



ANNUAL REPORT

1997

Konsernin tilintaloustiedot
31.12.1997, tilinvoiton perusteella

Kokonaan käyttökelpoinen
363 miljoonaa markkaa (8 195 A)

■ Liiketoiminta

■ Liiketoiminnan ja varain-
hoidon tulos

■ Aika- ja kassa-
tulo

■ Muut tulot ja menot

■ Vapaa sijoitus-
tulo

■ Muut tulot

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Notes to the Financial Statements are excluded from the English adaptation of Arsenal's Annual Report.

Highlights of the Financial Period

- The Group's total assets and guarantees diminished by FIM 4.5 billion.
- The loss for the financial period was FIM 117 million.
- Real estate assets worth FIM 2.1 billion were sold in 3,200 separate transactions.
- A total of FIM 0.4 billion in assets was acquired as collateral for unpaid receivables.
- In a single transaction, 2,700 leisure time-shares were sold in the holiday resorts of Ylläs, Ruka and Kalajoki.
- The Group's receivables from clients declined by FIM 1.6 billion. Client loan amortisations were FIM 1.0 billion and the reintegration of clients into the regular banking system reduced liabilities by FIM 0.3 billion.
- Subsidiary company Arsenal-SSP Ltd. paid back a debenture loan of FIM 1.4 billion to the Government Guarantee Fund.
- When the Group acquired the share capital of SKOP-Real Estate Ltd., it received real estate assets worth FIM 1 billion.
- The Finnish Government's unconditional guarantee of FIM 18 billion was reduced by FIM 3 billion and it totalled FIM 15 billion.
- Arsenal reduced its payroll by 70 persons during the financial period.
- As at January 1, 1998 Arsenal reorganised its administrative regions and branch offices by reducing their number from 9 to 5 and from 22 to 15 respectively.



- Arsenal completed the largest real estate transaction in its history in December of 1997, when Sponda Ltd. acquired four properties located in the center of Helsinki for FIM 531 million. The most valuable of the properties sold was the Kaivokatu 12 property, for FIM 235 million.

Group Key Figures

RESULTS AND BALANCE SHEET, MFIM	1997	1996	1995	1994
Balance sheet total	16,322	20,254	23,435	28,670
Guarantees	679	1,259	2,439	4,197
Shareholders' equity	4,262	4,379	1,931	(816)
Capital injections from				
the Finnish Government	22,800	22,800	19,000	11,000
Net income (loss) from				
financial operations	59	(67)	(320)	(1,039)
Securities trading income	619	260	(518)	(1,444)
Other operating income	820	727	731	806
Total operating income	1,499	920	(107)	(1,677)
Operating expenses	975	1,093	1,205	2,083
Depreciation and asset revaluations	300	209	221	3,510
Credit and guarantee losses				
From client receivables	14	503	2,713	3,617
From loans and advances	314	484	1,019	928
Loss for the financial period	(117)	(1,352)	(5,253)	(11,816)

CLIENT OPERATIONS	1997	1996	1995	1994
Total number of clients	8,680	10,215	12,209	12,685
Client receivables due, (MFIM)	3,007	4,610	7,385	11,391
Corporate clients				
Total number of viable clients	1,363	1,732	2,354	2,866
Total receivables due from				
viable clients, (MFIM)	2,048	2,788	4,072	5,900
Total number of non-viable clients	4,760	5,545	6,082	5,519
Total receivables due from				
non-viable clients, (MFIM)	732	1,494	2,855	5,500
Total number of private clients	2,557	2,938	3,773	4,300
Total receivables due from				
private clients, (MFIM)	227	328	458	617
Transfers to regular banking system				
Total number of clients	258	264	320	120
Total client receivables, (MFIM)	277	487	243	118
The average interest rate achieved, (%)	4.3	4.1	3.1	2.4
Loans and advances (MFIM)	4,161	5,210	6,182	6,817

REAL ESTATE OPERATIONS	1997	1996	1995	1994
Total capital employed in				
real estate portfolio, (MFIM)	7,563	8,195	8,737	8,735
Total area, (Mm ²)	2.4	2.4	2.4	2.3
Real estate disposals, (MFIM)	2,109	1,508	1,312	1,004
From balance sheet, (MFIM)	1,586	772	614	404
From guarantees, (MFIM)	523	736	698	600
Real estate acquired as guarantees, (MFIM)	362	525	611	530
Rental margin, (%)				
from capital employed, (%)	3.7	3.5	3.3	3.1

The President's Message

1997: OPERATIONS ON TARGET

1997 was Arsenal Group's fourth year of operations. The Group reached its targets in terms of results, sales and development. Operations were conducted in an efficient and controlled manner thanks to the efforts of Arsenal's personnel, clients and collaborators.

The Group's loss, FIM 117 million, was less than expected due to the increased value of the listed share portfolio, capital gains from sales of shares and higher-than-estimated returns from credit losses.

The Arsenal Group's total assets were reduced by FIM 3.9 billion to a total FIM 16.3 billion. Off-balance sheet liabilities diminished by FIM 0.6 billion to the current FIM 0.7 billion.

The Group's receivables diminished by FIM 1.6 billion during the 1997 financial period. Clients classified as viable continued to recover financially, making it possible to reintegrate them into a regular banking system. Over the 1997 financial period, a total of 260 clients and FIM 0.3 billion in receivables were transferred from Arsenal to the regular banking system.

The Group sold FIM 2.1 billion worth of real estate assets, which was higher than planned.

There were two significant developments in Arsenal's real estate holdings. SKOP-Real Estate Ltd., which was acquired as a wholly owned subsidiary in March, increased the Group's real estate assets by FIM 1 billion. In December Arsenal sold four properties in the center of Helsinki for FIM 0.5 billion, the largest transaction ever for the Group.

The Group's external funding requirements diminished thanks to the increase in total assets. The Finnish Government's unconditional guarantee, granted for the Group's funding, was reduced by FIM 3 billion to a total FIM 15 billion. A debenture loan of FIM 1.4 billion was paid back to the Government Guarantee Fund.

Arsenal's regional organisation was restructured to meet the future needs. From

the beginning of 1998 the number of administrative regions were reduced from 9 to 5 and the number of branch offices was reduced from 22 to 15. The Group will function under this new organisation for a projected two-year period.

THE DEVELOPMENT OF OPERATIONS FROM 1994 TO 1997

The total amount of assets and liabilities for which Arsenal Group assumed the responsibility between 1993 and 1997 from the Savings Bank of Finland – SBF Ltd., Siltapankki Ltd. and SKOP-Real Estate Ltd., was FIM 41 billion. Of those total assets, real estate represented FIM 13.2 billion and client receivables FIM 16.3 billion.

During the first four years of operations Arsenal's client and real estate assets and corresponding liabilities were reduced by FIM 18.9 billion. Properties worth FIM 6 billion were sold and FIM 2 billion in properties were acquired to secure loan receivables. Write-downs on the property portfolio totalled FIM 4.2 billion.

Clients' loan amortisations and sales of assets pledged as collateral totalled FIM 4.6 billion. FIM 1.1 billion in client receivables were transferred to the regular banking system. Credit and guarantee losses on client receivables amounted to FIM 6.8 billion.

Ten of the operating companies for which the Group has assumed responsibility, have been sold.

OUTLOOK FOR THE CURRENT FINANCIAL PERIOD AND FOR THE END OF THE CENTURY

It is expected that during the 1998 financial period the Group's total assets and guarantees will decline by FIM 3 billion to total approximately FIM 14 billion. The loss for 1997 was reduced by FIM 0.6 billion thanks to capital gains on share disposals and returns on write-downs. For the 1998 financial period no such one-off items are expected, therefore the loss for the current financial period will in-



crease when compared with the previous period, but this is in line with the long-term goals.

From 1993 to 1996 the Finnish Government and the Government Guarantee Fund injected a total of FIM 22.8 billion into Arsenal's shareholders' equity. During the 1997 financial period Arsenal did not require further capital injections and it is foreseen that it will not need it in the future either. It is estimated that the shareholders' equity remaining in 2000 will be sufficient to restructure or close down Arsenal's operations.

It will be possible to close down Arsenal's operations when both its total losses and future capital requirement become clear. The Group's operations are expected to continue in their present form until the end of the century. It has been estimated that total assets will diminish to approximately FIM 7 billion.

Arsenal's business after the asset management period will focus on the sale and development of its property portfolio as well as collection of receivables.

Helsinki, March 4, 1998

Seppo Sipola,

President and CEO

Group Structure

BUSINESS CONCEPT OF THE ASSET

MANAGEMENT GROUP

The objective of the Arsenal Group is to manage, develop and liquidate assets for which it has assumed responsibility in order to ensure optimal financial results under prevail-

ing circumstances, thus minimising any further Government investments in the Group and reducing the risk of loss on investments already made.

