OP Mortgage Bank Report by the Board of Directors and Financial Statements 2018

Contents

REPORT BY THE BOARD OF DIRECTORS

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 OP Financial Group's funding for the part of covered bond issuance. OP MB has no independent customer business or service network, but OP cooperative banks manage customer relationships and loan management at local level.

OP MB either underwrites intermediary loans on banks' balance sheets or buys home loans in security for bonds from OP financial Group member cooperative banks.

OP MB's intermediary loans and loan portfolio increased to EUR 13,771 million (13,580)*.

In June, OP MB issued in international capital markets one fixed-rate covered bond with a maturity of 7.25 years that got the highest credit rating from credit rating agencies. OP MB intermediated the bond with a nominal value of EUR 1,000 million in its entirety to OP cooperative banks as intermediate loans. The November intermediary loan with a nominal value of EUR 1,000 million 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 (4,766) in intermediate loans from OP MB.

Joint and several liability

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 members comprised altogether 156 cooperative banks as well as OP Corporate Bank plc, OP Mortgage Bank, OP Card Company Plc and OP Customer 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.

By law, companies belonging to the amalgamation are liable for each other's debts. OP Financial Group's insurance companies do not fall within the scope of joint and several liability. The amalgamation's central cooperative, OP Cooperative, is obliged, if necessary, to assist member banks as a support action with a sum that prevents them from going into liquidation. The central cooperative is also liable for the debts of a member bank which cannot be paid using the member bank'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.

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.

*) 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.

Profit performance

OP MB's key financial indicators in 2018 are shown below:

Thousand euros	Q1–4/2018	Q1–4/2017
Income		
Net interest income	71,893	74,984
Net commissions and fees	-49,193	-49,910
Net investment income	1	2
Other operating income	3	232
Total	**22,704**	**25,309**
Expenses		
Personnel costs	191	328
Depreciation/amortisation and impairment loss	783	836
Other operating expenses	5,099	4,528
Total	**6,073**	**5,692**
Impairment loss on receivables	**-382**	**-276**
Earnings before tax	**16,248**	**19,341**

The company's financial standing remained stable throughout the financial year. Full-year earnings before tax came to EUR 16,248 thousand (19,341).

On-balance-sheet and off-balance-sheet commitments

OP MB's balance sheet total was EUR 14,077 million (14,124) on 31 December 2018. The table below shows the development of key assets and liabilities.

Key asset sand liabilities

Million euros	31 Dec. 2018	31 Dec. 2017
Balance sheet	14,077	14,124
Receivables from customers	6,995	8,804
Receivables from credit institutions	6,910	5,140
Debt securities issued to the public	10,743	10,796
Liabilities to credit institutions	2,896	2,838
Equity capital	378	380
Off-balance-sheet items	0	0

The bank's intermediary loans and loan portfolio increased to EUR 13,771 million (13,580) in January–December.

On 31 December 2018, households accounted for 99.9% (99.9) of the loan portfolio and institutional customers for 0.1% (0.1). On 31 December 2018, OP MB’s non-performing receivables totalled EUR 297 million (303).

The carrying amount of bonds issued to the public was EUR 10,743 million (10,796) at the end of the year. In addition to bonds, OP MB financed its operations through debt financing from OP Corporate Bank plc. At the end of the financial year, the amount of debt financing came to EUR 2,896 million (2,838).

OP MB has hedged its loan portfolio against interest rate risk by means of interest rate swaps. Interest rate swaps are used to swap base rate cash flows of hedged loans to Euribor cash flows. OP MB has also changed the fixed rates of the bonds it has issued to short-term market rates. OP MB's interest rate derivative portfolio totalled EUR 17,393 million (19,035). OP MB has concluded all derivative contracts for hedging purposes, with OP Corporate Bank plc being their counterparty.

Capital base and capital adequacy

OP MB has calculated its capital base and capital adequacy in accordance with the EU capital requirements regulation (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 136.4% (109.5) on 31 December 2018. The statutory minimum for CET1 ratio is 4.5% and for the capital adequacy ratio 8%. The requirement for the capital conservation buffer of 2.5% under the Act on Credit Institutions increases in practice the CET1 ratio to 7% and the minimum capital adequacy ratio to 10.5%.

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.

Capital base and capital adequacy, TEUR	**31 Dec. 2018**	**31 Dec. 2017**
Equity capital	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	-2 672
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	27,924	349,700
Buffer for capital requirements	334,687	11,240

Formulas for key ratios:

Common Equity Tier 1 (CET1) capital ratio, %

$$\frac{\text{CET1}}{\text{Total risk exposure amount}}$$

Tier 1 capital (T1) capital adequacy ratio, %

$$\frac{\text{Tier1}}{\text{Total risk exposure amount}}$$

Capital adequacy ratio, %

$$\frac{\text{Total capital base}}{\text{Total risk exposure amount}}$$

Financial indicators

Ratio	2018	2017	2016
Return on equity (ROE), %	3.4	4.1	4.8
Return on assets (ROA), %	0.09	0.12	0.16
Equity ratio, %	2.68	2.69	3.21
Cost/income ratio, %	27	22	19

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), %

$$\frac{\text{Operating profit (loss) - Income tax}^{*}}{\text{Equity capital (average of the beginning and end of year)}} \times 100$$

Return on assets (ROA), %

$$\frac{\text{Operating profit (loss) - Income tax}^{*}}{\text{Average balance sheet total (average of the beginning and end of year)}} \times 100$$

Equity ratio, %

$$\frac{\text{Equity capital}}{\text{Balance sheet total}} \times 100$$

Cost/income ratio, %

$$\frac{\text{Personnel costs + Depreciation/amortisation and impairment loss + Other operating expenses}}{\text{Net interest income + Net commissions and fees + Net investment income + Other operating income}} \times 100$$

* Includes tax effect from appropriations.

Risk management and capital adequacy management

OP Financial Group's core values, strategic goals and financial targets form the basis for OP MB’s risk management and capital adequacy management. In OP Financial Group’s risk policy, the central cooperative's Executive Board confirms annually risk-management principles, actions, objectives and limits to be applied by the Group and its entities that are used to guide business to implement the policies confirmed in the Group's strategy and the principles of the risk tolerance system.

The central cooperative is in charge of the OP Financial Group level risk and capital adequacy management. OP MB is responsible for its own risk and capital adequacy management in accordance with the nature and extent of its operations.

OP MB’s Board of Directors makes decision on its risk and capital adequacy management in line with the principles adopted by the central cooperative Executive Board. In addition, the Board of Directors deals with, in terms of quality and extent, far-reaching and important matters in principle from the perspective of the company’s operations, and any unusual matters. The Board of Directors decides on principles and procedures to ensure that the company operates in compliance with external regulation and OP Cooperative’s guidelines.

The Managing Director is responsible for the implementation of risk and capital adequacy management according to the principles and guidelines that have been agreed on, and reports regularly on the company’s business and financial standing.

OP MB's risk and capital adequacy tasks are centralised within OP Financial Group's Risk Management. Risk and capital adequacy management falls under internal control. Its purpose is to ensure OP MB’s risk capacity and liquidity and, thereby, ensure business continuity. Risk capacity is made up of effective risk management that is proportionate to the extent and complexity of operations and of adequate capital resources and liquidity based on profitable business operations.

Risk and capital adequacy management has been integrated as an integral part of the company’s business and management. OP MB focuses on carrying out its role according to its service capabilities and risk-bearing capacities in accordance with shared business models. OP MB has a moderate attitude towards risk-taking.

Risk-bearing capacity

OP MB's risk-bearing capacity remained good owing to retained earnings. Its capital adequacy ratio stood at 136.4% (109.5). The return on equity was 3.4% (4.1).

OP MB does not seek to secure its capital base by retaining earnings. Rather, OP Cooperative guarantees OP MB's capital base.

Credit risk exposure

OP MB's loan portfolio totalled EUR 6,995 million on 31 December 2018 (8,808). The quality of the loan portfolio is good. Doubtful receivables totalled EUR 297 million (303). Doubtful receivables refer to receivables that are more than 90 days past due, other receivables classified as risky and forborne receivables due to the customer's financial difficulties. Forbearance measures consist of concessions agreed at the customers' initiative to contractual payment terms towards the customer to make it easier for them to manage through temporary payment difficulties. OP cooperative banks make every effort to find solutions to overcome customers' temporary financial difficulties. Loan modifications due to reasons other than the customer's financial difficulties are not classified as doubtful receivables.

The company did not record any major impairment losses during 2018 or the previous years.

The company does not have any group of connected clients with the total amount of customer risk exceeding the limit set in the Act on Credit Institutions of 25% of the bank's capital base. Thanks to the loan portfolio's diversity and hard collateral, OP MB's credit risk exposure is highly stable.

Market risks and liquidity risk

Market risks include the following risks both on and off the balance sheet: interest rate risk, price risks and market liquidity risk. The company's products and market instruments, funding and investment principles and applied risk monitoring methods have been defined in the market risk management guidelines confirmed by the Board of Directors.

Interest rate risk means the effect of changing market interest rates on the company's earnings, profitability and capital adequacy. OP MB has used interest rate swaps to hedge against interest risk. Interest rate swaps are used to swap base rate cash flows of hedged home loans to Euribor cash flows. OP MB has also changed the fixed rates of the bonds it has issued to floating market rates. OP Corporate Bank plc is the counterparty to all derivative contracts.

The purpose of liquidity risk management is to secure the company's ability to fulfil its payment obligations without endangering business continuity, profitability or capital adequacy. OP MB monitors its cash flows on a daily basis to secure funding liquidity and its structural funding risk on a regular basis as a part of company's internal capital adequacy assessment process (ICAAP).

OP MB's Board of Directors monitors regularly that the company's interest rate and funding risk exposure remain within the limits it has set.

The provisions of the Act on Mortgage Credit Banks also set limits on the bank's interest rate and funding risk-taking. According to the Act, the total amount of interest received during any 12 months for loans forming the collateral for covered bonds must exceed the total amount of interest paid on covered bonds for the same period. Additionally, the average residual term to maturity of covered bonds must be shorter than the average residual term to maturity of the assets as their collateral. During the entire financial year, OP MB's operations have been in compliance with law, both in respect of the interest flow assessment and maturity assessment.

Operational risks

Operational risk refers to the risk of financial loss or other harmful consequences resulting from inadequate or failed processes, lack of skills, or incomplete or faulty procedures, systems or external events. Operational risk may also materialise in terms of loss or deterioration of reputation or trust. Operational risk management tools include identifying and analysing risks and by ensuring that controls and management tools are appropriate and adequate. The bank assesses operational risks regularly and reports its risk status to the Board of Directors once a year.

Compliance risk forms part of operational risk. Compliance activities are aimed at ensuring that OP MB complies with laws, official instructions and regulations, self-regulation of markets, and internal guidelines, policies and instructions of OP Financial Group and OP MB. Compliance also ensures that customer relationship management complies with appropriate and ethically sound principles and practices.

Personnel and remuneration schemes

On 31 December 2018, OP MB had five employees. The company purchases all the most important support services from OP Cooperative and its Group companies, reducing the its need for its own personnel.

OP MB belongs to OP Financial Group’s OP Personnel Fund, which forms a long-term remuneration scheme for employees. The company pays the Personnel Fund profit-based bonuses in accordance with pre-agreed principles. Members of the Fund may withdraw fund units on the grounds specified in Fund Rules.

Management

Board of Directors

The Board of Directors manages OP MB's business. According to the Articles of Association, the Board of Directors is responsible for the company's administration and appropriate organisation of operations. The Board of Directors has general authority to decide on all issues related to the governance and other matters that, by law, are not the responsibility of the Annual General Meeting or the Managing Director. The Board of Directors decides on the strategy and key business goals. The Board of Directors' duty is to ensure that accounting and financial management have been organised appropriately.

Board of Directors:

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

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.

According to the Articles of Association, OP MB’s Board of Directors comprises a minimum of three and a maximum of eight members. Currently, the Board has three members. Board members are elected for a period of one year. Their term begins upon closing of the Annual General Meeting that elected them and ends upon closing of the Annual General Meeting that elects the new Board. A Board member must resign after he/she reaches the age of 65 at the latest. The Board of Directors has a quorum when more than half of its members are present. The Board of Directors held 13 meetings in 2018.

Managing director

OP MB's Managing Director must advance the company's interests carefully and manage the bank's daily operations according to laws and the guidelines and regulations issued by the Board of Directors. The Managing Director may take measures which, considering the extent and nature of the company’s operations, are unusual or far-reaching in nature only if duly authorised by the Board of Directors, or if the Board of Director’s decision cannot be awaited without causing material harm to the company’s operations. It is the statutory duty of the Managing Director to ensure that the company’s accounting is in compliance with the applicable law and that the bank’s treasury is managed in a reliable manner.

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

OP MB's Corporate Governance Statement is available at op.fi.

Audit

KPMG Oy Ab, a firm of authorised public accountants, was elected as the company's auditor in 2018 by the Annual General Meeting. Raija-Leena Hankonen, APA, has been acted as chief auditor.

OP Cooperative’s Internal Audit is in charge of the company’s internal audit.

Future outlook

It is expected that the bank'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 as well.

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 funds, 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.

