



NORDIC  
INVESTMENT  
BANK

FINANCING  
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# Risk Appetite Statement

Adopted by the Board of Directors of the Nordic Investment Bank  
on 7 June 2022 with entry into force as of 16 June 2022



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# RISK APPETITE STATEMENT

## 1 INTRODUCTION

As the international financial institution (IFI) of the Nordic and Baltic countries, the Nordic Investment Bank (“**NIB**” or the “**Bank**”) has a public policy mandate to promote productivity and benefit the environment of the Nordic and Baltic countries. The constituent documents (e.g. the Membership Agreement and the Statutes), the Bank’s internal policies, mandate framework, rules and guidelines create the overall framework for the Bank’s risk-taking. The Risk Appetite Statement (“**RAS**”) complements these key documents by outlining the main considerations in the Bank’s risk-taking, risk mitigation and risk avoidance.

The Bank’s risk appetite is set annually by the Board of Directors with the goal of aligning risk-taking with the statutory requirements, strategic business objectives and capital planning. The Board of Directors and the President have key roles in the implementation of the Bank’s risk appetite by steering the utilisation of different forms of financing, the Bank’s geographical operating areas and markets, and funding and liquidity management. They also monitor NIB’s adherence to the RAS, and make necessary changes to capture changes in the Bank’s strategic priorities, operating environment, and risk profile.

The purpose of the RAS is to state clearly the general principles for the Bank’s risk-taking, to raise risk awareness across the organisation, and to guide the staff regarding accepted and unacceptable behaviour. The RAS is implemented through the Bank’s operational policies and procedures, monitoring metrics, limit system and internal controls. The RAS is thereby embedded in the Bank’s core processes and affects the operations of the Bank in a holistic way.

The qualitative statements in the Bank’s RAS are complemented with a set of key risk indicators (KRIs) and their respective monitoring thresholds (see Appendix 2). The purpose of the indicators and thresholds is to support the evaluation whether the Bank operates within its risk appetite. The feasibility of the KRIs and thresholds is reviewed annually to take into account potential changes in the underlying factors of the RAS.

## 2 OBJECTIVES

Due to NIB’s legal status, national banking legislation does not apply to NIB, nor it is subject to direct supervision of any supervisory authority. Similarly to other IFIs, NIB does not require a banking licence for its operations. NIB monitors international regulations and standards and adopts those that it identifies to be relevant and represent best practice. This principle also applies to the Bank’s risk appetite framework.

The objectives of the RAS are the following:

- To provide a clear articulation of the Bank’s risk-taking, risk mitigation and risk avoidance, and to define the risk-taking at the aggregate level. The RAS creates a foundation for effective communication of risk among internal and external stakeholders.
- To increase understanding of NIB’s material risk exposures and raise risk awareness across the organisation.
- To positively impact the defined risk culture of the Bank.
- To support the Board of Directors and the senior management in planning, formulating and executing strategic business decisions to achieve the long-term targets of the Bank.

- To provide means for the Board of Directors and senior management to engage in discussions on risk-taking, risk management, and business strategy, and their interlinkages.
- To provide tools for the Board of Directors and senior management to continuously monitor and align the Bank's actual risk profile with the risk appetite.

### 3 MISSION, STRATEGY AND OPERATING MODEL

NIB finances projects that enhance productivity and the environment of the Nordic and Baltic countries. NIB adds value by providing long-term loans and guarantees to its clients as a complement to other sources of financing.

The Bank's risk-taking is primarily in its core activity of lending to governments, public sector entities, municipalities, corporations and financial institutions in the member countries. Furthermore, the Bank supports its clients in their efforts to grow and gain access to new markets by also financing projects located outside the member countries.

NIB finances its activities through equity and by issuing bonds on the international capital markets. The funding base is diversified across currencies, maturities and geographic areas. NIB's operating model relies on its ability to obtain funding at a favourable cost, which enables long-term lending, on attractive terms, to its clients. NIB's funding advantage builds on its sound financial profile and strong shareholder support (the member countries). This has enabled the Bank to maintain the highest possible credit rating (AAA/Aaa) from international rating agencies.

To support its lending and funding operations, the Bank maintains a portfolio of liquid assets. The primary objective of the liquidity portfolio is to ensure that the Bank is able to operate and continue its core activities even during stressed market conditions. The composition and maturity profile of the liquidity portfolio are aligned with this objective.

