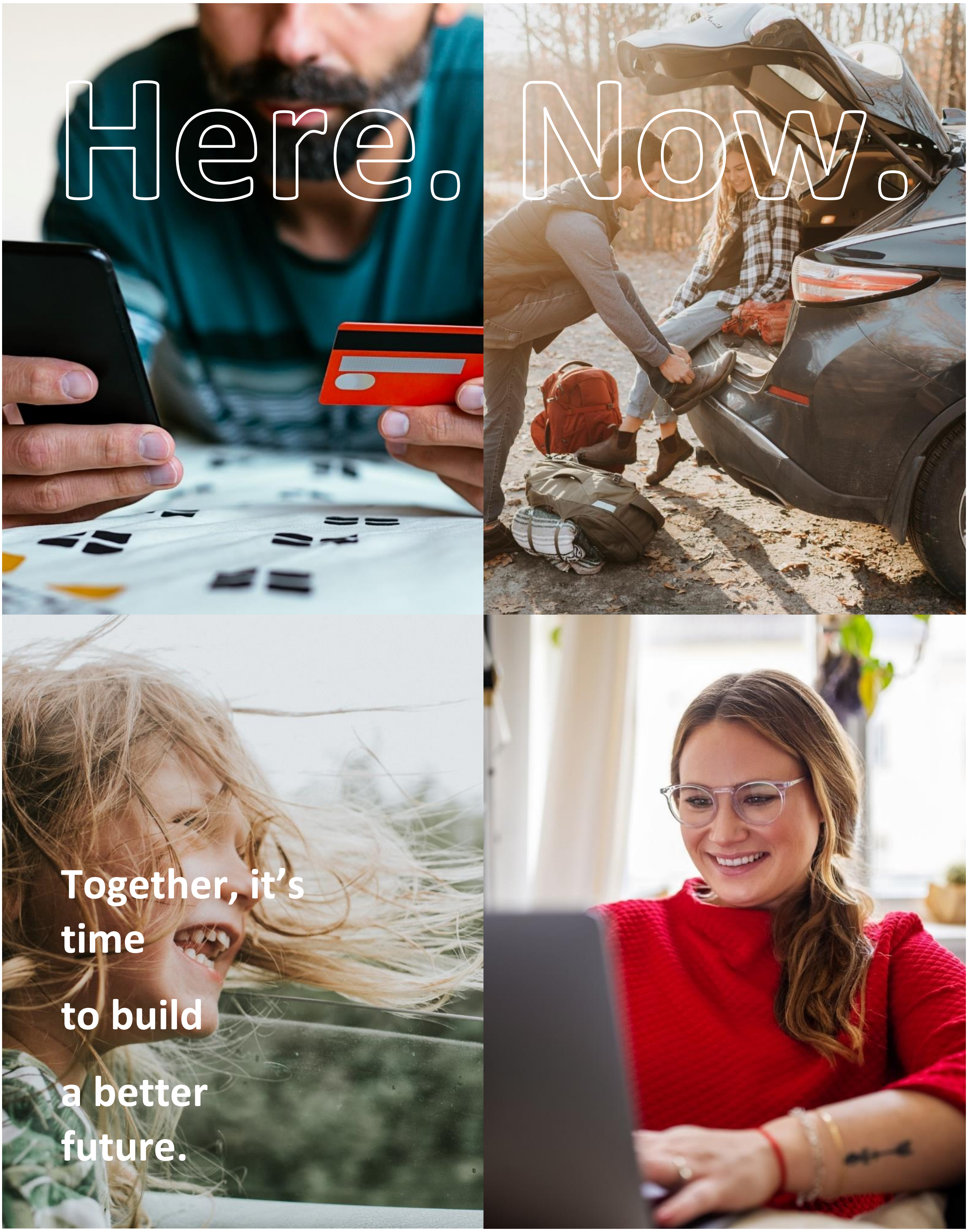


Pillar 3 Report **2021**

Santander Consumer Bank

Highlights in 2021

Risk Weighted Assets (MNOK)

127 890

Total Capital Ratio (%)

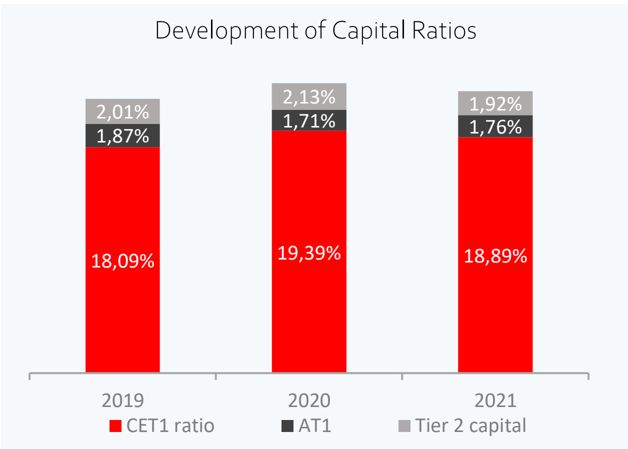
22.57

Common Equity Tier 1 Capital Ratio (%)

18.89

Leverage Ratio (%)

13.52



Pillar 1 Capital Reporting Methodologies

Credit Risk	Market Risk	Operational Risk
Standardized Approach	Standardized Approach	Basic Indicator Approach
Foundation-IRB	Internal Models	Standardized Approach
Advanced-IRB		Advanced Measurement

Indicate those methods applied by Santander Consumer Bank

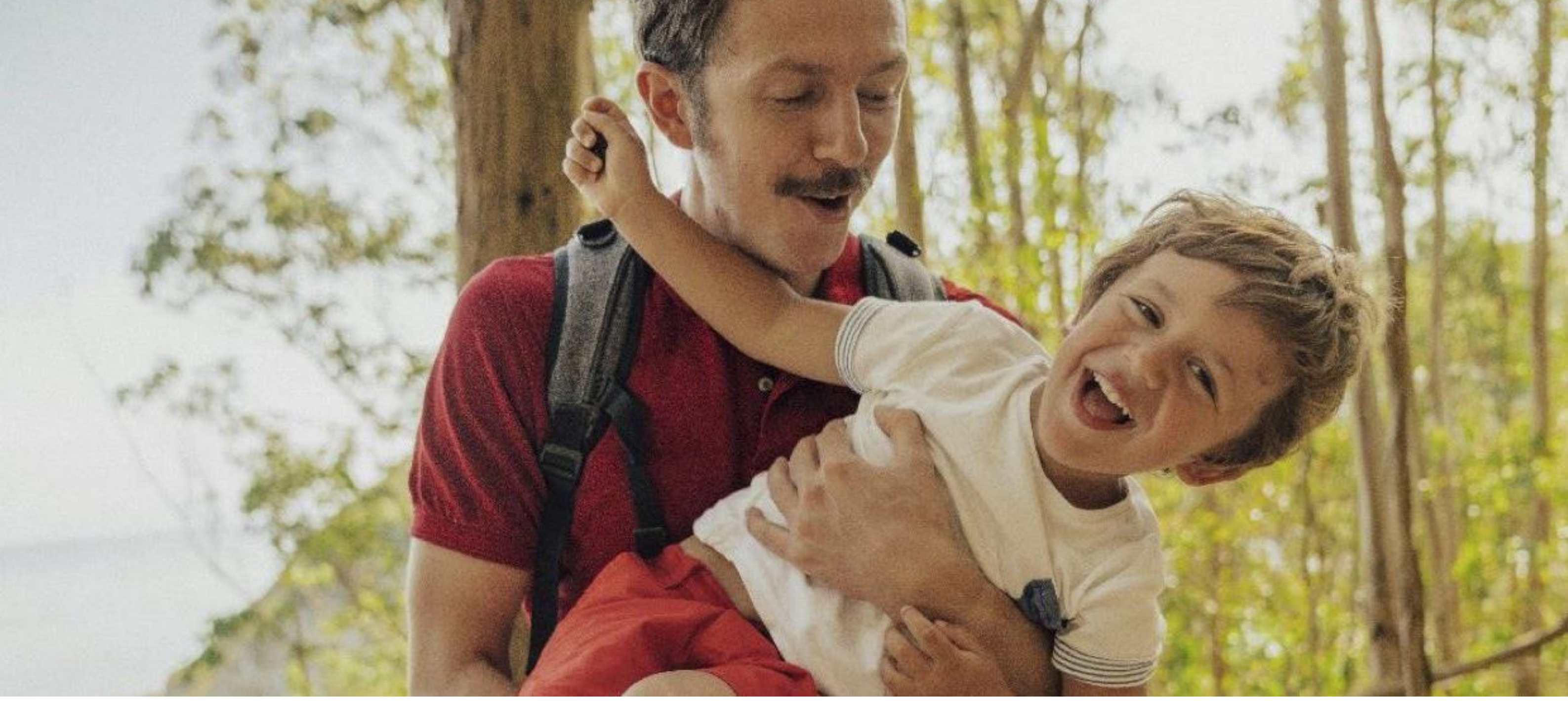
Contents

1 Purpose and Scope of Disclosure

The purpose of this report ("the Pillar 3 report") is to provide information to the market in order to assess the risk management, risk measurement and capital adequacy of Santander Consumer Bank AS. When including its subsidiary, Santander Consumer Bank AS will be referred to in this document as "SCB", "the Bank" or "SCB Group". When excluding its subsidiary, reference will be made to "SCB AS". SCB is a commercial bank 100% owned by Santander Consumer Finance S.A. in Spain, which is again owned by Banco Santander. This Pillar 3 report covers SCB's operations in Norway, its branches in Sweden and Denmark and its subsidiary in Finland, Santander Consumer Finance Oy (SCF Oy).

The report meets the information requirements in accordance with the "Regulation on capital requirements and national adaptation of CRR/CRD IV", the Norwegian Finanstilsynet (Norwegian FSA) Circular 5/2018 in *"Offentliggjøring av finansiell informasjon – kommisjonsforordninger og anbefalinger fra EBA"* and the guidelines issued by the European Banking Authority (EBA) in *"Guidelines on disclosure requirements under Part Eight of Regulation (EU) No 575/2013 (EBA-GL-2016-11)".* In addition, SCB publishes an appendix to the report (see Pillar 3 Appendix) displaying further information on capital adequacy position, terms of capital instruments, leverage ratio calculations, applicable countercyclical buffer calculations and own funds disclosure. This report and the appendix are prepared in accordance with CRR/CRD IV until the new EU Banking Package is in force (to be implemented from 1 June 2022 in Norway). The Pillar 3 report is currently updated annually.

For information on SCB's remuneration policy see SCB's 2021 Annual Report under "*Note 30 – Remuneration*".



2 Santander Consumer Bank AS

SCB is a Nordic commercial bank, operating in Norway, Sweden, Denmark, and Finland, with the head office located at Lysaker in Norway. As of 31 December 2021, the Bank had 1154 employees (excluding temporary hired employees) of which 547 worked in Norway, 228 in Sweden, 198 in Denmark and 151 in Finland.

The Bank is a leading consumer finance provider across the Nordic region offering car financing, consumer loans, credit cards and sales financing. The Bank also offers customer deposits in Norway, Sweden, and Denmark. Note that, in this document, car financing is referred to as "secured financing" due to collateral in the vehicle while consumer loans, credit card and sales finance are referred to as "unsecured financing" as these loans are without collateral. In addition, the Bank acts as an ancillary insurance mediator for insurance companies in the respective jurisdictions (CNP Santander Insurance Life DAC and CNP Santander Insurance Europe).

The Bank is governed by Norwegian law and is supervised by the Norwegian Financial Supervisory Authority (FSA) and the European Central Bank (ECB) as a Joint Supervisory Team (JST).

SCB's overarching commitment is to do business in a responsible and sustainable way. This is reinforced by the corporate purpose to help people and businesses prosper and underpinned by a values platform that ensures everything the Bank does is simple, personal, and fair. The Bank has a clearly defined strategic ambition of being the leading Nordic consumer finance platform. This means striving to meet all customer and partner needs in a seamless and collaborative manner.

Despite the challenges faced in 2021, the Bank was able to take significant strides towards executing on its corporate strategy and thereby future proofing its business. Reference is made to the 2021 Annual Report.

As of 31 December 2021, SCB possessed a strong capital adequacy position illustrated by a Common Equity Tier 1 (CET1) capital ratio of 18.89%, which represents a margin on 6.0%-points above the regulatory requirements (including Pillar 2 guidance). For SCB AS, the CET1-ratio at year-end was at 18.34%. The CET1 ratio is reduced compared to 31 December 2020, due to dividend payment of 1.7 BNOK in Q4 2021, and of 2 BNOK in Q1 2022. The dividend distribution in Q1 2022 represent almost 100% of profit after tax for SCB AS for the financial year 2021.

The Group has, until December 2021, published capital ratios both on a transitional rule basis (allowing for a reversal of 50% of IFRS 9 capital impact in 2021) and on a fully phased-in basis. Transitional capital ratios have been the official ratios required to meet the minimum capital requirements set forth by regulatory authorities and are the ones used in this report. From Q1 2022 and onwards, the Group will only report on a fully phased-in basis and no longer consider transitional rules.

The Bank is an Advanced IRB (A-IRB) bank with approximately one third of its portfolios currently under this approach. The remaining portfolios are under the Standardized Approach, but they are planned to be rolled out under the A-IRB approach in the coming years. The European Banking Authority's (EBA) introduction of new default definition (NDD) for capital calculation purposes was implemented for IRB portfolios in November 2020 and for the remaining portfolios in January 2021. In December 2021 the NDD was also adapted for the calculations of loan loss reserves under the IFRS9 framework. The NDD triggers the need to recalibrate the Bank's IRB models and updated IRB models was thus submitted to the Norwegian FSA for approval in July 2021.

2.1 Recent Developments

Covid-19 Pandemic

While 2020 was largely influenced by the COVID-19 pandemic, 2021 had prospects of being a year of recovery with the roll-out of vaccines and relaxed containment measures. However, as the Nordic economies gradually recovered during the year, the threats of new variants of the virus, surge in diagnosed cases and resistance to vaccinations raised questions about the speed and strength of an economic recovery in near future. The Bank's business has been gradually returning to normal levels during the year 2021, while most contingent measures were lifted. However, returning to "normal" has been characterized by the inflation being on the rise, driven by higher energy and gas prices.

During 2021, the Bank's Business Continuity Management Team has continued to support top management in the monitoring of the COVID-19 situation and have played a key advising role looking ahead. In accordance with the Bank's internal policies, the Bank's internal status has been on "alert" during different times of the year with continuous monitoring and assessing the development of the situation, taking necessary measures/adjustments to keep employees safe and protect the continuity of the Bank's business. Among others, during the year, the Bank activated, deactivated, and reactivated local task forces operating per location and convened different committees for handling the evolution and changes related to the pandemic and authorities' contingency measures.

Considering the Bank's experiences during the nearly two years of facing the pandemic, and the Bank and the Nordic economies gradually returning to normal, the Bank considers that it is well positioned to face the uncertainties and challenges going forward. The Bank, nevertheless, continues to monitor the situation and recovery.

Geopolitical instability

At the time of completing this Pillar 3 report as well as the Pillar 2 report (ICAAP/ILAAP) and submitting to relevant stakeholders for review and approval, the news of Russian invasion and war on Ukraine became evident. Following the aggression from Russia, the international community have imposed strict sanctions heavily impacting Russia's economy and markets.

The full effect of the war is still uncertaint and it is difficult to predict the long-term impact for the Bank. It is however evident that the conflict has caused a global turmoil. The Bank's exposure towards Russia and Ukraine is limited, however, the sanctions towards Russia can lead to increased compliance costs. The situation affects energy outlook and prices, and in combination with other macroeconomic changes, an increased credit risk towards households and companies. The implication so far is limited for the Bank, but the long-term ripple effects are yet to materialize.

In addition, the war has led to a significant increase in the cyber and technology risk landscape, which already has risen due to covid/home office and expansion of the IT perimeter of the Bank. The Bank has increased its measures against cyber- and technology risks and follows this situation closely. Furthermore, the Bank has operations in Sweden and Finland, countries currently not members of NATO, where the preparedness and uncertainty are increasing.

As a result of the war on Ukraine, the macroeconomic environment faces an intensified uncertainty. European banks with Russian exposures that default could potentially, and worst-case, lead to a new financial crisis. In addition, increased inflation, higher interest rates and currency fluctuations could impact the market and consumers credit worthiness. Moreover, businesses with interests in Russia could be impacted by the sanctions, causing additional ripple effects into the European markets.

A possible outcome of the war, which has already started to materialize, is the shortage of raw materials and components delivered from Russia or Ukraine. Specifically, the Bank acknowledge that there may be a shortage of important components or parts to the Auto industry going forward, which can impact the sales of new cars, which again can affect the Bank's Auto business. As the Bank's strategy is linked to the financing of Auto portfolios, the Bank considers that this can affect its performance going forward and monitors this closely.

Lastly, the duration and intensity of the war will be the key factor for how macro and local risks will materialize. The Bank monitors the situation closely and has established several work-streams and groups to assess the impact on the Bank's business going forward and proposing remediating actions to safeguard the Bank's operations.

Climate and Sustainability
Climate and sustainability have received increased attention in the market during the last years. The 2021 United Nations Climate Change Conference (COP26) towards the end of 2021, reinforced the trajectory and significance of climate change and more broadly, sustainability. Banks must respond and continue to play a significant role in this journey and there exists significant opportunities to build new propositions that are underpinned by sustainability principles. To meet these opportunities, it is imperative that the Bank maintains the required culture, skills, governance, and business practices to meet stakeholder's expectations. In addition, the need to secure robust compliance, conduct and internal control processes has never been greater and has been a key strategic priority of the Santander Group. The Bank has established sustainability policies which defines the Bank's sustainability approach, focused on creating long-term value and managing social and environmental risks, such as climate change, resource scarcity and social rights.

During 2021, the Bank launched its inaugural Nordic Responsible Banking agenda, which outlines an ambition to deliver a sustainable end-to-end value chain supporting Banco Santander's Net Zero by 2050 ambition. The value chain ambition takes into consideration all stakeholder groups, targeting a broad green funding offering to support the financing of green (and other sustainability-linked) commercial propositions. Furthermore, the reduction of internally generated emissions and introduction of sustainability requirements on partners and vendors are important long-term objectives of the agenda. To further analyse the risks and opportunities arising from matters related to sustainability, including climate risk, the Bank's Responsible Banking team is leading a project to develop a Nordic sustainability report that will be developed in line with leading standards – the Task Force on Climate-Related Financial Disclosures (TCFD) and the Global Reporting Initiative (GRI). Consequently, the Bank considers that it is prepared for the increased reporting requirements and expectations from stakeholders and regulators.

For more information, please refer to the Santander Consumer Bank 2021 Annual Report page 26 to 30.

3 Risk Management and Control

3.1 Role of the Board of Directors

In accordance with the Norwegian Financial Institutions Act section 13-6, the Board of Directors (or the "Board") shall monitor and manage SCB's overall risk and regularly assess whether management and control arrangements are tailored to the risk level and scale of SCB's activities. The Board of Directors has established a risk committee (the "Board Risk Committee" or "BRC") consisting of three members chosen by and among Board members, currently two of the Board's external directors and one internal director (non-executive) and carrying out the tasks set forth in section 13-6 of the Norwegian Financial Institutions Act and regulations connected thereto. Further information on the BoD sub-committees is outlined in section 3.4.

The Board of Directors instructs senior management to develop and maintain an appropriate, systematic, and consistently applied process to determine risk levels, provisions for loan losses and management aligned with the corporate guidelines. More information on SCB Senior Management team can be found in section 3.4.

The Board of Directors adopts and participates in the reassessment of credit authorizations. It also receives relevant reports in the risk area and instigates relevant action to reduce any undesired rise in risk level. It is established in the Nordic Retail Credit Policy that BoD shall approve parameter and management limits, as well as any proposed remedial action when facing breach of limits. All breaches of management limits must be reported to the BoD regardless of whether the breach is cured.

3.2 Risk Management and Control

An Advanced Risk Management Programme (ARM) and a forward-looking approach combined with a series of interrelated tools and processes in the Bank's strategic planning (risk appetite, risk identification and assessment, annual planning, and budgeting, etc.) provide a holistic control framework across the Bank.