INCOME STATEMENT

EUR	Note	2018	2017
Net interest income	3	71 893 437,25	74 984 383,15
Net commissions and fees	4	-49 192 961,65	-49 909 859,39
Net investment income		992,95	1 777,41
Other operating income		2 675,37	232 283,17
Total income		**22 704 143,92**	**25 308 584,34**
Personnel costs	5	190 940,12	328 105,92
Depreciation/amortisation and impairment loss	6	783 380,85	835 860,83
Other operating expenses	7	5 099 082,82	4 527 637,13
Total expenses		**6 073 403,79**	**5 691 603,88**
Impairment losses on receivables	8	-382 338,59	-276 445,40
Earnings before tax		**16 248 401,54**	**19 340 535,06**
Income tax	9	3 249 400,30	3 867 693,16
Profit for the financial year		**12 999 001,24**	**15 472 841,90**
Earning/share (EPS), EUR		**169,72**	**202,02**
Profit for the financial year / Average share-issue adjusted number of shares during the period			

STATEMENT OF COMPREHENSIVE INCOME

EUR	2018	2017
Profit for the financial year	**12 999 001,24**	**15 472 841,90**
Items that will not be reclassified to profit or loss		
Gains/(losses) arising from remeasurement of defined benefit plans	60 433,00	626,00
Income tax on gains/(losses) arising from remeasurement of defined benefit plans	-12 086,60	-125,20
Total comprehensive income for the financial year	**13 047 347,64**	**15 473 342,70**

BALANCE SHEET

EUR	Note	31 Dec 2018	31 Dec 2017
Receivables from credit institutions	10	6 909 629 586,47	5 139 777 973,53
Derivative contracts	11	139 667 675,47	129 810 123,38
Receivables from customers	12	6 994 872 834,91	8 803 821 548,76
Investments assets	13	40 000,00	40 000,00
Intangible assets	14	120 225,71	903 606,56
Other assets	15	32 525 405,54	49 386 178,41
Tax assets	16	0,00	705 004,43
Total assets		**14 076 855 728,10**	**14 124 444 435,07**
Liabilities to financial institutions	17	2 896 000 000,00	2 838 000 000,00
Derivative contracts	18	8 596 795,34	38 025 334,93
Debt securities issued to the public	19	10 742 840 373,21	10 796 102 279,52
Other liabilities	16	51 624 642,58	72 259 345,07
Tax liabilities	17	73 502,74	0,00
Total liabilities		**13 699 135 313,87**	**13 744 386 959,52**
Shareholders' equity			
Shareholders' interest			
Share capital		60 000 000,00	60 000 000,00
Reserve for invested unrestricted equity		245 000 000,00	245 000 000,00
Retained earnings		72 720 414,23	75 057 475,55
Total equity	21	**377 720 414,23**	**380 057 475,55**
Total liabilities and shareholders' equity		**14 076 855 728,10**	**14 124 444 435,07**

CASH FLOW STATEMENT

TEUR	2018	2017
Cash flow from operating activities		
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		
B. Net cash used in investing activities		
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+D)	**-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		
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**

STATEMENT OF CHANGES IN EQUITY

TEUR		Share capital	Other reserves	Retained earnings	Total
Shareholders' equity on 1 January 2017	21	**60 000**	**245 000**	**68 622**	**373 622**
Reserve for invested unrestricted equity					
Profit for the financial year				15 473	15 473
Other comprehensive income for the period				1	1
Profit distribution				-9 038	-9 038
Shareholders' equity on 31 December 2017		**60 000**	**245 000**	**75 057**	**380 057**
Effect of IFRS 9 transition 1 Jan. 2018				**90**	**90**

	Share capital	Other reserves	Retained earnings	Total
Shareholders' equity on 1 January 2018	**60 000**	**245 000**	**75 147**	**380 147**
Reserve for invested unrestricted equity				
Profit for the financial year			12 999	12 999
Other comprehensive income for the period			48	48
Profit distribution			-15 472	-15 472
Shareholders' equity on 31 December 2018	**60 000**	**245 000**	**72 720**	**377 720**

NOTES TO THE FINANCIAL STATEMENTS

Table of contents for the notes to the financial statements

APPENDIX 1. Accounting policies

OP Mortgage Bank (OP MB) is a credit institution engaged in mortgage banking in Finland.

The company is part of an amalgamation of cooperative banks (OP Financial Group). Ultimately, OP Cooperative and its member credit institutions are liable for each other's debts and commitments.

A separate service company, OP-Services Ltd, which is wholly owned by OP Cooperative, is tasked with the development and provision of centralised services for OP Financial Group and its member banks. OP Cooperative acts as the entire OP Financial Group's strategic owner institution and as a central cooperative in charge of Group control and supervision.

In order to ensure uniformity in the accounting policies of entities within OP Financial Group, OP Cooperative shall issue guidelines on the preparation of financial statements to its member credit institutions. According to the Act on Cooperative Banks and Other Cooperative Institutions, the Executive Board of OP Cooperative must confirm any applicable accounting policies that have no directions from IFRS.

OP MB is domiciled in Helsinki and the address of its registered office is Gebhardinaukio 1, FI-00510 Helsinki.

A copy of OP MB's financial statements is available at www.op.fi or the company's office at Gebhardinaukio 1, FI-00510 Helsinki.

OP MB belongs to OP Financial Group, and OP MB's accounts are included in its consolidated financial statements. A copy of OP Financial Group's consolidated financial statements is available at www.op.fi or the Group's office at Gebhardinaukio 1, FI-00510 Helsinki.

OP MB's Board of Directors approved the financial statements on 5 February 2019.

BASIS OF PREPARATION

OP MB's financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS), applying IASs, IFRSs and SIC and IFRIC interpretations effective on 31 December 2018. The International Financial Reporting Standards refer to standards and their interpretations adopted in accordance with Regulation (EU) No. 1606/2002 of the European Parliament and of the Council. OP MB's notes also conform to the requirements of Finnish accounting and company legislation that complement IFRS regulations.

In 2018, OP MB adopted the following standards and interpretations:

- IFRS 9 Financial Instruments. Adjustments made to carrying amounts were recognised in equity in the opening balance sheet on the adoption date of 1 January 2018. OP MB has not adjusted comparatives for prior years. The effects of transition to IFRS 9 on the classification and measurement of financial instruments have been presented in the Chapter New standards and interpretations.

- IFRS 15 Revenue from Contracts with Customers. On 1 January 2018, OP MB adopted IFRS 15 using the retrospective transition method. The effects of transition to IFRS 15 have been presented in the Chapter New standards and interpretations.

- Annual improvements to IFRS for cycles 2014 2016 (applicable mainly to accounting periods beginning on or after 1 January 2018). Minor amendments are annually made to standards through the Annual Improvements process. The effects of the amendments vary by standard but they are not significant.

- Amendments to IFRS 2 and IFRIC 22 that took effect on 1 January 2018. The amendments did not have any significant effect on OP MB's financial statements.

OP MB's financial statements were prepared at historical cost with the exception of derivative contracts and hedged items in fair value hedging.

The figures in the income statement and the balance are presented in euros and cents; other figures in the financial statements are presented in thousands of euros.

Use of estimates

The preparation of the financial statements in conformity with IFRS requires the management to make judgements, estimates and assumptions in the application of the accounting policies. The Chapter Critical accounting estimates and judgements provides more detailed information on applying accounting policies requiring management assessment and judgement.

FINANCIAL INSTRUMENTS

Section Financial instruments in the accounting policies changed due to IFRS 9 as of 1 January 2018, except for Chapters Fair value determination, Derivative contracts and Hedge accounting. Only the accounting policies regarding 2017 dealing with financial instruments are presented in the Chapter Accounting policies regarding financial instruments in 2017. For the avoidance of doubt, the headings in the accounting policies for 2017 indicate the year 2017.

Fair value determination

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date.

The fair value of financial instruments is determined using either prices quoted in an active market or the company's own valuation techniques where no active market exists. Markets are deemed to be active if price quotes are easily and regularly available and reflect real and regularly occurring market transactions on an arm's length basis. The current bid price is used as the quoted market price of financial assets.

If the market has a commonly used valuation technique applied to a financial instrument to which the fair value is not directly available, the fair value is based on a commonly used valuation technique and market quotations of the inputs used by the technique.

If the valuation technique is not a commonly used technique in the market, a valuation model created for the instrument in question will be used to determine the fair value. Valuation models are based on widely used measurement techniques, incorporating all factors that market participants would consider in setting a price, and are consistent with accepted economic methodologies for pricing financial instruments.

The valuation techniques used include prices of market transactions, the discounted cash flow method and reference to the current fair value of another instrument that is substantially the same. The valuation techniques take account of estimated credit risk, applicable discount rates, the possibility of early repayment and other factors affecting the reliable measurement of the fair value of financial instruments.

The fair values of financial instruments are categorised into three hierarchy levels, depending on the inputs used in valuation techniques:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1)
- Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices) (Level 2)
- Inputs for the asset or liability that are not based on observable market data (Level 3)

If the inputs used to measure fair value are categorised into different levels of the fair value hierarchy, the fair value measurement is categorised in its entirety at the same level as the lowest level input that is significant to the entire measurement. The significance of inputs has been assessed on the basis of the fair value measurement in its entirety.

Financial assets and liabilities

Amortised cost

Amortised cost is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

The effective interest method uses the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset or to the amortised cost of a financial liability. When calculating the effective interest rate, OP Mortgage Bank shall estimate the expected cash flows by considering all the contractual terms of the financial instrument excluding the expected credit losses (ECL). The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts. Fees that are an integral part of the rate of a financial instrument include office and origination fees related to loan drawdown and they are amortised over the expected life of the financial instrument or a shorter period if that is appropriate. Fees that are not an integral part of the effective interest rate of a financial instrument and are accounted for in accordance with IFRS 15 include fees charged for servicing a loan, for example.

OP Mortgage Bank incorporates the impact of expected credit losses in the estimated future cash flows when calculating the credit-adjusted effective interest rate for financial assets that are considered to be purchased or originated credit-impaired at initial recognition (POCI).

Loans are entered in OP MB's balance sheet if they have been granted directly from its balance sheet or if a member cooperative bank has sold the loans to OP MB at market price, with the credit risk, interest rate risk and funding risk having transferred to OP MB with the sale. These loans are presented in the balance sheet under 'Receivables from customers'.

The loan is not transferred to OP MB's balance sheet in the intermediate loan model referred to in the Covered Bond Act (688/2010), whereby OP MB issues mortgage-backed bonds and uses the funds obtained to make an intermediate loan to OP cooperative banks, presented under 'Receivables from credit institutions' in the balance sheet. In the intermediate loan model, the OP cooperative bank's mortgage-backed loan's credit risk, interest rate risk or funding risk are not transferred to OP MB but are entered as collateral of the bond issued by OP MB.

Interest revenue

Interest revenue has been calculated by applying the effective interest rate to the gross carrying amount of a financial asset except for:

a) purchased or originated credit-impaired financial assets. For those financial assets, OP MB applies the credit-adjusted effective interest rate to the amortised cost of the financial asset from initial recognition
b) financial assets that are not purchased or originated credit-impaired financial assets but subsequently have become credit-impaired financial assets (or that are in stage 3). For those financial assets, OP MB applies the effective interest rate to the amortised cost of the financial asset (i.e. to the net carrying amount after the deduction of the expected credit loss).

Initial recognition and measurement

At initial recognition, OP MB measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability. Immediately after initial recognition, an expected credit loss allowance of a financial asset will be recognised if the financial asset is measured at amortised cost or at fair value through other comprehensive incomes. This results in accounting loss recognition for newly originated or newly purchased financial assets in the income statement.

Classification and subsequent measurement of financial assets

OP MB has classified financial assets into the following categories since 1 January 2018:
- Fair value through profit or loss (FVTPL)
- Fair value through other comprehensive income (FVOCI)
- Amortised cost.

Loans

The classification of loans and notes and bonds depend on the following factors:
a) OP MB's business model for managing the financial assets
b) the contractual cash flow characteristics of the financial asset.

On the basis of these factors, OP MB classifies loans into the following three measurement categories:

1) Financial assets measured at amortised cost shall be held within a business model whose objective is to hold financial assets in order to collect contractual cash flows that are solely payments of principal and interest on the principal amount outstanding. The financial asset's carrying amount is adjusted by any allowance for expected credit losses and interest revenue is recognised in interest revenue using the effective interest method.

2) Financial assets recognised at fair value through other comprehensive income are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets. In addition, the contractual terms of the financial asset give rise on specified dates that are solely payments of principal and interest on the principal amount outstanding. Changes in the fair value are recognised in the fair value reserve. Impairment gains or losses and foreign exchange gains or losses are recognised in profit or loss. When a financial asset is derecognised, the cumulative profit or loss in the fair value reserve is reclassified from equity to profit or loss in net investment income as a reclassification adjustment. Interest calculated using the effective interest method is recognised in interest revenue or net investment income.

3) Financial assets measured at fair value through profit or loss are held for trading or assets that do not meet the criteria for amortised cost or FVOCI. Gains and losses are recognised in net investment incomes.

Business model

A business model refers to how OP MB manages its financial assets in order to generate cash flows. OP MB's business model determines whether cash flows will result solely from collecting contractual cash flows or from collecting contractual cash flows and cash flows and by selling a financial assets, or whether the purpose is held for trading. Financial assets within the trading business model are measured through profit or loss. When assessing the business model, OP MB takes account of future measures to achieve the objective of the business model. The assessment includes previous experience in collecting cash flows, how the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel, how risks are managed and how managers of the business are compensated. For example, OP MB holds home loans and intermediate loans and it has granted to collect contractual cash flows.

Cash flow characteristics

When OP MB's business model is other than trading, OP MB assesses whether contractual cash flows are consistent with a basic lending arrangement. In the basic lending arrangement, contractual cash flows are solely payments or principal and interest on the principal amount outstanding (SPPI) where consideration for the time value of money, credit risk, lending risks and profit margin are typically the most significant elements of interest. The majority of OP MB's financial assets are basic lending arrangements.

All loans to private customers granted by OP MB contain the option for early repayment. The terms and conditions are, however, consistent with the basic lending arrangement because the prepayment amount substantially represents the contractual par amount and accrued (but unpaid) contractual interest, which may include reasonable additional compensation for the early termination of the contract.

When contractual cash flows are exposed, for example, to change in stock prices or a borrower's financial result, this is no basic lending arrangement and such financial assets are measured through profit or loss. These are typically various mutual fund investments which do not fulfil the definition of equity in the issuer's financial statements under IAS 32.

Embedded derivatives included in financial assets are not separated from the host contract but they are considered in the overall assessment of contractual cash flows.

If OP MB has to change its business model for managing financial assets, it may have to reclassify financial assets. The reclassification must be applied prospectively from the reclassification date. Such changes are expected to be very infrequent.

Equity instruments

Equity instruments are instruments that evidence a residual interest in the assets of a company after deducting all of its liabilities. These are typically equity investments.

Equity instruments are subsequently measured at fair value through profit or loss, except when OP MB has made an irrevocable election at initial recognition for particular investments in equity instruments that would otherwise be measured at fair value through profit or loss to present subsequent changes in fair value in other comprehensive income. These investments comprise OP MB's strategic investments in OP Cooperative's cooperative capital, the nominal value of which corresponds to their fair value. No capital gains or losses are realised from these investments. The interest on cooperative capital is recognised in net investment income. OP Cooperative's Cooperative Meeting confirms the amount of interest payable on an annual basis.

Modification of contractual cash flows

Modifications in the contractual payment terms are made as a normal measure related to the management of customer relationship but also in situations where the customer's repayment capacity has deteriorated. In such a case, a concession resulting from weaker repayment capacity has to be given to the loan terms – such as a repayment holiday – for a limited period. Generally in these cases, the contractual cash flows of a loan are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that loan. Modifications in payment terms are subject to regular monitoring and reporting to the management as an indicator anticipating customers' solvency.

If modifications to the loan terms are significant or the loan is renegotiated, OP MB derecognises the original loan and recognises the modified new loan in the balance sheet. The date of renegotiation is consequently considered to be the date of initial recognition for the impairment calculation purposes. This typically means measuring the loss allowance at an amount equal to 12-month expected credit losses. OP MB uses internal rating to classify reasons for modifications and severity classes to monitor whether there has been evidence that the new loan recognised has deemed to be credit-impaired at initial recognition. Accordingly, it is recognised as an originated credit-impaired financial asset. This might occur, for example, in a situation in which there was a substantial modification of a distressed asset.

Otherwise, OP MB derecognises financial assets when the contractual rights to the cash flows from the financial asset expire or it transfers the financial asset to another party and the transfer qualifies for derecognition.

Impairment

Expected credit losses are calculated on all balance sheet items amortised at cost and those recognised at fair value through other comprehensive income (FVOCI) (instruments other than equity instruments) and on off-balance-sheet loan commitments and financial guarantee contracts. Expected credit losses are recognised at each reporting date, reflecting:

a) an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes
b) the time value of money and
c) reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Classification of contracts into three impairment stages

Contracts are classified into three stages. The different stages reflect credit deterioration since initial recognition.

