3Q23 Financial Results

26 October 2023

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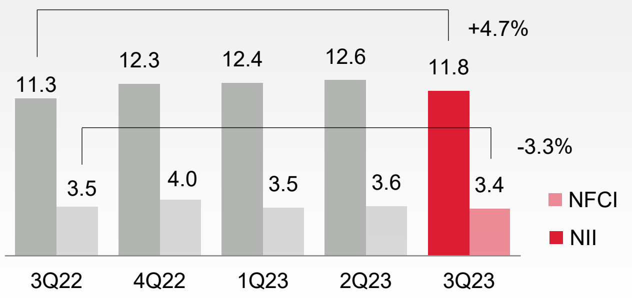
ROE of 11.0% in 3Q23 in a mixed business environment

Asset quality remains strong despite high inflation

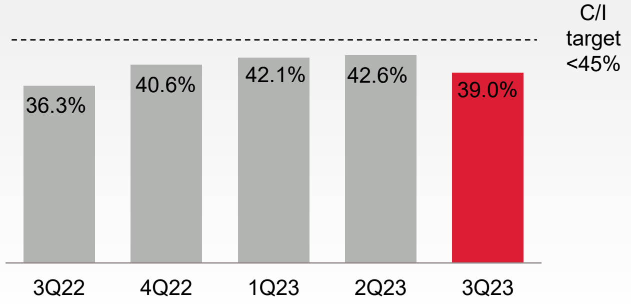
Core income growth between years

NII and NFCI, ISKbn



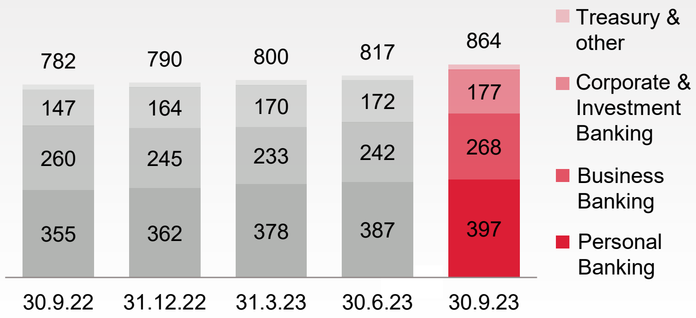
C/I ratio below guidance

C/I ratio[1]



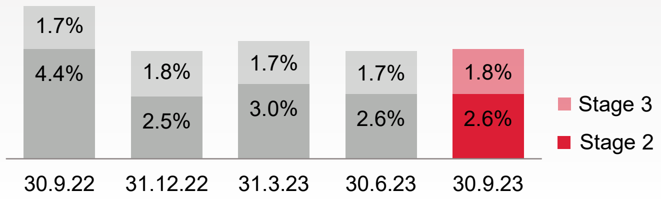
Diversified and growing deposit base

Deposits from customers



Asset quality continues to be strong

Loans to customers: Stage 2 and 3 (NPL)



1. C/I ratio in 2Q23 excludes a charge of ISK 860m due to an administrative fine. C/I ratio for 4Q22 included a provision of ISK 300m made in connection with an administrative fine, the C/I ratio has been restated so it excludes the provision.

Delivering on financial targets in the third quarter

CET1 ratio buffer increased during the quarter

	Target	3Q23
Return on equity	>10%	11.0% ✓
Cost-to-income ratio	<45%	39.0% ✓
CET1 capital buffer	100-300bp	580bp ✓
Dividend-payout-ratio	50%	

Highlights

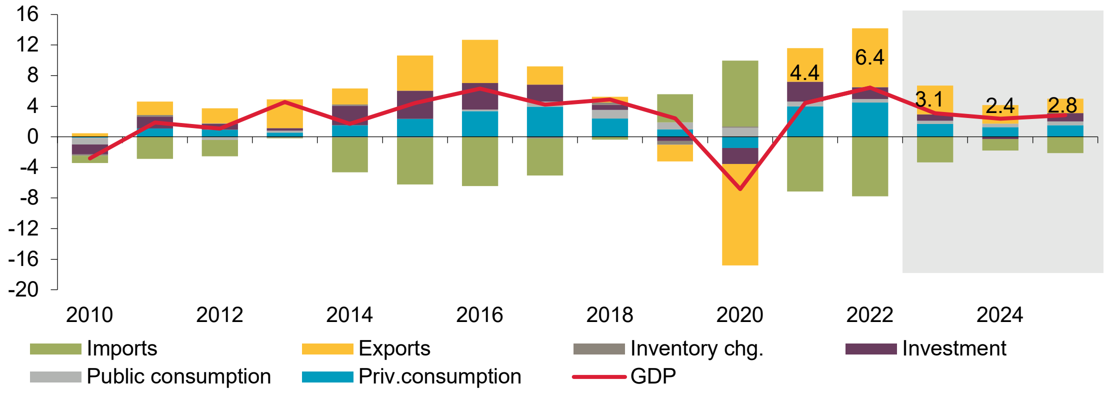
- Updated ROE guidance for 2023 is towards a range of 10.7-11.7%
- 2023 guidance for C/I ratio remains in the range of 40-45%
- Pillar 2-R requirement lowered from 2.6% to 2.4%
- Current CET1 target range of 16.2-18.2% and optimal operational CET1 capital at 17.2%, based on a 200bp capital buffer
- CET1 requirement will increase by 50bp in 1Q 2024 with an increase in the CCyB

Economy cooling as tighter policy has impact

GDP growth to lose steam in 2023 and then gradually regain strength

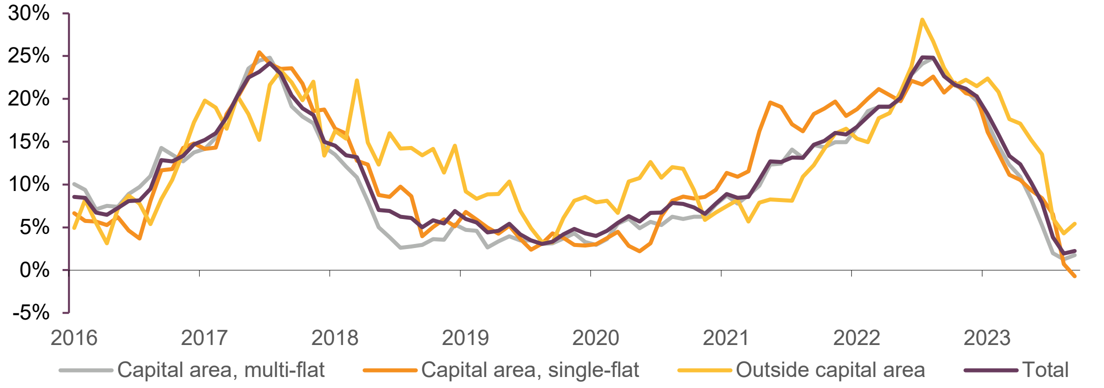
Considerably slower GDP growth tempo ahead as exports take lead..

Real GDP and main subitems, YoY change, %



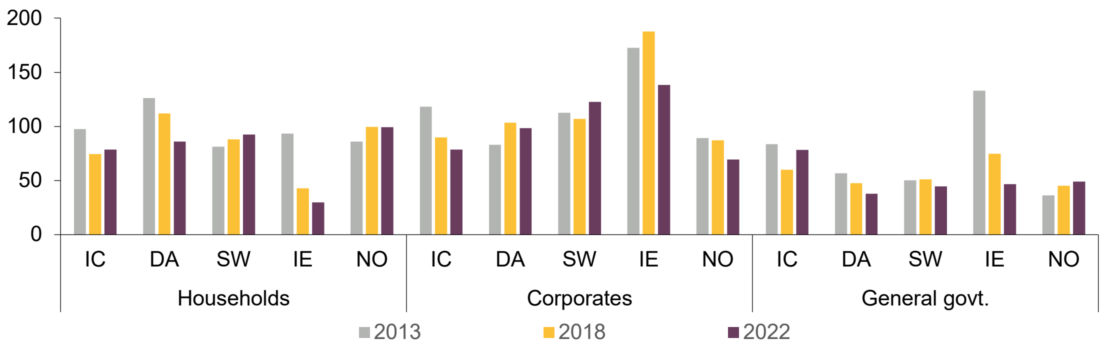
..and housing market prices have levelled off after steep price increases

Year-on-year increase in residential house prices



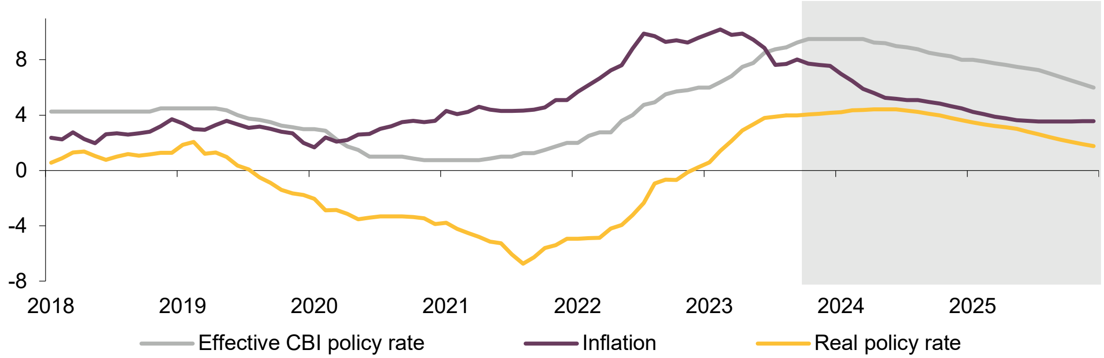
Moderate economy-wide leverage increases resilience to possible headwinds..

Gross debt of main economic sectors as % of GDP, Nordics and Ireland



...while tighter monetary policy is increasingly impacting demand and inflation

Inflation and policy rate,% Real policy rate b.o. expected forward inflation



Shaded areas indicate ISB Research forecasts. Source: Statistics Iceland, the Central Bank of Iceland and ISB Research.

Robust earnings in a mixed quarter

Universal banking model supports a solid result

Personal Banking

- **21.5%** ROE
- **40.4%** Cost-to-income ratio
- **3.0%** NIM

- All mortgages granted in September were granted through digital channels
- Enhanced customer services relating to fraudulent activities, including a 24/7 emergency service
- Fríða, the Bank's reward programme, exceeds the ISK 1bn turnover mark and is the biggest loyalty system locally

Business Banking

- **22.7%** ROE
- **29.8%** Cost-to-income ratio
- **6.3%** NIM

- Growth in lending volumes in 9M23 was 8.4%
- Highest NPS score amongst domestic peers for SMEs and 39% market share[2]
- Green car loans were 49% of all car loans granted during 9M23

Corporate & Investment Banking

- **11.9%** ROE
- **32.9%** Cost-to-income ratio
- **3.9%** NIM

- Strong market share amongst Iceland's 300 largest companies
- Asset management demonstrates resilience in a challenging market environment
- Derivatives Desk and FX Sales continue their solid performance

Iceland Funds

- **20.5%** ROE
- **63.8%** Cost-to-income ratio[1]
- AUM ISK **361bn**

- New PE fund, IS HAF fjárfestingar concluded its first two investments
- Slight decrease in total operating income compared to 9M22, by 1.5%

Allianz Ísland hf.

- **30%** ROE in 3Q23
- **70%** Cost-to-income ratio

- YTD results good despite despite increased clawback in 3Q23
- Continued robust results driven by revenue generation

1. As calculated from the Bank's Consolidated Income Statement. 2. Average of last two Gallup Surveys conducted in Q1 and Q2 2023.

Our fight against fraud

- Fraud attempts have increased alongside increased digital activity in banking services
- Íslandsbanki is raising awareness through training and education
- We offer enhanced services to customer who are victims of frauds – including a 24/7 emergency service

How we limit effects of fraud

Increased use of customer specific electronic ID to confirm purchase online

Newly implemented solution to sign out on all devices with a single click

24/7 emergency service

Fróði the friendly chatbot & NLP innovation

Leveraging AI to boost customer service and efficiency

> **85%**
Fróði customer satisfaction

> **96%**
Questions fully or partly answered

> **51%**
Requests answered by Fróði vs human advisors

> **1,575**
Requests that Fróði knows the answers to

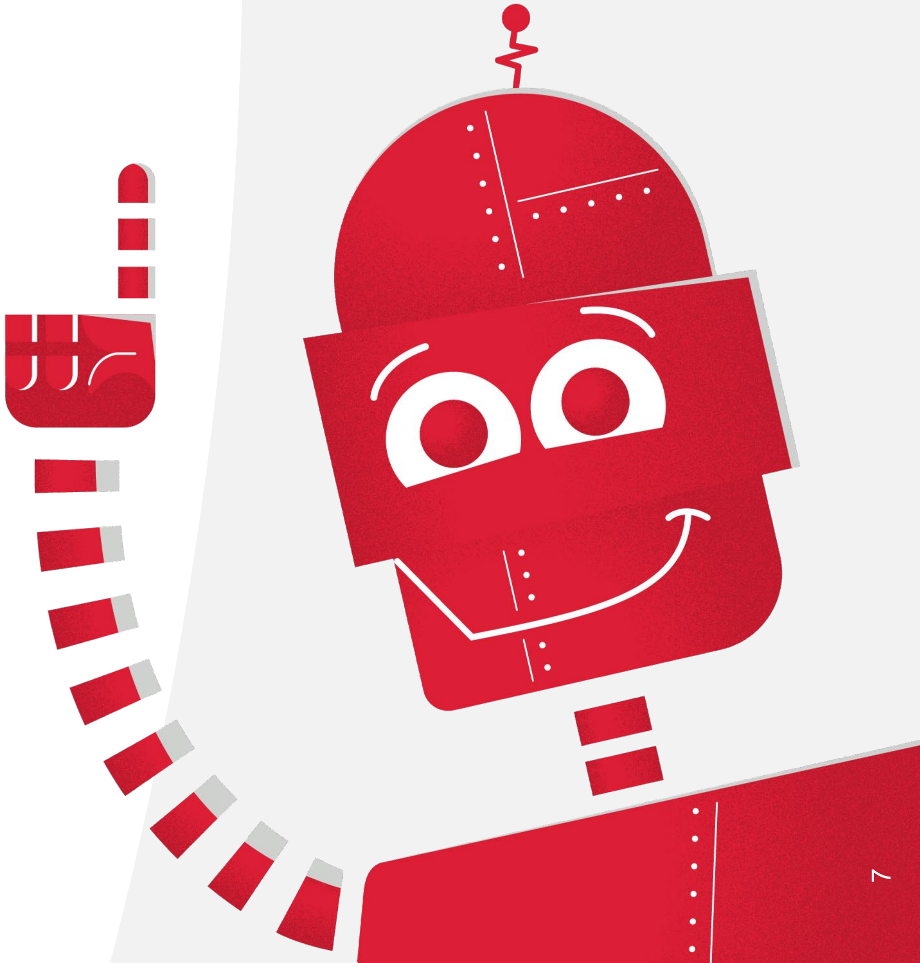
- Fróði was introduced as a staff member of Íslandsbanki 3 years ago and now answers more than half of all customer service chats
- Fróði consistently gets positive feedback from our customers
- Fróði has a near perfect track record when it comes to answering customer requests, solving most requests partly or fully
- Fróði got an award for being the „most likeable“ of all boost.ai chatbots, based on customer satisfaction ratings
- Fróði is constantly evolving and can now provide account balance, last transactions and IBAN numbers to customers, with digital authentication

Innovative NLP

- Íslandsbanki has implemented an innovative solution based on Natural Language Processing, in partnership with the Icelandic AI & NLP innovation company Miðeind
- The solution can process, review and correct text, grammar and suggest improvements
- The solution can even detect whether the text complies with the Íslandsbanki **tone of voice**, in line with marketing and PR guidelines

“Are you a living person or is the program really that well created?”

- Happy Fróði customer



Íslandsbanki's Entrepreneurship Fund

We support the blossoming start-up and entrepreneurial community in Iceland

ISK 165 million awarded in last three years

Íslandsbanki contributes a part of the annual balance of Vaxtasproti savings account to the Fund

The fund will offer support to projects that support the four UN Sustainable Development Goals that the Bank has chosen to focus on

4 QUALITY EDUCATION

5 GENDER EQUALITY

9 INDUSTRY, INNOVATION AND INFRASTRUCTURE

13 CLIMATE ACTION

Applications for grants from the Fund are accepted until 1 November 2023

We believe in great ideas

11,307
participants of all ages

ISK 200 million raised
for charities by participants

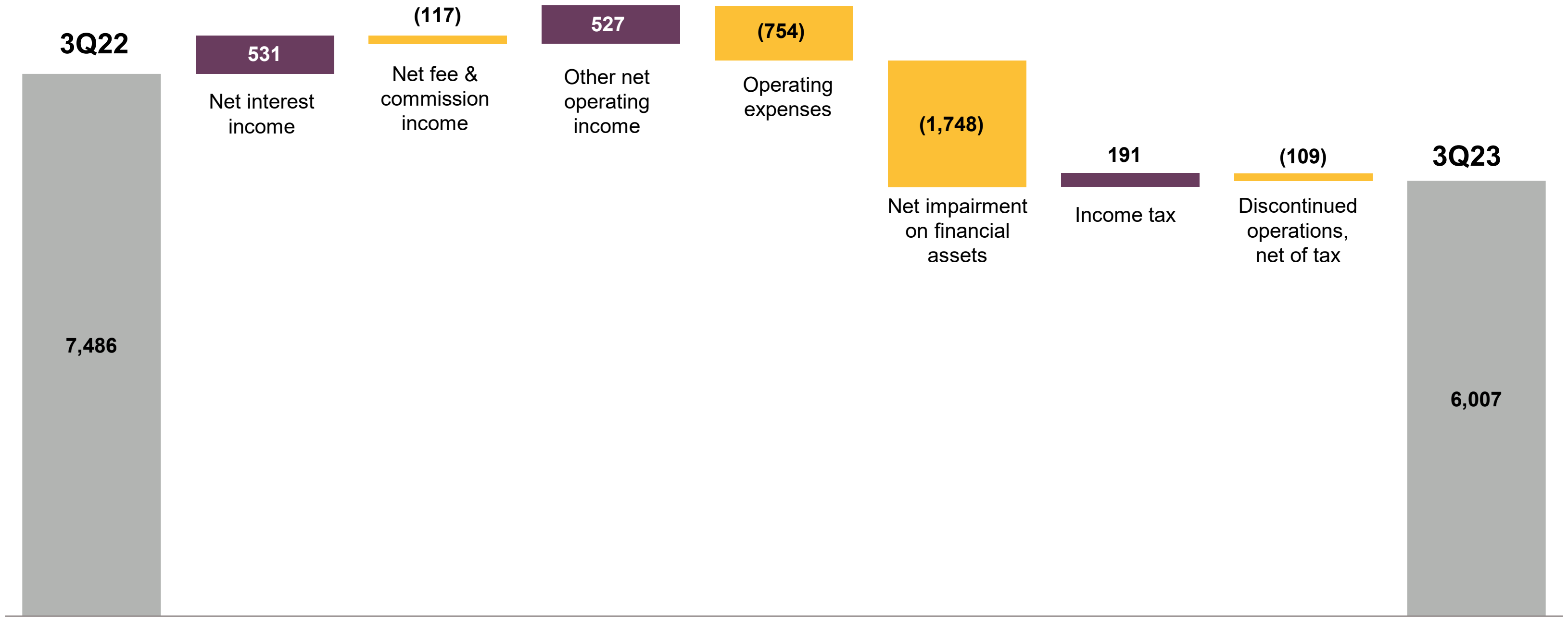
175
charitable organisations benefit

Financial overview

Core banking operations remain solid

Normalising impairments affect 3Q23

Profit for the period – 3Q22 vs 3Q23
ISKm



Core NII holding steady

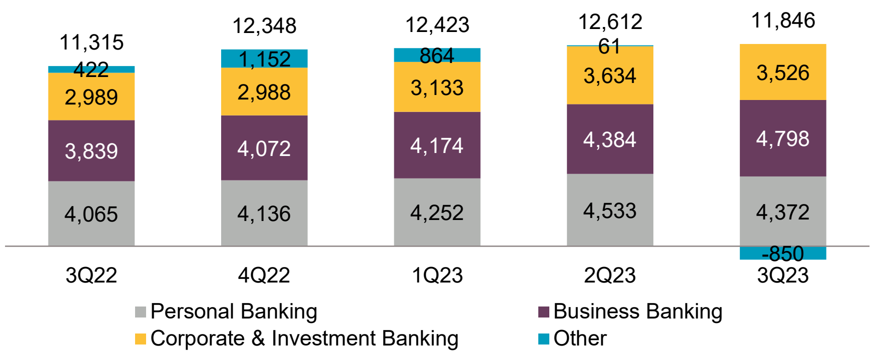
Central Bank policy rates unchanged in October meeting

Highlights

- Lending margin was 1.8% in 3Q23 (1.9% in 3Q22)
- Deposit margin was 2.0% in 3Q23 (2.1% in 3Q22)
- Net interest margin was 2.9% in 3Q23 (3.0% in 3Q22)
- Average CB policy rate rose from 5.1% in 3Q22 to 9.0% in 3Q23
- NII decreasing from 2Q23 due to higher Central Bank reserve requirements, loss on CPI imbalance compared to gain in 2Q23 and higher FX funding cost due to new issuance at the end of May

