# Íslandsbanki

## J.P. Morgan - Investor update

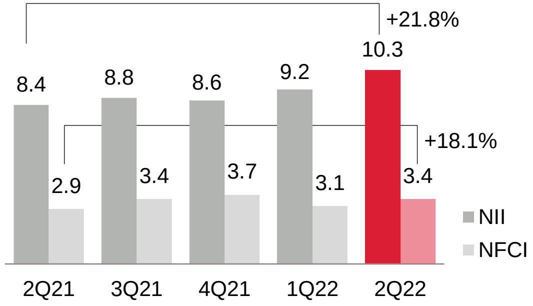
islandsbanki.is

# Sound operations deliver strong performance

## ROE of 11.7% driven by higher revenues

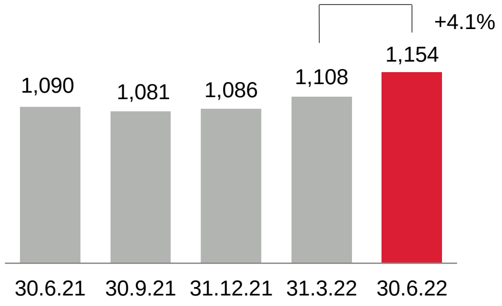
### Growth above 2022 guidance

**NII and NFCI, ISKbn**



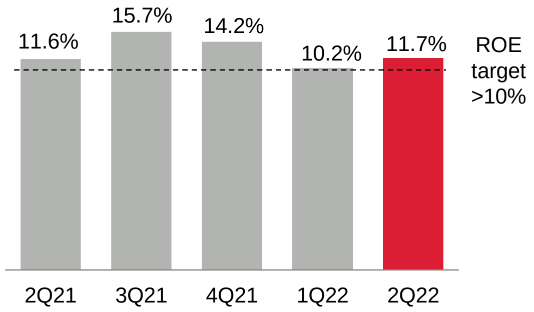

### Strong growth in lending

**Loans to customers, ISKbn**



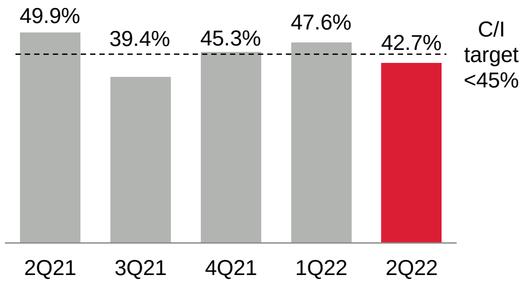

### ROE above 2022 guidance

**ROE**




### C/I ratio below 2022 guidance

**C/I ratio**



# Revised 2022 guidance and financial targets on track

## Guidance of over 10% ROE for 2022 following good financial result

| Targets | Targets | Revised 2022 Guidance | Previous 2022 Guidance | 2Q22 | 1Q22 | 2021 |
|---|---|---|---|---|---|---|
| Return on equity | >10% | **>10%[1]** | 8-10% by 2023 | 11.7% ✓ | 10.2% ✓ | 12.3% ✓ |
| Cost-to-income ratio[2] | <45% | **44-47%** | 45-50% | 42.7% ✓ | 47.6% ✓ | 46.2% ✓ |
| CET1 capital ratio[3] | ~16.5% | Unchanged | Normalise before YE2023 | 18.2% ✓ | 18.8% ✓ | 21.3% ✓ |
| Dividend-payout-ratio | 50% | Unchanged | 50% | | | 50% ✓ |

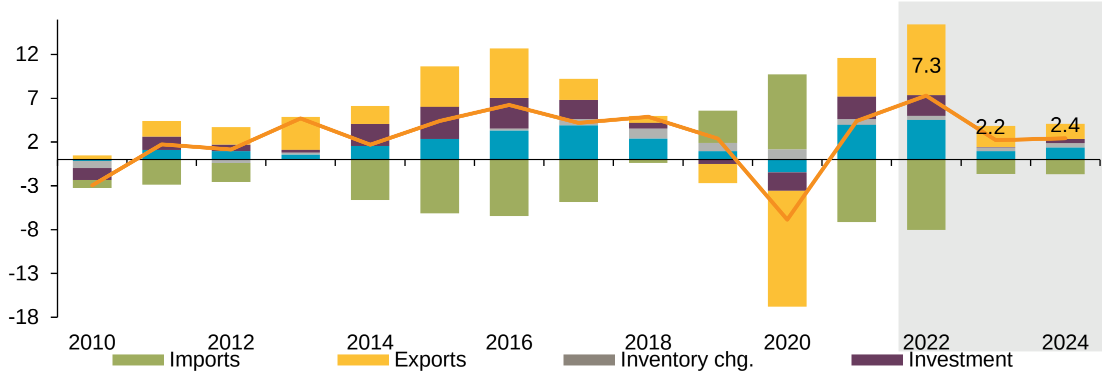
1. ROE is highly dependent on the cost of risk. Cost of risk was negative 17bp in 1H2022 and with CoR of zero, ROE for that period would have been approximately 10.0%. 2. Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund – One-off items) / (Total operating income – One-off items). 3. Long term CET1 capital target is subject to regulatory requirements and includes a management buffer of 50-200bp.

# Adjustment phase ahead in the Icelandic economy

## Moderate GDP growth in the cards after an impressive surge

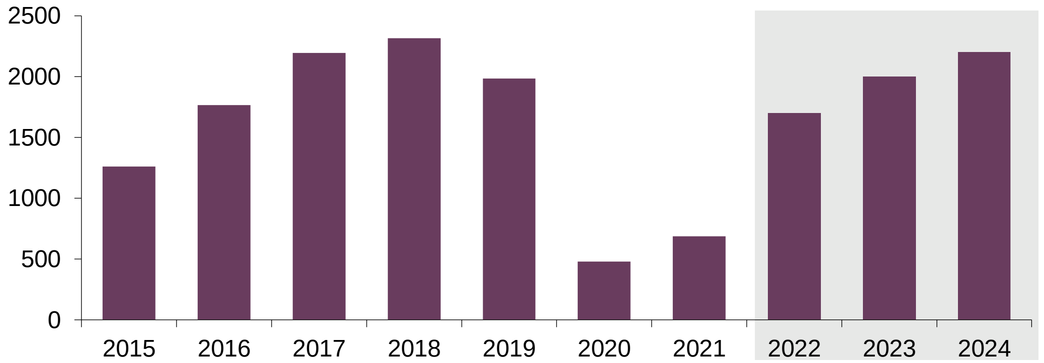
### Exports replace domestic demand as the key catalyst of healthy GDP growth…

Real GDP and main subitems, YoY change, %



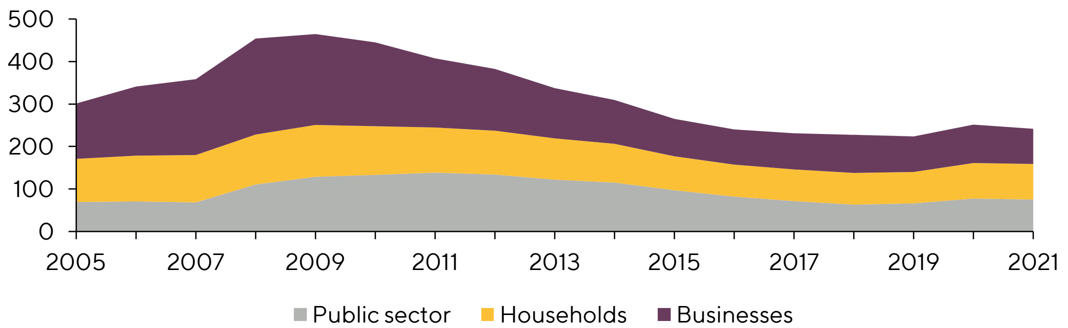

### ..as tourism sector recovery continues following receding pandemic impact

Number of foreign tourists per year, thousands



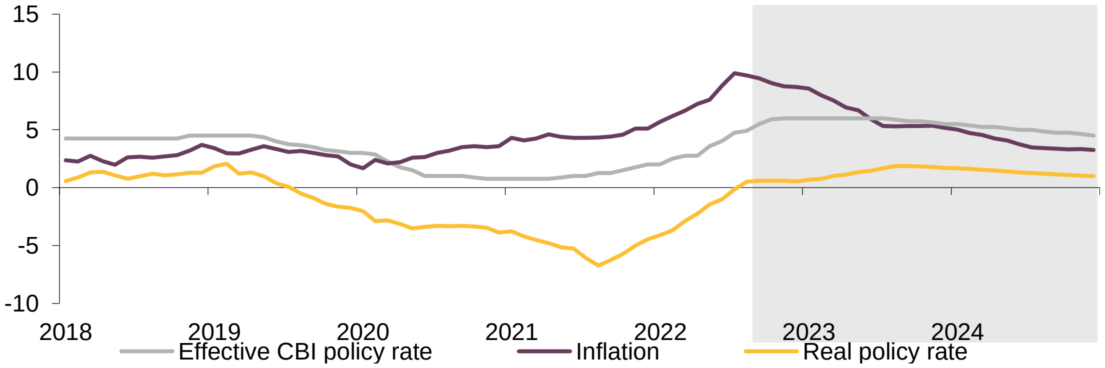

### Moderate leverage throughout the economy increases resilience to shock…

Gross debt as % of GDP




### …and the CB has tightened the monetary policy in response to inflation spike

Inflation and policy rate, %




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


# Strong second quarter of 2022

## Íslandsbanki awarded the Euromoney "Award for Excellence" in 2022

### Personal Banking

- **16.2%** ROE
- **49.2%** Cost-to-income ratio
- **2.7%** NIM

- Growth in mortgages lending of 4.4% in 2Q22
- Increased card spending supports strong fee revenue
- New pension platform enables self service for pension customers