- Stage 1: contracts whose credit risk has not increased significantly since initial recognition and for which a 12-month ECL is calculated.
- Stage 2: contracts whose credit risk has increased significantly since initial recognition and for which a lifetime ECL is calculated.
- Stage 3: defaulted contracts for which a lifetime ECL is also calculated.

In addition, originated credit-impaired contracts are always within the scope of the lifetime expected credit loss (POCI).

Definition of default

In the IFRS 9 based calculation, OP MB applies the same definition of default as in internal credit risk models (IRB). OP MB assesses default using its internal rating system based on payment behaviour. Default as definition for private customers is applied on a contract-by-contract basis. A customer is classified as a default customer when it is probable that the customer will not pay loan obligations in full without OP MB resorting to measures (e.g. realisation of collateral) or no later than when payment related to financial assets is more than 90 days past due.

The definition of default is based on Article 178 of Regulation No. 575/2013 (CRR) of the European Parliament and of the Council.

The customer's default ends when it no longer meets the criteria for the definition of default. After that, the payment behavioural class will be restored with a delay of 6 months.

Significant increase in credit risk

The expected credit losses are calculated for each contract for 12 months or lifetime, depending on whether the instrument’s credit risk on the reporting date has increased significantly since initial recognition. Both qualitative and quantitative criteria are used to assess whether the credit risk has increased significantly. Forbearance is regarded as a qualitative criterion. Other qualitative factors consist of various credit risk indicators (e.g. breach of covenants) to be taken into account in credit rating models or in the assessment of the payment behavioural category.

OP MB has included relative and absolute thresholds for the determination of significant quantitative increases in credit risk considering all reasonable and supportable information.

A quantitative change is assessed based on the relative change in lifetime PD figures (PD curve). The original lifetime PD curve is calculated on the origination date of the loan taking account of macroeconomic factors. Next, the acceptable natural range of variation is determined for the limits within which the credit risk is not considered to increase significantly during the remaining maturity of the loan. This yields a so-called threshold value curve. On each reporting date, the current lifetime PD curve is compared to the threshold value curve. If the threshold value is exceeded, the credit risk has increased significantly and a credit loss (calculated for the entire remaining maturity of the loan) is recognised. In addition to this limit of the relative change, a further requirement is that a borrower grade has deteriorated since initial recognition so that shifting to the lifetime ECL calculation does not occur only on the basis of the passage of time. In addition, an absolute threshold is used for the weakest borrower grades.

In addition to the aforementioned criteria, credit risk on a financial asset has increased significantly since initial recognition when contractual payments are more than 30 days past due.

In the assessment of a significant increase in credit risk, OP MB has not applied a transitional rule on the assumption of low credit risk permitted by IFRS 9 to contracts, for which it is not possible without undue cost or effort, to calculate the original lifetime PDs.

OP MB monitors regularly how effectively the abovementioned criteria perceive a significant increase in credit risk before contractual payments have been over 30 days past due and that the contracts do not generally move from impairment stage 1 directly to impairment stage 3, and performs the required calibrations to the calculation method of the relative change.

Measurement methods

Expected credit losses are mainly measured on a system basis using the PD/LGD method on a contract-specific basis for all private customer exposures.

PD/LGD method

Expected credit losses are calculated using modelled risk parameters with the formula probability of default (PD) x loss given default (LGD) x exposure at default (EAD) for majority of portfolios per contract and they reflect expectations of future credit losses at the reporting date. PD describes probability of default according to the definition of default. The probability of default applied to OP Financial Group's internal loans is zero due to the joint and several liability. LGD describes the share of an asset if a borrower defaults. It is affected, for example, by the quantity and type of collateral securities and various financial guarantees. EAD describes the exposure amount at default, including exposure in the balance sheet (capital and accrued interest) and expected use of off-balance-sheet items at default.

The ECL calculation is based on three different scenarios. Risk parameters PD, LGD and EAD are calculated for yearly time buckets in each scenario. Yearly ECL figures are discounted to the reporting date and a probability-weighted ECL is calculated from the figures of different scenarios. The contract's effective interest or its estimate is used as the discount factor. The contract's maximum residual term to maturity is limited to 30 years in the calculation.

The lifetime probability of default (lifetime PD) models for a contract have been prepared for private customers. The PD models are substantially affected by the contract's credit rating, loan age (private customers) as well as the model's sub-segment, which is determined for private customers on the basis of the product type. In addition, PD estimates are dependent on macroeconomic factors and their forecasts in each scenario.

The lifetime LGD for a contract consists of the following three components: 1) cure rate, 2) collateral return and 3) non-collateral return. The values of the different components depend substantially on the product type, industry (companies) and the type of collateral. The macroeconomic factors and their forecasts affect the first two components.

The lifetime exposure at default (lifetime EAD) for a contract is based on contractual cash flows, utilisation rate, prepayment rate and maturity model, depending on the product type.

Determining the period of a contract

The period of a contract for promissory notes is a contractual maturity that takes account of repayments under the payment terms. The prepayment model applies to secured promissory notes (excl. default). It does not reduce the contractual maturity but is taken into account as part of the contract's EAD.

Revolving credit facilities (such as credit cards) are contracts valid until further notice and an expected maturity has been modelled for them. The modelled maturity depends on the product type and borrower grade, averaging some 15 years.

Forward-looking information

The calculation model includes forward-looking information and macroeconomic scenarios. OP Financial Group's economists update macroeconomic scenarios on a quarterly basis and the scenarios are the same that OP MB uses otherwise in its financial annual planning. Macroeconomic forecasts span five years and have been extrapolated for up to 30 years ahead using a production function. The macroeconomic factors used are: GDP growth, unemployment rate, investment growth rate, inflation rate, change in income level and 12-month Euribor rate. In addition, the house price index is used in LGD models. Three scenarios are used: baseline, upside and downside. Scenarios also include probability weights.

Preparing macroeconomic forecasts and projecting them into the future up to 30 years involves a large amount of uncertainty, which is why actual results may differ significantly from the forecasts. OP MB has analysed that the relationship of the change in the components of risk parameters and macroeconomic factors used in the ECL calculation is not linear. Accordingly, the macroeconomic forecasts represent OP MB's best view of potential scenarios and outcomes.

Model based on credit rating information

In the model, credit ratings are sought for purchase lots on the purchase date and the reporting date, and they are converted into PD figures. OP MB primarily uses the averages of external credit rating and secondarily internal credit rating, in case no external credit ratings exist.

The PDs correspond to the actual historical default rates by credit rating for each period from the date of issuing the credit rating. The historical data, for which the determined correspondence is based on, is comprehensive and on a long-term basis. The LGDs also correspond to the studied historical actuals by investment class/insurance line and these are not separately assessed by issuer or investment. Because external credit ratings measure total credit risk (ECL), not PD, the LDG in these cases affect only the division of the ECL between PD and LGD components.

Impairment of off-balance-sheet items

Products offered by OP MB may include an off-balance-sheet loan commitment. For loan commitments, the date that OP MB becomes a party to the irrevocable commitment shall be considered to be the date of initial recognition for the purposes of applying the impairment requirements.

The expected credit loss is calculated for these items using the same principles as for loans. Likewise, increases in significant credit risk are assessed on the same grounds. OP MB models EAD for such products that forecasts exposure at default. It includes both the utilisation rate and credit conversion factor. In addition, a maturity model is applied to contracts valid until further notice. The model takes account of cases where OP MB has a contractual ability to demand repayment and cancel the undrawn commitment but it does not limit OP MB’s exposure to credit losses during the contractual notice period.

Recognition of expected credit losses

OP MB mainly recognises a loss allowance for expected credit losses on a loan in a separate account. For loan commitments and financial guarantee contracts the loss allowance is recognised as a provision. For products that include both a loan (i.e. financial asset) and an undrawn commitment (i.e. loan commitment) component and OP MB cannot separately identify the expected credit losses on the loan commitment component from those on the financial asset component, the expected credit losses on the loan commitment are recognised together with the loss allowance for the financial asset.

Write-off

A write-off constitutes a derecognition event. When OP MB has no reasonable expectations of recovering a financial asset in its entirety or a portion thereof, it directly reduces the gross carrying amount of the financial asset.

A loan is derecognised when collateral securities have been realised or debt rescheduling has come to an end or when collection measures have ended. Payments received after the derecognition are recognised as an adjustment to impairment losses on receivables.

Cash and cash equivalents

Cash and cash equivalents consist of cash and receivables from credit institutions repayable on demand.

Classification and subsequent measurement of financial liabilities

Financial liabilities include liabilities to credit institutions, debt securities issued to the public and other financial liabilities.

Financial liabilities are classified at amortised cost using the effective interest method, except for derivative liabilities measured at fair value through profit or loss.

Upon initial recognition, OP MB has not designated financial liabilities as measured at fair value through profit or loss.

OP MB derecognises a financial liability (or a part of a financial liability) when it is extinguished – i.e. when the obligation specified in the contract is discharged or cancelled or expires.

An exchange between OP MB and original lenders of financial liabilities with substantially different terms must be accounted for as an extinguishment of the original financial liability. In such a case, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, the amortised cost of the modified financial liability will be recalculated by discounting the modified contractual cash flows using the original effective interest rate. Changes in the amortised cost of the financial liability is recognised through profit or loss. Costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability. OP MB has not made any exchanges of financial liabilities for the existing financial liabilities.

Netting

Financial assets and liabilities are offset in the balance sheet if OP MB currently has a legally enforceable right of set-off in the normal course of business and in the event of default, insolvency or bankruptcy, and intends to settle the asset and liability on a net basis. OTC interest rate derivatives for central counterparty clearing are offset in the balance sheet, which are cleared in the daily clearing process with London Clearing House.

Derivative contracts

Derivative contracts are classified as hedging contracts and derivative contracts held for trading. OP MB uses derivatives only for hedging purposes. Derivatives are measured at fair value at all times. OP MB has prepared methods and internal principles used for hedge accounting, whereby a financial instrument can be defined as a hedging instrument.

In accordance with the hedging principles, OP MB can hedge against interest rate risk by applying fair value hedge or cash flow hedge. Fair value hedging refers to hedging against changes in the fair value of the hedged asset, and cash flow hedging to hedging against changes in future cash flows.

Hedge accounting

Hedge accounting is used to verify that changes in the fair value of a hedging instrument or cash flows fully or partially offset the corresponding changes of a hedged item.

The relationship between hedging and hedged instruments is formally documented, containing information on risk management principles, hedging strategy and the methods used to demonstrate hedge effectiveness. Hedge effectiveness is tested at the inception of the hedge and in subsequent periods by comparing respective changes in the fair value or cash flows of the hedging and hedged instrument. The hedge is considered effective if the change in the fair value of the hedging instrument or in cash flows offsets the change in the fair value of the hedged contract or portfolio or in cash flows within a range of 80–125%.

Fair value hedges

Fair value hedging against interest rate risk involves long-term fixed-rate debt instruments (OP MB's own issues), individual loan portfolios, as well as individual loans. Interest rate swaps are used as a hedging instrument.

Changes in the fair value of derivative contracts that are documented as hedging the fair value and are highly effective hedges are recognised in the income statement. Hedged assets and liabilities are also measured at fair value during the period for which the hedge is designated, and any fair value changes are recognised through profit or loss.

In fair value hedge accounting, changes in the fair value of the hedged item and hedging instrument are recorded in the income statement under "Net interest income".

ACCOUNTING POLICIES REGARDING FINANCIAL INSTRUMENTS IN 2017

This Chapter only presents the accounting policies regarding 2017 that deal with financial instruments.

Impairment of financial assets in 2017

At the end of each reporting period, OP MB assesses whether there is objective evidence that a financial asset other than that carried at fair value through profit or loss is impaired.

A financial asset is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset and that the loss event has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

The criteria used to determine whether there is objective evidence of an impairment loss include:

- significant decline in the issuer's financial results, credit rating, balance sheet, payment status or business plans, and unfavourable changes in the issuer's economic and operating environment;
- a debtor's bankruptcy or other reorganisation becomes probable;
- a debtor's breach of contract;
- a concession granted to the debtor;
- impairment recognised earlier;
- the disappearance of an active market for a financial instrument.

In addition, a significant or prolonged decline in the equity instrument's fair value below its cost constitutes objective evidence of impairment.

A more detailed description of recognition of impairment losses can be found under the various financial instruments below.

Classification and recognition of financial instruments in 2017

Upon initial recognition, financial assets and liabilities are classified as follows: financial assets and liabilities at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets and other financial liabilities. The classification depends on the purpose for which the financial assets and liabilities were acquired.

Loans are entered in OP MB's balance sheet if they have been granted directly from its balance sheet or if a member cooperative bank has sold the loans to OP MB at market price, with the credit risk, interest rate risk and funding risk having transferred to OP MB with the sale. These loans are presented in the balance sheet under 'Receivables from customers'.

The loan is not transferred to OP MB's balance sheet in the intermediate loan model referred to in the Covered Bond Act (688/2010), whereby OP MB issues mortgage-backed bonds and uses the funds obtained to make an intermediate loan to OP cooperative banks, presented under 'Receivables from credit institutions' in the balance sheet. In the intermediate loan model, the OP cooperative bank's mortgage-backed loan's credit risk, interest rate risk or funding risk are not transferred to OP MB but are entered as collateral of the bond issued by OP MB.

Loans and receivables, held-to-maturity investments and other financial liabilities are measured at amortised cost.

The purchase and sale of financial assets and liabilities at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets are recognised in the balance sheet on the transaction date, or the date on which the company agrees to buy or sell the asset or liability in question.

Financial assets and liabilities are offset in the balance sheet if OP MB currently has a legally enforceable right of set-off in the normal course of business and in the event of default, insolvency or bankruptcy, and intends to settle the asset and liability on a net basis.

OP MB derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Financial liabilities are derecognised when they are extinguished, i.e. when the obligation is discharged, cancelled or expires.

Loans and receivables in 2017

Financial assets classified as loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Loans and receivables are initially recognised at cost, which is the fair value of consideration given plus directly attributable transaction costs. Loans and receivables are carried at amortised cost after their initial recognition.

Impairment losses on loans and receivables are recognised on an individual or collective basis. Impairment will be assessed and recognised on an individual basis if the debtor's total exposure is significant. In other respects, impairment is assessed and recognised on a collective basis.

Impairment is recognised and impairment losses incurred if there is objective evidence that the receivable cannot be recovered in full. The receivable has impaired if its present value of the estimated future cash flows – collateral included – is lower than the aggregate carrying amount of the loan and the related unpaid interest. Estimated future cash flows are discounted at the loan's original interest rate. If the loan carries a variable interest rate, the discount rate for measuring any impairment is the current effective interest rate determined under the agreement.

Impairment loss recognised in profit or loss equals the difference between the carrying amount of the loan and the lower present value of future cash flows.

Impairment assessment is a two-phase process. Impairment is assessed individually for loans and receivables. If it is not necessary to assess impairment for financial assets included in loans and receivables on an individual basis, they will be assessed collectively for impairment. Collectively assessed impairment includes losses incurred but not yet reported, which cannot yet be allocated to a certain loan. Collectively assessed impairment provisions are based on a statistical model used in the measurement of economic capital. The model is derived from the expected credit loss model used in capital adequacy measurement, adjusted to correspond to the requirements under IFRS. Through-the-cycle component and the official minimum capital adequacy requirements have been eliminated from the PD and LGD estimates used in the economic capital requirement model so that they better reflect the point in time approach and the current economic cycle. In the model, the so-called emergence period is used to measure the identification of a loss event. The emergence period is based on OP MB's impairment assessment process by customer segment from the loss event to testing a loan for impairment on an individual basis. In addition, the receivables in the model are grouped into customer segments on the basis of similar credit risk characteristics. Collectively assessed impairment is measured by customer segment on the basis of the expected loss and the measurement also takes account of the emergence period and the discounted present values of collateral.