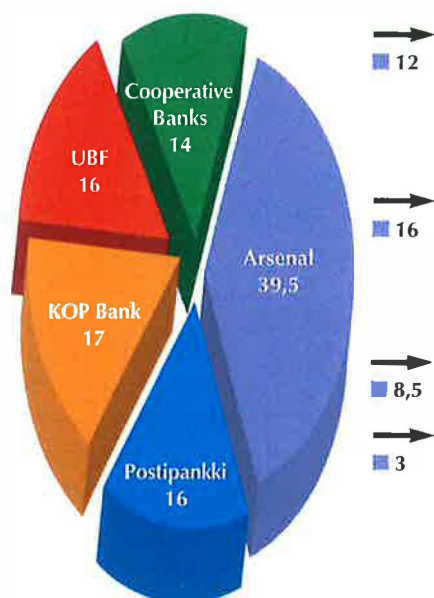
Arsenal's mission is of limited tenure and it is estimated that it will be completed by

the end of the century.

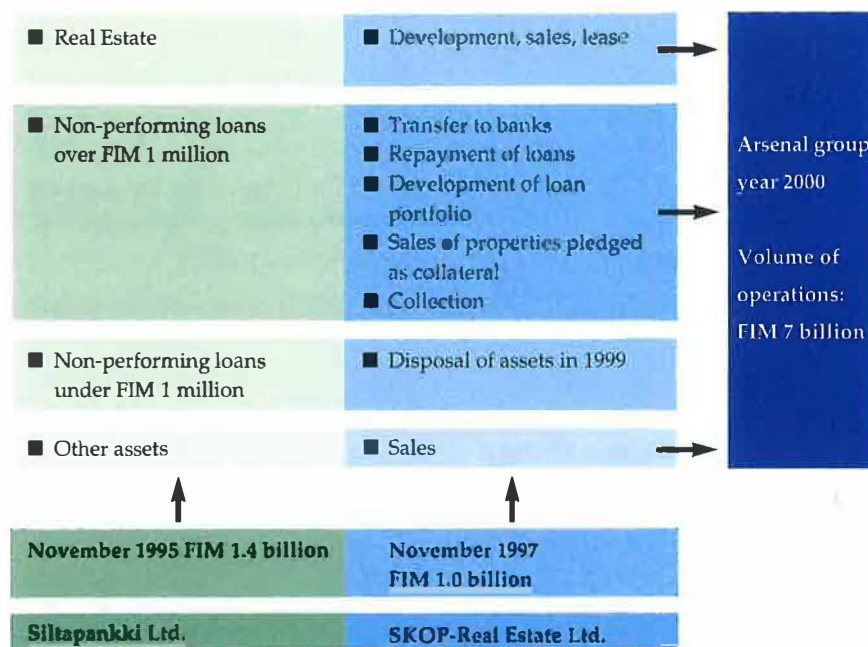
This task is carried out by the parent company Arsenal Ltd and its subsidiaries, Asset Management Company Arsenal-SSP Ltd, Asset Management Company Arsenal-Silta Ltd and SKOP-Real Estate Ltd.

■ The Arsenal Process since the split of the SBF assets in October 1993, FIM billion.

Split of SBF-assets October 22, 1993



Arsenal

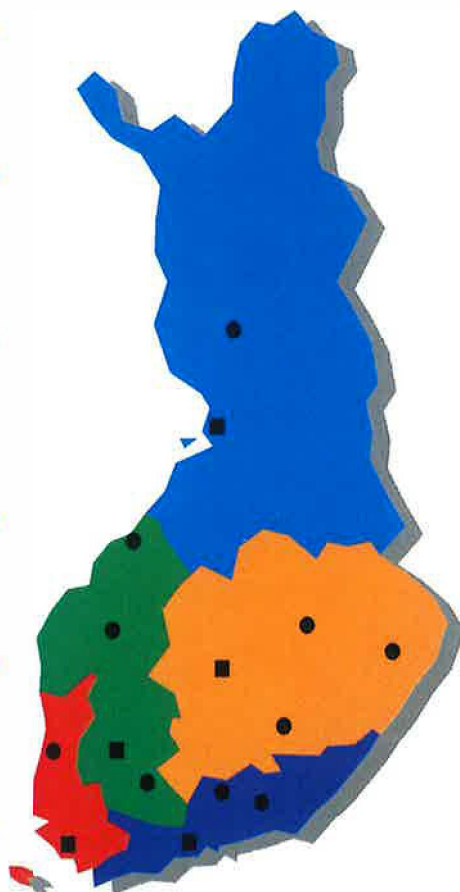


■ Arsenal organisation as at December 31, 1997.



■ Regions and branches January 1, 1998.

- Southern Finland**
 - Regional office Helsinki
 - Lahti ● Kouvola
- Eastern Finland**
 - Regional office Jyväskylä
 - Joensuu ● Kuopio ● Mikkeli
- Western Finland**
 - Regional office Tampere
 - Hämeenlinna ● Kokkola
 - Seinäjoki
- Northern Finland**
 - Regional office Oulu
 - Rovaniemi
- Southwestern Finland**
 - Regional office Turku
 - Pori
- Group Administration**
 - Helsinki



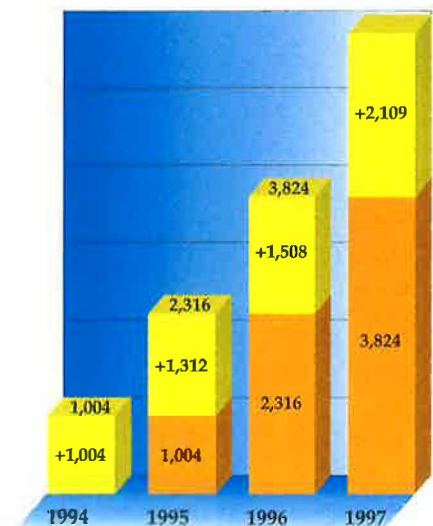
Real Estate



- FIM 2.1 billion in real estate assets sold;
- FIM 0.4 billion in real estate assets purchased;
- Total capital employed in real estate portfolio came to FIM 7.6 billion.
- Rental income amounted to FIM 0.6 billion and the occupancy rate was 70 %.

Total sales of real estate assets during the financial period clearly outstripped the Group's target. The sales targets would have been surpassed even without

■ Disposals of properties between 1994 and 1997, in FIM millions. A total of FIM 2,109 million of which on-balance sheet real estate asset sales were FIM 1,586 million and the sale of the assets pledged as collateral were FIM 523 million.



■ Total sales during the 1997 financial period, MFIM

■ Since the beginning of Arsenal's operations, MFIM

Arsenal's largest single property sale to date: a FIM 531 million transaction closed in December 1997 via Sponda Ltd.

During the 1997 financial period, total sales of real estate assets came to FIM 2,109 million (1,508 MFIM). Of total disposals, real estate asset sales represented FIM 1,586 million (772 MFIM) and assets pledged as collateral FIM 523 million (736 MFIM). The consolidated results for the 1997 financial period include the financial income generated by the subsidiary SKOP-Real Estate Ltd. starting from november 1, 1997.

There were fewer collateralised properties acquired than anticipated, as the total value came to FIM 362 million (525 MFIM). The lesser amount of real estate assets under collection will in turn reduce both sales and acquisitions of collateralised properties in the future.

Of total sales of real estate assets, commercial and office space represented FIM 1,043 million (260 MFIM) and apartment

buildings FIM 265 million (338 MFIM).

The number of single properties representing over FIM 10 million in capital employed was 13 (6). The total capital employed for all these properties was FIM 749 million (83 MFIM).

In December, 1997 Arsenal sold four properties to Sponda Ltd., including the building where the company's head office is located, at Korkeavuorenkatu 45. In connection with this transaction, Arsenal acquired FIM 30 million worth of commercial properties from Sponda Ltd. in the cities of Lahti, Kuopio, and Vantaa.

In September of 1997 Arsenal sold 2,700 leisure time-shares in the holiday resorts of Ylläs, Ruka and Kalajoki. After the transaction, as at December 31, 1997 Arsenal owned a total of 4,400 leisure time-shares, primarily in the Katinkulta and Koli resorts.

Capital gains from the sale of property assets amounted to FIM 117 million (66

MFIM) and capital losses amounted to FIM 214 million (98 MFIM).

CAPITAL EMPLOYED IN THE REAL ESTATE PORTFOLIO: FIM 7.6 BILLION

The total capital employed in the Group's real estate portfolio was FIM 7,563 million (8,195 MFIM). Most of the capital was invested in commercial and office properties, totalling FIM 5,472 million (MFIM 6,121). Capital employed in industrial and storage space amounted to FIM 873 million (747 MFIM) and FIM 652 million (776) was invested in apartment buildings.