The Bank continuously focus on developing its approach to risk management and initiated an ARM programme in 2019, which is mainly aimed at helping the Bank shift towards advanced risk management, laying down the foundations to have the best enterprise-wide risk management model in the financial industry. Through the annual roll-out of ARM, initiatives are being consolidated, including all strategic projects related to data and reporting, evolving the risk appetite, reinforcing the control environment, strengthening the governance of the risk function, and developing new initiatives such as cyber or model risk management. The program is also helping to reinforce the risk culture which is one of the Bank's hallmarks.

ARM is a holistic risk management program with the following characteristics:

1. It aims to consolidate the Operating Risk model with a strong connection to the Bank's business strategy.
   It is integrated into the daily narrative of the management, as part of the risk culture consolidation process.
   It is a structured tracking system with a quarterly follow-up to check on progress. The progress is presented to the Board and Executive Committee.
2. Availability of an online portal to record achievements and the evidence that support them.

Lines of Defence Framework
SCB adopts the three lines of defence mechanism for management and control of risk:

- First line: Comprises all business units and support functions that originate risks. It is responsible for establishing an appropriate environment for the management of all risks associated with business, for proposing appetite and limit levels, and for implementing the mechanisms to manage the risks and maintain them within risk appetite limits.
- Second Line: The Risk and Compliance & Conduct functions from the second line of defence provide independent oversight and challenge to risk management decisions from the first line. The second line of defence vouches for effective control of the risks and ensures they are managed according to the Bank's risk appetite, strengthening the risk culture across the Bank
- Third Line: Internal audit, as the last layer of control in the Bank, regularly assesses the quality and effectiveness of internal controls, risk management, governance, and systems, helping to safeguard the Bank's value, solvency, and reputation.

There is a sufficient degree of segregation between the risk control function, the compliance function, and the internal audit function, to ensure that their functions are performed and that they have access to the BoD and/or its committees through their heads.

Risk Identification and Assessment
Identifying and evaluating all risks is the first step to controlling and managing risks. The Risk Map covers the main risk categories in which SCB has its most significant exposures, current and/or potential.

The key risk types identified in the risk map are:
- Credit Risk: risk of financial loss arising from the default or credit quality deterioration of a customer or other third party, to which SCB has provided credit or for which it has assumed a contractual obligation.
- Liquidity Risk: risk that SCB does not have enough liquid resources to meet its obligations when they fall due.
- Structural Risk: the risk arising from the management of different balance sheet items (i.e., interest rate risk or currency risk).
- Capital Risk: the risk of the SCB not having an adequate amount or quality of capital to meet its internal business objectives, regulatory requirements, or market expectations.
- Operational Risk: the risk of loss resulting from inadequate or failed internal processes, people, and systems or from external events.
- Reputational risk: risk of losses caused by events that can worsen the public perception of the bank.
- Model Risk: the risk of losses arising from inaccurate predictions, causing a bank to make sub-optimal decisions, or from a model being used inappropriately.
- Strategic Risk: the risk of loss or damage arising from strategic decisions or their poor implementation, or from an inability to adapt to external developments.
- ESG – Climate Risk: is considered under the two primary types of clmate-change related risks: physical and transitional, both with potential to result in financial and non-financial impacts for the Bank.

Apart from the risks identified in the risk framework and classified in the risk map, the Risk Identification and Assessment process (RIA) also aims to identify and assess all the risks to which the bank is exposed to or could be exposed to in the future. The goal is to define SCB's risk through a quantitative and qualitative evaluation of the relevant risks composed of:

- Risk performance: assesses the current risk exposure and performance through a set of dimensions, metrics, and thresholds.
- Control environment: evaluate the level of compliance of the SCB's risk management target operating model, identifying possible gaps and weaknesses.
- Top risks: is a process carried out to allow the early identification of potential threats to the profitability, solvency, or strategic objectives of the entity, promoting an effective risk management and mitigation. Top Risks have a three-year horizon, and two sorts of events are considered, depending on their estimated likelihood and/or severity: plausible and tail risk events.

The exercise is conducted semi-annually, with the involvement of 1st, 2nd, and 3rd lines of defence, and with the purpose of monitoring the Bank's risk profile.

Material risks identified in the RIA are incorporated in the Risk Appetite Statement ("RAS").

Risk Appetite

Risk appetite is the maximum level and type of risk that SCB is willing to assume, within its risk capacity, to achieve its strategic objectives and the development of its business plan.

SCB aims to maintain a medium-low risk profile that is predictable. This profile is achieved by means of earnings stability (low P&L volatility), maintaining robust capital and liquidity under both normal and stressed conditions, limiting the impact in earnings and capital base due to concentration on large exposures and individual counterparties, controlling and limiting non-financial risk events (fraud events, operative, technological, legal, and regulatory breaches, conduct issues or reputational damage).

The risk appetite is defined by risk limits and alerts for the identified material risks: Credit, Default, Liquidity, Structural, Capital, Operational, Compliance & Conduct (and by extension customers, products, and business practices), Reputational, Model and Strategic risk.

The limits and alerts are set by Risk in cooperation with Financial Management and Compliance and are approved by the Board of Directors. For 2022, the new limits and alerts were approved on 20 January 2022 by the Board of Directors.

All the metrics are monitored monthly by the Enterprise Risk Management function and reported at least quarterly to the BoD.

Risk Culture

The Bank's risk culture (RiskPro) is deeply rooted in the principle: "Risk is Everybody's Business", where all employees are risk managers and responsible for managing the risks they encounter, regardless of their level or role. RiskPro culture is embedded in all steps of an employee's lifecycle: recruitment, onboarding, growth and development, day-to-day operations, and leadership across all businesses.

During 2021, greater efforts was made across the Nordics to boost the RiskPro culture with the re-launch of the Bank-wide "Risk-Pro Academy" and the establishment of more consistent, frequent and multifaced "RiskPro Communications". Both initiatives aim to ensure that every employee fully understands well all the risks the Bank is facing and is fully equipped to manage them.

Having a strong risk culture is one of the key success factors that have allowed the Bank to effectively respond to changes in economic cycles, new customer demands, increased competition, and increased regulatory pressure. It is an integral part of how the Bank is defined and the way it operates: Simple, Personal and Fair.

Risk Data Aggregation
In line with Basel Committee on Banking Supervision's standards number 238, the Risk Data Aggregation project ensures that the risk data reported to senior management reflects the basic principles enforced in the regulation: captures all types of risks with appropriate accuracy and timeliness.

During 2021, the Chief Data Officer (CDO), Risk Data and the Risk Data Quality Reporting System (DQRS) teams continued to focus on providing a proper data governance along with the entire data life cycle, robust IT processes and reliable risk reporting. Data quality and traceability controls were set to ensure that risk reports contained accurate granularity and appropriate data sources.

Risk reports contain appropriate balance between data, analysis, and qualitative comments, including forward-looking measures, risk appetite data, limits, and emerging risks, and are distributed in due time and form to the senior management.

Strategic Commercial Plan
Once the RIA process has identified material risks and the risk appetite has set the corresponding risk tolerance accepted by the Board of Directors, the latter is cascaded down via the Strategic Commercial Plan (SCP). The SCP is the strategic tool utilized by the Bank to manage and control its credit portfolios. The SCP integrates the commercial and risk strategies, policies, means and infrastructure necessary to meet the annual budget. These features are considered on a joint basis, thereby guaranteeing a holistic view of the Bank's credit portfolio.

Regular monitoring of the SCP will anticipate any undesirable deviations observed with respect to the initial budget and will enable management to identify significant changes to risk, assess their potential impact, and apply any courses of corrective action that may be necessary.

This will also continuously provide management an updated view of the creditworthiness of the portfolios, and identify any key weaknesses in terms of policies, processes and means to help the Bank implement the mitigation mechanisms required.

3.3 Monitoring and Reporting

The main objective of risk monitoring and reporting is to ensure all risk types are managed in conformity with the risk appetite level approved by the Board. For this purpose, an array of different reports has been developed with different contents, audience, and frequencies.

The responsibility for developing risk reports rests with the Risk department, which is also responsible for securing the quality, standards, content, timeliness, and the distribution of risk information. The scheduled risk management information flows via the corporate Management Information System (MIS) reporting tool, which is in use for Risk reporting purposes at the SCB consolidated level internally and towards SCF HQ Risk Area.

The Bank's strong risk reporting structure is characterized by:

- Balancing data and qualitative comments, including forward-looking measures, risk appetite alerts, limits, and emerging risks.
- Covering all risk factors in the risk framework.
- Combining a holistic and reliable view with deeper analysis of each risk factor.
- Following risk data aggregation (RDA) criteria to report on metrics, ensuring data quality and consistency.

3.4 Internal Control

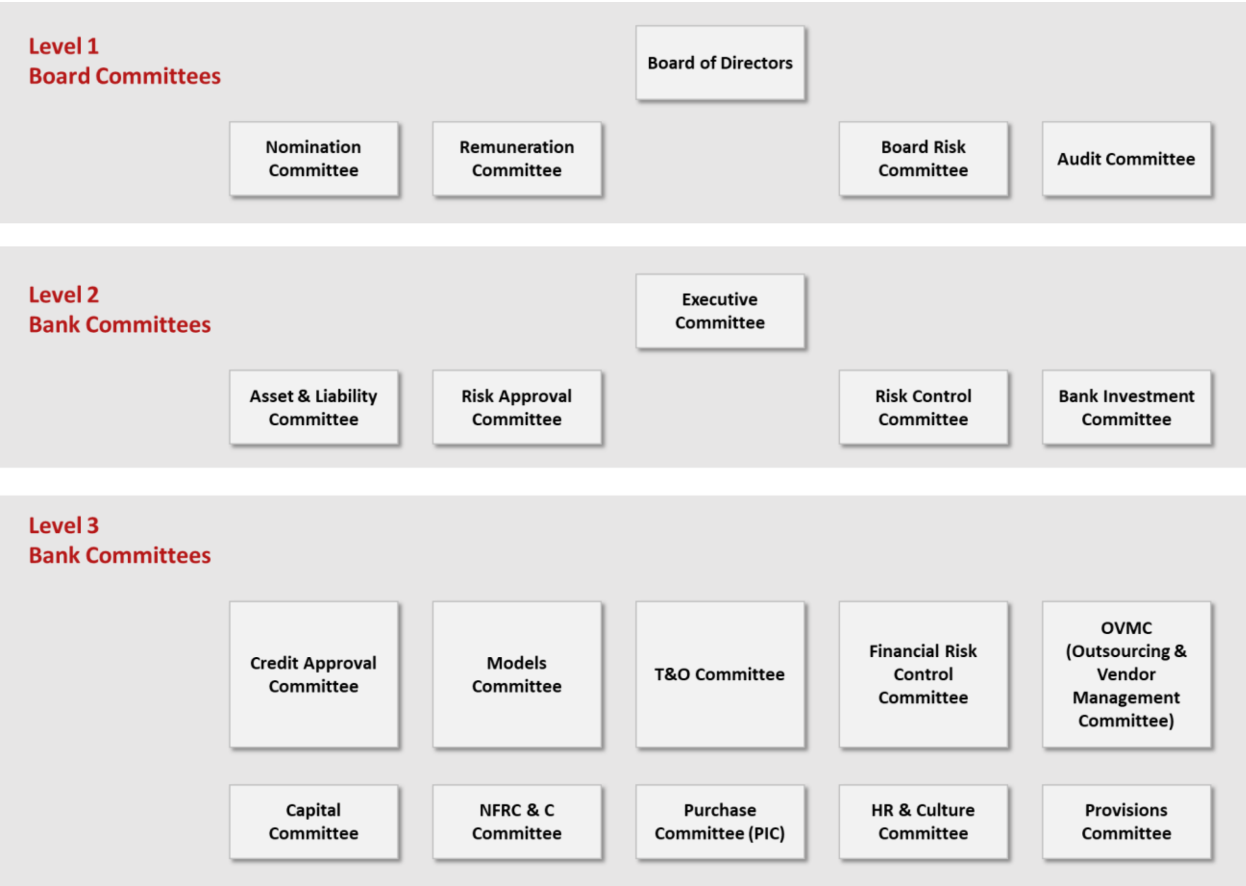
The BoD has established sub-committees with powers of supervision, information advice and proposals. An overview of the main objectives of the sub-committee is detailed below:

- Board Risk Committee (BRC): advise the BoD on current and future risks, risk appetite and risk strategy. This includes ensuring the establishment of appropriate internal control systems and the compliance with laws, ordinances, and internal regulations as well as generally accepted practices or standards.

- Audit Committee: review SCB's financial information and internal control systems and serve as the communication channel between the BoD and the external auditor. The committee also supervises the Internal Audit department. Further details on the Internal Audit function are detailed below.
- Nomination Committee: oversee the balance, knowledge, diversity, and experience of the BoD and to identify, when applicable, candidates to fill vacant positions in the BoD.
- Remuneration Committee: preparation of remunerations decisions to be adopted by the BoD and ensure compliance with and transparency of the remuneration policy.

The figure below illustrates how SCB's corporate governance is structured. It identifies the allocation of authority and responsibilities and how decision-making and reporting lines between the shareholder, the BoD, management, and Internal Audit are arranged.

Figure 3.4.1: SCB Governance Structure Overview



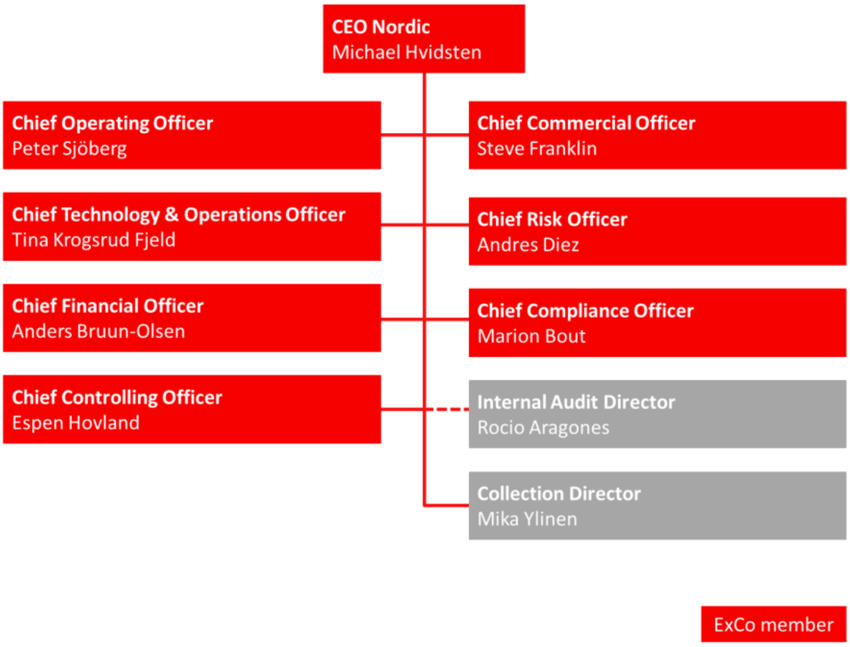
SCB operates with a pan-Nordic management structure, consisting of the CEO and heads of the different functions (departments).

Figure 3.4.2 shows the current management structure. Members of the senior management marked in red constitute the Bank's Executive Committee (ExCo). ExCo is responsible for:

- Draft, review and revise SCB's strategy and propose to the Board for approval
- Review and recommend revision of SCB's long-term strategic plan, three-year business, financial plan and annual budget, and validating it before sending to the Board for approval.
- Ensure execution of the Bank's strategy and value creation for the bank.
- Monitor the SCB's strategic, financial, and operational performance, and decide on corrective actions where needed, propose corrective actions or Board approval when required

- Monitor SCB's commercial performance, decide on corrective actions where needed, propose corrective actions or Board approval when required.
- Review and revise SCB's operating model and governance structure, recommend for Board approval when required
- Monitor and ensure that the bank is managed in accordance with regulations and Santander frameworks.
- Provide monthly updates to the Board via the CEO Update
- Act as SCB Special Situation Management Committee, conducting and monitoring the management of events of any kind (financial or of an operational/reputational nature) which may result in a severe deterioration of the SCB liquidity and/or solvency levels, and compromise the development of its activity.

Figure 3.4.2: SCB Senior Management per December 2021[1]



Finnish Subsidiary and Board of Directors

The subsidiary in Finland, Santander Consumer Finance Oy (SCF Oy), has its own Board of Directors who is overall responsible for the organization and administration of the subsidiary's affairs, including internal governance and control structure. However, it is the Board of the Bank's responsibility to ensure sound and proper communication with the Board of SCF Oy, including ensuring that the Board of SCF Oy receives relevant information, with regards to resolutions that may concern them, in a timely manner and prior to any related resolution being made by the Board of SCF Oy. The Board consists of two members and one deputy.

Internal Control Framework

The internal control framework within SCB is based on: (1) the Santander Internal Control Framework, (2) the requirements of The Sarbanes-Oxley Act (SOX), (3) the Committee of Sponsoring Organizations of the Treadway Commission Framework (COSO) and (4) the local requirements by Nordic regulators. The Santander Internal Control Framework sets the foundations for the Internal Control function in SCB and the internal control methodology.

[1] Effective from April 2022, Chief AML-Officer Cicilie Blakkisrud was included as member of the SCB Senior Management.

4 Capital Adequacy

4.1 Capital Management Governance

Governance and responsibilities related to capital management are outlined in the Bank's Capital Framework and Policy documents. The objective of the Capital Management governance framework is to ensure adequate solvency levels, regulatory compliance, and efficient use of capital.

The Board of Directors have the ultimate responsibility for the solvency and capital adequacy of the bank. Capital management decisions requiring Board approval must be approved and recommended by the Capital Committee before being recommended to the Board. Certain items may also need to be reviewed in the Board Risk Committee (BRC) before being presented to the Board. Capital management decisions will include those relating to capital adequacy, capital targets, capital composition, capital plan, dividend policy and capital contingency plans. The Capital Committee consist of members of senior management (the Chief Financial Officer, Chief Risk Officer and the Chief Controlling Officer) who have voting power and representatives from Risk, Financial Management and Financial Control who have an advisory role.

The Board approves target capital ratios, at least on an annual basis. Capital positions and forecasts are presented to the Board on a regular basis. Capital reporting to the Norwegian FSA is approved by the Capital Committee before submission. Any dividends proposed by the Board, must be finally approved in the SCB General Meeting.

Increase and reduction of capital is subject to the approval of the Board and the general meeting of SCB (either directly or through a power of attorney). Corporate authority to issue subordinated debt lies with the General Meeting of SCB (although such authority may be delegated to the Board through a power of attorney). All other debt issuances (including senior non-preferred debt) may be authorized by the Board, or any other person(s) authorized by the Board. In case of repayment of hybrid capital and subordinated debt, approval by the Board or any other person(s) authorized by the Board will be sufficient.

Dividend Policy

The dividend policy is an essential consideration when establishing capital targets and capital planning and must be fully consistent with the capital plan for SCB. The Policy states that "As a reference criterion, the pay-out ratio shall, over time, be at least 50%. However, the policy will be adapted to SCB's specific circumstances". Hence, SCB will assess its capital position prior to every potential dividend payment to ensure sufficient capitalization to cover all risks as well as all regulatory requirements.

Since the outbreak of the COVID-19 pandemic and until the last quarter of 2021, banks were encouraged by regulators not to distribute dividend. With no dividend payments since 2019 and large accumulated capital reserves, the Bank was in a position to distribute dividend of BNOK 1.7 from the financial year 2020 in Q4 2021 and further BNOK 2.0 from the financial year 2021, in Q1 2022. After such dividend distribution, the CET1 ratio for the the Bank was still 6%-points above the regulatory requirement per December 2021.

4.2 Capital Requirements

SCB is supervised by the Norwegian FSA and must comply with the capital requirements for banks in Norway. Norwegian banks are subject to ongoing capital adequacy requirements, which implement EU Directives and Regulations based on the Basel III regime. In line with the recommendations of the Basel Committee on Banking Supervision (the Basel Committee), the regulatory approach in the Financial Undertakings Act is divided into three pillars:

- Pillar 1: Minimum regulatory capital of 8% of risk-weighted assets: banks shall, at all times, satisfy capital adequacy requirements reflecting credit risk, operational risk and market risk.
- Pillar 2: Assessment of overall capital needs and individual supervisory review: banks must have a process for assessing their overall capital adequacy in relation to their risk profile and strategy for maintaining their capital levels – the Internal Capital Adequacy Assessment Process or ICAAP. The regulator evaluates the ICAAP and, following completion of the Supervisory Review and Evaluation Process (SREP), publishes the Pillar 2 requirement (P2R) for the bank. In addition, the Norwegian FSA will assess SCB's own stress test performed in ICAAP, and other stress tests conducted by other regulators (European Banking Authority and International Monetary Fund) to communicate Norwegian FSA's expectations of a Pillar 2 guidance (P2G) over and above the overall capital requirement.
- Pillar 3: Disclosure of information: banks are required to disclose relevant information on their activities, risk profile and capital situation to the market.