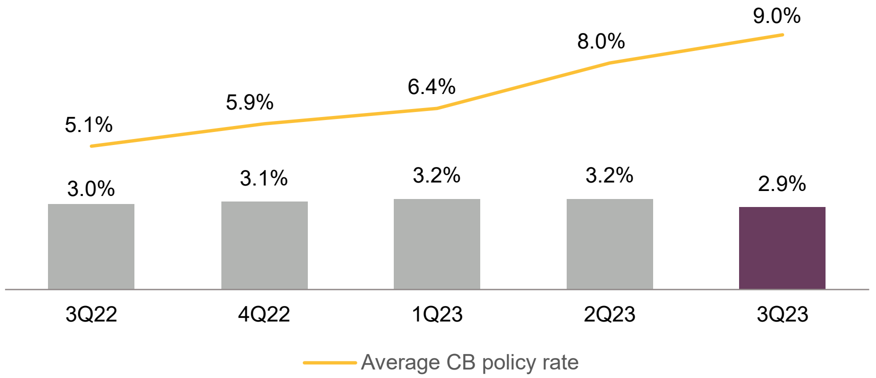
Net interest income

By business segments, ISKm



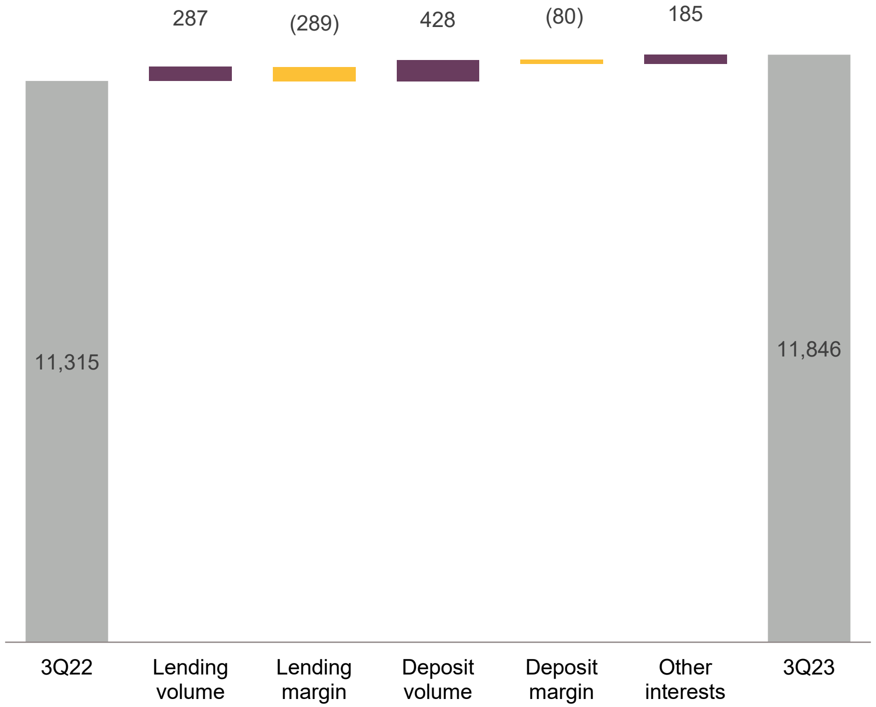
Net interest margin

On total assets



Net interest income – YoY comparison

ISKm



26 October 2023

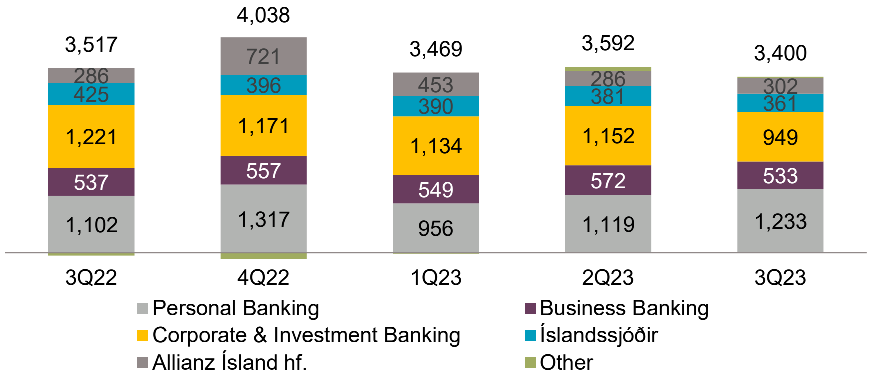
Strong fee income from cards and payment processing

Allianz Ísland hf., a subsidiary of the Bank, continues to contribute to NFCI growth

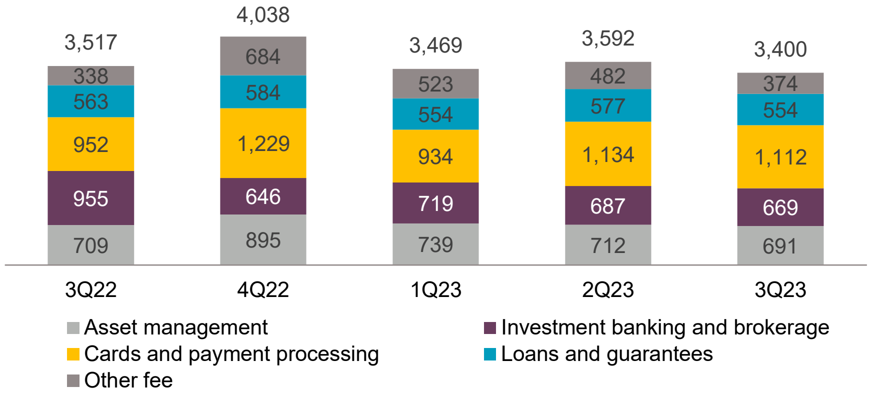
Highlights

- Income from cards and payment processing remains the largest type of NFCI
- Allianz Ísland hf., a subsidiary of the Bank is the largest contributor to other fee and commission income
- Lower income from asset management is explained by continuing drop in AuM due to market conditions and negative returns
- Fees from investment banking and brokerage decreased due to rough market conditions

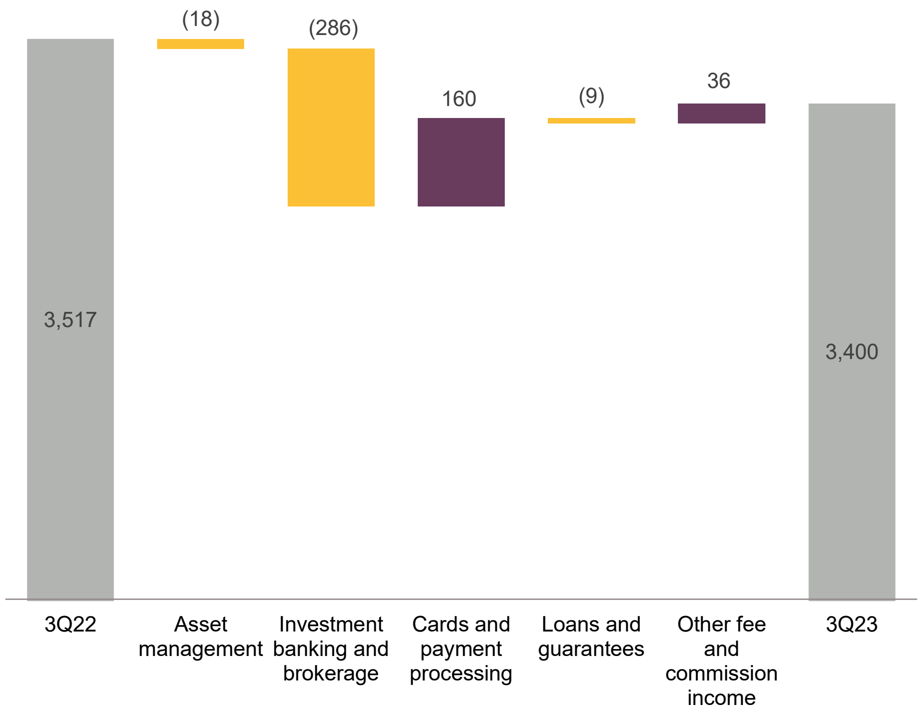
Net fee and commission income
Business segments, ISKm



Net fee and commission income
By type, ISKm



Net fee and commission income – YoY comparison
ISKm



NFI affected by volatile market environment

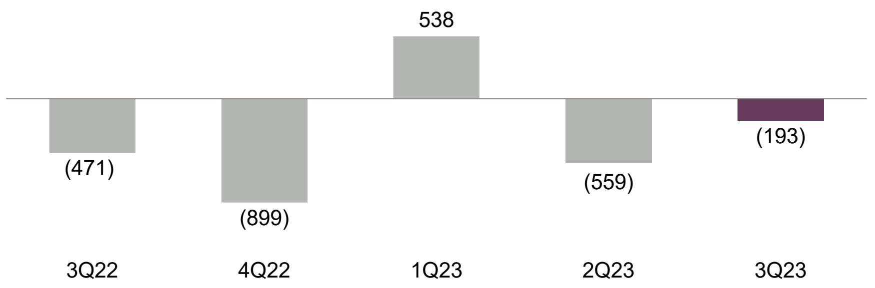
Equity exposures remain modest

Highlights

- Loss in NFI in the quarter is mainly due to loss from the liquidity portfolio due to a rise in ISK rates this year continues in the third
- Very challenging quarter on local and international bond markets
- Loss in bonds and related derivatives is resulting from a rise in ISK rates this year

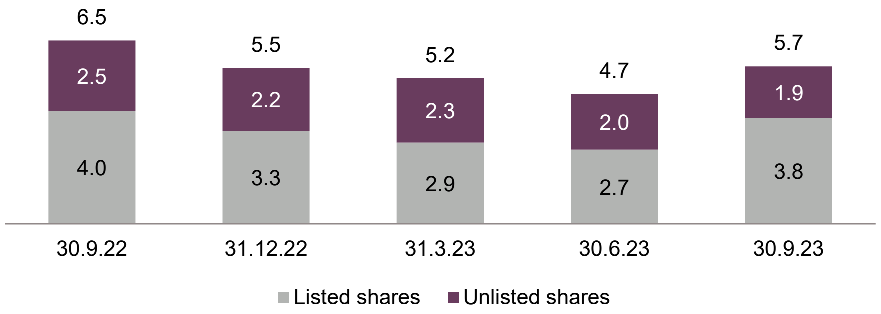
Net financial income (expense)

ISKm



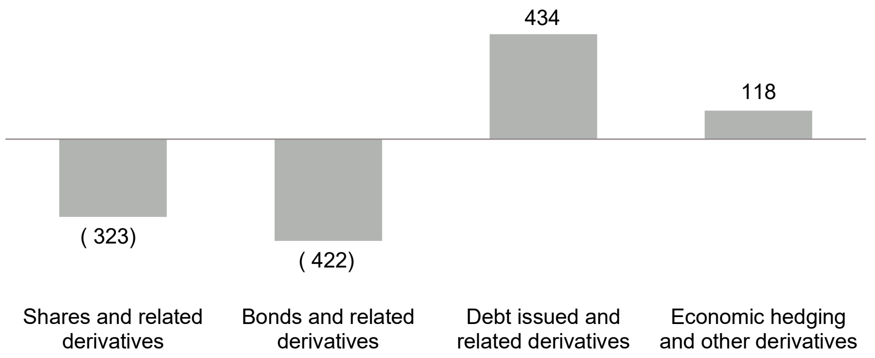
Shares and equity instruments [1]

ISKbn



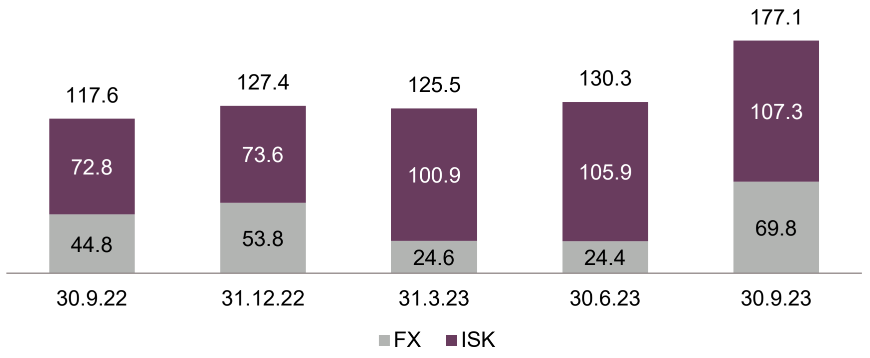
Net financial income (expense) by type in 3Q23

ISKm



Bonds and debt instruments [2]

ISKbn



1.Excluding listed shares and equity instruments used for economic hedging. 2. Excluding listed bonds and debt instruments used for economic hedging.

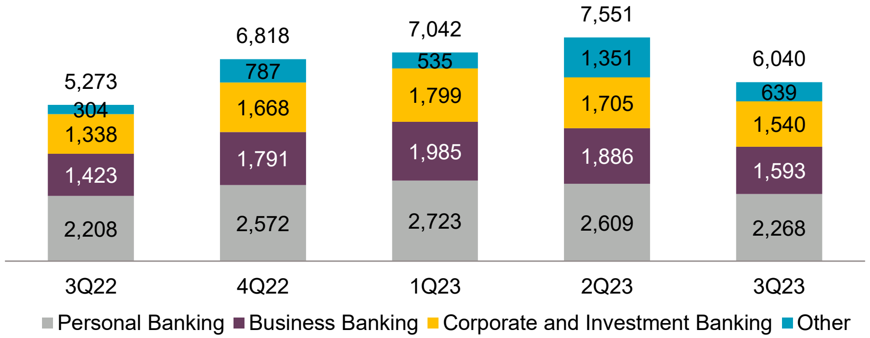
Cost-to-income ratio beats target

Seasonality in salary expenses supports low C/I ratio

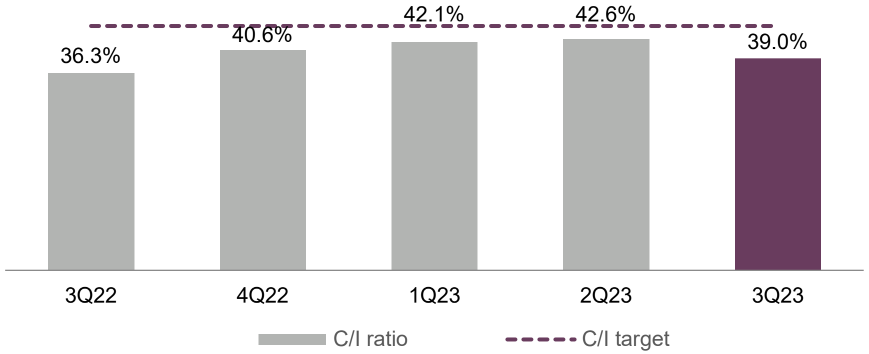
Highlights

- Decrease in salaries in 3Q23 is affected by seasonality in accrued leave
- Other operating expenses rose 14.0% YoY, mostly due to higher inflation, investments in IT and strategic advisory, consulting cost and increased AML costs

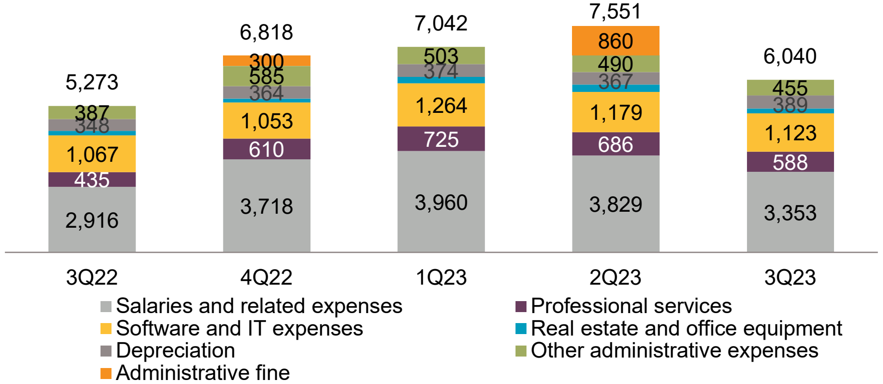
Administrative expenses
ISKm



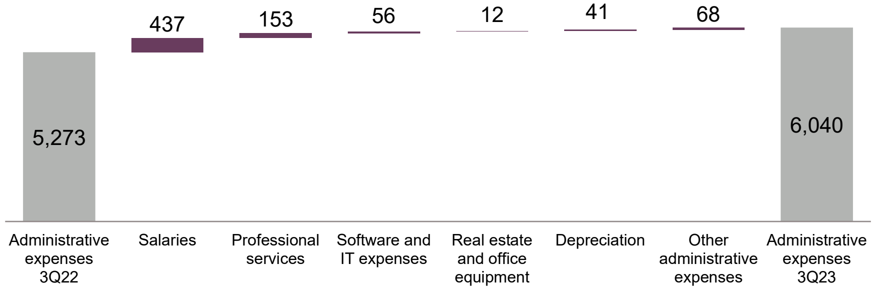
Cost-to-income ratio[1,2]



Administrative expenses – by type
ISKm



Administrative expenses – YoY comparison
ISKm



1. Calculated as (Administrative expenses + Contribution to the Depositor's and Investors' Guarantee Fund – one off items) / Total operating income – one-off items). 2. C/I ratio in 2Q23 excludes a charge of ISK 860m due to an administrative fine. C/I ratio for 4Q22 included a provision of ISK 300m made in connection with an administrative fine, the C/I ratio for 4Q22 has been restated so it excludes the provision.

Lending growth moderates

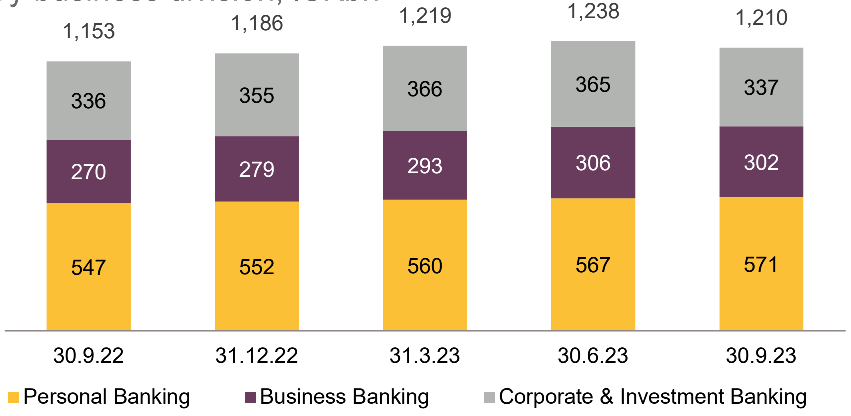
Diversified and highly collateralised loan portfolio

Highlights

- The credit quality of the Bank continues to be robust due to its strong risk management practices and conservative lending policies
- Loans to the construction industry has gradually increased and is now shown as a separate sector
- Credit exposure fully covered by collateral is ISK 1,128bn or 93% of loans to customers

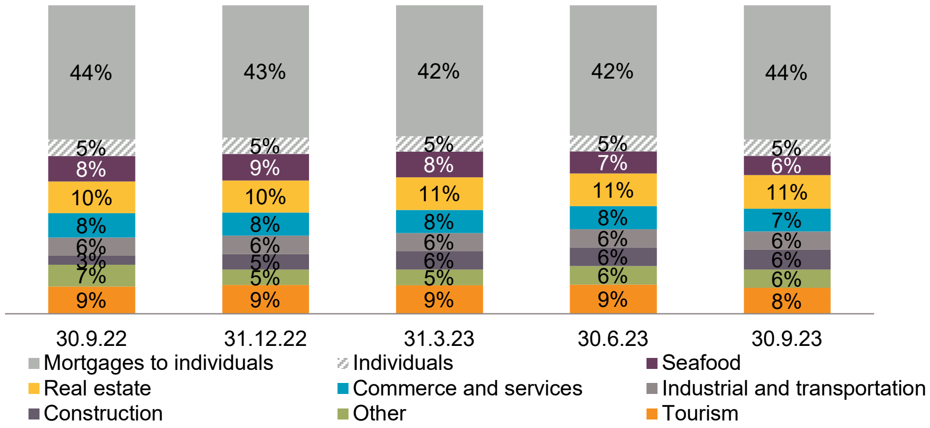
Loans to customers

By business division, ISKbn



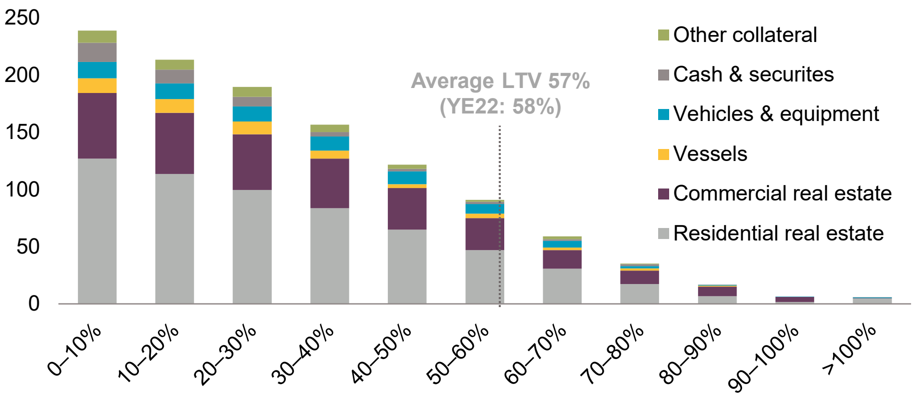
Loans to customers

By sector, with tourism as a separate sector



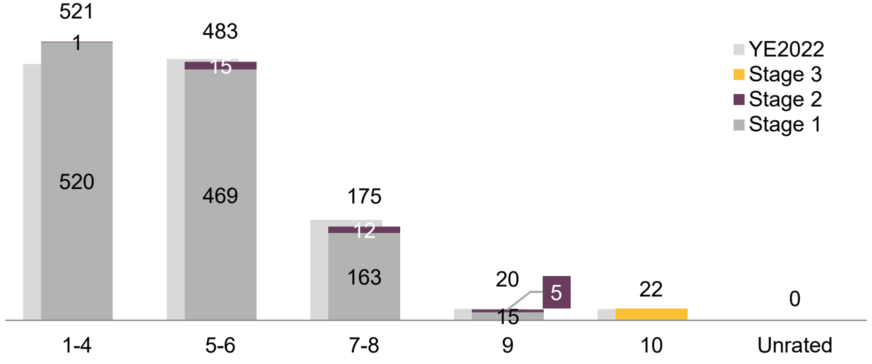
LTV distribution by underlying asset class

