



At a Glance

SEB MERCHANT BANKING - CREDIT RESEARCH

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Landshypotek AB

A2/Stable/P-1
BBB+/Stable/A-1
A/Stable/F1

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On the road to covered bonds

- Landshypotek specialises in lending to the Swedish agricultural and forestry sectors and holds a 50% share of first mortgage lending in this market and a third of total lending to the Swedish agricultural and forestry sectors.
- Landshypotek's membership base is gradually contracting due to consolidation within the agricultural sector, while subsidiary lending has ceased due to asset quality problems. Nonetheless, group lending has been stable. Landshypotek's gross lending has increased by an average of 3% annually over the past seven years.
- We maintain our view of Landshypotek's A- credit based on its strong market share in mortgage lending to the agricultural and forestry sectors in Sweden and the solid capitalisation of its stable core agricultural mortgage lending portfolio. We upgrade our outlook to stable from negative reflecting positive asset quality trends with reductions, from high levels, of problem loans and net loan losses. Our view takes into account the sincerity of management's intentions to reduce non-core lending at subsidiary level.
- We regard the introduction of Swedish covered bond legislation as a positive development. Following conversion to covered bond status, investors will benefit from better protection. Landshypotek has stated its ambition to issue covered bonds, which became possible under Swedish law in July 2004. We believe that Landshypotek will probably make its application to the Swedish Financial Supervisory Authority (SFSA) by the turn of the year to enable conversion during H2-2006.
- Landshypotek's bond spreads have recently tightened considerably. The spread contraction has significantly exceeded the general market's tightening primarily reflecting the anticipated conversion to covered bonds. Consequently, we believe only limited potential remains for Landshypotek's bonds to tighten further.

SEB

Business risk profile

First mortgage agricultural and forestry lending

Landshypotek specialises in first mortgage lending to the Swedish agricultural and forestry sectors and enjoys a strong market position as the largest provider of mortgage loans to these sectors. Landshypotek holds a market share of first mortgage lending of nearly 50% and a third of total lending to the Swedish agricultural and forestry sectors.

All lending is against collateral

Lending activities are administered by Landshypotek's 10 regions, providing a competitive advantage in the form of proximity to and a close relationship with clients as well as a strong local knowledge useful when assessing the value of collateral. All lending is provided against collateral, the majority of which takes the form of first mortgage deeds against agricultural properties. Loans granted represent no more than 75% of the value of the property serving as collateral although the loan to value ratio is usually lower. On average the portfolio of loans amounts to around one third of the assessed value of the properties.

An economic co-operative with 62,000 members

The parent company Landshypotek Ekonomisk Förening (LEF) is an economic co-operative with around 62,000 members who are also Landshypotek's borrowers. Borrowers become members of LEF and are required to maintain a capital contribution to LEF equivalent to 8% of their loan principal, thereby participating in the group's capitalisation. Capital contributions are used to subscribe to shares in Landshypotek. As a result, Landshypotek receives substantial capital injections through retained earnings as lending grows. Over the past five years shareholders' equity has grown at an annual average rate of 6%, although equity increased only 2% in 2004. In return members receive a share in LEF's surplus through dividends and interest received on capital contributions.

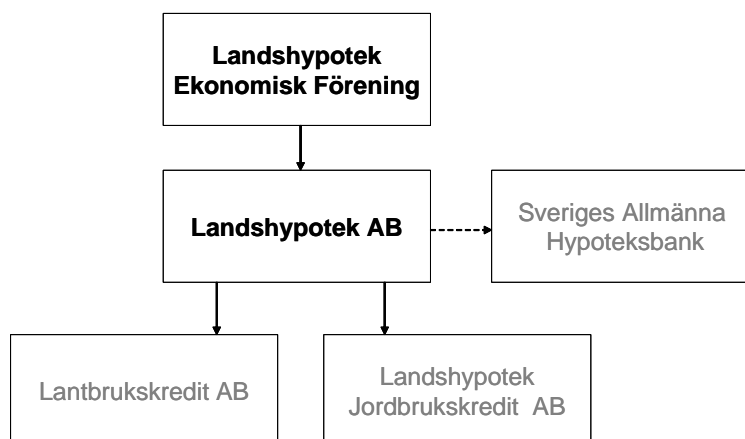
Promotes the interests of its members rather than maximise profits

The choice of an economic co-operative as the preferred business form reflects the Group's main objective, which is to promote the financial interests of its members, and to provide them with competitive lending, rather than maximise profits. Instead of a profitability target, Landshypotek has a Tier 1 capital ratio target of 8%.

Co-operation agreement with Länsförsäkringar

In 1998, Landshypotek entered into a co-operation agreement with the insurance group Länsförsäkringar and its bank subsidiary Länsförsäkringar Bank (LF Bank; A3/A-). This enables Landshypotek to offer its members a wider range of financial services, including bank credit, payment services and insurance products, while at the same time gaining access to Länsförsäkringar's nationwide retail network. It offers to Landshypotek the possibility of diversifying its earnings base and increasing its fee-based income. However, so far net fee and commission income only comprises a small fraction of Landshypotek's revenues.