If the contractual payment terms of a loan are modified, the reason for such modification and the severity class are documented using an internally defined scale. Loans may also be modified for reasons related to the management of customer relationships, not to the financial difficulties of the customer. Such modifications do not affect loan impairment recognition. In some cases, the Group may, due to the customer's financial difficulties, modify the loan terms and conditions, such as in terms of repayment holiday for a limited period or another loan modification, which are aimed at securing the customer's repayment capacity and limiting credit risk associated with liabilities. Such renegotiated loans are reported as doubtful receivables. Modifications in the contractual payment terms that are due to the customer's financial difficulties are forbearance measures and together with other criteria reduce the customer's credit rating and thereby increase collective impairment allowance. In addition, they will also have an effect on the loan being assessed on an individual basis for impairment. If the customer has adhered to the new payment terms and no impairment allowance has been recognised for the customer's exposure, it will be removed from doubtful debt classification after two years. Modifications in payment terms are subject to regular monitoring and reporting to the management as an indicator anticipating customers' solvency.

Both individual and collective impairment loss is recorded in a separate allowance account to reduce the carrying amount of receivables in the balance sheet. Impairment losses are presented in the income statement under Impairment losses on receivables. Recognition of interest on the impaired amount continues after the recognition of impairment.

The loan is derecognised after the completion of all debt-collection measures if the loan terms are substantially modified (such as refinancing). Payments received after the derecognition are recognised as an adjustment to impairment losses on receivables. If there is subsequent objective evidence of the debtor's improved solvency, the amount of the impairment loss recognised earlier will be reassessed and any change in the recoverable amount will be recorded in the income statement.

Cash and cash equivalents in 2017

Cash and cash equivalents consist of cash and receivables from credit institutions repayable on demand.

Other financial liabilities in 2017

Other financial liabilities include financial liabilities other than those at fair value through profit or loss, comprising other liabilities to credit institutions and customers, debt securities issued to the public and other financial liabilities. Other financial liabilities are recognised in the balance sheet on the settlement date and carried at amortised cost after initial recognition.

The difference between the nominal value and the acquisition cost of fixed-rate bonds is recognised in interest expenses over the estimated residual term to maturity.

INTANGIBLE ASSETS

Intangible assets are stated at cost less amortisation and any write-downs. These assets are amortised over their estimated useful lives, which is 2–6 years for computer software and licences.

LEASES

On the date of inception, leases are classified as finance leases or operating leases depending on the substance of the transaction. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incident to ownership to the lessee. All other leases are classified as operating leases.

Assets leased under finance lease are recognised as property, plant and equipment and the corresponding finance lease liability is included in other liabilities. At the inception of the lease term, these leased assets are recorded as assets and liabilities at the lower of the fair value of the asset and the present value of the minimum lease payments. PPA assets are depreciated over the shorter of the lease term or the life of the asset. Finance charges are recognised in interest expenses so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Lease payments for leased assets under operating lease are recognised as expenses on a straight-line basis over the lease term.

EMPLOYEE BENEFITS

Pension benefits

Statutory pension cover for OP MB’s employees is arranged through pension insurance taken out with OP Bank Group Pension Fund. The supplementary pension plan has been arranged through OP Bank Group Pension Foundation.

With respect to funded disability and old-age pensions, pensions managed by OP Bank Group Pension Fund are defined benefit plans. All of the plans managed by OP Bank Group Pension Foundation are defined benefit plans.

Expenses arising from pension plans are recognised under “Personnel costs” in the income statement. Contributions under defined contribution plans are charged to expenses for the financial year to which they relate. No other payment obligations are included in defined contribution plans. Curtailing the defined benefit pension plan or fulfilling or changing the related obligation is recognised through profit or loss at the time of occurrence.

Defined benefit plans managed by OP Bank Group Pension Fund and OP Bank Group Pension Foundation are funded through payments based on actuarial calculations.

The liability recognised in the balance sheet in respect of the defined benefit plan is the present value of the defined benefit obligation on the balance sheet date less the fair value of the plan assets of OP Bank Group Pension Fund, OP Bank Group Pension Foundation and acceptable insurance.

Defined benefit obligations are calculated separately for each plan using the projected unit credit method. Pension costs are charged to expenses over the employees' expected working lives on the basis of calculations performed by authorised actuaries. The discount rate for the present value of the defined benefit obligation is determined on the basis of the market return on high-grade corporate bonds on the closing date of the reporting period.

Items resulting from remeasurements of the net defined benefit liability are recognised in other comprehensive income in the period they occur. Remeasurements of the net defined benefit liability recognised in other comprehensive income will not be reclassified to income statement in later financial periods.

Personnel fund

OP MB belongs to OP Financial Group's OP Personnel Fund into which bonuses are paid on the basis of pre-agreed principles, depending on the achievement of OP Financial Group's targets. Bonuses transferred to the Fund are recognised under "Wages and salaries" in the income statement. The counterpart is recognised under "Deferred expenses" in the balance sheet until disbursed to beneficiaries.

INCOME TAX AND DEFERRED TAX

Income tax expense shown in the income statement includes current tax, based on the taxable income of the financial year and income tax for prior financial years and deferred tax expense or income. Taxes are recognised in the profit and loss except when they are directly linked to items entered into equity or other items in other comprehensive income. In such a case, the tax is recognised in the items in question. The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date.

Deferred tax liabilities are recognised for all temporary differences between the carrying amount and tax base of assets and liabilities. Deferred tax assets are calculated on tax-deductible temporary differences between the carrying amount and taxable value included in the financial statements, and on losses confirmed for tax purposes. Deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

OP MB offsets deferred tax assets and liabilities. Deferred tax assets and liabilities are measured at the tax rate that is expected to apply to the period when the asset is realised or the liability is settled, based on tax rates enacted or substantively enacted by the balance sheet date.

REVENUE RECOGNITION

Interest revenue

Interest income and expenses for interest-bearing assets and liabilities are recognised using the effective interest method. More detailed information on the effective interest method can be found in the Chapter Amortised cost in these accounting policies. Interest on receivables with non-settled, due payments is also recognised as revenue. The difference between the receivable's acquisition cost and its nominal value is recognised as interest income and that between the amount received and nominal value of the liability in interest expenses. The difference between the nominal value and the acquisition cost of fixed-rate bonds is recognised as interest income or expenses over the residual term to maturity.

Net commissions and fees

Fees that are not an integral part of the effective interest rate of a financial instrument are accounted for in accordance with IFRS 15 Revenue from Contracts with Customers. Fees and commissions under IFRS 15 are recognised as revenue when a service's agreed performance obligations are transferred to the customer and the key criterion is transfer of control. Commissions and fees are recognised to the amount to which an entity expects to be entitled in exchange of transferring promised services to a customer. Commission expenses are recognised in net commissions and fees on an accrual basis.

Commissions and fees consist of commissions from lending to private customers. Their performance obligations are fulfilled over time. The amount of consideration for the services is the list price or a contractually stated price. OP MB charges its customers the fees on a monthly basis according to the contract terms.

OP MB refunds OP cooperative banks the amount of the returns of loans managed by OP MB agreed in the fee model. Commission expenses consist mainly of the payment to OP cooperative banks of commissions charged from lending and fees for loan management, and of commission expenses relating to the issuance of bonds.

SUMMARY OF PRESENTATION OF INCOME STATEMENT ITEMS

Net interest income	Received and paid interest on fixed-income instruments, the recognised difference between the nominal value and acquisition value, interest on interest-rate derivatives and fair value change in fair value hedging, interest expense on issued debt securities
Net commissions and fees	Commission income from lending, commission expenses from lending and loan management fees to OP cooperative banks, and commission expenses from issued debt certificates
Personnel costs	Wages and salaries, pension costs, social expenses
Other operating expenses	Office expenses, ICT costs, other administrative expenses, charges of financial authorities and auditors, rents and other expenses
Impairment loss on receivables	Expected credit losses from customers and final credit losses and their reversals.

SEGMENT REPORTING

Since OP MB is engaged only in residential lending, segment reporting is not presented.

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of financial statements requires making estimates and assumptions about the future and the actual results may differ from these estimates and assumptions. It also requires the management to exercise its judgement in the process of applying the accounting policies.

The determination of the measurement models for expected credit losses (ECL) involves several factors requiring management judgement, such as:

- Selection of appropriate ECL models so that they describe the expected credit losses on the contract portfolio as well as possible
- Different assumptions and expert judgements made in the models
- Selection of the estimation methods of the parameters for the ECL models
- Determination of model risk associated with the quality of the available modelling data and other data
- Proper grouping of contracts into different segments so that their ECL can be calculated using the appropriate model
- Selection of macroeconomic factors in such a way that their changes correlate with the contracts' probability of default
- Forecasting future macroeconomic scenarios and their probabilities.

Management judgement has also been used in the assessment of a significant increase in credit risk, such as in:

- The expert judgement used in the assessment of change in relative credit risk associated with private customers to ensure a true number of contracts that move to stage 2 before moving to stage 3 (so-called default capture rate)
- The selection of the absolute threshold that is based on historical default behaviour and OP MB’s credit risk process
- The determination of the length of a period during which the customer must prove proper payment behaviour so that the impairment stage 3 can improve to stage 2 or 1.

CHANGES IN ACCOUNTING POLICIES AND PRESENTATION

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.

OP MB continued to apply hedge accounting under IAS 39 after adoption of IFRS 9. Comparatives for the financial statements included in the first opening balance sheet of 1 January 2018 were not adjusted. Changes in the notes to the financial statements arising from the application of IFRS 9 are only presented for the financial year 2018.

OP MB shifted from the calculation of impairment on an individual basis to that of the expected credit loss calculated using models under IFRS 9. Consequently, prior impairment losses on an individual and collective basis under IAS 39 have been revoked and expected credit losses under IFRS 9 have been recognised.

Balance sheet items, TEUR	**Impairment loss on receivables (IAS 39) 31 Dec. 2017**	**Revaluation**	**Expected credit losses (IFRS 9) 1 Jan 2018**
Receivables from customers	898	112	-786
Total	**898**	**112**	**-786**

Since the amount of expected credit losses, EUR 0.8 million, was below the expected loss (EL) calculated in capital adequacy measurement, EUR 4 million, the Loss allowance had no impact on OP MB's CET1 on 1 January 2018.
The allowance for equity capital due to expected credit losses on 1 January 2018 totalled EUR 786,000. Impairment loss on receivables assessed individually and collectively on 31 December 2017, amounting to EUR 898,000, was reversed to retained earnings. In addition, total equity capital on 1 January 2018 was affected by a deferred tax change concerning these items.

Changes in shareholders' equity, TEUR	**Share capital**	**Other funds**	**Retained earnings**	**Total**
Shareholders' equity 31 Dec. 2017	60,000	245,000	75,057	**380,057**
Reversal of previous IAS 39 impairment provision			898	**898**
New loss allowance under IFRS 9			-786	**-786**
Net change in deferred tax			-22	**-22**
Shareholders' equity 1 Jan 2018	**60,000**	**245,000**	**75,147**	**380,147**

IFRS 15 Revenue from Contracts with Customers

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. IFRS 15 led to added information presented in the Notes to the Financial Statements.

Net commissions were 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 significant effect on OP MB’s financial result. OP MB adopted IFRS 15 using the retrospective transition method.

Below is a description of the retrospective changes made previously to the specification of net commissions and fees:

- 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”

NEW STANDARDS AND INTERPRETATIONS

The IASB (International Accounting Standards Board) has issued the following significant future IFRS amendments:

IFRS 16 Leases

OP MB will adopt IFRS 16 Leases from 1 January 2019. The new standard will change the lessor's accounting and affect the Group's accounting for operating leases. As a result, all the lessor's leases will be recognised in the balance sheet since operating leases and finance leases will no longer be separated from each other. The adoption of the standard will not have any major effect on OP MB’s financial statements.

Other upcoming amendments to standards

Amendments to IFRS 3, IFRS 9, IFRS 11, IAS 12, IAS 19, IAS 23, IAS 28, IAS 40, IFRIC 22 and IFRIC 23 took effect on 1 January 2019. The amendments will not have any major effect on OP MB’s financial statements.

APPENDIX 2. OP Mortgage Bank's risk and capital adequacy management principles

1 General principles of risk and capital adequacy management

OP Financial Group's core values, strategic goals and financial targets form the basis for OP MB's risk management and capital adequacy management. The purpose of risk management is to identify threats and opportunities affecting strategy implementation. Risk management aims to achieve the targets set in the strategy by controlling that risks are proportional to risk-bearing capacity. OP MB has a moderate attitude towards risk-taking.

In OP Financial Group's risk policy, the central cooperative's Executive Board confirms annually risk-management principles, actions, objectives, limits to be applied by all Group entities that are used to guide business to implement the policies confirmed in the Group's strategy and the principles of the risk tolerance system.

1.1 Risk and capital adequacy management

Risk and capital adequacy management falls under internal control. Its purpose is to ensure OP MB's risk-bearing capacity and liquidity and, thereby, ensure business continuity. Risk-bearing capacity is made up of effective risk management that is proportionate to the extent and complexity of operations and of adequate capital resources and liquidity based on profitable business operations.

Risk and capital adequacy management has been integrated as an integral part of the company's business and management. OP MB focuses on carrying out its role according to its service capabilities and risk-bearing capacities in accordance with shared business models.
Risk and capital adequacy management consists of

- identifying, measuring, assessing and mitigating risks;
- determining reliably and independently how much capital and liquidity is required for various risk types and business operations; and
- allocating capital and liquidity systematically by business segment in line with current and planned risk-taking.

OP MB's remuneration scheme does not encourage excessive risk-taking. The remuneration scheme takes into account OP Financial Group's capital adequacy and profitability.

1.2 Risk identification, assessment, measurement and mitigation

The risk management and ICAAP process consists of the continuous identification and assessment of risk associated with business and the operating environment. Before the company launches any products or services or adopts new operating models or systems, it assesses their risks using procedures as laid down by the central cooperative's Risk Management.

Quantifiable risks are mitigated by means of limits set by the central cooperative's Executive Board. The Executive Board has set limits for OP MB's capital adequacy and interest rate risk.

OP MB assesses its capital base in relation to the economic capital requirement and the existing and predictable regulatory minimum capital requirements. Such assessment also makes use of the results of stress tests.

The central cooperative's independent Risk Management monitors the development of OP MB's risk exposure and risk-bearing capacity. It provides regular reports on its observations and assessments to OP MB's Board of Directors, the central cooperative's Executive Board and the Risk Management Committee of the central cooperative's Supervisory Board.

1.3 Economic capital requirement

The economic capital requirement is OP Financial Group's own estimate of the amount of capital sufficient to cover any annual losses with a 99.97% probability that may arise from risks associated with business and the operating environment. The economic capital requirement is calculated using models for each risk type, the results of which are combined taking account of correlations between the risk types and the resulting diversification benefits.

