

Capital Adequacy and Risk Management Report 2008

Pillar 3

NIBC
Holding

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Introduction

Goal and overview

NIBC's Risk Management and Capital Adequacy (Pillar 3) report contains information that enables an assessment of the risk profile and capital adequacy of NIBC Holding N.V. This publication fulfils the requirements of the Basel II framework, as stipulated in the *Capital Requirements Directive (CRD)*. The CRD is legally enforced by Dutch law by the Financial Supervision Act (Wet Financieel Toezicht).

The CRD is based on the Basel II framework, which contains three pillars:

- Pillar 1 defines the regulatory minimum capital requirements by providing rules and regulations for measurement of credit risk, market risk and operational risk. These capital requirements need to be covered by regulatory own funds. NIBC received approval from the *Dutch Central Bank (DNB)* to use as of 1 January 2008, the *Advanced Internal Ratings Based (AIRB)* approach for calculating solvency requirements regarding credit risk for its most important exposure classes, namely corporates and retail, and the *Internal Model Approach (IMA)* regarding market risk in the Trading book. Solvency requirements for the remaining portfolios and for operational risk are calculated using the Standardised approach.
- Pillar 2 covers the Supervisory Review Process. This consists of the *Internal Capital Adequacy Assessment Process (ICAAP)*, the bank's own assessment of its capital adequacy in relation to all its risks and the *Supervisory Review and Evaluation Process (SREP)*, the response of the Supervisor on the institution's ICAAP.
- Pillar 3 focuses on disclosure requirements, covering all relevant pieces of information for a market participant to assess the risk profile and capital adequacy of the credit institution. The risk disclosures are connected to the first pillar of the Basel II framework, as information is provided regarding the underlying exposures, risk weighted assets and regulatory capital.

NIBC's Capital Adequacy and Risk Management Report is prepared to meet the requirements of Pillar 3, as well as the increased need for transparency in the financial market. The Capital Adequacy and Risk Management Report follows the structure below:

- Risk management strategy & process
- Credit risk
- Market risk
- Operational risk
- Liquidity risk
- Securitisation exposures
- Internal Capital Adequacy Assessment Process
- Capital base components
- Capital adequacy

The scope of application in this report refers to NIBC Holding, henceforth referred to as NIBC. The main entity of NIBC Holding is NIBC Bank. Where necessary, a distinction between NIBC Holding and NIBC Bank is made explicitly. The starting point of the Basel II prudential scope of application is the consolidation scope of NIBC, according to the *International Financial Reporting Standards (IFRS)*. In line with the requirements of the CRD, a prudential filter is applied for non-financial subsidiaries. These entities are excluded from the consolidation scope and are, instead, treated as investments in associates. Appendix 1 provides further details regarding the consolidation scope.



The credit exposures in this report are not directly comparable to the numbers in the Annual Report. The numbers in the Annual Report refer to book values and classifications in line with the IFRS requirements. The numbers in this report refer to *exposure at default (EAD)*, which is a risk measure of the potential amount outstanding in the event of default. EAD is, therefore, a different measure than on-balance sheet and off-balance sheet amounts, and the method employed for its calculation differs per exposure class. A more detailed explanation on EAD can be found in the Credit Risk chapter.

NIBC's Risk Management and Capital Adequacy (Pillar 3) Report is produced at least on an annual basis and is published on NIBC's website (www.nibc.com). The report may also be published more frequently if special market circumstances require so. Information regarding risk management and key data on capital adequacy are presented in NIBC's Annual Report as well.



Risk Management Strategy & Process

Highlights of 2008

The financial crisis that intensified in 2008 left few in the markets unscathed. What began the year as an inter-bank crisis spread into the real economy, with slowdown and recessionary conditions taking an ever-wider toll.

NIBC was significantly affected by the financial crisis from its start in spring 2007 and risk management has been a major focus throughout 2008. However, because much of the balance sheet was accounted on a fair-value basis, losses became visible at NIBC earlier than at many other institutions. As a result, early actions were taken to de-risk the portfolio and the activities of NIBC:

- NIBC disposed of its US residential mortgage-backed securities portfolio back in August 2007.
- NIBC considerably reduced its US commercial real estate-backed securities' portfolio in 2007 and transferred it from NIBC Bank to NIBC Holding. At the end of 2008 this portfolio was marked down to a level of 28% of the original nominal value.
- Other non-client related portfolios of securities were drastically reduced and marked down.

To withstand the global credit crisis, Risk Management set three priorities in 2008: tightly controlled liquidity management, controlling structured credits portfolios and keeping a close watch on the loan portfolio.

Risk appetite and risk management strategy

NIBC has a clearly defined business model around two strategic pillars – Merchant Banking and Specialised Finance – focusing on mid-sized corporate clients in the Benelux and German areas, as well as being a meaningful player in a select number of asset classes. Indispensable to those pillars and the entire business of NIBC are the Treasury, Risk Management and Corporate Center departments. Because of its focus and the in-depth understanding of the business and its clients, NIBC has good understanding of the risks in this select number of markets. The risk strategy of NIBC is aligned with this business model, resulting in the following markets and portfolios, where the risks are concentrated:

- Credit risk in the loan portfolio in six different asset classes (Corporate Lending, Leveraged Finance, Shipping, Oil & Gas Services, Infrastructure & Renewables and Real Estate, including Dutch and German residential mortgages).
- Investment risk in equity and mezzanine loans related to the Merchant Banking business.
- Market risk in the Treasury portfolios, consisting of interest rate risk in Trading and Mismatch portfolio, and credit spread risk in the structured credits portfolio and Financial and Sovereign portfolio.

NIBC uses *Economic Capital (EC)* as a universal risk measure throughout the company. For each business activity EC is allocated and reported to the Asset & Liability Committee once every two weeks.



Risk management processes and governance

Under the supervision of NIBC's Managing Board and the Risk Policy Committee of the Supervisory Board, formal authority and ultimate decision-making in respect of risk management matters is the responsibility of four committees: the Transaction Committee, the Investment Committee, the Asset & Liability Committee and the over-arching Risk Management Committee. These committees are chaired by the Chief Risk Officer (CRO) and they ensure that assessment and acceptance of credit, market, investment and liquidity risk exposure are made independently of the business originators within the operating segments.

The *Risk Management Committee (RMC)* determines the overall risk appetite and risk profile at a strategic level, evaluates the risk management elements of new activities and products as well as reviews risks at portfolio level, sets country risk limits, approves acceptance policies and guidelines and approves the risk policies and manuals. Three members of the Managing Board are members of the RMC, which also includes representatives from the Transaction Committee and the Asset & Liability Committee. As necessitated by the topics to be discussed, specialists in certain areas are also invited to the meetings of the RMC. The RMC meets on a monthly basis.

The *Asset & Liability Committee (ALCO)* monitors the development of the balance sheet and market risk profile. The ALCO monitors traded market risks, exposure to interest rates and currency risks, NIBC's capital structure and liquidity position. The ALCO also approves large transactions such as securitisations and sets overall limits on risk exposures. The ALCO receives reports on all breaches of risk limits. Three members of the Managing Board are members of the ALCO. The ALCO meets once every two weeks.

The *Transaction Committee (TC)*, NIBC's credit committee, makes decisions on individual senior debt transactions, including credit conditions and parameters and lending and underwriting strategies, as well as evaluates opportunities for potential subsequent distribution of the asset. The TC sets credit limits and monitors exposure and impairments. Two members of the Managing Board are members of the TC. Meetings of the TC take place twice a week.

The *Investment Committee (IC)* is responsible for investment risk. The IC approves transactions with respect to equity, mezzanine, and subordinated debt exposures as well as impairments and revaluations for these exposures. Two members of the Managing Board are members of the IC. The IC meets, in principle, on a weekly basis. Investment decisions of the Funds (limited partnership investments in funds set up and managed by NIBC) managed by Investment Management are made by the Investment Committees of the various Funds.

In addition to the above risk management committees, there is also the *Engagement and Compliance Committee (ECC)*, which is responsible for the prevention of potential commercial conflicts of interest and compliance issues in evaluating potential assignment for NIBC's clients. All four members of the Managing Board are members of the ECC.

The responsibility for monitoring and managing operational risk is shared between NIBC's Operational Risk Manager and the business unit manager. Significant operational issues and oversight regarding the adoption of best practices are discussed on a regular basis within the Managing Board.

Overlap of committee membership among Managing Board members contributes to consistency in communication and decision-making. In all risk management committees, at least two members are members of the Managing Board.

The CRO is supported by centralised risk management functions, which consist of three risk management departments, the *Credit Risk Management* department (CRM), the *Asset & Liability Management and Market*



Risk department (**ALM/MR**), and the *Risk Policy* department (**RP**). These departments support the various risk management committees dedicated to monitoring the different risk categories NIBC faces.

CRM is responsible for the credit risk management of the corporate loan portfolio. CRM develops and implements policies and procedures regarding credit risk, advises on credit proposals and reviews potential impairments. The *Distressed Assets* department (**DA**) is a sub-department of CRM. DA manages assets which are impaired, or at significant risk of becoming impaired. Credit risk management of the mezzanine investments, as well as investment risk management of the private equity positions is the responsibility of the IC or the Investment Committee of one of the NIBC Funds (depending on whether the specific mezzanine or equity position is part of NIBC's direct portfolio or part of one of the NIBC Funds).

ALM/MR is responsible for managing risks within the Treasury department and the residential mortgage portfolio. Key risks managed by ALM/MR are market risk (interest rate, foreign exchange and credit spread risk) liquidity risk and *Counterparty Credit Risk (CCR)*. This type of credit risk, despite being classified as a non-market risk, is monitored by ALM/MR as part of its comprehensive management of all financial markets' risks. On a company level, ALM/MR is also responsible for managing the risks related to the Asset and Liability management on a Group level.

RP monitors credit risk on a portfolio level. RP develops policies and methods for measuring risk, notably the credit rating system used to evaluate the *probability of default (PD)*, *loss given default (LGD)* and *exposure at default (EAD)* in the corporate loan portfolio, as well as the credit risk economic capital models. Furthermore, RP designs and implements company-wide stress tests, undertakes the credit loss registration and represents NIBC in the Pan-European Credit Data Consortium. RP is also responsible for the reporting of credit portfolio information to the various users within NIBC.



Credit Risk

NIBC defines credit risk as the current or potential threat to the company's earnings and capital as a result of a counterparty's failure to make required debt payments on a timely basis or to comply with other conditions of an obligation or agreement, including the possibility of restrictions on or impediments to the transfer of payments from abroad.

Credit risk is present in almost all portfolios of NIBC and it is the largest source of risk it is exposed to, representing approximately 90% of total *Risk Weighted Assets (RWA)* and of the company's capital requirements.

The Pillar 3 disclosure requirements prescribe that a credit institution classifies its assets in a number of standard exposure classes. For a credit institution using the AIRB approach, these exposure classes are defined in article 86 of the CRD. Table 1 presents the relationship between the classification in this report and the portfolios in the Annual Report:

Table 1: Comparison between Pillar 3 exposures classes and portfolios in NIBC's annual report

Pillar 3 exposure classes	Portfolios in Annual Report
Sovereigns	Debt investments from sovereigns and cash at central banks
Institutions	Debt investments from financial institutions, structured investments and cash and derivative transactions with financial institutions
Corporates	Corporate loan portfolio, including guarantees and derivatives, and mezzanine loan portfolio
Retail	Dutch and German residential mortgage portfolio, excluding securitised portfolios
Equities	Equity investments and credit fixed income funds
Securitisations	Structured credits EU, structured credits US and retained notes of own securitisations
Other	Non-credit related exposures

Apart from the above differences in classification, differences can also be found between the numbers presented in this report and the numbers in the risk paragraph and risk notes in NIBC's Annual Report. The main reasons that these numbers are not directly comparable are the following:

- For exposures treated under the AIRB approach, Pillar 3 numbers refer to EAD, a risk measure of the potential outstanding amount in the event of default.
- For derivative transactions, Pillar 3 numbers refer to the market value and add-on including the effect of netting and collateral.
- For undrawn parts of credit facilities, a *credit conversion factor (CCF)* is applied on the Pillar 3 numbers, which cannot be recognised on the balance sheet.



Credit risk exposures

This section presents NIBC's credit risk exposures based on the definitions and approaches that are used in the calculation of capital requirements. In 2007, NIBC received approval by the DNB to use, as of 1 January 2008, the AIRB approach for the calculation of its capital requirements for the corporate and retail exposure classes. Furthermore, NIBC uses the internal ratings-based method for the securitisation exposure class and the simplified risk-weight approach for the equity exposure class. The AIRB approach is the most sophisticated approach within the Basel II framework for the calculation of capital requirements and it is based on internal estimation of various risk parameters. The section *Calculation of Risk Weighted Assets* further in this chapter provides more information on the ways that NIBC uses for the estimation of these parameters.

The Standardised approach applies to all other NIBC exposure classes containing credit risk. Over the course of 2009, NIBC aims to obtain regulatory approval for AIRB-compliant models for the institutions' exposure class. The sovereigns' exposure class will remain under the Standardised approach, as NIBC has received a permanent exemption for this class by the DNB.