Organisational chart



Source: Company reports, SEB Merchant Banking

Landshypotek funds its operations in capital markets

The company's core business is concentrated within Landshypotek AB, where lending is handled by twelve regional sales offices, while borrowing is processed centrally. Landshypotek is funded in capital markets. Desired flexibility is achieved through the use of several borrowing programs and credit facilities.

LBK lending was halted in 2003 following a sharp increase in large exposures and problem loans

Landshypotek AB has two subsidiaries, Lantbrukskredit AB (LBK) and Landshypotek Jordbrukskredit AB (LJBK), whose borrowers do not automatically become members of LEF. LBK's lending policy has so far differed from that of Landshypotek with lending focused primarily on the food industry and other industries related to the agricultural sector including both the forestry and energy sectors. The subsidiary has financed a wider range of assets than Landshypotek and received assets other than land as collateral including guarantees and corporate mortgages. LBK's lending was halted in July 2003 following a sharp increase in large exposures, problem loans and provisions for possible credit losses. Consequently, LBK's lending to the public has fallen significantly to SEK 1.4bn at December 31, 2004 from SEK 2.8bn at December 31, 2002 and now accounts for 4% of group lending. LJBK's borrowers have been encouraged to become members of LEF, and as a result, virtually the entire loan portfolio in LJBK has been transferred to Landshypotek.

GMB administers the run-off of existing debt, with most maturing in 2005

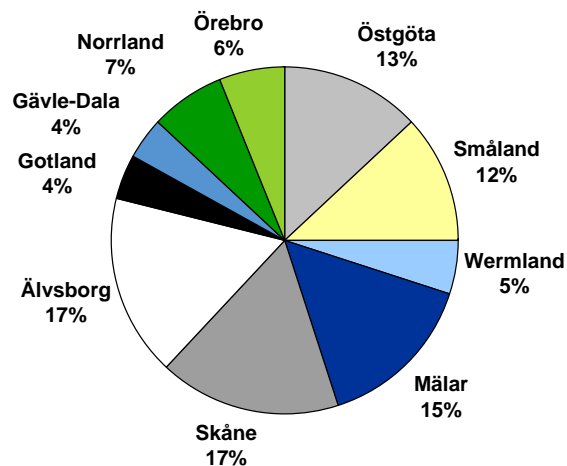
Until 1997, Landshypotek's primary funding vehicle was Sveriges Allmänna Hypoteksbank, or the General Mortgage Bank (GMB). Subsequently, Landshypotek has assumed responsibility for arranging its own funding with GMB now existing solely to administer the run-off of existing debt most of which has been redeemed in H1-05 (YE-04: SEK 620m; H1-05; SEK 4.7m). The company's longest longest-dated bond matures in 2014, however the goal is to redeem remaining bonds and dissolve the operations in 2006.

Market description

Decline in the number of borrowers, although lending volumes remain stable

A combination of consolidation in the agricultural sector and Landshypotek's focus on the Swedish market implies fairly limited growth prospects. The Group's membership base is gradually contracting as the number of farms in Sweden declines. There were around 62,000 members in 2004, compared to nearly 85,000 seven years ago. The decline in the number of borrowers reflects restructuring of the agricultural industry in favour of larger production units and therefore larger loan exposures. A substantial proportion of Landshypotek's lending is to the forestry sector, which has a high proportion of private owners and rising asset values among other things due to the asset class attracting investments by wealthy private individuals. Landshypotek's gross lending has been stable with an average annual increase of 3% over the past seven years. Lending is geographically dispersed across Sweden with concentrations reflecting the relative importance of agriculture in various regions.

Landshypotek's lending by region (excluding LBK) by year-end 2004



Source: Company reports, SEB Merchant Banking

Intense competition for credits to the agricultural sector

The market for first mortgage loans for agricultural properties is characterised by a relatively low interest margin and an administration that requires more industry knowledge and expertise than housing financing. The first mortgage lending rate is relatively low compared to the rate on loans for single family homes, despite the fact that the capital coverage requirement is twice as high for loans for agricultural properties. The Nordic credit market has undergone restructuring in recent years, marked by mergers and co-operation agreements. Although the number of banks is shrinking, more players have become active in the market for credits to agriculture and forestry. As a result the competitive situation has become considerably tougher.

Landshypotek has a share of 50% of the agricultural first mortgage market

Agriculture's total indebtedness in the form of first mortgage loans is estimated to total approximately SEK 70bn. With loans of approximately SEK 33bn outstanding, excluding LBK, Landshypotek has a share of nearly 50% of the first mortgage market. The aggregate tax assessment value of Sweden's privately owned agricultural properties amounted to approximately SEK 300bn in 2004 although their market value is estimated to be nearly double this sum. Aggregate liabilities amount to approximately SEK 114bn. Based on the market value of properties, we estimate the equity ratio at 80%, indicating low industry indebtedness.

Financial risk analysis**Financial targets and accounting treatment****Focusing on Landshypotek AB and its subsidiaries**

Landshypotek AB is the relevant entity for the purposes of issuing debt in capital markets. Consequently, we have focused our financial analysis on the Group accounts of Landshypotek AB and its subsidiaries LJBK and LBK.

