Swedbank

INFORMATION TO CLIENTS REGARDING THE CHARACTERISTICS OF, AND RISKS LINKED TO UNSECURED BANK BONDS, CALLED SENIOR BONDS

As a client, you must be aware that:

- Trading in senior bonds takes place at your own risk
- You must find out about and have a good understanding of the special statutory regulations that apply to senior bonds and of the terms and conditions (including the loan agreement) for the senior bond in which you invest and its characteristics and risks
- You must find out about and have a good understanding of the type of institution that the issuer of the senior bond is
- You are responsible for monitoring changes in the value of the senior bonds in which you have invested
- You must regularly assess your investments and make the necessary changes in order to adapt these to your investment strategy and risk profile

Senior bonds – in general about their characteristics and risks

A senior bond is an unsecured interest-bearing financial instrument and is thus a claim that has not fallen due against the issuer, which will normally be a bank or other institution that is subject to the capital adequacy requirement regulations and other financial legislation. The senior bonds referred to below are those issued by banks <u>but the same will apply to bonds issued by other financial institutions and investment firms that are covered by the same provisions of the Norwegian Financial Institutions Act.</u>

Both commercial banks and savings banks can be an issuer ("**Issuer**") of senior bonds. The objective of issuing this type of bond is to finance the banks' general lending activities.

According to the Norwegian Bankruptcy Act, debt settlement proceedings or bankruptcy proceedings cannot be instituted in relation to a bank. A crisis-hit bank will be subject to authority-controlled administration or liquidation and separate crisis-management regulations are applicable[1]. The purpose of these regulations is to ensure that a crisis-hit bank can continue important parts of its operations or be liquidated <u>without the Norwegian state having to contribute funds to the bank</u>. In other words, the holders of senior bonds cannot assume that the Norwegian state has provided an implicit guarantee that banks, including the major banks, will be rescued by contributions of state funds in a bankruptcy-like situation.

[1] Act of 10 April 2015 No. 17 on financial institutions and financial groups, chapter 20

There are two alternatives for crisis-hit banks. Either (1) authority-controlled crisis management or (2) authority-controlled liquidation. A crisis-hit bank will be liquidated unless it is in the public interest to "crisis manage" it in accordance with the special rules that apply to crisis management.

The statutory provisions governing crisis management authorise Finanstilsynet (The Financial Supervisory Authority of Norway) to among other things forcibly write-down unsecured senior bond debt or convert it into equity in the bank. This provision adds new risk elements to senior bonds that come in addition to the risk elements that apply in general to bonds. For further information on the general risk relating to bonds, read the risk memo entitled: *"Information to clients regarding the characteristics of, and risks associated with, financial instruments"*.

If a crisis-hit bank is liquidated according to the regulations governing authority-controlled liquidation, holders of senior bonds have priority over owners of equity instruments (shares or equity certificates), contingent convertible securities (CoCos) and subordinated loans, but have priority after deposits. If the bank has in addition issued senior "non-preferred" bond loans, these will also have priority after an ordinary senior bond loan.

<u>The following risk elements follow from the regulation of senior bonds:</u>

- It is uncertain whether a crisis-hit bank will be dealt with according to the regulations governing authority-controlled crisis management or the regulations governing authority-controlled liquidation.
- The legislation and other regulations may be amended after a senior bond has been issued, and this may directly affect the senior bond's characteristics and risks. The Ministry may also issue regulations granting banks exemption from the rules in the Bankruptcy Act, Enforcement Act and certain parts of the Dispute Act. Because any amendments to the regulations may affect the senior bond's characteristics and risks, any such amendments to the regulations in themselves comprise a risk that the senior bond's characteristics and thus risks may change.

<u>The following risk elements follow from the way in which the crisis management of banks is regulated</u>

- The new order of priority as from 1 January 2019 means that deposits from private individuals and the SME market have priority over all other unsecured obligations. This means that if a bank is subject to crisis management, any loss incurred by unsecured bond holders may be higher than it would have been according to previous regulations.
- The potential losses incurred by investors in senior bond debts may differ depending on whether the institution has issued instruments that qualify as senior non-preferred debt.
- Finanstilsynet (The Financial Supervisory Authority of Norway) can write down the value of outstanding senior bond debt to zero or convert outstanding amounts into ordinary shares or other equity instruments.
- Finanstilsynet can order the bank to stop paying interest.

- The bank's assets may be transferred to a bridging bank or sold, which may result in the bank having a limited opportunity to meet its payment obligations.
- The term to maturity of and interest on senior bonds may be changed and payments can be suspended for a certain period.

Other risk elements during the crisis management

- The liquidity in the secondary market for senior bonds may be sensitive to changes in the financial market.
- Participants in other liquidity arrangements, such as repurchase agreements (repos) to which the bank is a party, may risk having to sell senior bonds at a substantial discount compared to the agreed price.
- Holders of senior bonds may be entitled to compensation if the amount they receive after a liquidation that takes place according to the crisis-management regulations is less than the amount they would have received following normal insolvency proceedings. The payment of any such compensation may take place far later than the agreed maturity date for the senior bond.