

# Länsförsäkringar Hypotek

INTERIM REPORT, JANUARY–JUNE 2006

## Summary

- Lending increased by 25%, from SEK 27 billion to SEK 34 billion.
- The market share for mortgage lending rose from 2.7% to 2.9%.
- The market share of new lending in the home-mortgage market was approximately 4.5%.
- Operating income amounted to SEK 18.4 M (16.4).
- Net interest income increased by 7.7% to SEK 94.4 M (87.7).
- Capital adequacy was 10.97% (12.33) and the Tier 1 ratio 9.09% (9.98).
- The number of customers increased to 87,000 (77,000).

Figures in parentheses pertain to January–June 2005.

### Anders Borgcrantz, President and CEO of Länsförsäkringar Hypotek

The operations are continuing to perform favorably. Our ambition is to further strengthen our position through value-for-money mortgage loans and a strong local presence. I am very pleased that we have increased our net interest income despite intense competition.



## Key figures

	Jan 1, 2006– June 1, 2006	Jan 1, 2005– June 30, 2005	Full-year 2005
Return on equity, %	1.50	1.78	1.13
Return on total capital, %	0.11	0.26	0.08
Investment margin, %	0.56	0.69	0.60
Interest margin, average, %	0.38	0.53	0.45
Cost/income ratio before loan losses	0.66	0.61	0.68
Cost/income ratio after loan losses	0.58	0.56	0.60
Capital adequacy, %	10.97	12.33	12.07
Tier 1 ratio, %	9.09	9.98	10.00
Percentage of doubtful receivables, gross %	0.11	0.16	0.14
Percentage of doubtful receivables, net %	0.01	0.03	–0.04
Provision ratio for doubtful receivables, %	90.89	83.80	90.36

## Quarterly development

SEK 000s	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Q2 2005
Net interest income	47,518	46,909	39,236	39,248	44,554
Net commission income	–25,772	–25,524	–31,126	–29,454	–27,970
Other revenue	49	53	932	0	4,606
<b>Total operating revenue</b>	<b>21,795</b>	<b>21,438</b>	<b>9,042</b>	<b>9,794</b>	<b>21,190</b>
Personnel costs	–1,986	–1,400	–1,538	–522	–
Other expenses	–12,493	–12,503	–5,284	–8,276	–11,575
<b>Other expenses</b>	<b>–14,479</b>	<b>–13,903</b>	<b>–6,822</b>	<b>–8,798</b>	<b>–11,575</b>
<b>Total expenses before loan losses</b>	<b>7,316</b>	<b>7,535</b>	<b>2,220</b>	<b>996</b>	<b>9,615</b>
Loan losses	2,583	922	1,600	1,461	879
<b>Operating income</b>	<b>9,899</b>	<b>8,457</b>	<b>3,820</b>	<b>2,457</b>	<b>10,494</b>

## Total assets

After the second quarter, the company's total assets amounted to SEK 36.8 billion (27.5), an increase of 33.8%.

Lending to the public rose by 24.8%, or SEK 6.8 billion, to SEK 34.0 billion (27.2).

Borrowing rose by 35.6%, or SEK 9.0 billion, to SEK 34.3 billion (25.3).

## Capital adequacy

The capital adequacy ratio amounted to 10.97% (12.33) and the Tier 1 ratio was 9.09% (9.98).

The target level for capital adequacy is 10.5% and for the Tier 1 ratio 8.5%. A deviation of  $\pm 0.5$  percentage points is allowed for both targets.

## Earnings and profitability

Remuneration to the regional insurance companies, which was previously reported as general administration expenses, shall be reported as commission expense as from this interim report and shall therefore be included in net commission income. All comparative values are restated in the same manner.

The company's operating income amounted to SEK 14.9 M (14.7) before loan losses and SEK 18.4 M (16.4) after loan losses, corresponding to a return on equity, after standard tax, of 1.5% (1.8).

## Revenues

Net interest income rose by 7.7% to SEK 94.4 M (87.7), despite intense competition and shrinking margins. The company's investment margin amounted to 0.56% (0.69). The increase in net interest income is attributable to a higher volume of lending.

## Expenses

Operating expenses rose by 23.3%, or SEK 5.4 M, to SEK 28.4 M (23.0).

The cost/income ratio – costs in relation to income – was 0.66 (0.61) before loan losses and 0.58 (0.56) after loan losses.

