Annual report 2017

SPAREBANKEN SØR BOLIGKREDITT AS

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Report of the Board of Directors

GENERAL

Sparebanken Sør Boligkreditt AS is a wholly-owned subsidiary of Sparebanken Sør, and the company's business is operated from Kristiansand. The company is licensed by the Financial Supervisory Authority of Norway to operate as a mortgage company, and is allowed to issue covered bonds. Sparebanken Sør Boligkreditt AS is part of Sparebanken Sør's long-term financial strategy. All shares are owned by Sparebanken Sør, and the financial statements are consolidated into the financial statements of the Sparebanken Sør Group. Sparebanken Sør Boligkreditt AS' s operations are subject to supervision by the Financial Supervisory Authority of Norway. An investigator has been especially appointed for the mortgage company to attend to the quarterly analysis of the company's cover pool.

The cover pool consists of secured mortgages and interest bearing securities. The mortgages are granted by Sparebanken Sør and later taken over by Sparebanken Sør Boligkreditt AS. The secured mortgages meet the requirements established by the company for inclusion in the company's cover pool. One important requirement is that any outstanding loan balance taken over by the company must not exceed 75 % of the mortgaged property's market value at the date of acquisition.

At the end of 2017, the company had taken on a mortgage loan portfolio totalling NOK 30 974 million, transferred from Sparebanken Sør, of which NOK 30 880 million is included in the qualified cover pool. Sparebanken Sør Boligkreditt AS had issued covered bonds totalling NOK 26 495 million.

Sparebanken Sør Boligkreditt AS has established an EMTCN (European Medium Term Covered Note) Programme which enables the company to diversify funding by issuing covered bonds outside the Norwegian bond market. In 2017 the company issued cover bonds totalling EUR 500 million under the programme.

INCOME STATEMENT / BALANCE SHEET DEVELOPMENT

The financial statements for Sparebanken Sør Boligkreditt AS show a profit after tax of NOK 185.8 million at the end of 2017, compared with NOK 187.8 million in 2016.

The company had net interest income of NOK 360.3 million, compared with NOK 328.4 million in 2016. The increase in net interest income was mainly due to the increase in the mortgage portfolio in the period.

Net income from financial instruments shows a negative contribution of 47.5 million in 2017, compared with a negative contribution amounting to 14.7 million in 2016. In 2017, NOK 31.1 million of the negative contribution relates to basis swaps.

Basis swaps are derivative contracts entered into as part of long term financing in international capital markets, whereby currency is converted to NOK. These are hedging instruments, and assuming the underlying bond is held to maturity, the change in market value over the term of the instruments is zero.

Operating expenses totalled NOK 60.2 million in 2017, compared with NOK 58.4 million in 2016.

Total assets at 31 December 2017 were NOK 32 332 million, of which net loans to customers accounted for NOK 30 968 million. At the same time in 2016, the corresponding figures were NOK 29 207 million and NOK 28 125 million respectively.

The loan portfolio was financed through the issuance of bonds totalling NOK 26 495 million and through equity and drawing rights from Sparebanken Sør. At 31 December 2017, the company had paid-in capital totalling NOK 1 025 million, of which NOK 525 million is share capital and NOK 500 million is share premium.

Sparebanken Sør Boligkreditt AS has an overdraft facility of NOK 4 000 million with Sparebanken Sør, which at 31 December 2017, was drawn down by NOK 3 360 million.

In accordance with Norwegian accounting legislation, the Board of Directors confirms that the conditions for presenting the financial statements on a going- concern basis are met.

CAPITAL STRENGTH

At the end of 2017, the net core tier 1 capital in the company was NOK 2 376.7 million. This corresponds to both a total capital ratio, tier 1 capital ratio and common equity tier 1 capital ratio of 17.4 per cent, while regulatory minimums requirements are 15.5 per cent and 12 per cent respectively. The capital adequacy ratio has been calculated based on the standard method in the Basel II -regulations. The Board of Directors considers the company's financial strength and risk-bearing ability to be very good.

CORPORATE GOVERNANCE

Sparebanken Sør Boligkreditt's corporate governance principles include the objectives according to which the company is managed and governed to protect the owners and other stakeholders' interests in the company. The principles are based on the Norwegian Code of Practice for Corporate Governance (NUES). The company has adapted that framework, and Sparebanken Sør Boligkreditt AS`s principles and policy are intended to ensure that its corporate governance is in accordance with generally accepted and recognised perceptions and standards, and in compliance with laws and regulations.

The purpose is to clarify the division of roles between the company's governing bodies and the day to day management over and above what follows from the legislation. Furthermore, corporate governance has to ensure good interaction between different interested parties such as shareholders, lenders, customers, employees, governing bodies, management and society as a whole. The corporate governance principles have been specified in various documents governing the company's operations. This includes the company's articles of association, strategies and the governance framework. In the Board of Directors' opinion, the corporate governance of Sparebanken Sør Boligkreditt AS is satisfactory and in compliance with these principles and policies.

Sparebanken Sør Boligkreditt AS's mission follows from the company's articles of association. The company`s mission is to acquire mortgages and to fund lending activities primarily by issuing covered bonds. The operations will be run at satisfactory profitability and low risk. The company is wholly owned by Sparebanken Sør. The company's business strategy forms the basis for specification of the level of ambition in the company's overall operations, and thus for Sparebanken Sør Boligkreditt's financial return, growth and development.

The Board of Directors of Sparebanken Sør Boligkreditt AS has prepared an annual plan for its work and conducts an annual review of the company's strategic business plan. Seven board meetings took place in 2017. Follow-up of operations, strategy, risk and capital management and monitoring of the markets and framework conditions have been the areas of focus for the Board of Directors. The company's risk strategy has been adopted by the Board of Directors, which conducts an annual review of the company's risk management and internal control. Identified areas of risk and any material deviations are followed up and reported on a regular basis.

Sparebanken Sør Boligkreditt AS has signed operating agreements with Sparebanken Sør. These agreements cover, among other things, capital management, risk management, internal audit, financial reporting, internal financial control and internal financial reporting. This includes quarterly financial reporting and the preparation of a fixed template for reporting to ensure complete basis for reporting and consistent application of principle.

In addition to reviewing the accounts and risk reporting, the company`s management provides regular operational reporting in relation to the company's objectives to the Board at each Bboard meeting.

The company's ethical guidelines include a duty to report matters that warrant criticism, including breaches of internal guidelines, laws and regulations, and a procedure for how such information is to be given. Large companies must provide information about their management of corporate social responsibility (cf. Section 3-3c of the Norwegian Accounting Act). The parent bank, Sparebanken Sør, delivers such a statement for the group, which also covers its subsidiaries. For further information, refer to the parent bank's annual report.

Sparebanken Sør Boligkreditt AS is a wholly owned subsidiary of Sparebanken Sør and it is therefore exempt from the requirement for a separate audit committee. The Compliance function is taken care of through the company's agreement with Risk Management in Sparebanken Sør. The company has an independent external auditor (PWC) and internal audit (Sparebanken Sør). PWC has been appointed as reviewer by the Financial Supervisory Authority of Norway. Sparebanken Sør Boligkreditt AS's operations are subject to supervision by the Financial Supervisory Authority of Norway. The Board of Directors and management endeavour to maintain an open and constructive dialogue with the Financial Supervisory Authority of Norway.

RISKS

As a licensed mortgage company, Sparebanken Sør Boligkreditt AS is subject to a number of acts, regulations, recommendations and regulatory provisions. The objective of the company is to finance lending activities through the issuing of covered bonds with a high rating. This means that Sparebanken Sør Boligkreditt AS strives to maintain risk at a low level. The company has established Board approved guidelines and limits for management and control of various areas of risk, which meet regulatory, rating agency and investor requirements. The company places emphasis on identifying, measuring and controlling elements of risks in such a way that the market has high confidence in the company and that the company can achieve a high rating on issued bonds.

The company's credit strategy and credit policy constitutes a framework including requirements imposed on borrowers and collateral requirements for loans that may be taken on by the company. The Board of Directors considers the overall quality of the lending portfolio to be very good and the credit risk to be low.

In accordance with Board approved requirements, stress testing of the value of the cover pool was conducted in 2017 with simulation of a sharp fall in house prices. The Board of Directors believes that the result of the stress tests is satisfactory.

The company's mortgages to customers are in NOK at a floating interest rate with six weeks' notice of interest adjustment. Financing is met by issuance of both floating and fixed rate bonds in NOK and EUR. Foreign currency debt is swapped to NOK and fixed rate debt is swapped to floating rate. Foreign currency debt and debt at fixed interest rate, is accounted for using hedge accounting.

The Board of Directors considers the overall market risk to be low.

The company issues bonds with the unilateral right to extend the maturity period by up to 12 months. In other respects, financing needs are met by equity and credit facilities with Sparebanken Sør. In addition, the company also has a revolving credit facility with Sparebanken Sør, which can be used to refinance outstanding bonds. The Board of Directors considers the company's liquidity risk to be low.

At 31.12.2017 the company satisfied the liquidity requirements imposed on European banks and finance companies (LCR - Liquidity Coverage Ratio). The requirement was 80 % in 2017 and 100 % from 31.12.2017.

A Management Service Agreement has been established with Sparebanken Sør that encompasses the supply of all necessary services for the operation of the company, and the Board of Directors considers the company's operational risk to be low.

EMPLOYEES AND WORKING ENVIRONMENT

At 31 December 2017, the company had no employees and there are no relevant comments regarding the internal working environment. The Board is composed of four persons, one of whom is female.

RATING

Covered bonds issued by Sparebanken Sør Boligkreditt AS have been given an Aaa rating by Moody's.

SOCIAL RESPONSIBILITY

The company requires social responsibility work to take place in close cooperation with and according to the same guidelines as in Sparebanken Sør. The company does not carry out activities that pollute the external environment.

FUTURE PROSPECTS

The Board of Directors regards the future prospects for the company's operations as very good. Sparebanken Sør Boligkreditt AS plans further acquisition of loans from Sparebanken Sør, and the company intends to be able to issue new open covered bonds in secured mortgages, aimed at investors in Norway or abroad. Based on the company`s risk profile, losses on loans to customers are expected to be low in 2018.

