

OP Mortgage Bank: Financial Statements Bulletin for 1 January– 31 December 2018

OP Mortgage Bank (OP MB) is part of OP Financial Group and its role is to raise, together with OP Corporate Bank plc, funding for OP from money and capital markets. OP MB is responsible for the Group's funding for the part of covered bond issuance.

Financial standing

OP MB's intermediary loans and loan portfolio increased to EUR 13,771 million (13,580)*. OP MB issued a one billion-euro fixed-rate covered bond with a maturity of 7.25 years in international capital markets in June. The bond was intermediated in its entirety to OP cooperative banks in the form of intermediate loans.

The November one billion-euro intermediary loan was implemented by expanding the intermediary loan model to include an existing bond maturing in 2024. On 31 December 2018, 122 OP cooperative banks had a total of EUR 6,776 million (4,776) in intermediate loans from OP MB.

The company's financial standing remained stable throughout the financial year. Operating profit amounted to EUR 16.2 million (19.3).

*The comparatives for 2017 are given in brackets. For income statement and other aggregated figures, January–December 2017 figures serve as comparatives. For balance-sheet and other cross-sectional figures, figures at the end of the previous financial year (31 December 2017) serve as comparatives.

Collateralisation of bonds issued to the public

The programme amount of the Euro Medium Term Covered Note programme established on 12 November 2010 under the Laki kiinnityspankkitoiminnasta (688/2010) Act (Covered Bond Act) was increased from EUR 15 billion to EUR 20 billion in December and loans in security of the covered bonds issued under the programme totalled EUR 13,700 million on 31 December 2018.

Capital adequacy

The Common Equity Tier 1 (CET1) ratio stood at 136.4% (109.5) on 31 December 2018. The CET1 capital requirement is 4.5% and the requirement for the capital conservation buffer is 2.5%, i.e. the total CET1 capital requirement is 7%. The minimum total capital requirement is 8% and 10.5% with increased capital conservation buffer. Earnings for the financial year were not included in CET1 capital.

OP MB uses the Internal Ratings Based Approach (IRBA) to measure its capital adequacy requirement for credit risk. OP MB uses the Standardised Approach to measure its capital adequacy for operational risk.

The Financial Supervisory Authority has set a 15% minimum risk weight on housing loans from the beginning of 2018 for at least two years. According to the Authority, this floor is aimed at preparing for a systemic risk related to household indebtedness. The minimum risk weight floor does not apply to OP MB but applies only to OP Financial Group level.

Joint and several liability of amalgamation

Under the Act on the Amalgamation of Deposit Banks, the amalgamation of the cooperative banks comprises the organisation's central cooperative (OP Cooperative), the central cooperative's member credit institutions and the companies belonging to their consolidation groups as well as credit and financial institutions and service companies in which the above together hold more than half of the total votes. This amalgamation is supervised on a consolidated basis. On 31 December

2018, OP Cooperative's member credit institutions comprised 156 OP cooperative banks as well as OP Corporate Bank plc, OP MB, OP Card Company Plc and OP Customer Services Ltd (formerly OP Process Services Ltd).

The central cooperative is responsible for issuing instructions to its member credit institutions concerning their internal control and risk management, their procedures for securing liquidity and capital adequacy as well as for compliance with harmonised accounting policies in the preparation of the amalgamation's consolidated financial statements.

As a support measure referred to in the Act on the Amalgamation of Deposit Banks, the central cooperative is liable to pay any of its member credit institutions an amount that is necessary to prevent the credit institution from being placed in liquidation. The central cooperative is also liable for the debts of a member credit institution which cannot be paid using the member credit institution's assets.

Each member bank is liable to pay a proportion of the amount which the central cooperative has paid to either another member bank as part of support action or to a creditor of such member bank in payment of an amount overdue which the creditor has not received from the member bank. Furthermore, in the case of the central cooperative's default, a member bank has unlimited refinancing liability for the central cooperative's debts as referred to in the Co-operatives Act.

Each member bank's liability for the amount the central cooperative has paid to the creditor on behalf of a member bank is divided between the member banks in proportion to their last adopted balance sheets. OP Financial Group's insurance companies do not fall within the scope of joint and several liability.

According to Section 25 of the Covered Bond Act, the holder of a covered bond has the right to receive a payment for the entire term of the bond from the assets entered as collateral before other receivables without this being prevented by OP MB's liquidation or bankruptcy.

Personnel

On 31 December 2018, OP MB had five employees. OP MB has been digitising its operations and purchases all the most important support services from OP Cooperative and its Group members, reducing the need for its own personnel.