## Loan losses

Provisions have primarily been established based on the appraisal of groups of loans, and only to a minor extent on the appraisal

of individual loans. The low level of losses continues. Loan recoveries exceeded losses by SEK 3.5 M (1.7).

## Interest-rate risk

On June 30, 2006, an increase of market interest rates by 1 percentage point would have caused an increase in the value of Länsförsäkringar Hypotek's interest-bearing assets and liabilities, including derivatives, of SEK 21.5 M (decrease: 6.6).

## Covered bonds

As described in the preceding interim report, during the third quarter of 2006, Länsförsäkringar Hypotek will submit an application to the Swedish Financial Supervisory Authority (Finansinspektionen) for permission to issue covered bonds in accordance with the Act on Issuance of Covered Bonds (2003:1223). Development activities to realize this issuance are proceeding according to plan.

Provided the company is granted permission by the Swedish Financial Supervisory Authority (Finansinspektionen), future borrowings by means of bond issues will be in covered bonds. The goal is to achieve a triple A rating for the covered borrowing. When it files the application, the company will announce when the issuance of covered bonds may begin and how bonds and other debt instruments previously issued by the Parent Company, Länsförsäkringar Bank, will be handled.

The intention is that holders of previously issued bonds will be given the opportunity to exchange their holdings in order to participate in the subsidiary's secured debt.

## Market and customers

Despite an increasingly intense competition, with increased price pressure, the company has continued to grow. The company's share of the market for single-family homes and tenant-owned apartments amounted to 2.9% (2.7).

## Basel II

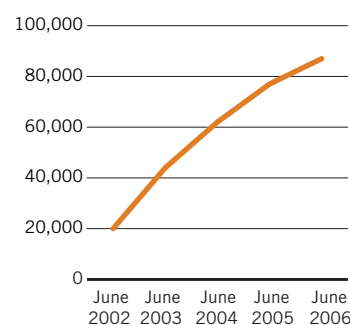
As of January 1, 2007, Länsförsäkringar Hypotek following approval by the Swedish

Financial Supervisory Authority will calculate capital adequacy for credit risks in accordance with the Internal Ratings-based Approach (the IRB approach) for household borrowings. Work with realizing this goal is progressing as planned.

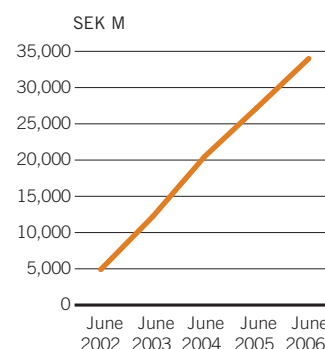
## IFRS

As of 2007, Länsförsäkringar Hypotek will apply the International Financial Reporting Standards (IFRS) in its reporting. The transition involves mainly changes with regard to the reporting of financial instruments in accordance with IAS 39. The company documented and established a model for hedge accounting in accordance with IAS 39 and is making necessary adjustments based on this model. Restated comparable values for the opening balances and the quarterly figures are being continuously determined during 2006.

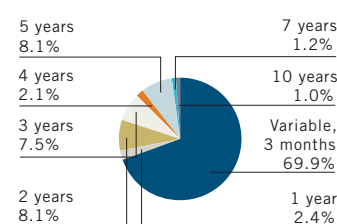
Number of customers



Lending to the public



Fixed interest periods, new loans June 30, 2006



## Income statement

SEK 000s		Jan. 1, 2006– Jun. 30, 2006	Jan. 1, 2005– Jun. 30, 2005	Full-year 2005
Interest income	Note 2	663,753	598,481	1,160,928
Interest expense	Note 3	–569,326	–510,775	–994,738
<b>Net interest income</b>		<b>94,427</b>	<b>87,706</b>	<b>166,190</b>
Commission revenue		741	695	1,388
Commission expense		–52,037	–55,281	–116,554
Net income from financial transactions		–	4,600	5,505
Other operating revenues		102	–24	3
<b>Total operating revenues</b>		<b>43,233</b>	<b>37,696</b>	<b>56,532</b>
General administration expenses		–28,167	–22,869	–38,629
Other operating expenses		–215	–143	–3
<b>Total expenses before loan losses</b>		<b>–28,382</b>	<b>–23,012</b>	<b>–38,632</b>
<b>Income before loan losses</b>		<b>14,851</b>	<b>14,684</b>	<b>17,900</b>
Loan losses, net	Note 4	3,505	1,717	4,778
<b>Total operating income</b>		<b>18,356</b>	<b>16,401</b>	<b>22,678</b>
Tax on income for the period		–5,140	–4,592	–6,356
<b>NET PROFIT/LOSS FOR THE PERIOD</b>		<b>13,216</b>	<b>11,809</b>	<b>16,322</b>

