1Q2020 Financial Results

6 May 2020

islandsbanki.is

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This is Íslandsbanki

Moving Iceland forward by empowering our customers to succeed

Vision and Values

Vision to be
#1 for service

Passion
Professionalism
Collaboration

The Bank

FTEs
746
Parent company end of March 2020

14 Branches

Market share[1]

31%	Personal banking
35%	Business banking
34%	Corporate and investment banking

Sustainability

Environment	**1.62** CO_2tn	Carbon emission per employee
Social	**1.14%**	Gender pay gap
Governance	**67%**	of women chairing committees at board level

Key Figures 1Q2020

ROE	**-3.0%**	LCR Group, all currencies	**177%**
Cost to income ratio	**62.9%**	NSFR Group, all currencies	**120%**
Total capital ratio	**21.9%**	Leverage Ratio	**13.5%**
Tier 1 capital ratio	**19.2%**	Total assets	ISK **1,256bn**

Ratings and certifications

S&P Global Ratings
BBB/A-2
Stable outlook

EQUAL PAY CERTIFICATE 2018 - 2021

EXEMPLARY IN CORPORATE GOVERNANCE

Digital milestones in 1Q2020

- Digital onboarding to securities trading
- Mortgages refinancing now digital
- Electronic signatures available
- Increased use of digital solutions in COVID-19 period

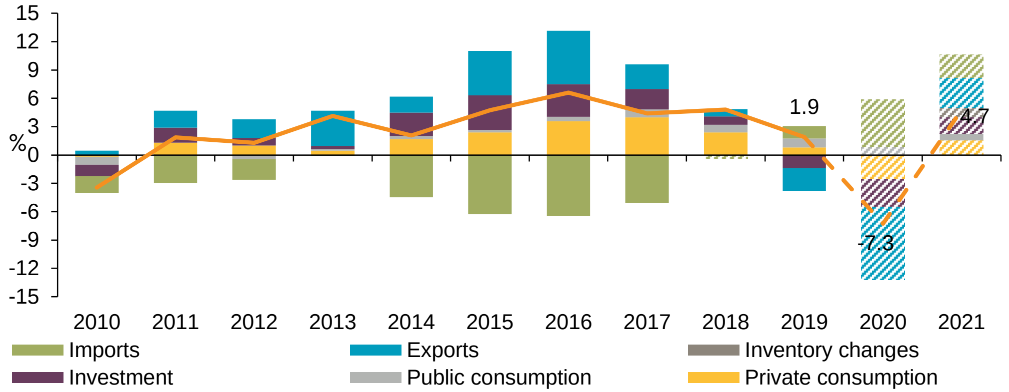
1. Based on Gallup surveys regarding primary bank

1. COVID-19 impact

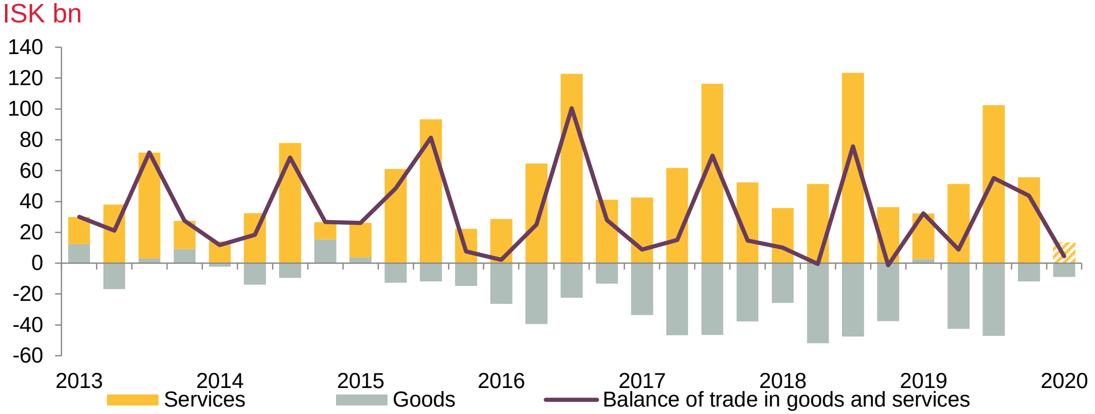
Pandemic impact will cause a recession in 2020

But a V-shaped recovery is probable

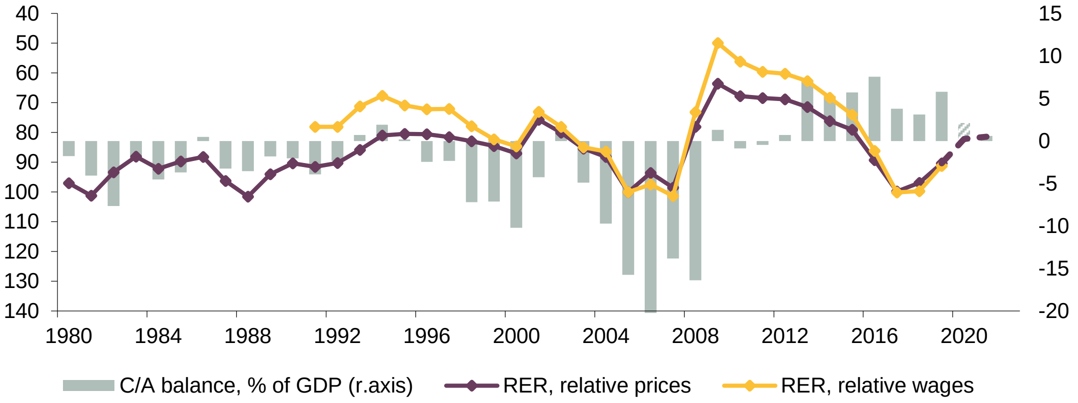
The economic impact of COVID-19 on GDP will be deep in 2020…



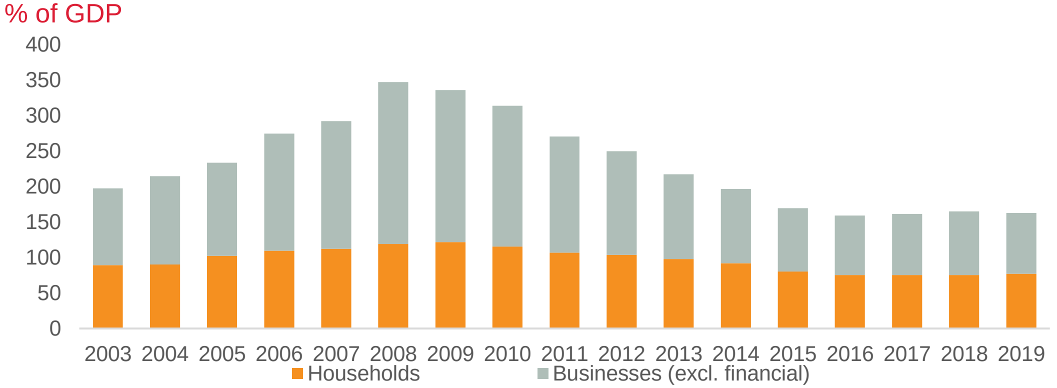
…although the trade balance could prove resilient in the medium term



A lower real exchange rate will facilitate export sector recovery..



…and moderate private sector debt has increased economic resilience



Shaded areas indicate ISB Research/ forecasts
Source: Statistic Iceland and ISB Research

COVID pandemic in Iceland

Declining number of cases a result of extensive and early measures by authorities

Main measures taken[1]

- Quarantine requirements
  - >19,000 people completed quarantine
  - 57% of diagnosed already in quarantine
- Ban on larger gatherings (20 person limit)
- University and upper secondary school-closures. Limited opening of elementary schools and preschools
- Active communication with the general public, including daily press briefings

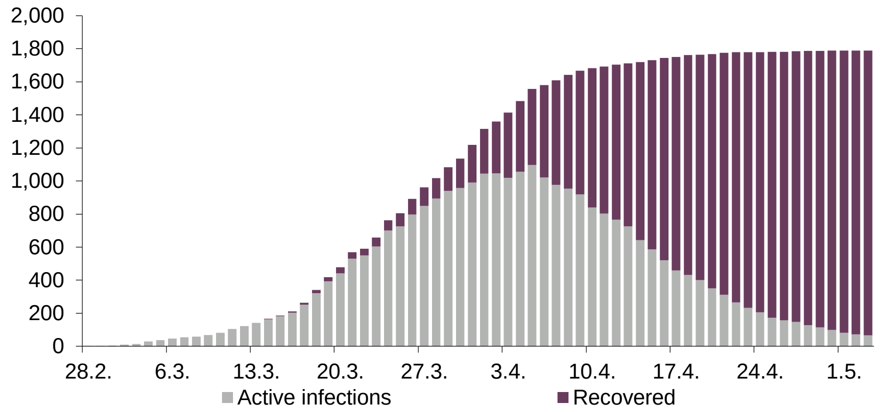
Large scale testing

- On average 813 test per day
- >50,000 samples, around 14% of the Icelandic nation
- >95% infection tracing rate and a tracing app to analyse individuals' travel in case of infection

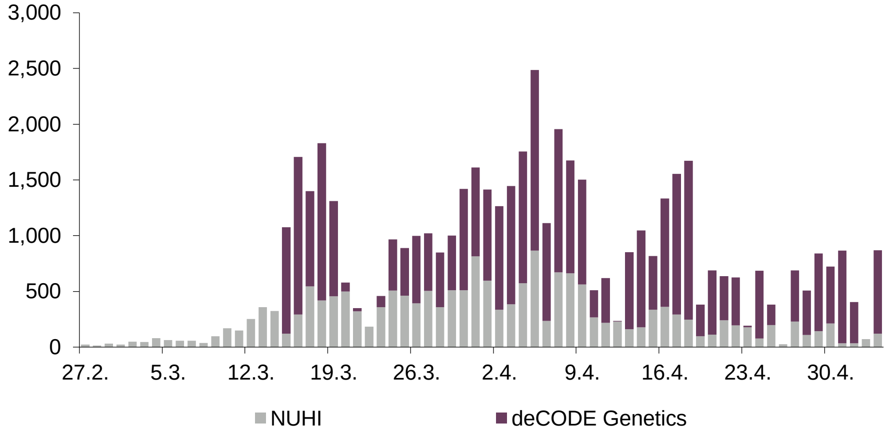
Ease of limitations at 4 May 2020

- 50 person gathering limit
- Schools open and more services available

Number of active infections and number of recovered



Number of tests per day[2]



1. Source: https://www.covid.is/english
2. NUHI: The National University Hospital of Iceland

Official actions to counteract COVID-19

The Government and the Central Bank have taken broad responses to counteract COVID-19

Government actions - individuals

- Wages ensured during quarantine
- Partial unemployment benefits enabling companies to maintain employment until 31 August
- Access to third-pillar pension savings
- Special child benefits
- Increased and expanded reimbursement of value-added tax on labour

Government actions - corporates

- Deferral of pay-as-you-earn (PAYE) tax and payroll tax
- Corporates who fulfil certain requirements will be able to defer certain taxes, levies and loan payments for up to six months
- Guarantees for up to 70% of new operating loans and up to ISK 6m to companies fulfilling certain conditions. The Treasury's total exposure to risk from these loans could range up to ISK 35 billion
- Bank tax reduced to 14.5 basis points from 31.8 basis points
- Pay of salary costs during notice period if revenue loss >75%

Central Bank's actions

- Countercyclical buffer lowered from 2% to 0%
- Base rate lowered from 3.0% to 1.75% during the year
- Temporary back-stop liquidity facility
- Reserve requirements lowered from 1% to 0%
- Direct purchases of Treasury bonds in secondary market start in May
- Treasury guarantees of credit institutions' supplemental lending to businesses in response to COVID-19

Revitalising the economy

- Increased public investment
- Simplified rules on financial restructuring of businesses
- Measures to support the tourism industry
- Increased investments in innovation and higher reimbursement for research and development

1. Source: Government of Iceland – see see announcements from 21 March, 21 April and 28 April
2. Source: Central Bank of Iceland – see here

Íslandsbanki's actions to support customers

The Bank has acted extensively to support clients and employees through COVID-19

Actions for private customers

- Improved digital solutions, e.g. electronic documents
- Phone advisory with bookable hours
- Special support for senior customers
- Deferral of payments of principal and interests of loans
- More than 1000 applications for deferral of mortgages loans approved, about 8% of number of mortgages. Reply within same day
- Enabler of access to 3rd pillar pension savings, about 1300 applications signed
- Short term lending available
- Education to help support our community

Actions for corporate customers

- Suspension of repayments and interests on loans for up to six months is available. This is in line with agreement between financial institutions and SFF (Icelandic Financial Services Association)
- Increased focus on proactively contacting customers to offer advice, conversation and solutions to challenges arising for corporate customers
- Electronic signatures have enabled quicker service and limited visits to branches as well as support offered to navigate via digital channels
- An early allocation from the Bank´s Entrepreneur Fund which is guided by the four UN SDGs it has chosen to support in its policy

Impact on Íslandsbanki

Business continues via remote work but impact mostly through higher impairments

Business continuity

- Branches have been closed except for matters of urgent importance but will reopen on 11 May
- 85% of employees have worked from home
- Technically the Bank was well prepared for remote working environment
- Survey shows that 92% of employees adjust well to new ways of working
- Frequent communication to employees
- Offices and branches cleaned more thoroughly and frequently
- Business continuity plans and epidemic plan in place and of good use

P&L

- Profit is impacted by negative impairment amounting to ISK 3.5bn mainly as tourism industry is moved to IFRS 9 stage 2 and loss in the banking book[1)]
- Decrease in NFCI due to less card- and currency exchange activity
- The Bank experienced losses in both the trading book and banking book for equity and equity like instruments

Capital and funding

- Capital ratios at similar levels compared to year-end 2019 and higher liquidity ratios
- The strength of the Bank´s foreign currency liquidity ratios has meant that liability management exercises have been feasible
- The annual AGM approved that dividend should not be paid in light of COVID-19 uncertainties. A shareholder meeting may be convened later this year where a proposal of payment of dividend could be suggested

1. For further information on impairment on financial assets see Note 2 in the interim financial statements

2. 1Q2020 highlights

Operational highlights

High satisfaction for corporate customers, three new board members and Tesla agreement

Agreement signed to sell 63.5% of share in Borgun hf.
Borgun hf. is classified as disposal group held for sale in the interim financial statements. Comparative figures in the income statement have been restated. The transaction is subject to the Central Bank's approval

Íslandsbanki's Annual General Meeting (AGM) was held 19 March. Flóki Halldórsson, Frosti Ólafsson and Guðrún Þorgeirsdóttir were elected as new members of the Board

Ergo and Tesla have signed an agreement where Ergo is Tesla's preferred partner. This supports the Bank's environmental protection policy and climate action

Íslandsbanki's Corporate Finance led the sale of Icelandair Group's 75% share in Icelandair Hotels

Satisfaction among corporate customers measured at a decade high in 1Q20

S&P lowered Íslandsbanki's rating to BBB/A-2 with a stable outlook from previous BBB+/A-2 with a negative outlook in late April 2020

Digital solutions in 1Q2020

Three new solutions released - make customers daily banking activities easier than ever

Mortgages refinancing

2x

Faster response

Customers can compare different loan options, apply and track their status via digital solution anytime and anywhere in a quick process.
All refinancing of mortgages now goes through this process.

Onboarding to securities trading

69%

Increase in sales (QoQ)

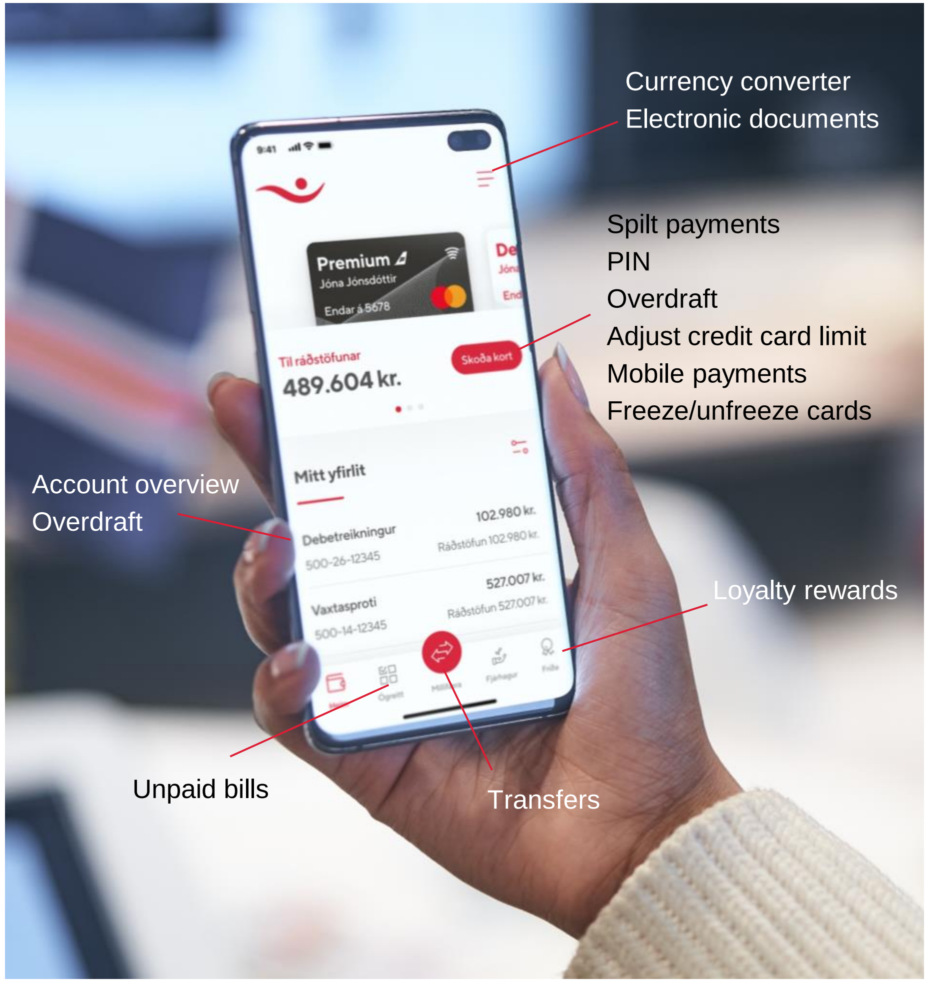
Private and corporate customers can onboard themselves to securities trading and start trading online in a fully automated solution.