The Representative Assembly of OP Bank Group Pension Fund, which manages statutory earnings-related pension for OP Financial Group, decided on 31 July 2018 to transfer the management of its pension liability and earnings-related pension insurance portfolio worth around EUR 1,068 million to Ilmarinen Mutual Pension Insurance Company. The transferred solvency capital totalled EUR 263 million. This decision was preceded by competitive bidding in which the Board of Trustees of OP Bank Group Pension Fund invited bids from the largest pension insurance companies. The insurance portfolio concerned accounted for some 90.8% of OP Bank Group Pension Fund's total pension liability. The transfer was executed on 31 December 2018. The transfer reduced OP Mortgage Bank's pension costs and improved its earnings before tax by EUR 150,000.

Management

The Board composition is as follows:

Chair	Vesa Aho	Chief Financial Officer, OP Cooperative
Members	Elina Ronkanen-Minogue	Head of ALM and Group Treasury, OP Cooperative
	Hanno Hirvinen	Head of Group Treasury, OP Corporate Bank plc

OP MB's Managing Director is Lauri Iloniemi, and his deputy was Hanno Hirvinen until 2 July 2018 and is Sanna Eriksson as of 3 July 2018.

The Chair of the Board of Directors was Harri Luhtala until 30 October 2018. Vesa Aho was appointed to member of the Board of Directors to replace Harri Luhtala as of 1 November 2018. He was also appointed the Board's Chair.

Risk exposure

The most typical types of risks related to OP MB are credit risk, structural funding risk, liquidity risk and interest rate risk. The key credit risk indicators in use show that OP MB's credit risk exposure is stable and the limit for liquidity risk set by the Board of Directors has not been exceeded. The liquidity buffer for OP Financial Group, managed by OP Corporate Bank, is exploitable by OP MB. OP MB has used interest rate swaps to hedge against its interest rate risk. Interest rate swaps have been used to swap housing loan interest, intermediary loan interest and interest on issued bonds into the same basis rate. OP MB has concluded all derivative contracts for hedging purposes, with OP Corporate Bank plc being their counterparty. The interest rate risk of OP MB may be considered low and it has been within the set limit.

Future outlook

It is expected that OP MB's capital adequacy will remain strong, risk exposure favourable and the overall quality of the loan portfolio good. This will make it possible to issue new covered bonds in 2019.

Executive Board's proposal on profit distribution

OP Mortgage Bank's equity capital on 31 December 2018

+ Share capital	60,000,000.00
+ Reserve for invested non-restricted equity	245,000,000.00
+ Profit for the financial year	12,999,001.24
+ Retained earnings	59,721,412.99
Total	377,720,414.23

Distributable funds totalled EUR 317,600,188.52.

As shown in the financial statements of 31 December 2018, the company's distributable earnings, which include EUR 12,999,001.24 in profit for the financial year, totalled EUR 72,600,188.52. The company's distributable funds totalled EUR 317,600,188.52.

The Board of Directors proposes that a dividend of EUR 169.71 be distributed per share, totalling EUR 12,998,428.32, and that following dividend distribution, the remaining amount of EUR 572.92 be recognised in retained earnings. Following dividend distribution, the company's distributable earnings total EUR 59,721,985.91 and its distributable funds total EUR 304,601,760.20.

The company's financial position has not undergone any material changes since the end of the financial year 2018. The company's liquidity is good and will not be jeopardised by the proposed profit distribution, in the Board of Directors' view.

Accounting policies

The Financial Statements Bulletin for 2018 has been prepared in accordance with IAS 34 (Interim Financial Reporting).

This Financial Statements Bulletin is based on unaudited figures. Given that all figures have been rounded off, the sum total of individual figures may deviate from the presented sums.

The Financial Statements Bulletin is available in Finnish and English. The Finnish version is official that will be used if there is any discrepancy between the language versions.

OP MB's related parties include the parent company OP Cooperative and its subsidiaries, the OP Financial Group pension insurance companies

OP Bank Group Pension Fund and OP Bank Group Pension Foundation, and the company's administrative personnel. Standard loan terms and conditions are applied to loans granted to the related parties. Loans are tied to generally used reference interest rates. The financial year saw no major changes in related-party transactions.

