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# **PARETO BANK**

## **Financial Results**

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**Fourth Quarter 2017**

**Pareto bank**  
Projektbanken

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# 2017 HIGHLIGHTS

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- 1 Record profit after tax of NOK 312.6m (NOK 247.3m for 2016).
- 2 Lending growth on high margins, cost efficiency and low write-downs and losses.
- 3 Targeted net lending growth of NOK 1,000m was reached by the end of Q3-17 due to attractive business opportunities within real estate financing and corporate financing.
- 4 In order to exploit a profitable deal flow and continue to serve customers, loans amounting to NOK 629m were syndicated (*avlastet*) in Q4-17.
- 5 Net lending growth of NOK 694m in 2017. Adjusted lending growth of NOK 1,323m (NOK 694m + NOK 629m in syndicated loans).
- 6 CET1 ratio of 17.7 % versus a minimum requirement of 15.2 %.
- 7 Proposed dividend per share of NOK 1.60. Delivering on dividend policy.

# ON TARGET IN 2017

	31.12.2017 STATUS	31.12.2017 TARGET	
LENDING GROWTH	NOK 694m	~NOK 1,000m	High growth within residential property development. Sales activity within corporate financing materializes in growth.
ROE	15.9 %	> 13.0 % *	Lending growth on high margins and cost efficiency yield high returns.
CAPITAL ADEQUACY	17.7 %	15.5 % **	High earnings and balance sheet management ensure solidity.
DIVIDEND POLICY	30 %	30-50 %	The payout ratio depends on the growth potential within the bank's markets.

Note(\*): Profit after tax excluding additional tier 1 interest costs after tax divided by average common equity tier 1 capital including retained earnings for the period

Note(\*\*): The minimum CET1 ratio requirement after receiving a pillar 2 requirement of 3.2 % from the NFSA is 15.2%. The CET1 target of 15.5% as of 31.12.2017 is revised up to 15.7 % as of 31.12.2018.

See page 14.

# STATUS PORTFOLIO GOALS 2017

BUSINESS AREAS	STATUS	ACTUAL 2017	TARGETS 2017
<b>Real estate</b> 	Entering 2018 with strong deal flow, but possible slowdown in residential property development going forward.	NOK 939m	NOK 600m
<b>Securities &amp; Corporates</b> 	Increasing deal flow in corporate financing. Limited competition.	Securities: - NOK 305m Corporates: NOK 388m	Securities: - NOK 300m Corporates: NOK 500m
<b>Shipping &amp; offshore</b> 	Positioned to take advantage of recovering shipping markets.	- NOK 268m	NOK 200m

# OVERVIEW PORTFOLIO COMPOSITION

## MAIN BUSINESS AREAS

### Real estate

*Real estate financing focused on residential property construction in the greater Oslo region*

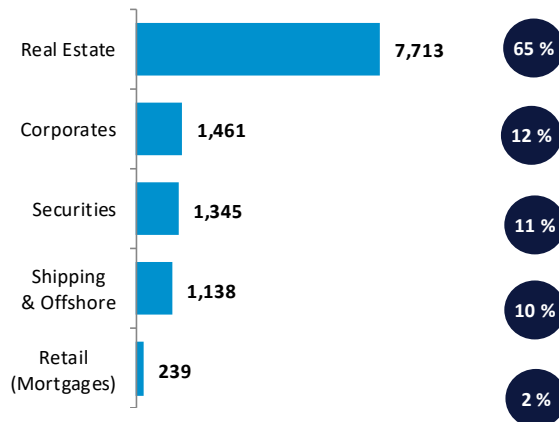
### Securities & Corporates

*A full scale provider of securities & corporate financing including investment services*

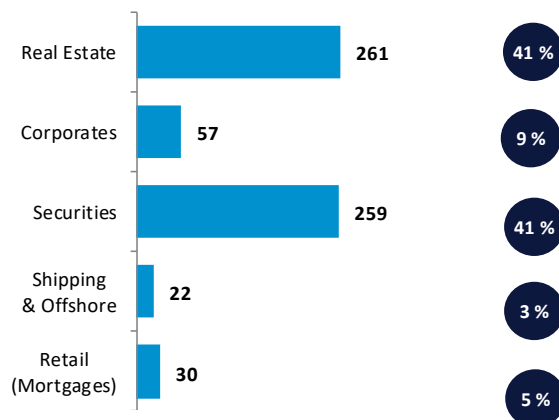
### Shipping & Offshore

*Focus on Norwegian clients, high quality charterers and liquid tonnage*

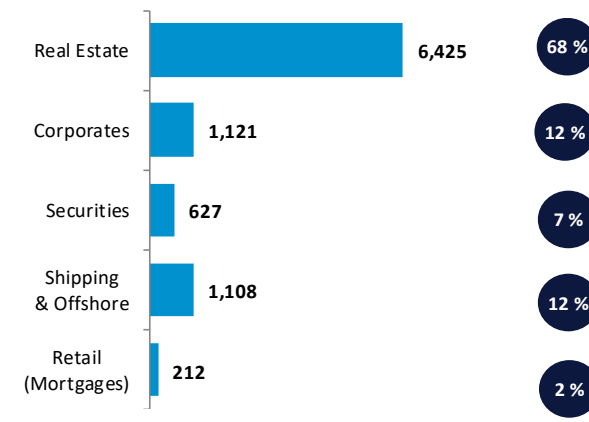
## Gross credit exposure (NOKm) $\Sigma = \text{NOK } 11,850\text{m}$



## Number of active clients $\Sigma = \# 629$

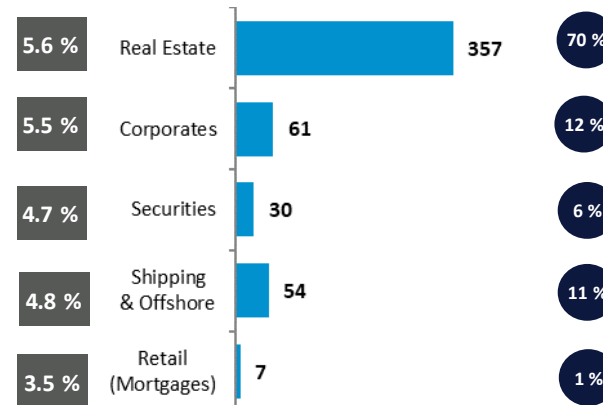


## Gross total lending (NOKm) $\Sigma = \text{NOK } 9,448\text{m}$



## Interest contribution (NOKm) \* $\Sigma = \text{NOK } 509\text{m}$

Margin over interbank rate \*\*



# PARETO BANK ADAPTS TO A MORE DIFFICULT RESIDENTIAL PROPERTY DEVELOPMENT MARKET

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- ✓ Focus on a high level of presale, adequate liquidity buffers and 20 % to 40 % equity contribution.
- ✓ Presale requirement: if the price of unsold units falls by 50 % compared to the price of presold units, the sales amount must still be sufficient to cover the bank credit.
- ✓ Presale quality: end-users are assessed and qualified.
- ✓ Restrictive attitude towards financing of projects with long-term exits.
- ✓ Approximately 50 % of the financed property lots are with rental income as they are utilized for residential purposes.
- ✓ Approximately 50 % of project exposure is in the small house segment (94 out of 150 projects).
- ✓ A high natural turnover rate on loans is in general risk mitigating.

# INCOME STATEMENT

## P&L (NOKm)

	Q4-17	Q4-16	2017	2016
Net Interest income	128.3	117.3	507.0	415.9
Total other operating income	2.1	9.0	32.0	42.0
<b>Total net income</b>	<b>130.3</b>	<b>126.4</b>	<b>539.0</b>	<b>457.9</b>
<b>Total other operating expenses</b>	<b>33.5</b>	<b>26.4</b>	<b>112.6</b>	<b>98.8</b>
Operating result before losses / write-downs	96.8	100.0	426.4	359.1
Losses / write-downs on loans	1.0	11.8	11.4	30.7
<b>Operating result before tax</b>	<b>95.9</b>	<b>88.1</b>	<b>415.0</b>	<b>328.5</b>
Tax payable	22.6	21.1	102.4	81.2
<b>Result after tax</b>	<b>73.3</b>	<b>67.1</b>	<b>312.6</b>	<b>247.3</b>
<i>Earnings per share (NOK)</i>	<i>1.24</i>	<i>1.11</i>	<i>5.28</i>	<i>4.08</i>
<i>Return on equity</i>	<i>14.3%</i>	<i>15.3%</i>	<i>15.9%</i>	<i>15.9%</i>
<i>Cost income ratio</i>	<i>25.7%</i>	<i>20.9%</i>	<i>20.9%</i>	<i>21.6%</i>

