Second Quarter 2021 Results

Íslandsbanki hf.

28 July 2021

FINANCIAL AND OPERATIONAL HIGHLIGHTS

Second quarter 2021 (2Q21) financial highlights – prosperous quarter with positive net impairment

- Íslandsbanki reported a net profit of ISK 5.4bn in the second quarter (2Q20: ISK 1.2bn) generating an annualised return on equity of 11.6% (2Q20: 2.8%) which is above the Bank's financial targets.

- Growth in loans to customers led an increase in net interest income YoY which totalled ISK 8.4bn in 2Q21 compared to ISK 8.2bn in 2Q20.

- Net fee and commission income grew 26% YoY and amounted to ISK 2.9bn in 2Q21. Fees from asset management, investment banking and brokerage as well as from loans contributed to the increase.

- Strong domestic equity market performance led to a net financial income of ISK 619m in 2Q21 compared to a loss of ISK 181m in 2Q20.

- Administrative expenses rose by 10.5% YoY totalling ISK 6.5bn in the 2Q21. Administrative expenses include an ISK 588m one-off cost in relation to the Bank's initial public offering (IPO), explaining the increase YoY.

- Cost-to-income ratio (C/I ratio) was 49.9% in 2Q21, down from 57.5% in 2Q20.

- The brighter outlook for the tourism industry contributed to a positive ISK 1.1bn net impairment on financial assets in 2Q21, in comparison to a net impairment charge, shaped by COVID-19, of ISK 2.4bn in 2Q20. The net impairment charge over loans to customers, the annualised cost of risk, was -0.42% in 2Q21 compared to 1.03% in 2Q20.

- Loans to customers grew 5.9% from end of March to ISK 1,090bn, and 8.2% for 1H21, driven in most part by mortgage lending but also by growth in loans to companies.

- At the end of the reporting period, the share of credit-impaired loans to customers was 2.1% (gross) down from 2.9% at year-end following full repayment of exposures in Stage 3.

- Deposits from customers grew ISK 67bn in the second quarter, and ISK 86bn for 1H21, large part of the increase is related to settlement of the Bank's IPO and thus temporary.

- The liquidity position remains strong with all ratios well above regulatory requirements and internal thresholds.

- Total equity amounted to ISK 190bn at the end of June and the Bank's capital ratio was 22.9%, up from 21.9% at 1Q21, considerably higher than the total capital ratio target which is currently at 18.3-19.8%. The leverage ratio was 12.4% at the end of June compared to 12.6% for 1Q21, indicating low leverage.

First half 2021 (1H21) financial highlights – net profit turnaround

- The Bank's net profit for the first half of year 2021 was ISK 9.0bn (1H20: ISK -131m) with annualised return on equity for 1H21 of 9.7% compared to a -0.1% in 1H20.

- Net interest income totalled ISK 16.6bn in 1H21, a fall of 1.2% YoY which is explained by lower interest rate environment between periods.

- Several factors contributed to a 20.2% increase in net fee and commission between years including fees from asset management, investment banking and brokerage as well as fees from loans. Net fee and commission income totalled ISK 5.8bn for the first half of the year.

- Net financial income was ISK 912m compared to a loss of ISK 1.9bn for 1H20.

- Administrative expenses rose between years, mostly explained by a one-off cost in relation to the Bank's IPO.
- Cost-to-income ratio dropped significantly YoY from 60.1% in 1H20 to 50.6% in 1H21.
- Net impairment on financial assets was a positive ISK 622m in the first half of 2021, due to brighter outlook for the tourism industry, compared to a charge of ISK 5.9bn in 1H20 which reflected the economic situation following the start of COVID-19.

