OP MORTGAGE BANK
Stock exchange release 3 August 2016
Interim Report

OP Mortgage Bank Interim Report for January–June 2016

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

Financial standing

The intermediate loans and loan portfolio of OP MB increased to EUR 10,926 million (10,354)* during the reporting period. The company increased its on-balance sheet loan portfolio by buying mortgage-backed loans from OP Financial Group's member banks worth a total of EUR 413 million. In May, OP MB issued a fixed-rate covered bond with a maturity of seven years in international capital markets. Out of the bond with a nominal value of EUR 1,250 million, OP MB intermediated EUR 1,119 million in intermediate loans to OP Financial Group member cooperative banks. A total of 84 member cooperative banks have intermediate loans from OP MB, worth a total of EUR 1,863 million (743)*.

The company's financial standing remained stable throughout the reporting period. Operating profit for January–June amounted to EUR 11.0 (12.9) million.

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, intermediate loan interest and interest on issued bonds into the same basis rate. OP MB has entered into all derivative contracts for hedging purposes, with OP Corporate Bank plc being their counterparty.

*The comparatives for 2015 are given in brackets. For income statement and other aggregated figures, January–June 2015 figures serve as comparatives. For balance-sheet and other cross-sectional figures, figures at the end of the previous financial year (31 December 2015) serve as comparatives.

Collateralisation of bonds issued to the public

On 30 June 2016, loans as collateral in security of the covered bonds issued under the Euro Medium Term Covered Note programme worth EUR 15 billion established on 12 November 2010 under the Laki kiinnityspankkitoiminnasta (688/2010) (Covered Bond Act) totalled EUR 10,512 million.

Capital adequacy

OP MB has presented its capital base and capital adequacy in accordance with the EU capital requirement regulation and directive (EU 575/2013). 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 Common Equity Tier 1 (CET1) ratio stood at 137.0% (140.2) on 30 June 2016. The CET1 capital requirement is 4.5% and the requirement for the capital conservation buffer is 2.5%, or a total of 7%.

OP MB's highest minimum capital requirement is determined by the Basel I floor. OP MB's capital base exceeded the Basel I floor by EUR 31.7 million in June. Information on the Basel I floor and capital surplus can be found in note "Capital base and capital adequacy".

In June 2016, the Financial Supervisory Authority decided to take measures to set a 10% minimum risk weight on housing loans in an effort, according to the Authority, to prepare for an increased systemic risk. OP MB's loan portfolio consists of low-risk home loans, on which the Authority's decision has relatively the strongest impact. However, even after the entry into force of the minimum risk weight, OP MB's capital adequacy remains solid and clearly above the minimum levels set by authorities. The Financial Supervisory Authority's decision will most probably enter into force by the end of 2016.

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 30 June 2016, OP Cooperative's members comprised 178 member cooperative banks as well as OP Corporate Bank plc, OP Mortgage Bank, OP Card Company Plc and 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 30 June 2016, OP MB had five employees. The Bank purchases all the most important support services from OP Cooperative and its Group members, reducing the need for its own personnel.

Administration

The Board composition is as follows:

Chairman	Harri Luhtala	Chief Financial Officer, OP Cooperative
Members	Elina Ronkanen-Minogue	Head of Asset and Liability Management and Group Treasury, OP Cooperative
	Hanno Hirvinen	Group Treasurer, OP Corporate Bank plc

OP MB's Managing Director is Lauri Iloniemi and Hanno Hirvinen is his deputy.

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 plc, 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, intermediate loan interest and interest on issued bonds into the same basis rate. The interest rate risk may be considered to be low.

Outlook

The existing issuance programme makes it possible to issue new covered bonds in 2016. It is expected that the Bank's capital adequacy will remain strong, risk exposure favourable and the overall quality of the loan portfolio good.

Accounting policies

The Interim Report for 1 January–30 June 2016 has been prepared in accordance with IAS 34 (Interim Financial Reporting).