The table below outlines the evolution of capital requirements for SCB Group as per December 2021 and 2022 (expected).

The Bank received a new Pillar 2 requirement and guidance in February 2022, which will be applicable from March 1, 2022. The decision from the Norwegian FSA was that the Pillar 2 requirement were to remain at 3.3%, and that Pillar 2 Guidance would increase from 1% to 1.5%.

In the spring of 2019, the EU adopted what is collectively called the "Banking Package", including changes to EU's capital requirements legislation and the Bank Recovery and Resolution Directive, CRR II, CRD V and BRRD II, which entered into force in the EU from the spring of 2021. The Norwegian implementation has been delayed and will enter into force in Norway from 1 June 2022. The regulatory changes in the Banking Package include minimum requirements for leverage ratio, requirement for NSFR, narrowing of the supervisory authority's ability to conclude on Pillar 2 requirement for systemic risk, and greater flexibility for national authorities to implement measures to deal with various forms for systemic risk, including increased capital buffers. In addition, the so-called "SME discount" will be continued and expanded. The Banking Package furthermore include additional rules on how the crisis management authority shall determine how much of the MREL requirements is to be met with subordinated debt. The Bank is well positioned to meet the changes to capital requirements and do not expect the changes to have material impact on the Bank's capital position.

The Bank uses the advanced IRB-approach for the private auto portfolios in Norway, Sweden, and Finland. In July 2021, the Bank submitted updated IRB models to the Joint Supervisory Team incorporating new regulations and guidelines. There is no timeline for when the new models will be approved and thus implemented.

The Joint Supervisory Team has communicated that the Bank can expect to receive MREL requirements in the near future. SCB will be required to issue internal MREL only (provided by parent) to ensure ownership is not diluted in resolution.

During second half of 2021, regulators in the Nordics have communicated their expectations towards increasing the countercyclical buffer requirements ("CCyB"). In Norway, the CCyB will increase from 1% to 1.5% effective from 30 June 2022 and further to 2.0% effective from 30 December 2022 and 2.5% effective from 31 March 2023. In Denmark, the CCyB will increase from 0% to 1% with effect from September 2022 and further to 2.0% with effect from 31 December 2022 and 2.5% with effect from 31 March 2023. In Sweden, the CCyB will increase from 0% to 1% with effect from 29 September 2022. Despite the increase in expected capital requirements, the Bank expects to maintain a solid capital adequacy position going forward.

The Systemic Risk Buffer (SRB) remains unchanged of 4.5% in Norway. However, the Bank is allowed to use the buffer requirements in the jurisdiction where it operates. In Sweden, Denmark, and Finland the SRB is 0%.

Table 4.2.1: SCB Group Capital Requirements December 2021 and Expected December 2022

December 2021	Capital Requirement (%)	December 2022E	Capital Requirement (%)
CET1		CET1	
Minimum requirement	4,50 %	Minimum requirement	4,50 %
Capital Conservation Buffer	2,50 %	Capital Conservation Buffer	2,50 %
Systemic Risk Buffer [2]	1,30 %	Systemic Risk Buffer [2]	1,30 %
Countercyclical Buffer (CCB) [1]	0,29 %	Countercyclical Buffer (CCB) [1]	1,32 %
Total Pillar 1 requirement	**8,59 %**	**Total Pillar 1 requirement**	**9,62 %**
Pillar 2 requirement (P2R)	3,30 %	Pillar 2 requirement (P2R)	3,30 %
Pillar 2 Guidance (P2G)	1,00 %	Pillar 2 Guidance (P2G)	1,50 %
Total CET1 requirement	**12,89 %**	**Total CET1 requirement**	**14,42 %**
Tier1 (T1)		Tier1 (T1)	
Additional T1 requirement	1,50 %	Additional T1 requirement	1,50 %
Total T1 requirement	**14,39 %**	**Total T1 requirement**	**15,92 %**
Tier2 (T2)		Tier2 (T2)	
Additional T2 requirement	2,00 %	Additional T2 requirement	2,00 %
Total T2 requirement	**16,39 %**	**Total T2 requirement**	17,92 %
Leverage Ratio (LR)		Leverage Ratio (LR)	
Minimum leverage requirement	3,0 %	Minimum leverage requirement	3.0 %
Buffer requirement for non-SIFI banks	2,0 %	Buffer requirement for non-SIFI banks	2.0 %
Total LR requirement	**5,0 %**	**Total LR requirement**	**5.0 %**

[1] Based on local CCB req. Dec21: NO 1%, SE 0%, DK 0%, FI 0%
[2] Based on local SRB req. Dec21: NO 4.5%, SE 0%, DK 0%, FI 0%

[1] Based on local CCB req. Dec22: NO 2%, SE 1%, DK 2%, FI 0%
[2] Based on local SRB req. Dec22: NO 4.5%, SE 0%, DK 0%, FI 0%

Pillar 1 Requirements

The minimum capital adequacy requirement of 8% shall consist of at least 4.5% Common Equity Tier 1 capital (CET1 capital), at least 1.5% of Additional Tier 1 capital (T1 capital) and the remaining 2.0% may consist of subordinated capital instruments (T2 capital). In addition, banking institutions are subject to various regulatory buffer requirements referred to as combined buffer requirements (CBR) which must be met with CET1 capital. Per 31 December 2021, the Bank's CBR consisted of a 2.50% capital conservation buffer, a 1.30% systemic risk buffer and a 0.29% countercyclical buffer (CCyB) which is calculated as a weighted average of country specific CCyBs in accordance with CRD IV Article 140.

Systemic important financial institutions should hold an additional 2% buffer of CET1 capital. However, SCB is not considered a systemic important financial institution ("SIFI") and therefore, has no SIFI buffer requirement.

In summary, the Pillar 1 CET1 capital requirement for SCB Group was 8.59% per 31 December 2021.

Pillar 2 Requirements

SCB conducts, at least annually, an internal capital adequacy assessment process (ICAAP) which is used as one input to determine the Bank's Pillar 2 capital requirement. Several departments are involved in the ICAAP process including Financial Management, Risk, Financial Control, Legal and Compliance & Conduct and IT Risk. Stress scenarios, as well as outcomes of various analysis in the ICAAP report are reviewed and approved by the Capital Committee. In addition, all analysis and governance processes leading to the ICAAP report are reviewed by Internal Audit.

Thereafter, the ICAAP is reviewed by the Risk Control Committee and the Board Risk Committee, which gives its recommendations to the Board of Directors. Finally, the ICAAP is reviewed and approved by the Board of Directors prior to submission to the Norwegian FSA.

The Bank received a new Pillar 2 requirement and guidance in February 2022, which will be applicable from March 1, 2022. The decision from the FSA was that the Pillar 2 requirement were to remain at 3.3%, and that Pillar 2 Guidance would increase from 1% to 1.5%.

Pillar 3 Requirements

This Pillar 3 report is updated at least annually in conjunction with the Annual Report, as outlined in the Capital Framework approved by the BoD. The report meets the information requirements in accordance with the "Regulation on capital requirements and national adaptation of CRR/CRD IV", the NFSA Circular 5/2018 "Offentliggjøring av finansiell informasjon – kommisjonsforordninger og anbefalinger fra EBA" and the guidelines issued by the European Banking Authority (EBA) in "Guidelines on disclosure requirements under Part Eight of Regulation (EU) No 575/2013 (EBA-GL-2016-11)". In addition, the Bank publishes an appendix to the report (see Pillar 3 Appendix), where terms of capital instruments, capital & own funds, leverage ratio, countercyclical buffer requirements and credit exposures are disclosed.

The senior management members of the Capital Committee, consisting of the Chief Risk Officer, the Chief Controlling Officer and the Chief Financial Officer, as voting members, approve the content of the Pillar 3 report.

Internal Audit assesses the quality of the disclosure of information about the bank's capitalization, risk profile and management and control of risk.

Leverage Ratio Requirements

In addition to the Pillar 1 and Pillar 2 capital requirements, banks are required to adhere to leverage ratio requirements. The leverage ratio is calculated in accordance with CRR Article 429 i.e., Tier 1 capital and total exposures (on and off-balance sheet). Since 30 June 2017, the Norwegian FSA has set a minimum leverage ratio requirement of 3%, a mandatory buffer of 2% for all banks and a 1% buffer for SIFI banks. SCB must comply with a leverage ratio requirement of 5%.

Recovery Plan and Minimum Requirements for Own Funds and Eligible Liabilities

The Bank has prepared a Recovery Plan in accordance with the Bank Recovery and Resolution Directive (BRRD) which is transposed into Norwegian legislation by amendments to the Financial Institutions and Financial Groups Act (Finansforetaksloven). The Bank's latest version of the Recovery Plan was approved by the Board on 22 September 2021 and was submitted at request from the Joint Supervisory Team comprised of the European Central Bank and the Norwegian Financial Supervisory Authority jointly. The Recovery Plan is presented as part of Banco Santander's Recovery Plan, and covers the Bank's operations in Norway, the branches in Denmark and Sweden as well as the subsidiary in Finland.

A Bank's Recovery Plan will be the foundation for the Minimum Requirement for own funds and Eligible Liabilities (MREL) so that banks have sufficient capital and convertible debt to handle crisis without the use of public funds. The Bank has been informed that it can expect to receive a MREL requirement in the near future. SCB will be required to issue internal MREL only (provided by parent) to ensure ownership is not diluted in resolution.

4.3 Capital Position per December 2021

SCB Group possesses a robust capital adequacy position. Per 31 December 2021, the CET1 capital ratio was 18.89% on a phased-in IFRS9 basis and 18.74% on a fully phased-in IFRS9 basis, representing a significant buffer of 6%-points above the minimum regulatory requirement. The corresponding numbers for SCB AS was 18.34% and 18.22%. Although official reporting to the Norwegian FSA is with transitional rules for IFRS 9 impact, the Bank manages its capital on a fully phased IFRS 9 basis. From Q1 2022 onwards, the Bank will report on a fully phased-in basis only.

Since the outbreak of the COVID-19 pandemic and until the last quarter of 2021, banks were encouraged by regulators not to distribute dividend. With no dividend payments since 2019 and large accumulated capital reserves, the Bank was in a position to distribute dividend of BNOK 1.7 from the financial year 2020 in Q4 2021 and further BNOK 2.0 from the financial year 2021, in Q1 2022 (captured in the 31 December 2021 CET1 ratio of 18.89%).

The Bank's leverage ratio was 13.52% (SCB AS: 13.84%) as of 31 December 2021, significantly above the 5% regulatory requirement. The Table below details SCB Group's surplus of capital vs. regulatory capital requirements in 2021. For more information on capital adequacy, please refer to "Note 9 – Capital Adequacy" in the 2021 Annual Report.

Table 4.3.1: SCB Capital Adequacy vs. Regulatory Requirements as at 31 December 2021

Composition of SCB's capital adequacy requirements	2021	
	%	NOK m
Minimum CET1 requirement	4,50	5 746
Systemic Buffer	1,30	1 665
Counter cyclical buffer	0,29	370
Capital conservation buffer	2,50	3 192
Pillar 2 requirement	3,30	4 214
Pillar 2 guidance	1,00	1 277
CET1 requirement	**12,89**	**16 464**
Additional Tier 1	1,50	1 915
Tier 1 requirement	**14,39**	**18 380**
Tier 2	2,00	2 554
Total Capital requirement	**16,39**	**20 933**
SCB CET1	**18,7**	**23 929**
- Surplus of CET1	5,9	7 470
SCB Tier 1	**20,5**	**26 179**
- Surplus of Tier 1	6,1	7 802
SCB Total Capital	**22,4**	**28 640**
- Surplus of Total capital	6,0	7 712

SCB uses both the Standardized approach and A-IRB approach for calculating risk weighted assets (RWAs) for credit risk, the Standardized method for calculating market risk and the Basic Indicator Approach for operational risk. The Bank's RWAs are used as the basis for calculating the combined buffer requirements. RWA decreased from MNOK 131 555 to MNOK 127 890 from December 2020 to December 2021, with a reduction in Retail exposure under the standard approach and an increase in Retail exposure under the IRB approach. This is mainly explained by a reduction in unsecured portfolios and increase in retail auto portfolios. NOK has strengthened versus SEK, DKK, and EUR during 2021 which dampened the increase in RWA.

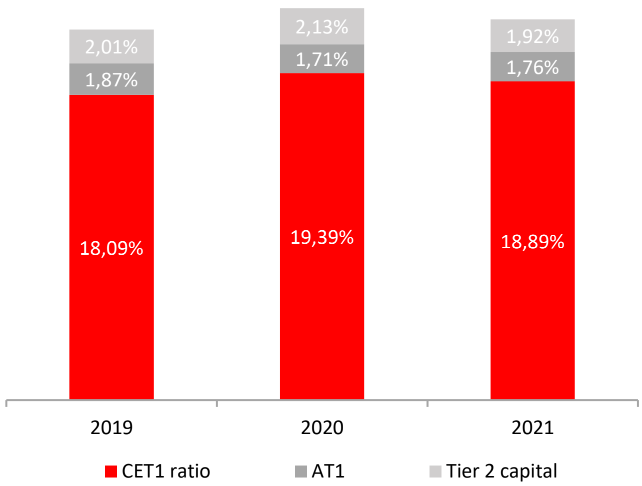
Table 4.3.2: SCB Group Risk Weighted Assets as at 31 December 2021

Risk Weighted Assets ("RWAs")	2020	2021
Standardised Approach		
Regional Governments	73	66
Institutions	988	700
Corporates	11 180	7 899
Retail	59 065	54 105
Default	1 209	3 229
Covered Bonds	100	64
Other	4 030	3 512
Total Standardised Approach	76 645	69 574
Internal Ratings Based Approach		
IRB	37 864	41 141
Total IRB Approach	37 864	41 141
Market Risk	2 472	2 684
Operational Risk	14 247	14 261
CVA	46	30
Total RWAs	131 275	127 690
IFRS 9 Transitional Adjustment	280	200
Total RWAs (After IFRS9 transitional rule)	131 555	127 890

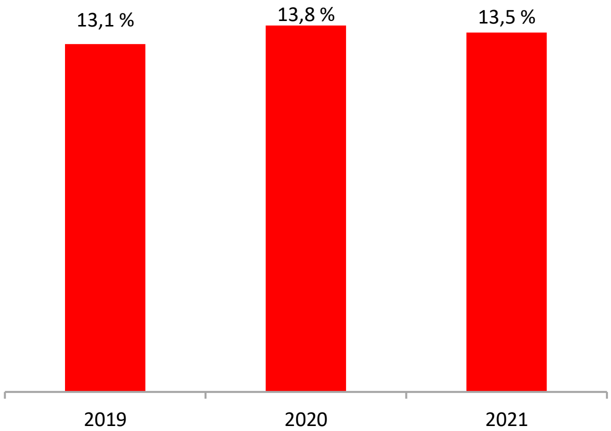
The figure below depicts the development of the Bank's key capital adequacy metrics.

Figure 4.3.1: SCB Group Development of Key Capital Adequacy Metrics

Total Capital Ratio (%)



Leverage Ratio (%)



Development of Risk Weighted Assets, 2020-2021 (million NOK)

The Pillar 3 appendix and *"Note 9 - Capital Adequacy"* in the 2021 Annual Report, discloses more information on SCB's capital adequacy position and requirements.

5 Counterparty Risk

The Bank defines counterparty credit risk as defined in Article 272 of CRR: "Risk that the counterparty to the transaction could default before the final settlement of the transaction cash flows".

Transactions within the scope of counterparty credit risk in the Bank are cross currency swaps and interest rate swaps. These types of derivatives are used to hedge currency and interest rate risk related to funding transactions. All the Bank's derivatives have signed collateral agreements with the counterparty with bilateral daily collateral posting.

The Bank holds derivatives for hedging purposes only and capital required for these transactions represent a very small share of total capital requirements - counterparty credit risk is thus not considered a significant risk for the Bank.

6 Credit Risk

SCB defines credit risk as "the potential that a borrower or counterparty will fail to meet its obligations in accordance with agreed terms."

SCB business is mostly focused on auto financing (auto loan, leasing, subscription, and stock finance) and unsecured products (consumer loans, credit cards and sales finance). Due to the type of business performed, credit risk is the most significant risk in SCB.

6.1 Strategy and Policies

SCB's credit risk strategy aims to maintain a predictable risk level, sustainable in the long-term in terms of portfolio profitability and in line with the Bank's risk profile.

SCB's credit risk strategy is detailed in the annual Strategic Commercial Plan (SCP). From a credit risk perspective, the SCP presents the relevant Risk Appetite metrics, the credit management limits, covering the entire credit cycle (credit granting processes, performance of SCB's existing credit portfolios, relevant metrics related to the collections and recoveries of delinquent customers). Particular attention is given to the credit management limit related to the Internal Rating Based (IRB) parameters both at new business and portfolio level.

SCB governs processes related to credit limits, their breach, and their governance in accordance with its internal policies.

SCB's corporate governance includes committees with various responsibilities over credit risk. Besides the Board Risk Committee (BRC), SCB's organizational structure includes Bank committees with several responsibilities for credit risk. Among the Bank's commitees there is a clear segregation of duties between approving commitees and controlling committees.

6.2 Credit Risk Monitoring and Reporting

In order to fulfil SCB's ambitions on credit quality and portfolio composition, the Bank has put in place information systems supported by analytical techniques that measure and report credit risk on both individual and portfolio levels throughout the credit risk cycle.

In addition to the Risk Appetite and credit management limits, SCB does extensive work monitoring and forecasting other key risk metrics. These include but are not limited to; net flows of non-performing loans, loan loss reserves, IFRS9 estimated losses, write-off and post write-off recoveries.

The purpose of the credit risk monitoring environment is to provide tools for risk management and control of the credit risk exposures of the Bank and to accurately forecast future developments. Four processes are key to achieve this:

- Credit risk budgeting processes are performed annually both for the upcoming year and towards the next three years.
- Credit risk forecasts are performed on a monthly basis both for upcoming month and towards year end.
- Simulation of the month close is performed shortly before month end in order to test changes which impact the credit risk process.
- Monthly credit risk reports where performance is evaluated against forecasted expectations and the budget of the month.

The four mentioned procedures enable SCB's management to identify any areas that may require further assessment.

While retail products are monitored through an aggregated/portfolio view, wholesale clients are monitored at an individual basis. The Wholesale customers are assigned an internal rating according to a rating model developed based on guidelines from Banco Santander, which will then derive an individual Probability of Default within 12 months (PD). The model considers the Bank's internal knowledge and expertise as well as an objective assessment of the customers financial and management structure.

For the different retail customer segments, the Bank operates specific credit admission processes and applications through a decision model. The objective of the decision model is to maximise the automation level of the credit decisions while retaining predictability of risk. Manual decisions may apply in order to review the creditworthiness of cases not decided automatically by the decision model. The level of automatic decisions needs to balance the expected risk/return relationship, the number of available resources and expected application volumes.

6.3 Admissions and Monitoring of Standardized and Non-Standardized Risk

To ensure business policy and practices are aligned with product features and characteristics, and with the needs of the Bank's customers, SCB divides its portfolios into two main segments:

- Retail Credit Risk: applicable to the part of the portfolio which follows a standard, highly automated credit approval process primarily based on system-generated decisions. It does not warrant individualized treatment of clients as the risk is well diversified, and each individual client has a low total exposure. Retail Risk clients includes private persons, as well as sole proprietorships and small and medium-sized enterprises ("SME") companies without a permanently assigned risk analyst.
- Wholesale Credit Risk or "Non-standardized risk": applicable to customers who, due to their volume of risk exposure or type of risk exposure with SCB, are permanently assigned to a risk analyst with a tailored and individualized credit approval process. Banco Santander's standard criterion is to assign analysts to companies with exposures over 0.5 million EUR. If the customer has stock finance as a product, regardless of the exposure size, the customer is included in the wholesale portfolio.