Economic capital is divided into quantitative and qualitative, or assessable, risks. OP MB's quantitative risks include credit risk and banking interest rate and equity risks. The assessable risks include operational risks. Credit risks account for 85% of OP MB's economic capital requirement.

1.4 Capital management

Capital management aims in all circumstances to proactively control and ensure that OP MB's capital adequacy meets the set targets and official requirements and thus ensure business continuity. A capital plan is made to assess the adequacy of OP MB's capital and proactively ensure an adequate capital base even in exceptional conditions. The capital plan consists, for example, of quantitative and qualitative targets set for capital adequacy, predicted changes in the capital base and capital requirements, a contingency plan, and capital adequacy monitoring and control procedures per threshold level.

OP MB is responsible for its own capital adequacy and sets its capital adequacy targets and limits according to guidelines set by the central cooperative.

2 Organisation of risk and capital adequacy management

OP MB follows the principles of OP Financial Group's risk-taking and risk tolerance system adopted by OP Cooperative's Supervisory Board. The principles specify how the Group's risk-taking is controlled, limited and supervised and how the risk management and internal capital adequacy assessment process (ICAAP) is organised.

The central cooperative is in charge of the OP Financial Group level risk and capital adequacy management. OP MB is responsible for its own risk and capital adequacy management in accordance with the nature and extent of its operations.

OP MB's Board of Directors makes decision on its risk and capital adequacy management in line with the principles adopted by the central cooperative's Executive Board. In addition, the Board of Directors deals with, in terms of quality and extent, far-reaching and important matters in principle from the perspective of the company's operations, and any unusual matters. The Board of Directors decides on principles and procedures to ensure that the company operates in compliance with external regulation and OP Cooperative's guidelines.

The Managing Director is responsible for the implementation of risk and capital adequacy management according to the principles and guidelines that have been agreed on, and reports regularly on the company's business, risk-bearing capacity and risk exposure to the Board of Directors.

OP MB's risk and capital adequacy tasks are centralised within OP Financial Group's Risk Management. OP Financial Group's Risk Management is a function independent of business that provides guidelines for, controls and supervises the overall risk management of the Group and its entities, and analyses their risk exposure. Risk management focuses on preventive work, preparation and proactive analysis of risk exposure. The objective is to secure the Group's and its entities' sufficient risk-bearing capacity and to ensure that any business risks taken do not threaten profitability, capital adequacy, liquidity, business continuity and the achievement of strategic targets. It is also responsible for maintaining and developing risk management systems and methods.

The fact that reports on measurable risks are produced for OP MB on a centralised basis and separate from any business operations also ensures the independence of risk reporting.
OP Financial Group's internal audit assists OP MB's Board of Directors and management by performing audits to assess the achievement of the strategic and operational goals, the quality of risk management, the reliability of reporting, compliance with laws and instructions and the efficiency and appropriateness of operations.

3 OP MB's risks

The table below presents OP MB's most significant risks. The paragraphs below the table describe the nature of the risks and how they can be managed.

Strategic risks	Risk caused by changes in the business environment, inadequate response to changes in the competitive environment or customer behaviour, poor choice of the strategy or poor strategy implementation.
Operational risks	Risk of financial loss or other detrimental consequences caused by inadequate or failed processes, inadequate competence, inadequate or flawed procedures or systems or some external factors. Operational risks also include ICT, security, data security and procedural risks.
Model risks	Risk of loss or of loss of reputation caused by such decisions made on the basis of the results of the models, in which the errors in the development, implementation or use are the reason.
Compliance risk	Risks caused by non-compliance with external regulation, internal policies, appropriate procedures or ethical principles governing customer relationships.
Reputational risk	Risk of deterioration of reputation or trust caused by negative publicity or realisation of some risk.
Credit risks	Credit risk means that a counterparty fails to fulfil its obligations established through a credit relationship or that the customer's weakening creditworthiness leads to an increase in capital requirement. Non-fulfilment of other obligations of a counterparty is also known as counterparty risk.
Market risks	Market risks consist of interest rate risk and market risks associated with investment operations.
Liquidity risks	Liquidity risk comprises funding liquidity risk, structural funding risk and funding concentration risk.
Customer behaviour risks	Risk of change in customer behaviour that affects, for example, early repayments of contracts.

4 Strategic risks

Strategic risk management tools include analysing the risks when drawing up the strategy and continuously monitoring and analysing changes in the operating environment and the implementation of the strategy. Strategic risk is reduced by regular planning, based on views of customer needs, developments in different sectors and market areas, and of competition. OP MB’s reports its strategic risks on a regular basis.

5 Operational risks

The aim of operational risk management is to ensure that operations have been organised appropriately and that risks do not result in unforeseeable financial losses or other negative consequences, such as loss of reputation. OP MB is continually maintaining and enhancing a corporate culture that takes a positive approach to operational risk management and internal control.

The target level set for operational risks is moderate. The key area of operational risk management involves identifying and assessing risks and assessing the effectiveness and adequacy of risk control and management tools. Before any new business models (including outsourcing) are carried out or products or services are launched, their risks are assessed as laid down by the central cooperative's Risk Management. OP Financial Group offers customers only products and applies business models that have been approved at Group level. Risks that may disrupt business continuity are prepared against by means of business continuity planning. Business continuity planning also forms the basis for preparation against emergency conditions referred to in the Emergency Powers Act. Business continuity plans are tested according to testing plans that have been made.

Any effect of a materialised operational risk may be transferred outside OP MB through insurance.

OP MB adheres to OP Financial Group's uniform, system-supported operating model in its operational risk management. In this model, OP MB assesses operational risks, involving identifying and assessing business risks and defining and monitoring measures designed to reduce them.

5.1 Monitoring and reporting operational risks

OP MB identifies operational risks associated with major products, services, functions, processes and systems, and outsourced services/functions. The company assesses the significance of identified risks on the basis of their financial effect and probability. The information obtained is used to support planning, decision-making and management.

Operational risks are regularly reported to OP MB’s Board of Directors.

6 Model risks

The significance of model risks has increased when risk assessment increasingly rests on quantitative methods, valuation methods used in accounting are used on a more extensive basis and business automation leads to decision-making to gradually hinge on model-based decision engines.

The OP MB manages model risk through well-defined roles and responsibilities as well as by ensuring adequate knowledge of quantitative methods and resource allocation. The development of models is segregated from their validation while the approval of models is segregated from the decisions of their implementation. The functionality of the models in use is assessed through monitoring and validation.

7 Compliance risks

Compliance risk forms part of operational risk. Compliance activities are aimed at ensuring that OP MB complies with laws, official instructions and regulations, self-regulation of markets, and internal guidelines, policies and instructions of OP Financial Group and OP MB. Compliance also ensures that customer relationship management complies with appropriate and ethically sound principles and practices.

Materialisation of compliance risk may result not only in financial loss but also other adverse consequences, such as sanctions. Such sanctions may include a corporate fine and separate administrative fines for violation of obligations, and public warnings and reprimands. Compliance risk may materialise in terms of loss or deterioration of reputation or trust.

Responsibility for regulatory compliance and its control within OP MB rests with the senior and executive management. Everyone employed by OP MB is responsible for his/her own part for regulatory compliance.

Guidelines, advice and support concerning compliance within OP Financial Group are the responsibility of the compliance organisation that is independent of the central cooperative. OP MB has concentrated its compliance function to this organisation.

7.1 Compliance risk management

Managing compliance risks forms part of internal control and good corporate governance practices and, as such, an integral part of business management duties and the corporate culture. Compliance risk management tools include monitoring legislative developments, providing the organisation concerned with guidelines, training and consultation in respect of observing practices based on regulation as well as supervising regulatory compliance with procedures applied within the organisation.

7.2 Compliance risk monitoring and reporting

Compliance risks are identified, assessed and reported regularly according to the operational risk management model as part of the assessment of operational risks. Any observations made by Compliance are reported on a regular basis.

8 Reputational risk

Reputational risk is managed proactively and in the long term by complying with regulation, good practices of the financial sector and the Group's Code of Business Ethics and by emphasising transparency of operations and communications. The Group adheres to international financial, social and environmental responsibility principles and international commitments.

Reputational risks are reported regularly to the management of OP MB and the central cooperative. Any threat to imminent reputational risk will be reported immediately.

9 Credit risks

Credit risk means that a counterparty fails to fulfil its obligations arising from debt relationship. The principles based on OP Financial Group's Risk-taking system and Risk Appetite Framework, and OP Financial Group's Risk Policy are used to control credit risk. The credit risk policy defines, for example, the target risk exposure level, risk-taking principles and restrictions as well as the principles governing customer selection and collateral.

OP MB's loan portfolio consists of mortgage loans placed as collateral for bonds, which OP MB has bought from OP Financial Group member cooperative banks, and of loans they granted to their customers on behalf of OP MB before 1 March 2016. OP MB ceased to buy loans from OP cooperative banks after IFRS 9 entered into force, and such purchases are now possibly only sporadically and in cases of crisis.

OP MB engages in funding by issuing bonds and lends funds thus acquired to OP Financial Group credit institutions in the form of intermediary loans referred to in the Covered Bond Act. OP MB uses mortgage loans from the loan portfolio of the OP cooperative bank receiving the intermediary loan as collateral for these bonds.

Framework agreements between OP MB and the OP cooperative banks specify obligations and rights related to the utilisation of OP MB's financing as well as credit risk management.

OP cooperative banks are in charge of loan decisions, loan management and customer relationship management in accordance with the guidelines issued by OP Financial Group and OP MB. The day-to-day credit approval process and its effectiveness play a key role in the management of credit risks. A customer's sufficient debt-servicing capacity is the prerequisite for all lending. Careful and deliberate lending decisions are based on decision-making guidelines and updated credit rating. OP MB ensures the repayment capacity of private customers against higher interest rates. Customers can protect their loans against higher interest rates by choosing an interest rate cap or corridor. Customers are also offered payment protection insurance in case of illness or unemployment. Collateral evaluation is based on the principle of independent evaluation and a prudent approach to fair value. In lending, OP MB avoids high financing percentages. Collateral values are changed where necessary and their development is monitored on a regular basis. OP MB monitors a borrower's creditworthiness and repayment capacity and reacts to any repayment problems as early as possible. In case a customer gets into difficulties, OP MB checks whether there is need for collateral re-evaluation.

OP MB monitors and reports on credit risks on a regular basis. Credit rating reports, the loan portfolio quality, past due receivables and doubtful receivables number among monitoring tools.

Credit rating controls customer selection, consequences of insufficient collateral and exposure pricing. Target values by borrower grade have been set for the Group's and its banks' new lending and loan portfolio to maintain good loan portfolio quality. OP Financial Group uses credit risk models for Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD). For OP MB, the rating model for private customers is the most important, in which agreements are grouped into borrower grades based on probability of default.

OP MB makes extensive use of credit risk models in measuring and managing credit risk, such as in

- lending and pricing;
- specifying financing decision-making powers;
- setting and monitoring the loan portfolio's qualitative targets;
- credit risk reporting;
- capital adequacy measurement using the Internal Ratings Based Approach (IRBA);
- measuring economic capital and expected loss; and
- measuring expected credit loss.

10 Liquidity risk

Liquidity risk comprises funding liquidity risk and structural funding risk as well as concentration risk associated with funding. Funding liquidity risk refers to the risk that OP Financial Group will not be able to meet its current and future cash flows and collateral needs, both expected and unexpected, without affecting daily operations or the bank's overall financial position. Structural funding risk refers to uncertainty related to long-term lending, arising from the refinancing risk due to the structure of funding. Funding concentration risk refers to the risk that the bank's funding becomes more difficult due, for example, to a transaction related to an individual counterparty, currency, instrument or maturity band.

Liquidity risk management is based on OP Financial Group's principles of the risk tolerance system and the Risk Policy lines and set risk limits. The ALM and Risk Management Committee of the central cooperative's Executive Board approves the qualitative targets set for the liquidity buffer, a funding plan, and a business continuity and contingency funding plan in the case of threat scenarios. The contingency plan contains a control model for liquidity for various threshold levels, funding sources and a contingency funding plan for liquidity management at operational level.

OP Financial Group manages its liquidity position through the proactive planning of the funding structure, the Group's risk limits and limits and control limits derived from them as well as target levels, the monitoring of the liquidity status and a well-balanced liquidity buffer, planning and management of daily liquidity, the business continuity and contingency plan based on emergency preparedness, as well as the effective and ongoing control of the Group's liquidity status.

Funding liquidity management is governed by the regulations governing the minimum reserve and marginal lending facility systems by the European Central Bank.

OP Financial Group safeguards its liquidity with long-term funding planning, the liquidity buffer and the sources of finance referred to in the contingency plan. The liquidity buffer has the size required for the time to implement the contingency plan in a liquidity crisis. Liquid funding may be made available for use by the Group by selling notes and bonds in the liquidity buffer or using them as collateral. The liquidity buffer consists mainly of deposits with the central bank and receivables eligible as collateral for central bank refinancing.

As OP Financial Group's central bank, OP Corporate Bank plc is tasked with securing the liquidity of the entire Group and each Group entity (incl. OP MB). OP Financial Group's daily liquidity management refers to managing liquidity of the companies engaged in banking. Any changes in OP MB's liquidity position will change OP Corporate Bank's liquidity position. The liquidity buffer of Banking within the entire OP Financial Group is managed by the Group's Treasury.

OP Financial Group's funding planning is based on the proactive planning of the funding structure and on the risk limits set for the liquidity risk. Deposits from the general public and wholesale funding form the basis of OP Financial Group's funding. Wholesale funding is aimed at actively and proactively covering funding needs arising from the growth differentials between the receivables and the deposit portfolio in the balance sheet, funding maturity and other internal objectives. A solid funding structure requires that the loan portfolio and OP Financial Group's liquidity buffer be funded not only through deposit funding and short-term funding but also through long-term wholesale funding. Diversifying funding sources will reduce OP Financial Group's dependence on an individual source and decrease price risk associated with funding. OP MB diversifies its funding by time, maturity, instrument and customer segment. Any surplus deposits with member banks are mainly channelled to the central cooperative consolidated accounts or instruments it has issued in order not to increase OP Financial Group's wholesale funding unnecessarily. OP Corporate Bank manages on a centralised basis OP Financial Group's wholesale funding in the form of senior bonds and equity capital and OP MB's funding based on covered bonds.

The central cooperative's Executive Board is responsible for OP Financial Group's liquidity risk management and controls funding liquidity management using various threshold levels. In cases of market disruption, liquidity management relies on the business continuity and contingency plan. Each entity within OP Financial Group controls its liquidity management within the framework of control limits issued by the central cooperative and guidelines and of account, deposit and loan terms and conditions.

As the central institution of the amalgamation of cooperative banks, OP Cooperative has given its member credit institution special permission, under the Act on the Amalgamation of Deposit Banks, whereby the liquidity requirements set for credit institutions mentioned in Part VI of the EU Capital Requirements Regulation are not applied to the member credit institutions. Liquidity based on the regulation is subject to supervision and reporting at the level of the cooperative banks' amalgamation.

10.1 Measuring, monitoring and reporting liquidity risks

OP Financial Group has set its liquidity risk tolerances for the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR).

