

FINAL TRANSCRIPT

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PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and welcome to the Swedbank's Q3 Interim Report from January to September 2008 conference call. My name is Louise. I'll be your coordinator for today's conference. For the duration of the call you will be on listen only. However, at the end of the call you will have the opportunity to ask questions. (Operator Instructions).

I'm now handing over to Jan Liden to begin today's conference.

Jan Liden - Swedbank AB - President & CEO

Thank you very much and good afternoon. I would try -- I will try to go through quickly a few slides, which we also showed during our presentation this morning. And if I start with the slide number three, there is a kind of summary of this -- of the situation right now.

We have a stable net interest income. We do also have negative valuation effect as a result of this financial crisis and turmoil. The net profit is actually for the first nine months a little bit higher than they were for the first months last year, which was the best result we have achieved, and it comes from net interest income, who has -- which has increased by 15%. Net commission

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income has decreased by 7% and that is mostly the fees that are related to equity, like mutual funds and brokerage that has gone down.

Then we have our subject of net gains and losses on financial items who this quarter actually had a very negative deviation. But if you look upon it on a three quarter perspective, it has decreased with the 15%, but this quarter was quite a negative deviation.

Loan losses net, that is the provisions less the recoveries and plus the write-offs, have increased during the period in totality to SEK1.5 billion. More than half of that comes from the Baltic banking operation, which now has a figure of SEK820 million -- 23 million and in Swedish banking it's SEK307 million.

And that -- I think there are a few slides in our presentation material that is trying to illustrate the weaker economic outlook that we see ahead of us. And it is very clear that we do see the beginning in the Nordic countries of a downturn in the economic cycle, which I think should be taken seriously.

In the Baltic countries there is a difference between the countries, but it's definitely so that both Estonia and Latvia technically are in recession, and the situation is somewhat better in Lithuania. Also, in the countries where we have small operations, like Russia and Ukraine, you have a financial situation which is somewhat in turmoil. So I think it's obvious that we are now facing a more difficult period ahead.

As a result of that, of course, if you look at slide number seven, we are now focusing very much on credit quality and efficiency; efficiency in our work streams and procedures to increase our productivity; and on credit quality to be very proactive with customers who might experience problems; and also, of course, be very, very professional -- or keep on being very professional in the new issues of credit. That goes for the Nordic countries, with Sweden ahead and also, of course, in all the three Baltic countries.

In Ukraine and Russia our expansion is slowing down and we are prioritizing infrastructure, competence, education, training and support systems implementation. So it will be a slower growth where we prioritize quality before the rapid expansion.

If we look at the funding markets, slide number nine, we have experienced a situation -- we, as a financial community, have a very difficult situation -- or a more difficult situation, since the experience with the file for bankruptcy of Lehman Brothers. And what you -- the capital market has almost dried up in terms of money markets and commercial paper.

We have had lower volumes in covered bonds and senior unsecured bonds. So, there is a small trail of new issuances. It is also so that it has been improved the last few -- the last period and that is seen that -- you can see that has spread between mortgage bonds and the government items. We have signs of increased trading and I think that is the fact -- the consequence of the introduction of the European package, followed by the Swedish version of supporting activities for the financial sector.

During this year, and also next year, you can see on Slide 10 that our funding activities are going well, both for Swedbank AB, which is the parent company, essentially everything except the Swedbank Mortgage portfolio, and then Swedbank Mortgage. As you, I'm sure, remember half of our portfolio -- lending portfolio, is Swedish real estate, which is in this portfolio, which is now financed -- refinanced by covered bonds.

And you see perhaps in this slide that we have issued as much as we should have, and we have a little bit left to do this quarter. Next year the volumes for refinance, we think, is a little bit smaller. Now this funding, for instance in Swedbank Mortgage of SEK25 billion this quarter, we are in -- the last quarter. We have, as up to now, financed 10 of these. So, I think we are getting back to a little bit of a more normal situation.

Deposits from the public is also a very important source for our refinancing and during this last period, that is mid-September to the beginning of October, we have had outflows of deposits. And those outflows have mainly gone to more secure products, or more perceived secure products, like interest rate funds and T-bills, and things like that.

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We have also had a flow of customers who have taken part of their savings, those who are exceeding the current guarantee for deposits, and taken those money to other banks. We have also received a lot of customers who have done the same thing when they are customers in our bank.

However, the net result of all these activities has led to that our deposit volume for the period has lessened by SEK5 billion. Though if you look at the change from the beginning of the year, we still have an increase of 7% or SEK22 billion. The same situation is also the fact for the Baltic countries, where we have also an increased activity of the first nine months, but a decrease in the last few weeks. The Swedish situation had a very clear rebound, so the last 10 days we have had a positive net gain in terms of deposit volumes.

If you look at the slide number 13, there is -- we have titled that slide like liquidity stress test, and that is a kind of theoretical example showing you what is the picture right now if we cannot fund ourselves anything more. And then you see that we have a lot of liquidity, of course, right now and if we don't add on to that it will, of course, decrease over the months to come. We still think that this is quite an assuring slide that sees that we are -- in the case of this theoretical situation that we were not able to fund ourselves anything more, we still have a lot of liquidity reserves.

What we think is, of course, that the funding situation for all banks, including the Swedish ones and including us, will improve when the Swedish support package will be implemented, as we have been told, should happen early next week. That program is divided into two parts; first of all a guarantee program, which will support lending facilities -- or borrowing facilities or funding facilities, like commercial paper and bonds. And the second is also a fund, who should -- which should be developed in order to be a source for injecting capital in banks who come into that need.

We think that these suggestions are very positive but, as you all know, the devil is in the detail and we need to see them before deciding how and how much we will use these facilities. In -- and for avoiding mistakes, we will all be a part, as I understand, to building up this fund. So that we know for sure, that we have to invest in.