### 4 HIERARCHICAL STRUCTURE OF KEY ELEMENTS

The RAS sets the tolerance for risk-taking in NIB's operations within the Bank's risk-bearing capacity. Risk limits and risk profile assessment are other key elements in the implementation of the Bank's risk appetite framework, as illustrated in Figure 1.

**Risk-bearing capacity** is defined as the financial and non-financial resources that the Bank has at its disposal. The risk appetite is set to a level within the risk-bearing capacity to ensure that the Bank's risk exposure remains sustainable.

Financial resources consist of the Bank's paid-in capital and reserves (allocations from the profits), together comprising the Bank's equity. NIB's capital position is further strengthened by callable capital, which is subscribed by the member countries but not paid in. Callable capital is an important factor in ensuring the Bank's viability, but it is subject to certain conditions and administrative procedures and is not immediately and readily available. Therefore, NIB does not consider callable capital part of its narrow definition of financial resources. For RAS monitoring purposes, financial resources are measured both excluding and including callable capital, depending on the measure.

Non-financial resources are the skills and competences of the staff, IT systems, internal procedures and control systems. The Bank's risk-bearing capacity builds on a careful customer selection process, project-by-project mandate reviews and a thorough credit-granting process. Therefore, financial resources and robust governance contribute both to maintaining the Bank's competitive position and its strong capital and liquidity position.

The **Risk Appetite Statement** is a written articulation of the Bank's risk-taking, risk mitigation and risk avoidance, taking into consideration the Bank's statutory requirements. It contains risk category-specific statements and forms a tool for the Board of Directors and senior management to guide and monitor the Bank's risk-taking activities.

**Risk limits** are used to allocate the aggregate risk-taking mandate to business lines and portfolios. The main risk limits are established in the Bank's risk management policies and approved by the Board of Directors. The limit system sets boundaries for the accepted level of credit, market, liquidity and operational risk within the established risk appetite.

**Risk profile** assessment aims to ascertain that the Bank's risk profile is within risk limits and consequently within the risk appetite and risk-bearing capacity. Risk profile assessment is a point-in-time evaluation of the level and types of the Bank's risk exposures. The assessment includes an evaluation of the Bank's material risks, like credit, market, liquidity, and operational risk.

At NIB, risks are monitored on continuous basis but at least annually the Bank conducts more holistic risk profile assessment that is based on the Bank's internal capital adequacy assessment process ("ICAAP"). The assessment methodology follows best market practices and produces an assessment of the Bank's capital and liquidity requirements. The resulting capital and liquidity requirements are compared against the Bank's risk appetite and risk-bearing capacity. This process creates a continuous interaction between RAS and ICAAP: RAS affects the Bank's risk profile and risk-bearing capacity; these in turn may affect how the Bank sets its risk appetite. Figure 1 below shows the hierarchy of key concepts: risk-bearing capacity, risk appetite, risk limits and risk profile.

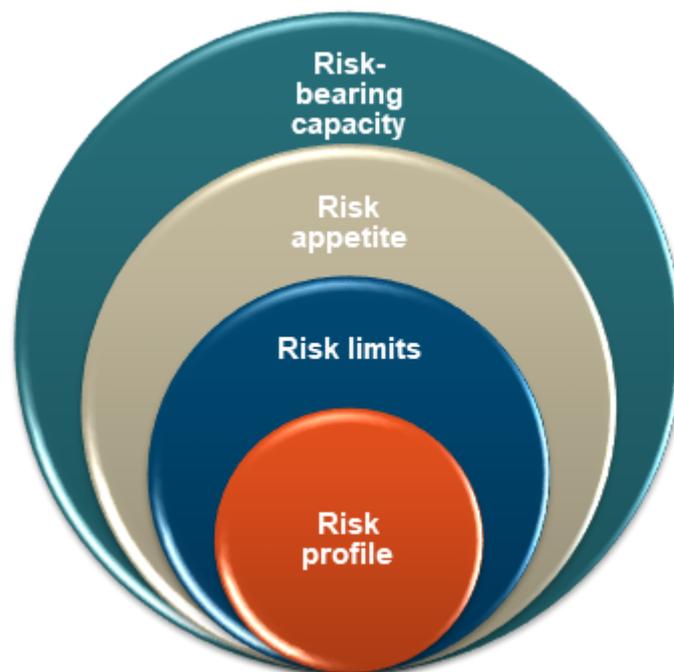


Figure 1. Hierarchical structure between risk-bearing capacity, risk appetite, risk limits and risk profile.