In addition, a Group-level limit has been set for net cash flows by maturity which guide the structural funding risk. The risk indicator for the structural funding risk indicates the maximum portion of the net cash flows in the balance sheet that may have a maturity within different time periods. Refinancing risk is associated with covered bonds issued by OP MB. OP MB monitors long-term funding maturity using a maturity distribution, for which it has set limits. OP Financial Group's and OP MB's structural risk is subject to monthly monitoring.

Furthermore, OP Financial Group also monitors Group-level liquidity risk in scenarios based on liquidity stress testing. The funding liquidity risk indicators show for how long the liquidity buffer will cover the known and predictable net cash flows payable daily outside the Group and any unexpected liquidity stress scenario. Liquidity risk is subject to monitoring on a daily basis.

11 Market risks

Market risks are the result of price, volatility and market liquidity changes in the financial market.

The most significant market risk relates to the effect of a change in interest rates on net interest income, i.e. interest income risk associated with the banking book. Market risk may also come from investment. Through its continuous funding and liquidity planning, OP MB aims to maintain a situation in which it does not have significant financing surplus to invest. Investments in notes and bonds issued by governments and other banks may also be used as supplementary collateral as specified in the Act on Mortgage Credit Banks.

When making investment decisions, OP MB assesses the investment's effect on the interest rate risk and funding risk.

The task of market risk management is to identify and assess market risks associated with business operations, mitigate them to an acceptable level, and report them regularly and efficiently. This ensures that changes in market prices or other external market factors will not excessively deteriorate the long-term profitability or capital adequacy within OP MB.

Guidelines that control and mitigate market risks include the principles of OP Financial Group’s risk tolerance system and the Group’s risk policy that supplement them, and the central cooperative's risk management guidelines and limits and control limit indicators.

11.1 Interest rate risk

OP MB's interest rate risk relates to the differences in the bases of interest rates concerning lending and funding. OP MB primarily manages interest rate risk by using derivatives and regulating the range of products and terms and conditions related to lending and regulating interest rate reset dates and the bases of interest rates. OP MB enters into derivatives contracts only for hedging purposes, with OP Corporate Bank plc being always the counterparty.

11.2 Monitoring and reporting

OP MB reports on market risks on a monthly basis. The central cooperative's Risk Management provides market risk reports for OP MB and regularly reports the development of the entire OP Financial Group's balance sheet structure and market risks to the central cooperative's management.

OP MB monitors risks associated with derivatives as part of the exposure using the same benchmarks as for balance sheet exposure.

NOTES TO THE INCOME STATEMENT

NOTE 3. Net interest income, TEUR	2018	2017
Interest income		
From receivables from credit institutions		
Interest	-7 877	-2 426
Negative interest	-288	-213
From receivables from customers	70 910	79 719
From derivative contracts		
From hedge accounting	-10 177	-11 392
Other interest income	19	5
Total	**52 587**	**65 692**
Interest expenses		
From liabilities to credit institutions	-3 151	-2 527
From derivative contracts		
From hedge accounting	-147 571	10 810
From debt securities issued to the public	131 416	-17 598
Other interest expenses	0	24
Total	**-19 306**	**-9 292**
Net interest income	**71 893**	**74 984**

Net income from hedge accounting

Net income from hedging instruments is -39,286 (122,443) and net income from hedged items is 39,286 (-122,443).

NOTE 4. Net commissions and fees, TEUR	2018	2017
Commission income		
From lending	5 972	6 465
Total	**5 972**	**6 465**
Commission expenses		
From lending to OP cooperative banks	5 783	6 336
Loan management fee to OP cooperative banks	49 297	49 936
Issue of bonds	72	92
Other	13	11
Total	**55 165**	**56 375**
Net commissions and fees	**-49 193**	**-49 910**

NOTE 5. Personnel costs, TEUR	2018	2017
Wages and salaries	264	258
Pension costs		
Defined contribution plans	34	41
Defined benefit plans	-110	23
Total	-76	64
Other indirect personnel costs	3	6
Total personnel costs	**191**	**328**

NOTE 6. Depreciation/amortisation and impairment loss, TEUR	2018	2017
Depreciation/amortisation		
On intangible assets	783	836
Total	**783**	**836**

NOTE 7. Other operating expenses, TEUR	2018	2017
Rental expenses	8	8
Government charges and audit fees	504	358
Membership fees	121	73
Office expenses	211	204
ICT costs	3 385	2 768
Telecommunications	32	41
Marketing	1	4
Other administrative expenses	132	157
Insurance and security costs	94	80
Experts' costs	556	708
Other	54	128
Total	5 099	4 528

Fees paid to auditors by assignment

Auditing	12	8
Other audit opinions		
Tax counselling		
Other services	69	61
Total	**81**	**69**

Non-audit services provided by KPMG Oy Ab totalled TEUR 16

NOTE 8. Impairment losses on receivables, TEUR	2018	2017
Receivables written down as loan and guarantee losses	127	38
Recoveries of receivables written down	-14	-1
Expected credit losses (ECL) on receivables from customers and off-balance-sheet items.	269	0
Increase in impairment losses on individually assessed receivables	0	341
Decrease in impairment losses on individually assessed receivables	0	-53
Collectively assessed impairment losses	0	-48
Total	**382**	**276**

NOTE 9. Income tax, TEUR	2018	2017
Current tax	3 227	3 863
Income tax paid for previous periods		
Deferred tax	22	5
Income tax expense on the income statement	**3 249**	**3 868**
Corporate income tax rate	20,0 %	20,0 %

Reconciliation between tax expense in the income statement and tax expense calculated by the applicable tax rate

Earnings before tax	16 248	19 341
Share of the profit according to the tax rate	3 250	3 868
Income tax paid for previous periods		
Other	0	0
Income tax expense on the income statement	**3 249**	**3 868**

NOTES TO ASSETS

NOTE 10. Receivables from credit institutions, TEUR

	31 Dec 2018	31 Dec 2017
Receivables from credit institutions		
Deposits		
Repayable on demand	133 460	363 609
Other		
Other than those repayable on demand	6 776 169	4 776 169
Total receivables from credit institutions	**6 909 630**	**5 139 778**

NOTE 11. Derivative contracts, TEUR

	31 Dec 2018	31 Dec 2017
Derivative contracts		
Hedging derivative contracts		
Fair value hedging		
Interest rate derivatives	139 668	129 810
Total derivative contracts	**139 668**	**129 810**

More detailed information on derivative contracts can be found in Note 27.

NOTE 12. Receivables from customers, TEUR

	31 Dec 2018	31 Dec 2017
Loans to the public and public sector entities	6 995 929	8 804 719
Loss allowance	-1 056	0
Collectively assessed impairments	0	-263
Individually assessed impairments	0	-635
Total receivables from customers	**6 994 873**	**8 803 822**

Loss allowance

	Receivables from customers and off-balance-sheet commitments			
	Stage 1	**Stage 2**	**Stage 3**	**Total**
TEUR	**12 mths**	**Lifetime**	**Lifetime**	
Loss allowance on 1 January 2018	17	97	673	786
Transfers from Stage 1 to Stage 2	-4	57	0	53
Transfers from Stage 1 to Stage 3	0	0	124	124
Transfers from Stage 2 to Stage 1	2	-11	0	-9
Transfers from Stage 2 to Stage 3	0	-9	167	158
Transfers from Stage 3 to Stage 2	0	4	-64	-60
Transfers from Stage 3 to Stage 1	0	0	-23	-23
Decreases due to derecognition	-1	-12	-86	-99
Changes in risk parameters	9	98	70	177
Allowances due to recognised write-offs	0	0	-52	-52
Total net result effect	**6**	**127**	**137**	**269**
Loss allowance on 31 Dec. 2018	**22**	**224**	**810**	**1 056**

NOTE 13. Investment assets, TEUR

	31 Dec 2018	31 Dec 2017
Financial assets measured fair value through other comprehensive income		
Shares and participations, unquoted	40	40
Total investment assets	**40**	**40**

Shares and participations other than those quoted publicly have been measured at cost.

NOTE 14. Intangible assets, TEUR

	31 Dec 2018	31 Dec 2017
Software, licences and user rights	120	904
Total intangible assets	**120**	**904**

Changes in intangible assets — **31 Dec 2018**

	Software	Total
Acquisition cost on 1 January	3 343	3 343
Increases	0	0
Decreases	0	0
Acquisition cost on 31 December	3 343	3 343
Accumulated amortisation and impairment losses on 1 January	2 440	2 440
Amortisation for the period	783	783
Decreases	0	0
Accumulated amortisation and impairment losses on 31 December	3 223	3 223
Carrying amount on 31 December	120	120
of which construction in progress		-

	Software	Total
		31 Dec 2017
Acquisition cost on 1 January	3 523	4 977
Increases	0	0
Decreases	0	0
Acquisition cost on 31 December	3 343	3 343
Accumulated amortisation and impairment losses on 1 January	1 783	3 237
Amortisation for the period	836	836
Decreases	179	0
Accumulated amortisation and impairment losses on 31 December	2 440	2 440
Carrying amount on 31 December	904	904
of which construction in progress	-	-

Amortisation, impairment losses and their reversals have been recognised under Depreciation/amortisation and impairment losses in the income statement.
The company had no impairment losses.

NOTE 15. Other assets, TEUR	**31 Dec 2018**	**31 Dec 2017**
Pension plan assets	83	82
Deferred income		
Interest	31 396	47 737
Other	1 047	1 568
Total	**32 525**	**49 386**

Note 21 Other liabilities describes the calculation of plan assets in greater detail.

NOTE 16. Tax assets, TEUR	**31 Dec 2018**	**31 Dec 2017**
Income tax asset	0	695
Deferred tax assets	0	10
Total tax assets	**0**	**705**
Income tax liabilities	-27	0
Deferred tax liabilities	-46	0
Total tax liabilities	**-74**	**0**
Specification of tax assets and liabilities		
Deferred tax assets		
Due to defined-benefit pension plans	0	34
Due to other items	30	53
Set-off against deferred tax liabilities	-30	-76
Total	**0**	**10**
Deferred tax liabilities		
From defined benefit pension plans	17	16
From other items	60	60
Set-off against deferred tax assets	-30	-76
Total	**46**	**0**
Changes in deferred taxes		
Deferred tax assets/liabilities on 1 January	10	15
Effect of IFRS 9 transition	-22	0
Recognised in the income statement		
Defined benefit pension obligations	-22	5
Other	0	-10
Recognised in statement of comprehensive income		
Items arising from remeasurement of defined benefit plans	-12	0
Total deferred tax assets/liabilities on 31 December	**-46**	**10**
Income tax assets	**-27**	**695**
Total tax assets and liabilities	**-74**	**705**

NOTES TO LIABILITIES AND EQUITY CAPITAL

NOTE 17. Liabilities to credit institutions, TEUR	31 Dec 2018	31 Dec 2017
Other than those repayable on demand		
Other liabilities	2 896 000	2 838 000
Liabilities to credit institutions	**2 896 000**	**2 838 000**

NOTE 18. Derivative contracts, TEUR	31 Dec 2018	31 Dec 2017
Derivative contracts		
Hedging derivative contracts		
Fair value hedging		
Interest rate derivatives	8 597	38 025
Total derivative contracts	**8 597**	**38 025**

More detailed information on derivative contracts can be found in Note 27.

NOTE 19. Debt securities issued to the public, TEUR	Average rate, %	31 Dec 2018	Average rate, %	31 Dec 2017
Bonds	0,63	10 742 840	0,88	10 796 102
Total debt securities issued to the public		**10 742 840**		**10 796 102**

Long-term bonds issued by OP Mortgage Bank

Bond	Book value	Interest rate base	Nominal interest %	Maturity
OP Mortage Bank rekisteröity Covered Bond (NSV)	114 815	Fixed	2,157	12.11.2024
OP Mortgage Bank Covered Bond 2014	998 065	Fixed	1,500	17.3.2021
OP Mortgage Bank Covered Bond 2014	999 435	Fixed	0,750	11.6.2019
OP Mortgage Bank Covered Bond 2014	997 364	Fixed	1,000	28.11.2024
OP Mortgage Bank Covered Bond 2015	19 991	Fixed	0,250	27.5.2020
OP Mortgage Bank Covered Bond 2015	1 248 294	Fixed	0,250	23.11.2020
OP Mortgage Bank Covered Bond 2015	997 371	Fixed	0,625	4.9.2022
OP Mortgage Bank Covered Bond 2016	1 245 926	Fixed	0,250	11.5.2023
OP Mortgage Bank Covered Bond 2017	994 236	Fixed	0,250	13.3.2024
OP Mortgage Bank Covered Bond 2017	995 226	Fixed	0,750	7.6.2027
OP Mortgage Bank Covered Bond 2017	996 891	Fixed	0,050	22.2.2023
OP Mortgage Bank Covered Bond 2018	995 767	Fixed	0,625	1.9.2025
	10 603 382			
Valuation	139 458			
Total	**10 742 840**			

Reconciliation of changes in liabilities in cash flows from financing activities against balance sheet items

Balance sheet value 1 Jan. 2018	**10 796 102**
Changes in cash flows from financing activities	
Increases in bonds	995 413
Increases total	**995 413**
Decreases in bonds	1 100 000
Decreases total	**1 100 000**
Total changes in cash flows from financing activities	**-104 588**
Valuations and foreign exchange changes	-51 326
Balance sheet value 31 Dec. 2018	**10 742 840**

Balance sheet value 1 Jan. 2017	**9 277 801**
Changes in cash flows from financing activities	
Increases in bonds	2 982 709
Increases total	**2 982 709**
Decreases in bonds	1 350 000
Decreases total	**1 350 000**
Total changes in cash flows from financing activities	**1 632 709**
Valuations and foreign exchange changes	114 407
Balance sheet value 31 Dec. 2017	**10 796 102**

NOTE 20. Other liabilities, TEUR	31 Dec 2018	31 Dec 2017
Other liabilities		
Payment transfer liabilities	276	91
Deferred expenses	0	169
Accrued expenses		
Interest liabilities	46 749	65 577
Other accrued expenses	4 217	6 183
Payables based on purchase invoices	398	216
Other	12	24
Total	**51 652**	**72 259**

Defined benefit pension plans

OP Mortgage Bank has funded assets of its pension schemes through OP Bank Group Pension Fund and OP Bank Group Pension Foundation. Schemes related to supplementary pensions in the Pension Foundation, as well as the TyEL (Employees' Pensions Act) funded old-age and disability pension schemes managed by the Pension Fund are treated as defined benefit plans. Contributions to the TyEL pay-as-you-go system are treated as defined contribution plans. The amount of the company's pension liabilities is not substantial.

The new TyEL came into force in 2017. Benefits under the employees pension scheme comprise old-age pension, partial early old-age pension, year-of-service pension, disability pension, survivors' pension and rehabilitation benefits. Partial early old-age pension based on the previous TyEL was replaced with partial old-age pension and it did not recognise years-of-age pension. The changes in benefits caused by the amended law were already recognised in the income statement before 2017.

The most significant actuarial risks of OP Bank Group Pension Fund/OP Bank Group Pension Foundation are associated with interest rate and market risks, future increases in pension benefits, systematically increasing life expectancy and inflation risk. A change in the discount rate for pension liabilities has a substantial effect on the amount of pension liabilities.