Credit Scorecards

The main credit risk management tool for the retail portfolio in the Bank is based on the use of scorecards. Admission and behavioural scorecards have been developed and implemented for all retail portfolios (except Denmark Auto SME and Credit Cards). The purpose of the admission scorecards is to distinguish between customers based on their creditworthiness, whilst behavioural scorecards monitor the customer's credit behaviour over time. Upon scoring, the customer is assigned a Probability of Default (PD) bucket which is used for risk monitoring purposes and in capital calculations under the Advanced Internal Ratings Based (A-IRB). In addition, the scoring models are used also as main segmentation drivers in the Bank's IFRS9 PD estimation models for Expected Credit Loss (ECL) calculation purposes. All implemented scorecards are monitored quarterly for their performance i.e., stability, accuracy, and predictability to ensure they work as intended. The goal is to ensure that portfolio delinquency rate is within acceptable limits by adjusting the score limits in line with the risk appetite of the Bank. In addition to performance monitoring, overall model risk level is also periodically monitored by senior management at SCB.

Internal Rating Model

The non-standardized customers in the Bank are composed of large and/or complex exposures evaluated individually by a risk analyst and are not scored by the retail scorecards. BoD delegates autority to approve credit risk proposals to the CEO which further delegates authority to different levels in the organization depending on size of the exposure, rating, profitability and more. Credit risk approvals above certain thresholds are presented in internal committees and approved by the CCO and CEO respectively.

An internal rating model developed centrally in Banco Santander (SCB's ultimate parent) is implemented in all units. This involves risk analysts reviewing all wholesale clients and setting a rating score, following the Santander Rating scale. Each rating point from the Santander Internal Rating model method will in turn result in a specific PD. Based on the historical delinquencies on wholesale clients, the rating model has been calibrated to a corporate scale converting rating to PD, estimating probability of default within 12 months. This internal rating model applies exclusively to non-standardized customers and should not be confused with the Advanced Internal Rating Based Model (A-IRB) mentioned in other parts of this document.

6.4 Credit Risk Profile

SCB's credit portfolio has a diversified risk composition with regards to single customers, business sectors, geographical areas, and market segments. The Bank operates in four different countries and the consumer lending business is composed of the following products:

- Auto Wholesale: Loans or Leasing solutions offered to SMEs and bigger corporate customers treated as wholesale clients and/or having Stock Financing products.
- Auto Retail: Loans or Leasing solutions offered to private persons, sole proprietorships, and SMEs.
- Consumer Loans: Offered to private persons only.
- Credit Cards: Offered to private persons only.
- Durables Financing: Offered to private persons only.

SCB's gross outstanding loans decreased from BNOK 181 to BNOK 176 between December 2020 and December 2021. As the figure below shows, the decrease is driven by a lower unsecured portfolio which saw a significant reduction in new sales when compared to 2020 impacted by restrictions and lockdowns due to COVID-19 as well as experiencing higher repayment rates (i.e. lower credit risk). The auto portfolio remains at a stable level.

Figure 6.4.1: Gross Outstanding by Country (MNOK)

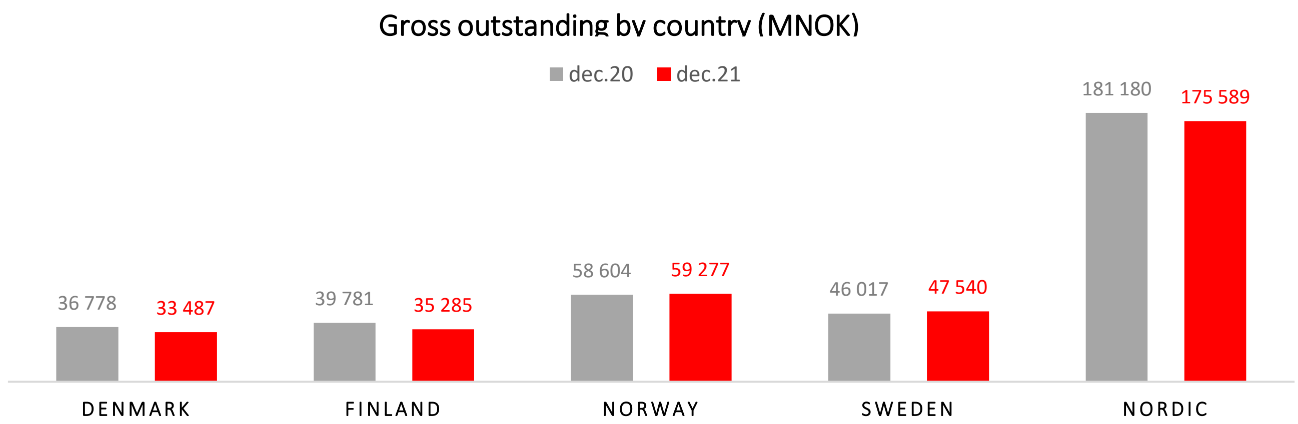
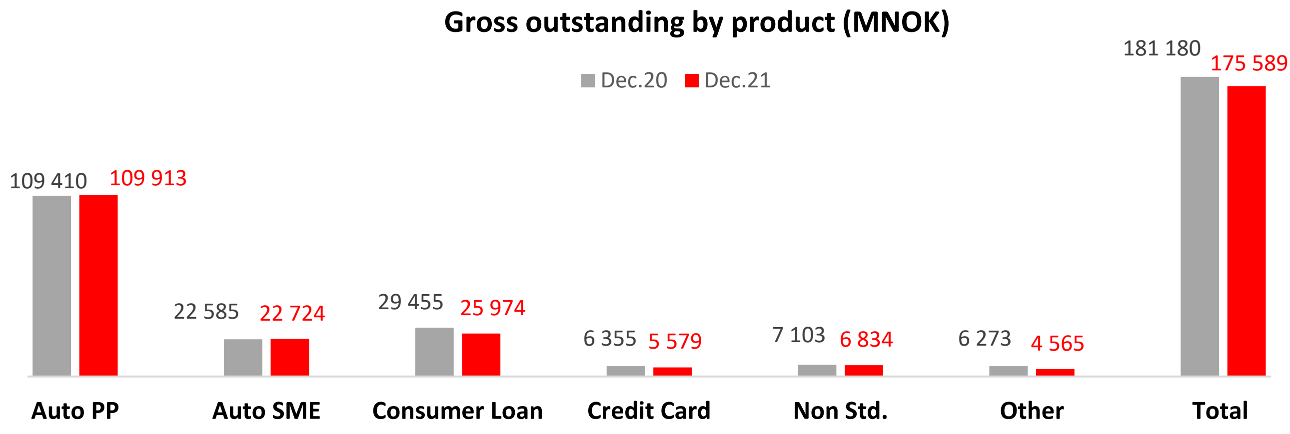
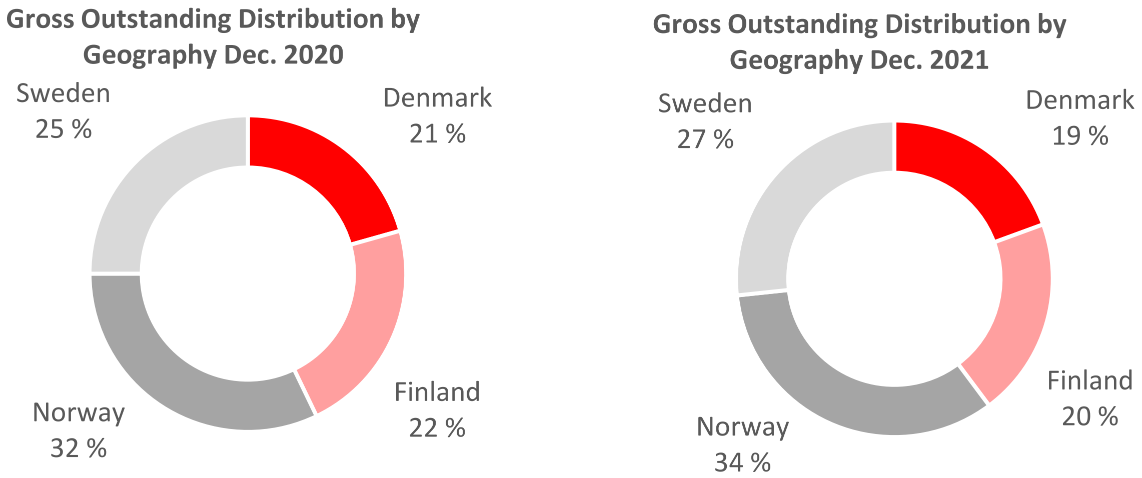


Figure 6.4.2: Gross Outstading by Product (MNOK)



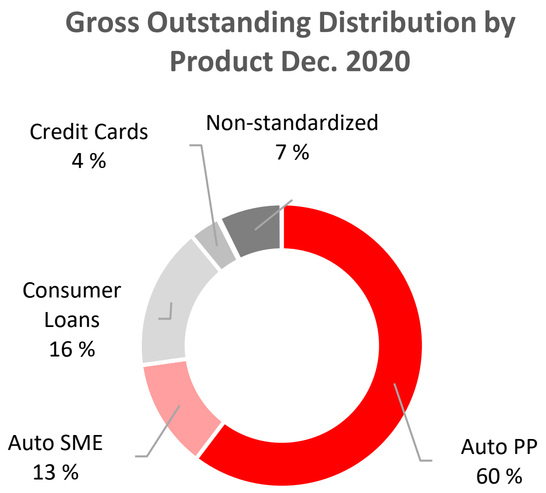
The figures below show the country break-down for December 2021 and December 2020. Compared to 2020, the asset distribution per country has remained stable. The portfolio grew in Sweden and Norway and the latter is further aided by the appreciation of the NOK over the course of 2021. Current distribution is well-balanced, in line with the SCB's business strategy.

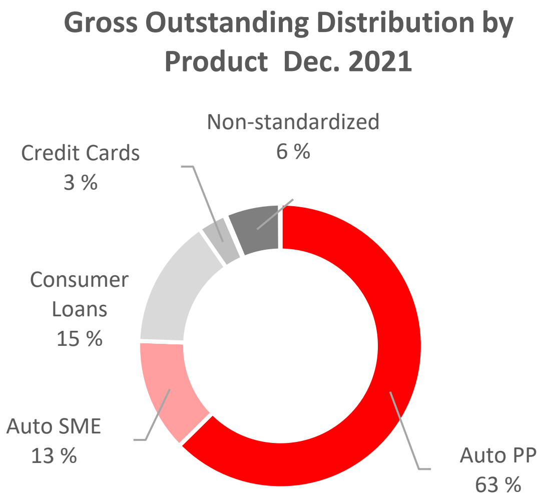
Figure 6.4.3: Gross Outstanding Distribution by Geographies



SCB's product mix is displayed in the figure below. As of December 2021, Auto Private Persons (Auto PP) continues to be the largest portfolio of the Bank, and Consumer Loans the second largest. Auto PP Norway accounts for a largest part of the Auto PP portfolio.

Figure 6.4.4: Gross Outstanding Distribution by Product

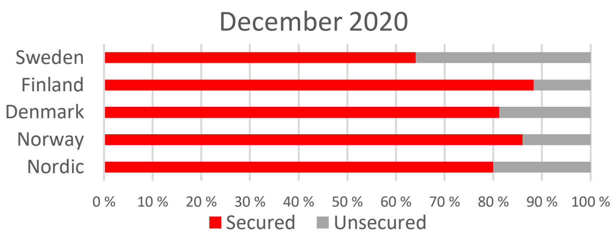


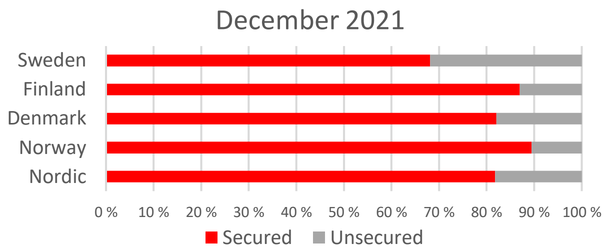


The relative share of secured loans (auto) relative to unsecured loans is continuing to grow and is, per December 2021, constituting 82% of gross outstanding loans at consolidated level. Auto PP in Norway, Sweden, and Finland are IRB portfolios and represent the biggest portfolios in each country.

Figure 6.4.5 shows the split between secured and unsecured portfolio per country and at consolidated level for December 2020 and December 2021. Year-to-Year ("YoY") the secured portfolio share increased by 2% points.

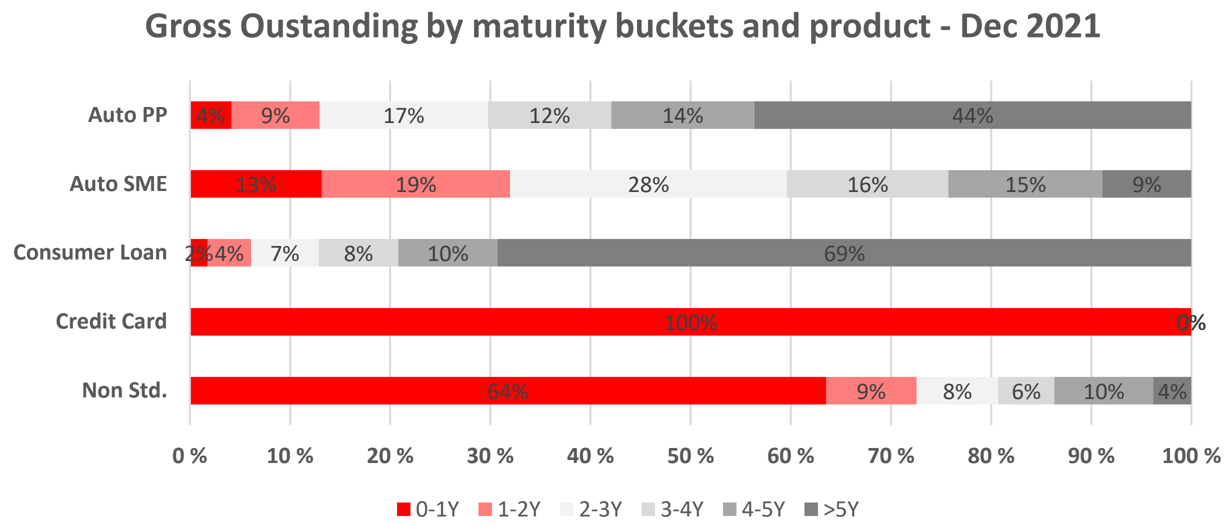
Figure 6.4.5: Gross Outstanding Distribution by Secured and Unsecured Portfolios





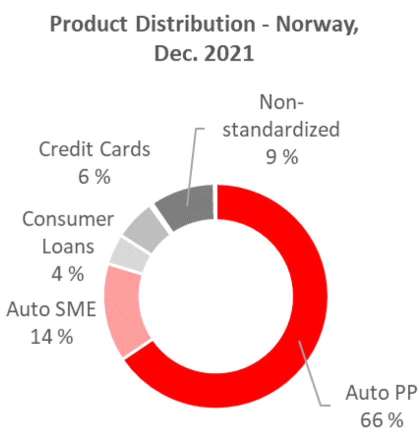
The figure below shows the distribution of gross outstanding loans by different residual maturity buckets (based on contractual maturity). Auto and consumer loan products have higher maturity due to higher ticket size. Credit card is an open-end loan; thus, it has been reported without any maturity split (based on the initial terms of the contract). Note that there is still a significant % of exposure with maturity over 5 years for consumer loans. This exposure refers to contracts set on books prior to the stricter regulations highlighted in FSA's circular 5/2019[2] on consumer lending practices.

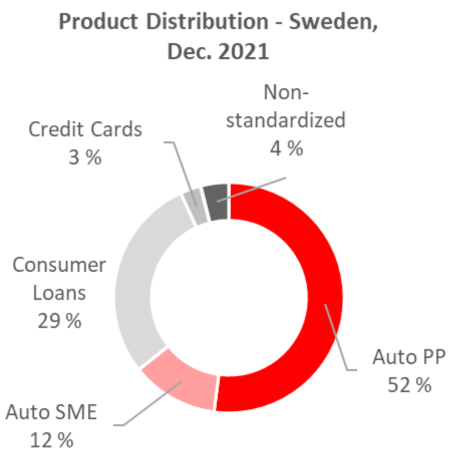
Figure 6.4.6: Gross Outstanding Distribution by Maturity Buckets as per December 2020



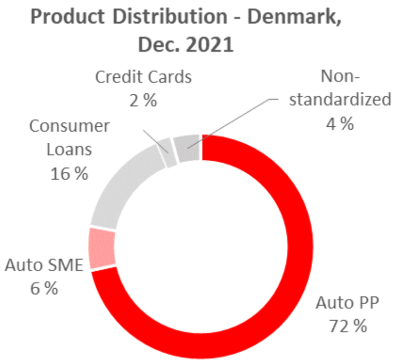
The following figures show the product distribution per country as of December 2021. As can be seen from the figures, Auto PP account for the largest share of business in all countries, ranging from 52% in Sweden to 72% in Denmark. Sweden has the largest share of Consumer loans with 29%.

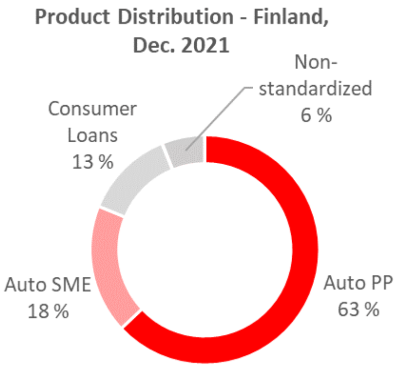
Figure 6.4.7: Gross Outstanding Distribution by product





[2] https://www.finanstilsynet.no/contentassets/adff29a42bcc4584acd7883a73e9eef1/krav-til-finansforetakenes-utlanspraksis-for-forbrukslan.pdf





The table below outlines exposure, risk weight and capital requirement for the credit risk categories used in capital reporting. As can be seen, the average risk weight of the Bank's exposures is c. 60% (RWA/EAD). As will be detailed in the following section, the Bank reports its credit exposures under the Standardized and Advanced Internal Ratings Based Approach ("A-IRB").

Table 6.4.1: Overview of Gross Exposures, Exposures as Default and RWAs as at 31 December 2020

million NOK	Gross Total Exposure	Total EAD	Total RWA	RWA Density (RWA/EAD)	Capital Required
Regional and Governments	13 790	13 790	66	0,5 %	5
Institutions	4 858	4 858	700	14,4 %	56
Corporates	17 369	8 130	7 899	97,2 %	632
Retail (Standardised approach)	101 824	76 306	54 105	70,9 %	4 328
Retail (A-IRB approach)	84 179	84 179	41 141	48,9 %	3 291
Exposures in Default	5 040	2 672	3 229	120,8 %	258
Covered Bonds	636	636	64	10,1 %	5
Other Exposures	3 092	3 092	3 512	113,6 %	281
Total Credit Risk	230 786	193 663	110 716	57,2 %	8 857

6.5 SCB's Application of Credit Risk Methodologies

SCB uses both the Standardized Approach and the Advanced-IRB Approach to calculate its capital requirements for credit risk.

- Standardized Approach: general risk weights are prescribed in the Capital Requirements Regulation (CRR) for each exposure type to determine credit risk weighted assets (RWA) amounts.
- Advanced-IRB Approach (A-IRB): banks use their own estimated risk parameters – Probability of Default, Loss Given Default and Exposure at Default – to determine credit risk RWA amounts. There are numerous and very stringent requirements that banks must adhere to be able to report under A-IRB.

SCB considers the implementation of advanced IRB approach to be strategically important and a key business driver for sustainable growth and future competitiveness. The operational benefits of IRB are related to improved client information, increased accuracy of models, improved scoring, processes, and routines, and in general improved risk management practice of the Bank.

Greater information regarding the Bank's adoption and use of A-IRB is detailed in Section 6.8.

6.6 Key Terminology: Credit Risk Metrics and IRB Parameters

The information below describes important terms used to describe credit risk across the Bank's credit portfolio. These terms will be used throughout the remainder of this chapter.

Risk Classification Models

Risk classification models refer to an SCB internal model that classifies a customer or engagement by risk. The customer or engagement is typically placed in a risk class. The risk class associates a probability of default (PD), a loss given default (LGD), or a mixture of these two, such as expected loss (EL). In some models, these parameters are produced directly without necessarily going through the classification process.