As a co-operative the pursuit of profit has never been main objective

Given Landshypotek's legal status as a co-operative credit group, the pursuit of profit has never been the Group's primary concern. Therefore, its ROE has generally been inferior to that of other Swedish financial institutions. However, because a substantial proportion of the operating profit is refunded to borrowers Landshypotek has a strong incentive to maintain its operating efficiency, since without a satisfactory refund Landshypotek would be unable to offer its members such competitive rates. Instead of a profitability target Landshypotek has set a Tier 1 capital ratio target of 8%.

Asset quality**Mortgage lending comprises most of the assets**

At the end of H1 2005, Landshypotek's total assets amounted to SEK 38.4bn (YE-04: SEK36.2bn, H1-04: SEK38.9bn). Like other specialised mortgage banks, assets predominantly comprise the loan portfolio, which amounted to SEK 35.3bn or 92% of assets on June 30, 2005. The Landshypotek group, which reported largely unchanged gross lending in 2004, experienced a slight increase in lending in H1-05 primarily due to a successful marketing effort within agricultural mortgage lending, but also a less rapid decrease of LBK's lending.

Credit losses have increased in recent years

Landshypotek's assets have historically been of high quality with generally very small credit losses, even during the banking crisis in the early 1990's. However, credit losses have risen in recent years due primarily to LBK's non-performing loans. All lending from this subsidiary was halted in July 2003.

LBK's losses primarily caused by a large single exposure

Currently, LBK's losses are almost entirely attributable to the single large exposure of SEK 620m (net of provisions) to the group Energisystem i Sverige AB (ESS Group). Landshypotek has put four of the Group's six operating companies into bankruptcy and has taken control of the group itself, with the aim of restructuring it and eventually eliminating its exposure. Landshypotek has made provisions totalling SEK 115m (of which SEK 75m was reported as a realised loss during H1-05) for the ESS Group. Further losses on the ESS Group can't be ruled out.

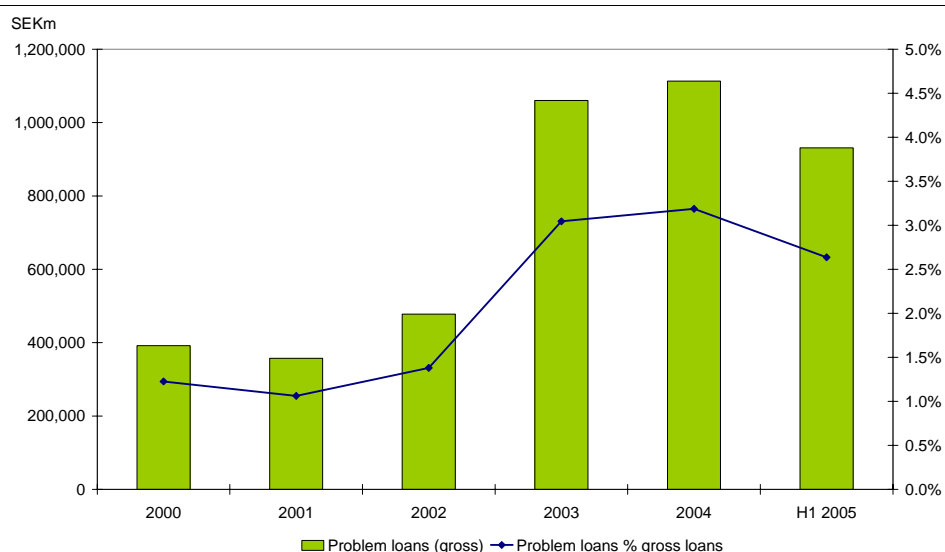
LBK's large exposures supported by guarantees

Landshypotek's first mortgage portfolio has no major exposure exceeding 10% of the capital base although LBK has some large exposures which are guaranteed by Landshypotek and LJBK. At the end of June 2005, Landshypotek and LJBK reported respective risk sharing guarantees of SEK 464m and SEK 95m, concerning LBK's ESS Group exposure. In addition LJBK has undertaken a risk guarantee of SEK 58m regarding other large exposures in LBK.

Positively, net loan losses and problem loans are decreasing

In 2004 net loan losses declined 21% compared to 2003. This positive trend continued in H1-05 with net loan losses of SEK 12m (H1-04: SEK 74m). Overall net loan losses accounted for 11% of pre-provision income (FY-04 31%, H1-04; 71%). Furthermore, problems loans, which developed negatively in 2004 increasing 5%, declined 16% in H1-05 and accounted for 2.64% of gross loans (YE-04: 3.19%, H1-04: 2.89%). As always core first mortgage agricultural lending reports insignificant asset quality problems, while LBK in H1-05 had to set aside SEK 12m for probable loan losses concerning a sawmill in Northern Sweden. The major storm that devastated forests in Southern Sweden in January 2005 has had insignificant asset quality implications.

