



First Half 2019 Results

Íslandsbanki hf.

First half 2019 (1H19) financial highlights

- Profit after tax amounted to ISK 4.7bn (1H18: ISK 7.1bn) generating a 5.4% annualised return on equity (1H18: 8.2%).
- Earnings from regular operations were ISK 5.7bn (1H18: ISK 6.8bn) with 7.2% annualised return on equity from regular operations normalised for 16% CET1 (1H18: 9.4%).
- Net interest income was ISK 16.8bn (1H18: ISK 15.3bn), an increase of 9.4% between years and the net interest margin was 2.8% (1H18: 2.8%).
- Net fee and commission income was ISK 6.6bn (1H18: ISK 5.8bn), up by 14% from the same time last year.
- Net impairment on financial assets generated a loss of ISK 1,848m in 1H19, compared to ISK 1,934 gain in 1H18.
- Administrative costs grew by approximately 4.7% between years and totalled ISK 14.4bn (1H18: ISK 13.7bn).
- The cost to income ratio for the Group by end-June was 62.0% compared to 67.3% for the same period in 2018, while the same ratio for the parent company was 55.4% and in line with the Bank's 55% long term target.
- Loans to customers grew by 5.7% (ISK 47.8bn) to a total of ISK 894bn at the end of June. Total new lending during the first half of 2019 amounted to ISK 107.4bn, split across business segments.
- Deposits from customers grew by 6.4% (ISK 36.9bn) to ISK 616bn at the end of June.
- The Bank's liquidity position is strong in both the Icelandic króna and foreign currencies and exceeds all internal and external requirements. Capital ratios are high and in line with the long term targets.

Second quarter 2019 financial highlights

- Profit after tax was ISK 2.1bn (2Q18: 5.0bn), generating a 4.9% annualised return on equity (2Q18: 11.6%).
- Earnings from regular operations were ISK 3.0bn (2Q18: 3.9bn) and annualised return on equity for regular operations normalised for 16% CET1 was 7.8% (2Q18: 11.1%).
- Net interest income amounted to ISK 8.6bn (2Q18: ISK 7.6bn) with 2.8% net interest margin (2Q18: 2.8%).
- Net fee and commission income was ISK 3.4bn (2Q18: ISK 3.0bn).

Key figures and ratios

		1H19	1H18	2Q19	2Q18	2018
PROFITABILITY	ROE 16% CET1 (regular operations) ¹	7.2%	9.4%	7.8%	11.1%	8.0%
	ROE (after tax)	5.4%	8.2%	4.9%	11.6%	6.1%
	Net interest margin (of total assets)	2.8%	2.8%	2.8%	2.8%	2.9%
	Cost to income ratio ²	62.0%	67.3%	61.4%	65.0%	66.3%
	After tax profit, ISK m	4,709	7,130	2,120	5,033	10,645
	Earnings from regular operations, ISK m ³	5,707	6,843	3,054	3,881	12,042
		30.06.2019	31.03.2019	31.12.2018	31.12.2017	31.12.2016
BALANCE SHEET	Total assets, ISK m	1,229,976	1,205,228	1,130,403	1,035,822	1,047,554
	Loans to customers, ISK m	894,446	873,530	846,599	755,175	687,840
	Deposits from customers, ISK m	615,869	611,303	578,959	567,029	594,187
	Customer deposit / customer loan ratio	68.9%	70.0%	68.4%	75.1%	86.4%
CAPITAL	Total equity, ISK m	175,784	173,621	176,313	181,045	178,925
	Tier 1 capital ratio	18.8%	19.1%	20.3%	22.6%	24.9%
	Total capital ratio	21.4%	20.9%	22.2%	24.1%	25.2%
	Leverage ratio	13.4%	13.5%	14.6%	16.2%	16.0%

1. Return from regular operations and corresponding ratios on normalized CET1 of 16%, adjusted for risk free interest on excess capital.
2. Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund – One off items) / (Total operating income – one off items)
3. Earnings from regular operations is defined as earnings excluding one-off items e.g. bank tax and one-off costs and income.