The Bank's definition of the default, write-off and loan loss reserves is detailed below:

Default: The Capital Requirements Regulation (CRR) from 2013 established the definition of default for the purposes of the internal ratings-based (IRB) approach and the standard approach for credit risk under the Article 178. However, the European Banking Authority (EBA) has identified different practices used by the entities when applying the definition of default, making comparison across different institutions difficult. To harmonize the default identification, the EBA published specific Guidelines (GL)[3] and Regulatory Technical Standards (RTS)[4] defining how to determine default, for capital calculation purposes applicable from January 2021.

The new definition of default includes the criteria for counting of days past due, indications of unlikeliness to pay, return to a non-defaulted status, etc. The RTS specifies that competent authorities (CAs) shall set the materiality thresholds for a defaulted amount. The Norwegian FSA has defined the following thresholds for arrears amount:

- For retail: 1000 NOK as absolute threshold and 1% as relative threshold.
- For non-retail: 2000 NOK as absolute threshold and 1% as relative threshold.

Counting of days past due starts when both absolute and relative materiality thresholds are triggered. An asset is considered in default when the days past due are more than 90 days and/or if an indication of unlikeliness to pay condition is triggered.

The Bank has since December 2021 applied the new default definition both for capital calculation purposes and for accounting reserves.

Derecognition ("write-offs"): credit obligation is written-off and removed from the balance sheet once the bank has no reasonable expectation of recovering a financial asset in its entirety or party thereof. SCB uses indicators such as days past due, expected cash flows and collateral to determine write-offs. In 4Q 2018, SCB's Board of Directors approved a change in write-off policy for its unsecured portfolios in Sweden, Denmark, and Finland. In Q2 2019, the Board approved the same policy for Norway. The revised policy dictates that, in order for an exposure to be written-off, it must meet the criteria of being more than 720 days past due (DPD) as opposed to 180 DPD as was previously applicable. The rationale for the change is to ensure that the exposures are written off once the Bank has no reasonable expectation of recovering a financial asset in its entirety or a portion thereof and is aligned with IFRS9 requirements. The impact of the change in write-off policy for the Bank was an increase in NPL exposures for the unsecured portfolios.

Loan Loss Reserves (LLR): Loan loss reserves calculated for accounting purposes, according to IFRS9 guidelines, divide the Bank's credit risk exposure into three stages according to the risk performance status. At origination and when the credit risk

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[3] EBA guidelines on the application of the definition of default under Article 178 of Regulation (EU) No 575/2013 (EBA/GL/2016/07)

[4] RTS on the materiality threshold for credit obligations past due under Article 178 of Regulation (EU) No 575/2013 (EBA/RTS/2016/06)

has not increased significantly since initial recognition, the loans are classified as "stage 1". For these loans, loan loss reserves (LLR) are calculated for 12-month expected credit losses. For loans where credit risk has increased significantly but where the Bank does not have objective evidence of impairment, these are classified as "stage 2". For stage 2, LLR is based on lifetime expected credit losses. Stage 2 includes risk exposures which fall under one or more of the following categories:

- Not in default state as of reporting date but was in default during any of last 12 months before reporting date.
- Loans with forbearance action and not normalized as of reporting date and not in stage 3.
- More than 30 days past due and not in stage 3.
- Has previously been in default and has not completed the Probation Period (following new definition of default guidelines).

Everything that is more than 90 days past due is classified as non-performing financial asset under stage 3. For assets without days past due where there is a well-founded reason to believe the asset is unlikely to pay in the future (for instance, a bankruptcy or fraud), the asset can also be classified as Stage 3 for reasons other than days past due. LLR for non-performing financial assets classified as "stage 3" is also based on lifetime expected credit losses.

Credit rating is one of the risk characteristics, as suggested in the IFRS9 guideline, for determining loan loss provisioning. During the lifetime of a customer loan, behaviour scores are directly translated to a corresponding PD, which is used as the key factor to identify any credit risk deterioration and thereby migration to stage 2 or 3. The Bank will compare the initial behaviour score of the customer at origination with the monthly updated behaviour score. Based on empirical data, a reduction in score below a defined threshold which is considered as significant change in credit risk, will trigger a change in staging.

IRB Parameters

In order to measure the credit risk of an exposure for capital requirement purposes, Expected Loss and Unexpected Loss needs to be determined. Unexpected Loss relates to the very high but improbable level of losses not considered recurring but must be absorbed by capital. For expected loss, SCB determines Probability of Default, Loss Given Default, and Exposure at Default in order to derive at the exposure's Expected Loss. If IRB Expected Loss is higher than the Expected Credit Loss (ECL) calculated for loan loss reseverve purposes, this shortfall has to be deducted from CET1 capital when reporting capital ratios.

- Probability of Default (PD): probability that a given customer will default on their credit exposure within the next 12 months. The PD used for regulatory capital is Through-the-Cycle (TTC) i.e., long term. A default is deemed to have occurred when either there exists reasonable doubt whether there will be a repayment or when a customer is more than 90 days past due on their credit obligation. Defaulted exposures are automatically assigned a PD of 100%. Calculation of PD is done based on the Bank's historical information.
- Loss Given Default (LGD): indicates how much the Bank expects to lose in the event of a default. For the purpose of regulatory capital, LGD is calculated based on a downturn economic cycle. In the calculation for LGD, customer collateral, future cash flows and other relevant factors are incorporated.
- Exposure at Default (EAD): the value of debt at the time of default.

The parameters and associated metrics include Expected and Unexpected Loss and are to be used not only for regulatory purposes but also for internal credit risk management. In SCB, the internal credit risk parameter estimates are used in a verity of management tools, including pre-classifications, profitability calculations (Return on Risk Weighted Asset), stress testing, and scenario analyses. The results are subsequently reported to senior management through various internal committees.

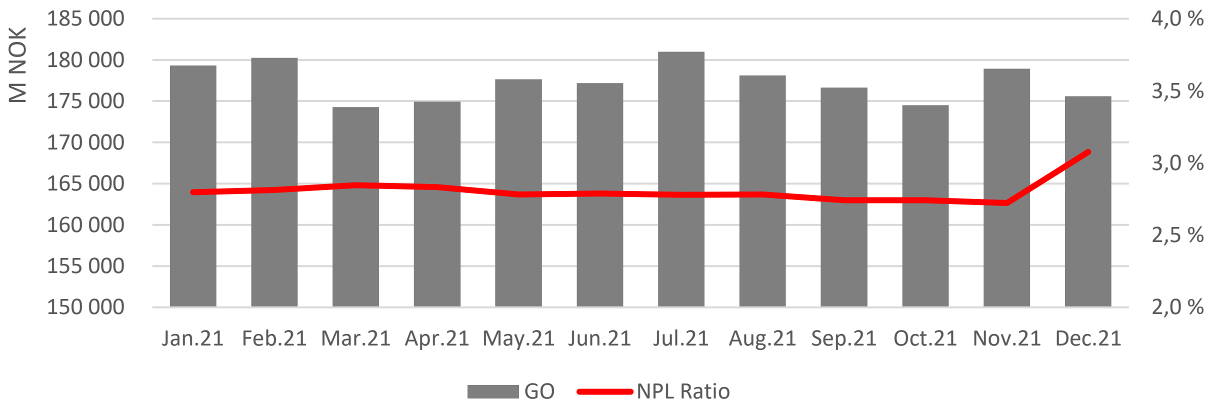
6.7 SCB Credit Performance

Non-Performing Loans

Non-performing loans ("NPLs") are loans where customer payments are more than 90 days past due (DPD) or are classified as non-performing due to other criteria and not written off. The NPL ratio is the amount of NPL relative to gross outstanding loans and provides a good indication of the development of the credit risk in the portfolio. Note however that changes in the NPL-ratio may be triggered by other factors than the underlying credit risk. The change in write-off policy in 2018 and 2019 has contributd to an increase in NPL-ratio together with the change to new default definition (NDD) for loan loss reserve calculations in December 2021.

The figures below show the 2021 evolution of total gross outstanding exposure (in MNOK) and NPL ratio at consolidated level. As can be seen, the NPL ratio has remained relatively stable ranging from 2.7% to 3.1%. Good risk performance in 2021 led to a steady decline in NPL ratio throughout the year until December, where the Bank implemented the more stringent European Banking Authority's NDD, which led to a 35 bps. increase in the NPL ratio.

Figure 6.7.1: Gross Outstanding Loans vs. NPL



The tables below show the development in the NPL ratio, divided into the secured (auto) and the unsecured portfolio, during 2019, 2020 and 2021. From December 2019 until December 2021, the NPL ratio increased for the unsecured portfolio mainly due to changes in the write-off policy. In Q4 2018, SCB's Board of Directors approved a change in write-off policy for its unsecured portfolios in Sweden, Denmark, and Finland. In Q2 2019, the Board approved the same policy for Norway (both secured and unsecured). The revised policy dictates that, in order for an exposure to be written-off, it must meet the criteria of being more than 720 days past due (DPD) as opposed to 180 DPD as was previously applicable. The rationale for the change is to ensure that the exposures are written off once the Bank has no reasonable expectation of recovering a financial asset in its entirety or a portion thereof and is aligned with IFRS9 requirements. The impact of the change in write-off policy for the Bank is an increase in NPL exposures for the unsecured portfolios. Further, the implementation of EBA's New default definition leads to the increase in NPL ratio in Dec. 21.

Table 6.7.1: NPL Ratio Developments per Type of Portfolio

NPL ratio	Dec-19	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
Secured	1,32%	1,34%	1,37%	1,26%	1,23%	1,62%
Unsecured	7,21%	8,30%	8,90%	9,26%	9,27%	9,63%
Nordic	***2,61%***	***2,73%***	***2,85%***	***2,78%***	***2,73%***	***3,08%***

The table below shows the NPL ratio development for the same period per country, indicating a good loan quality in all countries. Norway has the highest NPL ratio, mainly due to a higher share of credit cards than in the other countries.

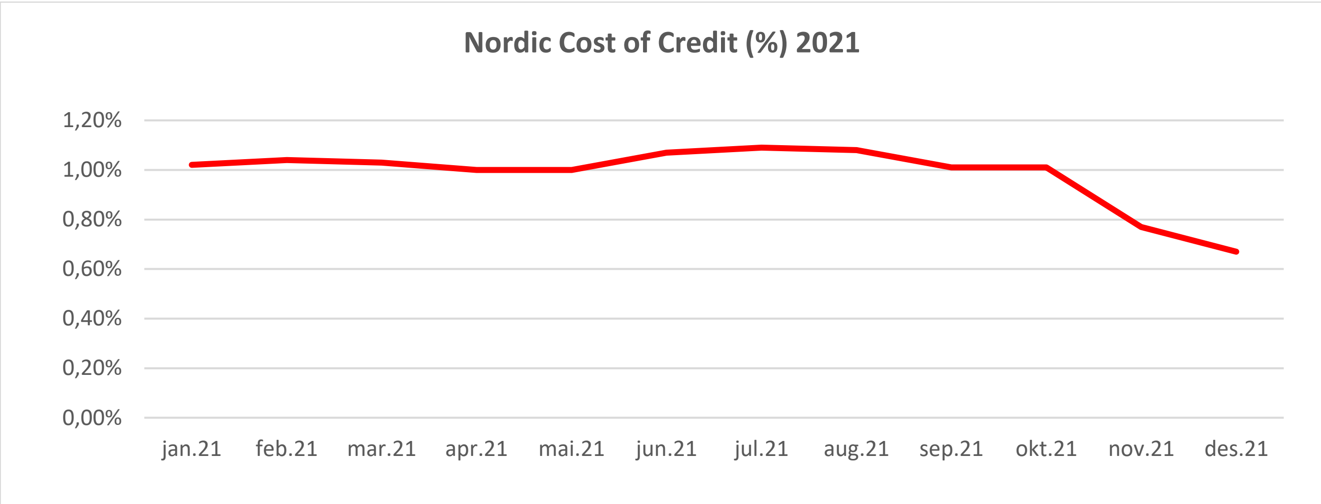
Table 6.7.2: NPL Ratio Developments per Country

NPL ratio	Dec-19	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
Denmark	2,68%	2,90%	2,86%	2,65%	2,44%	2,58%
Finland	1,35%	1,68%	1,87%	1,90%	1,88%	2,65%
Norway	3,74%	3,78%	3,77%	3,58%	3,56%	3,78%
Sweden	2,01%	2,17%	2,45%	2,58%	2,70%	2,87%
Nordic	***2,61%***	***2,73%***	***2,85%***	***2,78%***	***2,73%***	***3,08%***

Cost of Credit

Cost of Credit is defined as the ratio of 12 months Loan Loss Provisions to the average 12 months gross outstanding. Cost of Credit is an important metric to consider as it identifies the running loss rates the Bank has at a point in time. The ratio considers the changes in IFRS9 expected losses, loans that get written off, as well as written off assets that recover. The cost of credit is closely monitored and is part of SCB's risk appetite statement. Note however that this metric will typically be improved with bad debt sales (BDS), which are assets that are written off, or NPL sales.

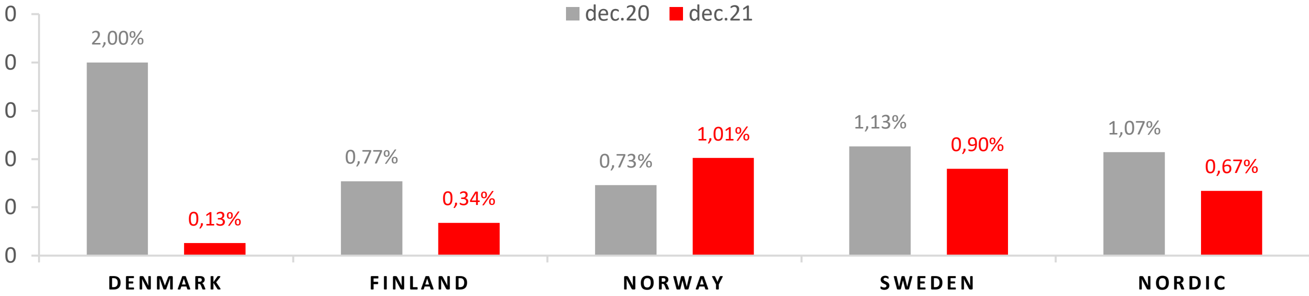
Figure 6.7.2: Cost of Credit development 2021



The Figure above demonstrates SCB's favourable development related to loan losses throughout 2021. The main explanation for the improvement in Cost of Credit during November 2021 is driven by a bad debt sale where SCB sold written off assets to third party collection agencies. December drops further as SCB decreased its IFRS9 model overlays. The COVID reserves overlay of MNOK 408 that was booked at the end of 2020 was replaced by new overlays and reduced to MNOK 188 as of December 2021. The new overlays are meant to reflect potential losses related to customers that was granted payment holidays during COVID and "post-COVID" macroeconomic forward-looking factors. Payment holidays (PH) reserves are booked to cover the increased risk of future potential losses for customers that cannot make upcoming payments after the PH expired. The macroeconomic forwards-looking factors scenario refers to the overall worsening of the macroeconomic indicators that lead to increased losses.

The graph below provides a country breakdown of cost of credit. Solid performance for the year is driven by product mix with strong growth in Auto and better repayment rates driven by improved credit quality in 2021 when customer repayment was abnormally good. Denmark has had the biggest improvement, which is caused mainly by better performance and higher repayment rates. Additionally, we had IFRS9 overlay reductions, as well as a IFRS9 parameter update which had a beneficial impact for Denmark 2021, whereas it had a negative impact for 2020.

Figure 6.7.3: Cost of Credit per Country (%)



SCB's Cost of Credit as per December '21 was equal to 0.67% corresponding to a 1.2 BNOK in Loan Loss Provisions. The latter, once compared with the Gross Margin generated through 2021 (7.4 BNOK) returns a solid credit loss absorption ratio of 6.3.

6.8 SCB Credit Risk under A-IRB Approach

Approved IRB portfolios

In December 2015, SCB received approval from the Bank of Spain and the Norwegian FSA to use the IRB approach for the portfolios referred to as "Wave 1", which includes Auto Private Person (Auto PP) portfolios in Norway, Finland, and Sweden. Auto PP in Norway, Sweden and Finland represent the biggest portfolios in their respective countries. According to European Banking Authority's (EBA) regulation, the new default definition (NDD) was implemented for IRB portfolios as of November 2020, while the remaining portfolios adopted the NDD for capital purposes in January 2021. The NDD, combined with other regulatory requirements, has triggered a need to recalibrate the IRB parameters. New IRB models, considering among others the NDD and a new admission scorecard for the Swedish portfolio, were submitted to the ECB/FSA for regulatory approval in July 2021.

The figure below displays the EAD, Risk Weighted Assets, and risk weights of the existing IRB portfolios (the "Wave-1 portfolios"). During 2021 an upward trend was observed for the EAD, RWA and RW of these portfolios. The deterioration of the risk weight for Wave 1 is due to an increase in the Norwegian and Finnish Auto PP risk weight, caused by an increase in the PD of the before mentioned portfolios.

Figure 6.8.1: EAD, RWA and Average RW

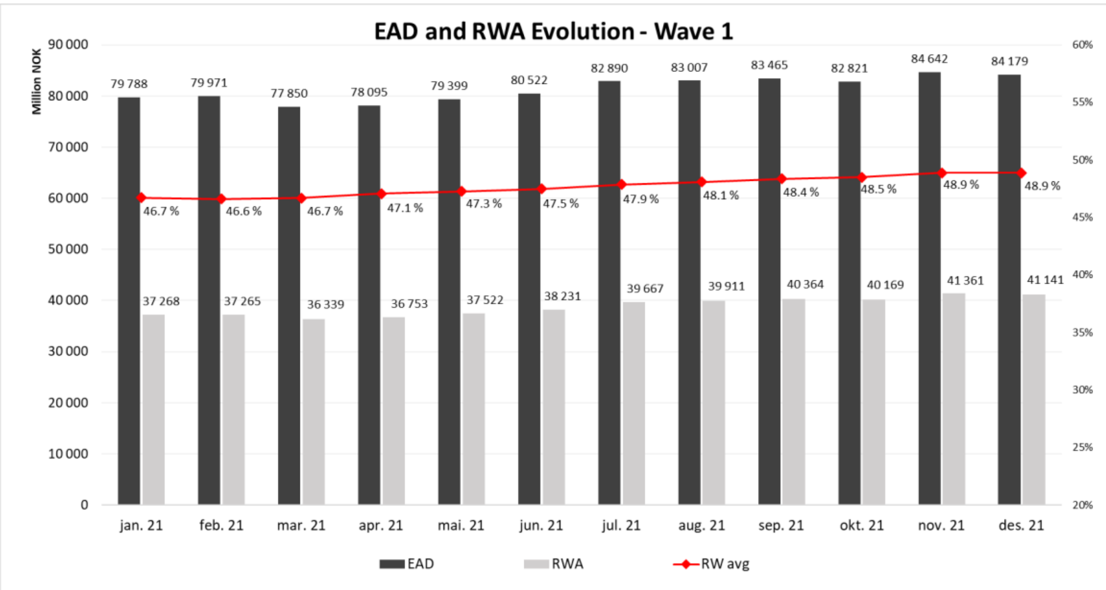


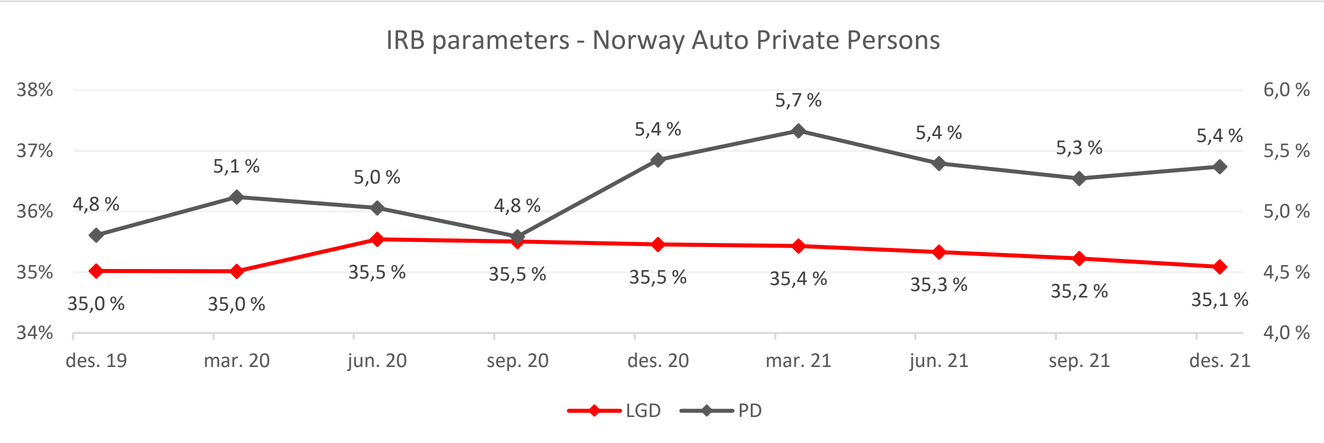
Table 6.8.1 below provides RWA and parameter details (data as of Dec 2021) for all Wave 1 portfolios currently under the IRB approach. This follows a quantitative study suggested by the Basel Committee on Banking Supervision (BCBS) in table CR9 of the document 'Revised Pillar 3 disclosure requirements', of January 2015. Since SCB IRB portfolios consist of instalment loans without any assigned credit limit, the columns for credit conversion factor (CCF) have not been reported.

