DANISH SHIP FINANCE

RISK REPORT 2016

CVR NO. 27 49 26 49

INTRODUCTION

The purpose of this risk report is to provide a description of 1) risk and capital management and 2) the composition of the own funds and risks in relation thereto in accordance with the disclosure requirements set out in Part 8 to the Capital Requirements Regulation (CRR). In addition, the report includes a description of the various types of balance sheet and off-balance sheet risks.

On 15 November 2016, it was announced that a consortium consisting of the private equity fund Axcel and the pension funds PFA and PKA had acquired almost 87% of the shares and a little more than 95% of the voting rights in Danish Ship Finance A/S (subsidiary). The shares are owned by a newly formed company Danish Ship Finance Holding A/S (parent company).

Furthermore, Den Danske Maritime Fond owns 10% of the shares, and the remaining 3.4% is owned by a small number of minority shareholders.

The parent company has no other activities than part ownership of the subsidiary.

The risk report is presented for the Group and the subsidiary (referred to as solo). The Group was established in November 2016, and there will be no comparative figures for 2015.

The risk report is published in connection with the presentation of the annual report. The risk report is available at www.shipfinance.dk/investor-relations/risk-and-capital-management/

The company regularly assesses whether there is a need for publication more frequently than once a year.

There is no audit requirement in respect of the risk report, and it has been decided not to have the Risk Report for 2016 be subject to an audit.

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RISK MANAGEMENT

Risk management is given top priority because the various risks may have an adverse impact on financial performance and solvency and, by extension, weaken future business opportunities.

ALLOCATION OF RESPONSIBILITIES

The Board of Directors has the overall responsibility for ensuring appropriate risk management procedures. The risk policies established by the Board of Directors, including written guidelines for the Executive Board, and the legislative framework govern the company's risk management.

The Executive Board has the overall day-to-day responsibility for managing risks and for reporting such risks to the Board of Directors. Risk management forms an integral part of the day-to-day operations and is pursued through policies and control measures prepared to retain an effective control environment. Based on regular reports about developments in the Group's risks, the Executive Board continuously assesses risk levels and resolves on any steps to mitigate identified risks.

Pursuant to the Executive Order on Governance, the company must appoint a Chief Risk Officer. The Chief Risk Officer is responsible for ensuring an adequate risk management process and that an overview is established of risk and total risk exposure. The Board of Directors has approved that a member of the Executive Board be appointed the company's Chief Risk Officer. The background is an assessment of the Group's size and complexity, and the Executive Board has found that it was unnecessary and inappropriate to appoint an employee with no other responsibilities than risk management.

In addition, the company has appointed a Head of Compliance, whose duties involve ensuring compliance with applicable legislation, market standards and internal rules and also ensuring that the company applies effective methods and procedures suitable for identifying and mitigating the risk of non-compliance.

REGULATION

The Group is governed by its own regulation in the form of the Act on a Ship Finance Institute (the Act) and the Executive Order on a Ship Finance Institute (the Executive Order). Pursuant to the Act and the Executive Order, the Group is governed by parts of the Danish Financial Business Act. The Group is governed by the regulation on prudential requirements for credit institutions and investment firms (CRR) via the Executive Order.

The Group is also governed by:

- The Executive Order on Bond Issuance, the Balance Principle and Risk Management (the Bond Executive Order)
- The Executive Order on Calculation of Risk Exposure Amount, Own Funds and Solvency Need
- The Executive Order on Governance, Risk Management, etc. for Financial Institutions (the Executive Order on Governance)
- The Executive Order on Financial Reports by Credit Institutions and Investment Companies, etc. (the Executive Order on Financial Reporting)

Like other financial enterprises, the parent company and the subsidiary are supervised by the Danish Financial Supervisory Authority.

INTERNAL AUDIT

In accordance with applicable legislation, the Board of Directors, including the Audit Committee, regularly assesses the need for an internal audit function. The Board of Directors has decided that the combination of an internal control function, which regularly monitors compliance with in-house business processes and control procedures in all significant areas, and sharp attention by the external auditors helps to provide a satisfactory audit and control level. The work of the internal control function is planned by the external auditors.

WHISTLEBLOWER SCHEME

In accordance with the Danish Financial Business Act, the company has implemented an internal whistleblower scheme, which enables its employees to report any instances of non-compliance with the financial legislation to an independent third party. On receipt of such reports, the independent third party will make a tentative screening of the report to assess whether the instance of non-compliance falls within the scope of the whistleblower scheme.

REPORTING TO THE BOARD OF DIRECTORS

Report	Frequency
Compliance reporting	Yearly
Report from Chief Risk Officer	Yearly
Authorisation list*)	Each ordinary board meeting
Financial reporting	Quarterly
Internal financial reporting	Quarterly
Credit reporting	Quarterly
Memorandum on weak credit exposures	Quarterly
Statement to be used for risk assessment	Yearly
Recovery plan	Yearly
Stress test	Quarterly
Annual asset review	Yearly

*) Definition: "Loans or guarantees, increases, debtor replacements and other material changes to loans, including the granting of any breach of loan agreements granted by the Executive Board".

REPORTING

The Board of Directors is provided with regular reports to ensure that its members have the necessary information about risk developments etc. On the basis of these reports, the Board of Directors assesses the overall policies, framework and principles for risk and capital management.

RISK TARGETS AND POLICIES

The Group is exposed to different types of risk. On the basis of the business model and strategic goals, the Board of Directors defines risk policies and principles of risk and capital management. The purpose of the risk management policies is to define limits for acceptable risks.

Credit risk represents the bulk of the overall risk exposure. Market risk and operational risk represent the other risks, whilst the Group has limited liquidity exposure due to the rules of the Bond Executive Order.

The credit risk should be seen primarily as the risk associated with the borrower's inability to repay the loan with interest in due time. The company provides financing against a first priority mortgage in vessels and in special cases financing of the shipowner's payment of instalments to a shipyard. The credit policy defines overall targets to ensure a controllable lending risk. As part of the credit policy, in its loan portfolio the company seeks to ensure good credit quality and risk diversification in respect of borrowers and vessel types. When granting credit to new as well as existing customers, focus will be on vessel characteristics, the financial standing of the borrower, the terms of the loan and on the loan's contribution to compliance with the diversification rules. Credit risk associated with financial counterparties is managed through a policy on managing counterparty risk. In this way, the company defines limits for the exposure to individual financial counterparties and the countries in which such counterparties are residents.

Market risk covers primarily interest rate, foreign exchange and liquidity risks, governed by lines defined in the Bond Executive Order and the Executive Order. The principal financial risks are centred on the securities portfolio. The overall goal is to avoid financial positions jeopardising the company's solvency or continued existence, and to make sure that interest rate and foreign exchange risks are managed by hedging or through intended open positions and that the company achieves the highest possible return with due consideration to the risk targets defined.

Liquidity risk represents a limited part of the overall risk exposure, as the company applies the specific balance principle in accordance with the Bond Executive Order. In addition, the liquidity policy defines liquidity risk limits in order to ensure consistently adequate liquidity. Liquidity management is generally carried out to ensure that the cost of funding does not become disproportionately high and to avoid that lack of funding prevents the company from retaining its business model. Ultimately, the purpose of the liquidity management is to ensure that the company is consistently able to meet its payment obligations.

Operational risks primarily concern the credit area, the finance area, compliance and IT application. Operational risks are managed by way of a policy for operational risks, business procedures and internal controls issued by the Board of Directors. The policy defines the overall limits for operational risks and instructions on how to meet these limits. On an ongoing basis, the company registers losses and events deemed to be attributable to operational risks. The registration is used as a basis for assessing whether business procedures etc. should be adjusted in order to avoid or mitigate operational risks.

USE OF ECAIS

The company uses Standard & Poor's Financial Services LLC (S&P) as its external credit rating institution (ECAI).

The credit assessment classes used by S&P are converted to credit quality steps using the Danish FSA's conversion table. Each credit quality step is designated a risk weighting to be used for the exposures at the individual credit quality steps when calculating the risk-weighted exposures under the standardised approach for credit risk.

The table below shows the Danish FSA's conversion of S&P's credit assessment classes for credit quality steps for exposures to business entities, institutions, sovereigns and central banks.

Credit quality step	The credit assessment classes used by S&P	Exposures to corporates (companies)	Exposures to institutions with a term to maturity of more than three months	Exposures to central governments or central banks
1	AAA to AA-	20%	20%	0%
2	A+ to A-	50%	50%	20%
3	BBB+ to BBB-	100%	50%	50%
4	BB+ to BB-	100%	100%	100%
5	B+ to B-	150%	100%	100%
6	CCC+ and below	150%	150%	150%

EXPOSURE CLASSES USING CREDIT ASSESSMENTS FROM STANDARD & POOR'S

Exposure class, DKK million	**Group** Exposure (unweighted)	**Solo** Exposure (unweighted)
Exposures to central governments or central banks	616	606
Exposure to public entities	521	521
Exposure to regional and local governments	-	-
Exposure to institutions	2,565	2,538
Exposure to corporates	37,077	37,077
Exposure in the form of covered bonds and mortgage covered bonds	3,385	3,385
Exposure in defaults	7,012	7,012
Items associated with particularly high risk	-	-
Exposure to institutions and corporates with short-term credit ratings	-	-
Exposure by way of units or shares in collective investment undertakings ('CIUs')	-	-
Equity exposures	-	-
Other items	365	365

CAPITAL MANAGEMENT

Pursuant to the Executive Order on Calculation of Risk Exposure, Own Funds and Solvency Need, Danish Ship Finance must maintain a certain amount of capital relative to its activities, so that the own funds as a minimum matches the company's risk profile and complies with the legislative framework.

There must be capital to cover the requirement at the existing and the expected level of activity in order to comply with the statutory rules and targets determined by the company itself.

The regulatory framework for capital management is defined in the Executive Order on Calculation of Risk Exposure Amount, Own Funds and Solvency Need. The framework builds on three pillars:

- Pillar I contains a set of rules for calculating the own funds requirement, which is 8% of the total risk exposure amount for the three types of risk: credit, market and operational risk
- Pillar II contains a set of rules for how to calculate the adequate own funds, taking into consideration the company's individual characteristics, and all relevant risk types are included, irrespective of whether they are included in Pillar I or not.
- Pillar III sets forth rules on disclosure obligations, as a result of which the company, at least once annually, must disclose information on capital matters, its risk profile etc.

The Executive Order on Calculation of Risk Exposure Amount, Own Funds and Solvency Need provides some freedom to choose methodology when calculating the adequate own funds. The reason is that the calculation method must match the risk profile.

CAPITAL TARGET

The capital target defined by the Board of Directors is based on own funds that are sufficient for the lending operations to continue even in case of large cyclical fluctuations and difficult business conditions.

The capital ratio at group level at 31 December 2016 was 15.8%.
At solo level, the capital ratio has been calculated at 17.2%.

The capital ratio is believed to be adequate to meet the above-mentioned target.

CALCULATION OF CAPITAL RATIO

DKKm / %	Group 2016	Solo 2016	Solo 2015
Own funds less deductions	8,076	8,781	9,896
Total risk exposure amount	51,033	50,995	57,234
Capital ratio	15.8	17.2	17.3

OWN FUNDS

The Group's own funds less deductions amounted to DKK 8,076 million at 31 December 2016. At solo level, the own funds amounted to DKK 8,781 million at 31 December 2016, against DKK 9,896 million in 2015.

The own funds is subordinated to ordinary creditors in the event that a financial undertaking goes bankrupt. The own funds can be composed of three different types of capital: tier 1 capital, additional tier 1 capital and tier 2 capital, and the relationship between own funds and total risk exposure amount is the capital ratio.

Tier 1 capital
Tier 1 capital is the capital that represents the core of the own funds of financial enterprises. The tier 1 capital primarily consists of paid-up share capital or guarantee capital and reserves in a credit institution.

Additional tier 1 capital
Additional tier 1 capital is a mixture of share capital and loan capital. There are special rules on how large a proportion of the additional tier 1 capital can be included as part of the tier 1 capital. The part of the additional tier 1 capital that cannot be included in tier 1 capital may instead be included in tier 2 capital.

Tier 2 capital
Tier 2 capital is the capital that supplements the tier 1 capital and the additional tier 1 capital in financial enterprises. Tier 2 capital consists, among other things, of subordinated loan capital subject to high risk exposure.

The total capital must consistently be higher than the sum of the own funds requirement, the adequate own funds and the combined capital buffer requirement.

Own funds requirement

The own funds requirement, or the Pillar I requirement, describes the statutory requirements for financial enterprises. For a credit institution, the own funds must represent at least 8% of the institution's total risk exposure amount. The own funds requirement is a hard requirement, which means that non-compliance will lead to withdrawal of the license.