### Business Banking

- **18.9%** ROE
- **39.0%** Cost-to-income ratio
- **5.4%** NIM

- Good growth in lending volumes with 6.5% growth in 2Q22
- ergo Brisk lending with 16.4% growth for Ergo financing in 2Q22 and over a third of new car loans are for Green cars[2]

### Corporate & Investment Banking

- **13.0%** ROE
- **33.7%** Cost-to-income ratio
- **3.1%** NIM

- Highest market share in equity sales and #2 in bonds brokerage in 1H22
- First loan granted in cooperation with the IS Corporate Credit Fund
- Corporate Finance completed many milestone transactions, including a sale of a real estate portfolio for SKEL

### Iceland Funds

- **18.0%** ROE
- **61.0%** Cost-to-income ratio[1]
- AUM ISK **392bn**

- Inflows to asset allocation, equity and covered bond funds but total AuM decrease due to outflow from short bond funds and market performance

### Sustainability

- $CO_2$ Íslandsbanki receives top ESG score (90/100) from Reitun for the second year in a row
- The Bank's score for environmental practices has risen by 12.9% year-on-year
- Good progress on Secondary objectives for 2022

1. As calculated from the Bank's Consolidated Income Statement. 2. Green financing is offered when a vehicle emits less than 50g/km CO2.

# Smarter, faster digital services for happier customers at the best bank in Iceland

EUROMONEY AWARDS FOR EXCELLENCE 2022
ICELAND BEST BANK

**99%**

of all touchpoints are via digital channels,10% YoY increase in active app customers

**25%**

of all active app customers under 40 years have activated carbon calculator in app

**80%**

of fund sales to retail customers digital. Savings, cards, loans and fund sales easy app access and securities in pipeline

**21%**

increase in corporate app visits in 1H22 and 95% have tried the app

**32%**

increase in use of electronic signatures YoY. The solution enhances better service for customers

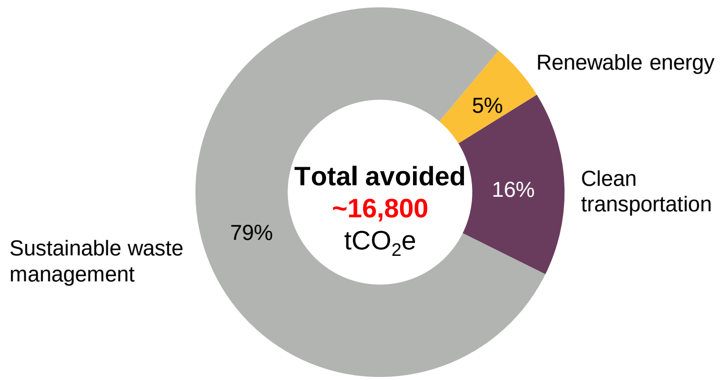
**3**

fintech initiatives: The Icelandic Fintech Cluster, Copenhagen Fintech and offering open APIs

# Summary of environmental and social impact in 2021

## Avoided emissions from sustainable lending increased by nearly 200% YoY

### Avoided greenhouse gas emissions in 2021




### Key developments in 2021

- Sustainable lending more than doubled year-on-year
- Sustainable Financing Framework categories in use increased from 7 to 11 out of 18 categories defined
- MSC certified seafood companies saw the biggest growth, accounting for 34% of eligible assets while green and social lending account for 50% and 16%, respectively
- Sustainable waste management created the most impact in terms of avoided emissions. Biogas produced by the financed waste management plant is assumed to replace fossil fuels, preventing 13,200 $tCO_2e$ from being released into the atmosphere[1]

### Additional impact indicators for sustainable lending

**2,200** clean vehicles

**97 GWh** of clean energy produced

**84,000 sqm** of eco-efficient buildings

**44,000** tonnes of MSC certified products sold

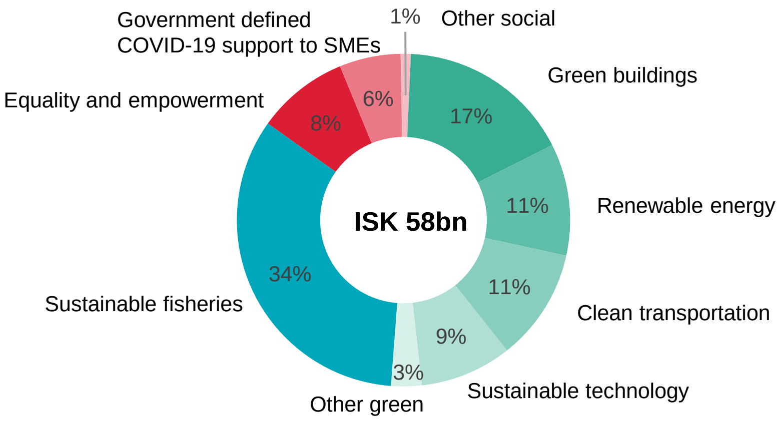
**60 social** housing units

**30 loans** to gender balanced companies

**2** early childhood education facilities

**440** companies supported with COVID-19 loans

### Sustainable loans by category at year-end 2021




Report link

1. In the impact calculations for sustainable waste management, biogas produced from waste is assumed to replace fossil fuels and estimated avoided emissions from recycling the two types of waste used in the production (which would otherwise have been landfilled and composted, respectively) are also considered.

# Íslandsbanki Reykjavík Marathon

20 August 2022

- The biggest charitable event of the year
- Key funding event for many charitable organisations
- Over 115 charitable organisations benefit
- ISK 1bn in total collected since 2006
- Around 15.000 runners participating yearly[1]

REYKJAVÍKUR MARAÞON ÍSLANDSBANKA

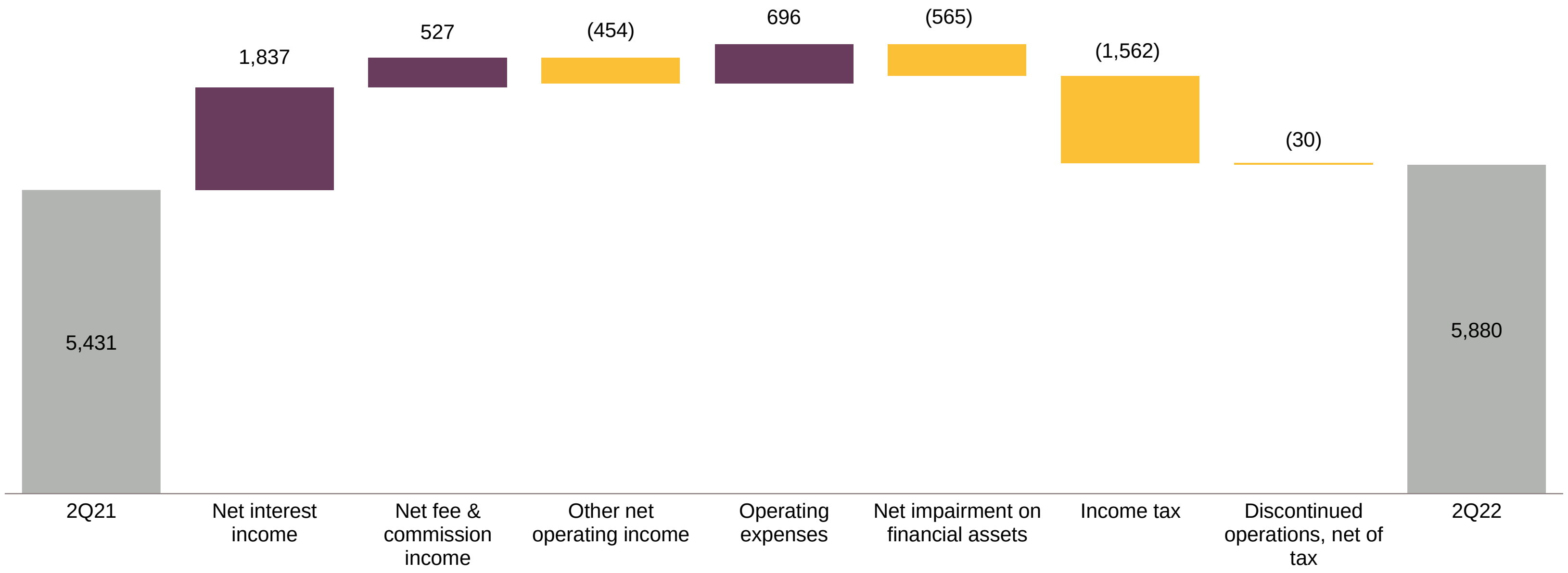
1. Not held in 2020 and 2021 due to COVID-19