Table 2 shows a breakdown of EAD, RWA and capital requirements between exposure classes and calculation approaches, as at 31 December 2008 and 2007. The increase of retail EAD in 2008 is the result of new origination, repurchases of residential mortgages from consolidated Special Purpose Entities and of the purchase of a Dutch residential portfolio from a third-party. Furthermore, the reduction of institutions' exposure (almost 45%) is a result of NIBC's de-risking policy. Due to this de-risking policy, the structured credits portfolios have been reduced significantly in 2008.

Table 2: Breakdown of EAD, RWA and capital requirement for credit risk

IN EUR MILLIONS	2008			2007		
	EAD	RWA	Capital requirement	EAD	RWA	Capital requirement
AIRB APPROACH						
- of which corporates	7,687	4,346	348	9,645	5,387	431
- of which retail	4,780	624	50	3,739	774	61
- of which equities	582	2,148	172	571	2,100	168
- of which securitisations	1,300	735	59	1,532	277	23
STANDARDISED APPROACH						
- of which sovereigns	1,466	1	0	1,458	0	0
- of which institutions	2,512	743	59	4,547	1,071	85
- of which corporates	638	638	51	1,179	1,179	94
- of which retail	690	298	24	826	289	23
- of which equities	38	38	3	144	144	13
- of which other	96	96	8	73	73	6
TOTAL CREDIT RISK	19,789	9,667	774	23,714	11,294	904

Breakdown of credit risk exposures

Table 3 shows a breakdown of exposure classes and exposure types under the AIRB and Standardised approaches, as at 31 December 2008. Table 4 shows a similar breakdown during 2008 on average. The most noticeable development is the decrease during 2008 of the institutions' exposures, which is related to the de-risking policy of NIBC.

Table 3: Breakdown of credit risk exposure types by exposure class, 31 December 2008

IN EUR MILLIONS					
Exposure Class	On-Balance	Off-Balance	Derivatives	Repo-Style	Total
AIRB APPROACH					
Corporates	6,281	997	409	0	7,687
Retail	4,749	31	0	0	4,780
Equities	409	173	0	0	582
Securitisations	1,269	31	0	0	1,300
SUBTOTAL	12,708	1,232	409	0	14,349
STANDARDISED APPROACH					
Sovereigns	1,456	10	0	0	1,466
Institutions	1,455	141	507	409	2,512
Corporates	402	52	183	1	638
Retail	690	0	0	0	690
Equities	38	0	0	0	38
Other	96	0	0	0	96
SUBTOTAL	4,137	203	690	410	5,440
TOTAL	16,845	1,435	1,099	410	19,789

Table 4: Breakdown of credit risk exposure types by exposure class, average 2008

IN EUR MILLIONS					
Exposure Class	On-Balance	Off-Balance	Derivatives	Repo-Style	Total
AIRB APPROACH					
Corporates	6,888	1,562	216	0	8,666
Retail	4,234	26	0	0	4,260
Equities	490	86	0	0	576
Securitisations	1,380	36	0	0	1,416
SUBTOTAL	12,992	1,710	216	0	14,918
STANDARDISED APPROACH					
Sovereigns	1,423	38	0	0	1,461
Institutions	2,613	193	426	469	3,701
Corporates	450	81	375	3	909
Retail	758	0	0	0	758
Equities	91	0	0	0	91
Other	85	0	0	0	85
SUBTOTAL	5,420	312	801	472	7,005
NIBC TOTAL	18,412	2,022	1,017	472	21,923

Tables 5 and 6 show the breakdown of exposures between regions and industry sectors, respectively. The geographical distribution of NIBC's assets corresponds to the company's strategy for focus in North Western Europe, with the Netherlands, the UK and Germany accounting for approximately 80% of EAD. This percentage increases to 90% when the entire European Union is included.

Table 5: Breakdown of EAD per region, 31 December 2008

IN EUR MILLIONS									
Exposure Class	The Netherlands	United Kingdom	Germany	Rest of EU	Non-EU Europe	North America	South East Asia	Other	Total
AIRB APPROACH									
Corporates	2,608	1,745	1,054	702	222	338	405	613	7,687
Retail	4,780	0	0	0	0	0	0	0	4,780
Equities	463	22	31	21	0	45	0	0	582
Securitisations	440	224	48	340	0	197	23	28	1,300
SUBTOTAL	8,291	1,991	1,133	1,063	222	580	428	641	14,349
STANDARDISED APPROACH									
Sovereigns	1,449	0	0	10	3	0	0	4	1,466
Institutions	961	557	63	729	14	121	14	53	2,512
Corporates	377	119	92	35	5	0	0	10	638
Retail	18	0	672	0	0	0	0	0	690
Equities	0	0	0	0	0	38	0	0	38
Other	0	0	0	0	0	0	0	96	96
SUBTOTAL	2,805	676	827	774	22	159	14	163	5,440
TOTAL	11,096	2,667	1,960	1,837	244	739	442	804	19,789

From an industry-sector point of view, the commercial real estate sector is spread over a variety of property financing, including multi-family properties, offices, retail properties, hotel financing and construction financing. About one fourth of this portfolio consists of financing of miscellaneous properties, including mixed use and industrial properties. In terms of geographical distribution, approximately 95% of the commercial real estate portfolio is located in the Netherlands and Germany, and the remainder in other EU countries.

Exposures to the shipping industry include the three main shipping sub-sectors tankers, container vessels and bulk vessels, which account for approximately 90% of the entire portfolio. The remainder of this portfolio includes, among others, financing of LNG tankers, container boxes and oil and gas support vessels, such as towing vessels. Shipping exposures are well diversified between different countries, of which European Union countries (including the Netherlands, the UK and Germany) account for approximately one third of Shipping's EAD, South East Asia for approximately 40% and North America for approximately 10%. Almost the entire exposure of NIBC to South East Asia relates to Shipping assets.

NIBC's Leveraged Finance portfolio amounted to almost EUR 1,000 million at year-end 2008. The portfolio is well-diversified over multiple industry sectors and spans over the Netherlands (approximately 30%), the United Kingdom (approximately 35%), Germany (approximately 20%) and other European Union countries (the remaining 15%).

Other important sectors in NIBC's portfolio are Financial Services, which contain the vast majority of NIBC's Institutions' exposure class, and Retail, which are composed of NIBC's residential mortgage portfolios in the Netherlands and Germany, and securitisation notes of residential mortgage-backed securities.



Table 6: Breakdown of EAD per industry sector, 31 December 2008

IN EUR MILLIONS														
Exposure Class	Aviation	Commer- cial Real Estate	Financial Services	Food / Agri- culture	Health / Educa- tion	Infra- struc- ture	Manu- factu- ring	Retail	Ship- ping	Govern- ments / Central Banks	Trade	Utilities	Other	Total
AIRB APPROACH														
Corporates	102	1,685	110	43	521	1,012	1,021	0	1,424	0	975	225	569	7,687
Retail	0	0	0	0	0	0	0	4,780	0	0	0	0	0	4,780
Equities	0	36	26	0	28	91	56	0	0	0	152	0	193	582
Securitisations	0	519	0	0	0	0	0	531	0	0	0	0	250	1,300
SUBTOTAL	102	2,240	136	43	549	1,103	1,077	5,311	1,424	0	1,127	225	1,012	14,349
STANDARDISED APPROACH														
Sovereigns	0	0	7	0	0	0	0	0	0	1,459	0	0	0	1,466
Institutions	0	54	2,458	0	0	0	0	0	0	0	0	0	0	2,512
Corporates	0	115	50	30	5	17	60	0	14	0	47	0	300	638
Retail	0	0	0	0	0	0	0	690	0	0	0	0	0	690
Equities	0	0	0	0	0	0	0	0	0	0	0	0	38	38
Other	0	0	0	0	0	0	0	0	0	0	0	0	96	96
SUBTOTAL	0	169	2,515	30	5	17	60	690	14	1,459	47	0	434	5,440
TOTAL	102	2,409	2,651	73	554	1,120	1,137	6,001	1,438	1,459	1,174	225	1,446	19,789

Table 7 provides a breakdown of credit risk EAD per maturity. Approximately 65% of all of NIBC's credit risk exposures mature after the next 5 years.

Table 7: Breakdown of credit risk EAD per maturity, 31 December 2008

IN EUR MILLIONS					
Exposure Class	≤ 1 year	> 1 year - ≤ 2 years	> 2 years - ≤ 5 years	> 5 years	Total
AIRB APPROACH					
Corporates	416	431	2,546	4,294	7,687
Retail	3	13	30	4,734	4,780
Equities	582	0	0	0	582
Securitisations	39	23	39	1,199	1,300
SUBTOTAL	1,040	467	2,615	10,227	14,349
STANDARDISED APPROACH					
Sovereigns	1,247	201	18	0	1,466
Institutions	681	303	414	1,114	2,512
Corporates	248	11	86	293	638
Retail	6	3	18	663	690
Equities	0	38	0	0	38
Other	17	5	16	58	96
SUBTOTAL	2,199	561	552	2,128	5,440
TOTAL	3,239	1,028	3,167	12,355	19,789

Calculation of Risk Weighted Assets

AIRB approach

Ratings and rating process in the AIRB approach

The AIRB approach for the corporate and retail exposure classes has been adopted by NIBC and approved by the DNB since 1 January 2008. The ratings framework consists of the calculation of 3 main parameters: PD, LGD and EAD.

The PDs, LGDs and EADs that are calculated through NIBC's internal models are used for the calculation of *Expected Loss (EL)* and Pillar-1 Regulatory Capital (**RC**). Internal ratings enable an objective comparison of the credit risk of different types of assets, making them an essential tool for the commercial and risk management departments to determine whether a transaction fits NIBC's strategy and portfolio, as well as to determine an appropriate pricing and the *Risk-Adjusted Return on Capital (RAROC)*. *Economic Capital (EC)* and stress testing are additional areas, within Pillar 2, which make use of the above-mentioned parameters, although the values and methodologies for both EC and stress testing differ from those employed in Pillar 1. In particular, a market risk instead of a credit risk approach is used for a number of portfolios in Pillar 2. NIBC has developed a variety of stress test scenarios, both on total portfolio and sub-portfolio level, to evaluate the impact of the scenarios on its RWAs and Tier-1 ratio.

In addition to these three internally calculated parameters, a fourth parameter which influences the calculation of the Pillar-1 RC is the maturity. The AIRB approach assumes a minimum maturity of 1 year and a maximum maturity of 5 years.

This section explains how the PD, LGD and EAD are applied within the AIRB corporate and retail framework of NIBC.

Corporates

NIBC applies its internally-developed credit rating methodology since 2000. This methodology consists of two elements: a counterparty credit rating that reflects the probability of default of the borrower, and an anticipated loss element that expresses the potential loss in the event of default. All counterparties are reviewed at least once a year.

The basis for both the PD and the LGD methodologies is the application of expert judgement on a number of rating indicators. From a risk perspective, NIBC considers its corporate exposures to fall within four broad asset classes (Corporate Lending, Asset Finance, Leveraged Finance and Project Finance), and for each of these asset types the relevant credit drivers and parameters are captured in the rating models.

NIBC enforces strict separation of responsibilities with respect to its internal rating methodologies and rating process, model development, model validation and internal audit.

Counterparty credit ratings and probability of default

The counterparty credit rating reflects the counterparty's capacity to meet its financial obligations in full and in time. Counterparty credit ratings do not incorporate any recovery issues, as these are captured through the LGD internal estimates.

NIBC's uses a through-the-cycle counterparty credit rating scale, which consists of 10 grades (1-10). Most of these grades are further divided in notches, by the addition of a plus or minus sign to show the relative standing within the rating grade. NIBC uses a total of 22 notches, each of which is mapped to the rating scale of the main international rating agencies. Furthermore, counterparty credit ratings are assigned a rating outlook. This



assesses the potential direction of the counterparty credit rating over the medium term. In determining a rating outlook, consideration is given to any changes in the economic and/or fundamental business conditions.

The general methodology for determining a counterparty's credit rating is based on several qualitative and quantitative rating indicators, such as the analysis of the business and financial profile of the counterparty, a cash flow analysis, a sovereign risk analysis, a peer-group analysis and a rating benchmark based on third-party models. Expert judgement is applied at the end of the rating process and determines what the final rating of the counterparty will be, taking into account the rating indicators of the various models.

Each notch carries a PD, which quantifies the likelihood that the counterparty will go into default in the next one year. The performance of the counterparty credit rating methodology is back-tested annually in order to ensure that consistency is kept throughout the portfolio and to measure the discriminatory power of the counterparty credit ratings. Furthermore, NIBC regularly benchmarks its counterparty credit ratings with external parties.

Loss given default

Whereas counterparty credit ratings are assigned on a counterparty level, LGD ratings are facility-specific. The LGD ratings reflect the loss that can be expected in a downward scenario on a facility, if a counterparty defaults. NIBC's internal LGD scale consists of 7 grades (A-F) and 10 notches, each of which represents a different degree of recovery prospects and loss expectations.