Development of problem loans



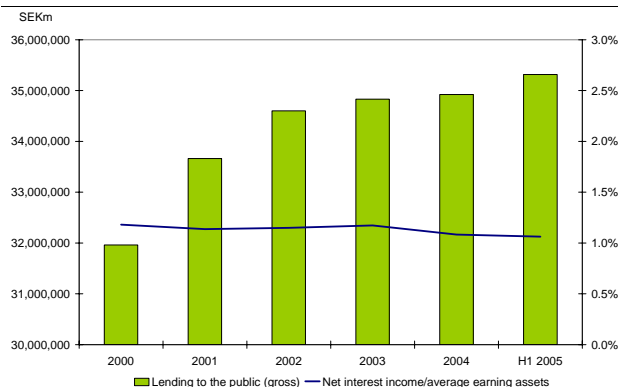
Source: : Company reports, SEB Merchant Banking

Revenues and profitability

Net interest income comprises most of the revenues

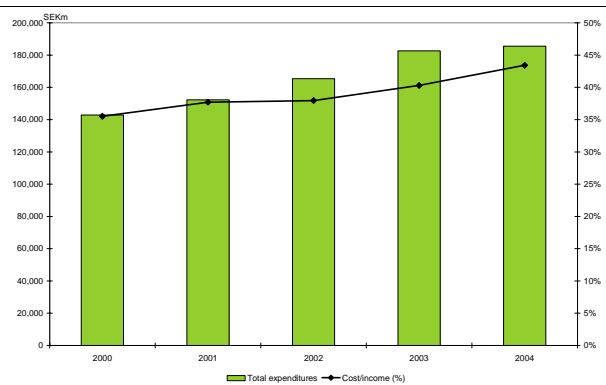
Landshypotek's revenues are derived mainly from net interest income, which in H1 2005 accounted for 92% (H1-04; 91%) of total revenues of SEK 209m (H1-04; SEK 202m). Other operating income, which in recent years has comprised a relatively insignificant 5-8% of total revenues, results from limited fee and trading income as well as income from real estate.

Development of lending and profitability



Source: Company reports, SEB Merchant Banking

Expenditures and cost to income ratio (%)



Source: Company reports, SEB Merchant Banking

Marginal pressure

Despite higher revenues, profitability has declined in recent years due to generally lower interest rates and higher costs. Furthermore, Landshypotek's loan portfolio almost exclusively comprises first mortgage loans with typically lower margins. The ratio of net interest income to average earning assets has decreased to 1.08% in 2004 from 1.18% in 2000.

Expenditures grow faster than revenues

Costs generally have increased slightly faster than income in recent years with the cost-to-income ratio rising to 43% in 2004 from 36% in 2000. A challenge for Landshypotek going forward is to maintain its low cost profile despite large projects such as BASEL II and conversion to covered bonds. In the longer term the winding down of GMB may enable the group to save some costs.

Negative trend in return on risk assets was reversed in H1

Landshypotek's return on risk assets has declined in recent years due to a combination of a slight increase in risk weighted assets, lower operating profitability and larger loan losses. In 2004 the return was 0.46% compared to 0.49% in 2003 and 0.73% in 2002. However, in H1-05 the annualised return on risk assets improved to 0.52% due to a significantly lower net loan loss charge.

Dividends have been maintained although pre-tax profit has fallen

Due to Landshypotek's legal status dividends paid to mutual members were included in the income statement until 2001. However, as a result of changes in accounting policies in 2002 dividends are now deducted directly from equity. For 2004 Landshypotek paid out SEK 200m in dividends (which is accounted for as group contributions and is therefore tax deductible). Although the dividend payment was unchanged compared to the previous year the dividend pay-out ratio was high as pre-tax operating profit fell to SEK 166m compared to SEK 174m in 2003. Positively, Landshypotek received a capital contribution of SEK 80m (2003; SEK 90m) from LEF.

Capitalisation

Solid capitalisation of agricultural mortgage lending

Consistent with Landshypotek's own objectives, its core capitalisation has improved in recent years and currently exceeds the company's 8% target. Capitalisation for the first mortgage agricultural and forestry loan book is strong as these sectors carry a 100% BIS weighting compared with 50% for mortgage loans to the household sector, while asset quality problems connected with secured agricultural lending have been very modest.