30.9.2023, loan splitting approach, ISKbn



Loans to customers: gross carrying amount[1]

30.9.2023, risk class and impairment stage, ISKbn



1. Risk class distribution at YE2022 shown as comparison

Credit quality remains strong

Stage 2 loans have reached normalised levels

Highlights

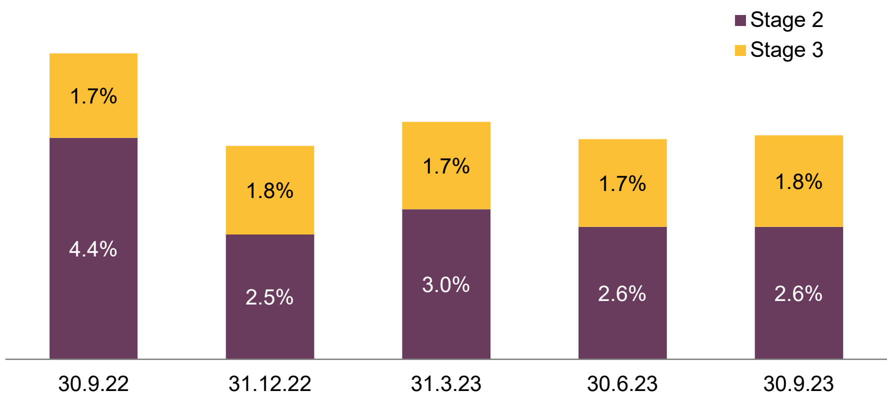
- The 3Q23 impairment increase is mostly due to a few distressed credit cases
- The definition of forbearance includes a 24-month probation period. Therefore, loans are classified as forborne even after normal payments have resumed
- Reserve coverage ratio (RCR) for impairment allowance on Stage 3 was 19.8% at end of 3Q23 reflecting good collateral position

Net impairment on financial assets

By period, ISKbn

Loans to customers: Stage 2 and 3 (NPL)

Development of gross carrying amount as ratio of total loans

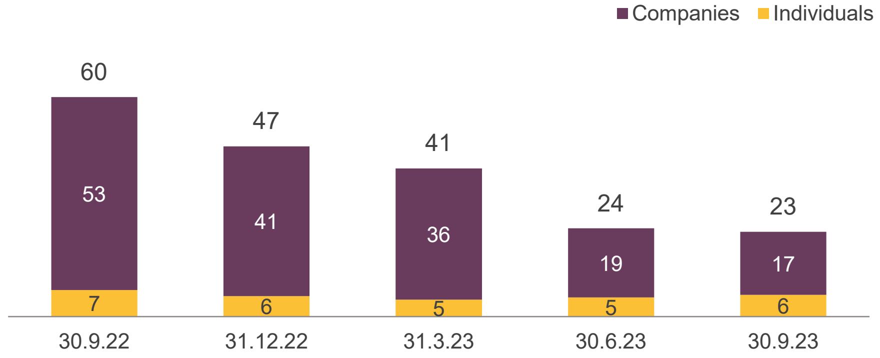


Current and expected cost-of-risk

- Annualised cost of risk was 19bp in 3Q23 (-40bp for 2Q23)
- Current impairment outlook relatively benign due to low unemployment and steady economic growth. Increased interest rates have not impacted the NPL ratio.
- The probability weights of economic scenarios were kept unchanged at 20% (good), 50% (baseline), and 30% (bad) at the end of 3Q23
- A shift of 5% from baseline to the bad scenario would increase the impairment allowance by ISK 0.3bn while 5% shift from the baseline to the good would decrease the allowance by ISK 0.2bn

Performing loans with forbearance

Gross carrying amount, ISKbn



Mortgage portfolio shows a shift to CPI-linked loans

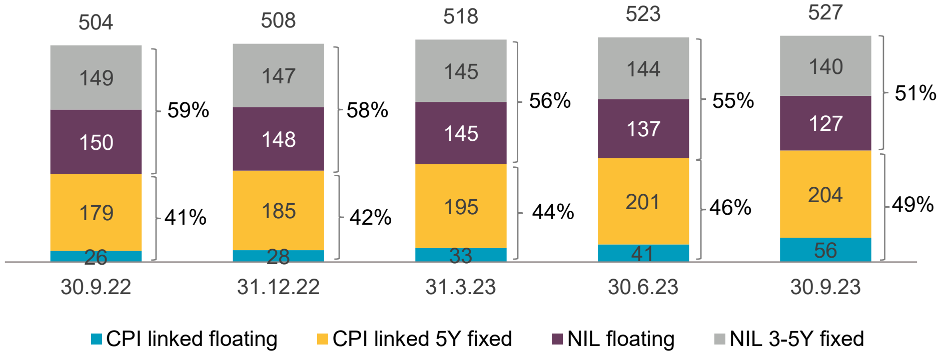
Loan to value is strong and supports this shift

Highlights

- Conservative payment assessment for non-indexed variable rate mortgages in the low interest environment means that households are well prepared for higher interest rate environment
- At origination, LTV is capped at 80% (85% for first time buyers) and debt service-to-income at 30% (35% for first-time buyers)
- Stage 2 loans have slightly increased since year-end 2022 without an uptick in NPL cases. This comes in conjunction with rising variable non-indexed linked (NIL) mortgage rates, elevated inflation, and marginally increased forbearance measures for households with mortgages.
- Growth in CPI-linked loans due to higher interest rate environment and increase in variable NIL mortgage rates

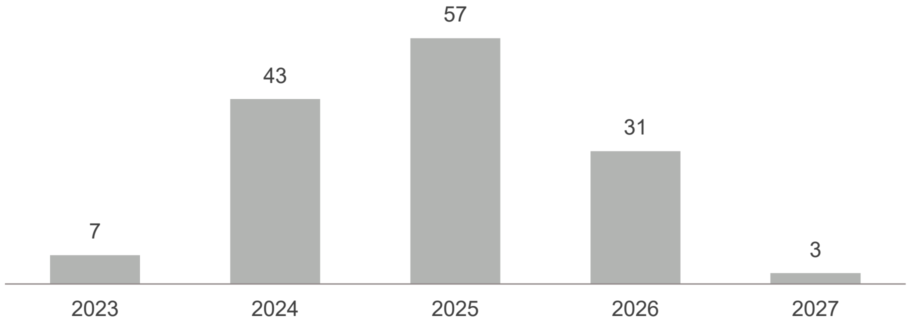
Mortgage portfolio

By interest rate type, gross carrying amount, ISKbn



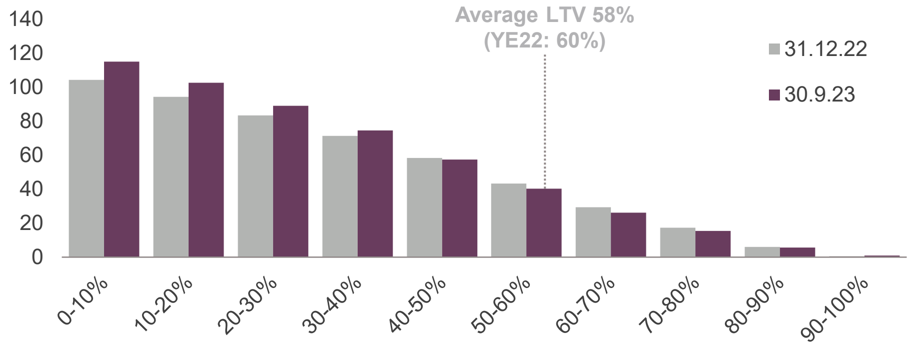
Interest rate reset profile for NIL 3-5Y fixed rate mortgages

Gross carrying amount, ISKbn



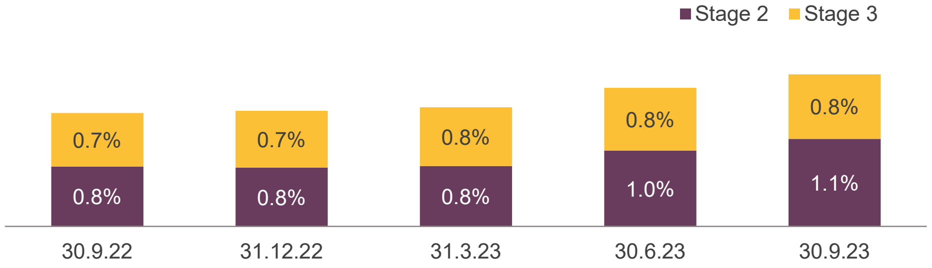
LTV distribution of mortgages

Gross carrying amount, loan splitting approach, ISKbn



Mortgages portfolio: Stage 2 and 3 (NPL)

Gross carrying amount as ratio of total mortgages



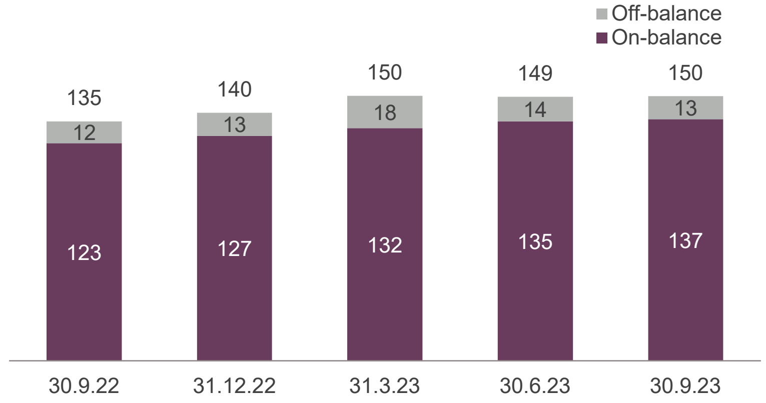
Real estate and construction sector in a good shape

High interest rates and inflation reduce loan growth

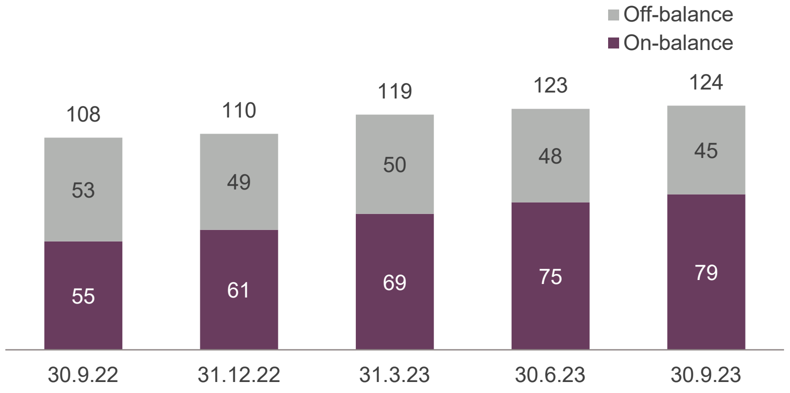
Highlights

- Loans to real estate companies and construction amount to 11% and 6% of loans to customers, respectively
- Disciplined origination with conservative LTV requirements and debt service criteria
- Third party security agents for largest real estate clients
- Most real estate companies use CPI-linked rental contracts as a form of hedging and have long-term financing to minimize influence of short- term changes in market value of real estate
- Loan commitments are disbursed in line with the construction progress
- Over half of exposure in the construction sector is for residential real estate, 20% for commercial real estate and the rest is mixed or to general construction contractors

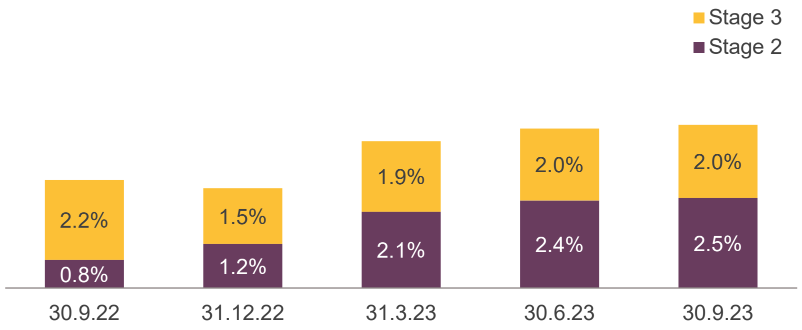
Development of exposure to real estate companies
Gross carrying amount by period, ISKbn



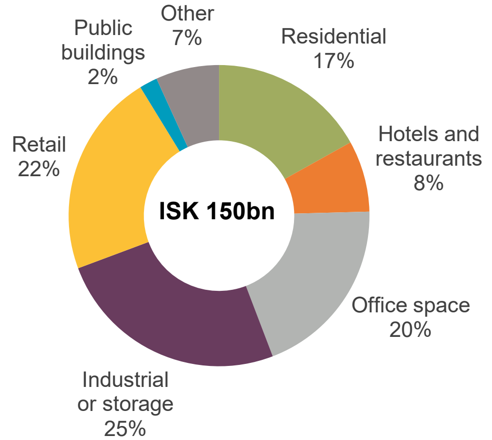
Development of construction exposure
Gross carrying amount by period, ISKbn



Real estate portfolio: Stage 2 and 3 (NPL)
Gross carrying amount as ratio of the real estate portfolio



Real estate collateral by type
30.9.2023



Deposits are the largest source of funding

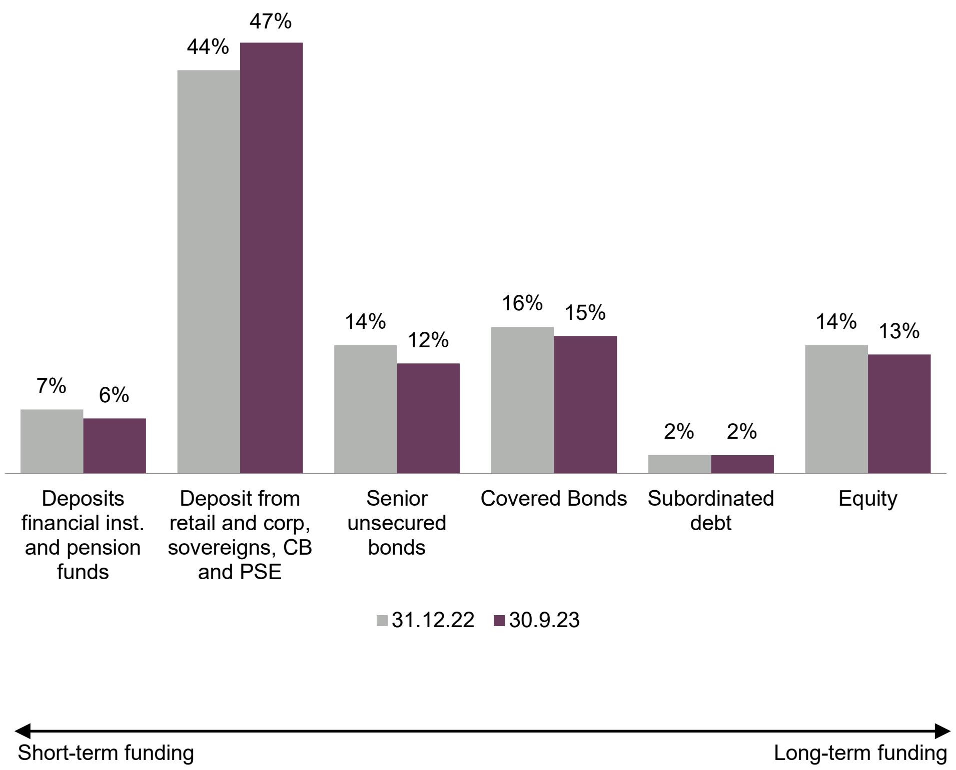
Significant growth in retail deposits

Highlights

- Term deposits are 21% of total deposits
- Deposit concentration stable, 11% of deposits belonged to the 10 largest depositors and 27% to the 100 largest, compared to 12% and 20% respectively at YE22
- The Bank conducts various internal stress tests and all tests required by the Central Bank
- A detailed split of the deposit base and LCR calculations is provided in the notes to the financial statements, providing investors with the necessary information to perform their own stress tests on deposits
- 75% of deposits held by individuals (across business segments) and 46% of all deposits covered by deposit guarantee scheme

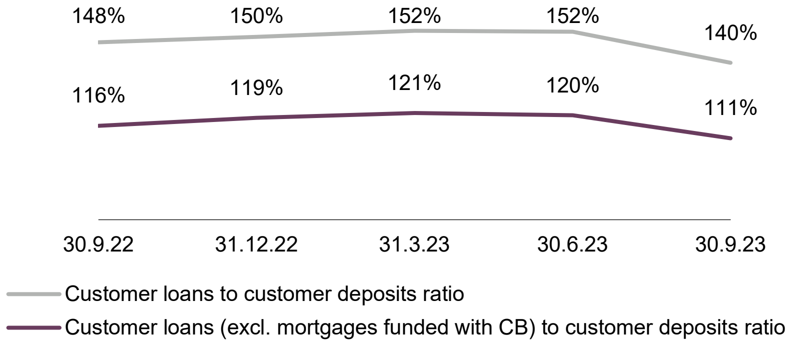
Funding sources

By type, % of total liabilities and equity



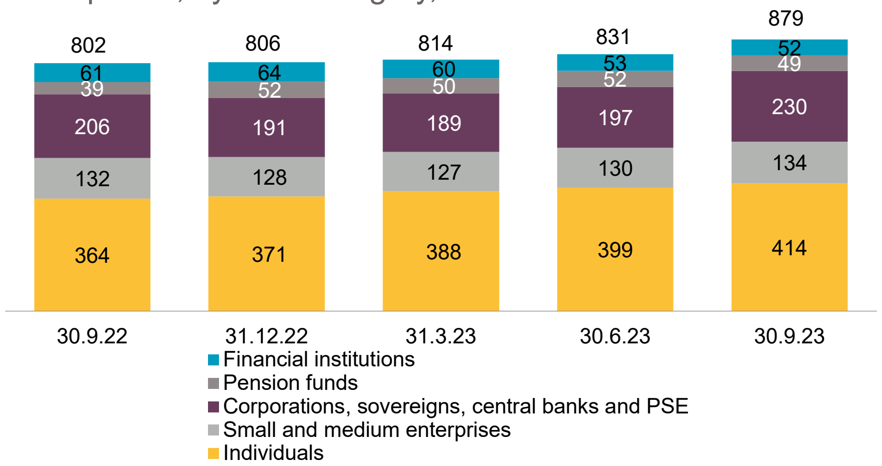
Customer loans to customer deposits ratio

Development, %



Deposits from customers and credit institutions

Development, by LCR category, ISKbn



Seasoned and diversified long-term funding programme

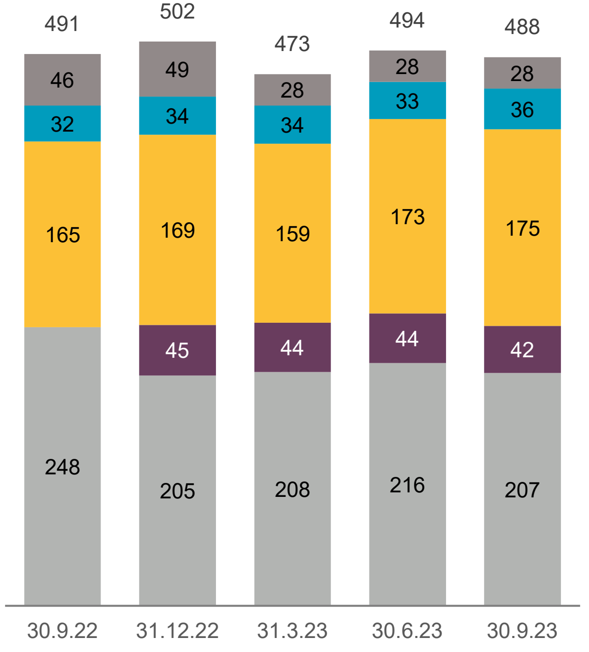
Focus on local issuance in 3Q23

Highlights

- The Bank has been assigned an A3 issuer rating by Moody's Investor Services (Moody's) with a stable outlook, reflecting the Bank's strong capitalization and good recurring profitability
- In August, the Bank exercised its call option on SEK 500m Tier 2 due August 2028
- The Bank issued a Tier 2 in ISK in September, a total of ISK 9.6bn

