



Topdanmark's

Capital model

Shareholders' equity alternatives

Topdanmark considers shareholders' equity to be just one of several instruments which can be used to protect against risk. The objective of shareholders' equity exceeding the statutory minimum is to protect the business against situations when major disasters could threaten future operations. However, such protection is often available by other means, for example reinsurance or financial instruments.

Overall, it is Topdanmark's opinion that shareholders' equity or substitutes thereof like subordinated loan capital, guarantees or other general hedging instruments are appropriate for protecting against fluctuations in the result on ordinary operations, while the cost of shareholders' equity is prohibitive when used to cover the risk arising from rare one-off events. Therefore, this type of risk should be transferred to other risk bearers by use of reinsurance or financial instruments.

Normally, Topdanmark's operations would generate a fairly stable cash flow. Therefore, Topdanmark usually operates with relatively limited cover in the form of shareholders' equity. To supplement this, Topdanmark has raised subordinated loan capital and bought significant reinsurance cover of disaster risks, i.e. both isolated events and combinations of isolated events that would threaten Topdanmark's ability to continue operating at its chosen level of shareholders' equity. Additionally, Topdanmark has invested in financial instruments reducing the danger of sharp falls in equity markets and also in instruments protecting the life insurance Group against any adverse consequences of marked reductions in interest rates.

How large should shareholders' equity be in order to be considered sufficient?

In setting a reasonable level of capital cover, Topdanmark takes into account the factors that would have a material adverse impact on shareholders' equity. At the same time, it allows for the effect of protection in the form of reinsurance and financial instruments.

Furthermore, other factors including current assumptions on the risk on insurance portfolios, asset portfolios and the financial markets are taken into account. Finally, Topdanmark's opinion of what is a reasonable level of capital cover is compared with the regulatory requirements. The goal of solvency capital is the highest value of what Topdanmark considers a reasonable level of capital cover and the regulatory requirement plus an appropriate buffer.

Given the current assessment of the future market conditions, Topdanmark estimates that the shareholders' equity, reduced by the value of intangible assets, must represent at least DKK 3,400 in accordance with the holding company's accounting policies, i.e. without any allowance for deferred tax on security funds. Furthermore, hybrid capital of DKK 400m and Tier 2 capital of DKK 1,350m has been issued.

Earnings distribution potential

Normally, Topdanmark generates a return which significantly exceeds the capital required to allow for the growth in the business. If it is not possible to find value creating investment opportunities, such surplus returns will be paid out to the shareholders. The size of the pay-out is determined by the ratio of shareholders' equity to the business' current requirements of capital.

From 1998 to 2017, it was Topdanmark's policy that earnings distribution should take place via buy-back of own shares.

In the Interim Report for Q1 2017, it was stated that Topdanmark will switch to distribution of dividends.

Earnings distribution policy Objective

The objective of Topdanmark's earnings distribution policy is to distribute excess capital to its shareholders.

Principle

Topdanmark has a disciplined approach to capital, in order that capital that is not necessary to maintain operations will be distributed to the shareholders and to avoid accumulation of unnecessary excess capital.

Future earnings distribution policy

Topdanmark's Board of Directors has adopted an earnings distribution policy, according to which earnings distribution will take place via annual distribution of dividends. Distribution of dividends will take place immediately after the AGM.

The dividends will correspond to a pay-out ratio of at least 70%.

Earnings distribution for 2017

Distribution of dividends for 2017 will take place immediately after the AGM on 12 April 2018.

Potential for earnings distribution in 2017

Basically, the earnings distribution potential in 2017 is planned to reflect the growth in what is considered a reasonable level of capital cover and the expected pre-tax profit and goodwill amortisation, as illustrated below:

DKKm	Jan 2018	
Shareholders' equity year-end 2018	6,497	
Intangible assets	<u>(965)</u>	5,532
Allocated dividend for 2017		<u>(1,710)</u>
		3,822
Assumed post-tax profit 2018 (mean value)	1,000	
Change, intangible assets	(100)	
Change in shareholders' equity (issue and utilization of options)	<u>200</u>	<u>1,100</u>
Assumed shareholders' equity for solvency, end of 2018		4,922
Estimated required shareholders' equity cover for solvency 2018		<u>3,400</u>
Excess capital 2018		1,522
Subordinated loan capital:		
DKK 400m tier 1 loan capital, call in 2022 without expiry date		
DKK 500m tier 2 loan capital, call in 2020, expiry in 2025		
DKK 850m tier 2 loan capital, call in 2021, expiry in 2026		
Solvency requirement, 1 January 2018	3,116	
Own funds, 1 January 2018	6,370	

Power of the Board of Directors to issue shares and/or acquire own shares

Topdanmark's Board of Directors has authorisation granted in the Articles of Association to increase the Company's share capital, to raise convertible loans and/or issue warrants.

The issues may be with or without pre-emptive rights for the Company's shareholders. The total authorisation is restricted to 2,500,000 shares and expires on 17 April 2018.