The slide number 15 is also a reminder, if you like, about situation we have for our Company, the lending structure. If you see there the Swedbank, which is, as I said, about half of our total lending portfolio, that is totally funded through the capital market with bonded CP programs. That has functioned well. The rest of the fund facilities is, to a large extent, covered by deposits and to a remaining capital market programs and equity. But when you look at the whole Company and try to get a grip of the loan to deposit ratio, you have to see this picture and remember how we do finance the mortgage portfolio in Sweden.

Then if we go to slide number 17 and look at the credit quality. I have first a slide about the Swedish banking and you see it is low. You see on the upper graph it's the impaired loans, which is still low; a little bit higher than the end of last year, but still on very low levels.

And at the lower graph on slide 17 you see the net losses; that is the new provisions, the write-offs and thus the recoveries. And there you see we come from quite an abnormal situation where we actually had a net recovery on the provision side and now are looking at the small, but nevertheless, the increasing part of new provisions, still I think low levels.

On slide 18, you see a further confirmation of the good quality in the Swedbank Mortgage portfolio, where you see practically nothing in -- both in terms of impaired loans and definitely not needed provision.

Then if you look to the slide 19, you see there an illustration of the situation in the three Baltic countries. And if you look at the upper slide there, to the left, you see that the impaired loans are increasing quite substantially over the quarters. The bars reflect the nominal numbers and the graph or the line represent the percentage. And, as you see, from the third quarter, the third quarter's result was 1.45% related to this lending volume.

And then you see at the lower graph, you see how we are, as a Company, responding to that by adding new provisions in order to be prepared to handle future problems. And in figures you see to the right, that we're actually now at this quarterly figure

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of point -- 85 basis points and we think -- and you see the distribution between the different countries. And we are now, if you look at the nine month perspective, at 62 basis points.

And we think that what we guided you earlier by saying that we think we are going to land at about 70 basis points for the whole of 2008, that is still an accurate forecast. We have also said that we think that 2009, we think it will come to 120 basis points.

However, taking into account the worsened economic situation, both in the Baltic countries and also internationally, we think that we have to -- or that the detailed analysis that we constantly are reviewing, might have to be revised. However, today we have no new number for you. We are still at the 120, but we'll constantly be back to you about it.

One final remark perhaps is that if you look at the same slide and you see the yellow bars that is the actual losses that we have experienced, the write-offs. So when you look at these bars, you see the provisions we are taking; that is the preparation for future problems, which we are, of course, trying to avoid as much as possible, but still we want to do prudent provisions.

There has been a lot of discussion regarding also Lehman Brothers' exposure. You see that on slide 21.

And what we had was two kinds of exposure. Number one, we had a normal bond issued by Lehman Brothers, and we had two derivatives, and -- which was an exposure to Lehman Brothers in the range of approximately [SEK202] million. Those, we think as a consequence of them filing for bankruptcy, we have provisioned 80% of, so SEK169 million are taken as a provision in the Swedbank market's result.

The other exposure was a much bigger bridge loan financing for real estate that we had with Lehman Brothers. That was when they filed for bankruptcy, in total \$1,350 billion. This has been a long functioning vehicle and they have used us, as I said, as a bridge financing source.

As a collateral for these findings, we have a number of loans -- loan agreements with different counterparties. They are 69 mortgage loans, and they are in their turn collateralized by 52 commercial real estates. It's quite a big geographic diversification and also in different asset classes. And they are also in a different way completed.

And what we have done since we have experienced this event with them filing for bankruptcy, we have done a lot of on site due diligence and dialogue with all the relevant parties, and we can now confirm that the value of the collateral is as we think it is; that is well in excess of the loans.

We have reserved the right to mortgage loans and associated cash flow, and we have already seen that that is happening. That is the interest rate payments and amortizations are now going directly to us. And we think that -- and, of course, going through this with the external auditors, that there's presently no need for any provisions in this case.

If you then directly go to slide 24, you see our breakup on the different business areas, and what I think, as perhaps I have said that earlier, reports like this, what is I think very assuring is the strong result we have in all the business areas.

Swedish Banking continues to have little change in the total income, but they are suffering from reduced fee incomes due to the equity linked revenues. They are able to keep their expenses at the same level, and they experience a slightly higher loss level, and still coming in at operating profit of almost SEK6.2 billion, which is, I think, during certain circumstances, very good.

Baltic Banking is, I think, even more impressive, because they have managed to continue their revenue increase and also the cost increases are very much controlled and also, in this P&L, are able to absorb the increased losses and after that show as good a result as they did the first nine months last year, even slightly better.

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International Banking is also performing very well and that is mostly Russia and Ukraine for -- which is still small in financial terms, but they are developing according and ahead of plan, and, as I said, we are now looking at a consolidated business, so we can -- until we can see what is really happening in this market.

Asset Management is going down, because they have not increased their costs, but the revenues are decreasing and that is again due to the equity linked revenues coming from the mutual fund.

So I think what is good, as I said, is that as we have a very strong result in most cases. I didn't talk about Swedbank Markets. I should have done that.

Swedbank Markets has endured problems during this quarter, but if you take away their revaluations of some SEK270 million and the one time, I hope, credit loss they experienced from this exposure to Lehman Brothers, it's still quite a good result. So the core business of Swedbank Markets is still -- it's still performing very well.

And with that, I think I maybe should stop a moment for Mikael to talk about some future slides -- some figures.

Mikael Inglander - *Swedbank AB - CFO*

Yes, thank you very much and let's go then directly to slide number 26 and the income statement, just a few short remarks. And as Jan already has mentioned, the income has increased substantially between the nine months this year comparison with '07.

I'll get back to NII commission income and net gains and losses in detail later on, but under other income, I'll just remind you of -- that we have some one-offs in 2008 and that's the divestments of branches and also divestment this quarter over SPS Insurance sellers, PKK the previous quarter, which adds up to SEK601 million of one-offs in comparison with one-offs of SEK40 million during 2007.

The costs have increased, not as much as the income, but still -- and I think it's important to underline that we have now -- for the full nine months have included our Ukrainian business, where we also have invested. That is the main reason for increasing costs, but also under other expenses, the write down of their brand name of Hansabank, which we have started, which is also a SEK63 million cost.