This Interim Report 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.

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.

Formulas for Alternative Performance Measures

The Alternative Performance Measures Guidelines issued by the European Securities and Markets Authority (ESMA) came into force on 3 July 2016. The Alternative Performance Measures are presented to illustrate the financial performance of business operations and to improve comparability between reporting periods. They should not be considered to be replacements for the performance measures defined in IFRS governing financial reporting.

The formulas for the used Alternative Performance Measures are presented below and they correspond to the previously presented performance indicators in terms of content.

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 + Other administrative expenses + Other operating expenses) / (Net interest income + Net commissions and fees + Net trading income + Total net investment income + Other operating income) × 100

Income statement, TEUR	H1/2016	H1/2015	Q2/2016	Q2/2015	2015
Interest income	45,898	54,746	21,598	27,544	106,362
Interest expenses	7,859	19,916	2,425	9,440	33,007
Net interest income	**38,039**	**34,830**	**19,173**	**18,104**	**73,355**
Impairment loss on receivables	-158	293	-91	343	210
Net commissons and fees	-24,176	-20,133	-12,020	-10,226	-43,361
Net trading income	0	0	0	0	0
Net investment income	2	1			22
Other operating income	1	1	0	0	1
Personnel costs	171	204	82	90	382
Other administrative expenses	1,529	1,181	787	569	2,612
Other operating expenses	1,000	754	577	353	1,924
Earnings before tax	**11,007**	**12,854**	**5,616**	**7,210**	**25,308**
Income tax expense	2,240	2,570	1,161	1,442	5,020
Profit for the period	**8,768**	**10,283**	**4,455**	**5,768**	**20,288**

Statement of comprehensive income, TEUR	H1/2016	H1/2015	Q2/2016	Q2/2015	2015
Profit for the period	8,768	10,283	4,455	5,768	20,288
Items that will not be reclassified to profit or loss					
Gains/(losses) arising from remeasurement of defined benefit plans					231
Income tax on gains/(losses) on arising from remeasurement of defined benefit plans					-46
Total comprehensive income	**8,768**	**10,283**	**4,455**	**5,768**	**20,473**

Key ratios	H1/2016	H1/2015	Q2/2016	Q2/2015	2015
Return on equity (ROE), %	4.8	5.7	4.9	6.4	5.6
Cost/income ratio, %	19	15	20	13	16

Cash flow from operating activities, TEUR	**H1/2016**	**H1/2015**
Profit for the financial year	8,768	10,283
Adjustments to profit for the financial year	3,213	5,398
Increase (-) or decrease (+) in operating assets	**-554,857**	**-264,840**
Receivables from credit institutions	-1,119,400	-19,969
Receivables from the public and public-sector entities	546,245	-272,837
Other assets	18,298	27,967
Increase (+) or decrease (-) in operating liabilities	**122,491**	**1,251,780**
Liabilities to credit institutions and central banks	143,000	1,285,000
Other liabilities	-20,509	-33,220
Income tax paid	-3,163	-859
Dividends received	2	1
A. Net cash from operating activities	**-420,385**	**1,002,622**
Cash flow from investing activities		
Purchase of PPE and intangible assets		-540
B. Net cash used in investing activities		**-540**
Cash flow from financing activities		
Increases in debt securities issued to the public	243,488	
Decreases in debt securities issued to the public		-980,003
Dividends paid and interest on cooperative capital	-16,282	-4,996
C. Net cash used in financing activities	**227,206**	**-984,999**
D. Effect of foreign exchange rate changes on cash and cash equivalents	**0**	**0**
Net change in cash and cash equivalents (A+B+C+D)	**-193,180**	**17,082**
Cash and cash equivalents at year-start	**245,120**	**109,046**
Cash and cash equivalents at year-end	**52,359**	**126,443**
Change in cash and cash equivalents	**-192,762**	**17,397**
Interest received	64,074	82,862
Interest paid	28,411	53,237
Adjustments to profit for the financial year		
Non-cash items		
Unrealised net gains on foreign exchange operations	0	0
Impairment losses on receivables	160	-292
Other	3,053	5,690
Total adjustments	**3,213**	**5,398**
Cash and cash equivalents		
Receivables from credit institutions payable on demand	52,359	126,443
Total cash and cash equivalents	**52,359**	**126,443**