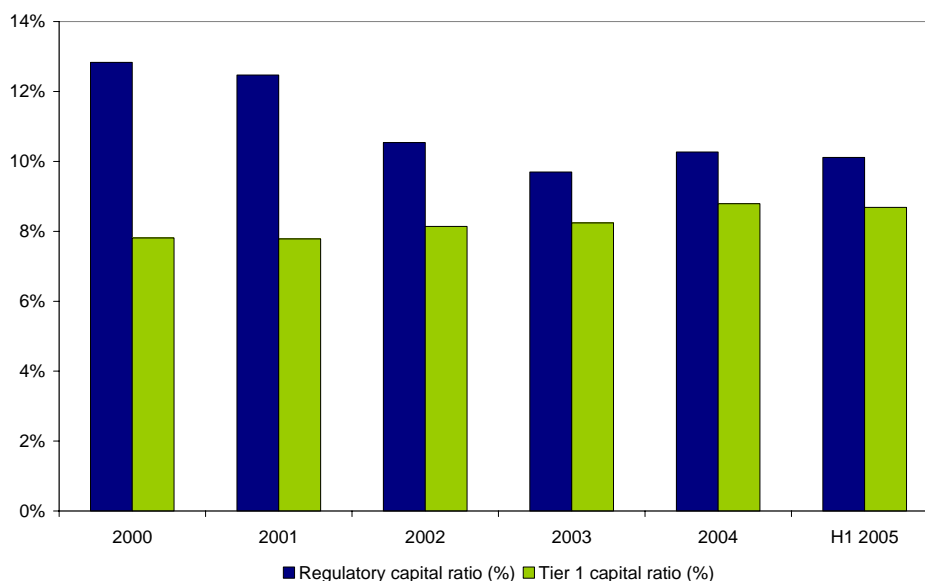
Reduced regulatory capitalisation

Landshypotek has supplemented its primary capital base by issuing dated and perpetual subordinated debt, which qualifies as Tier 2 capital. However, in recent years Landshypotek's Tier 2 instruments have matured, resulting in a reduction in the total capital ratio.

Strong core capitalisation maintained in H1-05

Landshypotek's Tier 1 and total capital ratios stood at 8.7% and 10.1%, respectively, at the end of June 2005 (YE-04: 8.8% and 10.3%, H1-04: 8.2% and 10.2%).

Landshypotek's Tier 1 and regulatory capital ratios (%)



Source: Company reports, SEB Merchant Banking

Funding

Landshypotek's primary source of funding is the Swedish capital market, although international markets are gaining in importance. Currently Landshypotek has the following borrowing sources:

- SEK 10bn Swedish commercial paper program
- SEK 20bn Swedish Medium Term Note program
- Swedish bond program unlimited by amount or time
- EUR 1bn EMTN program
- NOK bonds and certificates
- Schuldschein (in the German market)

Liquidity supported by bilateral facilities and liquid assets

To further support liquidity Landshypotek has several bilateral 364-day credit facilities in place in the Nordic market, a 5 year EUR 250m credit facility maturing in 2008 and another facility of EUR 125m maturing in 2006. In addition, Landshypotek has a portfolio of interest bearing securities (H1-05: 1.6bn). Landshypotek's liquidity policy is to have liquid assets or un-drawn credit facilities covering at least six months of maturing debt. It is actively maintaining a market in its own outstanding bonds through redemptions and exchange offers. Currency risks are limited since most lending and funding is in SEK, while foreign currency funding is hedged.

New Swedish covered bond legislation

Swedish covered bonds will carry 10% risk weighting

The introduction of Swedish covered bond legislation in 2004 is a positive development. Following conversion to covered bonds investors will benefit from better protection. As part of the new covered bond legislation Sweden introduced the 10% risk weighting for covered bonds. Swedish mortgage bonds are currently risk weighted at 20%, but when Swedish mortgage institutions convert their unsecured bonds to covered bonds, these will be eligible to carry a risk weighting of 10% for financial institutions in the countries adopting this practice, which includes Germany, Denmark, Spain, France, Luxemburg, Finland, Austria, Greece, Belgium, the Netherlands and Sweden.

Three mortgage institutions have applied for licences to convert into covered bonds

According to Swedish covered bond legislation, issuance of covered bonds requires a license from the Swedish Financial Supervisory Authority (SFSA). So far Nordea Hypotek, Stadshypotek, Swedish Housing Finance Corp (SBAB) applied for licences on May 30, September 14, and October 13, respectively. The SFSA will take around 6 months to consider these applications so we expect Nordea Hypotek to obtain a licence by end-November with conversion following around the turn of the year, while we expect Stadshypotek and SBAB to convert in Q1 and Q2 2006.

Swedish financial institutions that may convert to covered bonds

2004 (MSEK)	Landshypotek	LF Bank	Nordea Hypotek	SBAB	SEB Bolån	Spintab	Stadshypotek
Rating Moody's	A2/Stable	A3/Stable	Aa3/Stable	Aa3/Stable	--	Aa3/Positive	Aa1/Stable
Rating S&P	BBB+/Stable	A-/Stable	--	AA-/Stable	--	--	AA-/Stable
Rating Fitch	A/Stable	--	--	--	A+/Stable	AA-/Stable	AA-/Stable
Net interest income	389	830	2,111	1214	1,750	5,092	5183
Operating revenues	427	1,214	2,274	1,176	1,760	4,619	5,130
Provision income	242	171	1,823	671	1,753	4,556	4,980
Pretax income	166	127	1,507	678	1,765	4,602	5,150
Net income	121	186	1,011	485	1,271	3,313	3,708
Cost income ratio	43.40%	86%	19.70%	42.90%	0.40%	1.40%	2.90%
Net interest margin	1.08%	2.24%	0.94%	0.92%	1.07%	1.13%	1.29%
ROE (period end) (%)	3.81%	7.62%	9.65%	9.21%	16.32%	17.59%	19.47%
Return on average assets (%)	0.33%	0.49%	0.45%	0.36%	0.77%	0.73%	0.91%
Total assets	36,235	43,016	237,517	135,101	173,854	477,605	421,126
Gross loans	34,921	39,426	234,756	131,188	168,722	428,825	413,481
LLR % gross loans	0.37%	0.48%	0.01%	0.21%	0.01%	0.05%	0.06%
Problem loans % gross loans	3.19%	0.63%	0.16%	0.27%	0.10%	0.13%	0.23%
LLR % problem loans	12%	76%	8%	78%	14%	34%	26%
Tier 1 capital ratio	8.79%	11.37%	8.30%	8.40%	8.25%	8.20%	8.10%
Total capital ratio	10.27%	9.00%	9.40%	10.00%	9.48%	10.30%	8.10%
Shareholders' equity % total assets	8.76%	5.68%	4.40%	3.90%	4.50%	3.90%	4.50%