If we go down to the next line of loan losses, I think it's important to just remind ourselves of what it contains. So, it's a dramatic increase and then there are some confusions I've heard about, is it re-loan losses and write-offs? And it's important to underline here that the majority of the increase between the years is provisions for anticipated losses and the write-offs are a smaller part of the increase and that also goes for this quarter, which I will go back.

Tax is slightly down; with the tax rate, it's 21% in comparison with last year's 22%, and that is a refund of previous taxes and also taxes from tax exempt income, which we have had for this year, which leads us to an actual increase between '07 and '08, even if it's not more than 1% it's still going in the right direction.

If we then turn to the next page of 27, just a few remarks regarding the differences between quarters; I would like to point out one important thing when it comes to costs, and that is reminding of that we had in the second quarter a decrease of bonus reserves in the Baltic Banking operation with SEK185 million, which is a one-off event but, of course, pushes down the second quarter costs. And also that shows that we have an even higher increase if you make the comparison also taking that into account between Q2 and Q3.

Loan losses, as I stated earlier, out of the SEK812 million, more than SEK700 million is provisions and the rest is net write-offs.

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If we then continue to page 27 -- sorry, page 28, and break down all the NII in Swedish Banking. There's a few comments I would like to make. First of all, we have now seen for the first quarter of many in a row with increased lending margin in Sweden and that is, I would say, a trend change, and we hope it continues. We have slightly higher volumes as well, which has been positive. And we also have decreased deposit margins, which is as we have already earlier quarters informed about that. We have an overflow from low yielding accounts to better yielding accounts, which is a natural effect. And the majority of the deviation between quarters is under the item of other changes.

There we have the effect stemming directly from the mortgage company within Swedish Banking. And it's due to the fact that we have increased our liquidity. We have bought back bonds in advance, and that is also to increase liquidity and the maturity of the funding profile.

We also have a product, which we are -- today we have started closing down from one week ago, and that is the short-term [based] rates for part of the portfolio in Swedbank Mortgage, which is a variable good rate and we have a mismatch effect, which is quite substantial because of the volatility in the funding markets and the way we calculate that product. And therefore, we will close it down and -- but the cost will still remain as long as the customers keep that product.

If we go to the next page of 29, and there we have the breakdown of Baltic Banking and their NII. Volumes have increased slightly between quarters with 1%, which is positive. We have a pressure on net lending margins. That is mainly a factor of increased funding costs. We have a good discussion with customers, but there is a lag effect still, which we foresee to continue for a period.

Going down further on, exchange rates has been positive from an accounting perspective, since the Swedish krona has depreciated against euro, which has been positive for both deposits and lending.

Regarding in the deposits, we also have seen increased margins and that is two effects. First of all, that's domestic interest rates have increased the base rates. Half of the increase of the SEK83 million is due to the fact that we have seen a lowered fee for the deposit guarantee in Estonia. But all in all, it has been a positive development between quarters.

Turning to net commission income, slide 30, a few remarks there; payment continues to go up. That is due to the fact that we have attracted larger volumes. There is still a price pressure, but that has been mitigated by the volume growth.

Brokerage and Asset Management, has, of course, suffered from the bad stock market development, which has been down between Q2 and Q3 with 12%. That affects both Brokerage and Asset Management fees.

Corporate Finance is normally a low income during the third quarter, a seasonality effect taking into account, so that we have a [number] season, but also lower activity in general. And hopefully, that will turn the other way around during the fourth quarter. That remains to be seen. Still a slight decrease, so given the circumstances, we think it's still quite a strong development.

If you then turn to page, which is net gains and losses on financial items, there we have tried to break down all the different effects from the different business areas in that income line.

If we start with Swedish Banking, there you can see it is a volatile income line, and we have an effect which is negative due to the turbulence in the financial markets, which also have affected the hedging we are using to cover for [low] interest rate exposure in Swedbank Mortgage.

Baltic Banking slightly down, or down between quarters; it's still positive, but there we also have valuation effects in the liquidity portfolio and the trading assets, but also lower trading activities as such.

International Banking, there we have effects on the hedge account, in efficiencies between ruble and US dollar, and US dollar [rivne] and SEK, currency exchange rate, which has affected us negatively for this quarter.

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Swedbank Markets, there we have valuation of the credit portfolio, which is, as you can see, more than the whole negative figure. Again due to the turbulent financial markets, that is nothing we can do about. The trading has also been a little bit lower than we normally see.

Then if you go down to Shared Services and Group Staff; that is an effect where we already in second quarter said we will change the accounting rules of accounting the derivatives used for cover, the interest rate exposures between parent company and subsidiaries when we fund subsidiaries from the parent company.

We have changed the accounting method already and we said it will be reduced to zero which it's also is, as you can see here. But there is, of course, a strong volatility between quarters since it was very positive the second quarter; negative in the first quarter; now it has vanished but it's, of course, a large explanation to the downturn between the second quarter and the third quarter.

Expenses on next slide, again, I would like to remind you of what has been done in Baltic Banking. The expenses here, as you can see, has gone up between quarters. If you take into account what we did the second quarter of decreasing here the bonus reserve of SEK185 million, it's an actual decrease between quarters with 5%, and that also goes for the next item of staff cost in Baltic Banking, which has then if you make that calculation gone down with 8%. So it's definitely going in the right direction as Jan already has stated.

The last picture I would like to comment shortly is then our key figures and the return on equity which is lower this quarter.

We have financial targets for our return on the equity, which should exceed the average of our peers. And so far, looking at the first three quarters this year, we have a return on equity of 17%. And the peers, which has reported in Sweden, we have at least beaten them. We will see about DnB NOR and Danske next week, but we have achieved what we have as a target.

We also have achieved, when it comes to the cost income ratio, most of the long term target, which is being below the 0.50. We are at 0.50, so there is a way to go still. And our capital ratio is in line with what we have as a financial target, which is 8.5% to 9% and we are at 8.7%. If we look at the current transition rules, we have a slight increase between quarters of one or 10 basis points, up to 6.8%.