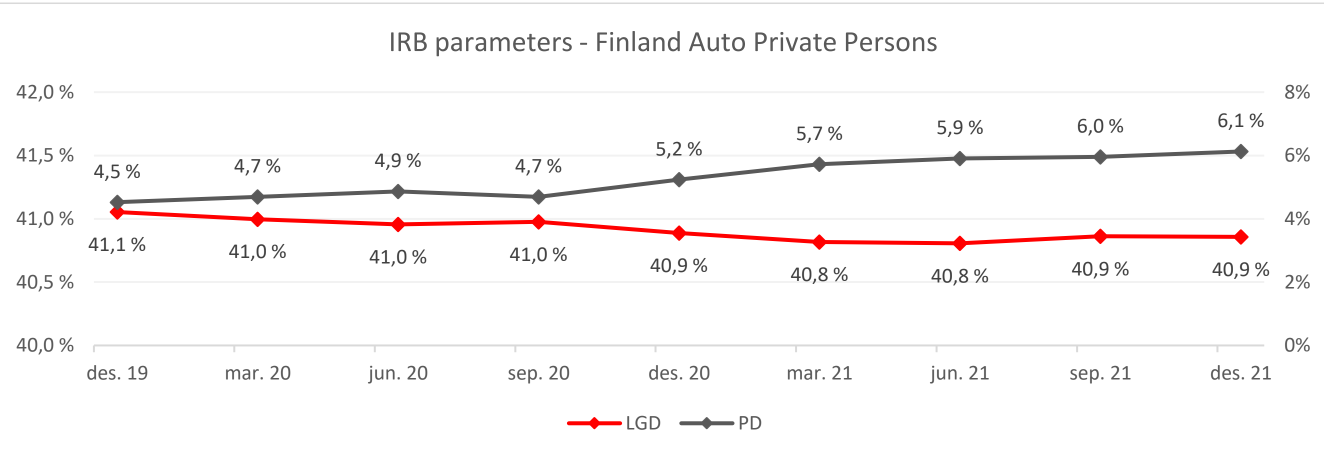
Table 6.8.1: Parameter Details for IRB portfolios as at 31 December 2021

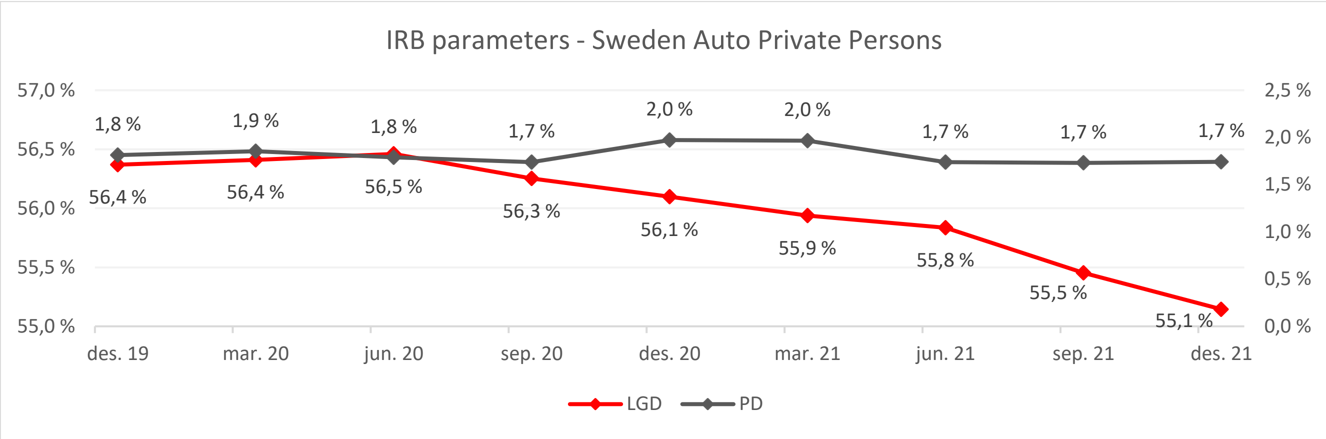
PD_Bucket	EAD	Average PD	Average LGD	# Obligors	Average Maturity	RWA	RW	EL	Provisions
[0.25-0.50]	6 791 518 736	0.26%	38.3%	40 924	3.34	1 215 922 419	17.9%	6 209 989	24 048 579
[0.50-0.75]	6 533 303 955	0.63%	36.8%	43 519	3.16	1 952 099 434	29.9%	14 289 231	32 586 669
[0.75-2.50]	55 559 568 258	1.26%	46.0%	344 426	3.25	27 233 592 177	49.0%	300 085 454	337 290 427
[2.50-10.00]	8 775 458 003	4.18%	49.1%	64 132	3.14	6 147 444 609	70.1%	170 022 651	68 442 791
[10.00-100]	5 020 586 659	24.38%	39.2%	31 804	3.34	4 394 386 907	87.5%	442 583 803	195 369 806
PD 100	1 498 195 145	100.00%	40.1%	12 449	2.52	198 053 076	13.2%	561 113 330	500 898 453
Total	84 178 630 756	4.57%	44.5%	537 254	3.23	41 141 498 622	48.9%	1 494 304 459	1 158 636 726

Figure 6.8.4 below outlines the LGD, and PD evolution separated per country. The increase in November 2020 is explained by the shift from ODD to NDD.

Figure 6.8.4: LGD and PD evolution for IRB portfolios as of December 2021



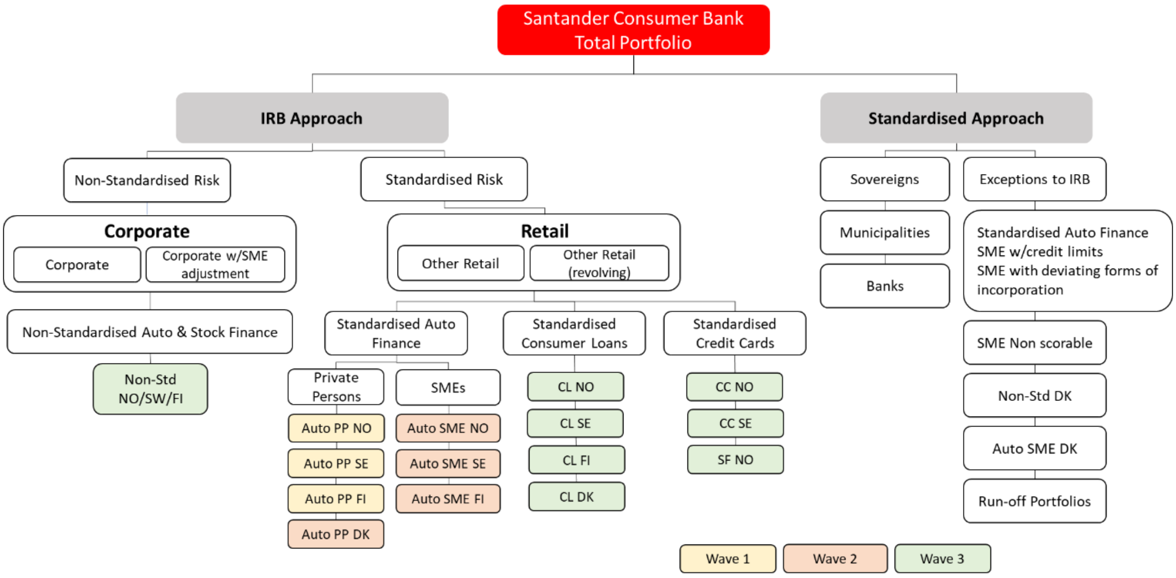




IRB Roll-Out Plan

The figure below provides an overview of the Basel II approach by segments and what portfolios the Bank plans to have under the IRB approach and the Standard approach going forward. As can be seen from the figure, some portfolios will remain under the standard approach based on the underlying obligor and the materiality of the portfolio as agreed with the regulator.

Figure 6.8.2: SCB Portfolios by Basel Approach



The new IRB rollout calendar is displayed in figure below. As mentioned, new IRB models, considering among others the NDD and a new admission scorecard for the Swedish portfolio, were submitted to the ECB/FSA for regulatory approval in July 2021. According to the roll-out plan approved by the BoD, the next wave of portfolios, "Wave 2", is planned to be submitted to the regulator Q2 2023 and then finally "Wave 3" in 2025. This will however depend on when the Bank receives feedback from the regulator on the model submission for Wave 1. The approved methodology used for Wave 1 portfolios, will provide guidance for the methodology used for Wave 2.

Figure 6.8.3: IRB Rollout Calendar

IRB Regulatory Limits

To measure any significant variations within the portfolios and ensure their stability, management and regulatory limits are established on key risk performance indicators every year per country and product. These limits are reviewed by and shared with relevant stakeholders (i.e., Modelling team, Internal Validation team, model owners and portfolio managers) monthly, with any point of attention clarified and managed if necessary. The limits are established every year based on historical performance and the Budget for that year. Limits are set for all dimensions including new business volume and existing portfolio outstanding. For ICAAP risk assessment purpose, only risk indicators have been shown.

For regulatory limits for the IRB portfolios, all but one KPI are within pre-established limits set by the Board as of December 2021. This relates to a slight deterioration in the metric "portfolio worsening" which was observed for the Norwegian and Finnish Auto Private Persons portfolios. It is worth noting that these limits were based on the old default definition (ODD) while the current production models are using the new default definitions (NDD). These limits have been revised during Q1 2022 to capture the NDD. The portfolio worsening is being monitored in the relevant reports to management and committees.

Credit Risk Mitigation

In the regulatory capital calculation, credit risk mitigation techniques affect the value of the risk parameters used for the calculation of capital. The identification and valuation of the collateral and/or guarantees associated with the contracts is essential. This process of mitigation is undertaken provided that the validity of the collateral and/or guarantee has been checked and they are considered eligible to be applied. Under the IRB approach, the presence of collateral impacts on the final value of the LGD used in the calculation of capital.

For LGD estimations on its IRB portfolios, SCB uses vehicles pledged as collaterals in form of other physical collaterals following the requirements specified under CRR article 199.1(c).

IRB Model Governance

A fundamental part of the process implementing A-IRB models is to establish robust control and review mechanisms by Internal Validation and Internal Audit. This to ensure effective monitoring, validation and documentation of the capital models and their integration into risk management. The governance model involves different levels of control structured around three lines of defence with an organizational structure and independent, clearly defined functions:

- Model owners, model developers and model users have responsibility for the primary management of model risk arising from their activities. These functions belong to stakeholders within SCB.
- Internal validation team (IVT) is responsible to validate and provide an independent opinion on a model. The validation function belongs to Santander Group, and is not part of SCB, ensuring its independence from model development.
- Model Risk Control function comprehensively oversees, controls the model risk management processes and monitors model risk in the Bank. This function is part of SCB.

Figure 6.8.3: Model Risk Roles

This governance model meets the regulatory requirements for IRB models:

1. Existence of a strong governance model.
2. Existence, separation and independence of the Risk Control and Supervision, Internal Validation, and Internal Audit areas.
3. Independent annual reviews by Internal Validation and Internal Audit (also at Banco Santander level)
4. Communication processes with Management which ensure all associated risks are reported.

Model Validation

Independent validation of models before implementation is not only a regulatory requirement in certain cases, but also a key feature for proper management and control of model risk. Within the Santander Group, a specialist unit outside SCB, completely independent of both model developers and users, draws up a technical opinion of the suitability of internal models to their purposes, and sets out conclusions concerning their robustness, utility, and effectiveness (initial validation). The intensity varies depending on the model tier, importance of the modification and it is higher, aligned with regulatory requirements, when the model is used for regulatory capital estimation. The validation function also performs recurrent validation after the models are in use. The frequency and depth[5] are also based on the importance of the model and considers regulatory requirements[6] in the case of the IRB rating system.

During validation, 5 different dimensions of the model are assessed, including data, IT environment, model foundations, model performance and use, and governance. The validation opinion for each dimension and overall, for the model is detailed in a validation report and summarized in the Model Risk Rating (MRR) of the model on a scale of 1 to 5, where 1 is low model risk, 2 is moderate-low, 3 is moderate, 4 is moderate high and 5 is high. In addition to the model risk rating (MRR), the validation function issues recommendations, tied to model weaknesses, categorized by relevance and relative impact on model risk implied by the model. They are followed up on a regular basis by the model risk function and model owners to ensure action plans are set and fulfilled.

Once the validation is finished, a consistency check is carried out to provide homogeneity and consistency to the validation process and outcome. Through this process, the validation conclusions are challenged by a different group of validators.

Model Monitoring

A model is designed and built based on certain information and circumstances, which may change over time. Models are subject to regular performance monitoring to ensure they are functioning correctly. Because of the monitoring, the model may be modified or retired (decommissioned).

The model owner and model developer are responsible for monitoring model performance according to corporate standards including measures of stability, calibration, and performance. The frequency of monitoring will vary depending on model uses, data availability and other factors. The monitoring results are presented to the relevant governance bodies.

Back-testing of IRB parameters

To manage model risk for the PD's and LGD's used for capital requirement calculation, SCB group has set up validation processes to monitor the quality of the models on an ongoing basis. Back-testing is a key quantitative validation tool in which predicted PD's and LGD's are compared with observed PD's and LGD's. Timely detection of inadequate performance of the

[5] Depth of validation refers to the rigour with which the validation is conducted, i.e., with regulatory models a more thorough validation is done, which is referred to as "enhanced validation"

[6] Delegated Regulation (EU) No 575/2013, Article 185 (b)

PD's and LGD's is crucial since they are used in the capital requirement calculation, and back-testing is thus conducted on a regular basis.

SCB has a comprehensive back-testing framework to test the IRB parameters validity on a quarterly basis. The aim of the PD back-test is to compare the regulatory PD (PD TTC) used for calculating capital requirements with actual Oberseved Default Ratetime (ODF). The purpose of this exercise is to assess the predictive power of the IRB models.

The regulatory PD is a through-the-cycle (TTC) PD, i.e., a long-term average that is not tied to any particular point in the cycle. However, the observed default frequency (ODF) is determined at a given point in time (2021). Given their different characteristics, the comparison between the two figures does not constitute a precise control of the regulatory PD, but it does serve to assess the size of the cyclical adjustment used in the calculation of the regulatory (TTC) PD.

For each portfolio, regulatory PD buckets, representing different PD levels, are established, which is done both to PDs resulting from Admission Score (ADM PDs) and from the Behaviour Score (BEH PDs). For each of these, the average TTC PD assigned is compared with the observed default frequency (ODF). To observe defaults, outstanding loans that were not in default at a reference date are selected, and the rate of new defaults among these outstanding loans over the subsequent 12-month period is observed.

TTC PDis compared with the ODF, which is influenced by cyclicality. The graphs below illustrate that the TTC PD is higher than the ODF for the vast majority of rating categories; nonetheless, the model's performance has deteriorated during the last year as the models were developed with a sample using ODD while the NDD has already been incorporated since November 2020. This issue has been approached in the new models submitted to regulators during 2021. In the graphs below, the labels on the x-axis represent the score buckets (i.e., BS 6 = Behavior score bucket 6). Higher buckets are associated with higher scores and the higher the contract's score the lower its PD.

Figure 6.8.5: Norway A-IRB: Observed default frequency by PD bucket and PD rate (for admission and behaviour score)

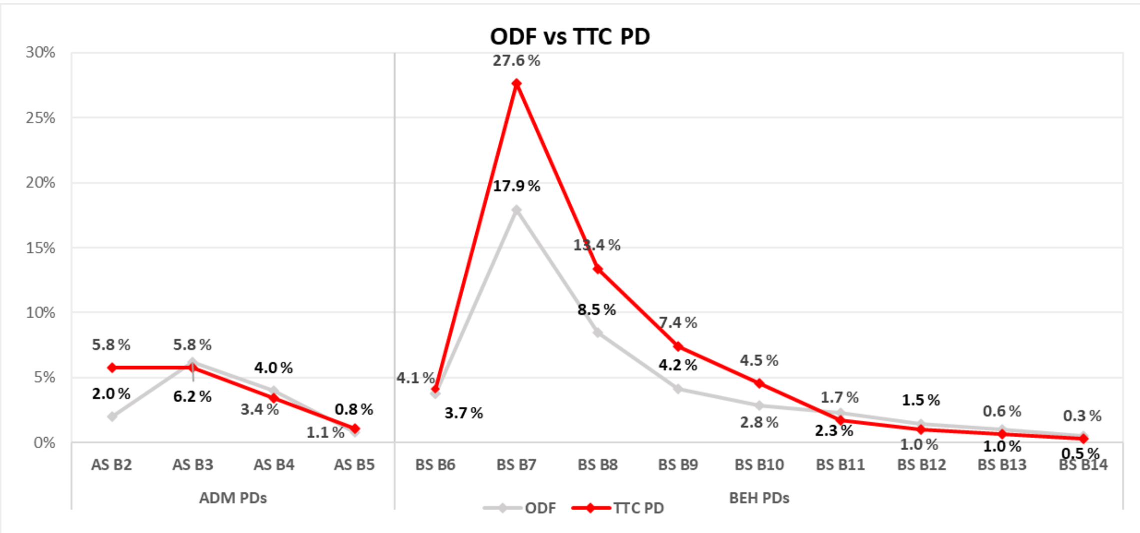


Figure 6.8.6: Finland A-IRB: Observed default frequency by PD bucket and PD rate (for admission and behaviour score)

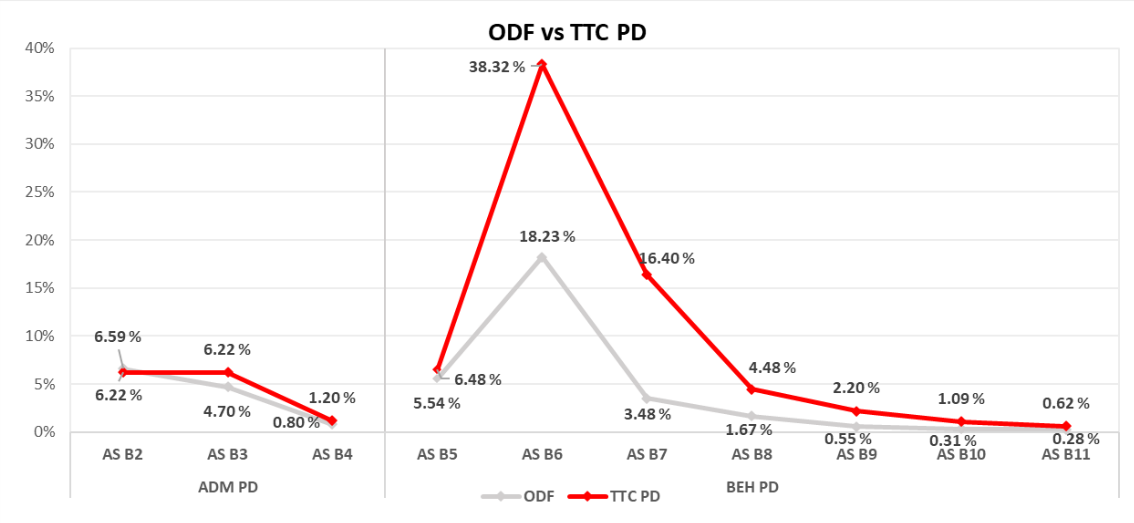


Figure 6.8.7: Sweden A-IRB: Observed default frequency by PD bucket and PD rate (only admission score in use)

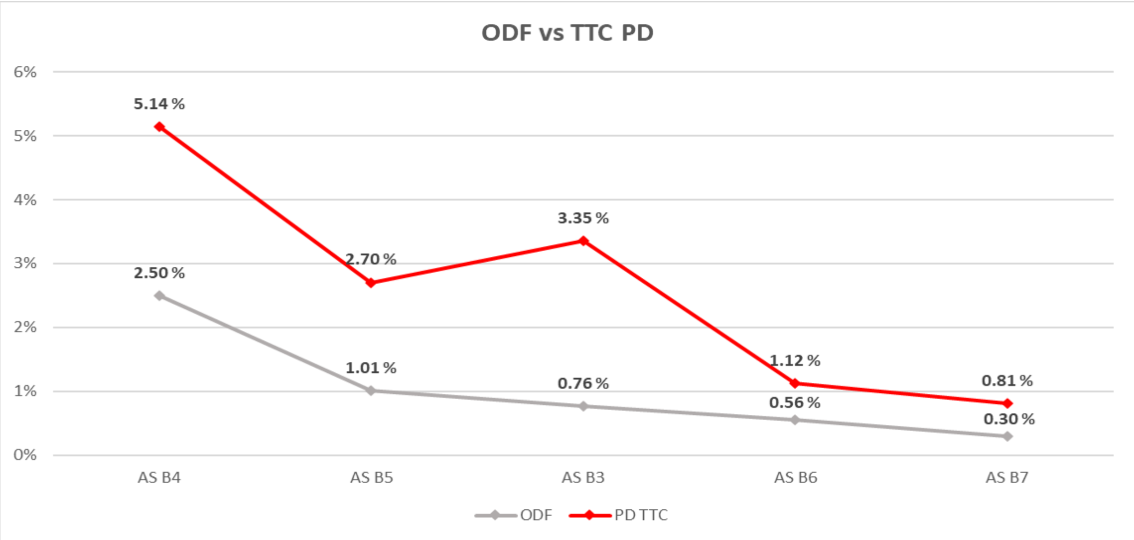


Table 6.8.2 below gives an overview of the back-testing exercise. As can be seen, there is no major difference between the average exposure-weighted PD and the simple average in each bucket, indicating that the different transactions are uniform with regards to exposure. The following columns are divided into two, which contain the number of obligors (or transactions in the case of retail) at two different dates: December 2020 and December 2021. The intention is to detect customers/transactions migrating between PD buckets, though sometimes the migration is due to a recalibration of regulatory models rather than to the dynamics of the rating system. For all models it can be observed that the distribution of obligors has been similar in these 2 years, meaning no significant rating migration and that portfolio quality is stable.

