SP MORTGAGE BANK PLC

BOARD OF DIRECTORS' REPORT AND
IFRS FINANCIAL STATEMENTS
31 DECEMBER 2018

Sp Mortgage Bank Plc's Board of Directors' Report and IFRS Financial Statements 31 December 2018

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Sp Mortgage Bank Plc's (henceforth also "Sp Mortgage Bank") objective is to strengthen the competitiveness of the Savings Banks Group through competitive funding and to promote the strategy of the Savings Banks Group through its own activity. Sp Mortgage Bank is responsible for the Savings Banks Group's covered bond issuance.

Sp Mortgage Bank does not have its own customer business operations or a service network; instead, the Savings Banks that belong to the Savings Banks Amalgamation intermediate and sell residential mortgage loans for the Sp Mortgage Bank. The Savings Banks also see to the local customer relationship management.

During the fiscal year, Sp Mortgage Bank's operations proceeded as planned and the loan portfolio reached at the end of the year the amount of EUR 1,854 million.

During the fiscal year, two targeted share issues to the owner banks were carried out and the share issues raised at total of EUR 12 million in new capital.

Sp Mortgage Bank's operating profit during the financial year amounted to EUR 2.7 million, and the balance sheet total amounted to EUR 1,906 million.

The Savings Banks Group and the Savings Banks Amalgamation

Sp Mortgage Bank belongs to the Savings Banks Group and the Savings Banks Amalgamation. The Bank's financial statements are consolidated with the Savings Banks Group's consolidated financial statements.

The Savings Banks Group (hereinafter also "the Group") is the most longstanding banking group in Finland. It comprises the Savings Banks forming the Savings Banks Amalgamation, the Savings Banks' Union Coop which acts as their Central Institution, as well as the subsidiaries and associated companies owned by the Savings Banks.

The member organisations of the Savings Banks Amalgamation (hereinafter also "the Amalgamation") form a financial entity as defined in the Act on the Amalgamation of Deposit Banks, in which the Savings Banks' Union Coop and its member credit institutions ultimately are jointly liable for each other's liabilities and commitments. The Amalgamation comprises the Savings Banks' Union Coop which acts as the Central Institution of the Amalgamation, 23 Savings Banks, Central Bank of the Savings Banks Finland Plc, Sp Mortgage Bank Plc and the companies within the consolidation groups of the above-mentioned entities, as well as Sp-Fund Management Company Ltd and Savings Bank Services Ltd.

The coverage of the Savings Banks Group differs from that of the Savings Banks Amalgamation in that the Savings Banks Group also includes institutions other than credit and financial institutions or service companies. The most notable of these are Sb Life Insurance Ltd and Sp-Koti Oy.

Further information about the structure of the Savings Banks Group can be found at *www.saastopankki.fi/saastopankkiryhma*.

Description of the operational environments

Global economic outlook

In the beginning of 2018, the outlook of the global economy was very positive. General economic confidence in Europe was the strongest it had been in more than 17 years and, in the United States, consumer confidence had risen to a level that substantially exceeded the highs seen before the financial crisis. By spring, however, it had become clear that global economic growth would not continue at the expected rate. With the exception of the United States, growth in the major industrialised countries began to slow down substantially around midyear. In the investment markets, the discrepancy between macroeconomic expectations and actual development was reflected in significant corrections in asset prices. The average GDP growth of industrialised countries was estimated to be only slightly over two per cent in 2018. Growth in the euro zone fell below two per cent. In the United States, however, the macroeconomic climate remained good, with tax cuts and other stimulus measures driving growth to a level approaching three per cent. GDP growth in the developing markets remained at approximately 4.5 per cent.

The slowing down of growth was partly due to fairly typical phenomena associated with economic boom periods. The expectation of rising interest rates, problems with the availability of skilled labour and other capacity limitations created friction in the economy. Political risks also played a role in the international operational environment, with the aggressive trade policy moves instigated by U.S. President Donald Trump being perhaps the worst of the them. Tariffs imposed on raw materials and intermediate goods had a broad impact on value chains in production. Uncertainty regarding the future development of trade wars also led to businesses postponing their investment decisions, which was reflected in slower growth in industrial orders in Germany and Finland, for example. The unpredictable Brexit talks, slower economic growth in China, the Turkish currency crisis and Italy's debt problems also fomented uncertainty.

The Federal Reserve accelerated the tightening of its monetary policy in 2018. The Fed raised its benchmark interest rate four times, ending the year in the 2.25–2.50 per cent range, and its tightening monetary policy began to have an impact on the global economy. The first to suffer the effects were the developing economies and their businesses, as they are dependent on foreign financing and the costs of their dollar-denominated loans rose substantially. However, towards the end of the year, the effects of tighter monetary policy began to be felt in the home market as well. The price of long-term fixed-rate home loans rose to approximately five per cent, which was already reflected in a slight slowing down of housing transactions and construction activity. While the European Central Bank did not yet introduce actual measures to tighten monetary policy, it discontinued quantitative easing at the end of the year.

Interest rate environment

On the whole, interest rates in the euro zone remained low in 2018. Movements in short-term interest rates were minor, with a slight increase seen towards the end of the year. Long-term interest rates declined to a lower level than at the start of the year after increasing temporarily early in the year and in the early autumn.

The prevailing relatively flat yield curve presents challenges to net interest income in banking operations due to the erosion of maturity transformation income. Regulatory requirements

(LCR, MREL) combined with the ECB's low deposit rate also weigh down on banks' net interest incomes.

Investment markets

Considerable movement was seen in the investment markets in 2018, with returns on investments declining significantly compared to the previous years. Economic growth remained favourable in the early part of the year, which helped support a higher risk appetite. In the second half of the year, investors' concerns regarding economic development and the simultaneous increase in political risks led to a downturn in the stock markets. The volatility of the stock markets increased significantly from the previous years and changes in share prices were particularly drastic during the autumn. Stock market returns were negative in all major markets.

Long-term interest rates increased substantially in the United States during the year, but their rise levelled off later in the year due to lowering inflation expectations. In Europe, there was no significant increase in long-term interest rates, which pushed the returns of government bonds to a higher level than expected. Changes in the political climate in Italy, following the new government taking office, became a concern among investors. As a result, the risk premiums of Italian government bonds rose significantly during the second half of the year. The risk premiums of corporate bonds rose correspondingly as uncertainty increased. The returns of corporate bonds were negative in almost all credit rating categories in both Europe and the United States.

The outlook of developing economies deteriorated in the face of growing trade policy risks and uncertainty. The currencies of developing economies depreciated significantly, which pushed the interest incomes of local currencies down to negative territory. The stock markets in developing countries also declined steadily in 2018 and showed negative returns for the year.

The prevailing mood at the start of the new year is one of uncertainty. Political risks play a major role and the uncertainty associated with them reduces risk appetite among investors. There are also risks related to economic growth, which are likely to push returns on investments lower than in the previous years.

The Finnish economy

In the Finnish economy, 2018 started in a very optimistic mood, but the outlook began to take a turn for the worse starting from the second quarter. Increased global uncertainty was reflected in exports. The development of industrial investments also fell substantially short of expectations. The growth of private consumption did not remain as strong as could have been expected based on the good employment situation and rapid rise in wages. In recent years, household debt has increased, the household saving rate has fallen into negative territory and the number of households in financial difficulties has grown. It would appear that households have become aware of the financial vulnerability and it is likely that there was an upturn in saving in 2018.

Thanks to strong development early in the year, employment again improved significantly in 2018. The unemployment rate continued to decline and the employment rate rose to a level that is very close to the government's target of 72 per cent. Nevertheless, net employment growth began to slow down in midyear. The underlying factors included both weaker demand factors in the economy and the deteriorating labour market mismatch problem. More and more businesses are reporting difficulties in finding suitable labour. However, on the whole, the rate at which the employment situation improved in 2018 was surprisingly high. The rate of increase in the total number of hours worked was even higher than GDP growth, which meant that the trend of increasing productivity levelled off.

Based on the available information, Finland's GDP growth in 2018 was approximately 2.3 per cent.

The housing market in Finland

The factors that influence housing transactions (employment rate, interest rates and consumer confidence) should have supported a positive climate in the housing market, but this was not the case. The transaction volume for old apartments fell by nearly three per cent compared to 2017. The factors behind the decrease include the large number of newly constructed apartments, lower investor interest in residential investments and a lower number of first-time home buyers. There was a growing divide between housing markets in different geographic regions. Uusimaa and other major cities saw continued growth, while many other regions, such as Kainuu, Kymenlaakso and Southern Savonia, moved in the opposite direction. This polarisation is significantly influenced by regional trends in population size and the size of the labour force. We predict that the transaction volume for old apartments will decrease by approximately 0–5 per cent in 2019.

The demand for residential investments declined substantially in 2018 due to strong growth in the supply of rental apartments and even excess supply in several cities. The increased supply curbed the rise in rents to a significant degree. Purchases by housing funds declined in particular. Many investors also decided to sell some of their residential investments, which was reflected in an increased supply of small apartments in several cities. The average number of days on market for small apartments increased significantly compared to 2016–2017.

New construction activity remained very strong in 2018 despite of decreasing demand. The number of issued building permits declined almost throughout the year, which suggests growing caution among construction firms. This cautious attitude is attributable to the decreasing demand for residential investments and the extensive public debate regarding the risks of large housing company loans. The low availability of plots in good locations is also a factor. Construction firms are increasingly focusing on renovation. We predict that the transaction volume for newly constructed apartments will decline by 10–20 per cent in 2019.

The prices of old apartments and terraced houses increased by approximately one per cent in 2018, which was a significantly lower rate of increase than in 2017. There were substantial geographic differences in the development of prices, with the Helsinki Metropolitan Area seeing an increase of approximately three per cent and the rest of Finland averaging about two per cent. We predict that the prices of old apartments will remain largely unchanged or even decline slightly throughout the country in 2019. The factors affecting prices include the increased uncertainty regarding the overall economic situation and the decrease in new construction.

Sp Mortgage Bank's profit and balance sheet

Sp Mortgage Bank's financial highlights

(EUR 1,000)	1.1.-31.12.2018	1.1.-31.12.2017	1.1.-31.12.2016 *
Revenue	21,838	18,544	4,083
Net interest income	17,157	9,622	-48
% of revenue	78.6 %	51.9 %	-1.2 %
Profit before taxes	2,686	5,097	-2,692
% of revenue	12.3 %	27.5 %	-65.9 %
Total operating revenue	4,723	6,904	-1,925
Total operating expenses	-2,056	-1,808	-768
Cost to income ratio	0.44	0.26	-0.40
Total assets	1,906,481	1,598,072	808,008
Total equity	88,184	74,695	42,768
Return on equity %	2.7 %	6.9 %	-8.2 %
Return on assets %	0.1 %	0.3 %	-0.5 %
Equity/assets ratio %	4.6 %	4.7 %	5.3 %
Solvency ratio %	13.4 %	13.5 %	16.4 %
Expected credit losses on loans and other receivables	20	0	0

*Actual mortgage banking operation was initiated on 29 March 2016.

Profit trends (comparison period 1-12/2017)

The result of the financial year consisted of net interest income, net fee and commission income and net trading income and operating expenses.

The Interest income increased to EUR 22.6 (14.4) million and consisted mostly of housing loan Interest payments. The increase in Interest income resulted from a growing loan portfolio. The Interest expenses was EUR -5.4 (-4.8) million consisted mostly of limit Interest and Interest expenses from liabilities to credit institutions. The net interest income amounted to EUR 17.2 (9.6) million.

The net fee and commission income mainly consisted of fees paid to the intermediating banks amounted to EUR -11.2 (-6.6) million. The negative growth arose from higher commissions paid to the intermediating banks.

Net profit from hedge accounting for the financial year was EUR -1.3 (3.8) million and it is presented under Net trading income on the income statement.

Operating expenses were EUR -2.1 (-1.8) million. Operating expenses mainly consisted of other operating expenses; especially of purchased services.

Operating profit for the financial year was EUR 2.2 (4.1) million.

Balance sheet and funding (comparison figures 31 December 2017)

The loan portfolio of Sp Mortgage Bank grew to EUR 1,854 (1,535) during the financial year. Sp Mortgage Bank funds its operations with covered bonds. Financial credit from Central Bank of the Savings Banks Finland Plc is used as short-term bridge financing.

The value of the covered bond was EUR 1,000 (990) million at the end of the financial year. At the end of the financial year, the amount of short term funding drawn from Central Bank of the Savings Banks Finland Plc was EUR 813 (528) million.

During the financial year two targeted share issues to the owner banks were carried out, which amounted to EUR 12 million. At the end of the financial year equity amounted to EUR 88 (75) million.

Capital adequacy and risk position

Capital adequacy (comparison figures 31 December2017)

Sp Mortgage Bank has adopted a capital adequacy management process, the objective of which is to ensure that the bank's risk-bearing capacity is sufficient in relation to all the major risks resulting from its business operations. Sp Mortgage Bank identifies and comprehensively assesses the risks associated with its business operations and ensures that its risk-bearing capacity is adequate when compared to the sum of all risks. The internal capital requirements specified through the capital adequacy management are based on the capital requirements under Pillar I and risks outside Pillar I, such as interest rate risk of the banking book, market risk of the investment portfolio and business risk. In the internal assessment process, Sp Mortgage Bank estimates the amount of capital that will also be sufficient for covering unexpected losses arising from risks outside Pillar I.

The Board of Directors of the bank has the overall responsibility for capital adequacy management. It approves the basis, objectives and principles of capital adequacy management. Moreover, it confirms the general requirements for the measurement and assessment of capital adequacy and the general principles for the capital adequacy management process. In practice this means that the Board of Directors approves the risk strategies and defines target levels for the capital needed to cover all material risks caused by the business operations and changes in the operating environment. The capital adequacy, liquidity and risk positions of the entities belonging to the Savings Bank Amalgamation are monitored and consolidated at the Amalgamation level. The Board of Directors of the Central Institution has set target levels for the capital adequacy of the Amalgamation and banks which are monitored quarterly.

Stress tests

As part of the capital adequacy management process, Sp Mortgage Bank uses stress tests to assess its own risk position and the adequacy of its capital. Stress tests are used when assessing how various exceptionally severe but possible scenarios may affect profitability, capital adequacy and adequacy of own funds. Stress tests are designed to identify the key risks to Sp Mortgage Bank and assess how vulnerable the structure of the Bank is in relation to the occurrence of those risks. The objective of the capital adequacy management is also to maintain and develop the quality of risk management framework.

Capital contingency plan

The capital contingency plan of Sp Mortgage Bank is made in order to be prepared for unforeseeable events that may threaten the bank's capital adequacy. The capital contingency plan includes target levels and thresholds set by the Board of Directors for the quantity and quality of the capital which are monitored quarterly. The capital contingency plan describes the actions to be taken by the management and the Board of Directors in the event that the capital adequacy ratio falls below the monitoring threshold.

Pillar I capital requirements

The biggest capital requirements of Sp Mortgage Bank are comprised of mortgage loan receivables. The standard method is applied to calculate the capital requirement for credit risk of the Bank. The capital requirement for operational risk is calculated by the standard method. The capital requirement relating to market risk is calculated by the basic method for the foreign exchange exposure.

Own funds and capital adequacy

Sp Mortgage Bank's own funds totalled EUR 88 (74) million. CET1 capital amounted to 88 million euro. Tier 1 capital also amounted to EUR 88 (74) million. The capital and reserves consist entirely of common equity tier 1 capital, core capital, and Sp Mortgage Bank has no equity classified as Tier 2 or other capital. The capital ratio of Sp Mortgage Bank was 13.4 % and the CET1 capital ratio was 13.4 %.

Sp Mortgage Bank's capital adequacy information is included in the consolidated financial statements of the Savings Banks Amalgamation. The Financial Supervisory Authority has granted permission not to deduct internal holdings of credit institutions included in the Amalgamation from own funds instruments when calculating own funds at the individual institution level and sub-consolidation group level. In addition, the Financial Supervisory Authority has granted permission to apply a 0 per cent risk weight to internal credit institution liabilities included within the scope of the Amalgamation's joint liability. These permissions are based on the European Union Capital Requirements Regulation (EU 575/2013) and the Act on the Amalgamation of Deposit Banks (599/2010). The Savings BanksGroup publishes Pillar III capital adequacy information separately in connection with the financial statements.

The Financial Supervisory Authority has granted permission to the Central Institution of the Amalgamation to waive fully the application of the requirements regarding liquidity set out in part six of Regulation (EU) No 575/2013 and its amending and supplementing acts to the Amalgamation's member credit institutions.

The capital requirement of Sp Mortgage Bank is formed by:

- 8 % minimum capital requirements set by Capital Requirement Regulation (CRR),
- 2.5% CET1 capital conservation buffer according to the Act on Credit Institutions
- The country-specific countercyclical CET1 capital requirements of foreign exposures.

