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INTERNAL CAPITAL ADEQUACY  
ASSESSMENT  
MARCH 31, 2010

Contents	Page
1. Introduction.....	3
2. Internal capital adequacy assessment process (ICAAP).....	4
2.1 Capital management framework .....	4
2.2. The ICAAP result .....	6
3. Definitions of main risk types .....	8
4. Stress testing methodology and scenarios.....	9
5. Additional information.....	10

*Internal Capital Adequacy Assessment is a translation of the original report in the Danish language (Individuelt solvensbehov). In case of discrepancies, the Danish version prevails.*

## 1. Introduction

The objective of this report on the internal capital adequacy assessment is to address the disclosure requirements stipulated by annex 20 to the Danish executive order No. 1470 of December 17, 2009, on capital adequacy, and the Danish Financial Business Act. The report concerns the Danske Bank Group and the legal entities Danske Bank A/S, the sub-group Realkredit Danmark group and Realkredit Danmark A/S.

The report is a supplement to the Danske Bank Group's annual Risk Management report, which contains more details. This document includes

- a description of the process and method for calculating the ICAAP result
- the statement of the total ICAAP result
- definitions of main risk types
- a description of the stress testing methodology and scenarios used

The Danske Bank Group monitors its risks through the coordinated efforts of the credit and risk departments both at Danske Bank A/S and Realkredit Danmark A/S. Realkredit Danmark A/S is a subsidiary of Danske Bank A/S and is included in the report on the Danske Bank Group in accordance with section 60(7) of the Danish executive order on capital adequacy. The report, including the description of the process and method used in the calculation of the ICAAP result, covers the companies mentioned, and it is published on the websites of the relevant companies.

### Conclusion

At the end of March 2010, the Danske Bank Group's ICAAP result was calculated according to the Basel II transitional rules. The ICAAP result amounted to DKr86.6bn, or 10.3% of risk-weighted assets (RWA). With an actual capital base of DKr149.8bn and a solvency ratio of 17.9%, the Group had a massive capital buffer of DKr63.2bn.

Without the Basel II transitional rules, the ICAAP result would have equalled the Pillar I+ result of 9.7% of RWA. This would have added DKr5bn to the buffer.

In addition to the internally estimated ICAAP result, the Group has taken account of a shortfall in relation to Pillar I+ of 1.2% of RWA.

## 2. Internal capital adequacy assessment process (ICAAP)

### 2.1 Capital management framework

The purpose of the Danske Bank Group's capital management is to ensure the efficient use of capital in the light of the Group's overall capital targets. The Group takes the capital targets into account in the determination of its risk profile. This means that the capital level must be sufficient to cover both organic growth and current fluctuations in the risks taken on.

Capital management policies and practices ensure that the Group has sufficient capital to cover the risks associated with its activities. To this end, it uses advanced approaches for all significant risk types in combination with adjustments based on expert assessments. The Group has developed its capital management framework over time, benchmarking it against international guidelines and best-practice recommendations on an ongoing basis. The Group also monitors national and international policy actions that may influence its capital position and capital management framework.

The Group ensures compliance with the approved risk limits and risk monitoring through a fixed cycle for reporting to the Board of Directors and the Executive Board on developments in risk measures.

Reporting to the Board of Directors and the Executive Board includes:

- A report on the ICAAP
- A monthly report on compliance with capital and placement requirements

The Danske Bank Group's ICAAP report is submitted quarterly to the Board of Directors for approval. Once a year, an extended ICAAP report is submitted together with a thorough analysis of the Group's risk profile.

Among other reports, Danske Bank's Board of Directors receives monthly reporting on and a statement of the ICAAP result for review at the monthly board meetings.