Adequate own funds and solvency need capital ratio

The adequate own funds is a capital requirement calculated on the basis of a financial institution's risk profile. It is based on the pillar I requirement of 8% of the total risk exposure amount plus a pillar 2 add-on for risks and matters that are not fully reflected in the statement of the total risk exposure amount.

The solvency need capital ratio is expressed as the adequate own funds as a percentage of the total risk exposure amount. Institutions must comply with the sum of pillar I, pillar II and the combined capital buffer requirement.

The solvency need capital ratio is a "soft requirement", so as to give a non-complying institution time to restructure its own funds. When relevant, the FSA will order the institute to take the necessary steps.

Combined buffer requirement

Pursuant to the Danish Financial Business Act, the combined capital buffer requirement means the total common equity tier 1 capital required to meet the requirement of a capital conservation buffer increased by a company-specific countercyclical capital buffer and a systemic risk buffer. Institutions must comply with the sum of pillar I, pillar II and the combined capital buffer requirement.

If the credit institution does not meet the combined capital buffer requirement, it will only be able to make distributions, disburse variable pay and make payments relating to additional tier 1 capital instruments if special conditions are met.

Developments in the own funds are determined primarily by the net profit for the year and the company's dividend policy.

The Group's own funds consists exclusively of common equity tier 1 capital in the form of share capital, tied-up reserve capital, retained earnings and tier 2 capital.

The tier 2 capital is issued in the parent company. The tier 2 capital is established on terms and conditions that meet the requirements for recognition in the own funds as a tier 2 instrument under CRR. The issued tier 2 capital amounted to DKK 2,000 million and is provided by the pension fund PFA and pension funds under management by PKA. These pension funds are also shareholders of the parent company. Annex 2 provides a more detailed description of the terms and conditions for the tier 2 capital.

The tied-up reserve capital may only be used to cover losses which cannot be covered by amounts available for dividend distribution. The tied-up reserve capital shall as far as possible be restored by advance transfer of the profit for the year, if, in prior years, it was wholly or partly used to cover losses. Hence, no dividends shall be paid and no distributions shall be made in connection with capital reductions until the tied-up reserve capital has been restored to the same nominal amount as the undistributable reserve had before being used wholly or partly to cover losses.

The tied-up reserve capital was established in connection with the conversion from a foundation into a limited liability company and has remained unchanged at DKK 8,343 million.

CALCULATION OF OWN FUNDS LESS DEDUCTIONS

DKKm	Group 2016	Solo 2016	Solo 2015
Common equity tier 1 capital			
Share capital	1,220	333	333
Tied-up reserve capital	4,967	8,343	8,343
Reserve for net revaluation according to the equity method	-	-	-
Retained earnings	113	466	1,692
Revaluation reserve	-	21	10
Total common equity tier 1 capital	**6,300**	**9,164**	**10,378**
Deductions from common equity tier 1 capital			
Proposed dividends	-	199	413
Deferred tax assets	-	-	-
Additional straining pursuant to the Executive Order	142	142	41
Prudent valuation of trading portfolio	28	28	27
Deductions pursuant to transitional rules	-	13	-
Total deductions from common equity tier 1 capital	**170**	**383**	**481**
Common equity tier 1 capital less statutory deductions	**6,130**	**8,781**	**9,896**
Tier 2 capital	1,946		
Own funds less deductions	**8,076**	**8,781**	**9,896**

OWN FUNDS REQUIREMENT

Pursuant to legislation, a ship finance institute must have own funds which as a minimum amounts to the sum of the own funds requirement for credit risk, market risk and operational risk.

Because the Capital Requirement Directive has been implemented in Danish legislation, the company may choose between different methods for calculating its risk exposure amounts for each of the three overall types of risk included in the determination of the own funds requirements.

The company has not applied for a permission from the Danish FSA to apply one of the internal methods. The company applies the standardised approach for calculating the total risk exposure amount and the own funds requirement for credit and market risks. When using the standardised approach, the risk weights are defined in the legislation. In addition, the basic indicator approach is applied to calculate the risk-weighted exposures for operational risk.

The next page shows risk-weighted exposures and own funds requirement for each exposure category.

RISK EXPOSURE AMOUNT

mio. DKK	Group Risk exposure amount (weighted) 2016	Group Own funds requirement 2016	Solo Risk exposure amount (weighted) 2016	Solo Risk exposure amount (weighted) 2015	Solo Own funds requirement 2016	Solo Own funds requirement 2015
Credit risk						
- Central governments or central banks	658	53	633	616	51	49
- Regional governments or local authorities	-	-	-	-	-	-
- Public entities	-	-	-	-	-	-
- Institutions	693	55	680	701	54	56
- Corporate	36,317	2,905	36,317	44,190	2,905	3,535
- Covered bonds and mortgage covered bonds	346	28	346	223	28	18
- Exposures in default	5,887	471	5,887	256	471	20
- High-risk exposures	-	-	-	-	-	-
- Exposures with short-term rating	-	-	-	-	-	-
- Equity exposure	-	-	-	-	-	-
- Other exposures	391	31	391	376	31	30
Total credit risk	**44,292**	**3,543**	**44,254**	**46,363**	**3,540**	**3,709**
Counterparty risk accounts for	738	59	725	780	59	62
Market risk						
- Debt instruments	3,959	317	3,959	7,756	317	620
- Shares, etc.	27	2	27	39	2	3
- Exchange rate risk	397	32	397	699	32	56
- Commodity risk	-	-	-	-	-	-
Total market risk	**4,383**	**351**	**4,383**	**8,494**	**351**	**680**
Credit Valuation Adjustment (CVA)	**633**	**51**	**633**	**690**	**51**	**55**
Total operational risk	**1,725**	**138**	**1,725**	**1,687**	**138**	**135**
Total amount	**51,033**	**4,083**	**50,995**	**57,234**	**4,080**	**4,579**

OWN FUNDS REQUIREMENT – CREDIT RISK

The standardised approach is used to calculate the own funds requirement for credit risk, as a result of which all loans generally carry a weight of at least 100%. Under the standardised approach, the value of the ships' mortgages cannot be deducted, and in terms of solvency the loans are thus treated as unsecured loans.

The Executive Order sets out that the following loans or shares of loans each carry a weight of more than 100%:

- Pursuant to section 24(3) of the Executive Order, building loans carry a weight of 200% if the sum of building loans does not exceed 125% of the solvency-related excess cover. If the sum of the building loan exceeds 125%, the excess amount must be deducted from the tier 1 capital. Building loans are secured through debtor's liability, assignment and subrogation in the building contract and assignment in the shipyard's collateral for payments under the building contract.
- Loans in which the loan exceeds 70% of the value of the mortgage at the date of grant must, in respect of the part that regularly exceeds 70%, result in a deduction ("additional straining") in the tier 1 capital. The maximum deduction is determined at the date of grant in Danish kroner.
- When the borrower either has an external rating corresponding to credit quality levels 5-6, or is unrated and also domiciled in a country where the country risk calls for a higher weighting, the loan will have a weighting of 150%.
- Pursuant to the definition in art. 178 of CRR, loans in default have a weighting of 150%.

At 31 December 2016, the company had no construction loans. Deductions in the tier 1 capital concerning loans, which at the end of 2016 exceeded 70% of the value of the mortgage and which at the time of grant also exceeded 70% of the value of the mortgage, and which are thus subject to the rules on additional straining, amounted to DKK 142 million.

RISK EXPOSURE AMOUNT FOR CREDIT RISK, BROKEN DOWN BY RISK WEIGHTS

DKKm	Group Exposure (weighted) 2016	Group Own funds requirement 2016
0	0	0
10	348	28
20	260	20
50	1,137	91
100	38,301	3,064
150	3,597	288
200	-	-
250	649	53
Total risk exposure amount for credit risk	**44,292**	**3,543**

The table shows that most of the credit exposure has a weighting of 100%.

Counterparty risk on derivatives and calculation of capital

The company applies the market value method to calculate the size of the exposures for derivatives.

When determining the value of the exposure using the market value method for counterparty risk, the following method is applied:

- Contracts are calculated at market value to obtain the current replacement cost for all contracts with a positive value.
- In order to generate a figure for the potential future credit exposure, the nominal principal of the contracts or the underlying values are multiplied by percentages determined by the Danish Financial Supervisory Authority. Swaps based on two floating rates in the same currency are exempt, because only the current replacement cost needs to be calculated.
- The sum of the applicable replacement costs and the potential future credit exposures represents the counterparty risk.

In its loan granting process and the ordinary monitoring of credit exposures, the company takes into consideration the calculated exposure value to ensure that this value does not exceed the granted credit line on the counterparty in question.

COUNTERPARTY RISK

	Group Exposure (weighted)
DKKm	**2016**
Netting of exposure value:	
The positive gross fair value of financial contracts after netting	
Counterparty with risk weight of 0%	-
Counterparty with risk weight of 20%	300
Counterparty with risk weight of 50%	1,002
Counterparty with risk weight of 100%	207
The value of the total counterparty risk calculated according to the market value method for counterparty risk	
Counterparty with risk weight of 0%	-
Counterparty with risk weight of 20%	60
Counterparty with risk weight of 50%	413
Counterparty with risk weight of 100%	207

CREDIT VALUATION ADJUSTMENTS (CVA)

Pursuant to the CRR, institutions must calculate a credit valuation adjustment risk (CVA charge). The CVA is a separate capital requirement for OTC derivatives to cover the risk of loss due to value adjustment caused by deterioration of counterparty credit quality.

The company has decided to use the standard method for calculating CVA. Based on the standardised approach, risk mitigation techniques such as netting and collateral may be used.

The company has entered into ISDA agreements that allow for netting to control the level of credit valuation adjustments. Furthermore, CSA agreements have been signed with the largest financial counterparties, which entail that collateral is received, and in some agreements provided, automatically if the positive market values exceed a specified level.

The CVA charge amounted to DKK 633 million at 31 December 2016.

CVA-CHARGE

DKKm	**Group** Exposure (unweighted) **2016**	**Group** Exposure (weighted amount) **2016**	**Group** Own funds requirement **2016**
Standard method	1,056	633	51

COLLATERAL AND GUARANTEES

The company receives the following types of financial collateral and guarantees:

- Deposit funds
- Securities (debt instruments, unit trust certificates), primarily listed
- Government and credit institution guarantees

FINANCED CREDIT RISK HEDGING

	Group	Solo	
	Exposure (weighted)	Exposure (weighted)	
DKKm	**2016**	**2016**	**2015**
Deposits in cash or cash-like instruments	53	53	128
Debt instruments issued by central governments or central banks	9	9	-
Debt instruments issued by institutions	7	7	61
Shares	-	-	-
Total financial collateral	**69**	**69**	**189**

UNFINANCED CREDIT RISK HEDGING

DKKm	Group Exposure (weighted) 2016	Solo Exposure (weighted) 2016	2015
Guarantees issued by central governments and central banks	-	-	-
Guarantees issued by regional and local authorities	-	-	-
Guarantees issued by institutions and finance institutes	-	-	-
Guarantees issued by companies	-	-	-
Total guarantees	-	-	-

The company has business procedures in place for the management and valuation of collateral, and the procedures form an integral part of the ordinary risk monitoring process.

The company uses the simple credit risk-reducing method. This means that the capital charge on a credit exposure can be reduced when financial collateral is mortgaged. The CRR stipulates the collateral that may be used for credit risk mitigating purposes.

In accordance with the rules of the CRR, the company uses financial collateral and guarantees to hedge its credit and counterparty risk. The table above shows for each exposure category the coverage of the collateral, i.e. the fully adjusted size of the collateral within each exposure category.

CLEARING

Like the rest of the Danish financial sector, Danish Ship Finance is subject to the Regulation on OTC Derivatives, Central Counterparties and Trade Repositories (known as “EMIR”). The regulation stipulates an obligation to clear certain types of derivatives via a central counterparty. This obligation applies to financial counterparties and non-financial counterparties that exceed the clearing threshold. The company is characterised as a non-financial counterparty (NFC), which is below the clearing threshold, as EMIR defines financial counterparties as credit institutions approved pursuant to the credit institution directive. The company is exempt from this directive.

Non-financial counterparties will have a central clearing obligation only if certain threshold values for trading volumes are exceeded. As the company’s trading volumes do not exceed these clearing thresholds, it is not under an obligation to perform central clearing.

The company has appropriate procedures to measure, monitor and mitigate operational risk and counterparty risk for non-cleared OTC derivatives. In addition, all OTC derivative transactions are reported to a trade depository, providing more specific details about the agreement.