DISTRIBUTION OF PROFIT

Profit after tax for 2017 is NOK 185.8 million. The Board of Directors proposes that the whole amount is transferred to retained earnings.

Kristiansand, 26 February 2018

The Board of Directors of Sparebanken Sør Boligkreditt AS

Geir Bergskaug	Seunn Smith-Tønnessen	Gunnar P. Thomassen	Bjørn Friestad
Chairman	Member	Member	Member

Marianne Lofthus

Managing Director

Income statement

NOK Thousand	Notes	2017	2016
Interest income	11,21	787 419	765 408
Interest expenses	11,21	427 148	437 057
Net interest income	**2**	**360 271**	**328 351**
Commission income		149	160
Commission expenses		5 000	5 000
Net commission expenses		**-4 851**	**-4 840**
Net income from financial instruments	**12**	**-47 484**	**-14 726**
Personnel expenses		54	44
Depriciation on intagilbe assets		-	-
Other operating expenses	13	60 127	58 310
Total expenses		**60 180**	**58 354**
Profit before losses on loans		**247 756**	**250 431**
Losses on loans	5,8	-	-
Profit before taxes		**247 756**	**250 431**
Tax expenses	14	61 939	62 604
Profit for the period		**185 817**	**187 828**

Notes 1 to 26 are an integral part of the consolidated financial statements.

Other comprehensive income

NOK Thousand	Notes	2017	2016
Profit for the period		**185 817**	**187 828**
Other income and expenses		-	-
Total profit for the period		**185 817**	**187 828**

Balance sheet

NOK Thousand	Notes	31.12.2017	31.12.2016
ASSETS			
Loans to and receivables from credit institutions	15,16,21	152 957	54 254
Net loans to customers	5,6,7,8,15,16	30 967 963	28 125 467
Bonds and certificates	15,16,17	808 817	857 661
Financial derivatives	15,16,18	368 812	151 191
Deferred tax assets	14	14 920	8 693
Other assets		18 097	10 079
TOTAL ASSETS		**32 331 567**	**29 207 346**
LIABILITIES AND EQUITY			
Debt to credit institutions	15,21	3 360 846	2 055 682
Debt incurred due to issuance of securities	10,15,19	26 495 406	24 633 278
Financial derivatives	15,16,18	22 975	249 503
Payable taxes	14	68 166	70 937
Other liabilities		7 444	7 033
Total liabilities		**29 954 837**	**27 016 433**
EQUITY			
Paid-in equity capital	4	1 025 000	1 025 000
Retained earnings	4	1 351 730	1 165 913
Total equity capital		**2 376 730**	**2 190 913**
TOTAL LIABILITIES AND EQUITY CAPITAL		**32 331 567**	**29 207 346**

Notes 1 to 26 are an integral part of the consolidated financial statements.

Kristiansand, 26 February 2018

The Board of Directors of Sparebanken Sør Boligkreditt AS

Geir Bergskaug
Chairman

Seunn Smith-Tønnessen
Member

Gunnar P. Thomassen
Member

Bjørn Friestad
Member

Marianne Lofthus
Managing Director

Cash flow statement

NOK Thousand	2017	2016
Interest received	783 006	762 375
Interest paid	-409 601	-405 207
Operating expenditure	-64 567	-62 871
Changes in loans to customers	-2 838 082	-2 437 937
Income tax paid	-82 776	-94 416
Net cash flow from operating activities	**-2 612 020**	**-2 238 056**
Changes in bonds and certificates	48 844	-757 393
Changes in other assets	72 431	-10 066
Changes in deposits from credit institutions	1 304 427	194 990
Changes in other liabilities	411	323
Net cash flow from current financing activities	**1 426 113**	**-572 146**
Paid in share capital	-	-
Payments received, bond debt	6 201 315	9 255 500
Payments made, bond debt	-4 916 706	-6 441 125
Net cash flow from long-term financing activities	**1 284 610**	**2 814 375**
Net change in liquid funds	**98 702**	**4 173**
Liquid funds as at 01.01	54 254	50 081
Liquid funds at the end of period	**152 957**	**54 254**

Equity statement

NOK Thousand	Equity capital	Share premium reserve	Retained earnings	Total
Balance 31.12.2015	**525 000**	**500 000**	**978 085**	**2 003 085**
Profit 2016	0	0	187 828	187 828
Balance 31.12.2016	**525 000**	**500 000**	**1 165 913**	**2 190 913**
Profit 2017	0	0	185 817	185 817
Balance 31.12.2017	**525 000**	**500 000**	**1 351 730**	**2 376 730**

NOTE 1 – ACCOUNTING POLICIES

1. GENERAL INFORMATION

Sparebanken Sør Boligkreditt AS is a wholly-owned subsidiary of Sparebanken Sør and has its registered office in Kristiansand. The company is licensed to operate as a mortgage company with the right to issue covered bonds.

The main object of Sparebanken Sør Boligkreditt AS is to offer and acquire loans secured through mortgages on residential property up to 75 per cent of the property value, and to issue covered bonds to national and international investors.

All amounts in the financial statements are stated in NOK thousand, unless otherwise indicated. The company's financial statements are presented in Norwegian kroner, which is the functional currency.

The financial statements for 2017 were presented by the Board of Directors on 26 February 2018, and will be adopted with final effect at the General Meeting on 22 March 2018. The General Meeting is the company's supreme body.

2. BASIS FOR COMPILATION OF THE FINANCIAL STATEMENT

The company financial statements have been compiled in accordance with the International Financial Reporting Standards (IFRS) as adopted by the EU, in addition to the Norwegian disclosure requirements pursuant to the Norwegian Accounting Act.

The measurement basis for the financial statement is historical cost with the exception of financial assets and liabilities, including derivatives that are assessed at fair value with change in value through profit or loss.

3. REVENUE

Interest income and costs related to assets and liabilities which are measured at amortised cost, are expensed as incurred using the effective interest method. All charges related to interest-bearing loans and borrowings are included in the calculation of the effective interest rate and are amortised over the expected term.

Commission income, which is direct payment for services provided, is recognised when the services have been delivered. Directly attributable transaction costs associated with financial instruments valued at amortised cost, are amortised over the anticipated lifetime of the instrument.

4. FINANCIAL INSTRUMENTS

4.1 Recognition and deductions

Financial assets and liabilities are recognised when the company becomes a party to the contractual decisions. A financial asset is deducted when the contractual rights to the cash flows from the financial asset expire, or the company transfers the financial asset in such a way that the risk - and profit potential of the asset in question is substantially transferred. A financial liability is deducted when the financial liability is discharged, cancelled or expired.

4.2 Offsetting

Financial assets and liabilities are offset and recognised as a net amount in the balance sheet only when the Company has a legally enforceable entitlement to offset, and intends to realise the asset and settle the liability simultaneously.

4.3 Classification

Financial instruments are classified into one of the following categories at initial recognition.

- Financial instruments designated as hedging instruments
- Financial instruments voluntarily categorised at fair value through profit or loss
- Loans and receivables at amortised cost
- Other liabilities at amortised cost

4.3.1 Financial instruments designated as hedging instruments

Financial derivatives must be valued at fair value with changes in value recognised through the income statement. Sparebanken Sør Boligkreditt AS has used interest rate and currency swaps. Financial derivatives will be recognised in the balance sheet at fair value with changes in value being recognised through the income statement. When calculating fair value, the applicable interest rate curve for the market at the time in question is used as a basis. The category includes interest swaps used as hedging instruments for fair value hedging of bonds issued with a fixed rate of interest.

4.3.2 Financial instruments voluntarily categorised at fair value with changes in value over profit or loss

Financial instruments included in a portfolio measured on an ongoing basis and reported at fair value are chosen to be recognised at fair value. For Sparebanken Sør Boligkreditt AS this concerns bonds and certificates that are assets.

4.3.3 Loans and receivables at amortised cost

This category includes loans and receivables that are measured at amortised cost.

4.3.4 Other liabilities at amortised cost

This category includes borrowings and liabilities that are measured at amortised cost.

4.4 Measurement at initial recognition

Initial recognition of financial assets and liabilities is at fair value. , Transaction costs that are directly attributable to the acquisition or the issuing of the financial asset or financial liability are added for instruments that are not derivatives or are measured at fair value through the income statement.

4.5 Subsequent measurement

4.5.1 Valuation at fair value

Fair value is the price that would be obtained upon the sale of an asset or the price that would be paid to transfer a liability in an orderly transaction between market participants at the time of valuation.

4.5.1.1 Measurement of financial instruments which are not traded in an active market

The fair value of financial instruments not traded in an active market is determined using a suitable valuation method. Valuation techniques are based on the recently signed transactions between independent parties, by refering to instruments with virtually the same content or by discounting cash flows. As far as possible, valuations are based on externally observed parameter values.

In calculating the fair value of interest swaps entered into, the market value of the relevant inter-bank interest rate curve is used at all times.

4.5.2 Measurement at amortised cost

Financial instruments not measured at fair value are measured at amortised cost. Revenues are calculated by using the instrument's effective interest rate.

Amortised cost is defined as the book value at the initial measurement, adjusted for received/paid installments and any cumulative accrual of fees, commissions etc., with any write-downs taken into consideration.

The effective interest rate method is one which calculates the amortised cost and the accrued interest income/expenses for the relevant period. Interest income is recognised using the effective interest method. The effective interest rate is the interest rate that by discounting the loan's cash flows over the anticipated term gives a value equal to the loan's amortised cost on the date of establishment. This means that any difference between the loan's original book value and the accrued value is accrued over the loan's expected maturity.

4.5.3 Write-down of financial assets

Losses on loans are calculated as the difference between the book value and net present value of estimated future cash flows, discounted by using the effective interest rate. Use of the effective interest rate method means that interest income on impaired loans is recognised.. These loans are recognised at the internal interest rate at the date of establishment adjusted for changes in interest rates until the time of impairment. The income interest rates are based on the loan's impaired value.

In the income statement, recognised losses consist of realised losses, changes in impairment losses on loans and input on past realised losses. Losses on loans are based on an assessment of the Company's loan portfolio in accordance with IAS 39. The Company determines the losses on loans on a quarterly basis. Defaulted and doubtful loans are followed up with regular reviews.