Calculated on the basis of capital em-

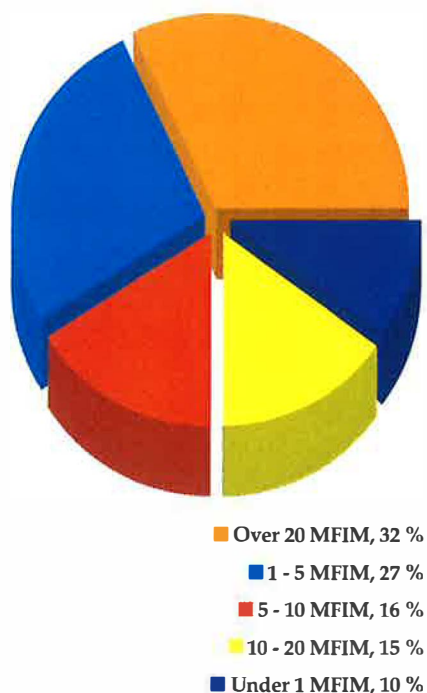
■ Properties bought as collateral on loan receivables between 1994 and 1997, in FIM millions.



■ On-balance sheet real estate asset sales according to use between January 1 and December 31, 1997, number of transactions, in FIM millions. During the 1997 financial period through 1,914 transactions a total of 2,698 properties were sold.

USE	NUMBER OF TRANSACTIONS		FIM	
	1997	1996	1997	1996
Office and commercial	473	395	1,043	260
Industrial and storage	120	88	164	73
Apartments	785	1,056	265	338
Leisure	233	167	42	45
Land	203	109	49	24
Other	100	56	23	32
Total	1,914	1,871	1,586	772

■ Breakdown of the Group's property holdings according to capital employed as at December 31, 1997. The total number of properties for sale 14,814 (15,861).



ployed, 49 percent (51%) of the Group's real estate assets were located in the Helsinki, Tampere and Turku economic regions.

The real estate portfolio was valued to align with the current price levels. Write-downs on real estate assets totalled FIM 295 million (205 MFIM), of which FIM 183 million were from the properties of SKOP-Real Estate Ltd.

In order to improve the efficiency of overall property management, tasks involving real estate administration, purchasing of supplies and elevator maintenance and cleaning services were outsourced via competitive bidding.

RENTAL PRICES INCREASED

The majority of new leases were signed for higher rents than in the previous financial period. The Group's rental income came to FIM 630 million (632 MFIM) despite the decrease in the number of properties in the portfolio. The rental margin (rental income less maintenance expenses) amounted to 3.7 percent (3.5%) of the Group's capital employed in real estate assets.

As at December 31, 1997 Arsenal Group was party to a total of 8,259 lease agreements (8,544). At the end of the financial period, leased floor area amounted to 1.6 million square meters (1.6 million sq.m.) while vacant leasable area amounted to 0.7 million square meters (0.7 million sq.m.). Of the total vacant leasable area, 0.3 million square meters (0.3 million sq.m.) were located in the Helsinki, Tampere and Turku economic areas. The Occupancy rate of the Group's property portfolio was 70 percent (69 %).

PROPERTY DEVELOPMENT

The Hotel Helsinki property development project, which began during the previous financial period, was completed as planned in February, 1997. The building was completely refurbished and 80 new rooms were added. Arsenal's share of the total FIM 60 million renovation costs was FIM 30 million.

Arsenal and the HYY Group made a joint announcement of a project to convert two properties – the one owned by Arsenal and almost all of the other owned by the HYY Group – into a new hotel and restaurant complex in the center of Helsinki. The companies are jointly seeking an operating company to further develop the project.

Both of Arsenal's properties were sold to Sponda Ltd. in December, 1997. Preparations for converting a commercial property in the city of Jyväskylä for residential use commenced towards the end of the financial period. The development work, expected to cost an estimated

■ Total lettable area rented as at December 31, 1997, sq.m. and percent of total lettable area.

USE	RENTED SQ.M.		% OF THE TOTAL LETTABLE AREA	
	1997	1996	1997	1996
Office and commercial	988,086	939,358	74	73
Industrial and storage	373,349	369,977	62	62
Apartments	114,197	137,443	68	64
Other	79,112	103,824	64	65
Total	1,554,744	1,550,602	70	69

FIM 19 million, is scheduled for completion in early 1999.

MARKETING

As in the previous financial periods a promotional campaign called "The Real Estate Calendar" saw branch offices independently organising "Arsenal Open House" marketing and sales days. The Group's property portfolio was on show at the Raisio summer property exhibition. Arsenal's real estate barometers were published in March and September.

During the spring of 1997 the Finnish Gallup Ltd. conducted a market survey by interviewing more than two hundred clients who have either bought or rented an apartment from Arsenal. Those clients indicated that they thought very highly of the professionalism of Arsenal's personnel.

In September of 1997 Arsenal organised a Property Market-2000 seminar for its clients and collaborators. In connection with that seminar, Arsenal published a survey concerning international institutional property investors' interest in the Finish property market. The outcome of the survey indicated that interest is still fairly limited.

In September a free fax service was launched through which potential clients can obtain information on the commercial properties currently for sale. In May a property buyers' guide was opened on Arsenal's Web site.

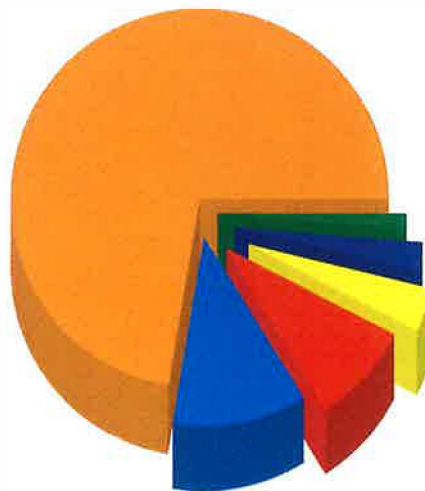
FOCUS FOR 1998

Arsenal will continue to focus its activi-

ties on selling properties. Through property development, active renting and reviewing the business concepts, Arsenal aims to improve its real estate portfolio's occupancy rate and rental yield even further.

Overall property management will be much more efficient after outsourcing real estate administration, supplies purchasing and elevator maintenance and cleaning services. The process, carried out via competitive bidding, is scheduled to be completed towards the end of 1998.

■ **Breakdown of the Group's real estate portfolio according to use as at December 31, 1997. Total capital employed FIM 7,563 million (8,195 MFIM).**



- Office and commercial 5,472 MFIM
- Industrial and storage 873 MFIM
- Apartments 652 MFIM
- Land 281 MFIM
- Leisure 188 MFIM
- Other 97 MFIM

Client-Related Operations



- A total of 8,700 clients represent receivables due to Arsenal of FIM 3.0 billion.
- Receivables due from corporate clients deemed viable: FIM 2.0 billion.
- Clients representing FIM 0.3 billion in liabilities were transferred to the regular banking system.

Clients deemed viable continued to recover during the 1997 financial period, enabling the Group to transfer clients to the regular banking system. The average interest rate received by Arsenal during the financial period rose to 4.3 percent (4.1%) on all receivables. The average interest rate paid by corporate clients classified as viable was 5.7 percent (6.8%).

258 clients (264) representing FIM 277 million worth of receivables (487 MFIM) were transferred to the regular banking system. In addition, 127 clients paid back their loans and ended their client relationship with Arsenal (117).

The clear sign of progress in the winding down of client-related operations was the decline in the number of credit decisions taken. The total number of credit decisions executed during the financial period was 10,200 (13,400).

CREDIT RECEIVABLES DECREASED BY FIM 1.6 BILLION

As at December 31, 1997 the Arsenal Group had a total of 8,680 clients (10,215). Of those, 2,557 (2,938) were private clients. Clients returning to the regular banking system, along with loan amortisations, disposals of assets pledged as collateral and credit losses entered on the books reduced the amount of credit receivables.

Client receivables decreased during the financial period by FIM 1,603 million (2,775 MFIM)

and amounted to FIM 3,007 million (4,610 MFIM), of which private clients re-presented total liabilities of FIM 227 million (328 MFIM).

Of the entire Group's corporate clients, 22 percent (24 %) were classified as viable. Total receivables of those viable corporate clients amounted to FIM 2,048 million (2,788 MFIM), while receivables due from clients to be collected on totalled FIM 732 million (1,494 MFIM).

The Group's credit and guarantee losses were reduced to FIM 307 million (738 MFIM). This reduction of credit and guarantee losses was due to returns on credit losses booked on previous financial periods and credit guarantee payments totalling FIM 293 million (235 MFIM).

REDUCTION IN ASSETS BOUGHT

AS COLLATERAL

Amortisations of client receivables due

from collections and sales of assets pledged as collateral totalled FIM 0.7 billion (1.1 billion). Arsenal assumed responsibility for a less-than-expected amount of assets pledged as collateral, totalling FIM 362 million (525 MFIM).

To make collecting more efficient, the clients in collection were transferred during the summer and autumn of 1997 to the new collection system and collection was concentrated in five regional branches.

