the security's value, such as licensing conditions or easements.

Møre Boligkreditt is the legal and beneficial owner of each loan in the portfolio and is secured rights to the collateral that is associated with each loan. Proper transfers of loans are handled through a separate agreement between the company and the Parent Bank. In cases where the collateral secures loans for both the company and the Parent Bank, it is agreed that Møre Boligkreditt AS is ranked first under the current security.

All loans in the cover pool had mortgages within 75 per cent of property value at the time of acquisition. The mortgage company had mortgages with loan balance exceeding 75 per cent of property value of a total of NOK 348 million as at 31 December 2017, see note 10.

# Note 6

## LIQUIDITY RISK

Liquidity risk is the risk that Møre Boligkreditt AS will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or other financial assets.

The Board of Møre Boligkreditt AS annually sets limits for management of liquidity risk in the company.

Pursuant to the Financial Institutions Act, a mortgage company which issues covered bonds must ensure that the cash flow from the cover pool enables the company to meet its payment obligations to holders of covered bonds and counterparties to derivative agreements at all times.

The loans acquired by Møre Boligkreditt AS are primarily financed through the issuing of covered bonds. The company's plan is to ensure that this type of funding shall over time account for a minimum of 80 per cent of the entity's financing of acquired loans.

Loans that are acquired and not included in a portfolio financed by covered bonds, and loans that serve as over-collateralisation, are financed through a facility the company holds in the parent bank, Sparebanken Møre, or equity. The long-term overdraft facility in Sparebanken Møre has a total limit of NOK 2.25 billion. Undrawn facility amounts to NOK 1.11 billion as of 31.12.

Receivables from credit institutions and investments in covered bonds, not used for LCR purposes, are used as part of the cover pool.

As of 31.12.2017 the requirement for liquidity coverage ratio for Norwegian covered bond companies is 100 % on total currency level, 100% in significant currencies and 50% in NOK if significant currencies equals EUR or USD. As of 31.12.2017 Møre Boligkreditt AS reports 295 % on total currency level and NOK. There are no LCR-outflows in EUR as of 31.12.2017.

| Remaining maturity as per 31.12.17 | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Above 5 years | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Loans to and receivables from credit institutions | 85 | 0 | 0 | 0 | 0 | 85 |
| Loans to and receivables from customers | 104 | 209 | 1 019 | 4 792 | 21 780 | 27 904 |
| Certificates and bonds | 0 | 0 | 30 | 31 | 0 | 61 |
| Total assets | 189 | 209 | 1 049 | 4 823 | 21 780 | 28 050 |
| **Liabilities** | | | | | | |
| Loans from credit institutions | 1 202 | 0 | 0 | 0 | 0 | 1 202 |
| Debt securities issued | 8 | 50 | 2 681 | 15 240 | 1 482 | 19 461 |
| Total liabilities | 1 210 | 50 | 2 681 | 15 240 | 1 482 | 20 663 |
| **Financial derivatives** | | | | | | |
| Cash flow in | 0 | 15 | 59 | 298 | 190 | 562 |
| Cash flow out | 1 | 15 | 49 | 231 | 61 | 357 |
| Total financial derivatives | -1 | 0 | 10 | 67 | 129 | 205 |

Cash flows from nominal interest payments are included for "Loans to and receivables from customers", for "Certificates and bonds" and for "Debt securities issued".

| Remaining maturity as per 31.12.16 | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Above 5 years | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Loans to and receivables from credit institutions | 271 | 0 | 0 | 0 | 0 | 271 |
| Loans to and receivables from customers | 97 | 193 | 731 | 4 482 | 20 505 | 26 008 |
| Certificates and bonds | 31 | 151 | 45 | 310 | 0 | 537 |
| Total assets | 399 | 344 | 776 | 4 792 | 20 505 | 26 816 |
| **Liabilities** | | | | | | |
| Loans and from credit institutions | 1 141 | 0 | 0 | 0 | 0 | 1 141 |
| Debt securities issued | 10 | 65 | 3 137 | 13 505 | 2 535 | 19 252 |
| Total liabilities | 1 151 | 65 | 3 137 | 13 505 | 2 535 | 20 393 |
| **Financial derivatives** | | | | | | |
| Cash flow in | 0 | 15 | 57 | 285 | 259 | 616 |
| Cash flow out | 1 | 12 | 36 | 161 | 101 | 311 |
| Total financial derivatives | -1 | 3 | 21 | 124 | 158 | 305 |

Cash flows from nominal interest payments are included for "Loans to and receivables from customers", for "Certificates and bonds" and for "Debt securities issued".

