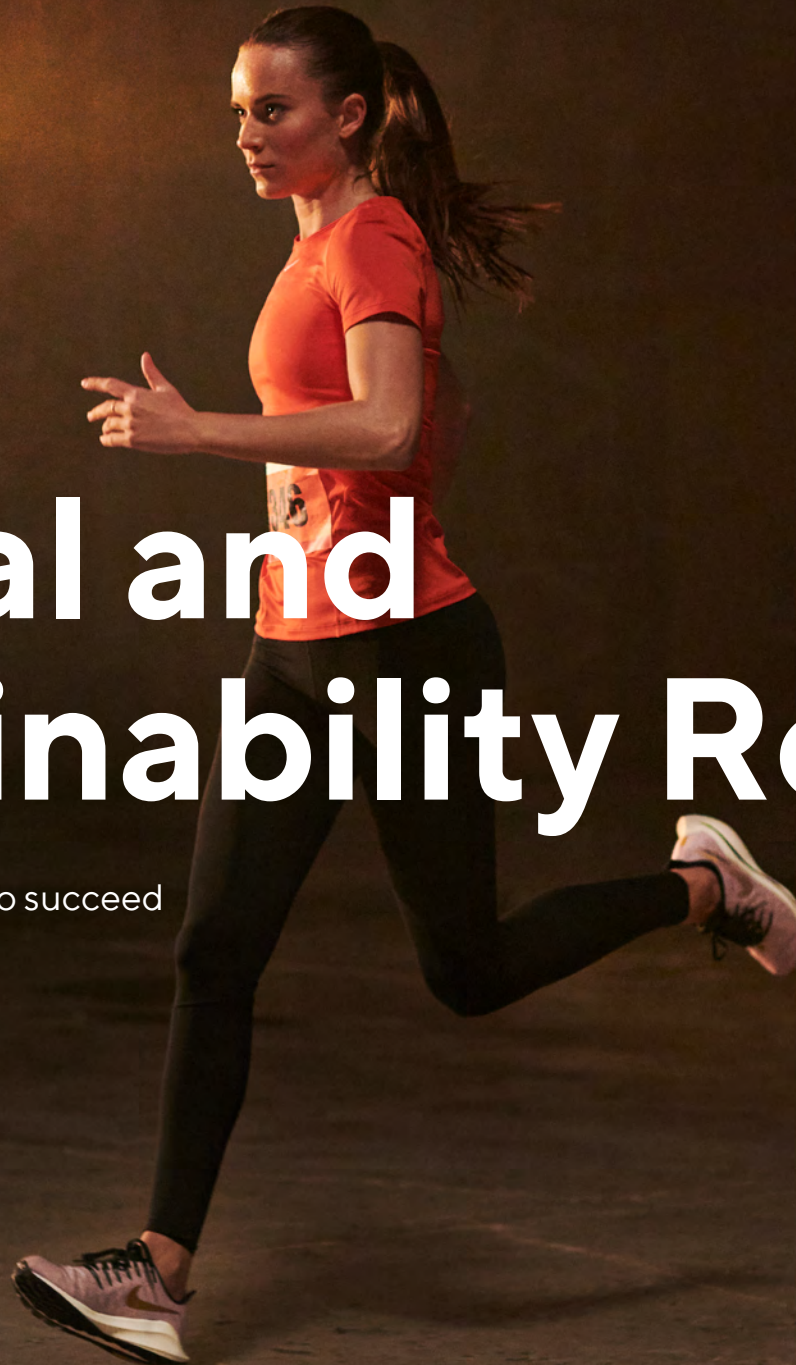


2020



# Annual and Sustainability Report

Empowering our customers to succeed





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This annual and sustainability report was written in Icelandic and translated to English. In case of discrepancy, the Icelandic original will prevail. This annual and sustainability report may include typos, discrepancies or other errors. If such errors are found the Bank reserves the right to correct them. This annual and sustainability report is published for information purposes only and should not be considered to include any investment advice, whether it be for the sale or purchase of securities.





Annual and Sustainability Report 2020

# 1 Highlights of 2020

# This is Íslandsbanki



Moving Iceland forward by empowering our customers to succeed

## Vision and Values

Vision to be  
**#1 for service**



Passion



Professionalism



Collaboration

## The Bank

**745** number of FTEs at Íslandsbanki at year-end  
**12** branches



## Market share<sup>1</sup>

**32%**  
Personal Banking

**35%**  
Business Banking

**35%**  
Corporate and Investment Banking

## Digital milestones

**31 million** visits to the app and online bank in 2020

The **first open banking** feature added to the app

**Continuous growth** in new and refinanced mortgages through automated digital channels

## Key Figures 2020

ROE	<b>3.7%</b>	LCR <small>Group, all currencies</small>	<b>196%</b>
Cost to income ratio	<b>54.3%</b>	NSFR <small>Group, all currencies</small>	<b>123%</b>
Total capital ratio	<b>23.0%</b>	Leverage ratio	<b>13.6%</b>
Tier 1 capital ratio	<b>20.1%</b>	Total assets	<b>ISK 1,344 bn</b>

## Ratings and certifications

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



EQUAL PAY  
CERTIFICATE  
2018 - 2021



EXEMPLARY IN  
CORPORATE GOVERNANCE

## Sustainability

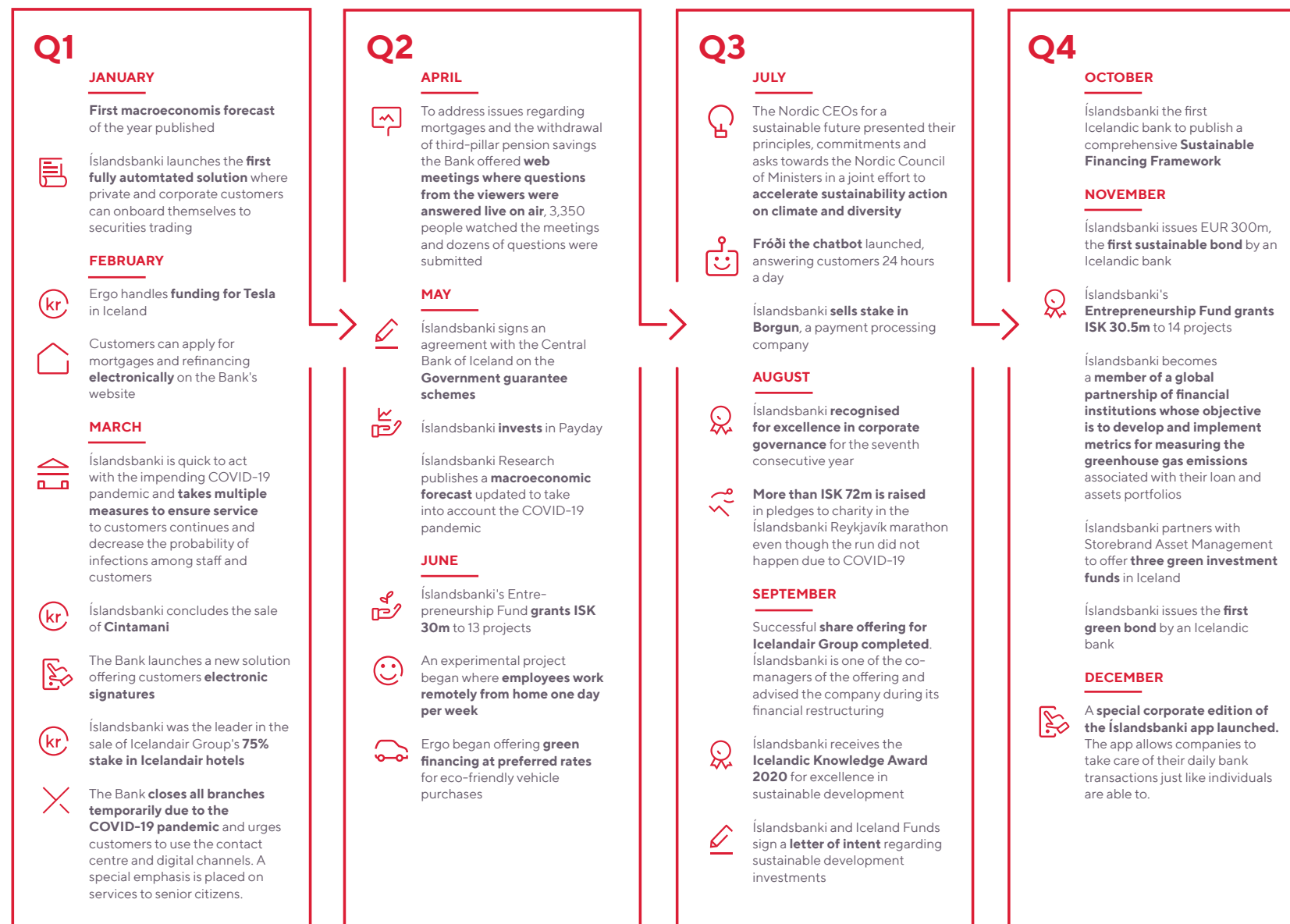
**54% less CO<sub>2</sub> carbon footprint** compared to 2019<sup>2</sup>

**13,000 people** watched 23 electronic educational meetings

**First Icelandic bank** to develop Sustainable Financing Framework



# Eventful year in memorable times



# Responses to COVID-19

The COVID-19 pandemic brought with it multiple challenges, and it certainly tested the Bank's commitment to being a force for good in Iceland. Íslandsbanki gave top priority to the health and safety of our customers and employees, and with a coordinated effort, the Bank kept disruptions at a minimum despite observing caution for public health reasons.

In response to the pandemic, a large number of measures were introduced for individuals and businesses, including freezing of loans and granting of special supplemental and support loans. The Bank prioritised digital developments so as to minimise the need for personal visits to branches, and rolled out innovations quickly and effectively, including electronic signatures, digital mortgage lending, our service chatbot, and other solutions.

The flexibility and enthusiasm of the Bank's employees, with the support of powerful technological equipment, ensured that the transition from on-site working to remote working was accomplished without sacrificing productivity.

**Íslandsbanki's response to the pandemic reflects the Bank's desire to be there for our customers, no matter what headwinds we may face. The Bank is committed to being a model of exemplary operations and participating actively in the community where we live. In the coming term, the Bank hopes to do its part to ensure that the Icelandic economy bounces back strongly once the pandemic has receded. This is how sustainability is promoted in the broadest sense.**





Annual and Sustainability Report 2020

# 2 To our stakeholders





Hallgrímur Snorrason

## Chairman's statement

Without a doubt, the year 2020 will linger long in our memory. COVID-19 made its presence known early on, and as soon as March the virus had developed into a global pandemic affecting most of the inhabited world. The impact was felt here in Iceland when demand for international flights collapsed as one country after another imposed a variety of travel restrictions. The global tourism industry was brought to its knees in a matter of days, and the Icelandic economy felt the effects very quickly. Other public health measures and restrictions on public gatherings put a damper on the economy – and the entire society, actually.

The imminent economic contraction was softened by the Government's strong foreign currency position and prudent economic policy in recent years, however. With various measures, the authorities managed to slow the rise in unemployment and protect the economy as a whole from severe shocks. Many companies had scope to respond to the contraction, and households were able to show resilience. As is discussed in Íslandsbanki's newly published macroeconomic forecast, a strong rebound can be expected in the next few years.

### **A vigorous economy with strong infrastructure**

The COVID-19 pandemic has done considerable economic damage, particularly in tourism and related sectors, but it is important to remember that the damage is unlikely to be long-lasting. Iceland has a vibrant economy and possesses extensive knowledge in important sectors such as energy, fishing, and tech manufacturing, to mention but a few.

The tourism industry is well positioned to recover quickly once international travel resumes. Iceland's captivating natural



surroundings will still be here once the pandemic has receded, and in recent years there has been enormous development in tourism infrastructure: hotels, restaurants, recreational activity providers, cross-border networking, and so forth. All of this is still in place and will generate foreign exchange revenue for the long term. The same is true of Iceland's marine products, energy-intensive industry, and knowledge and ingenuity. Seldom has emphasis on innovation and entrepreneurship been as strong as it is right now. This emphasis will foster the development of new companies, new sectors, new jobs, and new revenue-generating projects. Economic diversity is on the rise, and there is every reason to expect it to keep growing in the years to come.

#### **Simpler – and simply better – service**

Not all of COVID-19's side effects have been negative. On the plus side, the pandemic accelerated the digital communications trend that had already begun, and both technological advances and the embrace of new technological possibilities have taken place more rapidly than many could have imagined. This has also affected financial services. It has simplified communications and streamlined case handling, and the associated increase in automation and simplification of processes will help the Bank provide even better service.

With simpler and more targeted service, the Bank strengthens its competitive position

**On the plus side, the pandemic accelerated the digital communications trend that had already begun, and both technological advances and the embrace of new technological possibilities have taken place more rapidly than many could have imagined.**

vis-à-vis fintech companies and other new players in the financial market. This was put to the test when we had to respond in a variety of ways to the COVID-19 pandemic. It is clear that the Bank has strengthened its position as an efficient and effective provider of comprehensive financial services.

Íslandsbanki's response to the pandemic has changed the behaviour of its customers, who now consider it much more natural to conduct their key banking transactions using their phones and computers than to visit a branch to seek assistance or advice. This shift had already started, but the pandemic clearly expedited the process. This is extremely positive, and it gives the Bank and its employees the chance to provide even better and more personal service to customers seeking assistance with major decisions.

#### **Bank tax reduction a necessary move**

The reduction of the bank tax was approved by Parliament in 2019. At that time, the tax rate was 0.376% of the book value of commercial banks' liabilities, and the plan was to lower it to 0.145% in three increments from 2021 to 2024. When the pandemic struck, however, the reduction was expedited, and the tax rate was down to 0.145% by the end of 2020.

This long-awaited tax cut will deliver increased streamlining and healthier operations. Even so, the bank tax is still high – about five times the rate in neighbouring countries. The tax is levied on the banks' loans, thereby distorting market competition vis-à-vis other financial companies and pension funds, which grant loans but are exempt from the tax. In essence, the bank tax is a levy on private sector borrowing in Iceland. In the current situation, lowering the tax even further would have stimulated the economy more and enabled it to recover more strongly.

The bank tax and other levies that are higher in Iceland than in neighbouring countries reduce the likelihood of our being able to attract foreign investment – not least in connection with the potential sale of Íslandsbanki in coming years. A small economy with an independent currency does not need taxes and levies that ultimately distort its competitive position.

At the end of 2020, Icelandic State Financial Investments proposed that the Minister of

Finance and Economic Affairs begin the process of selling the State's holdings in Íslandsbanki, and at the end of January 2021 the Minister decided to do so, in accordance with the recommendation. It is clear, then, that another eventful year is in the offing for Íslandsbanki as it prepares for the sale.

### **Sustainability integrated into the Bank's operations**

Over the course of 2020, the Bank made significant progress in implementing its sustainability strategy, which had been approved at the end of 2019. Increased emphasis on sustainability accords well with Íslandsbanki's profitability objectives and other financial targets, but primarily it has strengthened the Bank's operations and its position in the community. Examples of the milestones we are proud of include the publication and application of our Sustainable

Financing Framework and the successful green and sustainable bond issues that followed. The Bank has also set ambitious sustainability objectives centring on both the expansion of our sustainable product offerings and the neutralisation of our carbon footprint. We are determined to be a model of sustainable operations as well as a force for good in the community.

### **Concluding remarks**

Friðrik Sophusson stepped down from his position as Chair of Íslandsbanki's Board of Directors last year, after a decade at the helm. I would like to thank him in particular for the tireless work he has done for the Bank during his tenure on the Board, often tackling demanding projects under equally demanding circumstances. Auður Finnbogadóttir, Tómas Már Sigurðsson, and Flóki Halldórsson also left the Board during the year, and we wish

to thank them for their contribution as well. Frosti Ólafsson, Guðrún Þorgeirsdóttir, and Herdís Gunnarsdóttir have joined the Board, and I would like to thank them and their fellow Board members – Anna Þórðardóttir, Árni Stefánsson, and Heiðrún Jónsdóttir – for fruitful collaboration over the past year.

The COVID-dominated year 2020 has been challenging for the Bank's managers and employees, who have done their jobs under extraordinary and often extremely taxing circumstances requiring innovative responses and hard work. In closing, I would like to thank the management and staff of Íslandsbanki for their dedication and outstanding performance during a very difficult year. With a team of employees and exceptional as ours, Íslandsbanki can be optimistic about the future.







Birna Einarsdóttir

## CEO's address

It is safe to say that 2020 was a memorable year for a number of reasons. The global COVID-19 pandemic changed our daily lives through its impact on our health and the associated bans on public gatherings. The impact on the economy and labour market will gradually come into focus, but it is already clear that businesses and individuals faced major challenges during the year.

The impact on Íslandsbanki is no exception, and our focuses and priorities changed radically with the onset of the pandemic. But every cloud does indeed have a silver lining. We made an even more concerted effort to increase the flow of information to our customers and employees, which is of key importance in times like these. To protect both groups, we had to impose limits on visits to branches and ask nearly all of our employees to work from home. This further accelerated the shift that has been underway in recent years, and more customers used our digital solutions for all of their main banking activities. Through instruction and regular messages, we increased the number of active Íslandsbanki app users, and the number of new customers who have begun their business relationship with us digitally is up 40% year-on-year.

The challenge underlying all of these changes was to continue providing personal service to customers taking major decisions, in line with the Bank's vision of providing the best service possible. Among our priorities was our desire to make a special effort to take good care of senior citizens and customers who cannot use digital services. We launched a dedicated telephone service line for this group, to the great satisfaction of our customers, and we receive thousands of calls each month. Service means everything to us, and when we look back, we hope to be able to say that we were successful in supporting our customers.

### A digital leap

We used the year well and developed new solutions, and our new product-centred IT Department structure played a major role in

the process. It can be said that the pandemic accelerated the trend towards digital signatures, greatly simplifying our communications with our customers. We also introduced our new chatbot, Fróði, the first chatbot of its kind in Iceland. Fróði handles over half of all customer queries himself – at any time of the day or night. Customers who have opted to speak on the phone with advisors have been given direct contact, but measurements show that those who have used Fróði are very happy with the service and the answers they receive.

On the corporate side, we made great digital strides, including a new app for companies and the option of setting up a business relationship digitally in just a few minutes. This will greatly simplify companies' banking business, and it is gratifying to offer them this additional service.

### Support during difficult times

At the beginning of 2019, we embarked on strategy formulation work and defined the Bank's role: empowering our customers to succeed by being a force for good. This has proven highly appropriate at times like these, when it is vital that banks help their customers through difficult circumstances. According to the Bank's macroeconomic forecast, with vaccines just around the corner, there is cause for optimism about the economic recovery, and a strong rebound is expected next year if current assumptions are borne out.

**During this time when we have supported our corporate customers as they face new challenges, there has been a surge in new lending.**

In 2020, we granted several hundred support loans and supplemental loans bearing Treasury guarantees, and we helped households and businesses to freeze loans as needed. In general, companies' position was strong before the pandemic struck, which was very important. The greatest challenge therefore lay in liquidity shortages due to a temporary setback, not in debt problems.