The capital management framework is based on the ICAAP. The Group's ICAAP, including the ICAAP conducted at each of the subsidiaries, constitutes the key governance parameter for the capital management. The regulatory framework for the capital management practices is rooted in the CRD<sup>1</sup> and consists of three pillars:

- Pillar I contains a set of rules for a mathematical calculation of the capital requirement based on risk-weighted assets for credit risk, market risk and operational risk.
- Pillar II describes the framework for the ICAAP and the supervisory review and evaluation process (SREP).
- Pillar III deals with market discipline and sets forth disclosure requirements for risk and capital management.

While Pillar I contains uniform rules for capturing a credit institution's risk and determining the capital requirement, Pillar II contains the framework for the ICAAP based on the situation and characteristics of the individual institution. Pillar II covers all relevant risks, including risks not addressed under Pillar I. Pillar II also treats stress testing and the SREP, which is the confidential dialogue between the FSA and a credit institution about the institution's ICAAP.

As part of the ICAAP, management assesses the Group's risk profile on the basis of a number of criteria and estimates. The process also calculates the total capital needed on the basis of internal models for economic capital and ensures that adequate risk management systems are used and refined as necessary. Further, the ICAAP includes capital planning to ensure that the Group holds sufficient capital for the years ahead. One of the planning tools is stress testing.

<sup>1</sup> The Capital Requirements Directive (CRD) is an EU directive that regulates the capital adequacy of banks and other financial institutions. It is based on Basel II, which is a set of international guidelines for banks' capital adequacy.

The Group's ICAAP consists of an assessment of all the significant risks to which the Group is exposed. Besides the Pillar I risk types – credit, market and operational risk – the ICAAP covers pension risk, insurance risk and business risk. The Group also determines qualitative add-ons to the ICAAP result, if required. The add-ons are included if the model-based calculations do not appear to be sufficiently conservative, for instance if the Group believes a more conservative approach than the Pillar I rules or the economic capital calculations is required. The Group has a process in which it identifies and assesses add-ons on the basis of inputs from in-house experts.

The Group does not set aside capital for liquidity risk, but it takes account of liquidity risk in stress testing. The Group recognises that a strong capital position makes it easier to maintain a strong liquidity position.

The Group is involved in a number of business activities. These activities can be divided roughly into five segments: banking, market, asset management, insurance and group-wide activities. The latter category covers management activities that are not unique to specific business activities but support these activities. Each of these activities entails various risks, which fall into the seven main categories of the risk management framework.

Activities	Danske Bank Group's risks						
	Credit risk	Operational risk	Market risk	Pension risk	Insurance risk	Business risk	Liquidity risk
Banking activities	✓	✓	✓			✓	✓
Market activities	✓	✓	✓			✓	✓
Asset management		✓				✓	
Insurance (Danica)					✓		
Group-wide activities		✓		✓			

The regulatory framework in Pillar II contains 17 risk items that must be assessed in the ICAAP, according to Danish legislation. The table below shows the relation between these 17 regulatory items (the rows in the table) and the Group's seven risk categories (the columns in the table) and also shows which of the 17 regulatory items are treated in the Group's stress tests.

Regulatory items	Danske Bank Group's risks							
	Credit risk	Operational risk	Market risk	Pension risk	Insurance risk	Business risk	Liquidity risk	Stress test
General, including strategic plans	✓	✓	✓	✓	✓	✓	✓	✓
Earnings			✓			✓		✓
Growth								✓
Credit risk	✓							✓
Market risk			✓					✓
Concentration risk	✓		✓					✓
Group risk					✓			✓
Liquidity risk							✓	✓
Operational risk		✓						✓
Control risk		✓						
Business size		✓						
Settlement risk	✓	✓						
Strategic risk						✓		✓
Reputational risk		✓				✓		✓
Interest rate risk on assets outside the trading book			✓					✓
External risks		✓				✓		✓
Other				✓				✓

## 2.2. The ICAAP result

The result of the Group's internal capital adequacy assessment (the ICAAP result) is the identified capital needed to cover all the Group's risks, including the highest of the following measurements:

- The capital requirement according to an internal economic capital model
- The capital requirement under Pillar I plus an add-on to address the risks that are not captured by Pillar I (Pillar I+)
- The capital requirement under the transitional rules of the CRD (based on Basel I)

### Economic capital

The Group uses economic capital as an internal method of measuring its capital needs over a twelve-month horizon. Economic capital plays a key role in the Group's stress testing methodology. It is also used for risk-based pricing and for allocation of capital on the basis of the Group's current capital level. The Group uses in-house models for calculating economic capital combined with a qualitative assessment of any add-ons.