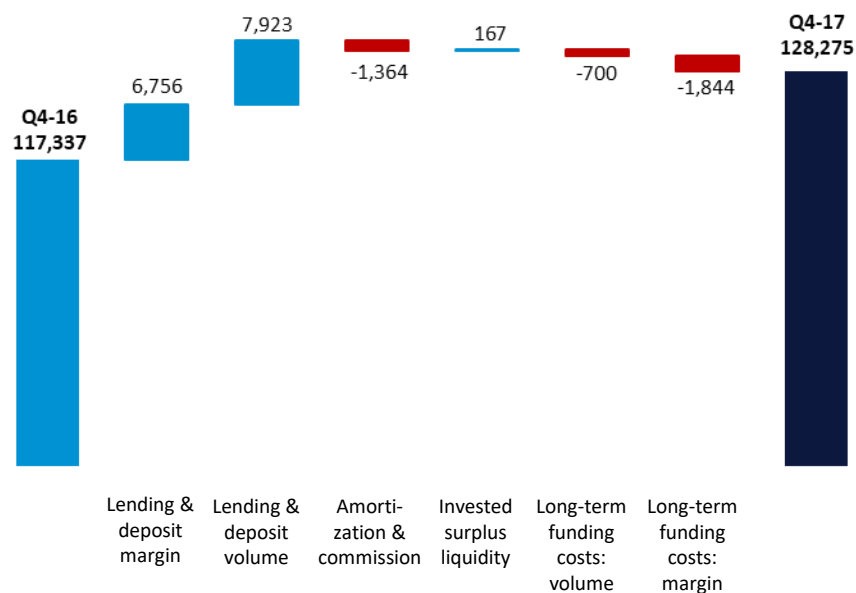
## Key comments

- Lending growth on a net interest margin of 5.5 %.
- Due to a strong deal flow within residential property development, loans amounting to NOK 629m were syndicated (*avlastet*) in Q4-17.
- NOK 8.4m (NOK 5.5m) was allocated to profit sharing in Q4-17. Allocated to profit sharing for 2017 NOK 19.7m (NOK 16.2m).
- No additional individual write-downs or group provisions in Q4-17, except costs relating to currency fluctuations of NOK 1.0m (NOK 11.8m). Write-downs and losses for 2017 amounted to NOK 11.4m (NOK 30.7m).



# GROWING NET INTEREST INCOME

## Net interest income (NOK 1,000)

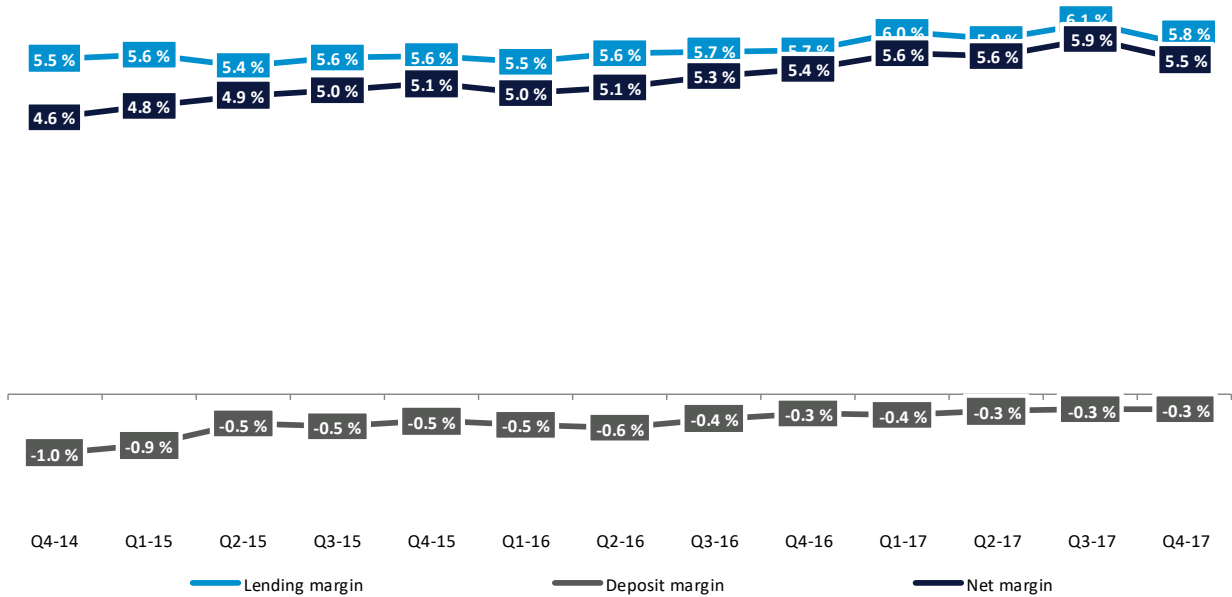


## Key comments

- Increased net interest income due to a combination of higher lending volumes and margins in the course of 2017
- Reduced deposit rates and improved market funding rates contributed to better net margins
- Net interest margin improved by 0.16 percentage points, mainly driven by lending margins

# STRONG MARGINS

Continuously improving net interest margins (vs. 3M NIBOR) \*



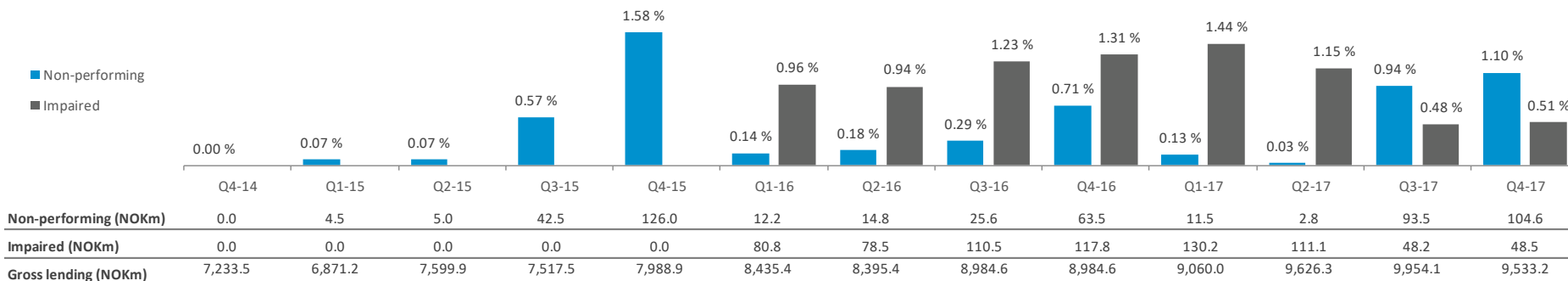
## Key comments

- The bank maintains margins on lending
- Fee income driven by real estate financing
- Fee income was particularly high in Q3-17
- Improved margin on deposits maintained in Q4-17
- Net interest margin for 2017 as a whole was 5.66 %

# LOAN PORTFOLIO QUALITY

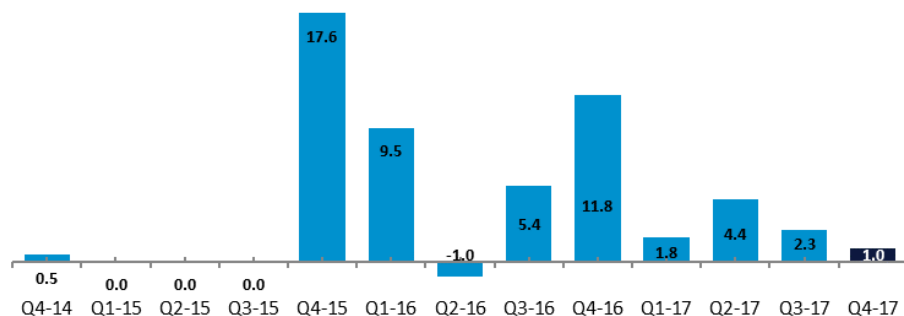
## Net non-performing and impaired loans \*

% of gross lending



## Individual losses, write-downs and reversals on loans & guarantees

Nominal (NOKm)

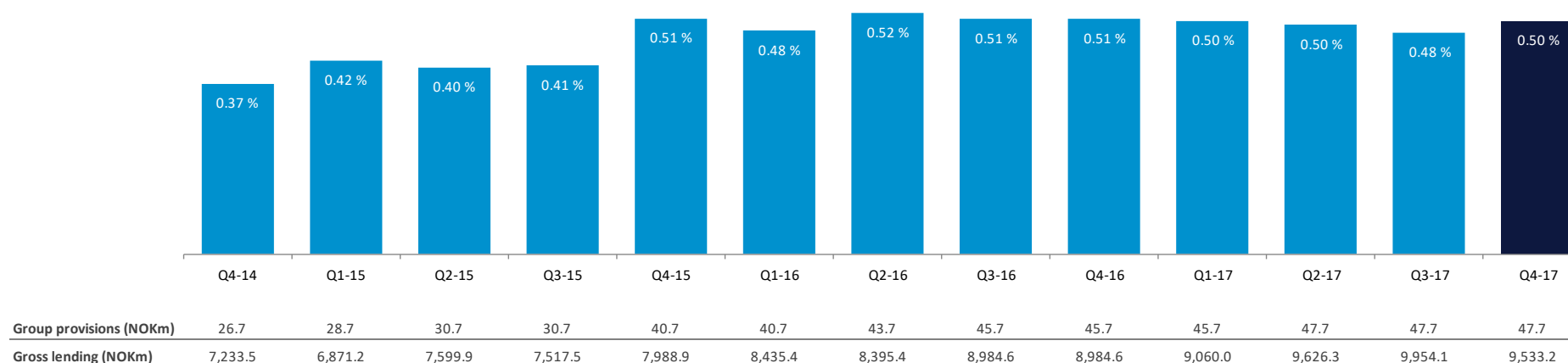


- Non-performing loans of NOK 104.6m consists mainly of three loans in real estate which are considered not impaired
- Two shipping & offshore loans of net NOK 82.2m are impaired by the end of Q4-17
- These two loans are performing and they have been written down with in total NOK 33.8m
- Write-downs of NOK 1.0m in Q4-17 are related to currency fluctuations

