GARANTIA INSURANCE COMPANY LTD REPORT BY THE BOARD OF DIRECTORS AND FINANCIAL STATEMENTS 2016

GARANTIA

OMISTAMISEN TUKENA

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GARANTIA'S YEAR 2016 IN BRIEF

Garantia Insurance Company ltd

Garantia makes investments and deals happen and enables the accumulation of wealth. Our solutions help to secure financing and improve capital efficiency.

Garantia was established in 1993. It is a private non-life insurance company specialising in guaranty insurance. The company is domiciled in Helsinki and its business practices are supervised by the Finnish Financial Supervisory Authority. Garantia's product selection includes corporate guaranties, commercial bonds, investment guaranties, residual value guaranties and residential mortgage guaranties that are offered to consumers via partners. Based on agreements made with pension insurance companies Garantia is also responsible for public quotation of employees' pension insurance (TyEL) interest rates according to calculation bases approved by the Ministry of Social Affairs and Health.

Garantia is a wholly-owned subsidiary of Taaleri Plc and part of the Taaleri Group. Taaleri provides wealth management and financing services to institutional investors, companies and private individuals. The parent company Taaleri Plc's share is listed on NASDAQ OMX Helsinki. The operations of Taaleri are supervised by the Finnish Financial Supervisory Authority.

Further information: www.garantia.fi, www.taaleri.com

Garantia's premiums written increased considerably and S&P changed Garantia's A- credit rating outlook to stable

- Premiums written increased 22% on the comparison period and came to EUR 12.2 million (10.0). The total insurance exposure increased 13.3%.
- The balance on the technical account was good. The claims ratio was 12% (15) and the combined ratio was 65% (64).
- Earnings before tax were EUR 7.7 million (8.5) due to lower net return on investments recognised in profit and loss than in the comparison period.
- The return on investments at fair value was 5.8% (4.6).
- Solvency remained strong and the solvency ratio was 435% (506)
- On 1 December 2016, S&P confirmed Garantia's financial strength rating A- and changed the rating outlook to stable.

Profit and loss account and key ratios

EUR t	2016	2015	Change
Premiums written	**12 218**	**10 019**	**22 %**
Other items*	-2 751	-170	
Earned premiums	**9 467**	**9 849**	**-4 %**
Claims incurred	-1 174	-1 492	-21 %
Operating expenses	-4 966	-4 778	4 %
Balance on technical account before changes in	**3 327**	**3 579**	**-7 %**
Change to equalisation provision**	1 174	-3 517	
Balance on technical account	**4 501**	**62**	
Investment income and expenses, net	3 212	8 460	-62 %
Earnings before tax	**7 713**	**8 523**	**-9 %**
Combined ratio, %	64,9 %	63,7 %	1,2 pp
Claims ratio, %	12,4 %	15,1 %	-2,7 pp
Expense ratio, %	52,5 %	48,5 %	3,9 pp
Return on investments at fair value, %	5,8 %	4,6 %	1,2 pp
Solvency ratio (S2), %***	435,4 %	505,8 %	-70,4 pp
Total insurance exposure, EUR bn	1,32	1,16	13 %
Average number of personnel	22	25	-3

The figures used for result comparison are those for the corresponding periods in 2015. The comparison data used for the balance sheet and cross-section items are the data for the end of 2015 unless otherwise indicated.

* Reinsurers' share of premiums written, change to provision for unearned premiums and reinsurers' share of change to provision for unearned premiums.

** The Solvency II regulations were not in force during the 2015 financial year and they do not fall within the sphere of statutory auditing under the Insurance Companies Act that entered into force on 1 January 2016. The Solvency II capital adequacy figures have not been audited.

REPORT BY THE BOARD OF DIRECTORS

Operating environment

The Finnish economy returned to growth during 2016, driven mainly by private consumption and construction investments. Fixed investments started to grow, but the level remained insignificant. The situation also improved in industrial production and the previous years' decrease in exports came to an end. Unemployment declined and consumers' confidence in the future strengthened.

Companies' investments and the resulting demand for investment finance remained at a low level. The excellent availability of financing for Finnish companies was reflected in demand for the TyEL premium loans granted by employment pension companies and over the period January–September the volume of pension companies' TyEL premium loans declined by EUR 0.2 billion to EUR 1.1 billion on 30 September 2016. The rapid revival of construction increased demand for commercial bonds. The recovery on the housing market boosted demand for mortgages and residential mortgage guaranties. During 2016, households took out new mortgages worth almost EUR 18 billion and banks' volume of housing loans denominated in euros grew 2.4% to EUR 94.1 billion.

There were many exceptional events during the 2016 investment year. At the beginning of the year there were concerns over the durability of economic growth, during the summer Britain voted to leave the EU and in November Donald Trump was the unexpected winner of the USA's presidential elections. The operating environment in 2017 will be marked by an increase in political risk and the resulting uncertainty in both the USA and Europe. Elections will be held in two major EU countries: France in the spring and Germany in the autumn. The rise of populism may lead to unexpected political decisions.

Insurance operations

Gross premiums written (excluding the reinsurers' share) increased 21.9% to EUR 12.2 (10.0) million. Ceded reinsurance accounted for EUR 0.8 (1.0) million of the premiums written total, which means that net premiums written (with the reinsurers' share deducted) increased by 26.8% to EUR 11.4 (9.0) million. Strong growth in the construction sector and the recovery on the housing market increased guaranty fees especially in commercial bonds and residential mortgage guaranties. There was a clear increase in new sales in corporate loan guaranties, but despite low interest rates, demand for corporate loan guaranties remained at a low level. Earned premiums declined, however, to EUR 9.5 (9.8) million on account of the change in the provision for unearned premiums. The change in the provision for unearned premiums was a result of strong growth in premiums written.

The insurance exposure grew 13.3% and was EUR 1,320 (1,164) million at the end of the year. Residential mortgage guaranties accounted for 35% (33) of the total exposure, loan guaranties 31% (37), commercial bonds 27% (22) and other guaranties 7% (8).

Claims paid remained at an exceptionally low level. The claims ratio was 12.4% (15.1) and claims incurred in relation to the insurance exposure was 0.09% (0.13). In 2016 a total of EUR 1.2 (1.9) million in claims were paid and about 72% of these were for residential mortgage guaranties, 15% for loan guaranties and 13% for commercial bonds. The proportion of this sum recorded as claims of recourse was EUR 0.2 (0.0) million. A total of EUR 0.6 (0.7) million was recovered from claims paid during and prior to the financial year. EUR 0.2 (0.1) million of this concerned claims of recourse.

The company is not involved in any litigation, and no other claims have been made against the company. However, in 2011 a claim totalling EUR 5.0 million was made against Garantia, though the company considers this to be unfounded. There were no significant changes in this matter during 2016, and the processing of the case continues.

Operating expenses grew by 3.9% to EUR 5.0 (4.8) million. The operating expenses were increased by investments in personnel, in IT, in development of risk models and in the corporate image. The company's expense ratio was 52.5% (48.5) and the combined ratio was 64.9% (63.7).

The balance on the technical account before the change to the equalization provision was EUR 3.3 (3.6) million. The equalization provision declined to EUR 1.2 (increased by 3.5) million, so the balance on the technical account increased to EUR 4.5 (0.06) million. Regulations on the equalization provision changed as a result of the Insurance Companies Act that came into force on 1 January 2016, and the Financial Supervisory Authority confirmed Garantia's calculation bases for the equalization provision on 21 October 2016.

Garantia and Taaleri Private Equity Funds Ltd produced their first joint product, Tuulitehdas III, which offered investors in the fund the opportunity to subscribe the profit participation loan with a guaranty from Garantia. In loan guaranties, Garantia started cooperation with Nordic Investment Bank NIB to launch a loan facility for SMEs and mid-caps. In commercial bonds Garantia developed its eService by starting electronic delivery of guarantees to customers and their beneficiaries. Garantia also broadened its partner network in residential mortgage guaranties by launching cooperation with Aktia Bank.

Investment activities

Net return on investments recognised in profit and loss were EUR 3.2 (8.5) million. The valuation difference of investment assets grew from EUR 6.7 million to EUR 9.9 million during the financial year.

The return on investments at fair value (excl. the cash and bank balances, and unallocated income, expenses and operating expenses) was 5.8% (4.6). Net return on investments from capital employed at fair value was EUR 6.5 (5.2) million, or 5.4% (4.4).

The investment portfolio (incl. cash and bank balances) was EUR 127 (120) million at the end of the year.

Risks and Risk Management

The principal risks associated with Garantia’s business operations are credit risks arising from guaranty insurance operations and investment risks regarding assets covering technical provisions.

Garantia’s risk position remained stable in 2016. The growth of insurance exposures took place in diversified mortgage guaranties and in short term commercial guaranties covered by comprehensive reinsurance. As a result of the shortening of loan guaranties, the share of the insurance exposure classified in investment grade, i.e. with a rating of AAA–BBB-, excluding residential mortgage guaranties, residual value guaranties and assumed reinsurance, declined to 21% (30), however. The share of those with lower credit ratings of C+ or lower remained low and was 2.8% (2.5). The biggest sectors in the insurance exposure were construction at 37% (33) and manufacturing 26% (33). The proportion of construction guaranties that is reinsured is 52% (58).