## 5 RISK APPETITE STATEMENTS

### 5.1 Risk culture

Risk culture consists of norms, attitudes and behaviour related to risk awareness, risk-taking and risk management, and the controls that affect decisions on risks. The Board of Directors, senior management and all members of staff contribute to the creation of a sound risk culture at NIB. Clear governance structure, policies and procedures support the creation of a sound risk culture. Ultimately, the risk culture is created by day-to-day actions and the way key decisions are made and communicated. Co-operation and constructive dialogue are part of the sound risk culture, as they foster an environment of open communication to reach common goals. A sound risk culture enables the organisation to do the right thing, even in challenging circumstances, and it supports the organisation to identify its risks, and to adhere to its values and principles of high ethical standards. It is everyone's responsibility to contribute to the sound risk culture.

***We promote a culture of integrity and high ethical standards. We aim for a high level of competence and support each other by sharing information, skills and experiences. We have strong risk awareness, and we critically review and challenge existing practices. We foster an atmosphere where constructive challenging is a natural part of discussions and decisions on risk-taking, risk awareness and risk culture.***

***We comply with internal policies, regulations and procedures, and we respect their spirit. All individuals are expected to contribute to and promote a sound risk culture.***

### 5.2 Internal control

An adequate internal control framework is one of the key elements for an organisation to reach its goals. Internal control framework enables the organisation to operate in line with sound banking principles and it provides the necessary basis for the Bank's risk taking.

Internal control consists of checks and balances in the daily operations, implementation of four eyes principle, segregation of duties when necessary, and necessary supervision and oversight of internal processes and operations. Information security and data management are important factors in maintaining good internal control environment.

NIB has implemented a three-lines-of-defence model. The first line consists of risk-taking business functions that are responsible for day-to-day risk management in line with their tasks and duties and the Bank's policies and procedures. The guiding principle is that those responsible for risk-taking are also accountable for managing the associated risks. The second line consists of internal control functions - risk management and compliance - providing oversight over the first line, and monitoring the risk-taking in the Bank. The third line consists of an independent internal audit function. The second and third line functions have an important risk monitoring and control role in the Bank, yet all organisational units in the Bank are necessary for maintaining an adequate internal control framework.

***We respect our mission as a Nordic-Baltic bank, and we follow sound banking principles. We are committed to maintain an adequate internal control framework and see it natural that internal controls are part of our daily operations. The framework is implemented via the three lines of defence model that provides the basis to manage the risks which the Bank is exposed, and enables the Bank to reach its goals.***

## 5.3 Operations

NIB's operations consist of day-to-day routines and activities that enable the Bank to achieve its business objectives. The Bank has organised its operations through processes that are designed to promote efficiency, and to mitigate potential for errors. We acknowledge that no bank can completely avoid errors and mistakes, though well-designed and robust processes support NIB's internal control framework, reduce the potential for losses, and also help to mitigate the impact on our reputation.

On a high-level, NIB's risk universe consists of financial and non-financial risks. Non-financial risks are due to inadequate or failed internal processes, people and systems or external events. Thus, errors in the Bank's operations typically fall under non-financial risk category. Non-financial risks are managed using specific tools, methodologies and procedures, across all the units and functions in the Bank.

The operations are heavily dependent on reliable ICT services, information security, data management and skilled resources. ICT services undergo continuous updating and development to provide a high quality service level in an evolving environment. Continuity of operations is a key consideration when introducing new technology. Business continuity capabilities are regularly tested as uninterrupted continuity of operations is of high importance for NIB.

Further, security of confidential client, business and staff information is of utmost importance for the Bank. A high level of information security is achieved through a risk management process structured to identify information assets and treatment of threats to those assets. In addition, critical business functions require a high level of integrity and availability of ICT systems and data.

