ANNUAL REPORT 2019

KOMMUNE KREDIT

STEADY & STABLE

MISSION

KommuneKredit shall contribute to financial latitude in Danish municipalities and regions by providing funding and financial advice at the lowest possible cost.

VISION

We will always be the best funding option for our customers, regardless of the given framework.

We will be modern, efficient and engaged, with a focus on high quality, steadiness and stability.

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CHAIRMAN'S REPORT

As Chairman of the Board of Directors of KommuneKredit, it is a top priority for me that we continue to professionalise our business. This is a key strategic focus area of our Strategy 2022, and we are in the process of completing the transition to a modern association that meets the standards and requirements of a well-run financial institution with public ownership.

We have strengthened our financial and operational risk management in recent years, and we are in the midst of radically modernising our IT landscape. As a result, KommuneKredit will become even stronger for the benefit of its members and the future funding of local government investments at the lowest possible costs – including for the green transition.

As part of the professionalisation of KommuneKredit, the Board of Directors is currently making efforts to continue to strengthen the boardwork. An important step is the Board's decision to appoint an additional independent board member with experience in accounting, auditing, financial or risk management as of June 2020. Diversity in the Board of Directors is important, so we can continue to perform our strategic, managerial and control tasks in the best way possible and for the benefit of our members.

This is in line with the change in the supervision of KommuneKredit which took place in connection with the change of government – from the Ministry of Social Affairs and the Interior to the Ministry of Industry, Business and Financial Affairs as well as the Danish Financial Supervisory Authority. I expect this change will contribute to a good and constructive dialogue on the structure of the business and the management of our financial risks – with an eye on what is relevant and proportional.

KommuneKredit is a special credit institution which is exempt from the EU's banking directive. There is a good reason for that as we only provide loans to projects considered and decided on at a political level in a municipality or region. The municipality or region assumes the financial risk of the projects, not KommuneKredit. Thus, municipalities and regions fund their capital expenditure through KommuneKredit's bond issues, in the same way as the Danish state funds its capital expenditure. KommuneKredit is more a common debt office for municipalities and regions than a credit institution. This is clearly illustrated by our 120-year history, during which we have never recorded a single loss on a loan.

We must retain the business model which has secured funding for local public projects in a cost-effective manner and on equal terms across Denmark.

KOMMUNEKREDIT FUNDS THE GREEN TRANSITION

In my opinion, KommuneKredit will play a major role in the green transition of society.

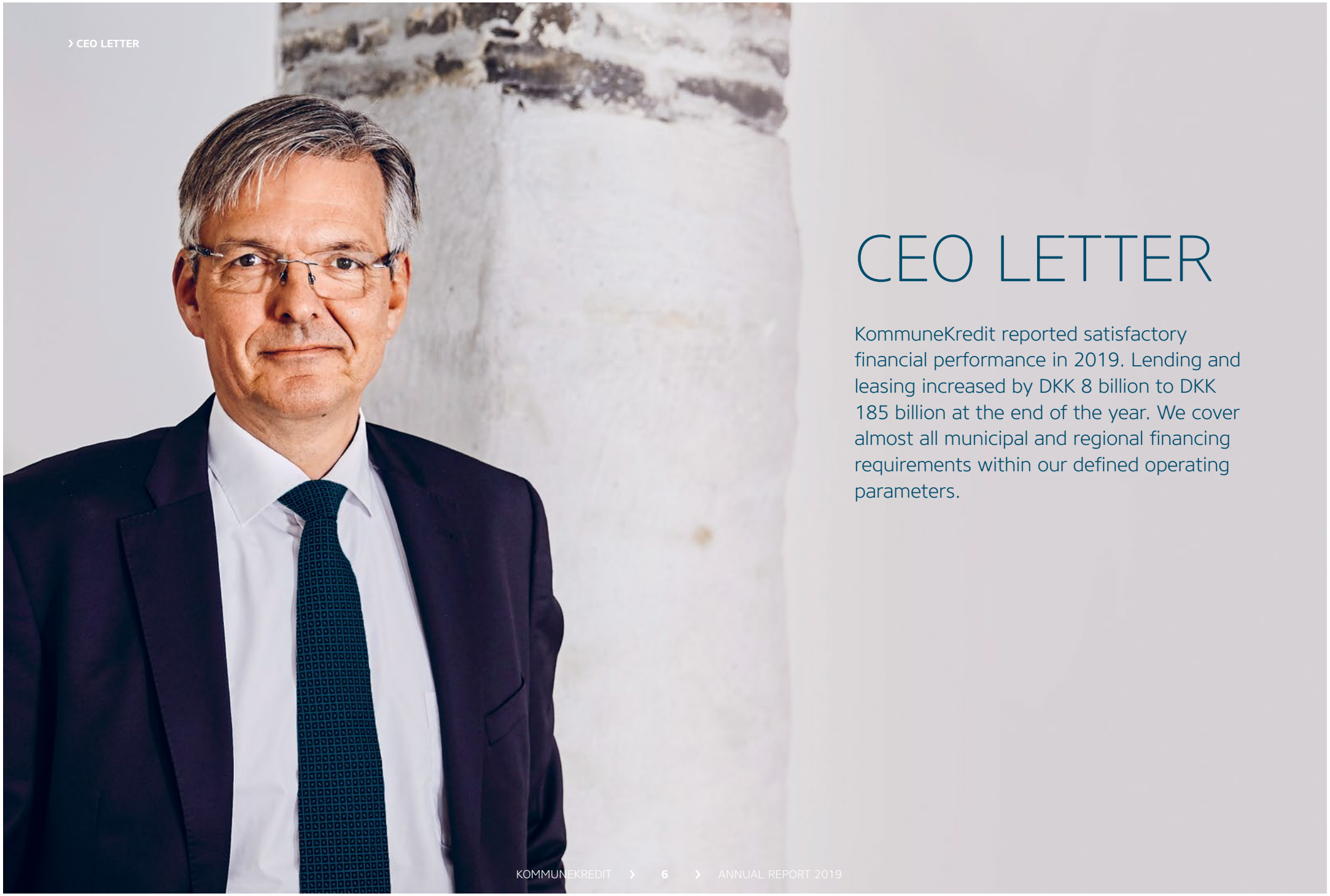
Current important agendas on reducing Denmark's CO_2 emissions and the need to implement various types of climate adjustment projects are areas to which KommuneKredit would like to contribute – and which I believe are in line with the association's business model and approach to corporate social responsibility.

Local implementation of green transition initiatives in various parts of the country – and thus substantial long-term investments – may with advantage be financed at the lowest possible costs through KommuneKredit. There are opportunities within the current regulations, e.g. climate adjustment, public transport, energy efficiency initiatives in public buildings and sustainable supply facilities, and new areas may be added if regulations are adjusted.

» We must retain the business model which has secured funding for local public projects in a cost-effective manner and on equal terms across Denmark."

We fund KommuneKredit's green loans by issuing green bonds. This allows green asset managers around the world to invest in our green projects. Green investment is a fast developing area in the international capital markets which we focus on strengthening further. We will make efforts to expand green funding locally in Denmark.

Lars Krarup
Chairman



CEO LETTER

KommuneKredit reported satisfactory financial performance in 2019. Lending and leasing increased by DKK 8 billion to DKK 185 billion at the end of the year. We cover almost all municipal and regional financing requirements within our defined operating parameters.

In 2019, we leased a gamma camera to the Region of Southern Denmark which has been installed at Odense University Hospital; we granted a loan of DKK 68 million to Balling-Rødding Varmeværk for the financing of a biomass and solar heating system; DKK 68 million to the Municipality of Favrskov for the financing of 60 social homes for the elderly in Hammel; and DKK 30 million to the Vifdam project, the purpose of which is to be able to handle the additional volumes of rain resulting from climate change in central Kolding.

We recorded net interest income of DKK 496 million in 2019, which was in line with expectations at the half-year. Costs were DKK 6 million higher than the expected DKK 120 million due to higher costs for IT development and licences. Positive value adjustments amounted to DKK 227 million, and KommuneKredit therefore reported a pre-tax profit of DKK 596 million and a net profit for the year of DKK 448 million.

As KommuneKredit may not pay dividends, the profit after tax is transferred to equity. KommuneKredit had an equity ratio of 3.5% at the end of 2019, against 3.4% at the end of 2018.

STRATEGY 2022

We are continuing to work with our Strategy 2022, focusing on Customer Relations, being Steady and Stable, and Professionalisation. In 2019, we came a long way in establishing a data warehouse and strengthening our internal control environment.

We are well underway to develop our technical infrastructure, and the outsourcing of our server platform to an external supplier in the autumn of 2019 marked an important milestone. At the same time, we embarked on a very large development task related to our business systems. We have made a thorough analysis, establishing the set-up of KommuneKredit's long-term processes and systems. Against this background, we have defined three tracks to serve as a platform for the transformation programme: Customer Journey, Balance Sheet Optimisation and Sustainable Finance. Finally, we have adjusted the organisation in order to strengthen our business development and thus the transformation programme. We have done this, among other things, by separating development and operations further and adding additional development resources.

Corporate governance was high on KommuneKredit's agenda in 2019. We adopted a set of principles for corporate governance which we are implementing throughout the organisation. Our satisfaction survey in the autumn indicates that we are well underway. The employees give high scores to their immediate superiors as well as senior management. In addition, the satisfaction survey shows a generally high level of satisfaction as regards job content. I am pleased that we have managed to sustain high employee satisfaction and loyalty in KommuneKredit during a period with many changes, resulting from our ambitious strategic development. The satisfaction survey also indicates a need for continuing to focus on developing efficient

» "I am pleased that we managed to sustain high employee satisfaction and loyalty in KommuneKredit during a period with many changes resulting from our ambitious strategic development."

Jens Lundager
CEO

tools and processes. This is an essential part of our transformation programme in the coming years.

NATIONAL AND EU LEGAL FRAMEWORK FOR KOMMUNEKREDIT'S LENDING

KommuneKredit provides loans within the regulation of public sector tasks performed by municipalities and regions as well as the rules on local government borrowing. Moreover, KommuneKredit's loans must be provided within the framework of the EU state aid rules.

This is ensured by specifically assessing the individual loan requests – in light of the ongoing development of rules and practices.

Regarding state aid, the European Commission has in recent years issued clear guidelines concerning infrastructure aid which we apply when assessing whether we can provide loans to e.g. investments in supply infrastructure. The European Commission has also adopted clear rules concerning aid to port infrastructure which we apply when providing loans to municipal industrial ports.

We are very focused on making a correct and specific assessment of the loan purpose in accordance with the EU regulations. On the other hand, it is important that Danish regulations or practices do not put up unnecessary barriers to municipal and regional authorities' access to cost-effective financing from KommuneKredit.

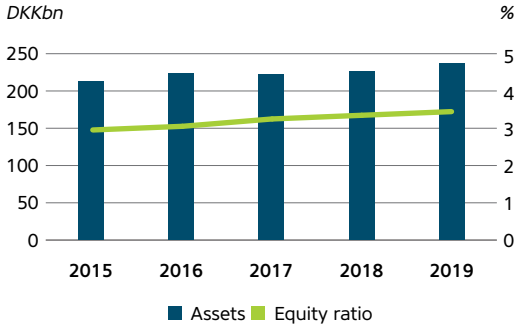
RATING

I am very satisfied that we achieved the important milestone of bringing back KommuneKredit to the safest category of financial counterparties as early as 2019, and have been given the highest rating by the two major rating agencies, Standard & Poor's and Moody's. Since Standard & Poor's downgraded KommuneKredit in the summer of 2018, we have devoted intensive efforts in all areas to regain our AAA rating, just as we have continued to be rated Aaa by Moody's. For example, our efforts included adjusting to some of Standard & Poor's calculation methods without changing our business model.

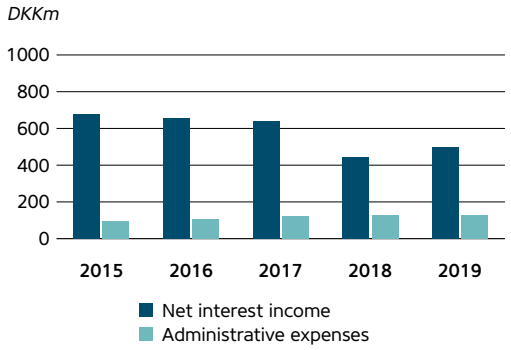
Jens Lundager
CEO

KEY FIGURES AND FINANCIAL RATIOS

ASSETS AND EQUITY RATIO 2015-2019



NET INTEREST INCOME AND ADMINISTRATIVE EXPENSES 2015-2019



Million	2019	2019	2018	2017	2016	2015
	EUR	*DKK*	*DKK*	*DKK*	*DKK*	*DKK*
KEY FIGURES						
Net interest income	66	496	441	637	656	675
Other operating income	2	13	11	11	10	9
Other operating expenses	-2	-13	-12	-14	-10	-10
Administrative expenses	-17	-126	-127	-123	-106	-96
Profit before value adjustments	50	369	314	511	550	578
Value adjustment of financial instruments	30	227	227	117	89	-451
Tax on profit for the year	-20	-148	-119	-138	-141	-23
Comprehensive income for the year	59	441	405	489	497	103
Lending and leasing	24,785	184,965	177,454	173,580	168,589	157,693
Portfolio of securities	6,027	44,982	42,944	42,361	34,049	33,983
Assets	31,749	236,935	226,609	222,564	223,938	213,199
Debt securities issued	29,336	218,932	208,218	202,145	202,642	193,382
Equity	1,096	8,179	7,736	7,333	6,844	6,347
ACTIVITIES DURING THE YEAR						
Lending and leasing, net additions in nominal value (net lending)	325	2,427	3,554	5,022	8,998	7,273
Lending and leasing, gross additions in nominal value	4,924	36,745	38,261	29,835	31,113	30,517
Debt securities issued, gross additions in nominal value	6,660	49,699	60,055	71,379	85,963	102,462
CAPITAL STRUCTURE						
Total risk exposure amount (REA)*	1,596	11,911	13,843	17,544	7,393	7,766
Common Equity Tier 1 (CET1) capital	1,096	8,179	7,736	7,333	6,844	6,347
Capital base	1,072	7,997	7,520	7,121	6,324	6,195
Capital ratio, pct*	67	67	54	41	86	80
Equity ratio, pct	3.5	3.5	3.4	3.3	3.1	3.0
SELECTED FINANCIAL RATIOS						
Losses on lending and leasing	0	0	0	0	0	0
Expenses/assets, pct	0.05%	0.05%	0.06%	0.06%	0.05%	0.05%
Net interest income/assets, pct	0.21%	0.21%	0.19%	0.28%	0.29%	0.32%
Liquidity resources, pct	19%	19%	19%	20%	16%	18%
Number of full-time employees	76	76	70	70	66	62

Key figures and financial ratios have been calculated in accordance with "Recommendations & Financial Ratios" issued by CFA Society Denmark.
Exchange rate at 31 December 2019: EUR 100 = DKK 746.2871. The format has been changed compared with last year.
* The figures are not directly comparable over time because the calculation method has been changed.

KOMMUNEKREDIT IS STEADY AND STABLE

KommuneKredit has been providing funding to Danish local authorities since 1899. KommuneKredit is a steady and stable partner.

That steadiness is founded on the structure as an association in which all Danish local authorities are jointly and severally liable for KommuneKredit's obligations.

Steadiness is also reflected in the association's low risk tolerance, prudent risk management and strong financial position.

KommuneKredit's stability is demonstrated by having provided a link between customer financing requirements and investors for more than a century.

KommuneKredit has been assigned a rating of Aaa from Moody's and AAA from Standard & Poor's, enabling the association to obtain funding at low interest rates. KommuneKredit must not generate dividends, allowing it to lend to its customers at a modest margin.

KommuneKredit plays an important part in society by creating financial latitude for local communities across Denmark.

KommuneKredit operates under a special legislative Act and is subject to supervision by the Danish Ministry of Industry, Business and Financial Affairs.

HIGH INTERNATIONAL CREDIT RATING

KommuneKredit is rated by Moody's and Standard & Poor's. The outlook is stable.

LONG-TERM DEBT: **Aaa/ AAA**

SHORT-TERM DEBT **P-1/ A-1+**

RISK WEIGHT:

0%

There is a risk weight of 0% when banks invest in KommuneKredit's issuances.

EQUITY RATIO

3.5%

With an equity ratio of more than 3%, KommuneKredit has a strong capital position.

LCR

HQLA

LEVEL 1 ASSETS

KommuneKredit's issues are rated in the highest liquidity category in the LCR Delegated Act.

CAPITAL RATIO

KommuneKredit has a total capital ratio of 67% as calculated in accordance with the solvency requirements for financial institutions.

67%

LENDING

185 DKKbn

In 2019, total lending amounted to DKK 185 billion, while profit before value adjustments and tax totalled DKK 369 million.

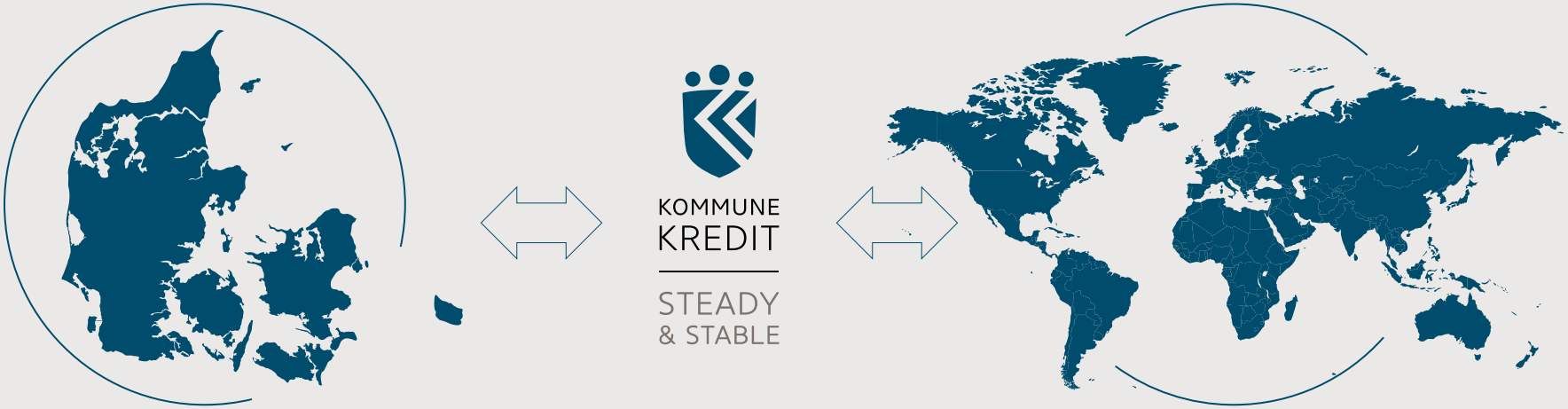
EMPLOYEES

The association employed 76 people on average in 2019.

76 employees

JOINT AND SEVERAL LIABILITY FOR ALL KOMMUNEKREDIT'S LIABILITIES

KommuneKredit plays an important role in society by creating a financial foundation for local communities in Denmark.



JOINT AND SEVERAL LIABILITY

KommuneKredit's members are Denmark's 98 municipalities and 5 regions, and the association thus represents the entire Danish population. The members are jointly and severally liable for KommuneKredit's liabilities. That is the members' musketeer oath where everyone is obligated – one for all, all for one.

KOMMUNEKREDIT IS A LINK

KommuneKredit acts as a steady and stable link between local lending and global funding.

FUNDING OF LENDING

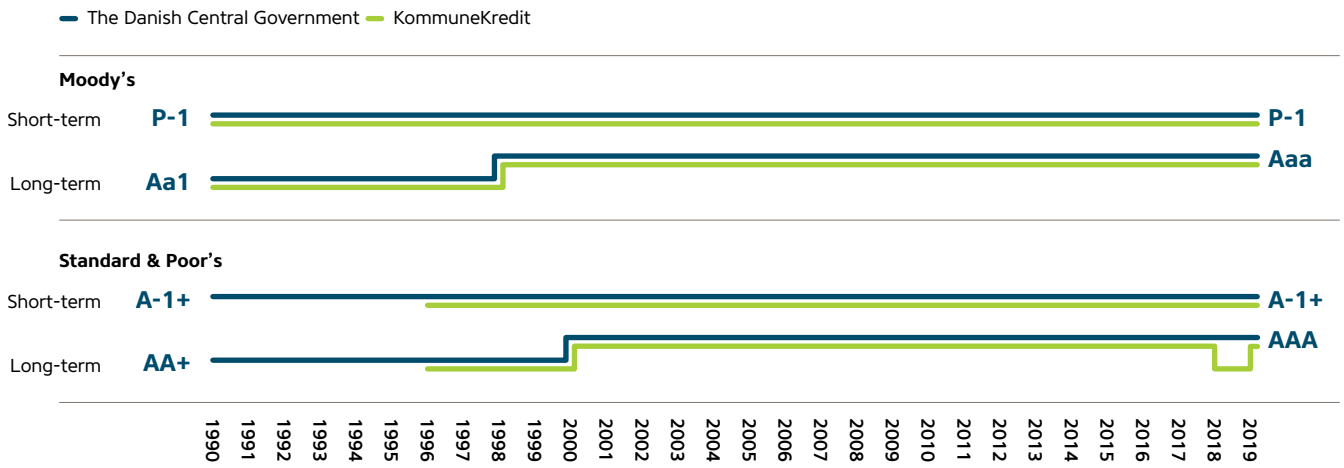
KommuneKredit's lending is financed by the issue of securities in the Danish and international capital markets.

KOMMUNEKREDIT AND DENMARK

All Danish local and regional authorities are jointly and severally liable for KommuneKredit's liabilities. This is a contributing factor to KommuneKredit's high credit rating.