# Financial overview

# Increase in core revenues in a good quarter

## Control of costs further boost a positive result

**Profit for the period – 2Q21 vs 2Q22**
ISKm



# NII rose strongly in all business segments

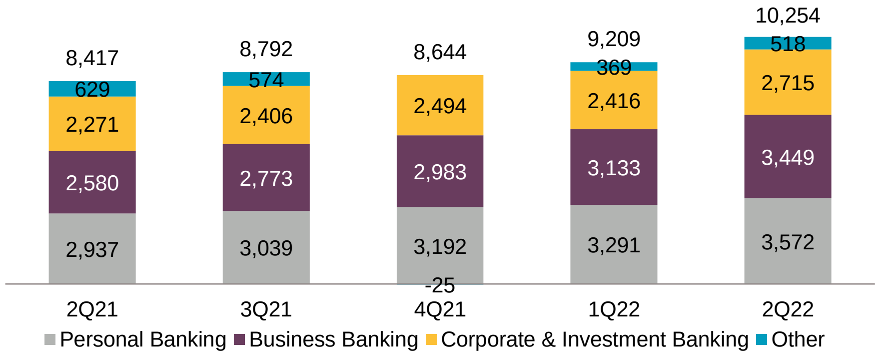
## NIM rose to 2.9% due to a higher interest rate environment

### Highlights

- NII continued a positive trend supported by higher interest rate environment leading to a rise in deposit margin YoY and positively affecting the Bank's liquidity portfolio
- Additional positive effect came from higher lending and deposit volumes which increased YoY across all business segments
- Lending margin was 1.9% in 2Q22 (2.2% in 2Q21) while deposit margin was 1.8% in 2Q22 (1.1% in 2Q21)

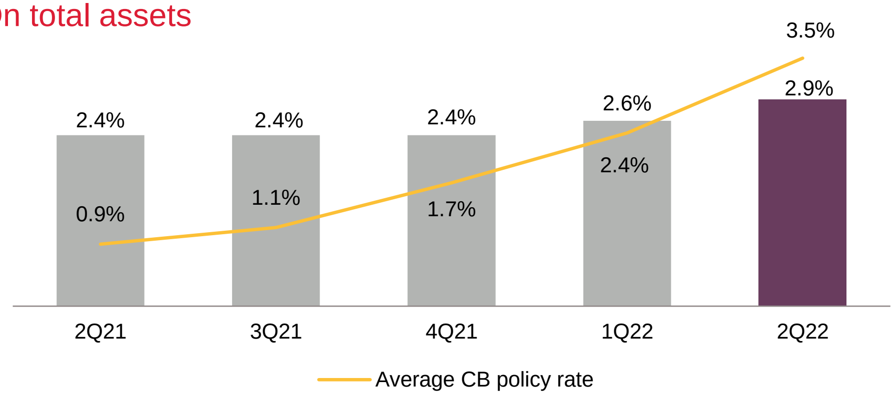
### Net interest income

By business segments, ISKm



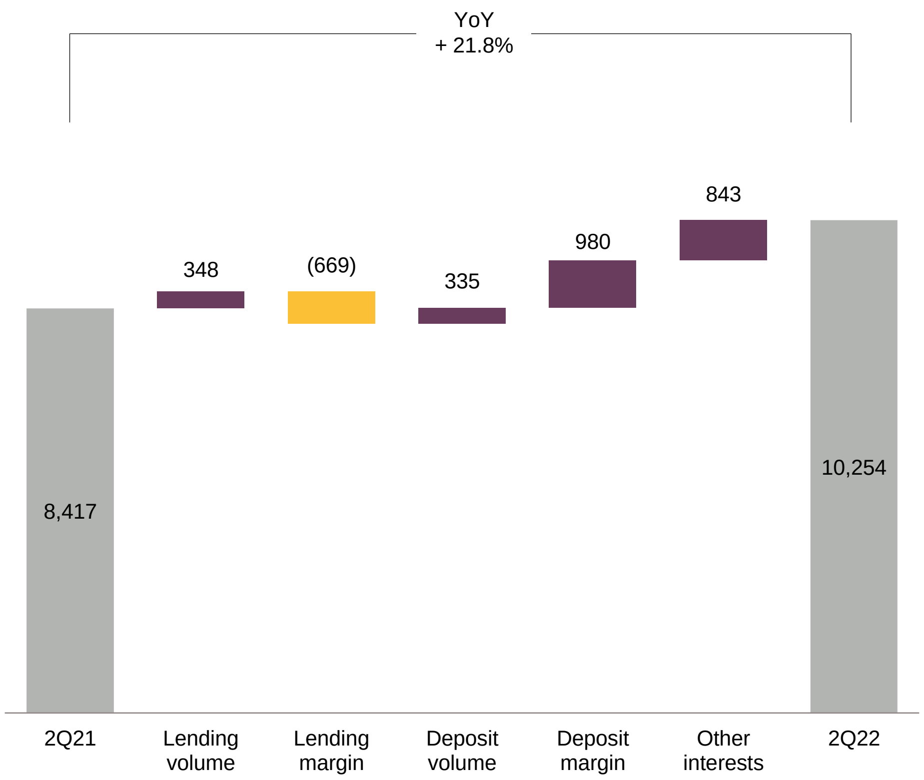

### Net interest margin

On total assets




### NII – comparison 2Q YoY

ISKm



# NFCI rose 18.1% YoY

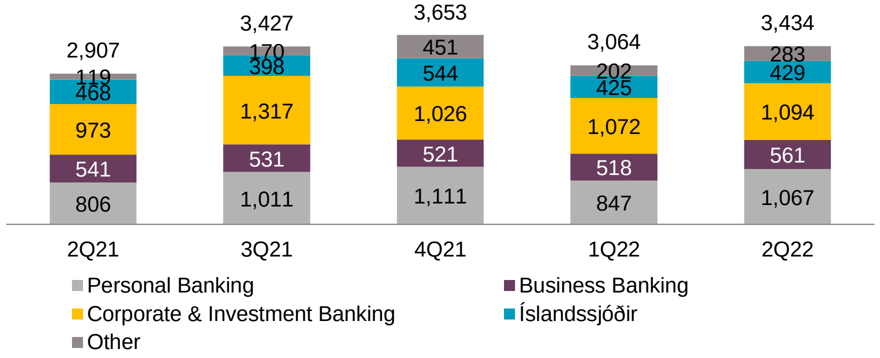
## Broad-based fee generation across the business units

### Highlights

- Revenues from investment banking and brokerage increase from currency sales and increased revenues from market making agreements
- Increased card transaction income and interchange income from cards, both domestic and foreign. Card expenses increased at the same time
- NFCI from loans and guarantees rose due to increased fees from guarantees and fees from changes of loan terms

