Principles of Balance Sheet Management (ALM)

Risk factors that are affecting both sides of balance sheet contribute considerably to economic values of insurance liabilities, market value of assets, risks and capital need. According to Sampo's definitions ALM risks include in addition to interest rate-, inflation- and FX-risk also liquidity risk and behavioural risks affecting maturities of insurance policies and some asset classes. Risk definitions related to ALM risks may be found in Appendix 2 (Risk Definitions).

ALM risk profiles are thoroughly analysed and taken into account for instance when investment policies are designed, insurance products are developed and internal capitalization targets are set.

In Sampo Group **companies,** insurance liabilities are the starting point for investment policy designing. Insurance liabilities are modelled and analysed to form an understanding of their expected future cash flows and their sensitivities to changes in factors such as inflation, interest rates and foreign exchange rates. Secondly, the solvency position at a time and its target levels (rating-agency and regulatory) and risk appetite define the general capacity and willingness to take market risks and liquidity risk. The stronger the solvency position and the higher the risk appetite, the more the investment portfolio can potentially differentiate from a portfolio replicating cash flows of insurance liabilities. Sampo Group companies manage their investment portfolios within the limits set on Investment Policies on a daily basis as described in more detail at section Principles of Investment Portfolio Management.

In Sampo Group, operative liquidity risk is managed by the legal entities, which are responsible for liquidity planning and maintaining adequate liquidity buffers. Liquidity risk is monitored based on the expected cash flows resulting from assets, liabilities and other business. In the subsidiaries, the adequacy of liquidity buffers is dependent on the underwriting cash flows. In the parent company, the adequacy of liquidity buffers is dependent also on potential strategic arrangements and strong liquidity and capacity to generate more liquidity if needed is generally preferred.

Since there is no unambiguous technique to quantify the capital need for liquidity risk, it is not directly taken into account in the internal capital need estimates. Thus only the interest rate, inflation and FX-risks of the ALM risks are accounted for in the capital need framework.

One form of liquidity risk is the access to markets when needed. Sampo Group companies maintain good business relationships with several creditworthy counterparties which mitigate the risk that Group is not able to enter into reinsurance or derivative transactions when needed.

At Group level Sampo plc monitors the ALM-profiles of the companies and may adjust its own risk profiles to mitigate the risks at group level. Because of this the major portion of Sampo's debt is tied to short term interest rates. Hence, risk profile of Sampo plc is opposite to daughter companies.