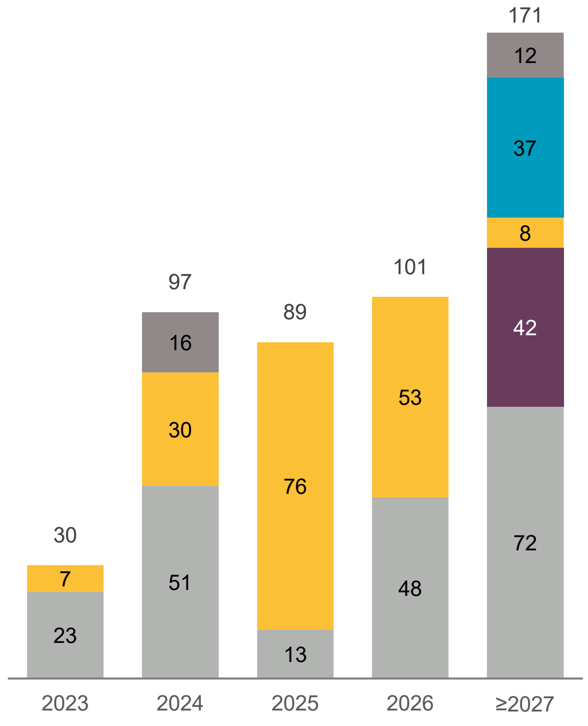
Sources of borrowings

Development, ISKbn



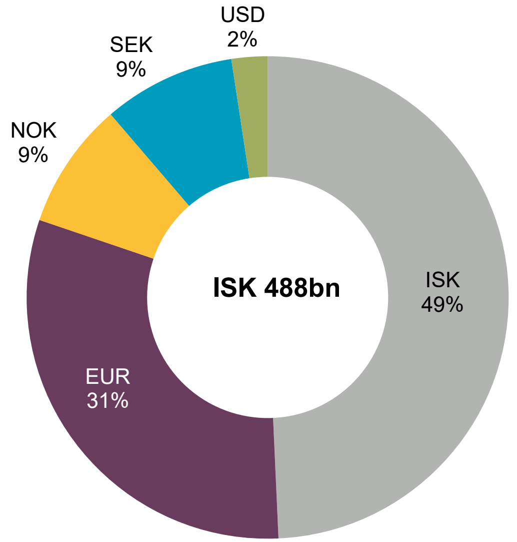
Contractual maturity profile of borrowings

30.9.23, ISKbn



Currency split of borrowings

30.9.23



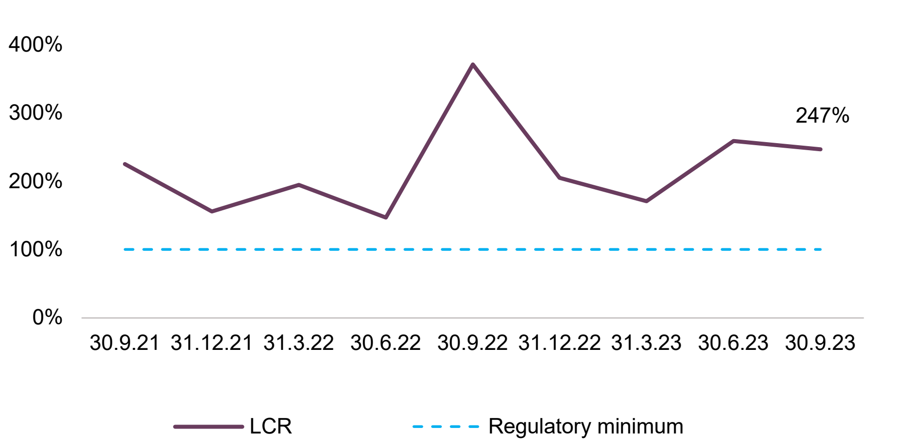
Sound liquidity management, ratios well above requirements

Liquid assets of ISK 371bn, representing 23% of total assets

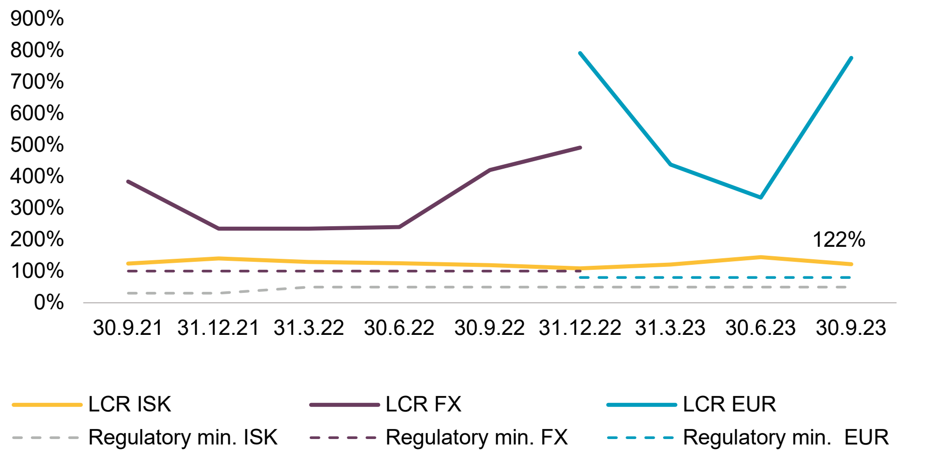
Highlights

- All liquidity measures above regulatory requirements
- Removal of regulatory minimum for LCR in FX at beginning of year; Introduction of new 80% minimum for LCR in EUR
- The Bank's EUR LCR at end of 3Q23 was 777%
- The securities portfolio is all MtM (FVTPL). There is no unrealised loss due to HtM (amortised cost).
- IRRBB is carefully monitored and managed. The Bank is fully compliant to the supervisory outlier test.

Total liquidity coverage ratio (LCR)

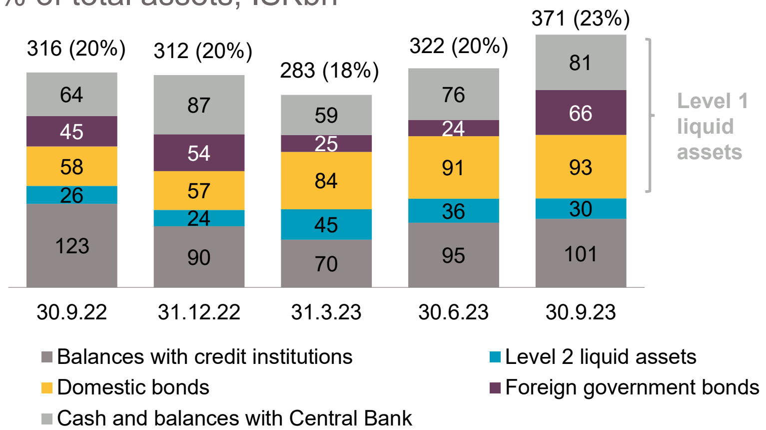


Liquidity coverage ratio – foreign currencies and ISK

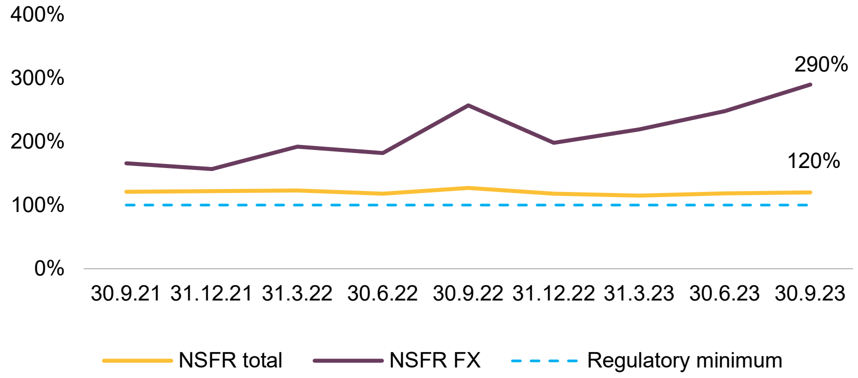


Liquid assets

% of total assets, ISKbn



Net stable funding ratio (NSFR)



Strong capital position

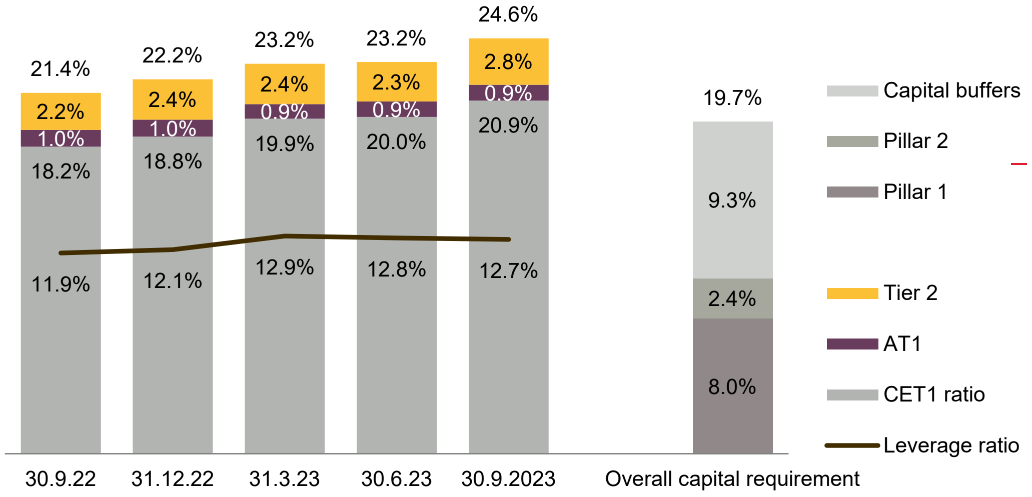
Capital ratios rise with issuance of Tier 2 bonds

Highlights

- The financial stability board has announced an increase in the counter-cyclical buffer in Iceland from 2.0% to 2.5% effective from March 2024
- This change will raise the Bank's overall capital requirement from 19.7% to 20.2% assuming no other changes
- MREL ratio, including the CET1 capital held to meet the combined buffer requirement, stood at 39.2% at end of 3Q23, 870bp above the requirement of 30.5%
- The Bank plans to continue its ISK 5bn share buyback in the coming months and to optimize its capital structure before year-end 2024, both being subject to market conditions

Capital ratios and leverage ratio

% of REA (% of total exposure for leverage ratio)



Capital requirements

- SREP: As of 30 June 2023, the Bank must maintain an additional capital requirement of 2.4% of the REA, a decrease of 0.2 percentage points from the previous assessment. The Bank's overall capital requirement, including capital buffers, was therefore decreased from 19.9% to 19.7%
- Increase in counter-cyclical buffer from 2.0% to 2.5%, effective from March 2024, raises overall capital requirement from 19.7% to 20.2% assuming no other changes

Strong capital position

- CET1 excess of 580bp
- Total capital excess of 490bp
- MREL excess of 870bp

Q&A

26 October 2023

Appendix I – About Íslandsbanki and additional financial information

This is Íslandsbanki

Our purpose is to be a force for good by empowering our customers to succeed

Vision and Values

To create value for the future
with excellent service

Passion · Professionalism · Collaboration

The Bank

FTEs
716
number of FTEs at Íslandsbanki at period end

12 branches

Listed on Nasdaq Iceland as of June 2021

Market share[1]

30% retail customers

39% SMEs

35% large companies

Sustainability 3Q23

- IS HAF fjárfestingar concluded its first two investments in companies working in sea related fields
- Íslandsbanki's Entrepreneurs' Fund opened for new grant applications
- The Sustainable Financial Disclosure Regulation and EU Taxonomy regulation came into force

Key Figures 3Q23

ROE	11.0%	LCR Group, all currencies	247%
Cost-to-income ratio	39.0%	NSFR Group, all currencies	120%
CET1 ratio	20.9%	Leverage ratio	12.7%
Total capital ratio	24.6%	Total assets	ISK 1,644bn

Ratings and certifications

Moody's
A3 Stable outlook

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

Euromoney Awards for Excellence 2023 Iceland Best Bank

Equal Pay Certificate

Jafnvægisvog FKA 2023 Viðurkenning

Digital milestones 3Q23

- Equity trading is now available in the app for legal entities
- The "My banking" user portal gives customers easy access to Íslandsbanki services
- Customers can now log out of all devices with one click in case of a suspected security threat

1. Based on Gallup surveys regarding primary bank. 6 months rolling average for retail customers, average of last two Gallup surveys conducted in Q1 and Q2 for SMEs and 2022 average for large companies.

Financial overview

Key figures & ratios

		3Q23	2Q23	1Q23	4Q22	3Q22
PROFITABILITY	Profit for the period, ISKm	**6,007**	6,139	6,211	5,982	7,486
	Return on equity	**11.0%**	11.5%	11.4%	11.1%	14.4%
	Net interest margin (of total assets)	**2.9%**	3.2%	3.2%	3.1%	3.0%
	Cost-to-income ratio[1,2]	**39.0%**	42.6%	42.1%	40.6%	36.3%
	Cost of risk[3]	**0.19%**	(0.40%)	0.22%	0.22%	(0.40%)
		30.9.23	30.6.23	31.3.23	31.12.22	30.9.22
BALANCE SHEET	Loans to customers, ISKm	**1,210,499**	1,237,758	1,218,999	1,186,639	1,153,047
	Total assets, ISKm	**1,643,600**	1,593,239	1,551,530	1,566,235	1,548,672
	Risk exposure amount, ISKm	**986,355**	1,015,197	1,004,978	999,491	1,012,986
	Deposits from customers, ISKm	**864,189**	816,641	800,071	789,897	781,614
	Customer loans to customer deposits ratio	**140%**	152%	152%	150%	148%
	Non-performing loans (NPL) ratio[4]	**1.8%**	1.7%	1.7%	1.8%	1.7%
LIQUIDITY	Net stable funding ratio (NSFR), for all currencies	**120%**	119%	115%	118%	127%
	Liquidity coverage ratio (LCR), for all currencies	**247%**	259%	171%	205%	371%
CAPITAL	Total equity, ISKm	**219,694**	215,524	210,385	218,874	211,613
	CET1 ratio[5]	**20.9%**	20.0%	19.9%	18.8%	18.2%
	Tier 1 ratio[5]	**21.9%**	20.9%	20.8%	19.8%	19.2%
	Total capital ratio[5]	**24.6%**	23.2%	23.2%	22.2%	21.4%
	Leverage ratio[5]	**12.7%**	12.8%	12.9%	12.1%	11.9%
	MREL ratio[6]	**39.2%**	38.4%	33.2%	34.5%	-

1.Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund – One-off items) / (Total operating income – One-off items). 2. C/I ratio in 4Q22 included the provision of ISK 300m in connection with an administrative fine (one-off item). This has now been updated. 3. Negative cost of risk means that there is a net release of impairments. 4. Stage 3, loans to customers, gross carrying amount. 5. Including 1Q23 profit for 31.3.23, 3Q22 profit for 30.9.22 and 3Q23 profit for 30.9.23. 6. MREL ratio includes the CET1 capital held to meet the combined buffer requirement.

Income Statement

Income growth continues and profitability is robust

Income statement, ISKm	3Q23	3Q22	Δ%	9M23	9M22	Δ%	2022
Net interest income	**11,846**	11,315	5%	**36,881**	30,778	20%	43,126
Net fee and commission income	**3,400**	3,517	(3%)	**10,461**	10,015	4%	14,053
Net financial income (expense)	**(193)**	(471)	(59%)	**(214)**	(358)	(40%)	(1,257)
Net foreign exchange gain	**176**	64	175%	**468**	305	53%	881
Other operating income	**248**	111	123%	**312**	435	(28%)	433
Total operating income	**15,477**	14,536	6%	**47,908**	41,175	16%	57,236
Salaries and related expenses	**(3,353)**	(2,916)	15%	**(11,142)**	(9,734)	14%	(13,452)
Other operating expenses	**(2,687)**	(2,357)	14%	**(8,631)**	(7,366)	17%	(10,166)
Administrative fine	**-**	-	-	**(860)**	-	-	(300)
Administrative expenses	**(6,040)**	(5,273)	15%	**(20,633)**	(17,100)	21%	(23,918)
Contribution to the Depositor's and Investors' Guarantee Fund	**-**	-	-	**-**	(165)	-	(165)
Bank tax	**(522)**	(535)	(2%)	**(1,469)**	(1,377)	7%	(1,858)
Total operating expenses	**(6,562)**	(5,808)	13%	**(22,102)**	(18,642)	19%	(25,941)
Net impairment on financial assets	**(583)**	1,165	(150%)	**(13)**	2,223	(101%)	1,576
Profit before tax	**8,332**	9,893	(16%)	**25,793**	24,756	4%	32,871
Income tax expense	**(2,334)**	(2,525)	(8%)	**(7,461)**	(6,319)	18%	(8,485)
Profit for the period from continuing operations	**5,998**	7,368	(19%)	**18,332**	18,437	(1%)	24,386
Discontinued operations held for sale, net of income tax	**9**	118	(92%)	**25**	116	(78%)	149
Profit for the period	**6,007**	7,486	(20%)	**18,357**	18,553	(1%)	24,535

Key ratios							
Net Interest Margin (NIM)	**2.9%**	3.0%		**3.1%**	2.8%		2.9%
Cost-to-income ratio (C/I)	**39.0%**	36.3%		**41.3%**	41.9%		41.6%
Return on Equity (ROE)	**11.0%**	14.4%		**11.3%**	12.1%		11.8%
Cost of risk (COR)	**0.19%**	(0.40%)		**0.00%**	(0.26%)		(0.14%)

Balance sheet reflects a balanced loan and funding profile

Conservative mix of assets and stable funding

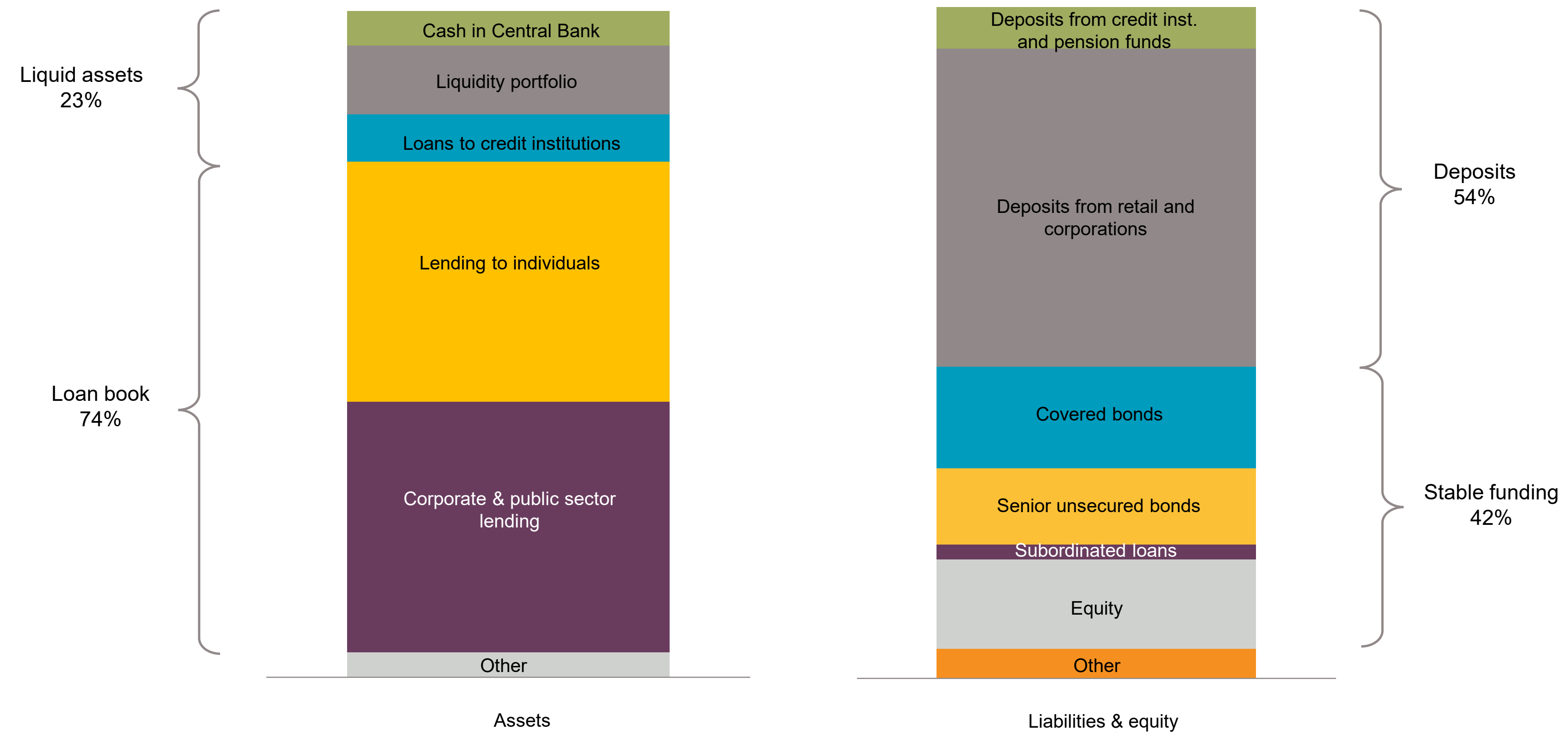
Assets

- Vast majority of assets consist of lending to both retail and corporates
- Strong liquidity portfolio is a consistent factor in balance sheet management
- Very limited exposure to non-liquid or non-lending assets

Liabilities

- Deposits from retail and corporates are the single largest funding source
- Bonds and debt instruments have become a more prominent part of the funding mix thanks to continuous focus on attracting new pockets of demand, including foreign currency and ESG issuance

Simplified balance sheet structure
30.9.23, ISK 1,644bn



Assets

Asset base mainly consists of loans and liquid assets

Assets, ISKm	30.9.23	30.6.23	Δ	Δ%	31.12.22	Δ	Δ%
Cash and balances with Central Bank	**84,332**	78,275	6,057	8%	94,424	(10,092)	(11%)
Loans to credit institutions	**117,699**	97,749	19,950	20%	110,364	7,335	7%
Bonds and debt instruments	**178,830**	131,471	47,359	36%	130,804	48,026	37%
Derivatives	**5,581**	5,374	207	4%	7,461	(1,880)	(25%)
Loans to customers	**1,210,499**	1,237,758	(27,259)	(2%)	1,186,639	23,860	2%
Shares and equity instruments	**13,270**	12,120	1,150	9%	15,868	(2,598)	(16%)
Investment in associates	**3,841**	3,828	13	0%	3,844	(3)	(0%)
Property and equipment	**6,528**	6,748	(220)	(3%)	6,752	(224)	(3%)
Intangible assets	**3,120**	3,241	(121)	(4%)	3,279	(159)	(5%)
Other assets	**19,156**	15,945	3,211	20%	6,072	13,084	215%
Non-current assets and disposal groups held for sale	**744**	730	14	2%	728	16	2%
Total Assets	**1,643,600**	1,593,239	50,361	3%	1,566,235	77,365	5%
Key ratios							
Risk Exposure Amount (REA)	**986,355**	1,015,197	(28,842)	(3%)	999,491	15,706	2%
REA/total assets	**60.0%**	63.7%			63.8%		
Non-performing loans (NPL) ratio[1]	**1.8%**	1.7%			1.8%		
Asset encumbrance ratio	**23.5%**	25.3%			26.5%		

1. Stage 3, loans to customers, gross carrying amount.

Liabilities and equity

Deposits continue to be the largest source of funding

Liabilities & Equity, ISKm	30.9.23	30.6.23	Δ	Δ%	31.12.22	Δ	Δ%
Deposits from Central Bank and credit institutions	**15,159**	14,306	853	6%	15,269	(110)	(1%)
Deposits from customers	**864,189**	816,641	47,548	6%	789,897	74,292	9%
Derivative instruments and short positions	**10,797**	12,064	(1,267)	(11%)	10,804	(7)	(0%)
Debt issued and other borrowed funds	**451,701**	460,913	(9,212)	(2%)	468,270	(16,569)	(4%)
Subordinated loans	**36,517**	33,104	3,413	10%	34,392	2,125	6%
Tax liabilities	**16,323**	14,832	1,491	10%	12,128	4,195	35%
Other liabilities	**29,220**	25,855	3,365	13%	16,601	12,619	76%
Total Liabilities	**1,423,906**	1,377,715	46,191	3%	1,347,361	76,545	6%
Total Equity	**219,694**	215,524	4,170	2%	218,874	820	0%
Total Liabilities and Equity	**1,643,600**	1,593,239	50,361	3%	1,566,235	77,365	5%

Key ratios	30.9.23	30.6.23	31.12.22
Customer loans to customer deposits ratio	**140%**	152%	150%
Net stable funding ratio (NSFR)	**120%**	119%	118%
Liquidity coverage ratio (LCR)	**247%**	259%	205%
Total capital ratio[1]	**24.6%**	23.2%	22.2%
Tier1 capital ratio[1]	**21.9%**	20.9%	19.8%
Leverage ratio[1]	**12.7%**	12.8%	12.1%
MREL ratio[2]	**39.2%**	38.4%	34.5%

1. Including third quarter profit for 30.9.23. 2. MREL ratio includes the CET1 capital held to meet the combined buffer requirements.