As part of the Taaleri Group, Garantia is subject to the regulations on large exposures as defined in the EU Capital Requirements Regulation. At the end of the year Garantia’s largest individual exposure was 38.9% (51.3) of the Taaleri Group’s own funds and the exposures of a total of 1 (7) group of connected clients exceeded the 25% exposure limit prescribed by law. The Financial Supervisory Authority approved an updated action plan drawn up by Garantia to reduce the exposure of guaranties to the level required by law by 30 October 2017.

The risk level of investment activities was raised moderately when the share of finance sector fixed income investments was reduced and the share of corporate sector fixed income investments and US equities was increased to secure the return level. Fixed income investments made up 79% (82) and equity investments 18% (17) of the investment portfolio (incl. cash and bank balances). Fixed income investments mainly consist of investments in the bonds of Finnish and Nordic companies and credit institutions with strong creditworthiness. The share of investment grade fixed income investments (excluding fixed income funds) was 70% (78). The modified duration of the fixed income investments was 3.0 (2.5).

Solvency

Garantia’s solvency remained strong. Garantia’s own funds amounted to EUR 100.9 (96.1) million and clearly exceeded the Solvency Capital Requirement (SCR) of EUR 23.2 (19.0) million. The solvency ratio, or the ratio of basic own funds to the Solvency Capital Requirement, was 435% (506). The increase in the Solvency Capital Requirement resulted from a growth in the market risk related to investments.

Solvency, €	31.12.2016	31.12.2015
Own funds	100 929 368	96 108 376
Solvency capital requirement		
Market risk	20 608 282	14 662 457
Non-life underwriting risk	15 201 856	14 746 074
Counterparty default risk	360 788	355 020
Operational risk	310 892	331 150
Diversification effect and adjustment for loss-absorbing capacity	-13 299 849	-11 093 632
Total	23 181 969	19 001 069
Amount of own funds in excess of the Solvency capital requirement	77 747 399	77 107 307
Solvency ratio, %	435,4 %	505,8 %

Garantia's own funds are formed in full of unrestricted Tier 1 basic own funds. Garantia does not use the matching adjustment or the volatility adjustment in the technical provisions calculation. Garantia applies the standard formula for the Solvency Capital Requirement calculation. Garantia does not apply the transition arrangements of technical provisions or market risk calculations. The final amount of Garantia's solvency capital requirement is still subject to supervisory assessment. Garantia's management view is that Garantia's solvency will remain strong despite the possible increase to solvency capital requirement for insurance risk.

Guarantia's solvency and financial condition report in accordance with chapter 8 of the Insurance Companies Act is published on the company's website at www.garantia.fi in accordance with the timetable prescribed by regulation. The solvency and financial condition report is also available from the following address: Garantia Insurance Company Ltd, Kluuvikatu 3, 00100 Helsinki.

The Solvency II regulations were not in force during the 2015 financial year and they do not fall within the sphere of statutory auditing under the Insurance Companies Act that entered into force on 1 January 2016. The Solvency II capital adequacy figures have not been audited.

Credit Rating

On 1 December 2016, Standard & Poor's Credit Market Services Ltd (S&P) confirmed Garantia Insurance Company Ltd's financial strength rating A- and changed the rating outlook from negative to stable.

Personnel

During the financial year, Garantia employed an average of 22 (25) people. The average age of the personnel at the end of the year was 42.3 (43.8), and their average duration of employment at Garantia was 6.1 (6.6) years. Women made up 43.5% (52.4) of the personnel and men 56.5% (47.6).

Shares and shareholders

Taaleri Plc owns 100% of Garantia Insurance Company Ltd's share capital. On 31 December 2016, the number of Garantia shares was 60,000, which was the same as the previous year.

Taaleri Plc and its subsidiary and associated companies form a financial and insurance conglomerate primarily engaged in insurance activities as defined in the Act on the Supervision of Financial and Insurance Conglomerates. The conglomerate's parent company is Taaleri Plc. The Taaleri Group prepares consolidated financial statements complying with International Financial Reporting Standards (IFRS). These statements include reporting on Garantia as part of the Financing segment.

The Taaleri Group's consolidated financial statements are available on the company's website www.taaleri.com and from the following address: Taaleri Plc, Kluuvikatu 3, 00100 Helsinki.

Management

The annual general meeting held on 8 March 2016 elected Hannu Tonteri as Chairman of the Board of Directors and Juhani Elomaa (Vice Chairman), Timo Hukka, Jukka Ohls, Antti Suhonen and Tomi Yli-Kyyny as members of the Board. All were re-elected to their positions. The term of the members of the Board of Directors lasts until the end of the following annual general meeting.

The company's Board of Directors convened 19 times during the financial year. The Board of Directors had no separate committees during the financial period.

During the financial year, Vesa Aho M.Sc (Econ. & Bus. Adm.) was the company's Managing Director and Titta Elomaa M.Sc (Econ. & Bus. Adm.) was the Deputy Managing Director. The Management Team consisted of the Managing Director, the Deputy Managing Director, Tuukka Fabritius, Martti Purhonen (as of 8 August 2016), Timo Lehikoinen (until 7 August 2016) and Niina Pullinen.

The annual general meeting of 8 March 2016 appointed Ernst & Young Oy as the auditor and Authorised Public Accountant Ulla Nykky as the responsible auditor and KPMG Oy AB as the company's other auditor and Authorised Public Accountant Juha-Pekka Mylen as the responsible auditor.

Garantia procures its actuarial function and appointed actuary from an external service provider as an outsourced service. In 2016 the service was provided by Kaippio & Kaippio Oy with actuary SHV Janne Kaippio as the appointed actuary.

Garantia procures its internal audit from external service provider as an outsourced service. In 2016 the service was provided by PricewaterhouseCoopers Oy.

Board of Directors' proposal for the treatment of net profit for the financial year and the use of distributable funds

The net profit for the financial year was EUR 6,138,993.64. The company's distributable profits amount to EUR 19,530,597.88 and its total distributable funds EUR 19,555,812.88. The Board of Directors proposes that the profit be transferred to the retained earnings account and that a total of EUR 4,000,000.00 from retained earnings be distributed as dividends.

Outlook for 2017

In 2016 the Finnish economy returned to growth and the positive trend is expected to continue in 2017. However, growth is anticipated to remain slow and to continue to rely heavily on domestic demand. The recovery on the housing market and strong growth in construction will support growth. Fixed investment is expected to continue to grow slightly but to continue to remain lower than normal in relative terms.

Despite the slight growth in investments, companies' financing demand is still largely dependent on refinancing. Central bank measures are creating surplus liquidity on the markets and the availability of funding for Finnish companies will remain at a good level. This will narrow corporate loan margin and increases price competition, particularly in companies with high creditworthiness. As a result of the recovery in the housing market, the guaranty requirements related to housing loans are expected to remain at least at the level of the previous year. The growth in construction is anticipated to support demand for commercial bonds also in 2017.

Investment markets' performance in 2017 will be affected by political solutions in global economy. Interest rates reached historical lows last July when Germany's 10-year bond yield fell to -0.10% and the yield for USA's corresponding bond was +1.36%. The rise of interest rates that started in the autumn may lead to a more lasting change in the interest rate levels.

The recovery of the financial outlook in Finland, products produced together with Taaleri, an active client-oriented approach, new personnel who have been recruited and new partners all create a good foundation for the continuation of growth. Garantia will continue to develop new guaranty solutions for corporate financing and investment activities.

FINANCIAL STATEMENTS

Profit and loss account

euro	Note	2016	2015	change, %
Technical Account				
Earned premiums				
Premiums written	1, 2, 3	12 217 588,24	10 018 859,90	21,9 %
Reinsurers' share		-810 122,02	-1 024 927,60	-21,0 %
Change to provision for unearned premiums		-1 854 513,01	1 019 473,16	
Reinsurers' share		-85 922,23	-164 652,02	-47,8 %
		9 467 030,98	**9 848 753,44**	**-3,9 %**
Claims Incurred				
Claims paid		-1 038 301,53	-1 459 258,79	-28,8 %
Reinsurers' share		104 627,07	38 504,92	171,7 %
Change in provision for outstanding claims		-100 426,95	-274 124,45	-63,4 %
Reinsurers' share		-140 047,80	203 223,88	-168,9 %
		-1 174 149,21	**-1 491 654,44**	**-21,3 %**
Operating expenses	5, 6, 7	-4 966 231,44	-4 777 713,42	3,9 %
Balance on technical account before change to equalisation provision		**3 326 650,33**	**3 579 385,58**	**-7,1 %**
Change to equalisation provision		1 174 149,21	-3 516 924,28	
Balance on Technical Account		**4 500 799,54**	**62 461,30**	
Non-technical account				
Investment income	4	4 664 641,37	9 058 130,51	-48,5 %
Investment expenses	4	-1 452 479,58	-597 997,33	142,9 %
Direct taxes on ordinary operations		-1 573 967,69	-1 711 924,96	-8,1 %
Net profit for the financial year		6 138 993,64	6 810 669,52	-9,9 %