Key figures and ratios

		2Q21	2Q20	1H21	1H20	2020
PROFITABILITY	After tax profit (loss), ISKm	**5,431**	1,245	**9,046**	(131)	6,755
	Return on equity	**11.6%**	2.8%	**9.7%**	(0.1%)	3.7%
	Net interest margin (of total assets)	**2.4%**	2.6%	**2.4%**	2.7%	2.6%
	Cost-to-income ratio[1]	**49.9%**	57.5%	**50.6%**	60.1%	54.3%
	Cost of risk	**(0.42%)**	1.03%	**(0.12%)**	1.28%	0.91%
		30.6.21	31.3.21	31.12.20	30.9.20	30.6.20
BALANCE SHEET	Loans to customers, ISKm	**1,089,723**	1,029,415	1,006,717	970,309	933,320
	Total assets, ISKm	**1,446,860**	1,385,235	1,344,191	1,328,724	1,303,256
	Risk exposure amount, ISKm	**924,375**	954,712	933,521	942,339	923,133
	Deposits from customers, ISKm	**765,614**	698,575	679,455	698,610	681,223
	Customer loans to customer deposits ratio	**142%**	147%	148%	139%	137%
	Non-performing loans (NPL) ratio[2]	**2.1%**	2.4%	2.9%	3.3%	3.6%
LIQUIDITY	Liquidity coverage ratio (LCR), for all currencies	**187%**	172%	196%	136%	179%
	Net stable funding ratio (NSFR), for all currencies	**122%**	119%	123%	113%	117%
CAPITAL	Total equity, ISKm	**190,355**	185,471	186,204	182,509	179,722
	Total capital ratio	**22.9%**	21.9%	23.0%	22.2%	22.2%
	Tier 1 capital ratio	**20.1%**	19.2%	20.1%	19.4%	19.4%
	Leverage ratio	**12.4%**	12.6%	13.6%	13.4%	13.4%

1. Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund - One-off items) / (Total operating income - One-off items)
2. Stage 3, loans to customers, gross carrying amount

Birna Einarsdóttir, CEO of Íslandsbanki

We are pleased to report that Íslandsbanki's profit in the second quarter was ISK 5.4bn, with an annualised return on equity of 11.6% which is above the Bank's target. Net impairment on financial assets was positive, amounting to ISK 1.1bn, a turnaround from a net impairment charge for the second quarter last year which was heavily impacted by COVID-19. Net fee and commission income is a good deal stronger compared to same period last year and the cost to income ratio is just under 50%. The loan book growth continues with 8% increase from year-end. The real estate market is robust, and we see an increase in mortgages but also in loans to both SMEs and large corporates.

The second quarter was an eventful one as the Bank's shares were listed on Nasdaq Iceland Main Market on 22 June - the largest initial public offering in Iceland. The Bank's flotation saw record participation from investors with a huge oversubscription resulting in the largest shareholder base of any listed company in Iceland.

Second quarter 2021 (2Q21) operational highlights

- Íslandsbanki was listed on Nasdaq Iceland Main Market on 22 June after the successful completion of the Bank's initial public offering (IPO) in which Icelandic State Financial Investments (ISFI), on behalf of the Icelandic Government, sold a 35% stake in the Bank. The IPO represented the largest one in Iceland's history and the largest European bank IPO since 2018. Citigroup Global Markets Europe AG, Íslandsbanki hf. and J.P. Morgan AG acted as joint global co-ordinators and joint bookrunners on the offering. Barclays Bank Ireland PLC, HSBC Continental Europe, Fossar Markaðir hf. and Landsbankinn hf. acted as joint bookrunners for the offering. Arion banki hf. and Kvika banki hf. acted as joint lead managers, and Arctica Finance hf., Íslenskir fjárfestar hf. and Íslensk verðbréf hf. as co-lead managers. STJ Advisors Group Limited acted as financial adviser to the selling shareholder, and ABN AMRO Bank N.V. as financial adviser to Íslandsbanki.

- The Bank held its shareholders' meeting on Wednesday 26 May at the Bank's headquarters. The meeting accepted a proposal to donate of a part of the Bank's art collection to art museums. Harpa Þórisdóttir, museum director of the National Gallery of Iceland, and Björn Steinar Pálmason, Chief Financial Officer of the National Gallery of Iceland, came to the meeting to accept the artwork. The meeting also approved a proposal to amend the Bank's Articles of Association and a proposal on the Rules of Procedure of the Nomination Committee.

- In April the refinancing of Míla, a subsidiary of Síminn was completed. Íslandsbanki, together with Lazard, has been mandated to advise on Míla's strategic goals and future possibilities.

- An ISK 6.5bn green long-term loan was extended to Reginn hf., a listed real estate company. The loan is aligned with Reginn's green financing framework and Íslandsbanki's sustainable financing framework. This was the second green loan facility allocated to Reginn.

