vestjyskBANK

Risk Report Addendum

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Introduction

The present risk report addendum has been prepared in accordance with the provisions set out in the Danish Executive Order on Capital Adequacy.

Risk report addenda are prepared quarterly in conjunction with the publication of the Bank’s solvency needs and are posted to the Bank’s website. Complete risk reports are published once annually in conjunction with the publication of the Bank's annual report for the previous year. In our assessment, both the published information and the frequency of publication are appropriate in relation to the Bank’s risk exposures. The disclosures have not been audited by internal or external auditors.

Adequate capital base and solvency need

Adequate capital base and individual solvency needs are calculated as distributed across the risk areas below.

	Calculation of solvency needs at 30 June 2013	Amount in TDKK	%
1	Column I requirement (8% of risk-weighted items)	1,830,932	8.0
+2	Earnings (capital designated for risk coverage as a result of weak earnings)	0	0.0
+3	Growth in loans (capital to cover organic growth in business volume)	0	0.0
+4	Credit risks, of which		
4a	Credit risks for major customers (2% of capital base) with financial problems	441,100	1.9
4b	Other credit risks	25,547	0.1
4c	Concentration risk of individual commitments	15,021	0.1
4d	Concentration risk by industry segments	0	0.0
+5	Market risks, of which		
5a	Interest rate risks	89,643	0.4
5b	Equity risks	0	0.0
5c	Exchange rate risks	0	0.0
+6	Liquidity risks (capital designated for coverage of more expensive liquidity)	0	0.0
+7	Operational risks (capital designated for coverage of operational risk in addition to Column I)	0	0.0
+8	Any statutorily required supplementary items	0	0.0
	Total capital need/solvency need	**2,402,243**	**10.5**

Commentary on solvency needs

Column I requirement (8% of risk-weighted items)

vestjyskBANK is subject to the requirement set out in section 124(2)(1) of the Danish Financial Business Act that its solvency must, at a minimum, constitute 8% of risk-weighted items.

Credit risk

In addition to what is covered by Column I, credit risk covers the risk of losses from debtor or counterparty defaults on payment obligations, including major customers with financial problems, concentration risk across individual commitments, and industry segments.

Major customers with financial problems

For major customers with financial problems, the Bank makes an assessment based on cautiously estimated losses for the individual commitment. Customers with financial problems comprise the following:

- Customers with objective indication of value impairment (OIV), and
- Customers with material signs of weakness but without OIV, credit quality category 2c.

Major commitments are commitments constituting at least 2% of the capital base.

The cautiously estimated loss represents the “net loss” that, based on a cautious and prospective assessment, may be lost if major commitments with customers with financial problems have to be settled due to default.

Other credit risks

The Bank performs an assessment of whether the general credit portfolio contains special credit risks (commitments below 2% of the capital base) not covered by the Column I requirement. For these commitments, the Bank has assessed a supplementary TDKK 25,547.

Concentration risk of individual commitments

Concentration risk across individual commitments represents risks associated with distribution across loan portfolio commitment amounts. The Bank determines the supplementary amount for concentration risk across individual commitments on the basis of the Financial Supervisory Authority’s "Guidelines on Adequate Capital Base and Solvency Needs of Credit Institutions.” In accordance with these guidelines, supplements are mandatory if the sum of the 20 largest commitments exceeds 4% of the commitment mass.

A supplement is required because the 20 largest commitments constitute 13%. In 2013, the supplement is weighted at 50%. The supplement will be phased in as of 2014. The Bank’s calculated supplement is TDKK 15,021

Concentration risk by industry segments

The concentration risk by industry segments covers risks associated with commitments' distributed across relatively few industry segments. The Bank determines concentration risk supplementary amounts across industry segments based on the Financial Supervisory Authority’s "Guidelines on Adequate Capital Base and Solvency Needs of Credit Institutions.” In accordance with these guidelines, the Bank uses the Herfindahl-Hirschman Index (HHI) to measure the degree of concentration across industry segments. Based on the HHI, the supplement is calculated as set out in the table below.