4.5.3.1 Reduction in value of loans and individual write-down losses

Impairment loss is made when there is objective evidence that a loan is impaired as a result of weakened creditworthiness. An impairment loss is reversed when the loss is reduced and can be related objectively to an event occurring after the impairment date. All loans that are considered significant will be assessed to see whether there is objective evidence of weakened creditworthiness, and the objective indication is likely to result in reduced future cash flows to the service of the engagement. Objective evidence may be defaults, bankruptcies, debt settlement, lack of liquidity or other significant financial problems.

4.5.3.2 Collective write-downs

Loans that have not been subject to individual impairment write-downs are included in collective write-downs. Loans are divided into groups with similar risk characteristics, with regard to servicing. Collective write-downs are calculated on sub-groups of loans where there is objective evidence that future cash flow for the loan service ability of the engagements is weakened. Collective write-downs made in order to cover expected credit losses caused by incidents that have occurred, must take into account losses in the portfolio at the time of measurement, but not yet identified at the individual's commitment level. Objective events could be a negative trend in risk classification, or adverse developments in collateral values.

4.5.3.3 Realised losses

When it is highly probable that the loss is final, this is recognised as a realised loss. This includes losses where the Company has lost its claim against the debtor as a result of bankruptcy, a debt settlement, an unsuccessful distress warrant, a legally binding court ruling or debt remission. This applies even if the company has otherwise suspended enforcement or waived part of or all loans. Some realised losses will be covered through the previous decision made on individual loan loss write-downs, and booked against the former provision. Realised losses, without coverage in individual impairment loss, as well as over - or under coverage in relation to previous impairment loss, are recognised.

4.6 Recognition in balance sheet and income statement

4.6.1 Loans

Loans are recorded as either loans and receivables to credit institutions or loans to customers. Interest is included in the income statement under interest income. Changes in value due to impairment charges are recognised in the income statement under losses on loans.

4.6.2 Bonds and certificates

The company`s portfolio of bonds and certificates is included in the balance sheet. Interest is included in the income statement as interest income. Changes in value are recognized through net income from financial instruments.

4.6.3 Financial derivatives (assets and liabilities)

The balance sheet includes financial derivatives. Value adjustments related to derivative instruments are recognised in the income statement under net change in value from financial instruments.

4.6.4 Debt to credit institutions

Balance sheet items include debts to credit institutions. Interests is recognised in the income statement under interest expenses.

4.6.5 Debt incurred due to issue of securities

The balance sheet item includes securities debt. Interests is recognised in the income statement under interest expenses.

5. HEDGE ACCOUNTING

Sparebanken Sør Boligkreditt AS employs hedge accounting in relation to the company's funding at fixed interest rate terms and in foreign currencies. Hedge instruments cover the interest risk and foreign exchange of the bonds.

The criteria for classification of a derivative as a hedging instrument are:

- The hedge accounting is expected to be very effective, in that it counteracts changes in the fair value of the bond issued.
- The effectiveness of the hedge accounting must be expected to be effective within the range of 80% to 125%.
- The effectiveness must be able to be reliably measured.
- Satisfactory documentation has been established prior to hedging that among other things shows that the hedging is effective and is expected to remain effective throughout the entire period.

Sparebanken Sør Boligkreditt AS utilises fair value hedging. Hedging is measured and documented every quarter to ensure that the hedging is effective. The dollar-offset method is used as a method of measuring the effectiveness of hedging.

When the hedging is established and effective, interest rate and foreign exchange swaps will be added to the balance sheet at fair value and added to the income statement under "Net value change from financial instruments".

The hedge object is recognised in the balance sheet at amortised cost. Changes in the fair value associated with the hedged risk are accounted for as an addition to or deduction from the balance-added value of the bond debt and are carried in the income statement under "net value change from financial instruments".

If circumstances should occur in which the hedging is not effective, the company will amortise the change in value associated with the hedged object over the remaining period. The associated hedging instrument will continue to be recognised at fair value with a change in value in the income statement.

6. ACCOUNTING OF EXCHANGE EFFECTS

Revenues and expenses in currencies are converted to NOK according to the exchange rate at time of transaction. Balance items in foreign currencies are secured by hedging. Debt in foreign currency is converted to NOK according to the company`s mid-rate at the balance sheet date. Changes in value are recognised in the income statement as net commission from financial instruments. The company`s currency exposure is related to funding and is fully secured by basis swaps.

7. FIXED ASSETS

Fixed assets are recognised at cost less accumulated depreciation and impairment. Ordinary depreciation is computed on a straight-line basis over the expected economic life of the asset. There is an annual reassessment of the remaining useful life and residual values for each asset.

At each reporting date, it will be assessed whether there are any indications of impairment. If there are indications of impairment of the value of an asset, the company will calculate the utility value of the asset. The asset is written-down to the higher of the fair value and the utility value. The basis of previous write-downs is considered at the same time.

8. INCOME TAX

Income tax is accrued as a cost, irrespective of the time of payment. The tax charge therefore reflects this year's and future taxes payable as a result of this year's activity. The tax is expected to offset net income included in this year's tax cost and in the balance sheet and is referred to as payable tax. Deferred tax is calculated on the basis of differences between the reported tax and accounting results that will be offset in the future. Tax increasing and tax reducing temporary differences within the same accounting period, are offset against each other.

Any net deferred tax assets are recognised as an asset in the balance sheet when it is probable that the tax reducing differences will be realised.

9. CASH FLOW STATEMENT

The cash flow statement shows receipts and payments of cash and cash equivalents during the year. Cash and cash equivalents are defined as loans to and receivables from credit institutions.

10. CCHANGES IN ACCOUNTING POLICIES AND NOTES

With effect from 1 January 2017, Sparebanken Sør Boligkreditt AS applieS the following new standards..

Changes in IAS 7.

Information MUST be provided that allows the user of the accounts to assess changes in liabilities arising from financing activities, including changes resulting from cash flows and changes that do not have cash effects, see Note 19.

11. STANDARDS AND INTERPRETATIONS THAT HAVE BEEN APPROVED, BUT NOT YET ENTERED INTO FORCE

The following new standards and interpretations to existing standards have been published and are mandatory for the company and consolidated financial statements in future accounting periods, but Management has not chosen early adoption:

IFRS 9 Financial instruments

In July 2014, IASB published the latest sub-project in IFRS 9 and the standard has now been completed. IFRS 9 will have consequences for classification and measurement, hedge accounting and impairment. IFRS 9 will replace IAS 39, Financial Instruments – Recognition and measurement with effect from 1 January 2018. The parts of IAS 39 that have not been changed as part of this project have been transferred and included in IFRS 9.

The standard was adopted by the European Commission on 22 November 2016 and implemented in Norwegian law on 18 December 2017.

Note 25 presents a more detailed statement of principles, assessments and effects regarding the implementation of IFRS 9 from 01.01.2018.

IFRS 15 Income from customer contracts

IASB and FASB have released a new common standard for revenue recognition, IFRS 15 Revenue from Contracts with Customers. This standard replaces all existing standards and interpretations for revenue. The core principle of IFRS 15 is that revenue is recognised to reflect the transfer of contracted goods or services to customers, and then in an amount that reflects the consideration the company expects to be entitled to in exchange for those goods or services. The standard applies with a few exceptions; all income-generating contracts with customers and provides a model for recognition and measurement of the sale of certain non-financial assets (sales of property, plant and equipment). The group is also considering clarifications in IFRS 15 issued by the IASB in April 2016 and will follow up any further changes to the standard.

IFRS 15 will be implemented using either the full retrospective or modified retrospective method. The standard is in effect as of 1 January 2018.

In addition to the aforementioned new standard and interpretation, there have also been changes to other standards that may affect the company's future reporting. The management considers the effect of the changes to these standards to have little significance for the company.

NOTE 2 – JUDGMENTS, ESTIMATES AND ASSUMPTIONS

With the preparation of financial statements, the management makes estimates and discretionary judgments. Areas that are largely comprised of discretionary estimates have a high degree of complexity, and where assumptions and estimates are significant for the company's financial statements, they are presented below.

GENERAL

In applying accounting policies, the company`s management has exercised discretion as a basis for accounting in some areas and has made assumptions about future events. There will naturally be inherent uncertainty in the financial records based on the use of discretion and assumptions about future events. In exercising discretion and determining assumptions about future events management will look at available information on the state of the balance sheet, historical experience with similar assessments and market and third-party assessments of current conditions. Although the management uses its best discretion and estimates and on best estimates available, it must be anticipated that the actual outcome in some cases may differ materially from what is the basis of accounting. Estimates, assumptions and conditions that represent a significant risk of substantial changes in the carrying value of assets and liabilities within the next financial year are discussed below.

WRITE-DOWNS ON LOANS

Assessment of individual and collective write-downs will always be based on a significant degree of discretion. Predictions based on historical information may prove to be incorrect because it can never be known for certain what relevance historical data have as a basis for decisions. The risk associated with the type of lending provided by the company is considered to be limited as the collateral objects consist of private residential property.

NOTE 3 – RISK MANAGEMENT

The objective of Sparebanken Sør Boligkreditt AS is to be a funding instrument for Sparebanken Sør so that the group can maximise its long-term value creation. With this objective, it is essential that risk is subject to active and satisfactory management.

The objective of Sparebanken Sør Boligkreditt AS is to utilise high-quality residential mortgage portfolios to allow the issuing of covered bonds. Part of the Sparebanken Sør Group's business strategy is to keep a low to moderate risk profile for all enterprises. Taking risks is a basic feature of banking, and risk management is therefore a key area in both daily operations and the Board's ongoing work. We also refer to the group's Pilar 3 document, which is available on the Bank's website.

ORGANISATION

Board of Directors

The Board has overall responsibility for the company's total risk management and aims to ensure that the company has appropriate systems in place for risk management and internal control. The Board determines risk strategies, framework for risk appetite, risk profile and tolerance. The Board also determines the strategy and guidelines for the capital plan and composition of the capital and approves the process to ensure an acceptably adequate capital level at all times.

The company's management

The management and day-to-day operation of Sparebanken Sør Boligkreditt AS is based on a Management Service Agreement between the company and the parent company, Sparebanken Sør.

The Managing Director has overall responsibility for the implementation of the company's credit strategy and credit policy within general mandates and limits adopted by the Board.