The Representative Assembly of OP Bank Group Pension Fund decided on 31 July 2018 to transfer the management of statutory earnings-related pension insurance and the pension insurance portfolio of 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. Based on the initial plan, the remaining pension liability will be transferred to Ilmarinen at a later date, but no earlier than at the end of 2020. The transfer reduced OP Mortgage Bank's pension costs and improved its earnings before tax by EUR 150,000.

	Defined benefit obligations		Fair value of plan assets		Net liabilities (assets)	
Balance sheet value of defined benefit plans, TEUR	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**
Opening balance 1 Jan.	689	634	-601	-569	88	65
Defined benefit pension costs recognised in income statement						
Current service cost	32	29			32	29
Interest expense (income)	11	11	-10	-10	2	1
Post service cost and settlements	-477		328		-150	
Administrative expenses			1	1	1	1
Total	**-435**	**40**	**319**	**-9**	**-116**	**31**
Losses (gains) recognised in other comprehensive income arising from remeasurement						
Actuarial losses (gains) arising from changes in economic expectations	-43	-6			-43	-6
Actuarial losses (gains) arising from changes in demographic expectations						
Return on TyEL interest rate difference and growth in old-age pension liabilities (net)	8	8	-8	-8		
Experience adjustments	-11	39			-11	39
Return on plan assets, excluding amount (–) of net defined benefit liability (asset)			-7	-33	-7	-33
Total	**-46**	**40**	**-14**	**-41**	**-60**	**-1**
Other						
Employer contributions			6	-8	6	-8
Benefits paid	-22	-25	22	25		
Total	**-22**	**-25**	**28**	**18**	**6**	**-8**
Closing balance 31 Dec.	**186**	**689**	**-268**	**-601**	**-83**	**88**

Liabilities and assets recognised in the balance sheet, TEUR	**31 Dec 2018**	**31 Dec 2017**
Net liabilities/assets (Pension Foundation)	-83	-82
Net liabilities/assets (Pension Fund)	0	169
Total net liabilities		**169**
Total net assets	**-83**	**-82**

Pension Foundation assets, grouped by valuation technique, 31 Dec. 2018, TEUR	**Total**
Shares and participations	47
Notes and bonds	99
Real property	9
Mutual funds	93
Structured investment vehicles	0
Derivatives	0
Other assets	21
Total	**268**

Pension Fund and Pension Foundation assets, grouped by valuation technique, 31 Dec. 2017, TEUR	**Total**
Shares and participations	58
Notes and bonds	142
Real property	37
Mutual funds	312
Structured investment vehicles	2
Derivatives	1
Other assets	48
Total	**601**

Contributions payable under the defined benefit pension plan in 2019 are estimated at TEUR 1 thousand.

The duration of the defined benefit pension obligation in the Pension Foundation on 31 December 2018 was 2.8 years.

Key actuarial assumptions used, 31 December 2018	Pension Foundation
Discount rate, %	1,8
Future pay increase assumption, %	2,4
Future pension increases, %	1,8

Key actuarial assumptions used, 31 December 2017	Pension Fund	Pension Foundation
Discount rate, %	1,7	1,5
Future pay increase assumption, %	2,6	2,5
Future pension increases, %	1,2	1,9

NOTE 21. Shareholders' equity, TEUR	31 Dec 2018	31 Dec 2017
Share capital	60 000	60 000
Unrestricted reserves	245 000	245 000
Retained earnings		
Profits for previous years	59 721	59 585
Profit for the financial year	12 999	15 473
Total equity	**377 720**	**380 057**

The IFRS 9 transition of 1 January 2018 increased retained earnings by EUR 90,000.

Development costs (non-distributable item)	**-120**	**-904**
Distributable reserves	**317 600**	**319 154**
Distributable profits	**72 600**	**74 154**

Reserve for invested non-restricted equity consists of OP Cooperative's capital investment of EUR 245,000,000.

Share capital and number of shares

	Total
Share capital, EUR thousand	60 000
Number of shares	76 592
Proportion of share capital, %	100

OP Cooperative holds 100% of OP Mortgage Bank.

The minimum share capital of the Company is EUR 8,500,000 and the maximum share capital is EUR 150,000,000, within which limits the share capital may be increased or reduced without altering the Articles of Association. The minimum number of shares is 34,000 and the maximum number is 136,000. Permission from the Company is required for the acquisition of shares through transfer. The shares have no nominal value.

OTHER NOTES TO THE BALANCE SHEET

NOTE 22. Classification of financial assets and liabilities, TEUR

Assets	Amortised cost	Recognised at fair value through profit or loss	Fair value through other comprehensive income	Carrying amount total	Fair value total
Receivables from credit institutions and central banks	6 909 630			6 909 630	6 909 630
Derivative contracts		139 668		139 668	139 668
Receivables from customers	6 994 873			6 994 873	6 994 873
Shares and participations			40	40	40
Other receivables	32 525			32 525	32 525
Total on 31 Dec 2018	**13 937 028**	**139 668**	**40**	**14 076 736**	**14 076 736**

Liabilities	Recognised at fair value through profit or loss	Amortised cost	Carrying amount total	Fair value total
Liabilities to credit institutions		2 896 000	2 896 000	2 896 000
Derivative contracts	8 597		8 597	8 597
Debt securities issued to the public		10 742 840	10 742 840	10 883 185
Other liabilities		51 625	51 625	51 625
Total on 31 Dec 2018	**8 597**	**13 690 465**	**13 699 062**	**13 839 406**

Assets	Loans and receivables	Recognised at fair value through profit or loss	Fair value through other comprehensive income	Carrying amount total	Fair value total
Receivables from credit institutions and central banks	5 139 778			5 139 778	5 139 778
Derivative contracts		129 810		129 810	129 810
Receivables from customers	8 803 822			8 803 822	8 803 822
Shares and participations			40	40	40
Other receivables	49 386			49 386	49 386
Total on 31 Dec 2017	**13 992 986**	**129 810**	**40**	**14 122 836**	**14 122 836**

Liabilities	Recognised at fair value through profit or loss	Amortised cost	Carrying amount total	Fair value total
Liabilities to credit institutions		2 838 000	2 838 000	2 838 000
Derivative contracts	38 025		38 025	38 025
Debt securities issued to the public		10 796 102	10 796 102	10 954 460
Other liabilities		72 259	72 259	72 259
Total on 31 Dec 2017	**38 025**	**13 706 362**	**13 744 387**	**13 902 745**

Debt securities issued to the public are carried at amortised cost. On 31 December, the fair value of these debt instruments was approximately EUR 140,345 thousand (158,358) higher than their carrying amount, based on information available in markets and employing commonly used valuation techniques.

NOTE 23. Financial instruments classification, grouped by valuation technique, TEUR

Recurring fair value measurements of assets	31 Dec 2018 Balance sheet value	Fair value measurement at year end Level 1*	Level 2**
Derivative contracts	139 668		139 668
Total	**139 668**		**139 668**

Recurring fair value measurements of assets	31 Dec 2017 Balance sheet value	Fair value measurement at year end Level 1*	Level 2**
Derivative contracts	129 810		129 810
Total	**129 810**		**129 810**

Recurring fair value measurements of liabilities	31 Dec 2018 Balance sheet value	Fair value measurement at year end Level 1*	Level 2**
Derivative contracts	8 597		8 597
Total	**8 597**		**8 597**

Recurring fair value measurements of liabilities	31 Dec 2017 Balance sheet value	Fair value measurement at year end Level 1*	Level 2**
Derivative contracts	38 025		38 025
Total	**38 025**		**38 025**

Financial liabilities not measured at fair value	31 Dec 2018 Balance sheet value	Fair value measurement at year end Level 1*	Level 2**
Debt securities issued to the public	10 742 840	10 738 905	144 280
Total	**10 742 840**	**10 738 905**	**144 280**

Financial liabilities not measured at fair value	31 Dec 2017 Balance sheet value	Fair value measurement at year end Level 1*	Level 2**
Debt securities issued to the public	10 796 102	10 710 871	243 589
Total	**10 796 102**	**10 710 871**	**243 589**

*Level 1 includes equities listed on major stock exchanges, quoted debt instruments issued by companies, governments and financial institutions as well as exchange-traded derivatives. The fair value of these instruments is determined on the basis of market quotes.

** Valuation techniques based on observable input parameters. The fair value of the instruments included within Level 2 means value derived from the market price of a financial instrument's components or similar financial instruments; or value which can be determined using commonly used valuation models and techniques if the inputs significant to the fair value measurement are based on observable market data. The fair value hierarchy level at OP Financial Group's includes OTC derivatives, quoted debt instruments issued by companies, governments and financial institutions which have not been included in Level 1, and repo agreements as well as securities lent or borrowed.

Transfers between hierarchy levels of recurring fair value measurements

OP Mortgage Bank plc does not hold any transfers between the levels of fair value measurement.

NOTES CONCERNING CONTINGENT LIABILITIES AND DERIVATIVES

NOTE 24. Off-balance-sheet commitments, TEUR	31 Dec 2018	31 Dec 2017
Binding loan commitments	2	3
Total off-balance-sheet commitments	**2**	**3**

NOTE 25. Leases, TEUR	31 Dec 2018	31 Dec 2017

OP Mortgage Bank plc as the lessor

OP Mortgage Bank has leased office premises.

Leases of facilities	4	4

OP Financial Group's internal service charges have been transferred to other expenses.

NOTE 26. Derivative contracts, TEUR

Derivative contracts held for hedging – fair value hedging on 31 Dec 2018

	Nominal values/residual term to maturity				Fair values		
	Less than 1 year	1 to 5 years	More than 5 years	Total	Assets	Liabilities	Credit equivalent
Interest rate derivatives							
Interest rate swaps	2 450 856	8 092 527	6 849 439	17 392 822	139 668	8 597	319 910
Total interest rate derivatives	**2 450 856**	**8 092 527**	**6 849 439**	**17 392 822**	**139 668**	**8 597**	**319 910**

Derivative contracts held for hedging – fair value hedging on 31 Dec 2017

	Nominal values/residual term to maturity				Fair values		
	Less than 1 year	1 to 5 years	More than 5 years	Total	Assets	Liabilities	Credit equivalent
Interest rate derivatives							
Interest rate swaps	2 648 299	7 824 977	8 561 488	19 034 765	129 810	38 025	334 303
Total interest rate derivatives	**2 648 299**	**7 824 977**	**8 561 488**	**19 034 765**	**129 810**	**38 025**	**334 303**

OTHER NOTES

NOTE 27. Personnel and related party

The average number of employees was five (5) in 2018.

OP Mortgage Bank's related parties include 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. OP Mortgage Bank's administrative personnel comprise the company's Managing Director, Board members and their close family members. Related parties also include companies over which a person among administrative personnel or his/her close family member exercises significant influence.

Business transactions with related parties, TEUR

	2018		2017	
	OP Cooperative	Other	OP Cooperative	Other
Other receivables		1 587 316		1 241 752
Other liabilities	79	2 994 894	7	2 993 417
Interest income		12 583		10 620
Interest expenses		146 158		-6 175
Net commission income and expenses		-8 948		-10 925
Other operating income		0		232
Operating costs	357	2 715	388	2 175

Shares held by related parties

The parent company holds all of the 76,592 shares.

NOTE 28. Variable remuneration

OP Personnel Fund

OP Mortgage Bank belongs to OP Financial Group's OP Personnel Fund.

Payment of profit-based bonuses to OP Financial Group's Personnel Fund in 2018 was based on the achievement of the following targets: OP Financial Group's EBT with a weight of 60%, use of digital services with a weight of 20%, service encounter NPS with a weight of 15% and brand NPS with a weight of 5%. Profit-based bonuses for 2018 transferred to the Fund account for some 1.7% of the combined salaries and wages earned by the Fund's members.

Bonuses recognised in 2018 totalled EUR 4 thousand (7).

Short-term remuneration schemes

In short-term schemes, the performance period is one calendar year and the bonus is paid in cash. Short-term remuneration schemes are based on targets set by each company, covering all personnel of OP Financial Group.

The shared metrics at OP Financial Group Central Cooperative determine the maximum bonus payable under the short-term scheme. The shared metrics include OP Financial Group's EBT (weight of 50%), OP Financial Group's operating expenses (weight of 25%) and OP Financial Group's service encounter NPS (weight of 25%). Targets shown in the balanced scorecards and derived from annual planning are decided by the business lines/functions.

Expenses for the scheme are recognised from the beginning of the performance period up to the date of payout (vesting period) as personnel costs, and the equivalent liability is recognised under deferred expenses. A liability recognised under the scheme amounted to EUR 24 thousand (21) on 31 December 2018.

NOTE 29. Events after the balance sheet date

No significant events after the reporting period.

NOTES CONCERNING RISK MANAGEMENT

NOTE 30. Capital base and capital adequacy

Information about own funds and capital adequacy has been presented in the report of the Board of Directors.

NOTE 31. Financial assets and impairment losses recognised on them for the financial year

OP Mortgage Bank's financial assets comprise the items disclosed under Notes 10-13. Impairment losses on loans on a collective basis of EUR -48 thousand (-48) have been recognised as financial assets.