# GROUP PROVISIONS

## Cumulative group provisions

% of gross lending

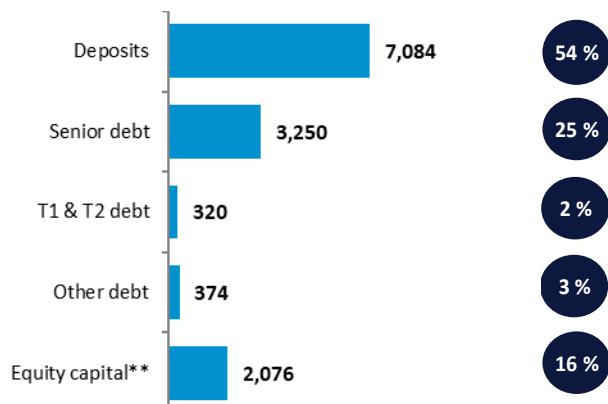


- Group provisions were unchanged in Q4-17 at NOK 47.7m or 0.5 % of gross lending
- Group provisions are based on uncertainty in housing prices in Oslo and ship values within certain segments
- Based on the bank's stress test of its property development portfolio, there is no need to increase group provisions despite the fall in housing prices
- The bank will make loss provisions under IFRS 9 as of 01.01.2018. Provisions as of 31.12.2017 do not materially differ from provisioning under IAS 39.

# FUNDING | OVERVIEW

## Sources (NOKm)

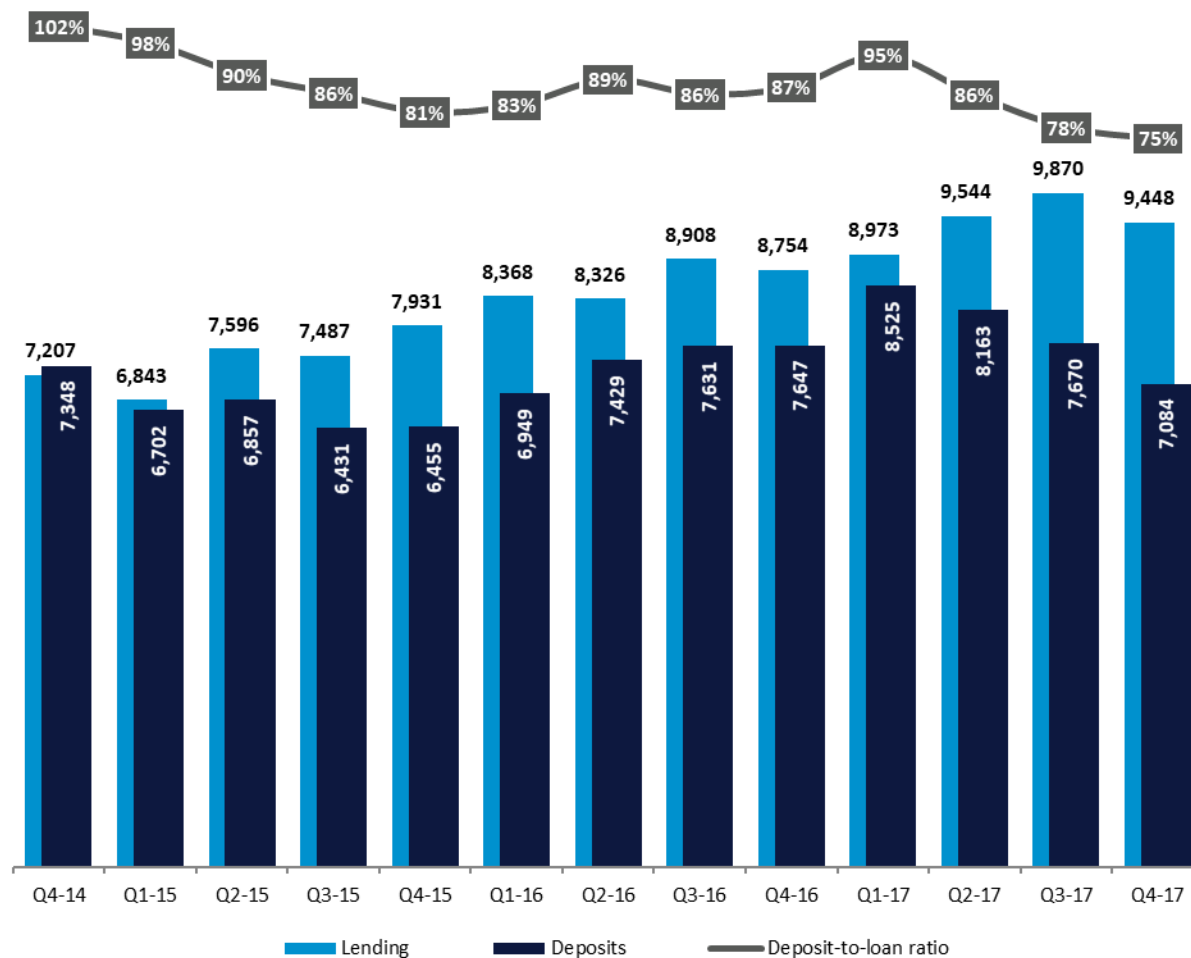
Σ = NOK 13,104m



## Key ratios

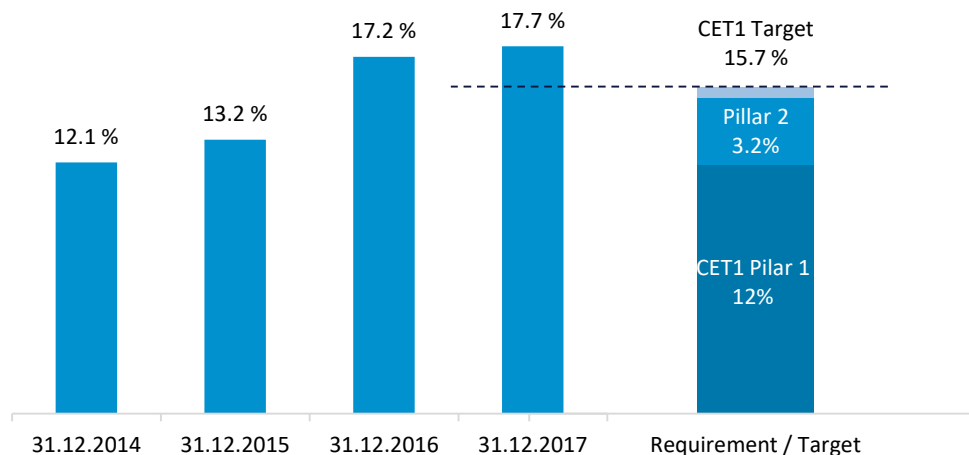
Deposits with liquidity restrictions	41 %
Corporate deposits	71 %
Deposit-to-loan ratio	75 %
Long-term NFSA liquidity ratio	127 %
LCR	135 %

## Historical development in deposits vs. lending (NOKm)

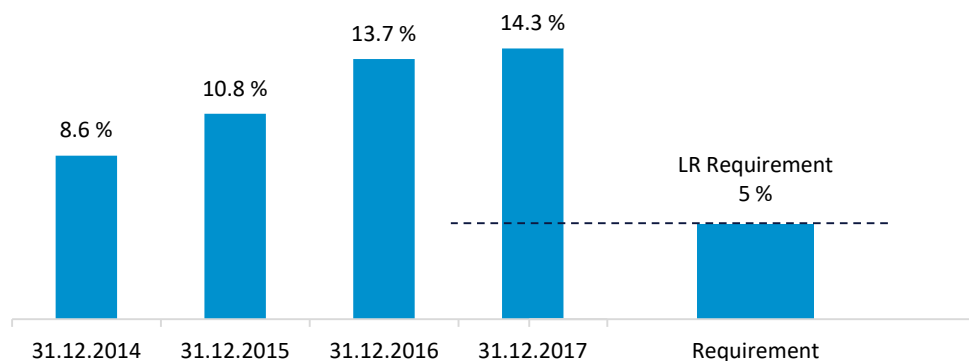


# CAPITAL REQUIREMENTS

## Core equity tier 1 ratio (CET1 ratio)



## Leverage ratio



## Key comments on capital

- The NFSA has given the bank a pillar 2 requirement of 3.2 % of risk weighted assets.
- The bank's minimum CET1 ratio requirement is 15.2 % as of 31.12.2017.
- The board has set a new CET1 ratio target of 15.7 % as of 31.12.2018.
- The bank has the ability to manage its balance sheet to meet capital targets.
- The bank has a strong leverage ratio.