Responsibility for implementation of the annual assessment of the risk situation and the capital adequacy requirement has been delegated to the Risk Management division of Sparebanken Sør and is regulated by a supply agreement between the Mortgage Company and Sparebanken Sør. This analysis will be coordinated and integrated with other planning and strategy work in the group.

Sparebanken Sør has risk management at group level, including Sparebanken Sør Boligkreditt AS. This unit will identify measure and evaluate the overall risk and take responsibility for compliance.

Internal auditor

Sparebanken Sør`s internal auditors cover internal auditing of Sparebanken Sør Boligkreditt AS, as regulated in a separate agreement. This is a monitoring function independent of the administration in general, designed to perform risk assessments, controls and investigations of the company's internal control and governance processes in order to assess whether these are appropriate and proper.

Risk control process

There are reasonable and appropriate strategies and processes for risk management and the assessment of capital needs and how this can be maintained. The collective term for this is ICAAP (Internal Capital Adequacy Assessment Process).

RISK CATEGORIES

All risks are managed through a framework for risk appetite and risk tolerance. There are targets for the different risk parameters, which are:

Credit risk / counterparty risk

Credit risk is the risk of loss due to the Company's counterparties or customers not having the ability or willingness to meet its payment obligations to Sparebanken Sør Boligkreditt AS. Credit risk concerns all claims on counterparties/customers. This means loans and credits, securities and counterparty risk arising from derivatives and foreign exchange contracts.

Credit risk is a function of two factors (events): ability and willingness to pay, and the value of underlying collateral. Both factors must occur for losses to take place. The first is the lack of ability to pay or willingness to pay of the debtor, and the other is the value of the underlying collateral not being sufficient to cover the Company's requirements for any default and subsequent realisation of security.

Credit risk is defined as a significant risk, and the Company's policy is that credit risk exposure should be low. The Board approves the Company's credit strategy and credit policy, and credit risk is controlled by adopted limits and measures linked to the risk profile and exposure on portfolio levels.

The Board receive regular reports on credit risk. The development of lending by the various risk classes and migration between these classes are vital in this respect.

Settlement risk

Settlement risk is a form of credit risk where a contracting party fails to fulfil its obligations regarding settlements in the form of cash or securities, upon the Company has given notice of the payment or transfer of a security or guarantee. Settlement risk that the Company is exposed to is considered to be low.

Liquidity risk

Liquidity risk is defined as the risk of Sparebanken Sør Boligkreditt AS being unable to meet its obligations or unable to fund its assets, but also not being possible to achieve funding without incurring significant additional costs, in the form of an impairment in value of assets that must be realised, or in the form of funding at an above normal cost level. Liquidity risk also includes the risk of the financial markets, which the company wishes to use ceasing to function.

Sparebanken Sør Boligkreditt AS will have a liquidity risk in accordance with the regulatory requirements. The risk must be low and comparable with similar companies and meet the requirements of investors in the Company's bonds. The monitoring is done by the control of exposure in relation to adopted limits and control of qualitative requirements. The company`s liquidity risk should be positive.

Market risk

Market risk includes risks related to profit variations on unsecured interest and exchange rate transactions due to changes in interest and exchange rates and adjustments in share prices and may be divided into interest rate risk and credit spread risk Sparebanken Sør Boligkreditt AS must have a low market risk.

Interest rate risk

Interest rate risk is defined as the risk of revenue losses arising from changes in interest rates if the fixed rate period for the Company's liabilities and assets, does not coincide. The interest rate risk limit is determined as an upper limit on how great the loss on unsecured interest rate positions may be in case of a 2 percentage point parallel shift in the interest rate level.

Currency risk

Risk of financial (earnings-related) losses arising from an unfavorable change in the value of asset and liability items (on and off the balance sheet) measured in the base currency (NOK) due to changes in exchange rates. Exposure is measured as the size of the potential losses in a stress scenario where the exchange rates change by 10 per cent and the currency risk is regulated by limits for maximum aggregated currency position.

Spread risk

Spread risk is defined as the risk of changes in the market value of interest-bearing securities due to a general change in the credit spread. A general increase in credit spreads would lead to a reduction in value of a portfolio of interest-bearing securities. Changes in credit spread are a consequence of changes in investors' requirement for risk premium for a shift in anticipated credit risk and / or changes in other market conditions. The company's credit spread exposure is mainly related to the liquidity portfolio.

Business risk

Business risk is defined as the risk of unexpected revenue fluctuations based on factors other than credit risk, market risk and operational risk. The risk can occur in various business and product segments and is linked to cyclical fluctuations and changes in customer behavior. Business risk can also arise as a result of government regulations. The risks also include the reputational risk, which is the risk, associated with increased losses, reduced income and/or increased costs as a result of the company's reputation having been damaged.

Strategic risk

Strategic risks are defined as internal matters where the risk relates to the strategies, plans and changes that the Company either has or has proposed.

Operational risk

Operational risk is the company`s exposure to financial losses or loss of reputation due to inadequate or failing internal processes or systems, human errors or external events. Operational risk includes risk of default. Examples of operational risk may be several types of adverse actions and events, including money laundering, corruption, embezzlement, insider trading, fraud, robbery, threats to employees, authorisation beaches and breaches of adopted procedures, the failure of IT systems, etc.

Operational risk is monitored by regular qualitative assessments. The estimated capital requirements for operational risk are carried out under the basic method. The operational business in Sparebanken Sør Boligkreditt AS has been secured through supply agreements with Sparebanken Sør. Sparebanken Sør Boligkreditt AS's operational risk is considered to be low.

Concentration risk

Concentration risk is credit risk arising from high overall exposure to a single counterparty or issuer of security, associated groups of counterparties, counterparties with operations in the same sector or geographical area and enterprises that use the same kind of security, trade in the same goods or have the same type of operations.

With regards to credit risk, it is an objective to avoid major risk concentrations, including large exposure to individual customers or customer groups and groups of commitments in classes within high-risk industries or geographic areas.

The company's view is that Sparebanken Sør Boligkreditt AS is not exposed to any additional risk as a result of debtor concentration. This is a result of low credit exposure taking into account the quality of security pledged.

HEDGING INSTRUMENTS

The Company uses the following hedging instruments:

- IInterest rate swaps - agreements to exchange interest rates for a particular nominal amount over a specified number of periods
- Basis swaps – agreements to exchange both interest rates and foreign currencies

The purpose of using these instruments is to hedge interest rate- and currency exposure.

NOTE 4 – CAPITAL ADEQUACY

Sparebanken Sør has an objective of maximising long-term value creation. The Group also has an objective that the risk profile should be moderate to low. This means that effective risk and capital management is a key strategic element. Sparebanken Sør Boligkreditt AS is an instrument to underpin this objective.

Sparebanken Sør has established a strategy and process for risk measurement, -management and -control that provides an overview of the risks the company is exposed to. This therefore provides the basis for the assessment and calculation of the Group's total capital needs, and how this can be maintained to meet the specific risks in an adequate manner. The process is referred to as ICAAP (Internal Capital Adequacy Assessment Process). The assessment of capital needs including size, composition and the distribution of their capital needs and the level of the risks the Group is or may be subjected to, based on the completed stress tests that show what changes in macro-variables can inflict major losses on Group losses.

Sparebanken Sør Boligkreditt AS uses the standard method for credit- and market risk and applies basic method for operational risk to calculate capital adequacy in accordance with the capital adequacy rules – Basel II.

Capital adequacy has to ensure that the company has the necessary buffer capital for events that arise in addition to ordinary loss provisions. In order to have greater flexibility in terms of strategic choices and business opportunities, the Sparebanken Sør Group has higher equity and subordinated loan capital than the need which is calculated from ICAAP.

The minimum requirement for core equity tier 1 ratio was 12.0 per cent, core capital ratio 13.5 per cent and total capital adequacy 15.5 per cent.

NOK Thousand	31.12.2017	31.12.2016
EQUITY CAPITAL		
Equity capital	525 000	525 000
Equity premium reserve	500 000	500 000
Other equity capital	1 351 730	1 165 913
Deductions	-1 201	
Commom equity tier 1 capital	**2 375 529**	**2 190 913**
Minimum requirement for equity capital		
Credit risk	990 345	881 921
Market risk		
Operational risk	56 264	61 545
CVA addition	45 833	24 001
Deductions		
Total minimum requirement for equity capital	**1 092 442**	**967 467**
Risk-weight balance (calculation basis)	13 655 525	12 093 338
Commom equity tier 1 capital ratio	**17.4 %**	**18.1 %**
Tier 1 capital ratio	**17.4 %**	**18.1 %**
Total capital ratio	**17.4 %**	**18.1 %**
Leverage Ratio	**7.0 %**	**7.2 %**

NOTE 5 – CREDIT AREA AND CREDIT RISK

Credit risk represents the greatest area of risk for the company. The Board of the Group sets the credit strategy, which together with credit policies and guidelines for credit processes has to ensure that the customer portfolio has an acceptable risk profile and helps the Group to maximise its long-term value creation.

Loans broken down by risk classes

The models used have been based on internal and external data for calculation of probability of default (PD) in the next 12 months and expected losses (EL) at customers and portfolio level. Customers are scored each month, and are divided into 11 classes (A – K) based on the probability of default. Class K consists of default loans and commitments with individual write-downs. The table below shows the intervals for the different risk classes based on the probability of default.

All customers must be classified inn terms of risk before the loan is transferred from Sparebanken Sør to Sparebanken Sør Boligkreditt AS, and loans that are taken on by Sparebanken Sør Boligkreditt AS must have a probability of default (PD value) not exceeding 2.00 per cent. Customers who have a weaker risk classification after transfer to the company may remain as part of the cover pool if the requirement of a loan-to-value ratio not exceeding 75 per cent is met.