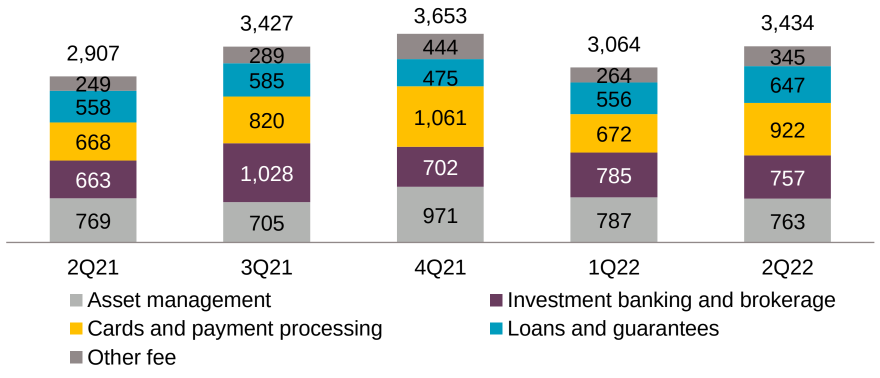
### Net fee and commission income

Business segments, ISKm



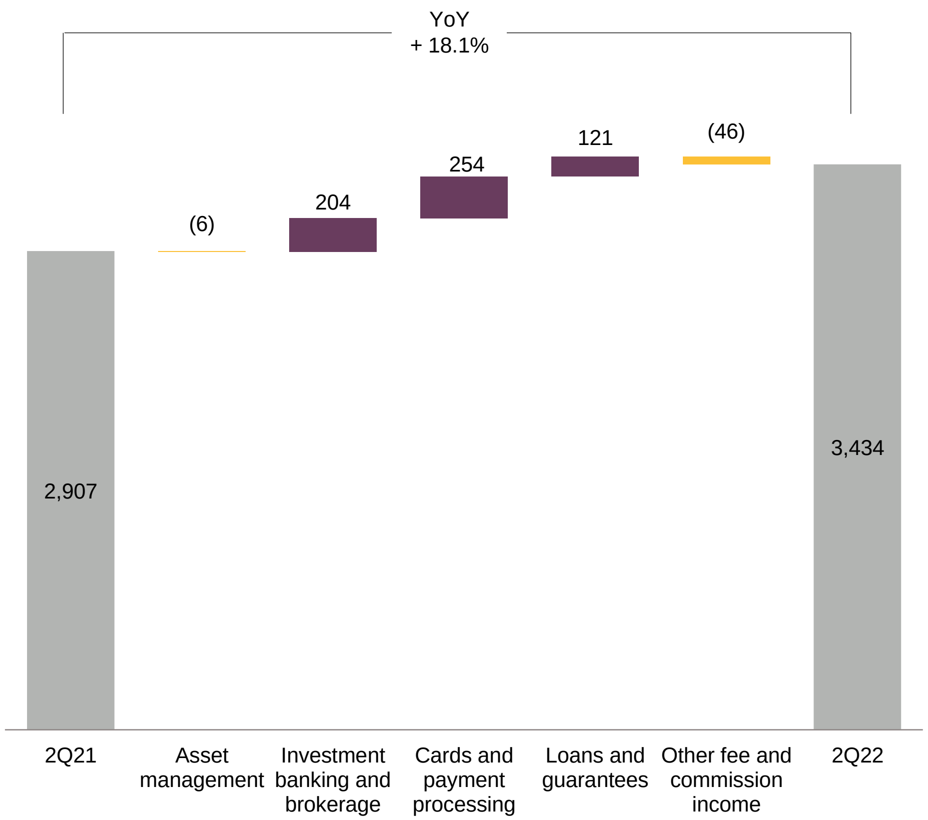

### Net fee and commission income

By type, ISKm




### NFCI – comparison 2Q YoY

ISKm



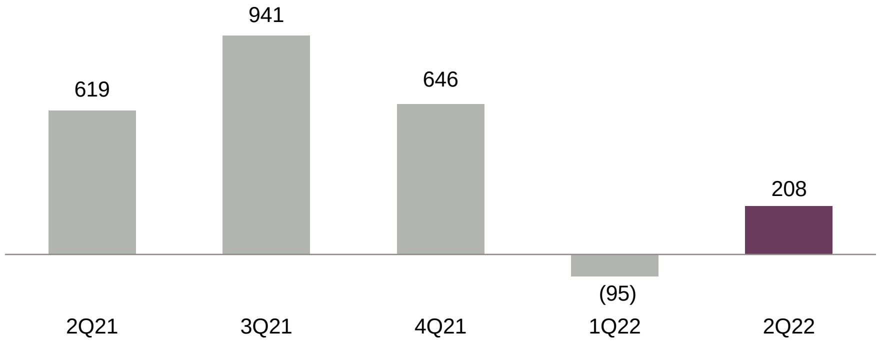
# Positive NFI in turbulent markets

## Rising benchmark interest rates do however support financial income in other derivatives

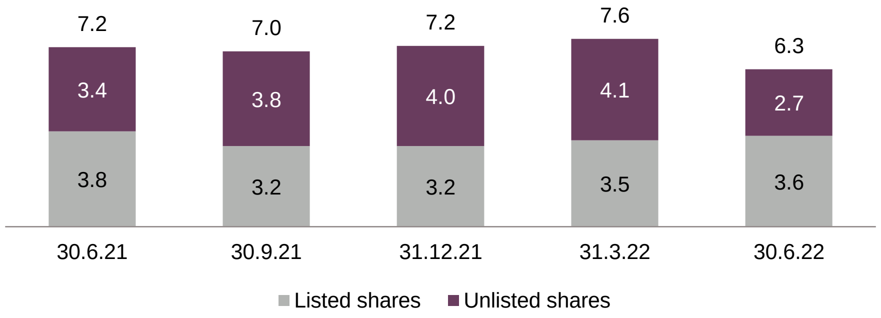
### Highlights

- Reduction in shares and equity instruments in 2Q22 is explained by Norðurturninn hf. (owner of the Bank's headquarters) which was classified as shares and equity instrument but is now classified as an associate

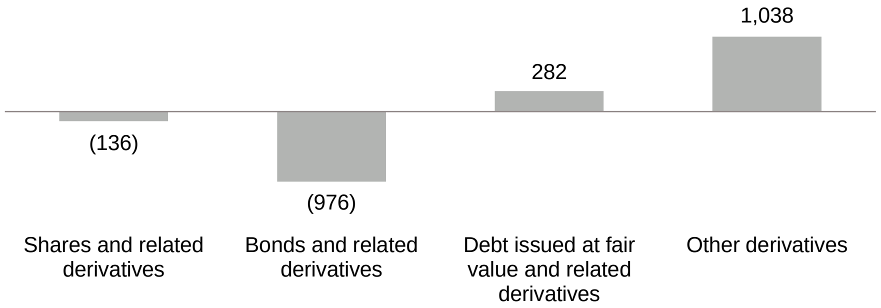
### Net financial income
ISKm



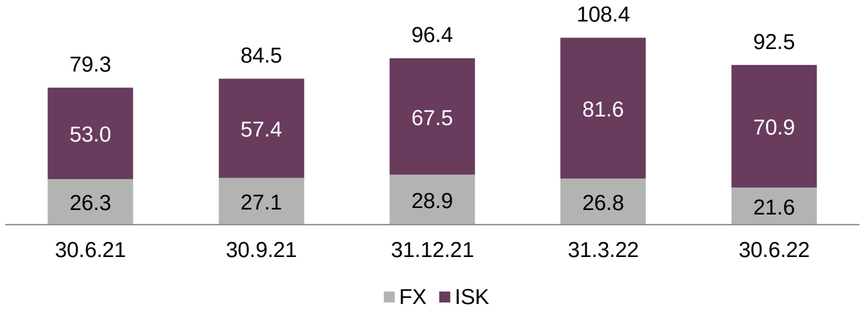

### Shares and equity instruments[1]
ISKbn




### Net financial income by type in 2Q22
ISKm




### Bonds and debt instruments[2]
ISKbn

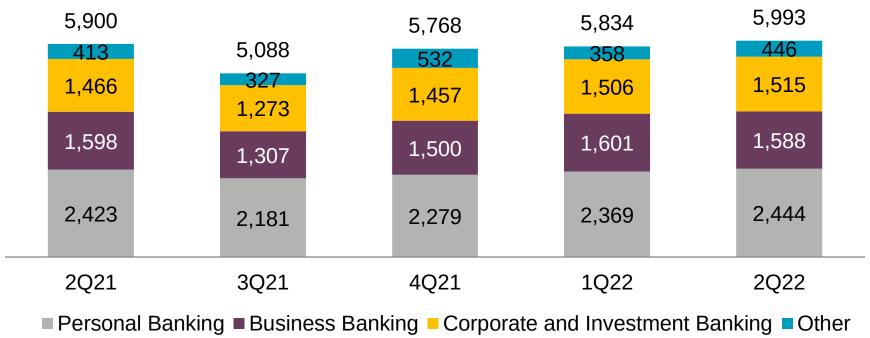



1.Excluding listed shares and equity instruments used for economic hedging. 2. Excluding listed bonds and debt instruments used for economic hedging.