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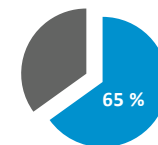
**2 BUSINESS AREAS**

**3 AMBITIONS FOR 2018**

# NORWAY'S LEADING PROJECT BANK

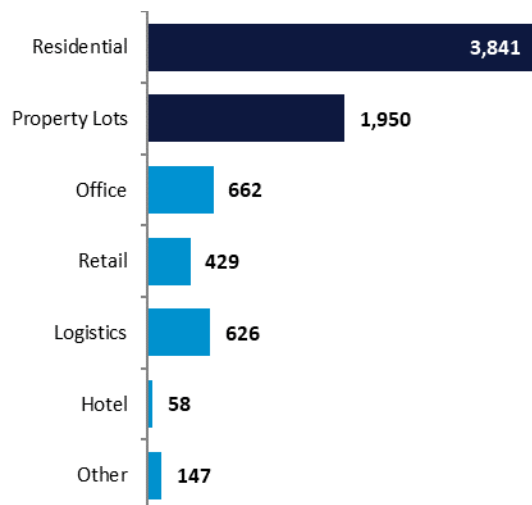
BUSINESS AREAS	PROJECTS / CREDITS	AREA EXPOSURE	AVG. PRINCIPAL
<b>Real estate</b> 	Property lot financing Building construction facilities Commercial property financing	<b>65 %</b>	<b>NOKm 30</b>
<b>Corporate &amp; Securities</b> 	M&A loans Bridge loans Investment loans Securities financing	<b>24 %</b>	<b>NOKm 5-30</b>
<b>Shipping &amp; Offshore</b> 	Ship owners Family offices Shipping and offshore projects	<b>10 %</b>	<b>USDm 5-10</b>





## Real estate credit exposure (NOKm)

Σ = NOK 7,713m

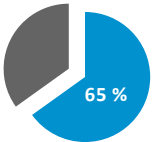


Residential  
property  
development  
NOK 5,791m  
75 %

Commercial  
property  
NOK 1,922m  
25 %

## Description of real estate credit exposure

- A split between financing of residential property development (75 %) and commercial property (25 %)
- A large majority of the property development projects are construction of small houses (*småhus*)
- Financing of regulated property lots purchased for development with a clear exit strategy
- Approximately 50 % of the financed property lots are with rental income as they are utilized for residential purposes
- Financing of renovation and conversion projects
- Financing of commercial property such as office, retail, and logistics

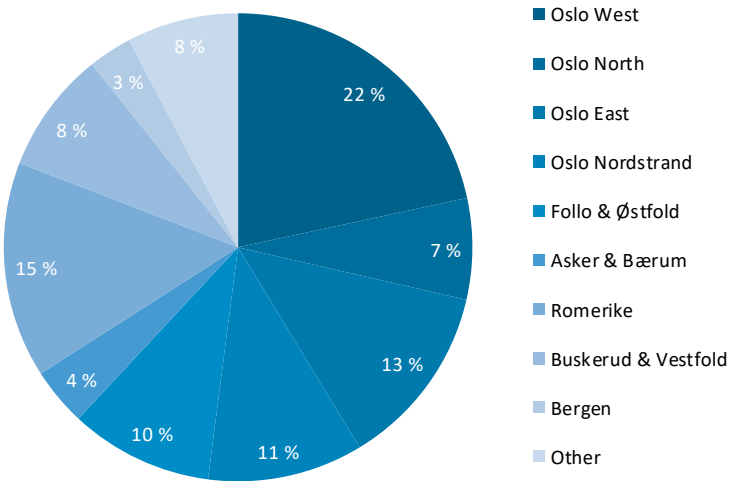


## A diversified portfolio

- The residential property exposure is diversified by geographic area, project type and size
- The portfolio is made up of 150 different addresses with an average project size of NOK 41m
- 94 projects are construction of small houses (*småhus*), while the rest are apartment projects. Exposure to small house projects amounts to approximately 50 %
- Apartments vary from large, exclusive units to smaller units.
- Approximately 35 % of the projects have presold all units, exposing the bank to little or no market risk
- The residential property development portfolio is stress tested semi-annually by simulating a drop in housing prices
- The portfolio performs well in a theoretical stress test, but a scenario with a substantial drop in prices and a complete shutdown of the new-build market will have a negative effect on profits and volumes
- In the case of a distressed project, focus will be on completing the project and selling remaining units. The potential loss is normally limited due to the high presale requirement

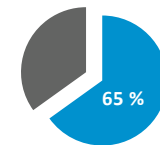
## Geographical residential property exposure (NOKm)

Σ = NOK 5,791m



Largest areas:

Oslo	52 %
Akershus & Østfold	29 %
Buskerud & Vestfold	8 %



## Market observations

- A differentiated market in Oslo: demand for small apartments (50 square meters or less) is low due to regulation (*boliglånsforskriften*) and high supply
- Continued demand for small houses (*småhus*) is supporting the level of sales and prices
- Variation between regions: prices are still falling in Oslo, while prices in surrounding regions are more stable

## Strategy

- On average 20 % to 40 % equity to finance a property lot purchase
- Primarily financing of regulated lots in Oslo and other well functioning liquid markets purchased for development with a clear exit strategy
- Restrictive attitude towards financing of projects with long-term exits
- Market risk is reduced by requiring a high level of presale
- Presale requirement: if the price of unsold units falls by 50 % compared to presold units, the sales amount must still be sufficient to cover the bank credit
- Presale quality: end-users are assessed and qualified
- Primarily turnkey projects to minimise cost overruns
- External third-party professional building inspectors follow up projects on a monthly basis on behalf of the bank



# CORPORATES | INCREASING DEAL FLOW



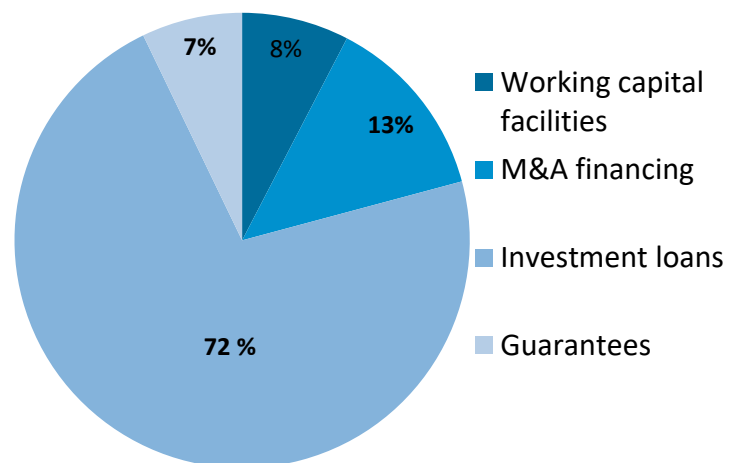
## Status

Total exposure of NOK 1,461m within a variety of industries. 57 customers with credit facilities in the range of NOK 0.2m to NOK 150m.

Total exposure increased by NOK 482m in 2017.

Investment loans comprise 72 % of total exposure.

More M&A financing is expected going forward.



## Products

### INVESTMENT LOANS

Financing of investments for a client who backs the investment with a financially solid parent company.

### WORKING CAPITAL FACILITIES

Normally given in combination with other loans. Client pays a commitment fee for access to a credit line that can be drawn to meet short-term borrowing needs.

### M&A FINANCING

Traditional M&A and LBO financing to Norwegian small and medium-sized enterprises (SME's).

### BRIDGE LOANS

Bridging of liquidity for clients who have both bought and sold assets, but not timed the cash flow. Short term financing until a more permanent funding source is in place.

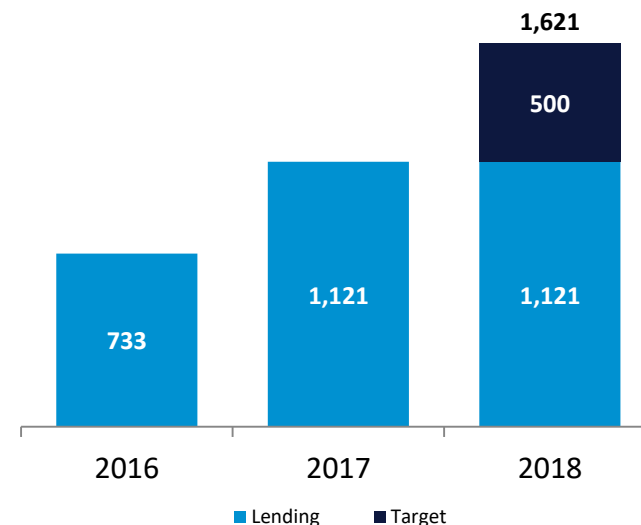


## Market observations

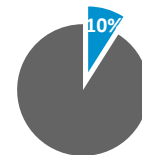
- Limited competition within corporate financing for small and medium-sized Norwegian enterprises (SMEs)
- The larger banks allocate capital to private customers, large corporates and large transactions, and the bond market is no real alternative for SME's as the amounts are too small
- Transactions are often too large or complex for local savings banks