The company`s risk categories are as follows:

Risk classes	Lower limit of default (PD-values)	Upper limit of default (PD-values)
A	0.00 %	0.10 %
B	0.10 %	0.25 %
C	0.25 %	0.50 %
D	0.50 %	0.75 %
E	0.75 %	1.25 %
F	1.25 %	2.00 %
G	2.00 %	3.00 %
H	3.00 %	5.00 %
I	5.00 %	8.00 %
J	8.00 %	99.99 %
K	100.00 %	

Probability of default	
Low risk (A-D)	0.00 - 0.75%
Medium risk (E-G)	0.76 - 3.00 %
High risk (H-J)	3.01 - 99.99 %
Default (K)	100 %

Specification within risk categories at 31 December 2017

NOK Thousand	Commitments	Commitments in %	Gross loans	Potential exposure
Low risk	27 224 371	81.8 %	25 058 050	2 166 321
Medium risk	5 534 012	16.6 %	5 429 235	104 777
High risk	451 961	1.4 %	445 117	6 844
Non performing and write-downs	0	0.0 %	0	0
Unclassified	51 029	0.2 %	41 561	9 468
Total	**33 261 373**	**100.0 %**	**30 973 963**	**kr 2 287 410**

Specification within risk categories at 31 December 2016

NOK Thousand	Commitments	Commitments in %	Gross loans	Potential exposure
Low risk	25 993 025	85.5 %	23 798 376	2 194 649
Medium risk	4 091 435	13.5 %	4 009 933	81 502
High risk	290 171	1.0 %	288 989	1 182
Non performing and write-downs	1 173	0.0 %	1 173	0
Unclassified	42 534	0.1 %	32 996	9 538
Total	**30 418 338**	**100.0 %**	**28 131 467**	**2 286 871**

Commitments include gross loans and potential exposure. Potential exposure consists of unused credit facilities on flexi-loans.

NOTE 6 – COVER POOL AND LOAN-TO-VALUE RATIO

	Fair value	
NOK Thousand	31.12.2017	31.12.2016
Loans secured by mortgages on residential properties (1)	30 967 963	28 125 467
Deduction of ineligible loans (2)	-87 624	-84 296
Pool of eligible loans	30 880 339	28 041 171
Sertificates and bonds	556 484	-
Receivables on derivatives	345 837	137 889
Total cover pool (1,2)	**31 782 659**	**28 179 060**
Debt incurred due to issuance of securities	26 704 357	24 746 000
Commitments on derivatives	-	236 201
Total commitments	**26 704 357**	**24 982 201**
Collateralisation ratio (OC)	**19,0 %**	**12,8 %**

1) Cover pool composition is defined in the Norwegian Financial Institution Act Section 11-8.

2) Loans with LTV (loan to value) higher than 75 % is included in the cover pool. However, the part of the loan exceeding 75 % (ineligibles) is excluded when calculating the OC above. Assuming the ineligibles is included, the OC would have been 19.3 % as at 31.12.2017 and 13.1 % as at 31.12.2016.

	Nominal value	
	31.12.2017	31.12.2016
OC based on nominal value, eligibles only	19.0 %	14.5 %
OC based on nominal value	19.4 %	14.8 %

The calculation of OC has been changed compared to previous periods, and as a result comparative figures for 2016 have been restated.

	31.12.2017	31.12.2016
Average debt to assets ratio in %	57.0 %	54.7 %
Portfolio divided into intervals of debt to assets ratio:		
Less than og equal to 40%	16.9 %	20.8 %
41 - 50 %	12.3 %	13.3 %
51 - 60 %	19.4 %	19.4 %
61 - 70 %	31.9 %	30.7 %
71 - 75 %	13.3 %	11.7 %
More than 75 %	6.1 %	4.0 %
Total	**100.0 %**	**100.0 %**

NOTE 7 - LOANS

NOK Thousand	31.12.2017	31.12.2016
Loans assessed at amortized cost		
Flexi-loans (loans without installments)	7 518 339	6 758 883
Loans with installments	23 455 623	21 372 584
Gross Loans	**30 973 963**	**28 131 467**
Collective write-downs	6 000	6 000
Net loans	**30 967 963**	**28 125 467**
Undrawn credit on Flexi-loans	2 287 410	2 286 871

NOK Thousand	30.09.2017	31.12.2016
Loans distributed to sectors and industries		
Retail customers	30 943 401	28 064 368
Corporate customers*)	0	40 950
Accrued interests	30 562	26 149
Gross loans	**30 973 963**	**28 131 467**
Collective write-downs	6 000	6 000
Net loans	**30 967 963**	**28 125 467**

*Loans to corporate customers are mortgage loans for customers in sector 8200.

	31.12.2017		31.12.2016	
Loans distributed by geographical areas				
Vest-Agder	13 514 160	43.6 %	12 431 648	44.2 %
Aust-Agder	8 621 345	27.8 %	8 017 979	28.5 %
Telemark	3 052 322	9.9 %	2 571 798	9.1 %
Oslo	2 324 234	7.5 %	2 197 082	7.8 %
Akershus	1 275 585	4.1 %	1 081 387	3.8 %
Other counties	2 180 317	7.0 %	1 825 573	6.5 %
Total	**30 967 963**	**100.0 %**	**28 125 467**	**100.0 %**

NOTE 8 - DEFAULTED LOANS

NOK Thousand	31.12.2017	31.12.2016
Gross non-performing loans > 90 days	0	1 173
Individual write-downs	0	0
Net non-performing loans	0	1 173
Net non-performing loans > 90 days in % af gross loans	**0.0 %**	**0.0 %**

A non-performing loan is defined as the sum of a customer`s total loan amount if part of the loan has been overdrawn, or has arrears exceeding NOK 1000 for more than 90 days.

NOTE 9 - INTEREST RATE RISK

Interest rate risk occurs in connection with the company's ordinary lending and borrowing activities and in relation to the activities in the Norwegian and international money and capital markets. Interest risk exists when fixed-interest periods for assets and liabilities differ. An interest risk limit has been adopted by the Board of Directors, and is measured as maximum loss as a result of parallel displacement of the yield curve by two percentage points as well as assumed changes to the yield curve.

Interest rate risk is managed through fixing of interest rates for asset and liability items and by use of financial derivatives. The company reports to the Board of Directors on a quarterly basis.

At 31 December 2017, Sparebanken Sør Boligkreditt AS`s portfolio of loans to customers consists solely of floating rate loans.

Two NOK denominated fixed rate interest bonds have been issued, and have been swapped to floating interest rate. In addition two EUR denominated fixed rate bond has been issued, and converted into NOK and floating interest rate by use of basis swaps (cross currency interest rate swaps). Hedge accounting is applied for all fixed interest rate and foreign currency financing.

The interest risk exposure was NOK 6.9 million at 31.12.2017 (NOK 3.9 million at 31.12.2016).

According to the company`s internal rules, the total accounting effect by a 10 percent exchange rate movement should not exceed NOK 10 million. The currency exposure was NOK 0 million as at 31.12.2017 (NOK 0 million as at 31.12.2016).

NOTE 10 - LIQUIDITY RISK

Liquidity risk is defined as the risk of the company failing to fulfil its obligations as they fall due. The company's liquidity risk was generally low in 2017, as illustrated by the fact that most of the company's loans were financed on a long-term basis through covered bonds. Long-term financing is defined as financing from the money and capital markets with maturities exceeding one year, as well as unutilised committed drawing rights. The company has to have sufficient liquid funds in order to fulfil its obligations at all times. In 2017, the company's funding structure complied with requirements imposed by law and instructions by the Board of Directors.

As of 31 December 2017, Sparebanken Sør Boligkreditt AS has an overdraft facility amounting to NOK 4 000 million with Sparebanken Sør. In addition, the company has a revolving credit facility with the parent bank, which can be used to refinance outstanding bonds. Annual commission is paid on the drawing rights.

Covered bonds issued by Sparebanken Sør Boligkreditt AS contain a clause giving the borrower an option to extend the loan by 12 months beyond the maturity date.

LIQUIDITY RISK

The table shows cash flows including contractual interest payments. The figures therefore cannot be reconciled with the balance sheet.

						31.12.2017
NOK million	**TOTAL**	**1 mth.**	**3 mth.**	**1 year**	**5 years**	**Over 5 years**
Liabilities / non derivative obligations						
Debt to credit institutions	3 360	3 360				
Debt incurred due to issue of securities	27 442	20	73	843	25 523	983
Other liabilities	75	3	3	69	0	0
Loan commitments an unused credit facilities	2 287	2 287				
Total liabilities	**33 164**	**5 670**	**76**	**912**	**25 523**	**983**
Derivative committments						
Financial derivative gross payments						
Payments made	-9 847				-9 847	
Payments received	9 454				9 454	
Total derivative committments	**-393**	**0**	**0**	**0**	**-393**	

						31.12.2016
NOK million	**TOTAL**	**1 mth.**	**3 mth.**	**1 year**	**5 years**	**Over 5 years**
Liabilities / non derivative obligations						
Debt to credit institutions	2 056	2 056				
Debt incurred due to issue of securities	25 881	20	443	945	23 456	1 017
Other liabilities	167	3	3	72	6	83
Loan commitments an unused credit facilities	2 287	2 287				
Total liabilities	**30 391**	**4 366**	**446**	**1 017**	**23 462**	**1 100**
Derivative committments						
Financial derivative gross payments						
Payments made	-4 760				-4 760	
Payments received	4 545				4 545	
Total derivative committments	**-215**	**0**	**0**	**0**	**-215**	**0**

Debt securities issued as at 31.12.2017

ISIN Number	Ticker	Currency	Nominal value	Interest		Due date	Book value	Fair value
NO0010673296	SORB21	NOK	685 000	Floating	3M Nibor	14.09.2018	684 971	687 704
NO0010679806	SORB10	NOK	5 000 000	Floating	3M Nibor	22.05.2019	5 004 630	5 032 414
NO0010664659	SORB07	NOK	28 000	Floating	3M Nibor	27.11.2019	28 082	28 224
NO0010714058	SORB24	NOK	5 000 000	Floating	3M Nibor	24.06.2020	4 971 181	5 017 020
XS1383921803		EUR	500 000	Fixed	0.25 %	22.03.2021	4 919 153	4 977 972
NO0010778954	SORB27	NOK	5 000 000	Floating	3M Nibor	22.11.2021	5 006 819	5 055 769
XS1622285283		EUR	500 000	Fixed	0.125 %	30.05.2022	4 897 623	4 920 716
NO0010671597	SORB09	NOK	350 000	Fixed	3.85 %	13.02.2023	393 427	395 394
NO0010670409	SORB08	NOK	500 000	Fixed	4.00 %	24.01.2028	589 521	589 144
TOTAL							**26 495 407**	**26 704 357**

NOTE 11 - INTEREST INCOME AND INTEREST EXPENSES

NOK Thousand	2017	2016
Interest on loans given to and receivables from credit institutions	645	298
Interst on loans given to customers	774 119	762 093
Interest on certificates/bonds/interst-bearing securities	12 655	3 017
Total interest income	**787 419**	**765 408**
Interest on debt to credit institutions	33 474	26 453
Interest on issued securities	393 673	410 604
Other interest cost	1	0
Total interest expenses	**427 148**	**437 057**
Net interest income	**360 271**	**328 351**

NOTE 12 - INCOME FROM FINANCIAL INSTRUMENTS

NOK Thousand	2017	2016
Profit (loss) and change in value from covered bonds	-541	-867
Net income from covered bonds	**-541**	**-867**
Change in value fixed rate bonds - hedge accounting	-573 039	209 745
Change in value derivatives fixed rate bonds - designated as hedging instruments	547 802	-242 821
Net income hedging	**-25 237**	**-33 076**
Whereof effects from basis swaps (1)	-31 072	-31 859
Profit (loss) buyback of own bonds - amortized cost	-21 706	19 217
Net other financial instruments and derivatives	**-21 706**	**19 217**
Net income from financial instruments	**-47 484**	**-14 726**

1) The company has issued covered bonds in Euro that have been hedged using basis swaps. Change in the value of the basis swaps as a result of changes in market conditions, is presented as hedging-inefficiency. This ineffective portion is recognized in the income statement.