The Finnish Financial Supervisory Authority is responsible for domestic macro prudential decision making after hearing the Bank of Finland, Ministry of Finance and Ministry of Social Affairs and Health. Decisions on the activation of macro prudential instruments are taken on a quarterly basis except for decisions on O-SII buffers, risk weights for loans secured by mortgages on immovable property (CRR Article 124 and 164) and systematic risk Buffer. Decisions on the activation of these instruments are taken at least once a year.

In the beginning of the year 2018, the Institution Act was updated to include a new macroprudential measure, Systemic Risk Buffer (SRB). FIN-FSA may impose SRB on the basis of the structural characteristics of the financial system. FIN-FSA defined the level of systemic risk buffer requirements for Finnish credit institutions on 29 June 2018. The systemic risk buffer requirement for the Savings Banks Amalgamation will be 1 % of risk weighted assets, and this requirement enters into effect on 1 July 2019.

Sp Mortgage Bank publishes the relevant information with regard to capital adequacy calculation each year as part of its Annual Report and Notes to the Financial Statement. The main capital adequacy information has been published in the Half-year Report.

The Savings Banks Group's financial statements and Pillar III capital adequacy information are available online at *www.saastopankki.fi/saastopankkiryhma* or from the Savings Banks' Union Coop offices at Teollisuuskatu 33, 00510 Helsinki, Finland.

Sp Mortgage Bank's capital adequacy's main items

Own funds (EUR 1,000)	31.12.2018	31.12.2017
Common Equity Tier 1 (CET1) capital before regulatory adjustments	88,184	74,695
Total regulatory adjustments to Common Equity Tier 1 (CET1)	-394	-752
Common Equity Tier 1 (CET1) capital	87,791	73,943
Additional Tier 1 (AT1) capital before regulatory adjustments	0	0
Total regulatory adjustments to Additional Tier 1 (AT1) capital	0	0
Additional Tier 1 (AT1) capital	0	0
Tier 1 capital (T1 = CET1 + AT1)	87,791	73,943
Tier 2 (T2) capital before regulatory adjustments	0	0
Total regulatory adjustments to Tier 2 (T2) capital	0	0
Tier 2 (T2) capital	0	0
Total capital (TC = T1 + T2)	87,791	73,943
Risk weighted assets	654,052	547,507
of which: credit and counterparty risk	634,720	529,621
of which: credit valuation adjustment (CVA)	8,432	4,940
of which: market risk	0	0
of which: operational risk	10,900	12,946
Common Equity Tier 1 (as a percentage of total risk exposure amount)	13.4 %	13.5 %
Tier 1 (as a percentage of total risk exposure amount)	13.4 %	13.5 %
Total capital (as a percentage of total risk exposure)	13.4 %	13.5 %
Capital requirement		
Total capital requirement	87,791	73,943
Capital requirement total*	68,677	57,499
Capital buffer	19,113	16,445

* The capital requirement of 10.5% is formed by the statutory minimum capital adequacy requirement of 8%, the capital conservation buffer of 2.5% according to the Act on Credit Institutions, and the country-specific countercyclical capital requirements of foreign exposures.

Leverage ratio

The leverage ratio of the Sp Mortgage Bank was 4.6 (4.6) % The leverage ratio has been calculated according to the known regulation, and it describes the ratio of the Sp Mortgage Bank's Tier 1 capital to total liabilities. The Sp Mortgage Bank monitors the indebtedness as part of the ICAAP process.

Leverage ratio

(EUR 1,000)	31.12.2018	31.12.2017
Tier 1 capital	87,791	73,943
Leverage ratio exposure	1,913,797	1,602,220
Leverage ratio	4.6 %	4.6 %

Resolution plan

The Directive of the European Parliament and of the Union 2014/59/EU on the recovery and resolution framework of credit institutions and investment service firms was brought nationally into force as of 1 January 2015 (the Act on the crisis solution of credit institutions and investment service firms). To implement the resolution act, the Financial Stability Authority was established (the Act on the Financial Stability Authority, 1995/2014). In May 2017 the Stability Authority decided to set a minimum requirement of own funds and eligible liabilities (MREL) at amalgamation level and this requirement will be applied starting 31 December 2018. The requirement will not be directed at the member credit institutions. The MREL requirement is in nature a Pillar 2 -type continuously required minimum requirement. The Financial Stability Authority has decided that the minimum amount of eligible liabilities is the minimum requirement of own funds times two. Currently, the requirement is 22 % of the total risk of Amalgamation.

Risk Position

Objective of risk management

The objective of risk management is to secure the bank's risk-bearing capacity and ensure the continuity of its operations. The risk-bearing capacity comprises adequate and effective risk management based on the nature and scale of the operations, as well as a sufficient degree of liquidity and capitalisation for profitable business operations.

Principles and organisation of risk management

Risk management is defined as the identification, assessment, quantification, limitation and monitoring of risks caused by business operations and closely related risks. The purpose of risk management is to minimize the likelihood of unforeseeable losses or reputational risk in order to ensure the implementation of the Group's strategy. Risk and capital adequacy management are part of internal control. Sp Mortgage Bank has a risk control function that is independent of business operations.

Risk and capital adequacy management enables the identification, assessment and measurement of risks, limiting them to a level of Sp Mortgage Bank's risk appetite. The capital needed for the various risk areas and business lines is determined in a reliable and independent manner and allocated systematically. This is done based on current and planned risk-taking and taking into account the requirements of appropriate liquidity management.

In its operations in 2018, Sp Mortgage Bank was exposed to credit, market and operational risks, as well as business and liquidity risks.

Credit and counterparty risks

Credit risk is defined as a possibility that counterparty may not meet its contractual obligations. The main source of credit risk is lending, but credit risks (counterparty risk) may also arise from other types of assets, such as bank deposits, securities in the portfolio and derivative contracts, as well as off-balance-sheet liabilities, such as undrawn credit facilities and limits as well as granted guarantees.

The business of Sp Mortgage Bank is to issue euro-denominated covered bonds with residential mortgage loans as collateral under the Act on Mortgage Credit Banks and grant residential mortgage loans referred to in the Act on Mortgage Credit Banks. Sp Mortgage Bank finances only retail customers, i.e. are private persons and entrepreneurs. The main target groups according to the Savings Banks Group's strategy are active-age households. The mortgage lending is focused on the private customer sector. The Savings Banks distributing residential mortgage loans comply with the lending goals set and approved by the each Savings Bank.

Liquidity risk

Liquidity risk is the risk that the bank is unable to meet its present or future expected or unexpected obligations as they come due, or is unable to do so without incurring unacceptable losses.

Sp Mortgage Bank does not take deposits from the public. Sp Mortgage Bank has an agreement on the use of liquid assets with the Central Bank of Savings Banks Finland Plc. A distributing Savings Bank or the Central Bank of Savings Banks Finland Plc representing it will finance the loans it has distributed with the amount that corresponds to the collateral requirement set by the rating agency. The overcollateralization amount is funded through the credit facility granted by the Central Bank of Savings Banks Finland Plc.

Market risk management

Limits and thresholds have been set for market risk measurement. The capital adequacy management process (ICAAP), which allocates capital to cover market risks of the banking book in normal and stress scenarios, is the main tool for measuring and monitoring market risks included in the banking book.

Operational risk

Operational risk refers to the risk of loss arising from inadequate or failed internal processes, personnel, systems or external factors. Legal and compliance risks are also included in the operational risks. In addition, reputational risks are managed as a part of operational risks.

Sp Mortgage Bank has identified the operational risks associated with the most important products, services, operations, processes and systems. Identifying operational risks helps determine their monitoring and controls. Some of the losses caused by operational risks are covered by insurance. The continuity plan of the bank also helps prepare for significant interruptions in operations.

Business risk

Business risk describes the impact of uncertainties caused by the operating environment on Sp Mortgage Bank's business. Business risks arise from competition, from changes in markets and customer behavior as well as from unexpected income fluctuations. Business risks may also be caused by choosing a wrong strategy, ineffective management or slow response to changes in the operating environment.

Business risks are managed and minimized through strategic and business planning.

Sp Mortgage Bank's Board of Directors and Auditors

The bank's Board of Directors includes at least three and at most five members according to the Articles of Association.

The Board of Directors consists of the following:

Tomi Närhinen, Chairman
Juhani Huupponen
Jussi Hakala
Hannu Syvänen as of 15.3.2018
Risto Seppälä until 15.3.2018

Tero Kangas acts as Managing Director of Sp Mortgage Bank.

At the annual general meeting of the Sp Mortgage Bank Plc on 15 March 2018, KPMG Oy Ab, Authorised Public Accountants, was elected as the auditor of Savings Banks' Union Coop. The chief auditor designated by the firm is Petri Kettunen, Authorised Public Accountant.

Personnel

Sp Mortgage Bank does not have own personnel, all the necessary functions and support services are bought from the companies in the Savings Banks Amalgamation or from companies offering services to the Savings Banks Amalgamation.

Owners

Sp Mortgage Bank is wholly owned by the 23 Savings Banks belonging to the Savings Banks Amalgamation.

Main outsourced functions

Sp Mortgage Bank's banking systems are outsourced to Oy Samlink Ab, which the Savings Banks owns. Sp Mortgage Banks' bookkeeping and accounts are handled by Paikallispankkien PP-Laskenta Oy.

Social responsibility

The social responsibility policy report of the Savings Banks Group is published during the year 2019 and is available after publishing on the Savings Banks Group website at www.saastopankki.fi or from the Savings Banks Union Coop offices at Teollisuuskatu 33, 00530 Helsinki, Finland. Sp Mortgage Bank's social responsibility refers to its responsibility for the impacts of its business activities on surrounding society and the company's stakeholder groups. By acting as the Savings Banks' central credit institution, Sp Mortgage Bank in its part supports the social responsibility of the local Savings Banks.

Material events after the closing date

Sp Mortgage Bank's Board of Directors are not aware of any facts that would materially influence the financial position of the Sp Mortgage Bank after the completion of the Financial statement.

Outlook for the year 2019

Outlook for the operational environment

The predictive economic indicators of the real economy point towards a continued slowing down of global economic growth in the near future. The movements of many market prices that are sensitive to business cycles—such as industrial metals and oil—support this assessment. The current basic view is that the global economy is facing a dip in growth, but a recession will be avoided for the time being. Nevertheless, it should be noted that the global operational environment is characterised by a large number of variables (including trade wars, Brexit, the situation in Italy and geopolitical risks) that may push the global economy to a sharper decline than anticipated.

At the same time, it is also possible to identify positive risks in the global economy. Economic growth in the United States has remained robust, and the strength of the U.S. economy may continue to bolster the state of the global economy going forward. Meanwhile, China has introduced stimulus measures in its monetary policy, which has usually supported the growth of the global economy. It can also be expected that the speed at which the Fed raises interest rates will become more moderate in 2019, particularly if the global growth outlook continues to weaken.

According to the ECB's latest estimate, the first interest hikes in the euro zone may take place after summer 2019. However, the euro zone's macroeconomic development in the second half of 2018 was significantly weaker than expected, and it also appears that the rate of inflation will again turn to a decrease. With this in mind, it is entirely possible that the first interest rate increases will be postponed further. A significant increase in interest rates is not expected in the euro zone in the next few years.

In the Finnish economy, the change in the economic situation and outlook is clearer than in industrialised countries on average. The changes in economic cycles in Finland are leveraged by the significant cooling down of the construction cycle. Finnish GDP growth is currently predicted to slow down to 1.4 per cent in 2019 and 1.2 per cent in 2020. The fastest phase of improving employment was already seen in the first half of 2018, and employment will improve only slightly during 2019-2020. The unemployment rate will decline to 7.0 per cent towards the end of the forecasting period. Private consumption may be affected much more than expected by lower economic growth and the weaker employment outlook, or the potential rise of interest expenses.

Business outlook

Sp Mortgage Bank expects the loan portfolio to continue to grow through sales of new contracts and the quality of the loan portfolio to remain at a high level. The capital adequacy of Sp Mortgage Bank is estimated to remain strong and the risk position to remain stable. The covered bond programme established in 2016 allows for covered bond issuances 2019.

The Board of Directors' proposal on the disposal of distributable funds

Sp Mortgage Bank's distributable funds amount to EUR 31,6 million.

The Board of Directors of Sp Mortgage Bank proposes to the Annual General Meeting that the profit for the financial year EUR 2.2 million is entered as accumulated retained earnings with no dividend paid.

Information

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Releases and other corporate information are available on the Savings Banks Group's website at
www.saastopankki.fi/saastopankkiryhma

Formulas used in calculating the financial highlights:

Revenues	Interest income, fee income, net trading income, net investment income, other operating revenue
Total operating revenue	Net interest income, net fee and commission income, net trading income, net investment income, net life insurance income, other operating revenue
Total operating expenses	Personnel expenses, other operating expenses, depreciation and amortisation of plant and equipment and intangible assets
Cost to income ratio	$\frac{\text{Total operating expenses}}{\text{Total operating revenue}}$
Return on equity %	$\frac{\text{Profit}}{\text{Equity, incl. non-controlling interests (average))}}$
Return on assets %	$\frac{\text{Profit}}{\text{Total assets (average)}}$
Equity/assets ratio %	$\frac{\text{Equity (incl. non-controlling interests)}}{\text{Total assets}}$

Alternative Performance Measures

European Securities and Markets Authority's Guidelines on Alternative Performance measures came into effect on 3 July 2016. An alternative performance measure is a financial measure of historical or future financial performance, financial position or cash flows, other than a financial measure defined or specified in the IFRS framework. Alternative Performance Measures are used to reflect financial development and enhance comparability between different reporting periods.

Sp Mortgage Bank is not using any alternative performance measures that are not directly calculated using the information presented in the financial statement, nor have any changes occurred in the financial highlights.

SP MORTGAGE BANK'S CONSOLIDATED IFRS FINANCIAL STATEMENTS

Sp Mortgage Bank's income statement

(EUR 1,000)	Note	1-12/2018	1-12/2017
Interest income		22,550	14,377
Interest expense		-5,394	-4,756
Net interest income	6	**17,157**	**9,622**
Net fee and commission income	7	-11,165	-6,558
Net trading income	8	-1,269	3,841
Total operating revenue		**4,723**	**6,904**
Personnel expenses	10	-33	-7
Other operating expenses	11	-1,662	-1,468
Depreciation of intangible assets	12	-361	-332
Total operating expenses		**-2,056**	**-1,808**
Net impairment loss on financial assets	13	20	
Profit before tax		**2,686**	**5,097**
Taxes	14	-520	-1 019
Profit		**2,167**	**4,077**

Sp Mortgage Bank's statement of comprehensive income

(EUR 1,000)	1-12/2018	1-12/2017
Profit	2,167	4,077
Total comprehensive income	2,167	4,077

Sp Mortgage Bank's statement of financial position

(EUR 1,000)	Note	31.12.2018	31.12.2017
Assets			
Loans and advances to credit institutions	16	44,151	59,227
Loans and advances to customers	16	1,852,994	1,534,830
Derivatives	17	5,776	0
Intangible assets	18	390	752
Tax assets	19	96	0
Other assets	20	3,074	3,264
Total assets		**1,906,481**	**1,598,072**
Liabilities and equity			
Liabilities			
Liabilities to credit institutions	21	815,240	528,000
Derivatives	17		2,315
Debt securities issued	22	1,000,243	990,215
Tax liabilities			481
Provisions and other liabilities	23	2,814	2,366
Total liabilities		**1,818,297**	**1,523,377**
Equity			
Share capital	24	56,601	48,597
Reserves		28,258	24,262
Retained earnings		3,325	1,836
Total equity		**88,184**	**74,695**
Total liabilities and equity		**1,906,481**	**1,598,072**

Sp Mortgage Bank's statement of cash flows

(EUR 1,000)	1-12/2018	1-12/2017
Cash flows from operating activities		
Profit	2,167	4,077
Adjustments for items without cash flow effect	1,961	-3,028
Change in deferred tax	169	538
Cash flows from operating activities before changes in assets and liabilities	**4,297**	**1,588**
Increase (-) or decrease (+) in operating assets	**-318,801**	**-767,776**
Loans and advances to customers	-318,991	-805,469
Other assets	190	37,692
Increase (-) or decrease (+) in operating liabilities	**288,355**	**762,103**
Liabilities to credit institutions	287,240	263,000
Debt securities issued	668	497,970
Other liabilities	447	1 133
Income taxes paid	-927	
Total cash flows from operating activities	**-27,076**	**-4,086**
Cash flows from investing activities		
Investments in property, plant and equipment and intangible assets		-5
Total cash flows from investing activities	**0**	**-5**
Cash flows from financing activities		
Increase in basic capital	8,004	18,576
Other monetary increases in equity items	3,996	9,274
Total cash flows from financing activities	**12,000**	**27,850**
Change in cash and cash equivalents	**-15,076**	**23,760**
Cash and cash equivalents at the beginning of the period	**59,227**	**35,467**
Cash and cash equivalents at the end of the period	**44,151**	**59,227**
Cash and cash equivalents comprise the following items:		
Receivables from central banks repayable on demand	44,151	59,227
Total cash and cash equivalents	**44,151**	**59,227**
Adjustments for items without cash flow effect		
Changes in fair value	1,269	-3,841
Depreciation, amortisation and impairment of property, plant and equipment and intangible assets	361	332
Other adjustments	330	481
Total	**1,961**	**-3,028**
Interest received	22,898	13,086
Interest paid	4,109	3,526
Dividends received	0	0

Sp Mortgage Bank's statement of changes in equity

(EUR 1,000)	Share capital	Share premium	Retained earnings	Total equity
Equity 1 January 2017	30,021	14,988	-2,241	42,768
Comprehensive income				
Profit			4,077	4,077
Total comprehensive income			**4,077**	**4,077**
Transactions with owners				
Subscription issue	18,576	9,274		27,850
Total equity 31 December 2017	**48,597**	**24,262**	**1 836**	**74,695**
Effect of IFRS 9 transition 1 January 2018			-678	-678
Equity 1 January 2018	48,597	24,262	1,159	74,018
Comprehensive income				
Profit			2,167	2,167
Total comprehensive income			**2,167**	**2,167**
Transactions with owners				
Subscription issue	8,004	3,996		12,000
Total equity 31 December 2018	**56,601**	**28,258**	**3,325**	**88,184**

BASIS OF PREPARATION

NOTE 1. INFORMATION ON THE REPORTING COMPANY AND DESCRIPTION OF THE SAVINGS BANKS GROUP AND THE SAVINGS BANKS AMALGAMATION

Sp Mortgage Bank Plc (hereinafter "Sp Mortgage Bank") is a mortgage bank wholly owned by the Savings Banks that belong to the Savings Banks Amalgamation. The role of Sp Mortgage Bank is, together with Central Bank of Savings Banks Finland Plc, to be responsible for obtaining funding for the Savings Banks Group from money and capital markets. Sp Mortgage Bank is responsible for the Savings Banks Group's mortgage-secured funding by issuing covered bonds. Sp Mortgage Bank does not have independent customer business operations or service network; instead, the Savings Banks that belong to the Savings Banks Amalgamation intermediate and sell residential mortgage loans for Sp Mortgage Bank. The Savings Banks also see to the local customer relationship management.