# Note 7

## MARKET RISK

Market risk arises as a consequence of open positions in foreign exchange and interest rate.

Møre Boligkreditt AS has funding in foreign currency. Currency risk associated with this funding is hedged and minimized by use of currency swaps. The financial derivatives are recognised at fair value, with value changes recognised in the profit and loss account, and are carried in the balance sheet on a gross basis per contract as assets or liabilities respectively. The estimated fair value of financial OTC derivatives is adjusted for counterparty credit risk (CVA) or for the company's own credit risk (DVA).

Through its regular operations, the company is exposed to interest rate risk. Interest risk occurs in the company's portfolio in connection with its activities relating to loans and bond debt in which different interest terms apply to the company's receivables and liabilities. Depending on the relationship between the interest terms for receivables and liabilities, changes to interest rates could result in increased income or expenses. Møre Boligkreditt AS uses interest rate swaps as part of its risk management to manage interest rate risk. The company's borrowings with fixed interest rates are swapped to floating interest rates. Potential effect of a 1 year period change in interest rate of 1 percentage point, is an increase/decrease in interest income of NOK 15 million. Relative to the company's total equity of NOK 1 667 million, the company's interest rate risk is considered to be insignificant.

The table shows the potential effect of the change in market value of financial assets and liabilities of the company due to a one percentage point increase in interest rates. The calculation is based on current positions and market rates as of 31 December.

| Amounts in NOK million | Up to 3 months | 3 - 12 months | 1 - 5 years | Above 5 years | Total |
|---|---|---|---|---|---|
| 2017 | 1 | 1 | -2 | 0 | 0 |
| 2016 | 1 | 1 | -3 | -1 | -2 |

The table below shows nominal values on financial derivatives according to type of derivative as well as positive and negative market values. Positive market values are recognised as assets in the balance sheet, whereas negative market values are recognised as liabilities.

| | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|
| **Financial derivatives** | **Nominal value** | **Asset** | **Liability** | **Nominal value** | **Asset** | **Liability** |
| Interest rate swaps | 2 050 | 204 | 4 | 2 050 | 217 | 4 |
| Cross currency interest rate swaps | 2 900 | 235 | | 1 119 | 151 | |
| Total financial derivatives | 4 950 | 439 | 4 | 3 169 | 368 | 4 |
| - hereof applied in hedge accounting | 4 681 | 391 | | 2 264 | 296 | 2 |

The table below provides detail on the contractual maturity of financial derivatives based on nominal values.

| | 2017 | | 2016 | |
|---|---|---|---|---|
| **Maturity** | **Interest rate swaps** | **Cross currency swaps** | **Interest rate swaps** | **Cross currency swaps** |
| 2017 | | | | 647 |
| 2018 | | | | |
| 2019 | | | | |
| 2020 | | 269 | | 258 |
| 2021 | | | | |
| 2022 | 1 000 | 2 408 | 1 000 | |
| 2023 | | | | |
| 2024 | | | | |
| 2025 | 1 050 | | 1 050 | |
| 2026 | | | | |
| 2027 | | | | |
| 2028 | | 223 | | 214 |
| | 2 050 | 2 900 | 2 050 | 1 119 |

# Note 8

## FINANCIAL INSTRUMENTS

All lending and receivables are recorded at amortised cost. Amortised cost is also used for fixed and floating rate securities issued.

The company's debt securities issued with fixed interest rates are accounted for using fair value hedging. Losses and gains, resulting from changes in value due to changes in market interest, of debt securities with fixed interest are recognised in the income statement in the period they arise.

For floating rate loans to customers, the interest rates and margins are changed when the market rates change. The customers have to be notified of all changes in advance of the changes being put into effect, so there is a short period of time where the terms of the loans diverge from market rates. However this delay in timing is considered to have an immaterial effect to the total value of the loans hence the carrying value of these loans are considered to be a relevant measure for fair value.

There are no major differences between the book value and the fair value of loans to credit institutions and customers, and liabilities to credit institutions agreed at variable rates and recognised at amortised cost. Fair value of debt securities is calculated allowing for change in the market interest rates and change in the credit margin.