KommuneKredit provides lending and finance leases to Danish municipalities, regions, inter-municipal partnerships and to companies undertaking municipal or regional tasks. KommuneKredit is governed by Act No. 383 dated 3 May 2006 on the Credit Institution for Local and Regional Authorities in Denmark (lov om kreditforeningen af kommuner og regioner i Danmark). Section 5 of the act stipulates that members of KommuneKredit are jointly and severally liable for all of KommuneKredit's liabilities. The 98 municipalities and 5 regions are all members. Thus, KommuneKredit has close ties to the Danish municipal and regional sectors.

HISTORICAL RATINGS OF THE DANISH CENTRAL GOVERNMENT AND KOMMUNEKREDIT



KOMMUNEKREDIT'S RATING IS IN LINE WITH THAT OF THE CENTRAL GOVERNMENT

KommuneKredit has been assigned the highest possible rating by the international rating agencies Moody's Investor Service and Standard & Poor's: Aaa and AAA, respectively. This is in line with the credit rating assigned to the Danish state.

The ratings are based on the following arguments:

- strong capitalisation;
- highly creditworthy borrowers and high-quality assets;
- very strong market position; and
- the members' joint and several liability for all of KommuneKredit's liabilities.

Another factor behind the high credit rating is KommuneKredit's important role in the economy as the main provider of funding to the Danish local and regional authorities.

DANISH ECONOMY CONTINUES TO EXPAND

The Danish economy is characterised as being strong and competitive. Danish society is based on high institutional efficiency, mature political and institutional frameworks that encourage fiscal discipline and a relatively low national debt.

Denmark has been a member of the EU since 1973, but opted out of the single currency, the euro (EUR), which means that the currency in Denmark is the krone (DKK).

Macroeconomics 2018	DK	EU
GDP real growth	2.4%	2.3%
Consumer prices	0.7%	1.9%
Unemployment	5.0%	6.8%
Government budget balance as % of GDP	0.8%	-0.7%
EMU debt as % of GDP	34.2%	80.4%

Source: Eurostat

The Danish economy is currently in a buoyant phase of decent economic growth, low unemployment and subdued inflation.

MUNICIPALITIES AND REGIONS ARE KEY TO THE DANISH WELFARE SOCIETY

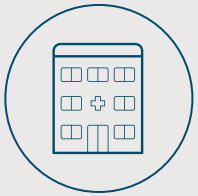
Denmark has one of the most decentralised public sectors in the world, with public sector tasks divided between the central government, municipalities and regions.

Municipalities attend to most of the tasks directly related to citizens and are responsible for most of the public services offered by the Danish welfare system. Municipal responsibilities include schools, elder care, day care facilities for children and young people, employment-creating measures, social integration of marginalised people, roads, the environment, culture and the arts, and preventive healthcare services. Municipalities are also responsible for planning various utility services to citizens, such as water supplies and heating, as well as the access to provide these services.

MUNICIPALITIES AND REGIONS ARE KEY TO THE DANISH WELFARE SOCIETY

GOVERNMENT

Foreign policy, defence, police, universities, major roads, railways, supervision and equalisation.



5 REGIONS

Hospitals and healthcare, regional development and public transport as well as specialised social institutions.

98 MUNICIPALITIES

Day care facilities for children and young people, elder care, schools, public transport, utilities, the environment and employment.

The municipalities and regions are responsible for most of the services offered by the Danish welfare society.

Municipalities and regions are defined by law and their right of self-government is set out in the Danish constitution and other legislation.

The regions are responsible for tasks which require a larger catchment population than that represented by the municipalities. The regions' responsibilities include hospitals, regional development, participation in regional public transport companies, and specialist social institutions. The municipalities and regions combined represent more than half of public expenditure.

CENTRAL GOVERNMENT BEARS THE RISK ASSOCIATED WITH ECONOMIC TRENDS

Income taxes represent the principal source of income for municipalities and account for more than half of total municipal funding. Municipalities are also funded through block grants and central government reimbursements as well as user fees and property taxes that are set by the individual municipalities.

As a general rule, municipalities have to finance their own capital expenditure from their current income without raising loans. However, municipalities may raise loans for municipal capital expenditure within the framework set by the Danish Ministry of Social Affairs and the Interior. In addition, municipalities can provide loan guarantees for other entities' capital expenditure to the extent that such guarantees are authorised under municipal law. The Danish municipalities' debt-to-equity ratios are low in an international perspective.

Denmark has a very extensive economic equalisation system between the municipalities. Equalisation comprises the tax base as well as the service expenditure, and it aims at ensuring consistency in the ability to render the required services in all Danish municipalities.

The overall economy of the municipalities is not affected by economic cycle setbacks, as central government bears the risk associated with general economic trends. Municipalities receive compensation for excess expenditure related to transfer payments and reduced tax revenues caused by an economic slowdown.

It is a basic principle under Danish administrative law that a municipality cannot be declared bankrupt. This principle was also upheld in a High Court ruling, referring to the fact that the supervisory authority, the Government, must ensure that a municipality is able to meet its financial obligations.

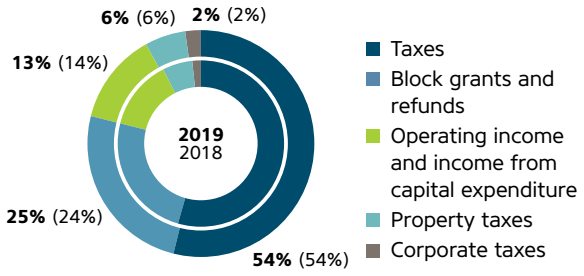
Regional funding consists of government grants and municipal contributions and charges.

Throughout KommuneKredit's history, no municipality or region has ever defaulted on a loan. The Danish municipalities and regions are characterised by high creditworthiness, which is expressed in a CRR/CRD IV risk weight of 0%. The risk weight is used to calculate credit institutions' capital requirements, and a risk weight of 0% means that municipalities and regions belong to the most secure category, in which no losses are expected.

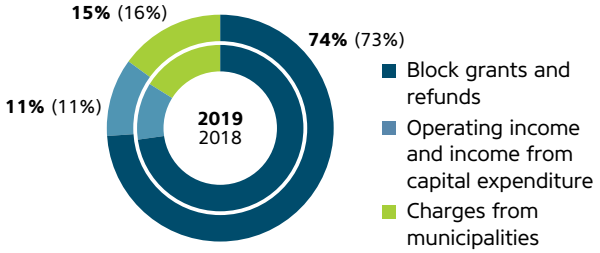
MINISTERIAL SUPERVISION

The Ministry for Social Affairs and the Interior is the ultimate supervisory authority in respect of local authorities. Supervision ensures that local authorities can meet their obligations at all times.

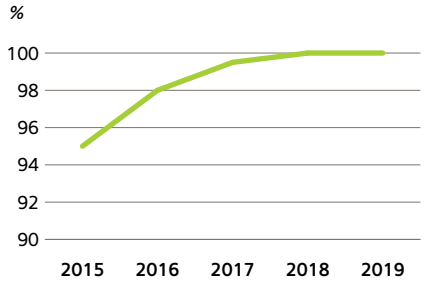
BUDGET FOR THE MUNICIPALITIES' INCOME BASE



BUDGET FOR THE REGIONS' INCOME BASE



KOMMUNEKREDIT'S MARKET SHARE OF LOANS TO LOCAL AUTHORITIES



OMØ'S DIKES – AN EXAMPLE OF FINANCING CLIMATE PROOFING INITIATIVES

KOMMUNEKREDIT PROVIDES FINANCING FOR CLIMATE INVESTMENTS AND COASTAL PROTECTION PROJECTS. AS LONG AS PROJECTS FALL WITHIN THE FRAMEWORK OF THE APPLICABLE LEGISLATION, MUNICIPALITIES, UTILITY COMPANIES AND DIKE GUILDS MAY APPLY FOR LOANS. MUNICIPALITIES MAY DECIDE TO RAISE LOANS THEMSELVES OR PROVIDE A MUNICIPAL GUARANTEE FOR THE DIKE GUILD'S LOANS.

On 2 November 2006, the inhabitants on the Danish island of Omø woke up to an island almost divided into halves by flooding. The ferry had blown ashore, and 24 private homes and 14 holiday homes in Kirkehavn were flooded. At its highest level, the water reached 1.80 metres above average, and it was absolutely clear that the island needed coastal and climate proofing of quite a different calibre. Omø dike guild (Omø Digelag) was established and began what turned out to be a long, tough haul to protect the island against flooding. A general classification of Omø as a 'valuable geological area' and a beach meadow protected by Natura 2000 meant that flora and fauna had to be given special consideration. For example, vinyl sheet piling had to be used in the beach meadow instead of earth walls to avoid taking up too much of the protected area. Thus, landowners' costs increased slowly but surely, and the project was on the verge of collapse. In 2010, the dike guild succeeded in obtaining just over DKK 5 million under the finance bill, and combined with LAG funds (Local Action Group subsidy scheme under the Nature Business Authority) and a municipal guarantee provided by the Municipality of Slagelse, the first steps were taken to construct coastal and climate protection on Omø in 2013.

Omø's new dikes are designed to resist flooding similar to the 2006 level plus an additional expected sea-level rise of 0.5 centimetre annually over the next 50 years. The dikes integrate well with the natural beauty of the area and are constructed of Azobé wood, clay and stone, where possible, and the rest of vinyl sheet piling. They cater for fauna with 'passages' for amphibians and small animals as well as for visitors with integrated recreational areas, such as a playground, a volleyball court and small shelter spots. A project which creates value, not only in relation to coastal and climate proofing, but also for fauna, islanders and visitors.

DO YOU WANT TO LEARN MORE?
Contact Christian Jeppesen, Director, Head of Lending and Leasing, chj@kommunekredit.dk

KOMMUNEKREDIT COVERS THE LOCAL FINANCING REQUIREMENT

For more than 120 years, KommuneKredit has provided funding to the Danish welfare society. The association offers financing on equal terms irrespective of size and post code. Today, KommuneKredit covers more or less the entire local financing requirement in Denmark.

At the end of 2019, total loans and leasing amounted to DKK 185 billion. 57% of the lending was granted directly to municipalities and regions for the funding of public purposes, such as port infrastructure, housing for the elderly, climate proofing initiatives, hospital equipment and vehicles for the municipal home care service.

The remainder of the loans was provided to companies or institutions which carry out public tasks, for example local sports centres, theatres and schools as well as companies providing public utilities and services such as waste and wastewater management and the production of drinking water.

Total lending and leasing increased by DKK 2.4 billion in 2019, against DKK 3.6 billion in 2018.

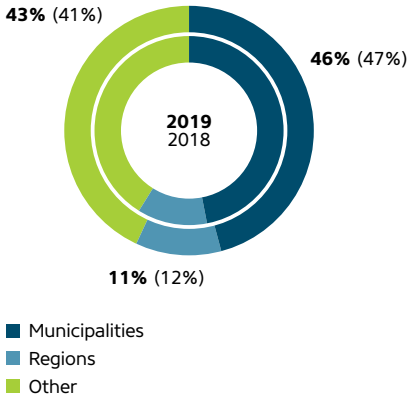
CONTINUED HIGH LENDING AND LEASING ACTIVITY

KommuneKredit's pricing model, under which the price of an individual loan product must reflect KommuneKredit's costs of establishing the loan, has made it possible to offer customers remortgaging of loans with longer refinancing intervals at lower interest rates.

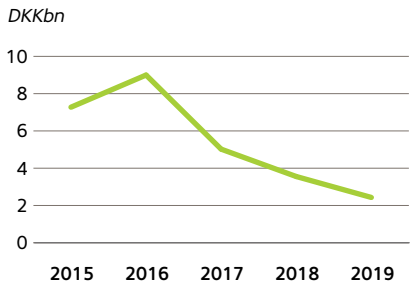
This led to strong remortgaging activity in 2019, and loans with short-term refinancing intervals were replaced by loans with long-term refinancing intervals.

The demand for fixed-rate loans increased steadily throughout 2019 and is also expected to increase in 2020, partly due to the revised pricing structure, and partly due to the very low interest rate level.

TOTAL LENDING AND LEASING BY BORROWER



DEVELOPMENT IN NET LENDING



CUSTOMER NEEDS COME FIRST

KommuneKredit provides funding for projects whose implementation is determined on the basis of democratic processes. Specifically, this means that the investment constitutes a municipal or regional task and that local or regional support for the investment has been established.

CASE: NEW SPORTS CENTRE

1. **City council approves the erection of a sports centre**
2. **The borrower contacts KommuneKredit with a loan request**
3. **Loan application is processed**
4. **Advice on and selection of loan**
5. **Establishment of loan**

IS THE CUSTOMER QUALIFIED TO RAISE A LOAN?

- ✓ Municipality
- ✓ Region
- ✓ Association of local authorities
- ✓ Entities with a municipal guarantee

IS THE CUSTOMER CREDITWORTHY?

- ✓ Municipal/regional credit risk
- ✓ Guarantee transferring credit risk from borrower to the municipality

DOES THE PURPOSE QUALIFY FOR A LOAN?

- ✓ EU state aid rules
- ✓ Rules on local authority borrowing
- ✓ Local authority mandate or relevant sector legislation

» We endeavour to create financial latitude in Danish local communities by offering funding at the lowest possible cost."

Henrik Andersen
Managing Director

KommuneKredit has at times been able to offer both floating rate loans and fixed-rate loans with negative interest rates.

As a result of the strong remortgaging activity, more than 700 new loans were established in 2019 for a total amount of DKK 41 billion.

In addition, municipalities and regions entered into more than 3,000 new lease agreements with KommuneKredit for an amount of DKK 2.7 billion. The lease agreements cover a wide range of assets, but typically vehicles, vans, IT equipment and hospital equipment.

GREEN LOANS

KommuneKredit's Green Bond Committee must approve a loan in order for it to become a green loan. In 2019, the Green Bond Committee approved 81 loans with total project costs of almost DKK 2 billion. The majority of the approved green loans financed projects in district heating and water and wastewater management, while a small part of the loans were granted for projects within energy-saving initiatives.

As a new feature, customers can now receive a digital green certificate as proof that they have taken out a green loan with KommuneKredit. Customers may use the certificate on their websites and in publications.

KommuneKredit expects green funding to account for an ever-increasing proportion of the overall loan portfolio in the future. Developing green funding is one of the three tracks of KommuneKredit's transformation programme, which provides the framework for our strategic efforts in the time to come.

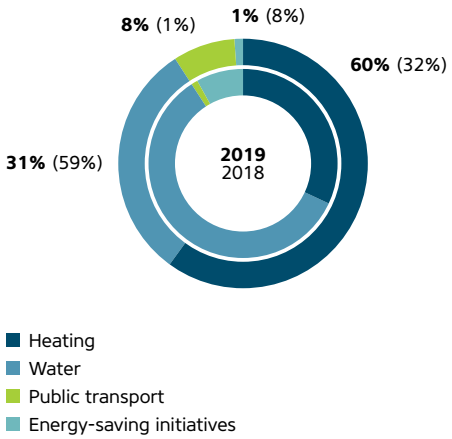
DIGITAL CUSTOMER JOURNEYS

Customer journeys are also one of the three tracks of KommuneKredit's transformation programme. The ambition is to establish processes based on Straight Through Processing (STP), which ensures system support for loan and lease agreements throughout their lifecycle. The digital transformation of customer journeys will be completed over the coming years.

» We expect green funding to account for an ever-increasing proportion of the overall loan portfolio in the future."

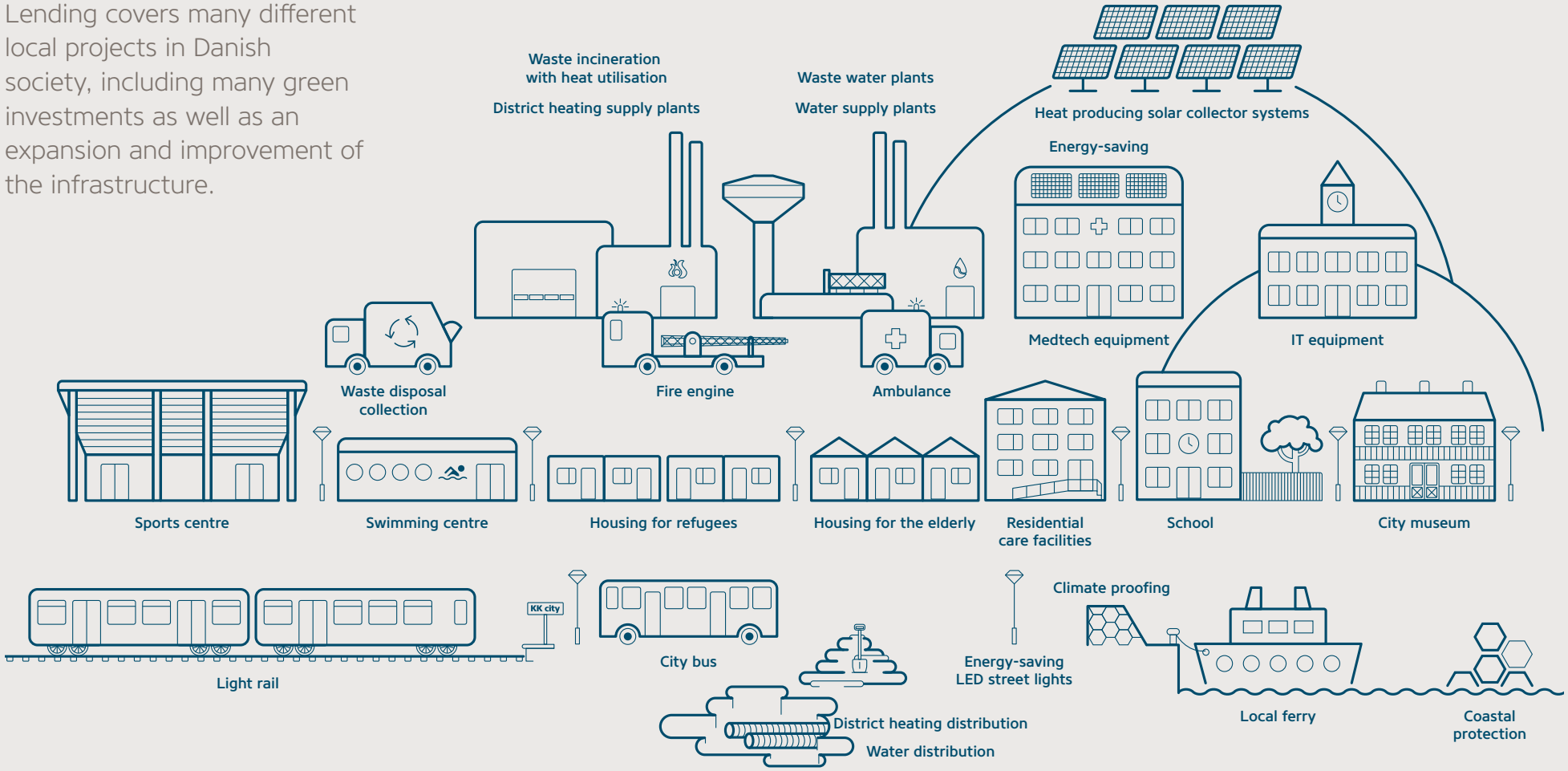
Christian Jeppesen
Director, Head of Lending & Leasing

APPROVED GREEN LOANS BY PURPOSE



KOMMUNEKREDIT FUNDS PUBLIC UNDERTAKINGS

Lending covers many different local projects in Danish society, including many green investments as well as an expansion and improvement of the infrastructure.



KOMMUNEKREDIT FUNDS INNOVATIVE CLOUDBURST PROJECT IN FREDERIKSBERG

WITH FINANCING FROM KOMMUNEKREDIT, THE MUNICIPALITY OF FREDERIKSBERG IS CURRENTLY IMPLEMENTING AN INNOVATIVE CLOUDBURST PROJECT WITH CLIMATE PATHWAYS TO FUTURE-PROOF ITS SEWER SYSTEMS AND TO MAKE THE CITY BETTER PREPARED FOR FUTURE CLIMATE CHANGE, INCLUDING EXTREME VOLUMES OF RAIN.

In recent years, municipalities across Denmark have faced climate change challenges, resulting, among other things, in flooded roads and basements, because sewer networks in the majority of the country lack the capacity to accommodate extreme volumes of rain.

The purpose of the Municipality of Frederiksberg's new cloudburst project is not only to drain rainwater from flooded areas, but also to reuse the rainwater as a resource throughout the city and not least for its green spaces. Some of the rainwater is collected in specially designed collection ponds, such as the central retention pond near the sports centre 'Frederiksberg Idrætsanlæg', where rainwater may evaporate.

And some of the rainwater is absorbed by the new tile paving, referred to as 'NO NOx tiles', allowing rainwater to infiltrate as well as to have a cooling effect on the city and reduce temperatures.

Finally, some of the rainwater is collected in roadside ducts and transported via climate pathways to rainwater gardens and areas planted with 'thirsty' species of trees, thereby creating better growth conditions. Thus, pressure on the sewer system is relieved and at the same time the water is reused as a valuable resource.

CLIMATE PROOFING PROJECTS ARE FINANCED BY WAY OF GREEN LOANS FROM KOMMUNEKREDIT

KommuneKredit is happy to support its members' investments in sustainable infrastructure. When a municipality takes out a loan which fulfils KommuneKredit's conditions for being a green loan, the positive green impacts must be documented. Ultimately, this data collection means that, in collaboration with its customers, KommuneKredit contributes to strengthening the green profile of Denmark's public sector.

DO YOU WANT TO LEARN MORE?

Contact Christian Jeppesen, Director, Head of Lending and Leasing, chj@kommunekredit.dk

EXTENDED FUNDING MATURITIES

KommuneKredit has extended the maturity of its funding as its customers have opted for loans with longer binding commitments.

LONG-TERM FUNDING

Being an Aaa/AAA issuer, KommuneKredit endeavours to diversify its issuance activities on several markets in order to maintain a broad and diversified investor base. Most of the funding is sourced from public issues in USD, EUR and DKK. In addition, the association may issue bonds in other currencies and in the form of private placements to accommodate specific investor demand.