NOTE 32. Liabilities, TEUR

	31 Dec 2018 Finland			31 Dec 2017 Finland		
	Carrying amount	Impairment losses	Interest carried forward	Carrying amount	Impairment losses	Interest carried forward
Assets						
Receivables from credit institutions	6 909 630		2 312	5 139 778		901
Receivables from customers	6 994 873	1 056	2 741	8 803 822	897	4 856
Derivative contracts	139 668			129 810		
Total	**14 044 170**	**1 056**	**5 053**	**14 073 410**	**897**	**5 757**
Off-balance-sheet commitments						
Unused standby credit facilities and limits	2			3		
Total	**2**			**3**		
Total liabilities	**14 044 172**	**1 056**	**5 053**	**14 073 413**	**897**	**5 757**

NOTE 33. Liabilities by sector, TEUR

	31 Dec 2018			31 Dec 2017		
	Net balance sheet exposure	Off-balance-sheet		Net balance sheet exposure	Off-balance-sheet	
	Domestic	Domestic	Total	Domestic	Domestic	Total
Companies	8 984		8 984	11 344		11 344
Financial and insurance institutions	7 046 985		7 046 985	5 268 762		5 268 762
Households	6 985 145	2	6 985 147	8 797 259	3	8 797 262
Non-profit organisations						
Total	**14 041 114**	**2**	**14 041 116**	**14 077 365**	**3**	**14 077 368**

NOTE 34. Receivables from credit institutions and customers, and doubtful receivables, TEUR

31 Dec 2018	Not impaired (gross)	Loss allowance	Accounting balance (total)
Receivables from credit institutions and customers			
Receivables from credit institutions	6 909 630		6 909 630
Receivables from customers	6 995 929	1 056	6 994 873
Total	**13 905 558**	**1 056**	**13 904 502**
Receivables from credit institutions and customers by sector			
Non-banking corporate sector	8 985	0	8 984
Financial institutions and insurance companies	6 909 630		6 909 630
Households	6 986 944	1 055	6 985 888
Total	**13 905 558**	**1 056**	**13 904 502**

31 Dec 2017	Not impaired (gross)	Impaired (gross)	Total	Impairment loss	Accounting balance (total)
Receivables from credit institutions and customers					
Receivables from credit institutions	5 139 778		5 139 778		5 139 778
Receivables from customers	8 803 403	1 315	8 804 718	897	8 803 822
Total	**13 943 181**	**1 315**	**13 944 496**	**897**	**13 943 600**
Receivables from credit institutions and customers by sector					
Non-banking corporate sector	11 343		11 343	2	11 341
Financial institutions and insurance companies	5 134 822		5 134 822		5 134 822
Households	8 797 017	1 315	8 798 332	895	8 797 437
Total	**13 943 181**	**1 315**	**13 944 496**	**897**	**13 943 600**

31 Dec 2018	Not impaired (gross)	Total	Capital arrears	Interest in arrears	Individually assessed impairment
Doubtful receivables					
Receivables from credit institutions					
Receivables from customers	297 169	297 169	4 076	72	910
Total	**297 169**	**297 169**	**4 076**	**72**	**910**
Doubtful receivables by sector					
Non-banking corporate sector					
Households	297 169	297 169	4 076	72	910
Total	**297 169**	**297 169**	**4 076**	**72**	**910**

31 Dec 2017	Not impaired (gross)	Impaired (gross)	Total	Capital arrears	Interest in arrears	Collectively assessed impairment	Individually assessed impairment
Doubtful receivables							
Receivables from credit institutions							
Receivables from customers	301 394	1 315	302 709	3 832	83	263	633
Total	**301 394**	**1 315**	**302 709**	**3 832**	**83**	**263**	**633**
Doubtful receivables by sector							
Non-banking corporate sector						2	
Households	301 394	1 315	302 709	3 832	83	261	633
Total	**301 394**	**1 315**	**302 709**	**3 832**	**83**	**263**	**633**

31 Dec 2018	Performing	Non-performing	Total portfolio	Loss allowance	Accounting balance (total)
Doubtful receivables					
Over 90 days past due		11 277	11 277	637	10 640
Classified as default		2 668	2 668	29	2 639
Forborne loans					
Renegotiated	279 017	4 207	283 224	245	282 979
Total	**279 017**	**18 152**	**297 169**	**910**	**296 258**

31 Dec 2017	Performing	Non-performing	Total portfolio	Total impairment loss	Accounting balance (total)
Doubtful receivables					
Over 90 days past due		13 112	13 112	431	12 681
Classified as default		1 483	1 483	13	1 470
Forborne loans					
Renegotiated	283 338	4 777	288 115	189	287 925
Total	**283 338**	**19 372**	**302 709**	**633**	**302 076**

The loan portfolio is diversified. OP Mortgage Bank has not any groups of connected clients whose exposures exceed 10% of the capital base.

The bank reports as the amount of a receivable that is more than 90 days past due whose interest or principal amount has been overdue and outstanding for over three months. Agreements with the lowest two borrower grades (F for private customers and 11–12 for other) are reported as potential default. Forborne loans include receivables that have been modified due to the customer's financial difficulties. The loan terms and conditions of other renegotiated receivables have been eased due to the customer's financial difficulties by means of such as granting a home repayment holiday of 6–12 months.

NOTE 35. Exposure by credit rating, TEUR

Personal exposure by credit rating	31 Dec 2018	31 Dec 2017
Personal exposure on the balance sheet, category A	5 502 472	6 869 574
Personal exposure on the balance sheet, category B	1 071 327	1 421 481
Personal exposure on the balance sheet, category C	237 980	301 970
Personal exposure on the balance sheet, category D	109 519	129 554
Personal exposure on the balance sheet, category E	52 607	64 498
Personal exposure on the balance sheet, category F	12 449	12 367
Personal exposure on the balance sheet, not classified	-1 210	-2 184
Off-balance-sheet personal exposure A	2	3
Off-balance-sheet personal exposure B		0
Total personal exposure	**6 985 147**	**8 797 262**

Corporate exposure by credit rating	31 Dec 2018	31 Dec 2017
Corporate exposure on the balance sheet, category 4.5	610	1 047
Corporate exposure on the balance sheet, category 5.0	4 878	4 650
Corporate exposure on the balance sheet, category 5.5	2 394	3 511
Corporate exposure on the balance sheet, category 6.0	545	358
Corporate exposure on the balance sheet, category 6.5	457	731
Corporate exposure on the balance sheet, category 7.0	47	980
Corporate exposure on the balance sheet, category 7.5	48	
Corporate exposure on the balance sheet, category 8.0		
Corporate exposure on the balance sheet, category 10.0	7	66
Total corporate exposure	**8 984**	**11 344**

NOTE 36. Structure of funding, TEUR

	31 Dec 2018	Share, %	31 Dec 2017	Share, %
Liabilities to credit institutions	2 896 000	20,6	2 838 000	20,1
Debt securities issued to the public	10 742 840	76,4	10 796 102	76,6
Other liabilities	51 625	0,4	72 259	0,5
Shareholders' equity	377 720	2,7	380 057	2,7
Total	**14 068 185**	**100,0**	**14 086 419**	**100,0**

NOTE 37. Maturity distribution of financial assets and liabilities by residual term to maturity, TEUR

31 Dec 2018	Less than 3 months	3–12 months	1–5 years	5–10 years	More than 10 years	Total
Financial assets						
Receivables from credit institutions	133 460		2 776 169	4 000 000		6 909 630
Receivables from customers	189 097	573 430	2 647 263	2 158 457	1 426 625	6 994 873
Total financial assets	**322 558**	**573 430**	**5 423 432**	**6 158 457**	**1 426 625**	**13 904 502**
Financial liabilities						
Liabilities to credit institutions	1 700 000	530 000	666 000			2 896 000
Debt securities issued to the public		1 138 893	5 506 538	4 097 409		10 742 840
Total financial liabilities	**1 700 000**	**1 668 893**	6 172 538	**4 097 409**		**13 638 840**

31 Dec 2018	Less than 1 year	More than 1 year	Total
Off-balance-sheet commitments*	2		2
Total off-balance-sheet commitments	**2**		**2**

31 Dec 2017	Less than 3 months	3–12 months	1–5 years	5–10 years	More than 10 year	Total
Financial assets						
Receivables from credit institutions	363 609		743 369	4 032 800		5 139 778
Receivables from customers	236 219	676 803	3 180 056	2 704 798	2 005 945	8 803 822
Total financial assets	**599 828**	**676 803**	**3 923 425**	**6 737 598**	**2 005 945**	**13 943 600**
Financial liabilities						
Liabilities to credit institutions	500 000	1 192 000	1 146 000			2 838 000
Debt securities issued to the public		1 116 211	4 335 849	5 344 043		10 796 102
Total financial liabilities	**500 000**	**2 308 211**	**5 481 849**	**5 344 043**		**13 634 102**

31 Dec 2017	Less than 1 year	More than 1 year	Total
Off-balance-sheet commitments*	3		3
Total off-balance-sheet commitments	**3**		**3**

* Binding loan commitments

NOTE 38. Funding risk

Centralised funding forms OP Mortgage Bank's most significant source of funding risk. OP Financial Group's liquidity management has been centralised within OP Corporate Bank which is OP Mortgage Bank can also exploit OP Financial Group's liquidity buffer.

NOTE 39. Maturity of financial assets and liabilities by due date or repricing, TEUR

Contractual repricing dates or earlier due dates on 31 December 2018.

31 Dec 2018	1 month or less	> 1–3 months	> 3–12 months	> 1–2 years	> 2–5 years	More than 5 years	Total
Financial assets							
Receivables from credit institutions	133 460	4 127 088	1 945 639	147 592	199 650	356 200	6 909 630
Receivables from customers	1 495 301	1 753 545	3 727 604	3 884	7 395	7 143	6 994 873
Total financial assets	**1 628 762**	**5 880 633**	**5 673 243**	**151 476**	**207 045**	**363 343**	**13 904 502**
Financial liabilities							
Liabilities to credit institutions	1 730 000	1 166 000					2 896 000
Debt securities issued to the public		0	1 138 893	1 268 286	4 238 252	4 097 409	10 742 840
Total financial liabilities	**1 730 000**	**1 166 000**	**1 138 893**	**1 268 286**	**4 238 252**	**4 097 409**	**13 638 840**

31 Dec 2017	1 month or less	> 1–3 months	> 3–12 months	> 1–2 years	> 2–5 years	More than 5 years	Total
Financial assets							
Receivables from credit institutions	363 609	2 452 088	1 657 139		147 592	519 350	5 139 778
Receivables from customers	1 932 669	2 241 870	4 604 531	4 175	11 649	8 927	8 803 822
Total financial assets	**2 296 278**	**4 693 957**	**6 261 671**	**4 175**	**159 241**	**528 277**	**13 943 600**
Financial liabilities							
Liabilities to credit institutions	2 380 000	458 000					2 838 000
Debt securities issued to the public		100 000	1 095 957	998 188	3 261 271	5 340 686	10 796 102
Total financial liabilities	**2 380 000**	**558 000**	**1 095 957**	**998 188**	**3 261 271**	**5 340 686**	**13 634 102**

NOTE 40. Interest rate risk

At OP Mortgage Bank, the interest rate risk indicator applied is a key figure in which the effect of a 1 pp increase in the interest rate on the present value of interest rate exposure excluding customer margin is compared with the Bank's capital base. At the end of the year, the value of the key figure was -0.13%. The interest rate risk may be considered low.

Sensitivity analysis for interest rate risk

			Impact on equity	
TEUR	Risk parameter	Change	31 Dec 2018	31 Dec 2017
Interest rate risk	Interest rate	1 pp	-505,6	-1.349.8

NOTE 41. Real estate risk

OP Mortgage Bank does not possess any properties, or shares or interests in housing or real estate companies as a result of unpaid receivables.

SIGNATURES TO THE FINANCIAL STATEMENTS AND ANNUAL REPORT

Helsinki, 5 February 2019

Vesa Aho Chairman	Elina Ronkanen-Minogue	Hanno Hirvinen

Lauri Iloniemi
Managing Director

AUDITOR'S NOTE

We have today issued an auditors' report on the performed audit.

Helsinki, 13 February 2019

KPMG Oy Ab
Authorised Public Accountants

Raija-Leena Hankonen
Authorised Public Accountant

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This document is an English translation of the Finnish auditor's report. Only the Finnish version of the report is legally binding.

Auditor's Report

To the Annual General Meeting of OP Mortgage Bank Plc

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of OP Mortgage Bank Plc (business identity code 1614329-2) for the year ended 31 December, 2018. The financial statements comprise the balance sheet, income statement, statement of comprehensive income, statement of changes in equity, statement of cash flows and notes, including a summary of significant accounting policies.

In our opinion the financial statements give a true and fair view of the bank's financial performance and financial position in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and comply with statutory requirements.

Our opinion is consistent with the additional report submitted to the Board of Directors.

Basis for Opinion

We conducted our audit in accordance with good auditing practice in Finland. Our responsibilities under good auditing practice are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

We are independent of the parent company and of the group companies in accordance with the ethical requirements that are applicable in Finland and are relevant to our audit, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To our best knowledge and understanding, the non-audit services that we have provided to the parent company and group companies are in compliance with laws and regulations applicable in Finland regarding these services, and we have not provided any prohibited non-audit services referred to in Article 5(1) of Regulation (EU) 537/2014. The non-audit services that we have provided have been disclosed in note 7 to the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Materiality

The scope of our audit was influenced by our application of materiality. The materiality is determined based on our professional judgement and is used to determine the nature, timing and extent of our audit procedures and to evaluate the effect of identified misstatements on the financial statements as a whole. The level of materiality we set is based on our assessment of the magnitude of misstatements that, individually or in aggregate, could reasonably be expected to have influence on the economic decisions of the users of the financial statements. We have also taken into account misstatements and/or possible misstatements that in our opinion are material for qualitative reasons for the users of the financial statements.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. The significant risks of material misstatement referred to in the EU Regulation No 537/2014 point (c) of Article 10(2) are included in the description of key audit matters below.

We have also addressed the risk of management override of internal controls. This includes consideration of whether there was evidence of management bias that represented a risk of material misstatement due to fraud.

THE KEY AUDIT MATTER	HOW THE MATTER WAS ADDRESSED IN THE AUDIT
Receivables from customers and receivables from credit institutions (accounting policies, notes 8, 10, 12, 32 and 34 to financial statements)	
— Receivables from customers, €7.0 billion, and receivables from credit institutions, €6.9 billion are significant items on the OP Mortgage Bank's balance sheet comprising 99% of the total assets. Receivables from customers are mortgage-backed loans purchased from OP Financial Group's member banks and receivables from credit institutions are mainly intermediary loans issued to OP Financial Group's member banks. — OP Mortgage Bank adopted the IFRS 9 Financial instruments standard on 1 January 2018. The adoption resulted in a shift from calculating impairments on an individual and collective basis to the expected credit loss models set out in IFRS 9. — The calculation of expected credit losses involves assumptions, estimates and management judgements for example in respect to the probability and amount of the expected credit losses as well as determining significant increases in credit risk. — Due to the significance of the carrying amount involved, adoption of IFRS 9 standard, complexity of the accounting methods and management judgement involved, receivables from customers are addressed as a key audit matter.	— We evaluated the compliance with the internal instructions in respect of purchased loans from OP Financial Group's member banks and intermediary loans issued to OP Financial Group's member banks. We assessed the key controls and IT systems relevant to receivables from customers and receivables from credit institutions. — We evaluated the appropriateness of expected credit loss models by using OP Financial Group's centralised audit process. — Furthermore, we considered the appropriateness of the notes provided by OP Mortgage Bank in respect of receivables and expected credit losses.

Responsibilities of the Board of Directors and the Managing Director for the Financial Statements

The Board of Directors and the Managing Director are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, and of financial statements that give a true and fair view in accordance with the laws and regulations governing the preparation of financial statements in Finland and comply with statutory requirements. The Board of Directors and the Managing Director are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Board of Directors and the Managing Director are responsible for assessing the parent company's and the group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting. The financial statements are prepared using the going concern basis of accounting unless there is an intention to liquidate the parent company or the group or cease operations, or there is no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with good auditing practice will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with good auditing practice, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the parent company's or the group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the Board of Directors' and the Managing Director's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the parent company's or the group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the parent company or the group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events so that the financial statements give a true and fair view.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Other Reporting Requirements

Information on our audit engagement

We were first appointed as auditors by the Annual General Meeting in 2002 and our appointment represents a total period of uninterrupted engagement of 17 years.

Other Information

The Board of Directors and the Managing Director are responsible for the other information. The other information comprises the report of the Board of Directors. Our opinion on the financial statements does not cover the other information.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. Our responsibility also includes considering whether the report of the Board of Directors has been prepared in accordance with the applicable laws and regulations.

In our opinion, the information in the report of the Board of Directors is consistent with the information in the financial statements and the report of the Board of Directors has been prepared in accordance with the applicable laws and regulations.

If, based on the work we have performed, we conclude that there is a material misstatement of the report of the Board of Directors, we are required to report that fact. We have nothing to report in this regard.

Helsinki, 13 February 2019

KPMG OY AB

RAIJA-LEENA HANKONEN
Authorised Public Accountant, KHT