Source: Company Reports, SEB Merchant Banking

Landshypotek is likely to convert in H2-2006

Landshypotek, which aims to convert all of its long-term unsecured bonds to covered bonds, is currently upgrading its IT system and introducing new routines in the credit application and review processes. It is likely monitoring how the other Swedish mortgage institutions and primarily Spintab (which subsidiary Jordbrukskredit is a major competitor within lending to the agricultural and forestry sectors) are handling the covered bond process. We believe that Landshypotek will probably make its application to the SFSA by the turn of the year to enable conversion during H2-2006.

Moody's has adopted a structural finance approach for rating European covered bonds

In June 2005 Moody's revised its rating approach for European covered bonds, moving from a strict fundamental approach (notching) towards a structural finance approach. This revised methodology continues to employ a joint-default approach which takes into account both the credit strength of the issuing entity and the value of the cover assets. The rating of the mortgage institution therefore remains the analytical starting point, while the final covered bond rating will continue to be determined by the strength of the legal framework, any contractual commitments and the cover assets. The principal difference between the new and previous approaches is that the revised methodology enables the rating to be determined on a more quantitative basis.

We expect the major mortgage institutions focusing mainly on residential lending to obtain AAA ratings from both Moody's and S&P

In July 2005 S&P announced a policy for rating Swedish covered bonds based primarily on an assessment of the quality of the cover assets rather than on the counterparty credit rating of the issuing institution (a "de-linked" rating). S&P stated that it would assign covered bond ratings on a case-by-case basis and that it would, in principle, be possible to achieve a 'AAA' rating, regardless of the issuer's counterparty credit rating. Given the financial strength and high quality of collateral, we expect the five major mortgage institutions primarily involved in residential mortgage lending (Stadshypotek, Spintab, Nordea Hypotek, SBAB and SEB BoLån) to obtain AAA ratings on their covered bonds from both Moody's and S&P.

Covered bonds backed by agricultural mortgage lending assets are rare

However, there are few European agricultural mortgage institutions currently issuing covered bonds. This means that rating agencies are less familiar with this type of collateral than residential mortgages and public sector loans. The Swedish agricultural sector is also different from the European in that many combine agriculture and forestry activities, while families often have a second source of income from non-farming related work.

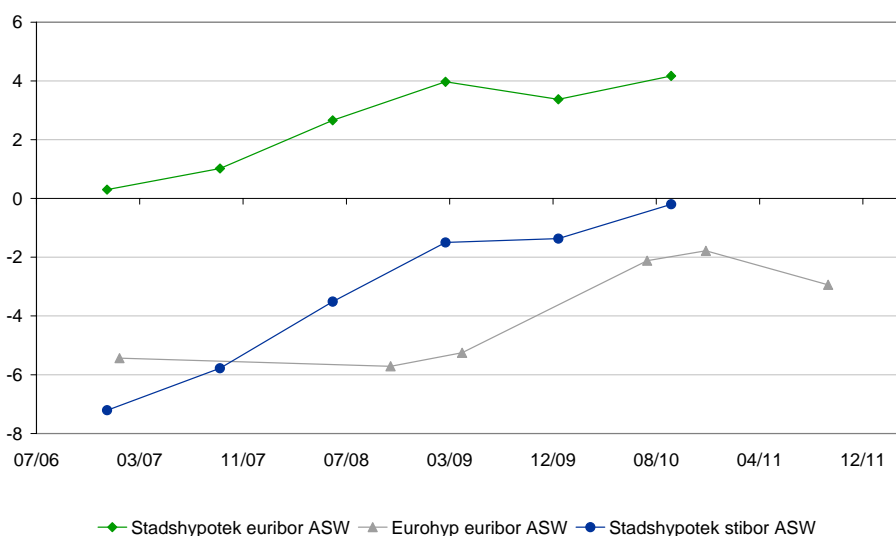
Higher over-collateralisation may be a way of offsetting rating agencies' concerns

Consequently, the rating agencies claim that they need to review the liquidity of Swedish agricultural and forestry properties, the origination and foreclosure process, the geographical diversification of the portfolio and absence of jumbo loans to determine whether it will be possible to achieve a AAA rating with cover assets comprising agricultural and forestry first mortgage loans. Landshypotek's long record of insignificant loan losses within its first mortgage lending operation and low loan to value ratios are clearly positive factors. System enhancements and improvements to credit risk management currently being implemented are also measures that probably will be regarded confidently within the covered bond due diligence process. Increased over-collateralisation may well be a way of offsetting rating agencies' concerns regarding liquidity of cover assets and refinancing risk allowing Landshypotek to obtain a AAA or at least AA rating on its covered bonds.