- New lending to SMEs totalled ISK 27bn in 1H21 which represents a 74% increase YoY.

- June saw the largest month in new car financing to individuals since Ergo, the leasing arm of the Bank, was founded.

- Due to strong inflows into equity funds, balanced funds and asset portfolios from all client segments total assets under management at Iceland Funds grew by 8% during 1H21 and total ISK 377bn at the end of June.

- Íslandsbanki launched Meniga's Carbon Insight service to help customers fight climate change, enabling the Bank's app users estimate their carbon footprint based on spending.

- In April Íslandsbanki was awarded the 2021 Kuðungur prize (the Conch), the Ministry for the Environment and Natural Resources' environmental prize, for its outstanding work on environmental affairs in the past year. According to the adjudication panel, Íslandsbanki has made outstanding progress in environment-related matters and has created positive incentives to accelerate investment in green solutions via responsible lending, investment, and purchasing.

- In April, the Bank was rated with the highest rating (90 out of 100 points) for sustainability that has yet been awarded by local ratings agency Reitun.

- Íslandsbanki announced its commitment to achieving full carbon neutrality no later than 2040. The Bank's own operations have been carbon neutral for the past two years, and with this decision, its commitment will also extend to "financed emissions" which include the carbon footprint of Íslandsbanki's entire loan and asset portfolio. The Bank is the only Icelandic founding member of NZBA (Net-Zero Banking Alliance), an international alliance of 43 banks aiming for carbon neutrality.

- On 21 May, the Norwegian Finance Ministry, the Nordic CEOs for a Sustainable Future (of which Íslandsbanki is a member), and the Oslo Stock Exchange declared their support for the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), demonstrating a commitment to building a more resilient financial system and safeguarding against climate risk through better disclosures. Norway joins other Nordic countries – Sweden and Denmark – in its support of the TCFD, bringing the total number of national governments endorsing the Task Force's work to 12.

- The Bank continued on its digital journey and introduced the "funds in app" solution which enables retail clients to trade any of IS funds as well as view fund details and performance in the app. Furthermore, the app supported the biggest listing in Iceland during the Bank's IPO through the mobile app. Enabling "SmartId" in all the Bank's channels allows customers to move seamlessly from the internet to the mobile app without having to log in again. In June the Bank saw a monthly record number for digital origination of trading accounts.

- Íslandsbanki's branch in the Westman Islands was moved to a new address. The new branch is economical and designed with the customer experience in mind.

- 9 strategic projects have been defined and started for the later part of the year, to ensure further implementation of the Bank's strategy and to reinforce the path to the Bank's ROE target.

Operational highlights after close of period

- The Financial Supervisory Authority of the Central Bank of Iceland carries out an annual assessment of risk in the operations of systematically important financial institutions by means of a Supervisory Review and Evaluation Process (SREP). The process involves an assessment of the capital requirement for financial institutions which results in an additional capital requirement under Pillar 2. On 1 July the conclusion of this annual process for Íslandsbanki was made available. The Bank shall as of 30 June 2021 maintain an additional capital requirement of 2.5% of risk-weighted assets, which is an increase of 0.8 percentage points from the previous assessment. The Bank's total capital requirement, taking into account capital buffers, therefore increases from 17.0% to 17.8%. The increase is mostly due to temporary effects of COVID-19 and partially offsets the 2.0% reduction of the counter-cyclical capital buffer in March 2020. In the prospectus published on 7 June 2021 the Bank anticipated that the capital requirement was expected to rise and that such increase should be less than the reduction of the counter-cyclical buffer. This conclusion is therefore in line with the Bank's expectations.

- On 2 July the Bank signed an agreement with Arion Banki hf. under which Arion Banki hf. will act as market maker for shares issued by Íslandsbanki which are listed in the trading system of Nasdaq Iceland under the ticker symbol ISB. The agreement became effective as of 5 July 2021. The purpose of the market making agreement is to facilitate trading in the Bank's shares on Nasdaq Iceland to increase the liquidity of the Bank's shares, create market prices and to promote efficiency and transparency of price formation of shares.