Electronic signatures

~6,500

Customers used solution and thereby decreased branch visits

Enables signing of pdf documents in non-digital processes.



Overview
Key figures & ratios

		1Q20	4Q19	3Q19	2Q19	1Q19
PROFITABILITY	Return on equity (after tax)	**-3.0%**	3.7%	4.7%	4.9%	5.9%
	Net interest margin (of total assets)	**2.8%**	2.7%	2.7%	2.8%	2.7%
	Cost to income ratio[1]	**62.9%**	62.9%	56.3%	56.5%	59.6%
	After tax profit (loss), ISKm	**(1,376)**	1,659	2,086	2,120	2,589
		31.3.2020	31.12.2019	30.9.2019	30.6.2019	31.3.2019
BALANCE SHEET	Total assets, ISKm	**1,255,691**	1,199,490	1,233,855	1,229,976	1,205,228
	Loans to customers, ISKm	**923,850**	899,632	909,175	894,446	873,530
	Risk exposure amount, ISKm	**911,375**	884,550	912,843	911,784	886,901
	Deposits from customers, ISKm	**647,795**	618,313	610,281	615,869	611,303
	Customer loans to customer deposits ratio	**142.6%**	145.5%	149.0%	145.2%	142.9%
LIQUIDITY	Liquidity coverage ratio (LCR)	**177%**	155%	174%	185%	158%
	Net stable funding ratio (NSFR)	**120%**	119%	117%	117%	115%
CAPITAL	Total equity, ISKm	**179,542**	180,062	177,984	175,784	173,621
	Tier 1 capital ratio	**19.2%**	19.9%	19.0%	18.8%	19.1%
	Total capital ratio	**21.9%**	22.4%	21.4%	21.4%	20.9%
	Leverage ratio	**13.5%**	14.2%	13.6%	13.4%	13.5%

1. Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund – One off items) / (Total operating income – one off items).

3. Income statement

Strong growth in NII and admin expense decreases[1]

Negative net impairments main cause for lower profits in the quarter

ISKm	1Q20	1Q19	Δ	4Q19	Δ	2019
Net interest income	**8,580**	7,937	643	8,291	289	32,822
Net fee and commission income	**2,491**	2,647	(156)	2,945	(454)	10,899
Net financial income (expense)	**(1,738)**	442	(2,180)	(840)	(898)	(820)
Net foreign exchange gain (loss)	**55**	(121)	176	116	(61)	139
Other operating income	**19**	1,141	(1,122)	920	(901)	2,125
Total operating income	**9,407**	12,046	(2,639)	11,432	(2,025)	45,165
Salaries and related expenses	**(3,247)**	(3,464)	217	(3,624)	377	(14,019)
Other operating expenses	**(2,445)**	(2,749)	304	(2,823)	378	(10,469)
Administrative expenses	**(5,692)**	(6,213)	521	(6,447)	755	(24,488)
Contribution to the Depositor's and Investors' Guarantee Fund	**(228)**	(312)	84	(216)	(12)	(936)
Bank tax	**(359)**	(880)	521	(814)	455	(3,528)
Total operating expenses	**(6,279)**	(7,405)	1,126	(7,477)	1,198	(28,952)
Profit before net impairment on financial assets	**3,128**	4,641	(1,513)	3,955	(827)	16,213
Net impairment on financial assets	**(3,490)**	(907)	(2,583)	(1,463)	(2,027)	(3,480)
Profit before tax	**(362)**	3,734	(4,096)	2,492	(2,854)	12,733
Income tax expense	**(769)**	(1,196)	427	(659)	(110)	(3,909)
Profit (loss) for the period from continuing operations	**(1,131)**	2,538	(3,669)	1,833	(2,964)	8,824
Discontinued operations, net of income tax	**(245)**	51	(296)	(174)	(71)	(370)
Profit (loss) for the period	**(1,376)**	2,589	(3,965)	1,659	(3,035)	8,454

Highlights

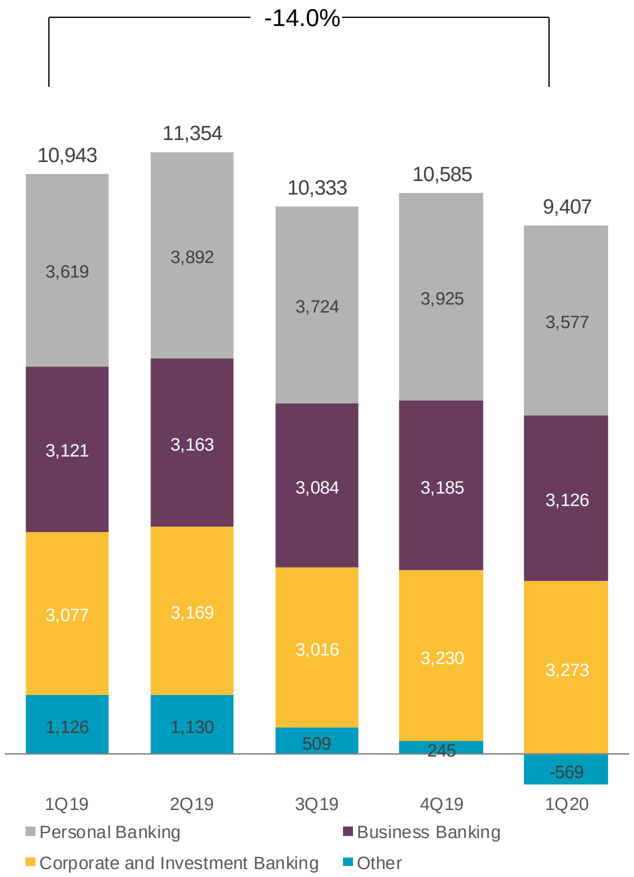
- Total income decreased by 21.9% between years as a result of loss in net financial income
- Interest income rose by 8.1% between years explained by continued loan growth
- Net fee income showed a 5.9% decrease year on year as a result of less card and currency exchange activity and higher cost related to cards in the quarter
- Net financial loss due to loss in trading and banking books for equity and equity like instruments
- Decrease in other operating income as income in 1Q19 was settlement of a claim relating to the acquisition of Byr and income in 4Q19 was a release of a provision related to deposit insurance
- Administrative expenses were down by 8.4% due to FTE reductions in 2019
- The bank tax has been reduced to 14.5 basis points from 31.8 basis points, reducing the Bank´s taxes by ISK 1.7bn annually
- Loss for the period is largely caused by negative net impairment
- The cost of risk for loans to customers was 38bp in the quarter (about 153bp annualised)

1. Borgun hf. has been classified as disposal group held for sale in the interim financial statements. The comparative figures in the Consolidated Interim Income Statement for the first quarter of 2019 have been restated

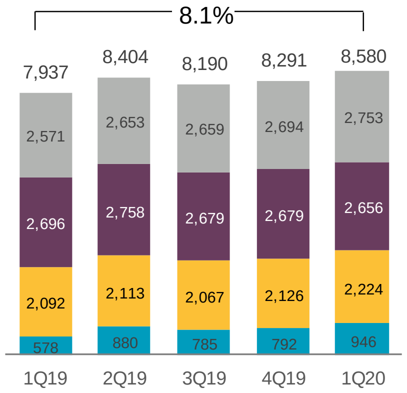
Strong growth in interest income but decrease in total income

Decrease in total income mainly due to lower NFCI and considerable net financial loss.

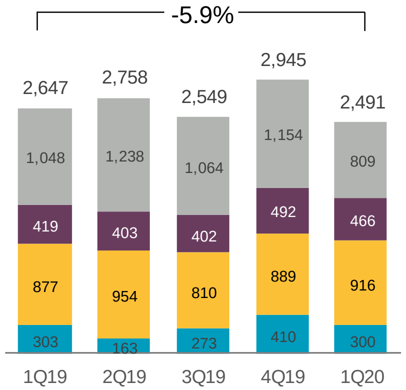
Total operating income[1]
ISKm



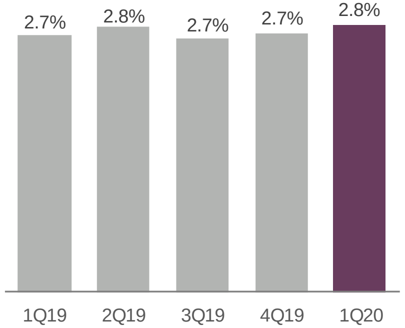
Net interest income
ISKm



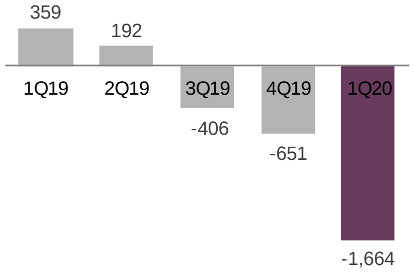
Net fee and commission income
ISKm



Net interest margin



Other net operating income[1]
ISKm

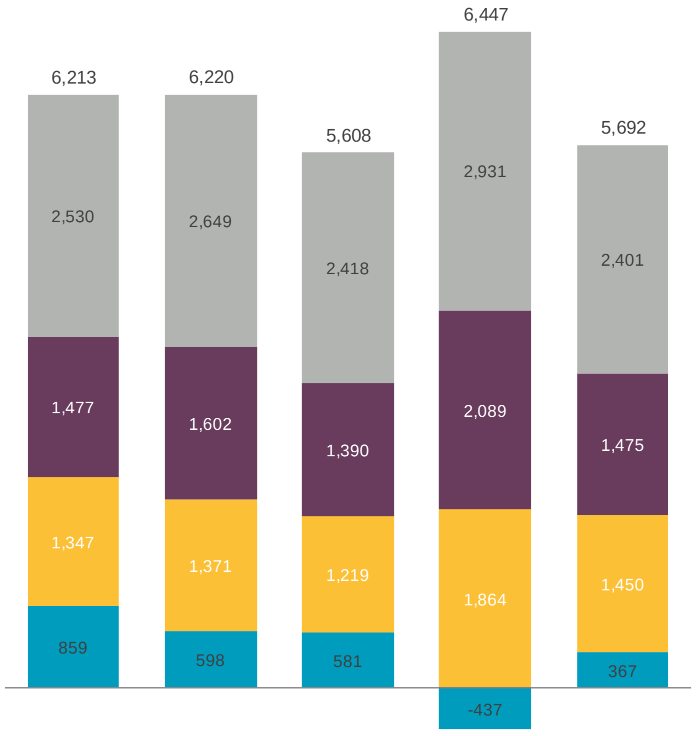


1. Excluding one-off income

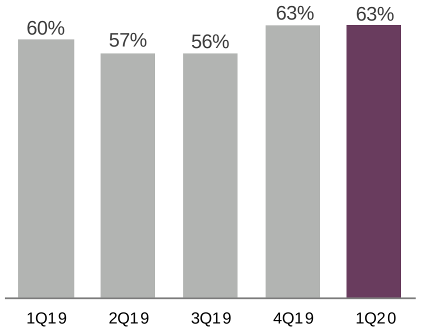
Administrative expenses decrease

Decrease in administrative expenses driven by lower salary cost and operating expenses fall

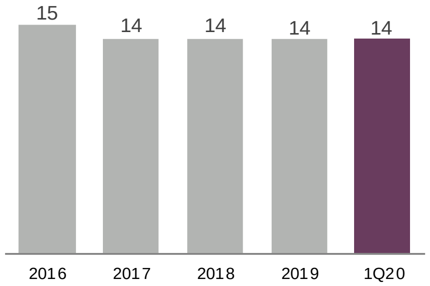
Administrative expenses[1]
ISKm



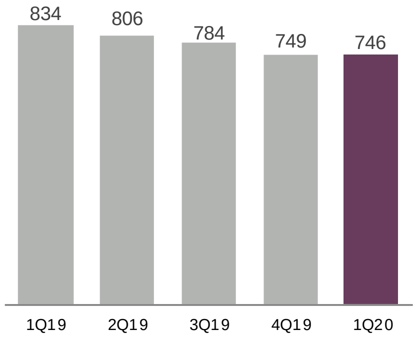
Efficiency – Cost to income ratio[2]



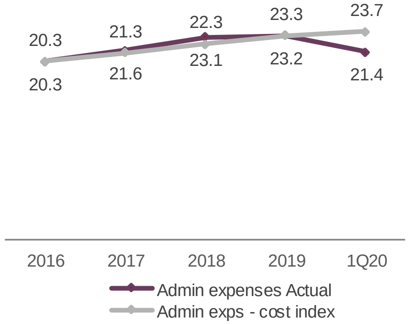
Branch network



Period end FTE numbers[3]
Parent company



Annualised admin. exp. vs cost index[4]
ISKbn. excl. one-off cost. parent company



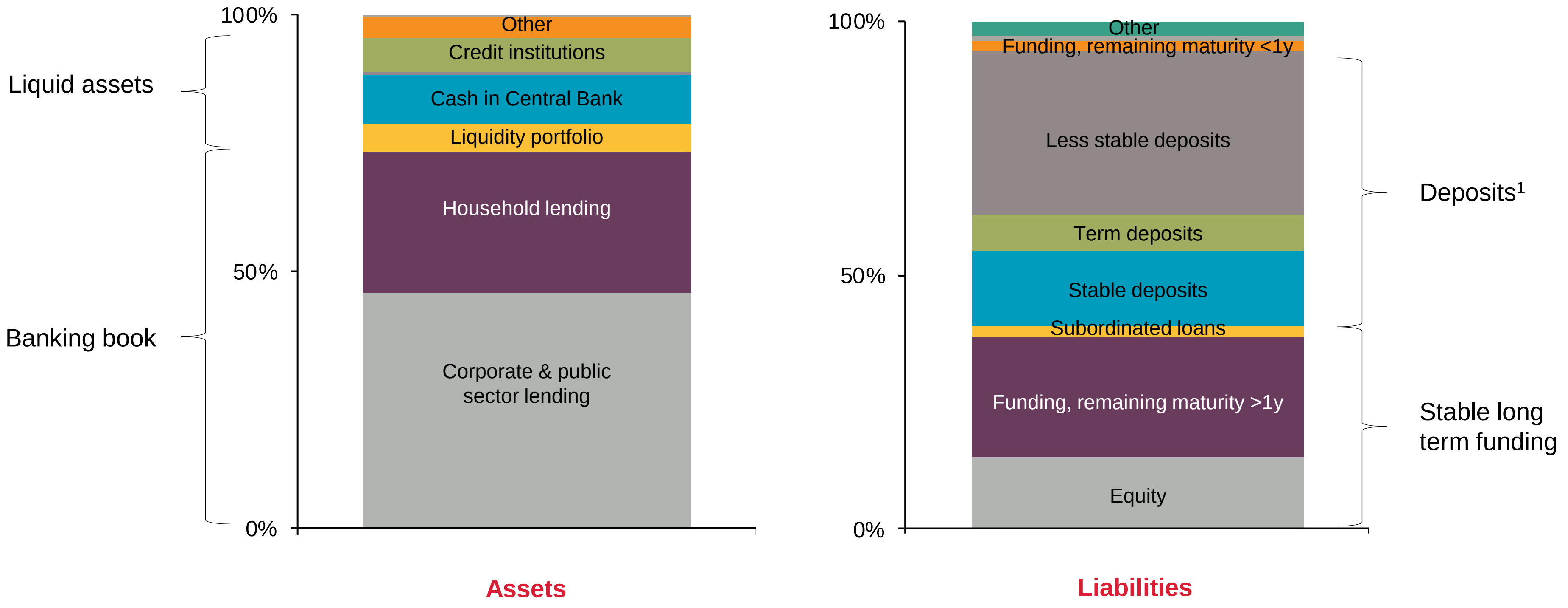
1. Negative cost in Other segment in 4Q19 due to changes in internal cost allocations
2. The cost-to-income ratio excludes bank tax and one-off items
3. FTE numbers exclude seasonal employees
4. Administrative expense - cost index is calculated as 40% inflation and 60% salary index excluding one-off items

4. Balance sheet

Balance sheet overview

Strong balance sheet structure with deposits as primary source of funding

Simplified balance sheet structure at March 31, ISK 1.256bn



1. As defined by LCR categories.

Assets

Total assets are 4.7% up from year-end 2019 but lending growth impacted by ISK depreciation

Assets, ISKm	31.3.2020	31.12.2019	Δ
Cash and balances with Central Bank	**123,062**	146,638	(23,576)
Loans to credit institutions	**84,263**	54,376	29,887
Bonds and debt instruments	**69,368**	52,870	16,498
Derivatives	**4,772**	5,621	(849)
Loans to customers	**923,850**	899,632	24,218
Shares and equity instruments	**12,496**	18,426	(5,930)
Investment in associates	**712**	746	(34)
Property and equipment	**8,015**	9,168	(1,153)
Intangible assets	**3,736**	4,330	(594)
Other assets	**5,154**	6,608	(1,454)
Non-current assets and disposal groups held for sale	**20,263**	1,075	19,188
Total Assets	**1,255,691**	1,199,490	56,201

Highlights

Liquid assets

— Three line items – cash and balances with the Central Bank, loans to credit institutions and bonds and debt instruments – amount to about ISK 277bn of which ISK 253bn are liquid assets

Loans to customers

— Net increase in loan portfolio amounted to ISK 24.2bn since year-end 2019, an increase of 2.7%, there of 20.8bn from depreciation of ISK

Shares and equity instruments

— Decrease as a subsidiary classified as held for sale is moved to non-current assets and closure of derivatives against shares

— ISK 4.7bn open unhedged exposure to equities

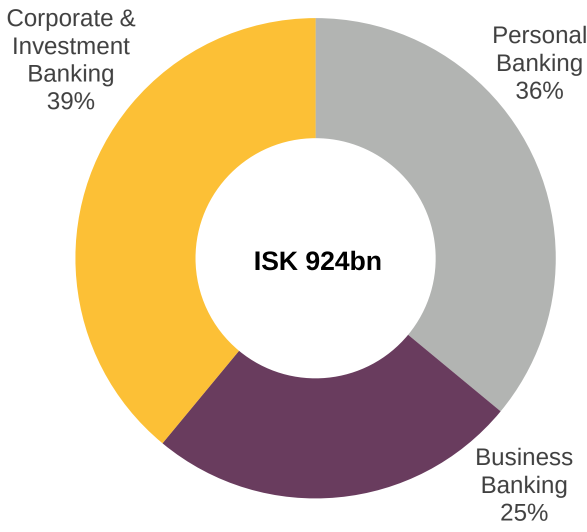
Asset encumbrance

— The Bank’s asset encumbrance ratio was 18.2% at end of 1Q20 compared to 18.1% at year-end 2019