Sp Mortgage Bank received authorisation to operate as a mortgage bank, granted by the European Central Bank, in March 2016, and the Bank's operations began immediately. Sp Mortgage Bank has been Savings Banks' Union Coop's member credit institution starting from March 2016.

Sp Mortgage Bank is part of the Savings Banks Amalgamation and the Savings Banks Group. The Savings Banks Group (hereinafter also "the Group") is the most longstanding banking group in Finland. It comprises of Savings Banks forming the Savings Banks Amalgamation (hereinafter also "Amalgamation"), the Savings Banks' Union Coop which acts as the central institution and the subsidiaries and associated companies owned by the Savings Banks. The Savings Banks are independent regional and local banks. Together the Savings Banks form a banking group that operates locally as well as nationally. The basic objective of the Savings Banks is to promote thrift, the financial wellbeing of their customers and to operate near their customers.

The Savings Banks focus on retail banking, particularly services related to daily business, saving and investments, and lending services. The service and product range offered is complemented with the other financial services and products provided in cooperation with the service and product companies within the Savings Banks Group. The service and product companies within the Group support and promote the operations of the Group via producing centralised services or having responsibility for certain products. The most significant service and product companies of the Group are Sp Mortgage Bank Plc, Central Bank of Savings Banks Finland Plc, Sb Life Insurance Ltd, Sp-Fund Management Company Ltd, Savings Bank Services Ltd and Sp-Koti Oy.

The member organisations of the Savings Banks Amalgamation form a financial entity as defined in the Act on the Amalgamation of Deposit Banks, in which the Savings Banks' Union Coop and its member credit institutions are jointly liable for each other's liabilities and commitments. The Amalgamation comprises the Savings Banks' Union Coop, which acts as the Central Institution of the Amalgamation, 23 Savings Banks, the Central Bank of Savings Banks Finland Plc , Sp Mortgage Bank Plc, Savings Bank Services Ltd and Sp-Fund Management Company Ltd as well as the above-mentioned companies within the consolidation groups.

The coverage of the Group differs from that of the Savings Banks Amalgamation in that the Savings Banks Group also includes institutions other than credit and financial institutions or service companies. The most significant of these are Sb Life Insurance Ltd and Sp-Koti Oy. The Savings Banks Group does not form a consolidated corporation or a consolidation group as defined in the Act on Credit Institutions because the Savings Banks' Union Coop and its member Savings Banks do not have control over each other as referred to in the general consolidation accounting principles and therefore it is not possible to define a parent company for the Group.

The Savings Banks' Union Coop steers the operations of the Group and is the Central Institution responsible for the internal control framework. According to the Act on the Amalgamation of Deposit Banks, the Savings Banks' Union Coop acting as the central institution of the Savings Banks Amalgamation is obligated to prepare consolidated financial statements for the Group. Sp Mortgage Bank is also consolidated into these financial statements. The financial statements are prepared for the financial group formed by the Savings Banks Group.

The head office of Sp Mortgage Bank is in Helsinki, and its registered address is Teollisuuskatu 33, FI-00510 Helsinki, Finland. A copy of Sp Mortgage Bank's Annual Report is available online at *www.saastopankki.fi/saastopankkiryhma* or at Sp Mortgage Bank's offices at Teollisuuskatu 33, FI-00510 Helsinki, Finland.

Similarly, copies of the Group's financial statements and half-year reports are available online at *www.saastopankki.fi/saastopankkiryhma* or at Savings Banks' Union Coop's offices at Teollisuuskatu 33, FI-00510 Helsinki, Finland.

Sp Mortgage Banks Board of Directors has approved the Bank's financial statement 2018 on 5th February 2019, and the financial statement will be presented to the Annual General Meeting of 2019 for approval. The Annual General Meeting has the choice of approving or not approving the financial statement.

NOTE 2. ACCOUNTING POLICIES

1. General

Sp Mortgage Bank's financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) as implemented by the EU.

Sp Mortgage Bank is part of the Savings Banks Amalgamation and in accordance with the principles of the Act on the Amalgamation of Deposit Banks and the IAS 8 standard concerning accounting policies, adjustments and errors in accounting estimates, the Board of the Savings Banks' Union Coop confirms any accounting policy for which no guidance is available in the IFRS.

Sp Mortgage Bank's financial statements are presented in euros, which is the Bank's accounting and functional currency. The financial statement is presented in thousands of euros, unless stated otherwise.

Sp Mortgage Bank's financial statements are prepared based on original acquisition cost except for the derivatives and hedged items in fair value hedges (for hedged risks), which are measured at fair value.

Assets and liabilities are offset only in the event that Sp Mortgage Bank and the counterparty have a legally enforceable right to offset amounts and Sp Mortgage Bank intends either to settle the balance on a net basis or realise the asset and settle the liability simultaneously.

2. Financial instruments

2.1 Financial assets and liabilities

IFRS 9 Financial Instruments entered into force on 1 January 2018. More information on the transition is provided in the section Adoption of New IFRS Standards and Interpretations.

2.1.1 Initial recognition

A financial asset or liability is recognised on the balance sheet when, and only when, the entity becomes a party to the contractual provisions of the instrument. A regular way purchase or sale of financial assets is recognised and derecognised by Sp Mortgage Bank using trade date accounting.

When a financial asset or liability is recognised initially, it is measured at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. These transaction costs are recognised through profit or loss. Immediately following the initial recognition, for financial assets that are measured at fair value through other comprehensive income items and measured at amortised cost, expected credit loss (ECL) is recognised, due to which the book loss is recognised through profit or loss in conjunction with the initial recognition of the loan.

2.1.2 Classification of financial assets and the determination of classification

Business model assessment

Sp Mortgage Bank defines the business model in a manner that best reflects the principle of how groups of financial assets are managed in accordance with the business principle applied.

The business model refers to how Sp Mortgage Bank manages its financial assets in order to generate cash flows. That is, the business model determines whether cash flows will result from collecting contractual cash flows, selling financial assets or both. Consequently, this assessment is not performed on the basis of scenarios that the entity does not reasonably expect to occur, such as so-called "worst case" or "stress case" scenarios. If cash flows are realised in a way that is different from Sp Mortgage Banks expectations on the date that Sp Mortgage Bank assessed the business model, that does not give rise to a prior period error in Sp Mortgage Bank's financial statements nor does it change the classification of the remaining financial assets held in that business model as long as Sp Mortgage Bank considered all relevant information that was available at the time that it made the business model assessment.

Assessment of cash flow criteria

The business model assessment is followed by the assessment of the contractual cash flow characteristics of the financial asset, which is used as the grounds for deciding on the classification of the financial asset.

For the purpose of testing cash flow criteria, principal refers to the fair value of the financial asset at initial recognition, which can change during the term of the contract. Contractual interest consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin.

When assessing cash flow criteria, it is determined whether the contractual cash flows are solely payments of principal and interest on the principal amount outstanding, for example, interest only consists of consideration for the time value of money, credit risk and other basic lending risks. If the terms of the contract include factors that cannot be considered typical terms for lending, the financial asset is classified as measured at fair value through profit or loss.

Sp Mortgage Bank uses the following classes of financial assets in accordance with IFRS 9:

- Amortised cost (AC)
- Fair value through other comprehensive income (fair value reserve) (FVOCI)
- Fair value through profit or loss (FVTPL)

Amortised cost

A financial asset is measured at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows, and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Sales of financial assets classified as measured at amortised cost

Financial assets that are held within a business model whose objective is to hold assets in order to collect contractual cash flows are managed to realise cash flows by collecting contractual payments over the life of the instrument. That is, Sp Mortgage

Bank manages the assets held within the portfolio to collect those particular contractual cash flows (instead of managing the overall return on the portfolio by both holding and selling assets). In determining whether cash flows are going to be realised by collecting the financial assets' contractual cash flows, it is necessary to consider the frequency, value and timing of sales in prior periods, the reasons for those sales and expectations about future sales activity.

Measured at fair value through other comprehensive income

A financial asset is measured at fair value through other comprehensive income if both of the following conditions are met:

- The financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets, and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of interest and payments of principal

Sp Mortgage Bank may irrevocably designate an equity instrument as measured at fair value through other comprehensive income at the time of the instrument's initial recognition. Financial assets that are equity instruments classified as measured at fair value through other comprehensive income are measured at fair value in Sp Mortgage Banks accounting and the change in value is recognised, less deferred taxes, in the statement of comprehensive income. Dividends from equity instruments are recognised in profit or loss when the right to receive payment is established. Capital repayments from the share are recognised in the statement of comprehensive income.

Debt instruments are measured at fair value and changes in value, less deferred taxes and expected credit loss, are recognised in the statement of comprehensive income.

For debt instruments, the gain or loss on the transfer or sale of a financial asset measured at fair value through other comprehensive income is recognised through profit or loss. For equity instruments, unrealised gains or losses accrued in the fair value reserve are not transferred to be recognised through profit or loss at any stage. Instead, the recognition is made through retained earnings under equity.

Financial assets measured at fair value through profit or losst

All items that are not measured at amortised cost or recognised at fair value through other comprehensive income are recognised at fair value through profit or loss. However, a financial asset may, at initial recognition, be irrevocably designated as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

Also classified as measured at fair value through profit or loss are debt instruments for which the cash flow criteria cannot be considered to be met. Sp Mortgage Bank assesses the cash flow criteria separately for each instrument to determine whether the contractual terms of the item give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Changes in the classification of financial assets

On initial recognition, a financial asset is entered into one of three measurement classes. Debt instruments are reclassified when, and only when, Sp Mortgage Bank changes the business models applied in the management of financial assets. Sp Mortgage Bank expects that such changes will be highly infrequent.

Changes in contractual cash flows

When the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that financial asset in accordance with IFRS 9, the entity shall recalculate the gross carrying amount of the financial asset and shall recognise a modification gain or loss in profit or loss.

2.1.3 Derecognition of financial assets and liabilities

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire or the financial asset is transferred and the transfer qualifies for derecognition. A financial asset is considered to be transferred if, and only if, Sp Mortgage Bank either:

- transfers the contractual rights to receive the cash flows of the financial asset; or
- retains the contractual rights to receive the cash flows of the financial asset, but assumes a contractual obligation to pay the cash flows to one or more recipients in an arrangement that meets the conditions stipulated by IFRS 9. A contract can be considered to meet the conditions for such an arrangement if:
  - There is no obligation to pay amounts to the eventual recipients unless equivalent amounts are collected from the original asset
  - The selling or pledging of the original asset is prohibited by the terms of the transfer contract

When transferring a financial asset, the transfer qualifies for derecognition only if:

- The significant risks and rewards of ownership are transferred; or
- The significant risks and rewards of ownership are not transferred or they have been retained, but control has been transferred.

A financial liability is derecognised from the statement of financial position when, and only when, it is extinguished, i.e. when the obligation specified in the contract is discharged or cancelled or expires. An exchange between an existing borrower and lender of debt instruments with substantially different terms must be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The difference between the carrying amount and the consideration paid is recognised in profit or loss.

2.2. Determining fair value

Fair value is the price that would be attained if the asset was sold or would be paid to transfer the liability from one market party to another in a standard business transaction taking place on a valuation day.

A financial instrument's fair value is based on price quotations obtained from active markets or, if active markets do not exist, on the company's own valuation methods. A market is considered active if price quotations are readily and regularly available and if they reflect real and regularly occurring arm's-length market transactions. Current bid price is used as the quoted market price of financial assets. If the market has a well-established valuation technique for a financial instrument for which there is no direct market price available, the fair value is based on the commonly used valuation model and on the market quotations of the input data used in the model.

If there is no well-established valuation technique in the market, the fair value is determined based on a specific valuation model created for the product in question. The valuation models are based on widely used measuring techniques, incorporating all the factors that market participants would consider when setting a price. The valuation prices used include market transaction prices, the discounted cash flow method, as well as the fair value of another substantially similar instrument at the reporting date. The valuation methods take into account an estimate of credit risk, applicable discount rates, early repayment option, and other such factors that may impact reliable determination of the fair value of the financial instrument.

The fair values of financial instruments are divided into three hierarchical levels, depending on how the fair value is defined:

- Fair values quoted in active markets for identical assets or liabilities (Level 1)
- Fair values that are determined using other input data than the quoted prices at Level 1, which are observable for the assets or liabilities either directly (e.g. prices) or indirectly (e.g. derived from prices) (Level 2)
- Fair values that are determined using input data which is essentially not based on observable market data (Level 3).

The fair value hierarchy level into which an item measured at fair value is fully classified is determined by the input data which is at the lowest level and is significant in respect of the whole item. The significance of input data is evaluated considering the whole item which is valued at fair value.

2.3. Impairment

The IFRS 9 provisions on impairment are based on an expected credit loss model and they deviate from the earlier model, which was based on an actual credit loss model. The calculation of expected credit losses includes financial assets measured at amortised cost, financial assets measured at fair value through other comprehensive income, debt instruments, loan receivables, guarantees and loan commitments. Expected credit losses are not calculated on shares and holdings nor financial assets measured at fair value through profit or loss.

Impairment is assessed in two ways. As a rule, expected credit losses are recognised by assessing the probability of default for the next 12 months or, alternatively, based on the lifetime expected credit loss.

Sp Mortgage Bank calculates expected credit loss (ECL) for low-risk credit using the Loss Rate model (ECL = Loss Rate * EAD). Low-risk counterparties include the public sector, financial institutions and state-guaranteed student loans. For other credit and securities, the calculation is based on the PD/LGD model (ECL = PD * LGD * EAD).

Loss Rate model components:

- Loss rate %, i.e. the calculation is based on percentage figures established for each counterparty. Determined by the counterparty's sector code.
- EAD, short for Exposure at Default, is the annual average. Due to upcoming instalments, it is usually lower than the contract balance.
- As a rule, the assigned stage is stage 1.

The components used in the PD/LGD model:

- PD % (Probability of Default) is based on external and internal credit ratings.
- LGD % (Loss Given Default) takes into consideration the contract's available collateral at the time of default.
- EAD (Exposure At Default). The amount takes into consideration instalments and advance repayments, calculated for the term of the contract and for the year, for products for which early repayment has been modelled. Off-balance sheet items are considered to remain fixed until the end of the lifecycle of the contract. The undrawn commitment component is included in the calculation in full.

In calculating expected credit losses (ECL), Sp Mortgage Bank assigns contracts to one of three stages when the credit risk changes from the time of initial recognition. A receivable may migrate between stages according to creditworthiness:

Stage 1: 12-month ECL

- If credit risk has not significantly increased since the loan was originated, the expected credit loss on non-defaulted exposures is calculated based on 12-month expected credit loss.

Stage 2: Lifetime ECL – not credit-impaired

- If credit risk has significantly increased since the loan was originated, impairment on exposures that are not credit-impaired is calculated based on lifetime expected credit loss.

Stage 3: Lifetime ECL – credit impaired

- If the contract is assessed as credit-impaired, impairment is recognised based on lifetime expected credit loss. Stage 3 consists of exposures involving one or more occurred negative events impacting cash flows.

Occurred loss: Is deducted from the balance sheet and the proportion of the exposure recognised as a loss is no longer included in the calculation of expected losses.