Balance sheet

Assets euro	Note	31.12.2016	31.12.2015
INTANGIBLE ASSETS			
Intangible rights	8	4 992,30	12 702,03
Other long-term expenditure	8	91 007,93	261 511,46
		96 000,23	**274 213,49**
INVESTMENTS	9		
Other investments			
Shares and participations		23 142 072,06	19 769 510,75
Other financial instruments		90 424 224,10	87 631 415,53
		113 566 296,16	**107 400 926,28**
Total		**113 566 296,16**	**107 400 926,28**
DEBTORS			
Arising out of direct insurance operations			
From policy holders		634 736,13	403 202,30
Arising out of reinsurance operations		136 197,34	35 876,69
Other		1 257 797,63	1 251 817,72
		2 028 731,10	**1 690 896,71**
OTHER ASSETS			
Tangible assets			
Equipment		76 554,25	102 072,35
Other tangible assets		49 250,40	49 250,40
		125 804,65	**151 322,75**
Cash and bank balances		2 410 436,25	4 024 287,27
Total		**2 536 240,90**	**4 175 610,02**
PREPAYMENTS AND ACCURED INCOME			
Accured interest and rental income		1 530 068,36	1 836 553,14
Other accured income		98 059,39	22 595,49
		1 628 127,75	**1 859 148,63**
TOTAL ASSETS		**119 855 396,14**	**115 400 795,13**

Liabilities euro	Note	31.12.2016	31.12.2015
SHAREHOLDERS' EQUITY AND RESERVES	10, 11		
Share capital		10 200 000,00	10 200 000,00
Reserve for invested unrestricted equity		25 515,00	25 515,00
Retained earnings		13 391 304,24	9 580 634,72
Profit / loss of the financial year		6 138 993,64	6 810 669,52
Total		**29 755 812,88**	**26 616 819,24**
TECHNICAL PROVISIONS			
Provision for unearned premiums		13 249 008,23	11 394 495,22
Reinsurers' share		-324 048,81	-409 971,04
		12 924 959,42	**10 984 524,18**
Claims outstanding	12	1 296 774,70	1 196 347,75
Reinsurers' share		-386 801,30	-526 849,10
		909 973,40	**669 498,65**
Equalisation provision		73 614 597,79	74 788 747,00
Total		**87 449 530,61**	**86 442 769,83**
CREDITORS			
Arising out of direct insurance operations		75 000,00	125 000,00
Arising out of reinsurance operations		377 004,79	355 445,24
Other		180 977,08	239 184,37
		632 981,87	**719 629,61**
ACCRUALS AND DEFERRED INCOME			
Other		2 017 070,78	1 621 576,45
		2 017 070,78	**1 621 576,45**
TOTAL LIABILITIES		**119 855 396,14**	**115 400 795,13**

Cash flow statement

euro	2016	2015
Cash flow from operations		
Profit / loss from ordinary operations	6 138 993,64	6 810 669,52
Adjustments		
Change in technical provisions	1 006 760,78	2 733 003,71
Write-downs and revaluations on investments	146 316,93	91 573,17
Planned depreciation	203 731,36	228 217,76
Other adjustments	348 290,86	-5 394 806,28
Cash flow from operations before financing items and taxes	**7 844 093,57**	**4 468 657,88**
Change in working capital		
Short-term non-interest-bearing trade receivables increase (-)/decrease (+)	-106 813,51	-166 624,80
Short-term non-interest-bearing liabilities increase (+)/decrease (-)	308 846,59	239 473,39
Cash flow from operations before financing items and taxes	**8 046 126,65**	**4 541 506,47**
Intrest paid and payments for other financing expences of operating activities	0,00	0,00
Direct taxes paid	-1 063 472,32	-864 048,18
Cash flow from operations	**6 982 654,33**	**3 677 458,29**
Cash flow from investments		
Placements in investments / capital gains on investments (excl. Financial assets)	-5 596 505,35	8 550 716,97
Investment and capital gains (net) related to intangible and tangible assets and other assets	0,00	176 645,57
Cash flow from investment operations	**-5 596 505,35**	**8 727 362,54**
Cash flow from financing		
Dividends paid / interest on guaranty capital and other distribution of profits	-3 000 000,00	-10 000 000,00
Cash flow from financing	**-3 000 000,00**	**-10 000 000,00**
Change in financial assets	**-1 613 851,02**	**2 404 820,83**
Cash and bank balances at the start of the financial year	4 024 287,27	1 619 466,44
Cash and bank balances at the end of the financial year	2 410 436,25	4 024 287,27
	-1 613 851,02	**2 404 820,83**

NOTES TO THE FINANCIAL STATEMENTS

Accounting principles for the financial statements

The financial statements have been prepared in accordance with the Accounting Act, the Finnish Limited Liability Companies Act and the Insurance Companies Act, and in compliance with the decisions, regulations and guidelines of the public authorities supervising insurance companies.

Insurance premiums

Insurance premiums for the premium contribution periods that began during the financial period as agreed in the insurance contracts have been recognised as premiums written. Those premium receivables for which it is likely that payment will not be received have been deducted from premiums written as credit losses.

Valuation of intangible assets and the accrual concept

Rights to use computer software have been capitalised under intellectual property rights, and modernisation expenses related to the development of the insurance system have been capitalised under other long-term expenditure. These have been recognised on the balance sheet at acquisition cost less planned depreciation.

Valuation of investments and receivables on the balance sheet

Shares and holdings have been valued at acquisition cost or at fair value, if this is lower. Any write-downs made have been revalued through profit or loss in so far as the fair value of the investment at the closing date exceeded the acquisition costs written down. Any revaluations are recognised up to the original acquisition cost.

In the case of short-term debt instruments, financial market instruments have been valued at the acquisition price, whereas treasury bonds and other bonds have been valued at the acquisition price, which is steadily adjusted towards the nominal price on a bond-specific basis over its maturity. If the fair value of a bond is lower than its acquisition cost less prior write-downs, a further write-down is recognised to adjust the acquisition cost through profit or loss. Other financial market instruments have been valued at acquisition cost or fair value, whichever is lower.

Undisputed claims of recourse due to a loss event have been recognised on the balance sheet at probable value in compliance with the principle of prudence and taking into account any counter-collateral remaining with the company.

Premium receivables and other receivables have been valued at nominal value or at lower probable value.

Account of methods for determining the fair value of investments

The fair value of listed shares is taken to be the final available purchase price during continuous trading at the closing date or, if this is not available, the last trading price.

The fair value of bonds is taken to be the last purchase price for the year or, if this is not available, the last trading price.

The fair value of other investments is taken to be the most probable assignment price.

Items denominated in foreign currencies

Business transactions denominated in foreign currencies have been entered at the transaction date rate. In the financial statements, the fair values of investments have been converted into euros at the closing date rate.

Account of how pensions have been provided for personnel

The pensions of personnel have been arranged by means of a pension insurance policy in accordance with the Finnish Employees' Pensions Act (TyEL) taken out with Elo Mutual Pension Insurance Company. Pension contributions have been entered as expenses on an accrual basis.

Principles for planned depreciation

Asset	Depreciation method
Intangible assets	
IT programs	Straight-line depreciation over 5 years
Other long-term expenditure	
Modernisation expences	Straight-line depreciation over 10 years
Equipment	Reducing balance depreciation 25 %
Other tangible assets	Reducing balance depreciation 25 %

The planned depreciation corresponds to depreciation in accordance with the Finnish Business Income Tax Act.

Direct taxes

Direct taxes have been recognised in the income statement on an accrual basis.

Other liabilities

Liabilities other than technical provisions have been recognised in the balance sheet at nominal value.

Technical provisions

Technical provisions include that part of the premiums written accrued during the financial year and during previous years for which the respective risk concerns the period following the financial year.

Provisions for outstanding claims include the amounts of claims to be paid by the company after the financial year that are caused by loss events taking place during the financial year or earlier. The provisions include an equalization amount, which is a buffer calculated for years with a large number of loss events.

The calculation bases for the equalization provision confirmed by the Financial Supervisory Authority on 21 October 2016 have been applied in the financial statements.