The total number of receiverships where in Arsenal is a creditor fell to 1,650 (2,500). The Group's outstandings from receiverships as at December 31, 1997 totalled FIM 0.4 billion (1.0 billion).

THE LOANS AND ADVANCES PORTFOLIO DIMINISHED BY FIM 1.1 BILLION

Loans and advances due fell to FIM 4,161 million (5,210 MFIM) and related contin-

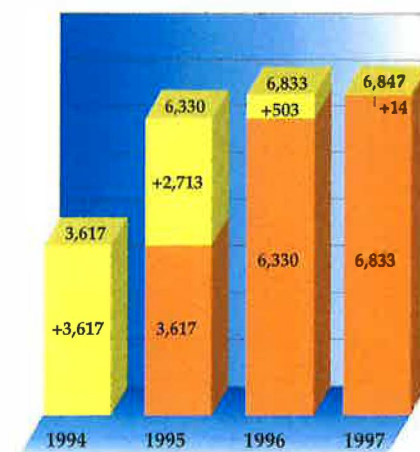
■ Arsenal Group's clients and client receivables, including contingent liabilities by number of clients, in FIM millions.

ARSENAL-GROUP	1997	1996
Clients	8,680	10,215
Receivables due, MFIM	3,007	4,610
Viable		
corporate clients	1,363	1,732
receivables due, MFIM	2,048	2,788
Non-viable		
corporate clients	4,760	5,545
receivables due, MFIM	732	1 494
Private clients		
total	2,557	2,938
receivables due, MFIM	227	328
Non-performing, MFIM	1,294	2,437

■ Arsenal Group's viable clients and client receivables according to business sector as at December 31, 1997 and as at December 31, 1996. Other companies- categories includes independent contractors and private clients.

BUSINESS SECTOR	Clients		Receivables, MFIM	
	1997	1996	1997	1996
Finance	0	1	-	1
Leisure	32	39	80	101
Hotel and restaurant	58	62	107	123
Transport	107	147	180	252
Agriculture and forestry	243	280	186	226
Corporate services	146	159	189	295
Construction	134	204	241	342
Industry	223	313	396	538
Real estate investment	126	117	227	255
Retail and commercial	234	323	383	576
Other companies	60	87	59	79
Total	1,363	1,732	2,048	2,788

■ Group credit and guarantee losses from client receivables during 1994-1997, in FIM millions.



■ Increase during the 1997 financial period, MFIM
 ■ Since the beginning of Arsenal's operations, MFIM

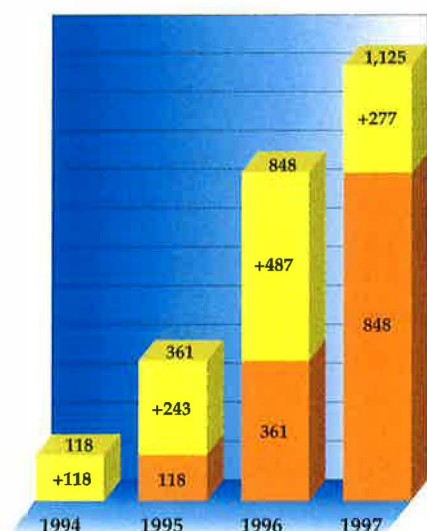
gent liabilities to FIM 206 million (295 MFIM).

Loans and advances due, and related contingent liabilities, will be sold in 1999 to the banks that have managed the portfolios (Merita Bank, Cooperative Banks and Postipankki). Preparations for this transaction commenced during 1997.

■ **Number of clients transferred to the regular banking system.**

	1994	1995	1996	1997
Transfers during the financial period	120	320	264	258
Transfers since the beginning of Arsenal's operations		440	704	962

■ **Client transfers to the regular banking system during 1994-1997, in FIM millions.**



■ Increase during the 1997 financial period, MFIM
 ■ Since the beginning of Arsenal's operations, MFIM

COMPANIES MANAGED BY ARSENAL

As at December 31, 1997 Arsenal Group managed a total of 18 associated or subsidiary companies (16). Of the subsidiaries six (2) were golf course holding companies.

During the financial period the Group sold Kirjapaino Koliprint Ltd., Mäkelän Auto Ltd. and Mäkelän Kone Ltd. and the two subsidiaries of the Uptime Group Ltd., Ekopoint Ltd. and Eino Talsi Ltd. Ownership of the latter two companies was transferred on January 1, 1998. In addition, Stevena Ltd. and Turun Tankki Ltd. were sold. The combined turnover of the companies sold was FIM 163 million and they employed a total of 76 persons.

During the 1997 financial period the Group acquired six (3) operating subsidiaries. Five of these companies were acquired in connection of the acquisition of SKOP-Real Estate Ltd. in October. Arsenal-SSP Ltd.'s shareholding in its associa-

ted company, Ylläs-Ski, Finland Ltd., increased from 33.4 percent to 50.2 percent.

In February of 1998, Arsenal sold Sairaala Lasaretti Ltd., a private hospital company located in the City of Kuopio. Also in that month, Arsenal's subsidiary Uptime Group Ltd. sold its 72 percent holding in Pointo Ltd. and in Pointo Ltd.'s subsidiary company, JTT-Pointo Ltd.

FOCUS FOR 1998

For the current accounting period Arsenal will concentrate actively on increasing the number of clients transferred to the regular banking system. The number of clients in collection will diminish when they qualify for post-collection and the number of receiverships will be reduced.

The earnings of operating subsidiaries will be enhanced as a result of company development programs implemented with a view to selling them.

■ **Arsenal Group's client entities according to size of receivables as at December 31, 1997 and December 31, 1996. Figures do not include credits or guarantees granted by Asset Management Company Arsenal-SSP Ltd to subsidiaries of Arsenal or Arsenal-SSP.**

RECEIVABLES OVER	Client entities		Receivables, MFIM	
	1997	1996	1997	1996
60 MFIM	0	0	-	-
50 MFIM	1	1	53	54
40 MFIM	0	1	-	44
30 MFIM	0	3	-	95
20 MFIM	11	16	264	376
10 MFIM	26	40	341	541
5 MFIM	62	100	431	689
under 5 MFIM	2,468	3,231	1,691	2,483
Total	2,568	3,392	2,780	4,282
Wage-earners and households	2,557	2,938	227	328
Total	5,125	6,330	3,007	4,610

1997 Financial Period

Arsenal's client-related businesses are almost entirely domestic Finnish operations. The major part of Arsenal's real estate assets are also located in Finland. The positive trend in the Finnish business climate, especially with interest rates remaining low, a strong stock market performance and recovering property markets, have contributed to Arsenal's success in reaching its business development goals.

The recovery in the real estate market, already begun during the 1996 financial period continued in 1997 resulting in higher rental levels in new lease contracts and increased property sales. The market trend was particularly positive in large university cities and the outlying economic areas.

The amount of vacant office space in major cities fell to less than six percent, which is almost in line with the regular market situation. In the Helsinki metropolitan area, the vacancy rate in office and industrial spaces was three percent, as a result of higher rent level. In other cities the rent increases have been modest, but in the future there will probably be upwards pressure on for higher rents.

The reduction of vacant office space and higher rents will increase the sales of office properties in 1998 as well as the sales prices.

GOALS FOR THE 1997 FINANCIAL PERIOD

The Arsenal Group posted better-than-anticipated results during its fourth year of operations was better than anticipated. The real estate sale targets were clearly exceeded, more clients than was initially estimated were transferred to the regular banking system and the winding-down of operations progressed according to plan.

During the 1997 financial period the focus on Group's operations shifted more clearly towards the real estate operations. At the end of the financial period almost a half of the Group's assets, FIM 7.6 billion (FIM 8.2 billion) were real estate related. The receivables due from clients ended at FIM 3.0 billion (FIM 4.6 billion), loans and advances totalled FIM 4.2 billion (FIM 5.2 billion) and securities investments amounted to FIM 1.5 billion (FIM 1.5 billion).

A NEW SUBSIDIARY:

SKOP-REAL ESTATE LTD.

On November 5, 1997, Asset Management Company Arsenal Ltd. acquired SKOP-Real Estate Ltd. from Skopbank Ltd. According to the sale agreement Arsenal-SSP Ltd. assumed also the responsibility of for financing of SKOP-Real Estate Ltd., taking it

over from Skopbank Ltd.

SKOP-Real Estate Ltd. was established in 1992 to sell the assets which were pledged as collateral to Skopbank Ltd.. Arsenal's regional organisation facilitates more effective sale of SKOP-Real Estate Ltd.'s geographically spread out real estate assets, leisure and time-shares as well as shares of golf courses.

CHANGES IN THE GROUP'S ORGANISATION

Arsenal's operations and regional organisation were restructured. As at January 1, 1998 Arsenal changed its regional organisation by reducing the number of branch offices from 22 to 15. Arsenal's Group's administrative structure was adapted to match the situation.