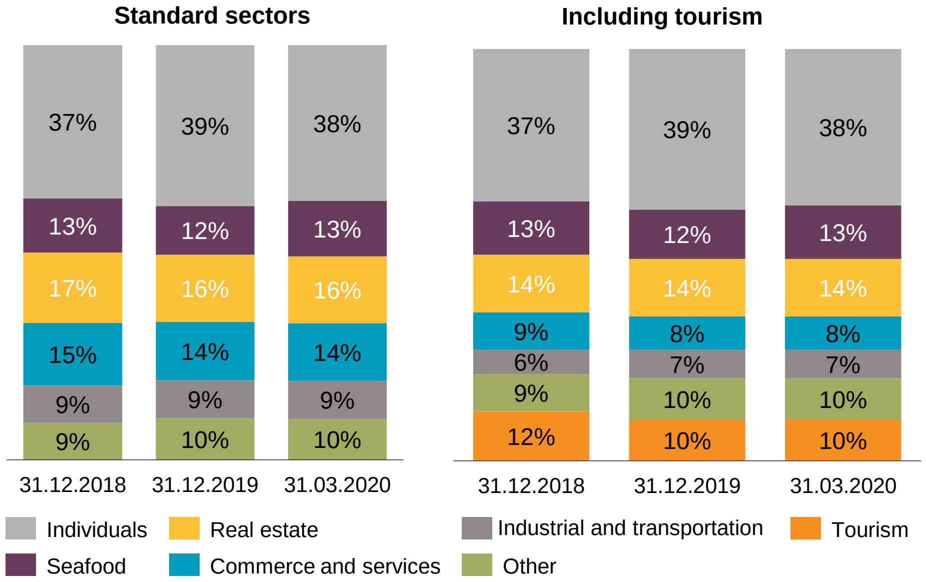
Diversified loan portfolio

Exposure to tourism is 10% of loans to customers

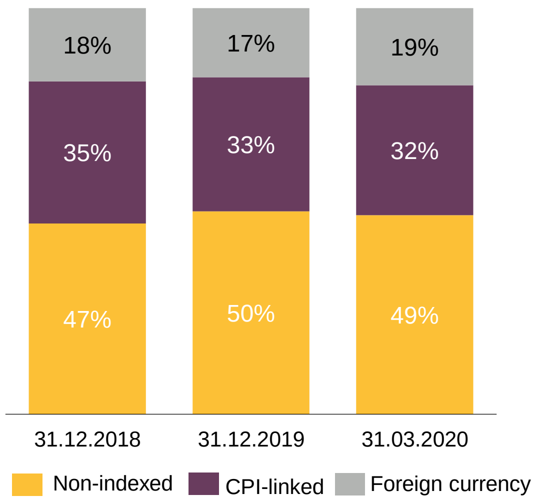
Loans to customers by business divisions
31.03.2020, consolidated



Loans to customers
By sector, consolidated



Loans to customers
% of loans by currency type, consolidated



Highlights

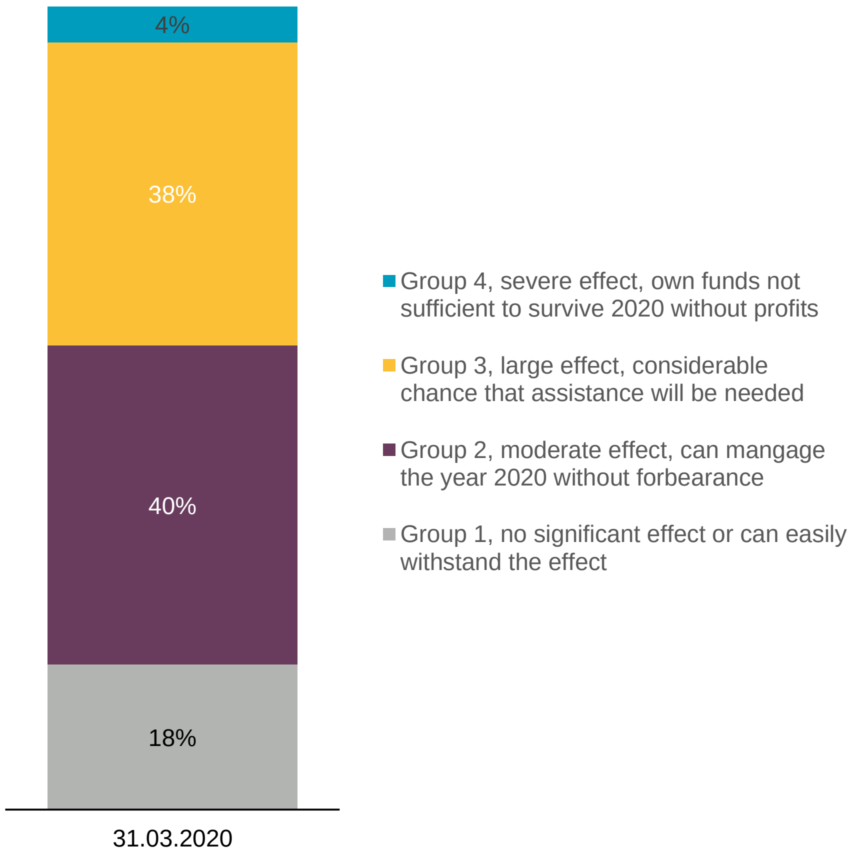
- The loan portfolio is evenly spread out by the three business divisions
- The Bank had two large exposures at end of 1Q20
- The share of loans in foreign currency increased because of a 12% depreciation of the ISK
- The sector-split is shown both with tourism activities in its relevant sectors and with tourism as a sperate quasi-sector. Real estate (hotels), commerce & services (car rentals, restaurants, tour operators) and industrials and transportation are the largest underlying sectors in tourism
- The tourism sector in Iceland is expected to be greatly affected by the COVID-19 pandemic
- Many customers have been granted temporary payment holiday and have received assistance from the Government. Because of significant increase in credit risk, most of the tourism portfolio has been transferred to IFRS 9 stage 2

COVID-19 and the loan portfolio

In Iceland, tourism is the sector that is most affected by the pandemic

- The Bank carefully considered how the pandemic was likely to affect its customers ability to service their debt
- An assessment was made whether there were common risk factors not captured by the modelling process where a general adjustment was warranted in terms of IFRS 9
  - It was determined to be the case for loans to the tourism industry
- Companies in the tourism industry were classified into four groups based on an assessment of how much an increase in credit risk these companies face in the short, medium and long term
  - Where the increase was found to be significant (groups 2-4), the exposure was transferred to Stage 2
  - In addition, an overlay factor was applied to the expected credit loss, comparable to an increase by one risk class for group 2 and two risk classes for groups 3 and 4
- Both the Icelandic Government and the Bank have offered various measures to assist companies and households through temporary drop in income
- The Icelandic Central Bank has provided guidelines saying that: "It is important that the selection of scenarios in the application of IFRS 9 reflect the general expectation that the current situation is temporary, whereas the impact assessment must be conducted on a medium- and long-term basis."

Exposure to tourism by effect of Covid-19 crisis
Net carrying amount, a proportion of ISK 92bn



Macroeconomic scenario

Base case, uncertainty is high

Change in economic indicators (%)	2019	2020	2021	2022	2023	2024
Economic growth	1.9	(5.0)	3.7	2.5	2.3	2.3
Housing prices in Iceland	3.4	1.6	0.8	3.0	3.5	3.5
Purchasing power	1.8	1.8	1.8	1.7	2.1	2.1
ISK exchange rate index	8.6	8.5	1.9	(2.5)	-	-
Policy rate, Central Bank of Iceland	3.9	2.2	2.8	3.3	3.5	3.5
Inflation	3.0	2.6	2.8	2.5	2.4	2.4
Capital formation	(6.3)	(11.3)	9.5	2.3	2.4	2.8
thereof capital formation in industry	(17.5)	(22.0)	16.3	5.0	3.5	3.5

Base scenario

- The base case assumes a gradual easing of COVID-19 containment measures in Q3 and normalization of travel over H2 2020
- Sizeable impact due to share of tourism in the economy and negative effects on private consumption and investment
- GDP rebound expected in 2021 as tourism recovers, business investment increases and private consumption resumes robust growth

Applying scenarios to IFRS 9

- The impairment model of IFRS 9 is forward-looking and reflects a probability weighted average of possible outcomes
- The effects of the economy is accounted for with the use of scaling factors
- In addition to the base forecast, scaling factors are produced for a good and a bad case

Future development

- Keeping in mind the recommendation from the Central Bank, the base forecast assumes that the current situation is temporary and is built on what was known at the end of Q1
- Since then it has become more likely that the tourism industry in Iceland will take longer to recover
- That change in scenario will be reflected in the impairment allowance at end of June 2020

Significant increase in credit risk to the tourism sector

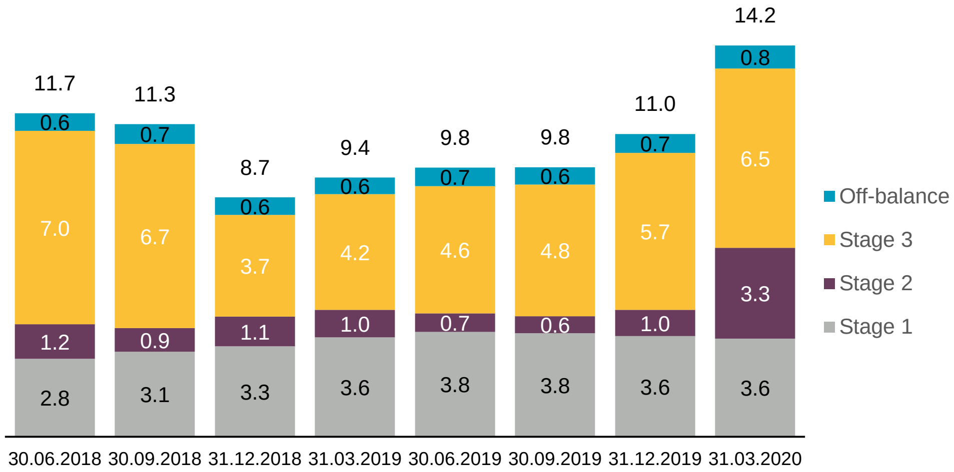
Exposure in Stage 2 increases due to the COVID-19 pandemic but Stage 3 has not yet increased

Highlights

- In 1Q20 the impairment charge amounted to ISK 3.5bn, mostly due to the COVID-19 pandemic
- Majority the tourism portfolio was transferred to Stage 2 and an additional overlay factor was applied to the expected credit loss in tourism
- This resulted in an ISK 2.6bn increase in impairment allowance and a rise in the share of gross loans in Stage 2 from 2.6% to 11.4%
- The Bank furthermore adjusted the weights of the scaling scenarios from 25%-50%-25% (good-base-bad) to 20%-50%-30% which increased impairment by another ISK 0.4bn
- The pandemic has not yet lead to new defaults and the NPL ratio actually decreased from 3.0% to 2.8%
- Revaluation of certain loans in Stage 3 increased impairment by ISK 0.3bn
- Using EBA's definition of NPL, which does not only include loans to customers but also loans and advances to central banks and credit institutions, the Bank's NPL ratio was 2.3% at the end of Q1 2020, compared to 2.7% average for European banks[1]

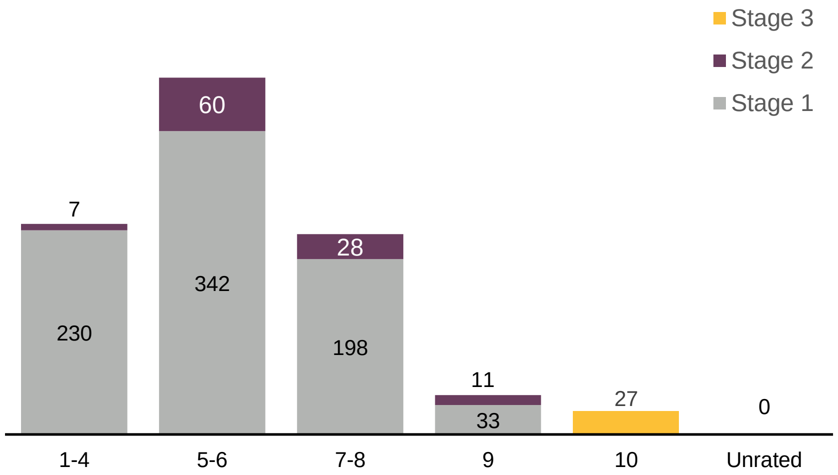
Loans to customers & off-balance sheet items: impairment allowance account

Development of allowance account, ISK bn



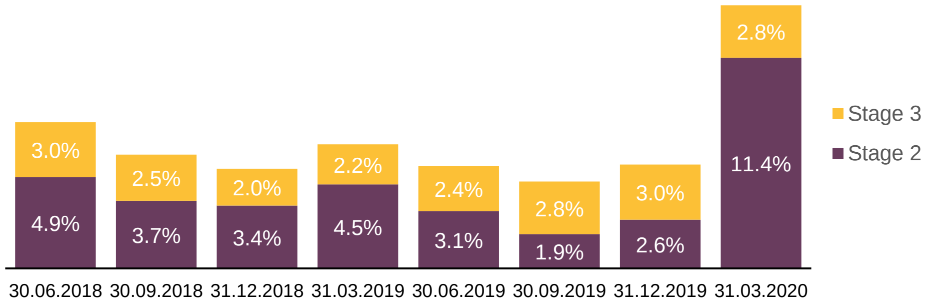
Loans to customers: gross carrying amount

31.03.2020, risk class and impairment stage, ISK bn



Loans to customers: Stage 2 and 3

Development of gross carrying amount as ratio



1. Source European Banking Authority, data as of Q4 2019.

Loans to customers: credit quality

31.03.2020, Break-down of loans to customers

	Gross carrying amount		Impairment allowance		Net carrying amount	
	(ISK bn)	% of total	(ISK bn)	RCR	(ISK bn)	% of total
Stage 1	804	85.8%	3.6	0.4%	801	86.7%
Stage 2	107	11.4%	3.3	3.1%	103	11.2%
Stage 3	27	2.8%	6.5	24.5%	20	2.2%
Total	937	100.0%	13.4	1.4%	924	100.0%

Loan portfolio well covered with collateral

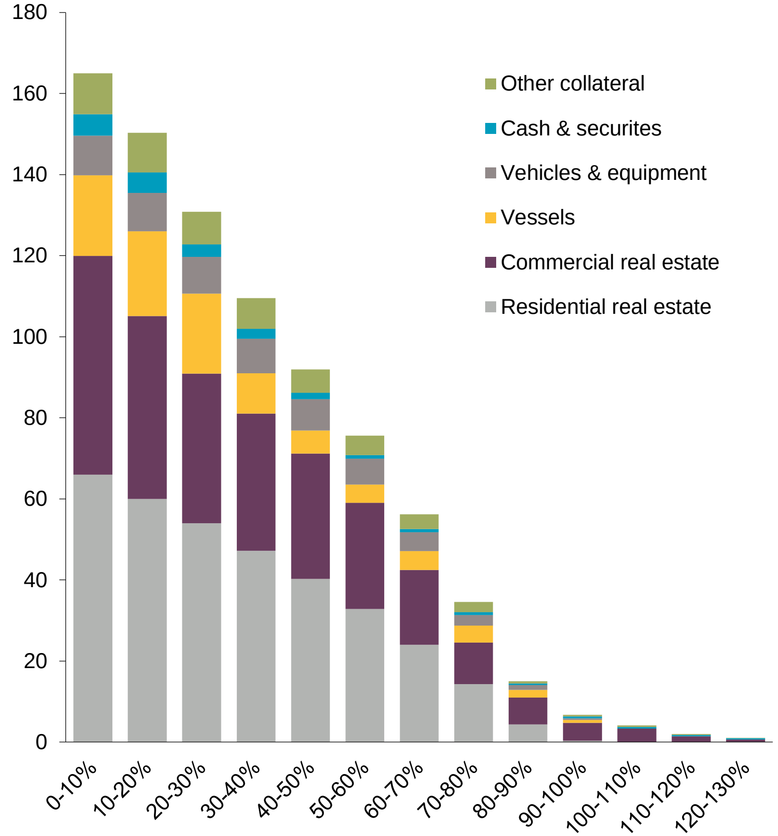
Majority of collateral in residential and commercial real estate

Highlights

- Most of the Bank's collateral is in the form of residential and commercial real estate
- The second most important collateral type is vessels, mostly fishing vessels
- For seasoned mortgages, the LTV distribution is calculated from tax value of properties, which is published annually in June, but for newly granted mortgages the purchase price of the property is used as a valuation while it is considered more accurate
- The increase in LTV of mortgages is party due to additional loans available to first-time buyers now being included in the definition of mortgages
- First-time buyers can get additional loans of ISK 3m, but never higher than 90% LTV

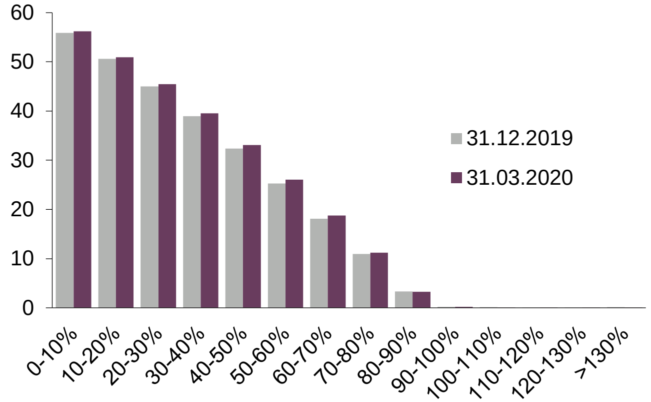
LTV distribution by underlying asset class

ISK bn, by type of underlying asset, as of 31.03.2020



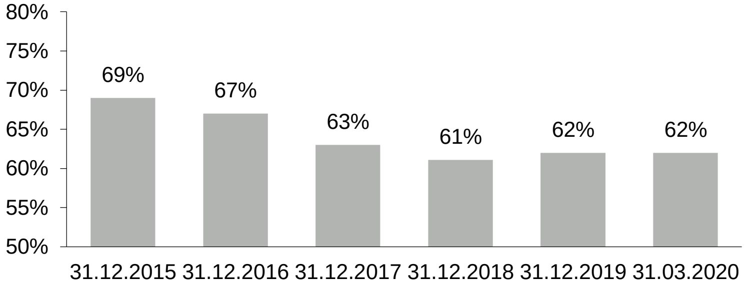
LTV distribution of mortgages to individuals

ISK bn



Average LTV of mortgages to individuals[1]

Development of average LTV



1. The average LTV can be calculated in many different ways and therefore the definition is important for comparison to other banks. The weight is Íslandsbanki's total amount outstanding on the property and the LTV used is the maximum LTV of all Íslandsbanki's loans of the property.