Íslandsbanki worked closely with Icelandair on its financial restructuring plan, and the Bank's Corporate Finance Department oversaw the airline's share capital offering. The project was important, and not only for Icelandair and Íslandsbanki. It is vital to maintain reliable air travel to and from Iceland and to ensure that the airline will be ready to participate in a robust recovery.

### Service merged in the corporate banking centre

Services to small and medium-sized enterprises (SME) were merged during the year with Íslandsbanki's corporate banking centre in Norðurturn, the Bank's headquarters. The objective of the merger was to boost synergy and efficiency and provide good service. We believe it is possible to provide personal and reliable service no matter where the customer is. We also launched a corporate banking centre in Akureyri, for North and East Iceland.

Íslandsbanki has been a leader in the market for small and medium-sized enterprises (SME), with Iceland's largest market share, and the results of this year's annual SME service survey were the best ever. We are determined to continue on this path, providing businesses with personal service combined with powerful digital service.

During this time when we have supported our corporate customers as they face new challenges, there has been a surge in new lending. The market for new and used motor vehicles rallied strongly, and many types of retail and wholesale trade have benefited from increased local spending by Icelanders, although the lack of foreign tourists is felt keenly. It was gratifying to see the surge in green car loans from Ergo, as customers shift towards eco-friendly vehicles. Ergo was





also the first player in the market to offer financing for electric bicycles and charging stations for electric cars. This is in line with our sustainability strategy and our goal of increasing the share of green financing in our loan portfolio.

### Strong investment banking

Corporate and Investment Banking had a good run in 2020, with the successful Icelandair share offering, and Corporate Finance had a record year. The Bank was also a leader in FX sales and had the largest trading volume on Nasdaq Iceland.

Funds managed by Íslandsbanki's subsidiary, Iceland Funds, were valued at over ISK 200 billion, and the company led the domestic fund market with a market share of 35%. The Liquidity Fund, Iceland Funds' largest, is also the largest in the Icelandic market, at about ISK 60 billion. It is extremely popular among those who want to invest liquid assets, which is challenging in the current interest rate environment.

We have seen growth in the Green Bond Fund, which invests in bonds that finance sustainable projects with a positive impact on the environment and the community. Customers receive a separate impact report that shows how their savings reduce carbon emissions. Interestingly, every million krónur invested in the fund reduces carbon emissions equivalent to seven

round-trip flights to London each year.

### Carbon-neutral operations

At the end of 2020, the Board of Directors approved the Bank's Sustainability Policy, which is in line with the priorities laid down in the strategy formulated at the beginning of 2019. In consultation with the Bank's employees, we decided to prioritise four of the UN Sustainable Development Goals: Climate Action; Gender Equality; Quality Education; and Industry, Innovation, and Infrastructure. Our tasks have been anchored by the Bank's vision of being a force for good and, equally important, a model of sustainability in the community.

One of our biggest projects for the year was to formulate a framework for sustainable loans in the asset portfolio. Íslandsbanki was the first Icelandic bank to do this. The framework covers projects focusing on the environment, sustainable fisheries, and social development. The objective is to increase the share of such projects in the Bank's loan portfolio. We are exceedingly proud of this work, which will be very important for the Bank's sustainability journey.

Íslandsbanki has also become a member of a global partnership of financial institutions whose objective is to develop and implement metrics for measuring the greenhouse gas emissions associated with their loan and asset

**One of our biggest projects for the year was to formulate a framework for sustainable loans in the asset portfolio. Íslandsbanki was the first Icelandic bank to do this.**

portfolios. The Bank aims to shrink the carbon footprint from its operations by 50% between 2019 and 2024. Since 2019, the Bank has ensured that its operations are carbon-neutral by using mitigating measures to offset the portion that it has not reduced.

We are very proud of having completed the largest sustainable bond issue ever undertaken by an Icelandic company. Investors showed keen interest, demand far outstripped supply, and the financing terms were favourable. The proceeds will be used solely for sustainable loans and investments, and the Bank has already allocated ISK 25 billion to sustainable projects. Taken together, these projects prevented emissions equivalent to 5,800 tonnes of carbon in 2020.

Last but not least, I want to thank our customers for the fruitful dialogue we have had on these matters in the past year. We introduced our Suppliers' Code of Conduct

and initiated dialogue on equal rights and environmental affairs with our biggest suppliers. It is clear from those conversations that we are all moving in the same direction, which will bring us a more diverse and even more powerful business community.

### **A demanding operational year**

As I have mentioned just now, Íslandsbanki's operations were highly unconventional due to the extraordinary circumstances brought on by the pandemic, and many of our customers suffered temporary loss of income. The Bank participated in a general agreement among Icelandic lenders to grant those customers moratoria on payments, and about 1,500 households and 600 businesses took advantage of the option. In spite of headwinds in much of the domestic economy, 2020 was a strong year for Íslandsbanki. Our overall expenses declined by 13.6%, and at the same time we saw growth in both deposits and lending – by 9.9% and 11.9%, respectively. The loan growth was mostly due to strong demand for mortgages. The consolidated profit for the year, ISK 6.8 billion, corresponds to an annualised return on equity of 3.7%, which is below the Bank's long-term profitability target. The uncertainty due to COVID-19 could be seen in significant negative impairments in the first half of the year, although the performance was much stronger in the second half, with a return on equity of 7.6% in the fourth quarter. Both liquidity ratios and capital

ratios strengthened during the year and are well above internal targets and regulatory requirements.

Íslandsbanki demonstrated its strength as a universal bank with service at the forefront, and its robust financial position reflects this. The battle with COVID-19 is not yet over, but we are determined to stand by our customers throughout periods of uncertainty, with the aim of regaining a strong footing when the pandemic has passed.

### **Passion and collaboration**

The Bank's values are passion, professionalism, and collaboration. These three words have truly been a guidepost for us throughout the past year, and it is safe to say that they describe the Íslandsbanki team. Our employees have adapted to seismic changes with humility and a positive attitude. Before they began working from home due to COVID-19, we had been working towards reducing the Bank's carbon footprint. Staff members will continue to work according to a flexible structure that includes some remote working. Measurements taken during the year showed the highest job satisfaction ratings ever, which is enormously important to us. I want to thank our employees for continuing to work tirelessly under circumstances that are truly unparalleled.

I look very much forward to the coming year and the journey ahead with our customers and employees.





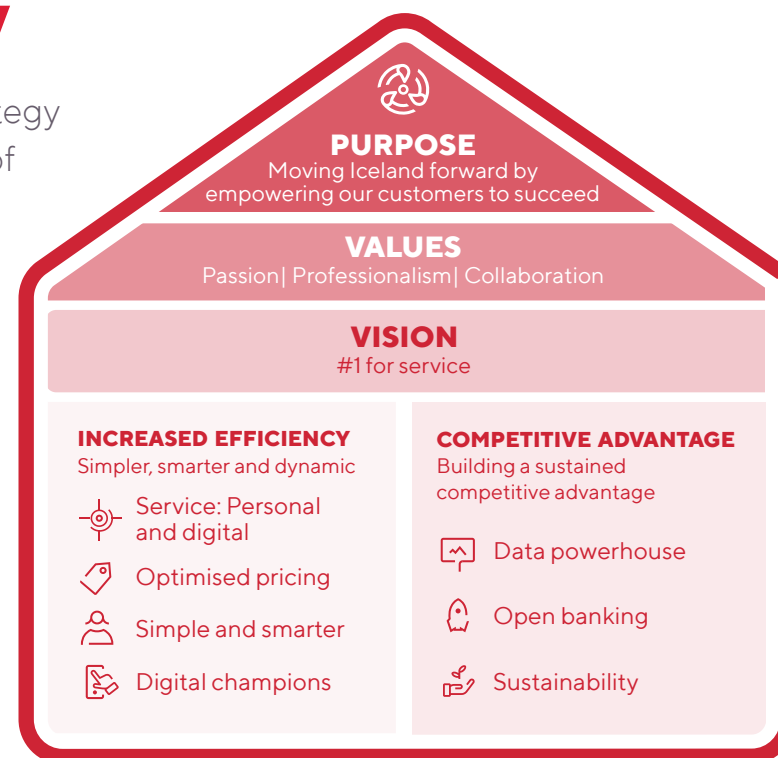
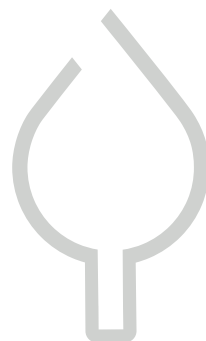
Annual and Sustainability Report 2020

## 3 Empowering our customers to succeed

# Íslandsbanki's strategy

Today Íslandsbanki operates in accordance with a strategy approved by the Board of Directors at the beginning of 2019, following extensive work involving customers, employees, and other stakeholders.

According to the strategy, Íslandsbanki's objective is to be a force for good in the community, and its vision is to provide customers with the best banking service possible at all times. In order to contribute to the intended outcome under the new strategy, the Bank defined seven strategic themes for a five-year period. The themes fall into two broad categories: Sharpening our focus and achieving simplification and greater efficiency; and thinking big, thereby securing a competitive advantage for the future.



## A catalyst since 1875

Íslandsbanki has a long history stretching back to 1875. In its earliest years, the Bank participated in the development of the fishing industry, acting as a springboard for the Icelandic economy. From the beginning, then, Íslandsbanki has been a force in the community. Although sustainability has been one of the Bank's main priorities since 2014, the step taken with the strategy formulation

work in 2019 put sustainability and a positive impact on society into even sharper focus as the Bank's main purpose. To us, focusing on sustainability is not merely an act of altruism; it is also an opportunity to distinguish ourselves, an important element in risk management, and a boon to long-term profitability. In 2020, significant progress was made towards integrating sustainability into the Bank's overall

activities – an effort that has been widely praised and has received deserved attention. For instance, Íslandsbanki received the 2020 Icelandic Knowledge Award for outstanding performance in the area of sustainable development.





Sharpening our focus

## Simplification and greater efficiency

During the year, the Bank's goal was to move closer to boosting efficiency and sharpening focus, as can be seen in the reduction in the cost-to-income ratio.



### Service: personal and digital

In recent years, the way in which customers seek out banking services has changed radically. Digital solutions have become steadily more popular, while visits to branches have been on the decline. Visits to branches fell by almost half between 2014 and 2019, and by 72% between 2014 and 2020. The COVID-19 pandemic ushered in even faster change than had been foreseen at the beginning of the year, but even though the situation was extraordinary, the change would be a permanent one in many ways.

It is clear that digital solutions will continue to gain ground, but that which cannot be digitised will become even more important. We are determined to remain #1 for service, and we are convinced that the secret to success lies in providing service that is both personal and digital.



### Optimised pricing

A well-defined pricing structure has led to more price efficiency. A clear presentation of price information in systems for various types of customers has also expedited processes relating to interest rate changes, product development, and loan applications. Particular emphasis has been placed on using data even more effectively for preparation of pricing models and measurement of compliance with the Bank's profit objectives. A clear strategy for asset management and pricing in line with the Bank's objectives, together with successful implementation of the strategy, supports appropriate pricing decisions, so that the Bank offers the right products at appropriate prices.



### Simple and smarter

During the year we continued to focus on simplification and enhanced efficiency. An increasing number of teams are adopting lean methodology, and key Bank processes have been streamlined. Furthermore, the introduction of robotics is proceeding apace, as can be seen in the automation of processes relating to mortgage lending and payment services.

During the year, Íslandsbanki also took a major step in merging nearly all of its back office projects at one location in a single unit called Back Office. This merger brings with it considerable streamlining, as comparable tasks will be carried out in the same location, boosting efficiency.



### Digital champions

During the year, the Bank established a product-centred approach to digital development. The aim is to respond more quickly to customers' needs and ensure effective and fruitful cooperation between business units and the Bank's IT team. Product teams are led by product managers from the business units. The business units set goals and strategies for the product teams and participate in product development.

A single team is responsible for the strategy, design, development, and operation of each product, which simplifies communications, improves product quality, and enhances operational sustainability.



Thinking big

# A competitive advantage for the future

Three of the Bank's strategic themes centre on securing a competitive advantage for the future: being a data powerhouse, having a unique position in an open banking environment, and being a leader in sustainability. We worked hard and effectively on all of these fronts during the year, thereby better preparing the Bank to meet customers' diverse needs.



## Data powerhouse

Early in the year, we established a strong product team to support this strategic theme. We also updated our tech strategy early in the year, sharpening our focus on data and data utilisation. We have placed stronger emphasis on using data intelligently so as to serve our customers and ensure efficiency from beginning to end. This entails harnessing valuable data in order to understand our customers' needs and offer targeted services, products, and prices. Our chatbot Fróði is another good example of data harnessing, as Fróði is always learning and adding on knowledge based on the queries he receives from customers.



## Unique position in an open banking environment

At the beginning of the year, we opened a developer portal for our open banking partners to connect with the Bank, and the first open application programming interfaces (API) are now accessible to our partners. In 2020, the Board and the Executive Committee approved a concise strategy on the Bank's unique position in an open banking environment. Under the strategy, the Bank will begin by concentrating on opportunities relating to lending. In this area, we plan to give serious consideration to opportunities for cooperation over and above what is needed or provided for in the second EU Payments Services Directive (PSD2).



## Leader in sustainability

The Bank introduced its Sustainable Financing Framework during the year and then obtained sustainable and green funding based on the framework. We also added sustainable investment offerings and approved our first sustainable corporate loans under the framework. The Sustainability Committee began work during the year, and both processes and administrative structure relating to sustainability were strengthened significantly, in keeping with the Bank's determination to realise its ambitious sustainability objectives and be a leader in the field.



## Strong together

# Our people

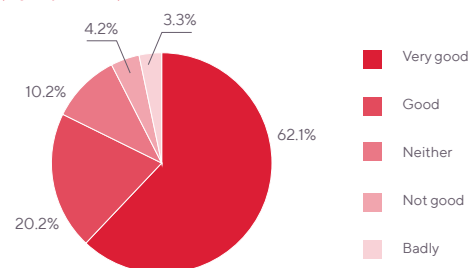
Íslandsbanki strongly emphasises creating a positive work environment with passion, professionalism, and collaboration as guideposts. Our people are our most important resource, and we want everyone to be satisfied at work and have the opportunity to grow in their jobs.

### The work environment and remote working

Rapid technological developments in recent years have expanded the possibilities for a more diverse work environment than has been known hitherto. Íslandsbanki's activity-based workplace is an excellent example of this. Íslandsbanki has also been a leader in formulating and implementing remote working strategies. An experimental project and preparation for remote working began at the turn of the year, and all of the Bank's preparatory work, training, and planning were well underway by the time employees began working from home in March. This facilitated the sudden switch to teleworking and enabled employees and managers to adjust unusually well to the new set of circumstances.

Three staff surveys that were carried out in 2020 showed clearly that employees are willing and able to work remotely and can adapt to it, that social connections among staff members remained intact, and that managers were well able to manage their teams under such conditions. The surveys also showed that

How do you feel about continuing working partly remotely?  
(e.g. 1x per week).



employees view Íslandsbanki as a force for good in the community, in line with the Bank's vision, and that they want to do their part to ensure that this vision is realised. Remote working gives employees the opportunity to contribute to sustainability objectives, as it eliminates the need to drive to and from work, thereby reducing carbon emissions.

The shortening of the work week took effect during the year. It takes the form of one half-day off per month from 1 September through 31 May. The implementation of the shorter work week went smoothly and contributes to employees' health and well-being, which is one of the Bank's key priorities.



### Awe-inspiring adaptability

*"The year 2020 will go down in history for a number of reasons, but the impact of the global COVID-19 pandemic on the economy and employment will be chief among them. Developments following the onset of the pandemic put Íslandsbanki in the unprecedented position of having most of its staff forced to work from home, and the lessons learned from this challenge were invaluable. The shift occurred virtually from one day to the next, and because our outstanding staff members are so accustomed to a flexible work environment, it went far more smoothly than we had hoped. Our employees demonstrated awe-inspiring adaptability, admirable resilience, and a spirit of collaboration that we can all be proud of. We closed ranks during this difficult year and came back twice as strong."*

**Hafsteinn Bragason**  
Head of Human Resources



## Remote working and well-being

The surveys conducted during the year clearly showed the success of the remote working scheme. In the surveys, employees were asked about their general well-being, job satisfaction, and anxiety levels, and how remote working was going for them. The results were gratifying, with high job satisfaction levels in all of the surveys – the highest in years, in fact – better-than-expected general well-being, high levels of dedication among employees, and greater overall success with remote working than had been hoped for.

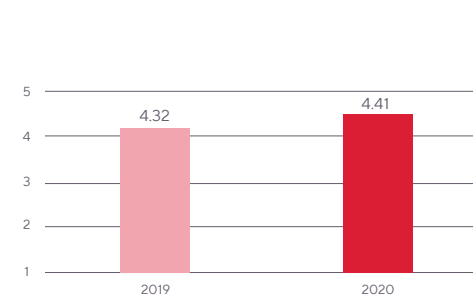
## Social objectives

Although climate issues dominate the sustainability discourse at present, it is still important for the Bank to adopt clear objectives for social issues such as equal rights and diversity. Placing strong emphasis on social issues delivers better operations, lower risk, and a more cohesive culture within the Bank.

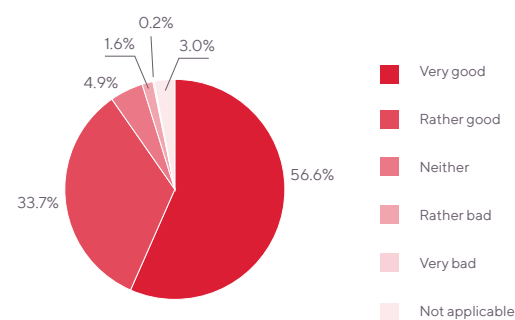
Íslandsbanki aspires to have equal gender ratios in all of its divisions, departments, committees, councils, boards, and executive positions. In addition, the Bank aims to increase the proportion of women in its investment banking and information technology activities and to increase the share of men in front-line positions.

As in previous years, the Bank received equal pay certification and was awarded professional certification under the ÍST 85:2012 Equal Pay Standard for 2020.

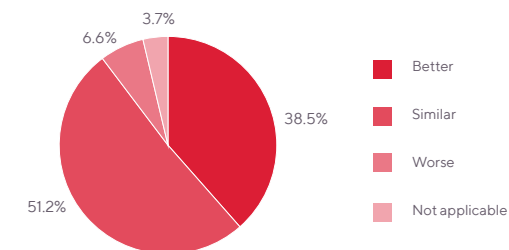
On the whole, I am satisfied in my job with Íslandsbanki



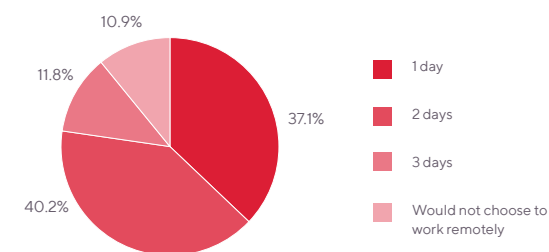
On the whole, how has remote working been for you?



Do you consider your remote work performance better than, similar to, or worse than your on-site work performance?



How many days per week would you choose to work remotely?