Basis swaps are derivative contracts used to convert obligations in foreign currency into NOK. Basis swaps are used when the company has entered into long term funding in international capital markets. These are hedging instruments, and assuming the underlying bond is held to maturity, the change in market value over the instruments duration equals zero. Accounting effects are therefore reversed over time.

NOTE 13 - OTHER OPERATING EXPENSES

NOK Thousand	2017	2016
External fees	1 769	1 501
Management of loans / services purchased	55 459	52 934
Other operating expenses	2 898	3 874
Total other operating expenses	**60 127**	**58 310**

Remuneration to auditors is included in other operating expenses

NOK Thousand	2017	2016
Ordinary audit fees, statutory audit	137	132
Other attestation services	363	373
Fees on other services		0
Total remuneration of elected auditor (incl. VAT)	**500**	**505**

NOTE 14 - TAX

Tax cost for the year

NOK Thousand	31.12.2016	31.12.2015
CALCULATION OF DEFERRED TAX / TAX DEFERRED ASSETS		
Tax-increasing temporary differences		
Fixed assets	-222	-278
Bond debt - adjustment of hedge accounting	-487 188	85 575
Total tax-increasing temporary differences	**-487 410**	**85 297**
Financial derivatives	428 477	-119 325
Bond assets	-748	-747
Total tax-reducing temporary differences	**427 729**	**-120 072**
Basis for deferred tax (+) / deferred tax assets (-)	**-59 681**	**-34 775**
Calculated deferred tax (+) / deferred tax assets (-) (25 %)	**-14 920**	**-8 694**
Deferred tax / deferred tax assets as at 01.01	0	-360
Change in deferred tax in the profit	-6 227	-8 334
Deferred tax / deferred tax assets as at 31.12	**-6 227**	**-8 694**
Profit before tax expenses	247 756	250 431
Permanent differences	0	-16
Change in temporary differences	24 906	33 334
Taxable income	**272 662**	**283 749**
Tax payable in the balance sheet (25%)	**68 166**	**70 937**
Effective tax rate	27.5 %	28.3 %
Tax payable on net income	68 166	70 937
Changes in deffered tax	-6 227	-8 334
To little tax provision in previous year	0	0
Tax cost for the year	**61 939**	**62 604**

Deferred tax assets are recognised and justified based on expected future earnings.

NOTE 15 - FINANCIAL INSTRUMENTS BY CATEGORY

NOK Thousand	Financial instruments voluntary categorised at fair value (1)	Financial derivatives used as hedging instruments	Financial assets and liabilities at amortised cost (2)	31.12.2017 Total
Loans to credit institutions			152 957	152 957
Net loans to customers			30 967 963	30 967 963
Bonds and certificates	808 817			808 817
Financial derivatives		368 812		368 812
Total financial assets	**808 817**	**368 812**	**31 120 920**	**32 298 550**
Debt to credit institutions			3 359 909	3 359 909
Debt incurred due to issue of securities			26 495 406	26 495 406
Financial derivatives		22 975		22 975
Total financial liabilities	**0**	**22 975**	**29 855 315**	**29 878 291**

NOK Thousand	Financial instruments voluntary categorised at fair value (1)	Financial derivatives used as hedging instruments	Financial assets and liabilities at amortised cost (2)	31.12.2016 Total
Loans to credit institutions			54 254	54 254
Net loans to customers			28 125 467	28 125 467
Bonds and certificates	857 661			857 661
Financial derivatives		151 191		151 191
Total financial assets	**857 661**	**151 191**	**28 179 721**	**29 188 573**
Debt to credit institutions			2 055 482	2 055 482
Debt incurred due to issue of securities			24 663 278	24 663 278
Financial derivatives		249 503		249 503
Total financial liabilities	**0**	**249 503**	**26 718 760**	**26 968 263**

1 – Maximum credit risk is equivalent to the recognised value of financial instruments voluntarily categorised at fair value.
2 – Debt included in hedge accounting is presented as financial assets and liabilities at amortised cost

NOTE 16 - FAIR VALUES OF FINANCIAL INSTRUMENTS

METHODS TO DETERMINE FAIR VALUE

GENERAL

For financial instruments for which the booked value is a reasonable approximation of fair value, valuation methods to calculate fair value are not used. This relates mainly to assets and liabilities that mature within three months or where interest is due or fixed within three months.

INTEREST RATE SWAPS

Valuation of interest rate swaps at fair value is done through the use of valuation techniques in which the expected future cash flows are discounted to the present value. The calculation of expected cash flows and the discounting of these are carried out by the use of observable market rates for different currencies and observable exchange rates. The estimated present value is checked against the corresponding estimates from the counterparties in the contracts.

CERTIFICATES AND BONDS

The valuation of certificates and bonds is through the use of valuation techniques based on future cash flows and credit risk, assessed on the balance sheet date. The valuation is based on observable market interest rates. The Company's assessment of credit risk is based on information from various brokers.

LOAN

For loans with a floating interest rate, fair value is considered to be equal to the nominal value.

DEBT

For debt the valuation is made through the use of valuation techniques and the discounting of expected future cash flows. A risk-free interest rate is regarded as the interest rate on loans between credit-worthy banks. The mark-up for credit is made on the basis of the ongoing assessments which other market players make of the Company's creditworthiness.

DEPOSITS

For floating rate deposits, the fair value is considered to be equal to nominal value.

Classification of financial instruments

Financial instruments are classified in different levels.

Level 1:

Includes financial assets and liabilities valued using the unadjusted observable market values. This includes listed shares, derivatives traded on active market places and other securities with quoted market values.

Level 2:

Instruments valued based on valuation techniques where all assumptions (all input) is based on directly or indirectly observable market data. Values can be obtained from external market players or reconciled with the external market players that offer these types of services.

Level 3:

Instruments are based on valuation techniques in which at least one essential requirement cannot be supported based on observable market values. This category includes investments in unlisted companies and fixed rate loans, for which no market information exists.

				31.12.2017
	Recognised		Fair value	
NOK Thousand	value	Level 1	Level 2	Level 3
Assets recognised at amortised cost				
Loans to and receivables from credit institutions	152 957		152 957	
Net loans to customers (floating interest rate)	30 967 963			30 967 963
Assets recognised at fair value				
Bonds and certificates	808 817		808 817	
Financial derivatives	368 812		368 812	
Total financial assets	**32 298 550**	**0**	**1 330 587**	**30 967 963**
Liabilities recognised at amortised cost				
Debt to credit institutions	3 359 909		3 359 909	
Debt incurred due to issue of securities	26 495 406		26 704 357	
Liabilities recognised at fair value				
Financial derivatives	22 975		22 975	
Total financial liabilities	**29 878 291**	**0**	**30 087 241**	**0**

				31.12.2016
	Recognised		Fair value	
NOK Thousand	value	Level 1	Level 2	Level 3
Assets recognised at amortised cost				
Loans to and receivables from credit institutions	54 254		54 254	
Net loans to customers (floating interest rate)	28 125 467			28 125 467
Assets recognised at fair value				
Bonds and certificates	857 661		857 661	
Financial derivatives	151 191		151 191	
Total financial assets	**29 188 573**	**0**	**1 063 106**	**28 125 467**
Liabilities recognised at amortised cost				
Debt to credit institutions	2 055 482		2 055 482	
Debt incurred due to issue of securities	24 663 278		24 746 022	
Liabilities recognised at fair value				
Financial derivatives	249 503		249 503	
Total financial liabilities	**26 968 263**	**0**	**27 051 007**	**0**

HEDGE ACCOUNTING

Sparebanken Sør Boligkreditt AS uses hedge accounting for debt issued at fixed interest rate and for bonds issued in foreign currency. The bonds included in hedge accounting are initially recognised at cost. Subsequent measurements at amortised cost, with the change in fair value related to the hedged risk. Derivative instruments are used as a hedge of interest rate and foreign currency risk.Hedge accounting requires the Company to measure and document hedge effectiveness.

All bonds issued at fixed rate or in foreign currency are accounted for using hedge accounting. Sparebanken Sør Boligkreditt AS uses fair value hedge accounting. The hedge is measured and documented every quarter to ensure that is effective within 80-125%. The 'dollar offset method' is used to measure the effectiveness of the hedge.

Result of hedge accounting

NOK Thousand	2017	2016
Result / ineffectivenes in hedge accounting		
Net income from other financial instruments	-25 237	-33 076
Total	**-25 237**	**-33 076**
Whereof effects from basis swap	-31 072	-31 859

Inefficiency in hedge accounting is recognised as a change in value and also appears in Note 12.

Hedge accounting in the balance sheet

The hedging instrument is recognised as financial derivatives. Value related to the hedged risk is recognised as debt incurred due to issue of securities.

NOK Thousand	2017	2016
Recognitions concerning hedge accounting		
Financial derivatives (clean value)	411 126	111 687
Total financial assets	**411 126**	**111 687**
Nominal hedged items	10 215 404	5 610 000
Adjustment of hedged items - hedged risk	458 987	-98 797
Financial derivatives (clean value)	13 222	244 234
Total financial liabilities	**10 687 612**	**5 755 437**

The table shows changes in value of the hedging instrument during the financial year.