From the back-testing point of view, the average historical default rate is particularly important, as it averages the default rates experienced in each of the past five years for each PD bucket. Comparing this column with columns Weighted average PD (which are the PDs used for calculating capital requirements) and simple average PD, gives an idea of how well our regulatory PD matches the actual experience over the medium term. In general, it is observed that the PD assigned to IRB portfolios for capital requirement is conservative when compared with average defaults over the last 5 years. This observation is in line with economic cycle development in the respective countries.

Table 6.8.2: Back Testing IRB Parameters as of 31 December 2021

des.21	des.21	des.20	des.20-des.21	des.21		des.21	des.21	From 2015 onwards				
PD range	External rating equivalent	Number of obligors			Observed average default rate (%)	Weighted average PD	Arithmetic average PD by obligors	Average historical annual default rate	Number of obligors at end of			
		End of previous year	Defaulted obligors in the year	End of the year					2019	2018	2017	2016
0.00 to < 0.15	**AAA to BBB+**											
0.00 to < 0.10												
0.10 to < 0.15												
0.15 to < 0.25	**BBB+ to BBB**											
0.25 to < 0.50	**BBB to BB+**	55 005	253	40 846	0.46 %	0.26 %	0.26 %	0.31 %	54 833	55 027	55 256	52 639
0.50 to < 0.75	**BB+ to BB**	**63 823**	**514**	**43 477**	**0.81 %**	**0.63 %**	**0.63 %**	**0.55 %**	**67 002**	**65 453**	**60 619**	**56 785**
0.75 to < 2.50	**BB to B+**	**310 449**	**2 311**	**347 051**	**0.74 %**	**1.30 %**	**1.27 %**	**0.56 %**	**311 977**	**302 579**	**262 295**	**227 693**
0.75 to < 1.75		276 889	2 032	297 721	0.74 %	1.16 %	1.11 %	0.56 %	277 346	272 273	238 650	209 433
1.75 to < 2.5		33 560	279	49 330	0.83 %	2.20 %	2.20 %	0.59 %	34 631	30 306	23 645	18 260
2.50 to < 10.00	**B+ to B-**	**71 034**	**2 026**	**65 148**	**2.85 %**	**4.31 %**	**4.22 %**	**2.01 %**	**71 547**	**71 793**	**65 848**	**60 090**
2.5 to < 5.00		48 386	1 001	47 529	2.07 %	3.60 %	3.53 %	1.43 %	49 219	49 000	44 905	42 013
5.00 to < 10.00		22 648	1 025	17 619	4.53 %	6.27 %	6.14 %	3.35 %	22 328	22 793	20 943	18 077
10.00 to < 100.00	**B- to C**	**28 560**	**4 537**	**32 267**	**15.89 %**	**23.01 %**	**24.22 %**	**13.53 %**	**34 100**	**33 219**	**30 499**	**25 378**
10.00 to < 20.00		12 202	1 157	15 839	9.48 %	14.66 %	14.95 %	6.21 %	14 191	14 275	13 157	11 181
20.00 to < 30.00		7 000	1 558	7 913	22.26 %	27.62 %	27.62 %	16.94 %	10 822	10 834	10 786	8 343
30.00 to < 100.00		9 358	1 822	8 515	19.47 %	41.02 %	41.51 %	22.13 %	9 087	8 110	6 556	5 854
100.00 (default)	**D**	**59 294**		**64 932**		**100.00 %**	**100.00 %**	**100.00 %**	**44 116**	**39 213**	**35 518**	**31 280**

7 Market Risk

Market risk is the potential loss of value in assets and liabilities due to changes in the market prices such as foreign exchange and interest rates. SCB's strategy is not to actively assume market risk other than what results directly from the Bank's operations. For SCB, market risk can be split into the following categories:

- Currency risk: risk of loss resulting from changes in foreign exchange rates. The key metric is the open exposure amount in the relevant currencies
- Interest rate risk: risk of loss resulting from changes in interest rates. The key metrics are Net Interest Margin (NIM) and Market Value of Equity (MVE) sensitivities
- Credit spread risk: risk of loss as a result of changes in credit spreads

Market risk is managed by the Financial Management Division and controlled by the Risk Division.

As alluded to above, SCB's strategy is not to take on market risk beyond what results directly from our normal business operations in the four countries where SCB is present. The Bank is exposed to currency risk because it operates in four different countries with different currencies and through its use of international funding markets. The Bank has interest rate risk to the extent there is a mismatch between interest rate exposure on the asset side and liability side. SCB does not have an active trading portfolio or positions in securities and commodities but does possess a liquidity portfolio consisting of High-Quality Liquid Assets (HQLAs) where the intention is to hold the bonds to maturity. HQLAs comprises, amongst others, marketable securities backed by sovereigns and central banks and covered bonds.

7.1 Governance of Market Risk

SCB maintains two documents directly relating to Market Risk that are approved by the BoD. These two documents are the Structural Risk Model document and the Liquidity Risk Model, providing a broad overview of all requirements of the Bank's Market Risk organization and governance. Both models are supported by underlying policies and procedures which further details how all processes are structured, and various requirements are fulfilled. In addition, the Risk Appetite Model forms the foundation of the Bank's Market Risk limit structure.

The Bank maintains a balance sheet composition that ensures that the market risk is managed at prudent levels and within established limits, as detailed in the Liquidity and Market Risk Policy.

SCB's Risk Appetite statement (RAS) contains the Bank's risk appetite limits for Market Risk. In addition, the Bank has a set of Management limits, subject to annual review and approval, which encompasses more metrics and stricter limits than the RAS. All limits are monitored by internal committees.

7.2 Currency Risk

SCB operates in four countries – Norway, Sweden, Denmark, and Finland - with four different currencies. The Bank is to strive for a composition of the balance sheet that minimizes currency risk by ensuring that the assets and liabilities are primarily denominated in the same currency. When raising funding such as Euro Medium Term Notes ("EMTN") or Asset Backed Securities ("ABS") through international debt markets, the Bank closes any open position through the use of derivatives.

The Banks routines ensure that the currency exposure is continuously monitored and controlled. The Bank operates with management limits for currency risk. The limits are set for each currency and for the total foreign currency exposure; both for SCB AS and SCB Group, which is subject to regularly internal review and approval. Per December 2021, the Bank had a net EUR position of the equivalent of 2 485 million NOK. The EUR position mainly stems from net assets built up through retained earnings in the Finnish subsidiary, SCF Oy.

The Bank has with the growth in assets in the countries outside Norway, seen how the capital ratios are sensitive to fluctuations in the FX rate between NOK and SEK, DKK, and EUR. While most of the equity of the Bank is in NOK, risk weighted assets (RWA) are distributed across all the four currencies. This means that if NOK depreciates, the RWA will increase without a subsequent increase in capital, thus reducing capital ratios. In orer to mitigate this risk, the Bank has approved a strategy where the Bank intentionally increases the exposure in EUR in order to reduce capital ratio volatility. The implementation of the full strategy is however subject to approval by the Norwegain FSA to except such EUR exposure from capital requirements under CRR Article 352 (2). The application for such exception was submitted to the Norwegain FSA in 2021 but has not yet been approved.

7.3 Interest Rate Risk

Interest rate risk is the risk of reduced earnings or reduction in the economic value of the equity due to changes in market interest rates. SCB aims to achieve a balance sheet composition that minimizes the interest rate risk by balancing the total weighted interest term for both assets and liabilities. The Bank is only exposed to interest rate risk that follows directly from the Bank's operations, as does not actively take on interest rate risk.

The strategy of managing interest rate risk involves the use of variable/ fixed rate intragroup loans, interest rate derivatives and variable/fixed rate customer deposits. The interest rate gap positions for all significant currencies are monitored and reported monthly. The Bank also calculates the six interest rate risk scenarios as described by the Basel committee for interest rate risk in the banking book (IRRBB). In addition, a sensitivity analysis and a forecast of future interest rate risk is performed.

The Financial Management department (risk taker) proposes interest rate risk limits to the Risk department, which assesses the proposal and submits it to the BoD for final approval. Limits must be reviewed annually for each of the following metrics:

- Net Interest Margin (NIM) sensitivity: The sensitivity of the NIM is a measure of the difference between the return on assets and the financial cost of the liabilities over a 12-month horizon. The impact is measured as the worst effect on NIM of +/-25, 50, 75, 100 and 200 bps parallel movement in the interest rate curves
- Economic Value or Market Value of Equity (MVE) sensitivity: The sensitivity of MVE is a measure, which complements the sensitivity of NIM. It measures the implicit interest rate risk in the MVE from a variation in interest rates (worst of +/-25, 50, 75, 100 and 200 bps parallel movement in the interest rate curves) on the Bank's financial assets and liabilities.

The interest rate is calculated by distributing all interest rate sensitive assets and liabilities into tenor buckets and then calculating the MVE and NIM sensitivities. The assets and liabilities are assigned re-pricing maturities following certain assumptions that are regularly reviewed. The assumptions include the behavioural aspects of non-maturity deposits that do not have contractual maturity and the re-pricing criteria of the loan portfolio that are contractually neither fixed nor floating rate products. The repricing distribution for non-maturity deposits is based on a runoff assumption (exponential distribution), whose parameters are estimated based on historical deposits data. For the loan portfolio, the repricing distribution is based on a prepayment model, which is governed by a Constant Prepayment Rate, estimated by each business unit.

The table below shows the NIM and MVE sensitivities per currency per year-end 2021.The table shows for example that for NIM sensitivity for NOK, a 200bps parallel shift upwards for the interest rate curve, would improve the NIM with MNOK 317, while a 200bps parallel shift downwards would reduce the Bank's NIM with MNOK 335, measured per 31.12.20021. For the MVE sensitivity for NOK on the other side, we can see that a 200bps parallel shift upwards would reduce the equity of the Bank with MNOK 226, while a 200bps parallel shift downwards would increase the Bank's equity with MNOK 218, measured per 31.12.2021. With more interest rate sensitive assets than interest rate sensitive liabilities, an interest rate increase in Norway is expected to improve the Bank's gross margin and hence the NIM. For MVE sensitivity, the interest curve is used to discount future cash flows frome asset and liabilities. With increased interest rates, present cash flows will decrease. Since a higher percentage of assets than liabilities are interest rate sensitive, the net impact is a negative effect on the Bank's equity.

Table 7.3.1: Interest Rate Risk per December 2021

Interest Rate Shock Bps	+200	+100	+75	+50	+25	-25	-50	-75	-100	-200
NIM Sensitivity per 31.12.2021, million NOK										
Exposure in NOK	317	159	120	80	40	-40	-80	-121	-161	-335
Exposure in SEK	-102	-52	-38	-25	-13	12	25	33	29	-134
Exposure in DKK	54	19	15	20	-30	9	-1	-13	-25	-74
Exposure in EUR	-27	-14	-10	-7	-3	5	4	-20	-46	-183

Interest Rate Shock Bps	+200	+100	+75	+50	+25	-25	-50	-75	-100	-200
MVE Sensitivity per 31.12.2021, million NOK										
Exposure in NOK	-226	-113	-85	-56	-28	28	56	84	112	218
Exposure in SEK	-153	-70	-62	-41	-21	21	42	63	96	-19
Exposure in DKK	435	257	211	166	-41	31	43	51	53	-245
Exposure in EUR	213	113	86	58	29	-30	-62	-94	-127	-270

7.4 Credit Spread Risk

Credit spread risk is defined as the risk of changes in market value of securities or any credit derivatives resulting from an overall change in credit spreads. SCB's strategy is not to take on any credit risk in excess of what follows directly from the operations of the Bank. The value of the liquidity bond portfolio per 31 December 2021 was 10 631 million NOK.

Credit spread risk in the bank is managed through strict policy mandates setting the structure of our liquidity bond portfolio. Only the highest quality bonds are allowed with maturities of up to 1 year for fixed rate bonds and 3 years for floating rate bonds. The bond portfolio is also classified as "Hold to collect" following the IFRS9 definitions which means that SCB is holding the bond portfolio to maturity and not making profit or loss from market changes. This results in a very low and stable credit spread risk, defined as non-material. The Bank monitors the credit spread risk on a weekly basis by monitoring changes in the market value of the bond portfolio but has not established limits towards it based on a low materiality. SCB believes this is covered by LCR limits and liquidity stress test limits; should the credit spread risk materialize, it will decrease the value of the bond portfolio for the LCR and liquidity stress test horizon calculation.

7.5 Capital Requirements for Market Risk

The Bank's market risk capital requirements are calculated in accordance with capital adequacy regulations under CRD IV and CRR regulations. The approach to calculate market risk regulatory capital can be either the internal model approach or the standardized approach. SCB reports according to the standardized approach for market risk. The table below outlines SCB's Pillar 1 for market risk over the previous three financial years.

Table 7.5.1: SCB Group Pillar 1 for Market Risk (million NOK)

SCB Pillar 1 Market Risk	2019	2020	2021
Currency Risk	117	198	215
CVA Risk	2	4	2
Total	119	202	217

The capital requirement for currency risk for 2021 was 215 million NOK due to the total net currency position exceeding 2% of total own funds. The net currency position mainly derives from equity position in the Finnish subsidiary SCF Oy. CVA risk is minimal due to the net mark-to-market value of derivates and thus results in a minor Pillar 1 capital charge of 2 million NOK.

8 Exposure to Securitisation Positions

Securitization risk is, for SCB, defined as a reversal of capital relief obtained through securitization, which would result in an immediate and substantial increase in required capital.

To date none of the securitization transactions executed by SCB and its subsidiaries has resulted in a reduction in capital for SCB[7]. The intention of the securitization programs has been primarily to provide access to the international debt capital markets and potentially to access the liquidity provided by Central Banks to ensure functional credit and money markets.

Securitization programs have been implemented across the four Nordic units over the past nine years and serve as an integral part of the Bank's funding strategy. The Bank has completed 20 securitization funding transactions: seven transactions with Norwegian collateral, ten from its Finnish subsidiary (including two revolving transactions), two transactions from the Swedish branch (including a warehouse structure) and one from the Danish branch. Total external funding raised equals approximately BNOK 14.5 and BEUR 2.8 (swapped to NOK) from the Norwegian business, BEUR 5.58 from Finland, BSEK 23.3 from Sweden and BDKK 4.2 from Denmark.

Out of the 20 funding transactions completed, 15 have been wound down, with full payment to external investors. SCB closed one transaction in 2021. This was the tenth Kimi transaction out of the Finnish subsidiary and included a 6- month revolving period. The transaction was issued in the public ABS markets.

In June 2019 the Norwegian Ministry of Finance released a consultation paper on the adoption of the new regulations. In December 2020, the Norwegian Ministry of Finance published a proposal to implement the EU Securitisation Regulation into Norwegian law. The proposal was adopted by the Norwegian Parliament on 23 April 2021 and is expected to enter into force once the relevant EU regulations have been implemented in the EEA Agreement. The exact timing of the latter is currently unknown but is likely to occur during 2022. Once adopted, the legislation will align the Norwegian securitisation legal framework with that under which European financial institutions currently operate.

This new regulation will allow Norwegian banks to issue traditional securitizations and obtain capital relief. If implemented, SCB will assess whether it will utilize the new regulation for capital relief at local level. Should SCB utilize capital relief at local level the Bank would reassess the need for any capital relating to the securitization risk.

[7] SCF HQ utilized the significant risk transfer obtained for four transactions launched in 2018 to 2021 to reduce their risk-weighted assets, with a corresponding reduction in capital.

9 Non-Financial Risks

Non-financial risk in the Bank captures risks within the following areas:

- Operational Risk
- Reputational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, and systems or from external events. It includes events that may arise due to legal or regulatory risk, compliance and conduct risk, model risk, vendor, and supplier risk as well as cybersecurity and technology risk.

Reputational risk is defined as the risk of current or potential negative economic due to damage to the perception of the Bank on the part of employees, customers, shareholders/investors, and the wider community.

SCB is currently applying the Basic Indicator Approach for calculating the Bank's capital requirement for operational risk under Pillar I in accordance with the Basel capital adequacy framework.

Non-Financial Risk Development

In addition to continuing monitoring the evolution of the COVID-19 pandemic in 2021, the Bank increased its attention towards aspects with special relevance such as fraud, cybersecurity and vendor risk management as well as continuing monitoring and managing ongoing projects.

At the end of April 2021, five operational risk events with medium crticiality were internally identified and subsequently reported to the Norwegian FSA. The root cause of the events was linked to change management deficiencies identified on the testing and quality assurance before implementation and deployment. Consequently, an improvement initiative was launched and in course with the aim of addressing the identified deficiencies under the close monitoring of management. In 2021, several minior GDPR related events were reported to local data protection authorities.

The Bank's risk culture (RiskPro) is rooted in the principle that "Risk is Everybody's Business", where all employees are responsible for manging the risks they encounter, regardless of their level or role. In 2021, greater efforts were made across the Nordics to boost the RiskPro culture with the re-launch of the "RiskPro-academy" and the establishment of more consistent, frequent and multifaced "RiskPro Communications". Both initiatives aim to ensure that every employee fully understands all the risks the Bank is exposed to and is fully equipped to manage them.

The Bank's operational risk profile remained stable during 2021 and is expected to remain stable within medium-low risk profile in 2022.

9.1 Management process and framework

SCB's non-finanial risk framework aims to ensure that the Bank is operating within the given risk appetite limits and minimize the likelihood and/or reduce the impact of unexpected and adverse events.

The Non-Financial Risk Framework includes the identification and assessment of events inducing lossess as well as consolidation, aggregation, calculation, development of mitigation plans/activities for and the reporting of events that have occurred or could potentially occur. In order to assure that all functions are covered in first line, Operational Risk Coordinators safeguard the operational risk loss reporting process and acts as a promoter for operational risk management within the bank.