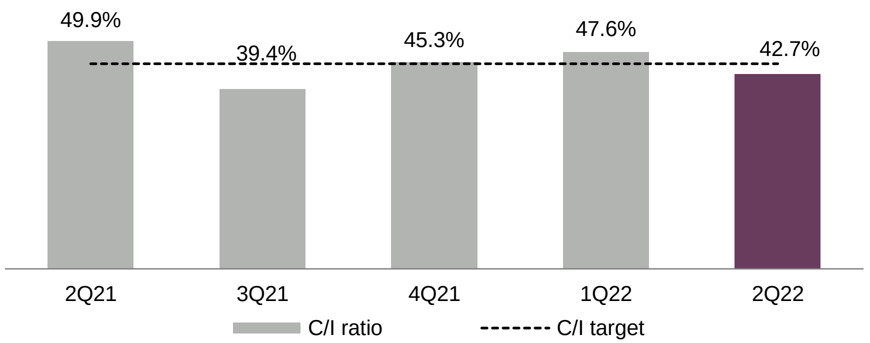
# Administrative expenses stable in 2Q22

## 5.9% reduction in real terms driven by lower salary costs

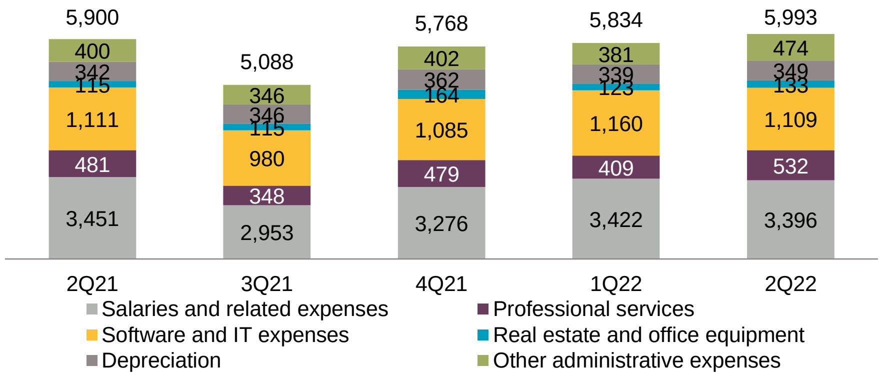
### Administrative expenses[1]
ISKm



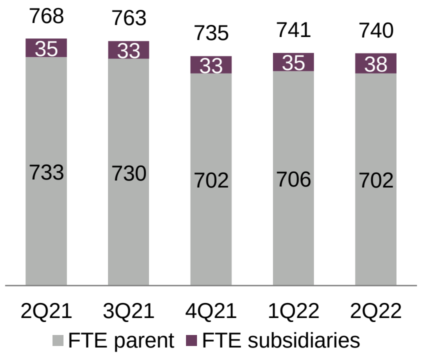

### Cost-to-income ratio[2]



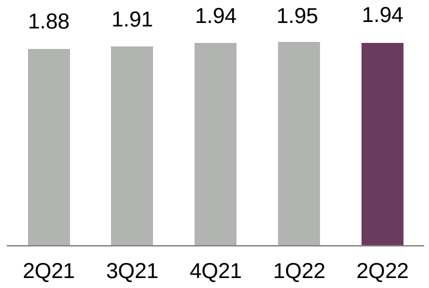

### Administrative expenses[1] – by type
ISKm




### FTE period end[3]




### Total assets / FTE[3]
ISKbn




1. Administrative expenses in 2Q21 are excluding 588m one-off cost related to the Bank's IPO. 2. Calculated as (Administrative expenses + Contribution to the Depositor's and Investors' Guarantee Fund – one off items) / Total operating income – one-off items). 2. Target was updated in 1Q21 from the previous <55% 3. FTE numbers exclude seasonal employees.

# Impairment reversals continued in 2Q22

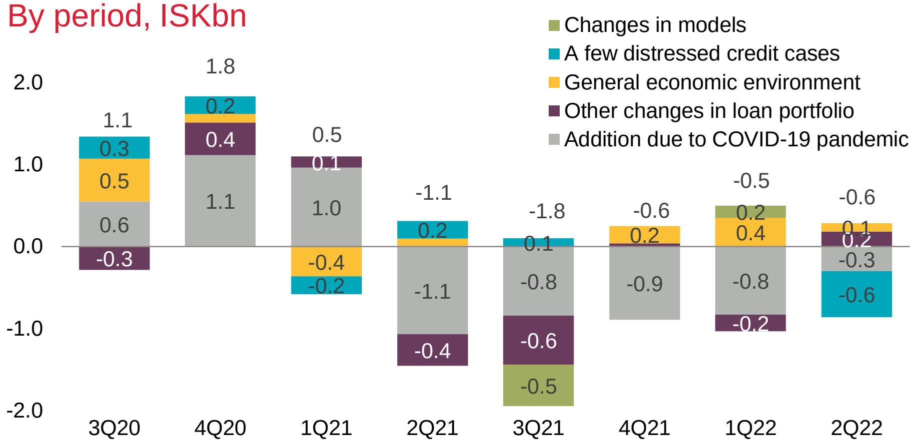
## Majority of forborne borrowers have resumed payments

### Highlights

- Reserve coverage ratio (RCR) for impairment allowance on Stage 3 was 24% at end of 2Q22
- The RCR fell when a disputed loan that had been fully impaired was paid up following a favourable court ruling
- The definition of forbearance includes a 24-month probation period. Therefore, loans are classified as forborne even after normal payments have resumed
- Loans amounting to ISK 66bn (80% of total) are expected to exit forbearance probation in 2022

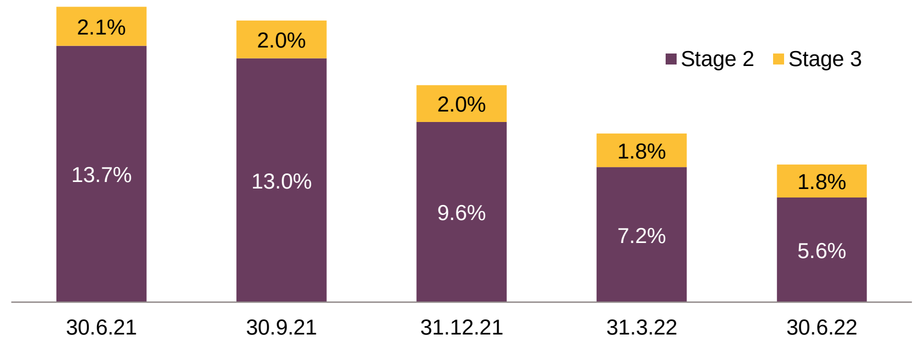
### Net impairment on financial assets

By period, ISKbn




### Loans to customers: Stage 2 and 3 (NPL)

Development of gross carrying amount as ratio of total loans

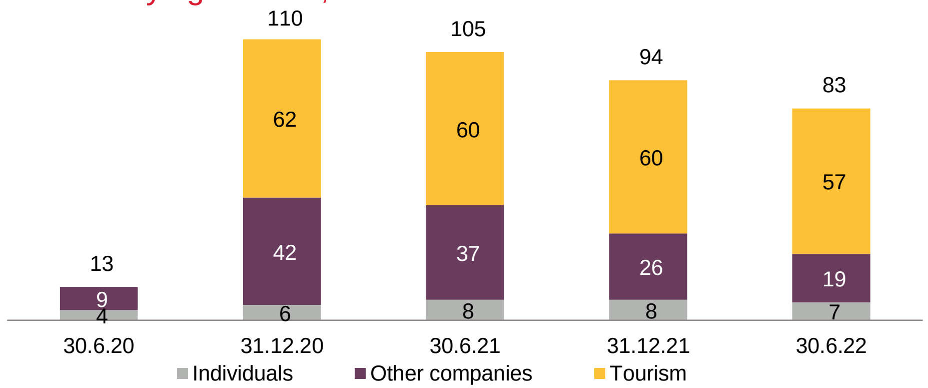



### Current and expected cost-of-risk

- Annualised cost of risk was -20bp in 2Q22 compared to -42bp for 2Q21
- Additional impairment allowance currently attributable to the tourism overlay and stage transfer is approx. ISK 0.9bn at end of 2Q22 down from 2.0bn at YE21
- The probability weights of economic scenarios were shifted to 20% (good), 50% (baseline), and 30% (bad) at end of 2Q22. A shift of 5% from baseline to the bad scenario would increase the impairment allowance by ISK 0.3bn while a 5% shift from the baseline to the good would decrease the allowance by ISK 0.15bn
- In 2Q22 a total of approximately ISK 750m of impairment reversals was a result of a favourable court ruling regarding a fully impaired loan