In order to sell and develop properties effectively, it is essential to maintain a regional presence where the assets are located. By centralising operations in 15 regional branches Arsenal has secured its expertise on regional property markets and built up an efficient service network.

Due to the above restructuring, the total number of Arsenal's staff personnel will be reduced by 62 persons in the spring of 1998.

Group and Parent Company Results



■ Arsenal's group structure and ownership as at December 31, 1997.

COMPANIES INCLUDED IN THE CONSOLIDATED FINANCIAL STATEMENTS

Losses incurred by the companies included in the consolidated financial statements for the financial period totalled FIM 491 million (1,181 MFIM) and total assets amounted to were FIM 15,176 million (15,801 MFIM).

SKOP-Real Estate Ltd. was made part of the Arsenal Group on November 7, 1997. It's balance sheet items are incorporated in Arsenal's financial statements and it's income statement has been consolidated in the Group's financial statements, beginning on November 1, 1997.

The Arsenal Group comprises a total of 1,098 subsidiaries (1,120) of which 1,057 were commercial or residential property holding companies (1,075). Participations and associated companies totalled 413 (464) of which 405 were real estate holding companies (459).

Companies taken over have not been included in the consolidated financial statements.

THE GROUP'S LOSS FOR THE FINANCIAL PERIOD

The Group's net loss after tax and minority interest for the period ending December 31, 1997 decreased to FIM 117 million

(-1,352 MFIM). The results of the financial period were affected by credit and guarantee losses amounting to FIM 328 million (987 MFIM). The Group's depreciation and write-downs on real estate assets totalled FIM 300 million (209 MFIM). Certain write-downs on assets included in the portfolio of listed shares taken during previous financial periods were able to be reversed, producing a profit on securities trading of FIM 619 million (260 MFIM). The Group's financial expenses were reduced to FIM 438 million (716 MFIM).

THE GROUP'S BALANCE SHEET

The Group's balance sheet total was reduced to FIM 16,322 million (20,254 MFIM) for the year ending December 31, 1997. Guarantees diminished over the financial period to FIM 679 million (1,259 MFIM). The Group's shareholders' equity totalled FIM 4,262 million (4,379 MFIM).

INCOME STATEMENT

NET INCOME FROM FINANCIAL OPERATIONS

The Group's interest income was FIM 497 million (646 MFIM), of which FIM 188 was received from clients (260 MFIM) and FIM 272 million from loans and advances of the parent company Arsenal (360 MFIM). The

decline in interest rates and the winding-down of operations reduced interest expenses which diminished to FIM 438 million (716 MFIM).

The Group's net income from financial operations rose to FIM 59 million (-67 MFIM).

OTHER OPERATING INCOME

The Group's other operating income totalled FIM 1,440 million (987 MFIM). Income from the real estate portfolio amounted to FIM 754 million (702 MFIM), of which capital gains from property sales represented FIM 117 million (66 MFIM). Dividends and fee income totalled FIM 33 million (14 MFIM).

Income on securities trading totalled FIM 619 million (260 MFIM). This figure includes FIM 94 million (12 MFIM) in capital gains on securities sold and FIM 525 million (248 MFIM) of revaluations of earlier write-downs of the value of stock exchange listed shares.

ADMINISTRATIVE EXPENSES

The Group's administrative expenses were FIM 232 million (366 MFIM), of which personnel costs amounted to FIM 160 million (167 MFIM) and other administrative expenses amounted to FIM 72 million (199 MFIM). Of the personnel costs, FIM 11 mil-

lion corresponded to one-off redundancy payments.

OTHER OPERATING EXPENSES

The Group's other operating expenses totalled FIM 743 million (727 MFIM), of which real estate management expenses were FIM 654 million (598 MFIM) and miscellaneous operating expenses were FIM 89 million (129 MFIM). Of the real estate management expenses, FIM 214 million (98 MFIM) were related to losses on disposals of real estate holdings.

The Group's miscellaneous operating expenses include management and collection fees of FIM 37 million (26 MFIM) paid out in connection with loans and advances. Losses on loan claims totalled FIM 8 million (85 MFIM).

DEPRECIATION AND WRITE-DOWNS ON REAL ESTATE ASSETS

The Group's depreciation amounted to FIM 300 million (209 MFIM). Depreciation includes FIM 295 million (205 MFIM) in write-downs on individual properties. Depreciation on machinery and equipment was FIM 3 million (4 MFIM).

CREDIT AND GUARANTEE LOSSES

Credit and guarantee losses, less the income reduced by income received from collections and write-backs of previous provisions, totalled FIM 328 million (987 MFIM). Of the credit and guarantee losses, client receivables represented FIM 14 million (503 MFIM) and loans and advances were FIM 314 million (484 MFIM).

THE GROUP'S BALANCE SHEET

DUE FROM FINANCIAL INSTITUTIONS

The Group's receivables due from financial institutions totalled FIM 4,252 million (6,365

	Arsenal Group		Arsenal	
INCOME STATEMENT HIGHLIGHTS, MFIM	1997	1996	1997	1996
Net income from financial operations	59	(67)	217	140
Other operating income				
Securities trading income	619	260	529	253
Income from real estate portfolio	754	702	-	1
Other	67	25	264	252
Total operating income	1,499	920	1,010	646
Operating expenses				
Personnel costs	160	167	155	162
Real estate management expenses	654	598	12	16
Other	161	328	113	112
Depreciation	300	209	3	4
Credit and guarantee losses	328	987	314	484
Asset revaluations	9	3	526	1,163
Other items	(4)	20	-	23
Loss for the financial period	(117)	(1,352)	(113)	(1,272)

MFIM), of which loans and advances from the banks that acquired the assets and liabilities of the Savings Bank of Finland-SBF Ltd., amounted to FIM 4,161 million (5,210 MFIM).

RECEIVABLES AND GUARANTEES

Loans, guarantees and foreign currency-denominated receivables after loan write-offs declined to FIM 3,859 million (5,119 MFIM). Guarantees diminished to FIM 679 million (1,259 MFIM).

DEBT SECURITIES

Debt securities held totalled FIM 0.3 million (306 MFIM) at the end of the financial period.

SHARES AND PARTICIPATIONS

The book value of the Group's shares and participations increased to FIM 1,515 million (1,234 MFIM). The book value of the equity shares portfolio rose by FIM 525 million (248 MFIM) due to the price increase of shares that had been earlier written-down previously.

REAL ESTATE HOLDINGS, SHARES AND PARTICIPATIONS IN REAL ESTATE COMPANIES

The book value of real estate holdings, shares and participations in real estate companies totalled FIM 6,300 million (6,841 MFIM).

ACCRUED LIABILITIES AND DEFERRED PAYMENTS

Accrued liabilities and deferred payments totalled FIM 167 million (169 MFIM).

FUNDING

The Group's total liabilities totalled FIM 8,084 million (11,861 MFIM). Of the total funding, bond- and debenture-based funding represented FIM 3,200 million (4,987 MFIM). The majority of the funding, FIM 4,434 million (6,145 MFIM), was raised via short-term debt securities issued by Arsenal.

STATUTORY RESERVES

The Group's statutory reserves include an-

ticipated credit losses on loans and advances. It also includes fees and other charges related to the Group's agreements.

The Group's statutory reserves declined to FIM 2,906 million (2,966 MFIM). FIM 33, million corresponding to, write-downs on overvalued acquisition prices and FIM 11, million related to the redundancies are booked under accruals.

MINORITY INTEREST

Group's minority interest totalled FIM 1,070 million (1,048 MFIM). Arsenal-Silta Ltd.'s results, preferred capital loans and other shareholders' equity are booked in consolidated financial statements as minority interest for a total of FIM 992 million (973 MFIM). The minority interest relating to SSP-Service was FIM 78 million (75 MFIM).

SHAREHOLDERS' EQUITY

The Group's shareholders' equity after the results for the 1997 financial period amounted to FIM 4,262 million (4,379 MFIM). The restricted equity of Arsenal Group is FIM 22,800 million (22,800 MFIM) and distributable equity a negative FIM 18,538 million (-18,421 MFIM).

PARENT COMPANY RESULTS

The losses booked by the parent company of the Arsenal Group's loss for the financial period were reduced to FIM 113 million (-1,272 MFIM). The total assets of the Arsenal Group's parent company amounted to FIM 17,561 million (18,711 MFIM).

PARENT COMPANY INCOME STATEMENT NET INCOME FROM FINANCIAL OPERATIONS

Arsenal's net income from financial operations totalled FIM 217 million (140 MFIM).

Interest income was FIM 641 million (753 MFIM) of which FIM 341 million (384 MFIM) derived from financing Arsenal-SSP Ltd. and FIM 272 million (360 MFIM) from loans and advances granted.