Liabilities

Diversified funding strategy

Liabilities & Equity, ISKm	31.3.2020	31.12.2019	Δ
Deposits from Central Bank and credit institutions	**33,773**	30,925	2,848
Deposits from customers	**647,795**	618,313	29,482
Derivative instruments and short positions	**12,045**	6,219	5,826
Debt issued and other borrow ed funds	**322,280**	306,381	15,899
Subordinated loans	**24,456**	22,674	1,782
Tax liabilities	**8,155**	7,853	302
Other liabilities	**14,392**	27,063	(12,671)
Non-current liabilities and disposal groups held for sale	**13,253**	-	13,253
Total Liabilities	**1,076,149**	1,019,428	56,721
Total Equity	**179,542**	180,062	(520)
Total Liabilities and Equity	**1,255,691**	1,199,490	56,201

Highlights

Deposits

- Customer deposits increased by 4.8% in the period
  - There of 12.0bn from depreciation of ISK. Increase in most customer groups, but with significant increases in pension funds and corporations
  - The customer loans to customer deposit ratio was 142.6% at end of March 2020

Debt issued and other borrowed funds

- Íslandsbanki issued covered bonds totalling ISK 6bn in the quarter in two auctions
- No issuance of senior or subordinated debt during the quarter due to good funding position
- The Bank bought back in full a SEK 350m bond maturing in July 2020

Equity

- The annual AGM approved that dividend should not be paid in light of COVID-19 uncertainties

Deposits remain the main source of funding

Core deposits continue to be stable

Highlights

Stable core deposit base

- Deposits remain the main funding source for the Bank and the deposit to loan ratio remains high
- At the end of the period, 70% of the deposits were in non-indexed ISK, 15% CPI linked and 15% in foreign currencies

Deposits concentration stable

- 17% of the Bank's deposits belonged to the 10 largest depositors and 33% belonged to the 100 largest depositors at the end of March 2020, compared to 17% and 32% respectively at year-end 2019

Deposits development

- Total increase in deposits is ISK 32bn since year-end 2019, there of 12.0bn from depreciation of ISK. Increase in most customer groups, but with significant increases in pension funds and corporations

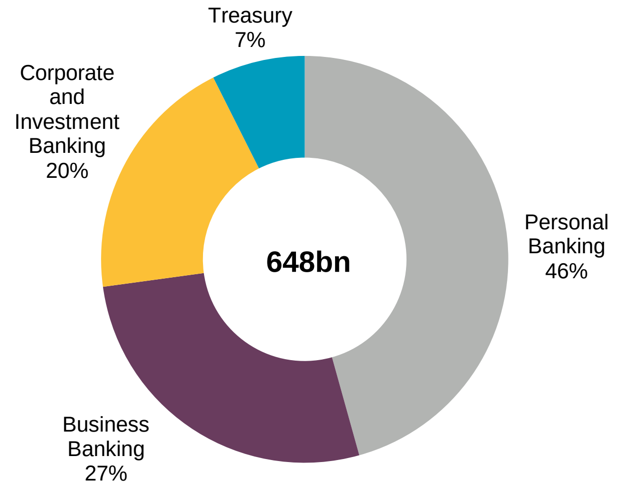
Customer and credit institutions deposits by LCR category

31.03.2020 compared with year end-2019, ISK bn, consolidated

	Deposits maturing within 30 days							
Customer type	Less stable	Δ	Stable	Δ	Term deposits	Δ	Total deposits	Δ
Retail	**231**	2	**87**	3	**86**	7	**403**	12
Operational relationship	**3**	0	**-**	-	**-**	-	**3**	0
Corporations	**81**	8	**0**	0	**24**	(1)	**106**	7
Sovereigns, central-banks and public sector entities	**9**	2	**0**	0	**1**	1	**10**	2
Pension funds	**42**	6	**-**	-	**25**	0	**66**	6
Domestic financial entities	**34**	5	**-**	-	**41**	(6)	**74**	(0)
Foreign financial entities	**8**	0	**-**	-	**11**	4	**19**	5
Total deposits	**407**	24	**87**	3	**187**	5	**682**	32

Breakdown of deposits from customers by divisions

31.03.2020, consolidated



Successful funding journey

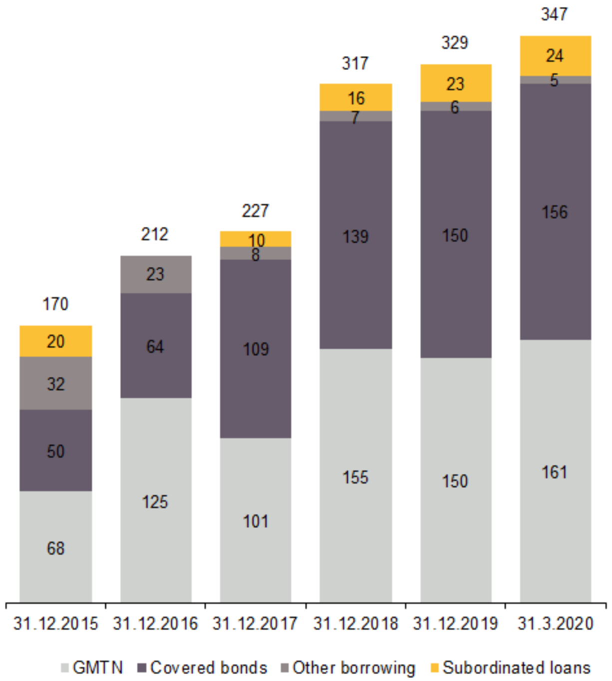
Minimal 2020 funding requirement in FX due to limited refinancing need in 2020 and 2021

Highlights

- The Bank´s funding model is straightforward designed to:
  - Limit refinancing and liquidity risks
  - Optimise cost of funding and use of proceeds
- Funding is raised to match the lending programme of the Bank using three main funding sources:
  - Deposits
  - Covered bonds
  - FX wholesale funding

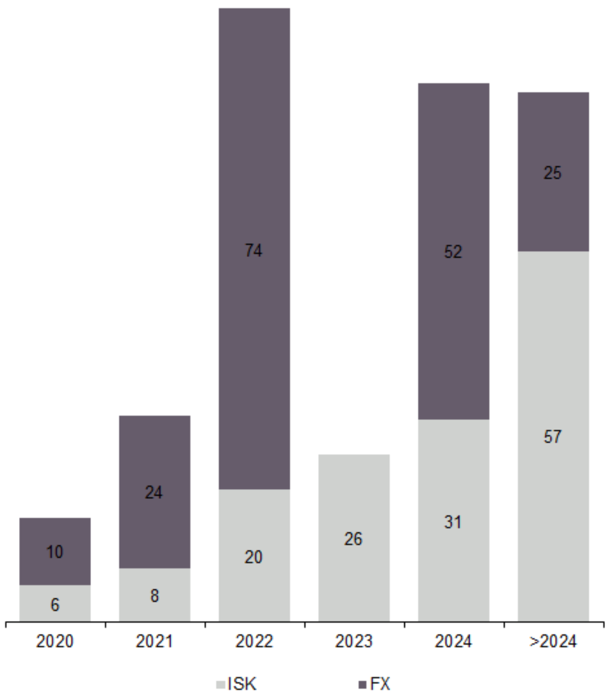
Sources of market borrowings

Book value, ISK bn



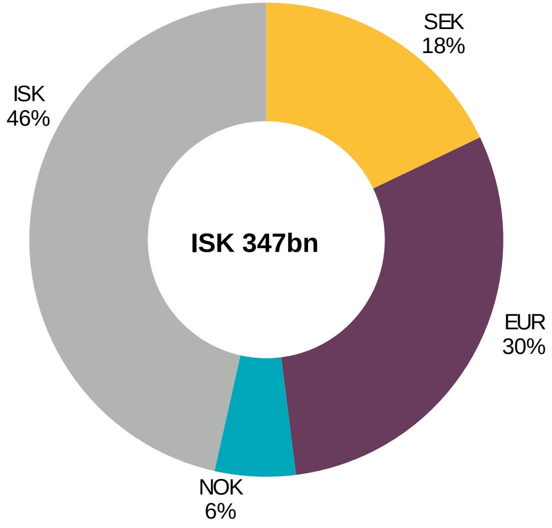
Maturity profile of long-term debt and repayment of long term debt

31.03.2020, Nominal value, ISK bn



Currency split of market borrowing sources

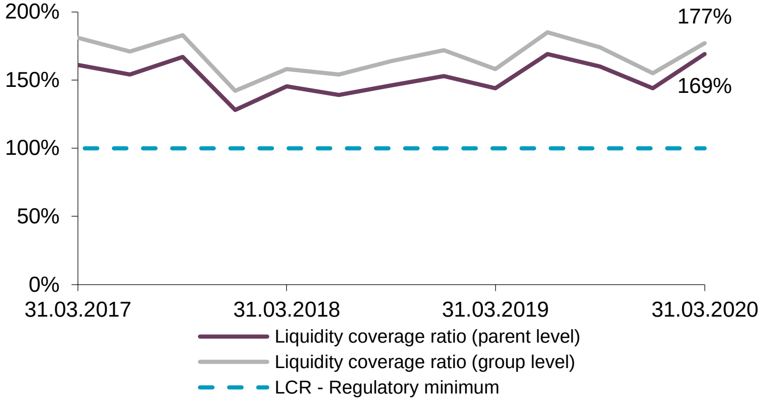
31.03.2020, Nominal value, ISK bn



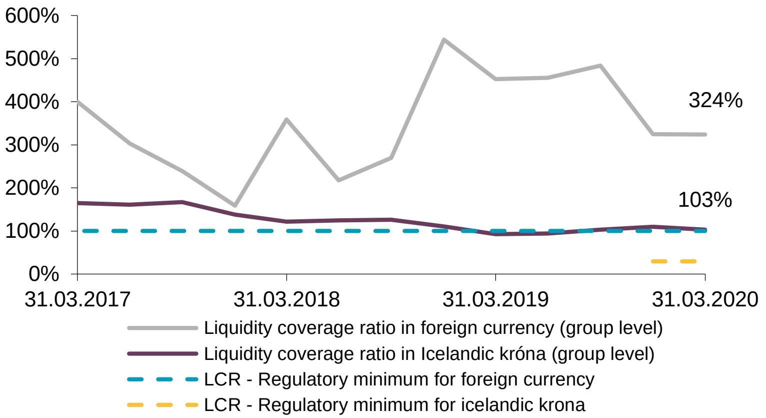
Sound management of liquidity – all ratios above requirements

Liquid assets of ISK 253bn are prudently managed

Liquidity coverage ratio (LCR)



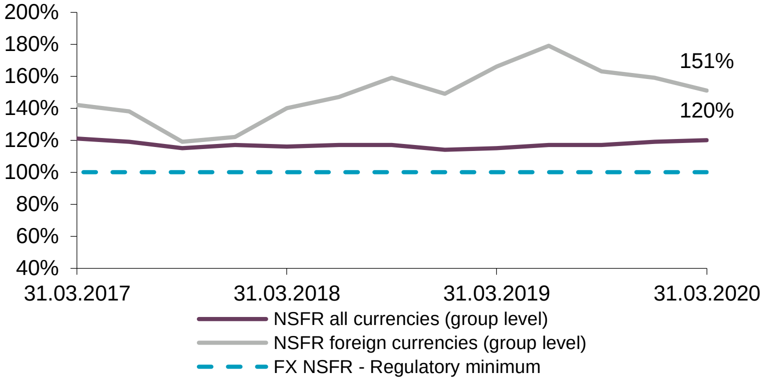
Liquidity coverage ratio – foreign currencies and Icelandic króna



Highlights

- All liquidity measures well above regulatory requirements
- FX liquid assets are composed of government bonds that have a minimum requirement of AA rating and cash placed with highly rated correspondent banks
- Borgun, a subsidiary currently held for sale, is still included in the group LCR and NSFR
- Liquidity and Capital Contingency Plan is tested regularly

Net stable funding ratio (NSFR)

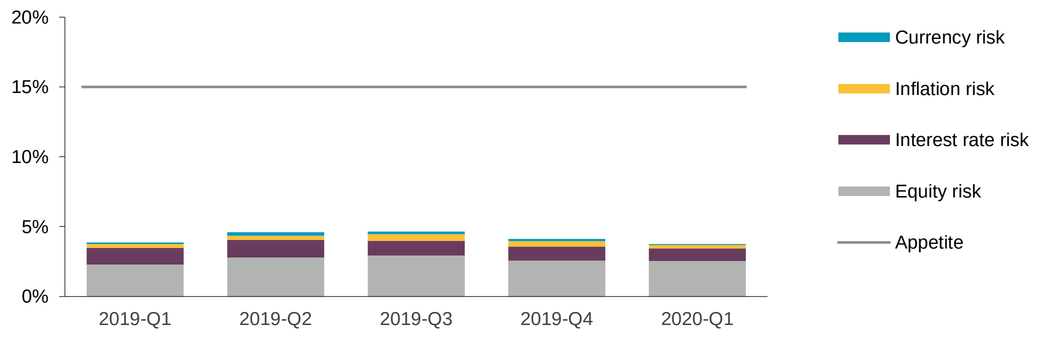


Market risk well within appetite

The Bank has a very modest market risk profile

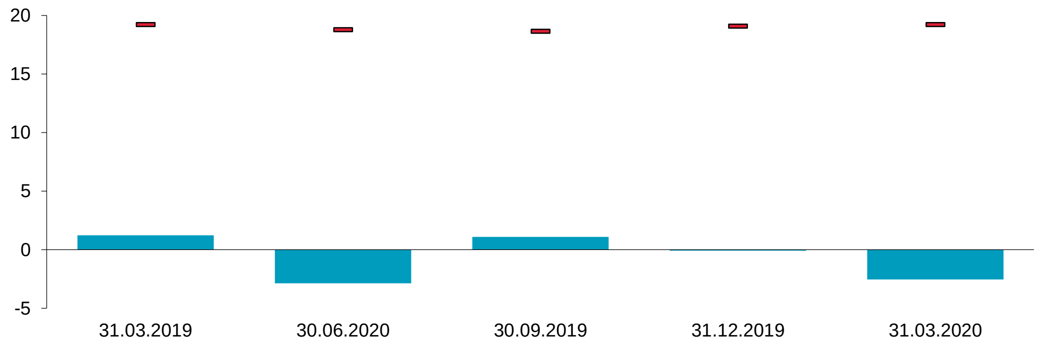
Market risk exposure and market risk appetite

Average positions per quarter, as percentage of total capital base, consolidated



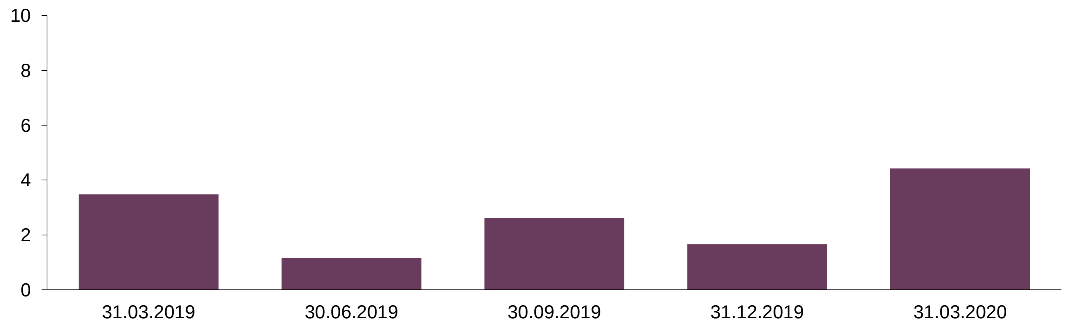
Development of the currency imbalance compared with regulatory limit

ISK bn, end of quarter, consolidated



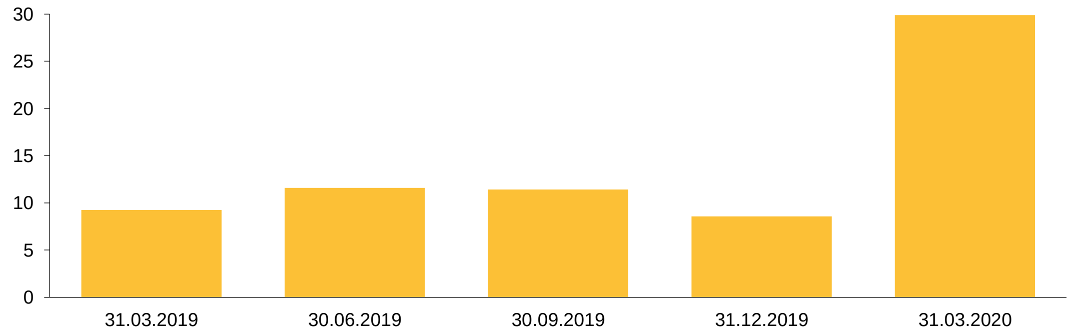
Development of interest rate risk in the banking book