Notes to the profit and loss account

Note 1: Insurance premiums written

euro	2016	2015
Non-life insurance		
Direct insurance		
Domestic	12 215 790,23	9 974 871,07
Reinsurance	1 798,01	43 988,83
Insurance premiums written before the share of insurers	**12 217 588,24**	**10 018 859,90**

Note 2: Profit per insurance class

Columns:
1 = Insurance premiums written before the share of the reinsurers
2 = Insurance premiums earned before the share of the reinsurers
3 = Claims incurred before the share of the reinsurers
4 = Operating costs before the fees of the reinsurers and shares of profit
5= Share of the reinsurers
6 = Balance on technical account before the changes to equalization provision

Primary insurance

euro	1	2	3	4	5	6
Guarantee						
2016	12 215 790,23	10 322 694,45	-1 140 838,02	-4 966 231,44	-931 464,98	3 284 160,01
2015	9 974 871,07	10 993 970,56	-1 732 835,54	-4 777 713,42	-947 850,82	3 535 570,79
2014	11 217 221,41	12 666 221,34	-387 738,77	-4 645 538,31	-1 660 559,40	5 972 384,86
Reinsurance						
2016	1 798,01	40 380,78	2 109,54	0,00	0,00	42 490,32
2015	43 988,83	44 362,50	-547,71	0,00	0,00	43 814,80
2014	33 034,73	40 363,52	335,67	0,00	0,00	40 699,19
Total						
2016	12 217 588,24	10 363 075,23	-1 138 728,48	-4 966 231,44	-931 464,98	3 326 650,33
2015	10 018 859,90	11 038 333,06	-1 733 383,24	-4 777 713,42	-947 850,82	3 579 385,58
2014	11 250 256,14	12 706 584,86	-387 403,10	-4 645 538,31	-1 660 559,40	6 013 084,05
Change in equalization provision						
2016						1 174 149,21
2015						-3 516 924,28
2014						-6 100 731,45
Balance on technical account						
2016						4 500 799,54
2015						62 461,30
2014						-87 647,40

Note 3: Items deducted from the insurance premiums written

euro	2016	2015
Credit losses of insurance premium receivables	0,00	0,00

Note 4: Breakdown of investment income

euro	2016	2015
Investment income		
Income from other investment		
Dividend income	314 693,39	370 026,40
Interest income	2 617 353,41	2 172 762,73
Other income	6 184,79	11 298,43
	2 938 231,59	**2 554 087,56**
Revaluation of write-offs	917 863,28	245 188,49
Capital gains	808 546,50	6 258 854,46
	1 726 409,78	**6 504 042,95**
Investment income, total	**4 664 641,37**	**9 058 130,51**
Investment expenses		
Expenses from other investments	-293 934,33	-260 235,44
Interest expenses and other capital expenses	-1 000,00	-1 000,23
	-294 934,33	**-261 235,67**
Write-downs	-1 064 180,21	-336 761,66
Capital loss	-93 365,04	0,00
	-1 157 545,25	**-336 761,66**
Investment expenses, total	**-1 452 479,58**	**-597 997,33**
Net profit from investments	**3 212 161,79**	**8 460 133,18**

Note 5: Breakdown of operating costs

euro	2016	2015
Insurance sales expenses	2 076 105,75	1 998 075,37
Insurance management expenses	1 102 048,97	901 186,16
Administrative expenses	1 788 076,72	1 878 451,89
	4 966 231,44	**4 777 713,42**

Note 6: Total operating costs by operations

euro	2016	2015
Processing of claims	420 717,44	194 968,73
Operating costs	4 966 231,44	4 777 713,42
Investment management expenses	255 797,83	228 260,27
	5 642 746,71	**5 200 942,42**

Note 7: Auditor’s fee

euro	2016	2015
KPMG Oy Ab ja Ernst & Young Oy		
Auditor's fee	47 367,02	32 941,85
Other fees	0,00	44 221,50

Notes to the balance sheet

Note 8: Change in intangible and tangible assets

euro	Intangible assets	Tangible assets	Total
Acquisition cost 1 January	891 066,27	320 683,71	1 211 749,98
Depreciated fully during the previous year	0,00	-311 800,33	-311 800,33
Increases	0,00	0,00	0,00
Deductions	0,00	0,00	0,00
Acquisition cost 31 December	**891 066,27**	**8 883,38**	**899 949,65**
Accrued depreciations 1 January	-616 852,78	-169 360,96	-786 213,74
Depreciated fully during the previous year	0,00	311 800,33	311 800,33
Accrued depreciation on deductions	0,00	0,00	0,00
Depreciations of the financial year	-178 213,26	-25 518,10	-203 731,36
Accrued depreciations 31 December	**-795 066,04**	**116 921,27**	**-678 144,77**
Book value 31 December 2016	**96 000,23**	**125 804,65**	**221 804,88**

Note 9: Fair value and valuation differences of investments

euro	Remaining acquisition cost	Book value	Current value
Investments 31 December 2016			
Other investments			
Shares and units	23 142 072,06	23 142 072,06	29 855 342,59
Other financial instruments	90 424 224,10	90 424 224,10	93 607 238,90
Total	**113 566 296,16**	**113 566 296,16**	**123 462 581,49**
The remaining acquisition cost of financial instruments includes the difference between the nominal value and the acquisition value allocated as interest income or expenses	-1 464 224,09		
Valuation difference			**9 896 285,32**

Note 10: Change in shareholders' equity

euro		2016		2015
Restricted				
Share capital 1 January = 31 December		10 200 000,00		10 200 000,00
Unrestricted				
Reserve for invested undistricted equity 1 January		25 515,00	10 025 715,00	
Return of Capital			-10 000 200,00	25 515,00
Profit / loss of the previous accounting periods 1 January	16 391 304,24		9 580 634,72	
Distribution of dividends	-3 000 000,00	13 391 304,24	0,00	9 580 634,72
Profit/loss of the financial year		6 138 993,64		6 810 669,52
		19 555 812,88		**16 416 819,24**
Shareholders' equity total		**29 755 812,88**		**26 616 819,24**

Note 11: Distributable funds

euro	2016
Profit / loss of the financial year	6 138 993,64
Profit / loss of the previous financial years	13 391 304,24
Distributable capital	**19 530 297,88**
Reserve for invested unrestricted equity 1 January	25 515,00
Distributable funds total	**19 555 812,88**

Note 12: Provision for claims outstanding

Adequaty of provisions

	2016	2015
Loan and guarantee		
euro	-756 767,46	-675 944,91
% of claims outstanding 1 January	-63,3 %	-73,3 %

Section 10 (4)(1) Ministry of Social Affairs and Health (decree governing pension institutions, STMtpA 614/2008): If there is a material difference, the difference between the outstanding claims provision set aside at the start of the year for claims that have occurred in previous years, and the payments made for claims that have occurred in previous years and the outstanding claims provision still set aside for these claims.

Other notes

Note 13: Notes to the liability obligations

euro	2016	2015
Total gross exposures of guarantee insurance	1 319 745 597,41	1 164 465 749,96
Total gross exposure of guarantee insurance deducted with the collateral value (hair cut)	1 007 858 311,07	847 307 330,50
Rental liabilities		
Rents of the following financial year	150 249,18	149 019,78
Rents paid later	34 751,82	173 759,10
Leasing liability agreements		
Lease of the following financial year	56 462,49	68 611,68
Leases paid later	45 697,73	104 116,76
Capital commitments	1 649 024,00	2 378 771,00

Garantia received a notification of a possible claim of EUR 5 mn on 30 Decemer 2011.
Garantia considers this claim unfounded and has therefore not recorded it in the provision of known claims in its book keeping. There has been no material change in the status of the matter during 2016 and the process continues.

Note 14: Personnel and members of bodies

euro	2016	2015
Personnel expenses		
Salaries and remunerations	2 957 406,67	2 786 723,68
Pension expenses	381 246,73	469 741,38
Other indirect employee costs	234 519,30	66 936,93
	3 573 172,70	**3 323 401,99**
Salaries and remunerations paid to		
CEO	259 888,07	558 523,79
Members of the board of directors	167 000,00	117 900,00
Average number of employees during fiscal year	**22**	**25**

Note 15: Ownerhip in other companies

euro	Book value	Current value
Shares and fund units		
Ishares S&P 500	4 762 263,11	7 545 172,80
Ishares Europe 600	3 735 441,71	4 263 340,00
SPDR S&P US Dividend	2 509 734,48	3 962 700,00
Db Stoxx Europe 600	1 884 107,50	1 884 107,50
DBx-TrackersDax Ucits etf	992 108,02	1 088 146,00
	13 883 654,82	**18 743 466,30**
Share funds		
Fourton Stamina A	1 239 954,49	2 319 487,04
Mikro Rein Osake	1 000 000,00	1 036 647,06
Arvo Kruunu Osake	1 000 000,00	1 133 563,17
	3 239 954,49	**4 489 697,27**
Property funds		
CapMan Buyout X Fund B Ky	2 353 916,24	2 437 511,97
Taaleritehtaan Tonttirahasto Ky	977 271,14	983 730,00
	3 331 187,38	**3 421 241,97**
Fixed income		
Evli European Investment Grade	2 687 275,38	3 200 937,05
	2 687 275,38	**3 200 937,05**

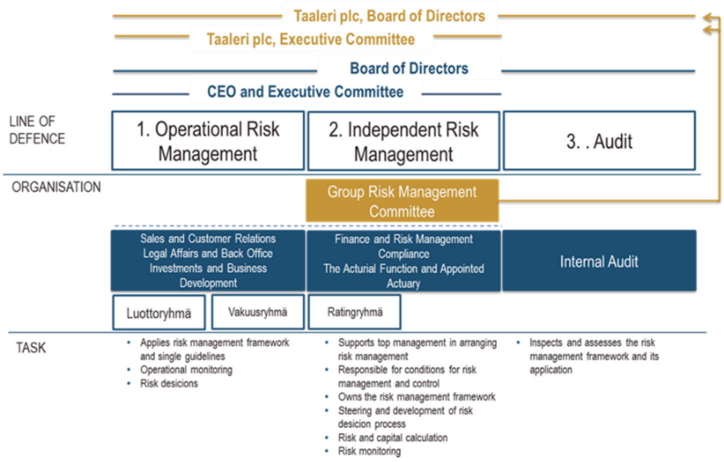
Note 16: Risk and risk management

The company’s risk management and solvency management are based on Garantia’s values, Code of Conduct, strategy and business objectives. The purpose of risk management is to support the achievement of the company’s objectives by identifying the company’s threats and opportunities and ensuring that they remain within the limits of risk appetite and risk-bearing capacity. Internal control that has been reliably organised ensures the observance of the company’s business strategy, the set targets and the principles and procedures related to risk and solvency management.