New standards and interpretations

IFRS 9 Financial Instruments

On 1 January 2018, OP MB adopted IFRS 9 Financial Instruments, issued by the IASB in July 2014 and approved by the EU in November 2016. For OP MB, the most significant change was that impairment losses are recognised on a more front-loaded basis, based on expected credit losses (ECL). IFRS 9 also entailed changes to accounting policies, adjustments to receivables recognised earlier in the balance sheet and changes to classification of financial instruments. Adjustments made to carrying amounts were recognised in retained earnings in the opening balance sheet on the adoption date. The effects of transition to IFRS 9 on the classification and measurement of financial instruments have been presented in OP MB's Notes to the Financial Statements 2017 and Interim Report for 1 January–31 March 2018. OP MB has not adjusted comparatives for prior years.

Adoption of IFRS 15 Revenue from Contracts with Customers on 1 January 2018

OP MB has applied IFRS 15, Revenue from Contracts with Customers, since 1 January 2018. In OP MB, IFRS 15 mainly applies to fees not included in the calculation of the effective interest rate.

Net commissions are presented in the notes to the Financial Statement. Net commissions are divided into groups according to commission income and expenses recorded from customer agreements. IFRS 15 did not change the revenue recognition time of the fees included in the scope of application of the standard in comparison with the previous practices. The adoption of IFRS 15 did not have any financial effect on OP MB's result. OP MB started to apply IFRS 15 using the retrospective transition method.

Changes made to the specification of net commissions that previously were only presented in the Financial Statements are presented below:

- Commission expenses "From lending" have been named "From lending to OP cooperative banks"
- Commission expenses "Service charges to banks" have been named "Loan management fee to OP cooperative banks"
- Commission expenses from "Securities" have been named "Issue of bonds"

Formulas for Alternative Performance Measures

The Alternative Performance Measures are presented to illustrate the financial performance of business operations and to improve comparability between reporting periods.

The calculation of the used Alternative Performance Measures is presented below.

Return on equity (ROE), % = Annualised profit for the period / Equity capital (average equity capital at the beginning and end of the period) × 100

Cost/income ratio, % = (Personnel costs + Depreciation/amortisation and impairment loss + Other operating expenses) / (Net interest income + Net commission and fees + Net investment income + Other operating income) × 100

Income statement, TEUR	Q4/2018	Q4/2017	Q1-4/2018	Q1-4/2017
Net interest income	17,279	20,249	71,893	74,984
Interest income	11,500	16,286	52,587	65,692
Interest expenses	-5,779	-3,964	-19,306	-9,292
Net commissions and fees	-11,317	-12,830	-49,193	-49,910
Net investment income	0	1	1	2
Other operating income	1	232	3	232
Total income	5,962	7,652	22,704	25,309
Personnel costs	-69	87	191	328
Depreciation/amortisation and impairment loss	156	209	783	836
Other operating expenses	1,308	1,175	5,099	4,528
Total expenses	1,395	1,471	6,073	5,692
Impairment loss on receivables	-417	-38	-382	-276
Earnings before tax	4,150	6,144	16,248	19,341
Income tax	830	1,229	3,249	3,868
Profit for the period	3,320	4,915	12,999	15,473

*Impairment losses on receivables have been calculated under IFRS 9 in 2018.

Statement of comprehensive income, TEUR	Q4/2018	Q4/2017	Q1-4/2018	Q1-4/2017
Profit for the period	3,320	4,915	12,999	15,473
Items that will not be reclassified to profit or loss				
Gains/(losses) arising from remeasurement of defined benefit plans	60	1	60	1
Income tax on gains/(losses) arising from remeasurement of defined benefit plans	-12	0	-12	0
Total comprehensive income for the financial period	3,369	4,916	13,047	15,473

Key figures	Q4/2018	Q4/2017	Q1-4/2018	Q1-4/2017
Return on equity (ROE), %	3.5	5.2	3.4	4.1
Cost/income ratio, %	23	19	27	22

Cash flow from operating activities, TEUR	Q1-4/2018	Q1-4/2017
Profit for the financial year	12,999	15,473
Adjustments to profit for the financial year	12,327	12,335
Increase (-) or decrease (+) in operating assets	-171,108	-2,681,266
Receivables from credit institutions	-2,000,000	-2,923,400
Receivables from the public and public sector entities	1,812,031	235,309
Other assets	16,861	6,826
Increase (+) or decrease (-) in operating liabilities	37,365	944,884
Liabilities to credit institutions and central banks	58,000	950,000
Other liabilities	-20,635	-5,116
Income tax paid	-2,505	-4,113
Dividends received	1	2
A. Net cash from operating activities	-110,920	-1,712,685
Cash flow from investing activities		
Purchase of PPE and intangible assets	0	0
B. Net cash used in investing activities	0	0
Cash flow from financing activities		
Increases in debt securities issued to the public	995,413	2,982,709
Decreases in debt securities issued to the public	-1,100,000	-1,350,000
Dividends paid and interest on cooperative capital	-15,424	-9,037
C. Net cash used in financing activities	-120,012	1,623,671
D. Effect of foreign exchange rate changes on cash and cash equivalents	0	0
Net change in cash and cash equivalents (A+B+C)	-230,932	-89,014
Cash and cash equivalents at year-start	363,609	451,787
Cash and cash equivalents at year-end	133,460	363,609
Change in cash and cash equivalents	-230,148	-88,178
Interest received	68,928	73,705
Interest paid	-478	-2,469
Adjustments to profit for the financial year		
Non-cash items		
Unrealised net gains on foreign exchange operations	0	0
Impairment losses on receivables	396	277
Price difference recognised on debt securities issued to the public	8,683	8,192
Other	3,248	3,866
Total adjustments	12,327	12,335
Cash and cash equivalents		
Receivables from credit institutions payable on demand	133,460	363,609
Total cash and cash equivalents	133,460	363,609