Yearly risk assessment processes covering all the Bank's functions allows for 1st line of defence identification and self-assessment of risks and efficiency of controls. The purpose of the yearly risk and control-self assessment (RCSA) is to identify the largest operational risks with associated controls. Conduct risks (Basel IV Client, Product and Business Practices) are assessed in the Conduct Risk Assessment and included in the RCSA process in order to assess the residual risk and is considered in the operational risk's statements. After consolidation and ranking of risks, the outcome is presented in management committees for either acceptance or decisions regarding mitigation actions.

The SCB Non-Financial Risk team is the 2nd line of defence. Its key functions include ensuring that the Bank has in place effective non-financial risk management processes, challenging the operational risk tolerance and monitoring risk limits in the Bank, ensuring that management bodies received overview of all relevant risks, guaranteeing appropriate communication and reporting to Senior Management and the Board of Directors (via the established governance bodies) and helping to analyze operational risks of new products and services.

The internal control framework within SCB is based on the internal control methodology of Grupo Santander, as well as requirements and frameworks set by international and local organizations and regulators. The requirements of The Sarbanes Oxley Act (SOX), the Committee of Sponsoring Organizations of the Treadway Commission Framework (COSO) and the local requirements by Nordic regulators are included in the Santander Internal Control Framework, which in turn sets the foundations for the Internal Control function in SCB and the internal control methodology.

SCB aims to establish and maintain appropriate internal regulations which are designed to mitigate all relevant risks. Internal regulations aim to reflect the way in which risk is managed in the Bank but is also used to encourage evolution of activities towards best practices.

Operational risk limits

To ensure that the Bank operates within the Board approved operational risk limits, and operational risk appetite is set at least annually. The Bank also defines its operational risk loss budgets annually. This is monitored by second line on a monthly basis and its development is monitored by management committees. In addition, the Bank has implemented a number of Operational Risk Indicators across all functions of the Bank. Breach of such indicators are followed up monthly in management committees and depending on criticality, action plans are implemented.

9.2 IT and Technology Risk

The Bank continuously work with improving and developing its management of IT and technology risks during 2021.The aggregate risk level of IT and technology risk in 2021 for the Bank has remained largely unchanged from 2020 considering continued impact of remote mode of working driven by COVID-19 pandemics, coverage for potential extreme cybersecurity related scenarios and internal improvements implemented in the course of the year. This considers especially the improvements made to the Bank's security infrastructure, processes, and knowledge, in the context of the changes to the threat landscape.

Through established metrics, IT and technology risk are measured monthly. These metrics are collected from the first line of defence and validated by the second line of defence and are all associated with thresholds and targets. Any deviations from the targets are followed up on with structured mitigation plans.

9.3 Compliance and Conduct Risk

Compliance Risk is defined as a risk of legal and regulatory sanctions, financial loss or damage to the reputation of the Bank arising from the Bank or its directors, officers and employees not adhering to applicable laws, rules, regulations, and internal policies.

The Bank has adopted the three lines of defence mechanism with first line of defence as responsible for the risk management and control of the compliance risk. To oversee the compliance processes in the Bank and to secure that management and the Board of Directors are provided with independent information regarding the compliance status in the business, SCB has an independent Compliance and Conduct function in second line of defence. The Compliance and Conduct function promote adherence to rules, supervisory requirements, principles of good conduct and values by acting as a second line of defence – establishing standards, challenging, advising, and reporting – in the interest of employees, customers, shareholders, and the wider community. The function performs independent assessments by performing independent risk-based monitoring, controls, testing, and thematic reviews. Annual risk assessment forms the risk-based approach of the Compliance and Conduct function activities, and the prioritizing between the activities is concluded in the Annual Compliance Plan.

The Bank has high focus on ensuring that it is not being used for any illegal activities and that the Bank is complying with, and have focus on, all applicable financial crime regulations and mitigating actions. In 2021, the Bank has continued to improve the financial crime program – the "Financial Crime Prevention Unit" has been transformed into the "Anti-Money Laundering Office," moving activities to Operations to align with risk ownership to further strengthen and clarify the structure, mandates, roles, and responsibilities of the unit. Compliance and Conduct has introduced the AML taxonomy to focus on the financial crime regulations and have re-assessed the Bank's AML control program and rebuilt the existing 2nd line AML Control Framework to better address this area.

The Bank continuously improve and develop the conduct program to ensure that we treat costumers fairly throughout all stages of the customer lifecycle. This includes a "new product approval process" to ensure that the compliance and conduct risk is mitigated in the design and development of new and significantly changed products and services, as well as further development of a product monitoring framework across all products of the Bank.

Compliance with GDPR requirements continues to be a high focus area in the Bank. To improve the GDPR framework and to ensure sufficient resources and knowledge in the business, the Bank has established a Data Privacy Officer in first line of defence. In addition, a new control framework has been implemented within first and second line of defence.

Reputational risk is defined as the risk of current or potential negative economic impact to the Bank due to damage to the perception of the Bank on the part of employees, customers, shareholders/investors, and the wider community. The risk of damage to the reputation of SCB is assessed to be increasing, due to the social media environment, reduced trust in the financial sector and a general focus on ethics and consumer protection. To reflect the growing importance of this risk and its potential damaging impact on the Bank's reputation, a new compliance taxonomy for Reputational risk was created in 2021. Throughout the year significant steps have been taken to lay down the foundations and control mechanisms required to sufficiently enable 2nd line monitoring and oversight of the Reputational risks facing the Bank.

The Group's General Code of Conduct is applicable to all employees and members of the Board and sets the ethics principles and rules of conduct by which all activities of the Group's should be governed, and therefore comprises the central component of the Santander Group's Compliance Programme. All employees are required to complete a mandatory training in the Code of Conduct to ensure proper knowledge and awareness of the ethical principles.

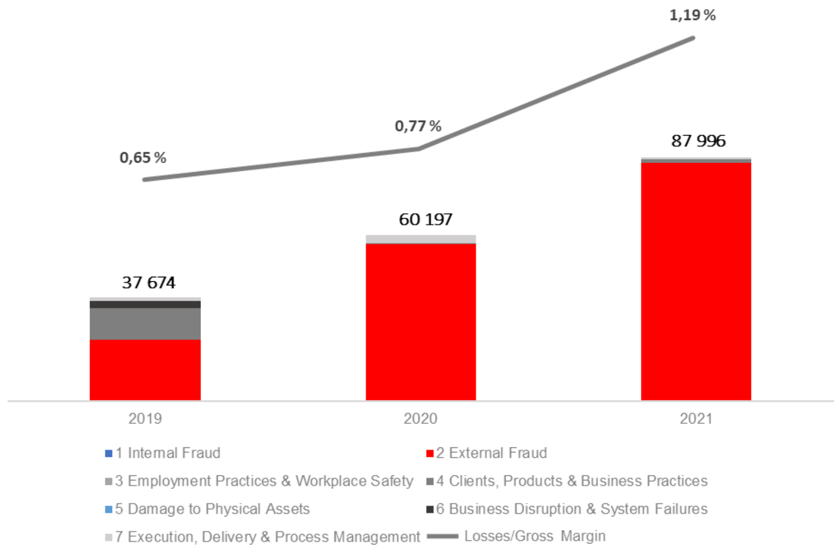
The Group have a digital and secure whistlelowing channel. Reporting should be made on improper conduct that is believed illegal or which violates the Group's Code of Conduct and policies. Employees are free to report their concerns anonymously to the Compliance and Conduct function and employees who report such concerns in good faith are protected from retaliation.

9.4 Operational risk loss Performance in 2021

The Bank held 1 141 million NOK of operational risk capital under Pillar 1 whilst operational losses amounted to 87.9 million NOK in 2021. External fraud events constitute most of the the operational risk losses. The number of detected operational risk events in 2021 has been stable, however total losses increased year-to-year due to update of Bank's write-off policy. Total losses were still within the Bank's Operational risk losses/gross margin risk appetite limit for 2021.

The figure below identified SCB operational losses by category over the three previous years. As can be seen, external fraud accounted for the majority of the operational losses.

Figure 9.4.1: Operational Losses by Basel Category (TNOK)



9.5 Capital Requirements for Non-Financial Risk

SCB applies the Basic Indicator Approach (BIA) for calculating its capital requirement for non-financial risk. Under the BIA, the RWA's for operational risk are calculated as a percentage (alpha) of the three-year average gross income amount multiplied by 12.5. This alpha is given by article 315 (1) of the CRR and is currently 15%. The table below details the Bank's BIA calculation for 2021.

Table 9.5.1: SCB Application of Basic Indicator Approach (NOK million)

Basic Indicator Approach	2019	2020	2021
SCB Gross Margin	7 595	7 816	7 406
3-year average Gross Margin			7 606
15% BIA Capital Charge			1 141
RWA			14 261

10 Liquidity Risk

Liquidity Risk is the risk that an entity becomes unable to meet its obligations as they fall due because of an inability to liquidate assets or obtain adequate funding.

Liquidity risk management in the Bank aims to ensure sufficient funds to support daily operations, a balance between weighted average life of the assets and liabilities, diversified funding sources and sufficient amount of liquidity reserves across all four currencies in order to survive a stress scenario.

The key ratios for assessing liquidity risk are the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR).

LCR is established as a metric to measure short-term liquidity risk. This ratio indicates the short-term resilience of the entity's liquidity risk profile, ensuring that there are sufficient high-quality liquid assets to withstand an event of combined systemic and global stress over a period of 30 calendar days. SCB calculates this ratio on an ongoing basis and reports on a monthly basis according to CRD IV. Since September 2017, the Bank is now also compliant with the change to the specific Norwegian legislations regarding LCR, so to meet the requirements not only on a consolidated level, but also per significant currency. For the Bank the significant currencies are NOK, SEK, DKK and EUR. As at December 31st, 2021, LCR was 144% at consolidated level, 77% in NOK, 208% in SEK, 201% in DKK and 124% in EUR.

NSFR is the long-term funding ratio which compares the structural funding needs to the entity's stable funding sources. This ratio requires the banks to maintain a stable funding profile in relation to the composition of their assets and off-balance sheet activities. From June 2021 onwards SCB started to calculate and report NSFR monthly. From 1 June 2022 a minimum requirement of 100% NSFR will become effective for the Bank with the implementation of "Bankpakken". As of December 31st, 2021, the Bank's NSFR was 110.14%.

10.1 Diversification of Funding Sources

SCB's objective is to maintain a well-diversified funding composition and within that, to reduce its reliance on funding from the parent company. As of December 31st, 2021, the Bank had a self-funding ratio of 81%[8].

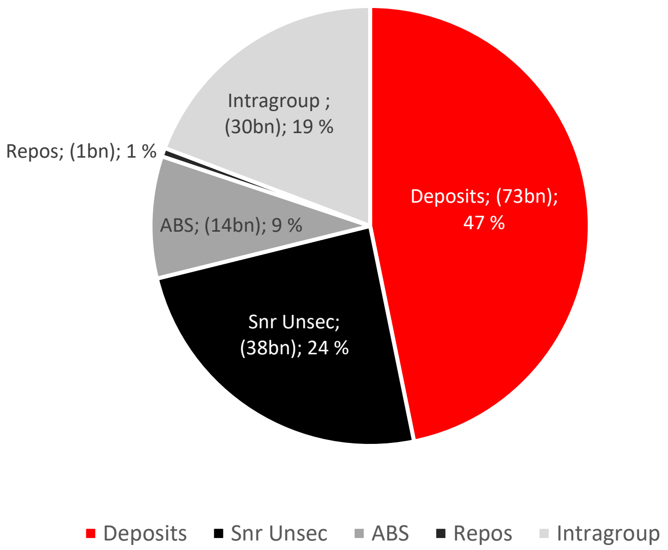
The Bank is raising funds through the following sources:

- Customer deposits in Norway, Sweden, and Denmark. The customer deposit products are demand deposits, fixed rate deposits and notification products
- Secured funding in the Nordic countries (Asset Backed Securities)
- Senior Unsecured funding in the local Nordic markets and in international markets
- Intragroup funding from the parent company
- Repo capabilities with Nordic counterparties

The figure below shows the funding composition on a consolidated Nordic level as of December 31st, 2021.

[8] Calculated as a proportion of senior debt, excluding equity and subordinated debt.

Figure 10.1.1: Funding Composition as of December 31st, 2021 (numbers in NOK)



Recurrent issuer in secured and unsecured debt markets: SCB has continued to issue in NOK, SEK, and EUR Unsecured debt also in 2021, raising 8bn NOK equivalent through these markets. In addition, ABS funding continues to be an important source for SCB, in particular for the subsidiary in Finland where we are a repeat issuer under the KIMI program. The transaction executed in 2021 generated 450 mill EUR in liquidity and a new transaction is planned for 2022.

Customer deposits: following SCB key management principles of promoting stable funding, customer deposits is a strategic funding source for SCB. The bank has in 2021 seen reduction in outstanding balances reflecting reduction in outstanding assets. For 2022, SCB expects to return to growth in deposit base through improved capabilities and new products in the future. SCB has a strategy of asset growth and deposits will be a key source of funding to support this growth.

Self-funding: One of the main pillars of SCB is still to become more independent from SCF for liquidity needs. The Bank ended 2021 with 81% self-funding. The plan is to continue at levels of 80%+, in line with the overall SCF strategy. We believe a high level of self-funding will strengthen not only the Bank, but also the parent bank as less reliance for funding is placed with the Spanish entity. At the moment there is not a goal for full independence from SCF, as it provides a good supplement, in particular for short term funding for SCB.

Short term funding: SCB today mainly relies on its intragroup facilities for its short-term funding. In the end of 2020, the Bank had paid down all of its CPs, as pricing in the local markets has not been attractive in comparison to intragroup funding and as of end of 2021, SCB has not returned to CP markets. However, access to these markets has not been lost despite pause in issuances. Bank has also continued to utilize repo and reverse repo markets for its short-term liquidity management. Repos, CP's and Intragroup will all be important sources of short-term funding in 2022, providing safe and diversified sources of funding for the Bank.

As a final point, SCB is continiously looking to enhance its liquidity management and will under 2022 have a particular focus on the funding structure over the coming years, to ensure a safe and prudent implementation of MREL and NSFR requirements. In addition, the Bank will continue to improve its capabilities in the short-term funding area, utilizing the capabilities derived from the Treasury system and have a particular focus on executing on the deposit strategy to ensure a stable funding base for the coming years. The infrastructure will be a priority to further improve the operational se-tup and controls around liquidity transaction execution and control.

10.2 Liquidity Portfolio

The Bank's liquidity reserve portfolio consists of government bonds issued by European countries with rating from AA- to AAA, AAA rated covered bonds and AAA rated supranational bonds. All qualify as Level 1 securities under the LCR rules and are High Quality Liquid Assets (HQLA). SCB maintains a portfolio which is obliged to exceed the liquidity flows in each significant currency according to ratios set by the Norwegian FSA. The Bank has also defined several internal threshold levels above the regulatory requirement to minimize operational risk and ensure that the liquidity buffer is of sufficient size.

In addition to holding bonds, SCB utilizes central bank deposits for covering its liquid asset needs. During 2021 Liquid asset needs for SEK where primarily met with central bank deposits and purchases of certificates issued by Swedish Central Bank rather than bond investments.

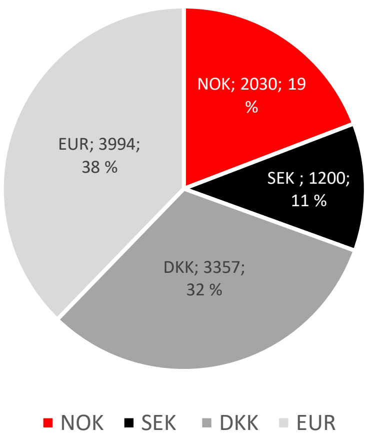
SCB does not have a trading book and the bonds in the liquidity portfolio are under normal circumstances held to maturity. The Bank's policy only allows for the purchase of bonds with a maximum 3 years' maturity if floating coupon and 380 days maturity if fixed rate, limiting the impact on market value of any change in the discount rate.

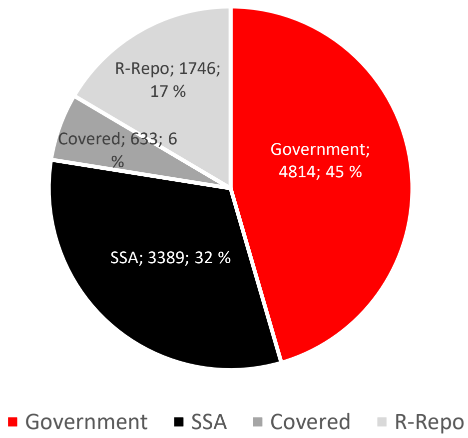
To manage very short-term needs in the portfolio, SCB has entered into Global Master Repurachase Agreements (GMRA) agreements with Nordic counterparties to allow for reverse repo transactions. This has proved a valuable tool for the Bank.

Valuation of the Bank's HQLAs and LCR reporting is conducted at a daily basis. The bond portfolio is well diversified in terms of country/currency, issuer, instrument type and issue. The short average duration of the portfolio also limits the inherent credit risk. The Minimum Liquidity Buffer level is calculated monthly, based on the internal stress tests, and adjusted for specific transactions after the last run of the stress test. The buffer composition and size are calculated daily and measured against the minimum liquidity buffer by Risk.

The Bank will always hold most of the NOK & SEK denominated portfolio with the respective Central Banks, to ensure availability of O/N liquidity, if needed. However, in 2021 SCB utilized Riksbanken deposit facility directly, instead of holding SEK denominated bonds, leading to lower share of SEK denominated papers in the bond portfolio. As of year-end 2021, SCB had 3.7Bn SEK deposited in the Swedish central bank.

Figure 10.2.1: Overview of the HQLA allocations (MNOK per December 31st, 2021)[9]





[9] "SSA" refers to Sovereigns, Supranational and Agencies

10.3 Asset Encumbrance

The asset encumbrance ratio is calculated and reported on a quarterly basis. As of December 2021, the main source of asset encumbrance in the Bank are Auto Asset Backed Securities issued and retained or placed in the market. In addition, the bank had outstanding repurchase agreements of 805 MNOK. During 2021 the Bank has issued a new Finnish ABS (Kimi 10) with a deal size of 450 MEUR. No new true sale ABS transactions have been issued in Sweden, Denmark or Norway since 2015, with only SCF Oy issuing Finnish transactions annually. See table below for breakdown of the balance of encumbered and unencumbered asset per 31 December 2021.

Table 10.3.1: Summary of F 32.01 - Assets of reporting institution - December 21 (NOK '000)

Total Encumbered Assets	15 860 125
Loans on demand	621 832
Retained asset-backed securities issued	805 657
Sold asset-backet securities issued	488 206
Total Non-Encumbered Assets	176 496 932
Loans on demand	7 552 691
Debt securities	8 866 573
Loans and advances other than loans on demand	156 206 928
Other assets	3 870 739
Asset Encumbrance Ratio	8,25%

10.4 Liquidity Management and Governance

The Risk Appetite Framework defines the Bank's risk appetite limit for liquidity risk. The currently approved risk appetite limits for liquidity risk in SCB address NSFR, LCR, Liquidity Survival Horizon (minimum survival days in liquidity stress test scenarios).

All three metrics are considered primary metrics in the Risk Appetite Statement, and risk excess has to be communicated to the Board of Directors. The Risk Appetite metrics are reported to the BoD in every meeting, at least on a quarterly basis. Metrics are also monitored by the Board Risk Committee and the Risk Control Committee.

SCB also has a set of management limits on additional liquidity risk metrics including, amongst others, asset encumbrance, intraday liquidity limits and intragroup limits. The management limits must be reviewed annually and must be approved by the Risk Approval Committee. The management limit metrics covered in the risk appetite statement must also be approved by the BoD in accordance with the SCB governance structure.

These limits are being managed by the Treasury and Analysis department and controlled by the Market Risk department on a monthly basis, and some on a daily basis. Breach of any management limits are reported to the relevant controlling committees in SCB.

10.5 Liquidity Stress Tests

SCB maintains a Liquidity Stress Test model, which is run on a monthly basis. The liquidity stress test of the Bank complies with regulatory requirements and is used both as a tool for measuring liquidity risk and for managing funding and liquid assets.

The liquidity stress test results are presented to Senior Management on a quarterly basis and to the BoD on a semi-annual basis. The objective of the liquidity stress test is to ensure that the Bank has sufficient liquidity to survive a given period under defined stress scenarios. The stress test is used as part of the liquidity risk management of the Bank.