OWN FUNDS REQUIREMENT – MARKET RISK

The standardised approach is used to calculate the own funds requirement for market risk. Positions with market risk are items in the trading portfolio and positions with foreign exchange risk outside the trading portfolio.

RISK EXPOSURE AMOUNT FOR MARKET RISK

DKKm	**Group** Exposure (weighted amount) **2016**	**Group** Own funds requirement **2016**
Debt instruments, specific risk		
Total specific risk *)	1,302	104
Debt instruments, general risk		
Total general risk	2,657	213
Shares, etc.		
Total shares, etc.	27	2
Currency positions		
Total long-term currency positions	397	32
Total risk exposure amount for market risk	**4,383**	**351**

*) Specific risk for debt instruments is calculated for all debt instruments in the trading portfolio, including unweighted and weighted amounts for repo transactions.

OWN FUNDS REQUIREMENT – OPERATIONAL RISK

The own funds requirement for the operational risks must cover the risk of losses as a result of inappropriate or insufficient internal processes, human error and system error or as a result of external events, including legal risks.

The basic indicator approach is used to calculate the own funds requirement for operational risks. As a result, the risk exposure amount for operational risks is calculated at 15% of a three-year average of net interest income and non-interest related net income.

RISK EXPOSURE AMOUNT FOR OPERATIONAL RISK

DKKm	2016	2015*	2014*	Average
Accounting items				
Interest income	1,514	1,886	2,061	1,820
Interest expenses	(698)	(1,021)	(1,241)	(987)
Dividends from shares, etc.	-	-	-	-
Fees and commission income	32	41	114	62
Fees and commissions paid	0	0	0	0
Market value adjustments	124	(177)	123	23
Sum of accounting items	**973**	**730**	**1.057**	**920**
Risk exposure amount (weighted) under the basic indicator approach				
2016				**1,725**
2015*				**1,687**

*) Based on accounting figures for the subsidiary.

An assessment of the own funds requirement for operational risks is performed regularly. If the own funds requirement is deemed to be higher than mentioned above, the company will make corresponding adjustments to its adequate own funds.

OWN FUNDS REQUIREMENT FOR OPERATIONAL RISK

	Group
DKKm	Own funds requirement
2016	138
2015*)	135

*) Based on accounting figures for the subsidiary.

SOLVENCY NEED CAPITAL RATIO AND ADEQUATE OWN FUNDS

The capital management is anchored in the so-called ICAAP (Internal Capital Adequacy Assessment Process), which is a review aimed at identifying risks and determining the solvency need capital ratio.

The Board of Directors and the Executive Board ensure that the company maintains adequate own funds. The considerations made by the Board of Directors and Executive Board in this regard must lead to the determination of a solvency need capital ratio. Adequate own funds covers the minimum amount of capital which, in the opinion of the Board of Directors and Executive Board, is required to ensure that the bondholders are only exposed to a minute risk of suffering a loss in case the company becomes insolvent during the next 12 months.

INTERNAL PROCESS

The method used to calculate the adequate own funds and the solvency need capital ratio must, as a minimum, be approved by the Executive Board and the Board of Directors once a year, whereas the calculations are made quarterly. The company has established segregation of duties to the effect that the adequate own funds and the solvency need capital ratio are not calculated by the same persons who are in charge of the risk management process.

SOLVENCY NEED CAPITAL RATIO AND ADEQUATE OWN FUNDS

DKKm / %	Group 2016	Solo 2016
Total risk exposure amount	51,033	50,995
Pillar I requirement (8 per cent of total risk exposure amount)	4,083	4,080
Earnings	-	-
Growth in lending	-	-
Credit risk		
- Credit risks for large customers in financial difficulty	375	375
- Other types of credit risk	-	-
- Concentration risks	57	57
Market and liquidity risk	-	-
Operational and control risk	512	502
Gearing risk	-	-
Other risks	-	-
Own funds, total	**5,027**	**5,014**
Solvency need capital ratio, per cent	**9.9**	**9.8**
Capital conservation buffer, per cent	0.6	0.6
Countercyclical capital buffer requirement, per cent	0.2	0.2
Individual solvency need, including the combined capital buffer requirement, per cent	**10.7**	**10.7**

At the end of 2016, the adequate own funds and the solvency need capital ratio for the Group amounted to DKK 5,027 million and 9.9%, respectively.

METHODOLOGY

Credit institutions are free to choose the methodology when calculating the adequate own funds provided the resulting solvency need provides a fair view and is prudent. The company follows the Danish FSA's Guidelines on Adequate Own Funds and Solvency Needs for Credit Institutions. The guidelines contribute an interpretation of Annex 1 to the Danish Executive Order on Calculation of Risk Exposure Amount, Own Funds and Solvency Need. The guidelines stipulate a so-called 8+ approach based on an own funds requirement of 8% (pillar I requirement), which is assessed to cover "normal" risks. Add-ons are then added for "higher-than-normal" risks. In its guidelines, the Danish FSA has defined benchmarks for a large number of items with respect to expectations of "higher-than-normal" risks.

The guidelines define benchmarks and calculation methods within seven risk areas that an institution would usually find relevant when determining its adequate own funds.

In addition, the Executive Order defines a number of aspects that should also be included in the assessment.

Institutions must assess whether there are other relevant risk elements they should consider when calculating their adequate own funds.

The solvency need capital ratio is calculated by dividing the adequate own funds with the total risk exposure amount.

Based on the risk areas defined by the Executive Order and the guidelines as well as other risk elements deemed relevant, the company's calculation of the adequate own funds builds on the following seven risk areas:

1. Earnings
2. Growth in lending
3. Credit risk
4. Market and liquidity risk
5. Operational and control risk
6. Gearing risk
7. Other risks

A capital requirement deemed to be adequate to cover the underlying risks is fixed for each risk area. The company has also stress-tested its operating results to demonstrate, among other things, whether it will require additional capital on a 12-month horizon.

The Board of Directors and the Executive Board have defined the risks which the company should be able to withstand and thus also the factors that should be included in a calculation of the adequate own funds. In a number of areas, the FSA guidelines and the Executive Order on Calculation of Risk Exposure Amount, Own Funds and Solvency Need stipulate that companies must perform stress tests (sensitivity analyses) indicating whether there is a need for additional capital. In the stress tests, the financial figures are tested for a number of adverse events in order to illustrate how the ratios would respond in such a scenario.

The combined stress test shows that the company has a robust capital structure and liquidity buffer capable of withstanding a number of highly adverse events.

The company believes that the risk factors included in the calculation cover all the risk areas that, pursuant to legislation, the Board of Directors and Executive Board must take into consideration when determining the adequate own funds.

SPECIFICATION OF RISK AREAS

This review describes the risk areas and the general considerations used by the company to determine the adequate own funds. The results of the calculation are shown in the table “Individual solvency need and adequate total capital” on page 25.

1. Earnings. Mortgage credit institutions with core earnings representing less than 0.1% of loans and guarantees before loan impairment charges and market value adjustments should consider whether this gives rise to increasing the solvency need. Core earnings relative to loans and guarantees amounted to 1.8% for 2016.

In addition to the level of earnings, earnings stability also forms part of the assessment of the solvency need. The company’s core earnings have increased over the past few years but are henceforth expected to remain relatively stable around the level recorded in the past few years.

The earnings ability should also be assessed in relation to the company's dividend policy and capital procurement opportunities. Based on the results of the stress test of the operating profit, the company will, even in a severe stress scenario, not be facing a need for additional capital on a 12-month horizon.

Based on the above, the company finds that the Pillar I requirement is sufficient to cover risks relating to earnings.

2. Lending growth. The Danish FSA defines that a combined year-on-year lending growth of 10% or more could expose an institution to higher-than-normal credit risk. Consequently, institutions must allocate additional capital.

Since 2010, the company's lending growth has been below 10%. The average annual growth rate for the period 2010-2016 was (3.2)%. Against this background, the company believes that the Pillar I requirement is sufficient to cover risks resulting from lending growth.

3. Credit risk. In its guidelines, the Danish FSA divides credit risks into three sub-groups: credit risks for large customers in financial difficulty, other credit risks and credit risk concentration:

- Credit risks for large customers in financial difficulty
For large customers in financial difficulty, an assessment should be made of a conservatively estimated loss on each loan. Large customers in financial difficulty are defined as customers whose total loans account for more than 2% of the own funds and where there is objective evidence of loan impairment of the exposure or material signs of weakness but no objective evidence of loan impairment (financial standing categories 1 and 2c on the Danish FSA scale).

A detailed description of these financial standing categories is provided in Appendix 8 of the Danish FSA's instructions for financial reporting in credit institutions and investment companies, etc.

Based on the above, a large customer may be defined as a customer with a credit exposure of more than DKK 175.6 million (DKK 8,781 million * 2%). Financial standing categories 1 and 2c will be equivalent to customers with a rating between 9 and 12 on the company's 12-point classification scale (12 being the lowest).

Pursuant to the guideline method for calculating capital supplements for large customers in financial difficulty, the company's Pillar 2 add-on amounted to DKK 375 million at 31 December 2016.

- Other credit risks

Other credit risks primarily cover *"other risks in the loan portfolio"* and *"risks associated with financial counterparties"*.

In its assessment of "other risks in the loan portfolio", the company considers assessment areas laid down in the Guidelines on Adequate Own Funds and Solvency Needs for Credit Institutions and sensitivity analyses based on a number of scenarios and their importance for the need to make loan impairment charges.

Based on these assessments and sensitivity analyses, the company concludes that "other credit risks in the loan portfolio" are covered by the Pillar I requirement.

The assessment of *"other credit risks associated with financial counterparties"* is based on an evaluation of the financial standing of the financial counterparties. The principal risks relate to the investment of the trading portfolio, the vast majority of which is placed in Danish mortgage bonds.

The financial standing of financial counterparties and, by extension, the credit risk associated with the investment of the trading portfolio, interest rate and currency hedging etc. is monitored regularly, including an assessment of the capital required to hedge the exposures. Furthermore, bilateral collateral agreements (CSA) have been signed with a number of bank counterparties, which reduce the counterparty credit risk.

Based on the current standing of its financial counterparties, the company concludes that the Pillar I requirement adequately covers the capital requirement concerning *"other credit risks associated with financial counterparties"*.

- Credit risk concentration

Concentration risks are calculated with respect to single name concentration and sector concentration. Pursuant to the Executive Order on Calculation of Risk Exposure Amount, Own Funds and Solvency Need, the capital requirement in an institution with a high risk diversification is generally lower than in an institution with a high risk concentration.

In its guidelines, the Danish FSA notes that Danish mortgage credit institutions have a unique profile on account of their core business. Against this background, the calculation of sector concentration does not apply to mortgage credit institutions as per the guidelines. Meetings with the FSA have led to the conclusion that this also applies to Danish Ship Finance.

However, the guidelines stipulate that institutions exempt from these rules must consider the extent to which they have a concentration risk that should be addressed and for which capital should be allocated. Based on the sensitivity analyses used in connection with the assessment of “other risks in the loan portfolio”, the company has found that there is no material risk of loss in relation to sector concentration not covered by the Pillar I requirement.

In connection with single name concentration, the institution must consider imbalances in the distribution of loan sizes in its loan portfolio, irrespective of whether a customer has a good financial standing. The company applies the guideline calculation method with adjustments approved by the FSA. The Pillar 2 add-on for customer concentration has been calculated at DKK 57 million.

4. Market and liquidity risk. Due to the specific balance principle, which caps the risk that the company may undertake, market and liquidity risks are considered limited. Furthermore, limits defined in the company’s internal policies further mitigate the risks.

According to the FSA guidelines, mortgage credit institutions and similar institutions are exempt from making capital supplements with respect to market and liquidity risks. Nevertheless, the company makes a risk assessment of its market and liquidity risks on the basis of the guidelines, concluding that the market and liquidity risks are covered by the Pillar I requirement.

5. Operational and control risk. The capital reservation relating to operational risks based on the Pillar I requirement amounts to DKK 512 million.

An additional amount of DKK 502 million has been reserved with respect to lack of hedging of negative interest rates. The reservation must continue until a hedge has been established for the interest rate risk arising because of negative CIBOR rates and their correlation with terms of swap contracts and loan and bond terms and conditions.

Due to the new activity of owning and operating a holding company, which must establish governance, management reporting, notification procedures etc., an additional amount of DKK 10 million has been reserved.

6. Gearing. The leverage ratio is calculated as tier 1 capital relative to the institution's total exposure value (unweighted). At 31 December 2016, the leverage ratio was calculated at 12.4% at group level and 13.6% at solo level.