To match customer demand for loans with extended binding commitments, funding maturities were extended in 2019. As a result of the extended maturities, the number of issues and total issue amounts were lower than in the preceding years.

In 2019, KommuneKredit issued green bonds totalling EUR 500 million. The bonds have a maturity of 20 years and were issued in accordance with ICMA's Green Bond Principles. The green bonds attracted a lot of interest especially from European investors, and several ESG investors put in a bid for the issue. Since 2017, green bonds have been issued for a total amount of EUR 1.75 billion, or DKK 13 billion.

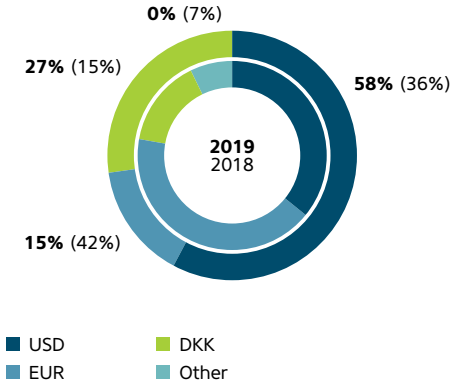
In addition, two public issues were carried out for USD 1 billion with a 3-year maturity and EUR 500 million with an 11-year maturity, both of which were acquired by international investors.

In Danish kroner, bonds for DKK 5 billion were issued with a 3-year maturity and DKK 5 billion with a 20-year maturity, which were primarily sold to Danish investors.

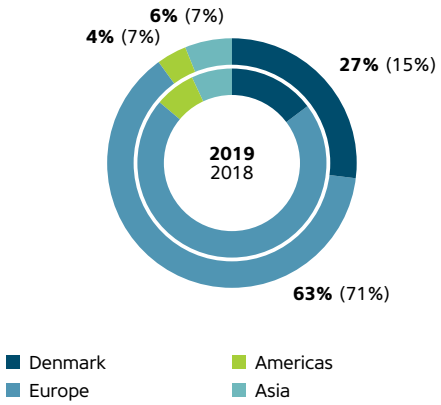
Other issues in 2019 primarily comprised adjustable-rate loans for the funding of subsidised loans for municipally-owned residential care facilities and housing for the elderly in the amount of DKK 4 billion. In 2019, these issues were again comprised by the government's purchase of bonds to fund subsidised housing. The strategy defined by the Danish state is to continue to buy these bonds and, therefore, upcoming bond maturities are not subject to any refinancing risk for KommuneKredit.

The short end of the market saw issues of commercial papers with maturities of less than 12 months in 2019, totalling DKK 22 billion to cover short-term liquidity requirements.

THE YEAR'S FUNDING BY CURRENCY



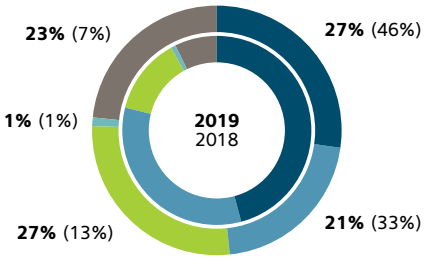
THE YEAR'S FUNDING BY MARKET



»The strategy will still be to diversify bond issues across different markets and thereby optimise access to funding, while also ensuring a broad and well-diversified investor base.

Jette Moldrup
Director, Head of Treasury

INVESTOR DISTRIBUTION FOR BENCHMARK ISSUES



- Banks and treasury departments
- Central banks and supranationals
- Asset managers
- Corporations and pension funds
- Insurance companies and similar

Securities totalling DKK 50 billion were issued in 2019, and by the end of the year debt securities issued amounted to DKK 219 billion.

BUYBACK STRATEGY

In recent years, KommuneKredit has carried out public issues of bonds with a concurrent possibility for investors to buy back existing bonds with short terms to maturity. The buyback strategy contributes to actively managing the [[balance sheet maturity profile]]. This helps KommuneKredit to obtain a closer match between maturities of loans and funding while also reducing the refinancing risk in connection with large maturities.

In connection with the USD issue in 2019, bonds in two different ISIN codes were bought back for an amount of USD 450 million. All the bonds were due to mature in 2019 and 2020, respectively.

FUNDING BUDGET 2020

The budgeted requirement for new funding with a maturity of more than 12 months is DKK 30 billion, or EUR 4 billion. The strategy will still be to diversify bond issues across different markets and thereby optimise access to funding, while also ensuring a broad and well-diversified investor base.

KommuneKredit expects 4-6 public issues in EUR, USD and DKK but will also consider opportunities to make issues in other markets. Issues are expected to have relatively long maturities to match the binding commitments on the loans.

Commercial papers will still be used to cover short-term liquidity requirements.

KommuneKredit expects an increase in the green loan portfolio, which would enable the association to issue at least one green bond in 2020.

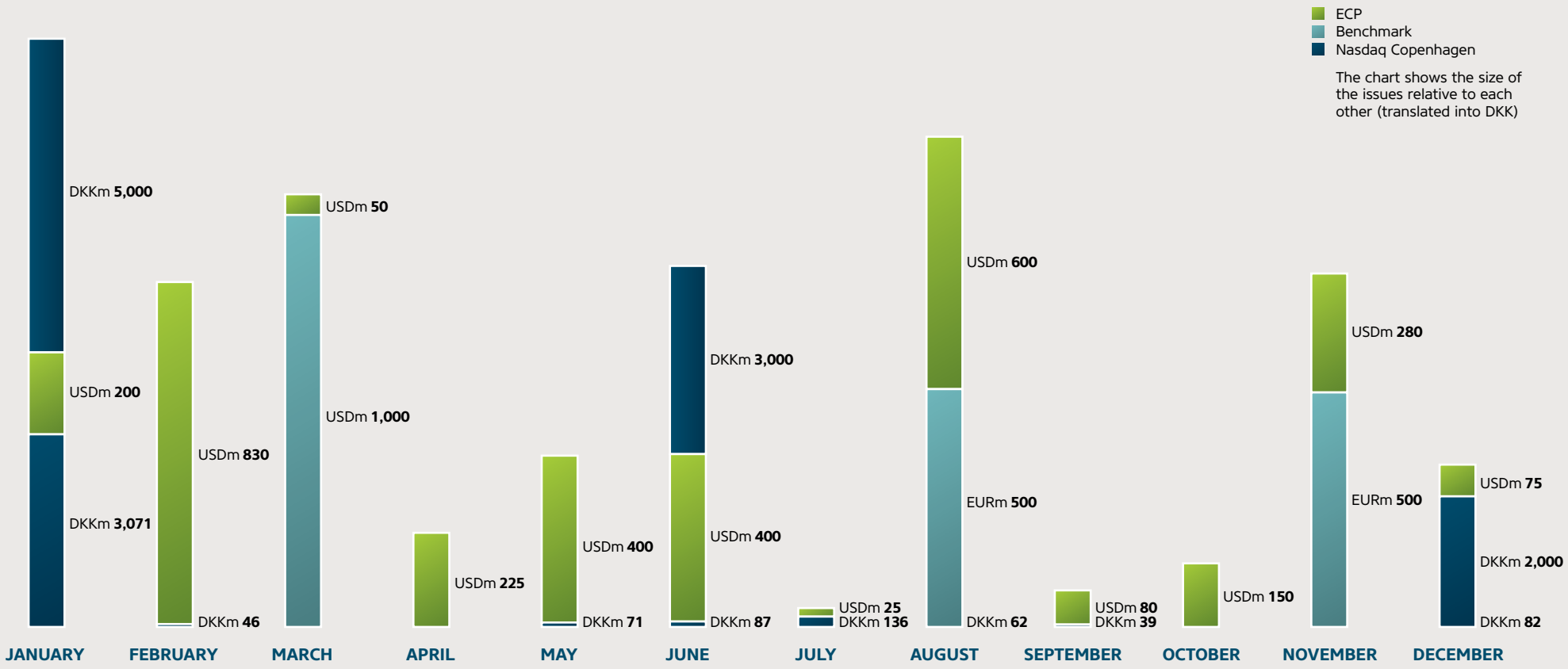
INVESTMENTS

KommuneKredit is authorised by the supervisory authority to raise additional funding at a maximum of 25% of total lending. Such funding contributes to KommuneKredit's liquidity resources. The liquidity resources and KommuneKredit's equity make up the total liquidity resources, which are regularly invested in bonds with a very high credit quality.

Throughout the period, KommuneKredit's total liquidity resources were invested primarily in AAA and AA-rated government bonds and mortgage bonds. The investments are diversified across many issuers and generally have short maturities. 56% of the portfolio will expire in 2020.

KommuneKredit's liquidity resources and, by extension, the investment portfolio were regularly adjusted throughout 2019. The liquidity resources rose from DKK 43 billion to DKK 45 billion at the end of 2019.

BOND ISSUANCE IN 2019 BY MARKET AND MONTH



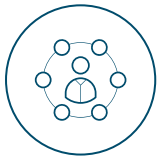
JANUARY	FEBRUARY	MARCH	APRIL	MAY	JUNE	JULY	AUGUST	SEPTEMBER	OCTOBER	NOVEMBER	DECEMBER
DKKm 9,378	DKKm 5,498	DKKm 6,898	DKKm 1,501	DKKm 2,731	DKKm 5,756	DKKm 301	DKKm 7,815	DKKm 583	DKKm 1,014	DKKm 5,635	DKKm 2,588

TRANSFORMATION PROGRAMME

KommuneKredit's 2022 Strategy forms the backbone of its transition to a modern association that meets the requirements of a well-run financial institution with public ownership.

In 2019, KommuneKredit made a dedicated effort to establish the foundation for a comprehensive transformation programme, which will represent the next step in its strategic development. The programme consists of three tracks, the combination of which is intended to drive the ambitions for KommuneKredit going forward. These three tracks are a) Customer Journey, b) Balance Sheet Optimisation and c) Sustainable Finance. Concurrently with this three-track programme, KommuneKredit will seek to professionalise its business in line with Strategy 2022.

A key component of the efforts in 2019 was an in-depth analysis of how processes and systems may be optimised to support the core business and the customer journey in KommuneKredit going forward. The tracks are described here.



CUSTOMER JOURNEY

Customer Journey is about establishing processes based on Straight Through Processing (STP), which ensures complete system support for loan and lease agreements from advisory services commence until the agreement expires.

The lending process must be intuitive for our customers, who must be able to carry out a large part of the process without the assistance of customer advisers. The ambition is to achieve a higher degree of customer self-service, allowing customer advisers to focus more on advisory services than producing loans and leases.

Lastly, loan and lease agreements should be integrated to a higher degree than they are today, providing customers with a swift 360-degree overview of all exposures.

BALANCE SHEET OPTIMISATION

Balance Sheet optimisation is about improving our asset/liability management. This involves adapting our business model to optimise the correlation between loans, funding, hedging and investment.

KommuneKredit must further improve its ability to make forward-looking impact calculations. It is not enough to be steady and stable in the short term – the association must also ensure that the action it takes today will contribute to stability in both the short and the long term, while simultaneously minimising costs.

KommuneKredit needs to implement analytical and management tools that will in an instant enable it to form a complete overview of the impact of new initiatives, both now and going forward.

SUSTAINABLE FINANCE

Sustainable Finance is an initiative to integrate sustainability throughout our operations, including advancing the use of green funding. To date, KommuneKredit has approved nearly DKK 20 billion of green loans for sustainable projects.

With members and investors increasingly demanding green solutions, green funding is expected to account for an ever-increasing proportion of the overall loan portfolio.

In addition, this track is expected to progress KommuneKredit's continuing CSR initiatives, including further development of its ESG efforts and integration of the UN Sustainable Development Goals in its strategic business development.

STEADY AND STABLE IT PLATFORM

THE IT STRATEGY SUPPORTS KOMMUNEKREDIT'S AMBITION OF BEING A MODERN AND WELL-RUN FINANCIAL BUSINESS, MEETING ALL THE REQUIREMENTS THAT CUSTOMERS, INVESTORS AND AUTHORITIES HAVE. THE STRATEGY PROVIDES A STRONG FOUNDATION FOR THE DIGITAL TRANSFORMATION OF KOMMUNEKREDIT.

KommuneKredit's digital transformation started in the summer of 2016 with the drafting of a new IT strategy. The strategic purpose was to create a steady and stable IT platform.

Outsourcing of the server platform to external data centres was completed in December 2019 and has enabled us to react much faster to any hardware breakdown or other incidents preventing us from running our business at Kultorvet.

As regards cyber security, we have made considerable efforts to expand and improve our protection against malware and hacking. Firewalls have been upgraded to larger and more powerful versions, and they are tested regularly by way of penetration tests. E-mails to customers are sent and received via a secure message system. Employees' laptops have been encrypted and protected with antivirus solutions. All employees are trained and tested on an ongoing basis in good and safe IT behaviour.

By introducing a new and improved IT governance process, we have established better management of and follow-up on IT development projects, including ongoing improvements of existing systems. The process ensures transparency in all decisions and prioritisations. The digital platform has been modernised and updated to the latest version, supporting steady and stable business applications. Laptops and digital meeting rooms with Skype facilities have produced a modern and flexible workplace for our employees. With the implementation of a data warehouse and a Business Intelligence solution, KommuneKredit has taken steps to have a more modern reporting platform so that the use of data can be optimised to enhance the management of the business.

Wanting to build on the improvements achieved with the IT strategy and as part of the transformation programme, KommuneKredit will this year focus on improving customer service efficiency to provide its customers and investors with more and better digital solutions and offerings, on improving internal processes and systems, on developing employee skills and on expanding its steady and stable IT platform.

Nadeem Zafar
Director, Head of IT, CIO

LOW RISK, HIGH LEVEL OF SECURITY

KommuneKredit must always be a steady and stable link between the Danish local authorities and investors.

KommuneKredit is exposed to a number of risks which are identified, controlled and mitigated on an ongoing basis so as to match KommuneKredit's low risk tolerance at any given time.

The Board of Directors has laid down overall guidelines for KommuneKredit's financial risk management, including risk tolerance decisions. The supervisory authority is further authorised to order the Board of Directors to make changes to the guidelines it has adopted.

LOW RISK TOLERANCE

KommuneKredit must be a steady and stable link between customers and investors and cannot pay dividends to its members. KommuneKredit therefore has a low risk tolerance which is limited to financial risks deemed absolutely necessary in order to accomplish KommuneKredit's mission. As Danish local authorities are jointly and severally liable for KommuneKredit's liabilities, risks assumed by KommuneKredit are ultimately also their risks.

KommuneKredit sources funding denominated in different currencies. Through its lending operations, which are in Danish kroner, KommuneKredit relends liquidity to Danish local authorities. This means KommuneKredit's role as a link is to schedule its funding to match the lending profile the customers want.

LOW MARKET RISK

All funding is converted into the required currency and interest profile for lending and liquidity resources by way of derivatives.

Interest rate and currency exposure is hedged to a wide extent to keep KommuneKredit's market risk at a low level. The low market risk reduces the risk of loss resulting from changes in market prices.

LOW CREDIT RISK

KommuneKredit is exposed to credit risk in respect of investment counterparties as the liquidity resources are invested in bonds, and in respect of financial counterparties with whom KommuneKredit has entered into derivatives agreements. The credit risk related to investment counterparties is limited by high credit quality requirements – both in relation to the type of counterparty and the rating of the counterparty. The credit risk in respect of financial counterparties is also limited by high credit quality requirements. KommuneKredit can only trade financial instruments with financial counterparties with whom a collateral agreement has been entered into.

Lending and leasing are only granted to Danish local authorities. Loans may also be granted against a 100% guarantee from these authorities. Danish local authorities are subject to strict regulation and close supervision by the Ministry of Social Affairs and the Interior. During its 120-year lifetime, KommuneKredit has never written off a loan or a lease.

LOW LIQUIDITY RISK

To limit liquidity risk, binding commitments on lending liquidity cannot be entered into unless at least corresponding equity or binding funding commitments are in place with at least corresponding terms to maturity.

This ensures that KommuneKredit's lending is financed throughout the commitment period.

The liquidity resources and equity make up KommuneKredit's total liquidity resources, which must also cover KommuneKredit's liquidity requirement relating to bilateral collateral agreements.

The Board of Directors has determined that KommuneKredit must have total liquidity resources to cover a situation of extreme stress in the financial markets for an extended period of time. As a supplement to the survival horizon, KommuneKredit has a liquidity resource contingency plan which can be activated in case of pressure on liquidity.

Moreover, the Board of Directors has defined guidelines for KommuneKredit with respect to Liquidity Coverage Ratio and Net Stable Funding Ratio, which are calculated in accordance with CRR/CRD.

The low liquidity risk ensures that KommuneKredit can at all times settle its financial obligations.

PRICE RISK ON OWN FUNDING SPREADS

KommuneKredit adjusts all of its funding to fair value. This entails that KommuneKredit is exposed to changes in own funding spreads. By maintaining relatively constant lending margins, changes to KommuneKredit's own funding spreads are transferred to lending prices. Since loans, other than leasing, are also recognised at fair value, the price risk on own funding spreads is reduced. The remainder of the risk arises primarily for two reasons.

The first reason is that KommuneKredit's funding commitment is sometimes longer than the binding lending commitment. This is done, among other things, to mitigate liquidity exposure. The other main reason is that KommuneKredit has liquidity resources consisting of high-quality liquid assets (HQLA). The risk here is due to the fact that the fair value of funding is exposed to KommuneKredit's funding spreads, while that is not the case for the bonds in the liquidity resources. The liquidity resources consist primarily of bonds with a high rating issued by governments or public authorities and AAA-rated Danish mortgage bonds.

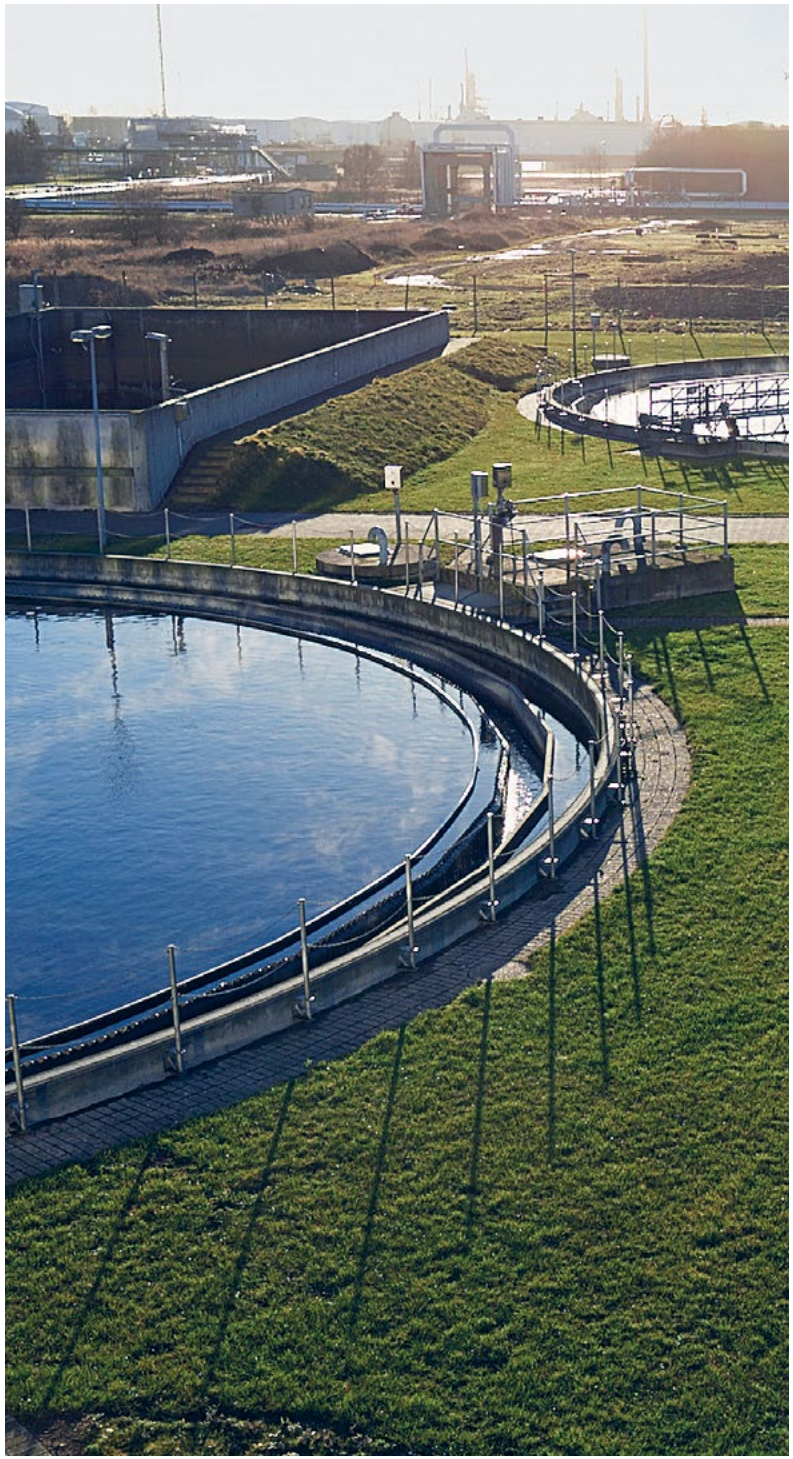
An increase in KommuneKredit's funding spreads would have a positive effect on fair values. The reason is that the fair value of KommuneKredit's funding falls more than the fair value of customer loans. Similarly, a fall in KommuneKredit's funding spreads would have a negative impact on fair values. Efforts are made to keep the risk on own funding spreads at a low level, but the risk is a part of KommuneKredit's business model and cannot be avoided.