## Strategy

- Focus on SME's with revenue between NOK 20m to NOK 500m
- Main focus on corporate transactions (M&A, MBO, LBO)
- No specific sector or industry criteria, but focus on business model, corporate governance, management and financials
- Thorough fundamental credit analyses of all companies
- A conservative approach to leverage and strict financial covenants
- Tenor varies depending on product. Within M&A financing an average tenor of 3 to 5 years
- Investment loans cover a wide range of uses and are tailored to fit client needs
- Commitment size from NOK 20 to 100m



# SHIPPING & OFFSHORE | DIVERSIFIED PORTFOLIO

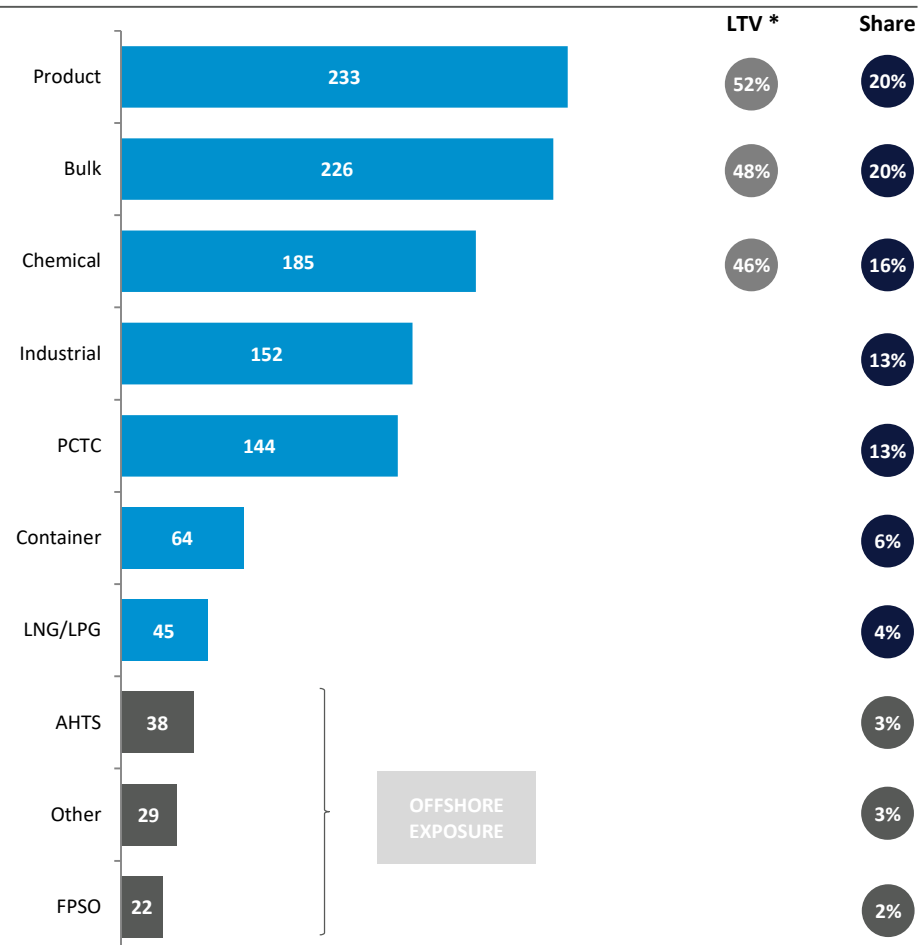


## Status

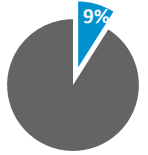
- A diversified portfolio where a single segment will normally not exceed 25% of the total S&O exposure
- 22 customers and a total of 34 vessels
- Largest exposure is USD 14.6m and average commitment size is USD 6.5m
- Only 2 commitments towards the offshore sector equalling approximately 0.5 % of total credit exposure

## Total S&O credit exposure & Loan to value (NOKm) \*

Σ = NOK 1,138m



# SHIPPING & OFFSHORE | MARKET AND STRATEGY



## Market observations

- Few banks are currently supporting clients and offering financing in Pareto Bank's targeted loan size segment. Right time to increase profitability.
- Several shipping markets look promising.
- Growth ambition in 2018 is subject to attractive opportunities

## Strategy

- Focus on Norwegian ship owners, majority shareholders and family offices
- Focus on profitability, owners with strong balance sheets and counterparty risk
- Target LTV of 50 %
- Tight covenant setting with respect to minimum value clauses and working capital
- Higher loan amounts on average to fund modern tonnage and multiple vessels
- Diversification between S&O segments where none will exceed 25 % of the portfolio
- Maximum S&O credit exposure is 15 % of the bank's total credit exposure
- Strategy to be revised annually to reflect market development and ensure a dynamic risk management



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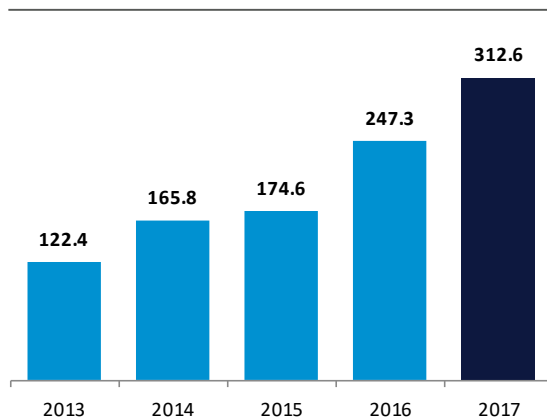
**2 BUSINESS AREAS**

**3 AMBITIONS FOR 2018**

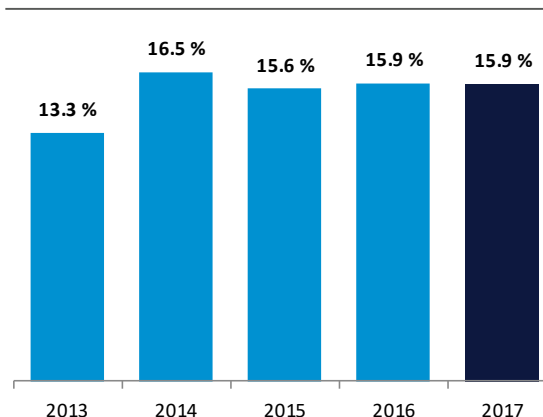


# SOLID FOUNDATION AND STRONG PERFORMANCE

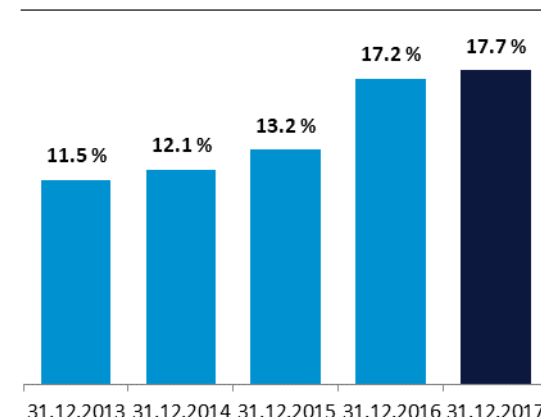
Result after tax (NOKm)



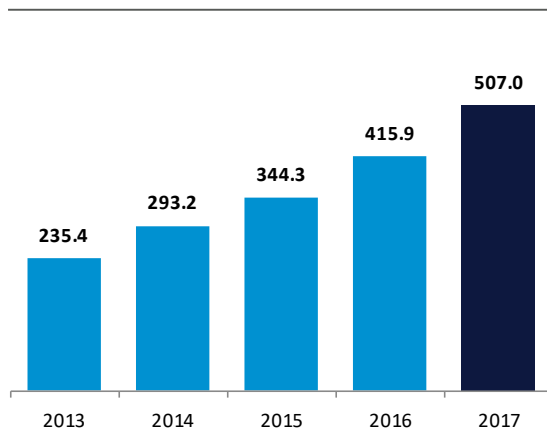
Return on Equity \*



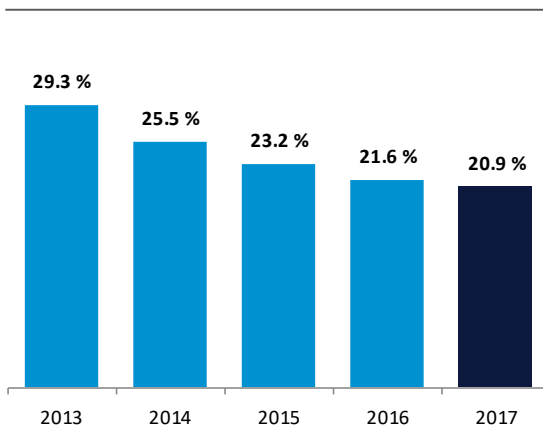
CET1 ratio \*\*



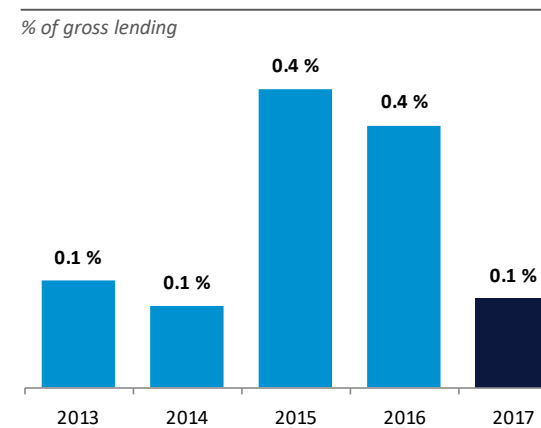
Net interest income (NOKm)



Cost/income ratio



Loss ratio \*\*\*



% of gross lending

# FINANCIAL TARGETS 2018

NET LENDING GROWTH	<b>~NOK 700m</b>	Profitable net lending growth. Growth ambition is subject to attractive market opportunities.
RETURN ON EQUITY	<b>&gt; 13.0%</b>	Cost effective and commercially oriented bank.
CAPITAL ADEQUACY	<b>15.7 %</b>	CET1 ratio target of 15.7 % versus NFSA requirement of 15.2 %.
DIVIDEND POLICY	<b>30 - 50 %</b>	The payout ratio depends on the growth potential within the bank's markets.