Balance sheet, TEUR	30 June 2016	30 June 2015	31 Dec 2015
Receivables from credit institutions	1,915,128	156,412	988,490
Derivative contracts	315,908	191,919	192,206
Receivables from customers	9,063,453	9,600,216	9,610,252
Investments assets	40	40	40
Intangible assets	2,157	2,835	2,575
Other assets	60,525	62,080	78,823
Tax assets	0	2	0
Total assets	**11,357,211**	**10,013,505**	**10,872,386**
Liabilities to credit institutions	1,518,000	2,790,000	1,375,000
Derivative contracts	6,039	22,769	12,971
Debt securities issued to the public	9,380,372	6,748,760	9,002,669
Provisions and other liabilities	87,976	88,896	108,485
Tax liabilities	402	1,333	1,325
Total liabilities	**10,992,789**	**9,651,758**	**10,500,450**
Shareholders' equity			
Share capital	60,000	60,000	60,000
Reserve for invested unrestricted equity	245,000	245,000	245,000
Retained earnings	59,422	56,747	66,937
Total equity	364,422	361,747	371,937
Total liabilities and shareholders' equity	**11,357,211**	**10,013,505**	**10,872,386**

Off-balance-sheet commitments, TEUR	30 June 2016	30 June 2015	31 Dec 2015
Irrevocable commitments given on behalf of customers	51	1,822	858

Statement of changes in equity, TEUR	Share capital	Other reserves	Retained earnings	Total equity
Shareholders' equity 1 Jan 2015	**60,000**	**245,000**	**51,459**	**356,459**
Reserve for invested unrestricted equity				
Profit for the period			10,283	10,283
Total comprehensive income				
Other changes			-4,996	-4,996
Shareholders' equity 30 June 2015	**60,000**	**245,000**	**56,747**	**361,747**
Shareholders' equity 1 Jan 2016	**60,000**	**245,000**	**66,937**	**371,937**
Reserve for invested unrestricted equity				
Profit for the period			8,768	8,768
Total comprehensive income				
Other changes			-16,282	-16,282
Shareholders' equity 30 June 2016	**60,000**	**245,000**	**59,422**	**364,422**

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	**30 Jun 2016**	**31 Dec 2015**
Shareholders' equity	364,422	371,937
Common Equity Tier 1 (CET1) before deductions	**364,422**	**371,937**
Intangible assets	-2,157	-2,575
Excess funding of pension liability, indirect holdings and deferred tax assets for losses	-75	-74
Share of unaudited profits	-8,768	-20,288
Impairment loss – shortfall of expected losses	-2,325	-2,046
Common Equity Tier 1 (CET1)	**351,098**	**346,954**
Tier 1 capital (T1)	**351,098**	**346,954**
Total capital base	**351,098**	**346,954**
Risk-weighted assets		
Credit and counterparty risk	222,349	219,560
Operational risk	33,898	27,846
Total	**256,247**	**247,407**
Key ratios, %		
CET1 capital ratio	137.0	140.2
Tier 1 capital ratio	137.0	140.2
Capital adequacy ratio	137.0	140.2
Basel I floor		
Capital base	351,098	346,954
Basel I capital requirements floor	319,448	324,461
Capital buffer for Basel I floor	31,650	22,493