At Garantia, the principal goal of internal control and risk management is to secure the company’s risk-bearing capacity and thus ensure the continuity of operations. Risk management includes the identification, measurement, monitoring, management and reporting of the individual risks and combined effect of risks that the company is exposed to. Risk and solvency management is also integrated as a fixed part of Garantia’s business processes, and planning and monitoring of operations.

Organisation, responsibilities and control of risk management

Internal control and risk management in Garantia are organised in accordance with a model in which internal control has three lines of defence. In accordance with this model, the tasks have been assigned to (1) units that take business risks in their operations by processing insurance policies, by making decisions binding on the company and by operating at the client interface (Operational risk management); (2) units that are responsible for risk control, carry out independent risk assessments and ensure that company guidelines and acts and other legal provisions are complied with (Independent risk management); and (3) independent internal audit (Internal audit). External control is the responsibility of the auditors and supervisory authorities.



Picture 1: The organisation of Garantia's risk management, Picture 2: Decision-making bodies and reporting relations

The Group Risk Management Committee of the Taaleri Group is responsible for the functioning and effectiveness of the group's risk management process. The independent Group Risk Management Committee supports and steers internal control and risk and solvency management at Garantia in order to ensure that group-level principles and guidelines are also applied in the company. The committee reports to the Taaleri Group's Management Team and Taaleri Plc's Board of Directors.

Garantia's Board of Directors is the supreme decision-making body in matters concerning Garantia's internal control, risk management and solvency management. The Board approves the principles and policies (incl. the risk-taking limits) concerning internal control and risk management and their organisation and monitors and controls their effectiveness and the development of the risk and solvency position. Garantia's CEO, supported by the Management Team, is responsible for the arrangement of internal control and risk management practices in accordance with internal control and risk management principles.

The Board has appointed a Credit Committee, Collateral Committee and a Rating Committee, which, in accordance with the decision-making system approved by the Board, decide on matters within their purview. The Credit Committee is responsible for decisions relating to guaranty, claims and investments. The Collateral Committee is responsible for collateral assessment and for ensuring the quality and effectiveness of the collateral assessment process. The independent Rating Committee is responsible for approving credit ratings and for ensuring the quality and effectiveness of the ratings process. The Collateral Committee and Rating Committee report to the CEO and the Credit Committee reports to the Board of Directors.

The units in Garantia's organisation that are responsible for risk control carry out independent risk assessments and ensure that company guidelines and acts and other legal provisions are complied with, and thus form a so-called independent risk management function. The task of the independent risk management function is to assist the Board of Directors and other functions to ensure efficient risk management, to monitor the functioning of the risk management system and the company's general risk profile as a whole, to report on exposure to risks and to advise the Board in risk management matters, to identify and assess developing risks and to ensure the appropriateness of the risk models used to measure risks. The independent risk management function reports its activities to the Taaleri Group Risk Management Committee, and Garantia's Board of Directors and CEO.

Internal audit is an assessment, verification and consulting function that is independent of the company's operational activities. The task of internal audit is to support the company's management in the achievement of targets by providing a systematic approach to the assessment and development of the adequacy and efficiency of the organisation's risk management, control, management and administration processes. Internal audit's activities are based on an action plan that is compiled annually. Internal audit reports on its observations, conclusions and recommendations to the Board of Directors of Taaleri Plc and Garantia.

Risk management process

Garantia's risk management process is made up of the following areas:

1. Operational planning;
2. Capital management;
3. Risk appetite;

4. Identification and assessment of risks;
5. Measurement of risks; and
6. Control and reporting of risks.

Garantia's operational planning is made up of long-term (about 3 years) strategic planning and short-term (1 year) annual planning. Operational planning is based on an analysis of the operating environment, the competitive environment and own operations and also on the Taaleri Group strategy. Profit and solvency scenarios, and stress tests, risk survey results, and a risk and solvency assessment are used to define the company's goals, projects supporting achievement of these goals and risk appetite. Every year the actuary presents the statements required by the Insurance Companies Act to the Board of Directors to support operational planning. The strategy and annual plan, including the own risk and solvency assessment, are confirmed by the company's Board of Directors, and the entire personnel are involved in its preparation.

Garantia's goal is to be a reliable partner and the company maintains strong solvency to ensure the continuity and stability of its operations. The Board has set Garantia's target level for capitalisation above the statutory solvency capital requirement and the minimum capital requirement required by credit rating agency Standard & Poor's for an AAA credit rating, and at the economic capital model defined at a confidence level of 99.9%. Garantia only distributes dividends or returns capital to the owner when this does not put the A- credit rating at risk. The purpose of capital management is to ensure in an anticipatory way that the company has adequate capital reserves for exceptional situations. The principal means to maintain balance between risks and actual capitalisation is to ensure profitable business operations and active risk management. If an imbalance is detected, balance is restored with management of profit and risk position or by acquiring new capital.

Risk appetite means the amount and type of risks that the company is prepared to take in order to achieve the targets set for its business. Garantia has moderate risk appetite and this is defined with so-called "risk-taking limits / risk indicators". The Board of Directors approves the risk-taking limits / risk indicators annually as part of the capital plan (solvency limits), credit risk policy, reinsurance policy and investment plan.

Constant identification and assessment of risks in the business and operating environment are part of Garantia's risk and solvency management process. The principal risks associated with Garantia's business operations are credit risks arising from guaranty operations, investment risks regarding assets covering technical provisions, strategic risks and operational and compliance risks. The identification and assessment of risks are described separately for each risk later in this note.

Garantia defines and assesses its capital requirement / measures the risk of its business operations with three different Value-at-Risk-based risk indicators. The primary indicator used in the steering of operations, measurement of risk and assessment of capital adequacy is economic capital ("Internal risk capital") at a confidence level of 99.9 or 99.5%. When estimating its capital requirement, the company also uses the solvency capital requirement (SCR) based on the Solvency II standard formula at a confidence level of 99.5% and the minimum capital requirement corresponding to AAA credit rating that is in accordance with the S&P's Insurance Capital Model. In addition to VaR-based risk indicators, Garantia measures, monitors and assesses the risks of its business operations and their development with other quantitative and qualitative risk indicators. The measurement of risks is described separately for each risk later in this note.

Garantia's monitoring and reporting of risk and solvency position is divided into internal and external monitoring and reporting. External reporting means the information published for all stakeholders and reporting to the authorities. Garantia also reports on its operations to external credit rating agency Standard & Poor's. Internal reporting of risk and solvency position means reporting to Garantia's Management Team and Board of Directors at least once a month and quarterly reporting to the Taaleri Group Risk Management Committee and further to the Board of Directors of the Taaleri Group. The target of internal monitoring and reporting is to ensure that the company's risk and solvency position are within the limits of risk appetite.

Insurance risk

Insurance risk means a risk of loss arising from inadequate assumptions concerning pricing and technical provisions or an unfavourable change in the value of insurance liabilities. In guaranties, the insurance risk mostly consists of credit risk, i.e. the inability of the guaranteed counterparty to manage its financial and/or operational obligations under the contract in relation to the insured party. This may be the result of the default of the guaranteed counterparty (default risk) or the guaranteed counterparty may fail to fulfil a contractual obligation on time (delivery risk). The credit risk is also considered to include the counterparty risk of the reinsurers or the party providing other counter guaranties, which results from the default of the reinsurer or the party providing other counter guaranties, and the value change risk, which is caused by changes in the fair value of the collateral.

The aim in the management of credit risk is to ensure that the negative profit impacts arising from client and counterparty risks remain at acceptable levels and that the returns are adequate in relation to the risks taken. In guaranty insurance credit risks are reduced by means of client selection, active management of client relationships, monitoring of changes in the clients' operations, diversification and also typically with reinsurance and with collateral and covenant arrangements. Central to the management of credit risks is the process of underwriting insurance policies, which is controlled by the credit risk policy, reinsurance policy and decision-making system confirmed by the Board of Directors and the complementary process descriptions and guidelines on credit risk assessment, pricing, collateral and covenants approved by the Management Team. The risk management function monitors the functioning and quality of the insurance process. In addition to the daily insurance process, credit risks are identified and assessed at least once a year with a risk survey compiled in conjunction with the annual planning.