INCOME STATEMENT

Economic recovery yields positive net impairment on financial assets

Income statement, ISKm	2Q21	2Q20	Δ	Δ%	1H21	1H20	Δ	Δ%	2020
Net interest income	**8,417**	8,228	189	2.3%	**16,607**	16,808	(201)	(1.2%)	33,371
Net fee and commission income	**2,907**	2,307	600	26.0%	**5,769**	4,798	971	20.2%	10,525
Net financial income (expense)	**619**	(181)	800	-	**912**	(1,919)	2,831	-	(1,391)
Net foreign exchange gain	**95**	208	(113)	(54.3%)	**225**	263	(38)	(14.4%)	451
Other operating income	**82**	71	11	15.5%	**204**	90	114	126.7%	197
Total operating income	**12,120**	10,633	1,487	14.0%	**23,717**	20,040	3,677	18.3%	43,153
Salaries and related expenses	**(3,594)**	(3,447)	(147)	4.3%	**(7,168)**	(6,694)	(474)	7.1%	(12,917)
Other operating expenses	**(2,894)**	(2,424)	(470)	19.4%	**(5,172)**	(4,869)	(303)	6.2%	(9,829)
Administrative expenses	**(6,488)**	(5,871)	(617)	10.5%	**(12,340)**	(11,563)	(777)	6.7%	(22,746)
Contribution to the Depositor's and Investors' Guarantee Fund	**(162)**	(247)	85	(34.4%)	**(344)**	(475)	131	(27.6%)	(679)
Bank tax	**(451)**	(399)	(52)	13.0%	**(861)**	(758)	(103)	13.6%	(1,588)
Total operating expenses	**(7,101)**	(6,517)	(584)	9.0%	**(13,545)**	(12,796)	(749)	5.9%	(25,013)
Profit before net impairment on financial assets	**5,019**	4,116	903	21.9%	**10,172**	7,244	2,928	40.4%	18,140
Net impairment on financial assets	**1,140**	(2,439)	3,579	-	**622**	(5,929)	6,551	-	(8,816)
Profit before tax	**6,159**	1,677	4,482	267.3%	**10,794**	1,315	9,479	720.8%	9,324
Income tax expense	**(769)**	(119)	(650)	546.2%	**(1,805)**	(888)	(917)	103.3%	(2,472)
Profit for the period from continuing operations	**5,390**	1,558	3,832	246.0%	**8,989**	427	8,562	2,005.2%	6,852
Discontinued operations held for sale, net of income tax	**41**	(313)	354	-	**57**	(558)	615	-	(97)
Profit (loss) for the period	**5,431**	**1,245**	**4,186**	**336.2%**	**9,046**	**(131)**	**9,177**	**-**	**6,755**
Key ratios									
Net Interest Margin (NIM)	**2.4%**	2.6%			**2.4%**	2.7%			2.6%
Cost-to-income ratio (C/I)	**49.9%**	57.5%			**50.6%**	60.1%			54.3%
Return on Equity (ROE)	**11.6%**	2.8%			**9.7%**	(0.1%)			3.7%
Cost of risk (COR)	**(0.42%)**	1.03%			**(0.12%)**	1.28%			0.91%

26% increase in net fee and commission income YoY

- Total operating income grew 14% YoY in the second quarter amounting to ISK 12.1 bn (2Q20: ISK 10.6bn).
- Net interest income grew 2.3% YoY and amounted ISK 8.4bn in 2Q21 compared to ISK 8.2bn in 2Q20. Growth in loans to customers contributed to the increase but average CB policy rate was 0.87% in 2Q21, down from 1.25% in 2Q20.
- Net interest margin on total assets was 2.4% in 2Q21, in line with 1Q21. Net interest margin on loans remained 2.2% YoY and net interest margin for deposits decreased YoY from 1.4% in 2Q20 to 1.1% in 2Q21.
- The boost in net fee and commission income YoY of ISK 600m or 26% is diversely sourced. Asset management income rose ISK 164m due to strong inflows into equity funds, balanced funds and asset portfolios, as well as performance related fees, and net income from investment banking and brokerage grew by ISK 90m. Increase in fees from loans and guarantees is mainly explained by strong lending activity.
- In 2Q21 the Bank recorded a gain of ISK 619m in net financial income compared to a loss of ISK 181m in 2Q20. Strong domestic equity market performance impacted the quarter.