Financial derivatives related to the company`s debt securities issued are carried at fair value through profit or loss, and recognised gross per contract, as either asset or debt.

| CLASSIFICATION OF FINANCIAL INSTRUMENTS | Financial instruments at fair value through profit or loss | | Financial assets and liabilities carried at amortised cost | |
|---|---|---|---|---|
| | 31.12.2017 | 31.12.2016 | 31.12.2017 | 31.12.2016 |
| Loans to and receivables from credit institutions | - | - | 85 | 271 |
| Loans to and receivables from customers | - | - | 21 162 | 19 810 |
| Certificates and bonds | 60 | 522 | - | - |
| Financial derivatives | 439 | 368 | - | - |
| Total assets | 499 | 890 | 21 247 | 20 081 |
| Loans from credit institutions | - | - | 1 202 | 1 141 |
| Debt securities issued | - | - | 18 823 | 18 265 |
| Financial derivatives | 4 | 4 | - | - |
| Total liabilities | 4 | 4 | 20 025 | 19 406 |

| FAIR VALUE OF FINANCIAL INSTRUMENTS AT AMORTISED COST | 31.12.2017 | | 31.12.2016 | |
|---|---|---|---|---|
| | Fair value | Book value | Fair value | Book value |
| Loans to and receivables from credit institutions | 85 | 85 | 271 | 271 |
| Loans to and receivables from customers | 21 162 | 21 162 | 19 810 | 19 810 |
| Total assets | 21 247 | 21 247 | 20 081 | 20 081 |
| Loans from credit institutions | 1 202 | 1 202 | 1 141 | 1 141 |
| Debt securities issued | 18 894 | 18 823 | 18 257 | 18 265 |
| Total liabilities | 20 096 | 20 025 | 19 398 | 19 406 |

| FINANCIAL INSTRUMENTS AT AMORTISED COST - 31.12.2017 | Based on prices in an active market<br>Level 1 | Observable market information<br>Level 2 | Other than observable market information<br>Level 3 | Total |
|---|---|---|---|---|
| Loans to and receivables from credit institutions | - | 85 | - | 85 |
| Loans to and receivables from customers | - | - | 21 162 | 21 162 |
| Total assets | - | 85 | 21 162 | 21 247 |
| Loans from credit institutions | - | 1 202 | - | 1 202 |
| Debt securities issued | - | 18 894 | - | 18 894 |
| Total liabilities | - | 20 096 | - | 20 096 |

| FINANCIAL INSTRUMENTS AT AMORTISED COST - 31.12.2016 | Based on prices in an active market<br>Level 1 | Observable market information<br>Level 2 | Other than observable market information<br>Level 3 | Total |
|---|---|---|---|---|
| Loans to and receivables from credit institutions | - | 271 | - | 271 |
| Loans to and receivables from customers | - | - | 19 810 | 19 810 |
| Total assets | - | 271 | 19 810 | 20 081 |
| Loans from credit institutions | - | 1 141 | - | 1 141 |
| Debt securities issued | - | 18 257 | - | 18 257 |
| Total liabilities | - | 19 398 | - | 19 398 |

| FINANCIAL INSTRUMENTS AT FAIR VALUE - 31.12.2017 | Based on prices in an active market<br>Level 1 | Observable market information<br>Level 2 | Other than observable market information<br>Level 3 | Total |
|---|---|---|---|---|
| Certificates and bonds | - | 60 | - | 60 |
| Financial derivatives | - | 439 | - | 439 |
| Total assets | - | 499 | - | 499 |
| Financial derivatives | - | 4 | - | 4 |
| Total liabilities | - | 4 | - | 4 |

| FINANCIAL INSTRUMENTS AT FAIR VALUE - 31.12.2016 | Based on prices in an active market<br>Level 1 | Observable market information<br>Level 2 | Other than observable market information<br>Level 3 | Total |
|---|---|---|---|---|
| Certificates and bonds | - | 522 | - | 522 |
| Financial derivatives | - | 368 | - | 368 |
| Total assets | - | 890 | - | 890 |
| Financial derivatives | - | 4 | - | 4 |
| Total liabilities | - | 4 | - | 4 |

| MATURITY OF DEBT SECURITIES ISSUED, NOMINAL VALUE | 2017 | 2016 |
|---|---|---|
| 2017 | - | 2 878 |
| 2018 | 2 500 | 2 500 |
| 2019 | 2 500 | 2 500 |
| 2020 | 5 744 | 5 244 |
| 2021 | 3 000 | 2 500 |
| 2022 | 3 363 | 1 000 |
| 2025 | 1 050 | 1 050 |
| 2028 | 201 | 201 |
| Total | 18 358 | 17 873 |