Economic capital is the amount of capital needed to cover unexpected losses over the next year at a confidence level of 99.97%. The 99.97 percentile was chosen for internal purposes and reflects Danske Bank's long-term ambition of being AA-rated. In its capital requirement calculation, the Group uses a 99.9 percentile, in line with the confidence level for the CRD capital requirement (Pillar I). The difference reflects the Group's willingness to set capital aside in order to meet its rating ambitions.

Economic capital is a point-in-time (PIT) estimate and thus reflects the Group's current risk, unlike Pillar I+, which is based on credit risk parameters that reflect either an economic downturn or an average over a business cycle (TTC parameters). Economic capital therefore tends to react more sharply to changes in the business cycle.

The Group's aggregation of economic capital for various risk types does not take into account the potential benefit of diversification across risk types. In an internal study, the Group reached a preliminary, conservative estimate of a diversification effect of 10-20% from aggregating credit, market and operational risks. It obtained the estimate by combining the loss distributions of the three risk types into an overall loss distribution. The study confirmed that the results are quite sensitive to key assumptions, such as the current level of stress in the financial markets and the correlation between risk types, and the type of distribution applied in the calculation. Consequently, the Group does not include the diversification effect in the aggregation of risk.

### Pillar I+

The calculation of the Pillar I+ requirement includes an add-on to reflect the risks not adequately covered under Pillar I, for example, pension risk, business risk and, in the current macroeconomic situation, certain credit risks. The Pillar I+ requirement and the capital needed according to the internal economic capital model are supplemented by add-ons to reflect any uncertainty of the risk models, and the capital level is subject to ongoing qualitative adequacy assessments.

### Transitional rules

Banks opting for the advanced approaches for credit risk are subject to limits on the reduction of their capital requirements. Such reductions have been introduced gradually up to 2010. The Group expects an extension of the transitional rules to be adopted in Denmark in mid-2010 with effect until the end of 2011. It has therefore chosen to continue to take account of these rules. The maximum reduction allowed in 2010 under the Basel II transitional rules is 20% of the capital requirement under Basel I.

The regulatory framework provides some discretionary leeway for selection of ICAAP calculation method. The Group believes that it has adopted a sufficiently conservative approach:

- Capital is added to the capital requirement under Pillar I to reflect risks not captured by Pillar I.
- The Group takes account of the uncertainty of the risk models and makes qualitative adequacy assessments of the capital level on an ongoing basis.

The Group's ICAAP result can be broken down into capital for the most important risk types. The Group has chosen to base the breakdown on its economic capital at a 99.9 percentile.

### Danske Bank Group and Danske Bank A/S

#### BREAKDOWN OF DANSKE BANK'S ICAAP RESULT (IN DANISH, "INDIVIDUELT SOLVENSBEHOV")

At March 31, 2010	Danske Bank Group		Danske Bank A/S	
	(DKr bn)	% of RWA	(DKr bn)	% of RWA
Credit risk	52.0	6.2	52.0	7.9
Market risk	6.8	0.8	6.8	1.0
Operational risk	6.9	0.8	6.9	1.0
Other factors	5.9	0.7	5.9	0.9
Internally estimated ICAAP result	71.6	8.5	71.6	10.8
Shortfall in relation to Pillar I+	9.9	1.2	-	-
Shortfall in relation to transitional floor	5.1	0.6	-	-
ICAAP result	86.6	10.3	71.6	10.8
Capital base	149.8	17.9	145.7	22.0
Capital buffer	63.2	7.6	74.1	11.2