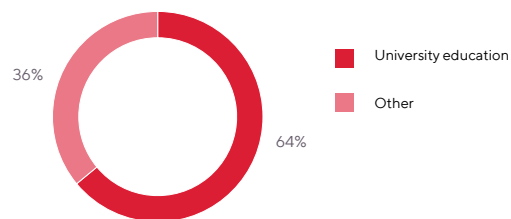
## Education and training

In modern knowledge-based companies it is critical to maintain and increase staff knowledge. The Bank offers over 200 courses and educational meetings each year. In most cases, the instructors are Bank employees who thereby share their expertise across departments. Although the instructional programme covers a wide range, employees are required to attend certain courses that pertain to their jobs, including courses on security matters, compliance or, for managers, leadership courses. In addition to these, the Bank offers a number of other courses centring on personal growth and job development. Among them are seminars in time management, project management, mental and physical health, and various work-related skills. Managers at all levels are supported with structured leadership training. The Bank also

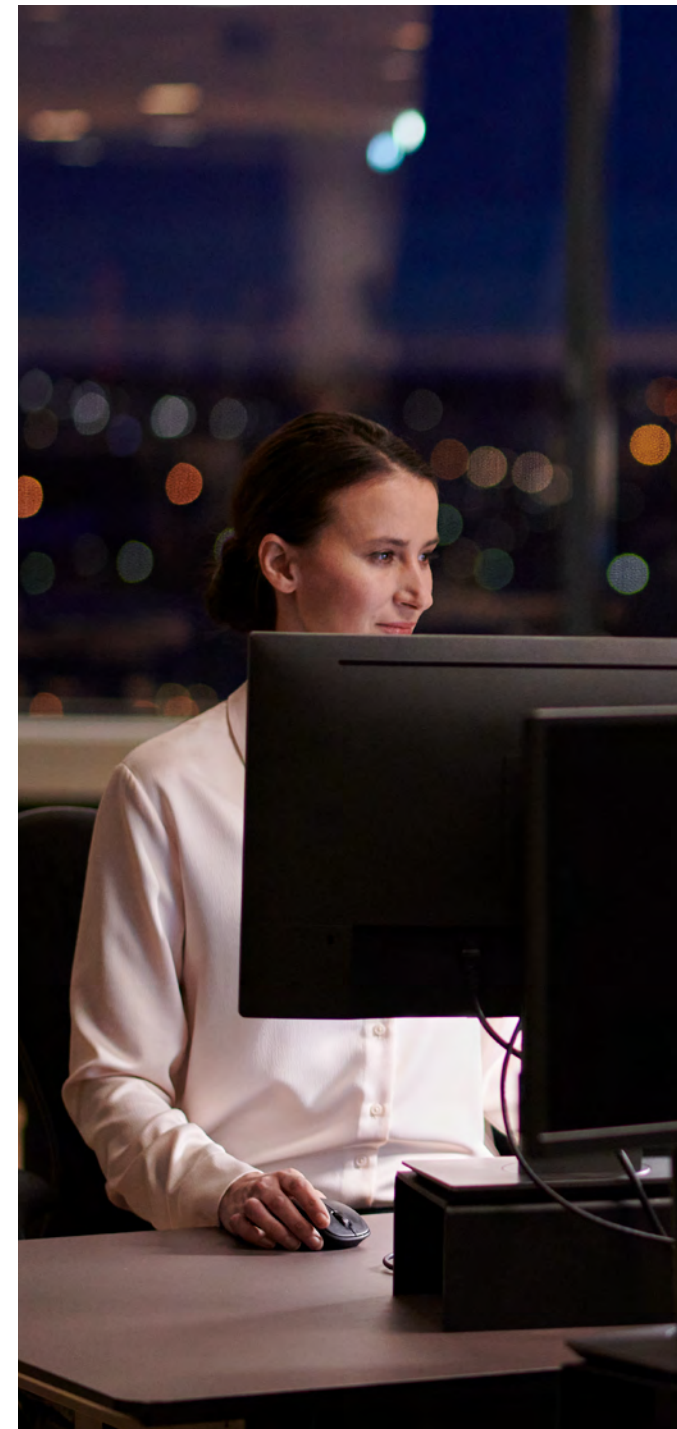
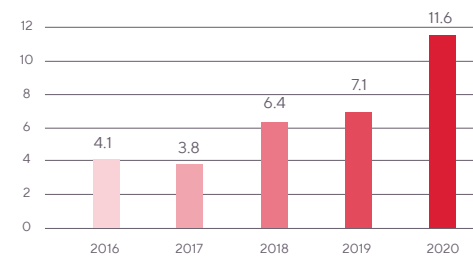
follows a management competency model that defines the conduct conducive to success in management. The objective of leadership training is to strengthen managers in these areas and help them to master their leadership role.

The educational programme is designed to be tightly structured, yet with a high degree of flexibility. The value of this approach became obvious in 2020, when it proved necessary to move all education and training to digital platforms from March through the year-end. The increased emphasis on digital education delivered a significant increase in the number of courses offered, the average number of courses per employee, and the range of options available to both managers and employees.

Education



Average number of courses per employee



# Positive effects of remote working

Íslandsbanki has established a structure where employees will work from home an average of one day a week. This will bring greater job satisfaction, a reduced carbon footprint, and positive operational impact.



## Increased flexibility and employee satisfaction

The trend of the past few years towards more flexibility in work and the working environment will continue, and it can be expected that the employees of the future will increasingly want the option of working from home part of the time. It is important to answer the call and be competitive in this respect, in the eyes of current and future employees.



## Sustainability considerations

Having employees work from home one day a week will do much to reduce the Bank's carbon footprint, and it is a key step towards achieving our objective of being carbon-neutral by 2025. Cutting the number of employees who travel to work each day by one-fifth is an important contribution to reduced traffic in the greater Reykjavík area, with the associated positive environmental impact. The Bank hopes that other companies, institutions, and even schools will follow suit.



## Positive operational impact

This change saves money and contributes to operational streamlining by reducing the use of heat, electricity, and parking space and decreasing food purchases, in addition to other benefits of having employees work from home one day a week.





Annual and Sustainability Report 2020

**4Through  
collaboration  
we are  
#1 for service**

# Personal Banking

## Market share

**32%**

individuals

**31%**

deposits

Personal Banking provides customers with a comprehensive range of financial services, with strong emphasis on digital distribution channels.

Providing high-quality service to customers, whether through personalised advice or through easy access to digital solutions, ensures that customers will be satisfied. Today, Íslandsbanki's Personal Banking customers can conduct their banking business day or night, seven days a week – whenever they choose. Distribution channels such as our ATMs and our app, online banking, and online chat functions are up and running 24/7/365. Our advisory centre and branches are open during conventional business hours, as has

been customary, although the COVID-19 pandemic greatly affected branches' opening hours in 2020. During the year, we took a number of steps to make banking services even more accessible, and our simple solutions – such as priority phone lines for senior citizens and mortgage loan customers – have been exceedingly popular. The same can be said of the digital innovations that make banking more accessible and user-friendly for customers who prefer self-service options.



The first Icelandic bank to offer **Fróði**, a **chatbot available 24 hours a day**



**47% increase** in new customers who begin their banking digitally, though our **Onboarding initiative**



App users **up 12% year-on-year**, to 87,000



The number of telephone calls on the **senior citizens' line is up 75%** since the beginning of 2020



**23% market share in mortgage lending** – the Bank finances more households nationwide than ever before



## Personalised digital banking services

*"2020 was an extraordinary year in many respects. The global COVID-19 pandemic made a strong impact, ushering in rapid changes and accelerating the implementation of solutions for day-to-day banking services. For much of the year, access to the Bank's branches was limited because of bans on gatherings, yet at the same time, customers' access to personalised service has been expanded. Concurrent with the first closure of branch offices*

*in the spring, we introduced priority telephone lines, a very well received service enhancement. The successful launch of our chatbot Fróði has proven to be a boon for the Bank during the flood of telephone calls from customers seeking information. The Bank also introduced a number of new smart solutions during the year, chief among them automated mortgage refinancing, a new digital securities trading solution, and various*

*enhancements to app and online bank functions, including loan prepayments, information services, etc. We welcome 2021 with open arms and look forward to meeting our customers' needs with outstanding personalised service."*

**Sigríður Hrefna Hrafnkelsdóttir**  
Director, Personal Banking

## Organisational structure

### Loans

Offers a wide range of loans for customers, from overdraft accounts to mortgages, with a fully digitised and automated credit assessment process. It is also possible to apply for a loan of up to ISK two million in a matter of minutes through the Íslandsbanki app.

### Savings

Offers savings options that suit customers' differing needs, including third-pillar pension savings and mutual funds. Now customers can use the app to open savings accounts tailored to their needs, including a new digital account. Customers can also use the app to open a custodial account and begin investing in funds and securities.

### Payment solutions

Offers simple, effective payment solutions in the front ranks of payment market products. Now Íslandsbanki customers can access all services relating to payment cards through digital distribution channels, making the service a simple and natural part of their everyday lives. Íslandsbanki was the first bank to offer payments via Apple and Android smartphones and via smart watches such as Garmin and Fitbit.

### Other services

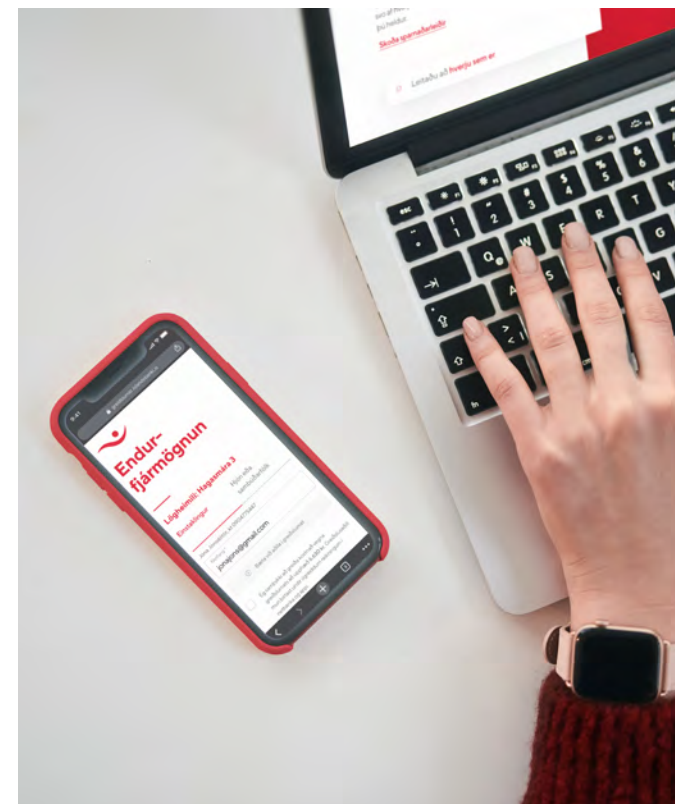
The advisory centre accepts customer queries by phone, e-mail, or online chat. Our chatbot Fróði has been programmed to provide banking assistance and guidance to individuals – with zero waiting time. Our mortgage lending service provides assistance on mortgage lending at branches, by phone, or through the Bank's online channels.

### Mortgage lending service

Demand for mortgages has been at an all-time high, with a surge in applications for supplemental loans for first-time buyers, new mortgage loans, and refinancing. In this high-demand environment, our automated digital credit assessment came in particularly handy. The credit assessment process, which delivers an answer in just a few minutes, is fully digitised, and application numbers have risen by 70% between years. The application is fully automated: from the customer's selection of a property, through the selection of a loan package, and to the submittal of the loan application. With these changes, the Bank has greatly expanded its service to those customers who turn increasingly to self-service options – both by shortening waiting periods considerably and by improving the flow of information. In order to support customers with refinancing, the Bank set up a dedicated phone line for queries on loans and the status of applications.

### Advisory centre and chatbot

Our chatbot Fróði has been programmed to provide banking assistance and guidance to individuals. The biggest advantage with Fróði is that there is no waiting time, and he is available 24 hours a day, every day of the year. Fróði cannot execute financial transactions as yet, but he can forward the chat to an advisor if necessary. As Fróði is a new service, he may not have all of the answers at his "fingertips" right away, but he is always learning, and his answers will improve steadily over time. To date, Fróði has handled nearly 20,000 queries and resolved 90% of them. Fróði handles 49% of the chats by himself.





# Business Banking

## Market share

**42%**

greater Reykjavik area

**35%**

Iceland total

Business Banking provides small and medium-sized enterprises (SME) with comprehensive financial services. Ergo, the Bank's asset financing service, is also part of Business Banking.

Business Banking serves a growing group of Icelandic SMEs in or near their home community and has built up strong business relationships. Guided by our goal of being #1 for service, Business Banking has a team of highly experienced employees with wide-ranging expertise.

While providing personalised services, we have greatly expanded access to digital solutions. We now welcome businesses to the Íslandsbanki app, where they can carry

out their daily banking activities. Customers can also open accounts with Íslandsbanki via the Bank's website. Business Banking has repeatedly received the highest rating in service surveys among peers.

During the year, we focused on being available to our customers. We had several thousand conversations with customers and emphasised personal interactions to the extent possible during these unprecedented times.



**50% of Iceland's outstanding companies** served by Business Banking



Over **700 companies** were assisted with **COVID-19-related measures** in 2020, and around **400 support loans** were granted



The Íslandsbanki Entrepreneurship Fund granted **ISK 60.5 million to 27 innovation projects**



**30% of loans and contracts** for new cars to individuals were made through **green financing**



**44% market share** in financing of new heavy machinery purchases



**Businesses are now welcome** to the Íslandsbanki app.

## Strengthening the foundations for a resilient recovery

*"2020 was a year of challenges for the Icelandic economy. From the beginning of the COVID-19 pandemic, we were determined to support our customers and work with them on solutions, thereby preparing for a strong recovery when the economy begins to normalise. Use of relief programs have largely been concentrated in tourism and related sectors. Otherwise, new lending for general investment projects has been brisk in sectors such as retail and wholesale trade, services, and construction. There has been an*

*increase in car financing as well. We have made it a priority to offer outstanding personalised service despite the temporarily closed doors of our branches. We have been aided in this effort by our digital services, which have been advanced significantly by the COVID-19 pandemic. During the year, we made structural changes in our service to small and medium-sized enterprises (SME), including the establishment of our Business Banking Centre in Norðurturn, where Business Banking services for the capital area were*

*merged into a single location. We are convinced that this change will result in better service and enhance momentum. In line with Íslandsbanki's sustainability strategy, we took our first steps towards more sustainable banking practices by offering green financing through Ergo. We aim to broaden our selection of green products and expand the share of green projects in our loan portfolio, in keeping with our goal of being a force for good in the community."*

**Una Steinsdóttir**

Managing Director, Business Banking



## Organisational structure

### Business Banking Centres and branches

Íslandsbanki operates 12 branches, three in greater Reykjavík and nine around the country. Our branches offer self-service solutions as well as personalised advisory services, which provides expanded access and better service to our customers. We strengthened our service to corporations during the year, through our Business Banking Centres at the Bank's headquarters in Kópavogur for the capital area and in Akureyri for North and East Iceland.

### Digital solutions

We now welcome businesses to the Íslandsbanki app. All corporate online banking users can now access their daily business activities through the Íslandsbanki app, and customers can open accounts through our website. This will greatly expand our digital service to companies, and we have high hopes for

the future of these distribution channels for service to companies, guided by our customers' interests. During the year, we began cooperating with the fintech provider Payday, which offers financial solutions for small businesses.

### Ergo

Ergo, as a part of Business Banking, specialises in financing of machinery, equipment, and housing for businesses, as well as financing of motor vehicles and travel equipment for individuals. With 35 years' experience in the asset leasing market, Ergo is determined to distinguish itself from its competitors by providing good, rapid service tailored to customers' needs.



### Are you going green?

We took a major step on our sustainability path in 2020, when we introduced our green financing product. Through green financing, we are helping our customers to finance the purchase of an environment-friendly car, an electric bicycle, or a charging station at more favourable rates. Through green financing, we join with our customers to make our mark in the fight against climate change, empowering our customers to succeed by being a force for good in the community.

The high-tech company Tesla entered the Icelandic market in 2020, and Ergo was selected as Tesla Iceland's official partner. This partnership has been highly satisfactory, and we welcome the opportunity to link our Bank to a company that has stood out from the crowd by building on the concepts of sustainability and eco-friendly living.

### Business Banking Centre

During the year, services to small and medium-sized enterprises (SMEs) were merged with Íslandsbanki's Business Banking Centre in Norðurtúrn, the Bank's headquarters. At the same time, we significantly expanded the advisory services provided at the centre, with the aim of providing even better service and boosting output and efficiency. Concurrent with these changes, we also launched a Business Banking Centre for North and East Iceland.

This new structure has already proven its worth during the demanding projects we worked on with our customers during the year.

# Corporate and Investment Banking

## Market share

# 35%

Iceland's 300  
largest companies

Corporate and Investment Banking offers a full range of financial and investment banking services to large companies, pension funds, municipalities, mutual funds, investors, and affluent individuals.

The department employs experts with decades of financial experience, including securities and foreign currency trading, investment advice, corporate finance, and lending. We place strong emphasis on knowing our customers' needs, and in support of this aim, we have a dedicated staff with expertise in all key sectors of the economy. Íslandsbanki has developed a clear strategy for lending outside Iceland, which falls within the purview of Corporate and Investment Banking, with primary emphasis on the North Atlantic fishing industry.

Building on its extensive experience of complex, wide-ranging projects, our team has led many of the largest transformational endeavours in the Icelandic economy in recent years. We focus on efficient and direct communications, and we emphasise cooperation across the units in the department, so as to meet our customers' needs as well as possible.



**#1 in Corporate Finance**, with 30 projects concluded in 2020



Private Banking increased its assets under management by **ISK 3.3 billion**



**Leader in trading volume** on Nasdaq Iceland. Íslandsbanki accounted for 18.7% of total trading across all asset classes and **led the market with 19% of turnover** in listed bonds



New lending totalling **ISK 72 billion**



## Headwinds and headway

*"A demanding and eventful year is behind us – a year that saw a global pandemic make its mark on our activities and those of most of our customers. Strong and solid business relationships are never more important than during challenging times. With that in mind, we placed strong emphasis on working closely with those customers that needed solutions and flexibility in order to weather the unprecedented storm that struck during the year.*

*Corporate and Investment Banking give priority to providing outstanding service, and it was therefore gratifying to see how many projects were concluded successfully in 2020 – whether in corporate finance, in the markets, in asset management, or in lending. We also worked closely with Governmental authorities to ensure that the pandemic response measures offered by the authorities would enable Icelandic companies*

*to deal with the pandemic. We took major steps in the area of sustainability, including the Bank's first sustainable bond issue and the set-up of a Sustainable Financing Framework that lays the foundations for sustainable lending."*

**Ásmundur Tryggvason**

Director, Corporate and Investment Banking



## Organisational structure

### Corporate Banking

Manages business relationships with large companies and institutions. The department is responsible for all of the Bank's service to these customers. With expertise in fishing, construction, and tourism, it provides service to all sectors of the Icelandic economy.