HHI	Supplement for adequate capital base/solvency need
HHI < 20%	0
20% < HHI < 25%	0.008*RWAindustry*(1-SRindustry)
25% < HHI < 30%	0.016*RWAindustry*(1-SRindustry)
30% < HHI < 40%	0.024*RWAindustry*(1-SRindustry)
40% < HHI < 60%	0.032*RWAindustry*(1-SRindustry)
60% < HHI < 100%	0.040*RWAindustry*(1-SRindustry)

A supplement is not taken because vestjyskBANK’s HHI has been calculated at 19.2%. In 2013, the supplement is weighted at 50%. The supplement will be phased in as of 2014.

Market risk

The market risk is the risk of losses owing to potential changes in interest rates, equity prices as well as foreign exchange rates, apart from what is covered in Column I. It is not based on vestjyskBANK’s current risk but on the maximum risk vestjyskBANK can assume within the limits established by the Supervisory Board for the Executive Board’s powers to assume market risks under section 70 of the Danish Financial Business Act.

The Bank bases its assessment whether all market risks have been adequately covered by Column I in the FSA's indicative benchmarks for interest rate risk, equity risk and foreign exchange rate risk. Based on these benchmarks as well as on an overall assessment of the Bank's market risks, it is the Bank's assessment that a supplement of TDKK 89,643 is required to cover market risks. Apart from the Column I requirement, the market risk supplement can be attributed to the interest rate risk for the Bank's fixed-rate deposits and subordinated debt. Market risk is primarily calculated by means of stress testing.

Operational risk

Operational risk comprises risk of losses resulting from inappropriate or defective internal procedures, human or system-related errors as well as external events, including legal risks, in addition to what is covered by Column I.

In assessing supplements for operational risks, the Bank considers these risk areas, including the Bank's organisation, cyber security and IT operations as well as the Bank's business model. On that basis, apart from what is covered in Column I, it is the Bank's assessment that a supplement is not needed.

Other risks

The Bank has performed an assessment of whether capital provisions should be made for hedging the risk of weak earnings, of organic growth in business volume and of more expensive liquidity from professional investors. It is the assessment that there is no need to make capital provisions to cover other risks.

Earnings

The Bank has based its assessment of whether extra capital provisions should be made to counter prospective credit losses across the Financial Supervisory Authority's relevant indicative benchmarks. The Bank has performed an assessment of core earnings in relation to total loans and guarantees. It is the assessment that there is no need to make capital provisions to cover weak earnings.

Growth

The Bank has based its assessment of whether extra capital provisions should be made for a growth in loans on the Financial Supervisory Authority's relative indicative benchmarks. It is the assessment that there is no need to make capital provisions to cover a growth in loans.

Liquidity

The Bank has a high liquidity surplus. In assessing whether capital provisions should be made as a result of additional costs related to raising liquidity, the Bank bases its estimate on the Bank's stress testing of liquidity for a one-year term. It is the assessment that there is no need to make capital provisions for raising liquidity.

Statutory requirements

The Financial Supervisory Authority has not established individual solvency requirements for vestjyskBANK.

Capital base and solvency ratio

The Bank’s capital structure, including solvency surplus, is detailed in the table below.

Capital structure and solvency surplus at 30 June 2013

	TDKK	%
Capital base less deductions/solvency ratio	2,552,990	11.2
Adequate capital base/solvency need	2,402,243	10.5
Surplus	**150,747**	**0.7**

The Bank’s surplus is reduced by 0.2 percentage points from 0.9% at 31 December 2012 to 0.6% at 30 June 2013. Management’s goal is to increase the surplus. The Bank’s Supervisory and Executive Boards will continue their efforts to execute the action plan set out in the Financial Statements and launch new measures to ensure that the Bank continues to meet the statutory solvency requirements and increases its surplus solvency.

Concluding remarks

For supplementary disclosures relating to risk management, please see the Bank's complete 2012 Risk Report as well as its 2012 Annual Report posted at www.vestjyskbank.dk.

The risk report will be updated in conjunction with the publication of the 2013 Annual Report.

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Vestjysk Bank A/S, Torvet 4-5, 7620 Lemvig, CVR 34631328