Group's Risks

In Sampo Group the risks associated with business activities fall, by definition, into three main categories: strategic risks, reputational risks and risks inherent in business operations. The first two risk classes are only briefly described in this Risk Management Disclosure as the focus is on the third risk class.

External Drivers and Strategic Risks

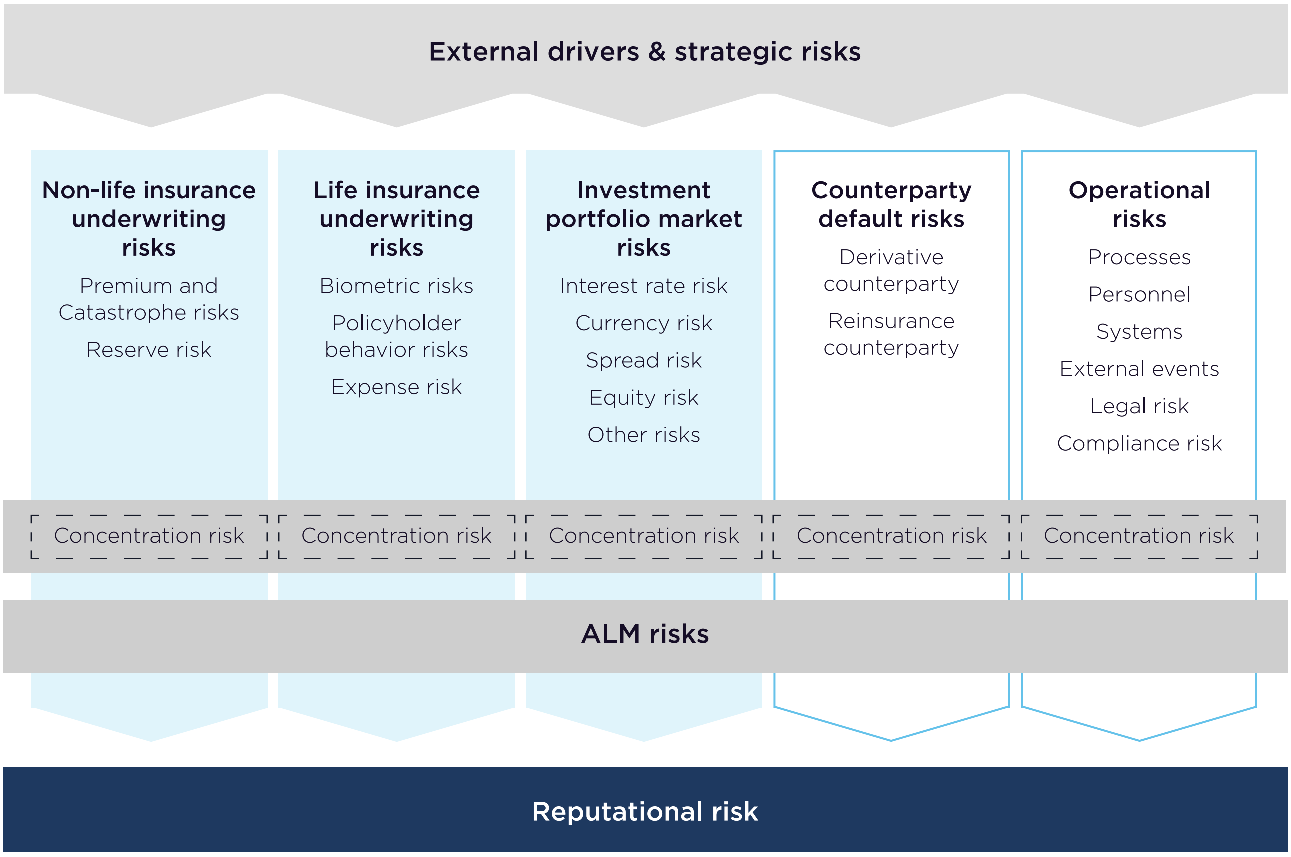
Strategic risk is the risk of losses due to changes in the competitive environment or lack of internal operational flexibility. Unexpected changes in the general business environment can cause larger than expected fluctuations in the financial results and in the long run these can endanger the existence of Sampo Group's business models. External drivers behind such changes are varied, and include for instance general economic development, development of the institutional environment and technological innovations. As a result of these external drivers, business models of the industry can change, new competitors may appear and customer demand and behaviour can change.