OPERATIONAL RISK

Most of KommuneKredit's activities are exposed to operational risk. By registering risk events in a database, focus is maintained on mitigating as many risks as possible while at the same time allowing KommuneKredit to systematically improve its business procedures and processes.

The written business procedures describe allocation of responsibilities, segregation of duties, process management and business practices. As many processes as possible are automated to reduce the risk of human error. All critical processes, be they automated or manual, must be supported by either peer checks or objective controls.

As KommuneKredit is highly dependent on its IT infrastructure, particular focus is placed on this area via a disaster recovery plan and an IT security policy that sets guidelines for access control, assignment of roles and rights, system crashes and errors, etc.



TOTAL RISK EXPOSURE AMOUNT (REA)

KommuneKredit's total risk exposure amount is DKK 11.9 billion. Risk exposure is calculated in accordance with the solvency rules for credit institutions and is used in the determination of the capital ratio. Risk exposure derives from:

- portfolio of securities;
- derivatives; and
- other risk exposure.

PORTFOLIO OF SECURITIES

KommuneKredit's risk exposure amount on its portfolio of securities totalled DKK 3.0 billion at the end of 2019. The portfolio of DKK 45 billion derives from bonds in the liquidity resources.

The bonds are highly liquid bonds with a very high credit quality. In 2019, all bonds were transferred to the banking book, as this carries less weight in Standard & Poor's calculation method.

DERIVATIVES

KommuneKredit's credit exposure on derivatives concluded with financial counterparties totalled DKK 6.0 billion at the end of 2019. The derivatives are used to hedge market risk arising as a result of KommuneKredit's role as link between the capital markets and the customers.

The risk exposure derives from a total principal against financial counterparties of DKK 464 billion. The financial counterparties are exclusively financial enterprises that hold an investment grade rating, i.e. BBB- or better, from the international rating agencies, and all derivatives with financial counterparties are concluded under agreements on bilateral collateral.

OTHER RISK EXPOSURE

Other risk exposure totals DKK 2.9 billion. Other risk exposure mainly consists of operational risk totalling DKK 0.9 billion and FX risk totalling DKK 1.7 billion.

OTHER RISKS

In addition to monitoring and managing the aforementioned financial and operational risks, a number of risks are given special attention in KommuneKredit's day-to-day operations and development. These risks are identified as risks that may cause KommuneKredit a material financial loss, lost or extended use of resources or loss of reputation.

CYBER RISK

It is impossible to fully avoid the risk that IT criminals may exploit, for example internet connections to launch a cyber attack that could potentially render KommuneKredit unable to access its IT platform, provide functionality to its customers or protect customer and employee data. Failure to train employees and give them knowledge of how to protect the association against cyber attacks would notably increase the cyber risk.

KommuneKredit has a large number of technical security measures which are regularly updated to counter cyber attacks.

Employee knowledge about how to counter cyber attacks is also updated through initiatives like e-learning courses.

HARDWARE BREAKDOWN

IT systems are essential for running KommuneKredit's business. There is always a risk that IT components such as servers or network equipment, will fail or break down due to wear or external factors such as power failure, water damage, lightning strikes, etc.

KommuneKredit deploys its systems in two separate data centres where data is mirrored and network traffic can be transmitted through different physical routes.

CRITICAL BUSINESS PROCESSES

Failure to establish well-documented, IT-supported process descriptions independent of specific individuals for all critical business processes involves a risk that the many different tasks in the association will not be handled correctly and adequately within an expected deadline.

KommuneKredit's processes are supported by IT systems to the fullest extent possible. In areas without IT support, a task involving risky or complex processes must be supported by a compensatory control, primarily a peer check.

An in-house operational risk function, working as a "second line of defence", monitors that operational risk is suitably managed by the business.

INTERNAL FRAUD

Inadequate systems, distribution of responsibilities or processes may expose KommuneKredit to the risk that an employee commits fraud against the association or its customers for personal financial gain.

Only a limited number of employees have administrative or extended system rights. Allocation of access rights and other privileges are subject to approval procedures.

Processes have embedded IT controls, peer checks and segregation of duties in relation to all transactions that involve valuables (money and securities).

There is continuous focus on the internal control environment, and managerial employees must complete an annual management inspection which includes assessing the adequacy of checks and controls.

STABLE EXPECTATIONS FOR THE YEAR FULFILLED

A continuing increase in lending activity resulted in an increase in total assets, while expectations for net interest income, administrative expenses and profit before value adjustments and tax were met.

EARNINGS AND CAPITAL BASE

Net interest income amounted to DKK 496 million in 2019, which is satisfactory in relation to maintaining an equity ratio of more than 3%. The net interest income expectations, which were upgraded in connection with the interim report, were to the tune of DKK 500 million.

In 2019, KommuneKredit continued its ongoing price adjustments relative to funding costs with a view to keeping lending margins at a relatively constant level.

Administrative expenses were DKK 126 million, which was largely at the same level as last year. Expenses relative to assets thus stood at 0.05%. The increase relative to the expected DKK 120 million was primarily due to higher IT costs, among other things due to the outsourcing of the server platform and development of business systems.

Profit for the year before value adjustments and tax increased by DKK 55 million to DKK 369 million, which was more or less in line with the expected level of DKK 380 million.

KommuneKredit's low risk tolerance provides a high degree of symmetry between assets and liabilities, and lending margins are kept at a relatively constant level. Consequently, under normal circumstances, value adjustments of financial instruments will be relatively moderate.

In 2019, end-of-month value adjustments of financial instruments amounted to between DKK 126 million and DKK 328 million. The fluctuations were mainly driven by the price risk from own funding spreads, but also to a limited extent by market risk and credit risk. At the end of 2019, value adjustments for the year amounted to DKK 227 million, which was on a level with 2018.

Comprehensive income for the year amounted to DKK 441 million compared with DKK 405 million in 2018. Comprehensive income for the year is transferred to equity, which now totals DKK 8,179 million. Equity consists in its entirety of retained earnings, which is Common Equity Tier 1 (CET1).

According to the Board of Directors' targets, earnings should provide appropriate capitalisation, corresponding to an equity ratio of at least 3%. At year-end 2019, the equity ratio was 3.5%.

The total risk exposure amount (REA) fell to DKK 11,911 million at year-end 2019 from DKK 13,843 million at the end of 2018. The decline was due to the fact that all bonds in 2019 were transferred to the banking book. As

OUTLOOK PROVIDED FOR 2019

	Annual report 2018*	Interim report 2019*	**Result in 2019**
Net lending, DKKm	2,000	2,000	**2,427**
Net interest income, DKKm	400	500	**496**
Administrative expenses, DKKm	120	120	**126**
Profit before value adjustments and tax, DKKm	280	380	**369**
Equity ratio, pct.	3.4	3.4	**3.5**

* Outlook provided for result in 2019

a result, the capital ratio was 67% against 54% at the end of 2018.

LENDING AND LEASING

Total lending incl. leasing rose by DKK 7.5 billion to DKK 185 billion. Of this amount, DKK 2.4 billion was net lending, which is new lending less repayment instalments and redemptions. The rest of the increase was attributable to value adjustments because of lower market rates on loans. Net lending was on a level with expectations for the year of DKK 2 billion.

The positive trend in net lending reflected moderately higher activity in lending as well as leasing. KommuneKredit has especially witnessed an increase in net lending to companies and institutions guaranteed by municipalities or regions. Leasing increased by DKK 840 million, or 12% in 2019.

KommuneKredit did not record any losses on lending or lease receivables in 2019, as was also the case in 2018.

FUNDING AND INVESTMENTS

Funding – due to credit institutions and debt securities issued – increased by DKK 10.2 billion to DKK 219 billion. The increase was primarily driven by a value adjustment caused by lower funding spreads, while a small part of the increase was due to increased funding for lending and investments.

The majority of the outstanding funding is still in EUR, USD and DKK.

Total investments – due from credit institutions and portfolio of securities – stood at DKK 45.0 billion at year-end 2019, against DKK 42.9 billion at year-end 2018. The increase reflects the growing balance sheet. KommuneKredit's liquidity resources accounted for 19% of total lending at year-end 2019, equal to DKK 35.9 billion.

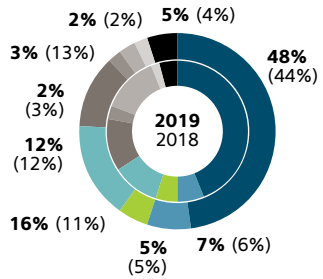
SPECIAL ACCOUNTING MATTERS

IFRS 16, Leasing was implemented with effect from 1 January 2019. The implementation of IFRS 16 has not had any impact on comprehensive income, financial position or equity because KommuneKredit only acts as lessor of finance leases.

» KommuneKredit's low risk tolerance provides a high degree of symmetry between assets and liabilities, and lending margins are kept at a relatively constant level.

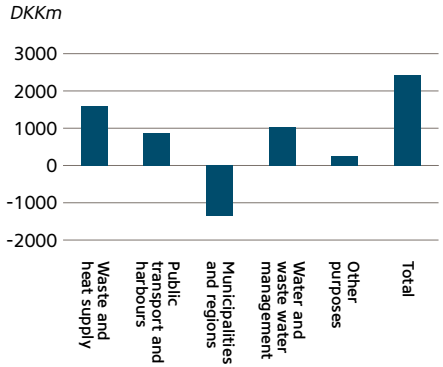
Morten Søtofte
Director, CFO

ADMINISTRATIVE EXPENSES



- Salaries and remuneration, etc.
- Pension contributions, etc.
- Other staff costs
- Consulting fees
- IT licences
- Charges
- Property management
- Depreciation and amortisation of property plant and equipment and intangible assets
- Other administrative expenses

DISTRIBUTION OF NET LENDING



EXPECTED DECREASED LENDING GROWTH REDUCES THE NEED FOR EARNINGS

Owing to KommuneKredit's strong market position and low risk tolerance, the association expects stable developments in 2020 and to maintain an equity ratio of more than 3%. Net lending is expected to be in the order of DKK 2 billion, and net interest income is forecast at DKK 400 million.

The current situation surrounding COVID-19 has an impact on the capital markets, but is not expected to influence KommuneKredit's ability to meet the needs of the customers. Should the markets shut down completely, KommuneKredit's total liquidity resources ensure that lending may continue unaffected for a very long time. All of KommuneKredit's tasks can be carried out regardless of where the employees are located.

Developments in KommuneKredit's lending depend on the legislative framework for lending and the provision of guarantees and on customer decisions to take out a loan. In 2019, there was a tendency of loans having longer refinancing intervals.

OUTLOOK FOR 2020

	Result in 2019	Outlook for 2020
Net lending, DKKm	2,427	2,000
Net interest income, DKKm	496	400
Administrative expenses, DKKm	126	150
Profit before value adjustments and tax, DKKm	369	250
Equity ratio pct.	3.5	3.5

Against that background, the maturity of KommuneKredit's funding has become longer, and the requirement for funding with a maturity of more than 12 months is expected to amount to roughly DKK 30 billion in 2020.

KommuneKredit's net interest income is not expected to be impacted by changed market conditions in 2020 as lending margins are kept relatively constant. Irrespective of sentiment in the financial markets, steady and stable investments will be in demand. This allows for low funding expenses for KommuneKredit and, hence, low lending rates for our customers.

Owing to KommuneKredit's strong market position and relatively constant lending margins, we expect net interest income of about DKK 400 million. Given the expected low level of net lending, this is expected to be an appropriate level of net interest income to consistently ensure adequate capitalisation in the long term. Administrative expenses are expected to be approximately DKK 150 million as costs related to the transformation programme will lead to higher IT development costs. As a result, the profit before value adjustments and tax is expected to be around DKK 250 million.

KommuneKredit generally hedges its financial risks, with the exception of price risk on its own funding spread. Under normal circumstances, value adjustments of financial instruments are expected to amount to a maximum of +/- DKK 500 million. The situation surrounding COVID-19 may, however, cause value adjustments of financial instruments in the short term that are greater than usual.

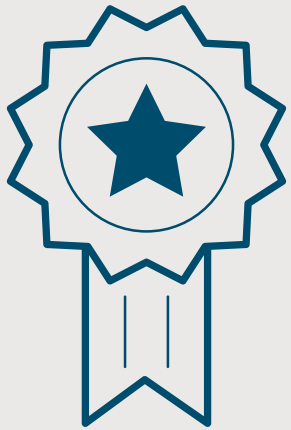
In line with KommuneKredit's strategy, the equity ratio will be maintained at at least 3% of total assets. In the short term, value adjustments of assets and liabilities could temporarily make the equity ratio deviate from the target. If the equity ratio deviates significantly from the target over a longer period of time, the lending margins will be adjusted in order to re-establish an equity ratio of at least 3%.

FORWARD-LOOKING STATEMENTS

The expectations stated in this annual report are inherently subject to uncertainties and may be affected by external factors. This may have the effect that actual developments and actual results may differ significantly from the expectations expressed in the annual report.

FINANCIAL HIGHLIGHTS

RATING



AAA

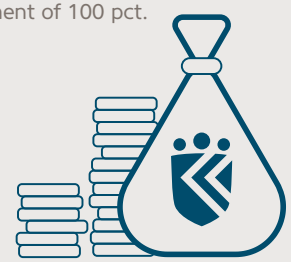
(2018: AA)

Since Standard & Poor's downgraded KommuneKredit iin the summer of 2018, we have devoted intensive efforts in all areas to regain our AAA rating, just as we have always been rated Aaa by Moody's. This happened as early as 2019 and KommuneKredit is back to the safest category of financial counterparties.

LIQUIDITY COVERAGE RATIO (LCR)

350%

KommuneKredit has a LCR of 350 pct. based on CRR/CRD IV, which is substantially higher than the legal requirement of 100 pct.



NET STABLE FUNDING RATIO (NSFR)

165%

Determined in accordance with the preliminary draft for calculating NSFR KommuneKredit has a NSFR of 165 pct.

TOTAL RISK EXPOSURE AMOUNT

11,911 DKKm

(2018: 13.843 mio. kr.)

The total risk exposure amount (REA) decreased to 11.911 DKKm as all the bonds were transferred to the banking book in 2019, as this carries less weight in Standard & Poor's calculation method.

SELECTED FINANCIAL RATIOS

NET INTEREST INCOME

496 DKKm

(2018: 441 DKKm)

PROFIT BEFORE VALUE ADJUSTMENTS

369 DKKm

(2018: 314 DKKm

CAPITAL RATIO

67 DKKm

(2018: 54 DKKm)

EXPENSES/ASSETS, PCT.

0.05%

(2018: 0.6%)

LIQUIDITY RESSOURCES, PCT.

19%

(2018: 19%)

RESPONSIBILITY HIGHLIGHTS 2019

SUSTAINABLE OPERATIONS

- Abolishing the use of plastic bottles
- Company wide use of sustainable paper
- LED lighting
- Weekly vegetarian day

THIRD GREEN BOND

KommuneKredit issues its third green bond

Corporate ESG Performance

Prime

RATED BY ISS ESG

ESG-RATING

KommuneKredit achieves improved ESG-rating

SUSTAINABLE DEVELOPMENT GOALS

Sustainable Development Goals integrated in KommuneKredit's responsibility reporting

TRANSFORMATION PROGRAM

Sustainable Finance becomes a key element in the strategic development of KommuneKredit with the launch of a new Transformation Program.

GREEN LOAN CERTIFICATE

KommuneKredit launches Green Loan Certificate for green loan borrowers

RESPONSIBLE AND EFFICIENT CORPORATE GOVERNANCE

KommuneKredit is organised as an association and has defined corporate governance as responsible and efficient management that benefits KommuneKredit's members and society at large.

MANAGEMENT STRUCTURE

The distribution of responsibilities between the Management Board and the Board of Directors is defined in a policy most recently reviewed by the Board of Directors in August 2019.

The Board of Directors is in charge of the overall and strategic management of KommuneKredit's business and affairs and must ensure a sound organisation of KommuneKredit's business. The Board of Directors make decisions on KommuneKredit's risk tolerance and risk policy and on capital and liquidity targets. Once a year, the Board of Directors takes a position on the matters related to the Board's performance of its responsibilities.

The Management Board is in charge of the day-to-day management of KommuneKredit in accordance with the Act on KommuneKredit and KommuneKredit's articles of association, the policies and guidelines laid down by the Board of Directors and any other instructions by the Board and applicable legislation. The Management Board is authorised, within the framework of the guidelines laid down by the Board of Directors, to make all necessary decisions.

BOARD OF DIRECTORS

The Board of Directors consists of nine members, six of whom are elected by the municipalities, two by the regions and one independent member, who is elected by the Board of Directors. In November 2019, the Board of Directors resolved to amend KommuneKredit's articles of association to the effect that, from 1 June 2020, the Board will be extended to ten members, of whom two are independent and must hold qualifications in the area of accounting, auditing, finance or risk management. The amendment to the articles of association has been approved by the Minister for Industry, Business and Financial Affairs as KommuneKredit's supervisory authority.

Board members are elected for a term of four years. Relative to the election terms applicable to municipalities and regions, the election terms applicable to the Board of Directors are staggered by five months. Election of members to KommuneKredit's Board of Directors was held in spring 2018 for the period from 1 June 2018 to 31 May 2022. The election term for one of the two independent board members is staggered relative to the other board members, and this member is elected for a term of four years starting two years after the others.

The Board of Directors holds at least four ordinary board meetings a year, and its duties follow an annual calendar covering every significant business area. In 2019, the Board of Directors met in March, June, August and November. A quorum exists when at least half of the members of the Board of Directors are present and participate in a vote. Resolutions are passed by a simple majority of votes. The Management Board usually participates in board meetings but is not a part of the Board of Directors. The Board of Directors evaluates its work on an ongoing basis.

AUDIT COMMITTEE

In accordance with the Danish Act on Approved Auditors and Audit Firms, the Board of Directors has resolved that audit committee tasks will be undertaken

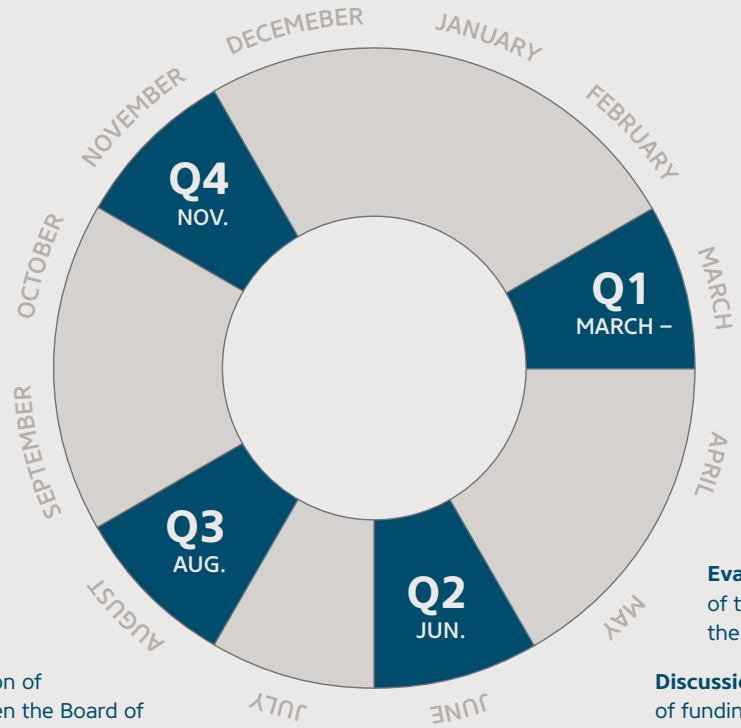
ANNUAL CYCLE OF WORK FOR THE BOARD OF DIRECTORS AND THE AUDIT COMMITTEE

KOMMUNEKREDIT

Audit Committee
Notification of the financial reporting process, forecasts and capitalisation, review of control systems and risk management

Discussion
of liquidity policy and resources

IT
security policy, etc.



Audit Committee
Annual report, long-form audit report

Goals
Goal achievement for last year and next year's goals

Evaluation
of the work performed by the Board of Directors

Discussion
of funding and investment strategy

Discussion
of lending and customer relations

Review
of policy for distribution of responsibilities between the Board of Directors and the Management Board

Audit Committee
Assessment of the auditors' independence, audit strategy and interim report

Reporting
of events involving reputational risk, whistle-blower events, rule overview and compliance

LEGAL BASIS AND ARTICLES OF ASSSOCIATION

KommuneKredit was established by way of Act no. 35 dated 19 March 1898, as repealed and replaced by Act no. 383 dated 3 May 2006 on the Credit Institution for Local and Regional Authorities in Denmark (lov om kreditforeningen af kommuner og regioner i Danmark).

› Read more on KommuneKredit's legal basis and articles of association at www.kommunekredit.com

KommuneKredit is supervised by The Ministry of Industry, Business and Financial Affairs.

While KommuneKredit is not directly encompassed by a corporate governance code, the association does, where relevant and within the provisions of the Act on KommuneKredit, apply the "Corporate governance recommendations" issued by the Danish Committee on Corporate Governance. The recommendations are available at the website of the Committee on Corporate Governance,www.corporategovernance.dk.

KommuneKredit issues bonds listed on a regulated market and is therefore subject to the EU market abuse regulation (596/2014/EU) on inside information and market abuse. The Legal department is responsible for maintaining the insider list.

DAY-TO-DAY MANAGEMENT

MANAGEMENT BOARD
Jens Lundager, Chief Executive Officer and Managing Director
Henrik Andersen, Managing Director

LENDING & LEASING
Christian Jeppesen
Director, Head of Department

TREASURY
Jette Moldrup
Director, Head of Department

RISK & BALANCE
Jonas Toft Månsson
Director, Head of Department

LEGAL
Helene Vinten
General Counsel

FINANCE
Morten Søtofte
Director, CFO

IT
Nadeem Zafar
Director, Head of Department, CIO

BUSINESS DEVELOPMENT & STRATEGY
Søren Steen Mortensen
Director, Head of Department

by the combined members of the Board of Directors. The terms of reference and the annual cycle of work were most recently updated in 2018 in accordance with the Danish Business Authority's guidelines on audit committees. The Audit Committee held three meetings in 2019. At least once a year, the Board of Directors has discussions with the external auditors without the participation of the Management Board or other KommuneKredit employees.