Classification of financial assets and liabilities 30 June 2016, TEUR				
Financial assets	**Loans and other receivables**	**Recognised at fair value through profit or loss**	**Available for sale**	**Total**
Receivables from credit institutions	1,915,128			1,915,128
Derivative contracts		315,908		315,908
Receivables from customers	9,063,453			9,063,453
Shares and participations			40	40
Other receivables	60,525			60,525
Other assets	2,157			2,157
Total	**11,041,263**	**315,908**	**40**	**11,357,211**
Financial liabilities		**Recognised at fair value through profit or loss**	**Other liabilities**	**Total**
Liabilities to credit institutions			1,518,000	1,518,000
Derivative contracts		6,039		6,039
Debt securities issued to the public			9,380,372	9,380,372
Other liabilities			88,378	88,378
Total		**6,039**	**10,986,750**	**10,992,789**
Valuation difference of debt securities issued to the public (difference between fair value and carrying amount) 30 June 2016			377,740	**377,740**

Classification of financial assets and liabilities 31 Dec 2015, TEUR				
Financial assets	**Loans and other receivables**	**Recognised at fair value through profit or loss**	**Available for sale**	**Total**
Receivables from credit institutions	988,490			988,490
Derivative contracts		192,206		192,206
Receivables from customers	9,610,252			9,610,252
Shares and participations			40	40
Other receivables	78,823			78,823
Other assets	2,575			2,575
Total	**10,680,140**	**192,206**	**40**	**10,872,386**
Financial liabilities		**Recognised at fair value through profit or loss**	**Other liabilities**	**Total**
Liabilities to credit institutions			1,375,000	1,375,000
Derivative contracts		12,971		12,971
Debt securities issued to the public			9,002,669	9,002,669
Other liabilities			109,810	109,810
Total		**12,971**	**10,487,479**	**10,500,450**
Valuation difference of debt securities issued to the public (difference between fair value and carrying amount) 31 Dec 2015			219,641	**219,641**

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" note.

Derivative contracts 30 June 2016, TEUR	Nominal values/residual term to maturity			
	Less than 1 year	1–5 years	More than 5 years	Total
Interest rate derivatives				
Hedging	2,705,096	8,316,977	6,861,177	17,883,250
Total	**2,705,096**	**8,316,977**	**6,861,177**	**17,883,250**

	Fair values		Credit
	Assets	Liabilities	equivalent
Interest rate derivatives			
Hedging	315,908	6,039	514,377
Total	**315,908**	**6,039**	**514,377**

Derivative contracts 31 Dec 2015, TEUR	Nominal values/residual term to maturity			
	Less than 1 year	1?5 years	More than 5 years	Total
Interest rate derivatives				
Hedging	2,387,456	8,816,977	7,118,958	18,323,391
Total	**2,387,456**	**8,816,977**	**7,118,958**	**18,323,391**

	Fair values		Credit
	Assets	Liabilities	equivalent
Interest rate derivatives			
Hedging	192,206	12,971	411,985
Total	**192,206**	**12,971**	**411,985**

Financial instruments classification, grouped by valuation technique, TEUR			
31 Jun 2016	**Fair value measurement at year end**		
	Balance sheet value	**Level 1**	**Level 2**
Recurring fair value measurements of assets			
Derivate contracts	315,908		315,908
Total	**315,908**		**315,908**
Recurring fair value measurements of liabilities			
Derivate contracts	6,039		6,039
Total	**6,039**		**6,039**
Financial liabilities not measured at fair value			
Debt securities issued to the public	9,380,372	9,376,175	381,937
Total	**9,380,372**	**9,376,175**	**381,937**

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

31 Dec 2015	Fair value measurement at year end		
	Balance sheet value	Level 1	Level 2
Recurring fair value measurements of assets			
Derivate contracts	192,206		192,206
Total	**192,206**		**192,206**
Recurring fair value measurements of liabilities			
Derivate contracts	12,971		12,971
Total	**12,971**		**12,971**
Financial liabilities not measured at fair value			
Debt securities issued to the public	9,002,669	8,872,880	349,430
Total	**9,002,669**	**8,872,880**	**349,430**

Helsinki, 3 August 2016

OP Mortgage Bank
Board of Directors

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