The amount of insurance risk is measured by amount of the economic capital model, the solvency capital requirement (SCR) and S&P's insurance capital model. The insurance risk's economic capital is defined separately for each contract with internal ratings-based approach according to Basel II which considers the exposure at default, the instrument's credit rating, duration, and the loss given default, which depends on counter-collateral and reinsurance. The economic capital model also includes concentration risk. Credit risk specific to clients and groups of connected clients are also assessed with the following indicators: client's rating and background variables, gross insurance exposure, the proportion reinsured and amount and type of other collateral, open position, covenants and risk client status. The credit risk of insurance exposure is assessed with the following indicators including: gross insurance exposure, proportion reinsured and other collateral, and open position and economic capital figures by product group, rating class, industry, average maturity of exposure, claims incurred in relation to earned premiums and insurance exposure. The insurance risk position is monitored and reported to the Management Team and the Board of Directors every month.

Quantitative information on insurance risks

Sensitivity analysis of Insurance operations, 31.12.2016*

Risk parameter	Total, EUR thousand	Change in risk parameter	Effect on equity, EUR	Effect on combined ratio, %
Premium revenue	9 467	Up by 10 %	757	improvement 5,90 pp
Claims incurred	1 174	Up by 10 %	0	weakening 1,24 pp
Large claim, EUR 10 million	0	EUR 10 mn	0	weakening 105,63 pp
Operating expenses	4 966	Up by 10 %	-397	weakening 5,25 pp

Sensitivity analysis of Insurance operations, 31.12.2015*

Risk parameter	Total, EUR thousand	Change in risk parameter	Effect on equity, EUR	Effect on combined ratio, %
Premium revenue	9 849	Up by 10 %	473	improvement 5,79 pp
Claims incurred	1 492	Up by 10 %	0	weakening 1,51 pp
Large claim, EUR 10 million	0	EUR 10 mn	0	weakening 101,53 pp
Operating expenses	4 778	Up by 10 %	-382	weakening 4,85 pp

*Sensitivity analysis is based on Garantia Insurance Company Ltd's FAS financial statements.

Trend in claims incurred

EUR thousand	Claims paid*	Change in provision for	Claims incurred	% of insurance exposure	Claims ratio, %
2016	-1 038	-100	-1 174	0,09 %	12,4 %
2015	-1 421	-71	-1 492	0,13 %	15,1 %
2014	-569	157	-412	0,03 %	3,7 %
2013	-2 526	121	-2 405	0,18 %	22,2 %
2012	-1 772	504	-1 268	0,09 %	11,7 %
2011	-4 827	-753	-5 580	0,44 %	50,8 %
2010	-2 098	26	-2 072	0,15 %	18,7 %

* incl. Reinsurers' share

Insurance exposure by product EUR million	2016	2015
Loan guarantees	407	431
Commercial bonds	353	258
Residential mortgage guarantees	467	383
Other guarantees	93	92
Total	**1 320**	**1 164**

Collateral position of insurance exposure EUR million	2016	2015
Reinsured	219	234
Collateral classes 1 and 2	93	83
Collateral classes 3 and 4	60	52
Uncovered position	948	795
Total	**1 320**	**1 164**

Collateral classes: 1 = A secure, liquid collateral, 2 = A secure collateral within the collateral value, 3 = A collateral within the current value, 4 = Other security

Insurance exposure by credit rating* EUR million	2016	2015
AAA - BBB-	165	204
BB+ - BB-	374	327
B+ - B-	208	143
C+ or weaker	22	17
Total	**769**	**690**

*Insurance exposure not including residential mortgage guaranties, assumed reinsurance and residual value insurance.

Insurance exposure by industry* EUR million	2016	2015
Construction	287	225
Manufacturing	196	224
Machinery and Equipment (incl. repair)	49	60
Metal	46	30
Forest and paper	39	54
Food	36	46
Other	26	34
Services	57	59
Wholesale and retail trade	47	34
Energy	39	46
Finance and insurance	36	14
Other industries	106	87
Total	**769**	**690**

*Insurance exposure not including residential mortgage guaranties, assumed reinsurance and residual value insurance.

Actuarial assumptions

Under the Insurance Companies Act, insurance companies must adopt prudent calculation criteria for determining the technical provisions. The value of the technical provisions must always be adequate so that the company can be reasonably assumed to be able to manage its commitments. The criteria for calculating the technical provisions must be submitted to the Financial Supervisory Authority before the end of the financial year.

The provision for unearned premiums is determined as ‘pro rata parte temporis’. The proportion of the premiums written of the valid insurance policies assigned to future financial years is determined on a product basis. The outstanding claims provision consists of known and unknown claims. The individual claims due after the closing date are allocated on a claims basis as part of the known outstanding claims. A proportion of the premiums written accrued by the company during a financial year is allocated to outstanding claims unknown to the company on the closing date as part of unknown outstanding claims, using a specific coefficient. Actual technical provisions are not discounted.

The purpose of the equalization provision is to balance the impact of years with exceptional technical results. The equalization provision acts as a buffer, especially against growth in claims incurred. In Garantia’s calculation bases for the equalization provision an amount corresponding to the claims incurred for the period in question of the provision is recognized annually into profit and loss until the equalization provision reaches the targeted amount. In the long term the equalization provision will gravitate to its target amount. The calculation of the target amount has been defined in the Insurance Companies Act.

Quantitative information about technical provisions

Technical provisions (FAS) EUR thousand	2016	2015
Provision for unearned premiums	12 925	10 985
Provision for claims outstanding	910	669
Known provision for claims outstan(	340	220
Unknown provision for claims outsta	570	450
Equalization provision	73 615	74 789
Total	**87 450**	**86 443**

Provision for unearned premiums and claims outstanding by estimated maturity 31 Dec 2016 EUR thousand	0-1 years	1-2 years	2-3 years	Over 3 year	Total
Provision for unearned premiums	5 272	2 257	1 721	3 675	12 925
Provision for claims outstanding	910	0	0	0	910
Total	**6 182**	**2 257**	**1 721**	**3 675**	**13 835**

Provision for unearned premiums and claims outstanding by estimated maturity 31 Dec 2015 EUR thousand	0-1 years	1-2 years	2-3 years	Over 3 year	Total
Provision for unearned premiums	4 856	2 006	1 472	2 649	10 985
Provision for claims outstanding	669	0	0	0	669
Total	**5 526**	**2 006**	**1 472**	**2 649**	**11 654**

The modified duration of the cash flow distribution of technical provisions (not including the equalization provision) is 2.1 (2.2) years.

Investment risks

The company's investments are used for covering the technical provisions and the equity capital, and their primary purpose is to secure the liquidity of insurance operations also in years with an exceptionally high claims. Garantia's investment activities are long-term and the objective is primarily to secure capital and achieve stable and steadily increasing asset growth. Market, counterparty (credit risk) and liquidity risk are the risks affecting the investment activities.

Market risk means the possibility of losses or an unfavourable change in the economic situation due directly or indirectly to the fluctuation in the market prices and volatility of assets, liabilities and financial instruments. Changes in prices affect the value of investment assets and annual returns. The principal market risks are equity risk, interest rate risk, currency risk and property risk. The credit risk of investments is made up of counterparty risk and credit spread risk. Counterparty risk means the risk of default pertaining to the contractual counterparty. Credit spread risk describes the difference in price of risky interest rate instruments and risk-free interest rate instruments, in other words, the risk arising from a change in the credit margin.

The main aim in the management of investment risks is to keep the negative profit impacts arising from investments and the changes in the values of investments at acceptable levels in the long term, to ensure that investment returns are adequate in relation to the risks taken and to safeguard the company's liquidity. Investment risks are managed through effective diversification of the investments by asset class, sector, geographical area, credit rating category and counterparty, and by ensuring adequate liquidity of the investments. Central to the management of investment risks is the daily implementation of investment activity, which is controlled by the investment plan and decision-making powers. In addition to the daily investment activities and monthly reporting, investment risks are assessed at least once a year with a risk survey compiled in conjunction with the annual planning.

Capital requirements for investment risks are measured by means of the economic capital model, the Solvency Capital Requirement (SCR) and S&P's insurance capital model. In the economic capital model, investment risks are measured on an instrument-specific basis with Value-at-Risk calculation models for equity risk, currency risk, interest rate risk and credit risk. The credit risk with fixed income and private equity investments is defined with internal ratings-based method according to Basel II which considers the amount of investment, the instrument's credit rating, the loss given default and duration. In addition to economic capital investment risks are measured based on asset class, by country, credit category, counterparty, modified duration, interest rate sensitivity and the amount of foreign currency denominated investments. The investment risk position is monitored and reported to the Management Team and the Board of Directors every month.

Quantitative information on investment risks

Investment mix at fair value		
EUR mn	**2016**	**2015**
Fixed income investments*	101	98
Equity investments	26	21
Land and buildings	1	1
Other investments	0	0
Total	**127**	**120**

* includes cash and bank balances. Fixed income investments include mainly bonds issued by Finnish corporates and Nordic banks.