***We are willing to accept limited exposure to non-financial risks as part of our operations. We actively manage our exposure to non-financial risks and aim to maintain our strong reputation. We acknowledge, that when fulfilling our mandate, we might engage in lending transactions which can expose the Bank to elevated compliance and reputational risks. We control these risks through appropriate and economically viable mitigating measures. Non-financial risks in our internal processes are mitigated through strong internal controls.***

***We acknowledge the critical nature information security has in the banking industry. As part of the overall organisation security, we maintain a strong information security culture, and have a conservative approach to information security.***

## 5.4 Mandate

NIB's mandate is to finance projects that promote productivity gains and environmental benefits for the Nordic and Baltic countries. Mandate rating is a mandatory part of the Bank's credit-granting process, and it supports the Bank's vision to work towards a prosperous and sustainable Nordic-Baltic region. Resource efficiency, climate change mitigation, pollution reduction, technical progress and innovation, human capital, infrastructure improvements, and general improvements in market efficiency and the business environment are aspects that the Bank considers during the mandate evaluation process.

NIB evaluates each investment project according to the mandate rating framework, in addition to credit risk and sustainability assessment (analysis of social and environmental standards). During the mandate assessment, the Bank evaluates whether the investment project improves productivity or benefits the environment in the Bank's member countries, or if both objectives can be achieved.

***We finance projects that promote productivity gains and environmental benefits. Each project is assessed carefully using our mandate rating***

***framework and sufficiently fulfilling the mandate is a prerequisite for financing from the Bank. The vast majority of the projects should achieve a high mandate rating.***

## **5.5 Rating**

NIB finances its lending by issuing bonds in the global financial markets. To maintain investor confidence in the Bank as a debt issuer, the Bank is rated by international credit rating agencies. The evaluation covers several areas, including the Bank's business operations, governance structures, and capital and liquidity management.

NIB has been able to keep its issuer rating at the highest possible level (AAA/Aaa) since NIB was first rated in the early 1980s. Having a strong external rating allows the Bank to obtain funding at a favourable cost and to extend financing on competitive market terms.

***Having a strong external rating supports the achievement of our objectives as it lays down the foundation for attractive funding and lending terms. We, therefore, strive to maintain our issuer rating at the highest possible level, and we maintain sufficient financial and other resources to support this target.***

## **5.6 Climate**

NIB has committed to the Principles for Responsible Banking (PRB) and thereby to aligning its business strategy with and contributing to the objectives of the Paris Climate Agreement. NIB has also endorsed the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) and endorsed the Principles for Responsible Investment (PRI).

The Bank recognises the need to reduce the use of fossil fuels and to support the transition to a low-carbon, climate resilient economy. Therefore, we acknowledge the importance of systematically reviewing our Lending clients' and Treasury counterparties' climate commitments, strategies, and performance to understand the transition and physical risks and opportunities related to their business models.

The challenges posed by climate change demands the development of an appropriate risk management framework. Recognising that climate change presents opportunities as well as risks, the Bank intends to adapt its business strategy as needed to further support the climate targets of its owner countries and to support its clients and counterparties in their transition to a more sustainable and green economy.

NIB engages its Lending clients on these issues and considers the material risks and mitigating factors in its credit decisions. This includes the mandate and sustainability assessments, where climate change mitigation is underlined as a key driver. Exclusions of fossil fuel related activities are, moreover, stated in the Bank's Sustainability Policy.

Regarding Treasury operations, to complement its traditional selection criteria, the Bank aims to systematically incorporate climate-related risks into counterparty and investment selections. Our responsible investment approach is described in the Responsible Investment Framework and accompanying Guidelines.

***We are committed to the objectives of the key international climate-related action plans for banks and recognise that climate change exposes the Bank to physical and transition risks but offers opportunities as well. We are committed to enhancing our climate risk management and to integrate it into our overall risk management framework. Our business strategy will support and assist our owners, clients, and counterparties in their journey towards a***

***climate resilient economy. We are willing to finance our clients to support their transition towards a low-carbon economy. We encourage our clients to clearly define and communicate their climate-related commitments and to develop and execute effective strategies to mitigate climate risks. We will actively favour business with Treasury counterparties that meet our framework for responsible investments. NIB is committed to conduct active engagement with the issuers and transaction counterparties.***

## **5.7 Lending**

NIB is exposed to risk primarily in its core activity of lending to governments, public sector entities, municipalities, corporations and financial institutions in the member countries. The Bank supports its clients in their efforts to grow and gain access to new markets by also financing projects located outside the member countries.

Long-term lending exposes the Bank to credit and concentration risks and to variation in the business cycles. To support the prosperity of the Nordic–Baltic countries, the Bank tolerates risk exposure arising from lending through the cycles and aims to continue financing viable investment projects during economic downturns. Each project is thoroughly analysed from several perspectives (for example financial risks, sustainability assessment, and customer due diligence) to ensure that financing decisions have sound foundations. The overall target of the credit risk management is to maintain high portfolio quality with appropriate risk diversification.