Pursuant to article 451(1) of the CRR, institutions shall disclose whether they use tier 1 capital as capital target, cf. article 499(1)(a) of the CRR, and that the leverage ratio is calculated at the end of the quarter.

According to the Basel Committee, the leverage ratio should not be lower than 3%. In other words, there is no need to determine a higher solvency requirement in order to reduce the gearing.

7. Other risks: Institutions must assess whether there is a need for a pillar 2 add-on in respect of reputational risks, strategic risks, group risks and external risks.

- The Group enjoys a good reputation and it is difficult to envisage an event that would substantially change this situation. Furthermore, a policy has been established for compliance with disclosure obligations, defining requirements for the external financial reporting, including the presentation of a true and fair view of the Group's financial results and activities. Reputational risks are believed to be covered by pillar 1.

- The Group has a well-established market position and a strong reputation among investors and customers. The past few years have brought comprehensive change in the competitive environment and customers' earnings capacity, but the company has managed to retain its position and stable earnings. Strategic risks are believed to be covered by pillar 1.
- The Group must consider the risks associated with owning one or more subsidiaries. This applies especially to the subsidiaries not included in the consolidated calculation in accordance with the Danish Financial Business Act. The Group consists of a holding company and a subsidiary. The subsidiary is fully consolidated. It is assessed that pillar 1 covers the associated risks.
- No risks have been identified that would challenge the business model. Against that background, no additional capital will be allocated to cover external risks.

COMBINED BUFFER REQUIREMENT

In 2016, the capital conservation buffer was 0.625% in Denmark. At 1 January 2017, the capital conservation buffer will be 1.25% of the total risk exposure amount. When the capital conservation buffer has been fully phased in on 1 January 2019, the capital conservation buffer requirement will be 2.5% of the total risk exposure amount.

A systemic risk buffer is defined by the Danish Minister for Business and Growth in order to prevent and limit long-term non-cyclical systemic or macroprudential risks not covered by the Capital Requirements Regulation (CRR). The systemic risk buffer was fixed at 0% in 2016.

The institution-specific countercyclical capital buffer may be applied if lending growth results in higher macroprudential risks. The institution-specific countercyclical capital buffer may be between 0-2.5% of the total risk exposure amount.

On the basis of the geographical distribution of credit risk, the capital requirement for the countercyclical capital buffer has been calculated at DKK 110 million at 31 December 2016. The capital requirement pertains to exposures in Norway, Sweden and Hong Kong, which have fixed the following countercyclical buffers:

- Sweden 1.5%
- Norway 1.5%
- Hong Kong 0.6%

INSTITUTION-SPECIFIC COUNTERCYCLICAL CAPITAL BUFFER

DKKm / %	2016	2015
Total risk exposure amount	50,995	57,234
Institution-specific countercyclical buffer requirement	110	97
Institution-specific countercyclical buffer requirement, per cent	0.2	0.2

GEOGRAPHICAL DISTRIBUTION

Country	Share (per cent)
Denmark	29
Norway	13
Bermuda	12
Germany	10
Marshall Island	7
United Kingdom	5
Cayman Islands	4
Sweden	4
The Netherlands	3
Luxembourg	3
Cyprus	2
Isle of Man	2
Italy	2
Belgium	1
Bahamas	1
Liberia	1
Singapore	1
Hong Kong	0
Iceland	0
China	0
Panama	0
Switzerland	0
Total	**100**

Annex 4 provides a more detailed description of the countercyclical capital buffer.

LIQUIDITY MANAGEMENT

Liquidity management is generally carried out to ensure that the cost of funding does not become disproportionately high and to avoid that lack of funding prevents the company from retaining the adopted business model. Ultimately, the purpose of the liquidity management is to ensure that the company is consistently able to meet its payment obligations.

BALANCE PRINCIPLE

The specific balance principle permits a future cash deficit between issued bonds and loans provided of up to 100% of the own funds.

The deficit occurs if the future payments related to bonds issued by Danish Ship Finance, other funding and financial instruments exceed the future incoming payments on loans, financial instruments and investments.

Through in-house policies, the company has defined strict requirements for any cash deficits between issued bonds and loans provided.

LIQUIDITY BUFFER

Bonds are typically issued in DKK, whereas most of the loans are disbursed in USD. The company has sourced USD for funding of USD loans disbursed via so-called basis swaps.

The risk caused by lack of access to convert DKK funding into USD involves higher financing costs or the loss of business opportunities. The opportunities for sourcing USD liquidity rely on an efficient capital market.

In-house policies govern the maximum limits for the need of USD over time.

LIQUIDITY POLICY

The company has prepared a policy for managing liquidity risk (liquidity policy) pursuant to the Executive Order on Governance.

The purpose of the liquidity policy is to ensure that the liquidity risk at any time matches the overall risk profile. The liquidity policy also serves to ensure adequate handling and management of liquidity, allowing the company at all times to meet its payment obligations, applicable legislation and plans for future activities and growth.

MANAGEMENT, MONITORING AND REPORTING

The company's liquidity management is anchored in the so-called ILAAP (Internal Liquidity Adequacy Assessment Process), which is a documentation paper aimed at identifying liquidity risks and determining liquidity targets.

The Board of Directors determines the overall guidelines for managing liquidity risk through the liquidity policy.

The Executive Board is responsible for ensuring that the guidelines established by the Board of Directors are laid down in business procedures that are regularly updated. The Executive Board, the Chief Risk Officer and relevant department managers must approve any changes when the guidelines are updated.

Compliance with the liquidity policy is monitored by the Risk Management function. Each quarter, the company prepares a financial report on compliance with the policy framework that is submitted to the Board of Directors.

LIQUIDITY MANAGEMENT

Moreover, a liquidity stress test is performed, consisting of the following components:

- Rising USD/DKK exchange rate
- An increase in interest rates
- A widening of credit spreads
- Write-offs

The results of the liquidity stress test are used to manage and adjust in-house limits. Furthermore, the test is used to create an overview of the liquidity profile in an actual and in a stressed scenario.

CONTINGENCY PLANS

Pursuant to the Executive Order on Governance, the company has prepared a liquidity contingency plan, which contains a catalogue of possible courses of action to strengthen the liquidity position in a critical situation.

The liquidity contingency plan takes effect if pre-defined triggers are activated.

CREDIT RISK

Credit risk reflects the risk of a loss due to default on the part of a counterparty. This applies to counterparties in the form of shipowners and financial institutions.

The limits for credit risk management are stipulated in the credit policy and policy on counterparty management. The policies build on the provisions in the company's own act and executive order. These provisions stipulate that the Board of Directors shall lay down risk diversification rules.

In its risk management activities, the company distinguishes between credit risk derived from lending operations and credit risks derived from transactions with financial counterparties. The day-to-day responsibility for the credit policy, the policy on counterparty management and for the periodical risk calculation and reporting of credit risk rests with the credit department.

LENDING

Ship financing is provided against a first priority mortgage in vessels. On a limited scale, the company also provides financing of shipowners' payment of instalments to a shipyard. The company is a leading provider of ship financing in Denmark, and it focuses primarily on large, reputable shipowners in Denmark and abroad.

The most significant risk facing Danish Ship Finance is believed to be credit risk, which is the risk of losses because the mortgage cannot cover the residual debt if the customers default on their loans.

When considering potential loans, focus will be on vessel characteristics, the financial standing of the borrower, the terms of the loan and the loan's contribution to compliance with the diversification rules.

LOAN LIMITS AND ADDITIONAL STRAINING

The company may grant loans up to 70% of the value of the mortgaged vessel(s).

However, the company may, on certain conditions, grant loans beyond 70% of the value against other collateral and/or against additional straining. The additional straining is maximised in Danish kroner, not later than when the loan offer is submitted.

As a result of the additional straining, for this part of the lending operations a deduction is calculated in the company's tier 1 capital in connection with the solvency calculation. The deduction equals the part of the loan in question that exceeds 70% of the mortgaged vessel(s) at the time of calculation, although capped by the maximum defined.

The calculation of the additional straining is made on the basis of an evaluation made or approved by the company on the basis of independent broker assessments of the market value of the mortgage.

In 2015 and 2016, the company did not grant any new loans with a loan-to-value ratio above 70% at the time of grant.

The weighted average loan-to-value ratio (LTV) after loan impairment charges at 31 December 2016 was 66%.

PERCENTAGE DISTRIBUTION OF LOANS INCLUDING GUARANTEES AFTER IMPAIRMENT CHARGES CALCULATED IN LTV INTERVALS (BY NOMINAL OUTSTANDING DEBT).

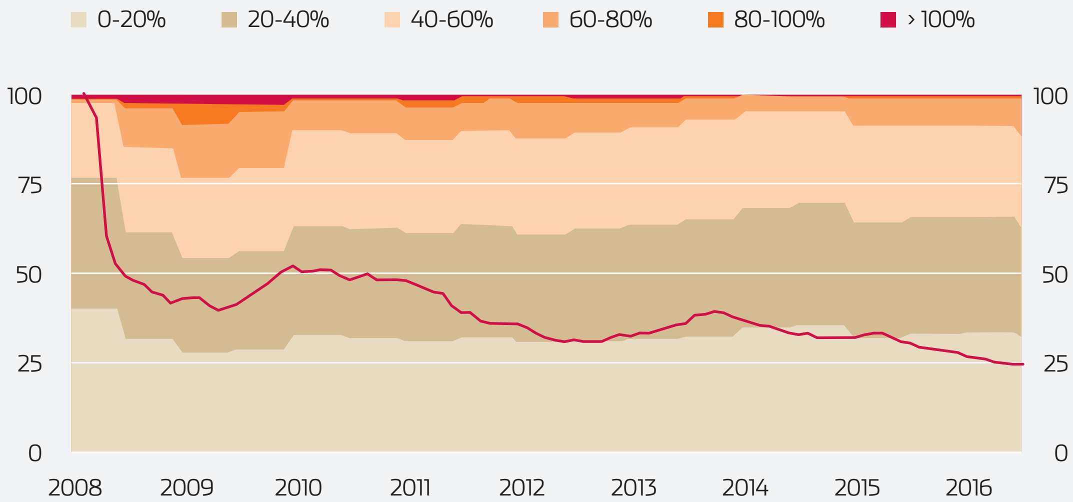
LTV interval	**Share of lending**	
%	**2016**	**2015**
0-20	32	33
20-40	31	33
40-60	25	25
60-80	11	8
80-90	1	1
90-100	0	0
Over 100	0	0

PERCENTAGE DISTRIBUTION OF LOANS INCLUDING GUARANTEES WITH INDIVIDUAL CHARGES. THE DISTRIBUTION IS MADE AFTER IMPAIRMENT CHARGES CALCULATED IN LTV INTERVALS (BY NOMINAL OUTSTANDING DEBT).

LTV interval	**Share of lending**	
%	**2016**	**2015**
0-20	34	35
20-40	33	35
40-60	27	22
60-80	6	8
80-90	0	0
90-100	0	0
Over 100	0	0

LOAN TO VALUE RATIO VS PRICE INDEX FOR ALL VESSEL TYPES

LOAN TO VALUE RATIO % OF TOTAL LOAN PORTFOLIO
PRICE INDEX FOR ALL VESSEL TYPES JUNE 2008 = INDEX 100



The chart above shows a breakdown of the loan portfolio into LTV intervals, which are calculated every six months. The LTV intervals show the proportion of the loans placed within a given range. For example, 88% of total lending including guarantees and after loan impairment charges are secured by mortgages within 60% of the valuations at the end of 2016. The breakdown is compared with developments in vessel prices based on a price index from Clarksons, showing price developments for all vessel types. The chart shows that even major declines in vessel prices do not materially change the collateral covering the loan. The reason is that instalments are regularly received and that a number of loan agreements include a right for the company to demand partial prepayment and/or additional collateral if the value of the vessel mortgage drops below an agreed minimum threshold (MVC).

LARGE EXPOSURES

Danish Ship Finance is exempt from the EU's credit institution directive and any related directives. The most important consequence of this exception is that the company will not be subject to a limitation in respect of large customers, cf. the CRR rules on large exposures. As a result, unlike other financial institutions the company is not bound by any statutory limits for maximum loans to an individual borrower. The Board of Directors shall instead lay down rules concerning risk diversification, including for its lending operations.

In connection with the management of large exposures, the company has defined guidelines for the extent to which and the assumptions on which the company will assume large exposures that exceed given limits in the credit policy relative to the own funds, including exposures that exceed 25% of the own funds.

One credit exposure exceeds 25% of the adjusted own funds. No financial counterparty exposure exceeds 25% of the adjusted own funds.