### Corporate Finance

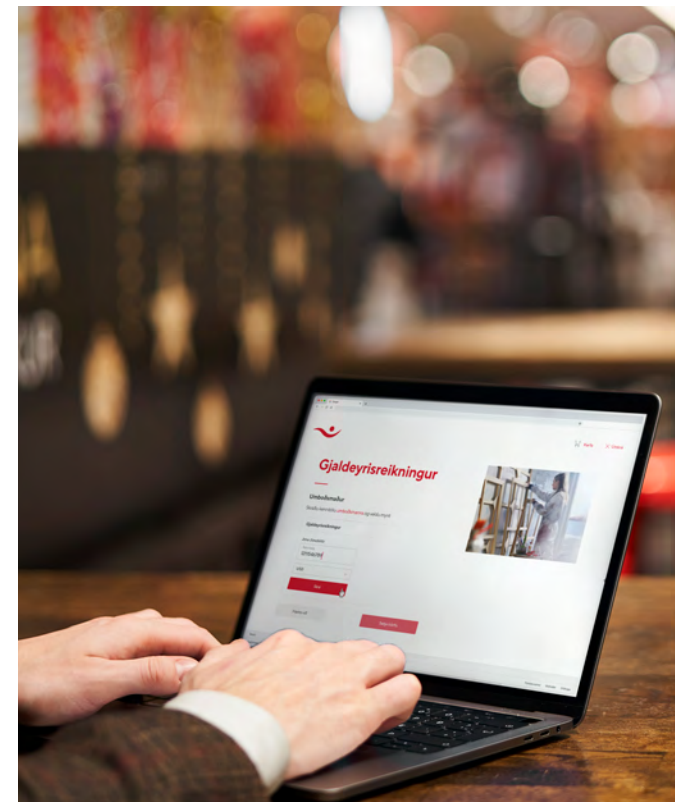
Provides investment banking advisory services to both companies and individuals, such as acquisition and disposition of company shares, mergers and other changes in ownership structure. Provides advisory services in connection with public listings including management of the share offering, preparation of the prospectus, and admission of securities to trading on the exchange. Corporate Finance also assists companies in obtaining funding, whether through banks or through the issuance and sale of bonds or equity to investors.

### Brokerage and Derivatives Desk

Brokerage includes trading in equities, bonds, currencies, and derivatives, which in turn include currency swaps, interest rate swaps, and forward contracts in stock and bond markets.

### Asset Management

Asset Management is split into two units: Private Banking and Institutional Investors. Íslandsbanki's Private Banking offers asset management and advisory services for affluent individuals, investment companies, funds, and charities. The Institutional Investors unit manages business relationships with large investors and is responsible for all of the Bank's services to these customers.



### Icelandair

Icelandair Group was not spared the impact of COVID-19 on tourism. Contractual negotiations with stakeholders began in March 2020 and concluded with a successful ISK 23 billion public share offering in September.

Íslandsbanki participated in the project, both as a lender and as an advisor during the process, as well as overseeing the offering. Many departments within the Bank worked together to deliver a highly successful project.

### Optimal capital structure

Corporate and Investment Banking offers a comprehensive range of products and works together with companies to streamline their financing, whether with bank loans, bond issuance, or a combination of the two. The bond market was lively in 2020, and among other activities, the Bank arranged an ISK 11 billion bond issuances for the real estate firm Eik and another ISK 4 billion issuance for the real estate firm Reginn. The Bank also arranged a loan to Reginn under the sustainable financing frameworks of both Reginn and Íslandsbanki.

# Iceland Funds

## Market share

# 35%

domestic funds

Iceland Funds hf., the oldest asset management company in Iceland, was founded in 1994 and is a subsidiary of Íslandsbanki.

The company manages 22 mutual and investment funds and six specialised investment funds, as well as providing service to investment companies that invest in unlisted equities and real estate. Iceland Funds has approximately ISK 350 billion in assets under management, and over 11,000 investors and depositors choose to invest their money with the company's funds.

For years, Iceland Funds has been a leading operator of bond funds in Iceland. In addition,

the company has specialised in real estate projects, including the company 105 Miðborg, which manages the development of the new neighbourhood at Kirkjusandur in Reykjavík. Iceland Funds adheres to the principles of responsible investment in all of its asset management, and in 2018 it established the only green bond fund in Iceland. Every year since 2013, Iceland Funds has been recognised for excellence in corporate governance. The recognition is now awarded by Stjórnvís.

## All of Iceland Funds' mutual and investment funds generated positive returns in 2020

Equity funds under active management by Iceland Funds outperformed the Nasdaq Iceland OMXI10 index during the year

### IS Equity Fund

Nominal return at year-end 2020

1 year	33.5%
2 years	21.9%
3 years	10.2%
4 years	6.5%
5 years	4.0%

### IS EQUUS Equity Fund

Nominal return at year-end 2020

1 year	42.4%
2 years	33.1%
3 years	18.0%
Since est.	14.9%

### IS Private Fund E

Nominal return at year-end 2020

1 year	23.0%
2 years	17.1%
3 years	12.8%
4 years	9.7%
5 years	8.5%

## Strong returns despite a challenging year

*"We accomplished a number of positive things during the year, which was an extraordinary one for many reasons. For the first time, we published an impact report for our green bond fund, which measures the impact of the fund's investments on carbon emissions. We also published Iceland Funds' ESG accounts, a report that reviews sustainability factors in the company's operations. We achieved strong returns in funds and asset*

*portfolios during the year, and owners of both stocks and bonds can be well satisfied with the return on their savings despite the worldwide wave of COVID-19-related shocks. Diversification of assets proved its worth once again, and blended asset portfolios delivered very good results overall. Our Private Fund E, for example, generated the best returns of all mixed funds in Iceland in 2020."*

**Kjartan Smári Höskuldsson**  
Director, Iceland Funds hf.



## Organisational structure

Within Iceland Funds are several business units. The company manages specialised investment vehicles as well as managing funds and asset portfolios. Also in place are strong risk management, business development, operations, and legal teams.

### Fund Management

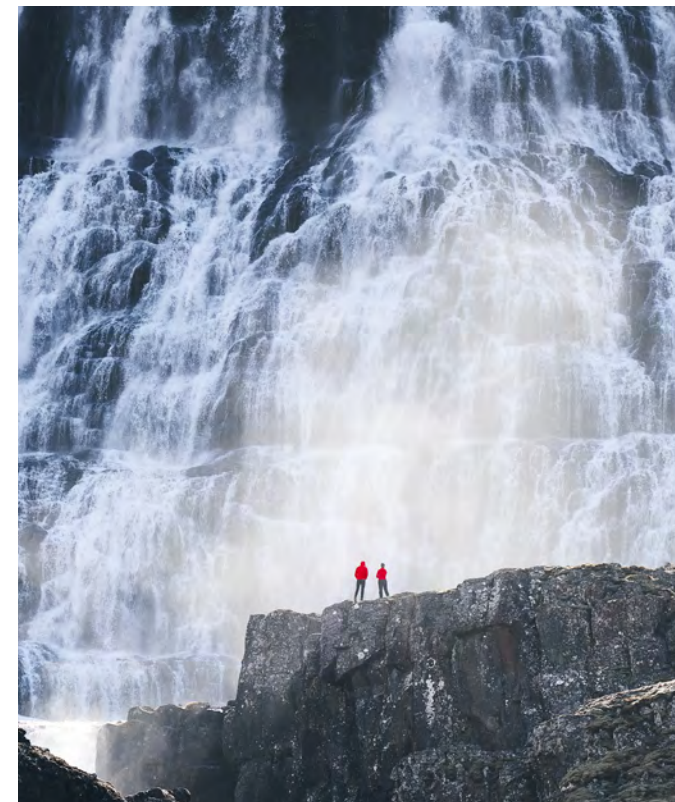
The company's fund managers oversee funds that invest in bonds, stocks, and other financial instruments. Funds are a sound and economical way for depositors to invest their money in a securities portfolio, thereby diversifying risk.

### Asset Management

Iceland Funds' strong Asset Management team manages assets for individuals, public entities, and institutional investors that have made asset management agreements with Íslandsbanki.

### Specialised Investment Vehicles

Since 2012, Iceland Funds accumulated substantial experience in real estate investments and property development, as well as venture capital investments. An experienced team of seven experts manages the company's specialised funds and investments through specialised investment vehicles. Iceland Funds also operates an institutional investment fund that specialises in commodities, as well as operating the Alpha institutional investment fund, which takes positions in the domestic stock market.



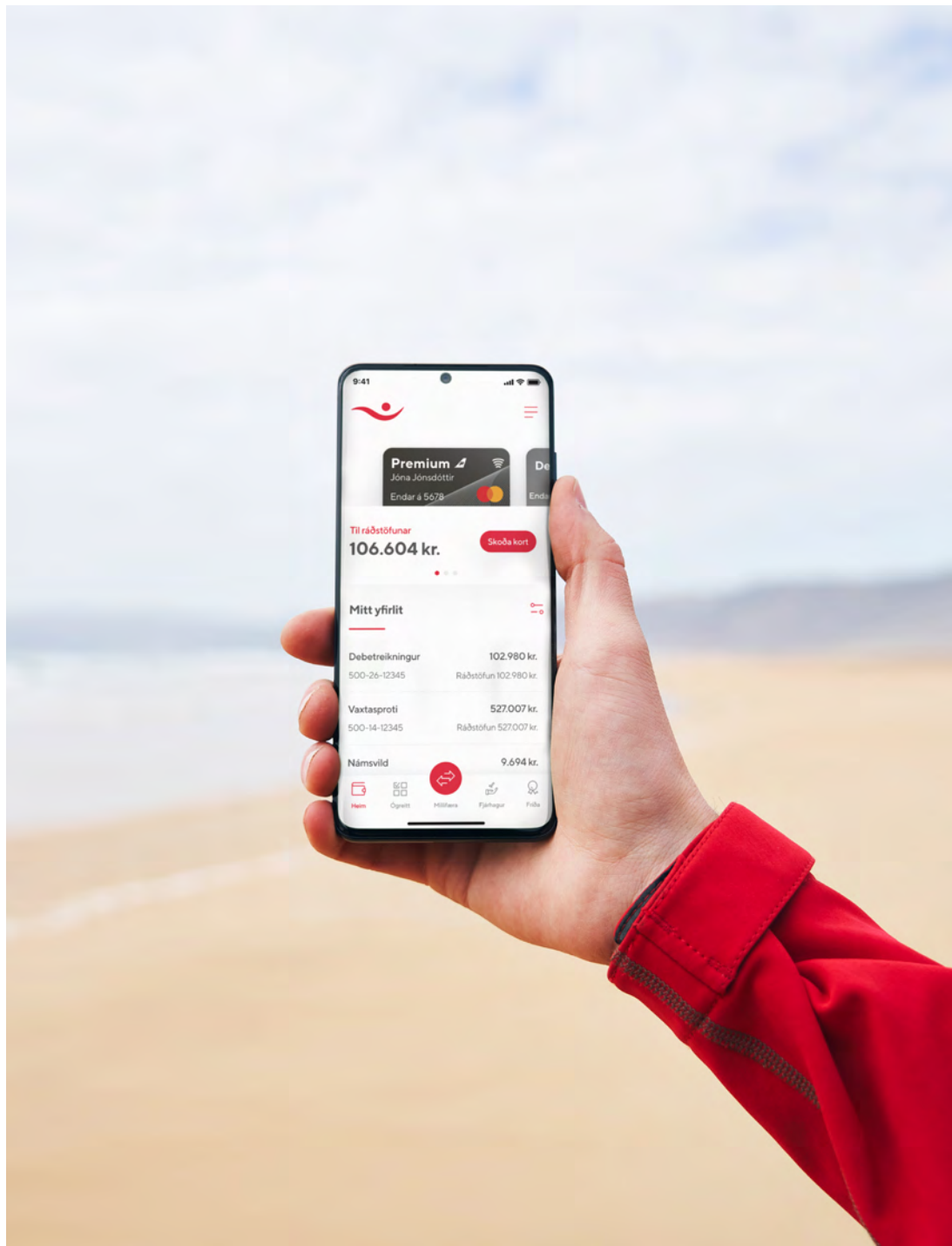
### IS Green Bond Fund

IS Green Bond Fund, Iceland's only green bond fund, is tailor-made for depositors who emphasise environmental and climate issues in their investments. The fund invests in bonds that have a positive impact on our environment and society, but without compromising on profit objectives. According to the fund's impact report, ISK 1 million invested in the IS Green Bond Fund supports projects that prevent emissions corresponding to 2.3 tonnes of CO<sub>2</sub> per year.

### IS Private Funds

IS Private Funds are investment funds that suit all depositors, as their chief objective is to deliver returns through effective diversification of assets. They achieve this by investing in a variety of asset classes in Iceland and abroad. The funds fall into five risk categories, from A to E, where the weight of equity securities increases from one category to the next, indicating the level of expected risk and returns. Investments in the funds benefit from tax concessions, as the funds do not pay investment tax when they buy and sell securities.





Annual and Sustainability Report 2020

# 5 Digitally connected banking companion IT

# Product-based development for customers

In 2020, Íslandsbanki formulated a digital strategy that functions as the guidepost for digital product development and implementation of tech innovations. The strategy is based on five main pillars where we connect with our customers and partners through digital solutions, recognised their needs, and provide them with frictionless banking services every step of the way.



I

## Service first for customers and partners

In order to put service to our customers and partners in first place, the solutions we develop are “open” and accessible to our customers whenever they need, and wherever they are. Our accessible solutions also open up the possibility of cooperating with fintech providers, giving us the opportunity to expand and improve our service offerings.

II

## Frictionless value chains

Frictionless self-serve processes are an important element in putting service first. This means automated processing from start to finish, from the moment the customer begins a process until all aspects of it are complete.

III

## Relevant data and insights when you need them

In order to automate processing at every step of the way, data are used intelligently to serve our customers. This entails harnessing valuable data to understand our customers' needs and offer custom-designed services, products, and prices.

IV

## Open and flexible products and pricing

Digitising our product offerings and pricing enables us to make modifications and introduce new products swiftly. When new products are introduced, they appear in all of the Bank's distribution channels automatically and in a harmonised way.

V







## Cost effective, optimised technical landscape

An economical and efficient system landscape underpins our digital services and is based on mobilising tech innovations to create solutions quickly, efficiently, and economically.

### A road map for product development

Our new product teams and product-driven organisational structure have evolved during the year and delivered improved cooperation between our IT and business units, which work together to formulate strategies for each product team, set priorities, and execute projects.

#### Íslandsbanki's product teams build on cooperation between the IT and business units

-  Day to day banking
-  Channels
-  Markets and Securities
-  Corporate Solutions
-  Information Management and Finance Solutions
-  Lending

The product teams have created a defined road map for their products so as to have a comprehensive overview of the Bank's digital product development.

New product teams have facilitated rapid development of digital solutions for our customers. Emphasis on product-centred development has enabled the Bank to support its customers through the COVID-19 pandemic with automated processes and self-serve channels for the solutions we offer.

We have invested in our tech infrastructure in recent years, enabling us to place even stronger emphasis on developing new solutions for our customers, building on a solid foundation. We have been working on the implementation of a loan system and an automated loan application process so as to improve the service we provide to our customers and streamline the loan application process.



### A new digital strategy creates opportunities in product development

*"Íslandsbanki's investment in digital solutions and product-centred development has prepared it well to face the challenges accompanying the COVID-19 pandemic with minimal disruption of day-to-day operations and service levels. With a coordinated effort by our IT and business units, we have been able to respond quickly and effectively to new circumstances and develop digital solutions and tactics that meet our customers' changing needs."*

*Íslandsbanki formulated a new digital strategy during the year. The new strategy puts the Bank at the forefront of open banking and creates opportunities for continuing growth and development."*

*With the experience of 2020 and a new digital strategy under our belt, Íslandsbanki is prepared for the challenges and opportunities of the future."*

**Riaan Dreyer**  
Director of IT



# Digital infrastructure for the future

In 2020, Íslandsbanki made excellent progress in developing infrastructure focused on digital product development and an open banking environment. Special emphasis was placed on the automisation of internal processes and on software quality.

**>99%**

of loan applications are digital

**74%**

of accounts are opened digitally

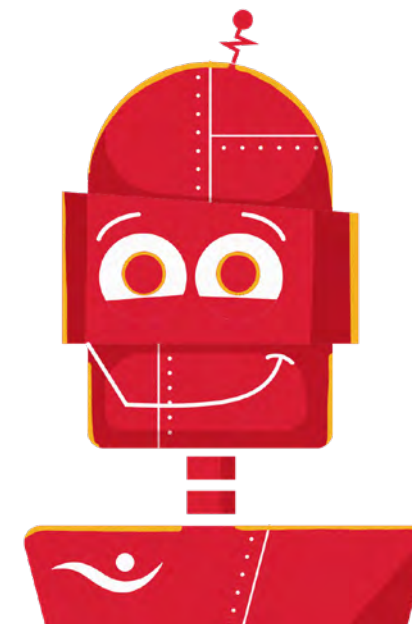
**>50%**

of software is delivered with automated processes

This work has shortened delivery times and enhanced operational security. During this unprecedented time of enormously increased customer demands for self-service, the Bank has met those needs successfully and provided better, more secure digital service. We have continued on this path and built up a tech environment where we develop infrastructure and cloud solutions using the newest technology, both in-house and in the cloud. In this way, we have prepared the Bank to participate in the competition for digital banking solutions in an open ecosystem. With smaller and more scalable units, we can continue to respond to a continuously changing external environment and provide outstanding digital service through our own solutions and those of our partners.

## Major digital advances

- The Íslandsbanki app for both Android and iOS is now available to companies.
- The new merged Íslandsbanki app has been well received, with a significant increase in use.
- Customers can now refinance their mortgages using our automated process in the online bank.
- Customers can sign up for securities trading and execute trades in the online bank.
- Íslandsbanki's responses to COVID-19 entailed digital support loans, freezing of loans, private pension savings withdrawals, and amendments of loan terms, among others.
- Digital signatures for individuals and legal entities have created opportunities for increased self-service and automation.
- Íslandsbanki's open banking strategy has been approved, the Bank has taken the first steps towards an open banking environment with a stronger authentication solution, the ability to view accounts from other financial institutions in the app and development of APIs.
- We introduced Fróði, the Bank's new customer service chatbot.
- Digital green car loans are part of the Bank's sustainable product offerings.
- The app has been in continuous development during the year, and new functions have been added. For instance, customers can now use the app to make extra payments on loans, transfer funds easily, receive notifications and service messages, and switch users without logging in.
- Íslandsbanki has partnered with Payday, as an element in its increased emphasis on fintech. The partnership opens up opportunities to offer small businesses solutions to simplify their operations.
- The Onboarding solution was rolled out for legal entities and companies. The solution entails a digital application process that allows companies to apply for products and services such as bank accounts, credit cards, corporate banking solutions, the Íslandsbanki app, and collections services.





Annual and Sustainability Report 2020

# 6 Sustainable Íslandsbanki

# Íslandsbanki as a model and a catalyst

Íslandsbanki is committed to being a model of exemplary operations and participating actively in the community where we live. By fostering sustainability in the broadest sense, the Bank makes a positive impact, which is important to us and our customers.

Íslandsbanki emphasises integrating sustainability into its operations, alongside its profit objectives. In addition to being a model of environmental, social, and governance (ESG) criteria in its operations, the Bank is committed to initiating broader collaboration on responsible business practices that contribute to sustainable development in the Icelandic economy. By doing this, the Bank is a genuine catalyst.