I am there and leave over to you Jan.

Jan Liden - Swedbank AB - President & CEO

Well thank you. Just to take on where Mikael finished, I also during the presentation this morning in Swedish mentioned the fact and reminded everybody that there has been interviews in the Swedish media, where people have been talking to the main shareholders of Swedbank; that is Swedish Savings Bank Foundations. And in that interview and statement, they stated that they are looking into possible capital injections. And I wanted to also say that that is being done and I confirm that such discussions are going on, but no decisions are made.

We have no other information to give, but I think it's prudent to also remind everybody about that when we now show, in our ways of thinking, a very strong report, because I think if you look at slide number 34, in spite of the fact that we have to be very cautious when we look at the future in terms of economic development, we still, for the first nine months of this year, have a very stable platform in terms of a very robust result. And that is very positive.

They have also been affected negatively by valuation effects. And that is, of course, not desirable but that is the fact. Hopefully these valuation effects will neutralize in the future. There is adequate liquidity of reserves, in spite of the fact that the funding markets are difficult for all [entities]. And we hope that newly released information about the state governed package of -- including guarantees, and building up funds, will ease that situation.

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So I think I should end there, and invite you to questions.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). We have a question coming through from the line of [Chintan Joshi]. Go ahead, Chintan.

Chintan Joshi - Nomura - Analyst

Hi, good afternoon. Two quick questions, one on your interest-bearing securities; you have stated that 81% of that is valued by theoretical models. I just wanted to know what the composition of that SEK81 billion is, and why it is that it's being modeled -- it's being valued by model and not by mark to market.

And second question on covered bonds. If I look at the covered bond prices over the last month, month and a half, there seems to be a premium, Swedbank and SEB bonds seem to be trading at 20, 22 basis points premium to Handelsbanken. I'm just wondering how this will impact your margins, especially given that you have a lot of covered bonds maturing over the next 12 months. Thank you.

Jan Liden - Swedbank AB - President & CEO

Well, thank you. I'll try to respond to your first question -- sorry to your second question, and maybe ask for some assistance for the first. The covered bond price is exactly as you have observed. They are a little bit higher for some of us, and the next biggest operator on the Swedish market, Handelsbanken, has more a advantageous pricing on covered bonds.

We think that the impact so far is very little, because the issuance of covered bonds lately is quite small, because the liquidity in the market has not been there. And on the short [tenure] funding, we have actually all of the operators more or less the same price. If that difference would prevail in the future, that would, of course, hurt us. But I don't really think that there is a rationale for [the differences] in pricing. They -- these are from all the institutions covered bonds. They are separated from everything else. They are triple-rated. So when the market comes back to a more normalized situation, I think that these differences will disappear. Then the impact will be nothing in terms of differences between the institutions.

As of your first question, regarding the interest-bearing securities, at least I can start telling you that there are different kinds of assets, like real estate or mortgage-backed securities; that is real estate-backed securities or bonds. It is also other kinds of bonds from other institutions, and we use them all, of course, as a liquidity reserve. But maybe you should say why the difference? Why we have 81% valued the way we have, that was your question?

Chintan Joshi - Nomura - Analyst

Yes.

Unidentified Company Representative

And this is Mr. (inaudible), who is Head of the Finance Department in our Bank.

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Unidentified Company Representative

And the reason is that the markets have not been very active. So even though there are prices, there has been very little trading done at these prices, and for that the reason when we looked on our portfolio, we felt that they were not really possible to use, since the market has not been active. And for that reason, such a large percentage of the portfolio has been marked according to a model, and this is primarily done credit bonds, but also some on the mortgage bonds and so on have been marked according to a theoretic model. Whereas, of course, Government bonds and Treasury bills, they are very easy to mark to market.

Jan Liden - Swedbank AB - President & CEO

And of course you understand that this is --

Chintan Joshi - Nomura - Analyst

Can I --?

Jan Liden - Swedbank AB - President & CEO

Sorry for interrupting, but this is also a very sensitive discussion, or delicate discussion, with everyone, including our external auditors. And we have been discussing back and forth, and, together with them, arrived at what we have been doing.

Chintan Joshi - Nomura - Analyst

Can you give me the size and composition of what you are marking to model?

Jan Liden - Swedbank AB - President & CEO

Sorry, please, again, there was a small disruption here.

Chintan Joshi - Nomura - Analyst

Sorry, can you give the size and composition of what you are marking to model?

Jan Liden - Swedbank AB - President & CEO

Mr. --?

Unidentified Company Representative

Well, it's 81%.

Chintan Joshi - Nomura - Analyst

You said RMBS bond from financial, bonds from other institutions, so what is (inaudible) --?

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Jan Liden - Swedbank AB - President & CEO

You mean the distribution between the different kinds of assets that we have done? That's what you mean?

Chintan Joshi - Nomura - Analyst

Yes, yes,

Unidentified Company Representative

I don't have the exact numbers available right now, but --

Chintan Joshi - Nomura - Analyst

And the total portfolio size, then?

Unidentified Company Representative

The total portfolio size is roughly SEK100 billion.

Chintan Joshi - Nomura - Analyst

Of which 81% is mark to model?

Unidentified Company Representative

Correct.

Chintan Joshi - Nomura - Analyst

Okay, so this is RMBS bonds from other financial institutions, or things like that?

Unidentified Company Representative

Correct.

Chintan Joshi - Nomura - Analyst

Okay. Thank you.

Jan Liden - Swedbank AB - President & CEO

Thank you.

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Chintan Joshi - *Nomura - Analyst*

Yes.

Operator

Thank you. Our next question comes from the line of Geoff Dawes from Fox-Pitt Kelton. Go ahead, Geoff.