Weighted average BPV, end of quarter, ISK m, consolidated



Development of the banking book inflation imbalance

ISK bn, end of quarter, consolidated



Sound capital position

The capital ratio exceeds target

Highlights

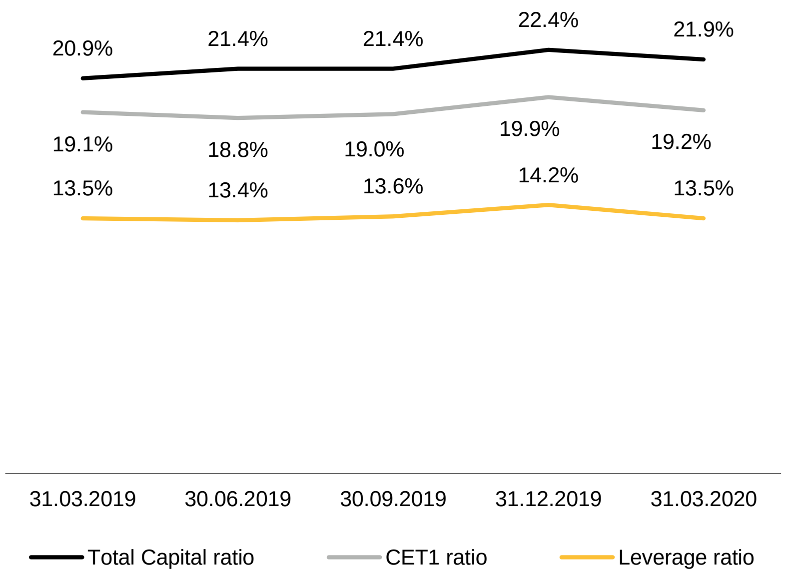
Capital ratios

- The CET1 capital was ISK 175bn at the end of March 2020 compared to 176bn at year-end 2019
- The capital base was ISK 199bn compared to ISK 198bn at year-end
- The depreciation of the ISK increased the value of the subordinated loan, increasing the capital base despite the decrease in CET1 capital
- The Annual General Meeting approved that a dividend to shareholders for the 2019 financial year should not be paid in light of uncertainties due to unprecedented circumstances in the financial markets following COVID-19
- Total capital ratio decreases as REA increases more that total capital in the quarter

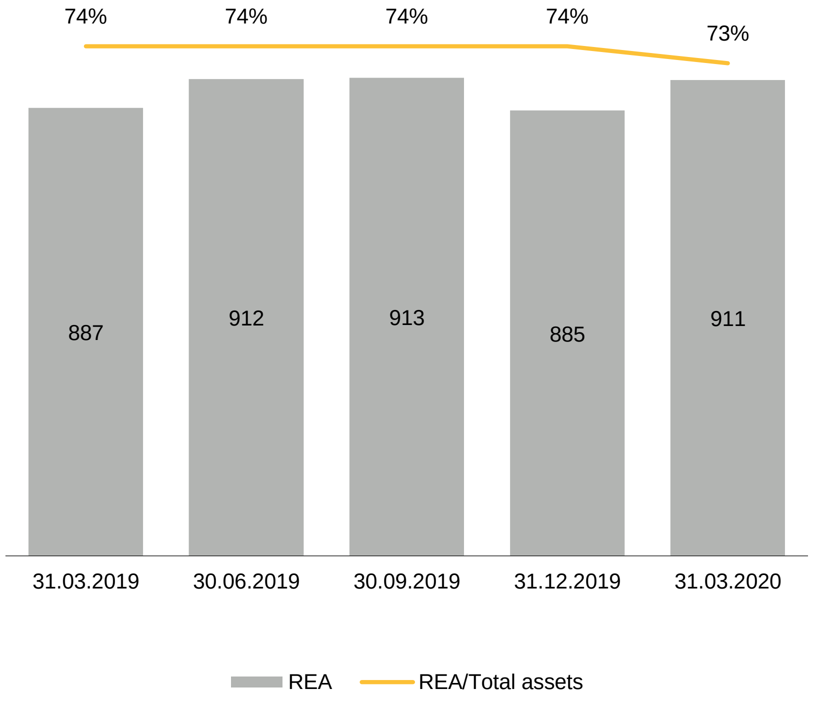
Risk exposure amount (REA)

- The REA increased during the quarter, mainly because of an increase in the loan portfolio due to the depreciation of the ISK.
- The ratio of REA of total assets lowered to 73%

Capital and leverage ratios



Risk exposure amount (REA)
ISK bn

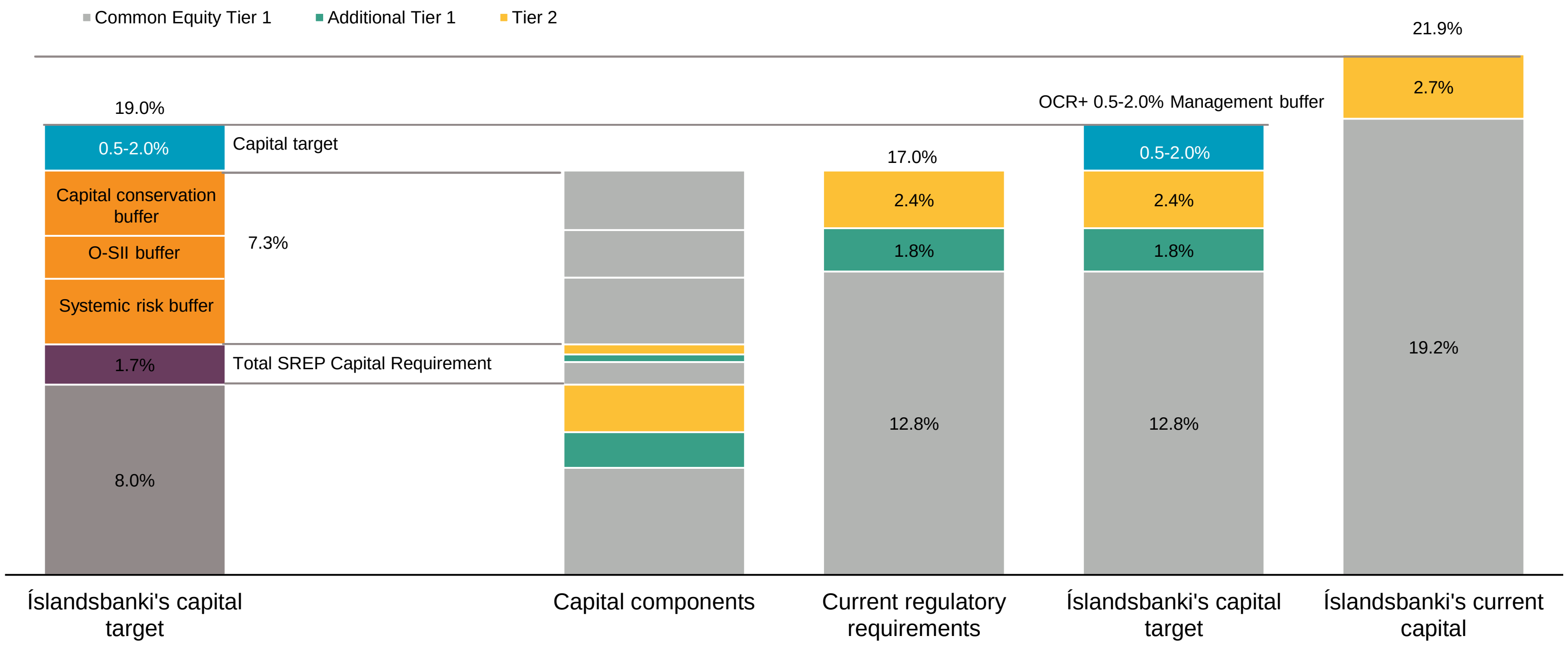


Íslandsbanki’s capital target

Based on the regulatory requirement and a 50 – 200bp management buffer

Íslandsbanki’s capital target

- The sum of Pillar 1, Pillar 2-R and the combined capital buffers form the overall regulatory capital requirement
- The countercyclical capital buffer was lowered to from 2% to 0% in March due to circumstances following COVID-19
- Based on the SREP 2019 results, published in October 2019, the overall capital requirement for Íslandsbanki is 17% of risk exposure amount (REA)
- Íslandsbanki's total capital target ratio is based on the overall regulatory requirement in addition to a 50-200bp management buffer
- The capital target is currently at 17.5–19.0%, taking into account the suspension of the countercyclical capital buffer in March 2020
- The size of the management buffer is based on factors such as volatility in the capital ratios due to currency fluctuations, volatility in earnings and REA and uncertainties in the regulatory or operating environment
- The Board may convene a special shareholder meeting later in the year where a proposal regarding payment of dividends of profit for previous fiscal years could be suggested



Íslandsbanki S&P credit rating

Rating lowered in April 2020

Íslandsbanki

	S&P
Long-term	BBB
Short-term	A-2
Outlook	Stable
Rating action	April 20

Icelandic sovereign

	S&P	FITCH	MOODY'S
Long-term	A	A	A2
Short-term	A-1	F1+	P-1
Outlook	Stable	Stable	Stable
Rating action	Nov 19	May 19	April 20

BBB/A-2 Stable Outlook

Press Release 24 April 2020

In late April 2020 S&P lowered Íslandsbanki's rating to **BBB/A-2** with a **stable outlook** from previous BBB+/A-2 with a negative outlook

In its report, S&P expects Íslandsbanki to enter this crisis on a more solid foothold than the 2008 financial crisis. The 'BBB' rating level and stable outlook factor in the **solid market position** of the bank in Iceland, which has a relatively **advanced digitalized banking platform**. In S&P's view, the bank is well ahead of many other European banks in its preparation for technological disruption. S&P also notes the Bank's funding and liquidity metrics are adequate for the Bank's risk profile, with **comfortable liquidity ratios and liquid assets** covering more than 3x the average short-term funding in 2019. Moreover, S&P states that the wholesale funding needs are limited in 2020, which coupled with the additional central bank liquidity facilities announced recently by the Icelandic Central Bank, **eases pressure on liquidity needs**

S&P's rational for the change is mostly derived from its view that economic activity will reduce in Iceland and Europe in 2020 and thus could impair Íslandsbanki's asset quality, increase credit losses, reduce business and revenue generation, and potentially erode its capital. S&P's view is that Iceland's operating environment will remain challenging, affected by the 2020 economic recession, declining interest rates, stiff competition from pension funds in mortgage lending and thus contributing to the declining profitability of the Bank

5. Financial targets and next steps

Financial targets

Negative ROE in the quarter has limited impact on capital ratios

	Target	1Q2020	2019	2018	Guidance
Return on equity	8-10%	-3.0%	4.8%	6.1%	— Target of 4-6% on top of risk free rate. Risk free-rate is currently 1.5% — 8-10% ROE is based on average expected risk free rates through the business cycle. Based on the current risk-free rate of 1.5% the ROE target in the very short term is 5.5-7.5% — The COVID-19 pandemic will have a material adverse effect on the Banks earnings in 2020 and it is therefore unlikely that the ROE target will be met this year. The Bank will strive to get back on track to reach its ROE targets from 2021 onwards
Cost/ Income ratio[1]	<55%	62.9%	62.4%	66.3%	— This is a medium to long term target. C/I ratio can be expected to be higher than target in the near term due to the COVID-19 pandemic — The Bank continues to invest in IT infrastructure and process efficiency to improve the C/I ratio in the medium to long term
CET1	>13.2 – 14.7%	✓ 19.2%	✓ 19.9%	✓ 20.3%	— Based on a management buffer of 50-200bp, the CET1 target range is currently 13.2-14.7% — Long term CET1 target is >16%. In line with the target range, the Bank expects to maintain a CET1 ratio of over 16% in the medium to long term — The Bank is substantially over capitalized with regard to the current regulatory requirement, which is a favourable position to be in in light of the economic uncertainties relating to COVID-19
Total capital ratio	> 17.5 – 19.0%	✓ 21.9%	✓ 22.4%	✓ 22.2%	— Based on the regulatory capital requirement with a 50 – 200 bp management buffer — Current capital requirement is 17.0% including recent suspension of the countercyclical capital buffer in March 2020
Dividend payout ratio	40-50%		✓ 50%	✓ 50%	— The Annual General Meeting approved that a dividend to shareholders for the 2019 financial year should not be paid in light of uncertainties due to unprecedented circumstances in the financial markets following COVID-19 — The Board of the Bank may convene a special shareholders‘ meeting later in the year to propose a dividend payment in 2020 if the economic conditions improve substantially“.

1.Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund – One off items) / (Total operating income – one-off items).

Key takeaways

Strong fundamentals should assist both Iceland and the Bank to weather conditions of economic slowdown following COVID-19

1 Pandemic will cause a recession in 2020 but official actions counteract

- The economic impact of COVID-19 expected to be deep in 2020 but moderate debt levels increases economic resilience
- Increased public investment, simplified rules on restructuring and measures to support tourist industry will help revitalise the economy
- Inflation expected to hold steady with low policy rate

2 Extensive COVID-19 actions by all parties

- The Government has introduced actions for individuals and corporates to counteract unemployment and to support and protect enterprises and innovation
- The Central Bank has acted to support the economy by e.g. lowering base rates and the countercyclical buffer

3 Íslandsbanki supports customers through COVID-19

- Deferral of loan payments for up to six months
- Phone advisory and helpline for senior customers
- Proactive conversations and guidance and support to navigate in digital channels

4 Impairments largest cause for loss in quarter

- NII grew by 8.1% while NFCI decreased by 5.9%
- Admin cost decreased by 8.4% due to fewer FTE's
- Loan impairment charges greatly affect profit as tourist industry loans largely moved to IFRS 9 stage 2
- Net financial loss due to loss in trading and banking books for equity and equity like instruments

5 Strong balance sheet structure with deposits as primary source of funding

- Loans to customers grew by 2.7% and deposits by 4.8% during 1Q20
- High asset quality but significant increase in credit risk to the tourism sector
- NPL ratio 2.3% at end of March, compared to 2.7% average for European banks using the EBA´s NPL definition

6 High liquidity ratios and limited funding needs and exceptional capitalisation

- Minimal 2020 funding requirement in FX due to limited refinancing need in 2020 and 2021
- Strong liquidity position with liquidity ratios above internal targets and regulatory requirements
- Total capital ratio at 21.9%, well above the Bank´s regulatory requirement of 17%

5. Annex – Icelandic economy update

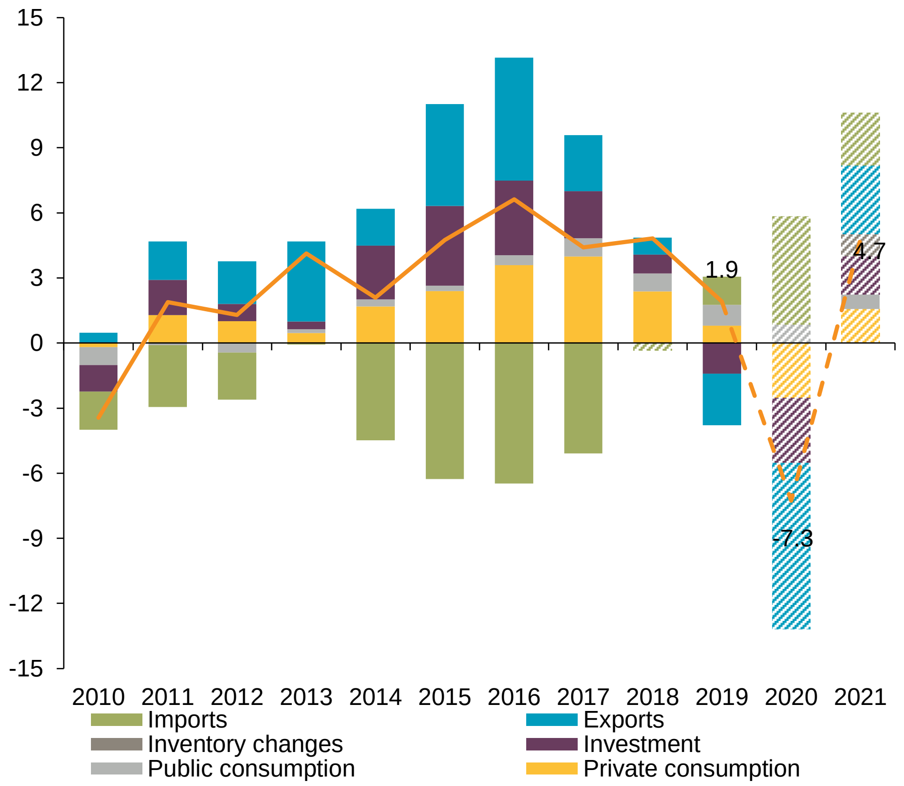
COVID 19 economic impact will be deep

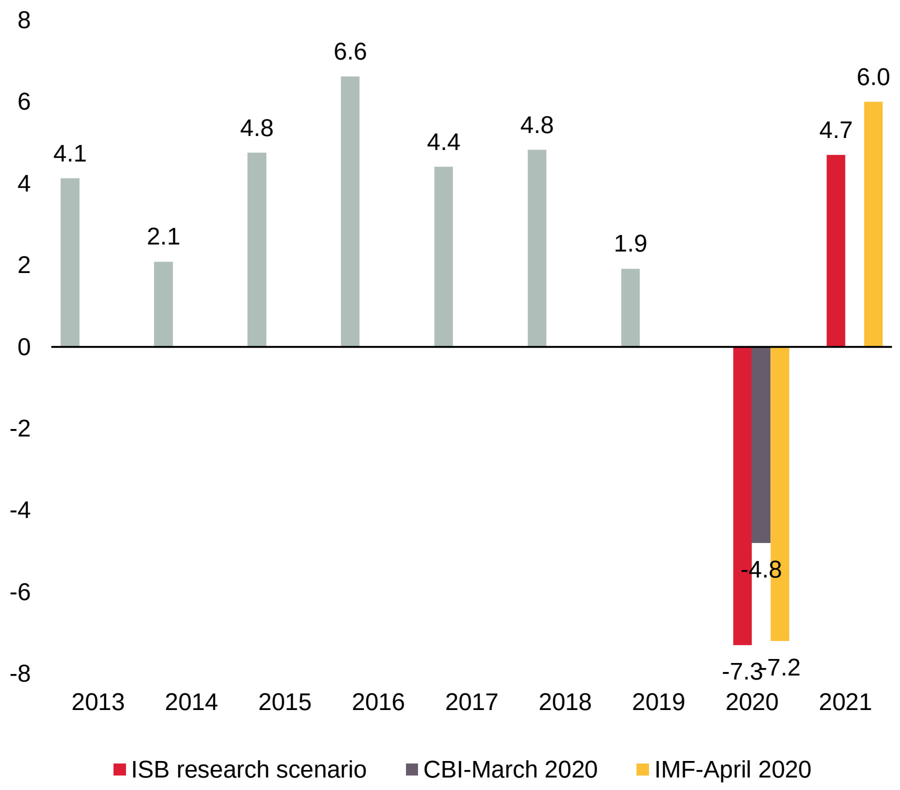
Sharp contraction likely in 2020 but robust growth could resume in 2021