In selecting the stage, the situation at the time of reporting is always compared to the situation at the time the contract was originated or acquired. The assessment of potential changes in credit risk takes into consideration all relevant and available information that can be obtained without unreasonable effort and cost. The contract's credit risk has increased significantly (the contract migrates from stage 1 to stage 2) when the contract involves payments that are more than 30 days past due (backstop), the contract's PD increases either by 10 basis points or 2.5 times its original value, or the contract is subject to forbearance (performing). The contract migrates to stage 3 when the contract is defaulted, i.e. when the contract or customer has a credit rating of D, the contract is more than 90 days past due, the contract is subject to (non-performing) forbearance or a forbearance concession has been made for the contract at the time of application. ECL calculation applies the same definition of default that the Group applies in its lending rules. A contract may migrate to a better stage after it has met the criteria for the stage in question for a period of time specified by Sp Mortgage Bank (known as the probation period).

The calculation takes the time value of money into consideration by discounting the expected credit loss calculated for the contract. The effective interest rate is the contractual interest rate and it is calculated on the gross carrying amount in stages 1 and 2 and on the adjusted carrying amount in stage 3 on the reporting date.

Four different scenarios are calculated for each contract using economic scenarios established by the Savings Banks Group's Chief Economist. The scenarios are the base scenario (50%), a mild downside (8%), a more extreme downside (2%) and an optimistic scenario (40%). The carrying amount entered in the books is calculated by applying weights to the various scenarios.

Expected credit losses are recognised as impairment under Impairment losses on financial assets in the income statement. Final credit losses are also recognised under the same item in the income statement.

2.4. Hedging and derivatives

For hedging relationships under general hedge accounting (fair value hedging), Sp Mortgage Bank has adopted IFRS 9.

Derivatives are measured at fair value starting from the contract date in the financial statements, and fair value changes are recognised in the balance sheet and income statement or in other comprehensive income.

Sp Mortgage Bank hedges its interest rate risk from changes in fair value and applies hedge accounting to hedging relationships. The hedged item in the fair value hedge are the issued fixed rate covered bonds.

Changes in the fair value of derivatives hedging fair value are recognised in the income statement under "Net trading income". When hedging fair value, the hedged item is also measured at fair value during hedging even if it would otherwise be measured at amortised cost. A change in the hedged item's fair value is recognised in the balance sheet as an adjustment to the balance sheet item and in the income statement under "Net trading income". Interest on hedging derivatives is presented as interest income and expense depending on their nature.

When hedge accounting begins, the hedging relationship between the hedged item and the hedging derivative is documented, along with the risk management objectives and the strategy for initiating hedging. The effectiveness of the hedging relationship is assessed on a continuous basis and always on reporting dates.

2.5 Financial instruments of comparison period

Financial assets 31.12.2017 are classified into the following category for valuation:

Loans and receivables

Sp Mortgage Bank's financial liabilities are classified into following category for valuation:

Other financial liabilities

Classification in the Sp Mortgage Bank's balance sheet is independent of the IAS 39 categories. Different valuation method may therefore apply to assets and liabilities presented on the same line in the balance sheet. Financial assets and liabilities by valuation category are presented in the Note 13.

Purchase and sale of financial instruments is recognised on the trade date. Financial assets are recognised when the Sp Morgage Bank gets a contractual right to cash flows or when the risks and income related to the financial asset have, to a significant degree, been transferred to the Sp Morgage Bank.

Upon initial recognition, all financial assets and financial liabilities are recognised at fair value. Transaction costs are included in the acquisition cost for the financial instruments.

Financial assets and liabilities are offset on the balance sheet if Sp Mortgage Bank currently has a legally enforceable right of set-off in the normal course of business and in the event of default, insolvency or bankruptcy, and it intends to settle the asset and liability on a net basis. Sp Mortgage Bank has not offset financial assets and liabilities on the balance sheet.

Financial assets are derecognised when the contractual rights to the cash flows of the financial item in the financial assets have expired or when the rights have been transferred to a third party so that substantially all risks and rewards have been transferred. Financial liabilities are derecognised when they are extinguished or when obligations is discharged or expired.

Loans and receivables

Financial assets classified as loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Loans and receivables are initially recognised at fair value net of directly attributable transaction costs. After initial recognition, loans and receivables are measured at amortised cost using the effective interest method.

Other financial liabilities

Other financial liabilities are initially recognised at fair value and subsequently carried at amortised cost using the effective interest method. With the exception of derivative contracts and the issued bond for which hedge accounting is applied, all financial liabilities are measured at amortised cost in the balance sheet.

Determining the fair value

Fair value is the price that would be received from selling an asset or paid to transfer a liability in a normal transaction between market participants at the measurement date.

The fair value of a financial instrument traded in active markets is based on quoted market prices or, based on the company's own valuation techniques if an active market does not exist. A market is considered active if quoted prices are readily and regularly available and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted bid price is used as the current market price of financial assets. If the market has a well-established valuation practice for a financial instrument, for which a quoted market price is not available, the fair value is based on a commonly used model for calculating the market price and the market quotation of inputs used in the valuation model.

If the valuation technique is not well established in the market, a valuation model created for the product in question is used to determine its market value. Valuation models are based on widely used calculation techniques, incorporating all factors that market participants would consider in setting a price. The valuation prices used consist of market transaction prices, discounted cash flow method and the current fair value of another substantially similar instrument at the reporting date. The valuation techniques take into account estimated credit risk, applicable discount rates, early repayment option, and other such factors that may impact the fair value of the financial instrument to be determined reliably.

The fair values of financial instruments are divided into three hierarchical levels, depending on how the fair value is defined:

- Quoted fair values in active markets for identical assets or liabilities (Level 1)

- Fair values that are determined using inputs other than Level 1 quoted prices that are observable for assets or liabilities, either directly (e.g. as prices) or indirectly (e.g. derived from prices) (Level 2)
- Fair values that are determined using input data which is essentially not based on observable market prices (Level 3).

The fair value hierarchy level to which an item measured at fair value is classified in its entirety is determined at the lowest level of input data that is significant for the whole item. The significance of the input data is evaluated in its entirety for the item which is valued at fair value.

Derivatives and hedge accounting

Derivative financial instruments are valued at fair value in the financial statements, and fair value changes are recognized in the balance sheet and income statement or in other comprehensive income.

Sp Mortgage Bank hedges its interest rate risk from changes in fair value and applies hedge accounting for the hedge relationships. The hedged item in the fair value hedge is the issued fixed rate bond.

Changes in the fair value of derivatives hedging fair value are recognized in the income statement under "Net trading income". When hedging fair value, the hedged item is also measured at fair value during hedging even if it would otherwise be measured at amortized cost. A change in the hedged item's fair value is recognized in the balance sheet as an adjustment to the balance sheet amount of the hedged item and in the income statement under "Net trading income". Interests on hedging derivatives are presented as interest income and expense depending on their nature.

Impairment losses of financial assets

Loans and receivables

The impairment losses of loans and other receivables are recognised on a receivable and collective basis. Impairment losses are estimated on a receivable basis if the amount of the customer's liabilities is significant. Other than this, impairment losses are estimated on a collective basis.

Impairment losses on loans and other receivables are recognised once there has appeared objective evidence that no payment will be received for the capital or interests of a loan or another receivable and that the collateral of the receivable is not sufficient to cover its amount. The assessment of objective evidence is based on the assessment of the customer's insolvency and the sufficiency of the collateral. When recognising an impairment loss, the collateral is valued to the amount that can be likely expected to be received for it at the time of realisation. The impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows that can be accrued from the receivable, taking into account the fair value of the collateral. The discount rate used is the receivable's original effective interest rate.

When impairment on a collective basis is calculated, loans and other receivables are classified into collectives, after which the need for impairment losses is assessed on a collective basis. The collectives are classified on the basis of similar credit risk characteristics in order to make it possible to assess the need for collective-specific impairment losses with regard to receivables for which no impairment basis applicable to a single receivable has been identified yet.

Impairment losses on loans and receivables are recognised in the allowance account. In the income statement, the impairment losses are recognised under impairment losses on loans and other receivables. If it later appears that the impairment is not permanent it is reversed.

Loans and receivables, whose collection is deemed impossible, are recognised as credit losses. Credit losses are recorded in the allowance account. Non-recoverable loans and receivables are recorded as a permanent credit loss, and the impairment loss is reversed when the normal collection process is completed and the final amount of the individual loan or receivable can be measured.

3. Leases

A lease is an agreement whereby the lessor conveys to the lessee the right to use an asset for the agreed period for a payment or a series of payments. When an agreement is concluded, leases are classified as finance leases or operating leases depending on the substance of the business transaction. A lease is a finance lease if it transfers substantially all the risks and rewards to the lessee. Otherwise, it is an operating lease.

Sp Mortgage Bank does not have leased assets under financial lease. Payments made under operating leases are charged to the income statement under other operating expenses on a straight-line basis over the period of the lease. Sp Mortgage Bank is the lessee in laptops, among other things.

4. Intangible assets

An intangible asset is an identifiable asset that has no physical substance. In Sp Mortgage Bank, intangible assets include computer software.

An intangible asset is recognised only when it is probable that economic benefits from the asset are likely to flow to the company and the acquisition cost of the asset can be reliably measured. Future economic benefits may include sales revenue from services, cost savings or other benefits resulting from Sp Mortgage Bank exercising the asset.

Intangible assets are initially measured at cost. The cost comprises the purchase price, including all costs that are directly attributable to the asset from acquisition to preparing it to its intended use. The acquisition cost does not include costs attributable to the asset's use and staff training, administrative expenses and other general overheads.

After initial recognition, an intangible asset is carried at its cost less accumulated amortisation and accumulated impairment losses. Intangible assets are amortised on a straight-line basis over their known or estimated useful lives. The useful life of intangible assets is reviewed annually.

An asset is amortised from the date when it is ready for use. An intangible asset that is not yet ready for use is tested annually for impairment.

The estimated useful lives are mainly as follows:

Information systems purchased
from external companies .... 3-5 years
Other intangible assets .... 5 years

Intangible assets are recognised in the "Intangible Assets" line item within the balance sheet. Amortisation and impairment losses are recognised in the income statement under "Depreciation, amortisation and impairment losses on tangible and intangible assets".

5. Taxes

Income taxes comprises tax based on the profit for the financial year, previous financial years' tax adjustments and changes in deferred taxes. Taxes are recognised in the income statement except if they relate directly to items recognised directly in equity or in other comprehensive income. In these circumstances the tax is also recognised directly in equity or in other comprehensive income, respectively.

Deferred taxes are calculated on the basis of temporary taxable differences between accounting and taxation. Deferred tax is determined on the basis of the IAS 12 standard using tax rates that have been enacted at the balance sheet date and that apply when the related deferred tax is expected to be realised. A change in deferred tax resulting from changing tax rates is recognised in the income statement or other comprehensive income if the tax was recorded there during earlier financial years.

A deferred tax asset is recognised for the carryforward of unused tax losses to the extent that it is probable that future taxable profit will be accrued and unused tax credits can be utilised.

6. Revenue recognition principles

Interest income and expenses

Interest income and expenses are amortised using the effective interest method over the contractual period of the loan and receivable or the liability. With this method, the income and expenses of the instrument are amortised in proportion to the remaining carrying amount of the loan and receivable or the liability in the balance sheet.

When a financial asset is impaired, the original effective interest rate is used to calculate the interest income to the carrying amount of the receivable reduced by impairment loss.

Fees and commissions

Fee and commission income and expense are generally recognised on an accrual basis. Fees and commissions for performing an action or a service are recognised when the related actions or services are performed. Fees relating to actions or services performed over several years are amortised over the service period. Fees that are directly attributable to the effective interest of a financial instrument are treated as an adjustment to the effective interest of that financial instrument.

Net Trading Incomet

Net profit from hedge accounting is recognised as Net Trading Income and consists of changes in fair value of hedged items and hedging instruments.

7. Segment information

Sp Mortgage Bank's management examines its operations as a single segment, meaning that segment-specific information is not provided in accordance with IFRS 8. Sp Mortgage Bank's operations are part of the Group's operations, and its financial statements are included in the consolidated financial statements, which is another reason why Sp Mortgage Bank's operations have not been divided into segments.

8. New IFRS-standards and interpretations

New and amended standards applied in financial year ended

Sp Mortgage Bank has applied as from 1 January 2018 the following new and amended standards that have come into effect.

IFRS 9 Financial Instruments

IFRS 9 replaced the previous IAS 39 in its entirety effective from 1 January 2018. The adoption of IFRS 9 has had a significant impact on Sp Mortgage Bank's accounting policies relating to the classification and measurement of financial assets and liabilities and the impairment of financial assets. IFRS 9 has also significantly amended other standards dealing with financial instruments such as IFRS 7: Financial Instruments: Disclosures. For notes disclosures, the IFRS 9 consequential amendments to IFRS 7 disclosures have only been applied to the current period. The comparative period disclosures repeat those disclosures in the prior year and are therefore not fully comparable with the previous year. The effects of the adoption of IFRS 9, amounting to EUR 678 thousand, have been entered directly in retained earnings in the opening balance of the transition period on 1 January 2018.

(EUR 1,000)	31.12.2017	Change	1.1.2018
Retained earnings	1,836		
Reclassifications			
Reclassification of loan loss provisions			
Expected credit losses		-847	
Expected credit losses, total			-847
Tax effect		169	
Profit (loss) for previous financial years	**1,836**	**-678**	**1,159**
Total equity quity	**74,695**	**-678**	**74,018**

The adoption of IFRS 9 changed the accounting for credit loss impairment by replacing the IAS 39 incurred loss approach with a forward-looking expected credit loss (ECL) approach. The expected credit loss allowance is calculated by evaluating financial assets' credit risk, and especially if financial assets' credit risk has significantly increased after initial recognition. Expected credit loss (ECL) is recognised for debt instruments classified as measured at amortised cost or measured at fair value through other comprehensive income, including commitments to grant credit, guarantees issued and trade receivables.

On 1 January 2018, Sp Mortgage Bank's expected credit losses stood at EUR 847 thousand, and on 31 December 2018, the corresponding figure was EUR 826 thousand. The expected credit losses for the transition period, presented in the 2017 financial statements, have been revised due to a change in the calculation model. The impact of expected credit losses as of 1 January 2018, presented in the 2017 financial statements, was EUR 838 thousand. Following the application of the adjusted calculation model, the corresponding figure is EUR 847 thousand. As a result of the adjustment to the calculation model, the expected credit losses were reduced by EUR 12 thousand in the opening balance sheet on 1 January 2018.

To determine their classification and measurement category, IFRS 9 requires all financial assets, except equity instruments and derivatives, to be assessed based on a combination of Sb Central Bank's business model for managing the financial assets and these instruments' contractual cash flow characteristics. Classification and measurement is described in more detail in section 2.1.2 of the accounting policies. The IAS 39 measurement categories of financial assets (fair value through profit and loss, available for sale, held-to-maturity and amortised cost) have been replaced by the IFRS 9 classification:

- Amortised cost (AC)
- Fair value through other comprehensive income (fair value reserve) (FVOCI)
- Fair value through profit or loss (FVTPL)

Sp Mortgage Bank's expected credit losses by financial asset class:

	1.1.2018	1.1.2019	31.12.2018	31.12.2018
(EUR 1,000)	Principal	Expected credit losses	Principal	Expected credit losses
Amortized cost (AC)	1,593,271	785	1,853,820	826

(EUR 1,000)	Measurement category IAS 39	Measurement category IFRS 9	Carrying amount IAS 39 31.12.2017	Carrying amount IFRS 9 1.1.2018
Loans and advances to credit institutions	Loans and receivables	Amortised cost	59,227	59,227
Loans and advances to customers	Loans and receivables	Amortised cost	1,534,830	1,534,044
Total assets			**1,594,056**	**1,593,271**

There were no changes to the classification and measurement of financial liabilities in IFRS 9.

The reconciliation of the carrying amounts of financial assets in accordance with IAS 39 and IFRS 9:

Financial assets (EUR 1,000)	IAS 39 carrying amount 31.12.2017	Reclassifications	Remeasurements	IFRS 9 carrying amount 1.1.2018
Amortised Cost				
Loans and advances to credit institutions				
Balance sheet 31 December 2017	59,227			
Remeasurements				
Balance sheet 1 January 2018				59,227
Loans and advances to customers				
Balance sheet 31 December 2017	1,534,830			
Remeasurements			-785	
Tase 1.1.2018				1,534,044
Financial assets measured at amortised cost, total	**1,594,056**		**-785**	**1,593,271**

IFRS 15 Revenue

IFRS 15 Revenue from Contracts with Customers entered into effect on 1 January 2018. The standard was endorsed for use by the EU in October 2016. It replaced the previous IAS 18 and IAS 11 standards and the related interpretations in the IFRS framework. Sp Mortgage Bank adopted the standard when it became mandatory on 1 January 2018. In IFRS 15, a five-step model is applied to determine when to recognise revenue, and at what amount. Revenue is recognised when (or as) a company transfers control of goods or services to a customer either over time or at a point in time.