Spreads have tightened due to the expected conversion to covered bonds

The anticipated conversion to covered bonds has resulted in increasing demand for bonds issued by major Swedish mortgage institutions and Landshypotek with asset swap spreads tightening significantly. Spread tightening has coincided with increased interest in Swedish mortgages from foreign investors.

Stadshypotek and Eurohyp ASW spreads (mid)



Source: SEB Merchant Banking

Compare the pricing of Swedish mortgages with Eurohypo

After conversion, we expect Swedish covered bonds to trade close to German mortgage Jumbo-Pfandbriefe issued by Eurohypo, which is a liquid instrument enjoying high ratings. Moody's and S&P hold A2/A long term unsecured debt ratings on Eurohypo. Meanwhile mortgage and public Pfandbriefe by Eurohypo currently enjoy respective ratings of Aa1/AAA and Aaa/AAA. To compare the pricing of Swedish mortgages with Eurohypo, we translate stibor ASW spreads into euribor ASW spreads by adding the mid EURSEK basis swap.

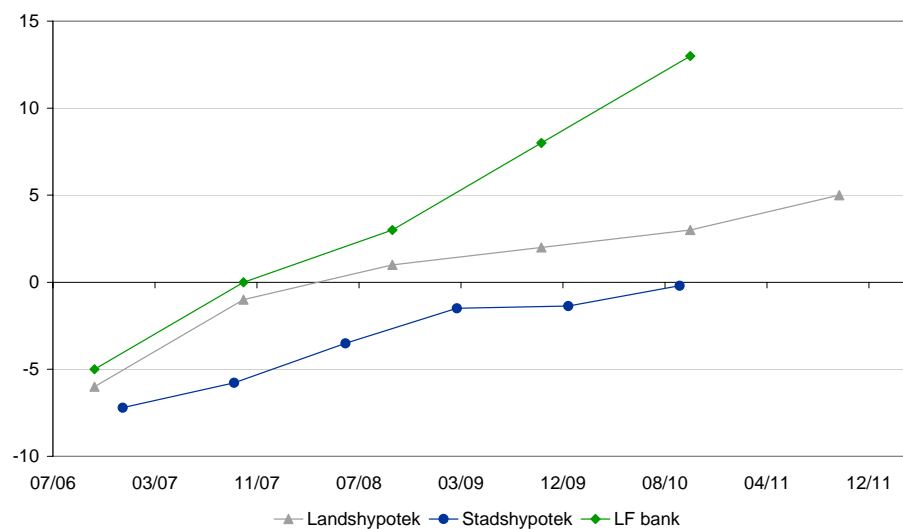
Once converted Swedish covered bonds are likely to trade close to German mortgage Pfandbriefe

We believe that pricing of Swedish covered bonds issued by major Swedish mortgage institutions will be in line with Eurohypo's Jumbo-Pfandbriefe as they are likely to obtain AAA ratings, while Eurohypo, which has split Aa1/AAA ratings, benefits from greater name recognition and significant liquidity as it is the largest Pfandbriefe issuer measured by outstanding bonds.

Tightening potential for Swedish mortgages of 5bps

Based on current pricing, we estimate a remaining tightening potential for Swedish mortgage bonds of approximately 5bps in asset swap spread terms. Based on our view that Nordea Hypotek, Stadshypotek and SBAB will be the first institutes to convert (Nordea Hypotek by the turn of the year and Stadshypotek and SBAB by end Q1 and during Q2 next year), we expect their bonds to richen by a couple of basis points relative to bonds from other institutes.

Landshypotek, LF Bank and Stadshypotek stibor ASW spreads (bps)



Source: SEB Merchant Banking

Landshypotek bonds likely to continue to trade wider than bonds issued by Swedish majors

Landshypotek's bonds currently trade wider than bonds issued by major Swedish mortgage institutions, since the latter are more highly rated and offer investors better liquidity through large benchmark issues. We believe this pattern will also persist after conversion to covered bonds. Still, Landshypotek has more to gain from conversion to covered bonds since even a covered bond rating of AA implies a rating uplift exceeding three notches.

Our view

We maintain our A-credit view, but upgrade our outlook to stable

We maintain our view of Landshypotek's A- credit based on its strong market share in mortgage lending to the agricultural and forestry sectors in Sweden, and solid capitalisation of its stable core agricultural mortgage lending portfolio. We upgrade our outlook to stable from negative reflecting positive asset quality trends with reductions, from high levels, of problem loans and net loan losses. Our view takes into account the sincerity of management's intentions to reduce non-core lending.