Appendix II – Icelandic economy update

GDP growth to lose steam in 2023, then gradually recover

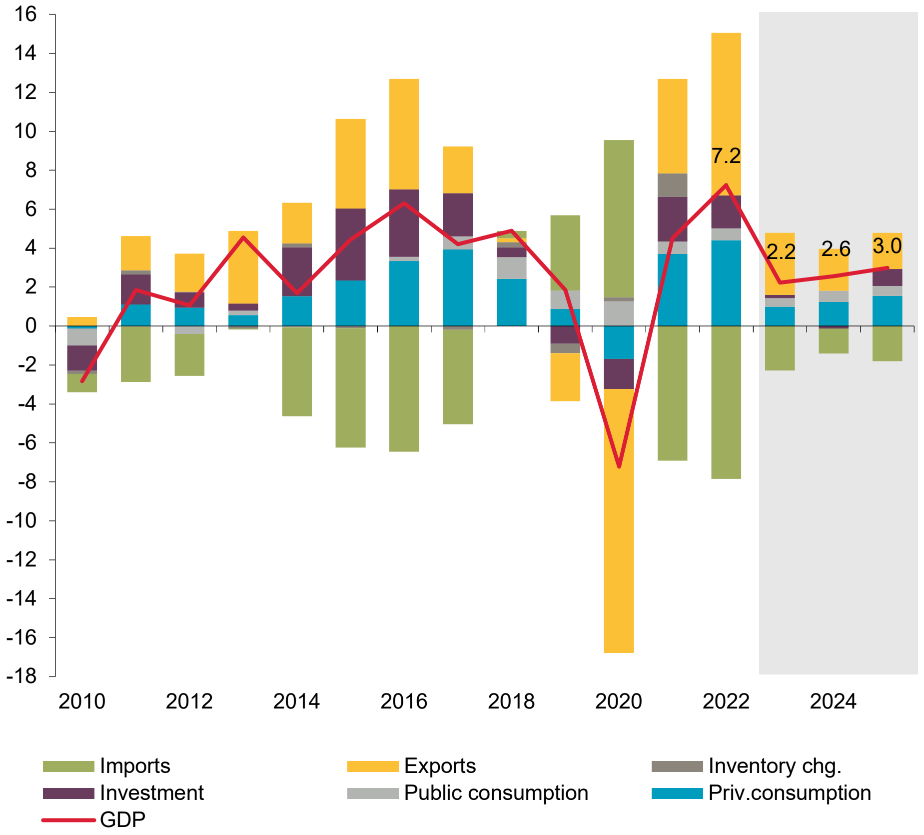
Exports set to drive near-term growth, with domestic demand picking up later in the forecast horizon

Highlights

- Iceland's GDP grew by 5.8% YoY in 1H23, following 7.2% growth in 2022 and 4.5% growth in 2021.
- Recent GDP growth has been mainly driven by strong growth in private domestic demand and the post-pandemic resurgence of tourism.
- ISB Research forecasts GDP growth at 2.2% in 2023. Export growth will be the main driver of output growth this year, and the contribution from domestic demand will be much smaller than in 2021 and 2022.
- For 2024, ISB Research forecasts GDP growth to rise to 2.6%, owing mainly to faster growth in consumption.
- The outlook is for 3.0% GDP growth in 2025, with growing domestic demand outweighing weaker export growth.
- Among key global uncertainties is whether and how geopolitical tension between economic blocks will come to the fore in the near future as well as how persistent inflation will prove to be.
- Domestically, key risk factors include the results of next winter's general wage negotiations, how strongly the tight monetary stance ultimately affects households and businesses and near-term developments in the residential housing market.

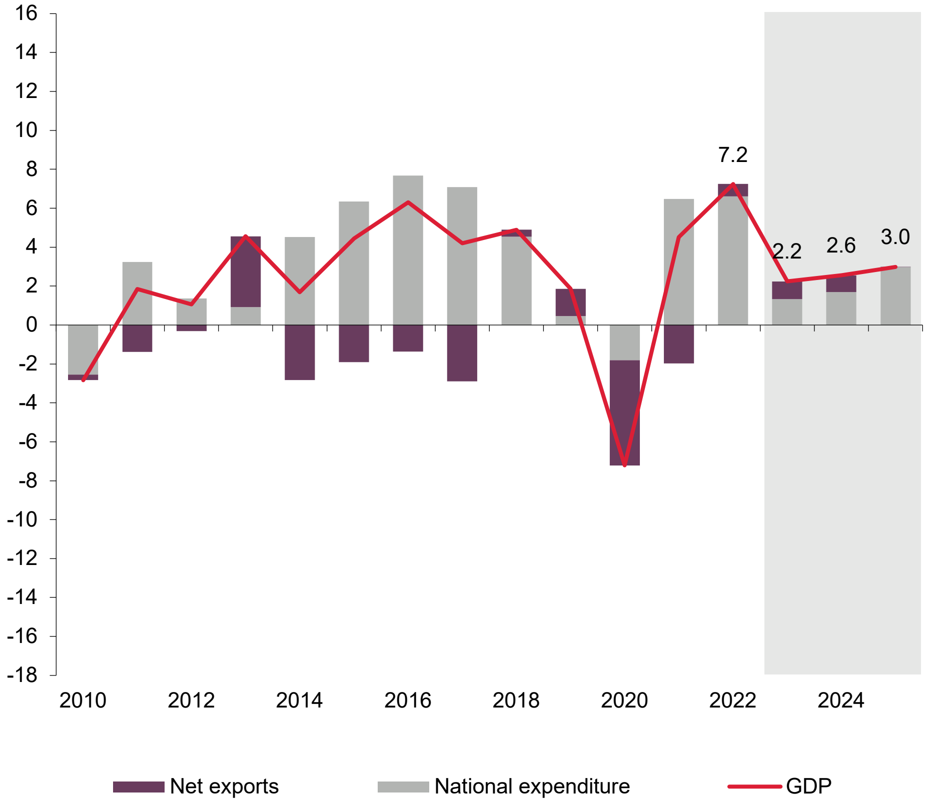
GDP and contribution of its subcomponents

Volume change from prior year (%)



GDP, domestic demand, and external trade

Volume change from prior year (%)



Sources: Statistics Iceland, ÍSB Research.

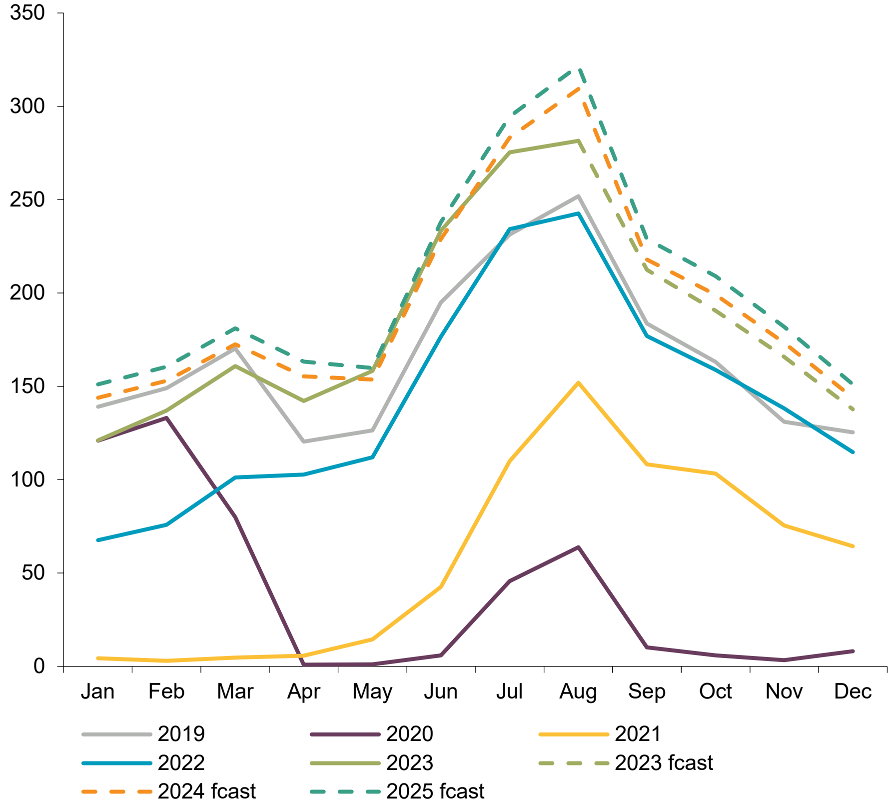
Tourism to set new records during the forecast horizon

Just over 2.2 million tourist arrivals expected in 2023, rising to more than 2.5 million in 2025

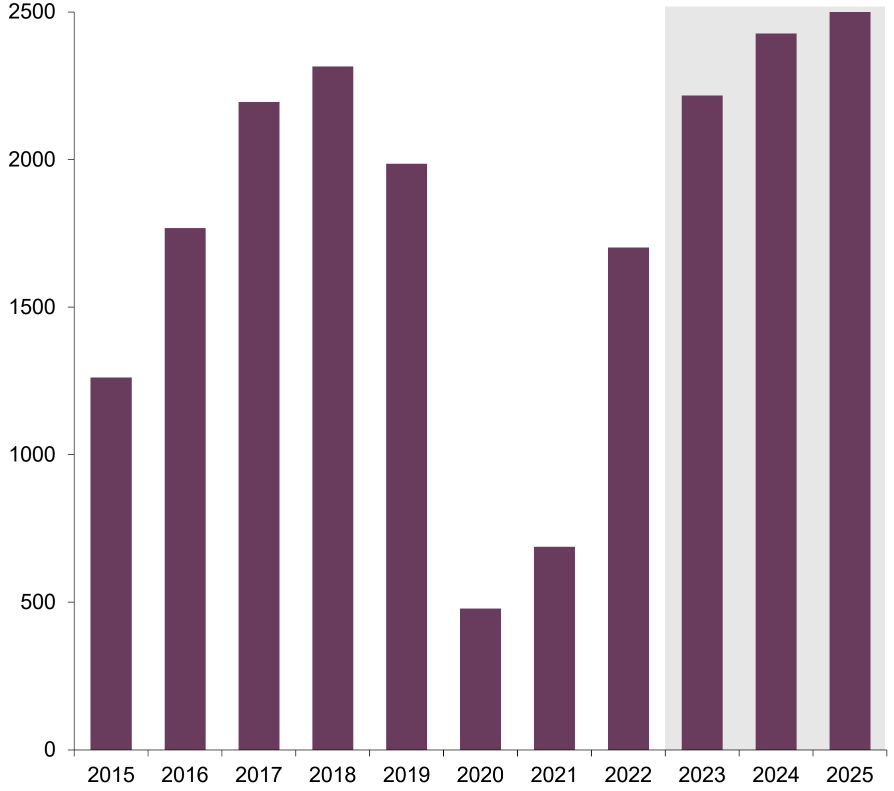
Highlights

- The post-pandemic rebound of the tourist sector has been swift.
- Around 1.7 million tourists visited Iceland in 2022, the largest total since 2019.
- In the year 2023 to September, 1.7 million tourists came to Iceland via KEF airport, amounting to more than 1/3 increase YoY
- The outlook for the coming winter is good, and most indicators suggest that next summer will be even busier than this one.
- ISB Research forecasts that over 2.2 million tourists will arrive via Keflavik Airport this year, potentially making 2023 the second-strongest year to date in terms of visitor numbers.
- We expect tourist numbers to exceed 2.4 million in 2024 and 2.5 million in 2025, thereby setting new records if our forecast materialises.
- Towards the end of the forecast horizon, visitor numbers will probably be constrained increasingly by a limited supply of accommodation during the peak season while a rising real exchange rate could dampen tourists' enthusiasm for Iceland further out.

Number of foreign tourists, by month
thousands



Number of foreign tourists, by year
thousands



Shaded areas and dotted lines denote ISB Research forecasts

Sources: Icelandic Tourist Board, ÍSB Research.

The European energy crisis has a small impact on Iceland

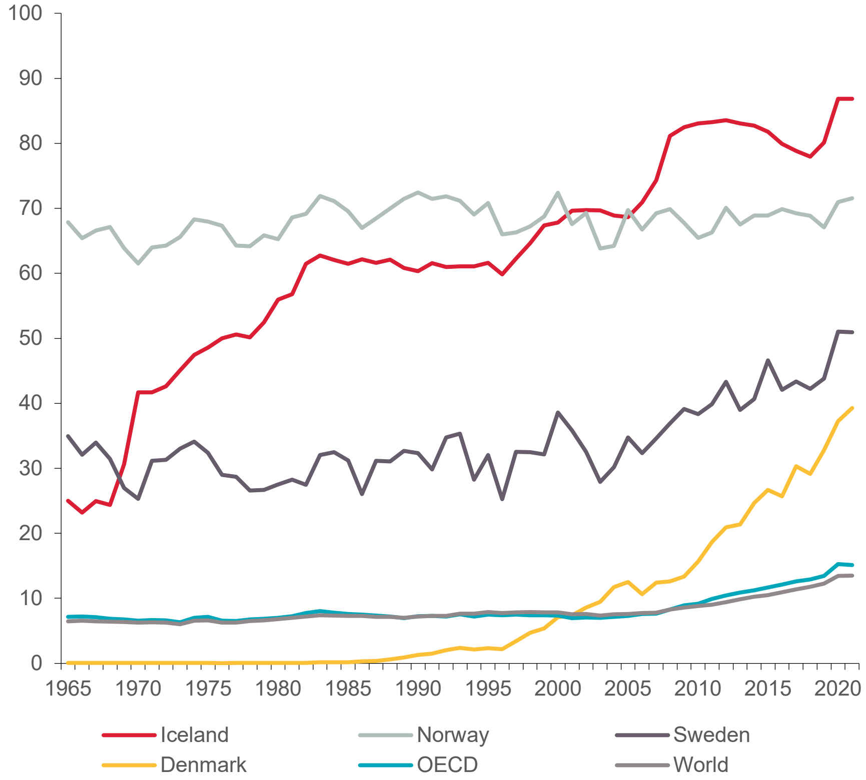
Geothermal heating keeps energy costs at bay

Highlights

- Being a small open economy, the economic impact of the Ukraine war and the resulting energy crisis is felt in Iceland although direct impact on trade is minimal
- However, as a commodity exporting economy with the highest share of renewable energy usage worldwide, Iceland is resilient to the energy crisis and terms-of-trade shock that most other European economies face in the coming winter
- Almost 90% of all housing in Iceland, measured in m^3, is heated by geothermal energy and a further 7% is heated by domestically produced electricity
- The cost-of-living shock to European households creates a downward risk to tourism in the coming winter although, so far, the sector has not seen a backlash in demand for coming quarters
- Seafood prices have increased considerably since the onset of the Ukraine war, offsetting the YoY reduction in allowable fish catch for the current season

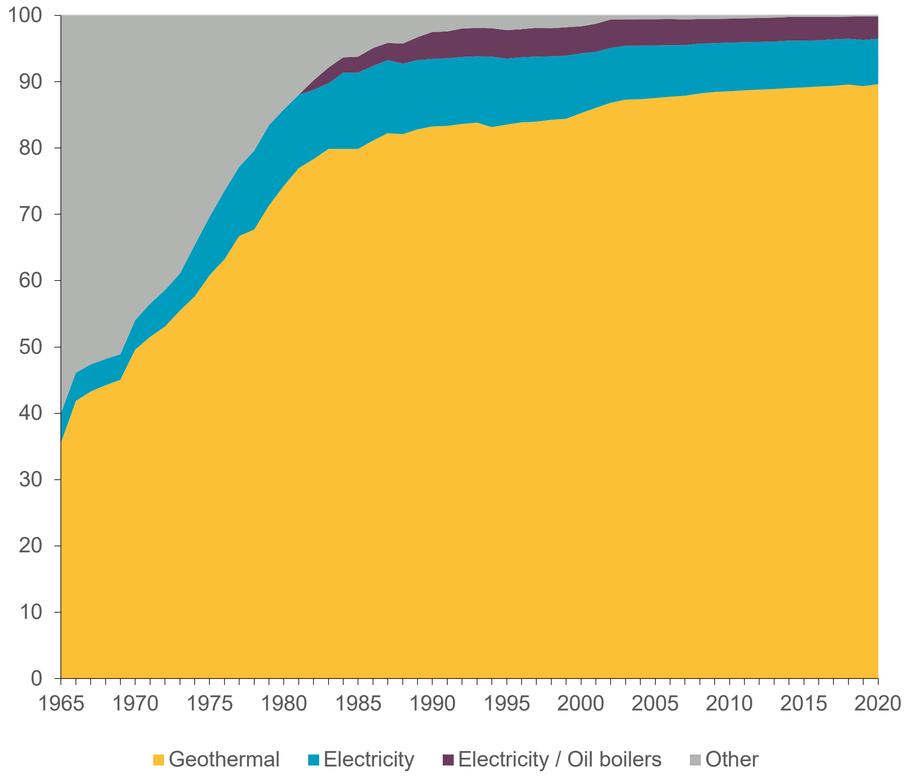
Share of primary energy from renewable sources

% of total



Proportion of energy source in space heating

%



Sources: Our World in Data, National Energy Authority

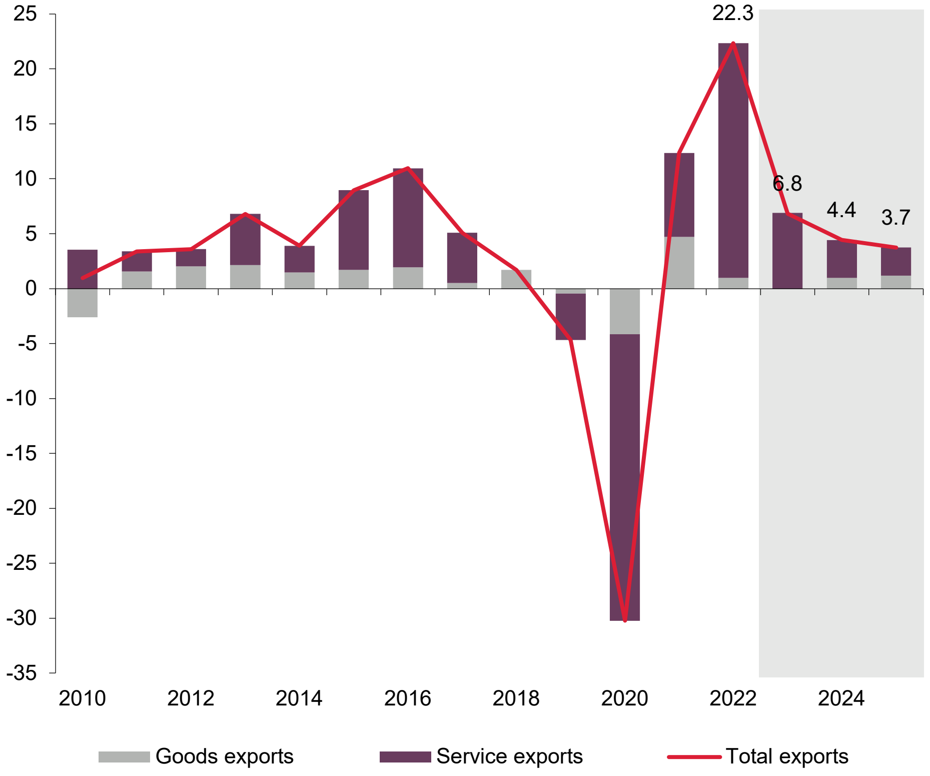
Current account broadly in balance in the coming term