Due to the predominantly external nature of the drivers and development in the competitive environment, managing strategic risks is the responsibility of the executive level senior management. Proactive strategic decision-making is the central tool in managing strategic risks which relate to competitive advantage. The maintenance of internal operational flexibility to be able to adjust the business model and cost structure when needed is also an efficient tool in managing strategic risks. Although strategic risks are not covered by the capitalization process in Sampo Group they may, however, have an effect on the amount and structure of the actual capital base, if this is deemed to be prudent in the existing business environment.

Reputational Risk

Reputational risk refers to the risk that adverse publicity regarding the company's business practices or associations, whether accurate or not, causes a loss of confidence in the integrity of the institution. Reputational risk is often a consequence of a materialized operational or compliance risk and often manifests as a deterioration of reputation amongst customers and other stakeholders. Reputational risk is related to all activities as shown in the figure Classification of Risks in Sampo Group. As the roots of reputational risk are varied, the tools to prevent it must be diverse and embedded in the corporate culture. The corporate culture, which is based on the core values of ethicality, loyalty, openness and entrepreneurship, is thus seen as an essential tool in preventing reputational risk in Sampo Group. These core values are reflected in Sampo Group's Corporate Governance system and in how Sampo deals with core stakeholders (i.e. customers, personnel, investors, other co-operation partners, tax authorities and supervisory authorities) and other parties, who may have an interest in Sampo's business.

Classification of Risks in Sampo Group



Risks Inherent in Business Operations

In its underwriting and investment operations, Sampo Group is consciously taking certain risks in order to generate earnings. These **earnings risks** are carefully selected and actively managed. Underwriting risks are priced to reflect their inherent risk levels and the expected return of investments is compared to the related risks. Furthermore, earnings related risk exposures are adjusted continuously and their impact on the capital need is assessed regularly.

Successful management of underwriting risks and investment portfolio market risks is the main source of earnings for Sampo Group companies. Day-to-day management of these risks, i.e. maintaining them within given limits and authorisations is the responsibility of the business areas and the investment unit.

Some risks, such as counterparty default risks and operational risks presented in the picture Classification of Risks in Sampo Group are indirect repercussions of Sampo's normal business activities. They are one-sided risks, which in principle have no related earnings potential. Accordingly, the risk management objective is to mitigate these risks efficiently rather than actively manage them. Mitigation of **consequential risks** is the responsibility of the business areas and the investment unit and the capital need for these risks is measured by independent risk management functions. It has to be noted that the categorization of risks between earnings and consequential risks varies depending on the industry. For Sampo Group's clients, for instance, the events that are subject to insurance policies are consequential risks and for Sampo Group these same risks are earnings risks.

Some risks such as interest rate, currency and liquidity risks are by their nature simultaneously linked to various activities. In order to manage these risks efficiently, Sampo Group companies have to have a detailed understanding of expected cash flows and their variance within each of the company's activities. In addition, a thorough understanding of how the market consistent values of assets and liabilities may fluctuate at the total balance sheet level under different scenarios is needed. These balance sheet level risks are commonly defined as Asset and Liability Management (ALM) risks. In addition to interest rate, currency and liquidity risk, inflation risk and risks relating to GDP growth rates are central ALM risks in Sampo Group. The ALM risks are one of the focus areas of senior management because of their relevance to risks and earnings in the long run.

In general, **concentration risk** arises when the company's risk exposures are not diversified enough. When this is the case, an individual extremely unfavourable claim or financial market event, for instance, could threaten the solvency of the company.

Concentrations can evolve within separate activities – large single name or industry specific insurance or investment exposures – or across activities when a single name or an industry is contributing widely to the profitability and risks of the company through both insurance and investment activities.

Concentration risk may also materialize indirectly when profitability and capital position react similarly to general economic developments or to structural changes in the institutional environment in different areas of business. This kind of indirect concentration risk can be seen as part of strategic risk.

More detailed risk definitions may be found in Appendix 2 (Risk Definitions).