Change in fair value of the hedged item that relates to the hedged risk is recognised as an adjustment of the hedged item in the balance sheet.

NOTE 17 - BONDS AND CERTIFICATES

NOK Thousand	31.12.2017	31.12.2016
Short-term investments designated at fair value through profit		
Certificates and bonds issued by public sector	151 047	200 300
Certificates and bonds issued by others	656 270	655 548
Accrued interest	1 500	1 813
Total	**808 817**	**857 661**

Classification of financial investments

Certificates and bonds are rated externally. Where securities have an official rating that will be used, in cases where the official rating does not exist an external broker will provide a credit assessment as a basis for risk classification.

Sparebanken Sør Boligkreditt AS owns only instruments with the lowest risk (Aaa rated) at 31 December 2017.

NOTE 18 - FINANCIAL DERIVATIVES

NOK Thousand	31.12.2017	31.12.2017 (1) presented as net	31.12.2016	31.12.2016 (1) presented as net
Assets				
Financial derivatives	368 812	345 837	151 191	137 889
Debt				
Financial derivatives	22 975	0	249 503	236 201

1) Shows assets and liabilities if the company had netted their financial derivatives for individual counterparty.

The company's counter-claim rights comply with general Norwegian law. Sparebanken Sør Boligkreditt AS has the right to offset other outstanding accounts under ISDA agreements in cases where certain events occur. The amounts have not been offset in the balance sheet at 31 December 2017 or 31 December 2016 because the transactions are generally not settled on a net basis.

NOTE 19 - DEBT DUE TO ISSUANCE OF SECURITIES

NOK Thousand	31.12.2016	Issued	Matured / redeemed	Other changes in period	31.12.2017
Bonds, nominal value	24 718 000	6 194 250	-4 895 000	392 650	26 409 900
Value adjustment	-146 038			173 068	27 030
Accrued interest	61 316			-2 840	58 476
Total debt due to issuance of securities	**24 633 278**	**6 194 250**	**-4 895 000**	**562 878**	**26 495 406**

NOTE 20 - AVERAGE INTEREST EXPENSES

NOK Thousand	31.12.2017	31.12.2016
Debt to credit institutions		
Debt to credit institutions	1.94 %	1.82 %
Debt incurred due to issuance of securities		
Bond debt, floating interest rate	1.19 %	1.57 %
Bond debt, fixed interest rate	3.94 %	3.94 %
Bond debt, fixed interest rate in Euro	0.19 %	0.25 %

Average interest rate, defined as annual interest in arrears, has been calculated as a weighted average of the actual interest rate conditions at 31 December 2017. No liabilities have special conditions. For fixed rate covered bonds, the coupon rate is specified. Fixed rate in NOK and foreign currency are swapped to floating rate in NOK.

NOTE 21 - RELATED PARTIES

NOK Thousand	2017	2016
Income statement		
Interest income from Sparebanken Sør on deposits	645	298
Interest expenses and commissions from Sparebanken Sør on loans/credit	38 474	31 453
Interest expenses on bond debts to Sparebanken Sør	0	529
Paid administration fees to Sparebanken Sør	55 409	52 888
Balance sheet		
Bank deposit in Sparebanken Sør	152 957	54 254
Cover bonds	0	0
Loans/credit in Sparebanken Sør	3 359 909	2 055 482

Sparebanken Sør Boligkreditt AS has a revolving credit facility with Sparebanken Sør that can be used to refinance outstanding bonds.

NOTE 22 - EMPLOYEES, MANAGEMENT AND REPRESENTATIVES

The company had no employees at 31 December 2017.

External board members receive a fixed annual fee determined by the General Meeting.

NOTE 23 - SHARE CAPITAL AND SHARE OWNERS

NOK Thousand						2016
Shareholders	Numbers of shares	Nominal value per share	Share capital (1)	Dividend (1)	Profit for the period (1)	Profit per share
Sparebanken Sør	100 000	5 250	525 000	0	185 817	1 858,17

NOK Thousand						2016
Shareholders	Numbers of shares	Nominal value per share	Share capital (1)	Dividend (1)	Profit for the period (1)	Profit per share
Sparebanken Sør	100 000	5 250	525 000	0	187 828	1 878,28

1) For equity movements and allocations, we refer to the equity statement.

NOTE 24 - SEGMENT REPORTING

The company consists of only one segment; lending to consumers in Norway. Please refer to Note 7 regarding the geographical break down of loans. The company's activity consists of residential mortgages up to 75% of the property's market value. None of the company's customers individually accounts for more than 10% of turnover. This applies to both 2017 and 2016.

NOTE 25 - ACCOUNTING EFFECTS OF TRANSITION FROM IAS 39 TO IFRS 9

On 1 January 2018, IFRS 9 Financial instruments will replace the current IAS 39, Financial instruments – Recognition and measurement. IFRS 9 includes requirements for recognition, derecognition, classification and measurement of financial assets and liabilities, as well as hedge accounting. From this point in time, the company will change its accounting policies in accordance with the new standard. The company has not chosen to make use of an early adaptation of IFRS 9, which means that all corresponding figures from previous periods have been prepared according to IAS 39.

The standard will be implemented retrospectively, with hedge accounting as an exception. Retrospective application means that Sparebanken Sør Boligkreditt AS will prepare the opening balance of 1 January 2018 as if the new principles had always been applied. The effect of the new accounting policies on the opening balance sheet for 2018 is charged to equity.

Recognition and derecognition

Financial assets and liabilities are initially recognised when the company becomes a party to the contractual provisions of the instrument. A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire, or the company transfers the financial asset in such a way that the risk and profit potential of the asset concerned is largely transferred. A financial liability is derecognised when the financial liability has been fulfilled, cancelled or has expired.

Classification and measurement of financial instruments

The measurement category is finally determined upon initial classification of the asset.

Compared with IAS 39, IFRS 9 has a more principle-based approach, as regards the assessment of whether financial assets must be measured at amortized cost or at fair value. The measurement categories for financial assets in IAS 39 (fair value through profit or loss, available for sale, held-to-maturity and amortised cost) have been replaced by the following three categories in IFRS 9: fair value with changes in value through profit, fair value with change in value through other comprehensive income (OCI) and amortised cost. Measurement of the financial asset is determined upon initial recognition of the asset. The business model for holding the financial instruments will be decisive for the choice of category. The principles for financial liabilites will essentially be the same, with a few exceptions. This concerns changes in value from own credit risk, where the liability is measured by using the fair value option and recognised through other comprehensive income (OCI).

Financial instruments held to collect contractual cash flows are initially measured at amortised cost.

Financial instruments held to collect contractual cash flows and for sale are initially measured at fair value through other comprehensive income (OCI).

Instruments with cash flows that are not solely payments of interest and or where the purpose of owning the instrument is not to collect contractual cash flows, will be measured at the fair value through profit and loss.

Derivatives used in hedge accounting are measured according to the hedge accounting policies. See separate section.

Upon transition to the new standard on 1 January 2018, we see the following changes in the balance sheet items.

NOK thousand	IAS 39		IFRS 9		
Financial assets	**Measurement**	**Book value**	**Measurement**	**Book value**	**Change**
Loans to and receivables from credit institutions	Amortized cost	152 957	Amortized cost	152 957	0
Net loan to customers	Amortized cost	30 967 963	Amortized cost	30 963 735	-4 228
Bonds and certificates	Fair value	808 817	Fair value	808 817	0
Financial derivatives	Fair value	368 812	Fair value	368 812	0
Financial liabilities	**Measurement**	**Book value**	**Measurement**	**Book value**	**Change**
Debt to credit institutions	Amortized cost	3 360 846	Amortized cost	3 360 846	0
Debt incurred due to issue of securities	Amortized cost	26 504 804	Amortized cost	26 504 804	0
Financial derivatives	Fair value	22 975	Fair value	22 975	0

All changes are dues to the new measurement model.

Amortised cost

Debt instruments whose sole purpose is to hold the instrument in order to collect contractual cash flows will be recognised at amortised cost. In the company, all borrowing and lending with floating interest rates are classified at amortized cost.

Fair value through profit

All derivatives will be measured at fair value with the changes in value through profit and loss. Derivatives designated as hedging instruments will be recognized in accordance with hedge accounting principles.

Sparebanken Sør Boligkreditt AS has also chosen to keep holdings of interest-bearing liabilities, certificates and shares at fair value through profit and loss. These are assets and liabilities that are managed, measured and reported to the management at fair value.

Hedge accounting

IFRS 9 simplifies the hedge accounting requirements by linking hedging efficiency more closely to risk management activities, and thus provides greater scope for assessment. The requirement of a hedging efficiency of 80-125 percent has been removed and has been replaced by more qualitative requirements. Among other things, there must be an economic relationship between the hedging instrument and the hedged element, and the effect of credit risk must not dominate changes in value in the hedge relationship. In accordance with IFRS 9, a prospective efficiency test is sufficient, while the hedging efficiency in accordance with IAS 39 must be considered both retrospectively and prospectively. Inefficiency in hedging, defined as the difference between the value adjustment of the hedging instruments and the value adjustment of the hedging item is recognised in the income statement as it occurs. The exception is the part of the value adjustment that is due to a change in the basic spread associated with the hedging instruments.

For interest and currency swaps created from and including 1 January 2018, the changes in value due to changes in spreads, will be recognised through other comprehensive income as a hedging effect. Interest and currency swaps created prior to 1 January 2018 will be recorded at fair value through profit and loss until these mature.