## Balance sheet

SEK 000s		June 30, 2006	June 30, 2005	Dec. 31, 2005
<b>Assets</b>				
Lending to credit institutions		2,773,319	230,852	409,230
Lending to the public	Note 5	34,002,606	27,243,531	30,964,061
Other assets		736	659	625
Prepaid expenses and accrued income		24,530	31,718	45,434
<b>TOTAL ASSETS</b>		<b>36,801,191</b>	<b>27,506,760</b>	<b>31,419,350</b>
<b>Liabilities and shareholders' equity</b>				
Liabilities to credit institutions		33,817,435	24,340,584	28,142,917
Borrowing from the public		454,856	937,114	795,802
Other liabilities		15,486	12,073	4,581
Accrued expenses and prepaid income		385,515	303,475	361,367
Subordinated debt		362,614	362,614	362,614
<b>Total liabilities</b>		<b>35,035,906</b>	<b>25,955,860</b>	<b>29,667,281</b>
<b>Shareholders' equity</b>				
Share capital, 70,335 shares	Note 6	70,335	70,335	70,335
Share premium reserve		–	12,965	–
Statutory reserve		14,067	1,102	14,067
Profit brought forward		1,667,667	1,454,689	1,651,345
Net profit for the period		13,216	11,809	16,322
<b>Total shareholders' equity</b>		<b>1,765,285</b>	<b>1,550,900</b>	<b>1,752,069</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>36,801,191</b>	<b>27,506,760</b>	<b>31,419,350</b>
<b>Memorandum items</b>				
Assets pledged for own liabilities		–	–	–
Contingent liabilities		–	–	–
Commitments				
loans approved but not disbursed		118,472	140,120	93,886
interest-rate swap agreements		11,235,000	7,330,000	10,420,000
		<b>11,353,472</b>	<b>7,470,120</b>	<b>10,513,886</b>

## Cash-flow statement

SEK 000s	Jan. 1, 2006– June 30, 2006	Jan. 1, 2005– June 30, 2005
<b>Liquid funds, January 1</b>	<b>409,230</b>	<b>52,126</b>
<b>Operating activities</b>		
Operating income	18,356	16,401
<b>Adjustment for items not included in cash flow</b>		
Booked non-chargeable tax	–5,140	–4,592
	<b>13,216</b>	<b>11,809</b>
Increase/decrease in lending to the public	–3,038,545	–3,497,224
Change in other assets	20,793	12,568
Change in other liabilities	35,053	–13,990
<b>Cash flow from operating activities</b>	<b>–2,969,483</b>	<b>–3,486,837</b>
<b>Investing activities</b>		
Change in fixed assets	–	–
<b>Cash flow from investing activities</b>	<b>–</b>	<b>–</b>
<b>Financing activities</b>		
Change in borrowing from the public	–340,946	–1,238
Change in other borrowing	5,674,518	3,277,801
Increase in subordinated loan	–	74,000
Shareholders' contribution received	–	315,000
<b>Cash flow from financing activities</b>	<b>5,333,572</b>	<b>3,665,563</b>
<b>CASH FLOW FOR THE PERIOD</b>	<b>2,364,089</b>	<b>178,726</b>
<b>Liquid funds, June 30</b>	<b>2,773,319</b>	<b>230,852</b>
<b>Liquid funds include:</b>		
Other lending to credit institutions	2,773,319	230,852
Interest received amounted to	684,691	609,321
Interest paid amounted to	538,460	541,319

## Notes

### NOTE 1 ACCOUNTING PRINCIPLES

This interim report is prepared in accordance with the Swedish Annual Accounts (Credit Institutes and Securities Companies) Act, and the application of the Financial Accounting Standards Council's regulations and general guidelines (FFFS 2002:22) and with additions in accordance with the transition provisions to the Financial Accounting Standards Council's regulations and general guidelines (FFFS 2005:53).