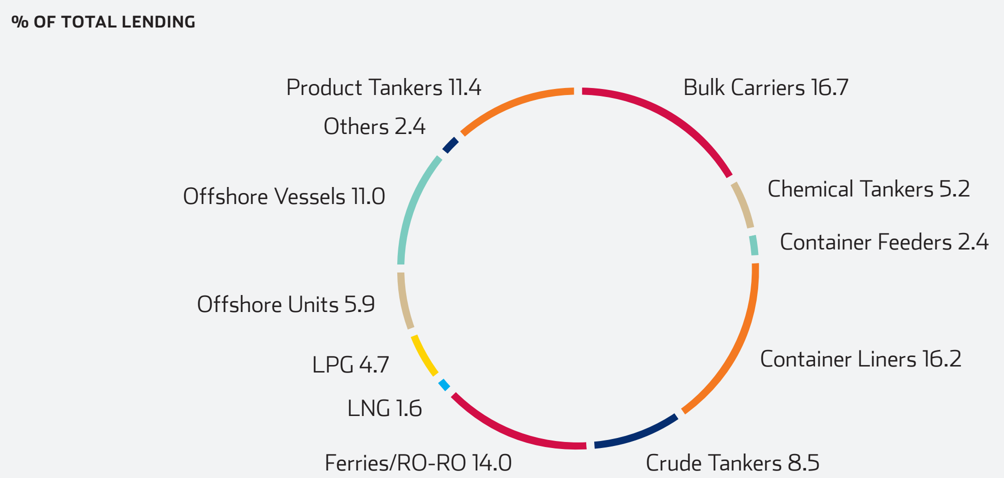
DIVERSIFICATION

The composition of the loan portfolio is governed by a set of diversification rules. The purpose of the diversification rules is to ensure adequate diversification by vessel type, borrower and country.

RISK DIVERSIFICATION ON VESSEL TYPES

Adequate loan portfolio diversification must be in place regarding vessel types. No single vessel type may be provided as security for more than 50% of the company's gross lending. Within each vessel type, no segment may be provided as security for more than 33% of the company's gross lending.

LOAN PORTFOLIO BY MORTGAGED VESSELS



RISK DIVERSIFICATION ON BORROWERS

The composition of borrowers must be adequately diversified in the loan portfolio. The diversification rule is related to the objects clause in the articles of association:

“The object of the company is to provide ship financing in Denmark. In addition, the company may provide ship financing on the international market, so long as such activities do not unnecessarily limit the company’s Danish operations.”

For large loans, the company should seek to diversify the risk on vessel types within the individual account.

For financing as defined in the second sentence of the objects clause, the overall account per borrower may not, at a consolidated level, exceed 25% of the most recently calculated own funds.

MOVEMENTS IN THE FIVE LARGEST EXPOSURES BEFORE LOAN IMPAIRMENT CHARGES

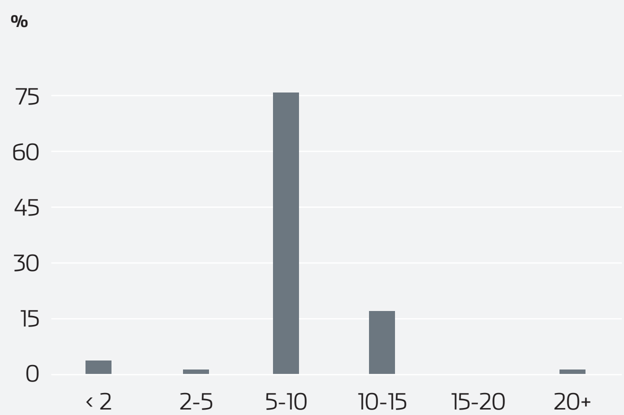
DKKm	2016	2015
Five largest exposures	13,686	15,443
Loans, advances and guarantees	42,699	45,602

The five largest exposures at 31 December 2016 were secured by mortgages in 77, vessels comprising 8 vessel types. One exposure is substantially larger than the rest and represented just over 20% of total loans and guarantees at 31 December 2016.

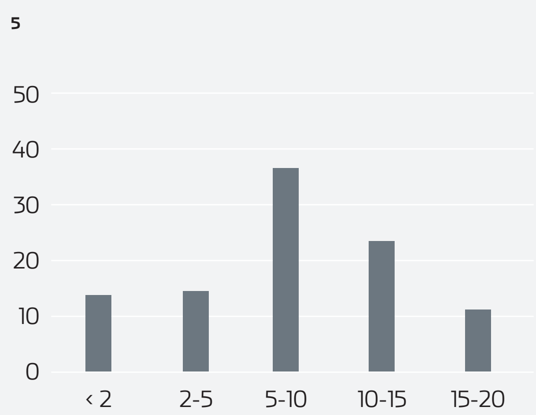
The risk diversification on borrowers also focuses on diversification on vessel types in each loan. The largest exposure was thus secured through mortgage on 27 vessels distributed on three different vessel types (loans for Container Liners represent the majority, and loans for Offshore Units and Offshore Vessels the rest).

AGE DISTRIBUTION OF MORTGAGED VESSELS (AS A PERCENTAGE OF TOTAL LENDING TO THE VESSEL TYPE)

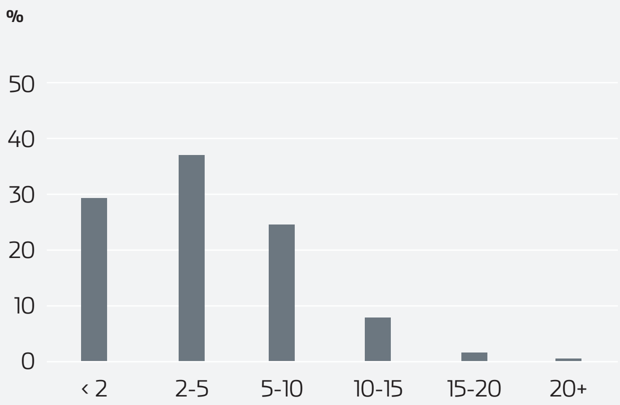
CONTAINER LINERS



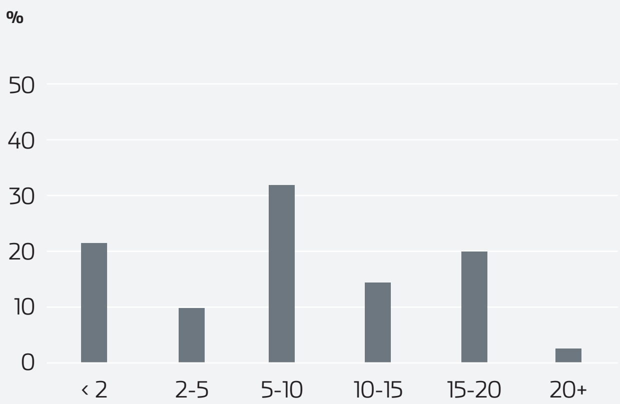
CHEMICAL TANKERS / CRUDE TANKERS / PRODUCT TANKERS



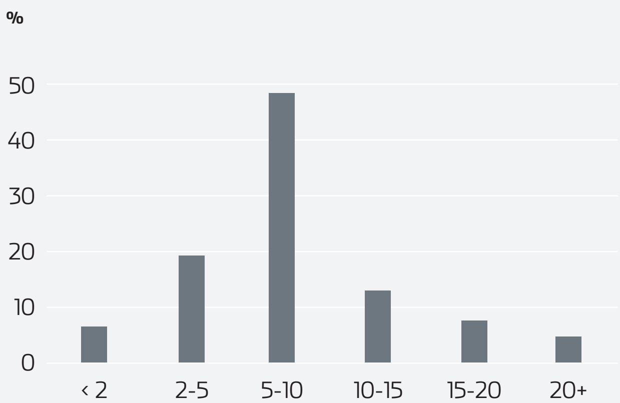
BULK CARRIERS



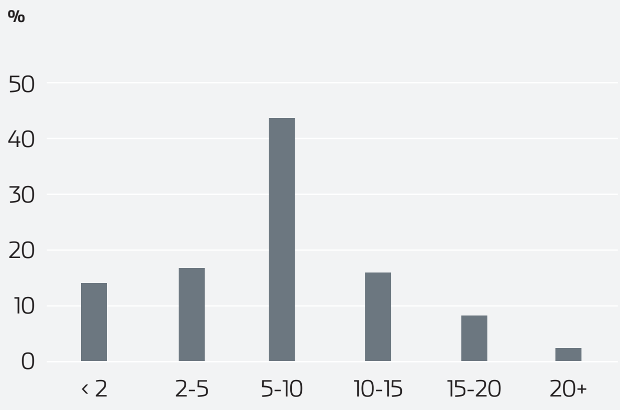
FERRIES / RO-RO



OTHERS



AGE DISTRIBUTION OF TOTAL SHIP PORTFOLIO

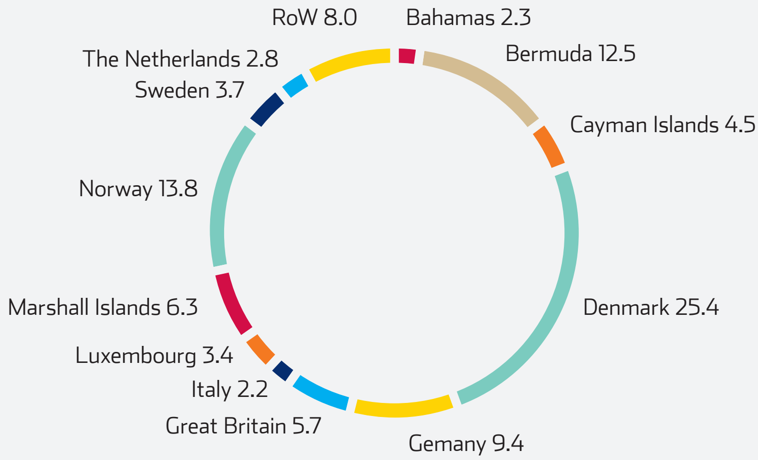


RISK DIVERSIFICATION ON COUNTRIES

The loan portfolio must be adequately diversified on countries. The country risk is calculated on the basis of the borrower's home country, or, in the case of guarantees, the guarantor's home country. Loans to borrowers in Norway, Switzerland and the USA and in certain EU countries are not subject to restrictions as to country risk. For loans to borrowers in other countries, the company has defined an overall limit per country of up to 25% of its gross lending.

DEBTOR DISTRIBUTION BY COUNTRY OF ULTIMATE RISK

% OF TOTAL LENDING



Countries with a share of at least 2% are shown separately. Other countries are grouped into 'Rest of world'.

The risk calculation method was selected on the basis of a wish to calculate and control the company's overall risk exposure using the legal system of a single country in case the need for a court order arises. The situation typically occurs in connection with default of an exposure in which the mortgaged vessels and any other collateral have been realised and the company must seek to collect a residual claim.

The company endeavours to mitigate the risk that may be associated with having to obtain a local court order by incorporating venue agreements into the loan documentation to the effect that any disputes must be settled in a court outside the debtor's home country. Denmark, Norway, Germany or the UK are often used as venues.

The company has deliberately avoided using the flag states of the vessels as an expression of the country risk, as the risk of loss associated with having to arrest and subsequently effect a forced sale of a vessel relies more on which jurisdiction the vessel is arrested in than the flag under which the vessel is sailing.

CREDIT RISK ON SHIPOWNERS

The credit policy contains specific guidelines for the ongoing risk management in the loan portfolio. A number of predefined procedures are used in the ongoing credit risk management process, the most important of which are described below.

GRANTING OF LOANS

The Executive Board and the Head of Credit have been allocated authorities by the Board of Directors allowing them to grant loans up to pre-determined limits. The granting of loans must be disclosed at the subsequent ordinary board meeting.

As in previous years, the Board of Directors approved the majority of all loans granted in 2016.

For existing loans, pre-defined limits have been established when approvals by the Executive Board or the Head of Credit must subsequently be reported to the Board of Directors.

ONGOING MONITORING

As part of the risk management process, all loans are assessed at least twice a year. All loans are assessed, and the current credit risk is assessed on the basis of current market valuations of the financed vessels and the most recent financial information of the borrower.

In addition, the portfolio is monitored in an ongoing process in relation to the borrowers' fulfilment of the individual loan agreement, comprising:

- Half-yearly updating of the market values of all financed vessels and verifying that any agreed requirements on maximum loan-to-value ratios are complied with.
- Verifying that any other collateral meets the specified minimum requirements.
- Verifying the existence of adequate insurance cover on financed vessels.
- Verifying compliance with all other material loan covenants.

If a loan is deemed to entail increased risk, the monitoring will be intensified to safeguard the company's interests to the best possible extent.