- The COVID-19 pandemic has changed the near-term outlook for the Icelandic economy drastically
- Following moderate GDP growth in 2019, the outlook is for considerable GDP contraction in 2020 due to negative impact by the pandemic on tourism as well as domestic demand
- Preliminary scenario analysis by Islandsbanki research indicates that GDP could contract by more than 7% in 2020
- The blow to exports could have a negative impact of almost 8% on GDP this year
- A sharp contraction in private investment as well as declining private consumption could decrease GDP by 5-6% in 2020
- Public sector investment and consumption will contribute positively to growth, as will a sharp contraction in imports
- Assuming H2 2020 will see a normalisation of the economy and easing of restrictions, 2021 could see GDP in Iceland growing by almost 5%
- IMF forecast for Iceland in April similar to the above scenario

GDP and the contribution of major subitems [1]

YoY change (%) Preliminary Islandsbanki research scenario analysis, Central Bank scenario and IMF forecast





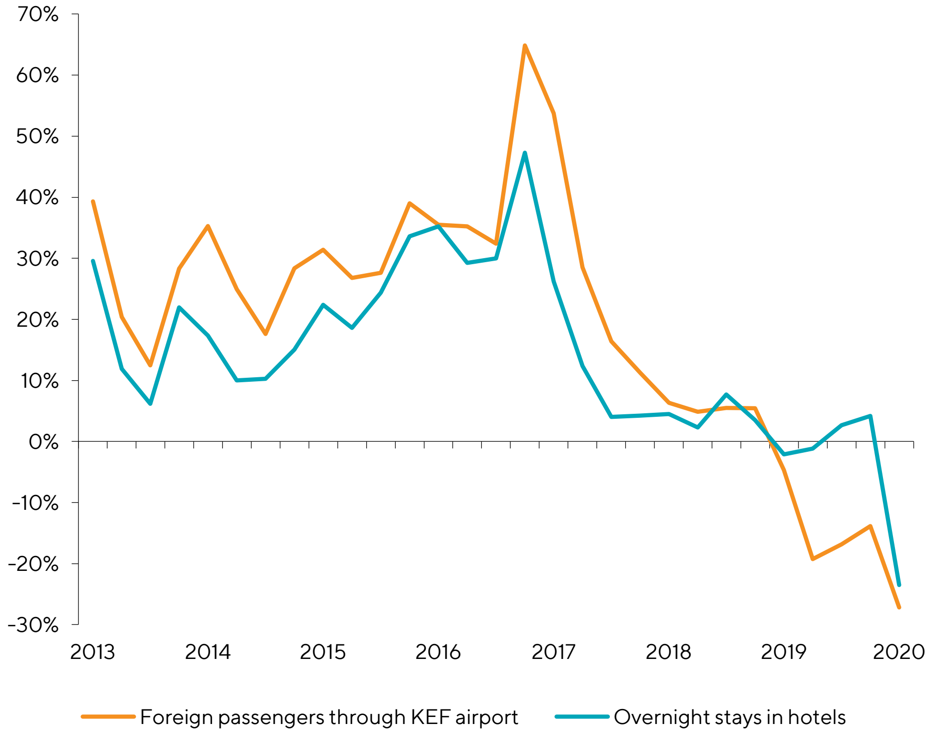
1. Shaded areas indicate ISB Research/ forecasts
Source: Statistic Iceland and ISB Research

Tourism sector hit by COVID pandemic

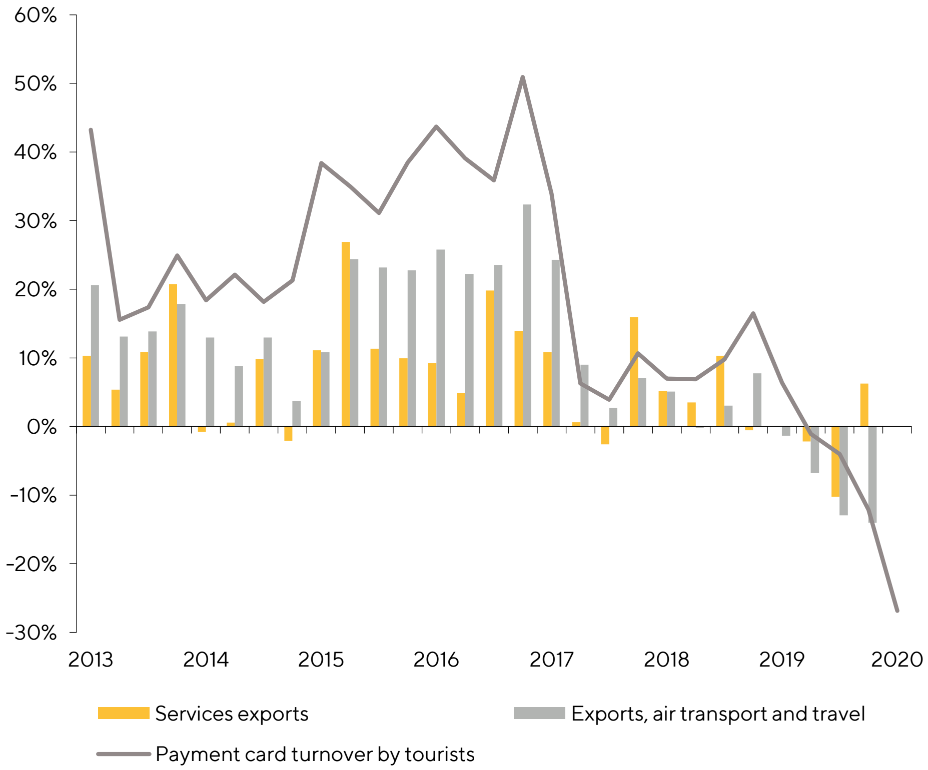
Number of tourists visiting Iceland likely to shrink by over 50% in 2020

- In Q1 2020, 334 thousand tourists visited Iceland, down by 27% YoY
- By early April, tourist visits had all but ceased due to widespread restrictions on cross-border travel and cancellation of over 90% of scheduled flights
- Due to the size of the tourist sector, Iceland's economy is quite exposed to pandemic effects on travel and tourism
- The Icelandic government has taken a number of steps to soften the impact on the sector, including deferral of paid taxes and other levies, partial unemployment benefits and guarantees on operational loan facilities
- Assuming similar assumptions to the IMF for the development of the pandemic and impact on worldwide travel, ISB research estimates that around 900 thousand tourists will visit Iceland in 2020, a YoY decrease of over 50%
- Tourism is assumed to pick up again in 2021 but uncertainty on medium term developments is great

Foreign visitors and overnight hotel stays
YoY change



Services exports and foreign card turnover
YoY change



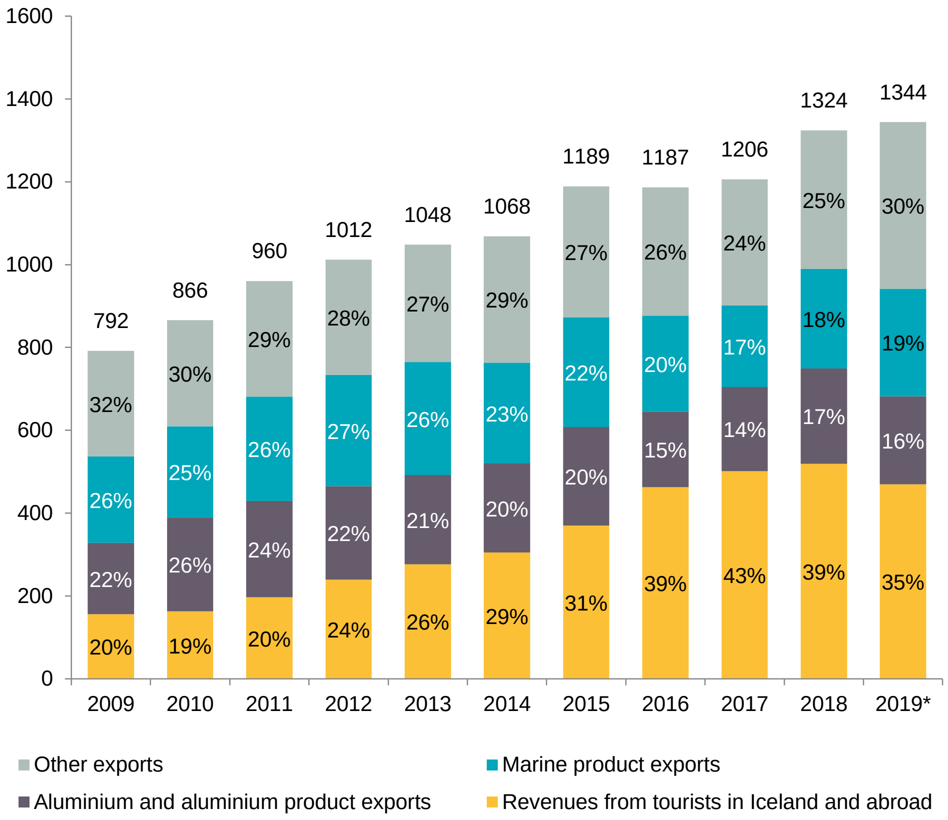
Source: Statistics Iceland, Centre for Retail Studies and Icelandic Tourist Board

Current account resilient to shock

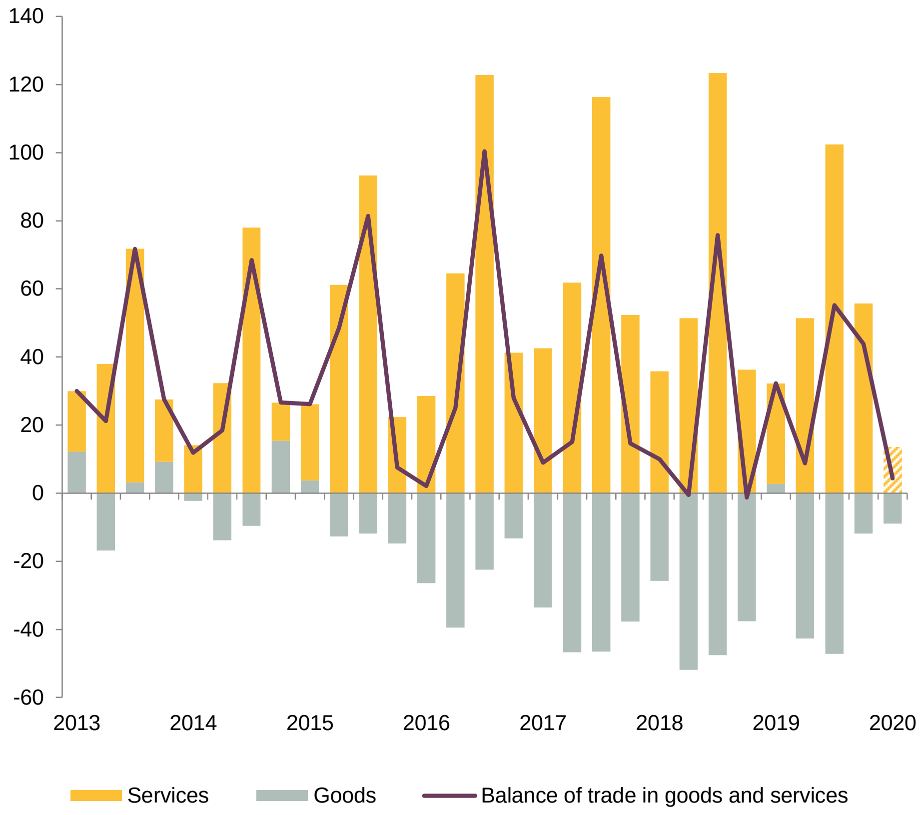
Dramatic fall in exports partially offset by a significant contraction in imports

- Inevitably, services export revenues will decline considerably in 2020 as tourism sector generated over 1/3 of total export revenues in 2019
- Goods exports are also likely to decrease somewhat, although for the seafood sector, a moderate contraction in volume will be offset by rising prices and the recent depreciation of the ISK
- Imports also look likely to contract considerably in 2020
- In 2019, 18% of domestic card turnover was turnover abroad, reflecting travel expenses and purchases in international online retail websites. As of March 2020, that ratio was down to just under 13%
- Goods imports are likely to contract significantly in 2020 as imported component of investment and private consumption is particularly sensitive to worsening short-term economic outlook and the recent depreciation of the ISK
- Iceland's C/A balance, which has been in surplus for the past 8 years, could therefore prove resilient to the export shock and a return to earlier deficits is by no means certain

Export revenues
ISK bn



Trade balance
ISK bn



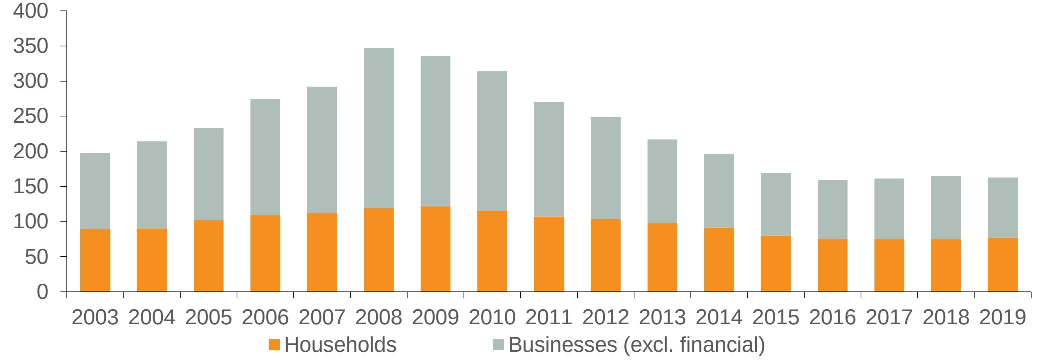
1. Shaded areas and dotted lines indicate ISB Research/ forecasts
Source: Central bank of Iceland, Statistics Iceland and ISB Research