NIBC's LGD philosophy is similar to the approach for counterparty credit ratings. The LGD methodology is also based on a combination of qualitative and quantitative rating indicators that include, among others, the assessment of the available collateral and/or guarantees, the seniority of the loan, the applicable jurisdiction, and the quality of the counterparty's assets. Once the various LGD drivers have been assessed, the final LGD rating is based upon expert judgement.

As is the case for counterparty credit ratings, the maintenance of NIBC's LGD models involves benchmarking and back-testing. Furthermore, NIBC is a founding member of the *Pan-European Credit Data Consortium (PECDC)*, the largest international loan loss data pooling entity. This enables NIBC to exchange anonymous loss data with other large international banks for the purposes of enhancing LGD modelling capabilities, sharing of best practices, LGD calibration and benchmarking.

Exposure at default and credit conversion factor

A third element of the AIRB approach is the calculation of the EAD. It is defined as the amount that is expected to be outstanding at the moment that a counterparty defaults. Counterparties typically tend to utilise their credit lines more intensively when approaching default, which implies that the amount outstanding at default is expected to be higher than the current outstanding amount.

In order to quantify the additional expected utilisation, NIBC applies a CCF on the undrawn portion of every credit facility. The main driver for the value of the CCF is the type of the credit facility (e.g. committed or uncommitted facility, loan, guarantee, derivative, etc.). NIBC produces its own internal estimates of CCF, based on the utilisation of defaulted credit facilities at the time of default and one year prior to default, which are a combination of internal defaulted facilities and defaulted facilities from the PECDC data pool. These internal estimates are then benchmarked to external estimates from other PECDC member banks.



Overview of AIRB corporate exposures

Table 8 provides an overview of corporate AIRB EAD types, broken down by NIBC rating grade (equivalent Standard & Poor's rating are provided in parentheses). The table also provides the average PD and LGD, weighted against EAD. As assets with a rating of 9/10 have already defaulted, the notion of LGD as used for non-defaulted assets is no longer applicable. Losses are therefore estimated through a separate impairment model, in order to determine the provision amounts.

Table 8: Breakdown of Corporate AIRB EAD by weighted average PD, weighted average LGD and EAD type, 31 December 2008

IN EUR MILLIONS						
Rating Scale	WA PD	WA LGD	On-balance	Off-balance	Derivatives	Total
1/2 (AAA/AA)	0.03%	9.77%	30	1	0	31
3 (A)	0.06%	15.86%	95	0	7	102
4 (BBB)	0.29%	16.77%	856	222	129	1,207
5 (BB)	1.56%	17.95%	3,030	527	191	3,748
6 (B)	3.54%	25.36%	1,685	234	71	1,990
7 (CCC)	8.02%	27.30%	282	11	8	301
8 (CC/C)	-	-	0	0	0	0
9/10 (D)	100.00%	n/a	303	2	3	308
TOTAL			6,281	997	409	7,687

Retail

The AIRB approach applies to NIBC's Dutch residential mortgage portfolio. The calculation of PD, LGD and EAD is performed by an in-house developed Basel II AIRB model, which has been in use since 2006. The PD estimates are dependent on a variety of factors, of which the key factors are Debt-to-Income and Loan-to-Value ratios. Minor factors which play a role in the PD estimates are several other mortgage loan characteristics, borrower characteristics and payment performance information. The PD scale is based on a continuous scale ranging from 0 - 100%.

The LGD estimates are based on a downturn scenario comparable to the downturn in the Dutch mortgage market in the 1980's. In this case, the indexed collateral value is stressed in order to simulate the proceeds of a (forced) sale of the collateral. The stress is dependant on the location and the absolute value of the collateral. Together with cost and time to foreclosure assumptions, an LGD is derived. The LGD estimate also takes into account whether a mortgage loan has a *Dutch government guarantee (NHG guarantee)*, for which the LGD estimate will be lower in comparison to a mortgage loan without the NHG guarantee. The LGD estimate is also based on a continuous scale.

The EAD is set equal to the net exposure (balance outstanding minus built-up savings value) for all mortgage loans, except for non-amortising (in this case interest-only loans). For the non-amortising loans, 3 months of accrued interest is added to the EAD.

The validation of these estimates is performed on historical data and is carried out on a yearly basis. For the PD and LGD, the estimates are back tested against realised defaults and realised losses. In this way it is ensured that the model still functions correctly in a changing economic environment.

At 31 December 2008, EUR 797 million of credit protection by means of a guarantee structured in a synthetic securitisation (Provide Orange) was in place in connection with NIBC's Residential mortgages own book.

Overview of AIRB retail exposures

Table 9 provides an overview of retail AIRB exposure at default types, broken down by PD buckets. The table provides also the average PD and LGD, weighted against EAD. Note that the numbers in this table refer to the Dutch residential mortgage portfolio of NIBC.

Table 9: Breakdown of Retail AIRB EAD by weighted average PD, weighted average LGD and EAD type, 31 December 2008

IN EUR MILLIONS					
PD bucket	WA PD	WA LGD	On-balance	Off-balance	Total
<1%	0.35%	15.08%	4,543	25	4,568
1% - 2%	1.29%	36.74%	54	4	58
2% - 5%	4.07%	16.67%	64	2	66
5% - 99%	16.89%	21.20%	68	0	68
100%	100.00%	18.33%	20	0	20
TOTAL			4,749	31	4,780

Equities

NIBC uses the simple risk weight approach for equity investments. Under the simple risk weight approach the RWA is calculated by multiplying the exposure amount by 190% for private equity exposures in sufficiently diversified portfolios, 290% for exposures traded on listed exchanges and 370% for other exposures. The EAD for equities amounts to EUR 582 million, of which EUR 574 million attracts a 370% risk weight (non-listed companies) and EUR 8 million a 290% risk weight (listed companies).

Securitisations

NIBC uses the internal ratings based approach for securitisations exposures, both for purchased securitisations as well as for retained notes of own securitisations. Under the internal ratings based approach, the RWA is calculated by multiplying the exposure amount by the appropriate risk weight. The risk weight depends upon the external rating, the granularity of the pool and the seniority of the pool. Alternatively, for retained notes of own securitisations, NIBC uses the IRB capital charge had the underlying exposures not been securitised (KIRB). More detailed risk information about NIBC's securitisation exposures can be found in the securitisation section.

Table 10: Risk weights of securitisation exposures, 31 December 2008

IN EUR MILLIONS							
Risk weight	<10%	10% - 20%	25% - 50%	60 - 100%	250% - 650%	1250% or deducted	Total
Retained	123	12	13	95	21	35	299
Purchased	0	813	65	79	34	10	1,001
TOTAL	123	825	78	174	55	45	1,300

Standardised Approach

For the calculation of RWA under the Standardised approach, the book value of the on-balance sheet exposure is multiplied by a risk weight, depending on the exposure type and the external rating. The off-balance sheet exposures are multiplied by both a risk weight and a credit conversion factor. The risk weights are prescribed in the CRD (Annex VI, part 1):

- Nearly all of NIBC's sovereign exposures are exposures with a zero risk weight.
- The risk weight for institutions is mostly 20% (short-term exposures of rating A- and higher, and long-term exposure of rating AA- and higher) or 50% (both short-term and long-term exposures of rating between BBB- and BBB+). Covered bond exposures have a 10% risk weight.
- The corporate exposure class carries a risk weight of 100% and consists mainly of derivatives to corporate clients. The reason why these derivatives fall under the standardised approach is a system's issue. Once this has been resolved, these exposures will be treated under the AIRB approach.
- The retail exposure consists of the German mortgage portfolio. Part of the exposure, which is fully secured by residential property, receives a 35% risk weight and the other part receives a 100% risk weight.
- The equity exposure refers to the *Credit Fixed Income Funds (CFIF)*, which receives a 100% risk weight.

Overview of Standardised portfolios

Tables 11 and 12 provide a breakdown of EAD and RWA, respectively, by exposure class, together with the applicable risk weight.

Table 11: Standardised EAD per risk weight, 31 December 2008

IN EUR MILLIONS									
Exposure Class	0%	10%	20%	35%	50%	100%	150%	Other	Total
Sovereigns	1,463	0	0	0	3	0	0	0	1,466
Institutions	0	296	1,034	0	700	14	6	462	2,512
Corporates	0	0	0	0	0	638	0	0	638
Retail	0	0	0	600	0	90	0	0	690
Equities	0	0	0	0	0	38	0	0	38
Other	0	0	0	0	0	96	0	0	96
TOTAL	1,463	296	1,034	600	703	876	6	462	5,440

Table 12: Standardised RWA per risk weight, 31 December 2008

IN EUR MILLIONS									
Exposure Class	0%	10%	20%	35%	50%	100%	150%	Other	Total
Sovereigns	0	0	0	0	1	0	0	0	1
Institutions	0	30	207	0	350	14	9	134	743
Corporates	0	0	0	0	0	638	0	0	638
Retail	0	0	0	208	0	90	0	0	298
Equities	0	0	0	0	0	38	0	0	38
Other	0	0	0	0	0	96	0	0	96
TOTAL	0	30	207	208	351	876	9	134	1,814

Credit risk mitigation

Institutions

The exposures to financial institutions are either related to *over-the counter* (OTC) derivative transactions, or to debt investments (in tradable securities), or to cash management activities (money market and repo transactions), or to credit derivatives. Details about credit risk management for OTC derivative transactions can be found in the relevant section about counterparty credit risk. NIBC only enters into repo transactions if they are secured by highly rated bonds. Some debt investments of financial institutions are secured by collateral (covered bonds) or benefit from state guarantees. The latter are classified as sovereign exposures.

Corporates

An important element in NIBC's credit approval process is the assessment of collateral. Almost all exposures under the corporate exposure class have some form of collateralisation, with the main exception of mezzanine exposures. Exposures can be collateralised by mortgages on real estate and ships, by receivables, leases or liens on machinery and equipments, or by third-party guarantees and other similar agreements. An exposure is deemed to be collateralised, fully or partly, if such assets are legally pledged in support of the exposure.

In general, NIBC requests collateral to protect its interests. NIBC ascribes value to collateral provided that the collateral is sufficiently liquid, that documentation is effective and that enforcing NIBC's legal rights to the collateral will be successful. The type and quantity of the collateral depends on the type of transaction, the counterparty and the risks involved. The most significant types of collateral securing the corporate exposure class are tangible assets, such as real estate, ships and equipment.

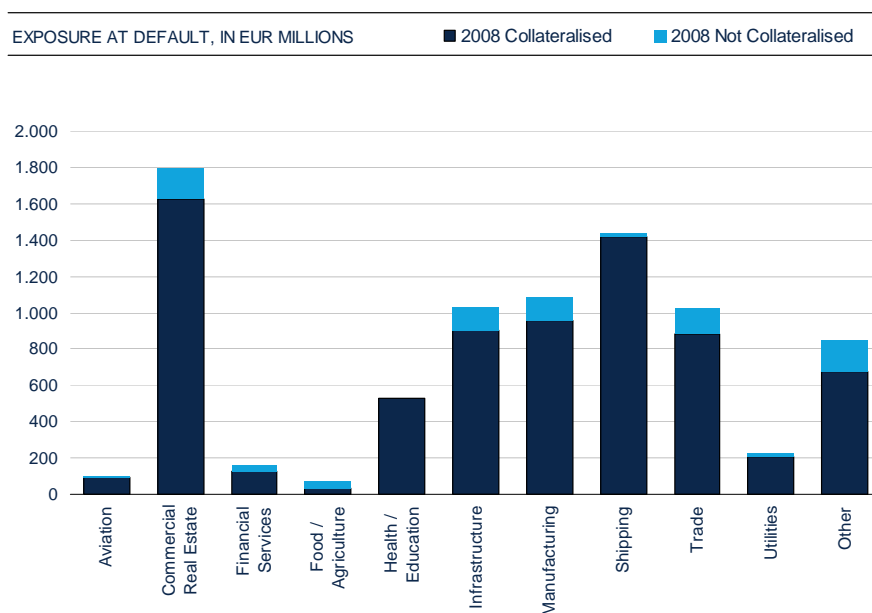
NIBC initially values collateral based on fair market value when structuring a transaction, and evaluates the collateral (semi-) annually during the lifetime of the exposure. NIBC typically confirms that its interest is legally enforceable with independent third-party experts. Exposures in the shipping and oil and gas sectors are secured by moveable assets such as ships and drilling vessels. Exposures in the commercial real estate sector are primarily collateralised by mortgages on financed properties. Collateral value is estimated using third-party appraisers, whenever possible, or valuation techniques based on common market practice.

Other corporate exposures are, to a large extent, collateralised by assets such as equipment, inventory, debtors, and third-party credit protection (e.g. guarantees). The value of these types of collateral can be more difficult to determine, therefore such collateral is attributed a nil value in order to be conservative.

The following graph shows the breakdown of collateralised and uncollateralised exposures by industry sector as per 31 December 2008. The term *collateralised* may indicate full or partial collateralisation.



Graph 1: Breakdown of (un)collateralised EAD per industry sector, 31 December 2008



Retail

Dutch residential mortgage portfolio

Credit losses are mitigated in a number of different ways:

- The underlying property is pledged as collateral.
- Under Dutch law NIBC has full recourse on the borrower.
- 15% of the Dutch own book portfolio and 43% of the securitised portfolio are covered by the NHG programme.
- Approximately 50% of the Dutch residential mortgage portfolio has been securitised.
- NIBC has concluded a synthetic securitisation by means of a *credit default swap (CDS)* with *Kreditanstalt für Wiederaufbau (KfW)*, a government-owned bank, in which the credit risk of the underlying portfolio of EUR 797 million is transferred.