Balance sheet, TEUR	31 Dec. 2018	31 Dec. 2017
Receivables from credit institutions	6,909,630	5,139,778
Derivative contracts	139,668	129,810
Receivables from customers	6,994,873	8,803,822
Investment assets	40	40
Intangible assets	120	904
Other assets	32,525	49,386
Tax assets	0	705
Total assets	14,076,856	14,124,444
Liabilities to credit institutions	2,896,000	2,838,000
Derivative contracts	8,597	38,025
Debt securities issued to the public	10,742,840	10,796,102
Provisions and other liabilities	51,625	72,259
Tax liabilities	74	0
Total liabilities	13,699,135	13,744,387
Shareholders' equity		
Share capital	60,000	60,000
Invested unrestricted equity fund	245,000	245,000
Retained earnings	72,720	75,057
Total shareholders' equity	377,720	380,057
Total liabilities and equity capital	14,076,856	14,124,444

Off-balance-sheet commitments, TEUR	31 Dec. 2018	31 Dec. 2017
Irrevocable commitments given on behalf of customers	2	3

Statement of changes in equity, TEUR	Share capital	Other funds	Retained earnings	Total share-holders' equity
Shareholders' equity 1 Jan. 2017	60,000	245,000	68,622	373,622
Invested unrestricted equity fund				
Profit for the period			15,473	15,473
Other comprehensive income for the period			1	1
Other changes			-9,038	-9,038
Shareholders' equity 31 Dec. 2017	60,000	245,000	75,057	380,057
Shareholders' equity 31 Dec. 2017	60,000	245,000	75,057	380,057
Effect of IFRS 9 transition 1 Jan. 2018			90	90
Shareholders' equity 1 Jan 2018	60,000	245,000	75,147	380,147
Invested unrestricted equity fund				
Profit for the period			12,999	12,999
Other comprehensive income for the period			48	48
Other changes			-15,472	-15,472
Shareholders' equity 31 Dec. 2018	60,000	245,000	72,720	377,720

OP MB has presented its capital base and capital adequacy in accordance with the EU capital requirement regulation and directive (EU 575/2013).

Capital base and capital adequacy, TEUR	31 Dec. 2018	31 Dec. 2017
Shareholders' equity	377,720	380,057
Common Equity Tier 1 (CET1) before deductions	377,720	380,057
Intangible assets	-120	-904
Excess funding of pension liability	-66	-65
Share of unaudited profits	-12,999	-15,473
ECL - shortfall of expected losses	-1,962	-2,676
Common Equity Tier 1 (CET1)	362,573	360,940
Tier 1 capital (T1)	362,573	360,940
ECL - excess of expected losses	38	
Tier 2 Capital (T2)	38	
Total capital base	362,611	360,940
Total risk exposure amount		
Credit and counterparty risk	223,980	289,070
Operational risk	41,893	40,554
Total	265,873	329,623
Key ratios, %		
CET1 ratio	136.4	109.5
Tier 1 capital ratio	136.4	109.5
Capital adequacy ratio	136.4	109.5
Capital requirement		
Capital base	362,611	360,940
Capital requirement	29,924	349,700
Buffer for capital requirements	334,687	11,240

Net commissions and fees, TEUR	Q4/2018	Q4/2017	Q1-4/2018	Q1-4/2017
Commission income				
Lending	1,411	1,541	5,972	6,465
Total	1,411	1,541	5,972	6,465
Commission expenses				
From lending to OP cooperative banks	1,353	1,533	5,783	6,336
Loan management fee to OP cooperative banks	11,338	12,826	49,297	49,936
Issue of bonds	34	9	72	92
Other	3	2	13	11
Total	12,728	14,370	55,165	56,375
Net commissions and fees	-11,317	-12,830	-49,193	-49,910