### Performing loans with forbearance

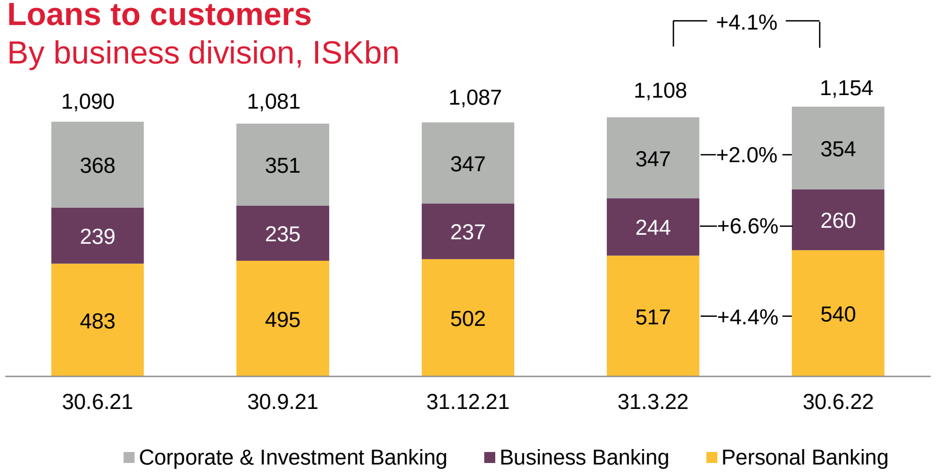
Gross carrying amount, ISKbn



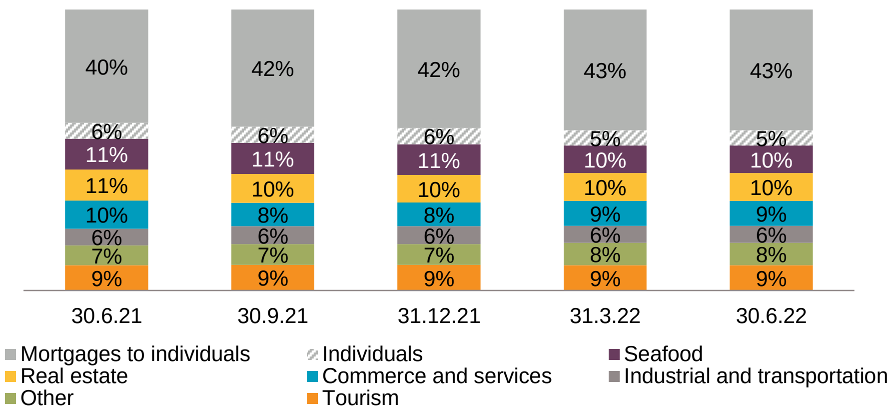
# Lending volume growth across all business units

## Credit quality remains strong and highly collateralised loan portfolio

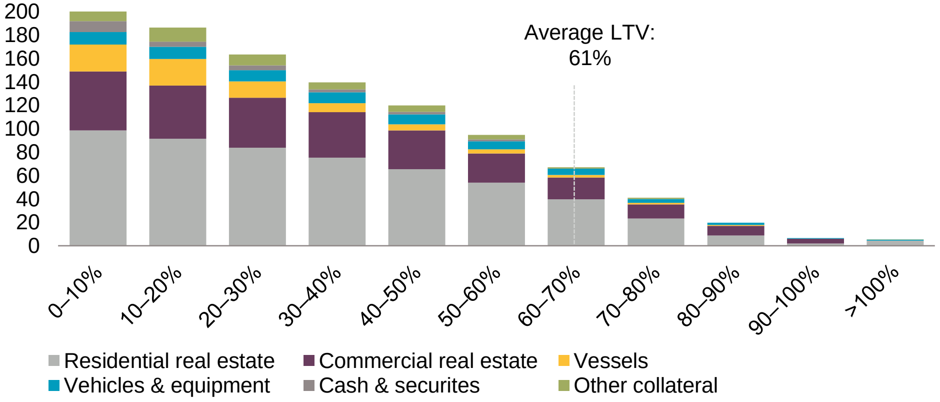
### Loans to customers
By business division, ISKbn



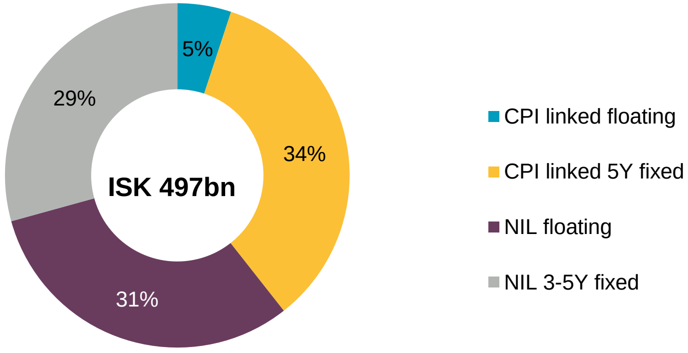

### Loans to customers
By sector, with tourism as a separate sector




### LTV distribution by underlying asset class
30.6.2022, loan splitting approach, ISKbn




### Mortgage portfolio[1]
Gross carrying amount, 30.6.2022




1. NIL stands for non-index linked loans.

# Mortgages portfolio resistant to rising rates

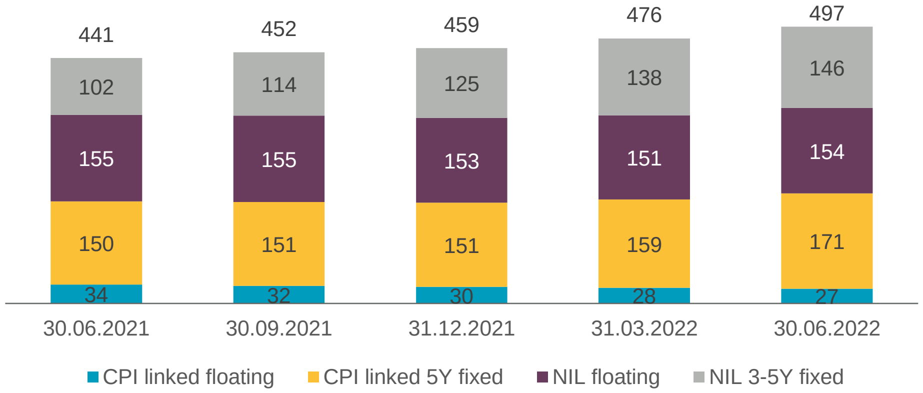
## Average LTVs stable and built-in buffers for rate increases

### Highlights

- Conservative payment assessment for non-indexed variable rates mortgages in low interest environment makes the Bank's customers well equipped for higher interest rate environment
- LTV is capped at 80% (85% for first time buyers) and debt service-to-income <35% (40% for first-time buyers)
- Sensitivity analysis conducted at year-end showed that if rates would rise by 5% it would not lead to a further capital requirement for the Bank. The Bank's rates have now risen by 3.6% since the analysis and are not expected to exceed the 5% range
- If official real estate value for 2023 was used instead of the official 2022 value, then property value within the Bank's mortgages portfolio would increase by 26% on average and LTVs would decrease