Geoff Dawes - *Fox-Pitt Kelton - Analyst*

Thank you, Geoff Dawes here from Fox-Pitt Kelton. I've got two questions, hopefully pretty brief and straightforward. The first one is going back to the funding issue. Now, you mentioned that you do not expect the situation to prevail, but currently it's quite a big issue, given that front-book mortgage margin's around 50, 60 basis points, and I believe the gap is around 25 basis points. So it's something that could be quite painful. If it does prevail, how would you intend to offset that? Will it be through pricing, maturity management, or fund and mix?

The second question is, if I look at the Baltics, you mentioned an NPL deterioration, mainly in real estate and in private individuals. Can I just comment -- or can I just ask what the increase in private individual NPLs is driven by, given unemployment is very low in the Baltics still, it hasn't really responded to the recession as yet; so two questions; first of all on funding, second of all Baltic NPLs. Thank you.

Jan Liden - *Swedbank AB - President & CEO*

Yes, I left you Mr. Raasuke, Erkki Raasuke, to answer the second question. The first question, I think, we will use all the measures you mentioned, if we find ourselves in the situation that this price differentiation will prevail. But on the other hand, I think that when markets do stabilize, I don't really see how that can be. But all the things that you mentioned, we will, of course, use that, if it comes to that. But I'm still pretty optimistic of things returning to normal.

And then Erkki should try to answer why the increase in NPLs on -- in private individuals.

Erkki Raasuke - *Swedbank AB - Head of Baltic Banking*

Yes, first of all, the official statistics of the unemployment is probably lagging somehow behind, because the changes in employment market, what we're observing on pretty much daily basis are telling us something differently. We also have been reporting by ourselves, and we don't think that we are any faster or slower than the rest of the market; that within the last -- well, less than six months, we have been reducing our workforce also more than 5%, 10%, about 5%, and this trend is continuing.

Secondly, is also overall in the Baltics, it's quite standard that in many areas that there is a partly significant -- or it's partly significant, part of the day is variable. And obviously, economy deteriorating, we see that this part of day has been reduced.

Thirdly, it -- the overviews are concentrating towards -- to the certain subs of the people are borrowers. It's people who have been working in construction, people who have been close to the real estate development, etc.

And fourthly, also, there is one group also, which does not come up very quickly in terms of unemployment; that is small sized entrepreneurs by themselves. So they also have been -- obviously have been hurt. It's a very sensitive part of the population, and also the group of the borrower.

So without ability to be more precise, these are basically the four drivers in it.

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Geoff Dawes - *Fox-Pitt Kelton - Analyst*

That's very clear, thank you.

Jan Liden - *Swedbank AB - President & CEO*

Thank you.

Operator

Thank you. Our next question comes from the line of Derek De Vries from Merrill Lynch. Go ahead, Derek.

Derek De Vries - *Merrill Lynch - Analyst*

Yes, I have a few questions. The first question relates to the Ukraine, and given the de-rating your shares have suffered from the Baltics, I would have thought you would have been very cautious in the Ukraine, and yet your quarter on quarter loan growth, currency normalized, I think is 19%.

So my question is; why are you still expanding so quickly? What cost of funding are you charging to the Ukraine? Are they getting group funding rates, or do you have a significant country-risk premium there? And do you think the Ukraine lending is really such a good opportunity, given what's going on there?

The second question, and I apologize, it's a bit of a detailed question, but every quarter, right below the cash flow statement, you give us this turnover of own debt instruments, and I've always assumed it was your market-making business. You show us issued and redeemed, but in the redeemed, it's a pretty big number this quarter. So maybe you could just give some clarity on what that is? It's on page 35 of your press release this time. And I'm just wondering, the SEK220 billion redeemed, why that's such a big number, given I wouldn't have thought there was a lot of market-making going on?

And then, my third question, third and final question, comes back to your comment that covered bond spreads are going to return to parity once the credit markets normalize. And I understand that all these covered bonds are AAA-rated, but I would have assumed as an investor, given the choice between buying a covered bond that's AAA-rated from an AA-rated entity, as opposed to an A-rated entity, I would have thought the rational investor would buy it from an AA-rated entity. So -- and given your rating downgrades from Moody's and S&P, why are you so confident that you'll go back to parity once the credit markets normalize?

Jan Liden - *Swedbank AB - President & CEO*

Well, I'll try to start to answer two of the questions. The first one, regarding Ukraine, yes, we are charging them a higher funding cost than we do for others, but that is our internal governance model, which we don't reveal, but it's higher.

The growth in the Ukrainian market is much higher now than actually our growth is, and we are monitoring very closely the quality of credit we are issuing, and hopefully we are doing the right thing. And so far, we have. But as we also stated, we are now entering quite a turbulent time, and we are being more cautious and conservative in terms of growth than we were before. And still, you have to remember that the numbers in financial terms are fairly small for the Group as such.

When it comes to your last question, regarding covered bonds, yes and no; I would say, the whole idea about covered bonds, is to isolate them, very clearly, making them very transparent in terms of collateral, and information about it, making them independent in the way that they are as instruments, rated as such. So I'm not totally with you that you should prefer a covered

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bond from one institution compared to another, because, I think, the whole idea about the covered bonds is actually to make them independent in that sense. If this difference prevails, which I hope and don't think it will, it's still quite an opportunity for a debt investor to have a nice return on an investment buying that covered bond with that higher margin, or higher price; so, yes.

As it comes to the redeemed -- I hope Mikael has tried to formulate an answer to your question there.

Mikael Ingländer - Swedbank AB - CFO

Yes, and then it's correct, the redemptions are larger than the new issued bonds, and you also have a difference in increased deposits and borrowings from the public, if you look at the same page. And that is due to [repo] activities with the National Debt Office, and the Swedish central banks.

Derek De Vries - Merrill Lynch - Analyst

Okay, so this is related to your funding, not so much your market making here, it's actually -- that's fine, I get then. Okay, thank you very much.

Jan Liden - Swedbank AB - President & CEO

Thank you.

Operator

Thank you. Our next question comes from the line of Per Gronborg from Danske Market. Go ahead, sir.