	Arsenal Group		Arsenal	
ASSETS, MFIM	1997	1996	1997	1996
Due from financial institutions				
Loans and advances	4,161	5,210	4,161	5,210
Other	91	1,155	81	1,086
Due from clients	3,859	5,119	11,137	10,082
Debt securities	-	306	-	299
Shares and participations	1,515	1,234	2,046	1,889
Intangible assets	1	0		
Tangible assets				
Land and buildings	1,374	1,696	-	-
Real estate shares and participations	4,926	5,145	-	-
Machinery and equipment, other tangible assets	6	10	3	5
Other assets, accruals and deferred payments	389	379	133	140
Total	16,322	20,254	17,561	18,711

	Arsenal Group		Arsenal	
LIABILITIES, MFIM	1997	1996	1997	1996
Liabilities to credit institutions	90	128	88	124
Bonds and debentures	3,149	3,251	3,141	3,110
Subordinated debt	51	1,736		
Asset management company's debt securities	4,434	6,145	4,434	6,145
Other liabilities	360	601	2,842	2,205
Minority interest	2,906	2,966	2,718	2,676
Participations	1,070	1,048	-	-
Shareholders' equity	4,262	4,379	4,338	4,451
Total	16,322	20,254	17,561	18,711

The interest expenses in connection with from funding through the money market declined to FIM 424 million (613 MFIM). Interest expenses in connection with from public securities issues were FIM 348 million (516 MFIM), and on debt related to subsidiary companies, FIM 63 million (70 MFIM).

OTHER OPERATING INCOME

Other operating income totalled FIM 793 million (506 MFIM).

Income from securities trading increased to FIM 529 million (253 MFIM) which includes FIM 3 million (5 MFIM) in capital

gains on securities sold and a FIM 525 million (248 MFIM) from revaluations of previous write-downs on the value of certain listed shares held.

Arsenal manages the administrative functions and operations of its subsidiary company Arsenal-SSP Ltd.'s administration and operations. Arsenal-SSP Ltd. itself does not employ operating personnel. Other operating income of FIM 240 million (239 MFIM) includes a FIM 224 million (232 MFIM) income in management fees that Arsenal charges to Arsenal-SSP Ltd. for managing its operations.

ADMINISTRATIVE EXPENSES

Arsenal's administrative expenses were FIM 205 million (216 MFIM) of which personnel costs amounted to FIM 155 million (162 MFIM) and other administrative expenses of FIM 50 million (54 MFIM). Administrative expenses include redundancy payments of FIM 11 million and operating expenses of FIM 35 million (36 MFIM) from data processing.

OTHER OPERATING EXPENSES

Other operating expenses totalled FIM 75 million (74 MFIM). Operating expenses included management and collection fees in connection with loans and advances as defined in the transfer agreement with the banks that acquired the Savings Bank of Finland - SBF Ltd., totalling FIM 37 million (26 MFIM).

General auditing expenses and special auditing expenses related to the loans and advances and professionals' fees came to FIM 14 million (17 MFIM). Rents for EDP-equipment amounted to FIM 6 million (8 MFIM).

CREDIT LOSSES FROM LOANS**AND ADVANCES**

Credit losses from loans and advances came to FIM 314 million (484 MFIM), considerably lower than the losses of the previous financial period.

WRITE-DOWNS ON SUBSIDIARY**COMPANY SHARES**

Shares in subsidiary companies, represent-

	Arsenal Group		Arsenal	
SHAREHOLDERS' EQUITY MFIM	1997	1996	1997	1996
Restricted equity				
Share capital	3,700	3,600	3,700	3,600
Share issue	-	100	-	100
Restricted reserves	19,100	19,100	19,100	19,100
Total restricted equity	22,800	22,800	22,800	22,800
Distributable equity				
Loss from previous financial periods	(18,421)	(17,069)	(18,349)	(17,077)
Loss for the financial period	(117)	(1,352)	(113)	(1,272)
Total distributable equity	(18,538)	(18,421)	(18,462)	(18,349)
Total shareholders' equity	4,262	4,379	4,338	4,451

ing FIM 596 million (962 MFIM), are valued in the financial statements at the subsidiary's net asset value at the end of the financial period. The total amount of write-downs on Arsenal's shares in its subsidiary companies was FIM 526 million (1,163 MFIM), of which the most significant single write-down was on Arsenal-SSP Ltd.'s shares, amounting to FIM 344 million (1,160 MFIM).

**PARENT COMPANY BALANCE SHEET
DUE FROM CLIENTS**

Arsenal's receivables due from clients of FIM 11,137 million are entirely due from Arsenal-SSP Ltd (10,082 MFIM).

SHARES AND PARTICIPATIONS

Shares in subsidiary companies amounted to FIM 596 million (962 MFIM), and other shares amounted to FIM 1,450 million (927

MFIM). The book value of other shares was increased by FIM 525 million (248 MFIM), corresponding to the increased value price on shares previously written down.

LIABILITIES TO CLIENTS

Arsenal's liabilities to clients, totalling FIM 2,729 million (2,083 MFIM), were entirely due to its subsidiary companies. Liabilities to Arsenal-SSP Ltd. represented FIM 753 million (232 MFIM), to Arsenal-Silta Ltd. FIM 792 million (673 MFIM), to the Mutual Insurance Company of the Savings Bank Ltd. FIM 837 million (880 MFIM), and to SSP-Service FIM 260 million (183 MFIM).

STATUTORY RESERVES

Statutory reserves were increased to FIM 2,718 million (2,676 MFIM).

Share Capital and Ownership

There were no changes in Arsenal's share capital or ownership structure during the 1997 financial period. The Government of Finland owns 78.95 percent of Arsenal's

shares and voting rights and the Government Guarantee Fund owns 21.05 percent. The total number of Arsenal's shares outstanding was 740,000.

Administration *and* Management

Arsenal's Annual General Meeting, held on June 11, 1997 approved the financial statements from the previous financial period and decided that the Board of Directors and the President of the company were discharged from liability for the financial period.

The Annual General Meeting appointed Financial Counsellor Urpo Hautala, Industrial Counsellor Veijo Kauppinen, Bachelor of Science (Econ.) Veli Korpi, Managing Director Gretel Sommar-Bogdanoff, Government Counsellor Auni-Marja Vilavaara and Budget Chief Erkki Virtanen as members of Arsenal's Board of Directors. Mr. Veli Korpi was appointed as the Chairman of the Board and Mr. Veijo Kauppinen as the Vice Chairman.

Arsenal's Board of Directors met 21 times during the 1997 financial period.

Chief Shop Steward Sinikka Leino represents personnel in Arsenal's board meetings. She is entitled to attend and participate in the meetings.

Mr. Seppo Sipola (Bachelor of Science of Economics) continues as Arsenal's Managing Director and his deputy was

■ **Arsenal Board of Directors :** In the second row (from the left) Financial Counsellor Urpo Hautala, Budget Chief Erkki Virtanen, Vice Chairman Industrial Counsellor Veijo Kauppinen and Chairman Veli Korpi. In the first row (from the left) Managing Director Gretel Sommar-Bogdanoff, Government Counsellor Auni-Marja Vilavaara and personnel representative, Chief Shop Steward Sinikka Leino.



Mr. Jukka Räihä (Master of Laws).

Arsenal's Extraordinary Board Meeting, held on February 6, 1998, passed a resolution deciding to change Arsenal's corporate status to that of a public limited company, Plc.

The change was entered in the Finnish Trade Register on March 23, 1998.

ARSENAL'S SUPERVISION AND ACCOUNTS

Arsenal's operations are supervised by Government Guarantee Fund, State Audit Office and State Auditors. The same confidentiality and client protection rules and regulations as those applying to banks apply to Arsenal, Arsenal-SSP Ltd. and Arsenal-Silta Ltd. In matters relating to banking confidentiality and client protection, Arsenal is under the supervision of the Financial Supervision agency.

Parent company Arsenal's auditors are the authorised auditing firms SVH Coopers & Lybrand Oy and Tuokko, Deloitte Touche Ltd. These firms also function as auditors for Arsenal-SSP Ltd. and Arsenal-Silta Ltd. and ordinarily for all other Arsenal Group companies. They also handle the Group's management auditing.

Inspection Committee

At Arsenal's Extraordinary General Meeting, held on December 19, 1996 it was decided to establish an Inspection Committee. The committee has five regular members representing the Finnish Parliament and their three alternate members. It also includes one member from the Ministry of Finance and one

member from both of Arsenal's auditing firms.

The Inspection Committee, appointed in its meeting held on April 16, 1997, appointed Mr. Kari Kantalainen (MP) as the Chairman of the Committee and Mrs. Ulla Juurola (MP) as his Deputy Chairperson. Mr. Klaus Bremer (MP), Mrs. Vuokko Rehn (MP), Mr. Kari Uotila (MP), Mr. Johan Kronberg (Authorised Auditor), Mr. Pertti Sundqvist (Authorised Auditor) and Mr. Yrjö Tuokko (Authorised Auditor) were appointed as members of the Committee. Mr. Matti Ryhänen (MP), Mr. Erkki Pulliainen (MP) and Mr. Janne Viitamies (MP) were appointed as deputy members of the Committee.