IFRS 15 does not affect the revenue recognition from financial instruments, leases or insurance contracts, and it thereby concerns mainly various net fee and commission income items. Fees and commissions for performing an action or a service are recognised when the related actions or services are performed. Fees relating to actions or services performed over several years are amortised over the service period. With regard to services, the fulfilment of the performance obligations of the customer contract can be clearly verified, and the adoption of IFRS 15 does not entail any changes to revenue recognition. Sp Mortgage Bank's products or services do not involve repurchase agreements, warranties or the right of return, which would affect the timing or amount of revenue recognition.

Going forward, the recognition of interest and dividend revenue will be based on IFRS 9, and no changes are expected in revenue recognition compared to the current treatment in line with IAS 18. The adoption of IFRS 15 will not have an impact on Sp Mortgage Bank's income.

Annual Improvements to IFRSs (2014-2016 cycle)

The annual improvements process provides a mechanism for minor and non-urgent amendments to IFRSs to be grouped together and issued in one package annually. The amendments relate to IFRS 1 and IAS 28. The impact of the changes vary by standard, but they are not significant.

IFRIC 22 Interpretation Foreign Currency Transactions and Advance Consideration

When foreign currency consideration is paid or received in advance of the item it relates to – which may be an asset, an expense or income – IAS 21 The Effects of Changes in Foreign Exchange Rates -standard is not clear on how to determine the transaction date for translating the related item. The interpretation clarifies that the transaction date is the date on which the company initially recognises the prepayment or deferred income arising from the advance consideration. For transactions involving multiple payments or receipts, each payment or receipt gives rise to a separate transaction date. The change in the standard does not have a significant impact on the financial statements of Sp Mortgage Bank, as of Sp Mortgage Bank has very few items denominated in foreign currencies and/or operations.

Adoption of new and amended standards in future financial years

Sp Mortgage Bank has not yet adopted the following new and amended standards and interpretations already issued by the IASB. Sp Mortgage Bank will adopt them as of the effective date or, if that date is not the first day of the financial year, from the beginning of the subsequent financial year.

* = not yet endorsed for use by the European Union as of 31 December 2018.

IFRS 16 Leases (effective for financial years beginning on or after 1 January 2019)

Adoption of IFRS 16 Leases

IFRS 16 Leases entered into effect on 1 January 2019. On transition, Sp Mortgage Bank has applied a simplified approach and the comparison figures have not been adjusted. Prior to the IFRS 16 transition on 1 January 2019, Sp Mortgage Bank had no finance leases as referred to in IAS 17 and IFRIC 4. Sp Mortgage Bank's new accounting policies concerning leases are described below in the section "Basis of preparation effective from 1 January 2019". The IFRS 16 transition had no effect on profit or loss or balans, nor did it affect retained earnings, because Sp Mortgage Bank has only leases which are under the IFRS 16 exemptions and Sp Mortgage Bank has decided to choose use exemptios possibility.

Basis of preparation effective from 1 January 2019

Leases

Sp Mortgage Bank as the lessee

At the inception of a contract and when the terms and conditions of a contract are changed, Sp Mortgage Bank assesses whether the contract contains a lease. This assessment is carried out for each lease component within the contract. A contract is a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. A contract conveys the right to control if:

- The contract pertains to an identified and separate asset.
- The contract conveys the right to obtain substantially all of the economic benefits from the use of the identified asset throughout the period of use.
- The contract conveys the right to direct the use and purpose of the identified asset.

At the commencement date of a lease, the lease liability is equal to the present value of the lease payments payable during the lease term. The leases consist of fixed payments and variable lease payments, which depend on an index. Lease liabilities are subsequently measured at amortised cost using the effective interest method. Lease liabilities are reassessed if the future considerations change as a result of a contractual change in an index or price, if the lease term or amount of residual value guarantee changes, or if a purchase option is exercised. If the amount of the lease liability is adjusted due to the reassessment, a corresponding adjustment is made to the right-of-use asset.

The lease term begins at the commencement date specified in the lease. The end of the lease term is determined by the lease. The lease term is reassessed if an option to extend the lease is exercised differently than initially assessed. If the lease term is indefinite, the end of the lease term is considered to be the earliest possible date of termination specified in the lease. The discount rate used is the interest rate at which the Central Bank of Savings Banks provides financing to Savings Banks Group banks.

The value of a right-of-use asset at the commencement date is the lease liability plus payments made to the lessor at or before the commencement date, estimated restoration costs at the end of the lease term and initial direct costs. A right-of-use asset is subsequently measured at cost and amortised according to the lease term. Sp Mortgage Bank recognises leases as a right-of-use asset under "Right-of-use assets" and a liability under "Provisions and other liabilities".

Short-term leases and assets of low value

IFRS 16 contains two exemptions concerning recognition and measurement. Sp Mortgage Bank has decided that leases with a term of 12 months or less and assets whose value does not exceed EUR 5,000 are not recognised as right-of-use assets and no lease liabilities are recognised for them. Sp Mortgage Bank expenses such short-term leases and assets of low value during the lease term.

Sp Mortgage Bank as the lessor

Sp Mortgage Bank does not act as a lessor.

IFRIC 23 Uncertainty over Income Tax Treatments (effective for financial years beginning on or after 1 January 2019).

The interpretation brings clarity to the accounting for income tax treatments that have yet to be accepted by tax authorities. The key test is whether the tax authority will accept the company's chosen tax treatment. When considering this the assumption is that tax authorities will have full knowledge of all relevant information in assessing a proposed tax treatment. The change in the standard will have no significant impact on SB Central Bank's financial statement.

Amendments to IFRS 9: Prepayment Features with Negative Compensation (effective for financial years beginning on or after 1 January 2019).

The amendments enable entities to measure at amortised cost some prepayable financial assets with so-called negative compensation. The change in the standard will have no significant impact on SB Central Bank's financial statement.

Plan amendment, Curtailment or Settlement (Amendments to IAS 19)* (effective for financial years beginning on or after 1 January 2019).

The amendments clarify that on amendment, curtailment or settlement of a defined benefit plan, an entity uses updated actuarial assumptions to determine its current service cost and net interest for the period and the effect of the asset ceiling is disregarded when calculating the gain or loss on any settlement of the plan and is dealt with separately in other comprehensive income (OCI). The change in the standard will have no impact on SB Central Bank's financial statement.

Annual Improvements to IFRSs (2015-2017 cycle)* (effective for financial years beginning on or after 1 January 2019).

The annual improvements process provides a mechanism for minor and non-urgent amendments to IFRSs to be grouped together and issued in one package annually. The amendments relate to IFRS 3, IFRS 11, IAS 12 and IAS 23.

Amendments to References to Conceptual Framework in IFRS Standards* (effective for financial years beginning on or after 1 January 2020)

The revised Framework codifies IASB's thinking adopted in recent standards. The Conceptual Framework primarily serves as a tool for the IASB to develop standards and to assist the IFRS Interpretations Committee in interpreting them. It does not override the requirements of individual IFRSs.

Definition of Material (Amendments to IAS 1 and IAS 8)* (effective for financial years beginning on or after 1 January 2020)

The amendments clarify the definition of material and include guidance for the definition. In addition, the explanations accompanying the definition have been improved. The amendments aim also to ensure that the definition of material is consistent across all IFRS Standards. The change in the standard will have no significant impact on SB Central Bank's consolidated financial statement.

NOTE 3. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

IFRS-compliant financial statements require Sp Mortgage Bank's management to exercise judgment and make estimates and assumptions that affect the reported amounts of assets and liabilities and other information such as the amounts of income and expense. Although these estimates are based on the management's best knowledge at the time, it is possible that actual results differ from the estimates used in the financial statements.

The critical estimates of Sp Mortgage Bank concern the future and key uncertainties related to estimates at the reporting date, and they relate in particular to determining fair value, impairment of financial assets and recognition of deferred tax assets on confirmed tax losses.

Fair value measurement

The management should consider whether an individual financial instrument is actively traded and whether the market price obtained is a reliable indication of the financial instrument's fair value. In addition, the management must determine when the financial instruments market is not active. The management's judgment is required in cases where the financial instrument's fair value is determined using valuation techniques. If observable inputs are not available in the market for the valuation models used, the management must assess what other inputs should be used in measuring the fair value. Fair value measurement is discussed in more detail in section "Determining the fair value" in the accounting policies.

Determination of expected credit losses

The models used in the calculation of expected credit losses include estimates and assumptions that may deviate from actual outcomes. The calculations involve several discretionary factors that require the management's judgement. The most significant of these factors are as follows:

- Criteria used to assess the significant increase of credit risk
- The bank's internal credit rating model, which determines the probability of credit loss for individual receivables
- The calculation models for expected credit losses, which include assumptions regarding the behaviour of receivables in various economic scenarios
- The macroeconomic scenarios included in the calculation of expected credit losses and their impact on the amount of expected credit losses
- The anticipation of the amounts and timing of future cash flows, the realisable value of collateral and the assessment of the borrower's financial situation.

Impairment of financial assets (comparison period)

The management must also regularly assess whether there is objective evidence of the impairment of loans and receivables. Impairment testing is performed on a single receivable or a group of receivables. Receivable-specific impairment is based on the management's estimate of future cash flows of the receivable. Recognising objective evidence and evaluation of future cash flows require management's judgment. The impairment principles are explained in more detail in section "Impairment losses of financial assets" in the accounting policies.

RISK MANAGEMENT AND CAPITAL ADEQUACY MANAGEMENT POLICIES

NOTE 4. RISK MANAGEMENT AND GOVERNANCE

Objective of risk management

The objective of risk management is to secure the bank's risk-bearing capacity and ensure the continuity of its business operations. The risk-bearing capacity comprises adequate and effective risk management based on the nature, scale and complexity of Sp Mortgage Bank's business operations, as well as a sufficient amount of liquidity and capitalization based on profitable business operations.

Principles and organization of risk management

Risk management is defined as identification, assessment, quantification, limitation and monitoring of risks arising from business activities and closely related risks. The purpose of risk management is to minimize the likelihood of unforeseeable losses or reputational risk in order to ensure the implementation of the Group's strategy. Risk and capital adequacy management are part of internal control.

Risk and capital adequacy management enables the identification, assessment and measurement of risks, limiting them to a level of Sp Mortgage Bank's risk appetite. The capital needed for the various risk areas and business lines is determined in a reliable and independent manner and allocated systematically. This is done based on current and planned risk-taking and taking into account the requirements of appropriate liquidity management.

Risk management is part of Sp Mortgage Bank's internal control and an integral part of its operational activities.

Internal control covers financial and other supervision. Internal control refers to the part of management and operations which aim to ensure:

- the achievement of set objectives and goals;
- economical and efficient processes;
- the management of the risks involved in operations;
- the fairness and accuracy of financial and other management information;
- compliance monitoring;
- the adequate protection of operations, data, as well as the entity's property and customers' assets; and
- adequate and appropriately organised manual and IT systems for the support of operations.

The purpose of internal control at Sp Mortgage Bank is to ensure that the objectives and aims set for different levels at the bank are reached in compliance with the agreed and set internal control guidelines. Internal control is supervision from the inside managed by the administrative organs and the organisation itself, and it primarily concerns the state, quality and results of operations. Internal control is carried out by the Board of Directors, Managing Director, risk control function, supervisors and employees. In addition, employees are required to report deviations and misconduct to those higher up in the organisation.

Sp Mortgage Bank's risk management is based on the business strategy and risk management guidelines confirmed by the Board of Directors and an authorisation system as well as the risk and deviation reports produced in terms of key business areas.

Sp Mortgage Bank does not have excessively large customer or investment portfolio risk concentrations in relation to its financial capacity, and in accordance with its strategy, Sp Mortgage Bank will take no such risks.

Sp Mortgage Bank maintains its capital adequacy at adequate level.

The Board of Directors is regularly informed on the risk positions and their changes affecting Sp Mortgage Bank. The Board also approves the authorizations and guidelines of risk-taking by determining risk limits for accepted risk types. The implementation of the risk stategy is monitored through monitoring and reporting of risk limits and thresholds, carried out by risk control unit independent of business operations. The Board of Directors also approves the authorities and framework for risk-taking by specifying the permitted risk thresholds for different risk types. The responsibility for daily risk monitoring and control is with the man-agement according to set authorizations. The systems and procedures regarding risk reporting and monitoring fulfil the criteria set for risk management, taking into account the nature, scale and complexity of Sp Mortgage Bank's business operations.

Sp Mortgage Bank has established the following functions, independent of business operations, to ensure effective and comprehensive internal control system:

- independent risk control
- compliance
- internal audit

The task of the independent Risk Control unit is to ensure and monitor that the risk management frame-work of the Sp Mortgage Bank is adequate in relation to the nature, scale, complexity and risk level of the Sp Mortgage Bank's business operations. The Risk Control unit assists the Board of Directors and senior management of the Sp Mortgage Bank in their task to arrange adequate risk management framework and monitor the functionality and efficiency of the risk management framework.

The Compliance unit ensures that Sp Mortgage Bank complies with the legislation and authorities' regula-tion and guidelines. The Compliance unit is responsible for monitoring that Sp Mortgage Bank complies with the internal guidelines, ethical guidelines given to the personnel and other guidelines applied within the financial markets.

The Board of Directors of Sp Mortgage Bank has established internal audit for the bank and approved the internal audit plan and reporting principles.

The task of internal audit is to assess the scope and adequacy of the internal control of the bank's operating organisation and monitor and assess the functioning of the risk management systems. Internal audit reports on its observations to the Managing Director and the Board of Directors.

The Board of Directors of Sp Mortgage Bank is responsible for organising internal control in accordance with legislation, requirements of the authorities and guidelines issued by the Board of Directors of the Central Institution.

The Managing Director and other executives of Sp Mortgage Bank are responsible for organising internal control in accordance with legislation, requirements of the authorities and more detailed internal guidelines issued by the Central Institution and the bank's Board of Directors.

The independent functions of Savings Banks' Union Coop are responsible for Sp Mortgage Bank's inde-pendent functions.

The methods of risk management in the Amalgamation are maintained and developed by Central Institution's Risk Control unit. The objective is to ensure that the risk management covers all material risks, including any new and previously unidentified risks.

All significant or risk bearing commitments including significant risk are made in accordance with collegial decision making processes, and mandates are limited according to a structure. Internal operational guidelines are used to steer business operations and processes. Compliance with the internal guidelines as well as the updating process of the guidelines is monitored. Decisions and significant business operations are documented and archived. An essential part of risk management is executed in daily supervision. The execution of made decisions is monitored through approval and verification process, controls and recon-ciliations together with adequate follow-up, monitoring and reporting.

In its operations Sp Mortgage Bank is exposed to credit, market and operational risks, as well as business and liquidity risks

Credit and counterparty risks

The credit risk is the most significant risk of the Banking segment. The management and monitoring of the credit risk plays a major role when ensuring the adequacy of capital compared to business risks and losses caused by risk occurrence.

Credit risk is defined as a possibility that counterparty may not meet its contractual obligations. The main source of credit risk is lending, but credit risks (counterparty risk) may also arise from other types of assets, such as bank deposits, securities in investment portfolio and derivative contracts, as well as off balance-sheet liabilities, such as undrawn credit facilities and limits as well as granted guarantees.

The business of Sp Mortgage Bank is to issue euro-denominated covered bonds with residential mortgage loans as collateral under the Act on Mortgage Credit Banks and grant residential mortgage loans referred to in the Act on Mortgage Credit Banks. Sp Mortgage Bank finances only retail customers, which are private persons and entrepreneurs. The main target groups according to the Savings Banks Group's strategy are families and household of active age. The mortgage lending is focused to the private customer sector. The Savings Banks distributing residential mortgage loans comply with the lending goals set and approved by the each Savings Bank.

Management of credit risk

The Board of Directors of Sp Mortgage Bank steers the credit risk management, the methods used, as well as the monitoring and reporting by approving the credit risk strategy, other guidelines and by setting the risk limits and other thresholds. Sp Mortgage Banks's Risk Control monitors that the bank comply with these principles.

The business strategy of Sp Mortgage Bank and the credit-underwriting policies define the maximum exposure limits to risk concentrations and steer the lending by customer groups, industries and credit ratings. Saving Banks distributing residential mortgage loans mainly grant credits within their operational areas ensuring one of the essentials features for the lending of the Savings Banks: local and comprehensive knowledge of the customers.

Sp Mortgage Bank have outsourced main part of the loan processes and operations the loan distributing Savings Banks and to Savings Bank Services Ltd, which is responsible for the back office operations of Sp Mortgage Bank.

A distribution agreement has been concluded between Sp Mortgage Bank and Savings Banks distributing Sp Mortgage Bank's loans. This distribution agreement determines the right of Savings Banks to grant residential mortgage loans directly on the balance sheet of Sp Mortgage Bank. In the agreement, the Savings bank is defined as having an obligation/right to repurchase a loan from Sp Mortgage Bank which does not qualify for the cover pool of the mortgage credit bank or which has become a defaulted loan.