Per Gronborg - Danske Market - Analyst

Yes, good afternoon. Three questions; the first two are partly inter-related. Solvency, you're now talking about rights issues vehicle vis- -vis earlier this regain in the Swedish press. If you look at your solvency ratios, they look pretty okay, if we look at the Basel II figures. If we take into account that you have now got -- or most likely got some guarantee from the Government, how does the situation look today compared to the situation two weeks ago, where we were reading in the papers about a potential run on Swedbank? And how necessary is a rights issue taking into account the guarantee?

My second question is on the Swedish Mortgage book. When I do the math on your figures from your mortgage company, it looks like the average margin has dropped down to the very low 30s. Can you comment on that?

And finally, on the Baltics, I can now see that you have higher margins on deposit than you actually have on lending in the Baltics. What are the situation competitive-wise in the Baltics? And will you be able to retain this extremely high deposit margin in the Baltics? Thank you.

Jan Liden - Swedbank AB - President & CEO

Yes, thank you. First, the question about solvency; first of all, I think it's important to mention that that discussion is going on. Secondly, no, I don't think there has been a talk about the run to Swedbank. We have seen some pretty irresponsible news articles, but I don't really -- haven't seen any signs of that. So that is out of the question.

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I think that the Government package is good, if it becomes, as it is tried. But again, devil is in the detail. Now, we'll see in the beginning, or during the weekend, when the details come out, but the way I presume and look at it, and knowing at least the stated ambitions for this package, that is to facilitate the capital market to start to function in a better way again. I think this will be a good thing for all operators, including us.

When it comes to the core one, the thing that also you as the financial community or analysts have started to look at is the core one capital ratio. I think it is fair to say that we, in our discussions with the regulator and the FSA, have agreed that our capitalization is enough, looking at our IRB models, now and in the -- for the future plans. However, if you take into account that we are moving -- we have a moving target, in the sense that it's not good enough to be good or enough. We have to be as good as our competitors, or even preferably better, also in the dimension of core one. We have to understand and accept that.

And thirdly, it is also the case that we are now going into worse times, into a downturn in the economic cycle. And if you understand the new IRB models, you will know that there is quite the leverage there. So if you have a migration in risk clauses, you will see quite rapidly an increase in risk weighted asset, which will require more capital. We are not at all there. We just want to be very proactive.

Per Gronborg - Danske Market - Analyst

Can I add in one question? Your current Basel II risk weighted assets are they based on one-time assumptions, or are they based on over the cycle assumptions? I assume it's the latter.

Jan Liden - Swedbank AB - President & CEO

Well, to give you a vague answer, I don't like to do that, but I think it's somewhere in between.

Per Gronborg - Danske Market - Analyst

Okay.

Jan Liden - Swedbank AB - President & CEO

So, that is the way we have done it. But again, that is the reason we're discussing that.

When it comes to your question regarding the mortgage and the margins, again, if you look at it in detail, you see that we have an increased cost during this quarter for securing the liquidity. And that is essentially a mismatch on the tenures, where we have a lot of loans issued at a variable rate, and where we have funded ourselves at the difference, in this case, a three months' tenure, and that has given a negative result for us. And we did it, of course, because we wanted to be extra-careful, and hopefully that will also, over time, disappear.

Then, about your question about lending in the Baltics, wasn't it?

Per Gronborg - Danske Market - Analyst

It was lending and deposits margins in the Baltics.

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Jan Liden - Swedbank AB - President & CEO

Deposit margins, sorry, yes; please Erkki?

Erkki Raasuke - Swedbank AB - Head of Baltic Banking

This always happens when the base rate is moving higher. So, we're actually gaining the margin in the Baltics. If we look to the deposit structure in the Baltics then, out of the total deposits, about EUR10.8 billion, there is EUR6.1 billion are demand deposits. These are the deposits which are short-term, but they are at the very lower or at no cost. So, basically, when the base rate is moving higher, which it has done over the third quarter, we gain the margin there.

Per Gronborg - Danske Market - Analyst

And there are no prior -- no indications of any price initiatives by competitors on the demand deposits, or are this money that just are extremely [sticking], regardless of [rising]?

Erkki Raasuke - Swedbank AB - Head of Baltic Banking

That's a very good question. It's that you don't really move the Tessa with the pricing. But also, what we have been communicating is that, due to the very same reason, what Jan was already covering of the unfortunate press, as well as the rumoring, we also have witnessed some loss of the deposits in the Baltics, and then it has been a different issue than the pricing really. Pricing doesn't move these deposits at all. There are different reasons to make them move.

Per Gronborg - Danske Market - Analyst

Okay. Thank you.

Operator

Thank you. Our next question comes from Rodney Alfven from Cheuvreux. Go ahead, Rodney.

Rodney Alfven - Cheuvreux - Analyst

Yes. Thank you very much. I just have a short question your costs in the Baltic where you now are starting to take down a number of staff. Can you just give us a feeling about what's the end plan, so to say? How many staff do you plan to keep? And how much more cost savings can you do?

And then also, when it comes to salaries, given that a large part of your salaries is variable, do you think that you actually can lower the cost per employee?

Jan Liden - Swedbank AB - President & CEO

Before Erkki responds to the details, I just want to make a statement that we are not initially looking at costs isolated. We are looking to produce a result, a performance, and to find the optimum in every time, point in time, to generate that profit. And that's why we are very, very, I think, dynamic in the sense and when we look at investments and costs which can generate revenue. So, you will never hear from us that we isolate costs and talk about that. We will adapt costs to our business generation capacity.

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But I think you had some detailed questions which deserves the answer from Erkki.

Rodney Alfven - *Cheuvreux - Analyst*

Okay. Thanks.

Erkki Raasuke - *Swedbank AB - Head of Baltic Banking*

Yes. The number of the people has been reduced, and will continue to reduce due to the two reasons. One thing; that there is less of the new business origination, which is that our distribution capacity, some of that has been left unused, and then we'll reducing that. And, secondly, now already for about year-and-half, we're doing -- running smaller programs of improving the efficiency and making operations more lean one area after another. And also, these exercises are giving us opportunity to reduce the people.