MANAGEMENT BOARD

The CEO is in charge of the day-to-day management of KommuneKredit. The CEO must to the extent possible perform his duties in cooperation with another member of the Management Board as decisions regarding lending, lease agreements, financing, the use of financial instruments and investments require Management Board consensus. In case of disagreement on such matters in the Management Board, the matter will be presented to the Board of Directors.

The Management Board presents to the Board of Directors all significant changes in KommuneKredit's affairs and reports on all important events of consequence for KommuneKredit's business. The Management Board provides the Board of Directors with accounting, financial and risk-related information to update the Board on KommuneKredit's development and allowing the Board to attend to its management duties. At every meeting of the Board of Directors, the Management Board reports on compliance with the Board of Directors' guidelines for financial and operational risk management.

RISK MANAGEMENT AND COMPLIANCE

The Board of Directors has resolved to establish an internal control environment at KommuneKredit, which to a relevant degree is in accordance with the Danish FSA's Executive Order on Management and Control of Banks etc. This entails a strengthening of the functions for operational risk, risk and compliance, which act as independent functions. Jointly, these functions set the framework for the future governance and risk management at KommuneKredit, which is to improve an understanding of risk and control through guidelines, training and support.

HEADS OF DEPARTMENT AND EMPLOYEES

Focus is on delegation of decision-making authority to the seven heads of department for Lending & Leasing, Treasury, Finance, Risk & Balance, Legal, IT and Business Development & Strategy, to the Heads of team within the respective departments and to the individual employees. As part of the ongoing strengthening of management and progress of our development projects and the strategic professionalisation of KommuneKredit's business, effective 15 January 2020 the association made an organisational change with a view to supporting its transformation programme.

In 2019, KommuneKredit had an average of 76 full-time employees. KommuneKredit gives high priority to developing its employees' professional and personal qualifications to enable them to meet the external demands. High priority is also given to knowledge sharing and overlapping of work functions to maintain stability in operations.

SUPERVISION

As of 27 June 2019, KommuneKredit is supervised by the Ministry of Industry, Business and Financial Affairs (previously the supervisory authority was the Ministry for Economic Affairs and the Interior). The Ministry of Industry, Business and Financial Affairs has delegated the task of conducting the ongoing supervision pursuant to the Act on KommuneKredit to the Danish FSA. In addition, it follows from the Act on KommuneKredit that the supervisory authority appoints an auditor. The auditor appointed by the ministry, Thorkil Juul, former head of the National Social Appeals Board, is to oversee, among other things, that KommuneKredit's lending is in accordance with applicable rules on local government borrowing and the delimitation of the association's customer group laid down in Danish legislation.

An agreement on segregation of duties has been signed by the auditor appointed by the ministry and the state-authorised public accountants by the Board of Directors.

REMUNERATION

KommuneKredit's remuneration policy is defined by the Board of Directors. The association's employees are not covered by collective agreement.

A bonus plan is in place, covering all employees with the exception of the Management Board.

EMPLOYEE COMPOSITION

While not formally subject to the rules on management gender composition in major Danish companies and the related reporting, KommuneKredit has decided to follow these rules.

KommuneKredit attaches importance to having a culture in which employees, regardless of gender, have equal opportunity to create a career.

At management level, 64% were men and 36% were women at the end of the year. We also aim to have a diverse gender composition among the other employees. Of the other employees, 60% are men and 40% are women.

KOMMUNEKREDIT'S EDUCATION FUND

KommuneKredit established its education fund in 1986. The purpose of the education fund is to further the development of training and education in public organisations and associations. The education fund offers grants for special projects dedicated to innovation and collaboration across municipal boundaries.

In 2019, KommuneKredit's education fund made grants totalling DKK 470,000 to three different projects.

KommuneKredit's ESG figures (environmental, social and governance data) are available in the appendix to the Responsibility Report.
https://www.kommunekredit.dk/en/about/responsibility/responsibility-report/

GENDER COMPOSITION

› BOARD OF DIRECTORS

Total	Men	Women
9	8	1

› OTHER MANAGEMENT (MANAGEMENT BOARD, HEADS OF DEPARTMENT, HEADS OF TEAM)

Total	Men	Women
14	9	5

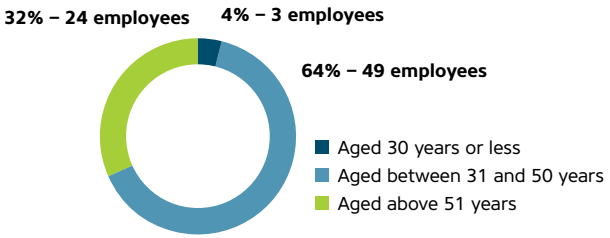
› OTHER EMPLOYEES

Total	Men	Women
62	37	25

AGE COMPOSITION

› AVERAGE AGE FOR EMPLOYEES, YEAR-END

Men	Women
49 years	44 years



BOARD OF DIRECTORS

LARS KRARUP, CHAIRMAN

MAYOR
MUNICIPALITY OF HERNING
Year of birth: 1972
Joined the Board of Directors:
1 January 2007
Up for election: 2022

Directorships:
Realdania
VIA University College

THOMAS LYKKE PEDERSEN, VICE CHAIRMAN

MAYOR
MUNICIPALITY OF FREDENSBORG
Year of birth: 1962
Joined the Board of Directors:
1 June 2018
Up for election: 2022

Directorships:
Fredensborg Forsyning A/S (chairman)
Nordsjællands Brandvæsen (chairman)
Espergærde Gymnasium og HF (chairman)
Dansk Fjernvarmes Handelsselskab (chairman)
Norfors I/S
HMN I/S
Gate 21

MARTIN GEERTSEN

REGIONAL COUNCIL MEMBER
CAPITAL REGION
Year of birth: 1970
Joined the Board of Directors:
1 June 2018
Up for election: 2022

Directorships:
Danish Regions
Fjordforbindelsen Frederikssund
Greater Copenhagen & Skåne Committee

Other fiduciary positions:
Member of parliament

KAJ V. HOLM

DEPUTY CEO OF ØRESUNDSBRO KONSORTIET
DIRECTOR OF FINANCE AT SUND & BÆLT HOLDING A/S
Year of birth: 1955
Joined the Board of Directors:
1 June 2014
Up for election: 2022

Directorships:
Rønne Havn A/S

MIKAEL KLITGAARD

MAYOR
MUNICIPALITY OF BRØNDERSLEV
Year of birth: 1954
Joined the Board of Directors:
1 June 2014
Up for election: 2022

Directorships:
North Denmark EU Office
BRN (Business Region North Denmark)
NBE (Netværk for Bæredygtig Erhvervsudvikling)
Holtegaard Køreforening
NT (Nordjyllands Trafikselskab)
EUC Nord

ERIK LAURITZEN

MAYOR
MUNICIPALITY OF SØNDERBORG
Year of birth: 1960
Joined the Board of Directors:
1 June 2018
Up for election: 2022

Directorships:
Valgbestyrelsen (chairman)
Project Zero Fonden
Sønderborg Havneselskab A/S
EUC Syd
Sct. Jørgens Hospital
Erhvervsakademiet
Erhvervshus Syd

LEILA LINDÉN

REGIONAL COUNCIL MEMBER
CAPITAL REGION
Year of birth: 1944
Joined the Board of Directors:
1 June 2018
Up for election: 2022

ERIK NIELSEN

MAYOR
MUNICIPALITY OF RØDOVRE
Year of birth: 1953
Joined the Board of Directors:
1 June 2014
Will not be standing for re-election in 2022

Directorships:
Boligselskabet DAB (Dansk Almennyttigt Boligselskab)
Realdania (board of representatives)
Realdania, Fagkomité for Byudviklingsforum

HANS TOFT

MAYOR
MUNICIPALITY OF GENTOFTE
Year of birth: 1947
Joined the Board of Directors:
1 January 1995
Up for election: 2022

Directorships:
I/S Vestforbrænding (vice chairman)
Copenhagen Capacity
Wonderful Copenhagen
Gentofte Idrætsfond (chairman)
Svenske Villa Fonden (chairman)

Other fiduciary positions:
Member of the Regional Council, Capital Region of Denmark

MANAGEMENT BOARD

JENS LUNDAGER

CHIEF EXECUTIVE OFFICER, MANAGING DIRECTOR
Year of birth: 1962
Joined the Management Board:
1 September 2015

Former positions:

2011-2015	Assistant Governor, Danmarks Nationalbank
2009-2011	Deputy Permanent Secretary, the Danish Ministry of Economic and Business Affairs
2000-2009	Head of Department, Danmarks Nationalbank
1997-2000	Counsellor (Financial), Royal Danish Embassy, Washington DC
1991-1997	Economist, Danmarks Nationalbank
1987-1991	Economist, Danish Ministry of Finance

Other fiduciary positions

2016-	Chairman, Committee on Auditors (Revisorrådet)

HENRIK ANDERSEN

MANAGING DIRECTOR
Year of birth: 1963
Joined the Management Board:
1 January 2018

Former positions:

2015-2017	Head of Group Treasury, Saxo Bank
2014-2015	Senior Vice President, Nykredit Realkredit A/S
2007-2014	Senior Vice President/Head of Treasury, Nykredit Bank A/S
1990-2007	Trainee, Economist, Head of Department, Nykredit A/S

FINANCIAL STATEMENTS 2019

STATEMENT OF COMPREHENSIVE INCOME

DKKm	Note	2019	2018
Interest income	1.1	1,724	1,725
Interest expense	1.2	-1,229	-1,284
Net interest income		**496**	**441**
Other operating income		13	11
Other operating expenses		-13	-12
Administrative expenses	2.1-2.3	-126	-127
Profit before value adjustments		**369**	**314**
Value adjustments of financial instruments	1.3,1.4	227	227
Profit before tax		**596**	**540**
Tax on profit for the year	3.1	-148	-119
Profit for the year		**448**	**422**
Other comprehensive income			
Actuarial gains and losses	2.3	-7	-22
Tax on actuarial gains and losses	2.3 , 3.1	0	5
Comprehensive income for the year		**441**	**405**
Allocated as follows:			
Transferred to equity		441	405
Total		**441**	**405**

STATEMENT OF FINANCIAL POSITION

DKKm	Note	2019	2018
ASSETS			
Due from credit institutions	1.4	5	2
Lending	1.4, 1.5	176,983	170,312
Leasing	1.6	7,982	7,142
Portfolio of securities	1.4, 1.7	44,982	42,944
Derivatives	1.4	6,610	6,056
Other assets		338	120
Current tax assets	3.2	35	33
Total assets		**236,935**	**226,609**
LIABILITIES AND EQUITY			
Liabilities			
Due to credit institutions	1.4	244	716
Debt securities issued	1.4, 1.8	218,932	208,218
Derivatives	1.4	8,327	8,800
Other liabilities		746	571
Pension obligations	2.3	0	80
Current tax liabilities	3.2	31	63
Deferred tax liabilities	3.3	476	425
Total liabilities		**228,756**	**218,873**
Equity		**8,179**	**7,736**
Total liabilities and equity		**236,935**	**226,609**

EQUITY

DKKm	Note	2019	2018
Equity			
Equity at 1 January		7,736	7,333
Impairment changes due to implementation of IFRS 9		0	-2
Change in payable tax due to implementation of IFRS 9		0	1
Net revaluation reserve		2	0
Change in deferred tax due to net revaluation		0	0
Transferred to equity			
Profit for the year		448	422
Other comprehensive income			
Actuarial adjustments		-7	-22
Tax on other comprehensive income		0	5
Other comprehensive income after tax		-7	-17
Transferred to equity in total		441	405
Equity at 31 December		8,179	7,736

The comprehensive income for the year is transferred to equity in accordance with the articles of association of KommuneKredit.

Equity increased to DKK 8,179 million at year-end 2019 from DKK 7,736 million at the end of 2018. At year-end 2019, equity amounted to 3.5% of total assets, representing a small increase relative to year-end 2018. Equity consists in its entirety of transferred comprehensive income.

Under the legal framework applying to KommuneKredit, equity must equal at least 1.0% of total liabilities, equal to DKK 2,288 million. The Board of Directors' target is for equity to amount to at least 3% of assets, which is considered adequate to support KommuneKredit's activities.

CASH FLOWS

DKKm	Note	2019	2018
Profit before tax		596	541
Depreciation, amortisation and impairment		2	3
Total		599	544
Net interest income reversed		-496	-441
Financial income received		1,724	1,725
Financial expenses paid		-1,229	-1,284
Taxes paid		-129	-109
Increase in lending		-7,511	-3,876
Other assets		-218	-16
Other liabilities		88	46
Cash flows from operating activities		-7,770	-3,955
Acquisition, etc. of assets		-1	-3
Sale of property, plant and equipment		0	0
Change in securities		-2,038	-583
Cash flows from investing activities		-2,039	-586
Change in debt securities issued		10,602	5,960
Derivative financial liabilities		-473	-1,579
Derivative financial assets		-554	427
Cash flows from financing activities		9,575	4,808
Change in cash and cash equivalents		364	811
Deposits in credit institutions		2	3
Short-term payables to credit institutions (< 12 months)		-440	-1,251
Cash and cash equivalents, 1 January		-438	-1,248
Deposits in credit institutions		5	2
Short-term payables to credit institutions (< 12 months)		-80	-440
Cash and cash equivalents, 31 December		-75	-438

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GENERAL

NOTE 1.0 ACCOUNTING POLICIES

GENERAL

The financial statements of KommuneKredit for 2019 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

The financial year follows the calendar year. The functional currency is Danish kroner (DKK), and the annual report is presented in millions of Danish kroner (DKKm).

The concept of materiality has been applied in preparing the annual report. Certain items have been aggregated, and certain disclosures have been omitted because they are immaterial, individually and in the aggregate, to the annual report.

Unless otherwise indicated, all amounts in the annual report are stated in DKK millions. The stated totals have been calculated on the basis of actual amounts before rounding. As amounts are rounded to DKK millions, there may be minor differences between the sum of individual amounts and the stated totals.

Except for the changes described below, the accounting policies are unchanged from the policies applied in the annual report for 2018.

CHANGE IN ACCOUNTING POLICIES

Effective 1 January 2019, KommuneKredit implemented IFRS 16, Leases. As KommuneKredit only acts as lessor of finance leases, the implementation will not have any material impact on results of operations or the association's financial position.

To provide a more fair presentation, KommuneKredit presents the item "Current tax liabilities" separately in the statement of financial position. This is not a change in accounting policies but only an adjustment in terms of presentation.

Comparative figures presented in the annual report have been restated to reflect the above changes.

NEW AND AMENDED STANDARDS

Other than the implementation of IFRS 16, no new or amended standards apply for the 2019 financial year which have had an effect on financial reporting for 2019.

There are no new or amended IFRS standards entering into force and effective for the financial year 2020 or later which are considered to have an effect on financial report for 2020.

SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGMENTS

In the preparation of the financial statements, management makes a number of accounting estimates and judgments. The estimates and judgments are made in accordance with the accounting policies based on assumptions that management finds reasonable and realistic but which are inherently uncertain and unpredictable. The accounting estimates and judgments are tested and assessed in an ongoing process to ensure that they reflect the historical experience and assessments of future conditions.

The accounting estimates and judgments that are deemed critical to the financial statements are where the calculation of fair value is based on input not directly observable in the market and where there are no opposite effect.

In particular, estimates and judgments with respect to the valuation of debt securities issued that are not a part of the bond circuit may affect the financial statements. For these securities, there is no active market for these securities, as a result of which significant accounting estimates are used in the valuation.

Estimates and judgments in the valuation of certain derivatives may also affect the financial statements, as there are no directly observable prices in the market. Observable input in generally accepted cash flow models is used instead.

In the valuation of loans which are not part of the bond circuit, there is no observable market, which means that KommuneKredit applies own current lending prices as market prices.

For all other financial instruments, valuation does not involve significant estimates. This is either because these instruments have quoted prices in an active market, or because there is no significant accounting impact of the estimates applied.

Note 1.4 describes the accounting estimates and judgments relating to the fair value measurement of financial instruments.

Relative to information in the annual report for 2018, no changes were made to the accounting estimates made.

CURRENCY TRANSLATION

The presentation currency used in the financial statements is Danish kroner (DKK). Items denominated in foreign currencies are translated at closing rates on the balance sheet date. Realised and unrealised exchange rate adjustments are recognised in the statement of comprehensive income.

RECOGNITION AND MEASUREMENT

Assets are recognised in the statement of financial position when it is probable that future economic benefits will flow to KommuneKredit.

GENERAL

NOTE 1.0 ACCOUNTING POLICIES (CONTINUED)

Liabilities are recognised in the statement of financial position when it is probable that future economic benefits will flow from KommuneKredit and the value of the liability can be reliably measured.

Income is recognised in profit or loss as earned. Costs are recognised when incurred by KommuneKredit.

Financial assets and financial liabilities are recognised at the transaction date. Realised and unrealised value adjustments of financial assets and financial liabilities to fair value using the fair value option over profit or less are recognised in profit or loss under Value adjustments of financial instruments. Derecognition of both financial assets and financial liabilities is made on expiry or at the time of sale.

The fair value is measured on the basis of quoted market prices of financial instruments traded in active markets. If an active market exists, fair value is based on the most recently observed market price.

If the market for one or more financial assets or financial liabilities is illiquid, fair value is determined using generally accepted valuation methods.

Transaction costs and income are measured on initial recognition.

OFFSETTING

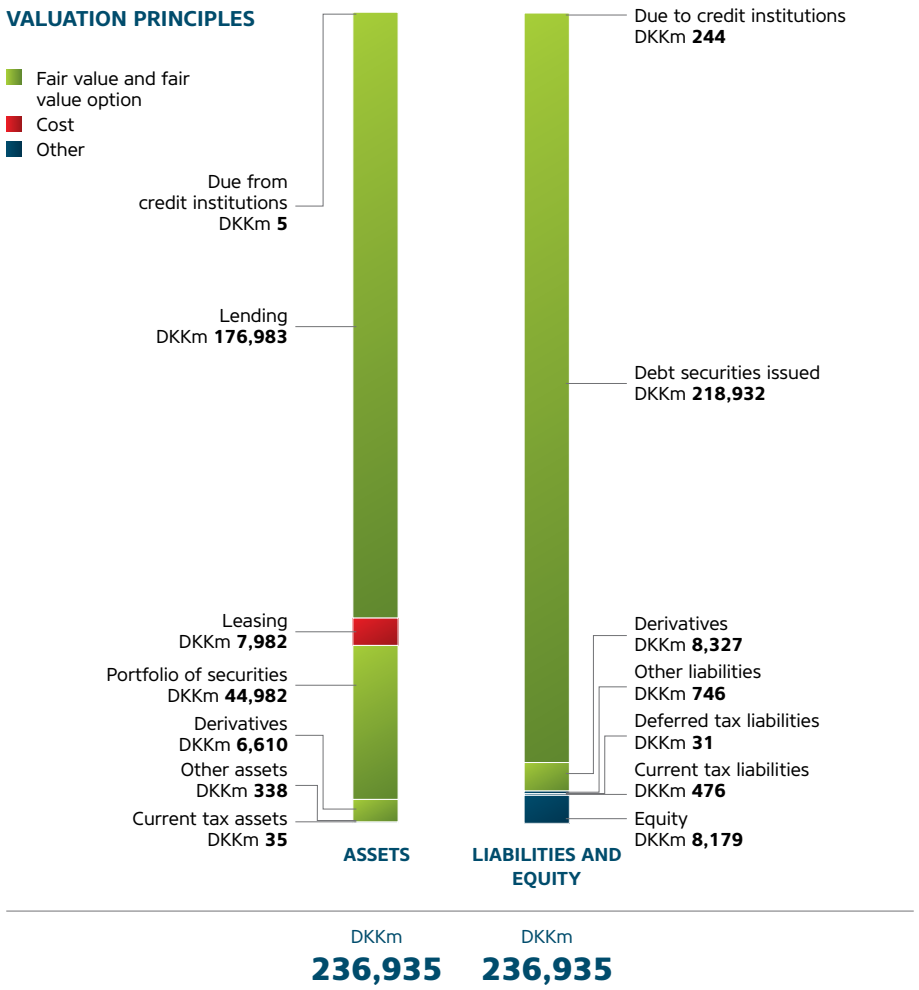
Positive and negative fair values of financial instruments are included in separate items in the statement of financial position, and positive and negative values are set off only when KommuneKredit has the right and the intention to settle several financial instruments on a net basis.

DETERMINATION OF THE VALUE OF FINANCIAL INSTRUMENTS USING THE FAIR VALUE OPTION

KommuneKredit has decided to use the fair value option under IFRS 9 to give the reader a transparent and easy-to-understand calculation of the statement of financial position components.

Using the fair value option also helps ensure consistent accounting treatment of amounts due from credit institutions, lending, portfolio of securities, debt securities issued and derivatives in respect of risk and matching hedges. This implies that lending, securities and derivatives are measured at fair value through profit or loss.

Overall, 96% of the balance sheet items are measured at fair value.



GENERAL

NOTE 1.0 ACCOUNTING POLICIES (CONTINUED)

Further, the fair value option is applied because KommuneKredit's measurement of investment returns is based on fair values, and the relating disclosures to the Management Board and the Board of Directors are based on fair values.

To mitigate the operational risks associated with determination and manual handling of non-observable market data for purposes of fair value measurement of lending, debt securities issued and derivatives, KommuneKredit has internal controls and business procedures in place which ensure distribution of responsibilities, segregation of duties and process management. All critical manual processes are supported by objective controls or peer checks.

More details on quantification of the sensitivity which is, nevertheless, associated with the use of non-observable data are given in note 1.4 regarding the fair value of financial instruments.