### Realkredit Danmark Group and Realkredit Danmark A/S

#### BREAKDOWN OF REALKREDIT DANMARK'S ICAAP RESULT (IN DANISH, "INDIVIDUELT SOLVENSBEHOV")

At March 31, 2010	Realkredit Danmark Group		Realkredit Danmark A/S	
	(DKr bn)	% of RWA	(DKr bn)	% of RWA
Credit risk	9.2	9.6	9.2	9.6
Market risk	0.3	0.3	0.3	0.3
Operational risk	0.6	0.6	0.6	0.6
Other factors	0.3	0.3	0.3	0.3
Internally estimated ICAAP result	10.4	10.8	10.4	10.8
Shortfall in relation to Pillar I+	-	-	-	-
Shortfall in relation to transitional floor	13.5	14.0	13.5	14.0
ICAAP result	23.9	24.8	23.9	24.8
Capital base	44.1	45.8	44.1	45.8
Capital buffer	20.2	21.0	20.2	21.0

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Without the Basel II transitional rules, the ICAAP result would have equalled the Pillar I+ result of 9.7% of RWA. This would have added DKr5bn to the buffer.

In addition to the internally estimated ICAAP result, the Group has taken account of a shortfall in relation to Pillar I+ of 1.2% of RWA.

The Danske Bank Group's economic capital amounted to 8.5% of RWA. At 6.2%, credit risk represented by far the largest component of the individual risks covered by economic capital, while market risk and operational risk combined represented 1.6%. The Other factors category, which represents 0.7% of RWA, includes pension risk, business risk and other components such as any qualitative add-ons.

### 3. Definitions of main risk types

- **Credit risk**

The Group's credit risk is the risk of losses arising because counterparties or debtors fail to meet all or part of their payment obligations to the Group. Credit risk includes the following types of risk:

- Country risk: the risk of losses arising from economic difficulties or political unrest in a country, including the risk of losses resulting from nationalisation, expropriation and debt restructuring.
- Settlement risk: the risk of losses arising when payments are settled, for example payments for currency transactions and trades in financial instruments, including derivatives. The risk arises when the Group remits payment before it can ascertain that the counterparty has fulfilled its obligations.
- Counterparty credit risk: the risk of losses on derivatives contracts resulting from a customer's default.

- **Market risk**

Market risk is the risk of losses arising because the fair value of assets and liabilities varies with changes in market conditions. It consists of:

- Interest rate risk
- Exchange rate risk
- Equity market risk
- Bond spread risk
- Inflation rate risk
- Commodity risk

- **Operational risk**

The risk of losses resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk, but excludes strategic and reputational risk.

- **Other factors**

The Other factors category includes pension risk, business risk and other components such as any qualitative add-ons.

The Group's pension risk is the risk of a shortfall in its defined benefit pension plans that requires the Group to make additional contributions to cover pension obligations to current and former employees.

The Group's business risk, including strategic and reputational risk, is the risk of losses caused by changes in external or internal circumstances that have an adverse effect on its reputation or profits.

This type of risk is driven mainly by factors that are outside the Group's control. Simply put, it is the risk of being in the market.

- **Other add-ons**

In addition to the internally estimated ICAAP result, the Group has also taken account of a shortfall in relation to Pillar I+ and add-ons required under applicable transitional rules.

Risk Management 2009, available at [www.danskebank.com/ir](http://www.danskebank.com/ir), provides more information about the individual components.

#### 4. Stress testing methodology and scenarios

Stress tests are part of the ICAAP and an important tool for analysing the Group's risk profile. The objective of stress testing is to assess the effect of possible unfavourable events on the Group's capital requirement under Pillar I and its economic capital. Stress tests are also part of the internal capital planning process.