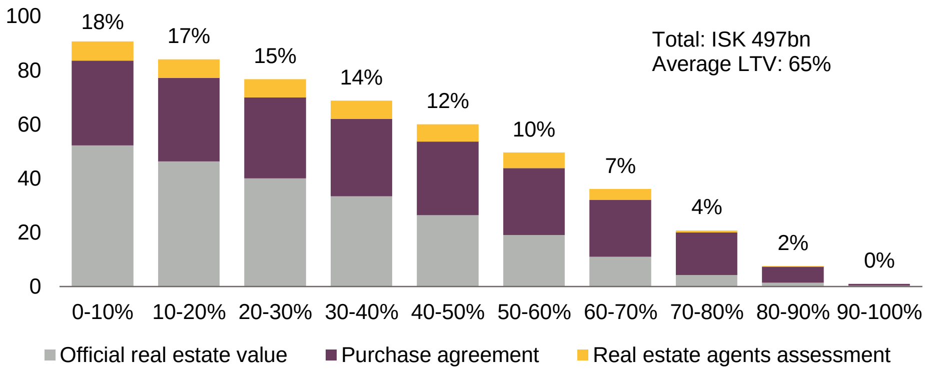
### Mortgage portfolio

Gross carrying amount, ISKbn



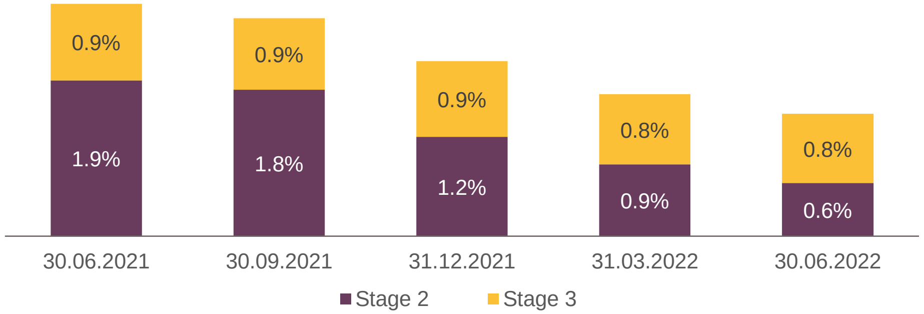

### LTV distribution of mortgages to individuals[1]

Gross carrying amount, ISKbn, 30.6.2022



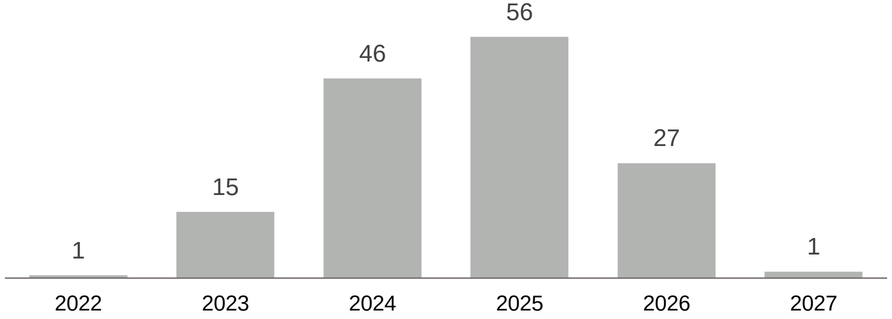

### Mortgages portfolio: Stage 2 and 3 (NPL)

Development of gross carrying amount as ratio of mortgages portfolio




### Interest rate reset profile for NIL 3-5Y fixed rate mortgages[2]

Gross carrying amount, ISKbn




1. Official real estate value 2022 is used for property value for 47% of the mortgage loan portfolio, purchase agreement for 44% and real estate agents assessment and other for 9%. 2. NIL stands for non-index linked loans

# Deposits are the largest source of funding

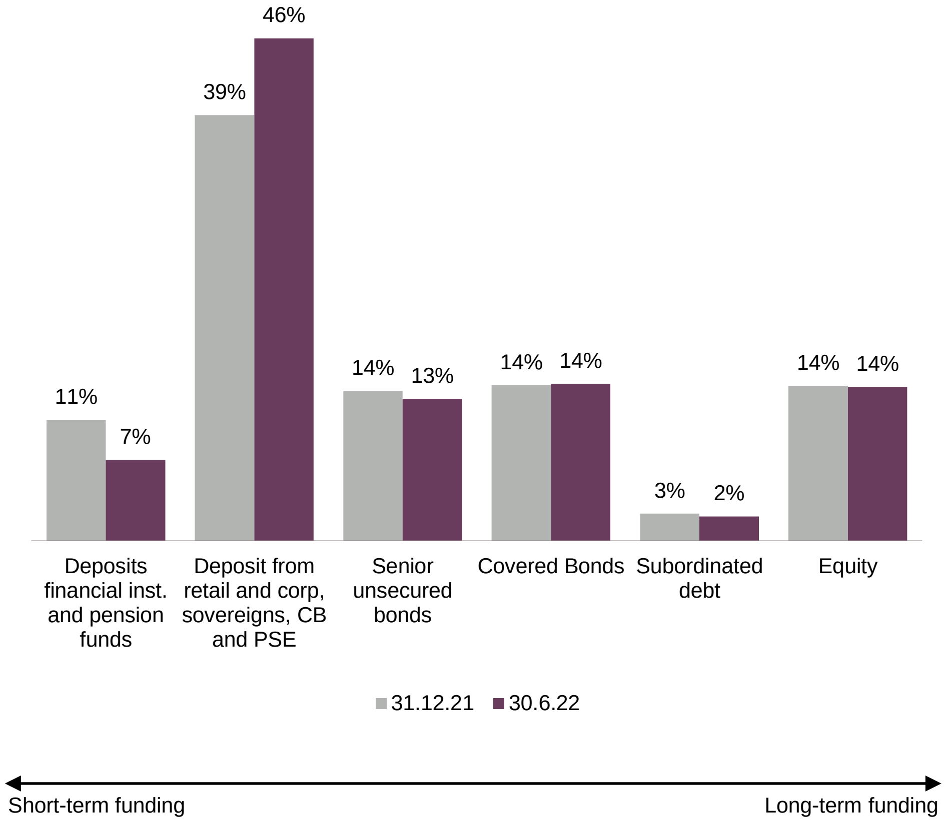
## Retail deposits continue to increase

### Highlights

- Term deposits are 18% of total deposits
- Deposit concentration is stable. 11% of the Bank's deposits belonged to the 10 largest depositors and 27% to the 100 largest depositors at 2Q22, compared to 12% and 28% respectively at YE21
- At end of 2Q22 75% of deposits were in non-indexed ISK, 13% CPI-linked and 12% in foreign currencies

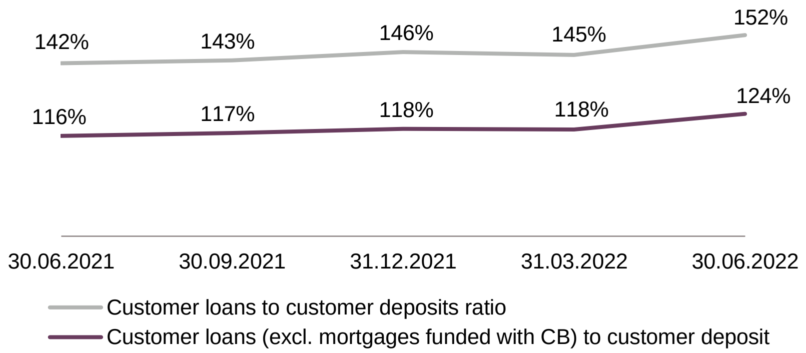
### Funding sources

By type, % of total liabilities and equity



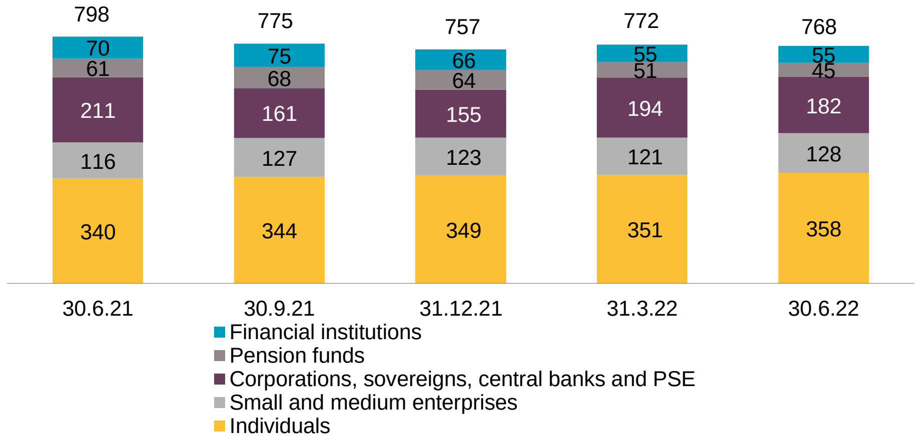

### Customer loans to customer deposits ratio

Development, %




### Deposits from customers and credit institutions

Development, by LCR category, ISKbn



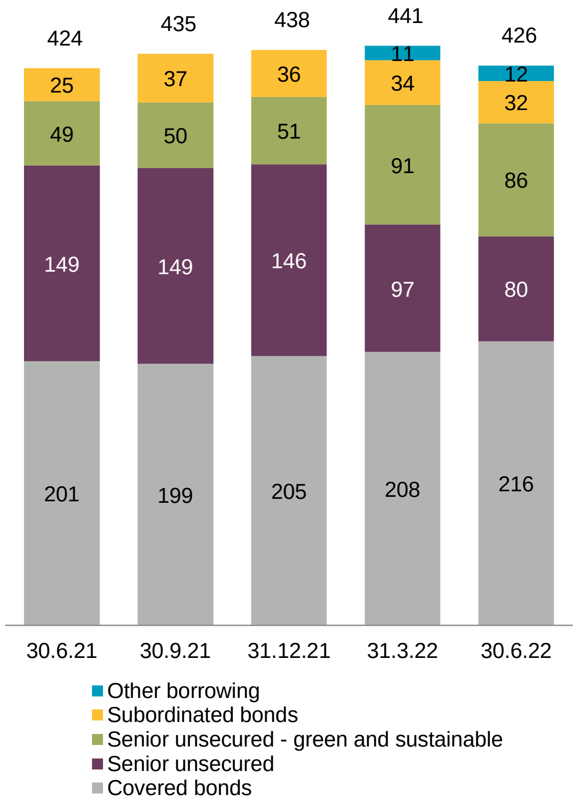
# Seasoned and diversified long-term funding programme