Fixed-income portfolio (excl. bond funds) by maturity* and credit rating ** 31 Dec 2016						
EUR mn / years	**0 - 1 years**	**1 - 3 years**	**3 - 5 years**	**Yli 5 years**	**Total**	**%**
AAA - AA-	2	5	-	10	17	18 %
A+ - A-	0	13	-	-	13	14 %
BBB+ - BBB-	3	15	11	10	38	39 %
BB+ or weaker	2	11	12	5	29	29 %
Not rated	0	-	-	-	0	0 %
Total	**7**	**44**	**23**	**24**	**98**	**100 %**

Fixed-income portfolio (excl. bond funds) by maturity* and credit rating ** 31 Dec 2015						
EUR mn / years	**0 - 1 years**	**1 - 3 years**	**3 - 5 years**	**Yli 5 years**	**Total**	**%**
AAA - AA-	3	23	0	0	27	28 %
A+ - A-	3	16	3	0	22	23 %
BBB+ - BBB-	0	6	17	2	25	26 %
BB+ or weaker	0	10	12	0	21	22 %
Not rated	0	0	0	0	0	0 %
Total	**7**	**55**	**32**	**2**	**95**	**100 %**

* The maturity is presented until the end of the term to maturity. If the paper includes call option, the maturity is presented until the first possible Call date.

** Rating is based on 1. Garantia's Internal Credit Rating, 2. External rating affirmed by external rating agency or 3. "Shadow rating" provided by Banks to bond investors.

Sensitivity analysis of investment activities, 31.12.2016*				
Investment category	Investments at fair values, EUR million	Risk parameter	Change	Effect on equity, EUR million
Bonds	98,3	Change in interest rates	1 %	2,43
Equities	23,2	Market value	10 %	1,86
Equity investments	3,4	Market value	10 %	0,27

Sensitivity analysis of investment activities, 31.12.2015*				
Investment category	Investments at fair values, EUR million	Risk parameter	Change	Effect on equity, EUR million
Bonds	91,7	Change in interest rates	1 %	1,77
Equities	18,6	Market value	10 %	1,49
Equity investments	5,7	Market value	10 %	0,45

*Sensitivity analysis is based on Garantia Insurance Company Ltd’s FAS financial statements. However, the effect of changes on calculations is the assumed market valuation before and after the change.

Operational risks

Operational risks mean the risk of loss resulting from deficient or faulty processes, human error, systems or external events.

Successful management of operational risks helps to ensure that the company's operations are properly organised and that the risks do not cause any unexpected direct or indirect financial losses. Garantia is determined to maintain and strengthen a corporate culture that is positively disposed towards management of operational risks and internal control by continuously providing personnel with training and guidelines.

In order to manage the operational risks, it is central to identify and evaluate risks as well as to ensure the adequacy of the control and management methods. The principal tools in the management of operational risks are risk surveys at least once a year on each unit, continuous registration of operational risks, identification of corrective measures and the monitoring and reporting of these, continuity planning, principles for outsourcing, the planning and implementation of new products, knowing your customer (KYC) and prevention of money laundering and terrorist financing, and process descriptions and other working instructions and operating guidelines.

The extent of the operational risks is measured by the solvency capital requirement (SCR) and the amount of economic capital employed by operational risks, which is determined on the basis of the annual survey of risks. Actual risk events and near misses are monitored and registered, the corrective measures concerning these are specified and the implementation of the measures is followed. Operational risks are reported to the Management Team and the Board of Directors on a quarterly basis.

Other risks

Strategic risks are the risks that result from changes in the operating and competitive environment, slow reaction to changes, selection of the wrong strategy or business model or the unsuccessful implementation of a strategy. Reputational and regulatory risks are part of strategic risks. The principal method in the management of strategic risks is systematic and continuous operational planning and monitoring process which makes it possible to identify and assess potential risks in the operating, competitive and regulatory environment and to update the strategy and manage the measures launched to manage risks. Strategic risks are monitored and assessed at least once a year with a risk survey compiled in conjunction with the annual planning.

Compliance risks are the risks pertaining to legal or administrative consequences, economic losses or loss of reputation that result from the failure of the company to comply with laws, decrees or other regulations applicable to its operations. Legislative changes are actively monitored and ongoing projects are regularly reported to the Board of Directors. The survey of risks conducted at Garantia in conjunction with annual planning also includes the identification and assessment of regulatory risks and the definition and monitoring of development measures to reduce the risks. Providing the personnel with guidelines and training is also central to managing compliance risks.

Concentration risk means all types of risks that if there were to materialise, the associated losses could be so large that they would endanger the solvency of insurance or reinsurance companies or financial position. The principal concentration risk in Garantia's business operations arises from the concentration risk of direct and indirect credit and counterparty risk in guaranty and/or investment operations. Garantia’s total exposures contain large, individual group of connected clients and industry-specific credit risk concentrations. In addition, Garantia’s guaranties and investments are concentrated in Finland. The selection of clients and investment targets and the continuous monitoring of changes in the situation of clients is emphasised above all in the management of the credit risk concentration risk. Concentration risk is measured and assessed in the economic capital model with a separate concentration risk model, according to large exposures, as laid down in the Capital Requirements Regulation of the EU and with risk limits specific to groups of connected clients.

Liquidity risk means the risk that insurance and reinsurance companies are unable to convert their investments or other assets into cash in order to meet their financial obligations that fall due for payment. Liquidity risk is limited at Garantia as premiums written is collected before claims are paid and the largest individual payments are insurance compensation payments to beneficiaries or distribution of profit / repayment of capital to shareholders and the payment dates for these payments are usually known well in advance. Garantia has no financial liabilities. Garantia’s principle measures in liquidity risk management are sufficient amount of cash for managing daily payments and the liquidity of the investment portfolio.

Key financial indicators and analyses

Note 17: Key financial indicators

	2016	2015	2014	2013	2012
Gross premiums written (before share of reinsurers), EUR	12 217 588	10 018 860	11 250 256	10 610 274	12 328 603
Claims ratio, %	12,4 %	15,1 %	3,7 %	22,2 %	11,7 %
Claims incurred without calculated interest expenses (+/-), EUR	1 174 149	1 491 654	-412 292	-2 404 875	-1 267 626
Claims ratio without calculated interest expenses, %	12,4 %	15,1 %	3,7 %	22,2 %	11,7 %
Expense ratio, %	52,5 %	48,5 %	42,0 %	36,3 %	31,7 %
Combined ratio, %	64,9 %	63,7 %	45,7 %	58,5 %	43,4 %
Combined ratio without calculated interest expenses, %	64,9 %	63,7 %	45,7 %	58,5 %	43,4 %
Operating profit (+) or loss (-), EUR	6 538 812	12 039 519	11 360 927	10 655 515	9 405 559
Adjustments in off-balance sheet valuation differences, current value reserve and revaluation reserve (+/-), EUR	3 210 059	-3 586 445	2 294 523	-28 448	2 728 971
Total result (+/-), EUR	9 748 871	8 453 074	13 655 450	10 627 067	12 134 530
Interest expenses and other financial expenses (+), EUR	1 000	1 000	1 000	1 062	1 682
Calculated interest expenses (+), EUR					
Return on total assets as a percentage (at fair value)	7,7 %	6,8 %	11,2 %	9,2 %	11,2 %
Net return on investments, % at fair value on capital employed (+/-)	5,4 %	4,4 %	7,1 %	5,9 %	6,1 %
Equalization provision, EUR	73 614 597	74 788 747	71 271 823	65 171 091	60 709 909
Average number of personnel during the financial period	22	25	25	24	23

Note 18: Earnings analyses

euro	2016	2015	2014	2013	2012
Insurance premium income (+/-)	9 467 030	9 848 753	11 070 914	10 828 016	10 835 847
Claims incurred (-/+)	-1 174 149	-1 491 654	-412 292	-2 404 875	-1 267 626
Operating costs (-)	-4 966 231	-4 777 713	-4 645 538	-3 934 512	-3 434 715
Other technical income and expenses (+/-)	0	0	0	0	0
Balance on technical account before changes in equalization provision (+/-)	**3 326 650**	**3 579 386**	**6 013 084**	**4 488 629**	**6 133 506**
Investment income and expenses, revaluations and their adjustments and changes in value (+/-)	3 212 162	8 460 133	5 347 843	6 166 886	3 272 051
Other income and expenses (+/-)					
Share of associated companies' profit (+) or loss (-)					
Operating profit (+) or loss (-)	**6 538 812**	**12 039 519**	**11 360 927**	**10 655 515**	**9 405 558**
Change in equalization provision (-/+)	1 174 149	-3 516 924	-6 100 731	-4 461 182	-6 053 726
Profit (+) or loss (-) before extraordinary items	**7 712 961**	**8 522 594**	**5 260 196**	**6 194 333**	**3 351 832**
Income taxes and other direct taxes (-/+)	-1 573 968	-1 711 925	-1 042 074	-1 516 421	-818 575
Minority shares (-)					
Profit (+) or loss (-) for the financial year	**6 138 993**	**6 810 670**	**4 218 122**	**4 677 912**	**2 533 257**