# Note 9

## HEDGING OF INTEREST RATE AND CURRENCY EXPOSURE

| HEDGE ACCOUNTING FOR FINANCIAL LIABILITIES WITH FIXED INTEREST RATE | 31.12.2017 | 31.12.2016 |
|---|---|---|
| Changes in fair value of derivatives established to hedge changes in market interest rates | -9 | -21 |
| Changes in fair value due to changes in market interest rates on hedged financial liabilities with fixed interest rate | 8 | 21 |

| HEDGE ACCOUNTING FOR FINANCIAL LIABILITIES IN FOREIGN CURRENCY | 31.12.2017 | 31.12.2016 |
|---|---|---|
| Changes in fair value of derivatives established to hedge currency exsposure and market interest rates on financial liabilities | 26 | -7 |
| Changes in fair value due to changes in the exchange rate and market interest rates in hedged financial liabilities | -27 | 7 |

# Note 10

## ISSUED COVERED BONDS

Securities issued at floating interest rates are measured at amortised cost. Securities issued at fixed interest rates are measured at amortised cost as well, and fair value hedge accounting with changes in fair value (due to the hedged risk) recognised in profit and loss is used for the company's securities issued at fixed rate terms.

**COVERED BONDS (MNOK)**

| ISIN code | Currency | Nominal value 31.12.2017 | Interest | Issue | Maturity | **31.12.2017** | **31.12.2016** |
|---|---|---|---|---|---|---|---|
| NO0010575079 | NOK | - | 3M Nibor + 0.55 % | 2010 | 2017 | - | 1 498 |
| NO0010588072 | NOK | 1 050 | fixed NOK 4.75 % | 2010 | 2025 | 1 235 | 1 251 |
| NO0010657232 | NOK | 2 500 | 3M Nibor + 0.65 % | 2012 | 2018 | 2 503 | 2 508 |
| XS0828616457 | SEK | - | 3M Stibor + 0.70 % | 2012 | 2017 | - | 666 |
| NO0010676018 | NOK | 2 500 | 3M Nibor + 0.47 % | 2013 | 2019 | 2 502 | 2 503 |
| XS0968459361 | EUR | 25 | fixed EUR 2.81 % | 2013 | 2028 | 295 | 282 |
| XS0984191873 | EUR | 30 | 6M Euribor + 0.20 % | 2013 | 2020 | 295 | 272 |
| NO0010696990 | NOK | 2 500 | 3M Nibor + 0.45 % | 2013 | 2020 | 2 497 | 2 496 |
| NO0010699028 | NOK | - | 3M Nibor + 0.37 % | 2013 | 2017 | - | 750 |
| NO0010720204 | NOK | 3 000 | 3M Nibor + 0.24 % | 2014 | 2020 | 2 998 | 2 498 |
| NO0010730187 | NOK | 1 000 | fixed NOK 1.50 % | 2015 | 2022 | 993 | 987 |
| NO0010777584 | NOK | 3 000 | 3M Nibor + 0.58 % | 2016 | 2021 | 3 003 | 2 498 |
| XS1626109968 | EUR | 250 | fixed EUR 0.125 % | 2017 | 2022 | 2 450 | - |
| Total securities issued | | | | | | 18 771 | 18 209 |
| Accrued interest | | | | | | 52 | 56 |
| Total borrowings raised through the issue of securities | | | | | | 18 823 | 18 265 |

| COVER POOL (MNOK) | **31.12.2017** | **31.12.2016** |
|---|---|---|
| Pool of eligible loans 1) | 20 814 | 19 430 |
| Supplementary assets | 85 | 743 |
| Financial derivatives to hedge issued securities (liabilities) | -4 | -4 |
| Financial derivatives to hedge issued securities (assets) | 439 | 368 |
| Total collateralised assets | 21 334 | 20 537 |
| Collateralisation in % | 113,3 | 112,4 |

1) NOK 348 million of total gross loans are not eligible for the cover pool as at 31.12.17.