The Bank's sustainability objectives through 2025 were approved by the Board of Directors based on ESG criteria. The objectives support the United Nations Sustainable Development Goals (SDGs) that Íslandsbanki has decided to prioritise, as well as supporting the Paris Agreement on the reduction of greenhouse gas emissions and Iceland's Climate Action Plan. The objectives take into account the Bank's obligations in connection with its participation in Nordic CEOs for a Sustainable

Future and its compliance with the UN principles for responsible banking.

Annual secondary objectives build on the work done in Íslandsbanki's departments and units as part of the Bank's annual five-year plan. They are published in the Annual and Sustainability Report, together with an overview of the progress made towards them.



*Íslandsbanki receives knowledge award from President of Iceland for excellence in sustainable development*

## Íslandsbanki Sustainability Policy

Íslandsbanki's objective is to be a model of exemplary operations



**Environmental issues**



**Social issues**



**Governance issues**

We want to be a catalyst for positive social action beyond our own footprint by supporting customers on their sustainability journey



**Responsible lending**



**Responsible investment**



**Responsible purchasing**



**Grants and innovation**



# Sustainability milestones during the year

In 2020, Íslandsbanki achieved an important milestone by implementing an ambitious sustainability strategy.

Emphasis was placed on implementing the strategy with broad consultation and cooperation within the Bank, particularly with the business, finance, treasury, risk management, and legal departments, as well as with Iceland Funds. The strategy was also discussed in depth by the Board of Directors. Four work groups were established to oversee

the implementation of the strategy, and significant progress was made through this arrangement. Employee participation is key to achieving the Bank's sustainability objectives and creating a corporate culture that supports the process.



## Work group I

### Operations, employees, and suppliers

- Suppliers' Code of Conduct
- Remote working
- Adoption of sustainability objectives and carbon neutrality in operations
- Green leader – workshops for employees
- Helping Hand reviewed and a new sustainability calendar developed
- Implementation of a new sustainability management platform from Klappir
- Carbon-neutralisation of operations

## Work group II

### Marketing, grants, and innovation

- Stronger connections between the Entrepreneurship Fund and the UN SDGs
- Increased allocations from the Entrepreneurship Fund due to COVID-19
- Grant policy updated to align more closely with the UN SDGs
- Increased emphasis on open banking and fintech

## Work group III

### Sustainable lending and financing

- Green motor vehicle loans
- ESG risk assessment for loan portfolio Sustainable Financing Framework
- Issuance of green and sustainable bonds
- Sustainable corporate lending
- Membership of the Partnership for Carbon Accounting Financials (PCAF)

## Work group IV

### Sustainable investments

- Sustainability workshops held for financial advisors, based on responsible investment criteria
- Corporate Finance and securities brokerage departments contributed to issuance of green and sustainable bonds

# Sustainable Financing Framework

Íslandsbanki is the first bank in Iceland to define and publish a separate framework for the loans and investments in its asset portfolio that are classified as sustainable. The publication and implementation of the framework was the Bank's biggest contribution in the area of sustainability in 2020.



The framework is based on international criteria for green, social, and sustainable bonds, which are published by the International Capital Market Association (ICMA), an international association of securities market participants. The framework is based on four pillars:

1. Identification of sustainable project categories
2. Selection process for sustainable projects
3. Financial matters
4. Reporting to investors

The framework supports the UN SDGs, the Government's Climate Action Plan, and the recent statement on sustainable investments.

Examples of projects falling within the framework are: Smaller hydropower plans, geo-thermal plants, wind and solar energy projects, eco-certified products (including in the fishing industry), green buildings, electric motor vehicles, loans to schools, and loans to job creation initiatives for women and minorities.

## Eligible project categories for the Sustainable Financing Framework

Green project categories		SDGs	Iceland's 2020 Climate Action Plan
G1	Clean Transportation	9, 11, 13	A. Land transport / H. Aviation and heavy industry
G2	Eco-efficient and circular economy adapted products, production technologies and processes	12, 13	E. Agriculture / F. Waste management / H. Aviation and heavy industry
G3	Energy efficiency	7, 9, 12, 13	C. Energy production and small industry
G4	Pollution prevention and control	9, 12, 13	A. Land transport / D. F-gases and chemical use
G5	Renewable energy	7, 9, 13	C. Energy production and small industry
G6	Green buildings	9, 11, 13	C. Energy production and small industry
G7	Environmentally sustainable management of living natural resources and land use, and terrestrial biodiversity conservation	11, 15	E. Agriculture / I. Land-Use
G8	Sustainable waste management	9, 12, 13	F. Waste management
G9	Information & communications technology	9	
Blue project categories			
B1	Eco-efficient and circular economy adapted products, production technologies and processes	12, 13, 14	F. Waste management
B2	Pollution prevention and control	9, 12, 14	B. Ships and ports / D. F-gases and chemical use / F. Waste management
B3	Clean Transportation	9, 11, 13, 14	B. Ships and ports
Social project categories			
R1	Government defined company support	1, 8, 9	
R2	Affordable housing	1, 10, 11	
R3	Education and vocational training	4, 10, 11	
R4	Financial support for MSMEs	8, 9, 11	
R5	Equality, diversity and empowerment	5, 10	
R6	Affordable basic infrastructure	9, 11	

Second party opinion by

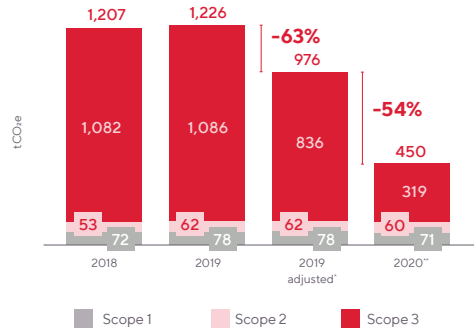




## Environmental 2020

### E1 Greenhouse Gas Emissions

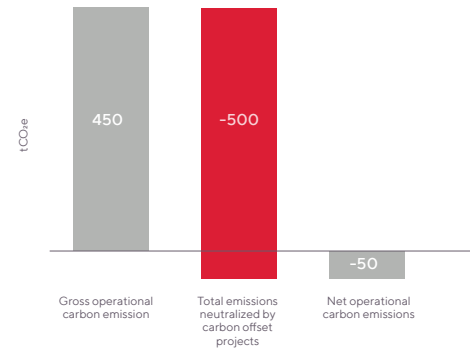
Gross operational carbon emission



\*In 2018 and 2019, CIRCULAR Solutions measured the Bank's carbon footprint. The 2020 measurement has been reviewed and certified by Klappir Green Solutions and is based on information collected by the company's EnviroMaster software over the course of the year. The methodological difference between measurements is estimated at 250 tonnes, as the 2020 measurement is based on more detailed data on indirect emissions, including those related to goods and services purchased by the Bank.

\*\*In 2020, COVID-19 had a significant impact on carbon emissions, which declined by an estimated 330 tonnes relative to 2019.

Net operational carbon emissions in 2020



The carbon footprint from our 2019-2020 operations has been offset in full (and more besides) in cooperation with the Wetland Fund and the UN Carbon Offset platform.

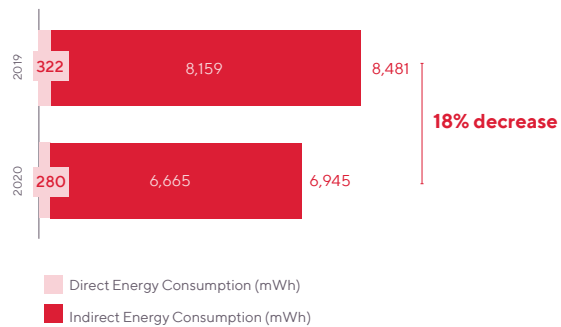


### E2 Emissions Intensity

GhG emissions per full-time equivalent (FTE) employee **0.6 tCO<sub>2</sub>e/FTEs**

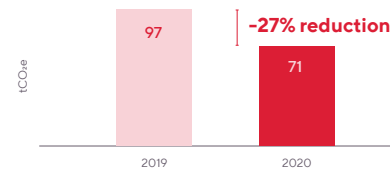
GhG emissions per unit of revenue **10.7 kgCO<sub>2</sub>e/million ISK**

### E3 Energy Usage



Direct Energy Consumption includes fossil fuel, Indirect Energy Consumption includes electricity and hot water.

Energy from fossil fuel



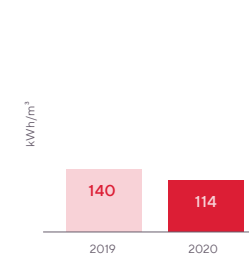
Use of fossil fuels accounts for **16% of the Bank's carbon footprint** for 2020



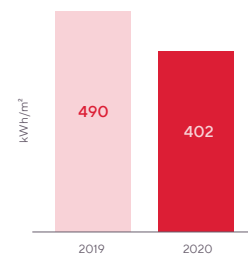
The Bank reduces fossil fuel use by investing in electric vehicles instead of petrol vehicles. In 2020, five petrol vehicles were replaced with investments in **three electric vehicles and one plug-in hybrid**

### E4 Energy Intensity

Energy per cubic meter



Energy per square meter



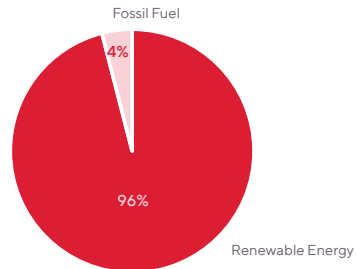




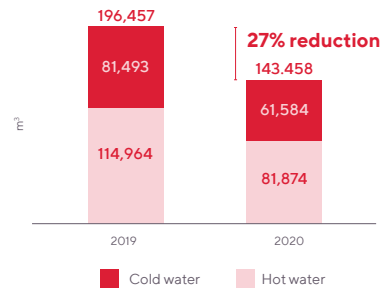
## Environmental 2020

### E5 Energy Mix

Gross operational carbon emission



### E6 Water Usage



### E7 Environmental Operations

Does your company follow a formal Environmental Policy?

See the Banks Sustainability Policy, chapter to on environmental factors.

Does your company follow specific waste, water, energy, and/or recycling policies?

In 2020, the Bank was awarded the Nordic Swan Ecolabel, which applies to 90% of its kitchen and catering services.

Does your company use a recognized energy management system?

Klappir Green Solutions and MainManager.

### E8 Climate Oversight / Board

Does your Board of Directors oversee and/or manage climate-related risk?

### E9 Climate Oversight / Management

Does your Senior Management Team oversee and/or manage climate-related risks?

### E10 Climate Risk Mitigation

Total annual investment in climate-related infrastructure, resilience, and product development **ISK 58 m.**

Investments in sustainability include electric vehicles, charging stations for electric vehicles, advisory services, carbon offset, membership fees, etc.

### Other environmental metrics

Are ESG factors considered in connection with the development of new and existing products?

Consideration is given to sustainability risk in product development.

Does the company offer employees regular education on ESG factors?

Education is offered regularly; for instance, on human-caused climate disasters and the UN Global Goals.

Has the company measured the carbon footprint from its loan and investment portfolios?

Not yet, but work on such measurements has begun.

Has the company's board of directors approved and published targets for reduction of greenhouse gas emissions?

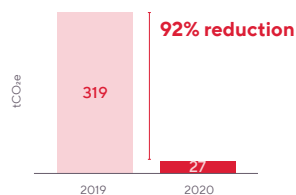
The Bank's objective is to shrink the carbon footprint from its operations by 50% between 2019 and 2024.

Does the company publish a discussion of sustainability risk and climate risk in compliance with international Task Force on Climate-related Financial Disclosures (TCFD) criteria?

The Bank's Pillar 3 Report for 2020 contains a separate chapter on sustainability risk and climate risk in compliance with TCFD criteria.

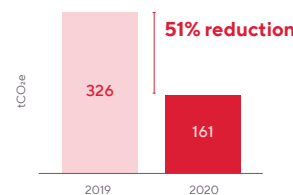
### Examples of changes in areas where the Bank has set targets for the reduction of its carbon footprint

Emissions from air transport



COVID-19 made a profound impact on the carbon footprint from air travel on behalf of the Bank, which declined by 92% year-on-year. The air travel-generated carbon footprint accounts for 6% of year-2020 emissions, down from 25% in 2019.

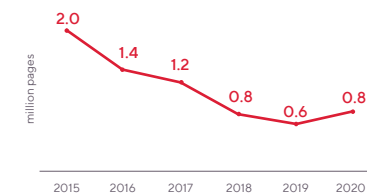
Emissions from employee commuting



The carbon footprint from employees' travel to and from work fell by half between 2019 and 2020, owing in large part to COVID-19. Some of the change can be considered permanent, however, as working from home and clean transportation have come to stay.

Annual reduction in printed paper

Both in-house printing and paper sent to customers



The carbon footprint from printing and paper use shrank by about 28 tonnes year-on-year (adjusted for methodological differences).

Six years ago, the Bank set the goal of being a paperless institution. Since then, the Bank has reduced printing by **seven million pages**, the equivalent of **eight Hallgrímskirkja churches**.

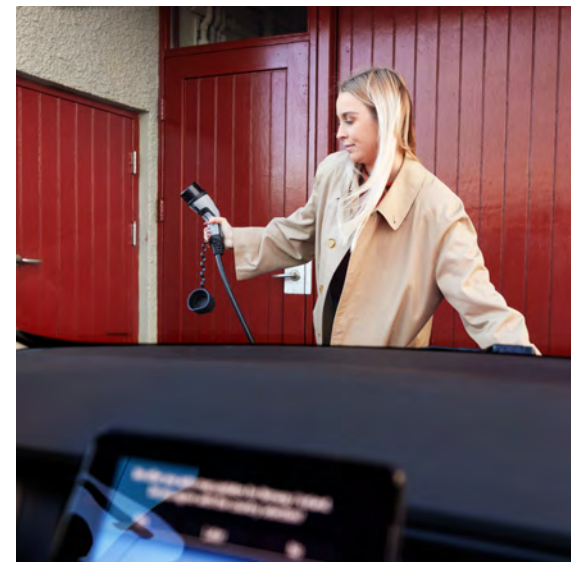




## Environmental

# Carbon neutrality in operations

Although bank operations are not an energy-intensive industry, the Bank nevertheless considers it important to set an example and adopt ambitious goals for measurement, reduction, and mitigation of carbon emissions. This way, the Bank carries its weight in terms of bringing about the mindset change that is essential in supporting climate action.



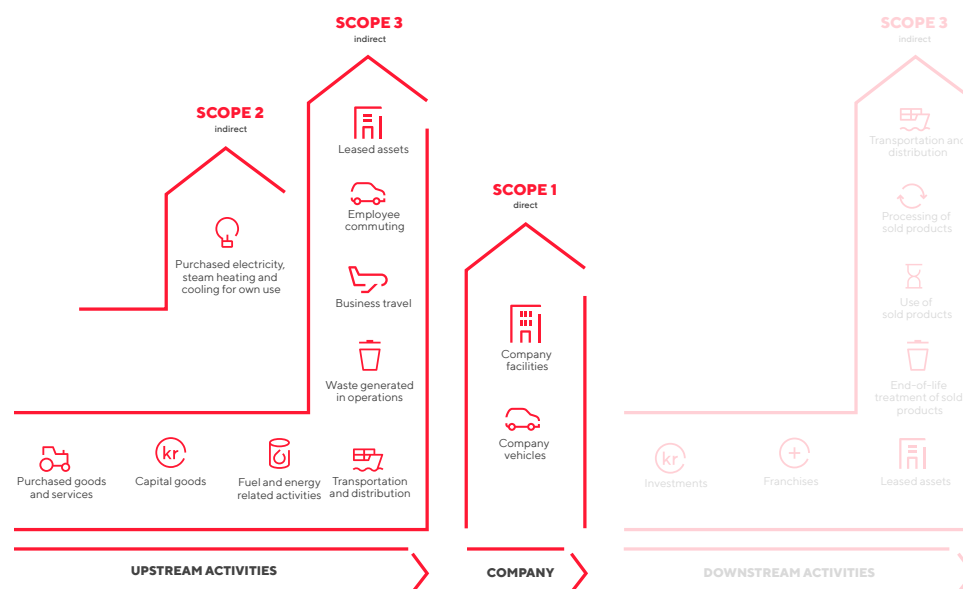
### We measure

When we calculated the Bank's carbon footprint for 2017–2019, we mapped out a large share of the greenhouse gas emissions from its operations, including direct emissions from the Bank's own operations and emissions caused by its employees, suppliers, or customers.

In 2020, the Bank implemented a new sustainability management platform from Klappir, with the aim of making more precise measurements and improving the administration of carbon accounting even further. In measuring our carbon footprint for previous years, we relied more on cost data, whereas in 2020, carbon emissions data for inputs – from production to end use – were obtained from manufacturers.

Íslandsbanki has been the only bank in Iceland to measure and include employees' travel to and from work in its carbon emissions data. A travel habit survey was conducted in December 2020 by Klappir Green Solutions.

Carbon footprint from the Bank's operations consists of direct impact (scope 1) and indirect impact (scope 2 and part of scope 3 emissions)



### We minimise

The Bank's objective is to shrink the carbon footprint from its operations by 50% between 2019 and 2024.

2020 was an extraordinary year in many ways because of the COVID-19 pandemic, and it is clear that not all of the year's contraction in carbon emissions will prove to be permanent. In 2020, the Bank achieved its goal of reducing carbon emissions by 20% relative to 2019. This is in excess of the impact of both the pandemic and the year-on-year changes in carbon footprint calculation methods.

#### Actions taken in 2020 that will deliver a permanent reduction in our carbon footprint include the following



**Fewer and more environment-friendly**  
trips to and from work



**Reduction** in air travel



**Reduction** in use of inputs



**Reduction** in paper use and printing



**Reduction** in fossil fuel purchases due to  
switch to electric vehicles

### We mitigate

The Bank intends to ensure that its operations are carbon-neutral by using mitigating measures to offset the portion that cannot be reduced.

The carbon footprint from our 2019-2020 operations has been offset in full in cooperation with the Wetland Fund and the UN Carbon Offset platform. Íslandsbanki was a founding member of the Wetland Fund in 2018 and has supported the Fund ever since. The mission of the Wetland Fund is to reclaim wetlands, thereby strengthening the ecosystem and improving land quality. The Bank has financed UN-certified projects: development work to improve cooking facilities in Malawi and the construction of a windmill in Guatemala. All of these cooperative projects prevent carbon emissions, and UN-certified projects also support social initiatives such as employment, social welfare, and education.

Íslandsbanki emphasises selecting a variety of projects for its mitigating measures. It focuses on effective certified international projects but also supports projects of importance in Iceland.







## Environmental

# The Bank's loan and asset portfolios

With responsible lending and investments, the Bank can truly be a force for good in terms of environmental issues. The first step is to understand the scope of carbon emissions in the Bank's loan and asset portfolios, give increased consideration to sustainability risk in overall lending and investment decisions, and create positive incentives to expedite investment in the transition that is needed to prevent climate change.



### We measure the carbon footprint from the Bank's loan and asset portfolios

Greenhouse gas emissions stemming from the Bank's borrowers or investors have not yet been measured. However, in autumn 2020, the Bank announced that it will participate in the Partnership for Carbon Accounting Financials (PCAF), whose goal is to create a climate metric that is custom-designed for financial institutions and enables them to measure and disclose the carbon emissions in their loan and asset portfolios.