In the Savings Banks the Board of Directors makes the most significant credit decisions. Each Board of Di-rectors delegates the necessary lending authorities to the banks' senior management/ management team/credit committee and other named persons involved in the lending. The credit decisions are made according to Sp Mortgage bank's credit-underwriting policy as approved by the Board of Directors. The main principle is decision making by two persons having lending authorization. The credit decisions are based on the customers' credit worthiness, ability to pay and other criteria, for example regarding acceptable collaterals, applied to credit decision making. The collaterals are valued at fair value conservatively and their fair values are regularly monitored using both statistical information and bank's comprehensive knowledge about its operating area. The Board of Directors approves the instructions and guidelines for the valuation of the different collateral types and their collateral value applied in lending. The evaluation of the fair value of the collateral is always done on a case-by-case basis.

The loans to private customers are granted against sufficient residential collateral. Sp Mortgage Bank's loans have to continuously meet the criteria of the Act on Mortgage Credit Bank operations and the separate instructions given by the Board of Directors of Sp Mortgage Bank. The collateral is required to be the first priority residential collateral.

Residential mortgage loan pledged as collateral for a covered bond may not exceed the fair value of the shares or real estate used as collateral. Only 70 per cent of the fair value of the shares or real estate used as collateral for each residential mortgage loan is counted in the total amount of collateral for covered bonds.

The credit risk instructions laid down by the Savings Banks Amalgamation are used to calculate the fair value of the collaterals. Sufficient information is required regarding collaterals when making credit decisions. The fair value of the collateral is approved by the credit decision which is based on the valuation of the collateral. Credit decision is done based on the current and valid Savings Bank's lending authorization.

The fair value of the real estate is measured based on good real estate practice. The value of the collateral is updated when material changes occur which increases Sp Mortgage Bank's risks; e.g. when the fair value of the collateral has decreased materially or when there are changes in the co-debtors.

In Sp Mortgage Bank, credit risk is regularly assessed by monitoring, for example, the amount of loans in arrears and the amount of non-performing loans. The customer account managers monitor the loan and collateral position of the customer based on the payment behavior and customers other activity. The Board of Directors of Sp Mortgage Bank receives regular reporting on customer exposures and non-performing loans. The reporting includes, among other things, the risk position and its development by customers, industries and credit ratings.

The loan portfolio of Sp Mortgage Bank increased during 2018 by 319 million and was 31.12.2018 EUR 1,854 (1,535) million. Loans on the balance sheet to private persons are 98 % and loans to entrepreneurs 2 %.

Breakdown of loans by customer groups

Customer group (EUR 1,000)	31.12.2018	31.12.2017	Change %
Private persons	1,823,909	1,508,915	21 %
Entrepreneurs	29,911	25,914	15 %
Total	**1,853,820**	**1,534,830**	**21 %**

The credit worthiness of a private customer is based on the local Savings Bank's comprehensive customer knowledge and the assessment of the customer's ability to pay. The credit decision is mainly based on the customer's sufficient repayment ability. The customer's ability to pay, earlier repayment behavior, the credit scoring of the application together with the loan-to-value ratio forms the basis for the credit decision and the risk-based pricing.

According to the IFRS 9 Financial instruments standard effective for reporting periods beginning on or after 1 January 2018 retail exposures are classified into 9 different risk-rating classes. With the IFRS 9 Financial instruments standard, entered into effect on 1.1.2018 the classification for loans changed from previously 14 classes to 9 classes.

Private lending by rating distribution

(EUR 1,000)		31.12.2018				% of portfolio	
Description	12 M PD	Stage 1	Stage 2	Stage 3	Total	31.12.2018	31.12.2017
1 Excellent	0.0 % - 0.3 %	19,860	25		19,885	1 %	2 %
2 Good	0.3 % - 0.4 %	226,324	359		226,683	12 %	4 %
3 Good	0.4 % - 1.0 %	545,109	5,994		551,103	30 %	23 %
4 Average	1.0 % - 1.9 %	679,951	31,275	382	711,609	38 %	47 %
5 Average	1.9 % - 3.7 %	240,511	51,537	322	292,369	16 %	21 %
6 Weak	3.7 % - 7.8 %	17,487	16,394		33,881	2 %	1 %
7 Past due but not impaired	7.8 % - 9.9 %	4,073	11,915	51	16,040	1 %	2 %
8 Past due but not impaired	9.9 % - 22.3 %		1,916	200	2,116	0 %	0 %
D Non-performing	100.0 %			134	134	0 %	0 %
Total		**1,733,316**	**119 414**	**1 090**	**1 853 820**	**100 %**	**100 %**

Retail customer ratings are mainly good or excellent. The ratings improved during 2018 due to for example faster and more efficient debt collection.

Concentration risks

The credit risk concentrations referred to in the credit risk strategy may arise when the loan portfolio contains large amounts of loans and other exposures to the following:

- Single counterparty
- Groups consisting of single counterparties and their interest groups
- Certain industries
- Against certain collateral
- With identical maturity
- Same product/instrument

The total amount of credit granted by Sp Mortgage Bank to a single customer and/or customer group must not exceed the maximum amounts set in the Credit Institutions Act or other acts, or the regulations given by the Financial Supervisory Authority or other regulatory authority. The concentration risks caused by an individual counterparty are restricted with limits and guidelines related to the maximum customer exposure.

Non-performing loans and payment delays

The non-performing loans and payment delays are followed regularly. Sp Mortgage Bank does not have any non-performing loans at 31.12.2018. In certain circumstances if the customer would otherwise face financial difficulties in the future the customer may be granted a change in the terms and conditions of the loan, for example interest-only period or restructuring the loan. The reason for these arrangements is to ensure the customers' ability to pay and avoid possible credit losses. The prerequisite for granting any forbearance measures to the loans is that the customers' financial difficulties are estimated to be short-termed and temporary.

Expected credit losses (ECL)

Expected credit losses have calculated in 2018 based on IFRS 9 standards, hence they are not completely comparable with previous years IAS 39 standards' calculations.

Expected credit losses have calculated on the contract level and those have divided by three different stages based on the condition of contract. On the top of the information about customer and contract, the calculations consider also the economy forecast from the Savings Banks Group Chief Economist. Note 2 Accounting policies includes the further description about ECL model.

The contract is in stage 1, if credit risk has not increased significantly since initial recognition, expected credit loss is calculated based on 12 months credit loss. The contract will be switched to stage 2, if credit risk has increased significantly since initial recognition, expected credit loss has calculated based on credit loss expected during the remaining duration. Lastly, stage 3 has used if contract has defaulted. Then expected credit loss has calculated based on credit loss expected during the remaining duration. Stage 3 includes exposures, which have one or more actual events that have negative impact on cash flows. All the stage 3 ECL amounts are evaluated at least quarterly.

Exposures is returning to stage 1, when it has fulfilled the stage 1 requirements for past 12 months. The same can be implemented for returning to stage 2 from stage 3. All returned exposures from stage 3 to stage 2 are under the monthly evaluations of expected credit losses.

Loans and receivables whose recovery is deemed impossible are recognized as credit losses. Credit losses have recognized in the deduction account. Non-recoverable loans and receivables are recognized as permanent credit loss and the impairment is cancelled when the normal recovery process is completed and the final amount of loss on an individual loan or receivable can be calculated.

Expected credit losses on loans and receivables was EUR 827 thousand 31.12.2018. Expected credit losses are 0.04 % of the credit portfolio. Note 2 explains more about the level movements of expected credit losses.

According to the IFRS 9 Financial instruments standard effective for reporting periods beginning on or after 1 January 2018 retail exposures are classified into 9 different risk-rating classes.

Market risk

In general, market risk refers to the impact of a change in market prices on the market value of financial assets and liabilities. The most important market risk in banking activities is the interest rate risk in the banking book, which is measured through both net present value and net interest income.

The business of Sp Mortgage Bank is to issue euro-denominated covered bonds with residential mortgage loans as collateral and grant residential mortgage loans as defined in the Act on Mortgage Credit Bank operations.

As defined, Sp Mortgage Bank does not have a trading book. Sp Mortgage Bank may acquire bonds used as temporary supplementary collateral or as a liquidity buffer, but otherwise it will not have an investment portfolio.

Sp Mortgage Bank does not take any equity risk, commodity risk or currency risk. Both the issued covered bonds and the residential mortgage loans used as their collateral and any temporary supplementary collateral and other balance sheet items and off-balance sheet items are all euro-denominated.

Market risk management

Limits and thresholds have been set for market risk measurement. The capital adequacy management process (ICAAP), which allocates capital to cover market risks of the banking book in normal and stress scenarios, is the main tool in measuring and monitoring market risks included in the banking book.

Interest rate risk in the banking book

Sp Mortgage Bank's key market risk is the interest rate risk in the banking book, which is monitored using both present value risk and income risk.

Interest rate risk refers to the adverse effect of interest rate changes on the market value (present value risk) or on the net interest income (income risk) of the balance sheet and off-balance sheet items. Interest rate risk may be further divided into the following risk types:

- yield curve risk, which arises as a result of the impact of changes in the interest rate curve on the present value of the future cash flows of assets and liabilities
- re-pricing risk, which arises from the difference between maturities for fixed rate assets and liabili-ties and from the timing mismatch between re-pricing for floating rate assets and liabilities
- basis risk, arising from the different interest rate bases of assets and liabilities
- optionality risk, arising from stand-alone and embedded options in which the decision to exercise may depend on interest rates. These include call and put options embedded in bonds which entitle to an early redemption of a loan or an early withdrawal without compensation.

In Sp Mortgage Bank interest rate risk arises from the different interest rate bases of lending and funding.

In Sp Mortgage Bank derivative contracts will only be concluded to hedge against risks. Sp Mortgage Bank manages its interest rate risks by pegging both sides of its balance sheet to short-term market interest rates. Any supplementary collateral or bonds in the liquidity buffer will be hedged using short-term market interest rates. Hedge accounting is applied to the hedges implemented. All hedging derivatives will be implemented directly from Sp Mortgage Bank with a credit institution outside the Savings Banks Group.

The interest rate risks are measured using both the net interest income and the change in the present value of the balance sheet. The net present value method measures the change of the net present value of the balance sheet resulting from a change in interest rates when each balance sheet item is valued as the present value of its cashflows. The income risk model predicts the future net interest income over one year with changing market interest rates.

Liquidity risk

Liquidity risk is the risk that the bank is unable to meet its present or future expected or unexpected obligations as they come due, or is unable to do so without incurring unacceptable losses.

The table below shows the net interest income's sensitivity to a 1 percentage point's parallel shift in the interest rate curve.

Net interest income sensitivity to a 1 % -point parallel shift in the interest rate curve

(EUR 1,000)	Change in net interest income			
	31.12.2018		31.12.2017	
Period	Down	Up	Down	Up
Change in the coming 12 months	4,281	1,083	4,088	503
Change in 12-24 months	9,087	1,793	8,437	542

Sp Mortgage Bank does not take deposits from the public. Sp Mortgage Bank has an agreement on the use of liquid assets with the Central Bank of Savings Banks Finland Plc. A distributing Savings Bank or the Central Bank of Savings Banks Finland Plc representing it will finance the loans it has distributed with the amount that corresponds to the collateral requirement set by the rating agency. The overcollateralization amount is funded through the credit facility granted by the Central Bank of Savings Banks Finland Plc.

The liquidity reserve and the liquidity requirement

Sp Mortgage Bank has a reserve of free liquid assets in case of a rapid and unexpected weakening of the liquidity situation. The size of the liquidity reserve is determined on the basis of the liquidity coverage requirement. The liquidity reserve, i.e. the liquidity portfolio, consists of assets held in a payment transaction account and an LCR account. The sufficiency of the liquidity reserve will be measured by the LCR ratio defined in the Delegated Regulation.

Assets 31.12.2018 (EUR 1,000)	Total	< 3 months	3-12 months	1-5 years	> 5 years
Loans and advances to credit institutions	44,151	44,151			
Loans and advances to customers	1,853,820	28,706	87,849	460,906	1,276,359
Financial assets total	**1,897,971**	**72,857**	**87,849**	**460,906**	**1,276,359**

Liabilities 31.12.2018 (EUR 1,000)	Total	< 3 months	3-12 months	1-5 years	> 5 years
Due to credit institutions and central banks	813,000	160,000	640,000	10,000	**3,000**
Debt securities in issue	1,000,000			1,000,000	
Financial liabilities total	**1,813,000**	**160,000**	**640,000**	**1,010,000**	**3,000**

Assets 31.12.2017 (EUR 1,000)	Total	< 3 months	3-12 months	1-5 years	> 5 years
Loans and advances to credit institutions	59,227	59,227			
Loans and advances to customers	1,534,830	22,425	70,972	372,261	1,069,172
Financial assets total	**1,594,056**	**81,651**	**70,972**	**372,261**	**1,069,172**

Liabilities 31.12.2017 (EUR 1,000)	Total	< 3 months	3-12 months	1-5 years	> 5 years
Due to credit institutions and central banks	528,000	300,000	220,000	**8,000**	
Debt securities in issue	1,000,000			1,000,000	
Financial liabilities total	**1,528,000**	**300,000**	**220,000**	**1,008,000**	**0**

Operational risk

Operational risk refers to the risk of loss arising from inadequate or failed internal processes, personnel, systems or external factors. Legal and compliance risks are also included in the operational risks. In addition, reputational risks are managed as a part of operational risks. The various stages of lending and trading processes also involve operational risks as well credit, liquidity and market risks, which are assessed in the evaluation of operational risks at the Group and Amalgamation level. Strategic risks have here been excluded from operational risks.

Sp Mortgage Bank's operations comply with the current legislation, government regulations, the rules of good banking practices as confirmed by the Federation of Finnish Financial Services and the principles of the management of operational risks, along with other internal guidelines of Sp Mortgage Bank.

The Board of Directors of Sp Mortgage Bank has the overall responsibility for the operational risks and for defining risk levels and operational risk management procedures related to their identification, measurement, mitigation, monitoring and control. The Board of Directors of Sp Mortgage Bank approves the principles and key operational guidelines of the operational risk management. The risk and compliance function monitors that the operational risk guidelines are implemented and complied with in all operations and functions in Savings Banks Group.

Sp Mortgage Bank has identified the operational risks associated with the most important products, services, operations, processes and systems. Identifying operational risks helps determine their monitoring and controls. Some of the losses caused by operational risks are covered by insurance. The continuity plan of the bank also helps prepare for significant interruptions in operations.

Within Sp Mortgage Bank, operational risks, realized losses and near misses are regularly reported to the management.

Legal risk

Legal risks refer to risk of loss due to an invalid contract or incomplete documentation and the risk of sanctions, liability to compensate customers and loss of goodwill due to non-compliance with laws or official regulations. Sp Mortgage Bank complies with standard terms worked out jointly by the banking industry. When finalizing non-standard agreements, legal services are used and external experts are consulted when needed.

Compliance function has been established to ensure that Sp Mortgage Bank comply with regulations and internal guidelines. Compliance function's responsibility is to ensure that the bank comply with laws, regulations and guidelines. Compliance function also monitors that the bank comply with its own internal guidelines, ethical principles for personnel and other instructions. There are no risk tolerance for compliance risks and necessary means are taken to prevent any compliance risks to materialize in Savings Banks Group.

Business risk

Business risk describes the impact of uncertainties caused by the operating environment on Sp Mortgage Bank's business. Business risks arise from competition, from changes in markets and customer behavior as well as from unexpected income fluctuations. Business risks may also be caused by choosing a wrong strategy, ineffective management or slow response to changes in the operating environment.

Business risks are managed and minimized through strategic and business planning.

NOTE 5. CAPITAL ADEQUACY MANAGEMENT

Sp Mortgage Bank has adopted capital adequacy management process, the objective of which is to ensure the bank's risk-bearing capacity is sufficient in relation to all the major risks resulting from its business operations. Sp Mortgage Bank identifies and comprehensively assesses the risks associated with its business operations and ensures that its risk-bearing capacity is adequate when compared to the sum of all risks. The internal capital requirements specified through the capital adequacy management are based on the capital requirements under Pilar I and risks outside Pillar I, such as interest rate risk of the banking book, market risk of the investment portfolio and business risk. In the internal assessment process, Sp Mortgage Bank estimates the amount of capital that will also be sufficient to cover unexpected losses arising from risks outside Pillar I.

The Board of Directors of the bank has overall responsibility for capital adequacy management. The Bank's Board of Directors approves the basis, objectives and principles of capital adequacy management. Moreover, the Board of Directors confirms the general requirements for the measurement and assessment of capital adequacy and the general principles for the capital adequacy management process. In practice this means that the Board of Directors approves the risk strategies and defines target levels for the capital needed to cover all material risks caused by the business operations and changes in the operating environ-ment, The capital adequacy, liquidity and riskpositions of the entities belonging to the Savings Bank Amal-gamation are monitored and consolidated at the Amalgamation level. The Board of Directors of the Central Institution has set target levels for the capital adequacy of the Amalgamation and banks, which are monitored quarterly.