For the portfolio not covered by the CDS or the NHG programme, the underlying property is the primary collateral for any mortgage loan granted, though savings and investment deposits may also serve as additional collateral.

A measurement for potential losses, taking into account indexation of house prices and seasoning, is achieved by calculating the *Loan-to-Indexed-Market-Value (LTiMV)*. The indexation is made using the index of the Dutch Land Registry Office (Kadaster), which is based on market observables. For the part of the portfolio not covered by the CDS or the NHG programme, only 7% has an LTiMV above 100%. For the remainder of the portfolio, the indexed collateral value is sufficient to cover the entire loan balance outstanding.

German residential mortgage portfolio

As is the case in the Netherlands, the underlying property is the primary collateral for any mortgage loan granted. In contrast to the Dutch market, most of mortgage loans contain an annuity repayment, leading to a lower outstanding balance during the lifetime of the loan. The majority of the underlying collateral for the German portfolio is located in former West Germany.



Overview of impaired and past-due exposures

Impaired and past-due exposures

Sovereigns and Institutions

In 2008 NIBC did not take any impairments on these portfolios. Some financial institutions defaulted in 2008 leading to limited losses for NIBC. However, these assets are classified as Held for Trading or Fair Value through Profit and Loss.

Corporates

NIBC assesses whether there is an indication of impairment of corporate loans classified as Available for Sale assets or as Loans and Receivables at Amortised Cost on an individual basis and at least quarterly. NIBC considers a range of factors that have a bearing on the expected future cash flows that it expects to receive from the loan, including the business prospects of the borrower and its industry sector, the realisable value of collateral held, the level of subordination relative to other lenders and creditors, and the likely cost and likely duration of any recovery process. Subjective judgements are made in the process including, among others, the determination of expected future cash flows and their timing, the market value of collateral, and market discount rates. Furthermore, NIBC's judgements change with time as new information becomes available, or as recovery strategies evolve, resulting in frequent revisions to individual impairments, on a case-by-case basis.

NIBC calculates an impairment amount by taking certain factors into account, particularly the available collateral securing a loan. An impairment amount is recorded only if the total outstanding amount is greater than the sum of the net present value of the realisable collateral value and any other cash flow that NIBC expects to collect on the loan.

Table 8 in the section *Calculation of Risk Weighted Assets* presented a breakdown of the corporate exposure class in NIBC's internal rating scale. EUR 308 million is allocated to counterparties with a default rating (9/10), which NIBC considers impaired, regardless of whether an impairment amount has been taken. Reasons for not always taking an impairment amount for a defaulted counterparty may be e.g. over-collateralisation or NIBC's expectation of future cash-flow generation.

Tables 13 and 14 show a breakdown per region and industry sector respectively, of the impairment amounts (EUR 99 million) on the corporate exposure class per year-end 2008. The column labelled *Impaired EAD Corporate* shows the EAD of those facilities only that carry an impairment amount (EUR 167 million). The difference between the impaired EAD on facility level and the impairment amount can be explained again due to the presence of collateral or to NIBC's expectation of future cash-flow generation.



Table 13: Breakdown of impairments on corporate exposure class per region, 31 December 2008

IN EUR MILLIONS			
Region	Total EAD Corporate	Impaired EAD Corporate	Impairment
The Netherlands	2,985	46	19
United Kingdom	1,864	51	39
Germany	1,146	25	17
Rest of EU	737	41	23
Non-EU Europe	227	0	0
North America	338	2	0
South East Asia	405	0	0
Other	623	2	1
TOTAL	8,325	167	99

Table 14: Breakdown of impairments on corporate exposure class per industry sector, 31 December 2008

IN EUR MILLIONS			
Industry sector	Total EAD Corporate	Impaired EAD Corporate	Impairment
Aviation	102	23	9
Commercial Real Estate	1,800	9	3
Financial Services	160	2	0
Food/Agriculture	73	2	1
Health/Education	526	5	4
Infrastructure	1,029	16	16
Manufacturing	1,081	47	25
Shipping	1,438	4	1
Trade	1,022	26	21
Utilities	225	0	0
Other	869	33	19
TOTAL	8,325	167	99

Past due loan amounts are reported to the TC on a monthly basis. Payments may be past due for any number of reasons. However, late payments are not automatically assumed to be uncollectible. Table 15 presents the corporate exposures with a past-due amount. The table also shows those EADs with technical past-due amounts. These are the past-due amounts between 1 and 5 days and may be caused by various operational reasons.



Retail

In order to manage credit losses more closely, the arrears management for residential mortgages has been largely in-sourced. This ensures a dedicated team focused on maximising recoveries.

The first month of arrears is managed by the services, as in many cases late payments within the first 30 days are related to operational issues. When past-due amounts are outstanding longer than one month, the arrears management is transferred to the NIBC Arrears Management department. At the end of 2008, about 70% of the portfolio was being managed in-house. As of 2009, all past-due amounts longer than one month will be managed in-house. Table 15 shows the past-due amounts' overview of the retail exposure class as at 31 December 2008. The table also shows those EADs with technical past-due amounts. These amounts contain those borrowers with a past-due amount below EUR 250.

In 2008, the impairment amount taken on the Dutch residential mortgage portfolio was EUR 1.2 million. No impairments were taken on the German residential mortgage portfolio.

Table 15: EAD with a past due amount, corporate and retail exposure classes, 31 December 2008

IN EUR MILLIONS	Corporate	Retail
	EAD	EAD
Technical past-due amounts	283	19
1-30 days	246	85
31-60 days	68	27
61-90 days	52	11
SUBTOTAL LESS THAN 90 DAYS	649	142
Over 90 days	93	22
No payment arrear	7,583	5,306
TOTAL	8,325	5,470

Equities

NIBC determines an impairment on the Available for Sale Equity investments held in NIBC's investment portfolio, if there has been a significant or prolonged decline in the fair value below its original cost (including previous impairment losses). NIBC uses expert judgement in determining what is 'significant' or 'prolonged' by evaluating, among other factors, whether the decline is outside the normal range of volatility in the asset's price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the company of which the securities NIBC holds, a decline in industry or sector performance, adverse changes in technology, or problems with operational or financing cash flows.

Tables 16 and 17 present an overview of impairments on equity exposures per region and industry sector respectively. The columns labelled *Impaired EAD Equity at year-end 2008* present the remaining EAD after the impairment has been taken.



Table 16 Breakdown of impairments on equity exposure class per region, 31 December 2008

IN EUR MILLIONS			
Region	Total EAD Equity	Impaired EAD Equity at year-end 2008	Impairment
The Netherlands	442	26	13
United Kingdom	17	17	2
Germany	11	7	18
Rest of EU	18	17	6
North America	94	33	43
TOTAL	582	100	82

Table 17: Breakdown of impairments on equity exposure class per industry sector, 31 December 2008

IN EUR MILLIONS			
Rating Sector	Total EAD Equity	Impaired EAD Equity at year-end 2008	Impairment
Commercial Real Estate	31	0	0
Financial Services	135	34	61
Infrastructure	82	0	0
Health/Education	13	0	0
Manufacturing	14	14	18
Shipping	4	4	1
Trade	101	0	0
Other	202	48	2
TOTAL	582	100	82

Securitisations

As of 1 July 2008 NIBC has reclassified all its securitisations exposures from Fair Value through P&L to Amortised Cost, with the exception of synthetics, as IFRS does not allow such an accounting treatment for these products. Therefore impairments for the securitisations exposures only refer to the period after 30 June 2008 and the impairment amount takes the market value as of 30 June 2008 as reference. NIBC uses a dedicated impairment process for securitisation exposures. As soon as an interest payment is missed, or a relevant covenant is breached, or payment of an interest or notional cash flow is highly unlikely, then an impairment is taken. For equity and mezzanine exposures the impairment amount is equal to the difference between the carrying value prior to the impairment and the current market value. For the higher rated tranches, the market value is based upon the expected cash flows.

Table 18 shows a breakdown of impairments on securitisations per collateral type. The column labelled *Impaired EAD Securitisation at year-end 2008* present the remaining EAD after the impairment has been taken.



Table 18: Breakdown of impairments on securitisation exposure class per collateral type, 31 December 2008

IN EUR MILLIONS			
Securitisation type	Total EAD Securitisation	Impaired EAD	
		Securitisation at year-end 2008	Impairment
RMBS	518	0	0
CMBS	325	0	0
CDO	182	5	1
CLO	56	13	6
ABS	22	0	0
US-Collateralised	2	0	0
TOTAL NIBC Bank	1,105	18	7
CMBS	13	0	0
CRE-CDO	182	56	29
TOTAL NIBC Holding	1,300	74	36

Expected loss versus realised losses

NIBC regularly reviews the methodology and assumptions used for estimating both the amount and timing of future cash flows, to reduce any differences between loss estimates (*Expected Loss*, EL) and actual loss (*Realised Loss*, RL) experience. The EL is a statistical measure that is based on the calculated PD, LGD and EAD, and it represents the average loss that NIBC expects to incur. The RL is the actual loss that NIBC has experienced at the end of a given year.

The impact of the credit crisis on the corporate exposure class has, until year-end 2008, remained fairly limited. There has been some increase in the level of provisioning but provisions did not reach extreme levels, in part due to the high level of collateralisation. A similar pattern was noted for the retail exposure class as well.

Table 19 shows the average losses in basis points since 2007. Losses are attributed to the year in which the counterparty enters default according to the Basel II definition. The losses are based on the actual write-off on the loans and on the outstanding provision (31 December 2008) in case the default was unresolved at year-end. The losses are related to the non-defaulted portfolio at the start of the year, containing on- and off-balance sheet amounts. With the exception of 2007, in which average losses were extremely low, the average losses at year-end 2008 remained relatively stable compared to past experience.

Table 19: Expected Loss (EL) versus Realised Loss (RL)

Exposure Class	2008		2007	
	EL	RL	EL	RL
Corporate	0.31%	0.34%	0.41%	0.07%
Retail	0.16%	0.02%	0.11%	0.02%



Counterparty Credit Risk

This paragraph deals with *counterparty credit risk (CCR)*. NIBC defines counterparty credit risk as the credit risk resulting from OTC derivative transactions, where there is no formal Exchange and none or limited initial investment, such as *interest rate swaps (IRS)*, *credit default swaps (CDS)* and *foreign exchange (FX)* transactions. Money market deposit transactions and repos are not included in CCR. Instead, these are included in the credit exposures on financial institutions.

NIBC is exposed to CCR from derivative transactions both with corporate clients as well as with financial institutions. For both types of counterparties, CCR is measured similarly, being the sum of the positive replacement value and add-on. The add-on reflects the potential future change in marked-to-market value during the remaining lifetime of the derivative contract. All derivative transactions are legally covered by *International Swaps and Derivatives Association (ISDA)* agreements. Derivative transactions with corporate clients are concluded as part of the relationship management. Capital and credit limits for corporate clients are allocated on a one-obligor basis. Although the credit risk resulting from CCR is monitored in conjunction with other exposures to these clients, no specific collateral is requested for these exposures. For its most important financial counterparties, NIBC has mitigated the CCR by using a *Credit Support Annex (CSA)*. Under this annex the credit exposures after netting are mitigated by the posting of (cash) collateral. Limits for financial counterparties cover both money market exposures and derivative exposures and are based upon a combination of external ratings, market developments like CDS spreads, and expert judgement. NIBC values derivative contracts in a uniform way, i.e. no counterparty-specific credit reserves are used in the valuation of derivatives contracts.

Table 20 shows the breakdown of EAD, RWA and capital requirements for derivatives as at 31 December 2008.

Table 20: Breakdown of EAD, RWA and capital requirement for derivatives, 31 December 2008

IN EUR MILLIONS	EAD	RWA	Capital requirement
AIRB APPROACH			
- of which corporates	409	188	15
STANDARDISED APPROACH			
- of which institutions	1,083	333	27
- of which corporates	184	184	15
TOTAL DERIVATIVES	1,676	705	57

As discussed above, the EAD for derivatives is based on the sum of the positive replacement value (marked-to-market value) and applicable add-on. For corporate exposures using the AIRB approach, the PD is derived from the counterparty credit rating and the LGD is equal to the facility weighted-average LGD. For institutions and corporate exposures for which the Standardised approach is used, the risk weight of the counterparty is used in the calculation of the RWA.