Carbon footprint from the Bank's loan and asset portfolios is part of scope 3 emissions



Source: The Greenhouse Gas Protocol

### Measuring and managing sustainability risk

During the year, the Bank approved an updated Risk Appetite Statement that explicitly discusses sustainability risk for the first time. What is particularly interesting about this is the Board's message to employees, which states that the Bank is prepared to pass up potentially profitable business if it conflicts with the Sustainability Policy.

One of the Bank's seven sustainability objectives is to assess and disclose sustainability risks and build a robust sustainability governance framework. This focus can be seen in the Bank's unaudited Pillar 3 Report for 2020, which contains a separate chapter on sustainability and climate risk based on international Task Force on Climate-related Financial Disclosures (TCFD) recommendations.

Furthermore, extensive work is underway towards integrating sustainability risk more effectively into key Bank processes relating to lending, investments, and product development.

### We support customers on their sustainability journey

The Bank's commitment to being a force for good in the Icelandic economy extends beyond its own operations and carbon footprint. This is reflected in greater emphasis on sustainable goods and services, through which the Bank aims to support its customers in their efforts to make a difference.

It applies to sustainable loans to companies and projects that make a positive social impact. Examples of such sustainable projects include smaller hydropower plants, eco-friendly and green buildings, and eco-friendly and circular economy-adapted projects, technologies, and processes. Green financing for electric cars, electric bicycles, or other electricity-powered transport equipment, as well as charging stations, which fosters a more rapid switch to clean transportation options, is also a part of the process. Furthermore, Iceland Funds has established the IS Green Bond Fund, which invests in bonds that aim to have a positive environmental and social impact; for example, by financing projects that mitigate the impact of climate change.

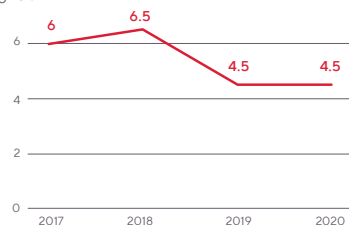




## S1 CEO Pay Ratio

Ratio: CEO total compensation to median FTE total compensation

The ratio of the CEO's pay to the median pay at Íslandsbanki in 2019 and 2020 was 4.5, which is a decrease from the 2018 when the CEO's pay was 6.5 times higher.



Does your company report this metric in regulatory filings? ☒

## S4 Gender Diversity

Percentage of women in enterprise **57%**

Percentage of women in entry- and mid-level position **59%**

Senior- and Executive-level Positions **48%**

## S7 Injury Rate

Total number of injuries and fatalities, relative to the total workforce **0**

## S10 Human Rights

Does your company publish and follow a human rights policy? ☒

The Bank's Sustainability policy states that the Bank emphasises respect for human rights and that it does not conduct business related to any human rights violations, such as discrimination based on gender, religion or race, inequality in the labour market as well as slavery and child labour.

If yes, does your human rights policy cover suppliers and vendors? ☒

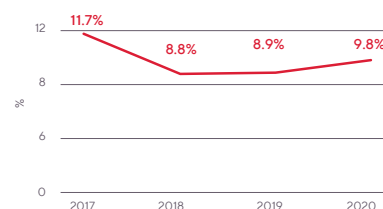
## S2 Gender Pay Ratio

Median total compensation for men to median total compensation for women **1.27**

Outcome of equal pay certification **1.1%**

According to an equal pay certification appraisal conducted in November 2020, the Bank's gender-based pay gap in comparable jobs is 1.14%, which is well below the 5% threshold set by the certification body.

## S5 Employee Turnover



## S8 Global Health & Safety

Does your Company publish and follow an occupational health and/or global health & safety policy? ☒

Íslandsbanki cares about its employees' well-being and supports their health in a number of ways, in line with its human resources policy. The policy covers factors such as the importance of an encouraging work environment.

## Other social factors selected based on sector and internal materiality assessment

Does the company have procedures for detection and Reporting of alleged misconduct that are well known by employees? ☒

Mechanisms for anonymous reporting of inappropriate conduct are available to all employees.

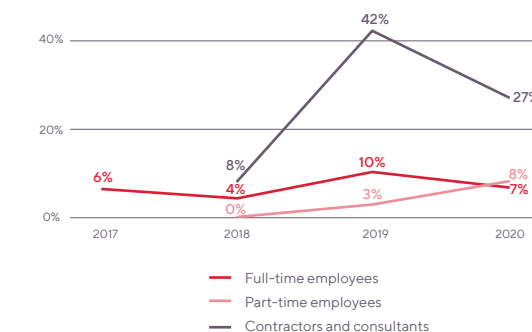
Are the company and its products accessible to marginalised groups, small companies, or communities? ☒

Various factors such as equal rights and accessibility are considered. Furthermore, the Bank stresses that its offices and branches must be accessible to marginalised groups, small companies, and communities.

Does the company offer sustainable loans that support the Government's social objectives? ☒

## S3 Employee Turnover

Year-over-year change in employees



## S6 Non-Discrimination

Does your company follow a sexual harassment and/or non-discriminatory policy? ☒

The Bank has in place a policy of sexual harassment and / or equality.

## S9 Child & Forced Labor

Does your company follow a sexual harassment and/or non-discriminatory policy? ☒

Íslandsbanki's Sustainability Policy states that the Bank will not do business with any party that is connected in any way with child labour or forced labour.

If yes, do your child and/or forced labor policy cover suppliers and vendors? ☒

The Bank refuses to conduct business with entities that violate human rights – i.e., through slavery or forced labour; child labour; discrimination on the basis of gender, religion, or race; or violation of wage agreements; cf. the Suppliers' Code of Conduct.

Are managers assigned responsibility for ethical marketing and reputational risk? ☒

Managers are responsible for ethical marketing and reputational risk, and there is targeted annual management training covering a large number of these and related factors.

Is there a plan for human resource development that includes targets for recruitment, staff development, and turnover? ☒

Has the company board of directors approved and published equal rights objectives? ☒

The Bank aims to have a gender ratio of 40% or better in its management teams.





## Social

# Financial education

The Bank's financial education initiatives were adapted to circumstances arising from the COVID-19 pandemic, with an increase in remote meetings and web-based publication of instructional materials.

Since 2015, some 30,000 guests have attended Íslandsbanki's educational meetings and lectures in person. The Bank's educational work was quickly adapted because of the pandemic, and most of it was moved online. In addition, particular emphasis was placed on household finances in connection with the pandemic, and on company finances.

During the year, 23 digital meetings were held, and 13,000 either attended or watched the videos afterwards. A number of smaller remote meetings with customers were held as well.

Examples of remote meetings include a special informational meeting on the COVID-19 pandemic and mortgage lending. About 1,700 people attended, and another 800 watched the video afterwards. Viewers submitted dozens of questions during the meeting, and Bank staff answered them during the webcast.

In addition, we composed and published 43 informative articles and 25 videos with a variety of information on finances and the economy, including a new web-based series on saving called Sparnaðarjátningar.

Based on responses to viewer surveys sent out after the meetings, there is keen interest in continued publication of such digital educational material. When the pandemic recedes and conditions normalise, we look forward to welcoming guests to our offices once again, but we intend to continue our digital education efforts.





## Social issues

# Equal rights and diversity

Íslandsbanki has been a leader in equal rights in Iceland for years and has made noticeable progress in gender equality. During the year, the Bank took systematic steps towards diversity, empowerment of other groups, and equal rights in a broader context.

### Equal rights for all

Íslandsbanki has long been a leader in gender equality, but in 2020 the Bank placed increased emphasis on equality in a broader sense than gender.

During the year, the Bank updated its Human Resources Policy to accord with the Act on Gender Autonomy,<sup>1</sup> which is designed to combat discrimination, introduce and maintain equal treatment of individuals irrespective of gender, and promote equal pay irrespective of gender. Work has begun on adapting user interfaces in the Bank's new digital service channels so as to eliminate the assumption of gender binarism.

Íslandsbanki is also a proud supporter of Hinseginleikinn, an educational forum intended to foster greater awareness of the affairs of queer people in Iceland, as well as increasing the number of queer role models

and reducing stereotyping. Lectures are held in Icelandic upper secondary schools, with support from Íslandsbanki. With this initiative, the Bank wants to do its part to promote equal rights in the community.

### Diversity and participation

Íslandsbanki's commitment to being a force for good in the community takes a variety of forms. One is its participation in Nordic CEOs for a Sustainable Future, a pan-Nordic partnership among several of the region's largest firms. Members of the organisation are companies that have been leaders in social responsibility or sustainability in their respective countries in recent years.

Íslandsbanki leads a group that focuses on equality, diversity, and inclusion, but Nordic CEOs for a Sustainable Future has adopted ambitious targets in several important



Founders of Hinseginleikans are María Rut Kristinsdóttir and Ingileif Friðriksdóttir.

categories. We intend to examine our own situation and discover what we can do to ensure that Íslandsbanki can be a bank for all – customers and employees alike.

The Bank intends to open dialogue with groups that have been underrepresented in the labour market and set ambitious goals in this area, thereby contributing to inclusion. We want Íslandsbanki to be a bank for all employees and all customers. To this end, the Bank will listen, learn, and try to do better today than it did yesterday.

<sup>1</sup> Act on Gender Autonomy no. 80/2019



## C1 Board Diversity

Total **board seats** occupied by women (as compared to men)

57%

**Committee chairs** occupied by women (as compared to men)

67%

## C4 Collective Bargaining

Share of total enterprise headcount covered by collective bargaining agreements

100%

## C7 Data Privacy

Does your company follow a Data Privacy policy?

The Bank's Data Privacy policy is comprehensive and available online. Data privacy is an important component to Íslandsbanki's operations and the Bank takes these responsibilities seriously.

Has your company taken steps to comply with GDPR rules?

## C10 External Assurance

Are your sustainability disclosures assured or validated by a third party?

Íslandsbanki's sustainability statement for 2020 was reviewed and certified by Klappir Green Solutions. The accounts are based on information collected by the company's EnviroMaster software over the course of the year.

## C2 Board Independence

Does the company prohibit CEO from serving as board chair?

According to Article 18 of the Board's Rules of Procedure, the CEO is not permitted to serve as Chairman of a Board, except with the special permission of the Board.

Total board seats occupied by independents

100%

## C5 Supplier Code of Conduct

Are your vendors or suppliers required to follow a Code of Conduct?

If yes, what percentage of your suppliers have formally certified their compliance with the code?

0%

## C8 Sustainability Reporting

Does your company publish a sustainability report?

Íslandsbanki publishes an annual sustainability report.

Is sustainability data included in your regulatory filings?

## Other governance factors selected based on sector and internal materiality assessment

Has the company examined ESG risk in connection with unlikely major occurrences?

Yes, as part of internal stress tests.

Has the company examined long-term risk in connection with ESG factors?

For further information, see the Pillar 3 Report for 2020.

Does the company enforce a competition law plan?

## C3 Incentivized Pay

Are executives formally incentivized to perform on sustainability?

According to Article 7 of the Bank's employment terms policy, the Bank does not authorise bonus payments.

## C6 Ethics & Anti-Corruption

Does your company follow an Ethics and/or Anti-Corruption policy?

Íslandsbanki has established a code of conduct for its employees and the Bank's Sustainability policy also addressed ethics and anti-corruption. The Bank furthermore has a policy against money laundering and other corruption.

If yes, what percentage of your workforce has formally certified its compliance with the policy?

99%

## C9 Disclosure Practices

Does your company provide sustainability data to sustainability reporting frameworks?

Íslandsbanki provides information on its sustainability activities to the UN Global Compact and UN Environmental Programme - Financial Initiative.

Does your company focus on specific UN Sustainable Development Goals (SDGs)?

Íslandsbanki places special emphasis on four of the UN's Sustainable Development Goals: # 4 education for all, # 5 gender equality, # 9 innovation and infrastructure, # 13 climate action.

Does your company set targets and report progress on the UN SDGs?

Íslandsbanki has published sustainability goals for 2025 with special emphasis on four of the UN SDGs.



# Sound governance

Íslandsbanki's Board of Directors has resolved to pursue exemplary corporate governance practices that are consistent with applicable regulatory provisions, internationally recognised criteria, and best practice in corporate governance.

## Guidelines on Corporate Governance

The Bank's governance practices are in line with the recognised Guidelines on Corporate Governance. Each year, Íslandsbanki conducts an assessment of whether the Guidelines have been followed and whether the Bank's practices at any given time are consistent with the Guidelines.

The Bank's corporate governance practices are described more fully in its Corporate Governance Statement.

## Excellence in corporate governance

Íslandsbanki was first recognised for excellence in corporate governance in March 2014. Since then, the Bank has been awarded the same recognition every year. Excellence in Corporate Governance recognition is now awarded by Stjórnvísir.

## Decision-making matrix

Íslandsbanki has adopted a decision-making matrix that maps out the requirements for all major decisions within the Bank. The matrix is an element in improving the decision-making process and thereby increasing stakeholders' confidence in the Bank. The decision-making matrix lays down requirements and recommends certain procedures for major decisions.



# Governance practices are continually evolving

As part of the Bank's Sustainability Policy, the Board has approved a Strategy for Sound Governance Practices, which obliges the Bank to comply with the applicable governance rules in place at any given time. As a result, the Bank's governance practices are constantly evolving.

## Íslandsbanki Sustainability Committee

Íslandsbanki established a new Sustainability Committee in November 2020. The Sustainability Committee, whose members are appointed by the Bank's Chief Executive Officer, is one of Íslandsbanki's business committees. Among other things, it is the Bank's official forum for scrutiny and discussion of issues pertaining to sustainability risk (including ESG risk), sustainable purchasing, and business opportunities.

## Competition law plan

During the year, the Board of Directors updated the competition law plan for the Bank and its subsidiaries. It is the Bank's policy to engage in active competition in the markets where it operates, and to ensure that it fulfils the obligations that follow from competition legislation at all times.

## Suppliers' Code of Conduct

In June 2020, the Bank's Executive committee approved a Code of Conduct for suppliers, based on the Bank's Sustainability Policy. The aim of the Code of Conduct is to ensure that Íslandsbanki and its suppliers can work together to be a force for good in the community. The Code applies to all of the Bank's contractual purchases exceeding ISK 50m per year, and to suppliers with an average of more than 50 annual full-time position equivalents. On the other hand, the Bank wishes to encourage all suppliers and partners to familiarise themselves with and adopt this Code of Conduct in their activities, and to disclose information to this effect in a public forum, such as in annual sustainability reporting. After issuing the Code of Conduct, the Bank met with several of its largest suppliers to review the Bank's priorities in this area.

## Policy on suitability of Board members, CEO, and key employees

Íslandsbanki's Board of Directors updated the Bank's policy on the suitability of Board members, the CEO, and key employees during the year. The aim of the policy is to ensure that the Board, the CEO, and key employees always satisfy the pertinent qualifications and requirements and that the framework for their appointment and/or employment is in compliance with the internal and external rules governing the Bank's activities.



# Support for the UN SDGs

The UN Sustainable Development Goals function as a unified whole, and Íslandsbanki supports them all. On the other hand, in order to sharpen its focus, the Bank has chosen to give particular support to four goals covering areas where it is especially well positioned to make a positive impact.

4 QUALITY EDUCATION



We produce educational videos that explain financial concepts in a simple and accessible manner.

We help young children to learn to read letters and numbers in our Georg apps, and we have an app that teaches children to tell the time.

Íslandsbanki has participated actively in the project Fjármálavít – financial education for students in junior high school. The Icelandic Financial Services Association (SFF) sponsors the project in cooperation with member companies and school teachers.

During the year, the Bank supported the Red Cross project Bridging the Digital Divide by loaning employees who helped Red Cross workers in Malawi to implement tech solutions.

5 GENDER EQUALITY



In 2020, Íslandsbanki was awarded the Equality Scale by the Icelandic Association of Business Women (FKA).

The Bank has held meetings on equal rights for five years in a row, welcoming over 2,000 guests. In September, the Bank cooperated with FKA to hold a symposium entitled Women and Finance: How do we become catalysts in the financial market?

According to an equal pay certification appraisal conducted in November 2020, the Bank's gender-based pay gap in comparable jobs is 1.14%, which is well below the 5% threshold set by the certification body.

9 INDUSTRY, INNOVATION AND INFRASTRUCTURE



In 2020, Íslandsbanki's Entrepreneurship Fund awarded over ISK 60 million in grants to 27 projects. In allocating the grants, consideration was given to projects that promote the four UN SDGs that the Bank has decided to support.

Íslandsbanki is a supporter of the Icelandic Seafood Cluster and has participated in the development of the Icelandic Geothermal Cluster.

During the year, the Bank continued collaborating with Reykjavík University (RU) on the operation of the university's Center of Financial Technology (Fintech Center), with the aim of developing technology, knowledge, and practical services for the banking systems of the future.

13 CLIMATE ACTION



In June 2020, Ergo began offering green financing at preferred rates for eco-friendly vehicle purchases.

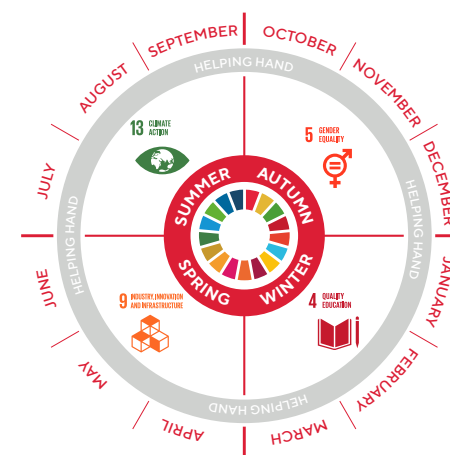
The Bank reached a milestone with the October 2020 publication of its Sustainable Financing Framework, the first of its kind in Iceland, and thereafter it obtained funding with two sustainable bond issues and began granting green and sustainable loans to corporate borrowers.

Íslandsbanki has set ambitious goals for shrinking the carbon footprint from its operations by 50% between 2019 and 2024 and enduring that its operations are carbon-neutral with mitigating measures from 2019 onwards.

Íslandsbanki's kitchen was awarded the Nordic Swan Ecolabel in December 2020, and all of the kitchen's operations are therefore Swan-certified.

# Sustainability is a journey – objectives for the road ahead





We are proud of the progress we have already made, but the challenges ahead are numerous. We must dare to talk about the things that matter even though we ourselves are not perfect. Broad participation in domestic and international cooperation is the key to making maximum progress in the area of sustainability.



The Bank's new sustainability calendar will be reflected in events, educational efforts, and opportunities to give a Helping Hand, with the aim of boosting awareness of the UN SDGs, fostering a sustainability culture, and giving all of our employees the opportunity to be a force for good.