Administrative expenses comparable YoY

- The rise in administrative expenses is mainly explained by a one-off cost related to Íslandsbanki's IPO. This one-off cost totalled ISK 588m in the second quarter and ISK 663m for the first half of the year. Excluding one-off cost, the Bank saw approximately 4% real reduction in YoY costs in 2Q21. Depreciation was lower in 2Q21 than in 2Q20 mainly because of higher depreciation of assets in 2Q20 as a result of a branch that was not reopened after COVID-19 shutdown.
- The number of FTEs at the end of the period excluding seasonal employees was 733 (745 at YE20) for the parent company and 768 for the Group (779 at YE20).

- The cost-to-income (C/I) ratio was 49.9% in 2Q21 compared to 57.5% in 2Q20. The C/I ratio excludes the bank tax and other one-off items.

Income tax expense

- Income tax expense for 1H21 amounted to ISK 1,805m compared to ISK 888m in 1H20.The effective tax rate for the period was 16.7%, compared to 67.5% in 1H20. Lower effective tax rate is explained by tax treatment of equity forwards. The bank tax accounted for ISK 861m in 1H21 (1H20: ISK 758m). The Bank is subject to the special financial tax of 6% on taxable profits over ISK 1bn, financial activities tax and social security charges, makes contributions to the Depositors' and Investors' Guarantee Fund, the Financial Supervisory Authority of the Central Bank, and the Office of the Debtors' Ombudsman. The contribution to the Depositors' and Investors' Guarantee Fund, was ISK 344m in 1H21 (1H20: ISK475m). Total taxes and levies amounted to ISK 4.0bn for the period compared to ISK 3.2bn for the same period 2020.

Positive net impairment on financial assets in 2Q21

- The positive net impairment of ISK 1.1bn in 2Q21 is mostly due to a brighter outlook for the tourism industry, reflected both in a shift between risk groups and in the weights of forward-looking scenarios.
- The annualised cost of risk, measured as net impairment charge over loans to customers, was -0.42% in 2Q21 and -0.12% in 1H21. The cost of risk for FY20 was 0.91%.
- The probability weights of the economic scenarios used to calculate the impairment were set to 15% (good), 50% (baseline), and 35% (bad) at end of 2Q21, effectively shifting 5% from baseline to good compared to end of 1Q21.

Strong financial performance in an eventful quarter

- Íslandsbanki reported a profit of ISK 5.4bn in 2Q21 (2Q20: ISK 1.2bn), generating a 11.6% annualised return on equity (2Q20: 2.8%). Positive net impairment charges on financial assets of ISK 1.1bn and strong domestic equity market performance contributed to financial results exceeding the Bank's financial targets. Strong underlying operations continue to support net interest income and net fee and commission income in the eventful quarter as the Bank listed its shares on Nasdaq Iceland Main Market.

BALANCE SHEET

Assets – 6% growth in loans to customers in 2Q21 driven by mortgages

Assets, ISKm	30.6.21	31.3.21	Δ	Δ%	31.12.20	Δ	Δ%
Cash and balances with Central Bank	**130,968**	88,748	42,220	47.6%	78,948	52,020	65.9%
Loans to credit institutions	**57,793**	103,333	(45,540)	(44.1%)	89,920	(32,127)	(35.7%)
Bonds and debt instruments	**110,499**	103,627	6,872	6.6%	128,216	(17,717)	(13.8%)
Derivatives	**2,649**	2,536	113	4.5%	6,647	(3,998)	(60.1%)
Loans to customers	**1,089,723**	1,029,415	60,308	5.9%	1,006,717	83,006	8.2%
Shares and equity instruments	**31,751**	25,763	5,988	23.2%	14,851	16,900	113.8%
Investment in associates	**911**	841	70	8.3%	775	136	17.5%
Property and equipment	**7,246**	7,191	55	0.8%	7,341	(95)	(1.3%)
Intangible assets	**3,307**	3,357	(50)	(1.5%)	3,478	(171)	(4.9%)
Other assets	**10,474**	17,566	(7,092)	(40.4%)	4,125	6,349	153.9%
Non-current assets and disposal groups held for sale	**1,539**	2,858	(1,319)	(46.2%)	3,173	(1,634)	(51.5%)
Total Assets	**1,446,860**	**1,385,235**	**61,625**	**4.4%**	**1,344,191**	**102,669**	**7.6%**
Key ratios							
Risk Exposure Amount (REA)	**924,375**	954,712	(30,337)	(3.2%)	933,521	(9,146)	(1.0%)
Non-performing loans (NPL) ratio[1]	**2.1%**	2.4%			2.9%		
Asset encumbrance ratio	**18.9%**	18.3%			18.7%		