SEGMENT INFORMATION

The annual report of KommuneKredit does not disclose information about operating segments, as KommuneKredit has one reportable business segment only.

CORE EARNINGS AND FAIR VALUE ADJUSTMENTS, ETC.

NOTE 1.1 INTEREST INCOME AND NOTE 1.2 INTEREST EXPENSE

Interest income and interest expense are accrued and recognised in the statement of comprehensive income. Interest income and interest expense comprise interest on financial instruments, leasing as well as administrative fees. Interest income and interest expense regarding financial instruments measured at fair value are presented under net interest income.

DKKm	2019	2018
Interest income		
Net financials at amortised cost		
Leasing	29	29
Net financials at fair value		
Fixed-term loans	1,148	1,102
Bond loans	382	480
Portfolio of securities	165	114
Total interest income	**1,724**	**1,725**
Interest expense		
Net financials at fair value		
Bond deposits	355	449
Other loans and derivatives	874	835
Total interest expense	**1,229**	**1,284**

NOTE 1.3 VALUE ADJUSTMENTS OF FINANCIAL INSTRUMENTS

Value adjustments comprise realised and unrealised value adjustments of financial instruments.

DKKm	2019	2018
Value adjustments of financial instruments		
Portfolio of securities	-137	-216
Lending	4,972	708
Impairment of leasing	0	2
Debt securities issued	-4,798	149
Derivatives	190	-416
Total value adjustments of financial instruments	**227**	**227**

FAIR VALUE ADJUSTMENTS, ETC.

1.4.1 SPECIFICATION OF FAIR VALUE OF FINANCIAL INSTRUMENTS

In accordance with IFRS 13, financial instruments measured at fair value must be classified in a fair value hierarchy ranging from level 1 to level 3, depending on how the fair values have been determined and the data on which they are based. The fair value is the amount for which a financial asset or a financial liability can be exchanged between knowledgeable, willing parties.

Fair value is measured on the basis of the following hierarchy:

LEVEL 1: Quoted prices in an active market for identical assets or liabilities.

LEVEL 2: Observable input based on quoted prices in an active market for similar assets or liabilities, or other valuation methods in which the valuation is based substantially on observable input.

LEVEL 3: Non-observable input where the valuation is not based substantially on observable input.

The valuation of fair values in levels 2 and 3 is based on generally accepted models. KommuneKredit uses both A) listed prices for similar issues adjusted for liquidity, credit risk and conversion rights and B) discounted cash flow models, where all estimated and fixed cash flows are discounted using zero coupon interest curves, interest structure and options models.

A) KommuneKredit uses listed prices for similar issues adjusted for liquidity, credit risk and conversion rights on the part of debt securities issued and loans which is referred to as the bond circuit. The bond circuit is characterised by being based on the mortgage credit balance principle where the terms and conditions underlying the debt securities issued by KommuneKredit are passed on directly to the bond loan to the customer plus a margin determined by KommuneKredit.

All of these securities are issued on Nasdaq Copenhagen, but the bonds are illiquid as the frequency and volume of trading is insufficient. Consequently, the listed price cannot be used, and listed prices from similar issues adjusted for liquidity, credit risk and conversion rights are used instead. Similar issues could be mortgage or government bonds with similar characteristics. As the credit risk on loans to customers corresponds to the issued debt securities, the price of the debt securities issued is also used for the bond loan. Price changes will thus not have any impact on the result.

B) KommuneKredit uses discounting of cash flows on derivatives, on loans raised at fair value and on the remaining part of the debt securities issued. These issued securities are also considered illiquid.

The calculation of fair value in level 2 includes observable input like swap rates, FX base swap spreads and exchange rates, etc. KommuneKredit's estimate of the actual funding expenses is also included in the valuation of debt securities issued. The valuation of lending also includes KommuneKredit's current lending prices. KommuneKredit aims to keep lending margins relatively constant by adjusting the actual lending prices on a regular basis against estimated, current funding expenses. The sensitivity associated with estimating actual funding expenses will thus be partly set off by changes in current lending prices. This means that the total value adjustment is considered to have a maximum net effect in the range of +/- DKK 250 million.

A small part of KommuneKredit's debt securities issued and derivatives is classified as fair value level 3. The level is used for structured issued debt securities and pertaining hedging derivatives for which input, in addition to input that applies to fair value level 2, also consists of non-observable input like volatility of currencies, shares and commodities and their correlation. The issued structured debt securities are micro-hedged by derivatives, and changes in the non-observable input will therefore not have any significant impact on the profit as changes in issuance will have an opposite effect on the derivative.

KommuneKredit pursues a risk management strategy of eliminating market risk by using financial instruments (see notes 1.9 -1.11). Consequently, the total net effect on the statement of comprehensive income and equity derived from changes in estimates and assumptions used to calculate the fair value under levels 2 and 3 is reduced to include changes in the funding expenses lending prices.

No transfers between the levels were made in 2019.

FAIR VALUE ADJUSTMENTS, ETC.

NOTE 1.4.1 SPECIFICATION OF FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

DKKm	Level 1	Level 2	Level 3	Total
2019				
Assets				
Due from credit institutions	5	0	0	5
Lending	0	176,983	0	176,983
Portfolio of securities	43,014	1,968	0	44,982
Derivatives	0	5,796	814	6,610
Total assets	**43,019**	**184,747**	**814**	**228,580**
Liabilities				
Due to credit institutions	80	164	0	244
Debt securities issued	0	211,110	7,822	218,932
Derivatives	0	7,973	354	8,327
Total liabilities	**80**	**219,247**	**8,176**	**227,503**

DKKm	Level 1	Level 2	Level 3	Total
2018				
Assets				
Due from credit institutions	2	0	0	2
Lending	0	170,312	0	170,312
Portfolio of securities	42,944	0	0	42,944
Derivatives	0	5,309	747	6,056
Total assets	**42,946**	**175,621**	**747**	**219,314**
Liabilities				
Due to credit institutions	440	276	0	716
Debt securities issued	0	199,617	8,601	208,218
Derivatives	0	7,583	1,217	8,800
Total liabilities	**440**	**207,476**	**9,818**	**217,734**

FAIR VALUE ADJUSTMENTS, ETC.

1.4.2 SPECIFICATION OF LEVEL 3 FAIR VALUE

DKKm	1 Jan.	Additions	Disposals	Recognised in profit for the year	31 Dec.
2019					
Assets					
Due from credit institutions	0	0	0	0	0
Lending	0	0	0	0	0
Portfolio of securities	0	0	0	0	0
Derivatives	747	0	-14	81	814
Total assets	**747**	**0**	**-14**	**81**	**814**
Liabilities					
Due to credit institutions	0	0	0	0	0
Debt securities issued	8,601	0	-919	140	7,822
Derivatives	1,217	0	-858	-5	354
Total liabilities	**9,818**	**0**	**-1,777**	**135**	**8,176**

DKKm	1 Jan.	Additions	Disposals	Recognised in profit for the year	31 Dec.
2018					
Assets					
Due from credit institutions	0	0	0	0	0
Lending	0	0	0	0	0
Portfolio of securities	0	0	0	0	0
Derivatives	905	0	-63	-95	747
Total assets	**905**	**0**	**-63**	**-95**	**747**
Liabilities					
Due to credit institutions	0	0	0	0	0
Debt securities issued	13,938	520	-5,724	-133	8,601
Derivatives	1,035	80	-231	333	1,217
Total liabilities	**14,973**	**600**	**-5,955**	**200**	**9,818**

FAIR VALUE ADJUSTMENTS, ETC.

NOTE 1.4.3 CHANGE IN CREDIT SPREADS

The monetary effect caused by credit spreads on fair value adjustments on the statements of comprehensive income and financial position (equal to CVA/DVA on derivatives) is shown below. The calculations are based on a model based on the future positive and negative exposure adjusted for the probability of default and resulting losses. The calculations are based on market-based probabilities of default.

DKKm	2018	Change	**2019**
Statement of comprehensive income			
Value adjustments of financial instruments	-48	31	-17
Total effect on statement of comprehensive income	**-48**	**31**	**-17**
Statement of financial position			
Assets	-42	5	-37
Liabilities	6	-26	-20
Total effect on statement of financial position	**-48**	**31**	**-17**

NOTE 1.4.4 OFFSETTING

KommuneKredit settles foreign exchange transactions and derivatives on a net basis when a master netting agreement (ISDA Master Agreement) includes an agreement on Cross-Transaction Payment Netting. The net settlement entails that the accounting values for derivatives contain offsetting in the financial position. Total offsetting amounted to DKK 5,289 million at 31 December 2019 against DKK 3,210 million at 31 December 2018. The change in the offsetting value was primarily due to the conclusion of seven new agreements on Cross-Transaction Payment Netting in 2019.

In ISDA Master Agreements where no Cross-Transaction Payment Netting is included, the accounting values will not include offsetting in the financial position. The netting value of derivatives not offset has been limited to the lesser of assets and liabilities calculated per counterparty. The amount is included in both assets and liabilities.

ISDA Master Agreements include unilateral or bilateral collateral agreements relating to derivatives. Collateral received and posted under these agreements solely includes bonds with a strong credit rating. The amount of collateral is calculated per counterparty and has been limited to the net value of the financial instruments for which the bonds have been provided as collateral. The collateral agreements only entitle offsetting of collateral in case of bankruptcy and not on a regular basis. No offsetting is applied for the value of the collateral.

KommuneKredit has not entered into any netting agreements and has not posted or received any collateral in relation to lending, leasing or debt securities issued. Accordingly, these financial instruments are not included in the table below. Carrying amounts appear from the statement of financial position.

Derivatives presented in the statement of financial position

	Values offset			Values not offset		
DKKm	Gross carrying amount	Set-off	Carrying amount	Financial instru-ments	Collateral	Net value
2019						
Assets	11,899	-5,289	6,610	-874	-4,069	1,667
Liabilities	13,616	-5,289	8,327	-874	-4,359	3,094
Net	**-1,717**	**0**	**-1,717**	**0**	**290**	**-1,427**
2018						
Assets	9,266	-3,210	6,056	-1,668	-2,481	1,907
Liabilities	12,010	-3,210	8,800	-1,668	-3,929	3,203
Net	**-2,744**	**0**	**-2,744**	**0**	**1,448**	**-1,296**

FAIR VALUE ADJUSTMENTS, ETC.

1.4.5 SPECIFICATION OF COLLATERAL

DKKm		Collateral posted		Collateral received	
Type of bond	Rating	Market value	Market value after haircut	Market value	Market value after haircut
2019					
Danish government bonds	AAA	0	0	0	0
Danish mortgage bonds	AAA	0	0	102	100
Danish mortgage bonds	AA+	0	0	379	372
German government bonds	AAA	0	0	82	79
British government bonds	AA	954	848	2,238	2,109
French government bonds	AA	3,888	3,761	1,823	1,692
Total		**4,842**	**4,609**	**4,624**	**4,352**
Of which non-nettable collateral		0	-250	0	-283
Total nettable collateral		**4,842**	**4,359**	**4,624**	**4,069**

DKKm		Collateral posted		Collateral received	
Type of bond	Rating	Market value	Market value after haircut	Market value	Market value after haircut
2018					
Danish government bonds	AAA	1,048	1.014	0	0
Danish mortgage bonds	AAA	0	0	181	174
Danish mortgage bonds	AA+	0	0	59	58
German government bonds	AAA	0	0	0	0
British government bonds	AA	0	0	1,973	1,884
French government bonds	AA	3,307	3,179	411	387
Total		**4,355**	**4,193**	**2,624**	**2,503**
Of which non-nettable collateral		0	-264	0	-22
Total nettable collateral		**4,355**	**3,929**	**2,624**	**2,481**

Reference is made to note 1.10.3 for a detailed description of requirements, etc.

FAIR VALUE ADJUSTMENTS, ETC.

NOTE 1.5 LENDING

Lending is measured at fair value through profit or loss. Lending is measured at amortised cost, but is presented here for the sake of completeness.

DKKm	No. of loans	2019	2018
Lending			
1 January	18,152	177,454	173,579
Additions	3,890	36,745	38,261
Disposals	3,361	29,234	34,386
Total lending	**18,681**	**184,965**	**177,454**
Bond loans	2,202	30,748	31,423
Fixed-term loans	4,953	146,235	138,889
Leasing	11,526	7,982	7,142
Total lending	**18,681**	**184,965**	**177,454**
Bond loans		30,748	31,423
Fair value adjustments		-2,082	-1,961
Bond loans in nominal values		**28,667**	**29,462**
Fixed-term loans		146,235	138,889
Fair value adjustments		-9,539	-4,576
Fixed-term loans in nominal values		**136,696**	**134,313**
Leasing		**7,982**	7,142
Impairment		2	2
Leasing in nominal values		**7,984**	**7,144**

NOTE 1.6 UNEARNED FINANCIAL INCOME RELATING TO LEASING

Leasing is not covered by the fair value option. KommuneKredit is the lessor of finance leases. Finance leases are recognised in the statement of financial position as a receivable at an amount corresponding to the future minimum lease payment discounted at the interest rate implicit in the lease. On subsequent recognition, leasing is measured at amortised cost. The difference between the value on initial recognition and nominal value is accrued over the term to maturity and is recognised as “interest on leasing” under Interest income.

DKKm	2019	2018
Net investments in finance leases, by lease term		
Up to 1 year	**1,416**	1,025
From 1 to 5 years	**3,640**	3,516
Over 5 years	**2,930**	2,603
Total net leasing	**7,986**	**7,144**
Gross investments in finance leases, by lease term		
Up to 1 year	**1,444**	1,049
From 1 to 5 years	**3,728**	3,591
Over 5 years	**3,104**	2,733
Total gross leasing	**8,276**	**7,373**
Unearned financial income	**291**	**229**

FAIR VALUE ADJUSTMENTS, ETC.

NOTE 1.7 PORTFOLIO OF SECURITIES

The portfolio of securities is measured at fair value through profit or loss.

DKKm	2019	2018
Portfolio of securities		
Government/public authorities	17,867	14,507
Multilateral counterparties	1,336	579
Mortgage credit institutions	25,419	27,233
Banks	360	626
Total portfolio of securities	**44,982**	**42,944**
Of this portfolio of securities used as collateral	3,486	4,339
Portfolio of unencumbered securities	**41,496**	**38,605**

NOTE 1.8 DEBT SECURITIES ISSUED

Debt securities issued are measured at fair value through profit or loss.

DKKm	1 Jan.	Additions	Disposals/ value adj.	31 Dec.	Value adjustment	Fair value 31 Dec.
2019						
Nasdaq Copenhagen	38,910	13,595	-4,351	48,154	2,823	50,976
ECP	0	22,068	-22,068	0	0	0
Private Placements	26,866	0	-3,247	23,619	2,981	26,600
Uridashi	6,469	0	-1,478	4,992	-1,016	3,976
Benchmark	128,412	14,036	-12,824	129,623	3,672	133,295
Kangaroo	3,670	0	61	3,731	354	4,085
Total issued securities	**204,327**	**49,699**	**-43,908**	**210,118**	**8,815**	**218,932**
2018						
Nasdaq Copenhagen	37,892	8,755	-7,737	38,910	2,498	41,408
ECP	0	9,815	-9,815	0	0	0
Private Placements	34,012	0	-7,146	26,866	2,205	29,071
Uridashi	5,960	805	-296	6,469	-2,155	4,314
Benchmark	116,445	40,438	-28,471	128,412	1,242	129,654
Kangaroo	3,626	242	-198	3,670	101	3,771
Total issued securities	**197,935**	**60,055**	**-53,663**	**204,327**	**3,891**	**208,218**

FINANCIAL RISK MANAGEMENT

GENERAL

Our function as a financial link between the capital markets and local authorities in Denmark exposes KommuneKredit to financial risks. Through prudent risk management, it is ensured that KommuneKredit's risk profile matches the Board of Directors' low risk tolerance. The low risk tolerance means that KommuneKredit only assumes financial risks that are absolutely necessary to accomplish KommuneKredit's mission. KommuneKredit has established in-house committees which meet regularly to discuss relevant risk exposures like market risk and credit risk.

KommuneKredit distinguishes between the following types of financial risks:

- Market risk is the risk that market factor fluctuations will affect the market value of a financial instrument. Market risk comprises currency risk, interest rate risk, volatility risk and other price risk.
- Credit risk is the risk of incurring a credit loss. Credit loss is defined both as the failure of a counterparty to honour its obligations towards KommuneKredit and as changes in market expectations to the ability of a counterparty to honour its obligations in general.
- Liquidity risk is the risk that KommuneKredit at any given time does not have and cannot source adequate liquid funds to cover its obligations and loan commitments given.

NOTE 1.9 MARKET RISK

KommuneKredit limits the market risk by using derivatives. The limited market risk mitigates the risk of loss resulting from changes in market factors.

KommuneKredit distinguishes between the following types of market risks:

- Currency risk is the risk that exchange rate fluctuations will affect the market value of a financial instrument.
- Interest rate risk is the risk that interest rate fluctuations will affect the market value of a financial instrument.
- Volatility risk is the risk that changes in volatilities on interest rates, currencies, share indices, commodity prices or similar factors will affect the market value of a financial instrument.
- Other price risk is the risk that changes in market factors other than those attributable to interest rate, currency and volatility fluctuations will affect the market value of a financial instrument. This includes exposures to e.g. commodity indices, equity indices and exposure to KommuneKredit's own funding spreads.

FINANCIAL RISK MANAGEMENT

NOTE 1.9.1 CURRENCY RISK

POLICIES AND PROCEDURES

KommuneKredit's risk tolerance in respect of currency risk is very limited, as it is most often not necessary to accept such risk to accomplish KommuneKredit's mission.

Currency risk is managed either by hedging funding in foreign currency using derivatives or by ensuring that total liquidity resources investments are made in the same currency as the funding. In this way, KommuneKredit minimises its currency position. In the principal funding currencies such as EUR and USD, KommuneKredit on a smaller scale assumes currency risk in the form of unrealised gains and losses.

According to the guidelines, the net position calculated as the present value of future payments in EUR must not exceed DKK 1,000 million, and the net position for all other currencies combined must not exceed DKK 100 million.

MEASUREMENT

The currency position is presented separately for receivables and liabilities as well as derivatives where the position is calculated using market values based on the same discount curve. The distribution shows how the derivatives are used to hedge the resulting currency position from receivables and liabilities.

At the end of 2019, KommuneKredit's currency position was DKK -27 million in EUR and DKK 3 million in USD, while all other currency exposures were zero.

FINANCIAL RISK MANAGEMENT

NOTE 1.9.1 CURRENCY RISK (CONTINUED)

Currency risk

DKKm		Assets	Liabilities	Derivatives	Currency position
2019					
Australian dollar	AUD	138	7,792	7,654	0
Brazilian real	BRL	0	1,043	1,043	0
Swiss franc	CHF	306	7,160	6,854	0
Euro	EUR	12,281	90,066	77,758	-27
Pound sterling	GBP	0	3,145	3,145	0
Japanese yen	JPY	0	2,074	2,074	0
Mexican peso	MXN	0	1,238	1,238	0
Norwegian kroner	NOK	0	4,130	4,130	0
Swedish kroner	SEK	0	3,206	3,206	0
US dollar	USD	7,965	48,189	40,226	3
Other currencies*		0	1,759	1,759	0
Total		**20,690**	**169,802**	**149,087**	**-24**

* Other currencies comprise CAD, HKD, INR, NZD, TRY, ZAR.

Currency risk

DKKm		Assets	Liabilities	Derivatives	Currency position
2018					
Australian dollar	AUD	133	7,346	7,212	-1
Brazilian real	BRL	0	1,216	1,216	0
Swiss franc	CHF	484	7,721	7,237	0
Euro	EUR	10,395	80,493	69,933	-165
Pound sterling	GBP	97	2,970	2,874	1
Japanese yen	JPY	0	3,538	3,538	0
Mexican peso	MXN	0	985	985	0
Norwegian kroner	NOK	0	5,675	5,675	0
Swedish kroner	SEK	1,717	3,153	1,437	1
US dollar	USD	2,392	53,553	51,137	-24
Other currencies*		310	1,834	1,524	0
Total		**15,528**	**168,484**	**152,768**	**-188**

* Other currencies comprise CAD, HKD, INR, NZD, TRY, ZAR.

FINANCIAL RISK MANAGEMENT

NOTE 1.9.2 INTEREST RATE RISK

POLICIES AND PROCEDURES

KommuneKredit's risk tolerance in respect of interest rate risks is limited, but it is deemed necessary to accept certain interest rate risks to accomplish KommuneKredit's mission.

KommuneKredit primarily accepts interest rate risks when the total liquidity resources are invested in bonds.

The interest rate risk is managed by hedging lending, funding and investments with a fixed rate of interest of a certain size one-to-one using derivatives. The remaining interest rate risk is also managed using derivatives with hedging at portfolio level.

According to the guidelines, the interest rate risk must not exceed 4.5% of equity, corresponding to DKK 368 million. The interest rate risk is calculated using a 1 percentage point parallel shift in the yield curve.

DKKm	**2019**	2018
Total interest rate risk	**180**	**164**
Equity used for limit	8,179	7,736
Interest rate risk limit of 4.5% of equity	**368**	**348**
Utilisation of the limit as a percentage	**49**	**47**

NOTE 1.9.3 VOLATILITY RISK

POLICIES AND PROCEDURES

KommuneKredit's risk tolerance in respect of volatility risk is very low, as it is not necessary to accept volatility risk to accomplish KommuneKredit's mission.

KommuneKredit may to very limited extent assume volatility risk in the form of interest rate volatility risk. Interest rate volatility risks arise when KommuneKredit invests in callable bonds or bonds with a cap or floor.

According to the Board of Directors' guidelines, the interest rate volatility risk must not exceed 0.2% of equity, corresponding to DKK 16 million. The interest rate volatility risk is calculated based on a 1 percentage point shift in the interest rate volatility. At the end of 2019, there was only limited interest rate volatility risk.