Tourism to drive export growth, with assistance from other sectors

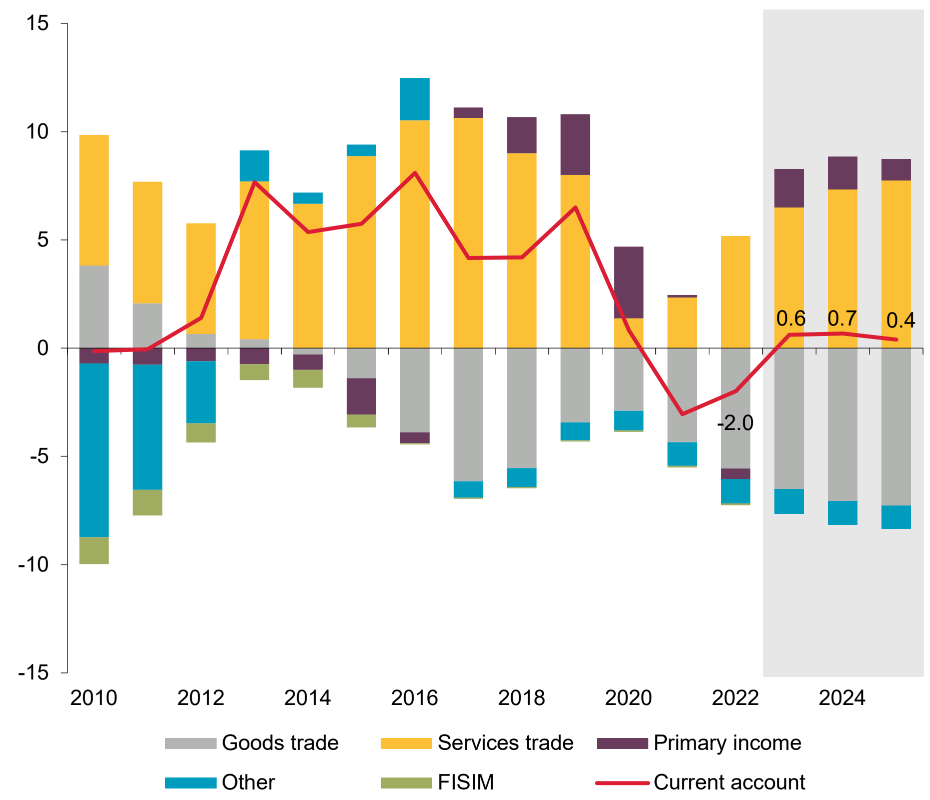
Highlights

- A buoyant tourism sector explains the lion's share of this year's forecasted 6.8% export growth as well as the more moderate growth expected in 2024-2025.
- The outlook is also for robust exports of intellectual property and other human capital-intensive services.
- Brisk growth in exports of farmed fish, modest growth in manufacturing goods exports and an uptick in groundfish exports later on also contribute to export growth.
- The past two years' CA deficit was a reversal after nearly a decade of uninterrupted surpluses.
- The outlook is for the CA balance to improve to a modest surplus in 2023 as export growth exceed import growth and the primary income balance moves back into surplus.
- The outlook is for a CA surplus measuring 0.6% of GDP this year, followed by modest surpluses in 2024 and 2025.
- Iceland's net external assets currently equal almost 29% of GDP, providing important support for the ISK and the economy as a whole.

Exports and contribution from subcomponents
% change



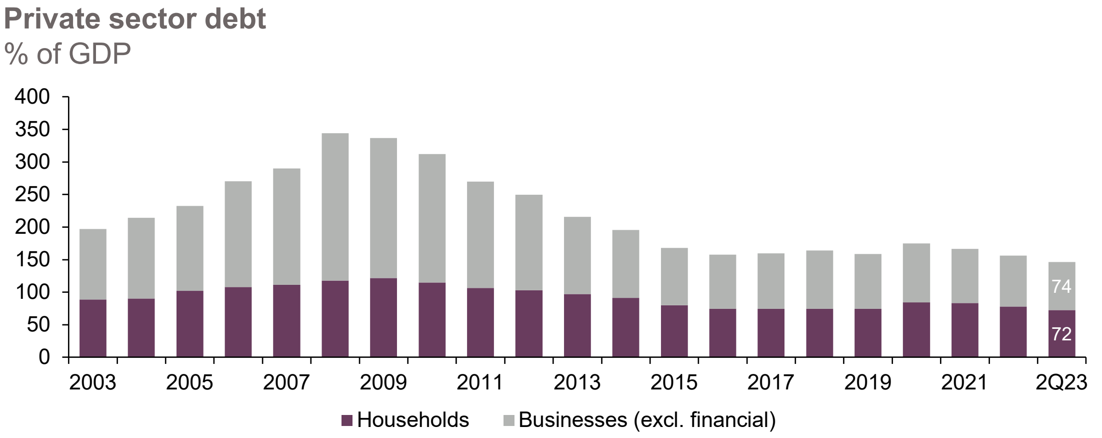
Current account balance
% of GDP

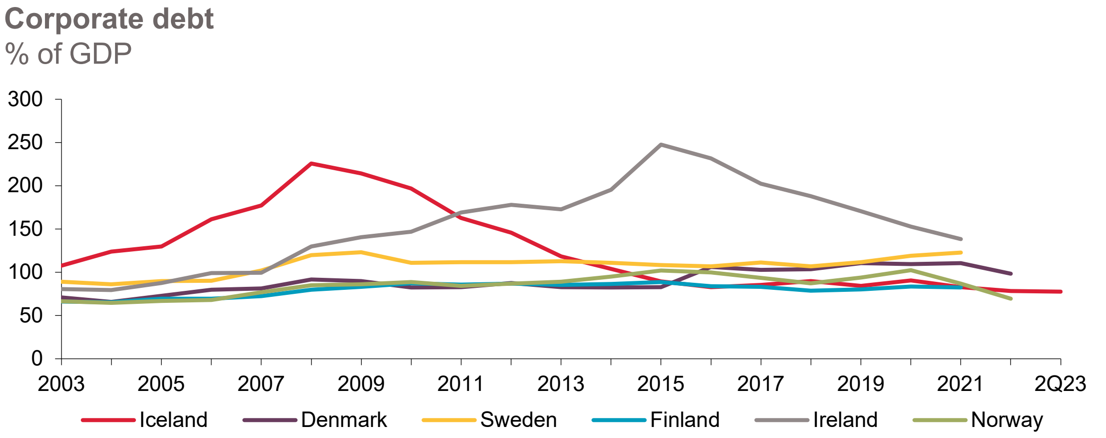


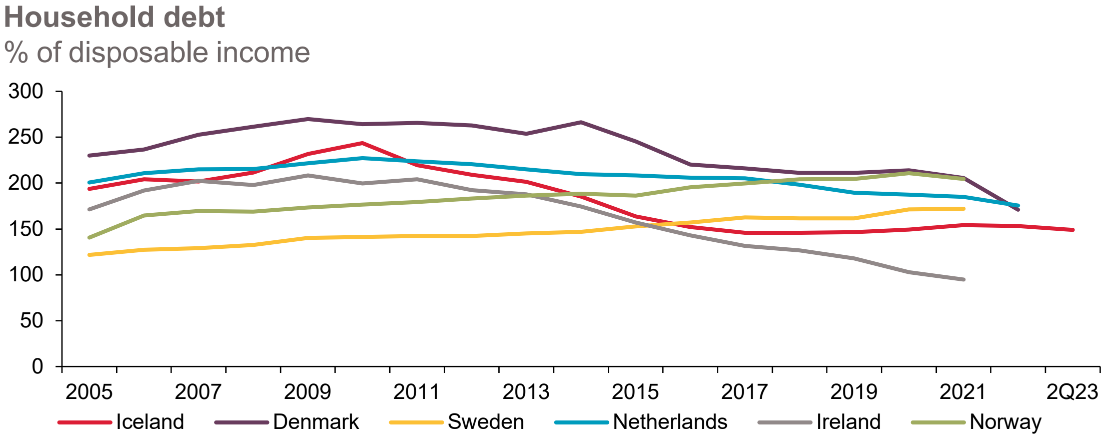
Sources: Statistics Icelandic, Central Bank of Iceland, ÍSB Research.

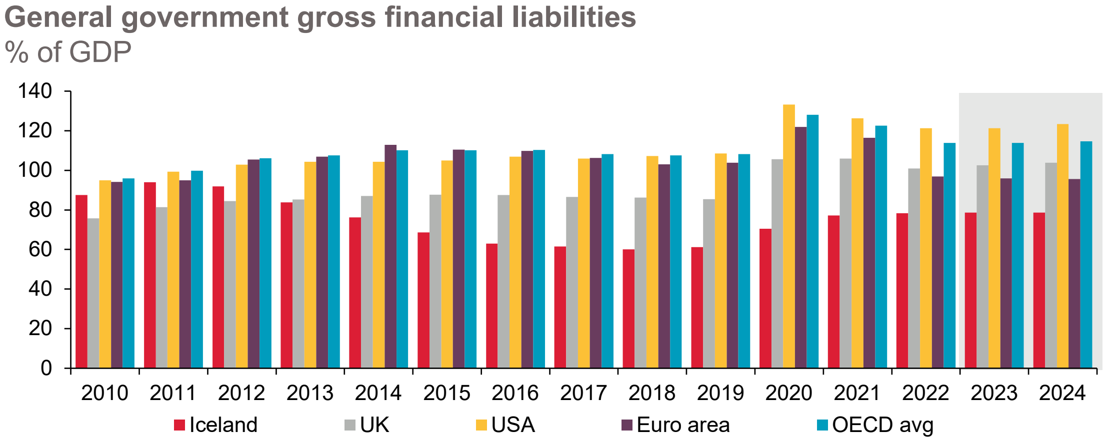
Domestic balance sheets remain healthy

Economy-wide leverage remains moderate as the ratio of private sector debt to GDP declines









Shaded areas indicate OECD forecasts.
Source: Central Bank of Iceland, Statistics Iceland, OECD.

26 October 2023

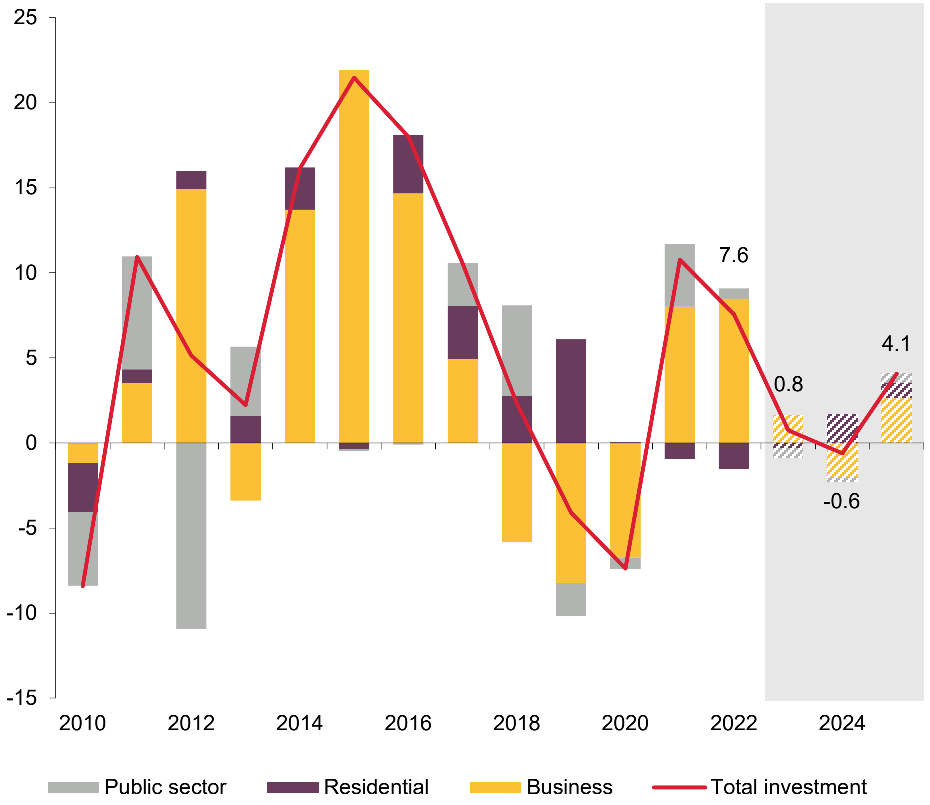
Investment virtually unchanged early on but set to surge later

Business investment the sole source of growth in 2023, but residential investment will gain momentum in 2024

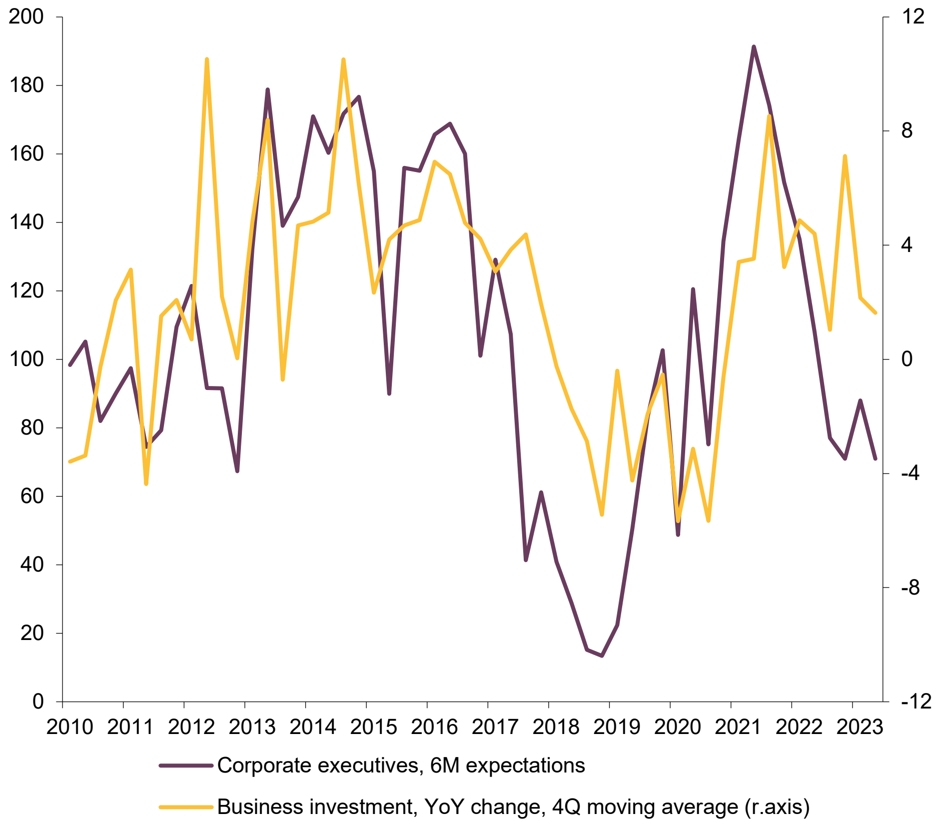
Highlights

- Investment growth was strong over the past two years, driven mainly by business investment, while residential investment slightly declined. From 2020 to 2022, investment increased by nearly one-fifth.
- The next two years, 2023 and 2024, will see stagnant investment growth overall.
- In 2023, slight decreases in residential and public investments will be somewhat offset by business investment, resulting in just under 1% growth.
- By 2024, business investment will decline due to factors like rising interest rates, although this is mitigated by developments in land-based aquaculture and infrastructure plans. As a result, there'll be a slight contraction in total investment in 2024.
- For 2025, ISB Research projections indicate over 4% growth in investment across all components, with sectors like hotel construction rebounding.
- Despite the fluctuations, the investment-to-GDP ratio remains acceptable throughout the forecasted period.

Investment, real change, and contribution of subcomponents
%



Executives' expectations and business investment
Index value (left) and % change year-on-year (right)



Source: Statistics Iceland, Gallup.

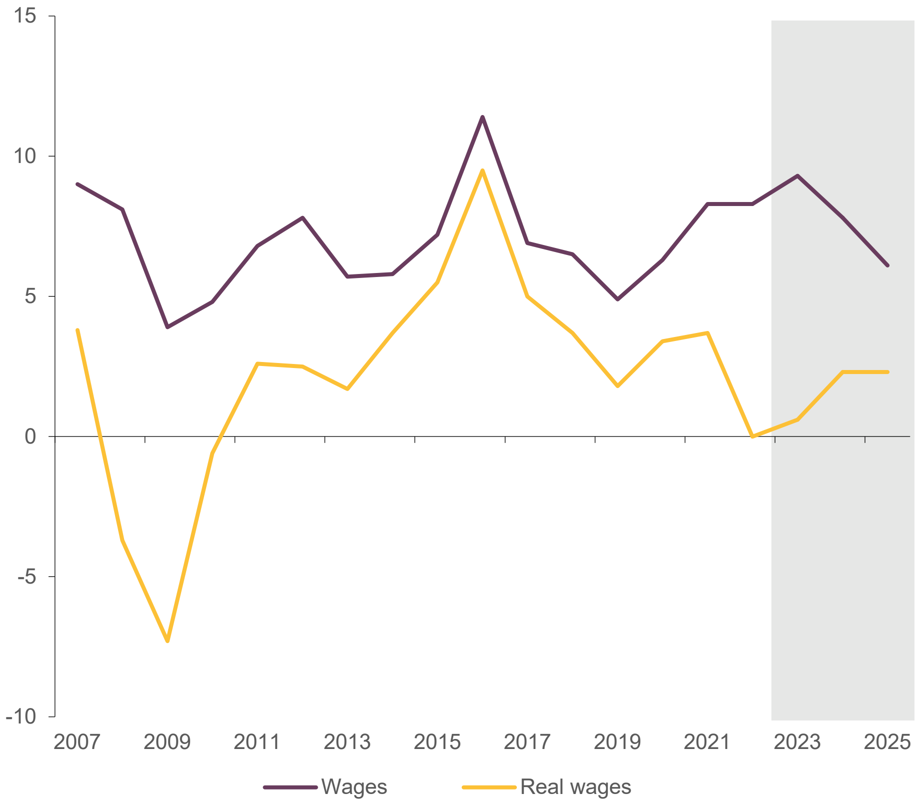
Labour market to remain relatively tight

Real wage growth limited early on but will regain momentum in 2024 and 2025

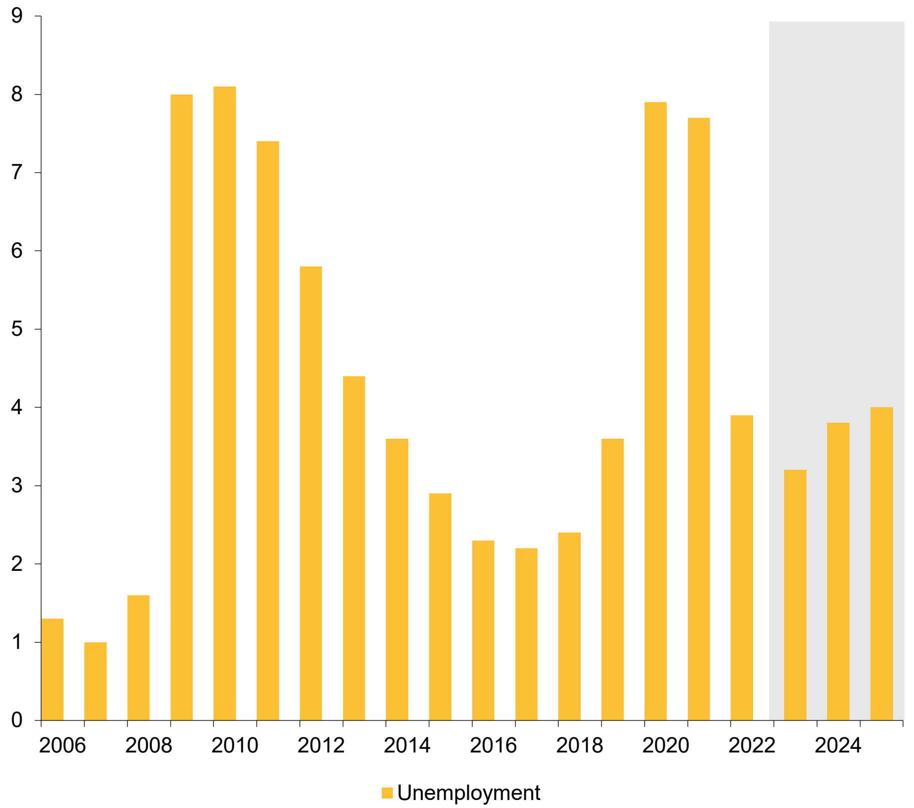
Highlights

- The labour market remains tight with a high demand for labour, largely fulfilled by foreign workers who now make up 23% of the workforce.
- This influx of foreign workers contributes significantly to the recent population surge, suggesting Iceland's population might reach 400,000 by end-2023.
- Unemployment, having decreased from its pandemic high, stood at 2.9% in August and is projected to average 3.2% for the year.
- Seasonal changes will cause a slight increase in unemployment, but by 2024 and 2025, the rates are expected to be 3.8% and 4.0%, respectively.
- Wages increased by over 8% in 2022, with real wages remaining stable even amidst high inflation.
- Current contracts are beneficial for wage-earners, causing a 9.3% nominal wage growth this year and a 0.6% real wage increase.
- Upcoming wage negotiations may be challenging due to slower-than-expected drops in inflation.
- Wages are predicted to grow by 7.8% in 2024 and 6.1% in 2025, resulting in real wage growth of approximately 2.3% annually.

Wages, year on year change
%



Unemployment[1]
% of workforce, annual average



1. Excluding recipients of part-time unemployment benefits.

Source: Statistics Iceland, The Central Bank of Iceland, Gallup.