Eventually, it's really the end state will be very much determined on what the market, or what the new issuance, as well as the business volume's going to be. If they drop further, if they become negative, we will react accordingly. And I think also what comes to the productivity improvement, and this is -- and that is really the never-ending story, is that, overall, the Baltics, as a market, have a significant capital [to the] Continental Europe, in terms of the productivity, there are many areas to improve.

We, in terms of the monthly personnel costs, also generated revenues; we are standing pretty well actually through our Eastern European peers as well as to the Nordic banks. But this is the -- it does not end anywhere. There is not a particular goal. We would run -- we today run less than 40 our cost-income. If we could do that at 20, we would definitely try to do that.

Jan Liden - *Swedbank AB - President & CEO*

Yes.

Rodney Alfven - *Cheuvreux - Analyst*

Okay. Thank you.

Operator

Thank you.

Rodney Alfven - *Cheuvreux - Analyst*

And -- sorry, and the cost per employee?

Erkki Raasuke - *Swedbank AB - Head of Baltic Banking*

We don't think that the cost per employee will really go down. No, I don't think so.

Rodney Alfven - *Cheuvreux - Analyst*

Okay. Thanks.

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Operator

Thank you. Our next question comes from the line of Johan Ekblom from Merrill Lynch.

Johan Ekblom - Merrill Lynch - Analyst

Hi. It's Johan Ekblom from Merrill Lynch. Just a few quick questions. First of all, in terms of coverage levels on your NPLS, we've seen a quite a dramatic reduction, it's down at 73% on a Group level, and maybe more significantly, 58% in the Baltic operation. What level -- given the collateral you have on your loan book, etc., what level of coverage would you see as the minimum? At what point would we have to see a dramatic increase in provisionings?

Secondly, just quickly coming back to Ukraine, you said that the market was growing very quickly in Q3. Having said that, September was, clearly, a very difficult month in Ukraine, and October, I believe, has started in a similar fashion, and I think volume growth is expected to slow dramatically. Could you give us some -- an update on what you are seeing currently, and what we should expect in terms of the deceleration in growth in Q4 and going forward?

And then, maybe lastly, on the costs in the Baltics, I just want to see if I understood you correctly. You said that if we add back the bonus reversal from last quarter, there was actually a decline in costs. Does that mean that the tax or the VAT recovery in Russia was actually not booked in the Baltic division, because I can't seem to make the numbers add up then? Thank you.

Jan Liden - Swedbank AB - President & CEO

Why don't we start with the last question and Erkki give you a comment about the cost in the Baltics.

Erkki Raasuke - Swedbank AB - Head of Baltic Banking

Yes. The cost decline in the Baltics is a result of the two things. One thing is, yes, the reduction of the people from one hand, but, secondly, there is a certain seasonality affect always in the third quarter. So, please, please take that one out as well. Do not take that as currently as a very strong trend to be continued.

Mikael Ingländer - Swedbank AB - CFO

No. And the Russian operation is part of the figures in International Banking, so it's not part of Baltic banking as a business area.

Jan Liden - Swedbank AB - President & CEO

And your question also regarding the net provision -- NPL numbers, and also the provision rate in the Baltics. You had a question whether how low we can go, as you said. And, first of all, I think it's important to remember that we are in the IFRS mode, which makes us move from collective provisions towards very individually-targeted provisions. And we are in a transformation phase here.

The thing that is very good about that is, of course, to see if we, in all markets, Sweden, Nordics and the Baltics, are doing the right kind of provisions, and time will tell. I have full confidence that when you look at the individual portfolios in the Baltics, given the relative high quality of these, I am of the opinion that we have done a prudent provisioning. But, please, if you want to comment further now the -- my friends here think I stated the truth in that sense.

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So, we don't really have, or I don't really have, a number for you how low can we go, because this is a very dynamic thing. We shall be enough provisioned. We are a Company, who has always been conservative on that, and we will continue to be conservative.

Now, you had a third question, yes, about Ukraine, about the guidance for the growth in that market. No, I think it's quite a volatile market in Ukraine. I think the statement you did yourself, that it will decelerate, it will be slower, is actually very true. But I think it's also very hard to predict the outcome the next few quarters. So, we will play along. We will be conservative. We will concentrate on productivity and quality, and we will see what that takes us.

Johan Ekblom - Merrill Lynch - Analyst

Maybe if I just could come back very, very quickly to --first to Ukraine. I realize it's hard to make any predictions here but, clearly, I think there was a dramatic deceleration with that it was experienced. Several of your competitors there have stopped opening branches, and have hiked rates to the extent that they're signaling that they're no longer lending at all. Do you have similar plans, or do you still have your branch expansion plan in place, etc.?

And then on the coverage service, I believe that after Q1, when you were at 104%, you indicated that -- I think someone asked if half that level would be sufficient, and I think the answer then was a clear no. Should we still expect that provisions, given the counter-cyclical, can continue to fall, but that sort of 50% could be some kind of floor?

Jan Liden - Swedbank AB - President & CEO

No. I really can't answer you there, because I don't know the outcome in respect this relations profit, net provisions, the NPLs, regarding the impaired loans. I think it's very hard for me to give you a figure there, because now we're looking at another methodology. Still, you can be assured, and I think we have an extremely good track record there, to be prudent in our provisioning.

When it comes to Ukraine, I think we are one of the operators you refer to. We have increased deposit rates to attract deposits. We have also increased the lending rate. We are not expanding the way we did before. We are much stricter now in our credit analysis of new issues. And we're following and monitoring the situation very closely. That does not mean that we're -- which I think is the worst thing you can do if you want to be a good bank in a society. But we are monitoring the situation closely, so it will -- we are also slowing down our growth.

Johan Ekblom - Merrill Lynch - Analyst

Excellent. Thank you very much.

Jan Liden - Swedbank AB - President & CEO

Thank you.