Birna Einarsdóttir, CEO of Islandsbanki

Íslandsbanki put in a solid performance in the first half of 2019. We are pleased to see that the Bank was responsible for over 40% market share of new loans to individuals during the period. Customers are always embracing new digital solutions, and the Bank has recently launched a new online mortgage service alongside the introduction of Apple Pay to our services.

According to Gallup, the Bank has the largest market share as primary bank for SMEs at 37% and surveys are showing that the Bank now enjoys its highest NPS scores since the start of measurements. The Bank also recorded the largest trading volume in the local bond market and the second largest in the stock market. Consequently, fee and commission income rose by 14% and interest income increased by 9.4% during the period.

The cost to income ratio of the parent company is now at the Bank's target of 55%, a very welcome development and a reflection of the hard work put in to improving both top and bottom line performance. However, the corresponding ratio for the Group as a whole is 62%. Overall loan growth has remained stable and the Bank's asset quality is strong by international comparison.

The Group generated a profit of ISK 4.7 billion in the first half of 2019, which is a drop since the same period last year. Negative net impairments are higher as a result of the weaker economic situation and the continuing losses of one of the Bank's subsidiaries adversely affected the results at Group level.

The Bank's liquidity ratios have strengthened over the course of the year and are well above internal and regulatory requirements. Capital ratios are in line with the Bank's long term targets. The Bank's funding operations have been successful, notably issuing a further subordinated bond in Swedish Kroner in the second quarter, and deposits have risen since the beginning of the year.



The Íslandsbanki Reykjavík Marathon is at hand and will be held on 24 August. This is the largest fundraising event of the year in Iceland and we are proud to be the main sponsor once again and we encourage people to run and support a good cause.

First half 2019 (1H19) operational highlights

- Íslandsbanki announced this summer that its customers can now use Apple Pay.
- A fully automated online mortgage application and evaluation procedure was recently introduced by the Bank.
- Íslandsbanki led the bond market in terms of trading volume in June, with a market share of 19.7%.
- In June, Íslandsbanki issued a SEK 500 m 10NC5 Tier 2 bond.
- Íslandsbanki published a new report on the Icelandic tourism sector in May and organised a conference on that topic at the Hilton Reykjavík Nordica.
- Íslandsbanki released a new macro-economic forecast in June 2019 and published an article „Is the krona in balance” on the Bank’s website in July.
- In July, Íslandsbanki lowered interest rates on housing and car loans, following a policy rate decision by the Central Bank of Iceland’s Monetary Policy Committee.
- In July it was announced that Riaan Dreyer had been appointed Director of Information Technology at Íslandsbanki.
- S&P Global Ratings affirmed Íslandsbanki's rating of BBB+/A2 but changed the outlook from stable to negative.

INCOME STATEMENT

ISKm	1H19	1H18	Δ	2Q19	2Q18	Δ	2018
Net interest income	16,778	15,342	1,436	8,626	7,602	1,024	31,937
Net fee and commission income	6,623	5,810	813	3,406	3,032	374	12,227
Net financial income (expense)	621	95	526	173	378	(205)	(962)
Net foreign exchange loss	(101)	(67)	(34)	(71)	(57)	(14)	1
Other operating income	1,173	1,600	(427)	29	1,587	(1,558)	1,784
Total operating income	25,094	22,780	2,314	12,163	12,542	(379)	44,987
Salaries and related expenses	(8,363)	(7,952)	(411)	(4,312)	(4,026)	(286)	(15,500)
Other operating expenses	(6,000)	(5,770)	(230)	(2,961)	(2,846)	(115)	(12,150)
Administrative expenses	(14,363)	(13,722)	(641)	(7,273)	(6,872)	(401)	(27,650)
Contribution to the Depositor's and Investors' Guarantee Fund	(510)	(579)	69	(198)	(287)	89	(1,173)
Bank tax	(1,814)	(1,597)	(217)	(934)	(812)	(122)	(3,281)
Total operating expenses	(16,687)	(15,898)	(789)	(8,405)	(7,971)	(434)	(32,104)
Profit before net impairment on financial assets	8,407	6,882	1,525	3,758	4,571	(813)	12,883
Net impairment on financial assets	(1,848)	1,934	(3,782)	(929)	1,846	(2,775)	1,584
Profit before tax	6,559	8,816	(2,257)	2,829	6,417	(3,588)	14,467
Income tax expense	(1,779)	(2,480)	701	(626)	(1,465)	839	(4,734)
Profit for the period from continuing operations	4,780	6,336	(1,556)	2,203	4,952	(2,749)	9,733
Discontinued operations, net of income tax	(71)	794	(865)	(83)	81	(164)	912
Profit for the period	4,709	7,130	(2,421)	2,120	5,033	(2,913)	10,645