Note 19: Investment at fair value

	Basic allocation				Risk allocation [8]			
	31.12.2016		31.12.2015		31.12.2016		31.12.2015	31.12.2014
	EUR million	%	EUR million	%	EUR million	%	% [10]	% [10]
Fixed income investments	**100 748 681**	**79,1**	**98 429 865**	**82,1**	**100 748 681**	**79,1**	**82,1**	**75,5**
Loan receivables [1]								
Bonds	98 338 244	77,2	94 405 577	78,7	98 338 244	77,2	78,7	64,4
Other financial market instruments and deposits [1] [2]	2 410 436	1,9	4 024 287	3,4	2 410 436	1,9	3,4	11,1
Equity investments	**25 670 676**	**20,1**	**20 615 834**	**17,2**	**25 670 676**	**20,1**	**17,2**	**22,5**
Listed equities [3]	23 233 164	18,2	18 557 891	15,5	23 233 164	18,2	15,5	20,9
Private equity investments [4]	2 437 512	1,9	2 057 943	1,7	2 437 512	1,9	1,7	1,6
Unlisted equities [5]								
Real estate investments	**983 730**	**0,8**	**902 295**	**0,8**	**983 730**	**0,8**	**0,8**	**2,0**
Direct real estate investments	0	0,0	0	0,0	0	0,0	0,0	1,7
Real estate investment funds and collective investments	983 730	0,8	902 295	0,8	983 730	0,8	0,8	0,3
Other investments	**0**	**0,0**	**0**	**0,0**	**0**	**0,0**	**0,0**	**0,0**
Hedge funds [6]								
Commodities								
Other investments [7]	0	0,0	0	0,0	0	0,0	0,0	0,0
Total	**127 403 086**	**100,0**	**119 947 993**	**100,0**	**127 403 086**	**100,0**	**100,0**	**100,0**
Effect of derivatives [9]								
Total investments at fair values	**127 403 086**	**100,0**	**119 947 993**	**100,0**	**127 403 086**	**100,0**	**100,0**	**100,0**
Modified duration of bond portfolio	3,0							

1) Includes accrued interest
2) Includes cash and bank balances, and receivables and debt relating to trading in securities
3) Includes balanced funds if they cannot be allocated elsewhere
4) Includes private equity funds and mezzanine funds and also infrastructure investments
5) Includes unlisted real estate investment companies
6) Includes all types of hedge fund units irrespective of the fund's strategy
7) Includes items that cannot be allocated to other investment groups
8)The risk allocation can be presented for comparison periods as the data accumulates (not retroactively)
If the figures are presented for comparison periods and the periods are not entirely comparable, then this must be stated.
9)Includes the effect of derivatives on the difference between risk allocation and basic allocation. The effect may be +/-. After the correction the final amount of the risk allocation matches the basic allocation.
10) The relative share is calculated using the final amount of "Total investments at fair value" as the divisor.

Note 20: Net return on investments from capital employed

	Net return on investments at market value [8]	Capital employed [9]	Return on capital employed, %	Return on capital employed (ROCE), %			
		31.12.2016		31.12.2015	31.12.2014	31.12.2013	31.12.2012
ROCE, EUR, %	**EUR**	**EUR**	**%**	**%**	**%**	**%**	**%**
Fixed income investments	4 662 236	97 127 739	4,8	2,5	4,6	1,8	5,4
Loan receivables [1]							
Bonds	4 669 461	93 242 789	5,0	2,5	4,6	1,8	5,4
Other financial market instruments and deposits [1] [2]	-7 224	3 884 950	-0,2	0,0	0,0	0,0	
Equity investments	2 075 253	21 033 593	9,4	9,8	14,3	20,2	12,0
Listed equities [3]	1 994 157	19 098 580	9,8	10,8	14,5	20,2	12,0
Private equity investments [4]	81 096	1 935 013	4,0	0,0	0,0		
Unlisted equities [5]							
Real estate investments	-20 705	888 953	-1,1	6,9	12,4	0,1	0,9
Direct real estate investments				10,7	12,6	0,2	
Real estate investment funds and collective investment	-20 705	888 953	-1,1	-7,8	11,5	-0,2	3,1
Other investments					0,0	0,0	0,0
Hedge funds [6]							
Commodities							
Other investments [7]					0,0	0,0	
Total	6 716 784	119 050 285	5,6	4,6	7,3	6,1	6,3
Unallocated income, expenses and operating expenses	-255 798						
Net return on investments at fair value	6 460 987	119 050 285	5,4	4,4	7,1	5,9	6,1

1) Includes accrued interest
2) Includes cash and bank balances, and receivables and debt relating to trading in securities
3) Includes balanced funds if they cannot be allocated elsewhere
4) Includes private equity funds and mezzanine funds and also infrastructure investments
5) Includes unlisted real estate investment companies
6) Includes all types of hedge fund units irrespective of the fund’s strategy
7) Includes items that cannot be allocated to other investment groups
8) Change in market value from beginning and end of reporting period less cash flows during the period.
Cash flow = difference between sales/returns and purchases/costs
9) Capital employed = market value at the beginning of the reporting period + daily/monthly time weighted cash flows

Note 21: Calculation of Key Financial Ratios

Gross premiums written	=	Insurance premium income before the share of the reinsurers
Claims ratio, %	=	$\frac{\text{Claims incurred}}{\text{Insurance premium income}}$ This key figure is calculated after the share of the reinsurers.
Expence ratio, %	=	$\frac{\text{Operating costs}}{\text{Insurance premium income}}$ This key figure is calculated after the share of the reinsurers.
Combined ratio, %	=	Claims ratio, % + Expense ratio, %
Operating profit or loss	=	Profit or loss before the change to the equalisation provision and taxes
Return on total assets, % (at fair value)	=	+/- operating profit or loss + interest expences and other financial expences +/- adjustments in the revaluation reserve / current value reserve +/- change of investment value differences ——————————————— + balance sheet total +/- valuation differences of investments The divider of the key figure is calculated as the average of the values of the accounting period and the previous year.
Basic own funds	=	+ Equity and reserves + Equiailization provision - Intangible assets + Valuation differences of investments - Forseeable dividends and distributions - Valuation differences of technical provisions (excl. equalization provision) * * Valuation differences between Solvency II and FAS technical provisions, net of reinsurance recoverables.
Solvency ratio, %	=	$\frac{\text{Basic own funds}}{\text{Solvency capital requirement}}$

SIGNATURES

Helsinki 23. February 2017

Hannu Tonteri	Juhani Elomaa
Timo Hukka	Jukka Ohls
Antti Suhonen	Tomi Yli-Kyyny

Vesa Aho, CEO

Report on the conducted audit was given out today

Helsinki 24. February 2017

KPMG Oy Ab	Ernst & Young Oy
Juha-Pekka Mylén Authorized Public Accountant	Ulla Nykky Authorized Public Accountant

This document is an English translation of the Finnish auditor's report. Only the Finnish version of the report is legally binding.

Auditor's Report

To the Annual General Meeting of Vakuutusosakeyhtiö Garantia

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Vakuutusosakeyhtiö Garantia for the year ended 31 December, 2016. The financial statements comprise the balance sheet, income statement, cash flow statement and notes.

In our opinion, the financial statements give a true and fair view of the company's financial performance and financial position in accordance with the laws and regulations governing the preparation of financial statements in Finland and comply with statutory requirements.

Basis for Opinion

We conducted our audit in accordance with good auditing practice in Finland. Our responsibilities under good auditing practice are further described in *the Auditor's Responsibilities for the Audit of Financial Statements* section of our report. We are independent of the company in accordance with the ethical requirements that are applicable in Finland and are relevant to our audit, 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.

Responsibilities of the Board of Directors and the Managing Director for the Financial Statements

The Board of Directors and the Managing Director are responsible for the preparation of financial statements that give a true and fair view in accordance with the laws and regulations governing the preparation of financial statements in Finland and comply with statutory requirements. The Board of Directors and the Managing Director are also responsible for such internal control as they determine 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, the Board of Directors and the Managing Director are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting. The financial statements are prepared using the going concern basis of accounting unless there is an intention to liquidate the company or cease operations, or there is no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of Financial Statements

Our objectives are to obtain reasonable assurance on 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 good auditing practice will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with good auditing practice, we exercise professional judgment and maintain professional skepticism 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 company'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 the Board of Directors' and the Managing Director's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the company'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 company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events so that the financial statements give 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 communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards

Other Reporting Requirements

Other Information

The Board of Directors and the Managing Director are responsible for the other information. The other information comprises information included in the report of the Board of Directors. Our opinion on the financial statements does not cover the other information.

In connection with our audit of the financial statements, our responsibility is to read the information included in the report of the Board of Directors and, in doing so, consider whether the information included in the report of the Board of Directors is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. Our responsibility also includes considering whether the report of the Board of Directors has been prepared in accordance with the applicable laws and regulations.

In our opinion, the information in the report of the Board of Directors is consistent with the information in the financial statements and the report of the Board of Directors has been prepared in accordance with the applicable laws and regulations.

If, based on the work we have performed, we conclude that there is a material misstatement in the information included in the report of the Board of Directors, we are required to report this fact. We have nothing to report in this regard.

Helsinki 24th of February

KPMG Oy Ab	Ernst & Young Oy
Juha-Pekka Mylén	Ulla Nykky
Authorized Public Accountant in Finland	*Authorized Public Accountant in Finland*