INSURANCE OF SHIP'S MORTGAGES

All vessels mortgaged as collateral for loans must be insured. Insurance is taken out by the borrower. Borrowers' insurances concerning financed vessels are assigned to Danish Ship Finance.

As a general rule, the insurance includes:

- Hull and machinery insurance, which covers damage to the vessel or total loss.
- P&I (Protection & Indemnity) insurance, which is a third party liability insurance to cover damage against persons or equipment.
- War Risks, which covers damage to the vessel, potential total loss and retention, etc. caused by war or war-like conditions.

In addition, most of the loans are covered by Mortgage Interest Insurance and Mortgagee Additional Perils Pollution Insurance. This insurance covers the risk in most situations which the primary insurance policies do not cover, for example if the vessel was not seaworthy at the time of the claim.

INSPECTION OF VESSELS

As a supplement to the half-yearly market valuations, physical inspections of the financed vessels are made on a spot-check basis. The inspection may be performed both during the loan period or prior to submitting a loan offer.

MARKET VALUATIONS

The company values each vessel semi-annually. The valuation is generally fixed by an external broker, who fixes a price for the financed vessels on the basis of supply and demand. The company may also determine the value itself, for example on the basis of a specific independent market price or if external assessments have been received for similar vessels.

Market valuations on vessels are, for example, used to determine the loan-to-value ratio on the company's loans and for control purposes, when reassessing the security value of a vessel, in connection with the company's half-yearly loan impairment review.

WRITE-OFFS AND IMPAIRMENT CHARGES

Twice a year, all exposures are reviewed in order to re-assess the current need for loan impairment charges. The assessment of any impairment on the individual loans is based on the borrower's present and expected future financial position and on the value of the ship's mortgage and any other collateral.

The overall guidelines for loan impairment charges are laid down in the Executive Order on Financial Reporting. The executive order stipulates that, in addition to individual impairment charges, the company must also make collective loan impairment charges.

The Danish FSA has accepted that Danish Ship Finance may omit to make collective loan impairment charges provided that the assessment of the individual loans be planned in such a manner that the assessment in practice covers an assessment consistent with that which would take place in a collective assessment and that loan impairment charges be made accordingly for each loan. Furthermore, it is a precondition that the assessment of any impairment of the individual loans be made on the basis of a probability weighting of the expected outcome in respect of payments from the borrowers.

The Danish FSA's guidelines for loan impairment charges thus assume:

- that all loans are subjected to an individual assessment;
- that the criteria for objective evidence of impairment at the individual assessment in addition to the individually conditioned criteria comprise all external developments, factors and events (observable data) that increase the likelihood of losses on the type of loans that the specific loan belongs to; and
- that each loan is tested for impairment for all the identified criteria for objective evidence of impairment based on the likelihood with which they are expected to reduce the cash flow from the loan.

Based on the FSA guidelines, all loans have been reviewed in order to identify any objective evidence of impairment (OEI) for the loan in question. It is also established whether a vessel segment is comprised by OEI for collective impairment charges.

All loans are reviewed to evaluate whether the existing classification and probability of default still provides the best estimate of the cash flows due from the specific borrower. Where this is estimated not to be the case, the loan has been reclassified.

Objective evidence of impairment

Objective evidence of impairment (OEI) is a concept used to express that a loan entails a higher probability of default. The concept is used for calculating individual impairment charges pursuant to Annex 10 of the Executive Order on Financial Reporting and the Danish FSA guidelines.

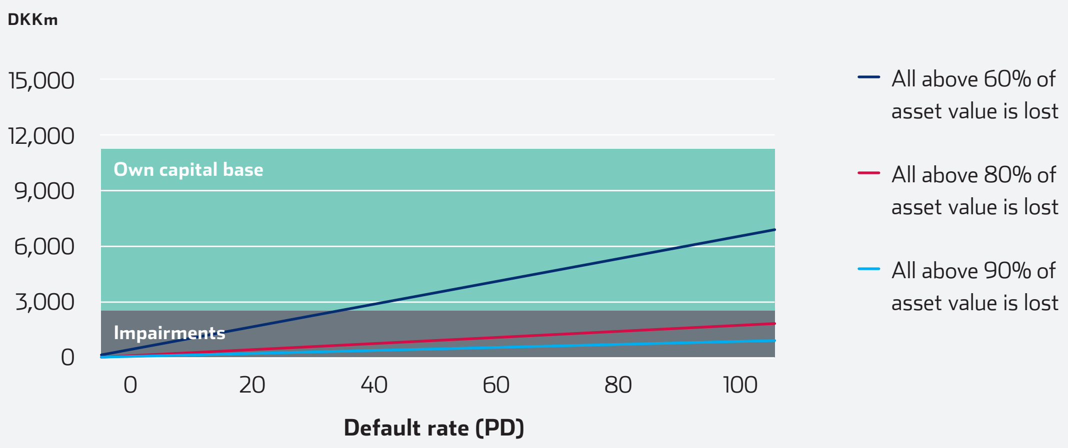
OEI exists if at least one of the following events has occurred:

- Default, cf. below
- The borrower is experiencing significant financial difficulty
- Past due/arrears, unless the problem is short-term and the amounts concerned are small by comparison to the borrower’s financial situation or if due to errors or technical problems
- Loans with more lenient repayment terms, including forbearance, which the company, for reasons relating to the borrower’s financial difficulty, would not otherwise have granted

If OEI is established for credit exposures, including loans without loan impairment charges, the borrower will be downgraded on the company’s internal classification scale (12-point scale with 12 being the weakest) to risk category 11 (or risk category 12 if the credit exposure is also in default) with a PD (probability of default) of 100%. Loans with OEI, i.e. loans in risk categories 11 or 12, are referred to as “Problem loans”.

When reconstruction, including agreements for composition or conversion of a loan into share capital/subordinated loan capital, has been completed, the OEI period will run for at least 12 months. Subsequently, a new impairment test will be performed on the credit exposure.

LOAN LOSSES AT GIVEN DEFAULT RATES



The chart is based on the own funds of the subsidiary.

Default

A loan is deemed to be in default if the borrower is not expected to be able to meet his obligations. That will be the case, if at least one of the following situations has occurred:

- A loss is deemed inevitable
- Bankruptcy or other in-court reconstruction
- Past due/arrears in 90 days or more
- Foreclosure
- Non-accrual interest

If a credit exposure is in default, the borrower will be downgraded to risk category 12 with a PD of 100%.

Calculation of loan impairment charges at credit exposure level

The company makes individual impairment charges on loans with objective evidence of impairment and also charges with a collective component on loans to customers operating in shipping segments in which the earnings prospects give rise to expect future losses but on which loans no objective evidence of impairment has been found.

The technical calculation model, which is the same for both impairment models, looks as follows:

Loan impairment = Loss given default (LGD) x probability of default (PD) – potential dividends (prudent estimate).

The individual customer's PD is determined on the basis of an internal classification system (rating) and it reflects a conservatively estimated likelihood of objective evidence of impairment being established for the customer within the next 12 months.

LGD is calculated in the following manner:

Loss given default = Market value of the loan (B) – the estimated collateral value of the ship's mortgage in a weak market (Sx) – the value of any other collateral (Ø).

For customers where individual objective evidence of impairment is established due to financial difficulty on the part of the customer, the PD is set at 100%. For impairment with a collective component, the customer's current PD is used.

The following serves to illustrate the calculation method for impairment with a collective component:

Customer's PD = 25%
Loans (B) = DKK 100 million
Market value of vessel = DKK 125 million
The estimated mortgage value of the mortgaged vessel(Sx) = DKK 70 million
Other collateral (Ø) = DKK 0 million
Dividends (D) = DKK 0 million
LGD = B – Sx – Ø = DKK 100 million – DKK 70 million – 0 = DKK 30 million
Impairment = (LGD x PD) – D = (DKK 30 million x 0.25) – 0 = DKK 7.5 million

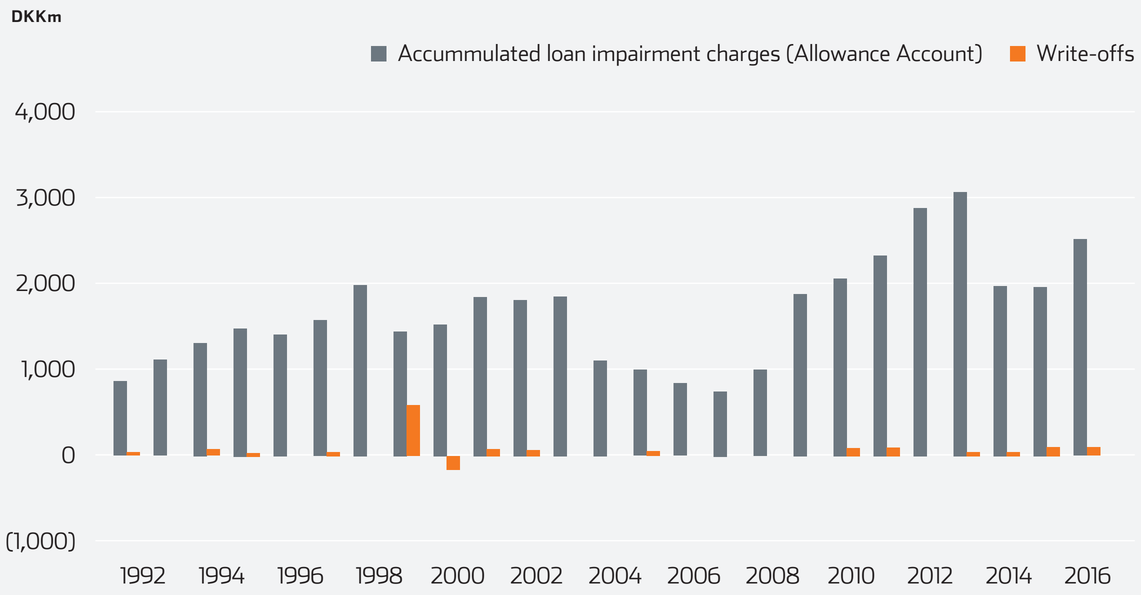
If the customer had individual objective evidence of impairment (a PD of 100%) in the above example, the impairment charge would instead have been DKK 30 million. In a few situations where the model is believed to either overestimate or underestimate the impairment, an adjustment is made on the basis of a management estimate.

The accumulated loan impairment charges amounted to DKK 2,516 million at 31 December 2016, against DKK 1,958 million at 31 December 2015.

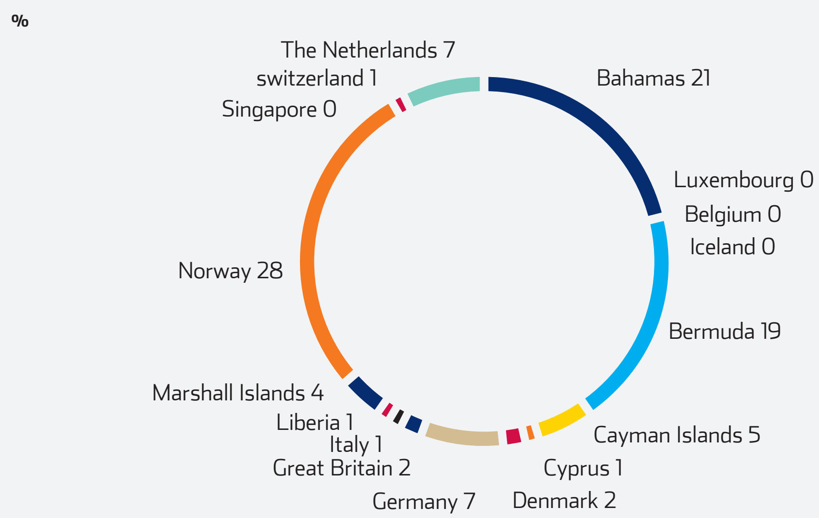
The accumulated loan impairment charges accounted for 5.9% of total loans and guarantees, against 4.3% at the end of 2015. Danish Ship Finance recorded net write-offs in the amount of DKK 89 million in 2016, against DKK 90 million in 2015. Write-offs thus remain at a very low level.

Accumulated write-offs since the company was established in 1961 were approximately DKK 1.1 billion at 31 December 2016. This corresponded to 2.6% of total gross lending at 31 December 2016.

