FINANSTILSYNET

MEMORANDUM

Danish Financial Supervisory Authority

29 June 2010

[Translation of memorandum from the Danish FSA (Finanstilsynet). In case of discrepancies, the Danish version prevails.]

Report on inspection of Danske Bank Denmark (retail customers)

1. Introduction

In March 2010, the Danish Financial Supervisory Authority (FSA) inspected Danske Bank's retail activities in Denmark. We performed a function-based inspection, that is, an inspection of one or more selected areas. In the inspection, the FSA assessed the degree of risk within the bank's lending to retail customers and the bank's credit management in the area.

This assessment is published in accordance with the Danish Executive Order on the Duty of Banks and Mortgage Credit Institutions to Publish the Danish FSA's Assessment of the Institution.

2. Summary and risk assessment

Danske Bank's lending to retail customers in Denmark represents some 7.9 % of the Group's total lending.

We inspected 367 loan exposures in the range of DKK 200,000 to DKK 10 million. The exposures were broken down into various random samples.

For loan exposures under DKK 5 million, the bank's determination of loan impairment charges and risk categorisation are based on models. The FSA did not find grounds to stipulate that the bank make further impairment charges on loans to retail customers in Denmark. Our assessment, however, is that the bank's impairment charges fall into the low end of the range that the accounting rules allow for.

We found examples of incomplete manual registration of signs of weakness in borrowers, and that has contributed to minimising the bank's collective impairment charges. Nevertheless, we do not believe that this has such significance for the bank's total impairment charges that we have grounds for requiring a change in the bank's total charges

In some cases, the bank's own risk classification of customers was too positive. The FSA has therefore ordered the bank to improve its model for assessing the risk on retail customers so that it is better at taking account of any deterioration in the value of the loans.

During the inspection we found that, although a very large proportion of the loan portfolio had a normal level of risk, the overall credit quality was below the level for retail lending at other large banks. Due to the bank's risk appetite in the period until the beginning of 2008, the loan portfolio contains risks that may lead to increased loan impairment charges. We found that the credit quality of loans that the bank has provided in 2009 and 2010 was significantly better and was at the same level as at other large banks.

The bank's risk increases particularly when the value of the customer's assets is less than the customer's total debt, typically as a consequence of a decline in property prices. The risk is aggravated because the bank to a great extent has provided loans without an agreed-upon repayment schedule on the basis of short-term interest rates, which are at present historically low.

We found that the basis for the bank's lending and the bank's credit management of retail customers, particularly follow-up, appears incomplete. The bank was therefore ordered to improve the basis for its lending and its credit management, particularly for the purpose of identifying weaknesses and ensuring an appropriate level of follow-up on exposures that exhibit signs of weakness.

The Danske Bank Group has calculated its ICAAP result (solvency need) at 31 December 2009 at 10.1%. Its actual solvency ratio at 31 December 2009 was 17.8%.

The inspection did not include an assessment of the bank's total ICAAP result. The FSA has informed the bank that it expects that the bank will take into consideration the conclusions of the inspection upon the next calculation of the ICAAP result.