The Bank prioritises projects that enhance the environment and productivity, and requires that all projects comply with certain environmental and social standards. Certain types of projects are completely excluded from the Bank’s lending portfolio due to their adverse impact on the environment, or because they are unethical in general (for example production of tobacco, toxic chemicals or ammunition).

***We provide long-term financing to our customers and want to support the development of their businesses. We value transparency in our business relationships, and we expect it from our customers.***

***As the bank of the Nordic and Baltic countries, we want to stay relevant for our member countries and fulfil our mandate, and we are willing to provide various forms of long-term financing through business cycles. The majority of our lending is in the member countries, but we are willing to finance projects outside the membership region with an adequate member country interest.***

***We take credit risk primarily in our core activity of lending. We aim to maintain the high quality of the loan portfolio, while acknowledging that some of our lending involves greater risks. We diversify lending across industries and geographies to avoid excessive risk concentrations.***

***We highlight the importance of sustainability, high ethical and social standards, and protection of the environment in our lending operations. We do not finance projects that are undesirable from a sustainability or social standards perspective. This includes potential deterioration of the physical, natural, or cultural environment, the surrounding community, or the health and safety of workers directly resulting from the business activity to be financed.***

## 5.8 Treasury

Treasury enables and supports NIB's lending operations and is thus an integral part of the Bank's business operations. Funding, asset and liability management, and management of the portfolio of liquid assets are the primary operations of the Treasury.

Treasury acquires funds by issuing bonds on the international capital markets. The funding base is diversified across currencies, maturities and geographic areas. The Bank effectively manages the risk exposures arising mainly through maturity mismatches between assets (loans and treasury investments) and liabilities (borrowing and equity). The Bank maintains a robust liquidity portfolio. The primary objective of the liquidity portfolio is to ensure that the Bank is able to operate and continue its core activities even during stressed market conditions. The liquidity portfolio is composed of assets that preserve their market value and liquidity during adverse market conditions.

NIB aims to mitigate operational risks in its Treasury operations, but accepts market and credit risks to manage its capital effectively and to provide stable earnings. NIB invests in fixed-rate assets in order to generate stable earnings and to preserve its capital base in the long term (interest rate risk). NIB's liquidity portfolio is invested in high quality assets and in doing so NIB takes limited credit risk (credit default and spread risk).

NIB mitigates its currency risk and most of interest rate risk arising from funding and lending operations by hedging with derivatives. The use of derivatives exposes NIB to counterparty credit risk, liquidity risk, currency basis risk and operational risks. NIB uses netting and collateral agreements to manage its risk towards derivatives counterparties.

***Treasury enables and supports our lending operations by acquiring cost-effective funding from diversified sources and by maintaining a strong liquidity position.***

***We accept interest rate and credit risk arising from the investments in the liquidity portfolio. We accept funding liquidity risk deriving from maturity mismatches between funding and lending. We hedge interest rate risk arising from funding and lending activities with the objective of protecting earnings and the economic value of assets and liabilities. We effectively mitigate currency risk, using derivatives, to protect the Bank against realised foreign exchange rate losses. We allow exposure to currency basis risk arising from the use of derivatives for hedging purposes.***

## 5.9 Earnings

Banking involves well-judged risk-taking, where all transactions should provide a reasonable margin to compensate for the risk taken. Earnings are important for capital accumulation and to secure the Bank's dividend payment capacity. A reasonable and stable level of earnings indicates that the Bank's operations have a sound and healthy basis, and they also support the Bank's viability in the long term. Business and capital planning processes are used to set earnings targets, which provide signals of desired operational efficiency and strategic priorities for the Bank.

***We offer financing on competitive market terms and aim for stable earnings enabling the formation of capital reserves, organic growth, and reasonable return on capital in the long term.***

***Lending operations, the primary source of credit risk, should provide appropriate return for the level of risk assumed.***

***Treasury operations, through cost-effective funding and prudent asset and liability management, should contribute to the Bank's overall returns in line***

***with the defined business objectives and given the core objective of safeguarding the Bank's liquidity.***

***We strive for operational efficiency and to use our resources in clever and sustainable ways.***

## **5.10 Capital**

Capital is required to absorb losses from unexpected risk events, and to ensure smooth operations even in adverse economic conditions. Having a strong capital position protects investors and thus, it benefits the funding conditions and the cost of funding. As capital has such an important role in the banking system, both at systemic and at individual bank level, the Bank sees that an adequate capital management framework, with a capital adequacy assessment process (ICAAP), is an essential part of NIB's operations. NIB is committed to maintaining a strong risk-based capital position.