Table 21: Gross positive fair value, netting benefits, reduction from collateral and resulting net fair value exposure from derivative contracts

IN EUR MILLIONS	2008
Gross exposure	3,109
Netting benefits	2,220-
Reduction from collateral	167-
Net current exposure	722

NIBC uses credit derivatives both to protect its debt investment portfolio as well as to create credit exposures, although the latter is significantly reduced as part of the de-risking policy that NIBC started implementing in 2007. Tables 22 and 23 show the breakdown of all CDS contracts:

Table 22: Breakdown of CDS contracts by exposure class

IN EUR MILLIONS		
CDS contract exposure class	Sold protection	Bought protection
Sovereigns	10	176
Institutions	167	134
Corporates	85	157
Securitisations	30	805
TOTAL	292	1,272

Table 23: Breakdown of CDS contracts by name type

IN EUR MILLIONS		
CDS contract name type	Sold protection	Bought protection
Single name	212	372
Multiple name	80	900
TOTAL	292	1,272

As discussed in the retail section, the largest exposure (EUR 797 million) is protection bought linked to a synthetic securitisation of the banks' mortgage portfolio.



Market Risk

NIBC defines market risk as the current and prospective threat to its earnings and capital as a result of movements in market prices. Market risk, therefore, includes price risk, interest rate risk and foreign exchange risk, both within and outside the Trading book. For fixed income products, market risk also includes credit spread risk, which is the risk due to movements of underlying credit curve. The predominant market risk drivers for NIBC are interest rate risk and credit spread risk.

The trading positions of NIBC are the result of customer-driven transactions and limited trading for its own account in interest rate risk products. Interest rate risk outside the Trading book of NIBC is limited to a centrally managed mismatch position. For all other banking activities only residual positions are allowed, as the basic principle of NIBC is to hedge the interest rate risk from assets, liabilities and off-balance sheet instruments.

In 2007, NIBC initiated a de-risking policy and this continued throughout 2008. As a result, policy and trading changed accordingly. In particular, all credit-related trading activities have been downscaled significantly and current portfolios, in so far these have not been sold, are transferred to the Banking book. This is visible in the Market Risk RWA and capital requirements shown in Table 24 and explains the significant reduction between year-end 2007 and 2008. An additional reason for the reduction of market risk RWA and capital requirement is the fact that, on 1 January 2008, NIBC received approval to use the internal model approach (IMA) for market risk in the trading portfolio. The reclassification of the structured credits portfolios from the Trading book to the Banking book (securitisations exposure class) further reduced Market Risk RWA.

Structural FX risk arises primarily from principal investments, customer-driven loans and funding or mismatch positions in foreign currencies. The general principle is to hedge FX risk completely, although small residual positions, e.g. from profits in foreign currencies, are allowed.

Table 24: Breakdown of EAD, RWA and capital requirement for market risk, 31 December

IN EUR MILLIONS	2008		2007	
	RWA	Capital requirement	RWA	Capital requirement
- of w hich trading book VaR	100	8		
- of w hich trading book Standardised approach	0	0	876	70
- of w hich FX Standardised approach	45	4	125	10
TOTAL MARKET RISK	145	12	1,001	80

Governance

The objectives of the market risk function are to measure, report and control the market risk of NIBC, both inside and outside the Trading book. For this purpose, a common framework applies across the whole institution. For all books with interest or credit spread risk, limits are defined and positions are monitored daily. The risk management and control function is independent of the trading activities. The market risk position is reported to the ALCO once every two weeks. Any requests for new limits also have to be approved by the ALCO.

The risk appetite for interest rate risk is set by the *Value-at-Risk (VaR)* limits. For the Trading book a VaR limit (99% confidence level, 1 day holding period) of EUR 3 million is set, for the mismatch book a VaR limit of EUR 7 million applies and the VaR on consolidated basis of EUR 10 million applies.

Measurement methods

NIBC uses multiple risk measures to capture all aspect of market risk. These include interest and credit basis-point sensitivity, VaR, economic capital and the outcomes of various stress tests.

VaR framework

The overall VaR framework for market risk consists of a 1-day, 99% confidence level model and is based upon 4 years of weekly historical market data and a full revaluation of the market value of the portfolio concerned. This VaR framework is used both for interest rate risk and credit spread risk. For the Trading book, additional VaR scenarios based upon daily historical market data and a 10 day holding period are used, both for limit setting as well as for the calculation of the capital requirement.

NIBC has chosen to use two different sets of historical data, one consisting of daily market data exclusively for the Trading book and one consisting of weekly data, for the Trading and Banking books and on a consolidated level. Not only is the use of daily market data for the Trading book a regulatory requirement, but this book only contains liquid plain vanilla interest rate products. For these products reliable daily market data are available. The Banking book, however, also contains a number of less liquid positions, where reliable daily market data, especially for credit spreads, are not available.

Stress testing

In addition to the VaR, NIBC has defined a number of stress tests. These stress tests consist both of historical events as well as potential extreme market conditions, which have not (yet) materialised. Stress tests are conducted and reported daily, both for the Trading book and the Banking book and on a consolidated level. Below some examples of stress tests are mentioned:

- Historical interest rate spike 1994, where long term interest rates rose 275 basis points in Europe and 250 basis points in the US.
- Credit crisis 2008, where credits spreads rose significantly.
- Hypothetical scenario, where interest rates shift by -100 basis points or + 100 basis points.
- Hypothetical scenario, where credit spreads rise significantly.

Regulatory capital for market risk in the Trading book

NIBC has obtained supervisory approval to use the Internal Models Approach (IMA) for market risk in the Trading book. The Trading book of NIBC contains exclusively interest rate risk positions. Annex VII, part B of the European directive 2006/48/EC sets the requirements for systems and controls regarding exposures in the Trading book. NIBC complies in all material aspects with these requirements. The capital requirement for market risk at the end of 2008 equalled EUR 8.4 million.

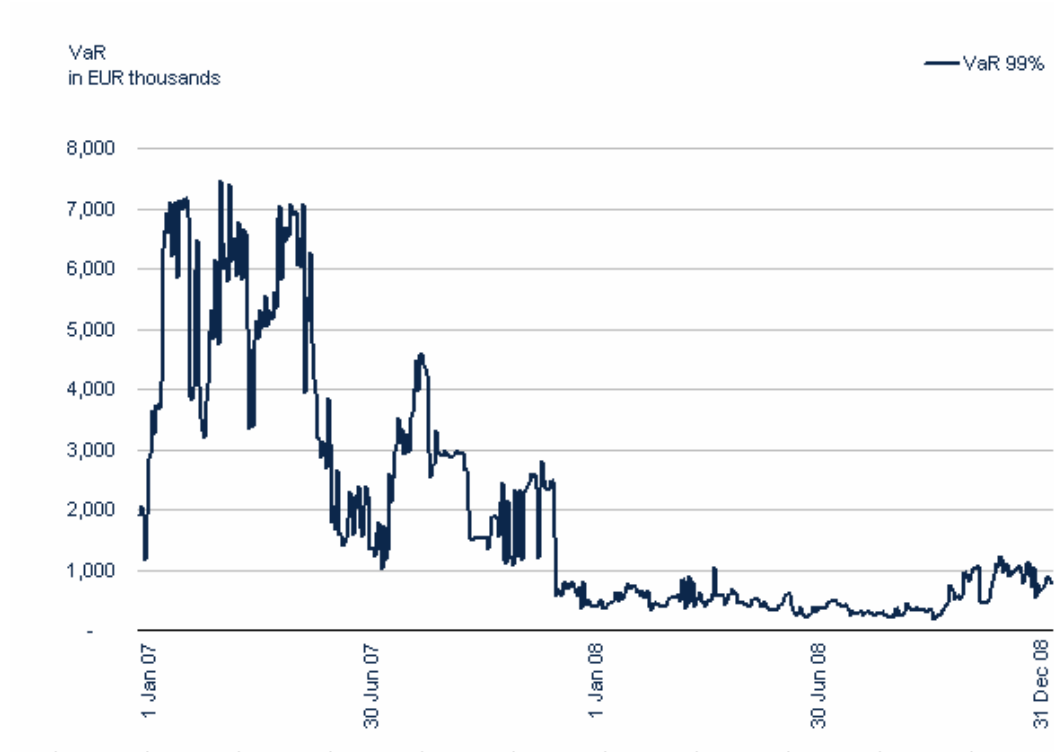
VaR

For the Trading book, the implemented de-risking policy can be clearly observed in the 2008 statistics. Although the VaR was higher at the end of 2008 than at the end of 2007, during the year the interest *basis-point value (BPV)* and the interest VaR were, on average, substantially lower.



The following graph shows the development of the VaR in 2007 and 2008.

Graph 2: development of VaR in the Trading book during 2007 and 2008



Tables 25 and 26 show the key statistics on the VaR numbers for the Trading portfolios in 2008 and 2007.

Table 25: Key risk statistics Trading portfolio, 31 December 2008

IN EUR THOUSANDS	Interest rate	
	BPV	VaR
High	113	1,237
Average	1	521
Low	(151)	186
YEAR-END 2008	(101)	773



Table 26: Key risk statistics Trading portfolio, 31 December 2007

IN EUR THOUSANDS	Interest rate	
	BPV	VaR
High	646	7,451
Average	42	3,384
Low	(706)	354
YEAR-END 2007	(26)	375

Back testing

Back testing for the Trading portfolios is conducted in accordance with the guidelines of the Basel Committee on Banking Supervision. For the Trading book the 1-day 99% VaR is back tested with the hypothetical P&L. The hypothetical P&L is calculated based upon the end-of-day trading position and the change in market rates from the trading day to the next business day. In 2008 the volatility in the markets increased significantly, causing an increase in the number of outliers. This has been the reason to investigate the assumptions in the VaR model.

Market risk outside the Trading book

Interest rate risk in the Banking book

Outside the Trading book NIBC is subject to interest rate risk in the Banking book. There are two primary sources of interest rate risk:

- The lending, debt investment and funding activities generate interest rate risk. For these activities only residual positions are allowed, which are controlled by small facilitating limits. The interest rate risk generated by these activities is transferred to the Corporate Treasury book.
- NIBC has a proprietary mismatch position, which reflects the long term view of the company on interest rates. This book is not part of the trading activities, as these positions have been taken with a long-term view. This book is managed by the Treasury department, monitored on a daily basis by risk management and reported to the ALCO once every two weeks.

NIBC uses an economic value approach to model interest rate risk in the Banking book. Corporate loans and deposits are modelled based upon the contractual re-pricing date, without prepayment. For mortgages, a dedicated prepayment model is used, where prepayment depends upon the remaining interest period and is calibrated regularly using realised historical prepayments. On-demand retail savings are treated like overnight deposits. All cash flows are discounted by applying a swap curve plus the appropriate credit spread curve. Table 27 shows the interest rate sensitivity from an economic perspective for euro, dollar and sterling. For the other currencies the interest rate risk is minimal. The impact of a larger interest rate movement (parallel shock of plus or minus 100 bp) is shown in table 28.

Table 27: Interest rate sensitivity at 31 December 2008

IN EUR THOUSANDS	BPV			Total
	Trading	Mismatch	Banking	
EUR	-89	19	38	-32
USD	-13	-329	67	-275
GBP	0	0	49	49
Other	1	1	-1	1
TOTAL	-101	-309	153	-257

Table 28: Effect of an interest rate shock on economic value at 31 December 2008

IN EUR THOUSANDS		
Interest rate shock	-100bp	+100bp
EUR	1,810	-4,434
USD	28,996	-26,128
GBP	-5,257	4,656
Other	-2,280	-25
TOTAL	23,269	-25,931

Credit spread risk

Besides interest rate risk, the other important market risk factor for NIBC is credit spread risk. In the context of market risk, this includes the portfolios in the financial markets environment. As a consequence of the de-risking policy overall credit risk sensitivity for the financial markets decreased from -1.156 million EUR/bp at year-end 2007 to -0.429 million EUR/bp at year-end 2008.

Foreign exchange risk

As stated previously, it is the policy of NIBC to hedge its currency risk as much as possible. NIBC uses the Standardised approach for the calculation of regulatory capital for currency risk. At year-end 2008, the capital requirement for FX risk was EUR 3.1 million.



Operational Risk

NIBC's definition of operational risk is based on the Basel II definition. Operational risk is the current or future threat to earnings and capital base as a result of inadequate performance in the day-to-day processing of transactions with clients or other parties (including the settlement of transactions), inadequate procedures and measures for timely detection of control failures, quantitative or qualitative shortcomings in human resources and deficient decision-making as a result of inadequate management information. In addition, reputation and strategic business risk are included as sub-categories of operational risk. For NIBC, both of these risk categories are driven by operational risk components.

The responsibility for monitoring and managing operational risk lies with NIBC's Operational Risk Manager and the business unit manager, who are responsible for implementing the enterprise-wide operational risk framework. The framework sets out the roles and responsibilities for management supervision, as well as those tools and methods used within NIBC for identifying, measuring, reporting, monitoring, and controlling operational risk. Sound Practices for the Management and Supervision of Operational Risk, published by the Basel Committee on Banking Supervision, has been used in the development of the operational risk framework to ensure robust and effective management and supervision. The framework is based on the principle that NIBC's Managing Board and Supervisory Board and senior management are actively involved in risk management, and that NIBC's risk management system is independent, conceptually sound and implemented with integrity. Finally, NIBC needs to ensure that there are sufficient resources available to execute the purpose and strategy of operational risk management and the business units as well as implement control, compliance, and audit functions.