The Inspection Committee met 11 times during the financial period and it submitted a statement to the Ministry of Finance on December 8, 1997 concerning Arsenal's and Arsenal-Silta Ltd.'s decision making relating to claims.

LAWSUITS

In addition to the ordinary lawsuits related to the collections, the Group was both a plaintiff and defendant in approximately 190 other lawsuits (200). These lawsuits are principally in connection with the disagreed credit and guarantee liabilities related to the collections of receivables and to the special audit, based on the law concerning the Government Guarantee Fund, performed in 1993.

The economic consequences of the lawsuits have been provided for in the statutory reserves.

Personnel

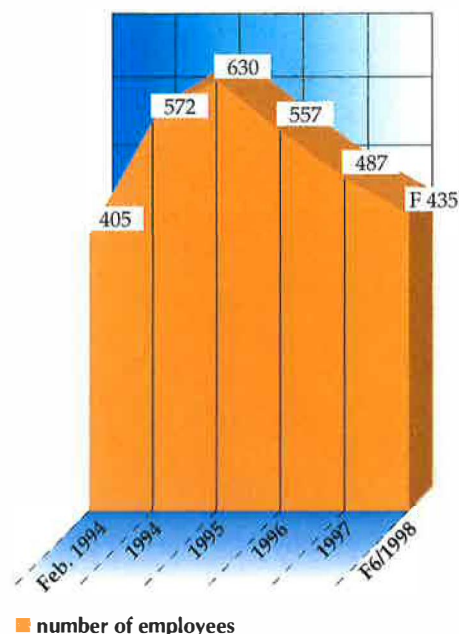
As at December 31, 1997 Arsenal employed a total of 547 (590) persons. Co-determination negotiations were conducted during the fall of 1997 concerning the new organisational plan's impact on the personnel. The

negotiations commenced on September 25, 1997 and ended on November 25, 1997. As a result of the negotiations Arsenal's personnel was reduced by 62 persons.

■ The number of Arsenal's employees between 1994 - 1997 and forecast for June 30, 1998.

■ Arsenal's average personnel and salaries paid, broken down divided by business sectors

BUSINESS SECTOR	PERSONNEL	MFIM
Client-related operations	217	42
Real estate	146	27
Other	186	41
Total	549	110



Future Outlook

General trends in the Finnish economy, in particular the more buoyant real estate market conditions and interest rate fluctuations, will have a significant impact on the value of the assets and loan guarantees as well as performances in the stock market.

The 1997 loss was reduced by capital

gains from share disposals and higher prices for shares previously written down. For the 1998 financial period there will be no such exceptional income, therefore a higher loss is expected in 1998, but this is in line with Arsenal's long-term goals. Credit losses and write-downs will decrease substantially from the previous fi-

nancial period. The business plan incorporates write-downs and credit losses for approximately FIM 0.3 billion. Total assets, as per the Group's balance sheet and factoring in contingent liabilities, are expected to decrease by approximately FIM 3 billion to a total of FIM 14 billion.

INCOME STATEMENT AND BALANCE SHEET

ARSENAL GROUP - CONSOLIDATED INCOME STATEMENT

Exchange rate USD 1 = FIM 5.4207 as at December 31, 1997

FIM millions

	December 31, 1997		December 31, 1996	
Interest income				
From financial institutions and Bank of Finland	2		6	
From loans and advances	272		360	
From clients	188		260	
From debt securities	26		7	
Other interest income	9	497	13	646
Net leasing Income		-		3
Interest expenses				
To financial institutions and Bank of Finland	13		40	
To clients	24		26	
On public debt instrument issues	349		530	
On subordinated debt	51		116	
Other interest expenses	1	438	4	716
NET INCOME FROM FINANCIAL OPERATIONS		59		-67
OTHER OPERATING INCOME				
Dividend income		21		1
Fee income and expenses		12		13
Securities trading income		619		260
Income from foreign exchange operations		0		0
Income from other operations				
Real estate portfolio	754		702	
Other	34	788	11	713
TOTAL OPERATING INCOME		1,499		920
OPERATING EXPENSES				
Administrative expenses				
Personnel costs				
Salaries	124		124	
Pension payments	14		21	
Social expenses	10		10	
Other personnel costs	12	160	12	167
Other administrative expenses		72		199
		232		366
Depreciation		300		209
Other operating expenses				
Real estate management expenses	654		598	
Miscellaneous operating expenses	89	743	129	727
Credit and guarantee losses		328		987
Asset revaluations		9		3
OPERATING LOSS		(113)		(1,372)
Extraordinary income		-		14
LOSS BEFORE APPROPRIATIONS AND TAXES		(113)		(1,358)
Direct taxes				
Taxes for the current financial year and from previous financial years		0		3
Minority interest		(4)		3
LOSS FOR THE FINANCIAL PERIOD		(117)		(1,352)

INCOME STATEMENT AND BALANCE SHEET

ARSENAL GROUP - CONSOLIDATED BALANCE SHEET

Exchange rate USD 1 = FIM 5.4207 as at December 31, 1997

FIM millions

	December 31, 1997		December 31, 1996	
ASSETS				
Cash in hand		0		0
Due from financial institutions and Bank of Finland				
From Bank of Finland		-		-
From financial institutions	91		1,155	
Loans and advances	4,161	4,252	5,210	6,365
Due from clients				
Loans	3,196		3,872	
From guarantees	487		807	
From foreign currency denominated loans	176	3,859	440	5,119
Leasing assets				0
Debt securities		0		306
Shares and participations				
Subsidiaries	22		17	
Associated companies	4		2	
Shares and participations	1,489	1,515	1,215	1,234
Intangible assets				
Other intangible assets		1		0
Tangible assets				
Land and buildings				
In own use		-	50	
Other	1,374		1,646	
Real estate shares and participations				
In own use	58		92	
Other	4,868		5,053	
Machinery and equipment	5		7	
Other tangible assets	1	6,306	3	6,851
Other assets		222		210
Accrued and deferred payments				
Accrued Interest	55		78	
Other	112	167	91	169
		<u>16,322</u>		<u>20,254</u>

INCOME STATEMENT AND BALANCE SHEET

ARSENAL GROUP - CONSOLIDATED BALANCE SHEET

Exchange rate USD 1= FIM 5.4207 as at December 31, 1997

FIM millions

	December 31, 1997		December 31, 1996	
LIABILITIES AND SHAREHOLDERS EQUITY				
Liabilities				
To banks and Bank of Finland				
Due on demand	-	-	-	-
Other	90	90	128	128
To clients		77		89
Debt instrument public issues				
Bonds and debentures	3,149		3,251	
Other	4,434	7,583	6,145	9,396
Other liabilities		86		134
Accrued and deferred liabilities				
Accruals due	32		148	
Other	165	197	230	378
		8,033		10,125
Statutory reserves		2,906		2,966
Subordinated debt liabilities		51		1,736
Minority interest		1,070		1,048
Shareholders' equity				
Restricted equity				
Share capital	3,700		3,600	
Share issue	-		100	
Restricted reserves	19,100	22,800	19,100	22,800
Distributable equity				
Loss from previous financial year	(18,421)		(17,069)	
Loss for the financial year	(117)	(18,538)	(1,352)	(18,421)
		4,262		4,379
		16,322		20,254
OFF-BALANCE SHEET ITEMS				
Commitments on behalf of customers				
in favour of the third part				
Guarantees pledged as collateral		444		938
Loans and advances		206		295
Irrevocable commitments				
in favour of customers		17		15
		667		1,248

Accounting Principles

The following accounting principles apply to the financial statements of the parent company Arsenal Ltd., Arsenal-SSP Ltd., Arsenal-Silta Ltd. and SKOP-Real Estate Ltd. and to the consolidated financial statements. The parent company Arsenal Ltd. and its subsidiaries Arsenal-SSP Ltd. and Arsenal-Silta Ltd. are asset management companies in the sense as stated in the law concerning the Government Guarantee Fund.

GENERAL ACCOUNTING PRINCIPLES

According to the exemption granted by the Accounting Board, the financial statements of the Asset Management Company Arsenal Ltd. and its subsidiaries Asset Management Company Arsenal-SSP Ltd. and Asset Management Company Arsenal-Silta Ltd. are drawn up and presented in accordance with bookkeeping and accounting regulations concerning financial institutions and as stated in the Financial Supervision regulations. Some of the financial items in the balance sheet and income statement have been adopted to correspond to the specific nature of Arsenal's activities.

Due to the fact that in the 1997 financial period Arsenal Group did not have any derivative instruments or foreign currency items the corresponding accounting principles are not included herein.

