

## **MEMORANDUM**

### **The Danish Financial Supervisory Authority**

13 February 2018

## **Statement on inspection at Danske Bank A/S (Swedish property loans)**

In May 2017, the Danish Financial Supervisory Authority (the FSA) conducted an inspection at Danske Bank. The purpose was to assess the bank's risk appetite and practices in granting loans to new or existing customers with commercial property in Sweden.

### **Summary and risk assessment**

The FSA reviewed 50 exposures primarily to customers whose loans increased substantially in 2016.

Based on a Nordic growth potential approach, Danske Bank's business strategy is to strengthen its position through a growth strategy in Sweden and Norway.

At the time of the inspection, the Swedish commercial property market had been seeing large price increases for some time. For example, the best located office properties in Stockholm were priced as high as SEK 98,000 per square metre in September 2015 and as high as SEK 135,000 per square metre in September 2017. This was equal to an increase of 38% for the period.

Certain price falls were subsequently seen in the Swedish property market.

The development in prices gives rise to a considerable risk of substantial price falls, not least during an economic downturn.

To this should be added that commercial property in Sweden is typically financed on a short-term basis and with short interest periods and moderate repayment before refinancing. Following periods of high property prices, this may put increased pressure on prices. In particular, this will be the case if market liquidity is reduced or if interest rates increase substantially.

As a consequence, the FSA provided risk information to the effect that Danske Bank's growth strategy and high concentrations of Swedish property loans lead to an elevated risk of losses.

Danske Bank has introduced measures to mitigate this risk since the FSA's similar inspection in 2015. This means that the bank's internal limits on growth have been targeted more at Swedish property loans. The bank has improved its analysis of the individual loans with a focus on liquidity, but it could improve the analysis of stress test results in many cases. This is the case when it comes to the risk of a price pressure on rent levels, for example.

The trend in prices and rent levels in the Swedish property market makes it particularly important for the bank to assess whether prices and rent levels are realistic in the long term. As a result, the FSA observes in its risk information that the Board of Directors and the Executive Board should consider additional measures to reduce the risk of losses.

In several cases, the FSA detected inconsistencies between the loan amounts listed in the bank's data sets and those specified in the approval documentation. Danske Bank's interim report for the first quarter of 2017 included a double entry of an exposure of about DKK 6.3 billion. Yet it was a double entry of unutilised loan facilities that affected the note information only and not the balance sheet at the end of the first quarter of 2017.

The FSA pointed out that Danske Bank must continue to have a managerial focus on ensuring a proper data quality.