1 Stage 3, loans to customers, gross carrying amount

Solid growth in loans to customers

- The growth of the Bank's assets by 4.4% in the quarter is mainly attributable to loans to customers which grew 5.9%. Since YE20 the Bank's assets have grown by 7.6%, driven by growth in loans to customers amounting to ISK 83bn or 8.2%. This growth is mainly driven by mortgages (ISK 63bn) which continue to grow in an active housing market driven by low interest rates. Loans to others than individuals grew by ISK 20bn from YE20.

- Outstanding loans to the tourism industry in Iceland at the end of June 2021 were 9% of the total loan portfolio.

- Loans are generally well covered by stable collateral, the majority of which is in residential and commercial real estate whilst the second most important collateral type is fishing vessels. The weighted average loan-to-value (LTV) ratio for the residential mortgage portfolio at end of June was 66%, comparable to 64% at YE20. Íslandsbanki's registered value of commercial real estate is less vulnerable to market fluctuations as collateral has risen at a much slower rate and lagged market prices in prior years.

- Four line-items, cash and balances with the Central Bank, loans to credit institutions, bonds and debt instruments, and shares and equity instruments, amounted to about ISK 331bn at the end of the period, of which ISK 312bn are liquid assets. Increase in equity instruments in 1Q21 are due to growth in equity forwards.

- Growth in other assets of ISK 6.3bn from YE20 is mainly because of more volume in unsettled transactions and includes increase in deferred tax assets.

- The Bank's asset encumbrance ratio was 18.9% at the end of 2Q21 compared to 18.3% at the end of March.

Quality of loan portfolio high and improving although COVID-19 aftermath is ongoing

- At the end of 2Q21, 9.7% of the gross performing loan book (not in Stage 3) was classified as forbearance, down from 11.1% at end of 2020. The majority of forborne loans are those that have had moratoria granted on a case-by-case basis to customers affected by COVID-19, mostly in the tourism sector. Despite being classified with forbearance, 62% have resumed regular payments.

- At the end of the reporting period, the share of credit-impaired loans to customers was 2.1% (gross) down from 2.9% at year-end following full repayment of material exposures in Stage 3.

Liabilities – strong capital and liquidity ratios combined with low leverage

Liabilities & Equity, ISKm	30.6.21	31.3.21	Δ	Δ%	31.12.20	Δ	Δ%
Deposits from Central Bank and credit institutions	**32,240**	31,565	675	2.1%	39,758	(7,518)	(18.9%)
Deposits from customers	**765,614**	698,575	67,039	9.6%	679,455	86,159	12.7%
Derivative instruments and short positions	**10,079**	9,533	546	5.7%	6,936	3,143	45.3%
Debt issued and other borrow ed funds	**398,786**	398,225	561	0.1%	387,274	11,512	3.0%
Subordinated loans	**25,297**	25,259	38	0.2%	27,194	(1,897)	(7.0%)
Tax liabilities	**6,025**	5,947	78	1.3%	5,450	575	10.6%
Other liabilities	**18,464**	30,660	(12,196)	(39.8%)	11,920	6,544	54.9%
Total Liabilities	**1,256,505**	1,199,764	56,741	4.7%	1,157,987	98,518	8.5%
Total Equity	**190,355**	185,471	4,884	2.6%	186,204	4,151	2.2%
Total Liabilities and Equity	**1,446,860**	**1,385,235**	**61,625**	**4.4%**	**1,344,191**	**102,669**	**7.6%**
Key ratios							
Customer loans to customer deposits ratio	**142%**	147%			148%		
REA/total assets	**63.9%**	68.9%			69.4%		
Liquidity coverage ratio (LCR)	**187%**	172%			196%		
Net stable funding ratio (NSFR)	**122%**	119%			123%		
Total capital ratio	**22.9%**	21.9%			23.0%		
Tier 1 capital ratio	**20.1%**	19.2%			20.1%		
Leverage ratio	**12.4%**	12.6%			13.6%		