Classification of financial assets and liabilities 31 Dec. 2018, TEUR				
Assets	Amortised cost	Recognised at fair value through profit or loss	Fair value through other comprehen- sive income	Total
Receivables from credit institutions and central banks	6,909,630			6,909,630
Derivative contracts		139,668		139,668
Receivables from customers	6,994,873			6,994,873
Shares and participations			40	40
Other receivables	32,525			32,525
Other assets	120			120
Total	13,937,148	139,668	40	14,076,856
Liabilities		Recognised at fair value through profit or loss	Amortised cost	Total
Liabilities to credit institutions			2,896,000	2,896,000
Derivative contracts		8,597		8,597
Debt securities issued to the public			10,742,840	10,742,840
Other liabilities			51,698	51,698
Total		8,597	13,690,539	13,699,135
Valuation difference of debt securities issued to the public (difference between fair value and carrying amount) 31 Dec. 2018			140,345	140,345
Classification of financial assets and liabilities 31 Dec. 2017, TEUR				
Assets	Loans and other receivables	Recognised at fair value through profit or loss	Available for sale	Total
Receivables from credit institutions and central banks	5,139,778			5,139,778
Derivative contracts		129,810		129,810
Receivables from customers	8,803,822			8,803,822
Shares and participations			40	40
Other receivables	49,386			49,386
Other assets	1,609			1,609
Total	13,994,594	129,810	40	14,124,444
Liabilities		Recognised at fair value through profit or loss	Other debts	Total
Liabilities to credit institutions			2,838,000	2,838,000
Derivative contracts		38,025		38,025

Debt securities issued to the public			10,796,102	10,796,102
Other liabilities			72,259	72,259
Total		38,025	13,706,362	13,744,387
Valuation difference of debt securities issued to the public (difference between fair value and carrying amount) 31 Dec. 2017			158,358	158,358

Debt securities issued to the public are carried at amortised cost. The fair value of these debt instruments has been measured using information available in markets and employing commonly used valuation techniques. The difference between the fair value and carrying amount is presented as valuation difference in the Classification of financial assets and liabilities table.

Derivative contracts 31 Dec. 2018, TEUR	Nominal values / residual term to maturity			
	Less than 1 year	1–5 years	More than 5 years	Total
Interest rate derivatives				
Hedging	2,450,856	8,092,527	6,849,439	17,392,822
Total	2,450,856	8,092,527	6,849,438	17,392,822

	Fair values		Credit equivalent
	Assets	Liabilities	
Interest rate derivatives			
Hedging	139,688	8,597	319,910
Total	139,688	8,597	319,910

Derivative contracts 31 Dec. 2017, TEUR	Nominal values / residual term to maturity			
	Less than 1 year	1–5 years	More than 5 years	Total
Interest rate derivatives				
Hedging	2,648,299	7,824,977	8,561,488	19,034,765
Total	2,648,299	7,824,977	8,561,488	19,034,765

	Fair values		Credit equivalent
	Assets	Liabilities	
Interest rate derivatives			
Hedging	129,810	38,025	334,303
Total	129,810	38,025	334,303

Financial instruments classification, grouped by valuation technique, TEUR			
31 Dec. 2018	Fair value measurement at the end of reporting period		
	Balance sheet value	Level 1	Level 2
Recurring fair value measurements of assets			
Derivative contracts	139,668		139,668
Total	139,668		139,668
Recurring fair value measurements of liabilities			
Derivative contracts	8,597		8,597
Total	8,597		8,597
Financial liabilities not measured at fair value			
Debt securities issued to the public	10,742,840	10,738,905	144,280
Total	10,742,840	10,738,905	144,280

31 Dec. 2017	Fair value measurement at the end of reporting period		
	Balance sheet value	Level 1	Level 2
Recurring fair value measurements of assets			
Derivative contracts	129,810		129,810
Total	129,810		129,810
Recurring fair value measurements of liabilities			
Derivative contracts	38,025		38,025
Total	38,025		38,025
Financial liabilities not measured at fair value			
Debt securities issued to the public	10,796,102	10,710,871	243,589
Total	10,796,102	10,710,871	243,589

OP MB does not hold any transfers between the levels of fair value valuation.

Schedule for Interim Reports in 2019

Interim Report Q1/2019	7 May 2019
Interim Report H1/2019	30 July 2019
Interim Report Q1–Q3/2019	29 October 2019

Helsinki, 5 February 2019

OP Mortgage Bank
Board of Directors

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