# APPENDIX

# LARGEST SHAREHOLDERS AS OF 02.01.2018

#	Investor	02 January 2018	
		# of shares	% total
1	Pareto AS	8,921,873	15.22 %
2	Pecunia Forvaltning AS	5,861,859	10.00 %
3	Saga Tankers ASA	5,052,547	8.62 %
4	Apollo Capital Management	4,875,998	8.32 %
5	Indigo Invest AS	4,382,711	7.48 %
6	Datum AS	1,493,996	2.55 %
7	Kolberg Motors AS	1,360,000	2.32 %
8	Verdipapirfondet Landkreditt Utbytte	1,350,000	2.30 %
9	Verdipapirfondet First Generator	1,240,907	2.12 %
10	Perestroika AS	950,413	1.62 %
11	Artel AS	900,820	1.54 %
12	Endre Røsjø	723,731	1.23 %
13	Nye Castel AS	689,779	1.18 %
14	Tycoon Industrier AS	683,317	1.17 %
15	Apollo Asset Limited C/O	675,000	1.15 %
16	Uthalden AS	612,451	1.04 %
17	Solan Capital AS	590,000	1.01 %
18	Svemorka Holding AS	500,000	0.85 %
19	Thabo Energy AS	452,486	0.77 %
20	AS Clipper	433,845	0.74 %
<b>Sum TOP 20</b>		<b>41,751,733</b>	<b>71.22 %</b>
<b>Other shareholders</b>		<b>16,867,955</b>	<b>28.78 %</b>
<b>Total</b>		<b>58,619,688</b>	<b>100 %</b>

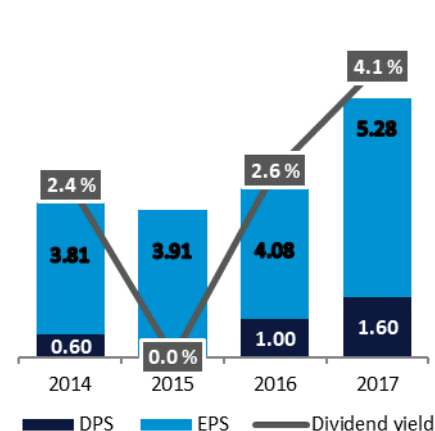
- The Company has 58,619,688 shares outstanding
- One class of shares where each share carries one voting right
- Diversified investor base with 839 shareholders
- The top 10 and 20 investors hold 60.5 % and 71.2 % of the shares respectively
- Employees in Pareto Bank own 1.8 %
- Top management in the Pareto Group owns 0.55 %
- All employees are covered by an annual bonus compensation scheme settled in Pareto Bank shares

# THE SHARE

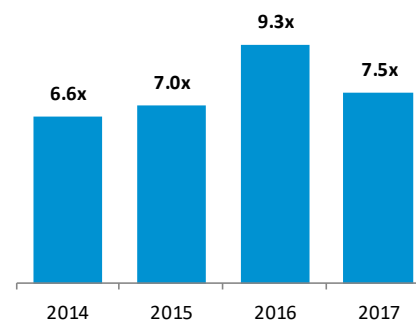
## Share price development since March 2014\*\*



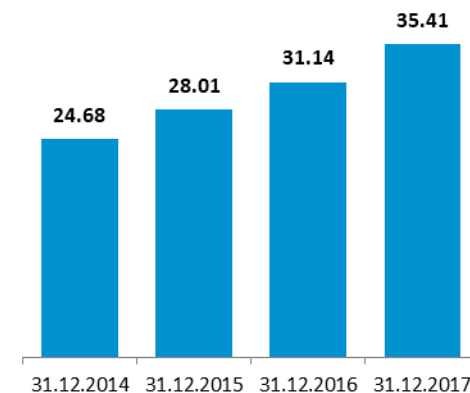
## EPS, DPS (NOK) & Dividend Yield \*



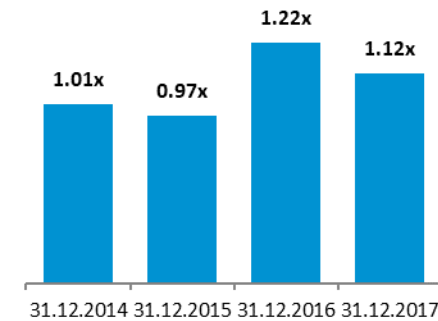
## Price / Earnings \*



## Book equity per share (NOK) \*



## Price / Book \*



# QUARTERLY INCOME STATEMENT

## P&L (NOKm)

	Q4-17	Q3-17	Q2-17	Q1-17	Q4-16
Net Interest income	128.3	138.7	124.6	115.4	117.3
Total other operating income	2.1	3.2	7.8	18.9	9.0
<b>Total net income</b>	<b>130.3</b>	<b>141.9</b>	<b>132.5</b>	<b>134.3</b>	<b>126.4</b>
<b>Total other operating expenses</b>	<b>33.5</b>	<b>24.2</b>	<b>26.8</b>	<b>28.0</b>	<b>26.4</b>
Operating result before losses / write-downs	96.8	117.7	105.6	106.2	100.0
Losses / write-downs on loans	1.0	2.3	6.4	1.8	11.8
<b>Operating result before tax</b>	<b>95.9</b>	<b>115.4</b>	<b>99.2</b>	<b>104.5</b>	<b>88.1</b>
Tax payable	22.6	29.4	24.2	26.1	21.1
<b>Result after tax</b>	<b>73.3</b>	<b>86.0</b>	<b>75.0</b>	<b>78.3</b>	<b>67.1</b>
<i>Earnings per share (NOK)</i>	<i>1.24</i>	<i>1.46</i>	<i>1.27</i>	<i>1.30</i>	<i>1.11</i>

## Key comments

- The principle of assessing financial instruments at fair value may cause profits to fluctuate between quarters
- For Q4-17 total net gains on financial instruments were NOK 0.6m (NOK 2.7m)
- Net write-downs totaling NOK 1.0m (NOK 11.8m) in Q4-17 due to currency fluctuations
- Loss provisioning under IFRS 9 does not materially differ from provisioning under IAS 39. Detailed provisions under IFRS 9 will be published in the annual report.

# QUARTERLY BALANCE SHEET

## BS (NOKm)

	Q4-17	Q3-17	Q2-17	Q1-17	Q4-16
Loans to credit institutions	357	165	350	884	804
Loans to customers	9,448	9,870	9,544	8,973	8,754
Bonds and other securities	3,174	3,331	3,309	4,094	3,315
Shareholdings in associated companies	36	42	40	40	15
Other assets	90	68	67	59	53
<b>Total assets</b>	<b>13,104</b>	<b>13,475</b>	<b>13,310</b>	<b>14,051</b>	<b>12,941</b>
Deposits	7,084	7,693	8,164	8,832	7,651
Senior securities issued	3,250	3,280	2,796	2,763	2,886
Other liabilities	374	178	112	292	149
Tier 2 subordinated securities issued	270	270	270	270	270
Additional tier 1 capital	50	50	50	50	160
Other equity	2,076	2,003	1,917	1,843	1,825
<b>Total liabilities and equity</b>	<b>13,104</b>	<b>13,475</b>	<b>13,310</b>	<b>14,051</b>	<b>12,941</b>