Growth in customer deposits

- Deposits from customers grew by ISK 67bn in the quarter, of which large part is linked to the settlement of the Bank's IPO and thus temporary. Deposits from customers have grown by 12.7% or ISK 86bn since YE20. The ratio of customer loans to customer deposits fell from 148% YE20 to 142% at end of June. Deposits from retail and corporations are the Bank's main source of funding, comprising 46% of the Bank's total funding sources and 83% of the Bank's total deposit base at period end. Total deposits grew during the year, up 19% from retail customers and corporations and decreased 17% from financial institutions and pension funds. All deposit concentration levels are monitored closely, with concentration falling slightly during the year.

- Funding is raised to match the lending programme of the Bank using three main funding sources: stable deposits, covered bonds, senior unsecured bonds.

- Debt issued and other borrowed funds increased marginally from ISK 398bn at end of March to ISK 399bn at the end of June as the Bank continued to build on its main long-term funding sources by issuing covered bonds and senior unsecured bonds.

- The Bank has three EUR benchmark bonds outstanding placed with over 200 discrete investors in more than 20 countries. The Bank is also an active issuer in Scandinavian local currency bond markets and has issued numerous senior unsecured deals in SEK and NOK. The Bank has issued all 3 of its Tier 2 bonds in SEK.

- The Bank has demonstrated great consistency of access to foreign capital markets even at times of market turbulence with very strong participation from real-money investors across Europe.

- Credit spreads continued to compress globally during the year, and the Bank saw an opportunity to print two transactions in late June. Firstly, a SEK 200 million floating rate note (FRN) and a NOK 475 million FRN. Placed with Scandinavian investors, both bonds had maturities of 3 years and paid spreads of 80 basis points over their respective indices. Nordea and SEB managed the placements.

- The Bank continued its successful issuance of covered bonds during the quarter to fund the increase in mortgage lending. In 2021 the Bank has sold ISK 28bn of outstanding series, thereof ISK 18bn in 2Q21.

- In April, the Bank increased its green issuance by tapping its outstanding ISK green bond, ISB GB 25, for ISK 1.2bn at a fixed rate of 3.5%.

- Increase in other liabilities in 1H21 is mainly explained by higher volume of unsettled transactions.

- The liquidity position remains strong with all ratios well above regulatory requirements and internal thresholds. The Bank's total liquidity coverage ratio (LCR) was 187%, down from 196% at YE20. The LCR in foreign currencies fell to 287% at the end of the reporting period from 463% at YE20 and LCR in ISK was 133% at end of June compared to 95% at YE20. Of the total 38% increase to the ISK LCR, 20% was due to the forementioned cash settlement relating to the Bank's IPO.

- On 28 June, the Central Bank implemented new regulations for NSFR in all currencies according to the CRR II regulation, setting the regulatory minimum at 100%. Simultaneously, minimum requirements for NSFR in foreign currencies were annulled.

- The total net stable funding ratio (NSFR) was 122% at period end compared to 123% at YE20 and the NSFR in foreign currencies was 154% compared with 179% at YE20.

- After the Central Bank decided to stop offering one-month term deposits the Bank shifted ISK liquidity to Treasury bills, short-dated Treasury bonds and covered bonds to earn higher yield.

- As the Bank's liquidity position remains strong across currencies and above requirements, the Bank may consider debt buybacks or exchanges of outstanding transactions during 2021.

Capital ratios well above targets, excess capital in the amount of ISK ~30bn including capital structure optimisation

- Total equity amounted to ISK 190bn at the end of June 2021, compared to ISK 186bn at YE20. Thereof, ISK 419m is attributable to non-controlling interests.

- The Financial Supervision Committee announced on 1 July 2021 the results of the SREP concerning additional capital requirements (Pillar 2-R). The Bank shall as of 30 June 2021 maintain an additional capital requirement of 2.5% of risk exposure amount (REA), which is an increase of 0.8 percentage points from the previous assessment. The Bank's overall capital requirement, taking into account capital buffers, therefore increases from 17.0% to 17.8%.