Remuneration to the regional insurance companies is now reported as commission expense instead of as general administration expenses as previously reported. The principle for the calculation of doubtful receivables has also changed. The changed accounting principles are also applied to comparative figures. In all other respects, the accounting principles remain unchanged compared with the 2005 Annual Report.

### NOTE 2 INTEREST INCOME

SEK 000s	Jan. 1, 2006– June 30, 2006	Jan. 1, 2005– June 30, 2005	Full-year 2005
Interest income, lending to the public	545,274	468,634	942,907
Interest income, Swedish credit institutes	118,476	129,843	218,016
Interest income, other	3	4	5
<b>Total interest income</b>	<b>663,753</b>	<b>598,481</b>	<b>1,160,928</b>
Average interest rate, lending to the public	3,2%	3,6%	3,5%

### NOTE 3 INTEREST EXPENSES

SEK 000s	Jan. 1, 2006– June 30, 2006	Jan. 1, 2005– June 30, 2005	Full-year 2005
Interest expense, borrowing from credit institutions	542,939	481,094	937,524
Interest expense, borrowing from the public	20,699	24,857	47,426
Interest expense, subordinated debt	5,688	4,824	9,788
<b>Total interest expense</b>	<b>569,326</b>	<b>510,775</b>	<b>994,738</b>

### NOTE 4 LOAN LOSSES, NET

SEK 000s	Jan. 1, 2006– June 30, 2006	Jan. 1, 2005– June 30, 2005	Full-year 2005
<b>Specific provision for individually appraised loan receivables</b>			
Write-off of confirmed loan losses during the period	2,863	1,399	1,722
Reversed provisions for probable loan losses reported in the interim accounts as confirmed losses	-2,660	-1,376	-1,376
Provision for probable loan losses during the period	141	–	286
Payment received for prior confirmed loan losses	-2,904	-3,837	-8,285
Reversed provisions no longer required for probable loan losses	-2,794	-312	-1,511
<b>Net expense during the period for individually appraised loan receivables</b>	<b>-5,354</b>	<b>-4,126</b>	<b>-9,164</b>
<b>Group-wise provisions for individually appraised loan receivables</b>			
Allocation/dissolution of provisions for group-wise provisions	–	–	–
<b>Group-wise, appraised by group, of loan receivables of limited value and similar credit risk</b>			
Allocation/dissolution of provisions for loan losses	1,849	2,409	4,386
<b>Net expense for the period for loan receivables appraised by group</b>	<b>1,849</b>	<b>2,409</b>	<b>4,386</b>
<b>Net expense for the period for loan losses</b>	<b>-3,505</b>	<b>-1,717</b>	<b>-4,778</b>

All data pertains to receivables from the general public.

**NOTE 5 LENDING TO THE PUBLIC**

SEK 000s	June 30, 2006	June 30, 2005	Dec. 31, 2005
<b>Loan receivables, gross</b>			
Commercial sector	157,295	165,985	168,361
Household sector	33,877,474	27,110,208	30,829,479
Other	2,875	4,777	4,724
	<b>34,037,644</b>	<b>27,280,970</b>	<b>31,002,564</b>

**Less:**
**Specific provisions for individually appraised loan receivables**

Commercial sector	-1,569	-7,515	-6,729
Household sector	-2,023	-2,304	-2,177
<b>Total individual provisions</b>	<b>-3,592</b>	<b>-9,819</b>	<b>-8,906</b>

**Provisions for group-wise appraised groups of loan receivables**

Commercial sector	-13	-11	-15
Household sector	-31,433	-27,609	-29,582
<b>Total group-wise provisions</b>	<b>-31,446</b>	<b>-27,620</b>	<b>-29,597</b>
<b>Total provisions</b>	<b>-35,038</b>	<b>-37,439</b>	<b>-38,503</b>

**Loan receivables, net**

Commercial sector	155,713	158,459	161,617
Household sector	33,844,018	27,080,295	30,797,720
Other	2,875	4,777	4,724
<b>Total loan receivables, net</b>	<b>34,002,606</b>	<b>27,243,531</b>	<b>30,964,061</b>

**Doubtful loan receivables**

Commercial sector	2,722	11,082	7,882
Household sector	35,829	34,595	34,730
<b>Total doubtful loan receivables</b>	<b>38,551</b>	<b>45,677</b>	<b>42,612</b>

**Non-performing receivables included among doubtful receivables**

Commercial sector	1,822	3,072	2,922
Household sector	14,536	16,413	13,597
<b>Total non-performing receivables included among doubtful receivables</b>	<b>16,358</b>	<b>19,485</b>	<b>16,519</b>

**Definitions:**

**Non-performing receivables** are loans for which interest payments, amortization or overdrafts are more than 60 days past due.