## The seven main goals until 2025

## Secondary objectives for 2021

 <b>Environmental</b>	1. Become carbon neutral in its operations	33% decline in operations-related carbon footprint from 2019-2021 (50% reduction from 2019-2024) Complete first round of assessment of "financed emissions" based on available data in accordance with PCAF standard
	2. Offer our customers green and sustainable products	Complete the classification of the current loan portfolio based on the Sustainable Financing Framework, set target for increase Market at least three new sustainable products, including two in H1/2021
 <b>Social</b>	3. Balance gender ratios through all of the Bank's operations	Ensure that gender ratio in the Bank's management team is always 40:60 or better Action plan and quantifiable targets to increase the number of women in investment banking and IT
	4. Create a working culture that celebrates diversity and inclusion	Assess diversity using the Equileap tool in cooperation with Nordic CEOs for a Sustainable Future After measuring, prepare an action and education plan for diversity and inclusion
 <b>Corporate Governance</b>	5. Work with suppliers and partners that champion sustainability	Meet with 20 large suppliers each year and steadily increase emphasis on sustainability Formulate procedures to ensure compliance with the Suppliers' Code of Conduct and respond to incidents that arise
	6. Assess and publish sustainability risk and define internal decision-making	Sustainability risk assessment based on ESG criteria incorporated into the formal procedures for granting large loans Publish sustainability information for 2020 in accordance with TCFD criteria.
	7. Place special emphasis on four of the UN Sustainable Development Goals	Implement a sustainability calendar in support of the UN SDGs and aim for >60% participation in Helping Hand Base allocations from the Entrepreneurship Fund on UN SDGs and update the grant policy to reflect the Goals



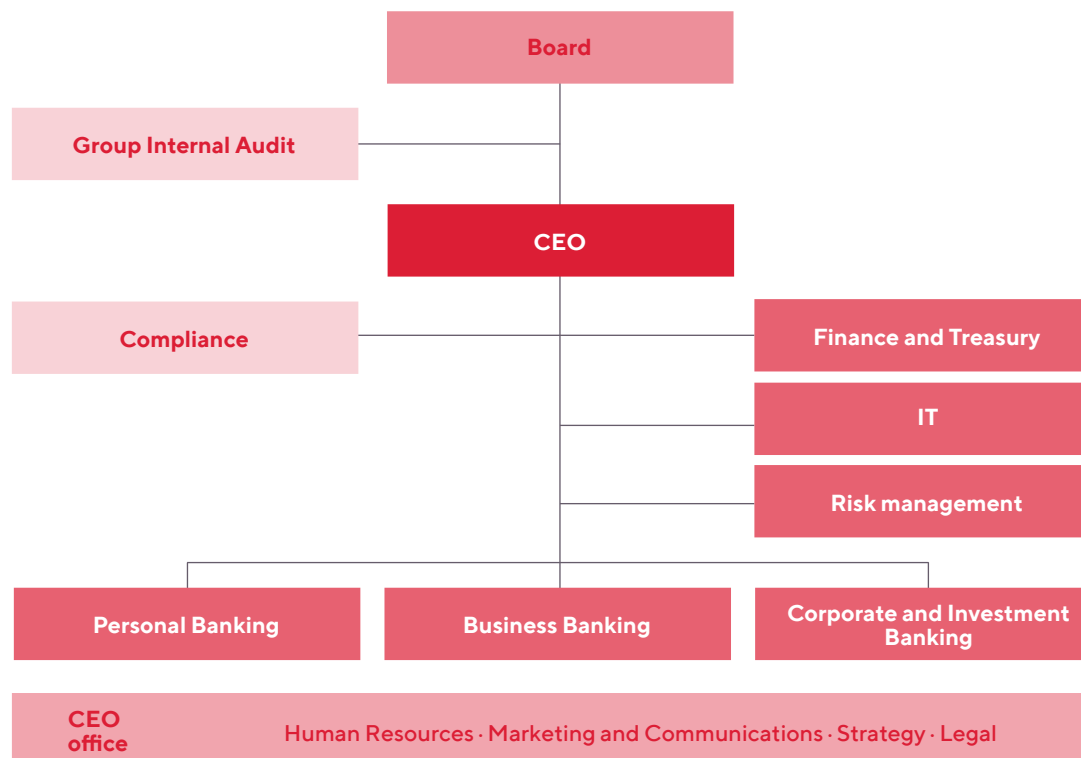


Annual and Sustainability Report 2020

# 7 Corporate and organi- sational structure

# Organisational structure

The management and ultimate control over Íslandsbanki is divided among shareholders, the Board of Directors, and the CEO, in accordance with the Bank's Articles of Association, other Board directives, and the applicable regulatory provisions.



## Íslandsbanki Articles of Association

The Articles of Association contain provisions on, among other things, the purpose of the Bank, its share capital, shareholders' meetings, election of the Board, the Board's duties, and provisions for amending the Articles of Association.

## Ownership structure

The Bank has been wholly owned by the Icelandic Government since January 2016. The State's holding in the Bank is administered by Icelandic State Financial Investments pursuant to the Act on Icelandic State Financial Investments, no. 88/2009.

**Iceland Funds**

# Board of Directors and Board subcommittees

The Board oversees the Bank's activities and ensures that they are in compliance with the applicable regulatory provisions, sound business and governance practices, and rules adopted by the Board for the Bank's activities.

## Íslandsbanki Board of Directors

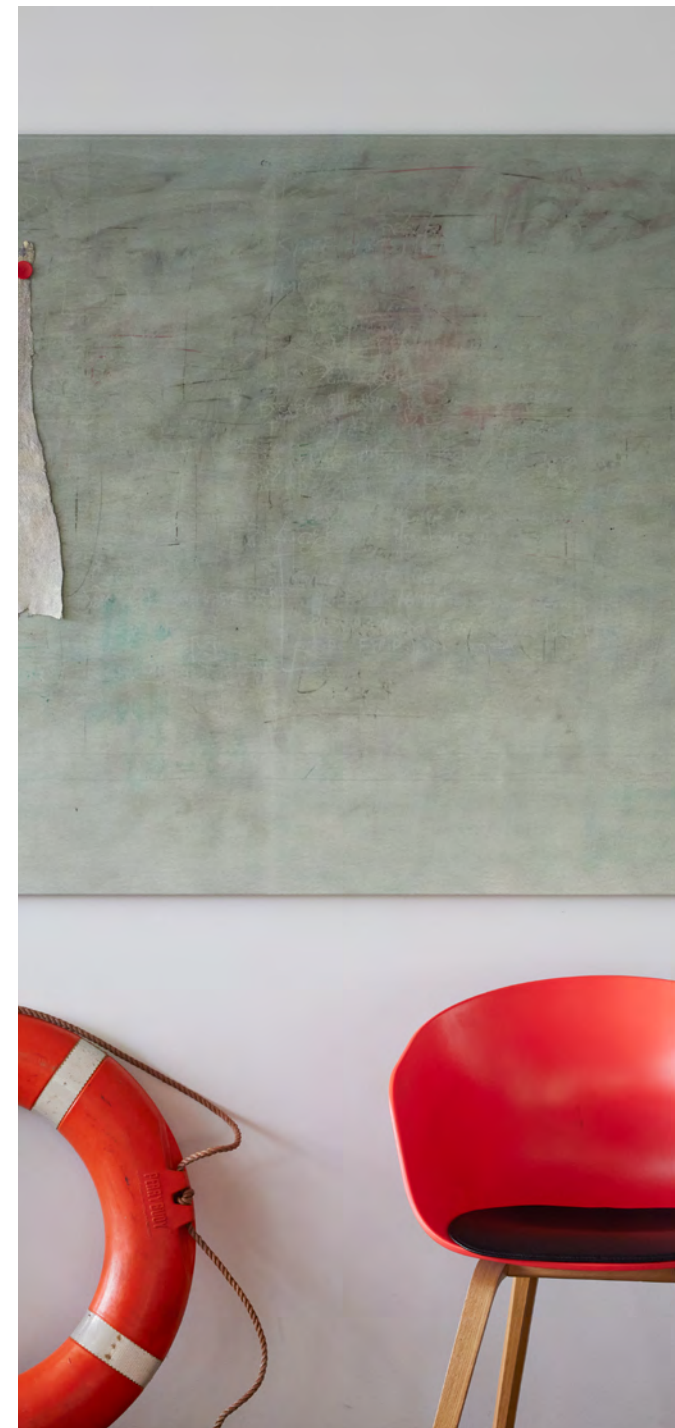
The Board of Directors comprises seven non-executive members and one alternate, who are elected at each Annual General Meeting for a term of one year. Further provisions on the functions of the Board can be found in the Board Rules of Procedure, which were updated in September 2020.

## Board subcommittees

In order to support the development, execution, and supervision of Board tasks requiring additional expertise or attention, the Board appoints subcommittees that operate according to a specific Board mandate.

There are three subcommittees, all comprising Board members.

- Board Risk Management Committee
- Board Audit Committee
- Board Corporate Governance and Human Resources Committee



# Board of Directors



**Hallgrímur Snorrason**

Chairman of the board since March 2020, joined the Board in April 2016



**Anna Þórðardóttir**

Joined the Board in April 2016



**Árni Stefánsson**

Joined the Board in April 2016



**Frosti Ólafsson**

Joined the Board in March 2020



**Guðrún Þorgeirsdóttir**

Joined the Board in March 2020



**Heiðrún Jónsdóttir**

Vice-Chairman of the board since March 2020, joined the Board in April 2016



**Herdís Gunnarsdóttir**

Joined the Board in November 2020



# CEO and CEO's advisory committees

The CEO is responsible for ensuring that the Bank's operations and activities are at all times in compliance with the Bank's Articles of Association, its approved policies and strategies, Board directives, and the applicable regulatory instruments.

The CEO hires Managing Directors for the Bank's divisions and appoints members to serve on the CEO's advisory committees. The CEO's advisory committees fall into two categories: Policy-Setting Committees, which implement Board policies, and Business Committees, which take a position on specific business matters.

The Executive Committee and the All-Risk Committee are considered policy-setting committees, and they take major decisions on the implementation of the policies set by the Board. Committee members include all of the Bank's Managing Directors, in addition to other managers appointed by the CEO.

**The Executive Committee** oversees and coordinates key aspects of the Bank's activities and has decision-making authority in matters assigned to it by the CEO, in accordance with

policies, goals, and risk appetite as defined by the Board.

**The All-Risk Committee** takes major decisions on implementation of the Bank's risk management and internal audit frameworks and conducts oversight to ensure that the Bank's risk profile is within the limits defined in the Board's risk appetite statement.

The Bank's Business Committees take decisions on individual business and operational matters in accordance with policy documents, rules, and other guidelines approved by the Board, Executive Committee, or All-Risk Committee. The Bank's Business Committees are **the Senior Credit Committee, the Asset and Liability Committee, the Investment Committee, the Operational and Security Committee, and the Sustainability Committee.**



# Executive committee



**Birna Einarsdóttir**

Chief executive officer  
since October 2008



**Ásmundur Tryggvason**

Managing director of corporate and  
investment banking since January  
2019



**Guðmundur Kristinn Birgisson**

Chief risk officer since October 2018



**Jón Guðni Ómarsson**

Chief financial officer since  
October 2011



**Sigríður Hrefna Hrafnkelsdóttir**

Managing director of personal  
banking since May 2017



**Riaan Dreyer**

Managing director of IT  
since september 2019



**Una Steinsdóttir**

Managing director of business  
banking since May 2017



Annual and Sustainability Report 2020

# 8 Economic review



# Economic review

Although the Corona Crisis inevitably dominated 2020, it also highlighted the increased resilience of the Icelandic economy and the stronger foundations on which it rests. Changed consumption patterns, economic policy responses, and a strong position at the beginning of the pandemic did much to cushion against the blow. The outlook is for GDP growth to gain momentum over the course of 2021.



## The year 2020

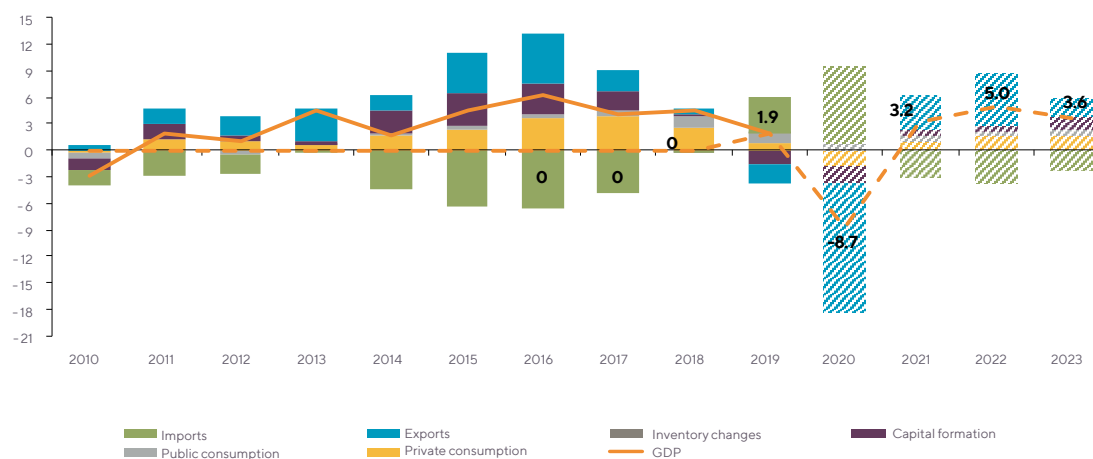
One of the longest and most fruitful economic growth episodes in Iceland's history came to an end in 2020. GDP had been based in large part on tourism, but unlike previous growth periods, the boom did not bring with it severe economic imbalances or debt accumulation by households, businesses, or the public sector.

But in a matter of weeks, the COVID-19 pandemic upended Iceland's largest export sector – tourism. Because of the pandemic and the public health measures introduced in response to it, tourist arrivals from abroad shrank by over 75% year-on-year. This was followed by a contraction in domestic demand, particularly to include investment. Mitigating measures introduced by the Government have blunted the economic impact considerably, and furthermore, the authorities in Iceland have been more successful than many of their

counterparts abroad in finding the optimum level of public health restrictions. GDP shrank by an estimated 8.7% in 2020, driven by a contraction in export revenues of nearly one-third, although private sector

demand declined as well. Pulling in the opposite direction were increased public sector activity and a marked contraction in imports.

**GDP and contribution of its subcomponents**  
Volume change from prior year (%)





### External trade in balance despite shocks

In spite of a severe blow to the tourism industry, Iceland's largest export sector, external trade was in balance in 2020, owing to a steep decline in imports and a sizeable surplus on the income account. Such a sustained external balance is something of a novelty for Iceland.

Investment sagged in 2020, contracting by an estimated 10%. The main driver of the downturn was a marked contraction in business investment, although residential and public investment declined as well. The housing market proved resilient during the year, fuelled by steady demand. House prices rose by an average of nearly 8% nationwide. Private consumption softened somewhat, but the downturn was concentrated entirely in spending abroad and a few isolated domestic

services hit especially hard by the pandemic.

The shift of consumption into the domestic economy played a role in mitigating the impact of the contraction in tourism on the current account balance.

The collapse of tourist arrivals severely affected the labour market in 2020, and registered unemployment surged from 4.8% at the beginning of the year to 10.7% by the year-end. The Government's mitigating measures prevented the jobless rate from rising even more, and at the end of the year, 1.4% of the labour force were participating in the part-time unemployment benefits programme. Even so, the year saw handsome wage growth, with real wages rising 3.5% despite a substantially increased slack in the labour market.

### Rising inflation due mainly to ISK depreciation

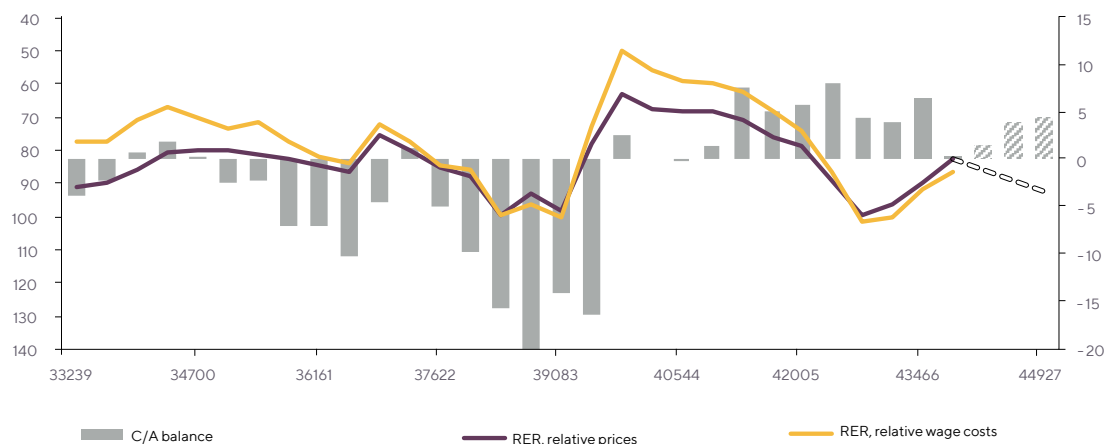
The exchange rate of the Icelandic króna (ISK) fell by nearly 10% in trade-weighted terms over the course of the year. The depreciation was due primarily to the steep decline in export revenues, although exportation of capital by foreign investors also caused the exchange rate to dip temporarily. The Central Bank (CBI) used its international reserves to smooth out short-term exchange rate volatility, particularly in H2/2020, selling approximately one-eighth of the reserves in a bid to stabilise the market. The CBI's reserves are still sizeable by all measures, however.

Inflation jumped from 1.7% to 3.6% over the course of the year, driven mainly by the rise in import prices following the depreciation of the ISK, although domestic wage inflation and a buoyant housing market played a role as well. The CBI lowered the policy interest rate from 3.0% at the beginning of the year to 0.75% by the year-end. As a result, short-term real rates plunged, as the response to the economic contraction was given top priority in the CBI's monetary policy conduct. Long-term inflation expectations have been stable, however, reflecting the increased credibility of monetary policy and giving the CBI greater flexibility to apply countercyclical measures.

### GDP growth likely to pick up in H2/2021

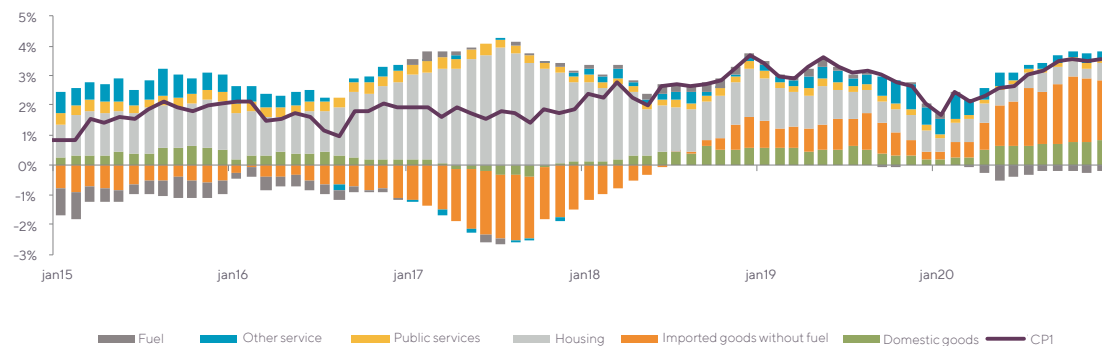
GDP growth is expected to be relatively robust in 2021, at 3.2%, with most of the growth concentrated in H2, as the COVID

Real exchange rate and current account balance  
Index and share of GDP



Shaded columns and broken lines: Íslandsbanki Research forecast / Source: Central Bank of Iceland

Inflation, by source (%)



Source: Statistics Iceland

endgame and the recovery of tourism will be the major determinants of overall economic developments during the year. GDP growth will stem largely from export growth, plus moderate growth in consumption and investment. Prospects for tourism are highly uncertain, however, and GDP growth could easily range anywhere between 1% and 5%, depending on how tourist arrivals develop.