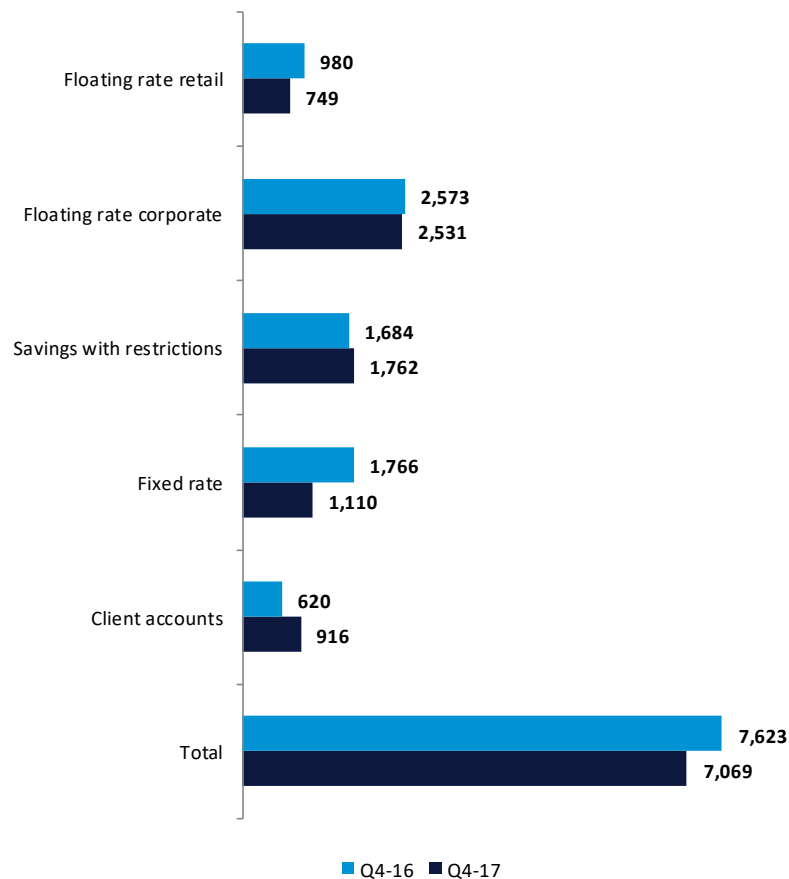
## Key comments

- Net lending fell by NOK 422m in Q4-17
- Adjusted lending growth of NOK 207m (-NOK 422m + NOK629m in syndicated (*avlastede*) loans)
- Reduction of deposits NOK 596 in Q4-17
- In the course of 2017 the bank has increased the volume of client deposits and reduced the volume of fixed-rate deposits while maintaining the level of floating rate retail and corporate deposits

# FUNDING | CUSTOMER DEPOSITS

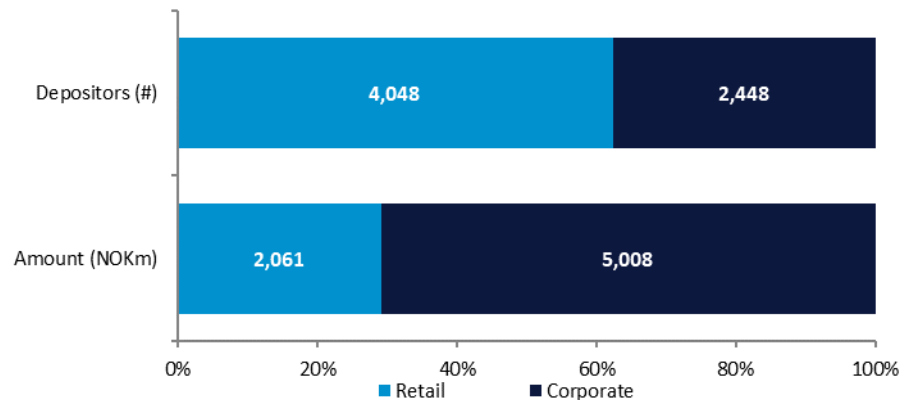
## Deposits by product

Σ = NOK 7,069m



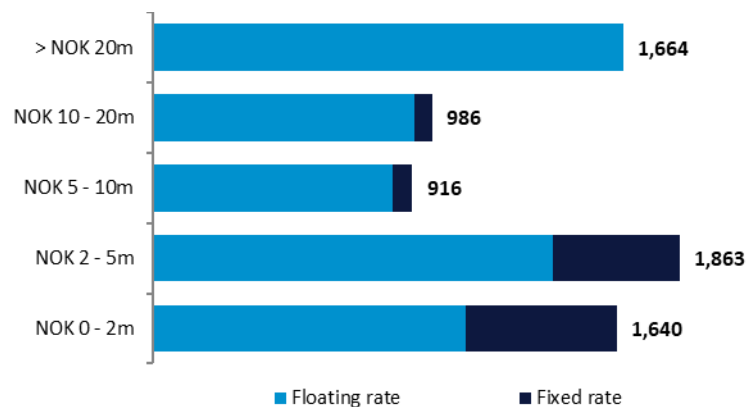
## Deposits by type

Σ = NOK 7,069m



## Deposits by size (NOKm)

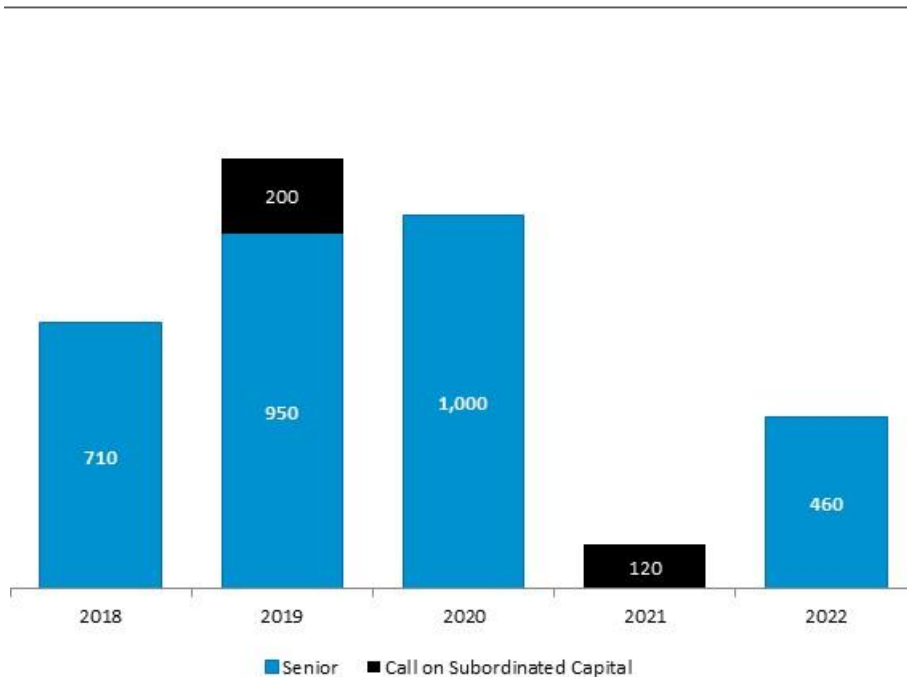
Σ = NOK 7,069m





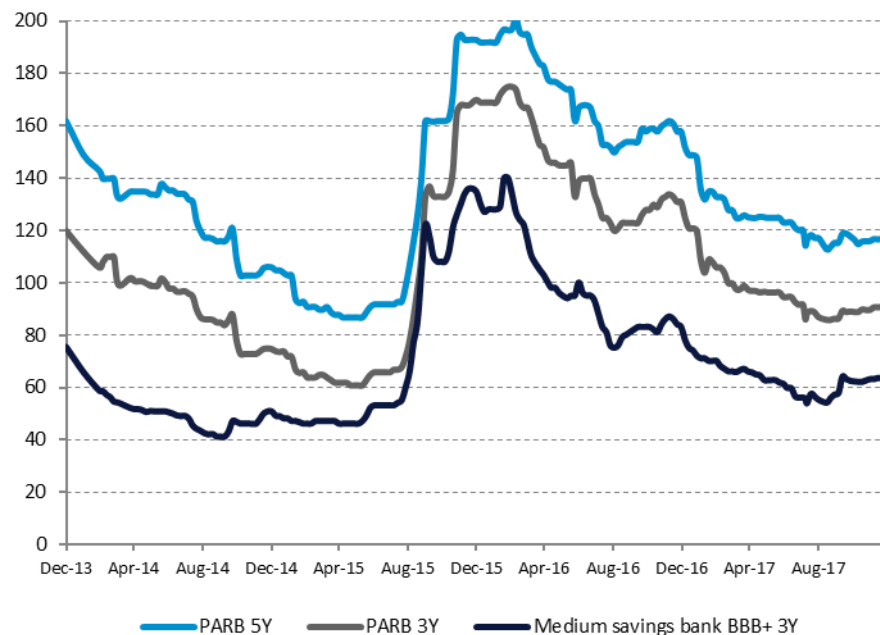
# FUNDING | MARKET FUNDING

Market funding maturities - net of own holdings (NOKm) \*



- The bank has seven loans outstanding with maturities up to five years
- The bonds are listed on Nordic ABM and the Oslo Stock Exchange

Credit spreads (bps)