Operational risk is managed at both a group and *strategic business unit (SBU)* level. The Managing Board provides consistency and oversight of significant operational issues, and oversees the adoption of best practice across NIBC. At the SBU level and below, managers are responsible for adherence to the operational risk management policy framework, for oversight of all operational risks specific to the business, and for reporting of all operational events and losses. The Operational Risk Manager, working in conjunction with business unit managers, has developed tools to assist in managing, monitoring, reporting and reducing the effects of operational risk. The tools utilised by managers provide an integrated view of the risk self assessment, control identification, action planning, and event and loss registration. This integrated view assists in identifying, evaluating, and reducing operational risk and planning mitigation measures. The evaluation process assists in identifying emerging operational risk issues and determining how they should be pro-actively managed.

NIBC has sought to build operational risk management into all its business processes. Operational risk is monitored on a daily basis and self-assessments are performed semi-annually. The year-end self-assessment forms the basis for NIBC's In Control Report section of the Annual Report. "In control" reporting seeks to ensure that the operational risk management policy framework is integrated into the daily activities of all employees of NIBC and that it forms an integral part of the internal control system. The reporting system is focused on control of the identified risks related to the operational execution of the different business activities.

The capital requirement under the Standardised Approach is a summarisation of the requirement per individual business line. Within each business line, gross income is the indicator that serves as a proxy for the scale of business operations and as such, the likely scale of operational risk exposure within each of these business lines. The capital requirement for each business line is calculated by multiplying the average gross income for the past three years by a factor assigned to that business line. This factor serves as a proxy for the industry-wide



relationship between the operational risk loss experience for a given business line and the aggregate level of gross income for that business line.

The calculation is used to determine the regulatory capital and the economic capital requirement for operational risk and is performed annually by NIBC's Finance department. Table 29 shows the amount of RWA and the capital requirement for operational risk as at year-end 2008 and 2007.

Table 29: Breakdown of EAD, RWA and capital requirement for operational risk

IN EUR MILLIONS	2008		2007	
	RWA	Capital requirement	RWA	Capital requirement
Standardised approach	704	56	1,065	85
TOTAL OPERATIONAL RISK	704	56	1,065	85



Liquidity Risk

NIBC defines liquidity risk as the inability of the company to fund its asset increase and meet its obligations as they become due, at acceptable cost. One of the cornerstones, therefore, of NIBC's liquidity risk management framework is to maintain a comfortable liquidity position. NIBC was able to maintain its sound liquidity position in the difficult times of 2008 due to the prudent and conservative liquidity and funding policy in the past, as well as by diversifying funding sources. The start of the online retail savings programme NIBC Direct, the start of the covered bond programme and of other secured funding initiatives, as well as a medium-term note issue using the Dutch State's Credit Guarantee Scheme, were the major new funding initiatives undertaken in 2008. In addition, NIBC was able to enhance the *European Central Bank (ECB)* eligible funding capacity that created additional liquidity buffers.

Stress scenario

Based on projections prepared by the business units and reviewed by risk management, and the current asset and liability maturity profiles, a stress tested liquidity forecast is prepared and presented once every two weeks to the ALCO, in order to create continuous monitoring of the liquidity position. This stress scenario assumes a worldwide liquidity shortage in which no unsecured wholesale funding can be raised by NIBC and external sales or securitisations of assets are not possible. In addition, the following assumptions are made:

- In order to maintain NIBC's business franchise, it is assumed that new asset production continues at a level where the current books are maintained constant.
- Conservative assumptions are made for prepayments, callable funding and collateral cash-out flows (payments from CSAs).
- A conservative liquidity buffer is maintained for intraday payments.
- In line with the Annual Report, the stress scenario at as year-end 2008 includes the realised government-guaranteed issue of EUR 1.5 billion in February 2009, but excludes the realised issue of EUR 1.5 billion at the end of March 2009. The latter has improved the liquidity buffers even further.
- A committed liquidity facility that is available to NIBC until May 2009 is excluded.

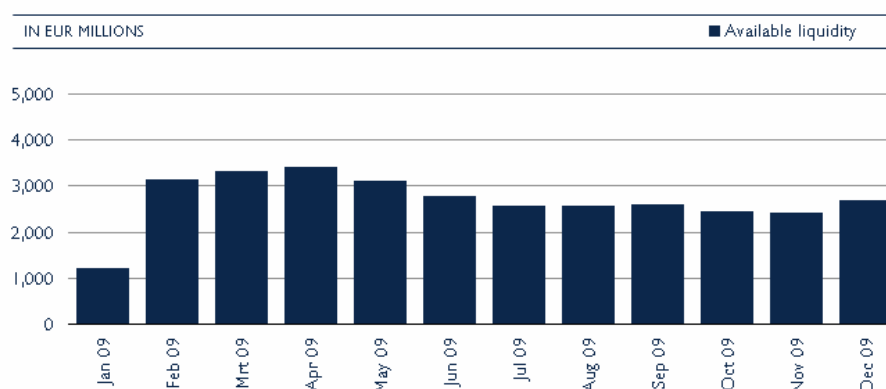
Graphs 3 and 4 show the strong liquidity buffer in the stress scenario. Although this analysis focuses on the next 12 months, the liquidity buffer in the liquidity stress test remains positive for longer periods.

The available liquidity, as presented in the graphs that follow, consists of:

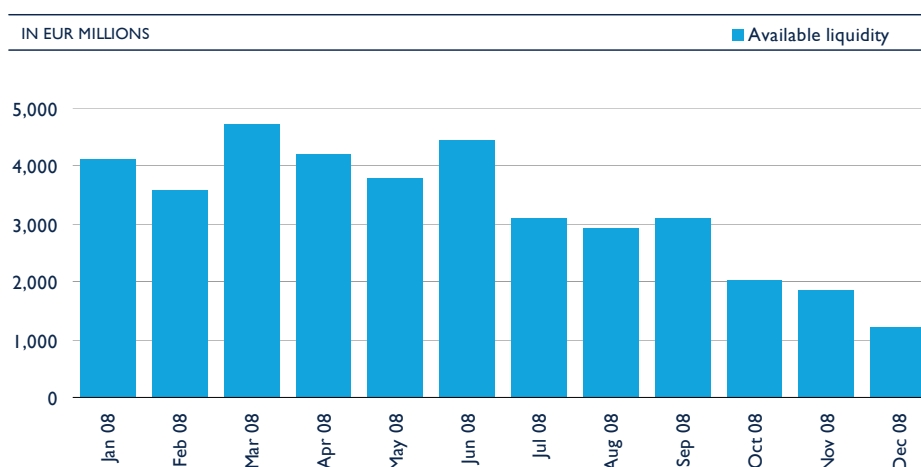
- A projected pool of cash plus collateral suitable for secured funding, minus a buffer for intraday payments, at each month end;
- A reduction to the available pool created by maturing liabilities and other projected outflows (e.g. from new business); and
- An increase in the available pool created by maturing assets, the government-guaranteed issue of February 2009 and April 2009 as well as a conservative estimate of retail funding proceeds in 2009.



Graph 3: Stress scenario, short-term analysis, 31 December 2008



Graph 4: Stress scenario, short-term analysis, 31 December 2007



A comparison of the 12-month liquidity stress test at 31 December 2007 with the test at 31 December 2008 shows that the outcome of the stress test after 12 months is positive in both years. The surplus remains positive after a year of severe liquidity stress.

At the end of 2007, a large buffer of cash and collateral for secured funding was available to cover the relatively high amount of expiring funding in 2008. This expiring funding made the liquidity buffer converge to the current level, in line with the expectations at the beginning of 2008.

In addition to the 12-month liquidity stress analysis above, NIBC also conducts a liquidity analysis over a period of 36 months once every two weeks. This analysis assumes a possible growth in the size of the books in combination with funding initiatives as, for example, certain forms of secured funding. The analysis assumes no ordinary wholesale unsecured funding. The outcome of this 36-month liquidity analysis shows again a comfortable liquidity position throughout the period.

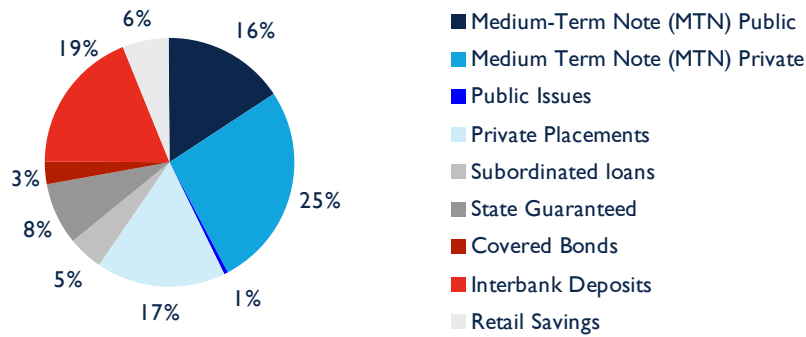
Funding

As a result of the current credit and liquidity crisis, the unsecured wholesale funding markets were closed in 2008 for many financial institutions, including NIBC. NIBC, therefore, further diversified its funding base by the initiatives mentioned earlier.

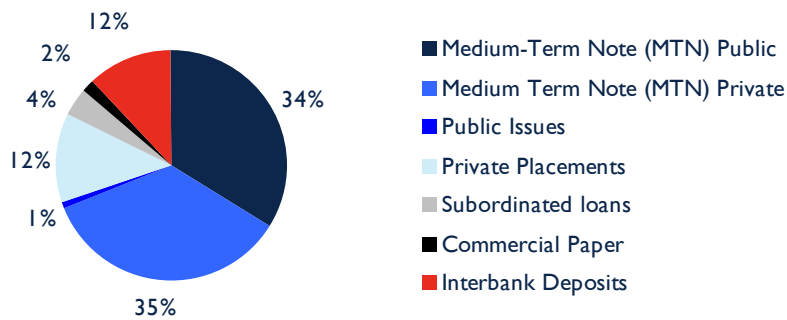


An overview of the funding portfolio as at 31 December 2008 and 31 December 2007 is shown in Graphs 5 and 6 respectively.

Graph 5: Breakdown of total funding portfolio, 31 December 2008



Graph 6: Breakdown of total funding portfolio, 31 December 2007



Securitisation Exposures

Overview and strategy

NIBC as originator

NIBC has been active in the securitisation and structuring market for over ten years. The types of collateral for these securitisations include residential mortgages, commercial mortgages, leveraged loans and structured credits. NIBC's *Dutch MBS* residential mortgage programme was established in 1997. In 2003, NIBC started its North Westerly *Collateralised Loan Obligations (CLO)* programme. In 2004, NIBC became the collateral manager of its first US *Collateralised Debt Obligations (CDO)* transaction. In 2006, NIBC launched its introductory *Collateralised Mortgage-Backed Securities programme (CMBS)* under its MESDAG programme. In addition, NIBC has acted as arranger and lead manager on a number of third-party transactions. Table 30 gives an overview of the cumulative nominal amounts, which are outstanding at 31 December 2008 and of which NIBC was originator:

Table 30: Cumulative nominal amounts of NIBC's securitisations

IN EUR MILLIONS	Traditional originator	Synthetic originator	Total
UNDERLYING ASSET			
Residential mortgages	5,318	813	6,131
Commercial mortgages	2,373	0	2,373
CLO	1,126	0	1,126
TOTAL	8,817	813	9,630

Objectives

NIBC's objectives in relation to securitisation activities are:

- Transfer of credit risk;
- Obtain funding, reduce funding cost and diversify its funding sources;
- Offer its real estate clients access to the capital markets;
- Earn management fees on the assets under management;
- Generate fee income by structuring third-party transactions;
- Earn fees on ancillary roles in securitisations.

Roles and involvement

NIBC has fulfilled the following roles in the securitisation process:

- Arranger (structuring) of both third-party and proprietary securitisation transactions;
- Underwriter in securitisation transactions involving both third-party and proprietary transactions;
- Collateral manager for a number of managed CDO/CLO transactions;
- Swap counterparty for a number of residential and commercial mortgage securitisations;
- Liquidity facility provider for a number of residential and commercial mortgage securitisations;
- Calculation agent and principal paying for a number of residential and commercial mortgage securitisations;
- Company administrator for a number of securitisations;
- Investor in structured credits.



Securitisation activity in 2008

During 2008, NIBC structured a number of asset-backed securities as collateral for collateralised funding purposes. This contributed to NIBC's sources of funding during 2008 in the face of the contracting market for inter-bank lending and the investor base for securitisations. The results of the above transactions are not included in the quantitative disclosures as credit risk transfer with regard to the exposures securitised has not been recognised for the purposes of Pillar-1 capital requirements.

Names of the External Credit Assessment Institutions used for securitisations

NIBC uses Fitch, Moody's and Standard & Poor's to rate its securitisations. Most of the RMBS securitisations are rated by Fitch and Moody's. For the other type of securitisations also Standard & Poor's is one of the rating agencies.

Accounting policy

NIBC consolidates securitisation *Special Purpose Entities (SPE)* in its financial statements when:

- It will obtain the majority of the benefits of the activities of an SPE;
- It retains the majority of the residual ownership risks related to the assets in order to obtain the benefits from its activities;
- It has decision-making powers to obtain the majority of the benefits;
- The activities of the SPE are being conducted on NIBC's behalf according to NIBC's specific business needs so that it obtains the benefits from the SPE operations. Such an evaluation is necessarily subjective.