- The Bank's total capital ratio target, which is the Bank's regulatory overall capital requirement in addition to the Bank's management buffer of 0.5-2.0% is currently 18.3-19.8%.

- Taking into account capital structure optimisation with the issuance of Additional Tier 1 instruments and assuming that the countercyclical buffer increases to 2%, the Bank estimates that long-term excess CET1 capital is approximately ISK 30bn.

- Due to the uncertainty in relation to the effects of COVID-19 on the capital base, the Bank aims to have an ample buffer above the current target until there is further clarity regarding international travel and other sources of uncertainty.

- At the end of June, the Bank's total capital ratio was 22.9% compared to 21.9% at the end of March. That is considerably higher than the Bank's total capital ratio target. The corresponding Tier 1 ratio was 20.1% up from 19.2% on 31 March.

- The capital base increased to ISK 212bn from ISK 209bn at March end based on retained earnings. The presentation of the total capital ratio has been changed, where expected dividend, based on 50% of the previous year's profit, is deducted from 1Q21 onwards.

- Íslandsbanki uses the standardised method to calculate its REA, which amounted to ISK 924bn compared to ISK 955bn at the end of March. REA amounts to 64% of total assets, compared to 69% at the end of March. The implementation of EU regulation 2019/876 in Iceland caused the reduction in REA, contributing to a 60bp rise in the capital ratios. The most material effect was the amendment of the SME supporting factor, which relaxes the conditions for obligors to be classified as small or medium sized enterprises allowing the supporting factor to be applied to a larger part of the Bank's loan portfolio lowering the REA. Another material amendment was the change in methodology for calculation of the exposure amount for counterparty credit risk, which leads to an increase in the REA.

- The leverage ratio was 12.4% at the end of June compared to 12.6% at the end of March, indicating low leverage.

Market risk well within appetite

- The Bank has modest market risk profile with market risk well within appetite. The Bank's market risk mainly derives from aggregate balance sheet imbalances in interest rate, inflation and currency positions as well as the Bank's liquidity portfolio managed by Treasury.

- The Bank is exposed to inflation risk because CPI-linked assets exceed CPI-linked liabilities. At the end of June, the Bank's consolidated net inflation (CPI) imbalance amounted to ISK 29.2bn, compared to ISK 25.1bn at the end of March. The imbalances are managed amongst other things via CPI-linked swaps, issuance of CPI-linked covered bonds and CPI-linked deposit programmes.

- The currency imbalance was ISK 1.2bn (0.6% of the total capital base) at the end of June, compared to ISK 3.6bn (1.7% of the total capital base) at the end of March. The Bank's imbalances are strictly monitored and are within regulatory limits.

Credit rating

- Íslandsbanki has a BBB/A-2 rating with a stable outlook, by S&P Global Ratings (S&P).

INVESTOR RELATIONS

An earnings conference call and webcast will take place on Wednesday 28 July

The Bank will host a virtual meeting in English for investors and market participants on Wednesday 28 July at 16.00 Reykjavík/GMT, 1700hrs London/BST, 1800hrs CET. Birna Einarsdóttir, CEO, and Jón Guðni Ómarsson, CFO, will give an overview of the second quarter financial results and operational highlights.

Participant registration is accessible **here**. A recording will be available after the meeting on the Investor Relations website. To participate in the webcast via telephone and in order to be able to ask questions please use the following dial-in details:

Iceland: +354 800 74 37
Denmark: +45 354 45 577
Sweden: +46 8 566 42 651
Norway: +47 235 00 243
United Kingdom: +44 33 330 00 804
United States: +1 631 913 1422

Confirmation Code: 67974052#

Financial calendar

Íslandsbanki plans to publish its financial statements according to the financial calendar below:

3Q21 results – 28 October 2021
4Q21 results – 10 February 2022
Annual General Meeting – 17 March 2022
1Q22 results – 5 May 2022
2Q22 results – 28 July 2022
3Q22 results – 27 October 2022

Please note that the dates are subject to change.

Additional investor material

All investor material will subsequently be available and archived on the Bank's Investor Relations website where other information on the Bank's financial calendar and silent periods is also available: https://www.islandsbanki.is/en/landing/about/investor-relations