The Bank complements risk-based capital adequacy measures with a volume-based leverage ratio measure. It protects the Bank from risks that relate to excessive growth of the balance sheet.

***We aim to maintain a strong capital position in relation to the aggregate risk exposure at all times. We use risk-based approaches to assess our capital needs, including stress testing, and the Bank holds robust capital buffers on top of the minimum capital requirement.***

***The growth of the Bank's balance sheet should be stable in the long run, while some variation is accepted in the medium term to account for natural variation in the business cycles.***

## **5.11 Liquidity**

The Bank maintains a robust liquidity portfolio. The primary objective of the liquidity portfolio is to ensure that the Bank is able to operate and continue its core activities without disruption even during stressed market conditions. The liquidity portfolio is composed of high-quality assets in order to preserve the market value and liquidity of the assets during adverse market conditions. The Bank strives to diversify its borrowing in terms of currencies, maturities, instruments and investor types in order to avoid excessive reliance on individual markets and funding sources.

***We maintain a liquidity portfolio where a large majority of the assets are of high quality to support the Bank's operations and liquidity position. Having a strong liquidity position enables us to carry out our core activities under severely stressed market conditions without access to new funding.***

***We diversify borrowing in terms of currencies, maturities, instruments and investor types in order to avoid excessive reliance on individual markets and funding sources.***

## Appendix 1. Terminology and definitions

The Financial Stability Board (FSB) has provided the following definitions for key concepts in RAF/RAS<sup>1</sup>. NIB applies these on a best-effort basis.

- **Risk Appetite Framework (RAF)** is defined as “the overall approach, including policies, processes, controls, and systems through which risk appetite is established, communicated, and monitored. It includes a risk appetite statement, risk limits, and an outline of the roles and responsibilities of those overseeing the implementation and monitoring of the RAF. The RAF should consider material risks to the financial institution, as well as to the institution’s reputation vis-à-vis policyholders, depositors, investors and customers. The RAF aligns with the institution’s strategy.”
- **Risk Appetite Statement (RAS)** is defined as “the articulation in written form of the aggregate level and types of risk that a financial institution is willing to accept, or to avoid, in order to achieve its business objectives. It includes qualitative statements as well as quantitative measures expressed relative to earnings, capital, risk measures, liquidity and other relevant measures as appropriate. It should also address more difficult to quantify risks such as reputation and conduct risks as well as money laundering and unethical practices.”
- **Risk capacity** is defined as “the maximum level of risk the financial institution can assume given its current level of resources before breaching constraints determined by regulatory capital and liquidity needs, the operational environment (e.g. technical infrastructure, risk management capabilities, expertise) and obligations, also from a conduct perspective, to depositors, policyholders, shareholders, fixed income investors, as well as other customers and stakeholders.”
- **Risk appetite** is defined as “the aggregate level and types of risk a financial institution is willing to assume within its risk capacity to achieve its strategic objectives and business plan.”
- **Risk profile** is defined as “a point in time assessment of the financial institution’s gross and, as appropriate, net risk exposures (after taking into account mitigants).”

### Other key terminology used in the RAS are the following:

**Callable capital** is capital that has been subscribed by the member states but has not been paid in. The amount of callable capital is defined in NIB’s Statutes.

**Cross-currency basis risk** refers to a risk of valuation losses due to changes in the cross-currency basis swap spreads. Cross-currency swaps are used to hedge foreign exchange risk.

**ICAAP** refers to the Internal Capital Adequacy Assessment Process. It is a process to define the risk-based capital need for the Bank. At NIB, it also includes liquidity adequacy assessment.

**Mandate rating framework** refers to procedures the Bank uses to assess whether the projects considered for financing support the vision of the Bank. The framework contains guidelines and tools that are used to assess how the projects provide productivity gains and environmental benefits for the Nordic and Baltic countries.

**Maturity mismatch** refers to a difference in maturities between (long-term) assets and (short-term) liabilities.

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<sup>1</sup> *Principles for an Effective Risk Appetite Framework*; Financial Stability Board (2013).