Operator

Thank you. Our next question comes from the line of Aaron Ibbotson from Goldman Sachs. Go ahead, Aaron.

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Aaron Ibbotson - *Goldman Sachs - Analyst*

I'll try to be very brief. I've just got two short questions. In Ukraine, what percentage of your book is local currency and what is FX lending?

And two, in the Baltics, what is the time lag between somebody stop paying on their mortgage and you having reposed and sold the house? Obviously, anecdotally, I've heard it's over a year, so I just wanted to clarify that. Thank you.

Jan Liden - *Swedbank AB - President & CEO*

Thank you. That was clear questions. Could Erkki start with the last one, please?

Erkki Raasuke - *Swedbank AB - Head of Baltic Banking*

Yes. In the Baltics, the loan is in default after the 90 days of late payment. If it does get then the default is provisioned by the defaulting loan provision level, and it moves on over into the hands of [foreclosure] unit if it has not already happened earlier, but after the 90 days that this is happening. Now, further is that that is the process really of the foreclosure actually is working out, it can be very quick, provided if that there is -- the client is also cooperative on that and we can succeed with the sale.

Also, there can be the case whereby the client can question the price at what we actually want to sell that, or at what the level of the price the bailiff is going to put that onto the market, client can actually claim that. That can go into the Court and decide, and either it's in our favor or client's favor. It can be put then back into the market, and that, basically, theoretically, subject to that if there is a bad will from the client side so, he or she eventually is going to be loser out of that, that actually can be also dragged on.

It is true that in some of the cases, we have been there in the process for more than 12 months. There is also is that there is more evidence is that it's rather, actually, rather quicker. But I think that, also going more into the process, we actually have gone through really small amount of the foreclosures as at today. So, we are -- we just need to monitor on how the things will develop, and also then react accordingly.

Aaron Ibbotson - *Goldman Sachs - Analyst*

And, sorry, just a very quick follow-up, Erkki. And what's your loss given default estimates? And how have they compared to reality when it comes to these foreclosure procedures?

Mikael Inlander - *Swedbank AB - CFO*

If I may comment on that, we have, in three Baltic countries, a different downturn loss given default levels used for risk-weighted assets calculation. They are in the range of 20% -- a little under 20%. Currently we're using provisioning rate of 20% for defaulted mortgage loans, meaning every loan over 90 day overdue will get a 20% provision rate.

Erkki Raasuke - *Swedbank AB - Head of Baltic Banking*

But, once again, Aaron, what you said is how they compare into the current is that we are in the beginning of the foreclosure process. And, so far, is that the true outcome has been, clearly, much more positive, but we should not read too much out of that.

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Jan Liden - *Swedbank AB - President & CEO*

Yes. So, and your second question, regarding the distribution of the lending portfolio in terms of currencies, the general remark is -- well, I'll leave it to you, Mikael, to tell them about euro, dollars, and [rivne].

Mikael Inglander - *Swedbank AB - CFO*

Yes. And the majority is denominated in dollars. It's 68% of the loan book. 60% of the assets by dollars, and then, 29% in [revne], the local currency, and the remaining two on that was the loan book. The remaining two is euro denominated.

Aaron Ibbotson - *Goldman Sachs - Analyst*

Okay. Thank you.

Operator

Thank you. Our next question comes from the line of Per Lofgren from Morgan Stanley. Go ahead, Per.

Per Lofgren - *Morgan Stanley - Analyst*

Thank you very much. I have one question left, and that relates to the Swedish Government's stability plan that you mentioned show up -- showed here in a slide. My understanding was that you said here, Mr. Liden, that you were generally positive to this plan. However, the devil is in the details, as you expressed it. What you are generally positive to, does that include the stability fund of the SEK50 billion also, or is it just the guarantee part?

Jan Liden - *Swedbank AB - President & CEO*

Well, we were correct. I said what you said I said. I am -- what I was thinking of was, of course, the guarantee program for different borrowing facilities, or refining facilities, which I think is good, provided they are priced and administered in a robust and simple way, which I think and hope they will be.

When it comes to the fund, I'm a little bit more, well, schizophrenic in that sense, because I think it's good that you have a fund. I think it's good that the Government makes provisions for necessary capital injections if it comes to that for system critical operators in the financial community.

I think, as an operator, that it looks like it's going to be very expensive for us as operators. If you do the quick math on this, it will mean that we have to pay something like a big bank, something like SEK700 million a year in financing this fund. And I think that is quite a high price, if I'm to be honest. But I think, as a phenomenon, I think it's good that they do provide these funds.

Per Lofgren - *Morgan Stanley - Analyst*

In your view, being very tied into the local markets and so on, I'm just thinking about this fund here. It feels like the regulator has been behind the curve for a long time, and now lately has stepped up very quickly, with the 50 basis point rate cut coming today. If this proposal is -- if it's approved on Monday, do you think it's likely that they will act using it as soon as possible?

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Jan Liden - Swedbank AB - President & CEO

Yes. I think it's likely, because that's what everybody wants them to do. And since, as you understand, of course, that as with all the banks, including myself, have been in daily contact with these authorities, the national debt office, the central banks, the department of finances, we know that the politicians want it to happen quickly. I think there are very experienced people who are put in charge of these operations. Yes, so I am quite optimistic about the implementation capacity.

Per Lofgren - Morgan Stanley - Analyst

And that implementation that is made as soon as possible would also include this stability fund, right? That is your view?

Jan Liden - Swedbank AB - President & CEO

I would assume so, yes.

Per Lofgren - Morgan Stanley - Analyst

All right. Those were my questions. Thanks a lot.

Jan Liden - Swedbank AB - President & CEO

Thank you.

Operator

Thank you. (Operator Instructions). We have no further questions coming through, so I'll hand back to your host to wrap up today's call.

Jan Liden - Swedbank AB - President & CEO

Well, thank you very much for listening in, and for all the interesting questions, and thank you for today.

Operator

Ladies and gentlemen, thank you for joining. You may now replace your handset.

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