Stress tests

As part of the capital adequacy management process, Sp Mortgage Bank uses stress tests to assess its own risk position and the adequacy of its capital. Stress tests are used when assessing how various exceptionally severe but possible scenarios may affect profitability, capital adequacy and adequacy of own funds. Stress tests are designed to identify the key risks to Sp Mortgage Bank and assess how vulnerable the structure of the Bank is in relation to the occurrence of those risks. The objective of the capital adequacy management is also to maintain and develop the quality of risk management framework.

Capital contingency plan

The capital contingency plan of Sp Mortgage Bank is made in order to be prepared for unforeseeable events that may threaten the bank's capital adequacy. The capital contingency plan includes target levels and thresholds set by the Board of Directors for the quantity and quality of the capital, which are monitored quarterly. The capital contingency plan describes the actions to be taken by the management and the Board of Directors in the event that the capital adequacy ratio falls below the threshold.

Pillar I capital requirements

The biggest capital requirements of Sp Mortgage Bank are comprised of mortgage loan receivables. The standard method is applied to calculate the capital requirement for credit risk of the Bank. The capital requirement for operational risk is calculated by the basic method.

Own funds and capital adequacy

Sp Mortgage Bank's own funds totalled EUR 88 (74) million. CET1 capital amounted to 88 million euro. Tier 1 capital amounted also to EUR 88 (74) million. The capital and reserves consist entirely of common equity tier 1 capital, core capital, and Sp Mortgage Bank has no equity classified as Tier 2 or other capital. The capital ratio of Sp Mortgage Bank was 13.4 % and the CET1 capital ratio was 13.4 %.

The information concerning Sp Mortgage Banks' capital adequacy is included in the consolidated financial statement of the Savings Banks Amalgamation. The Financial Supervisory Authority has granted a permission not to deduct internal holdings of credit institutions included in the Amalgamation from own funds instruments when calculating own funds at the individual institution level and sub-consolidation group level. In addition, the Financial Supervisory Authority has granted a permission to apply a 0 per cent risk weight to internal credit institution liabilities included within the scope of the Amalgamation's joint and several liability. These permissions are based on the European Union Capital Requirements Regulation (EU 575/2013) and the Act on the Amalgamation of Deposit Banks (599/2010). Savings BanksGroup publishes Pillar III capital adequacy information separately in connection with the financial statements.

The Financial Supervisory Authority has granted permission to the Central Institution of the Amalgamation to waive fully the application of the requirements regarding liquidity set out in part six of Regulation (EU) No 575/2013 and its amending and supplementing acts to the Amalgamation's member credit institutions.

The capital requirement of Sp Mortgage Bank is formed by:

- 8 % minimum capital requirements set by Capital Requirement Regulation (CRR),
- 2.5% CET1 capital conservation buffer of according to the Act on Credit Institutions
- The country-specific countercyclical CET1 capital requirements of foreign exposures.

The Finnish Financial Supervisory Authority is responsible for domestic macro prudential decision making after hearing the Bank of Finland, Ministry of Finance and Ministry of Social Affairs and Health. Decisions on the activation of macro prudential instruments are taken on a quarterly basis expect for decisions on O-SII buffers, risk weights for loans secured by mortgages on immovable property (CRR Article 124 and 164) and systematic risk Buffer. Decisions on the activation of these instruments have taken at least once a year.

In the beginning of the year 2018 Credit Institution Act was updated to include a new macro-prudential measure, Systemic Risk Buffer (SRB). FIN-FSA may impose SRB on the basis of the structural characteristics of the financial system. FIN-FSA made decision on the level of systemic risk buffer requirements for Finnish credit institutions on 29 June 2018. The systemic risk buffer requirement for Savings Banks Amalgamation will be 1 % of risk weighted assets, and this requirement enters into effect on 1 July 2019.

Sp Mortgage Bank has published the relevant information with regard to capital adequacy calculation each year as part of its

Annual Report and Notes to the Financial Statement. The main capital adequacy infor-mation has been published in the Half-year Report.

The Savings Banks Group's financial statements and Pillar III capital adequacy information are available online at *www.saastopankki.fi/saastopankkiryhma* or from the Savings Banks Union Coop offices at Teollisuuskatu 33, 00510 Helsinki, Finland.

Sp Mortgage Bank's capital adequacy's main items

Own Funds (EUR 1,000)	31.12.2018	31.12.2017
Common Equity Tier 1 (CET1) capital before regulatory adjustments	88,184	74,695
Total regulatory adjustments to Common Equity Tier 1 (CET1)	-394	-752
Common Equity Tier 1 (CET1) capital	87,791	73,943
Additional Tier 1 (AT1) capital before regulatory adjustments	0	0
Total regulatory adjustments to Additional Tier 1 (AT1) capital	0	0
Additional Tier 1 (AT1) capital	0	0
Tier 1 capital (T1 = CET1 + AT1)	87 791	73 943
Tier 2 (T2) capital before regulatory adjustments	0	0
Total regulatory adjustments to Tier 2 (T2) capital	0	0
Tier 2 (T2) capital	0	0
Total capital (TC = T1 + T2)	87,791	73,943
Risk weighted assets	654,052	547,507
of which: credit and counterparty risk	634,720	529,621
of which: credit valuation adjustment (CVA)	8,432	4,940
of which: market risk	0	0
of which: operational risk	10,900	12,946
Common Equity Tier 1 (as a percentage of total risk exposure amount)	13.4 %	13.5 %
Tier 1 (as a percentage of total risk exposure amount)	13.4 %	13.5 %
Total capital (as a percentage of total risk exposure)	13.4 %	13.5 %
Capital requirement		
Total capital requirement	87,791	73,943
Capital requirement total*	68,677	57,499
Capital buffer	19,113	16,445

* The capital requirement of 10.5% is formed by the statutory minimum capital adequacy requirement of 8%, the capital conservation buffer of 2.5% according to the Act on Credit Institutions, and the country-specific countercyclical capital requirements of foreign exposures.

Leverage ratio

The leverage ratio of Sp Mortgage Bank was 4.6 % (4.6 %). The leverage ratio has been calculated according to the known regulation, and it describes the ratio of the Bank's Tier 1 capital to total liability.

Leverage ratio

(EUR 1,000)	31.12.2018	31.12.2017
Tier 1 capital	87,791	73,943
Leverage ratio exposure	1,913,797	1,602,220
Leverage ratio	4.6 %	4.6 %

Resolution plan

The Directive of the European Parliament and of the Union 2014/59/EU on the recovery and resolution framework of credit institutions and investment service firms was brought nationally into force as of 1 January 2015 (the Act on the crisis solution of credit institutions and investment service firms). To implement the resolution act, the Financial Stability Authority was established (the Act on the Financial Stability Authority, 1995/2014). In May 2017 the Stability Authority decided to set a minimum requirement of own funds and eligible liabilities (MREL) at amalgamation level and this requirement will be applied starting December 31st 2018. The requirement will not be directed at the member credit institutions. The MREL requirement is in nature a Pillar 2 -type continuously required minimum requirement. The Financial Stability Authority has decided that the minimum amount of eligible liabilities is the minimum requirement of own funds times two. Currently, the requirement is 22 % of the total risk of Amalgamation.

PROFIT FOR THE PERIOD

NOTE 6. NET INTEREST INCOME

(EUR 1,000)	1-12/2018	1-12/2017
Interest income		
Loans and advances to customers	18,682	12,825
Derivative contracts		
Hedging derivatives	3,850	1,730
Other	18	-178
Total	**22,550**	**14,377**
Interest expense		
Liabilities to credit institutions	-2,819	-2,358
Derivative contracts		
Hedging derivatives	11	-11
Debt securities issued	-1,793	-1,027
Limits	-661	-1,267
Other	-131	-94
Total	**-5,394**	**-4,756**
Net interest income	**17,157**	**9,622**

NOTE 7. NET FEE AND COMMISSION INCOME

(EUR 1,000)	1-12/2018	1-12/2017
Fee and commission income		
Lending	557	325
Total	**557**	**325**
Fee and commission expense		
Securities		-2
Asset management*	-11,719	-6,877
Other	-3	-4
Total	**-11,722**	**-6,884**
Net fee and commission income	**-11,165**	**-6,558**

* Consists mainly of fees paid to the intermediating banks.

NOTE 8. NET TRADING INCOME

(EUR 1,000)	1-12 2018	1-12/2017
Net income from hedge accounting		
Change in hedging instruments' fair value	8 091	-2 920
Change in hedged items' fair value	-9 360	6 762
Net trading income	**-1 269**	**3 841**

NOTE 9. INCOME AND EXPENSES FROM FINANCIAL INSTRUMENTS

(EUR 1,000)	1-12/2018
Interest income on	
Amortized cost investments	18,701
Total interest income arising from financial assets not measured at fair value through profit or loss	**18,701**
Finance income	**18,701**
Financial liabilities measured at amortized cost - interest expense	-5,405
Loan receivables - impairment loss	20
Finance expenses	**-5,385**
Net income and expenses from financial instruments	**13,316**

(EUR 1,000)	1-12/2017
Interest income on	
Loans and receivables	12,648
Total interest income arising from financial assets not measured at fair value through profit or loss	**12,648**
Finance income	**12,648**
Financial liabilities measured at amortised cost - interest expense	-4,745
Finance expenses	**-4,745**
Net income and expenses from financial instruments	**7,903**

NOTE 10. PERSONNEL EXPENSES

(EUR 1,000)	1-12/2018	1-12/2017
Wages and salaries	-33	-7
Personnel expenses	**-33**	**-7**

NOTE 11. OTHER OPERATING EXPENSES

EUR (1,000)	1-12/2018	1-12/2017
Other administrative expenses		
Other personnel expenses	-2	-1
Office expenses	-799	-739
ICT expenses	-515	-336
Telecommunications	-5	-3
Marketing	-6	-7
Total	**-1,327**	**-1,086**
Other operating expenses		
Other operating expenses*	-335	-383
Total	**-335**	**-383**
Other operating expenses total	**-1,662**	**-1,468**

***Audit fees**		
Statutory audit	-15	-14
Other services	-1	-25
Total	**-16**	**-39**

NOTE 12. DEPRECIATION OF INTANGIBLE ASSETS

(EUR 1,000)	1-12/2018	1-12/2017
Depreciation of intangible assets	-361	-332
Total depreciation	**-361**	**-332**
Depreciation of intangible assets	**-361**	**-332**

NOTE 13. IMPAIRMENT LOSS ON LOANS AND OTHER RECEIVABLES

Expected Credit Losses (ECL), Loans and advances and off-balance sheet	Stage 1	Stage 2	Stage 3	Total
(EUR 1,000)	12 month ECL	Lifetime ECL	Lifetime ECL	
Expected Credit Losses 1 January 2018	**664**	**174**	**9**	**847**
New assets originated or purchased	103	189	3	295
Assets derecognised or repaid (excluding write offs)	-252	-126	-9	-387
Transfers from Stage 1 to Stage 2	-19	102		83
Transfers from Stage 1 to Stage 3			1	1
Transfers from Stage 2 to Stage 1	6	-20		-15
Transfers from Stage 2 to Stage 3		-1	2	
Transfers from Stage 3 to Stage 2		3		3
Net change in ECL				20
Expected Credit Losses 31 December 2018	**502**	**320**	**6**	**827**
Change in ECL 1.1.-31.12.2018 total				**20**

NOTE 14. INCOME TAXES

(EUR 1,000)	1-12/2018	1-12/2017
Current tax	-368	-481
Tax for prior years	17	
Change in deferred tax assets	-167	-538
Change in deferred tax liabilities	-2	
Income taxes	**-520**	**-1,019**
Total income taxes	**-520**	**-1,019**
Reconciliation between tax expense in the income statement and tax expense calculated by the applicable tax rate		
Reconciliation of effective tax rate		
Accounting profit before tax	2,686	5,097
Differences between accounting and taxable profit	-847	
Taxable profit	**1,839**	**5,097**
Tax using the domestic corporation tax rate	-537	-1 019
Tax for prior years	17	
	-520	**-1 019**
Corporate income tax rate	**20 %**	**20 %**

Additional information about deferred taxes is displayed in note 19.

ASSETS

NOTE 15. CLASSIFICATION OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

31.12.2018 (EUR 1,000)	Amortized costs	Financial assets at fair value through profit or loss	Other financial liabilities	Total
Loans and advances to credit instituti-ons	44,151			44,151
Loans and advances to customers	1,852,994			1,852,994
Total assets	**1,897,144**	**0**	**0**	**1,897,144**
Liabilities to credit institutions			815,240	815,240
Derivatives		5,776		5,776
hedging derivatives		5,776		
of which fair value hedging		5,776		
Debt securities issued			1,000,243	1,000,243
Total liabilities	**0**	**5,776**	**1,815,483**	**1,821,259**

31.12.2017 (EUR 1,000)	Amortized costs	Financial assets at fair value through profit or loss	Other financial liabilities	Total
Loans and advances to credit instituti-ons	59,227			59 227
Loans and advances to customers	1,534,830			1 534 830
Total assets	**1,594,056**	**0**	**0**	**1 594 056**
Liabilities to credit institutions			528,000	528,000
Derivatives		2,315		2,315
hedging derivatives				
of which fair value hedging		2,315		
Debt securities issued			990,215	990,215
Total liabilities	**0**	**2,315**	**1,518,215**	**1,520,530**

NOTE 16. LOANS AND ADVANCES

2018 (EUR 1,000)	Not impaired (gross)	Expected credit losses (ECL)	Balance sheet value
Loans and advances to credit institutions			
Deposits*	44,151		44,151
Total	44,151		44,151

*of which Deposits to Credit Institutions belonging to the Savings Banks Amalgamation EUR 44,150 thousand.

2018 (EUR 1,000)	Not impaired (gross)	Expected credit losses (ECL)	Balance sheet value
Loans and advances to customers			
Loans	1,853,820	-826	1,852,994
Total	1,853,820	-826	1,852,994
Loans and advances total	1,897,971	-826	1,897,144

2017 (EUR 1,000)	Balance sheet value
Loans and advances to credit institutions	
Deposits**	59,227
Total	59,227

**of which Deposits to Credit Institutions belonging to the Savings Banks Amalgamation EUR 59,226 thousand.

2017 (EUR 1,000)	Balance sheet value
Loans and advances to customers	
Loans	1,534,830
Total	1,534,830
Loans and advances total	1,594,056

NOTE 17. DERIVATIVES AND HEDGE ACCOUNTING

The Sp Mortgage Bank hedges its interest rate risk against changes in fair value and applies hedge accounting on hedging relationships. Fair value hedging is applied when fixed interest rate issued covered bonds are hedged.

Changes in the fair value of derivatives in fair value hedging are recognised in the income statement under "Net trading income". In fair value hedging, also the hedged item is measured at fair value during the hedging period even if the item is otherwise measured at amortised cost. Changes in the fair value of the hedged item are recognized in the balance sheet as an adjustment to the corresponding balance sheet item and in the income statement under "Net trading income". Interests on hedging derivatives are presented as interest income and expense depending on their nature.

(EUR 1,000)	Nominal value / remaining maturity		Fair value	
31.12.2018	1 - 5 years	Total	Assets	Liabilities
Hedging derivative contracts				
Fair value hedging	1,000,000	1,000,000	5,776	
Interest rate derivatives	1,000,000	1,000,000	5,776	
Total	**1,000,000**	**1,000,000**	**5,776**	
Derivatives total			**5,776**	**0**

(EUR 1,000)	Nominal value / remaining maturity		Fair value	
31.12.2017	1 - 5 years	Total	Assets	Liabilities
Hedging derivative contracts				
Fair value hedging	1,000,000	1,000,000		2,315
Interest rate derivatives	1,000,000	1,000,000		2,315
Total	**1,000,000**	**1,000,000**	**0**	**2,315**
Derivatives total			**0**	**2,315**

NOTE 18. INTANGIBLE ASSETS

(EUR 1,000)	31.12.2018	31.12.2017
Intangible assets	390	748
Intangible assets under development		4
Total	**390**	**752**

Intagible assets formed a significant part of information systems acquired from external operators.

2018 (EUR 1,000) Changes in intangible assets	Intangible assets	Intangible assets under development	Total
Acquisition cost 1 January	748	4	752
Transfers between items	4	-4	
Acquisition cost 31 December	752	0	752
Accumulated depreciation and impairments 1 January			
Depreciation for the financial year	-361		-361
Accumulated depreciation and impairments 31 December	-361		-361
Carrying amount 31 December	**390**	**0**	**390**

2017 (EUR 1,000) Changes in intangible assets	Intangible assets	Intangible assets under development	Total
Acquisition cost 1 January	0	1,080	1,080
Increases		5	5
Transfers between items	1,080	-1,080	
Acquisition cost 31 December	1,080	4	1,084
Accumulated depreciation and impairments 1 January	0	0	0
Depreciation for the financial year	-332		-332
Accumulated depreciation and impairments 31 December	-332	0	-332
Carrying amount 31 December	**748**	**4**	**752**

NOTE 19. DEFERRED TAXES

(EUR 1,000)	31.12.2018	31.12.2017
Income tax receivables	96	
Tax assets	**96**	**0**
Income tax liability		481
Tax liability	**0**	**481**

2017 (EUR 1,000)	1.1.2017	Change recognised in profit or loss	31.12.2017
Deferred tax assets			
Cash flow hedges	538	-538	0
Total	538	-538	0

NOTE 20. OTHER ASSETS

(EUR 1,000)	31.12.2018	31.12.2017
Accrued income and prepaid expenses		
Interest	2,307	1,853
Other accrued income and prepaid expenses	767	1,411
Other assets total	**3,074**	**3,264**

LIABILITIES AND EQUITY

NOTE 21. LIABILITIES TO CREDIT INSTITUTIONS

(EUR 1,000)	31.12.2018	31.12.2017
Other than those repayable on demand*	815,240	528,000
Total liabilities to credit institutions	**815,240**	**528,000**

*of which Liabilities to Credit Institutions belonging to the Savings Banks Amalgamation EUR 813,000 (528,000) thousand.

