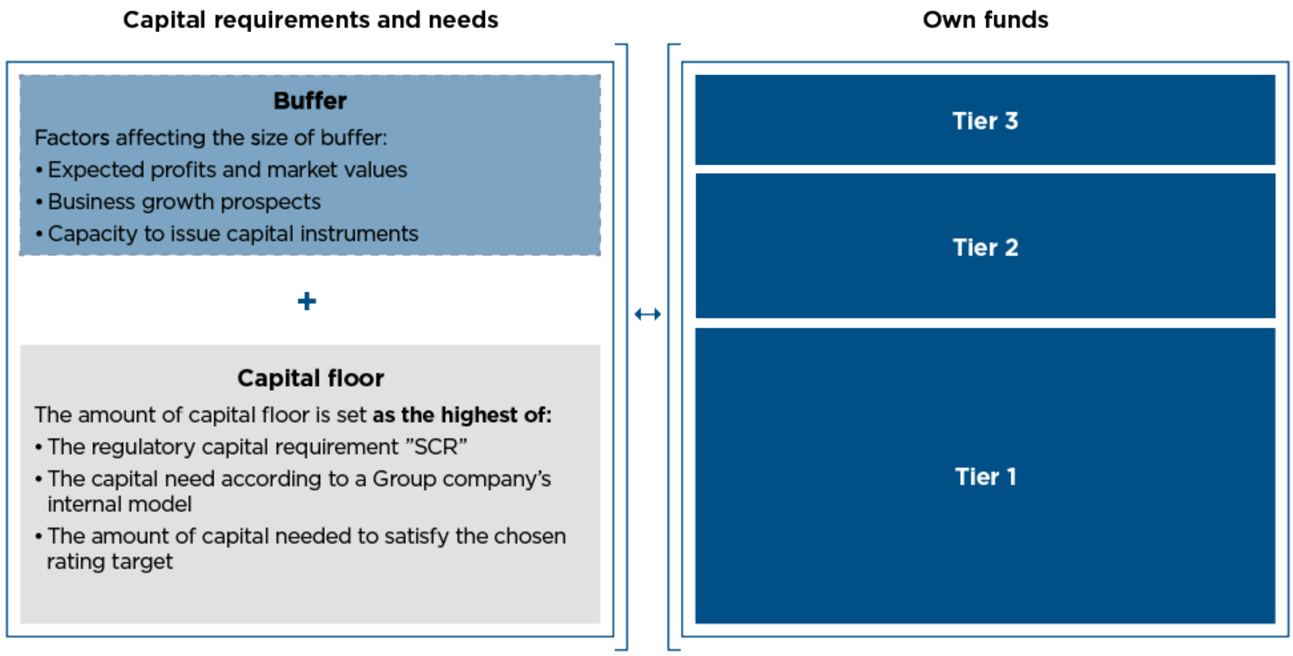
Capitalization at the Sub-Group Level

As noted earlier, in Sampo Group the first priority is to maintain **a balance between profits, risks and capital** in each of the separate business areas.

In a nutshell a balance between profits, risks and capital means that the actual amount of capital – or Own Funds ("OF") in Solvency II terminology - is maintained over risk based capital need with a certain buffer; the size of this buffer is dependent on many things but mainly on expected profitability.

The figure Sampo Group Companies' Capitalization Framework illustrates Sampo's approach to sub-group and company-level capitalization.

Sampo Group Companies' Capitalization Framework



The Solvency Capital Requirement ("SCR") sets the minimum level of capital at which a company is able to conduct its business without regulatory intervention. Regardless of whether the regulatory capital requirement is calculated using the internal model or the standard formula ("SF"), it reflects a 99.5 per cent confidence level, i.e. the same probability of default as a Triple-B rating from major rating agencies. If the company's clients and counterparties prefer a higher than Triple-B creditworthiness from their insurance company, the level of capital must always be higher than the SCR, to ensure the company's ability to serve its client base.

To serve its current clients, If P&C is maintaining a Single-A rating which effectively implies that If P&C's capital floor – the level to which it compares its actual capital – is higher than the SCR. Mandatum Life and Topdanmark consider the SCR to be an adequate capital floor. Topdanmark's group solvency is calculated according to Solvency II rules. Topdanmark uses a partial internal model to calculate the non-life insurance risk and the volatility-adjustment when calculating technical provisions, which are both approved by the Danish FSA.

There is a need to have a certain **buffer** between the actual amount of capital and the capital floor defined by the company, because risk exposures and profits evolve continuously over time and capital can sometimes erode rapidly due to stressed situations. An adequate buffer gives time for the company to adjust its risks and capital in times of stress and to maintain the balance between risks and capital. An adequate buffer also gives confidence to supervisors and counterparties (this being the other motivation for the buffer).

In Sampo Group the management steers the balance between SCRs and rating agency capital target and OF through their decisions on risk profiles, dividend payments, capital instrument issuances and technical provisions. In the long run a sound profitability and satisfied clients are the most important factors in maintaining an adequate capitalization.

The following factors are the most material when the size of buffer is considered in Sampo Group companies:

- The higher **the level of expected profits** and the lower **the volatility of profits and market value of balance sheet**, the less is the volatility of own funds and thus the smaller is the buffer.
- If **business is growing**, the buffer is larger than in the case of a run-off -business. For instance in Mandatum Life, capital consuming with profit business has already been in a virtual run-off mode for years.
- More ability and **capacity to issue SII compliant capital instruments** means that a lower buffer is needed.

When the balance between profits, risks and capital is met, the following three goals of Sampo Group are simultaneously obtainable:

i. The business activities can be conducted without supervisory intervention.
ii. The business activities can be conducted with all targeted client bases and the company has access to financial and debt issuance markets at terms and conditions implied by the company's creditworthiness.
iii. The targeted dividends can be paid to shareholders in the long run without endangering the balance between risk and capital.

On a sub-group and company level, a target can also be set for the **capital structure**. In general, Sampo Group is in favor of strong capital structures and as a result Sampo Group companies currently have, according to SII rules, room for new hybrid capital and subordinated debt instruments in their balance sheets.

In regards to **Nordea**, the Swedish requirements for banks' capital include components, which are country-specific and thus the total requirement is higher than in many other countries. The Swedish FSA has communicated the capital requirement for Nordea. Nordea's capital policy aims to maintain a management buffer of 50–150 basis points above the capital requirement. By the end of third quarter 2017, the communicated Common Equity Tier 1 ("CET1") ratio requirement for Nordea was 17.4 per cent.

The CET1 ratio of Nordea increased to 19.5 per cent (18.4 per cent) in 2017. The CET1 capital amounted to EUR 24.5 billion and its own funds were EUR 31.7 billion. Nordea's capital requirement based on the transitional rules was EUR 16.2 billion; without the transitional rules it was EUR 10.1 billion. Sampo consolidates its share of all Nordea's own funds items and minimum capital requirement to Group solvency under both Solvency II and conglomerate rules. From Sampo Group's perspective, Nordea is strongly capitalized and its contribution to Group's own funds and capital requirement is significant. Nordea's contribution to Sampo Group's capital requirement changes with effect from Q1/18 as so called transitional rules (Basel I floor) expire in Sweden and Sampo starts to use Minimum requirement for Own funds as defined in Nordea's quarterly Factbook as a capital requirement in Group solvency.