Domestic balance sheets strong before COVID-19

Economy-wide leverage moderate in comparison with peers and historical levels

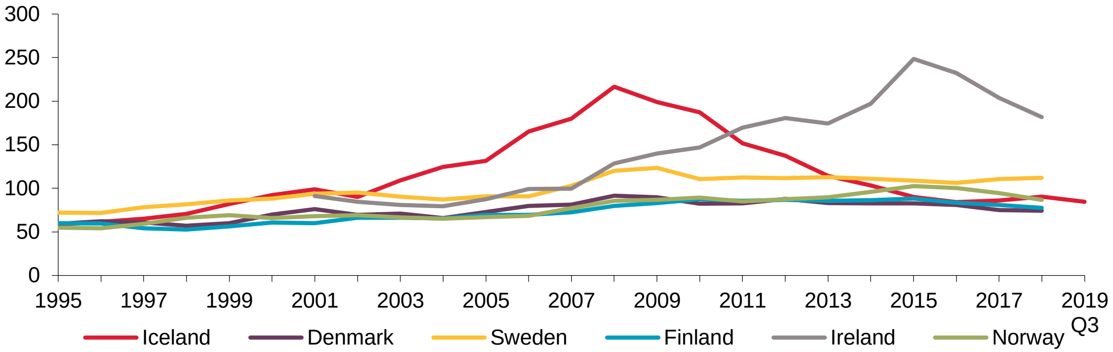
Private sector debt

% of GDP



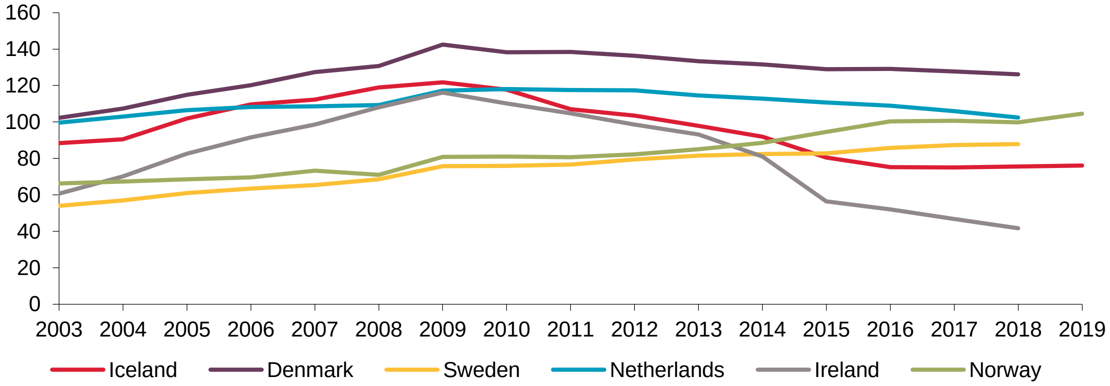
Corporate debt

% of GDP



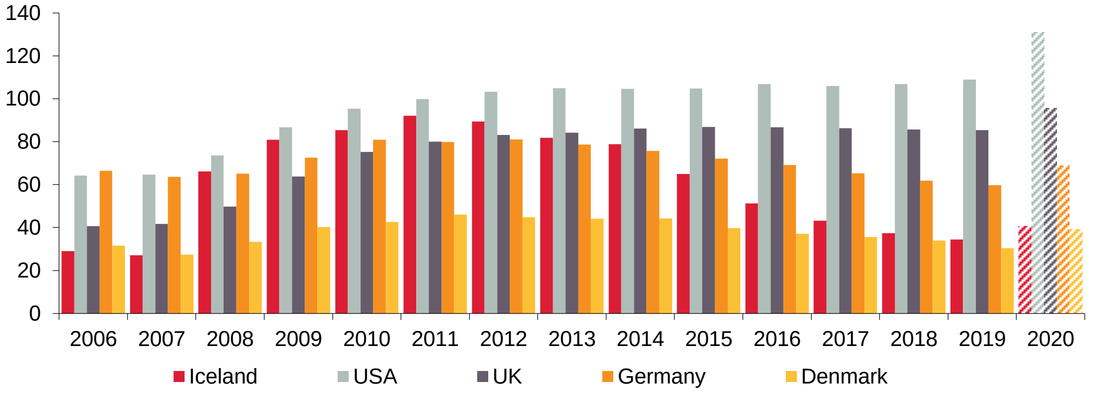
Household debt

% of GDP



General government gross debt

% of GDP



1. Shaded areas and dotted lines indicate ISB Research/ forecasts

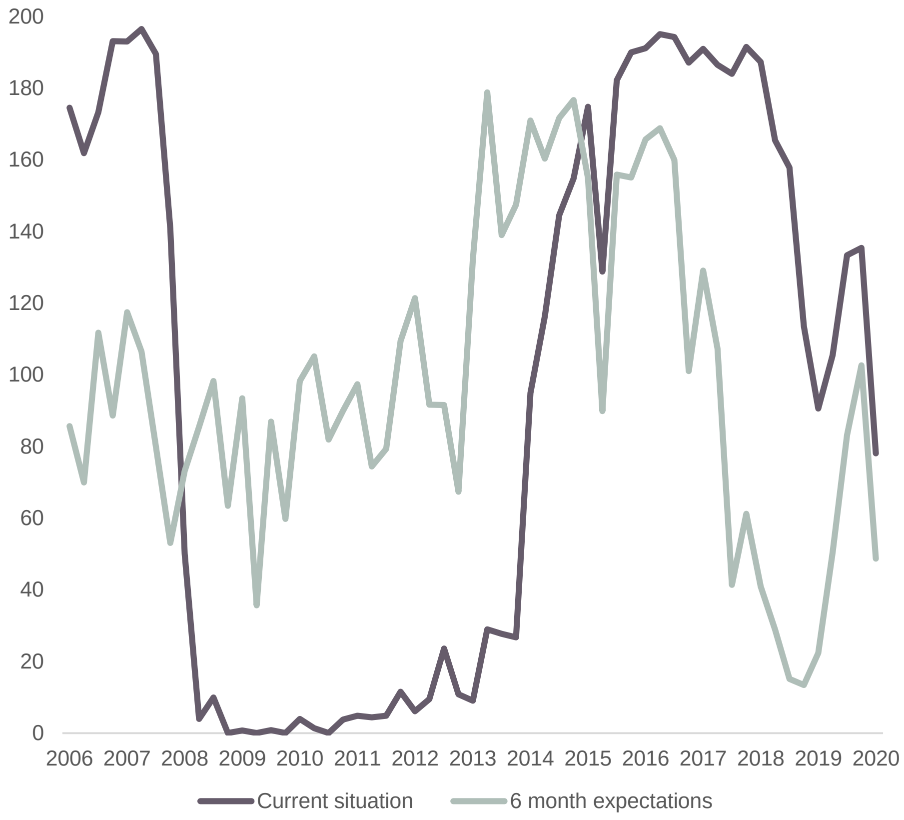
Source: Central bank of Iceland, Statistics Iceland and ISB Research

Businesses set for headwinds

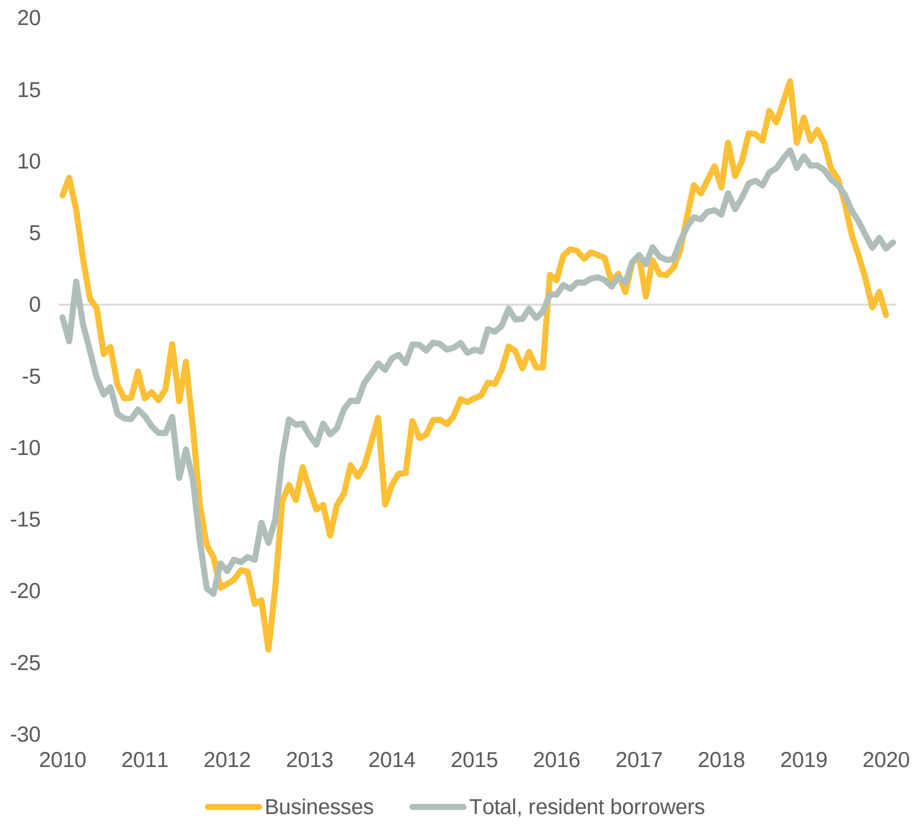
Lending growth to businesses slowed sharply throughout 2019 as business investment stalled

- Investment lost pace in 2019, after a five-year period of uninterrupted growth. In total, investment shrunk by 6.3% YoY. Business investment declined by 17.5% YoY, however
- The outlook is for further contraction in investment in 2020 as private investment declines due to the impact of COVID-19
- Partially offsetting this, an upturn in public investment is expected this year as the authorities engage in counter-cyclical infrastructure investment.
- Business sentiment has seesawed recently. After improving somewhat in late 2019, the pandemic has had a significant negative impact on sentiment
- Lending growth has slowed markedly after peaking in H2 2018. Corporate lending was almost unchanged over the year 2019

Business sentiment, 400 largest companies
Index



Credit system net lending
YoY % change



Source: Statistic Iceland, the Central Bank of Iceland and Gallup

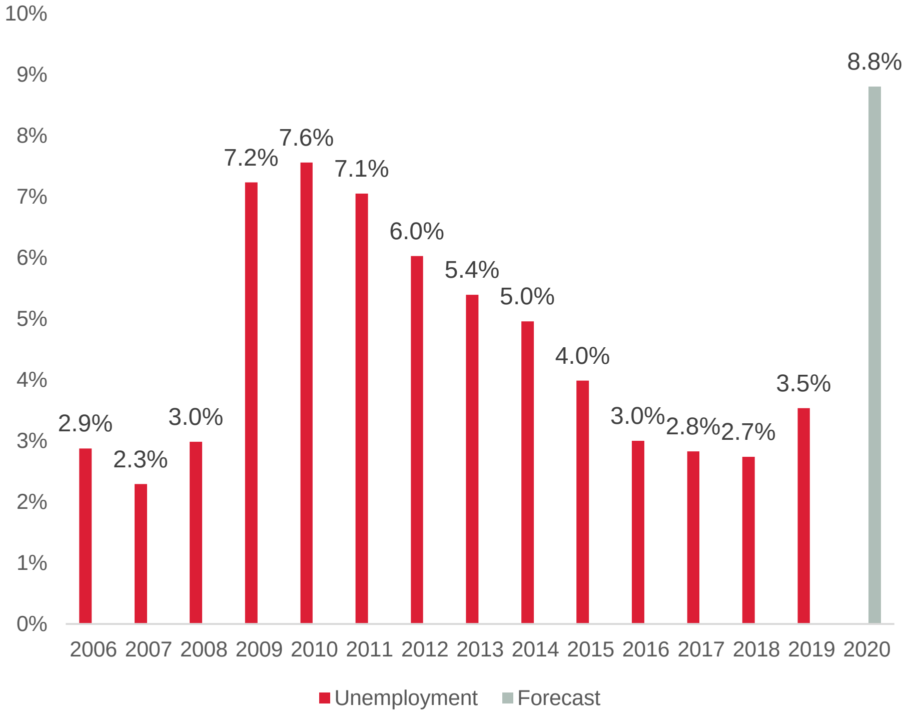
Labour market near-term prospects have deteriorated

The government is taking unprecedented measures in response

- Partial benefits is a measure that the government is providing to enable companies experiencing operational difficulties to reduce worker's employment percentage on a temporary basis
- The aim is impeding the rise in unemployment as much as possible, but it is foreseeable that conditions in the labour market will be difficult while COVID-19 causes a reduction in the number of tourist arrivals and in economic activity more generally
- 5.200 companies used the partial benefits in March and in total about 24,400 employees
- The total unemployment rate in March is 9.2% and has increased from 5.0% since February. Unemployment rose to 5.7% because of general unemployment and to 3.5% due to partial benefits
- Unemployment is likely to grow sharply in coming months when applications for partial employment rates appear for a full month in addition to increase in general applications

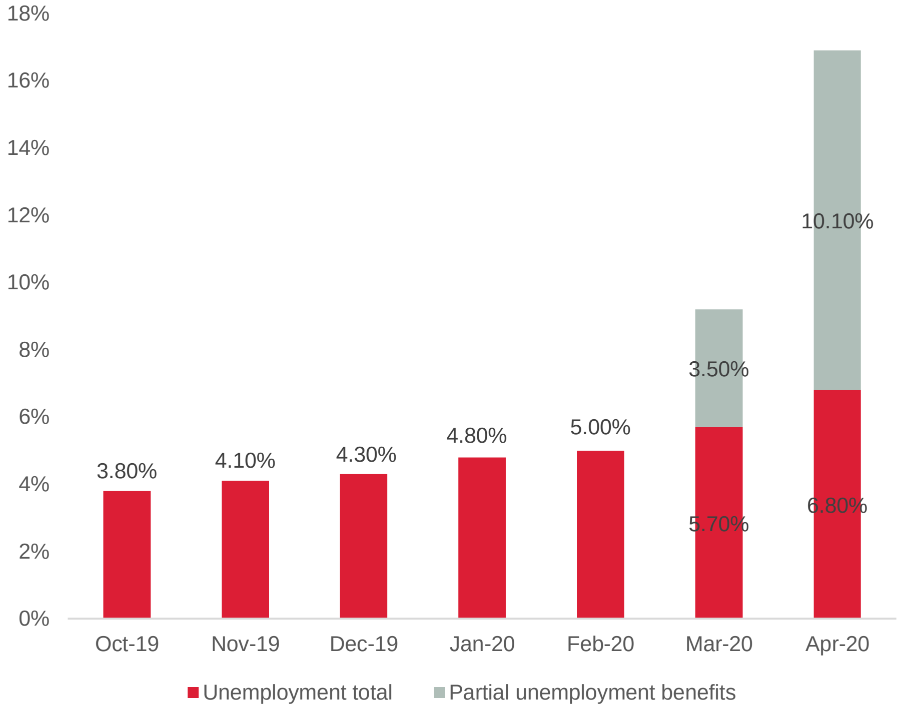
Unemployment annual figures

%



Unemployment monthly figures

%



Source: Statistics of Iceland and Directorate of labour

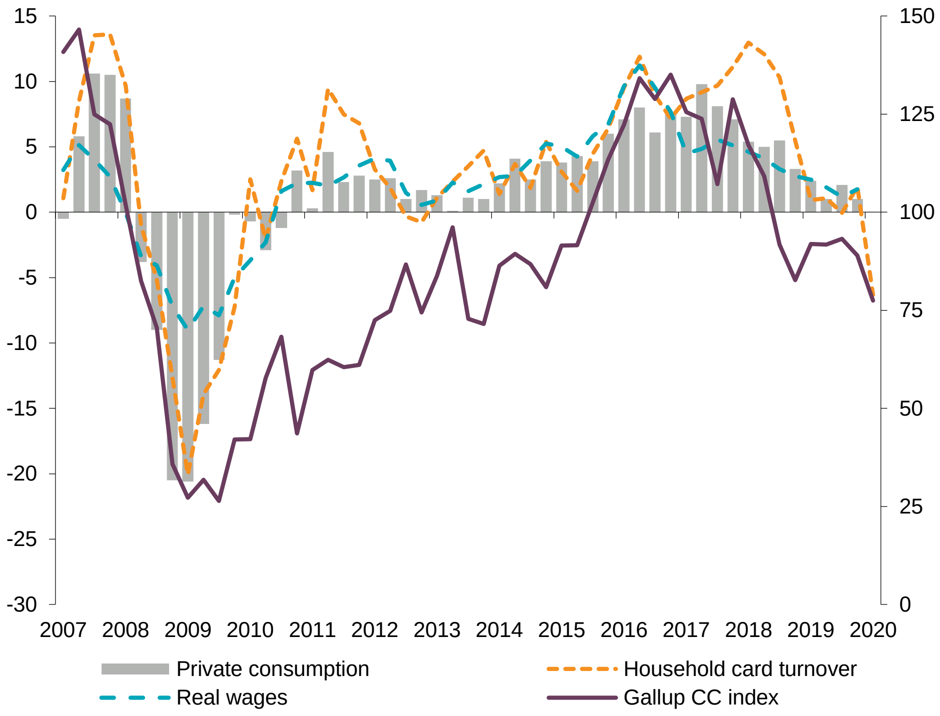
Household consumption contracts sharply

Consumption will inevitably be hit hard by the pandemic

- Restrictions on travel and gatherings will have a major impact on comsumption in coming term. The expectations surveys, unemployment rate and card turnover numbers indicate the bleakest private consumption scenario in nearly a decade
- Consumer sentiment and card turnover figures are already sounding the alarm. Consumer Confidence Index is at its lowest in over nine years and card turnover figures show a sharp contraction
- Consumption is sensitive to uncertainty at the best of times, and Icelandic households are clearly clutching their wallets tighter in response to the current situation
- Private consumption is an important factor in Iceland's GDP growth, accounting for about half of GDP in recent years. Consumption will inevitably be hit hard by COVID-19, and we expect it to contract sharply this year but pick up again next year
- The uncertainty centres on how long restrictions remain in place and households begin to see a glimmer of light at the end of the tunnel

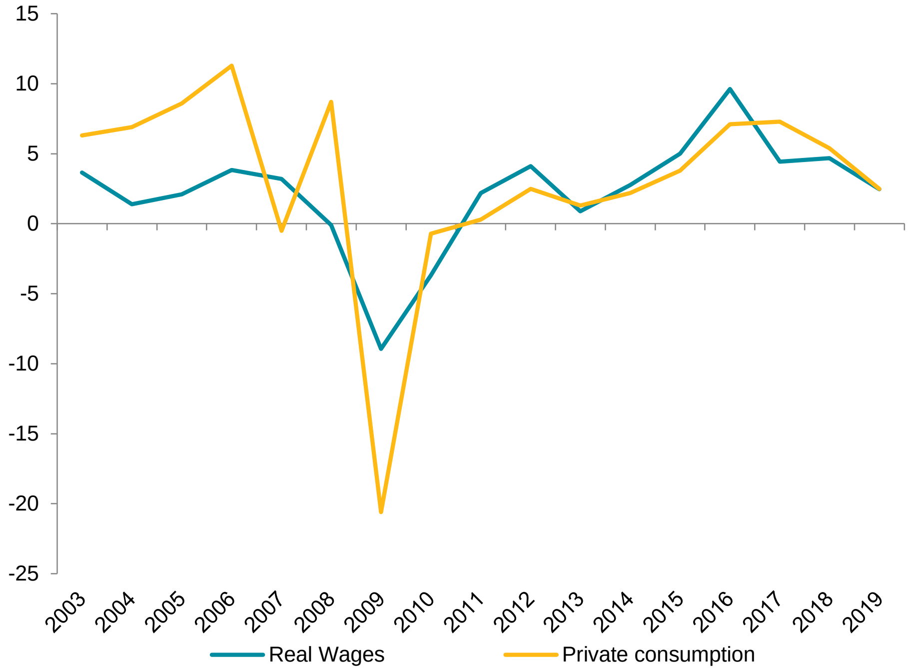
Private consumption and related indicators

YoY real change (l.axis) and index (r.axis)



Real wages and private consumption

YoY change (%)



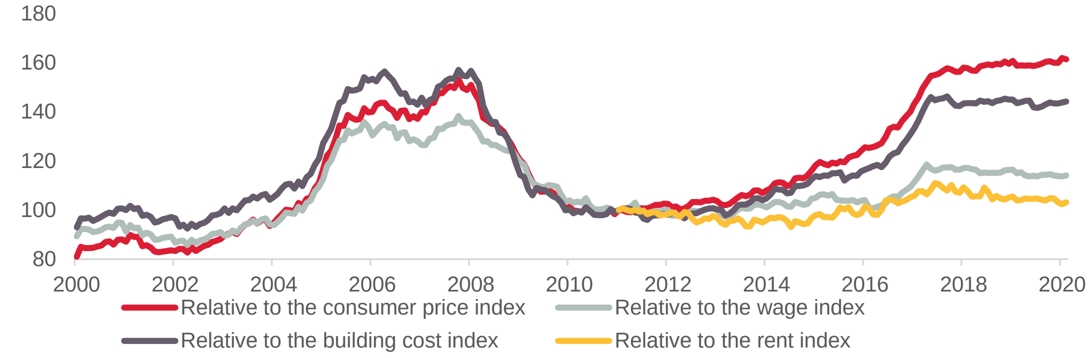
Source: Staitstics Iceland

Real estate market in balance

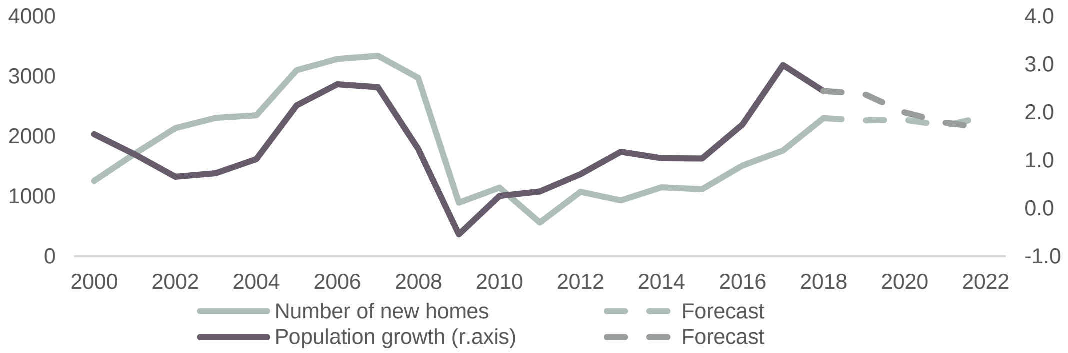
But COVID-19 pandemic likely to affect demand in coming term