**Debt securities issued**

| | 31.12.2017 | 31.12.2016 |
|---|---|---|
| Covered bonds, nominal value | 18 358 | 17 873 |
| Accrued interest | 52 | 56 |
| Value adjustments | 413 | 336 |
| Total debt securities | 18 823 | 18 265 |

**Changes in debt securities**

| | Balance sheet 31.12.16 | Issued | Overdue/redeemed | Other changes | Balance sheet 31.12.17 |
|---|---|---|---|---|---|
| Covered bonds, nominal value | 17 873 | 3 363 | 2 880 | 2 | 18 358 |
| Accrued interest | 56 | | | -4 | 52 |
| Value adjustments | 336 | | | 77 | 413 |
| Total debt securities | 18 265 | 3 363 | 2 880 | 75 | 18 823 |

# Note 11

## TRANSACTIONS WITH RELATED PARTIES

In order to conduct normal business, Møre Boligkreditt AS purchases services from Sparebanken Møre. There will also be transactions between the parties related to the acquisition of loan portfolio, and the fact that Sparebanken Møre provides loans and credits to the mortgage company.

Loans from Sparebanken Møre are transferred at market value. If the purchased mortgage loans have fixed interest rates the price is adjusted for the value above / below par. Sparebanken Møre is responsible for ensuring that the loans to be transferred to Møre Boligkreditt AS are properly established and in accordance with the requirements specified in the agreement between the mortgage company and the Parent Bank. In case of a violation of these requirements, the Parent Bank will be liable for any losses that the mortgage company would experience as a result of the error. Sparebanken Møre and Møre Boligkreditt AS have formalised the settlement of interest for transaction days from date of transfer of loan portfolio to date of settlement of the consideration.

Should Møre Boligkreditt AS for any reason experience difficulties in obtaining financing, a revolving guarantee provided by Sparebanken Møre has been established in order to ensure timely payments to owners of bonds and derivative counterparties.

The pricing of the services provided to Møre Boligkreditt AS by Sparebanken Møre distinguishes between fixed and variable costs for the mortgage company. Fixed costs are defined as costs the mortgage company must bear regardless of the activity related to the issuance of covered bonds, the acquisition of portfolio, etc. Variable costs are defined as costs related to the size of the portfolio acquired from Sparebanken Møre and the work that must be exercised by the Bank's employees to deliver satisfactory services given the number of customers in the portfolio.

Møre Boligkreditt AS is billed for costs related to the lease of premises at Sparebanken Møre. It is assumed that regardless of operations, a certain area of the bank attributable to the mortgage company is utilised during the year. Regardless of the extent of the activity and the loan portfolio acquired by Møre Boligkreditt AS, charges related to accounting, financial reporting, risk management, cash management, financing, governance and general legal services will incur.

Sparebanken Møre bills the mortgage company based on actual salary costs, including social security contribution, pension costs and other social costs. Parts of the mortgage company's expenses related to services provided by Sparebanken Møre relates to the size of the portfolio acquired from Sparebanken Møre. Management fee is calculated and billed monthly, in which the month's average portfolio size form the basis of billing.

The interest rate of the mortgage company's deposit and credit limit in Sparebanken Møre is based on 3 months NIBOR + a premium.

The most important transactions are as follows:

| (MNOK) | 31.12.2017 | 31.12.2016 |
|---|---|---|
| Statement of income | | |
| Interest and credit commission income from Sparebanken Møre related to deposits | 2 | 2 |
| Interest and credit commission income paid to Sparebanken Møre related to loan/credit facility | 17 | 18 |
| Interest paid to Sparebanken Møre related to bonded debt | 11 | 8 |
| Management fee paid to Sparebanken Møre | 30 | 26 |
| | | |
| Statement of financial position | | |
| Deposits in Sparebanken Møre | 85 | 271 |
| Covered bonds held by Sparebanken Møre as assets | 425 | 2 186 |
| Loan/credit facility in Sparebanken Møre | 1 202 | 1 141 |
| Accumulated transferred loan portfolio from Sparebanken Møre | 21 164 | 19 815 |

# Note 12

## WAGES, COMPENSATIONS AND FEES

| Amounts in NOK thousand | | 2017 | 2016 |
|---|---|---|---|
| Total wages and other cash payments | | 2 306 | 2 246 |
| - hereof salary to the Managing Director | | 955 | 923 |
| - hereof other remuneration to the Managing Director | | 41 | 54 |
| - hereof refunded premium regarding the pension plan for the Managing Director | | 60 | 63 |
| - hereof remuneration to the Board of Directors | | 100 | 100 |
| The Board of Directors | Kjetil Hauge, Chairman | 0 | 0 |
| | Sandra Myhre Helseth | 0 | 0 |
| | Elisabeth Blomvik | 0 | |
| | Geir Tore Hjelle | 50 | 50 |
| | Britt Iren Tøsse Aandal | 50 | 50 |
| | Former board member: | | |
| | Trond Lars Nydal | | 0 |
| Total fees paid to external auditor (all fees are stated including VAT of 25 %) | | 1 002 | 775 |
| - hereof statutory audit services | | 269 | 269 |
| - hereof tax-related services | | 38 | 35 |
| - hereof other attestation services | | 650 | 410 |
| - hereof other non-audit services | | 45 | 61 |