ACCUMULATED LOAN IMPAIRMENT CHARGES AND WRITE-OFFS

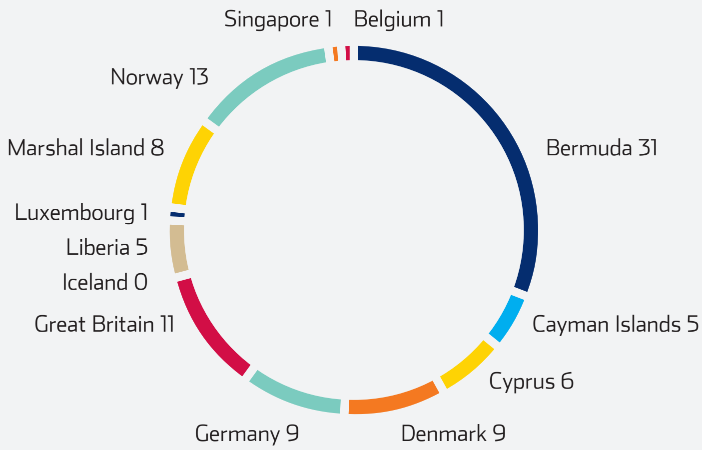


GEOGRAPHICAL DISTRIBUTION OF TOTAL IMPAIRMENT CHARGES



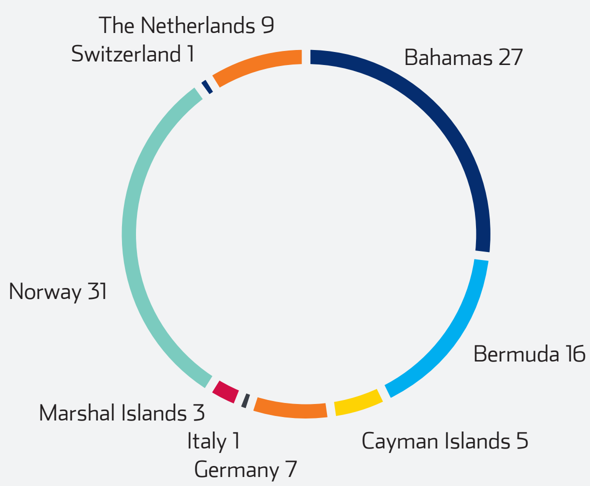
GEOGRAPHICAL DISTRIBUTION OF COLLECTIVE IMPAIRMENT CHARGES

%



GEOGRAPHICAL DISTRIBUTION OF INDIVIDUAL IMPAIRMENT CHARGES

%



DEVELOPMENTS IN IMPAIRED CLAIMS DUE TO VALUE ADJUSTMENT AND LOAN IMPAIRMENT CHARGES

DKKm	Loans 2016	Loans 2015	Financial counterparties 2016	Financial counterparties 2015
Individual impairment charges				
Impairment charges for loans and counterparties, 1 January	1,047	1,364	0	0
Impairment charges during the year	1,100	17	0	0
Reversal of impairment charges made in previous financial years, where there is no longer any objective evidence of impairment or the impairment is reduced	77	244	0	0
Other movements	0	0	0	0
Final loss (written off) on previous impairment charges	95	90	0	0
Accumulated impairment charges for loans and financial counterparties, 31 December	1,977	1,047	0	0
Sum of loans and financial counterparties where individual impairment charges have been made (calculated before impairment charges)	6,997	4,174	0	0
Impairment charges with a collective component				
Accumulated impairment charges for loans and financial counterparties, 1 January	910	610	0	0
Impairment charges during the year	59	375	0	0
Reversal of impairment charges, where there is no longer any objective evidence of impairment or the impairment is reduced	430	75	0	0
Other movements	0	0	0	0
Accumulated impairment charges for loans and financial counterparties, 31 December	540	910	0	0
Final loss (written off)	0	0	0	0
Sum of loans and financial counterparties where collective impairment charges have been made (calculated before impairment charges)	21,684	23,838	0	0

Accounting standards not yet in force

The IASB (International Accounting Standards Board) has issued a new accounting standard, IFRS 9, on financial instruments to replace IAS 39.

IFRS 9 was approved by the European Commission on 22 November 2016 and is expected to be effected for financial years starting on 1 January 2018.

For the past 18 months, the company has analysed the need for system adjustments and possible operational procedures pertaining to the implementation of the impairment provisions of IFRS 9. This work will be finalised in 2017. IFRS 9 is scheduled to be implemented in the Executive Order on Financial Reporting during 2017 and have effect for financial years starting on 1 January 2018.

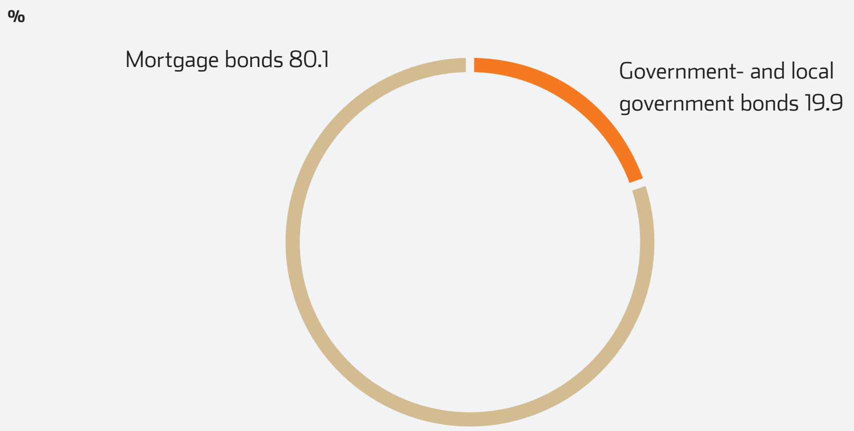
At the end of 2016, the company initially assessed that the new accounting standard would have a small negative impact on its accumulated loan impairment charges.

Financial counterparties

In addition to loans, the company's securities portfolio also represents a significant part of the assets. The securities portfolio comprises government and mortgage bonds, money market transactions and interest-sensitive financial instruments.

Most of the portfolio consists of mortgage bonds, which leads to an excess cover relative to the statutory requirement that at least 60% of the own funds requirement must be invested in high grade assets. At 31 December 2016, the market value of DKK 20,347 million was invested in high grade securities, corresponding to 371% of the statutory requirement.

DISTRIBUTION OF SECURITIES PORTFOLIO IN PCT



Transactions with financial counterparties are made in connection with investing own funds as well as excess liquidity from issued bonds. These transactions involve cash deposits, securities and financial instruments.

Financial contracts may entail a risk of losses if the contract has a positive market value, and the financial counterparty cannot fulfil its part of the agreement. This type of risk also includes settlement risk.

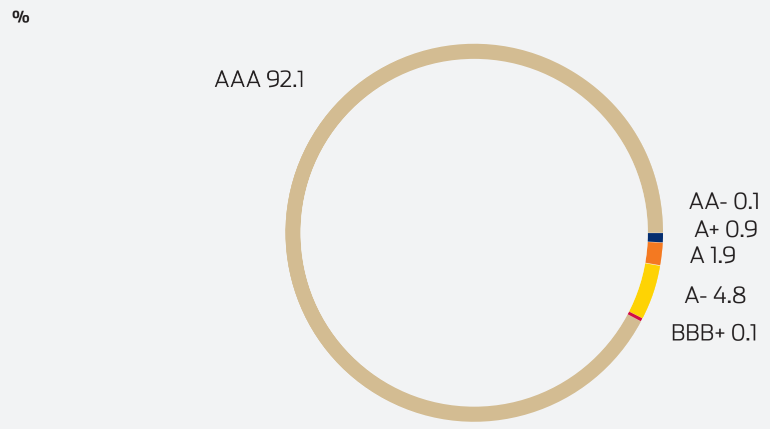
The policy for managing counterparty risk (counterparty policy) quantifies and defines limits for the exposure to individual financial counterparties and the countries in which such counterparties are residents. The counterparty policy is used in connection with the management of market risk and liquidity risk defines limits for maximum receivables (lines) under loans to and guarantees from credit institutions, export guarantee institutions and insurance companies. The policy also includes the Executive Board’s guidelines and options for delegating granting authorities.

Emphasis is on financial counterparties having high credit ratings, as a substantial proportion of business transactions with the counterparties involves long-term contracts with a potentially large increase in market value. Bilateral collateral agreements (CSA) have been signed with a number of bank counterparties, which reduce the credit risk.

Granting of lines

Financial counterparties are granted lines on the basis of defined criteria. Such approvals are made on the basis of, among other things, ratings assigned by recognised international rating agencies, when such ratings are available. Twice a year and when the financial standing of the counterparty changes, the allocated lines are re-assessed.

EXPOSURE ON FINANCIAL COUNTERPARTIES BY CREDIT RATING



The Executive Board and the Head of Credit have been allocated authorities by the Board of Directors allowing them to approval lines to financial counterparties within certain limits. Such authorities must within specific limits be disclosed at the subsequent board meeting. Lines the predefined limits are granted by the Board of Directors.

Legal framework

The legal framework for transactions with financial counterparties is based primarily on market standards such as ISDA and GMRA agreements, which allow netting in the case of default on the part of the financial counterparty. Furthermore, Danish Ship Finance has entered into agreements on market-value adjustments or collateral (CSA agreements) with a number of its counterparties in connection with derivative trading.

Ongoing monitoring

Exposures to each counterparty are monitored in an ongoing process, partly to ensure that the financial counterparties consistently comply with the requirements, partly to ensure compliance with the granted lines. The responsibility for ongoing monitoring is independent of the executing departments.

MARKET RISK

Market risk is the risk of losses caused by changes in the market value of assets and liabilities as a result of changing market conditions. The overall market risk is calculated as the sum of fixed income and exchange rate positions. The most significant market risks are associated with the securities portfolio, as the company is governed by the limits of the Bond Executive Order, which includes restrictions on interest rate, exchange rate and liquidity risk between the bond issues (funding) and the loans.

The company pursues a market risk policy to manage its market risks. The policy lays down clear and measurable limits for interest rate and exchange rate risks and builds on the provisions of the Bond Executive Order, among other things. The guidelines for market risks may be stricter than such external provisions.

The company's treasury department has the day-to-day responsibility for the market risk policy, while the responsibility for the current calculation and reporting of market risk lies with a function outside the treasury department. Market risks are monitored in an ongoing process and reported to the Board of Directors on a quarterly basis. In case of breach of the limits defined in the market risk policy, the Executive Board must be informed immediately and the Board of Directors not later than at the next board meeting.

Interest rate risks

Interest rate risk is the risk that the company will incur a loss as a result of a change in interest rates. Rising interest rates have an adverse impact on the market value of the securities portfolio.

Pursuant to the Bond Executive Order, the interest rate risk between funding and lending must not exceed 1% of the own funds. The company seeks to minimise the interest rate risk between funding and lending by applying conservative principles, but a loss or a gain may arise due to changes in interest rates.

The company has only moderate exposure to interest rate risk outside the trading portfolio because of the balance principle. At 31 December 2016, interest rate risk outside the trading portfolio was calculated at DKK 33 million, against DKK 76 million in 2015.

The Bond Executive Order also stipulates that the interest rate risk on assets, liabilities and off-balance sheet items must not exceed 8% of the own funds. Furthermore, interest rate risks are adjusted using a minimum and a maximum for the option-adjusted duration. The current maximum option-adjusted duration on the securities portfolio, including financial instruments, has been restricted to four years. Danish Ship Finance has calculated the option-adjusted duration at approximately 1 year at 31 December 2016.

Using the Danish FSA's guidelines for calculating interest rate risk in the trading portfolio, the risk was calculated at DKK 226 million at 31 December 2016, corresponding to 2.5% of the own funds, against DKK 665 million in 2015.

Furthermore, there are restrictions for interest rate risk distributed on maturities between 0.5 years and 30 years. The table below shows the interest rate risk broken down by maturities.

INTEREST RATE RISK BY MATURITIES

DKKm	0.5 year	2 year	5 year	10 year	15 year	30 year
2016	27	39	46	(30)	26	17
2015	50	46	79	29	9	15

Exchange rate risk

The Bond Executive Order stipulates that the combined exchange rate risk on assets, liabilities and off-balance sheet items must not exceed 2% of the own funds.

The market risk policy does not accept exchange rate risks arising due to mismatch of funding and lending except for inevitable, limited foreign exchange risks resulting from the ongoing liquidity management. The company's lending margin is collected in the same currency in which the loan was granted. Accordingly, net interest income from lending is affected by exchange rate fluctuations. The primary impact derives from the USD, which is the currency in which the vessels primarily generate earnings and are valued, and therefore also the preferred lending currency.

Exchange rate indicator 1 at 31 December 2016: DKK 397 million, equal to 4.5% of the own funds. Exchange rate indicator 1 corresponds to the company's overall net exposure in foreign currency on the total balance sheet items, calculated according to the guidelines of the Danish FSA.