Impairment and calculation of expected loss on 1 January 2018

In accordance with IAS 39, impairment losses have been based on objective evidence of impairment, an incurred loss model. In accordance with IFRS 9, from 1 January 2018 impairment losses will be based on an expected loss model. The impairment model under IFRS 9 has been described below. Calculation of the expected loss for the company as of 1 January 2018 results in an increase in total impairment losses of NOK 4.2 million. The implementation of IFRS 9 will have an insignificant effect on the equity and subordinated capital, and the company has no need to use the transitional

Changes in equity

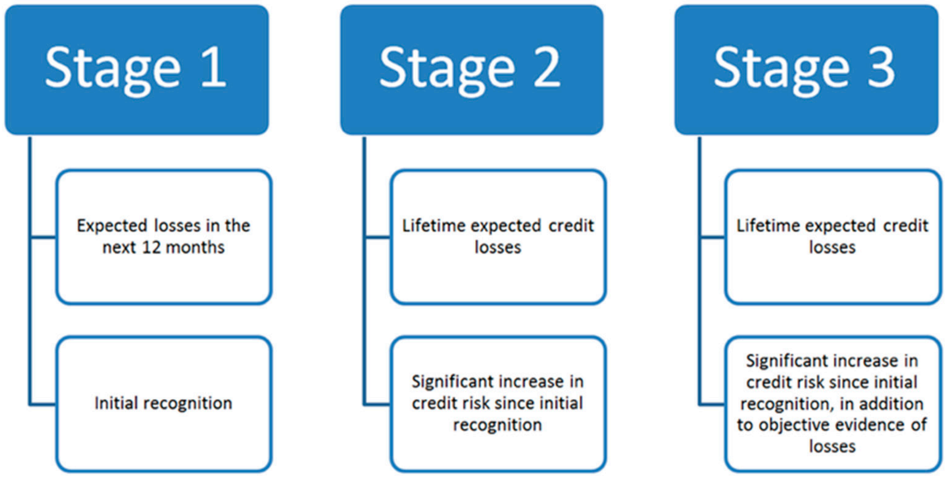
NOK thousand	Equity capital	Share premium reserve	Retained earnings	TOTAL
Balance as at 31.12.2017	**525 000**	**500 000**	**1 351 730**	**2 376 730**
Changes as a result of IRFS 9			-4 228	-4 228
Effect on taxes as a result of IFRS 9			1 057	1 057
Balance as at 1.1.2018	**525 000**	**500 000**	**1 348 559**	**2 373 559**

Impairment model

The model for impairment of financial assets under IFRS 9 applies to financial assets that are measured at amortised cost and financial assets that are measured at fair value through other comprehensive income. The new standard also requires loan loss provisions on new loans by making an impairment for expected credit loss due to expected defaults over the next twelve months. The model calculates the expected losses for all customers at account level. The model also includes loan commitments, guarantees and unused credit facilities. For loans where the credit risk has increased significantly since initial recognition, impairment should be recorded corresponding to expected credit losses over the term of the loan. This sets high requirements for the models used to calculate expected impairment losses.

Through 2017, the company has worked on model development in order to be able to meet the new requirements.

The model contains data for macro-conditions, and in the event of cyclical variations or macro-conditions, the relevant parameters must be changed accordingly before the model can be run. The model calculates the expected losses for all customers at account level. All loan commitments are placed in one of the three "stages" of the model based on their change in risk since initial recognition (change in credit risk). For a description of each "stage", refer to the explanations below. On initial recognition, all commitments are placed in stage 1 and are moved at a later date to stage 2 or 3 in the cases where there has been a significant increase in credit risk. For commitments where individual write-downs for impairment have been made, these are removed from the calculation basis for the model-based loss impairments, and the individual write-downs for impairment are added to write-downs for impairment in stage 3.



Stage 1

In most cases, this is the starting point for all financial assets that come under the general impairment model. Financial instruments that have the same credit risk as at initial recognition and which have not been classified under stage 2 and 3 comes under this stage. The estimated expected losses recognised in the balance sheet are equivalent to the expected losses over the next 12 months.

Stage 2

The financial assets that have had a significant increase in credit risk since initial recognition are placed in stage 2. Whether an account commitment has been significantly deteriorated or not, is defined as a function of the probability of default (PD) at the measurement date and the probability of default on the date of initial recognition (loan approval) . Expected losses on assets in stage 2 are calculated over the remaining term of the asset.

The model has the following additional indicators and overriding rules for customer commitments (loans to customers):

- For commitments that qualify for a one-year loss calculation (stage 1), it will be checked whether there is a 30-day default/account overdrawn. If this exists, the loan commitment will be transferred to lifetime ECL (stage 2). This applies to overdraws from the first krone, but older than 30 days.
- For commitments that qualify for a one-year loss calculation (stage 1), it will be checked whether there is a larger overdraw. If this exists, the loan commitment will be transferred to lifetime ECL (stage 2). This applies to overdraws exceeding the credit limit, starting from the first day.
- Commitment with changed payment obligations or refinancing (forbearance) is automatically moved to stage 2.
- An internal "watchlist" is also used to monitor certain commitments that have been deemed to potentially constitute a higher future risk of losses.

Stage 3

Stage 3, includes assets that have had a significant change in credit risk since initial recognition and where there is objective evidence of loss at the time of reporting. The bank has defined this as commitments in default or commitments where individual write-downs have been made. In this stage, the model calculates an expected loss over the remaining term of the asset. If individual write-downs have been made, these override the model-based calculation.

The model used by Sparebanken Sør Boligkreditt AS is the same model used by the parent bank Sparebanken Sør. Estimated losses will be calculated on the basis of 12 months probability of default (PD), loss given default (LGD) and exposure at default (EAD). The data basis contains historical data about the observed PD and LGD. This will form the basis for producing estimates of future PD and LGD values. The bank's PD model gives PD at individual customer level, one year ahead. The bank does not have a lifetime PD model. When calculating the expected credit loss over the lifetime of the commitment it is the probability of default over the same lifetime that should be used.

The assessment of significance is based both on a relative increase in PD and absolute change. The level has been set so that the relative change is significant and that the absolute level in itself is not insignificant compared with what is considered low risk. In addition, if there is a major absolute change, it should nevertheless be considered significant.

Estimated loss as of 1 January 2018 based on the various stages in the model.

Stage	Credit commitments	In %	Calculated loss	In %
1	30 302 220	91.1 %	1 643	16.1 %
2	2 941 231	8.8 %	8 191	80.1 %
3	17 923	0.1 %	393	3.8 %
Total	**33 261 373**	**100.0 %**	**10 228**	**100.0 %**

NOTE 26 – SUBSEQUENT EVENTS

Events of major significance to the accounts have not occurred after the balance sheet date.

In order to obtain sufficient equity to meet future expected growth, the Board of Directors in December 2017 adopted to increase the equity capital by NOK 600 million. As a result, in January 2018, the share capital will be increased from NOK 525 million to NOK 1 125 million.

Declaration from the Board of Directors and Managing Director

Declaration in accordance with Section 5-5 of the Securities Trading Act

The Board of Directors and Managing Director of Sparebanken Sør Boligkreditt AS hereby confirm that the Company's 2017 financial statements have been prepared in accordance with applicable accounting standards and that the information provided in the financial statements gives a true and fair view of the Company's assets, liabilities, financial position and overall result of operations.

In addition, we confirm that the Report of the Board of Directors gives a true and fair view of the Company's development, results and financial position, together with a description of the most central risks and uncertainties facing the Company.

Kristiansand, 26 February 2018

The Board of Directors of Sparebanken Sør Boligkreditt AS

Geir Bergskaug	Seunn Smith-Tønnessen	Gunnar P. Thomassen	Bjørn Friestad
Chairman	Member	Member	Member

Marianne Lofthus
Managing Director

To the General Meeting of Sparebanken Sør Boligkreditt AS

Independent Auditor's Report

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Sparebanken Sør Boligkreditt AS which comprise the balance sheet as at 31 December 2017, income statement, other comprehensive income, equity statement and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

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

Basis for Opinion

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

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

The company's business activities have largely remained unchanged during 2017. We have not identified regulatory changes, transactions or events that materially affect the financial statements for 2017. The focus areas of our audit have been the same in 2017 as in the previous year.

Key Audit Matter	How our audit addressed the Key Audit Matter
Loans to customers and regulations related to cover pool	
Sparebanken Sør Boligkreditt AS has provided mortgage loans to private individuals, secured by real estate, that are subject to special requirements related to	In accordance with regulations, the company has engaged us as independent investigator to test, each quarter, that the cover pool fulfils the requirements for companies that issue covered bonds. Our procedures

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Statsautoriserte revisorer, medlemmer av Den norske Revisorforening og autorisert regnskapsførerselskap

over-collateralisation and has issued covered bonds. Processes have been implemented to ensure the company complies with the requirements related to the cover pool when covered bonds are issued. The processes include formal controls and segregation of duties to ensure controls have been performed prior to sale of loans from the parent company to Sparebanken Sør Boligkreditt AS.

We focused on this area because compliance with regulations is fundamental to the company's operation.

See note 6 in the annual report for information on the cover pool.

included assessment and testing of the company's systems and controls as well as scrutinizing documentation on the composition and value of the cover pool. Further, we performed sample testing of loans sold from the parent company to Sparebanken Sør Boligkreditt AS during the year to test whether these loans fulfilled the requirements. Our procedures showed that the company complied with the requirements for companies that issue covered bonds.

IT systems supporting financial reporting

We focused on this area because the company's financial reporting system and business as a whole are dependent on complex IT systems. Potential weaknesses in automated processes and related IT dependent manual controls may disrupt the continuous operation of the IT systems and cause risk of misstatements.

The company used external service organisations to operate certain key IT systems. The auditors of the respective service organisations evaluated design and tested operating effectiveness of the controls addressing integrity of the IT systems that are relevant to financial reporting. We satisfied ourselves regarding the auditor's objectivity and competence and examined the reports received and assessed potential weaknesses and remediation initiatives. We also performed testing of access controls related to the company's IT systems and segregation of duties where this was considered necessary to our audit.

Our assessments and tests showed that we could rely on the IT systems relevant to our audit.

Other information

Management is responsible for the other information. The other information comprises the Board of Directors' report, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

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

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

The Board of Directors and the Managing Director (management) are responsible for the preparation in accordance with law and regulations, including fair presentation of the financial statements in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with laws, regulations, and auditing standards and practices generally accepted in Norway, including ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with laws, regulations, and auditing standards and practices generally accepted in Norway, including ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error. We design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.

- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

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

Report on Other Legal and Regulatory Requirements

Opinion on the Board of Directors' report

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

Opinion on Registration and Documentation

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

Kristiansand, 26 February 2018
PricewaterhouseCoopers AS

Reidar Henriksen
State Authorised Public Accountant

Note: This translation from Norwegian has been prepared for information purposes only.

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