Møre Boligkreditt AS has no employees at the end of 2017 . Møre Boligkreditt AS remunerated Sparebanken Møre for the use of two man-years, but only the Managing Director of Møre Boligkreditt AS is dedicated full time to the company. A number of services are also outsourced for performance by Sparebanken Møre, and these are regulated by a specific agreement between the mortgage company and the bank. The above-mentioned pay and other cash benefits, as well as employer's national insurance contributions, are cost refunds to Sparebanken Møre. The employees are members of Sparebanken Møre's pension scheme. The scheme satisfies the current requirements for mandatory occupational pensions. The company had as per 31 December 2017 no obligation to pay the Managing Director, chairman of the Board of Directors or other employees special remuneration upon them leaving the company or in the event of a change in their employment relationship or duties. Nor do any obligations concerning bonuses, options, or similar exist for any of the aforementioned people.

**Loans and guarantees**

| Amounts in NOK thousand | 2017 | | 2016 | |
|---|---|---|---|---|
| | **Loans** | **Guarantees** | **Loans** | **Guarantees** |
| **Board of Directors** | | | | |
| Kjetil Hauge, Chairman | 3 214 | 0 | 3 330 | 0 |
| Sandra Myhre Helseth | 2 414 | 0 | 2 835 | 0 |
| Elisabeth Blomvik | 0 | 0 | | |
| Geir Tore Hjelle | 0 | 0 | 0 | 0 |
| Britt Iren Tøsse Aandal | 0 | 0 | 0 | 0 |
| | | | | |
| Former board member: | | | | |
| Trond Lars Nydal | | | 925 | 0 |
| **Managing Director** | | | | |
| Ole Kjerstad | 3 579 | 0 | 3 761 | 0 |

Ordinary customer terms and conditions have been applied to loans provided for members of the Board of Directors.

Loans to the Managing Director and the Board members of Møre Boligkreditt AS, who also are employees in Sparebanken Møre, are given according to staff conditions.

# Note 13

## TAX

Temporary negative and positive differences which are reversed or which may be reversed during the same period, have been offset and included in the accounts on a net basis. Deferred tax is calculated on the basis of the differences which exist between the accounting-related and tax-related values at the end of the accounting year. The entire tax-cost is related to Norway.

Specification of total tax cost

| | 2017 | 2016 |
|---|---|---|
| Result before tax | 213 | 208 |
| Permanent differences | 0 | 0 |
| Changes in temporary differences | 5 | 8 |
| Income subject to tax | 218 | 216 |
| Tax payable at 24 per cent (25 per cent in 2016) | 52 | 54 |
| Change in deferred tax | -2 | -2 |
| Correction previous year | -2 | 0 |
| Total tax cost | 48 | 52 |

Specification of temporary differences and computation of deferred tax

| | 2017 | 2016 |
|---|---|---|
| Financial liabilities | -221 | -235 |
| Financial instruments | 213 | 233 |
| Net negative (-)/positive differences | -8 | -2 |
| Deferred tax asset (-) or liability as at 31 December | -2 | 0 |

Some financial instruments are measured in the financial statements at fair value, while financial instruments are taxed as they are realised.

A tax rate of 24 per cent is used as the prevailing tax rate in 2017. As of 2018 the corporate tax rate has been reduced to 23 per cent, which has limited effect on the company due to the temporary differences not being significant. Realisation of deferred tax benefit is based on future results liable to tax, based on empirical experience and prognoses, exceeding the tax benefit in question in the case of reversal of any existing temporary differences. No temporary differences exist in relation to items recognised against comprehensive income or directly against equity. All deferred tax relates to items recognised in the result for the accounting year.

Reconciliation of tax cost and pre-tax profit

| | 2017 | 2016 |
|---|---|---|
| 24 per cent of pre-tax profit (25 per cent in 2016) | 51 | 52 |
| Other permanent differences 24 per cent (25 per cent in 2016) | 0 | 0 |
| Correction previous year | -3 | 0 |
| Total tax cost | 48 | 52 |

# Note 14

## EQUITY AND RELATED CAPITAL

Møre Boligkreditt AS follows the EU's new capital adequacy regulations, CRR and CRD IV. The regulations are based on the Basel Committee's recommendations on new and stricter capital and liquidity standards, Basel III. The Sparebanken Møre Group has been granted permission to use the Internal Ratings Based ("IRB") approach for credit risk to calculate the total risk-weighted assets.