Capital area house prices relative to macroeconomic fundamentals

Index, January 2011=100

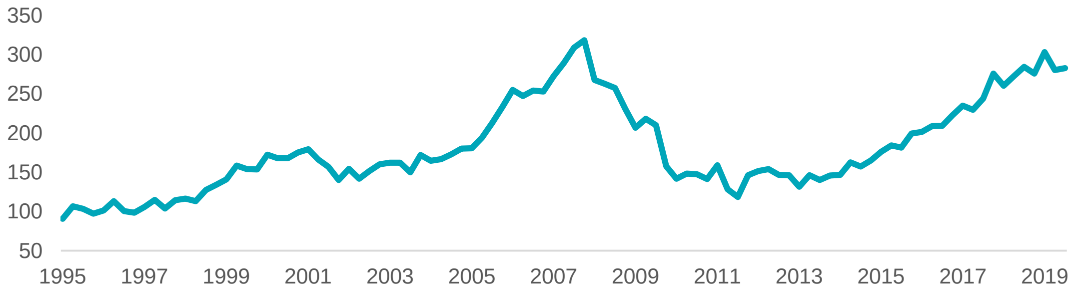


New apartments and population increase



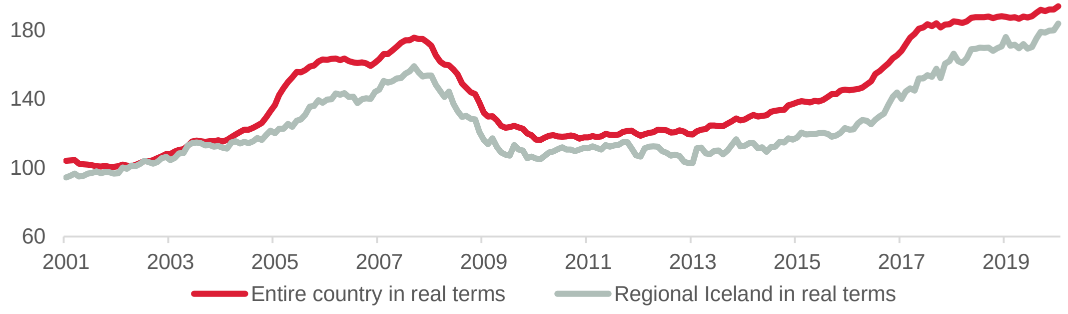
Commercial property real prices in greater Reykjavik

Index, 1995=100



Market price of residential housing

Index, 1995=100



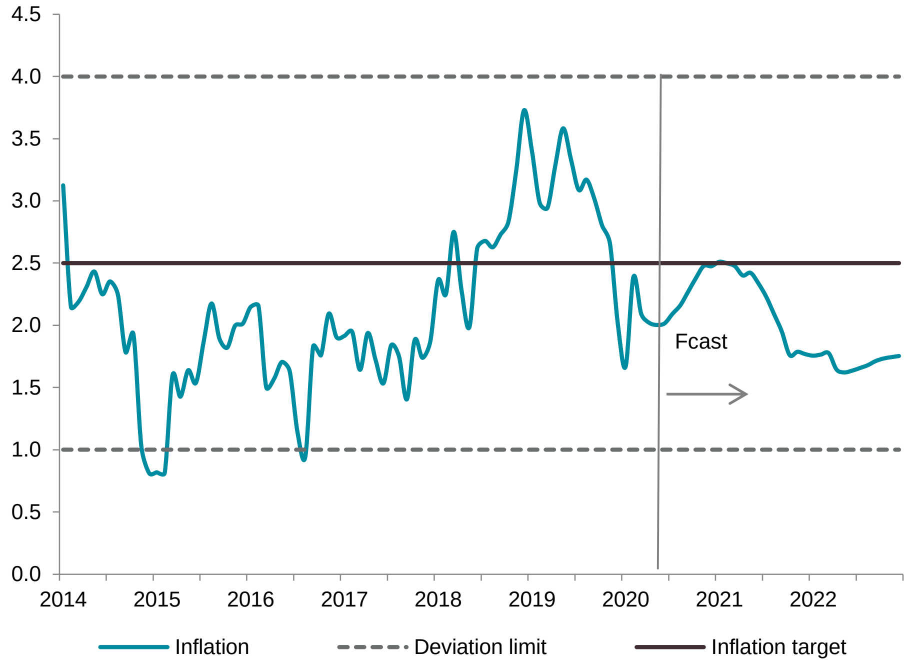
1. Dotted lines: forecasts by Statistics Iceland and the Federation of Icelandic Industry
Source: Statistic Iceland and ISB Research

Inflation holds steady

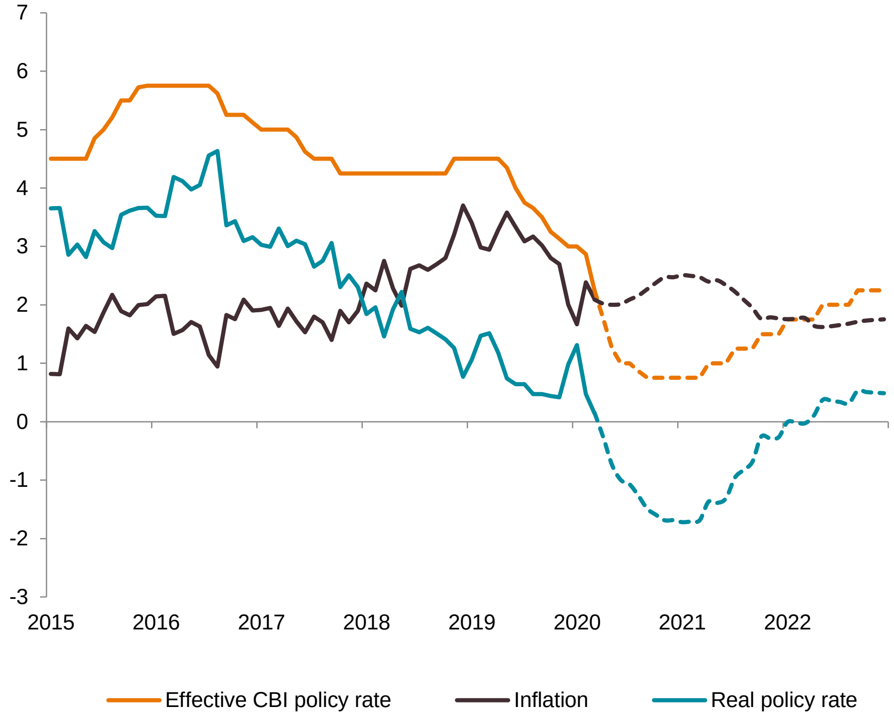
Policy rate historically low and will get lower

- ISK has depreciated by an average of 14% year-to-date against major currencies, owing to the COVID-19 pandemic
- Inflation measured 2.1% in March and the outlook is for modest inflation during forecast horizon despite ISK depreciation
- ISB Research expects inflation to remain at or below CBI's target this year, averaging 2.2%. In 2020 we expect it to reach 2.6% at the beginning but taper off again in few months. On average inflation will be 2.2% in 2021 and 1.7% in 2022
- The main uncertainties in the inflation outlook are potential ISK depreciation, reduced domestic inflationary pressures and stagnation/decline in house prices
- To mitigating the economic blows from the COVID-19 epidemic CBI's lowered policy rate by 1.0 percentage in March. CBI's policy rate has been lowered by 1.25 percentage total in 2020
- The policy rate is now lower than at any time since the adoption of the inflation target in 2001. We expect the policy rate to fall further and then begin rising in mid-year 2021 as the economic outlook improves

Inflation and contribution of main subitems
%



Inflation, policy rate and real policy rate
%



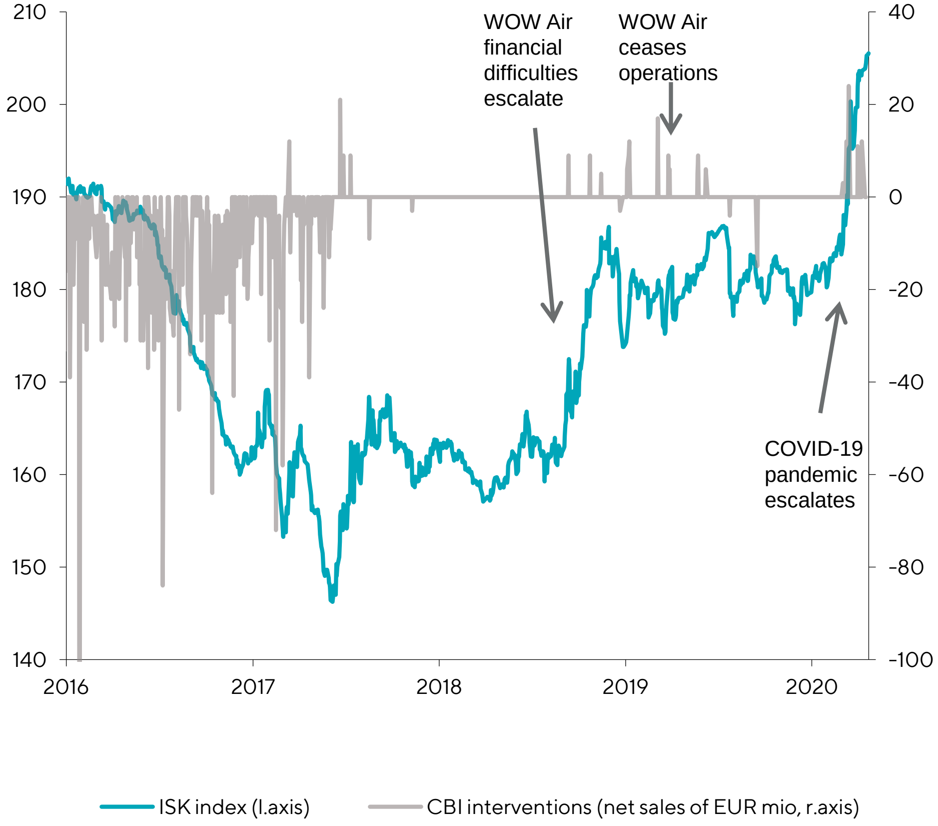
1. Dotted lines indicate ISB Research forecasts
Source: Statistic Icelandthe Central Bank of Iceland and ISB Research

ISK has depreciated as pandemic impact has deepened

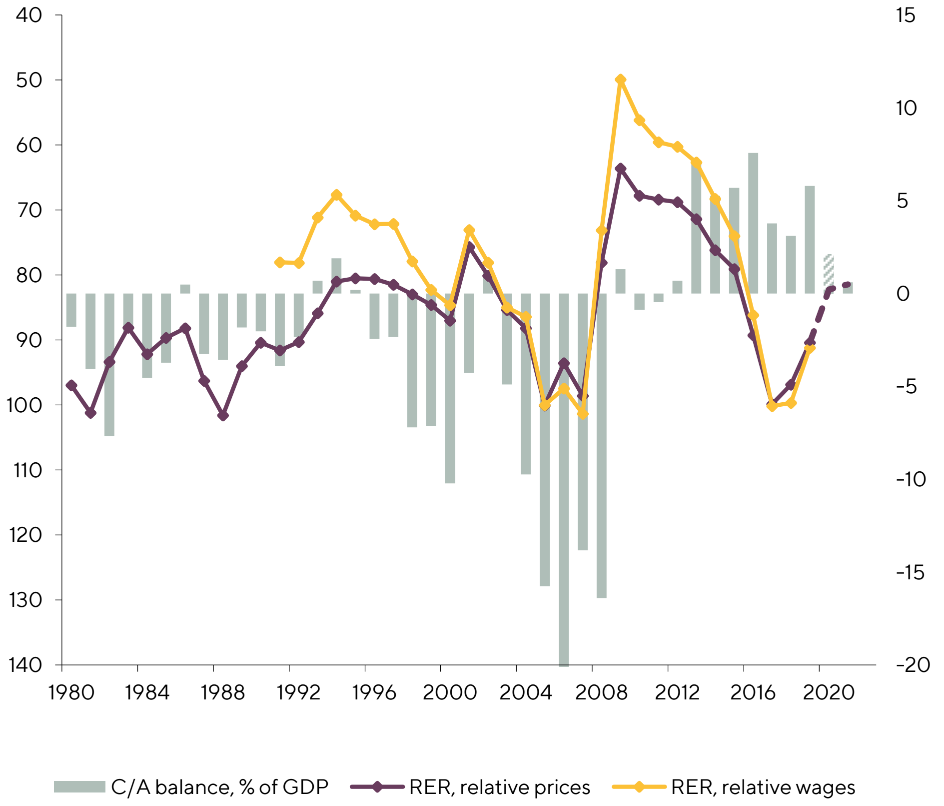
Real exchange rate likely to facilitate recovery of export sector in due course

- Following a period of relative stability throughout 2019 despite setbacks in the export sector, the ISK depreciated by 8% in Q1 2020.
- The pace of depreciation accelerated in line with darkening short-term prospects as the COVID-19 pandemic impact increased.
- The Central Bank has intervened in the market on numerous occasions in 2020, in line with its stated objective of providing short-term liquididty to the interbank FX market and reducing volatility
- Further depreciation cannot be excluded short-term, although at present levels the ISK would likely be broadly supportive for export sector recovery
- The real exchange rate has declined by almost 20% since peaking in 2017. Iceland is therefore in a considerably stronger competitive position once export sector conditions normalize.
- A positive net external position, sizeable FX reserves and a reasonably benign C/A outlook for the medium term should limit the risk of a substantial further depreciation of the ISK once the COVID-pandemic abates

ISK exchange rate and Central Bank FX interventions



Real exchange rate indices and current account balance



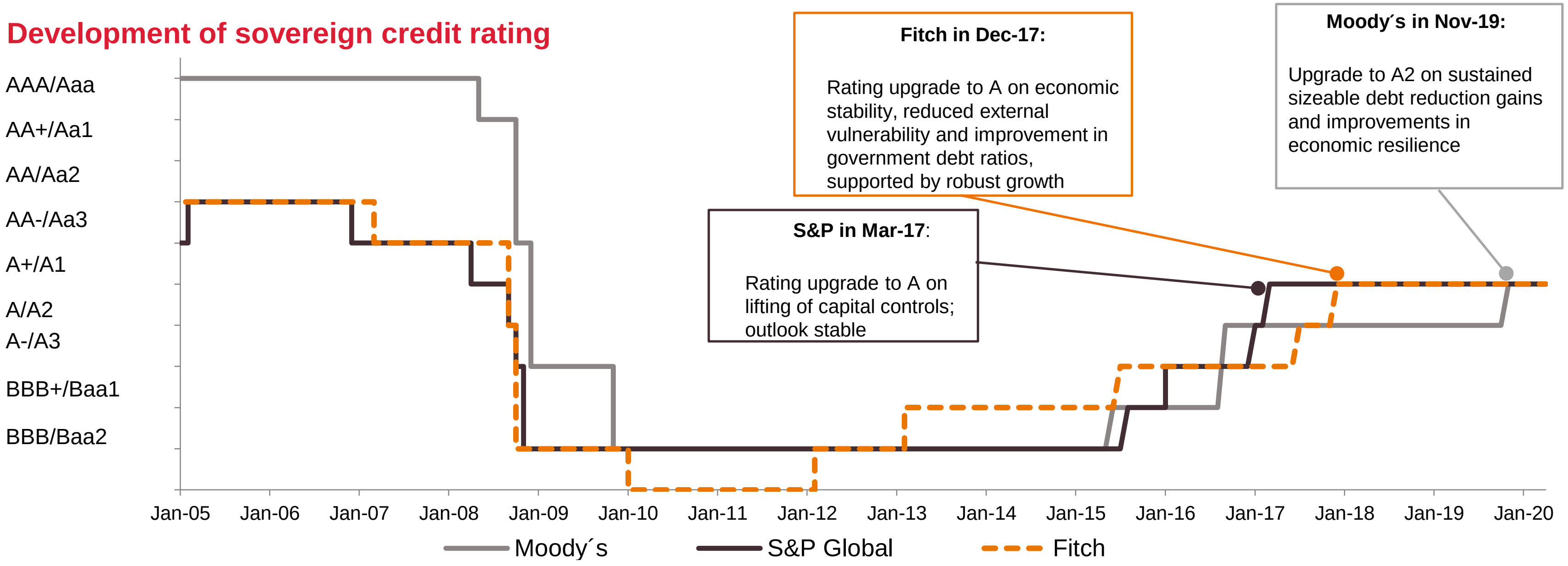
1. *Dotted lines indicate ISB Research forecasts*

Source: Central bank of Iceland, Statistics Iceland, Íslandsbanki Research

Iceland’s credit rating has remained stable

Setbacks in the tourist sector has not affected the sovereign ratings

Development of sovereign credit rating



MOODY’S IN NOVEMBER 2019

- The rating agency points out that Iceland‘s government debt has fallen substantially since 2011, more so than in any other rated sovereign in the post-crisis era.
- Refinements to the fiscal framework, including the Organic Budget Law, will further help to preserve these fiscal improvements.

FITCH IN MAY 2019

- Short-term rating upgraded to F1+
- The A rating balances the economy’s high income per capita, strong performance on governance, human development and doing business indicators against its high commodity export dependence, vulnerability to external shocks and experience of macroeconomic and financial volatility

S&P IN MAY 2019

- S&P Global Ratings affirmed its 'A/A-1' long- and short-term foreign and local currency sovereign credit ratings on the Republic of Iceland. The outlook is stable.
- The stable outlook reflects strong fiscal and external buffers, mitigated by risks stemming from the volatility of Iceland´s small open economy and a potentially abrupt slowdown in tourism

Source: Moody´s, S&P, Fitch Ratings and Central Bank of Iceland

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