Landshypotek's bond spreads have recently tightened considerably

We believe Landshypotek will convert to covered bonds within the next 12 months. This is likely to result in outstanding bonds achieving a multi-notch rating upgrade to AA or even AAA. Nevertheless, Landshypotek's bond spreads have recently tightened considerably. The spread contraction has significantly exceeded the general market's tightening primarily reflecting anticipated conversion to covered bonds, but also Landshypotek's active funding strategy. Consequently, we regard the outstanding tightening potential of Landshypotek's bonds as rather limited.

Financial Summary

Landshypotek SEKM	2000	2001	2002	2003	2004	H1 2004	H1 2005
Income statement							
Total revenues	402	404	436	453	427	202	209
Net interest income	372	376	395	419	389	184	192
Fees and commissions (net)	3	-2	6	5	6	2	4
Non-interest expense	143	152	165	183	186	97	102
Net credit losses	8.2	-18.2	-8.9	-96.2	-75.5	-74.1	-11.5
Net op.income after provisions (excl non-recurring)	268	233	262	174	166	31	96
Net income*	49	168	188	125	121	23	73
<i>Net interest income/revenues (%)</i>	92%	93%	91%	93%	91%	91%	92%
<i>Fee and commissions (net)/revenues (%)</i>	0.66%	-0.38%	1.46%	1.15%	1.35%	1.11%	1.86%
<i>Net interest income/average earning assets</i>	1.18%	1.14%	1.15%	1.17%	1.08%	0.99%	1.06%
<i>Cost/income (%)</i>	35.5%	37.7%	38.0%	40.3%	43.4%	48.1%	48.7%
<i>Net loan losses/pre-provision income</i>	-3%	7%	3%	36%	31%	71%	11%
<i>Pre-tax return on risk assets, adjusted for dividends (%)</i>	0.83%	0.68%	0.73%	0.49%	0.46%	0.17%	0.52%
<i>ROE (%) (after tax, before dividends to mutualists)</i>	9.9%	6.3%	6.6%	4.2%	3.8%	1.4%	4.6%
<i>Return on equity (%)</i>	1.9%	6.3%	6.6%	4.2%	3.8%	1.4%	4.6%
<i>Common dividend pay-out (mutualist)(%)</i>	70%	67%	60%	90%	95%	N.A.	N.A.
<i>Revenue growth (%)</i>	0%	0%	8%	4%	-6%	-9%	4%
Balance sheet							
Assets							
Lending to financial institutions (net)	66	150	113	405	128	88	80
Lending to the public (net)	31,950	33,652	34,589	34,726	34,791	34,613	35,247
Loan-loss reserves	10	11	11	106	131	181	67
Equity and liabilities							
Shareholders equity in the balance sheet	2,602	2,766	2,910	3,119	3,176	3,142	3,249
Core capital (tier 1)	2,602	2,766	2,910	2,981	3,153	2,969	3,221
Debt to financial institutions	1,826	2,000	1,566	1,556	1,094	1,568	482
Customer deposits	315	380	538	462	491	377	424
Securities issued	25,936	27,568	29,135	30,896	30,059	32,017	32,539
Total reported assets	33,593	35,681	35,918	37,529	36,235	38,918	38,409
<i>Lending to financial institutions/assets (%)</i>	0.2%	0.4%	0.3%	1.1%	0.4%	0.2%	0.2%
<i>Lending to the public/assets (%)</i>	95%	94%	96%	93%	96%	89%	92%
<i>Interest bearing securities/total assets (%)</i>	0.5%	0.5%	0.5%	4.0%	0.8%	7.8%	4.1%
Capitalisation							
<i>Tier 1 capital ratio (%)</i>	7.81%	7.78%	8.14%	8.24%	8.79%	8.17%	8.68%
<i>Regulatory capital ratio (%)</i>	12.83%	12.47%	10.54%	9.69%	10.27%	10.17%	10.11%
<i>Shareholders' equity in the balance sheet</i>	7.75%	7.75%	8.10%	8.31%	8.76%	8.07%	8.46%
<i>Shareholders' equity growth (%)</i>	8%	6%	5%	7%	2%	0%	1%
Asset quality							
<i>Lending growth (%)</i>	6%	5%	3%	0%	0%	0%	1%
<i>Problem loans/ gross loans (%)</i>	1.23%	1.06%	1.38%	3.04%	3.19%	2.89%	2.64%
<i>Loan loss reserves % of problem loans</i>	2.87%	2.94%	2.33%	9.95%	11.75%	17.94%	7.22%
<i>Non-performing loans/customer gross loans (%)</i>	1.23%	1.00%	1.31%	1.13%	2.52%	0.96%	2.04%
<i>Lending loss level (%)</i>	-0.03%	0.06%	0.03%	0.28%	0.22%	0.21%	0.03%
<i>Loan loss reserve/customer loans(gross) (%)</i>	0.03%	0.03%	0.03%	0.30%	0.37%	0.52%	0.19%
Funding and liquidity							
<i>Customer deposits/funding base (%)</i>	1.09%	1.23%	1.68%	1.37%	1.52%	1.09%	1.24%
<i>Interbank funds/funding base (%)</i>	6.30%	6.48%	4.89%	4.62%	3.38%	4.52%	1.41%

*New accounting principles have been implemented as of 2002 regarding dividends to mutualists.

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