However, as long as Norwegian transitional rules relating to full implementation of the IRB approach remain in force, the total risk-weighted assets cannot be reduced below 80 per cent of the Basel I requirements.

The legislation requires a minimum common equity Tier-1 of 11.5 per cent, including a conservation-buffer of 2.5 per cent, a systemic-risk buffer of 3.0 per cent and a counter-cyclical buffer of 2.0 per cent. Minimum capital adequacy ratio is 15.5 per cent. The current defined long-term target for Møre Boligkreditt AS is to meet minimum capital requirements. Møre Boligkreditt AS has as of 31.12.2017 capital adequacy/core capital ratio of 16.5 per cent.

| **Core capital and supplementary capital** | 31.12.2017 | 31.12.2016 |
|---|---|---|
| Share capital and share premium | 1 500 | 1 350 |
| Retained earnings | 167 | 159 |
| Total equity | 1 667 | 1 509 |
| Dividends | -152 | -156 |
| Expected losses exceeding actual losses, IRB portfolios | -40 | -39 |
| Common Equity Tier 1 capital | 1 476 | 1 313 |
| | | |
| Supplementary capital | 0 | 0 |
| Net equity and subordinated loan capital | 1 476 | 1 313 |

| **Risk-weighted assets (calculation basis for capital adequacy ratio)** | | |
|---|---|---|
| Credit risk loans and receivables (Standardised Approach) | 217 | 250 |
| Credit risk loans and receivables (Internal ratings based Approach) | 3 898 | 4 083 |
| Operational Risk (Basic indicator Approach) | 505 | 501 |
| Total risk exposure amount for credit valuation adjustment (CVA) (SA) | 320 | 300 |
| Risk-weighted assets less transitional rules | 4 941 | 5 134 |
| Additional RWA from transitional rules 1) | 3 995 | 3 587 |
| Total risk-weighted assets | 8 936 | 8 722 |
| Minimum requirement common equity Tier 1 capital (4,5%) | 402 | 392 |

1) Transitional rules require that RWA can not be less than 80 per cent of the corresponding Basel I requirement

| **Buffer Requirement** | | |
|---|---|---|
| Countercyclical buffer (2.0%) (1.5% 2016) | 179 | 131 |
| Capital conservation buffer (2.5%) | 223 | 218 |
| Systemic risk buffer (3.0%) | 268 | 262 |
| Total buffer requirements | 670 | 611 |
| Available common equity Tier 1 capital after buffer requirements | 403 | 310 |

| Capital adequacy as a percentage of the weighted asset calculation basis | | |
|---|---|---|
| Capital adequacy ratio | 16,5 % | 15,1 % |
| Core capital ratio | 16,5 % | 15,1 % |
| Core tier 1 capital ratio | 16,5 % | 15,1 % |

| Leverage ratio | | |
|---|---|---|
| Leverage ratio | 6,6 % | 6,1 % |

| Liquidity Coverage Ratio | | |
|---|---|---|
| Liquidity Coverage Ratio | 295% | 119% |

Møre Boligkreditt AS' capital requirements at 31st December 2017 are based on IRB-Foundation.

# Note 15

## SHARE CAPITAL

The share capital consists of 1 060 000 shares each with a nominal value of NOK 1 250. All shares are owned by Sparebanken Møre. Møre Boligkreditt AS is included in the consolidated financial statements of Sparebanken Møre and information about the consolidated financial statements can be obtained by contacting one of the bank's offices or via the bank's website: www.sbm.no.

| | 2017 | 2016 |
|---|---|---|
| Total number of shares 1 January | 940 000 | 780 000 |
| Issues of new shares | 120 000 | 160 000 |
| Total number of shares 31 December | 1 060 000 | 940 000 |
| Profit after tax as a percentage of average assets | 0,81 | 0,85 |

The Board of Directors has proposed a dividend of NOK 152 million per 31.12.17.

# Note 16

## EVENTS AFTER THE REPORTING DATE

No events of material significance for the financial statements for 2017 have occurred after the reporting date. The company is not involved in any legal proceedings.