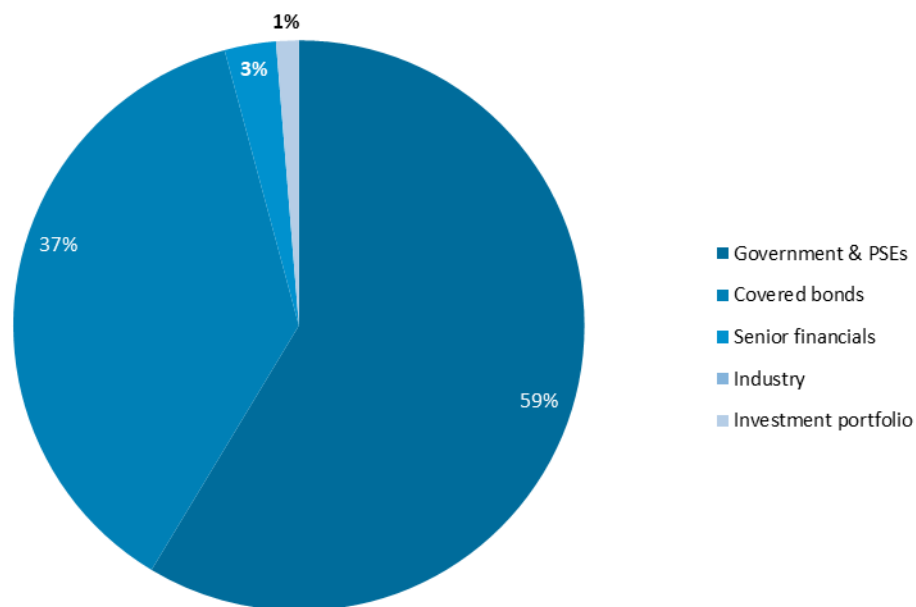


- The bank sends out target bid/offer spreads to brokers regularly
- Pareto Bank's focus is on continuously improving investor relations through transparent pricing and providing liquidity by market making

# SURPLUS LIQUIDITY

## Bond portfolio (NOKm)

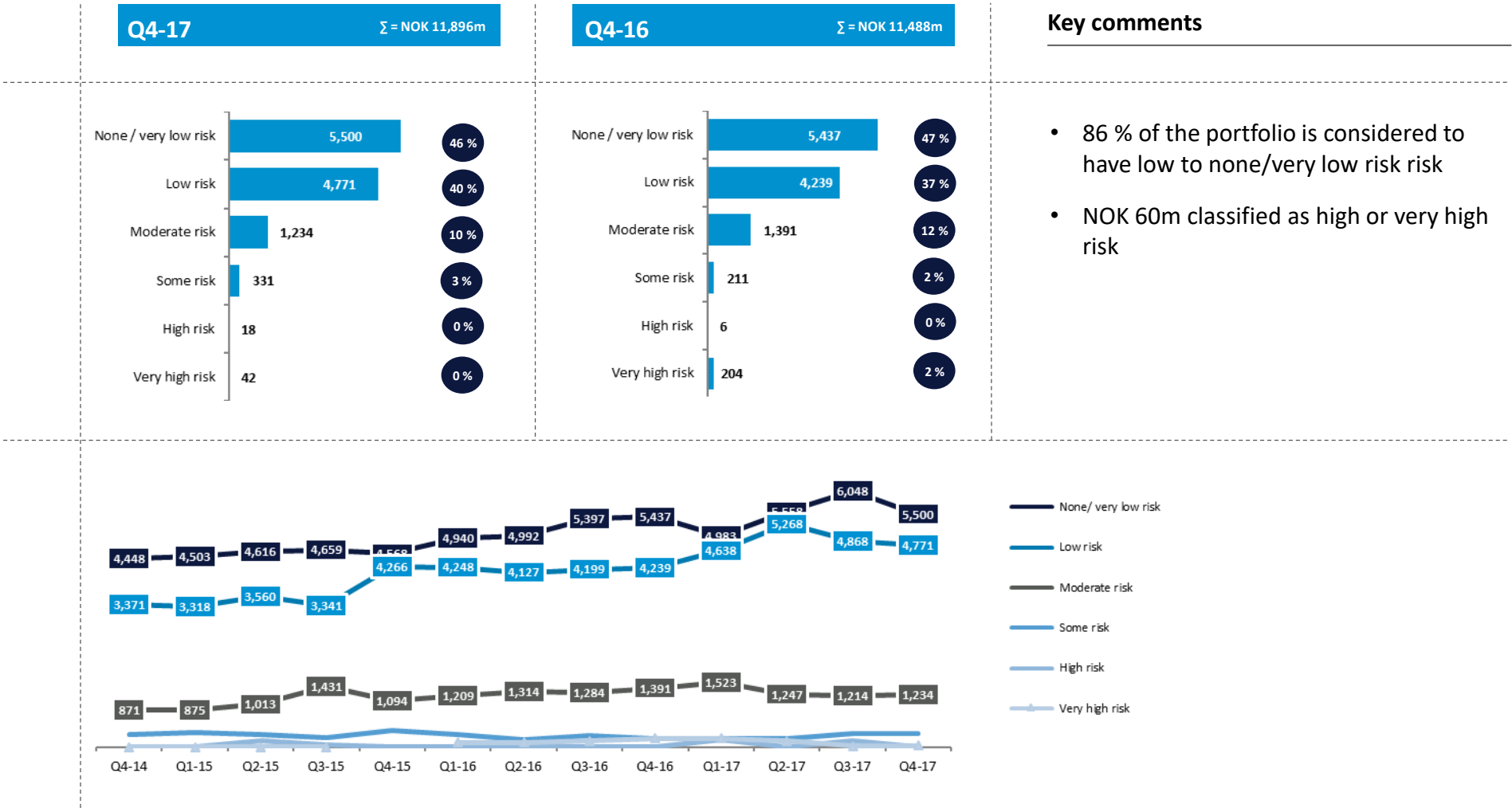
Σ = NOK 3,215m



## Key comments

- The bank's liquidity is comprised of cash and highly liquid bonds
- High share of government & PSEs to reduce credit spread risk and increase short-term liquidity
- Large share of covered bonds, mainly short to medium maturities
- The bank has shortened its duration in covered bonds and reduced its holdings in senior financials in the fourth quarter
- NOK 41m invested in high-yield bond funds in the investment portfolio (max limit NOK 500m)

# COMMITMENTS BY RISK CLASSIFICATION



4,448

4,503

4,616

4,659

4,558

4,940

4,992

5,397

5,437

4,983

5,558

6,048

5,500

4,771

4,868

5,268

4,638

4,239

4,199

4,127

4,248

4,266

3,341

3,560

3,318

3,371

871

875

1,013

1,431

1,094

1,209

1,314

1,284

1,391

1,523

1,247

1,214

1,234

None / very low risk

Low risk

Moderate risk

Some risk

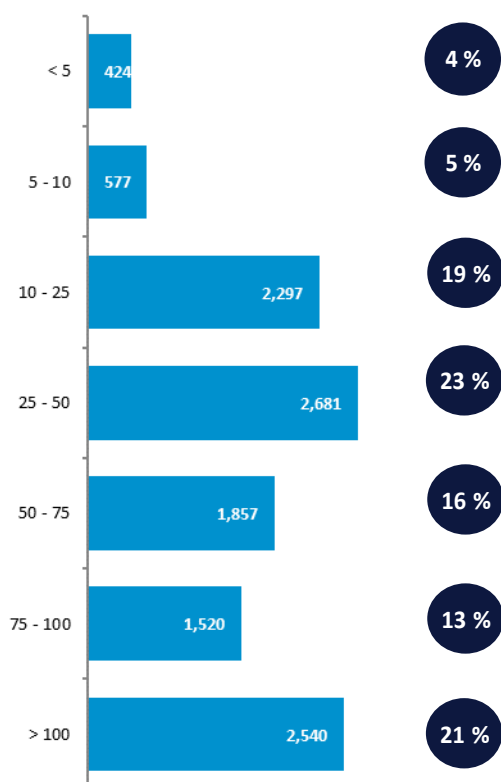
High risk

Very high risk

# COMMITMENTS BY SIZE

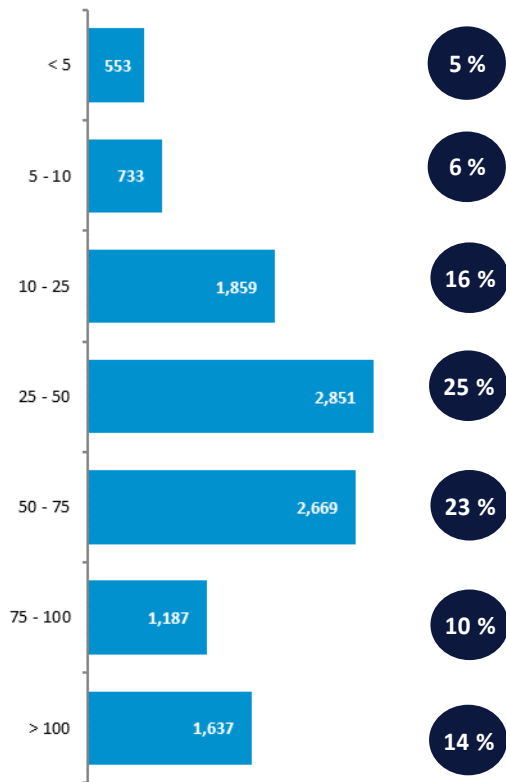
Q4-17

$\Sigma$  = NOK 11,896m



Q4-16

$\Sigma$  = NOK 11,488m



## Key comments

- A conservative policy with respect to size
- Maximum size on a single customer 10 % of total capital (NOK 227m)
- Maximum size on group / consolidated basis 15 % of total capital (NOK 340m)

 Pareto bank