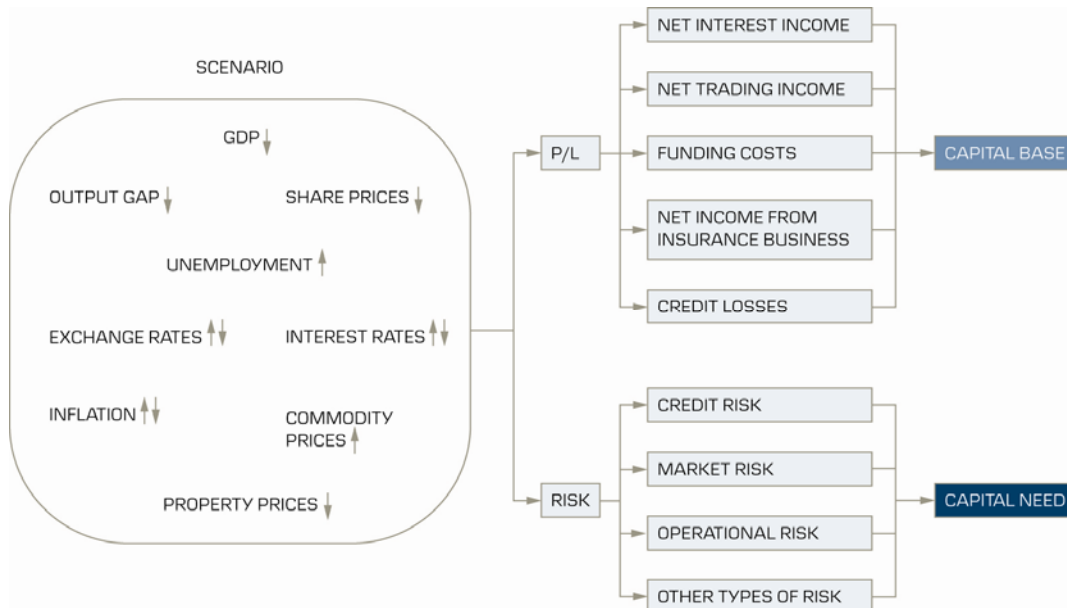
When calculating its ICAAP result, the Group uses a mild recession scenario in accordance with statutory obligations. In its internal capital planning, the Group uses a number of stress test scenarios that are more severe than a mild recession.

Macroeconomic variable (%)	Mild recession		
	Year 1	Year 2	Year 3
GDP growth	-0.5	1.4	2.2
Change in unemployment rate (percentage points)	1.1	0.5	-0.3
Property prices	-4.6	-0.6	1.5

Note: Figures are calculated as an RWA-weighted average of the markets in which the Group operates.

Since 2005, the Group has conducted quarterly stress tests showing the effects of various economic scenarios over a period of three to five years.

There are four phases in the Group's stress testing methodology: (1) choice of scenario; (2) translation of scenario; (3) stress test calculation; and (4) evaluation of results and methodology. The Group assesses its main scenarios and their relevance on an ongoing basis. At least once a year, this includes analysing the scenarios that seem to be the most relevant in terms of risks and the current economic situation. New scenarios may be added when necessary. The scenarios are an essential part of the Group's capital planning in the ICAAP.



The stress tests show that the Group is sufficiently capitalised to withstand all the scenarios in use. In the credit crunch scenario – an extreme scenario – the Group would remain solvent, but gradual management interventions would be required.

## 5. Additional information

This report will be updated quarterly and published together with the Danske Bank Group’s interim reports. It can be downloaded from Danske Bank’s and Realkredit Danmark’s websites ([www.danskebank.com/ir](http://www.danskebank.com/ir) and [www.rd.dk/investor](http://www.rd.dk/investor)).

The Risk Management report, published every year together with the Danske Bank Group’s Annual Report, contains a detailed description of the Group’s risk organisation, capital management, risk profile, exposure, etc. Risk Management is available in English only. It can be downloaded from [www.danskebank.com/ir](http://www.danskebank.com/ir).