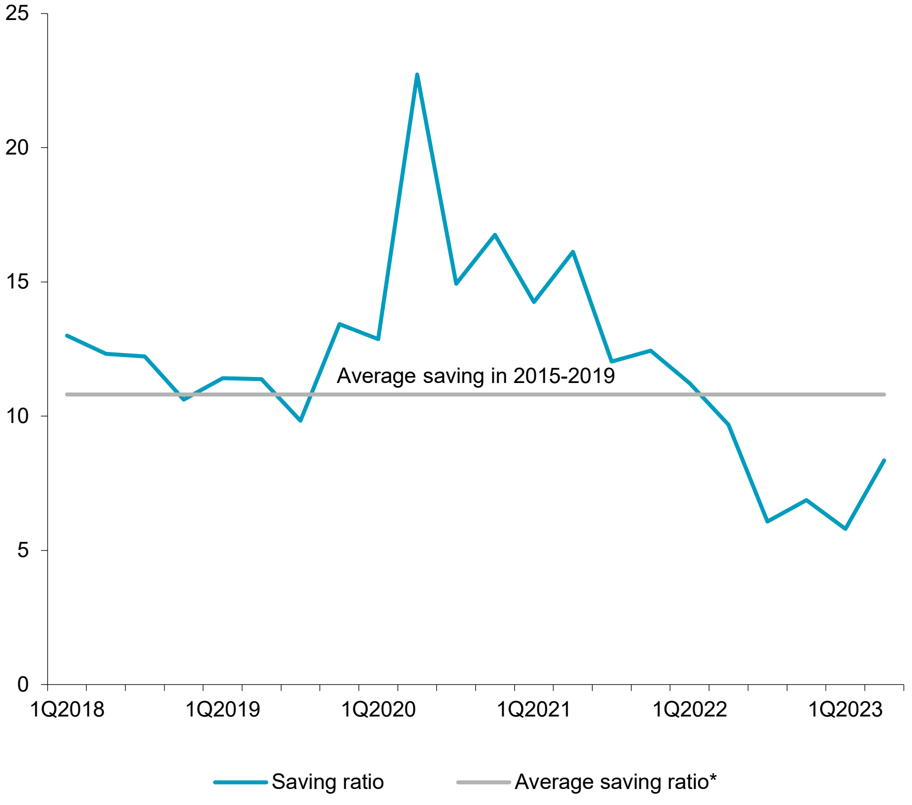
Private consumption growth slows compared to recent past

Icelanders are feeling the pinch from high inflation and interest rates

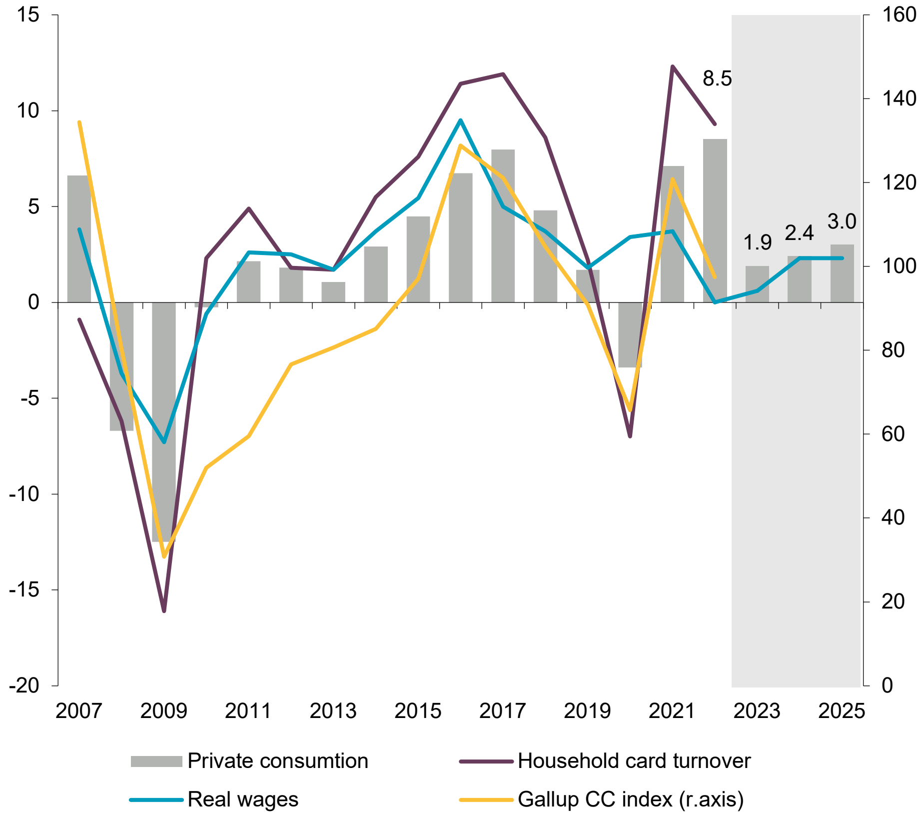
Highlights

- Private consumption increased by 8.5% YoY in real terms in 2022, but in H1/2023, growth slowed to 2.5%.
- Payment card data suggests an additional decline in consumption growth during H2, influenced by the Central Bank's frequent policy rate hikes and the impact of inflation on real wage growth.
- Other indicators, including consumer sentiment, show signs of decelerated private consumption.
- Real wage growth remains positive but modest, and household savings are below average.
- Considering these factors, the 2023 private consumption growth forecast has been adjusted down to 1.9%.
- This slower growth in private consumption significantly affects the overall GDP growth for the year.
- For 2024, private consumption is projected to rise by 2.4%, supported by easing inflation and improving real wage growth.
- In 2025, a 3.0% growth in private consumption is anticipated, with the economy expected to be more balanced and real wage growth stabilizing due to lower inflation and nominal wage adjustments.

Household saving
% of disposable income



Private consumption and related indicators
% change YoY (left) and index value (right)



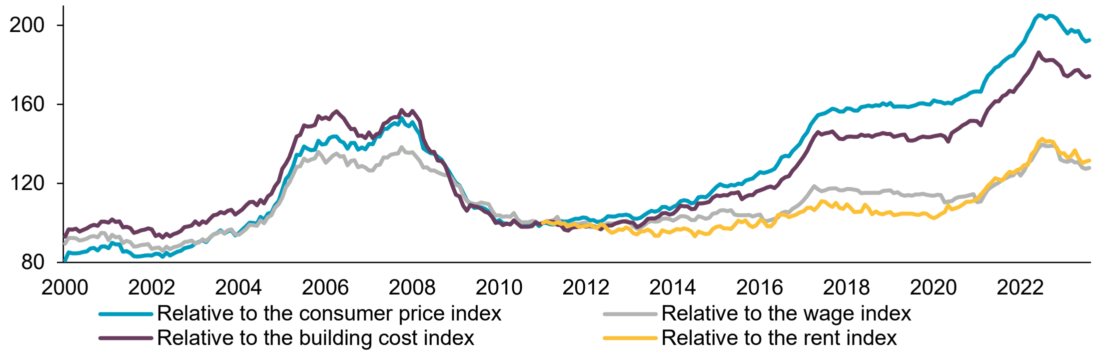
Sources: Central Bank of Iceland, Gallup, Statistics Iceland, ÍSB Research.

The real estate market appears to be stabilising

Central Bank measures have contributed to slower price increases of residential housing

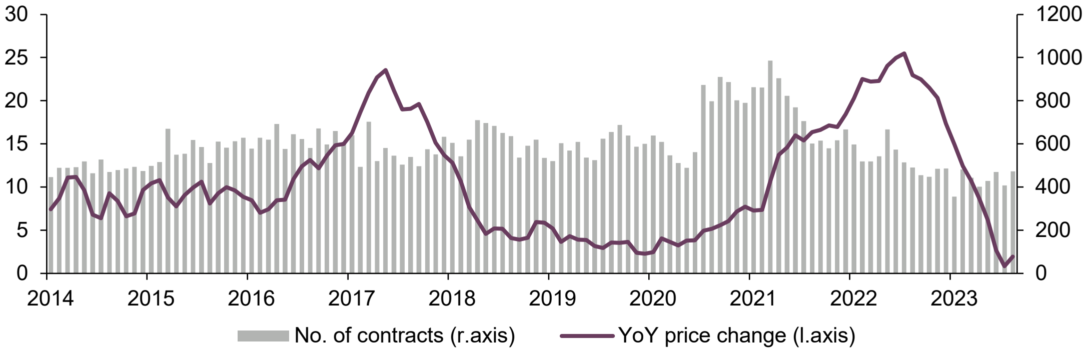
Capital area house prices relative to macroeconomic fundamentals

Index, January 2011=100



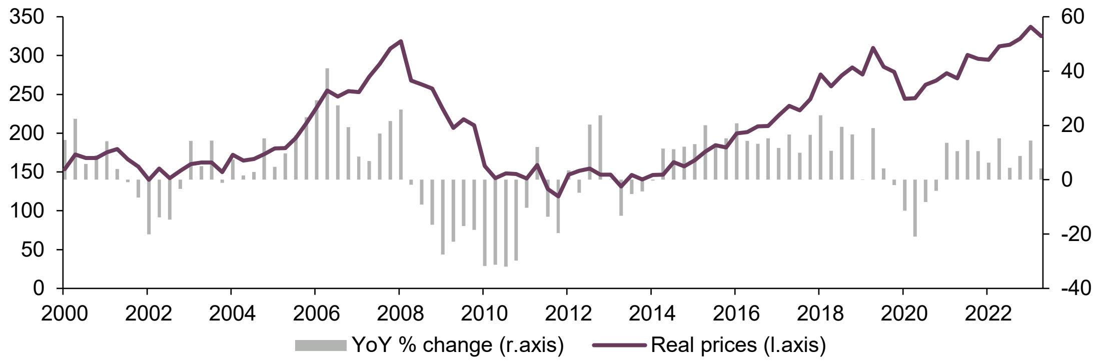
Residential house prices and turnover in greater Reykjavik

% change (l.axis) and number (r.axis)



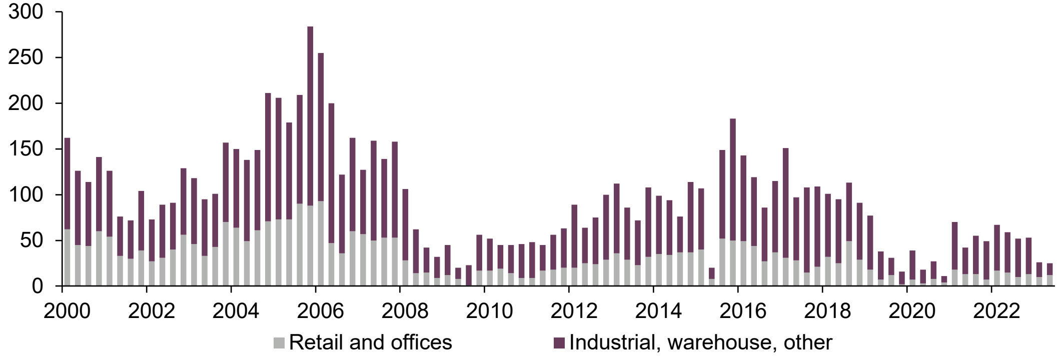
Commercial property real prices in greater Reykjavik

Index, 1995=100 (l.axis) and % change (r.axis)



Commercial real estate market activity

No. of registered purchase agreements



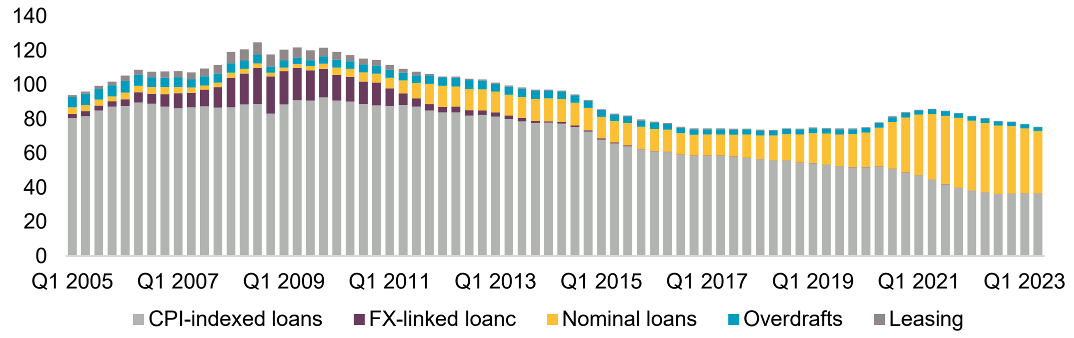
Source: The Central Bank of Iceland.

The Icelandic housing market is relatively resilient

Supply, demand, mortgage market factors combine to make a large price correction less likely

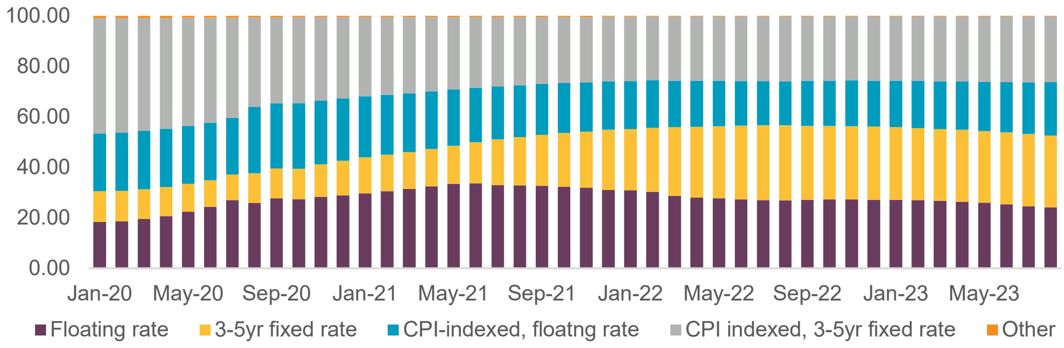
Households are not highly indebted compared to peers

Household debt, % of GDP



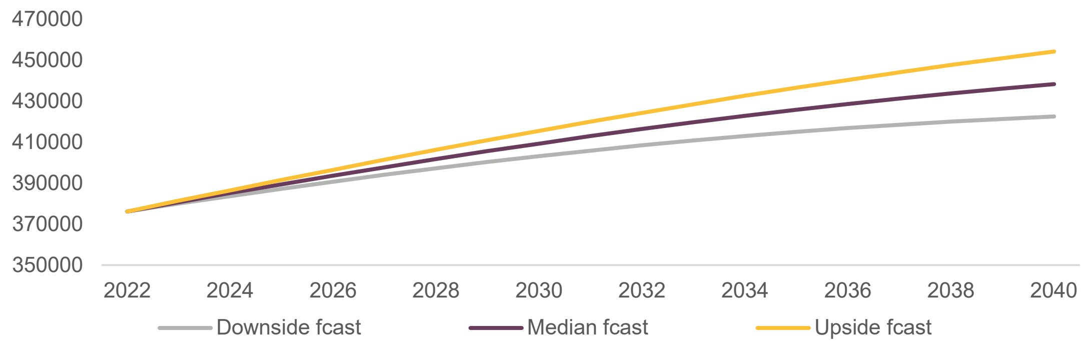
Mortgage market is flexible w.r.t. loan types with different payment burden

Outstanding mortgage loans, share of total



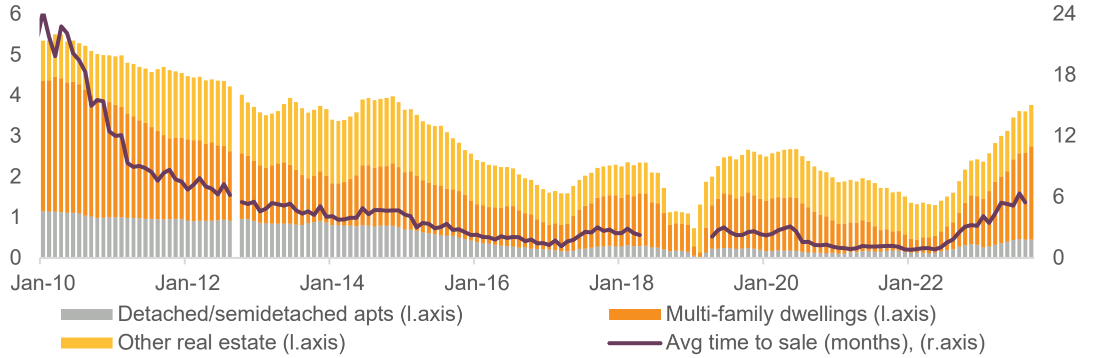
Underlying upward demand trend steady as population growth remains robust

Population forecast by Statistics Iceland



Market has until recently been characterised by limited supply

No. of purchase agreements, capital region (th.), and average time to sale



Source: The Central Bank of Iceland, Statistics Iceland.

Inflation to ease slowly at first, then fall faster in 2024

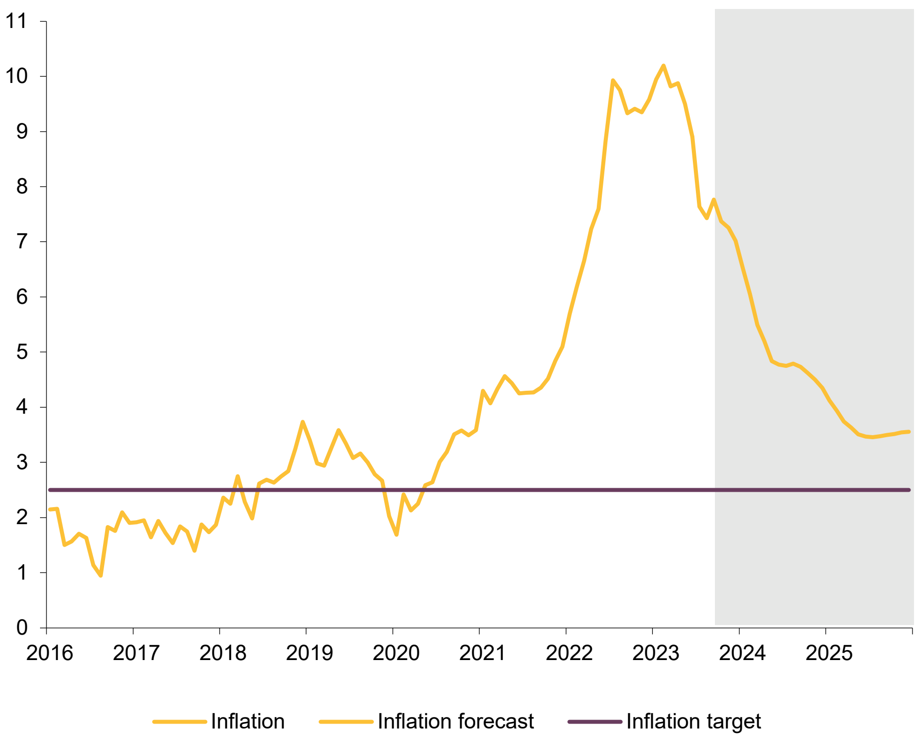
Domestic goods and services will account for a larger share of total inflation

Highlights

- In September, headline inflation was 8.0%, down from its February peak of over 10%.
- The decrease is attributed to a stable housing market and reduced imported inflation.
- Inflation is expected to stay consistent for 2021 and decline quickly in early 2024.
- Recently, house prices have increased at a slower rate, positively affecting inflation.
- By August, the combined impact of housing and imported inflation on the headline rate decreased to less than 4% from over 6% in February.
- These inflation components' significance is anticipated to decrease, with domestic goods and services playing a bigger role. Inflation from domestic costs can be challenging to manage.
- ISB Research predicts that inflation will not match the CBI's target of 2.5% in the forecast period. However, it's expected to fall below the upper limit in 2025, averaging 5.4% in 2024 and 3.7% in 2025.
- Upcoming wage agreements in early 2024 present a main uncertainty for long-term forecasts.

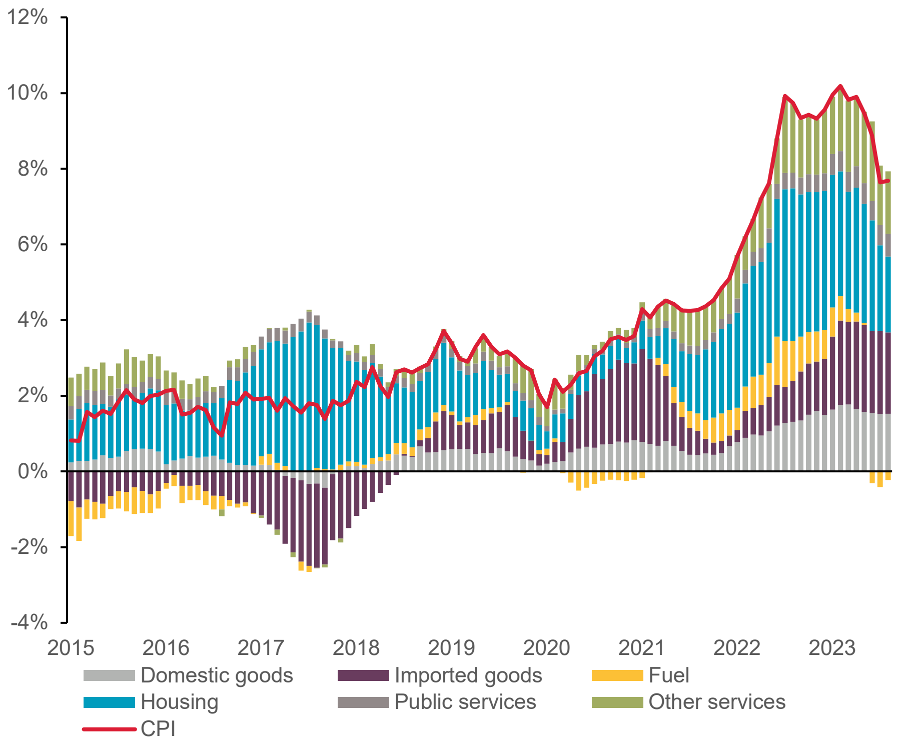
Inflation and the CBI inflation target

%



Inflation by contribution of main categories

%



Sources: Statistics Iceland, Central Bank of Iceland and ÍSB Research.