**A doubtful receivable** is a non-performing receivable or a receivable for which payments are unlikely to be made in accordance with the terms of the claim, and for which the value of the collateral is not adequate with a secure margin to cover both the principal and accrued interest, including penalties for possible late payments.



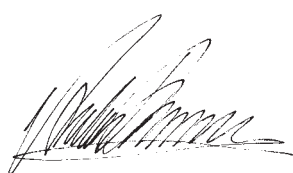
**NOTE 6 SHAREHOLDERS EQUITY**

SEK 000s	June 30, 2006	June 30, 2005	Dec. 31, 2005
<b>Restricted equity</b>			
Share capital	70,335	70,335	70,335
Share premium reserve	–	12,965	–
Statutory reserve	14,067	1,102	14,067
<b>Total restricted equity</b>	<b>84,402</b>	<b>84,402</b>	<b>84,402</b>
<b>Non-restricted equity</b>			
Profit brought forward	1,667,667	1,454,689	1,651,345
Net profit for the year	13,216	11,809	16,322
<b>Total non-restricted equity</b>	<b>1,680,883</b>	<b>1,466,498</b>	<b>1,667,667</b>
<b>Total shareholders' equity</b>	<b>1,765,285</b>	<b>1,550,900</b>	<b>1,752,069</b>
<b>Change in shareholders' equity</b>			
Opening balance	1,752,069	1,224,091	1,224,091
Unconditional shareholders' contribution from Parent Company		315,000	528,000
Group contribution paid			–22,700
Tax effect of Group contribution paid			6,356
Net profit for the period	13,216	11,809	16,322
<b>Closing balance</b>	<b>1,765,285</b>	<b>1,550,900</b>	<b>1,752,069</b>

**NOTE 7 DERIVATIVE INSTRUMENTS**

SEK 000s	Nominal value	Fair value
<b>Derivative instruments with positive value</b>		
Interest-rate derivatives	7,285,000	126,809
<b>Derivative instruments with negative value</b>		
Interest-rate derivatives	3,950,000	68,219

This interim report is unaudited.  
Stockholm, August 29, 2006.

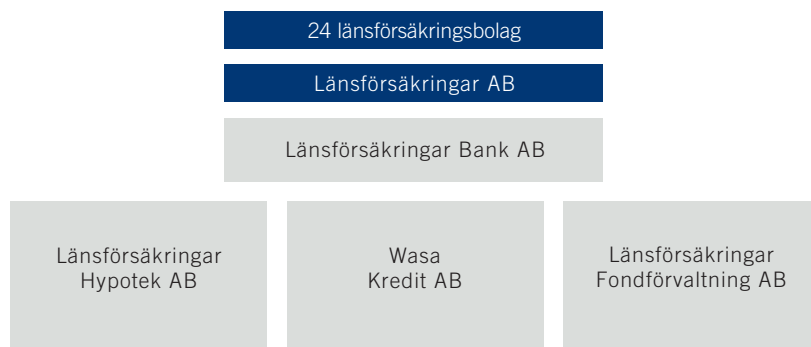


**Anders Borgcrantz**  
*President and CEO*

**Reporting dates for 2006:**

Interim report, January-September

October 23, 2006



The Länsförsäkringar Alliance organization is based on 24 local, independent and customer-owned regional insurance companies. The regional insurance companies jointly own Länsförsäkringar AB. In turn, Länsförsäkringar AB owns Länsförsäkringar Bank AB (Bank Group), with the Parent Company and the subsidiaries Länsförsäkringar Hypotek AB, Wasa Kredit AB and Länsförsäkringar Fondförvaltning AB. Customer contact always occurs at the regional insurance companies. There are a total of 90 offices. From the customer's viewpoint, the regional insurance companies operate as local banks, in the same manner as with non-life insurance and life assurance.

**For further information, contact:**

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