NOTE 22. DEBT SECURITIES ISSUED

	31.12.2018		31.12.2017	
(EUR 1,000)	Nominal value	Carrying amount	Nominal value	Carrying amount
Measured at amortised cost				
Covered bonds	1,000,000	997,099	1,000,000	996,430
Fair value hedging on covered bonds		3,145		-6,215
Total debt securities issued	**1,000,000**	**1,000,243**	**1,000,000**	**990,215**

Sp Mortgage Bank Plc's Covered bonds issued

(EUR 1,000)	Nominal value	Carrying amount	Maturity	Interest base	Coupon	Maturity date
Sp Mortgage Bank 2016	500,000	499,086	5 years	Fixed	0,10 %	29.11.21
Sp Mortgage Bank 2017	500,000	498,013	5 years	Fixed	0,125 %	24.10.22
Total	**1,000,000**	**997,099**				

Sp Mortgage Bank has not had any delays or defaults in respect of its issued debt securities.

NOTE 23. OTHER LIABILITIES

(EUR 1,000)	31.12.2018	31.12.2017
Other liabilities		
Payment transfer liabilities	63	47
Other liabilities		52
Total other liabilities	**63**	**98**
Accrued expenses		
Interest payable	1,484	837
Interest advances received	4	3
Other accrued expenses	1,263	1,428
Total accured expenses	**2,750**	**2,268**
Total provisions and other liabilities	**2,813**	**2,366**

NOTE 24. CAPITAL AND RESERVES

(EUR 1,000)	31.12.2018	31.12.2017
Share capital	56,601	48,597
Reserves		
Reserve for invested non-restricted equity	28,258	24,262
Retained earnings		
Profit (loss) for previous financial years	1,159	-2,241
Profit (loss) for the period	2,167	4,077
Total capital and reserves	**88,184**	**74,695**

Share capital
This item includes the paid share capital. If share capital is wholly or partly not entered in trade register, the unregistered amount must be presented in the balance sheet separately as a sub-item of this item.

Reserve for invested non-restricted equity
Reserve for invested non-restricted equity includes the portion of subscription price which is not recognised in share capital and, according to the Accounting Act, is not recognised in liabilities, as well as other equity investments which are not recognised in other reserves. Furthermore, the reserve includes the amount by which share capital is reduced and which is not used to cover confirmed loss nor is distributed to shareholders.

Retained earnings
This item includes the profit for the period as indicated by the income statement, as well as profit for prior periods to the extent that it has not been transferred to other equity items or distributed to shareholders.

OTHER NOTES

NOTE 25. COLLATERALS

(EUR 1,000)	31.12.2018	31.12.2017
Collateral given		
Given on behalf of Group's own liabilities and commitments		
Loans	1,782,148	1,485,159
Total collateral given	**1,782,148**	**1,485,159**
Collateral received		
Real estate collateral	1,853,574	1,534,549
Other	246	172
Total collateral received	**1,853,820**	**1,534,721**

NOTE 26. OFF BALANCE-SHEET COMMITMENTS

(EUR 1,000)	31.12.2018	31.12.2017
Loan commitments	13,473	16,427
Money Market Deposits*	60,000	40,000
Total off balance-sheet commitments	**73,473**	**56,427**

* Consists of loan agreements with Central Bank of Savings Banks Finland Plc, where the trade date is after the end of the reporting period.

NOTE 27. OFFSETTING OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The derivative contracts of the Sp Mortgage Bank are subject to either ISDA Master Agreement or the Master Agreement of the Finance Finland. Under these agreements, derivative payments may be offset by payment transaction on each payment date as well as in the event of counterparty default or bankruptcy. In addition, it is possible to agree on collateral on a counterparty-specific basis in the terms and conditions of the agreement. These derivatives are presented in the statement of financial position on a gross basis.

(EUR 1,000) 31.12.2018				Amounts which are not offset but are subject to enforceable master netting arrangements or similar agreements			
	Recognised financial assets, gross	Recognised financial liabilities offset in balance sheet, gross	Carrying amount in balance sheet, net	Carrying amount of Financial instruments in balance sheet, net	Carrying amount in balance sheet of financial instruments recieved as collateral	Cash held as collateral	Net amount
Assets							
Derivate contracts				5,776			5,776
Total	**0**	**0**	**0**	**5,776**	**0**	**0**	**5,776**
Liabilities							
Derivate contracts						2,240	2,240
Total	**0**	**0**	**0**	**0**	**0**	**2,240**	**2,240**

(EUR 1,000) 31.12.2017				Amounts which are not offset but are subject to enforceable master netting arrangements or similar agreements			
	Recognised financial assets, gross	Recognised financial liabilities offset in balance sheet, gross	Carrying amount in balance sheet, net	Carrying amount of Financial instruments in balance sheet, net	Carrying amount in balance sheet of financial instruments recieved as collateral	Cash held as collateral	Net amount
Liabilities							
Derivate contracts				2,315			2,315
Total	**0**	**0**	**0**	**2,315**	**0**	**0**	**2,315**

NOTE 28. FAIR VALUES BY VALUATION TECHNIQUE

Fair value measurement

Financial instruments are presented in the Sp Mortgage Bank's balance sheet at amortised cost and in fair value in derivatives. The classification of financial assets and liabilities by valuation technique as well as the criteria for measurement methods and for determining fair value are described in the accounting policies (Note 2).

The fair values of financial instruments are primarily determined using quotations on a publicly traded market or market prices received from third parties. If quoted market prices are not available, balance sheet items are mainly measured by discounting future cash flows using market interest rates at the balance sheet date. In respect of cash and deposits payable on demand, the nominal value is considered equivalent to the fair value.

Sp Mortgage Bank does not have assets measured at fair value on a non-recurring basis.

Fair value hierarchy

Level 1 consists of financial assets, for which the value is determined based on quotes on a liquid market. Market is considered liquid if the prices are available easily and regularly enough. Level 1 includes securities which are quoted on public.

Level 2 includes financial assets for which there is no quotation directly available on an active market and whose fair value is estimated using valuation techniques or models. These are based on assumptions which are supported by verifiable market information such as the listed interest rates or prices of similar instruments. This group includes e.g. loans to customers as well as commercial papers and certificates of deposit.

Level 3 includes financial assets whose fair value cannot be derived from public market quotations or through valuation techniques or models which are based on observable market data. Level 3 comprises unquoted equity instruments, structured investments and other securities for which there is currently no binding market quotation available. The fair value at level 3 is often based on price information received from a third party. Sp Mortgage Bank does not have financial assets for which the fair value has been determined according to level 3.

Transfers between levels

Transfers between the levels of the fair value hierarchy are considered to take place on the date when an event causes such a transfer or when circumstances change.

In the financial reporting period January to December 2018, there were no transfers between levels 1,2 and 3.

Financial assets 31.12.2018 (EUR 1,000)	Carrying amount	Fair value by hierarchy level			Fair value
		Level 1	Level 2	Level 3	Total
Measured at fair value					
Derivatives	5,776		5,776		**5,776**
Measured at amortised cost					
Loans and advances	1,897,144		2,345,433		**2,345,433**
Total financial assets	**1,902,920**	**0**	**2,351,209**	**0**	**2,351,209**

Financial liabilities 31.12.2018 (EUR 1,000)	Carrying amount	Fair value by hierarchy level			Fair value
		Level 1	Level 2	Level 3	Total
Measured at amortised cost					
Liabilities to credit institutions	815,240		817,936		**817,936**
Debt securities issued*	1,000,243	997,099			**997,099**
Total financial liabilities	**1,815,483**	**997,099**	**817,936**		**1,815,035**

* Carrying amount includes the adjustment from the hedging EUR 3.1 million.

Financial assets 31.12.2017 (1 000 euroa)	Carrying amount	Fair value by hierarchy level			Fair value
		Level 1	Level 2	Level 3	Total
Measured at amortised cost					
Loans and advances	1,594,056		1,991,940		**1,991,940**
Total financial assets	**1,594,056**	**0**	**1,991,940**	**0**	**1,991,940**

Financial liabilities 31.12.2017 (1 000 euroa)	Carrying amount	Fair value by hierarchy level			Fair value
		Level 1	Level 2	Level 3	Total
Measured at amortised cost					
Liabilities to credit institutions	2,289		2,289		**2,289**
Measured at amortised cost					
Liabilities to credit institutions	528,000		531,018		**531,018**
Debt securities issued*	990,215	1,001,550			**1,001,550**
Total financial liabilities	**1,520,504**	**1,001,550**	**533,307**	**0**	**1,534,857**

* Carrying amount includes the adjustment from the hedging EUR -6.2 million.

NOTE 29. RELATED PARTIES

The Board of Directors of Sp Mortgage Bank has defined the related parties of the Sp Mortgage Bank. The related parties of the Sp Mortgage Bank's comprise key management personnel as well as their close family members. In addition, related parties comprise entities which the key management personnel and/or their close family members control. The key management personnel of the Sp Mortgage Bank comprise the members of the Board of Directors, the Managing Director as well as the Executive Board of Sp Mortgage Bank.

Sp Mortgage Bank does not have own personnel, all the necessary functions and support services are bought from the companies in the Savings Banks Amalgamation or from companies offering services to the Savings Banks Amalgamation.

Key management personnel compensation * (EUR 1,000)	2018	2017
Short-term employee benefits	24	18
Total	**24**	**18**

*** Key personnel compensation**

2018	Salary and remuneration
Seppälä Risto	2
Hakala Jussi	7
Syvänen Hannu	7
Huupponen Juhani	10
Total	**24**

2017	
Seppälä Risto	6
Hakala Jussi	5
Huupponen Juhani	7
Total	**3**

NOTE 30. SUBSEQUENT EVENTS

The Board of Directors of Sp Mortgage Bank is not aware of any other factors, which would materially influence the financial position of Sp Mortgage Bank after the completion of the financial statements.

CAPITAL ADEQUACY INFORMATION

NOTE 31. PILLAR III DISCLOSURES

Sp Mortgage Bank is part of the Savings Banks Amalgamation and the Savings Banks Group. Sp Mortgage Bank's capital adequacy information is included in the information concerning the capital adequacy of the Savings Banks Amalgamation, presented in the consolidated financial statements of the Savings Banks Group. The Financial Supervisory Authority has granted a permission not to deduct internal holdings of credit institutions included in the Amalgamation from own funds instruments when calculating own funds at the individual institution level and sub-consolidation group level. In addition, the Financial Supervisory Authority has granted a permission to apply a 0 per cent risk weight to internal credit institution liabilities included within the scope of the Amalgamation's joint and several liability. These permissions are based on the European Union Capital Requirements Regulation (EU 575/2013) and the Act on the Amalgamation of Deposit Banks (599/2010). A copy of the financial statement of the Savings Banks Group is available online at *www.saastopankki.fi/saastopankkiryhma* or at the Savings Banks Union Coop offices at Teollisuuskatu 33, 00510 Helsinki, Finland.

Sp Mortgage Bank Plc

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This document is an English translation of the Finnish auditor's report. Only the Finnish version of the report is legally binding.

Auditor's Report

To the Annual General Meeting of Sp Mortgage Bank Plc

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Sp Mortgage Bank Plc (business identity code 2685273-8) for the year ended 31 December, 2018. The financial statements comprise the balance sheet, income statement, statement of comprehensive income, statement of changes in equity, statement of cash flows and notes, including a summary of significant accounting policies.

In our opinion the financial statements give a true and fair view of the bank's financial position, financial performance and cash flows in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

Our opinion is consistent with the additional report submitted to the Board of Directors.

Basis for Opinion

We conducted our audit in accordance with good auditing practice in Finland. Our responsibilities under good auditing practice 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 applicable in Finland and are relevant to our audit, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

In our best knowledge and understanding, the non-audit services that we have provided to the company in compliance with laws and regulations applicable in Finland regarding these services, and we have not provided any prohibited non-audit services referred to in Article 5(1) of regulation (EU) 537/2014. The non-audit services that we have provided have been disclosed in note 11 to the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Materiality

The scope of our audit was influenced by our application of materiality. The materiality is determined based on our professional judgement and is used to determine the nature, timing and extent of our audit procedures and to evaluate the effect of identified misstatements on the financial statements as a whole. The level of materiality we set is based on our assessment of the magnitude of misstatements that, individually or in aggregate, could reasonably be expected to have influence on the economic decisions of the users of the financial statements. We have also taken into account misstatements and/or possible misstatements that in our opinion are material for qualitative reasons for the users of the financial statements.

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 of the current period. 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. The significant risks of material misstatement referred to in the EU Regulation No 537/2014 point (c) of Article 10(2) are included in the description of key audit matters below.

We have also addressed the risk of management override of internal controls. This includes consideration of whether there was evidence of management bias that represented a risk of material misstatement due to fraud.

THE KEY AUDIT MATTER	HOW THE MATTER WAS ADDRESSED IN THE AUDIT

Valuation of receivables (loans and receivables from customers);
Notes to financial statements 2, 3, 4 and 13

— Sp Mortgage Bank adopted the IFRS 9 *Financial instruments* –standard on 1 January 2018. The adoption resulted in a shift from calculating impairments on an individual and collective basis to the expected credit loss models set out in IFRS 9. — The Calculation of expected credit losses is based on the valuation models used by the bank. The calculation of expected credit losses involves assumptions, estimates and management judgements for example in respect to the probability and amount of the expected credit losses, the realizable value of the collateral as well as determining significant increases in credit risk. — Due to the significance of the carrying amount involved, adoption of the IFRS 9 –standard, complexity of the accounting methods and management judgement involved, receivables from customers are addressed as a key audit matter.	— We assessed principles and controls over recognition and monitoring of loan receivables. Our audit procedures included testing of controls regarding determination and recording of expected credit losses on loans. — Our audit procedures included substantive procedures related to the technical appropriateness of the computations, such as recalculations. — Furthermore, we assessed the appropriateness of the note disclosures made in relation to receivables and impairment losses.

Valuation of derivative instruments;
Notes to financial statements 2, 8 and 17

- Sp Mortgage Bank hedges its interest rate risk from changes in fair value and applies hedge accounting to hedging relationships. For hedging relationships under general hedge accounting, Sp Mortgage Bank has adopted IFRS 9.
- At year-end the nominal value of derivatives is significant, amounting to € 1 billion. As derivatives are measured at fair value in preparing financial statements, this may result in significant volatility in the income statement.
- Fair values for the derivatives used by the company are not directly observable in an active market, instead the company determines fair values using applicable fair value models.

- We assessed the appropriateness of the measurement principles applied and the compliance with the applicable financial reporting standards.
- We also considered the accuracy of the fair values determined.
- Furthermore, we assessed the appropriateness of the note disclosures made in relation to derivatives.

Responsibilities of the Board of Directors and the Managing Director for the Financial Statements

The Board of Directors and the Managing Director are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, and that financial statements comply with statutory requirements. The Board of Directors and the Managing Director are also responsible for such internal control as they determine 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, the Board of Directors and the Managing Director are responsible for assessing the bank's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting. The financial statements are prepared using the going concern basis of accounting unless there is an intention to liquidate the company or cease operations, or there is 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 good auditing practice 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 the financial statements.

As part of an audit in accordance with good auditing practice, 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 the Board of Directors' and the Managing Director'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 so that the financial statements give a true and fair view.

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.

Other Reporting Requirements

Information on our audit engagement

We were first appointed as auditors by the Annual General Meeting on 16 of April 2015, and our appointment represents a total period of uninterrupted engagement of 4 years.

Other Information

The Board of Directors and the Managing Director are responsible for the other information. The other information comprises the report of the Board of Directors.

Our opinion on the financial statements does not cover the other information.

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. Our responsibility also includes considering whether the report of the Board of Directors has been prepared in accordance with the applicable laws and regulations.

In our opinion, the information in the report of the Board of Directors is consistent with the information in the financial statements and the report of the Board of Directors has been prepared in accordance with the applicable laws and regulations.

If, based on the work we have performed, we conclude that there is a material misstatement of the report of the Board of Directors, we are required to report that fact. We have nothing to report in this regard.

Helsinki, 5 February, 2019

KPMG OY AB

PETRI KETTUNEN
Authorised Public Accountant, KHT