Equity risk

Apart from small holdings of sector shares and shares received in connection with the reconstruction of credit exposures, the company has no shareholding interests in other companies.

Derivatives

Danish Ship Finance uses derivatives in specific areas. The market risk policy specifies which derivatives the company may use and for which purposes. These are transactions made to hedge risks between funding and lending and in connection with investment activities.

LIQUIDITY RISK

The company's liquidity management efforts and the liquidity requirements defined by law are aimed at reducing the liquidity risk to the greatest extent possible.

Liquidity risk involves the risk of:

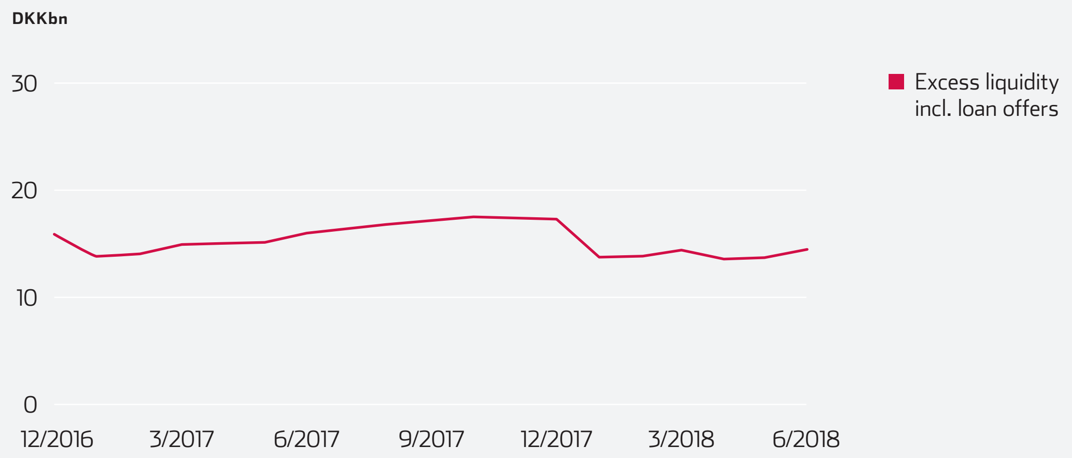
- a disproportionate rise in the cost of funding;
- the company not being able to meet its payment obligations due to lack of funding.

Through bond issues and the existence of a liquid portfolio of bonds, the company has secured ample liquidity coverage for all existing loans and loan offers until expiry. The company is therefore not exposed to any refinancing risk. A potential downgrade of the company's external rating would not change its robust liquidity situation, but it is expected to lead to higher funding costs in connection with new loans.

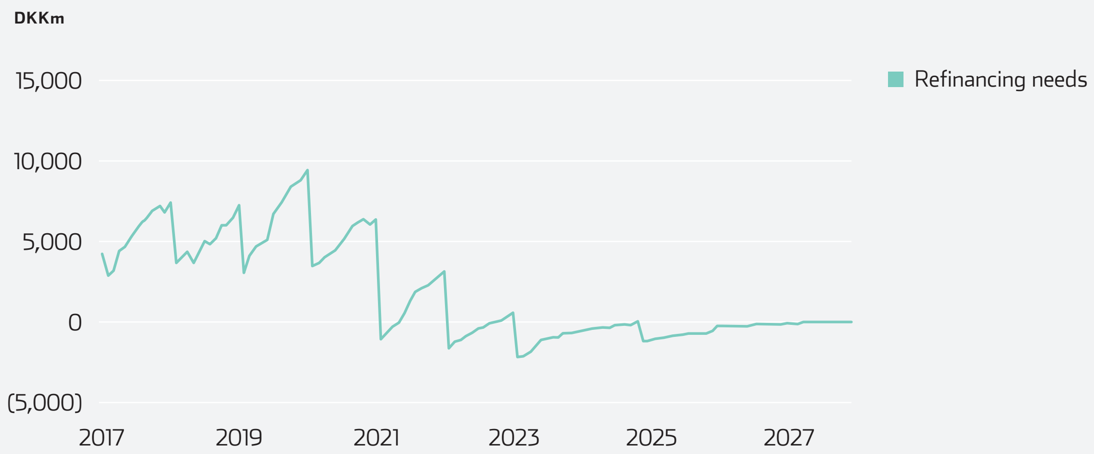
Shown below are charts of:

- Short-term excess liquidity including the market value of the securities portfolio
- Liquidity mismatch between funding and lending

SHORT-TERM LIQUIDITY



LIQUIDITYMISMATCH BETWEEN FUNDING AND LENDING



The average maturity of issued bonds exceeds the average maturity of the loans.

LIQUIDITY COVERAGE RATIO

Effective on 1 October 2015, the CRR introduced a requirement on adequate liquidity over a period of 30 days in a stressed scenario (LCR requirement). The LCR requirement will be phased in over a number of years.

Shown below is the LCR requirement for 2016:

$$\text{Liquidity Coverage Ratio} = \frac{\text{Liquid Assets}}{\text{Net liquidity outflows over a 30 days stress period}} \geq 70\%$$

The company's LCR at 31 December 2016 has been calculated at 631%.

In the calculation of liquid assets, covered bonds may not account for more than 70%, and at least 30 percentage points thereof must be covered bonds with a rating corresponding to credit category 1, which corresponds to S&P's AAA to AA- rating.

The 70% cap on covered bonds entails that the company has a substantial volume of mortgage bonds which are not eligible for inclusion as liquid assets. If these mortgage bonds are sold and government bonds are purchased instead, it would significantly increase the LCR.

PLEDGED ASSETS

The procurement of capital is made primarily via issuance of ship mortgage bonds on Nasdaq Copenhagen. The company is a component of the OTC market. As a result of this set-up, some assets will be pledged, cf. the European Banking Authority's (EBA) Guidelines on disclosure of encumbered and unencumbered assets.

The primary sources of pledging assets are:

- Issuance of ship mortgage bonds
- CSA collateral

Combined, pledged assets account for 74% of total assets plus collateral received that may be subject to pledging.

Information disclosed about pledged assets and collateral received is based on data at 31 December 2016 instead of median values for 2016. A specification of pledged assets is set out in annex 8.

OPERATIONAL RISK

The Board of Directors has defined a policy for operational risk, the purpose of which is to create an overview of operational risks and minimise the number of errors with a view to reducing losses caused by operational errors.

Operational risk is managed across the organisation through a comprehensive system of business procedures and control measures developed to ensure a satisfactory process environment.

Efforts to mitigate operational risk include segregation of functions between execution and control of the activity.

Operational errors are divided into three main groups by value:

- Small errors (<DKK 25,000)
- Medium-sized errors (DKK 25,000 – DKK 5 million)
- Large errors (> DKK 5 million)

Small errors are reported to the head of department. Medium-sized and large errors are reported to the Executive Board, and the Board of Directors must be informed about large errors.

REMUNERATION POLICY

The company has drawn up a remuneration policy covering the Board of Directors, Executive Board and all employees. Owing to the company's size, the Board of Directors has not set up a remuneration committee.

The Board of Directors defines the remuneration policy and reviews the policy at least once a year to realign it with the company's progress. The remuneration policy is approved by the general meeting.

Any variable salary to risk takers will be based on performance targets, existing and future risks attached to such results and the capital expenses, liquidity and credit risk required to obtain the results.

Most of the employees are covered by collective agreements and receive a fixed salary based on capabilities, experience and job function. In addition, employees may be awarded a bonus when specifically assessed to have performed beyond expectations in a calendar year. When deemed relevant by the Executive Board, key employees may also be offered a retention bonus.

Other employees are employed on individual contracts, including managerial-level employees. These employees receive a basic salary with the option of a bonus based on pre-defined criteria.

For members of the Executive Board and other risk takers and persons in designated functions, the variable salary component must not exceed 50% of the fixed basic salary including pension. At least 50% of the variable remuneration must consist of instruments such as bonds (senior contingent notes), shares, phantom shares or a combination thereof.

The variable salary components are subject to deferment requirements (four years for the Executive Board, other risk takes and persons in designated functions) and requirements on retention (lock-up) in accordance with the applicable statutory requirements.

There is no agreement on variable remuneration of the Board of Directors.

Set out below is information about all quantitative disclosures relating to remuneration, broken down by business area and for the Board of Directors, Executive Board, control functions and employees designated as material risk takers:

DKK'000	**Customer area**	**Finance and investment area**	**Other activities**	
Total variable remuneration for the 2016 financial year by business area	-	-	-	
	Board of Directors	**Executive Board**	**Control functions**	**Other material risk takers**
Total amount for the 2016 financial year distributed on fixed and variable remuneration				
- Number of full-time employees	9	2	5	6
- Number of employees designated as material risk takers at 31 December 2016	-	-	-	-
- Fixed remuneration	2,011	8,083	3,237	10,180
- Variable remuneration	-	3,459	-	-

Distribution of variable remuneration in 2016				
- Cash	-	1,729		
- Shares	-	-	-	-
- Share-based instruments	-	-	-	-
- Other	-	1,729	-	-
Variable remuneration earned in 2016 by disbursement form				
- Paid out	-	692	-	-
- Deferred	-	2,767	-	-
Sign-on fees and severance payments in 2016				
- Sign-on fees paid	-	-	-	-
- No. of recipients	-	-	-	-
- Severance payments	-	-	-	-
- No. of recipients	-	-	-	-
Amount provided for severance payments in 2016				
- Total amount	-	-	-	-
- Largest provisions for severance payments	-	-	-	-
- No. of recipients	-	-	-	-
Outstanding deferred remuneration				
- Outstanding deferred remuneration regarding previous years	-	-	-	-
- Payment in 2016 of deferred remuneration from previous years	-	-	-	-
- Forfeited deferred remuneration in 2016	-	-	-	-
- Reduced				
- Earned deferred remuneration in 2016	-	-	-	-
- Deferred remuneration at 31 Dec. 2016	-	2,767	-	-

No persons received a salary in excess of EUR 1 million in the financial year.

MANAGEMENT'S STATEMENT

The Board of Directors of Danish Ship Finance A/S (Danmarks Skibskredit A/S) and Danish Ship Finance Holding A/S (Danmarks Skibskredit Holding A/S) approved the risk report for 2016 on 28 February 2017.

The Board of Directors finds that the Group's risk management procedures are adequate and provide assurance that the risk management systems are adequate in relation to the Group's profile and strategy.

The Board of Directors also finds that the Group's overall risk profile in relation to its business strategy, business model and key figures provide a relevant and comprehensive picture of the Group's risk management, including how the risk profile and the risk tolerance defined by the Board affect each other.

The Board made its assessment on the basis of its adopted business model/strategy, material and reports presented to the Board by the Executive Board, internal controls, risk managers and compliance officers and on the basis of any supplementary information or reports obtained by the Board. A review of the business model and policies shows that the overall requirements set out in the model for specific risk areas are fully reflected in the more specific limits of the individual policies.

Focus is on the most creditworthy part of the shipping industry. The Group seeks to obtain profitable earnings by pricing its products to reflect the risk and the working capital assumed by the Group in combination with an overall assessment of the business volume with customers and counterparties. The Group seeks to ensure it has an appropriate and robust capital base supporting its business model.

The maximum risk tolerance defined by the Board of Directors is managed via limits set out in the individual policies. Shown below are a number of key figures that provide external players with an overview of the Group's and the subsidiary's risk management.

	Legislation	Group compliance at 31 December 2016	Solo compliance at 31 December 2016
Capital requirement			
Capital ratio	>8%	15.8 per cent	17.2 per cent
Tier 1 capital ratio	>6%	12.0 per cent	17.2 per cent
Common equity tier 1 capital ratio	>4.5%	12.0 per cent	17.2 per cent
Pillar II requirement			
Solvency need capital ratio	<capital ratio	Excess cover is 5.9 percentage points	Excess cover is 7.4 percentage points
Combined buffer requirement	<capital ratio	Excess cover is 5.1 percentage points	Excess cover is 6.5 percentage points
Liquidity			
Liquidity Coverage Ratio (LCR)	>70%	631%	631%
Gearing			
Leverage ratio	>3% (Basel III recommendation)	12.4%	13.6%
Write-offs			
Realiserede tab på udlån	N/A	Write-offs represent < 0.10% of lending	Write-offs represent < 0.10% of lending

Copenhagen, 28 February 2017

BOARD OF DIRECTORS

Anders Damgaard	Christopher Rex	Eivind Drachmann Kolding
Henrik Sjøgreen	Henrik Rohde Søgaard	Marcus Freuchen Christensen
Michael Nellemann Pedersen	Peter Nyegaard	Povl Christian Lütken Frigast

DANISH
SHIP FINANCE

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