Income higher compared to same period last year

- Total income increased by 10% between years and amounted to ISK 25bn in 1H19.
- Net interest income totalled ISK 16.8bn, an increase of 9.4% from the previous year mainly due to increase in the loan book. The net interest margin was 2.8%, which is at comparable levels to 1H18. The net interest margin is expected to be slightly below 3.0% in the near to medium term.
- Net fee and commission income amounted to ISK 6.6bn, compared to ISK 5.8bn in 1H18. Overall net fee income grew by 14% between years, partly due to higher fees and commissions from one of the Bank's fee generating subsidiaries.
- Core income (net interest income and net fee and commission income) contributed 93% to the Bank's total operating income during the first half of 2019. The Bank remains focused on strong core earnings and stable long-term income.
- The Bank recorded a net financial gain of ISK 621m in 1H19, compared to gain of ISK 95m in 1H18.
- Other operating income totalled ISK 1.2bn in 1H19, as opposed to ISK 1.6bn in 1H18 and is primarily attributed to the Bank's settlement with old Byr concerning the value of old Byr's loan book from when the Bank acquired old Byr in 2011.

Cost to income ratio on downward trend and parent company at 55% C/I target

- Administrative expenses grew by ISK 641m year-on-year or 4.7%.
- The number of FTE's at the close of the period excluding seasonal employees was 806 (841 in 1H18) in the parent company and 1,053 (1,013 in 1H18) for the Group.
- The cost-to-income (C/I) ratio at end-March was 62.0%, compared with 67.3% in 1H18. The C/I ratio excludes the bank tax and other one-off cost items. The C/I in the parent company was 55.4% in 1H19 for the same period, which is in line with the Bank's long-term target of 55%.
- The after-tax loss from discontinued operations was ISK 71m in 1H19, compared with ISK 794m gain in 1H18.

Negative net impairment on financial assets reflects changes in economic outlook

- Net impairment on financial assets generated a loss of ISK 1,848m in 1H19, compared to ISK 1,934m gain in 1H18, explained by specific impairments for large customers, less favourable economic environment, change in relative weighting of economic forecasts and an unfavourable ruling in a court case.

Taxes and levies continue to affect profitability

- The tax on the profit for the period amounted to ISK 1.8bn, compared to ISK 2.5bn in 1H18. The effective tax rate was 27.1%, compared to 28.1% in 1H18. The bank tax accounted for ISK 1,814m in 1H19, compared with ISK 1,597m in 1H18. The Bank is subject to the special financial tax of 6% on taxable profits in excess of ISK 1bn and makes contributions to the Debtors' and Investors' Guarantee Fund, the Financial Supervisory Authority, and the Office of the Debtors' Ombudsman. The contribution to the Depositors' and Investors' Guarantee Fund, was at ISK 510m, an ISK 69m decrease from the previous year. Total taxes and levies amounted to ISK 5.3bn in 1H19 which is comparable to 1H18.

Quality of loan portfolio measures high in international comparisons

- At the end of the reporting period, the ratio of impaired loans was 2.0% for the Group compared to a 3.1% weighted average for European banks at the end of March 2019. When only taking into account the quality of loans to customers, the NPL ratio was at 2.0% at the end of June (net carrying amount).

Profitability marked by negative net impairments

- Profit after tax was ISK 4.7bn in 1H19 (1H18: ISK 7.1bn) and annualised return on equity (after tax) was 5.4% in 1H19 (1H18: 8.2%). Earnings from regular operations were ISK 5.7bn, (1H18: ISK 6.8bn) and annualised return on equity from regular operations normalised for 16% CET1 was 7.2% in 1H19, compared to 9.4% in 1H18. Regular earnings decreased by ISK 1.1bn between years.