Monetary tightening phase to conclude by end-2023

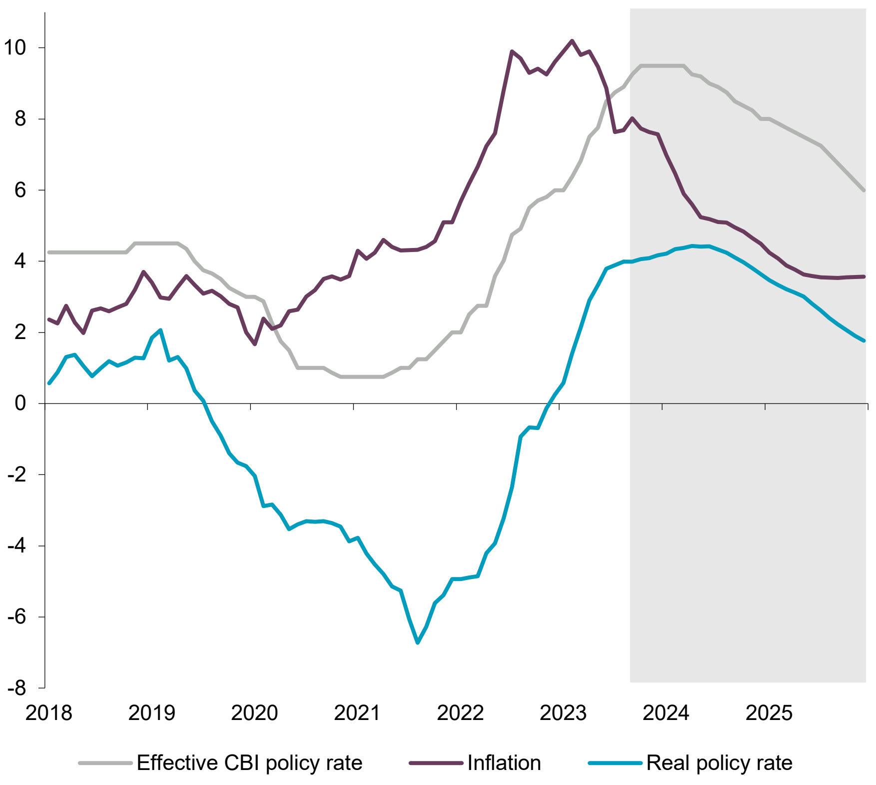
Interest rates to fall gradually towards equilibrium as inflation tapers off and demand pressures ease

Highlights

- The CBI began its monetary tightening phase in spring 2021, with the policy rate reaching 9.25% in August.
- In October, as they decided to keep the policy rate unchanged, the MPC gave particular consideration to a number of factors, including growth in deposits, lower inflation expectations, the increase in the real policy rate, and signs that previous rate hikes are having a growing impact.
- ISB Research expect the policy rate to peak at 9.5% by year-end 2023, followed by a gradual decline from Q2 2024 onwards og reach 6% in late 2025.
- Recent quarters have seen a significant in long-term interest rates, with benchmark nominal rates reaching 7,5% and real rates close to 2.9% at end-Q3.
- Long-term rates are expected to decline gradually following policy rate cuts from spring 2024 onwards.
- By the forecast's end, we anticipate equilibrium at approximately 5% for nominal rates and close to 2.0% for real rates.

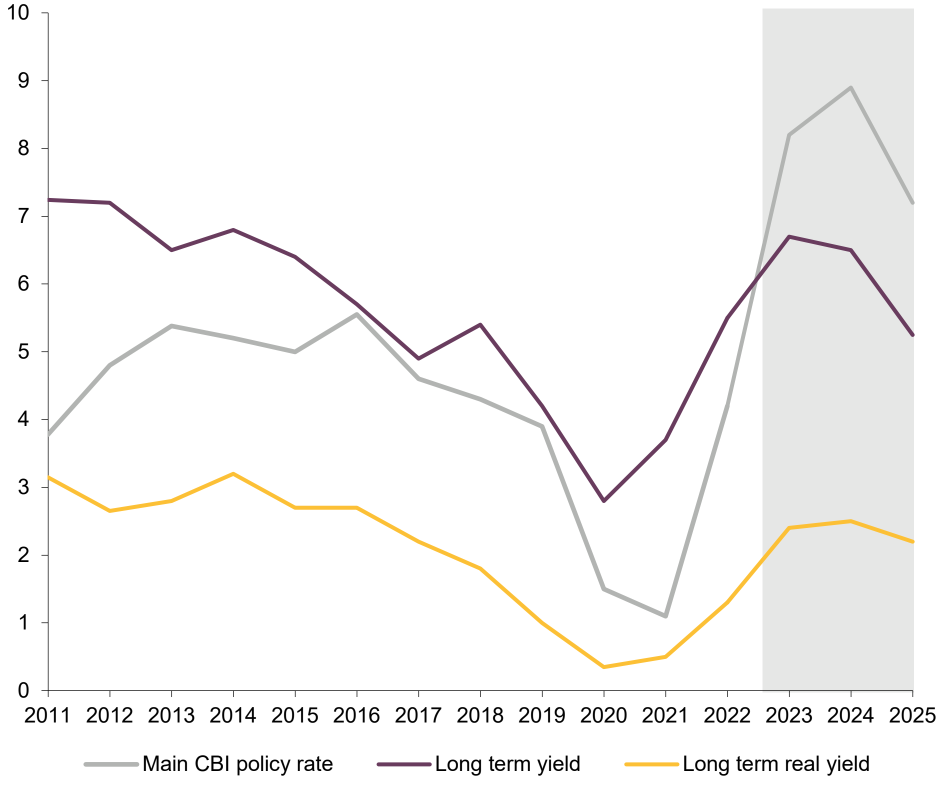
Policy rate and inflation

%, Real policy rate based on 12m forward forecasts



Key interest rates

%



Sources: Central Bank of Iceland, Kodiak, Statistics Iceland, ÍSB Research.

Modest further strengthening of the ISK in coming quarters

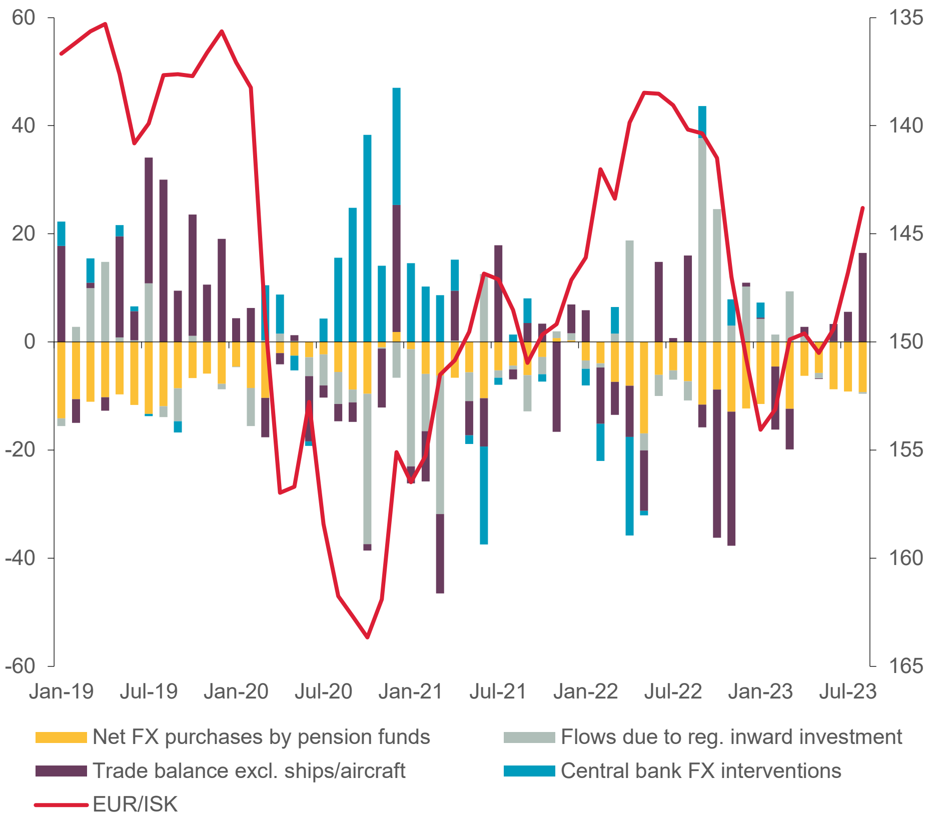
A high real exchange rate will, however, constrain the scope for further strengthening post-2025

Highlights

- The ISK has largely strengthened this year, averaging almost 6% stronger in September 2023 compared to December 2022.
- Near-term prospects for the current account indicate a small CA surplus averaging ISK 25bn annually.
- The interest rate difference with other countries seems likely to stay significant. Iceland also maintains a strong external position with a historically low stock of foreign-owned securities.
- However, potential FX inflows are counteracted by pension funds' foreign investments, totaling a net ISK 68bn in the first eight months of 2023.
- If the ISK strengthens significantly, other domestic entities might increase their foreign investments.
- Predicting exact exchange rate movements is challenging, but ISB Research anticipates the ISK to be about 5% above its September 2023 average by late 2025, equating to EUR/ISK 137.
- A potential appreciation, combined with fast wage growth and higher domestic inflation, will boost the real exchange rate.
- If domestic wages and prices continue to rise faster than those abroad, the likelihood of further ISK appreciation diminishes, while the chance of depreciation grows.

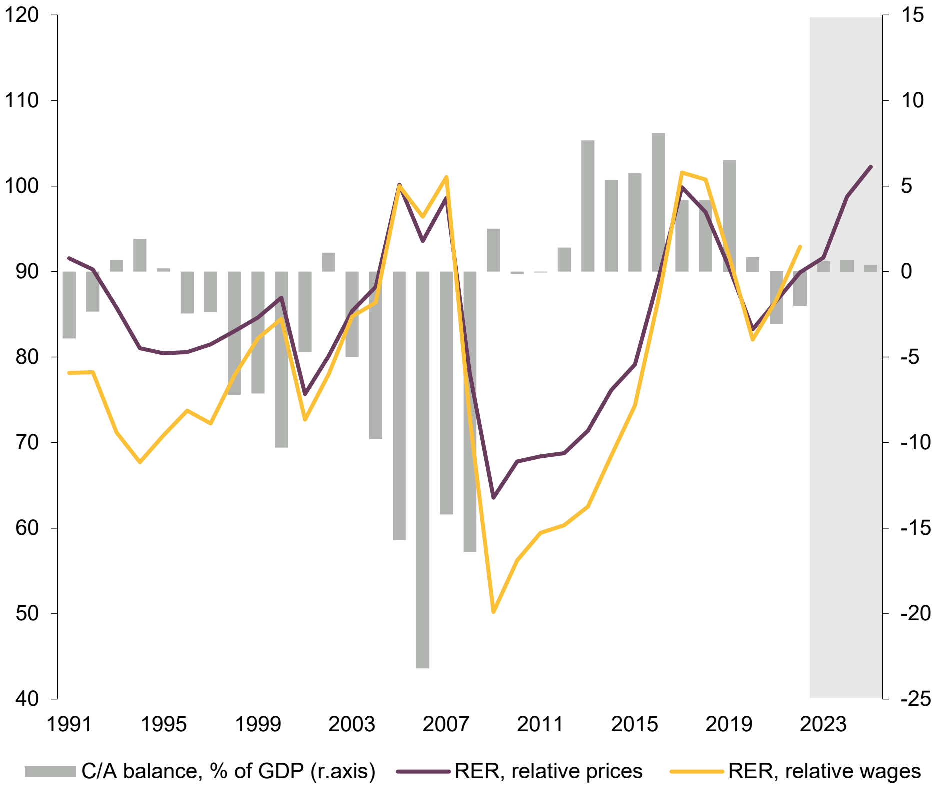
ISK exchange rate and selected determinants

ISK bn (left) and EURISK (right)



Real exchange rate and current account balance

Index and % of GDP

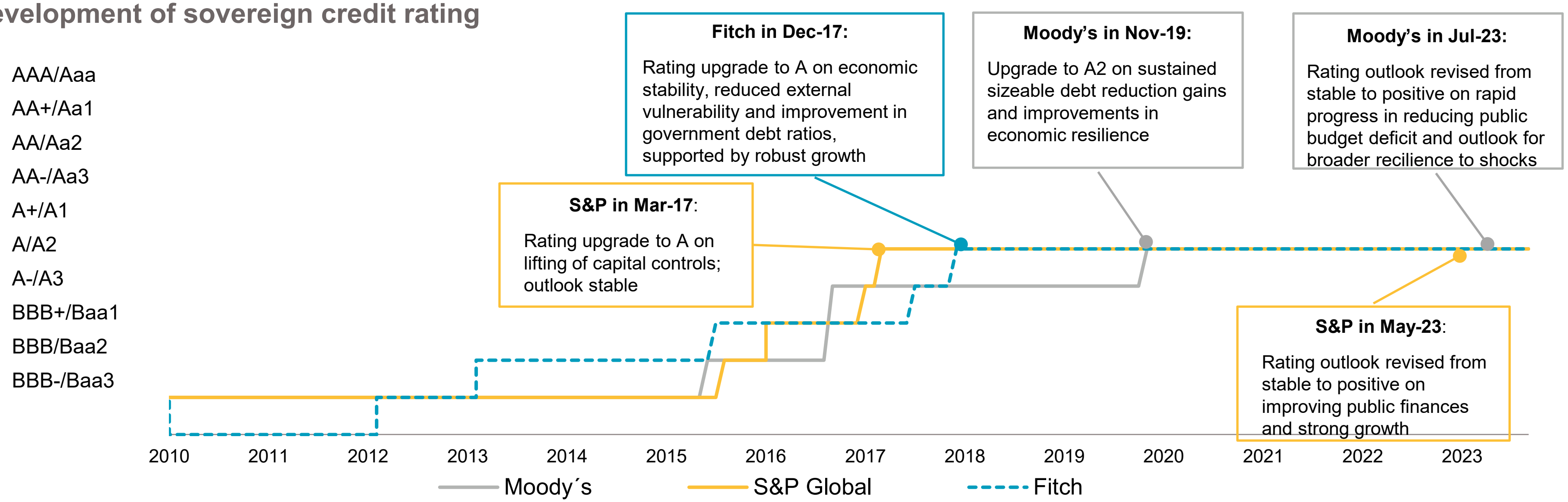


Source: Statistics Iceland, The Central Bank of Iceland, ISB Research.

Iceland's credit rating has been resilient in turbulent times

Rating companies acknowledge the flexibility of the economy and resilience to recent global shocks

Development of sovereign credit rating



MOODY'S IN AUGUST 2023

- "The credit profile of Iceland reflects the economy's flexibility, wealth, competitiveness and favourable demographics, all of which support its long-term growth prospects."
- "The economy has demonstrated its resilience to the twin shocks of the pandemic and the war in Ukraine, rebounding strongly on an effective policy response and a recovery in tourism."
- "The country has significantly strengthened its fiscal framework as well as banking supervision and regulation"

FITCH IN SEPTEMBER 2023

- "Iceland's 'A' rating is underpinned by its very high income per capita and governance indicators that are more consistent with those of 'AAA' and 'AA' rated sovereigns."
- "Strong credit fundamentals include the country's sizeable pension fund assets, sound banking sector, and strong private sector balance sheets."
- "The rating remains constrained by Iceland's small economy with its limited export diversification and high level of public debt."

S&P IN May 2023

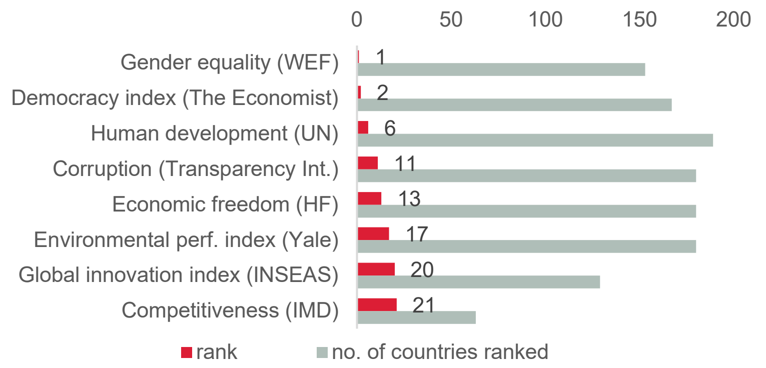
- "Strong ongoing economic recovery from pandemic fallout, alongside continued fiscal consolidation over the next few years, will improve Iceland's public finances beyond our previous expectations."
- "We expect high domestic demand and the ongoing recovery of tourism will result in real GDP growth of 3.3% this year and an average of 2.4% in 2024-2026."
- "Iceland has effectively managed external pressures, and the country's extensive energy independence has shielded the country from the fallout of the Russia-Ukraine conflict."

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

The Icelandic economy and society draw on many strengths

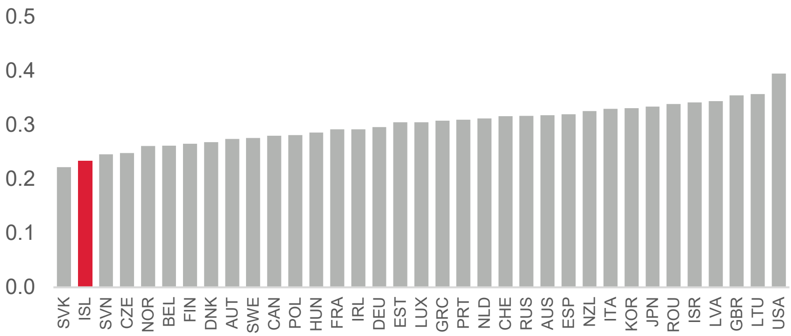
Icelanders enjoy high standards of living in a modern, open and egalitarian society

Iceland ranks highly on a variety of global development benchmarks



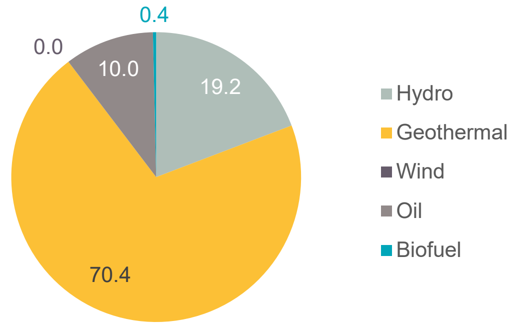
Income inequality is low compared to OECD peers

Gini coefficient, OECD, most recent data available



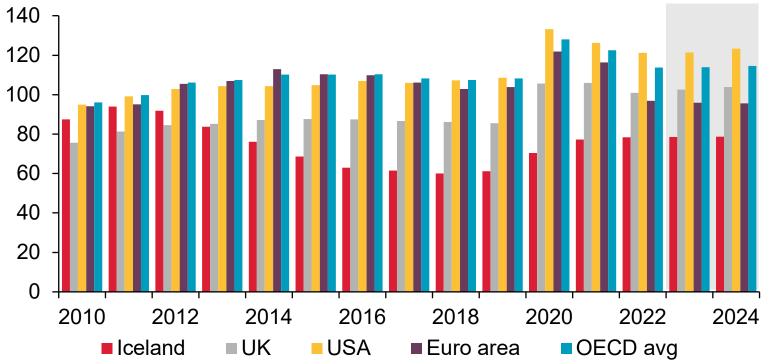
Sustainable energy usage is prevalent

Energy consumption by source, 2020



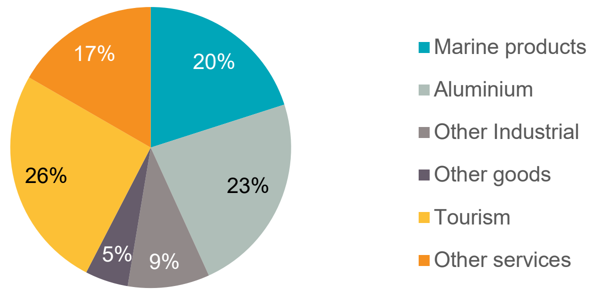
Public debt remains sustainable after pandemic

General govt. gross financial liabilities, % of GDP



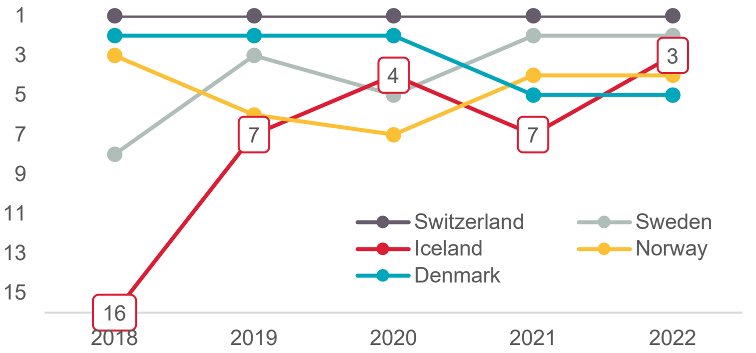
Export base has grown more diverse over time

Export contribution by industry, 2022



Iceland ranks highly in attracting/retaining talent

IMD World Talent Ranking 2018-2022



Shaded area denotes OECD forecast

Source: Statistics Iceland, OECD, IMF, WEF, IEP, The Economist, UN, Transparency Int., HF, Yale, IMD, INSEAS

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