NOTE 1.9.4 OTHER PRICE RISK

POLICIES AND PROCEDURES

KommuneKredit is exposed to risk associated with changes to its own funding spreads. By maintaining relatively constant lending margins, changes to KommuneKredit's own funding spreads are passed on to lending prices. As the funding is larger and has longer maturities than the binding loan commitments, part of the effect of changed funding spreads will not be passed on to lending prices. The risk on own funding spreads is a part of KommuneKredit's business model and will therefore be necessary in order to accomplish KommuneKredit's mission, but efforts are made to keep it low.

The risk associated with KommuneKredit's own funding spreads is measured and reported on a continuing basis.

KommuneKredit's risk tolerance in respect of other price risk than the risk of changes to its own funding spreads is very low.

Other price risk than the risk of changes to KommuneKredit's own funding spreads may arise when KommuneKredit issues bonds related to commodity indices or the like. According to the Board of Directors' guidelines, such other price risks must be hedged at the issue date.

FINANCIAL RISK MANAGEMENT

NOTE 1.10 CREDIT RISK

POLICIES AND PROCEDURES

KommuneKredit is exposed to credit risk in connection with investing in bonds for the liquidity resources and when entering into derivatives which reduce the market risk. Moreover, credit risk attaches to lending and leasing to the municipal and regional sector in Denmark.

Lending and leasing are only granted to Danish local authorities or against a 100% guarantee from these authorities. In this section, recipients of lending and leasing will be referred to as customers. Derivatives with customers are hedged in the same way as for lending and leasing. Investment counterparties and counterparties with respect to derivatives who are not customers will be referred to as counterparties.

Due to the special credit quality of its customers, KommuneKredit assesses that there is very limited credit risk associated with lending, lease agreements and derivatives with customers. However, in accordance with IFRS 9, credit risk on leases must be calculated as they are recognised at cost. The credit risk on leases has been calculated at DKK 2 million. KommuneKredit has a Grants Committee whose duties include approving loans for more than DKK 300 million or where a loan otherwise deviates from standard practice. Credit events such as a request for forbearance are also considered by the Grants Committee. KommuneKredit has never recorded a loss on a loan.

Credit risk on lending, leasing and derivatives with customers

DKKm	Carrying amount	Credit risk
2019		
Danish municipalities and regions	105,473	2
Institutions guaranteed by Danish municipalities and regions	80,542	0
Total	**186,015**	**2**
2018		
Danish municipalities and regions	105,390	2
Institutions guaranteed by Danish municipalities and regions	73,442	0
Total	**178,832**	**2**

In order to reduce the credit risk, KommuneKredit can only enter into financial instruments with counterparties with whom a bilateral collateral agreement has been concluded. According to the guidelines on the posting of collateral, such agreements must meet the following requirements as a minimum:

- Daily exchange of collateral and low threshold values.
- Collateral received under the agreements must be high-quality liquid bonds.

In order to further reduce the credit risk on other counterparties, the credit risk guidelines include strict requirements as to the credit quality, both in relation to the type of counterparty and the rating of the counterparty by credit rating agencies. As a result, financial instruments may only be entered into with the following types of counterparties:

- Central governments, regions, municipalities and other public authorities.
- Multilateral development banks and international organisations.
- Banks, other financial institutions and issuers of covered bonds.

Counterparties must either be resident in a country that has been granted the lowest risk classification in the OECD's Country Risk Classification or in a country that has not been audited or classified for these purposes, but is audited as a high-income OECD or Eurozone country.

In addition, counterparties must have a rating of at least AA- from Moody's Investors Services or Standard & Poor's or a similar rating from Fitch Ratings. If a collateral agreement has been entered into with the counterparty, ratings down to A- are accepted. Finally, agreements with lower-rated, systemically important Danish banks are permitted.

According to the Board of Directors' guidelines, counterparties satisfying these requirements may be granted a credit risk line by the Management Board.

Expected credit risk losses are recognised in the statement of comprehensive income on an ongoing basis.

FINANCIAL RISK MANAGEMENT

NOTE 1.10 CREDIT RISK (CONTINUED)

KommuneKredit sets limits for the concentration of credit risks based on large exposures in EU regulation on prudential requirements for credit institutions and investment firms. According to this regulation, exposures to a single customer or a group of connected customers, net of fully and completely secured exposures, cannot exceed 25% of the base capital, which for KommuneKredit's purposes substantially corresponds to equity. The Management Board has also defined limits for the maximum portfolio of securities issued by a specific issuer.

The concentration of credit risk by rating, counterparty type, instrument type and geographical area is shown in 1.10.2.

The Management Board and participants from Lending & Leasing, Treasury, Finance and Risk & Balance meet regularly in committees to assess the current risk.

NOTE 1.10.1 CREDIT RISK MEASUREMENT

MEASUREMENT

Credit risks can be broken down into two main components. The first component is the credit risk associated with amounts due from credit institutions and securities, collectively called investment credit risk. This derives from investments made using means from the liquidity resources. The other component is the credit risk associated with derivatives and related collateral, collectively called credit risk on derivatives. This derives from the hedging of, primarily, interest rate risk and currency risk.

The credit risk on both components is limited due to the high rating requirements and requirement for collateral agreements when trading in derivatives.

Total exposures associated with credit risk increased by DKK 1.9 billion from DKK 43.7 billion in 2018 to DKK 45.6 billion in 2019. The investment credit risk increased by DKK 2.0 billion, while the credit risk on derivatives decreased by DKK 0.1 billion.

The credit quality of investments remains very high with 99% of the exposure being placed in securities rated AA- or higher. Most of the investment portfolio consists of Danish mortgage bonds, French government bonds and other highly rated institutions and multilateral development banks.

The decrease in overall exposure on derivatives was due to the fact that a large part of the exposure is hedged by collateral. The exposure before collateral increased by DKK 1.5 billion, while the collateral after haircut increased by DKK 1.6 billion. At the end of 2019, 87% of the market value of the derivatives portfolio was covered by collateral received.

The rating is based on Moody's Investors Service, Standard & Poor's and/or Fitch Ratings. If the counterparty is rated by two rating agencies, the lowest rating will be applied. If the counterparty is rated by three credit rating agencies, the middle rating of the three credit ratings is used. When investing in securities, the rating of the securities is used, and for all financial instruments covered by a guarantee, the rating of the guarantor is used.

Any collateral received that exceeds the fair value of derivatives at counterparty level is not included in the credit risk-reducing collateral. In respect of counterparties posting collateral for their liabilities vis-a-vis KommuneKredit, the collateral is classified based on the rating of the counterparty. Thus, the classification does not reflect the rating of the collateral. The credit risk-reducing element of the collateral equals the value of the nettable collateral in note 1.4.5.

As the credit risk made up as fair value at counterparty level cannot be negative, an adjustment in this respect has been made in the column "Correction for neg. FV per counterparty".

FINANCIAL RISK MANAGEMENT

NOTE 1.10.1 CREDIT RISK MEASUREMENT (CONTINUED)

DKKm	Investment credit risk			Credit risk on derivatives					Total
				Derivatives					
Rating	Due from credit institutions	Securities	Total	Positive	Negative	Correction for neg. FV per counterparty	Collateral after haircut	Total	Net
2019									
AAA	0	29,611	29,611	0	0	0	0	0	29,611
AA+	0	6,589	6,589	0	0	0	0	0	6,589
AA	0	7,691	7,691	256	-90	0	-95	71	7,762
AA-	0	1,091	1,091	4,363	-5,636	2,471	-894	304	1,395
A+	3	0	3	1,918	-1,575	914	-1,042	215	218
A	2	0	2	1,523	-5,361	3,902	-64	0	2
A-	0	0	0	1,973	-636	163	-1,488	12	12
BBB+	0	0	0	796	-295	0	-486	15	15
Total	**5**	**44,982**	**44,987**	**10,829**	**-13,593**	**7,450**	**-4,069**	**617**	**45,604**
2018									
AAA	0	32,799	32,799	0	0	0	0	0	32,799
AA+	0	1,276	1,276	0	0	0	0	0	1,276
AA	0	8,302	8,302	179	-20	0	0	159	8,461
AA-	1	567	568	2,580	-3,978	1,929	-219	312	880
A+	0	0	0	723	-2,069	1,477	-87	44	44
A	1	0	1	2,064	-3,503	2,216	-535	242	243
A-	0	0	0	143	-1,040	897	0	0	0
BBB+	0	0	0	2,150	-1,431	922	-1,640	1	1
Total	**2**	**42,944**	**42,946**	**7,839**	**-12,041**	**7,441**	**-2,481**	**758**	**43,704**

FINANCIAL RISK MANAGEMENT

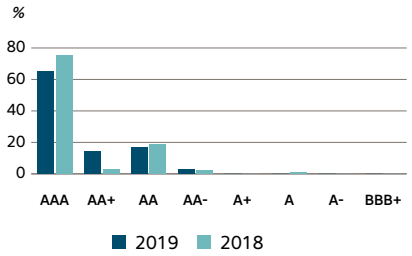
NOTE 1.10.2 CREDIT QUALITY

KommuneKredit has never incurred losses on loans or leases because its customers are exclusively Danish municipalities and regions and companies and institutions guaranteed by these bodies. At the end of the year, KommuneKredit had no overdue receivables.

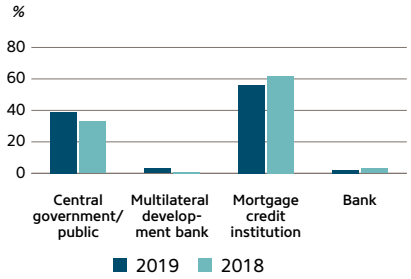
65% of the total exposure relates to counterparties with the highest rating, 34% has a rating between AA+ and AA-, and less than 1% has a lower credit rating. The credit quality of KommuneKredit's counterparties is thus very high.

Compared with 2018, a larger proportion of the investments at the end of 2019 was placed in bonds issued by a government or public authority than in Danish mortgage bonds. This resulted in a shift in rating exposure from AAA to AA+ of 10 percentage points.

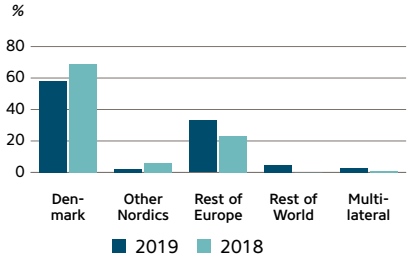
EXPOSURE BY RATING



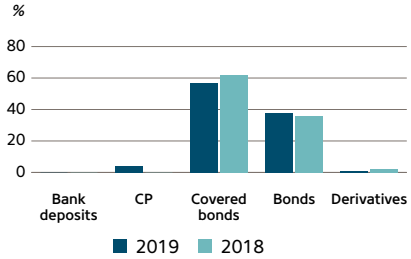
EXPOSURE BY TYPE OF COUNTERPARTY



EXPOSURE BY GEOGRAPHICAL AREA



EXPOSURE BY TYPE OF INSTRUMENT



1.10.3 COLLATERAL RECEIVED

All KommuneKredit's collateral agreements have been concluded as annexes (Credit Support Annexes) to ISDA Master Agreements. In order to ensure maximum credit risk reduction, low threshold values have been agreed as well as daily valuations and exchange of collateral.

When collateral is posted, a haircut (deduction) is calculated in respect of the collateral, depending on instrument, rating and term to maturity. This haircut is a buffer protecting the parties against fluctuations in the market value in case the collateral is to be realised.

2,602 transfers of collateral totalling DKK 79 billion in nominal value were made in 2019. This high level of activity is a reflection of the low threshold values and the daily exchange, which ensures that collateral is posted on a regular basis for as large a part of the credit risk as possible.

To further reduce the credit risk, the collateral agreements also include strict requirements as to the quality of the collateral posted. Under the collateral agreements, collateral must be highly rated mortgage credit bonds or government bonds issued by countries with a high rating. As indicated in note 1.4.5, 89% of the collateral received at year-end 2019 was thus British, French or German government bonds. The remaining 11 was Danish mortgage credit bonds with the highest or second-highest credit quality. Thus, all collateral received is high-quality liquid bonds.

A minor share of the collateral received exceeds the net value of the derivatives at counterparty level. Accordingly, these are not included as credit risk-reducing collateral.

FINANCIAL RISK MANAGEMENT

NOTE 1.11 LIQUIDITY RISK

POLICIES AND PROCEDURES

Even if KommuneKredit's risk tolerance in respect of liquidity risks is very low, such risks cannot be avoided. The Management Board meets on a regular basis in the Finance Committee to discuss the liquidity risk.

The overall principle for liquidity risk mitigation is based on a maturity match between the commitment period for funding and lending. As a consequence of the liquidity limit, binding lending commitments cannot be entered into unless at least corresponding binding funding commitments are in place with at least corresponding terms to maturity. Equity may be used for funding purposes.

According to the liquidity guidelines, the total holding of high-quality, unrestricted liquid assets (HQLA) must exceed the accumulated liquidity outflows in a 30-day stress scenario. This is achieved by keeping the liquidity coverage ratio (LCR) constantly above 110%. Furthermore, the stable medium-term and long-term funding, i.e. more than one year, must exceed the liquidity requirements in a stress scenario This is achieved by keeping the Net Stable Funding Ratio (NSFR) constantly above 110%. LCR and NSFR are based on the Liquidity Coverage Ratio and Net Stable Funding Ratio of CRR/CRD IV. At year-end 2019, LCR was 350%, and NSFR was 165%.

The guidelines also define a requirement on diversification of funding on sources, currencies and maturities, including requirements on diversification of funding maturities, to ensure the best possible access to new funding.

To ensure that the bonds in the liquidity resources are liquid, it is required that most the bonds are HQLA bonds and categorised as eligible collateral with either Danmarks Nationalbank or the ECB. At year-end 2019, 93% of all bonds were classified as HQLA, and 88% were categorised as eligible collateral with either Danmarks Nationalbank or the ECB.

The Board of Directors has determined a minimum 180 day requirement for the survival horizon in a going concern stress scenario. At year-end 2019, the survival horizon was 375 days. The stress scenario is based on assumptions that there is no access to the funding markets, that KommuneKredit continues new lending and that the markets are developing unfavourably for KommuneKredit in relation to investments and collateral for derivatives. Loans subject to renegotiation, for which the binding liquidity commitment is shorter than the term to maturity of the loan, are in the scenario considered as non-redeemable.

The survival horizon is supplemented by additional stress scenarios for short-term liquidity, and KommuneKredit has a liquidity resource contingency plan which can be activated in case of pressure on liquidity.

FINANCIAL RISK MANAGEMENT

NOTE 1.11.1 DISTRIBUTION OF MATURITY

The distribution of maturity is shown in nominal value according to term to maturity or the liquidity binding period where this is shorter, but excl. interest rates. Loan commitments with known disbursement dates are recognised on the basis of the current date, while loan commitments for which dates and amounts are unknown are recognised on the basis of the term to maturity for the credit lines in question.

DKKm	0-3 months	3-12 months	1-5 years	Over 5 years	Total
2019					
Financial assets					
Due from credit institutions	5	0	0	0	5
Portfolio of securities	9,332	14,704	18,605	0	42,641
Lending	46,186	21,681	33,894	63,599	165,360
Leasing	200	1,214	3,639	2,930	7,983
Total recognised financial assets	**55,723**	**37,599**	**56,138**	**66,529**	**215,989**
Funding commitments received	0	0	0	0	0
Total financial assets	**55,723**	**37,599**	**56,138**	**66,529**	**215,989**
Financial liabilities					
Due to credit institutions	94	100	50	0	244
Debt securities issued	8,182	20,515	100,212	81,210	210,118
Derivatives	141	100	-745	-790	-1,294
Total recognised financial liabilities	**8,417**	**20,715**	**99,517**	**80,420**	**209,068**
Loan commitments given	1,995	3,224	2,041	0	7,260
Total financial liabilities	**10,412**	**23,938**	**101,558**	**80,420**	**216,328**

DKKm	0-3 months	3-12 months	1-5 years	Over 5 years	Total
2018					
Financial assets					
Due from credit institutions	2	0	0	0	2
Portfolio of securities	2,012	5,440	35,088	0	42,540
Lending	62,769	26,808	34,322	39,876	163,775
Leasing	119	906	3,516	2,603	7,144
Total recognised financial assets	**64,902**	**33,154**	**72,926**	**42,479**	**213,461**
Funding commitments received	0	0	0	0	0
Total financial assets	**64,902**	**33,154**	**72,926**	**42,479**	**213,461**
Financial liabilities					
Due to credit institutions	436	113	163	0	712
Debt securities issued	9,211	10,390	111,339	73,385	204,325
Derivatives	520	-440	343	-816	-393
Total recognised financial liabilities	**10,167**	**10,063**	**111,845**	**72,569**	**204,644**
Loan commitments given	1,044	2,753	5,826	0	9,623
Total financial liabilities	**11,211**	**12,816**	**117,671**	**72,569**	**214,267**

FINANCIAL RISK MANAGEMENT

NOTE 1.11.2 LIQUIDITY RESOURCES

The supervisory authority allows KommuneKredit to build up liquidity resources, based on pre-funding of up to 25% of total lending at the end of the preceding quarter. The upper limit amounted to DKK 47.1 billion at the end of 2019, and KommuneKredit had liquidity resources of DKK 35.9 billion. The utilisation of the limit fluctuated throughout 2019, and the highest level of liquidity resources at the end of a month was 19%.

Liquidity resources are calculated as due to credit institutions, debt securities issued and derivatives less total lending and lease receivables recognised at carrying amount.

DKKm	2019	2018
Liquidity resources		
Due to credit institutions, debt securities issued and derivatives		
Due to credit institutions	244	716
Debt securities issued	218,932	208,218
Derivatives, liabilities	8,327	8,800
Derivatives, assets	-6,610	-6,056
Total due to credit institutions, debt securities issued and derivatives	**220,893**	**211,678**
Lending and leasing		
Lending	176,983	170,312
Leasing	7,982	7,142
Total lending and leasing	**184,965**	**177,454**
Liquidity resources	**35,928**	**34,224**
Liquidity resources cannot exceed 25% of total lending at the end of the preceding quarter.		
Liquidity resources	35,928	34,224
Total lending at 30 September 2019	188,371	176,046
Liquidity resources, pct.	**19**	**19**

ADMINISTRATIVE EXPENSES

NOTE 2.1 ADMINISTRATIVE EXPENSES

Administrative expenses comprise staff costs and other administrative expenses, adjustment of pension obligations and amortisation/depreciation and impairment of intangible assets and property, plant and equipment. Actuarial adjustments and changes are recognised in the line item "actuarial gains and losses" in comprehensive income and not in administrative expenses.

Intangible assets and property, plant and equipment are measured at cost less accumulated amortisation/depreciation and impairment charges.

Cost comprises the purchase price and any costs directly attributable to the acquisition until the date when the asset is available for use. Where individual components of an intangible asset or an item of property, plant and equipment have different useful lives, they are accounted for as separate items and amortised/depreciated separately.

Development costs regarding software comprise consultancy fees and other expenses attributable to KommuneKredit's development activities. Development projects that meet the applicable accounting requirements are recognised as intangible assets. As for intangible assets and items of property, plant and equipment, amortisation/depreciation is provided on a straight-line basis over the expected useful lives of the assets or components, respectively, as follows:

- Intangible assets (software, etc.), 3 years
- Value of the property less residual value, 75 years
- Operating equipment, including IT equipment, 3-5 years
- Cars, 3-4 years

Land is not depreciated.

The carrying amounts are tested annually to determine whether there is any indication of impairment. When there is evidence that an asset may be impaired, the recoverable amount of the asset is determined. The recoverable amount is the higher of an asset's fair value less expected costs to sell and its value in use.

DKKm	**2019**	2018
Administrative expenses		
Salaries, remuneration, etc.	61	56
Pension contributions, etc.	9	8
Other staff costs	6	6
Consultancy fees	20	14
IT licenses	15	15
Charges	3	4
Property management	4	16
Amortisation/depreciation and impairment of intangible assets and property, plant and equipment	2	3
Other administrative expenses	6	5
Total administrative expenses	**126**	**127**
Average number of employees	76	70

Developments in costs were driven by an increase in salaries because of a higher headcount, and an increase in consultants for IT development, while the lower property management expenses were due to completion of the refurbishment of KommuneKredit's property at Kultorvet last year.

DKK'000	**2019**	2018
Fees to auditors elected as per the articles of association:		
Statutory audit of financial statements	439	414
Other assurance engagements	30	29
Other services	158	186
Total audit fees	**627**	**629**

Fees for other services comprise various statements and comfort letter for the annual update of the funding programme, etc.

ADMINISTRATIVE EXPENSES

2.2 REMUNERATION OF THE BOARD OF DIRECTORS AND MANAGEMENT

Fees to members of the Board of Directors consist of a fixed amount plus a fixed fee for their membership of the Audit Committee. The Audit Committee tasks are undertaken by the combined members of the Board of Directors.

DKK'000	2019	2018
Remuneration of Management		
Remuneration of the Board of Directors		
Lars Krarup, Chairman (Vice-chairman until 1 June 2018)	226	181
Thomas Lykke Pedersen (from 1 June 2018)	124	70
Sophie Hæstorp Andersen (until 1 June 2018)	0	32
Anker Boye (until 1 June 2018)	0	32
Martin Geertsen (from 1 June 2018)	75	42
Kaj V. Holm	75	74
Mikael Klitgaard	75	74
Erik Lauritzen (from 1 June 2018)	75	42
Laila Lindén (from 1 June 2018)	75	42
Erik Nielsen, former Chairman	77	139
Anne V. Porse (until 1 June 2018)	0	32
Hans Toft	75	74
Henrik Zimino (until 1 June 2018)	0	32
Total remuneration of the Board of Directors	**877**	**866**

DKK'000	Contractual remuneration	Pension	
Remuneration of the Management Board			
2019			
Jens Lundager, CEO	2,489	266	2,755
Henrik Andersen, Managing Director	1,919	203	2,122
Total			**4,877**
2018			
Jens Lundager, CEO	2,368	253	2,621
Henrik Andersen, Managing Director	1,829	199	2,028
Total			**4,649**

The Management Board is not covered by KommuneKredit's bonus plan.