BALANCE SHEET

Assets – growing balance sheet through continued loan growth

- The balance sheet grew by 8.8% from year-end 2018, to ISK 1,230bn with loans to customers growing by 5.7%, or ISK 47.8bn. Demand for new credit came from all of the Bank's business segments but was concentrated mostly in Corporate & Investment Banking. Mortgage loans rose by ISK 18.5bn from year-end 2018. New lending amounted to ISK 107.4bn in 1H19, as opposed to ISK 98.5bn in the previous year, an increase of 9%. Outstanding loans to the tourism industry in Iceland have decreased and are now 11% of the loan portfolio which is well diversified.
- Loans are generally well covered by stable collateral, majority 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 61% at end June 2019 and is unchanged from year-end 2018. The Bank's asset encumbrance ratio was 17.2% at end-June 2019 compared to 18% at end 2018.
- Three items – cash and balances with the Central Bank, bonds and debt instruments, and loans to credit institutions – amount to about ISK 277bn, some ISK 235bn of which are liquid assets.

Assets, ISK m	30.06.2019	31.12.2018	Δ
Cash and balances with Central Bank	122,794	135,056	(12,262)
Bonds and debt instruments	77,033	69,415	7,618
Shares and equity instruments	19,176	13,074	6,102
Derivatives	5,843	4,550	1,293
Loans to credit institutions	77,387	41,577	35,810
Loans to customers	894,446	846,599	47,847
Investment in associates	687	682	5
Property and equipment	9,504	5,271	4,233
Intangible assets	4,882	5,002	(120)
Other assets	18,224	9,177	9,047
Total assets	1,229,976	1,130,403	99,573

Liabilities – successful funding through deposits and market activity

- Total liabilities amount to ISK 1,054bn, an increase of 10.5% from year-end 2018. The Bank maintained strong liquidity levels into 2019, and all regulatory and internal metrics were well above the set limits.
- At June 2019, the Bank's liquidity coverage ratio (LCR) for all currencies was 185% for the Group and 94% in Icelandic krónur and 169% for the parent company in all currencies. The net stable funding ratio (NSFR) for the Group in all currencies was 117% and the NSFR in foreign currencies for the Group was 179%.

- Total deposits increased by 6.4% from year-end 2018, to ISK 616bn. Deposits are still the Bank's main source of funding and concentration levels are monitored closely. The increase was mainly due to a rise in pension fund positions and institutional investors. The ratio of customer deposits to customer loans increased to 68.9% at end-June 2019, compared to 68.4% at end 2018.

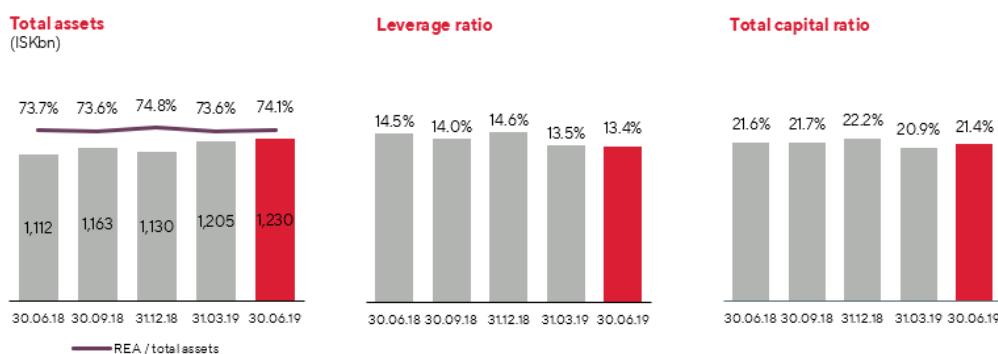
Liabilities & Equity, ISK m	30.06.2019	31.12.2018	Δ
Deposits from Central Bank and credit institutions	19,830	15,619	4,211
Deposits from customers	615,869	578,959	36,910
Derivative instruments and short positions	6,903	5,521	1,382
Debt issued and other borrowed funds	337,473	300,976	36,497
Subordinated loans	23,431	16,216	7,215
Tax liabilities	8,674	7,150	1,524
Other liabilities	42,012	29,649	12,363
Total Liabilities	1,054,192	954,090	100,102
Total Equity	175,784	176,313	(529)
Total Liabilities and Equity	1,229,976	1,130,403	99,573