The sizeable contribution of public investment to investment growth in 2021 is due to the Government's investment initiative. In addition, the outlook is for business investment to gain steam in H2 and grow steadily over the period. On the other hand, residential investment is expected to contract, and a reduced supply of new properties coupled with constant demand will probably push prices higher during the year.

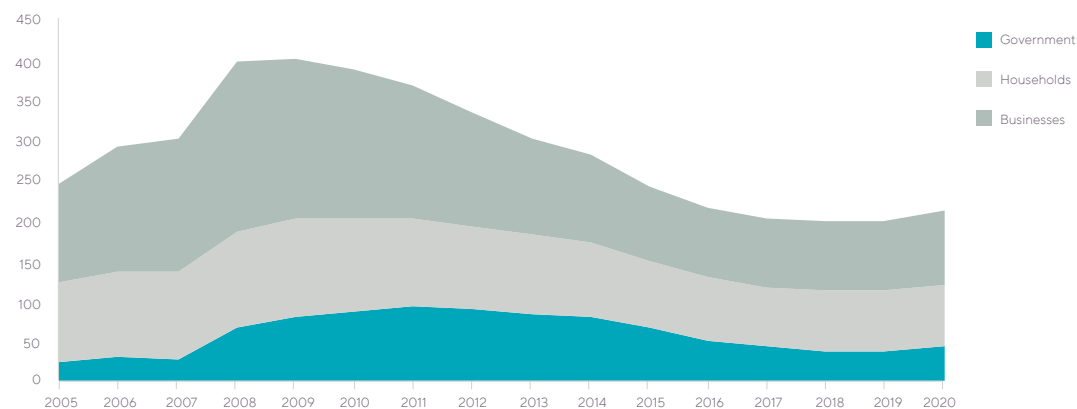
Unemployment will probably be high until mid-year, but with a rebound in tourism, increased construction activity, and growing demand

for domestic goods and services, the labour market situation should improve markedly in H2. A recuperating labour market and, for many individuals, rising purchasing power will support private consumption growth over time.

To a large extent, developments in the ISK will reflect developments in tourism-generated foreign exchange revenues. The ISK will probably be somewhat on the defensive early in 2021, but there is a growing likelihood that it

will appreciate as the year progresses. The ISK is one of the main drivers of developments in inflation, which will probably be a mirror image of last year's pattern. In the first months of the year, inflation will be around 4.0%, the upper deviation threshold of the CBI's inflation target, but then it will taper off quickly, probably aligning with the target by the year-end. Furthermore, the outlook is for a very low policy rate throughout 2021, and for long-term rates to be close to the lowest ever seen in Iceland.

If the pandemic subsides before next winter, there is a strong probability that 2021 will see the end of the Corona Crisis and the beginning of a new growth phase. Such an outcome is fostered by the strength of private and public sector balance sheets (in historical and international context) at the onset of the pandemic, as well as Iceland's successful economic policy response after the disease started to spread.

Household, corporate, and public debt  
% of GDP



Annual and Sustainability Report 2020

## 9 Financials and funding

# Financials and funding

Íslandsbanki's operations were successful in 2020, even though they were unconventional because of external conditions. We made good progress on the expenses side, and our deposit and loan portfolios expanded. Net interest income increased year-on-year, as the growth of the loan portfolio offset the impact of lower interest rates. Uncertainty relating to COVID-19 could be seen in negative impairments and an increase in forbearance, but even so, there has not been an increase in non-performing loans.

## Income statement

### Total operating income increased in the quarter

Net interest income remained stable in the fourth quarter but increased by 1.7% between years, as the balance sheet growth was somewhat offset by a lower interest rate environment, resulting in a slight fall of 0.1% in the net interest margin. A higher deposit margin compensated for a drop in lending margin both during the quarter and for the year as a whole.

Net fee and commission income remained stable during the quarter. A slight drop between years was mainly due to reduced payment card and currency exchange activity in the wake of COVID-19. Fees from loans and guarantees increased considerably between years.

In 4Q20 the Bank recorded a gain of ISK 783m in financial income. However, the Bank recorded a loss of ISK 1,391m for the full year 2020, compared to a loss of ISK 820m in 2019. This is attributable to losses in the trading book and the banking book, CPI hedges and fair value changes in shares.

### Cost / income ratio below the Bank's target of 55%

Administrative expenses dropped by 5.8% during the quarter and 7.1% for the year. The fall is mainly explained by lower salaries and related expenses and an overall reduction in the Bank's cost base, partly due to COVID-19.

The number of FTEs at the end of the period excluding seasonal employees was 745 (749 at YE19) for the parent company and 779 for



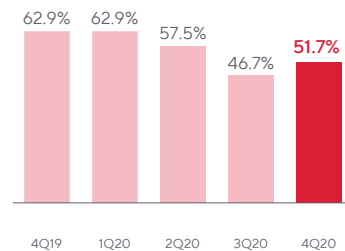
## Successful funding activities in uncertain times

*„Íslandsbanki's annualised after-tax return on equity was 3.7% in 2020. This is below our long-term target, but the return in H2/2021 showed strong resilience in the wake of the substantial uncertainty early in the year. Despite significant volatility in the financial markets, Íslandsbanki's funding activities were successful in 2020. Deposits grew apace, and the Bank had ready access to domestic and foreign bond markets. In large part, this is thanks to the strength of the Icelandic economy and the confidence that Íslandsbanki has built up among investors in recent years. During the year, Íslandsbanki became the first Icelandic bank to issue a sustainable financial framework, and soon afterwards it became the first bank in Iceland to issue green and sustainable bonds.“*

**Jón Guðni Ómarsson**  
Chief financial officer



Cost / income ratio



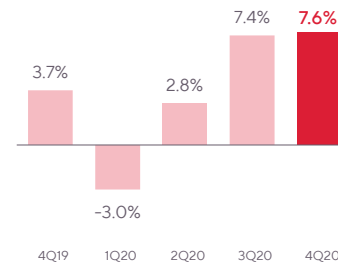
the Group (783 at YE19, not including FTEs from a subsidiary previously held for sale for comparability).

The cost-to-income (C/I) ratio for the Group was 51.7% in 4Q20 compared to 62.9% in 4Q19, therefore on target, which is a C/I ratio below 55%. For 2020 the C/I ratio was 54.3% compared to 58.8% in 2019. The C/I ratio excludes the bank tax and other one-off items.

#### Lower bank tax contributes to lower expenses

Income tax for the period amounted to ISK 2.5bn, compared to ISK 3.9bn in 2019. The effective tax rate for the period was 26.5%, compared to 30.7% in 2019. The bank tax accounted for ISK 1.6bn compared to ISK 3.5bn in 2019. The Bank is subject to the special financial tax of 6% on taxable profits in excess of ISK 1bn. The Bank pays 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

Return on equity



Depositors' and Investors' Guarantee Fund, was ISK 679m, an ISK 257m reduction from the previous year. Total taxes and levies amounted to ISK 6.6bn for the period compared to ISK 10.3bn in 2019.

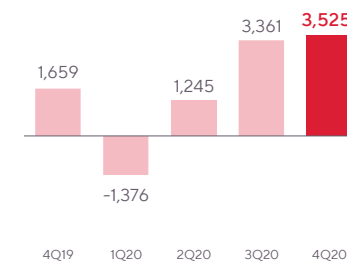
#### Impairment charges continue and uncertainty in operating environment still in place

The ISK 1,829m impairment charge in 4Q20 is mostly COVID-19 related and due to update to macroeconomic scenarios and other assumptions.

Loan impairment charges and net valuation changes generated a loss of ISK 8,816m in 2020, compared to a loss of ISK 3,480m in 2019. Thereof, ISK 6.1bn is COVID-19 related, ISK 1.2bn is related to a handful of customers and ISK 0.6bn linked to an update in macroeconomic scenarios and weights.

The net impairment charge over loans to customers was 0.18% in 4Q20 (0.73% annualised) and 0.91% in FY20.

Profit (loss) after tax (ISKm)



The economic scenarios used to calculate the impairment were updated in 4Q20, although it must be noted that determining the appropriate scenarios in the current environment is challenging. The main assumptions in the base scenario are that GDP will be -8.6% in 2020 and 3.1% in 2021. Additionally, the weights of the scenarios have been adjusted to reflect the outlook, the weights are now at 15%-55%-30% (good, base, bad) compared to 25%-50%-25% before the pandemic.

#### Underlying operations deliver stable operating income

Íslandsbanki reported a profit of ISK 3.5bn in 4Q20 (4Q19: ISK 1.7bn), generating a 7.6% annualised return on equity after tax (4Q19: 3.7%).

Profit after tax was ISK 6.8bn in 2020 (2019: ISK 8.5bn) and annualised return on equity after tax was 3.7% in 2020 (2019: 4.8%). The ISK 1.7bn lower profit between years is mainly explained by an increase in loan impairment charges and net financial loss. Contributing to higher profit in 2019 is a one-off item included in other operating income in 2019.

## Balance sheet

### Solid growth in loans to customers

The growth of the Bank's asset side by 12.1% is mainly attributable to loans to customers and bonds and debt instruments and depreciation of the Icelandic króna. The loan growth is a result of strong demand for residential mortgages (increase of ISK 60.3bn in 4Q20 and ISK 95.7bn from YE19). The rise in demand for mortgages was largely driven by the lower interest rate environment. Outstanding loans to the tourism industry in Iceland at year-end were 9% of the loan portfolio.

Loans are generally well covered by stable collateral, the majority of which is in residential and commercial real estate while the second most important collateral type is fishing vessels. The weighted average loan-to-value (LTV) ratio for the residential mortgage portfolio was 64% at the end of 2020 compared to 62% at YE19. Following a sharp rise in recent years, the Central Bank's CRE price index has fallen

in 2020. Íslandsbanki's registered value of commercial real estate as collateral has risen at a much slower rate and lagged market prices in prior years. The Bank's CRE loan portfolio is therefore less vulnerable to market price changes.

Three items, cash and balances with the Central Bank, loans to credit institutions and bonds and debt instruments, amounted to about ISK 297bn, of which ISK 285bn are liquid assets. 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.

### General moratoria taper off

Íslandsbanki entered into an agreement with other lenders in Iceland to provide a moratorium for corporate and household customers, uniformly executed across institutions. At its peak, around 1,500

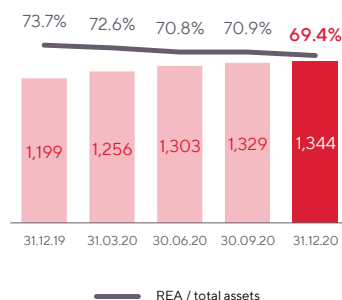
households and 650 companies benefitted from measure with loans amounting to around ISK 200bn.

The agreement expired on 30 September 2020 and the maximum length of the moratoria was through 2020. Further extensions of moratoria may be granted on a case-by-case basis, but such extensions will be classified as forbearance.

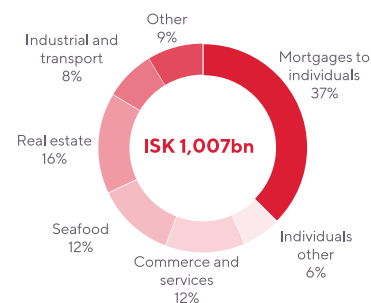
At year-end, 11.1% of the gross performing loan book (not in stage 3) was thus classified as forbearance, up from only 2.9% at end of Q3.

Support loans with government guarantees amounting to ISK 3.7bn were originated in 2H2020. Around 60% of the amount is with full government guarantee. These loans are part of the support measures that the Government has put in place following COVID-19 and Íslandsbanki facilitates the process.

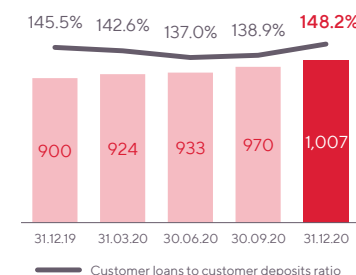
Total assets  
(ISKbn)



Loans to customers  
(Sector split as of 31.12.20)



Loans to customers  
(ISKbn)



### Quality of loan portfolio high but uncertainty of COVID-19 pandemic impact prevails

At the end of the reporting period, the share of credit-impaired loans to customers was 2.9% (gross) for the Group (2019: 3.0%). In January 2021 one material exposure was fully repaid as expected, bringing the ratio down to 2.7%. The collateral coverage in Stage 3 was 70% at the end of the year 2020 and the reserve coverage ratio was 25.3%.

### Growth in customer deposits YoY

Deposits from customers fell by 2.7% in the quarter but grew 9.9% from YE19. The ratio of customer loans to customer deposits rose to 148.2% at the end of the year. Deposits from retail and corporations are the Bank's main source of funding, comprising 42% of the Bank's total funding sources and 78% of the Bank's total deposit base at year end. Stable deposits are increasing from YE19, up 12% from retail customers and corporations and up 7% from financial institutions and pension funds. All deposit concentration levels are monitored closely, with concentration falling slightly during the year.

Other liabilities decreased between years due to less volume of unsettled transactions at the end of the period.

Debt issued and borrowed funds increased during the year as the Bank continued to build on its main long-term funding sources by issuing covered bonds and senior unsecured bonds.

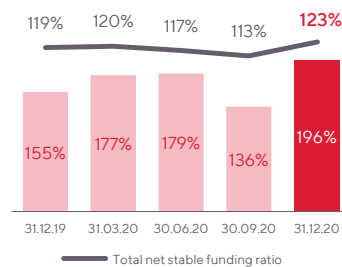
The Bank held seven covered bond auctions during 2020, issuing a total of ISK 26bn by tapping three outstanding bonds as well as issuing a new bond ISLA CB 27. Issuance in the fourth quarter amounted to ISK 18bn, net of maturities. The issuance of covered bonds is to fund the Bank's mortgage portfolio and furthermore to diversify and optimise the Bank's funding base.

In November, the Bank issued its first bonds in a sustainable format and the first sustainable bond by an Icelandic bank. Having just signed its Sustainable Financing Framework, the Bank approached investors with a 3-year, EUR 300 million benchmark bond through lead managers ABN Amro, Barclays, Goldman Sachs and UBS. Demand for the transaction proved to be very strong with the order book nearly reaching a 4x oversubscription. The resulting issue was priced at mid-swaps +100 basis points and placed with investors across Europe. This transaction was swiftly followed by a green bond, this time an ISK 2.7bn 5-year senior issue in the local market which was the first green bond issued by an Icelandic bank. The proceeds will be allocated to green, blue (sustainable fisheries) and red (social projects) over the course of the year ahead.

Due to successful capital market transactions and growing deposit base the Bank's liquidity ratios strengthened during the year. The Group's total liquidity coverage ratio (LCR) was 196% (194% for the parent) increasing from 155% at YE19. After the sale of the subsidiary



Total liquidity coverage ratio



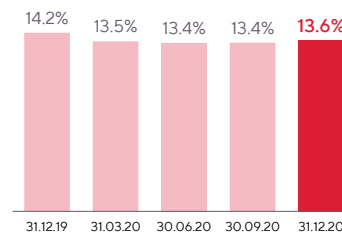
Borgun hf. in July 2020 the difference between Parent and Group LCR is negligible. The LCR in foreign currencies increased to 463% at end of 2020 from 325% at YE19 and LCR in ISK was 95% at year-end compared to 110% at YE19.

The Central Bank's reduction of the reserve requirement in 1Q20 resulted in increased liquidity. No unexpected increase was in the use of overdrafts and revolvers during the period.

The total net stable funding ratio (NSFR) was 123% at period end compared with 119% at YE19 and the NSFR in foreign currencies was 179% compared with 156% at YE19.

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.

Leverage ratio



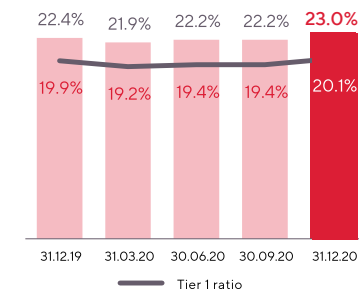
### Capital ratios strengthened during the year and are well above regulatory requirements

Total equity amounted to ISK 186bn at the end of 2020, compared to ISK 180bn at YE19. Thereof, ISK 1.5bn is attributable to non-controlling interests.

The Financial Supervision Committee announced in September 2020 that the results of the 2019 SREP assessment concerning additional capital requirements (Pillar 2-R) shall remain unchanged at 17% of REA.

In March 2020 the Central Bank of Iceland lowered the countercyclical capital buffer from 2.0% to 0% due to the economic uncertainty caused by the COVID-19 pandemic. This lowered the Bank's overall capital requirement from 19.0% to 17.0%. The Bank's capital ratio target, which is currently the Bank's regulatory total capital requirement in addition to the Bank's management buffer of 0.5–2.0%, lowered in line with the removal of the countercyclical capital buffer to 17.5–19.0%.

Total capital ratio



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 the year, the Bank's total capital ratio was 23.0% compared to 22.4% at YE19. That is considerably higher than the Bank's total capital ratio target. The Bank's Tier 1 ratio was 20.1% at the end of December compared to 19.9% at YE19. Implementation of IFRS 9 transitional rules in Iceland, where IFRS 9 impairment is partially included as CET1, increase the CET1 capital by ISK 5.0bn. The depreciation of the ISK increased the value of the Tier 2 subordinated bonds, increasing the capital base even further.

Íslandsbanki uses the standardised method to calculate its risk exposure amount (REA), which amounted to ISK 934bn at the end of December 2020 compared to ISK 885bn at year-end 2019. REA amounts to 69% of total



assets at year-end 2020 compared to 74% 2019. The large increase in mortgage lending lowered the ratio of REA total assets along with the SME supporting factor that was implemented in Iceland on 1 January 2020, resulting in an ISK 14bn deduction in the risk exposure amount at the end of December 2020. REA in total increased due to growth in loans to customers.

The leverage ratio was 13.6% at the end of year compared to 14.2% at YE19, indicating low leverage.

The Board of Directors proposes that ISK 3.4 billion will be paid in dividends to shareholders, which is 50% of profits in 2020 and is in line with the Bank's policy of paying dividends of 40–50% of the profit of the year. The Board may convene a special shareholders' meeting later in the year to propose payment of additional dividends if the Bank's accumulated capital reserves are considered to exceed its long-term capital requirements

### Strictly monitored imbalances

The Bank is exposed to inflation risk because CPI-linked assets exceed CPI-linked liabilities. At the end of December 2020, the Bank's consolidated net inflation (CPI) imbalance amounted to ISK 26.2bn, compared to ISK 20.7bn at YE19. 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 5.1bn (2.4% of the total capital base) at the end of 2020, compared to ISK -93m (0.05% of the total capital base) at year-end 2019. The Bank's imbalances are strictly monitored and are within regulatory limits.

### Credit rating

Íslandsbanki is rated by S&P Global Ratings (S&P). In late April 2020 S&P lowered Íslandsbanki's rating to BBB-/A-2 with a stable outlook from previous BBB+/A-2 with a negative outlook.

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

pension funds in mortgage lending and thus contributing to the declining profitability of Icelandic banks.

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