# Statement

## Statement pursuant to section 5-5 of the Securities Trading Act

We hereby confirm that the company's annual financial statements for the period 1 January 2017 to 31 December 2017, have been, to the best of our knowledge, prepared in accordance with applicable accounting standards and that the information in the financial statements provides a true and fair view of the company's assets, liabilities, financial position, and results as a whole.

We also hereby declare that the annual report provides a true and fair view of the financial performance and position of the company, as well as a description of the principal risks and uncertainties facing the company.

Ålesund, 31 December 2017

5 February 2018

**THE BOARD OF DIRECTORS OF MØRE BOLIGKREDITT AS**

Kjetil Hauge
CHAIRMAN

Britt Iren Tøsse Aandal

Elisabeth Blomvik

Geir Tore Hjelle

Sandra Myhre Helseth

Ole Kjerstad
MANAGING DIRECTOR

# Independent Auditor's Report

To the Annual Shareholders' Meeting of Møre Boligkreditt AS

**Report on the audit of the financial statements**

**Opinion**
We have audited the accompanying financial statements of Møre Boligkreditt AS, which comprise the balance sheet as at 31 December 2017, the statement of income, comprehensive income, changes in equity and cash flows for the year then ended and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the financial statements have been prepared in accordance with laws and regulations and present fairly, in all material respects, the financial position of the Company as at 31 December 2017 and its financial performance for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

**Basis for opinion**
We conducted our audit in accordance with laws, regulations, and auditing standards and practices generally accepted in Norway, including International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's *responsibilities for the audit of the financial statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in Norway, and we have fulfilled our ethical responsibilities as required by law and regulations. We have also complied with our other ethical obligations in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**Key audit matters**
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements for 2017. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the financial statements.

**Issued covered bonds – compliance with regulation**
Møre Boligkreditt issues covered bonds as their prime source of funding and is therefore subject to detailed requirements of the Norwegian Financial Institutions Act and related regulation (the "Regulation") as a mortgage company and covered bonds issuer. The covered bonds represent total liabilities, measured at amortised cost, of NOK 18 823 million which are collateralised against a pool of assets, the cover pool. The cover pool consists of assets deemed eligible by management in accordance with the Regulation referred to above, in all material aspects mortgage loans within certain loan-to-value ratios and other explicit thresholds. In addition, the cover pool may hold derivatives for financial hedging purposes and other supplementary assets, also within the thresholds defined in the Regulation. At all times, Møre Boligkreditt is required to be compliant with the Regulation and align its operations with the requirements of the Regulation. Since such compliance is of significant importance for the operations of Møre Boligkreditt, we considered this a key audit matter.

We have tested controls over amortized cost measurement of issued cover bonds presented as debt securities issued in the balance sheet. We have assessed the design and the operating effectiveness of internal controls over the process of transferring and measuring eligible mortgage loans from the parent bank, Sparebanken Møre, to Møre Boligkreditt and subsequent measurement of the mortgage loans in Møre Boligkreditt. We have performed procedures on the cover pool as set out the Regulation with respect to loan to value ratios as well as the valuation of derivatives and bonds held as supplementary assets. We have also tested the calculation of collateralization in percent, as described in note 10 of the entity's annual report.

See note 10 in the financial statements for further information

**Other information**
Other information consists of the information included in the Company's annual report other than the financial statements and our auditor's report thereon. The Board of Directors and Managing Director (management) are responsible for the other information. Our opinion on the financial statements does not cover the other information, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information, and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

**Responsibilities of management for the financial statements**
Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting, unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

**Auditor's responsibilities for the audit of the financial statements**
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. As part of an audit in accordance with law, regulations and generally accepted auditing principles in Norway, including ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management;
- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

**Report on other legal and regulatory requirements**

**Opinion on the Board of Directors’ report**
Based on our audit of the financial statements as described above, it is our opinion that the information presented in the Board of Directors’ report concerning the financial statements, the going concern assumption and proposal for the allocation of the result is consistent with the financial statements and complies with the law and regulations.

**Opinion on registration and documentation**
Based on our audit of the financial statements as described above, and control procedures we have considered necessary in accordance with the International Standard on Assurance Engagements (ISAE) 3000, *Assurance Engagements Other than* Audits *or Reviews of Historical Financial Information*, it is our opinion that management has fulfilled its duty to ensure that the Company's accounting information is properly recorded and documented as required by law and bookkeeping standards and practices accepted in Norway.

Ålesund, 5 February 2018
Ernst & Young AS

Einar Hersvik
State Authorised Public Accountant (Norway)