- In June, Íslandsbanki issued a 10NC5 SEK 500m Tier 2 bond. This was the Bank's third Tier 2 bond issue and with this transaction the Bank reached its Tier 2 target which is an important milestone in optimising its long-term capital composition.
- In April, the Bank issued a EUR 300m 3-year benchmark fixed rate bond at a spread of 130 basis points over 3-year mid swaps. The transaction was issued concurrently with a tender to buy back EUR 300m of the Bank's outstanding EUR 500m 2020 benchmark bond.
- In 1H19 the Bank issued five private placements amounting to EUR 11.5m, SEK 650m and NOK 1.4bn with maturities of between 18 months and 5 years.

Equity

- Total equity amounted to ISK 175.8bn at June 2019, compared to ISK 176.3bn at the end of 2018. Of that total, ISK 2.4bn is attributable to non-controlling interests. At the Bank's AGM in March shareholders approved the Board's proposal to pay dividends amounting to ISK 5.3bn. The nominal value of the Bank's authorised share capital was ISK 10bn at the end of the quarter, and total share capital amounted to ISK 65bn.
- At the end of June, the Bank's total capital ratio was 21.4%, compared to 22.2% at year-end 2018, which is in line with the Bank's target. The Bank's Tier 1 ratio was 18.8% at June 2019, compared to 20.3% at year-end 2018. In late 2018, the Icelandic Financial Supervisory Authority (FME) lowered the minimum requirement for total capital for Íslandsbanki from 19.8% to 18.8%. The decrease was credited to the Bank's lower risk profile.

- In light of recent changes to regulatory requirements and an updated assessment of the business environment, the Bank has decided to revise its management buffer from 0.5-1.5% to 0.5-2.0%. It is worth noting that the FME increased the countercyclical capital buffer from 1.25% to 1.75%, in May 2019.



- Íslandsbanki uses the standardised method to calculate its risk exposure amount (REA), which amounted to ISK 911.8bn at the end of June 2019, or 74.1% of total assets. The leverage ratio was 13.4% at the end of June compared to 14.6% at end 2018, indicating low leverage.

Ratings

- Íslandsbanki is rated by S&P Global Ratings (S&P) and in July S&P affirmed Íslandsbanki's BBB+/A-2 rating but changed the outlook to negative.
- In its report, S&P refers to Íslandsbanki's stable domestic market position and acknowledges the Bank's success in introducing new digital products and improving its IT infrastructure, placing Íslandsbanki well ahead of many other European banks. S&P also notes the Bank's exceptional capitalisation, strong liquidity levels and robust asset quality.
- S&P's rationale for the change to negative outlook is mostly derived from its view that Iceland's operating environment will remain challenging, affected by the 2019 economic recession, declining interest rates, still-high taxation, and stiff competition from pension funds in mortgage lending, and thus contributing to the declining profitability of the Bank.



INVESTOR RELATIONS

Investor call in English on Thursday 1 August at 9.00 AM (GMT)

The Bank will host an investor call in English at 9.00 AM on Thursday, 1 August. The call will start with a short macro update on the Icelandic economy, followed by a review of the financial results and Q&A.

Please register by replying to: ir@islandsbanki.is. Dial-in details and presentation will be sent out prior to the call.

Meeting with market participants on Thursday 1 August at 10.30 AM (GMT)

A meeting with market participants in Icelandic will take place on 1 August at 10.30 AM. The presentation will take place at the Islandsbanki headquarters, Hagasmári 3, 9 floor, 201 Kópavogur. Registration to the meeting is required. Please register by sending an e-mail to: ir@islandsbanki.is

Additional investor material

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

Financial calendar

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

Q3/2019 results – 30 October 2019
Q4/Annual 2019 results – 12 February 2020
Annual General Meeting – 19 March 2020
Q1/2020 results – 6 May 2020
Q2/2020 results – 29 July 2020
Q3/2020 results – 28 October 2020

Please note that the dates are subject to change.