ADMINISTRATIVE EXPENSES

NOTE 2.3 PENSION OBLIGATIONS

KommuneKredit has entered into pension plans with the majority of its employees. Liabilities relating to defined contribution plans are recognised in the income statement in the period in which they are earned, and payments due are recognised in the statement of financial position under other liabilities.

KommuneKredit has entered into defined benefit plans with a few former employees. For defined benefit plans, annual actuarial calculations are made of the net present value of future benefits to be paid under the plan. The net present value is calculated based on assumptions of the future developments of salary, interest, inflation and mortality rates, among other things. The net present value is only calculated for those benefits earned by the employees through their employment with KommuneKredit to date.

The actuarially calculated net present value is recognised in the statement of financial position as pension obligations. The calculations are based on the Danish Financial Supervisory Authority's benchmark for mortality rates and longevity improvements Adjustments to the calculated net present value attributable to changes in actuarial assumptions are recognised in other comprehensive income. The yield curve is that which the Danish FSA instructs institutions to use in connection with measurement of insurance obligations and which is used in the budget agreement for municipal civil servants.

In 2019, KommuneKredit opted to pay the pension obligation to Sampension, and the obligation is therefore not recognised in the statement of financial position. However, KommuneKredit still has the financial obligation for paying future benefits to former employees.

DKKm	**2019**	2018
Pension obligations		
Balance at 1 January	**80**	61
Adjustment	**0**	4
Additions	**7**	22
Disposals	**-3**	-7
Actuarial costs	**-3**	0
Adjustment of bonus provision	**-6**	0
Total pension obligations	**75**	**80**
Transferred to pension company	**-75**	0
Pension obligation on own statement of financial position	**0**	**80**
Hereof remuneration of the Management Board	**0**	**0**

TAX

NOTE 3.1 TAX ON PROFIT FOR THE YEAR

KommuneKredit computes tax on financial instruments based on the mark-to-market principle. The current corporate income tax rate is 22%.

Deferred tax is measured on all temporary differences between the carrying amount and the tax base of assets and liabilities. On this basis, the average tax rate is calculated at 22%.

Tax on profit for the year comprises current tax for the year, changes in deferred tax for the year, estimated tax on other comprehensive income and prior-year adjustments.

DKKm	2019	2018
Current tax	94	87
Deferred tax charge for the year	54	32
Prior-year adjustments	0	0
Total tax on profit for the year	**148**	**119**
Tax on profit for the year is explained as follows:		
Estimated tax on the pre-tax profit for the year	131	119
Non-deductible expenses	17	0
Prior-year adjustments to current tax	3	0
Adjustment of deferred tax relating to prior years	-3	0
Total tax for the year	**148**	**119**
Effective tax rate	25	22
Tax on other comprehensive income		
Tax on actuarial adjustment	0	-5
Tax on other comprehensive income, total	**0**	**-5**

NOTE 3.2 CURRENT TAX ASSETS

Current tax assets and tax liabilities are recognised in the statement of financial position as the sum of current tax, prior-year tax receivables or payables and tax paid for the year.

The tax asset concerns a pending case in Switzerland regarding withholding tax on matured bond investments.

DKKm	2019	2018
Balance at 1 January	33	32
Current tax	0	0
Value adjustment for the year	2	1
Income taxes paid for the year	0	0
Total current tax assets	**35**	**33**
Balance at 1 January	-63	-90
Prior-year adjustments	-3	0
Current tax	-94	-82
Income taxes paid for the year	129	109
Total current tax liabilities	**-31**	**-63**

TAX

NOTE 3.3 DEFERRED TAX LIABILITIES

Deferred tax assets and tax liabilities are measured on all temporary differences between the carrying amount and the tax value of assets and liabilities. Deferred tax assets and tax liabilities are measured on the basis of the tax rules which will, given the legislation in force at the balance sheet date, apply once the deferred tax is expected to be triggered as current tax. Deferred tax adjustments resulting from changes in tax rates are recognised in the statement of comprehensive income.

DKKm	2019	2018
Balance at 1 January	425	393
Prior-year adjustments	-3	0
Deferred tax charge for the year	54	32
Total deferred tax liabilities	**476**	**425**
Deferred tax liabilities break down as follows:		
Property, plant and equipment and intangible assets	5	8
Assets held under leases	488	435
Pension obligations	-17	-18
Total deferred tax liabilities	**476**	**425**

OTHER NOTES

NOTE 4.1 CONTINGENT ASSETS AND LIABILITIES

In 2014, the Danish Customs and Tax Administration selected KommuneKredit for an audit, ordering KommuneKredit to pay additional payroll tax. KommuneKredit has appealed this decision to the Danish National Tax Tribunal where the case is pending. In KommuneKredit's opinion, KommuneKredit will most likely win the case, and no expense or provision has consequently been recognised in the financial statements.

KommuneKredit has entered into dialogue with Udbetaling Danmark regarding the administration of subsidized loans and the distribution of the payments on these loans. This may result in KommuneKredit having to pay a compensation, the size of which is uncertain, for which reason KommuneKredit has not recognised the expense or provision in the financial statements.

NOTE 4.2 RELATED PARTIES

KommuneKredit has no related parties exercising control over KommuneKredit. KommuneKredit's related parties exercising significant influence comprise the members of KommuneKredit's Board of Directors and Management Board and their close family members.

BOARD OF DIRECTORS AND MANAGEMENT BOARD

Management's remuneration is disclosed in note 2.2. Fiduciary positions are mentioned in the "Corporate governance" section. No other transactions were carried out with members of the Board of Directors and Management Board in the year.

NOTE 4.3. EVENTS AFTER THE BALANCE SHEET DATE

No events have occurred after the balance sheet date that have a significant impact on KommuneKredit's results of operations.

NOTE 5

IFRS 9 IMPAIRMENT

KommuneKredit uses the fair value option for a significant part of its statement of financial position, as a result of which IFRS 9 only affects the measurement of leasing.

KommuneKredit grants loans and leasing exclusively to municipalities, regions and municipal companies with a full municipal guarantee. Danish municipalities and regions are subject to strict supervision by the Ministry for Social Affairs and the Interior.

It has been decided by court order that Danish municipalities cannot file for restructuring proceedings. The Ministry for Social Affairs and the Interior has laid down administrative rules (executive orders) to ensure that municipalities and regions maintain an adequate level of liquidity. Compliance with these rules is controlled and enforced by the ministry. Pursuant to the so-called "overdraft rule", liquidity in a municipality, calculated as a 12-month average, must as a minimum be positive.

This means that all Danish municipalities and regions are highly creditworthy and subject to a low Probability of Default (PD). Therefore, they are all placed in the category with the lowest PD level. The strong creditworthiness is reflected in the applied PD value in which the Credit Default Swap (CDS) price on the Danish State is used as a proxy to determine the current value.

The CDS price on the Danish State is determined on the basis of observable market data, and the calculation of value impairment is made using the same LGD value as for determining the CDS prices.

As a result of the use of IFRS 9, the measurement of leasing includes an expected credit loss. This means that, already when the lease agreement is established, the undertaking must recognise an impairment charge at an amount equal to the expected credit losses resulting from default events within 12 months. The impairment is recognised in three stages depending on credit risk developments:

STAGE 1:
If the credit risk has not increased significantly, the impairment equals the expected credit losses resulting from default events that are possible within the next 12 months. The impairment charge is recognised at the time when the lease agreement is established and is subsequently adjusted to reflect non-significant changes to the credit risk.

STAGE 2:
If the credit risk has increased significantly, the agreement is transferred to stage 2 and an impairment equal to the lifetime expected credit losses is recognised. A shift to stage 2 would take place in case of an increase in PD on the expected term to maturity of the financial asset of 100% and an increase in 12-month PD of 0.5 of a percentage point.

STAGE 3:
In the case of default or other credit impairment, the agreement is transferred to stage 3. Impairment is recognised using the same principles as in stage 2, but with the difference that interest income attributable to the write-down portion of the agreement is recognised on the basis of the write-down value.

When calculating the expected loss, the term to maturity of the agreement is capped at the contractual term. Model-calculated stage 1 and stage 2 impairment charges are based on transformations of PD - and LGD values at short term (12 months) or long term (term to maturity of agreement).

Throughout the history of KommuneKredit, there have been no losses on loans or leases to municipalities and regions, and therefore all leasing is classified as stage 1. There were no shifts between the stages during the reporting period.

IFRS 9 IMPAIRMENT – CONTINUED

The impairments at 31/12/2019 are shown in the table below. All lease agreements were in stage 1 at year-end.

Impairment of assets at cost

DKKm	PD level	Cost	Impairment	Carrying amount
Stage 1 (12-month expected loss)				
1 Jan. 2019	0.0% - 0.5%	7,144	2	7,142
Movement		840	0	840
31 Dec. 2019	0.0% - 0.5%	7,984	2	7,982

PD (Probability of Default) expresses the probability of default. At stage 1, the PD expresses the probability of the customer defaulting on its obligations towards KommuneKredit within the next 12 months.

LGD (Loss Given Default) expresses the proportion expected to be lost given default by the customer.

The change from 1 January to 31 December 2019 was exclusively due to a higher business volume.

NOTE 6

KEY FIGURES

Million	2019	2019	2018	2017	2016	2015
	EUR	*DKK*	*DKK*	*DKK*	*DKK*	*DKK*
KEY FIGURES						
Net interest income	66	496	441	637	656	675
Other operating income	2	13	11	11	10	9
Other operating expenses	-2	-13	-12	-14	-10	-10
Administrative expenses	-17	-126	-127	-123	-106	-96
Profit before value adjustments	50	369	314	511	550	578
Value adjustment of financial instruments	30	227	227	117	89	-451
Tax on profit for the year	-20	-148	-119	-138	-141	-23
Comprehensive income for the year	59	441	405	489	497	103
Lending and leasing	24,785	184,965	177,454	173,580	168,589	157,693
Portfolio of securities	6,027	44,982	42,944	42,361	34,049	33,983
Assets	31,749	236,935	226,609	222,564	223,938	213,199
Debt securities issued	29,336	218,932	208,218	202,145	202,642	193,382
Equity	1,096	8,179	7,736	7,333	6,844	6,347
ACTIVITIES DURING THE YEAR						
Lending and leasing, net additions in nominal value (net lending)	325	2,427	3,554	5,022	8,998	7,273
Lending and leasing, gross additions in nominal value	4,924	36,745	38,261	29,835	31,113	30,517
Debt securities issued, gross additions in nominal value	6,660	49,699	60,055	71,379	85,963	102,462

Million	2019	2019	2018	2017	2016	2015
	EUR	*DKK*	*DKK*	*DKK*	*DKK*	*DKK*
CAPITAL STRUCTURE						
Total risk exposure amount (REA)*	1,596	11,911	13,843	17,544	7,393	7,766
Common Equity Tier 1 (CET1) capital	1,096	8,179	7,736	7,333	6,844	6,347
Capital base	1,072	7,997	7,520	7,121	6,324	6,195
Capital ratio*	67	67	54	41	86	80
Equity ratio, pct.	3.5	3.5	3.4	3.3	3.1	3.0
SELECTED FINANCIAL RATIOS						
Losses on lending and leasing	0	0	0	0	0	0
Expenses/assets, pct.	0.05%	0.05%	0.06%	0.06%	0.05%	0.05%
Net interest income/assets, pct.	0.21%	0.21%	0.19%	0.28%	0.29%	0.32%
Liquidity resources, pct.	19%	19%	19%	20%	16%	18%
Number of full-time employees	76	76	70	70	66	62

Key figures and financial ratios have been calculated in accordance with "Recommendations & Financial Ratios" issued by CFA Society Denmark.
Exchange rate at 31 December 2019: EUR 100 = DKK 746.2871. The format has been changed compared with last year.

* The figures are not directly comparable over time because the calculation method has been changed.

STATEMENTS AND REPORTS

STATEMENT BY THE BOARD OF DIRECTORS AND MANAGEMENT BOARD

The Board of Directors and the Management Board have today considered and adopted the annual report of KommuneKredit for the financial year 1 January – 31 December 2019.

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

It is our opinion that the financial statements give a true and fair view of the financial position of KommuneKredit at 31 December 2019 and of the comprehensive income of KommuneKredit's operations and cash flows for the financial year 1 January – 31 December 2019.

Further, in our opinion, the Management's review gives a true and fair view of the development in KommuneKredit's operations and financial matters, principal risks and uncertainties, the comprehensive income for the period and KommuneKredit's financial position as such.

Copenhagen, 19 March 2020

MANAGEMENT BOARD

Jens Lundager
Chief Executive Officer
Managing Director

Henrik Andersen
Managing Director

/Morten Søtofte
Director, CFO

BOARD OF DIRECTORS

Lars Krarup
Chairman

Thomas Lykke Pedersen
Vice Chairman

Martin Geertsen

Kaj V. Holm

Mikael Klitgaard

Erik Lauritzen

Leila Lindén

Erik Nielsen

Hans Toft

INDEPENDENT AUDITOR'S REPORT

TO THE BOARD OF DIRECTORS OF KOMMUNEKREDIT

OPINION

We have audited the financial statements of KommuneKredit for the financial year 1 January - 31 December 2019, which comprise the statement of comprehensive income, financial position, statement of changes in equity, cash flow statement and notes, including the accounting policies. The financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the EU and additional Danish disclosure requirements for issuers of listed bonds.

In our opinion, the financial statements give a true and fair view of the Association's financial position at 31 December 2019 and of the results of its operations and cash flows for the financial year 1 January – 31 December 2019 in accordance with International Financial Reporting Standards as adopted by the EU and additional Danish disclosure requirements for issuers of listed bonds.

Our opinion is consistent with our audit book comments issued to the Audit Committee and the Board of Directors.

BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (ISAs) and additional requirements applicable in Denmark. Our responsibilities under those standards and requirements are further described in the "Auditor's responsibilities for the audit of the financial statements" section of this auditor's report. We are independent of the KommuneKredit in accordance with the IESBA Code of Ethics for Professional Accountants and additional requirements applicable in Denmark, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

To the best of our knowledge and belief, we have not provided any prohibited non-audit services as referred to in Article 5(1) of Regulation (EU) No 537/2014.

We were appointed auditors of KommuneKredit for the first time on 26 August 2016 for the financial year 2017. We have until now therefore been appointed by decision of the Board of Directors for a total contiguous engagement period of three years up to and including the financial year 2019.

STATEMENT ON THE MANAGEMENT'S REVIEW

Management is responsible for the Management's review.

Our opinion on the financial statements does not cover the Management's review, and we do not express any form of assurance conclusion thereon.

KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements for the financial year 2019. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

VALUATION OF FINANCIAL ASSETS AND LIABILITIES AT FAIR VALUE

The financial assets of KommuneKredit, including lending, portfolios of securities and positive derivatives, are measured at fair value, corresponding to 97% of total assets at 31 December 2019 (2018: 97%). The financial liabilities, including issued bonds and negative derivatives, are measured at fair value, corresponding to 96% of total liabilities at 31 December 2019 (2018: 96%).

As a result of materiality and complexity in connection with the valuation of financial assets and liabilities at fair values, this is a key audit matter in the audit. The principles governing the valuation are described in the accounting policies, and Management has further described the determination of fair values and the management of markets risks in the fair value adjustments etc. and financial risk management notes to the financial statements.

The fair values estimate is based on various assumptions and judgements, including both observable and non-observable data, which increases the degree of uncertainty. The areas which have therefore required increased attention in connection with the audit are recording of master data for contracts, the model and method application and the parameters:

- Currency margin
- Funding curves
- Credit spread
- Lending prices

HOW THE MATTER WAS ADDRESSED IN OUR AUDIT

Our audit included review of relevant procedures, testing of key controls and analysis of the fair value changes.

Our audit procedures have also specifically included:

- Testing of correct and complete recording of master data for concluded contracts
- Assessment, testing and validation of the applied model and method for fair value calculation
- Assessment and testing of relevance and accuracy for the key parameters applied in connection with the valuation.

Finally, the audit included testing of disclosure requirement compliance for the financial assets, liabilities and derivatives.

In connection with our audit of the financial statements, our responsibility is to read the Management's review and, in doing so, consider whether the Management's review is materially consistent with the financial statements or our knowledge obtained during the audit, or otherwise appears to be materially misstated.

Moreover, our responsibility is to consider whether the Managements' review contains the required information in accordance with Danish disclosure requirements for issuers of listed bonds.

Based on our procedures, we are of the opinion that the Management's review is in accordance with the financial statements and prepared in accordance with Danish disclosure requirements for issuers of listed bonds. We did not identify any misstatement of the Management's review.

MANAGEMENT'S RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as Management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, Management is responsible for assessing the Association's ability to continue as a going concern, for disclosing, as applicable, matters related to going concern, and for using the going concern basis of accounting in the preparation of the financial statements unless Management either intends to liquidate the Association or to cease operations, or has no realistic alternative but to do so.

AUDITOR'S RESPONSIBILITIES FOR THE AUDIT OF THE FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs and additional requirements applicable in Denmark will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs and additional requirements applicable in Denmark, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by Management.

- Conclude on the appropriateness of Management's use of the going concern basis of accounting in the preparation of the financial statements, and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Association's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit

evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Association to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures in the notes, and whether the financial statements represent the underlying transactions and events in a manner that gives a true and fair view.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Copenhagen, 19 March 2020

DELOITTE
Statsautoriseret Revisionspartnerselskab
Business Registration No 33 96 35 56

Anders Oldau Gjelstrup
State-Authorised
Public Accountant
MNE no mne10777

Bjørn Würtz Rosendal
State-Authorised
Public Accountant
MNE no mne40039

REPORT BY THE AUDITOR APPOINTED BY THE MINISTRY

TO THE BOARD OF DIRECTORS OF KOMMUNEKREDIT

As the auditor appointed by the Ministry, I have reviewed the financial statements of KommuneKredit for the financial year 1 January – 31 December 2019, prepared by Management. In addition, I have read the Management's review.

During my review, I did not identify any non-compliance with the Danish act governing KommuneKredit or KommuneKredit's articles of association. The audit procedures performed by Deloitte did not give rise to any comments on my part.

Copenhagen, 19 March 2020

Thorkil Juul

ADDITIONAL INFORMATION

DEFINITIONS AND FORMULAS

BENCHMARK: Public issues under a standard loan programme. Maturities often vary between 3 and 10 years depending on currency.

CRR/CRD IV: Capital Requirements Regulation and Capital Requirements Directive IV are the European implementation of the international Basel III rules on, among other things, financial institutions' capital and liquidity resources.

ECP: European Commercial Paper. Issues under a standard loan programme with a short term to maturity.

EQUITY RATIO = $\frac{\text{Equity}}{\text{Total assets}}$

COMMON EQUITY TIER 1 (CET1) CAPITAL: Equity less various deductions, which in KommuneKredit's case is zero.

FUNDING SPREAD: KommuneKredit's funding spread is its funding costs relative to the variable market rate in DKK. In other words, the funding spread is the price of KommuneKredit's funding in DKK.

HAIRCUT: Deductions in the quoted price of bonds, the size depending on the liquidity properties of the bond.

ISDA MASTER AGREEMENT: Bilateral framework agreement and master netting agreement for trading in OTC derivatives between financial counterparties.

KANGAROO: Issues in AUD primarily for Australian and Japanese investors under a standardised loan programme.

CAPITAL BASE: Common equity tier 1 (CET1) capital less various deductions (e.g. prudent valuation, current losses, intangible assets).

CAPITAL RATIO = $\frac{\text{Capital base}}{\text{Total risk exposure amount (REA)}}$

The capital ratio is calculated in accordance with the solvency requirements for financial institutions.

TOTAL LIQUIDITY RESOURCES: The total liquidity resources are composed of equity and liquidity resources.

LIQUIDITY COVERAGE RATIO (LCR): Indicates the ratio between the portfolio of liquid assets and the net runoff from cash flows over a 30-day horizon in a stress scenario. The financial ratio was introduced in connection with Basel III and subsequently CRR/CRD IV.

NASDAQ COPENHAGEN: Bonds listed on the stock exchange in Copenhagen. These bonds are often denominated in DKK.

NET STABLE FUNDING RATIO (NSFR): The ratio between defined stable funding and the estimated need for stable funding. The financial ratio was introduced in connection with Basel III and subsequently CRR/CRD IV.

NET LENDING: Net additions of loans and leasing in nominal value.

PRIVATE PLACEMENT: An issue directed at a single investor. Issues may be denominated in different currencies and maturities.

RISK WEIGHT: Weight attributed to the individual exposures when calculating the capital ratio. Given by the solvency rules for credit institutions.

TOTAL RISK EXPOSURE AMOUNT (REA): The value of total assets when calculating the capital ratio, allowing for the risk weight of the exposure. Total risk exposure amount is calculated in accordance with the solvency requirements for financial institutions.

COLLATERAL AGREEMENT (CREDIT SUPPORT ANNEX): Agreement between financial counterparties regarding exchange of collateral in case of fluctuations in the market value of derivatives.

LIQUIDITY RESOURCES: Amounts due to credit institutions, debt securities issued and derivatives minus lending.

URIDASHI: Issue for the Japanese retail market under a standard loan programme.

DISCLAIMER The annual report is prepared in Danish and translated into English. In case of discrepancies the Danish version shall prevail.

PHOTOS Hanne Schultz, Municipality of Frederiksberg and TRUX Studio.

THANKS to Omø Digelag and the Municipality of Frederiksberg for participating in our cases

DESIGN AND PRODUCTION Noted

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Managing Director

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KOMMUNE
KREDIT

STEADY
& STABLE