NIBC does not consolidate SPEs that it does not control.

NIBC as investor

Next to its role as originator of securitised products, NIBC has also been active as an investor in securitised products. Halfway through 2007 NIBC ceased its activities as an active investor in securitised products and started de-risking its structured credits portfolios. Consequently, the structured credits portfolios were transferred from a Trading book approach to a Banking book approach as per October 2007. The US RMBS portfolio was sold in August 2007, while the remaining US structured credits portfolio has been transferred from NIBC Bank to NIBC Holding, also in 2007. The European structured credits portfolio is held by NIBC Bank.

Securitisation exposures at NIBC Bank

Under this heading several overviews regarding the securitisation exposures (retained and purchased) of NIBC Bank are presented, detailing underlying collateral type, credit quality and vintage. The numbers in this section are slightly different from those in the risk notes of the annual report, because:

- Some of the retained notes of own securitisations are included in the structured credits portfolio in the annual report, whereas for Pillar 3 purposes, these should be mentioned separately.
- The IFRS rules for consolidating securitisation exposures may differ from Pillar 3 classifications under the securitisation framework, especially for derivative exposures.

Table 31 provides an overview of NIBC Bank's exposures in structured credits as at 31 December 2008.



Table 31: EAD of structured credits portfolio at NIBC Bank, 31 December 2008

IN EUR MILLIONS	Investor	Originator	Total
RMBS	437	81	518
CMBS	172	153	325
CDO	182	0	182
CLO	0	56	56
ABS	13	9	22
US COLLATERALISED	2	0	2
TOTAL STRUCTURED CREDITS NIBC BANK	806	299	1,105

Credit quality of structured credits portfolio

The credit quality is based on an internal composite, following Basel guidelines, including external ratings from Standard & Poor's, Moody's and Fitch. The non-rated portion of the portfolio relates to first loss positions in both NIBC's own securitisations as well as third party securitisations, which have been marked down to approximately 10% of their nominal value as per 31 December 2008.

Table 32: Rating distribution of structured credits portfolio (investor), 31 December 2008

IN EUR MILLIONS	AAA	AA	A	BBB	Below BBB	NR	Total
RMBS	258	48	59	62	10	0	437
CMBS	85	40	32	8	7	0	172
CDO	82	59	12	13	10	6	182
ABS	4	6	1	1	1	0	13
US COLLATERALISED	2	0	0	0	0	0	2
EUROPEAN STRUCTURED CREDITS	431	153	104	84	28	6	806

Table 33: Rating distribution of retained positions in the structured credits portfolio (originator), 31 December 2008

IN EUR MILLIONS	Derivatives	AAA	AA	A	BBB	Below BBB	NR	Total
RMBS	20	0	0	15	9	21	16	81
CMBS	0	97	2	0	54	0	0	153
CLO	2	30	2	2	1	2	17	56
ABS	9	0	0	0	0	0	0	9
EUROPEAN STRUCTURED CREDITS	31	127	4	17	64	23	33	299

Vintage of structured credits portfolio

NIBC's structured credits portfolio has a fairly favourable vintage with just over 60% stemming from 2005 and earlier, albeit this percentage can differ among collateral classes.

Table 34: Vintage of NIBC structured credits portfolio (investor), 31 December 2008

IN EUR MILLIONS	RMBS	CMBS	CDO	ABS	US Coll.	Total
2007	2	19	33	0	0	54
2006	68	77	35	0	0	180
2005	38	59	24	3	0	124
2004	109	15	72	3	0	199
2003	80	0	9	5	0	94
2002	82	2	9	0	0	93
2001	17	0	0	1	0	18
2000	18	0	0	0	0	18
1999	23	0	0	0	2	25
1998	0	0	0	1	0	1
TOTAL	437	172	182	13	2	806

Table 35: Vintage of NIBC structured credits portfolio (originator), 31 December 2008

IN EUR MILLIONS	RMBS	CMBS	CLO	ABS	US Coll.	Total
2007	17	0	0	0	0	17
2006	0	0	0	0	0	0
2005	40	0	0	0	0	40
2004	0	138	0	0	0	138
2003	24	15	8	9	0	56
2002	0	0	13	0	0	13
2001	0	0	22	0	0	22
2000	0	0	13	0	0	13
1999	0	0	0	0	0	0
1998	0	0	0	0	0	0
TOTAL	81	153	56	9	0	299

Securitisation exposures at NIBC Holding

In 2007 the US structured credits portfolio was sold from NIBC Bank to NIBC Holding. This section gives the characteristics of this portfolio. Tables 36 and 37 present the rating distribution and vintage of the US structured credits portfolio in NIBC Holding as at 31 December 2008.

Table 36: Rating distribution of structured credits US portfolio, 31 December 2008

IN EUR MILLIONS	AAA	AA	A	BBB	Below BBB	NR	Total
US CMBS	0	0	3	9	1	0	13
CRE-CDO	41	43	61	25	12	0	182
STRUCTURED CREDIT US	41	43	64	34	13	0	195

Table 37: Vintage of structured credits US portfolio, 31 December 2008

IN EUR MILLIONS	US-CMBS	CRE-CDO	Total
2007	4	42	46
2006	6	109	115
2005	3	20	23
2004	0	10	10
2003	0	0	0
2002	0	1	1
2001	0	0	0
2000	0	0	0
1999	0	0	0
1998	0	0	0
STRUCTURED CREDIT US	13	182	195



Internal Capital Adequacy Assessment Process

The *Internal Capital Adequacy Assessment Process (ICAAP)* of each institution refers to the process by which risks and related capital are internally measured, allocated and managed, and by which the adequacy of capital available is assessed.

The internal capital requirements of NIBC under the ICAAP are based upon an internal EC framework. In addition to this, NIBC has an extensive framework of historical and theoretical stress scenarios that analyse the impact of severe shocks in the market risk or credit risk environment. The outcomes of these stress scenarios are compared to the available economic capital as well as the calculated economic capital usage.

Economic capital

Economic capital is the amount of capital that NIBC allocates as a buffer against unexpected loss from business activities, based upon its assessment of risks. It differs from Basel II Pillar-1 regulatory capital, as NIBC sometimes assesses the specific risk characteristics of its business activities in a different way than the general regulatory method. Relating the risk-based economic capital of each business to its profit, results in a calculation of its RAROC. Economic capital and RAROC are key tools used in support of the capital usage process. These tools assist in allocating shareholders' equity as efficiently as possible based on expectations of both risk and return. The usage of economic capital is reported once every two weeks to the ALCO. The ALCO resets the maximum allocation level of economic capital to and within each business, taking into account business expectations and our desired risk profile. Economic capital allocation is based on a one-year risk horizon, using a 99.9% confidence level. This confidence level means that there is a probability of 0.1% that losses in a period of one year will be larger than the allocated economic capital.

Economic capital methodology

NIBC uses the business model of each activity as the basis for determining the economic capital approach. If the business model of an activity is trading, distribution, or investment for a limited period of time, a market risk approach is used based upon VaR and scaled to a one-year horizon to calculate the economic capital usage. A business model equal to 'buy-to-hold' or investment to maturity means that a credit risk approach is applied based upon estimations of PD and LGD. For all activities, add-ons for operational risk are calculated. In addition, NIBC allocates economic capital for business risk, reputation risk and model risk on a company-wide level.

The economic capital approach differs from the regulatory capital approach, in which only the Trading book is assigned a market risk approach. Activities that have a business model equal to distribution or investment for a limited period of time are, in some cases, assigned a credit risk approach in the regulatory capital framework due to Basel II regulations or regulatory industry practice. For these business model categories, NIBC applies a market risk approach in the economic capital framework similar to the trading activities, as for all of these activities the market price becomes relevant at a certain point in time. Risks and economic capital are therefore



monitored accordingly.

Furthermore, note that the terminology of portfolios in the economic capital framework differs from the exposure classes on which regulatory capital is calculated in Pillar 1. Table 1 in the chapter on Credit Risk provides a summary of how the various portfolios of NIBC are mapped to the Pillar 1 exposure classes.

The main differences between the economic capital and regulatory capital framework exist for the residential mortgage portfolio, the European structured credits portfolio and NIBC's interest rate mismatch position. Economic capital is determined by a market risk approach for these activities because of their business model. The regulatory capital approach for these portfolios is either included in credit risk (mortgages and structured credits) or not included at all within Basel II Pillar I (mismatch position). As economic capital methodology may differ significantly among financial institutions, it is more appropriate to compare regulatory capital for the purpose of industry comparison of market risk and credit risk exposures.

Economic capital usage

Economic capital is allocated to all business activities in the form of limits set by the ALCO, and the amount of economic capital usage is calculated for each business based on the risk of its activities.

- For the corporate loan portfolio, which uses a major part of economic capital, NIBC calculates economic capital usage using a credit risk approach largely based upon the Basel II regulatory capital formula and an add-on for concentration risk;
- For the debt investments and trading portfolios, residential mortgage portfolio and the interest rate mismatch position, NIBC uses a market risk approach to determine economic capital usage. Economic capital usage for these portfolios is calculated using VaR calculated with four years of historical data and scaled to a one-year horizon;
- For the mezzanine portfolio, economic capital usage is calculated by applying a credit risk approach based upon the Basel II regulatory capital formula; and
- For the private equity investment portfolio, NIBC uses fixed percentages.

The following table shows the economic capital usage per business activity. In its Market Risk Economic Capital calculation, NIBC takes diversification effects into account between credit spread and interest rate risk. Diversification occurs from the fact that not all risks will occur at the same time. Therefore, the sum of economic capital for these market risks on a stand-alone basis will be higher than the amount of economic capital if these risks are combined. This reduction of economic capital is defined as diversification. The economic capital framework does not take into account diversification effects between the different risk categories (credit, market and operational risk).

The diversification effect in the economic capital calculations is higher in 2008 than in 2007. The reason is an increased diversification effect in 2008 between interest rates and credit spreads, as well as the incorporation of a combined market risk VaR framework for residential mortgages and debt investments and trading portfolios. As a result of the latter, diversification effects between these two activities are now measured.



Economic capital per business activity

Table 38: Economic capital usage per business activity

IN EUR MILLIONS	2008	2007	Difference
Corporate loan portfolio	428	518	-17.4%
Residential mortgage portfolio	280	239	17.2%
Debt investments and trading portfolio	274	286	-4.2%
Mezzanine and private equity portfolio	201	151	33.1%
Interest rate mismatch portfolio	122	104	17.3%
Operational and other risk	95	122	-22.1%
Reputation risk	100	100	0.0%
Business risk	100	100	0.0%
Model risk	20	20	0.0%
ECONOMIC CAPITAL USAGE	1,620	1,640	-1.2%
Diversification effect	-295	-158	86.7%
TOTAL ECONOMIC CAPITAL USAGE NET OF DIVERSIFICATION EFFECT AT 31 DECEMBER	1,325	1,482	-10.6%

The changes in the usage of economic capital at year-end 2008 are owed to a variety of factors. The decrease of 17% noted for the corporate loan portfolio was the result of a decline in the size of this portfolio during 2008. On the other hand, the usage of the residential mortgage portfolio increased by 17%. This increase was due to the increased credit spread volatility in 2008. The market risk methodology for these assets is based upon the most advantageous methodology under IFRS. Instead of applying a securitisation exit model based upon RMBS spreads, NIBC now uses an approach based upon the origination spreads of residential mortgages. Furthermore, the economic capital usage of the debt investments and trading portfolios remained relatively stable due to further de-risking of these portfolios in 2008. An increase (of 33%) was also noted for the mezzanine and private equity portfolio due to the growth in the size of these portfolios.

Lastly, the economic capital usage of the interest rate mismatch position increased by 17%, because of an increase in interest rate volatility in 2008.

Stress scenarios

The event risk framework is part of the Pillar II framework for Basel II within NIBC. On a quarterly basis, results of the event risk analysis are presented to the ALCO and to the Risk Policy Committee, providing senior management and the Supervisory Board members with information that can be taken into account in decisions regarding risk appetite. At NIBC, stress scenarios focus on vulnerability testing of portfolios, assessing the impact of extreme events and benchmarking EC calculations. Several scenarios based on both historical events, as, for example, the Asian Crisis or the internet bubble, and hypothetical scenarios as, for example, a severe recession or stagflation, are applied.

Capital Base Components

The capital base, also referred to as regulatory capital, is calculated in accordance with the Dutch legislation and the EU Capital Requirements Directive. The available regulatory capital is based on capital contributed by subsidiaries covered by prudential consolidation accounts, which should without restrictions or time constraints be available to cover risks and absorb potential losses. All amounts are included net of tax charges.

The available regulatory own funds at NIBC are classified under two main categories, Tier-1 capital and Tier-2 capital. The two main components in the regulatory own funds are core equity and subordinated debt. The key terms and conditions of each of these categories are summarised below.

The capital ratio is calculated by dividing the regulatory capital with RWA.

Tier-1 capital

Tier-1 capital is composed of eligible capital, eligible reserve, innovative hybrid Tier-1 capital, and non-innovative hybrid Tier-1 capital after deduction of eligible items.

Eligible capital

Eligible capital consists of share capital, share premium and repurchased own shares (treasury shares) are deducted.