The financial statements of the subsidiaries are included in the consolidated financial statements in accordance with the accounting principles applied to the parent company. For items where the practices differ from the practices applied to the Group, the necessary adjustments in the

consolidated statements are based on the principle of material significance. The income statement's income and expenses are recognised as earned or as incurred and entered on an accrual basis.

SCOPE OF THE CONSOLIDATED FINANCIAL STATEMENTS

The consolidated financial statements of Arsenal Group include the financial statements of the parent company Arsenal Ltd., and of those subsidiaries and associated companies owned directly or indirectly by it.

Companies acquired as collateral for lending, and companies in the process of liquidation or receivership are not included in the 1997 consolidated financial statements. However, the major companies are listed under the financial notes in Arsenal's 1997 annual report in Finnish.

The financial results of the merged subsidiaries are included in the consolidated financial statements, taken from the financial statements of the merged subsidiaries. The consolidation of subsidiary companies in collection or receivership was ended in the beginning of the financial period and the net differences result between the acquisition prices and corresponding shareholders' equity has been booked in the results of current and previous financial periods.

CONSOLIDATION

The financial statements of the Group's companies are consolidated item by item. The subsidiary companies' financial statements have been adjusted to align with apply the same accounting standards

applied to the parent company.

Consolidated financial statements have been prepared according to the acquisition methods of accounting.

The income statements of Asset Management Company Arsenal-Silta Ltd., which was incorporated as Arsenal's subsidiary as from November 16, 1995, is not included in the 1995, 1996 and 1997 consolidated financial statements. However, the balance sheet items of Asset Management Company Arsenal-Silta Ltd. are included in the consolidated financial statements.

According to the agreements on the acquisition of Asset Management Company Arsenal-Silta Ltd., its preferred share certificates, net results and other distributable equity have been treated as minority interests.

As from November 1, 1997 SKOP-Real Estate Ltd. has been included in Arsenal's consolidated financial statements.

The fact that not all the subsidiary companies' financial statements are included in the consolidated financial statements has no major impact on the Group's operating results nor on its financial position.

INTEREST INCOME AND EXPENSES

A receivable is considered to be non-performing when its interest or principle is overdue by 90 days. A receivable originating from a guarantee is considered non-performing when a payment is made under such a guarantee. The interest accrued and unpaid on non-performing loans is cancelled when the receivable has been classified as non-performing.

OTHER OPERATING INCOME

Real estate and other operating income is entered when earned or accrued. Rental income is valued at its estimated future value.

The positive or negative difference between the sales price and the book value of the shares and participations is entered as securities trading income (income from the sales of shares and participations). The difference between the book value of the above mentioned securities and probable lower market value at the closing of the financial statements has been deducted from this income. If the market value of the shares and participations is higher than the book value, then it is included as income, but only up to the acquisition price of the shares and the participations.

PENSION AGREEMENTS

Pension schemes for employees of Arsenal Ltd. are arranged through a group insurance scheme. The Group's pension liabilities are fully covered.

EXPENSES FOR LAWSUITS

The anticipated expenses incurred as a result of these liabilities have been provided for in the statutory reserves. Based on agreements, the banks that acquired the Savings Bank of Finland - SBF Ltd. operations, are responsible for 20 percent of the greater-than-anticipated special audit expenses.

DEPRECIATION

The depreciation schedules of Arsenal Group companies have been made in accordance with depreciation policies ba-

sed on the estimated useful life of the assets. Real estate companies are not consolidated. Depreciation of assets of real estate companies is not entered according to the specific depreciation plan.

CREDIT AND GUARANTEE LOSSES

Realised and expected credit and guarantee losses are applied against receivables. A probable credit loss is charged against receivables when it is evident that the principal will not be repaid and the item is classified by client. These credit losses are deducted from receivables.

Realised credit losses from loans and advances are entered and deducted from the corresponding item. The expected credit losses, based on the reports from the banks that acquired the activities of the Savings Bank of Finland-SBF Ltd., are provided for in the statutory reserves. Items provided for in the statutory reserves are not directly deducted from loans and advances.

The net difference between outstanding receivables and the value of collateral securing those receivables is stated as credit and guarantee losses. The assets used as collateral are valued at the expected selling price.

TAXES

Direct taxes are recognised as incurred. Provisions have been set aside in the statutory reserves against Taxes incurred before October 22, 1993, relating to the Savings Bank of Finland - SBF Ltd. and its subsidiary companies.

TRANSFERABLE SHARES

Transferable shares held as investment as-

sets are valued at the lower of cost or market value.

SHARES OTHER THAN TRANSFERABLE SHARES

Shares other than transferable shares are valued at cost. Where the expected selling price is permanently lower than cost, the difference is deducted as an expense.

Subsidiary company shares are valued in Group's financial statements at the subsidiary's net asset value at the end of the financial period.

STATUTORY RESERVES

Statutory reserves cover future expenditure to which the Group's companies have committed themselves and which is not expected to yield corresponding income, and specific future losses that are considered evident. Statutory reserves are also provided against expected credit losses on loans and advances.

PROPERTY ASSETS REVALUATIONS

Permanent and substantial write-downs on properties and property holding companies are recorded as expenses under depreciations.

Write-downs are considered substantial if the difference between market price and book value is more than 20 percent. When evaluating the performance of write-downs, the property classification method and the estimated carrying time of each individual property are taken into consideration.

Proposal of the *Board of Directors*

Loss from the previous financial year	FIM	(18,349,402,007.41)
Loss for the financial year	FIM	(112,674,920.39)
Distributable equity	FIM	(18,462,076,927.80)

Given the year's negative results and the level of distributable equity from previous years, no dividends will be distributed. We propose that the loss for the year will be covered out of distributable shareholders' equity.

Helsinki, March 4, 1998

Veli Korpi
Chairman

Veijo Kauppinen
Vice Chairman

Urpo Hautala

Gretel Sommar-Bogdanoff

Auni-Marja Vilavaara

Erkki Virtanen

Seppo Sipola
President and CEO

Auditors' report

To the shareholders of Asset Management Company Arsenal Ltd.

We have audited the accounting, the financial statements and the corporate governance of Asset Management Company Arsenal Ltd. for the period of January 1, 1997 - December 31, 1997. The financial statements, which include the report of the Board of Directors, consolidated and parent company income statements, balance sheets and notes to the financial statements, have been prepared by the Board of Directors and the Managing Director. Based on our audit we express an opinion on these financial statements and on corporate governance.

We have conducted the audit in accordance with Finnish Standards on Auditing. Those standards require that we perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit includes examining on a test basis evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by the management as well as evaluating the overall financial statement presentation. The purpose of our audit of corporate governance is to examine that the members of the Board of Directors and the Managing Director have legally complied with the rules of the Companies Act.

In our opinion the financial statements, which state a loss of FIM 112,674,920.39 for the parent company and a loss of FIM 117,315,580.45 for the Group have been prepared in accordance with the regulations of the Accounting Act and other rules and regulations governing the preparation of financial statements.

The financial statements give a true and fair view as defined in the Accounting Act, of both the consolidated and parent company's operating results as well as of the financial position. The receivables and the contingent liabilities in the consolidated financial statements contain uncertainty due to the clients' financial situation as well as the deficit in the value of the collateral pledged as security in connection with the receivables.

The developments in the general economic climate, the level of interest rates and the value of real estate, as well as the development of clients' financial situation, are factors of substantial significance to the financial position of the company.

The financial statements with the consolidated financial statements can be adopted and the members of the Board of Directors and the Managing Director can be discharged from liability for the period audited by us.

The proposal by the Board of Directors concerning the appropriation of the loss for the financial year is in compliance with the Companies' Act.

Helsinki, March 5, 1998

Tuokko Deloitte & Touche Ltd
Authorised Public Accountants

Yrjö Tuokko
Authorised Public Accountant

SVH Coopers & Lybrand Oy
Authorised Public Accountants

Johan Kronberg
Authorised Public Accountant

Board of Directors *and* Auditors

■ Board of directors

CHAIRMAN

Mr. Veli Korpi
Bachelor of Science (Econ)

VICE CHAIRMAN

Mr. Veijo Kauppinen
Industrial Counsellor
Ministry of Trade and
Industry

MEMBERS

Mr. Urpo Hautala
Financial Counsellor
Ministry of Finance
Mrs. Gretel Sommar-Bogdanoff
Managing Director
Tammet Tuotanto Oy
Mrs. Auni-Marja Vilavaara
Government Counsellor
Prime Minister's Office
Mr. Erkki Virtanen
Budget Chief
Ministry of Finance

■ Auditors

SVH Coopers & Lybrand Oy
Authorised Public
Accountants
Tuokko, Deloitte & Touche Ltd
Authorised Public
Accountants

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- This document, prepared for the international business community, is an adaptation of Arsenal's 1997 annual report in Finnish.
- In the event of conflict in interpretation, reference should be made to the Finnish version of this report, which is the official text.

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ARSENAL plc