Eligible reserve

Eligible reserve consists primarily of retained earnings, minority interest and net profit from current year. Retained earnings are earnings from previous years. Minority interests reflect the equity of minority shareholders in a subsidiary. Net profit is included after verification by the external auditor.

Non-Innovative hybrid Tier-1 capital

Non-Innovative hybrid Tier-1 instruments are deeply subordinated debt instruments, senior only to Shareholders' Equity. They have an indeterminate duration and a relatively high capacity for loss absorption. These instruments must meet strict rules predefined by DNB.

Innovative hybrid Tier-1 capital

Innovative hybrid Tier-1 instruments are deeply subordinated debt instruments, senior only to Shareholders' Equity. They have an indeterminate duration, but step up calls that could give an incentive to exercise and have a relatively high capacity for loss absorption. These instruments must meet strict rules predefined by DNB.

Deduction from Tier-1 capital

Intangible assets

The deducted intangible assets contains of goodwill.

Securitisation exposures

NIBC has purchased subordinated bonds, which are either non-rated or have a sub-investment grade rating, issued by various securitisation entities. According to the CRD and Dutch legislation, these subordinated bonds are deducted from regulatory own funds. 50% should be deducted from Tier-1 capital and 50% should be deducted from Tier-2 capital.



AIRB provision excess of expected loss

The difference between EL and provision made for the related exposures are adjusted for in the regulatory own funds. The negative difference (when EL amount is larger than the provision amount) is included in the regulatory own funds as shortfall. According to the rules in the CRD and Dutch legislation, the shortfall amount shall be deducted from the regulatory own funds and be divided into 50% in Tier-1 capital and 50% in Tier-2 capital.

Tier-2 capital

The Tier-2 capital is composed of subordinated debt instruments, revaluation reserve after deduction of eligible items. Tier-2 capital includes two types of subordinated debt instruments; perpetual (upper Tier-2) and dated (lower Tier-2) instruments. The total Tier-2 capital may not exceed 50% of the amount of Tier-1 capital and lower Tier-2 capital may not exceed 50% of Tier-1 capital. The limits are set after deductions.

The amount eligible for inclusion in the Tier-2 capital is reduced by 20% per annum if the remaining maturity is less than five years.

Revaluation reserve

Revaluation reserve contains of unrealised gains from equity holdings classified as available for sale and revaluation of property.

Deductions from Tier-2 capital

Securitisation exposures

NIBC has purchased subordinated bonds issued by various securitisation entities. According to the CRD and Dutch legislation, the subordinated bonds are deducted from regulatory own funds. 50% should be deducted from Tier-1 capital and 50% should be deducted from Tier-2 capital.

AIRB provision excess of expected loss

Adjustments are made in the regulatory own funds for the difference between EL and provision made for the related exposures. The negative difference (when EL amount is larger than the provision amount) is included in the regulatory own funds as shortfall. According to the rules in the CRD and Dutch legislation, the shortfall amount shall be deducted from the regulatory own funds and be divided into 50% in Tier-1 capital and 50% in Tier-2 capital.

A summary of items included in the regulatory capital is presented in Table 39.



Table 39: Items included in the regulatory capital of NIBC Holding N.V.

IN EUR MILLIONS	2008	2007
TIER 1		
Called up share capital	1,408	1,363
Share premium	538	177
Own shares (Treasury shares)	-10	-6
Eligible capital	1,936	1,534
Retained earnings	89	96
Net profit	-414	-5
Minority interests	17	11
Eligibles Reserves	-308	102
Deduction of Intangibles assets	-121	-338
Deduction of certain securitisation exposures not included in risk-weighted assets	-16	-28
Deduction excess of expected losses over impairment allowances	-39	-25
Deductions from Tier 1 capital	-176	-391
CORE TIER-1 CAPITAL	1,452	1,245
Innovative hybride Tier-1 capital	130	136
Non-innovative hybride Tier-1 capital	229	220
TOTAL TIER-1 CAPITAL	1,811	1,601
TIER-2		
Qualifying subordinated liabilities		
Undated loan capital	0	6
Dated loan capital	268	302
Revaluation reserve		
Equity investments	15	51
Propert	23	23
Deduction of certain securitisation exposures not included in risk-weighted assets	-16	-28
TOTAL TIER-2 CAPITAL	251	329
TOTAL REGULATORY CAPITAL (capital base)	2,062	1,930

Capital Adequacy

The capital adequacy of NIBC is managed at NIBC Holding level.

The principal ratios for reviewing the capital adequacy of NIBC are the Tier-1 ratio and the BIS ratio. These ratios, which were implemented by the *Bank for International Settlements (BIS)*, are intended to promote comparability between financial institutions. They are based on the Basel II Accord.

NIBC monitors developments in the ratios on a monthly basis, including comparison between the expected ratios and the actual ratios. These ratios indicate capital adequacy to mitigate on-balance credit risks, including off-balance sheet commitments, market risks, operational risks and other risk positions expressed as risk weighted items in order to reflect their relative risk. During the year ended 31 December 2008, NIBC complied amply with the capital requirements imposed by the Dutch Central Bank, which require a minimum Tier-1 ratio of 4% and a minimum BIS ratio of 8%.

Capital ratios

The Tier-1 ratio is defined as Tier-1 capital divided by RWA.

The BIS ratio is defined as Total Capital (which is the sum of Tier-1 capital and Tier-2 capital) divided by RWA.

The Tier-1 ratio increased to 16.7% (2008, actual) and the BIS ratio increased from 13.7% (2007, pro forma) to 19.0% (2008, actual).

The following tables show the summary of capital ratios, capital requirements and RWA for NIBC.

Table 40: Capital ratios of NIBC Holding N.V.

	2008	2007
IN EUR MILLIONS	Basel II Actual	Basel II Pro-forma
CAPITAL RATIOS		
Core Tier-1 ratio	13.4	8.8
Tier-1 ratio	16.7	11.3
BIS ratio	19.0	13.7



Table 4I: Breakdown of EAD, capital requirements and RWA of NIBC Holding N.V.

IN EUR MILLIONS	2008			2007		
	EAD	RWA	Capital requirement	EAD	RWA	Capital requirement
CREDIT RISK	19,789	9,667	774	23,714	11,294	904
AIRB APPROACH						
- of w hich corporates	7,687	4,346	348	9,645	5,387	431
- of w hich retail	4,780	624	50	3,739	774	61
- of w hich equities	582	2,148	172	571	2,100	168
- of w hich securitisations	1,300	735	59	1,532	277	23
STANDARDISED APPROACH						
- of w hich sovereigns	1,466	1	0	1,458	0	0
- of w hich institutions	2,512	743	59	4,547	1,071	85
- of w hich corporates	638	638	51	1,179	1,179	94
- of w hich equities	38	38	3	144	144	13
- of w hich retail	690	298	24	826	289	23
- of w hich other	96	96	8	73	73	6
MARKET RISK		145	12		1,001	80
- of w hich trading book VaR		100	8			
- of w hich trading book Standardised approach		0	0		876	70
- of w hich FX Standardised approach		45	4		125	10
OPERATIONAL RISK		704	56		1,065	85
Standardised approach		704	56		1,065	85
ADJUSTMENTS FOR TRANSITION RULES		346	27		774	62
Add on Basel I floor		346	27		774	62
TOTAL (including Basel I floor)	19,789	10,862	869	23,714	14,134	1,131

Appendix 1

Scope of Application

NIBC financial consolidation scope is based on IFRS, which is determined in accordance with IAS 27 Consolidated and Separate Financial Statements, IAS 28 Investments in Associates, IAS 31, Interest in Joint Ventures, and SIC 12 Consolidation Special Purpose Entities.

Subsidiaries are all entities (including special purpose entities) controlled by NIBC Holding N.V. Control exists when the company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The existence and effect of potential voting rights that are currently exercisable or currently convertible are considered when assessing whether the company controls another entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

NIBC applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Minority interests in the net assets and net results of consolidated subsidiaries are shown separately on the balance sheet and income statement.

A joint venture exists where NIBC has a contractual arrangement with one or more parties to undertake activities typically, though not necessarily, through entities that are subject to joint control. The Group's interests in jointly controlled entities are accounted for by proportionate consolidation. NIBC combines its share of the joint venture's individual income and expenses, assets and liabilities and cash flows on a line-by-line basis with similar items in NIBC's financial statements.

Associates are those entities over which NIBC has significant influence, but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Except as otherwise described below, investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

With effect from 1 January 2007, all newly acquired investments in associates held by the venture capital organisation within the operating segment Merchant Banking, which is considered to be a venture capital organisation, as that term is used in IAS 28, are designated upon initial recognition as financial assets at Fair Value through Profit or Loss. These assets are initially recognised at fair value and subsequent changes in fair value are recognised in the Income Statement in the period of the change in fair value.



Tables 1-5 present the entities that form part of the capital base of NIBC Holding N.V.

Table 1: Group principal undertakings included in the capital base

Subsidiaries of NIBC Holding N.V.	Voting power	Domicile	Consolidation method
NIBC Bank N.V.	100%	Netherlands	Purchase method
NIBC Investment Management N.V.	100%	Netherlands	Purchase method
NIBC Investments N.V.	100%	Netherlands	Purchase method

Table 2: Principal undertakings of NIBC Bank N.V. included in the capital base

Subsidiaries of NIBC Bank N.V.	Voting power	Domicile	Consolidation method
NIBC Bank Ltd	100%	Singapore	Purchase method
BV NIBC Mortgage Backed Assets	100%	Netherlands	Purchase method
Parnib Holding N.V.	100%	Netherlands	Purchase method
NIBC Foreign Debt Fund XIII B.V.	100%	Netherlands	Purchase method
Counting House B.V.	100%	Netherlands	Purchase method
NIBC Principal Investments B.V.	100%	Netherlands	Purchase method
Vredezicht 's-Gravenhage 110 B.V.	100%	Netherlands	Purchase method

Table 3: Principal investments of NIBC N.V. in associates included in the capital base

Associates of NIBC Bank N.V.	Voting power	Domicile	Consolidation method
De Nederlandse Participatie Maatschappij voor de Nederlandse Antillen N.V. *)	100%	Netherlands	Equity method
PE Express I B.V., Breskens	37,5%	Netherlands	Equity method
PE Express II B.V., Breskens	37,5%	Netherlands	Equity method
PE Express III B.V., Breskens	35%	Netherlands	Equity method
PE Express IV B.V., Breskens	35%	Netherlands	Equity method
Welke Beheer B.V., Hoorn	25%	Netherlands	Equity method

*) In view of the control exercised by the government over the policy of NIBC's wholly owned associate De Nederlandse Participatie Maatschappij voor de Nederlandse Antillen N.V., this company has not been treated as a subsidiary.

Table 4: Prudential filter: subsidiaries treated as associates included in the capital base

Subsidiaries of NIBC Bank N.V.	Voting power	Domicile	Consolidation method
GRW Reinfurt GmbH	100%	Germany	Equity method
NIBusker Holding B.V.	75,0%	Netherlands	Equity method

Table 5: Joint Venture of NIBC Bank N.V. included in the capital base

Joint Venture of NIBC Bank N.V.	Voting power	Domicile	Consolidation method
SR-Hypotheek	50%	Netherlands	Proportionate method



Appendix 2

List of Abbreviations

ABS: Asset-Backed Securities
AIRB: Advanced Internal Ratings' Based (approach)
ALCO: Asset & Liability Committee
ALM/MR: Asset & Liability Management and Market Risk department
BIS: Bank for International Settlements
BPV: Basis-point Value
CCF: Credit Conversion Factor
CCR: Counterparty Credit Risk
CDO: Collateralised Debt Obligations
CDS: Credit Default Swap
CFIF: Credit Fixed Income Funds
CLO: Collateralised Loan Obligations
CMBS: Collateralised Mortgage-Backed Securities
CRM: Credit Risk Management department
CRO: Chief Risk Officer
CSA: Credit Support Annex
DA: Distressed Assets department
DNB: Dutch Central Bank
EAD: Exposure at Default
EC: Economic Capital
ECB: European Central Bank
ECC: Engagement and Compliance Committee
EL: Expected Loss
FX: Foreign Exchange
IC: Investment Committee
ICAAP: Internal Capital Adequacy Assessment Process
IFRS: International Financial Reporting Standards
IMA: Internal Model Approach
IRS: Interest Rate Swaps
ISDA: International Swaps and Derivatives Association
LGD: Loss Given Default
LTiMV: Loan-to-Indexed Market Value
NHG Guarantee: Dutch government guarantee
OTC: Over-the-Counter derivatives
P&L: Profit & Loss account
RAROC: Risk-Adjusted Return on Capital
RC: Pillar-1 Regulatory Capital
RL: Realised Loss
RMBS: Residential Mortgage-Backed Securities
RMC: Risk Management Committee



RP: Risk Policy department
RWA: Risk Weighted Assets
SBU: Strategic Business Unit
SPE: Special Purpose Entity
SREP: Supervisory Review and Evaluation Process
PD: Probability of Default
PECDC: Pan-European Credit Data Consortium
TC: Transaction Committee
VaR: Value-at-Risk