## Majority of 2022 maturities already funded through €300m sustainable bond issue in January

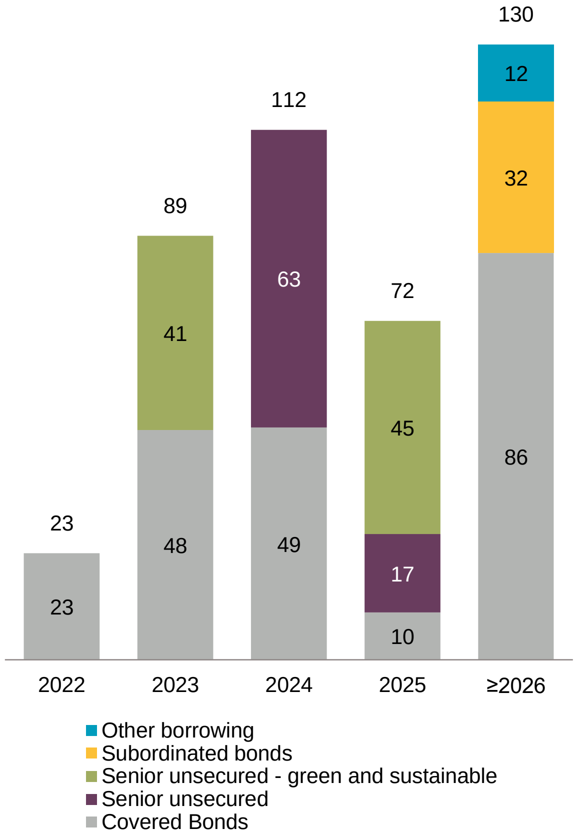
### Highlights

- S&P Global ratings BBB/A-2 with stable outlook confirmed on 13 July 2022
- In June, the Bank signed a new covered bond programme. Rated A by Standard & Poor's, it will permit issuance in foreign currencies, allowing broader market access and investor diversification
- The Bank has a call option on its SEK 750 Tier 2 of 2027 in November 2022 and a January 2023 call on its EUR 300m senior bond maturing in January 2024
- At end of 2Q22, total LCR ratio was 147%, FX LCR was 240% and total NFSR was 118%
- The Bank's MREL requirement is 21% of total risk exposure amount (TREA) and applies from the date of the announcement, 26 April 2022. The Bank will fulfil the MREL requirement from the outset

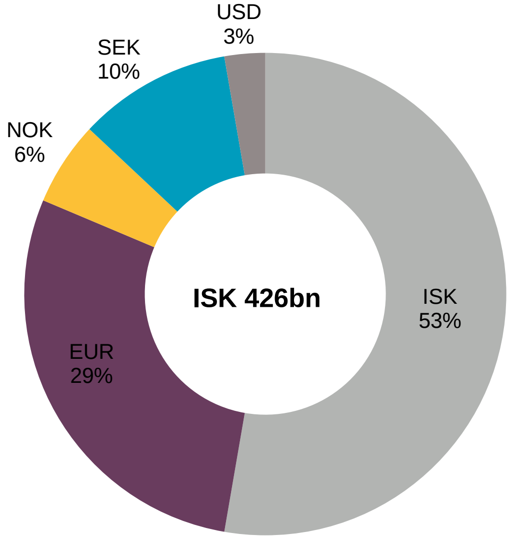
### Sources of borrowings
Development, ISKbn




### Contractual maturity profile of borrowings
ISKbn




### Currency split of borrowings
30.6.22



# Strong capital position and dividend capacity

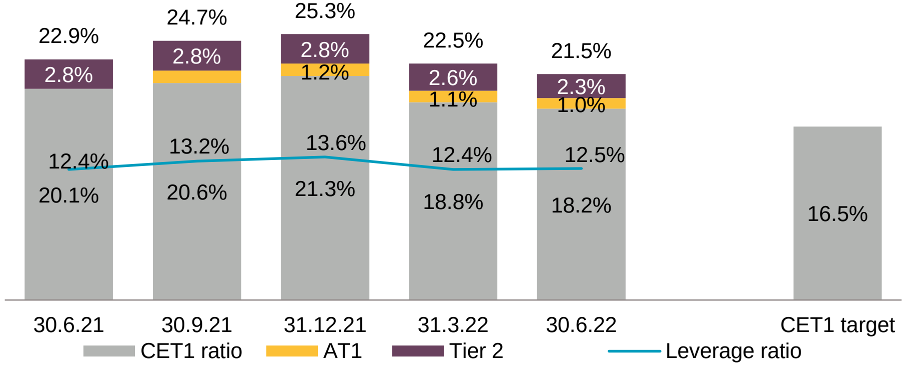
## Opportunity exists to optimise capital composition and to continue consistent dividends

### Highlights

- Current and long-term expected total capital requirements of 17.9% and 19.0% respectively
- Additional AT1 issuance potential of ISK 6-7bn to optimise capital structure
- Increase in REA in 2Q22 due to strong and profitable loan growth in 2Q22. This leads to drop in CET1 ratio and a reduction in excess capital

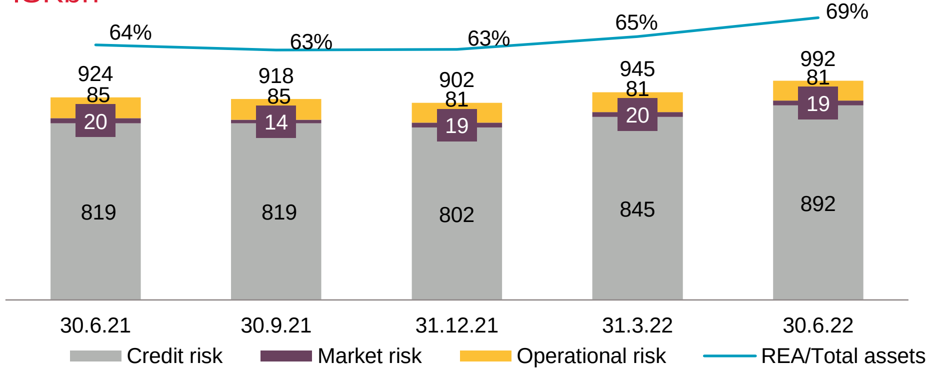
### Capital ratios and leverage ratio

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




### Risk exposure amount (REA)

ISKbn




### Capital distribution plans

- **ISK 30-35bn of excess CET1 capital**
  - Plan to optimise capital structure before year-end 2023
  - Distribution in the form of share buybacks or special dividends, method and timing subject to the market conditions
  - ISK 15bn of capital release planned in the coming months, subject to market conditions

# Q&A

# Appendix I – About Íslandsbanki and additional financial information

# This is Íslandsbanki

Moving Iceland forward by empowering our customers to succeed

## Vision and Values

Vision to be
**#1 for service**

Passion
Professionalism
Collaboration

## The Bank

**FTEs 702** number of FTEs at Íslandsbanki at period end

**12** branches

Listed to Nasdaq Iceland as of June 2021

## Market share[1]

**31%** retail customers

**37%** SMEs

**35%** large companies

## Sustainability 2Q22

Íslandsbanki receives top ESG score (90/100) from Reitun for the second year in a row

The Bank's score for environmental practices has risen by 12.9% year-on-year

Total avoided greenhouse gas emissions in 2021 ~16,800 tCO2e

## Key Figures 2Q22

| | | | |
|---|---|---|---|
| ROE | 11.7% | LCR<br>Group, all currencies | 147% |
| Cost-to-income ratio | 42.7% | NSFR<br>Group, all currencies | 118% |
| CET1 ratio[2] | 18.2% | Leverage ratio[2] | 12.5% |
| Total capital ratio[2] | 21.5% | Total assets | ISK 1,437bn |

## Ratings and certifications

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

EQUAL PAY CERTIFICATE 2018 - 2021

EXEMPLARY IN CORPORATE GOVERNANCE

## Digital milestones 2Q22

New pension platform released, enables self service for pension customers

Corporates can apply for and modify overdraft in app

App available in Polish

1. Based on Gallup surveys regarding primary bank. 12 months rolling average for retail customers, December 2021 survey for SMEs and 2021 average for large companies.

# Financial overview

## Key figures & ratios

| | | **2Q22** | 1Q22 | 4Q21 | 3Q21 | 2Q21 |
|---|---|---|---|---|---|---|
| **PROFITABILITY** | Profit for the period, ISKm | **5,880** | 5,187 | 7,092 | 7,587 | 5,431 |
| | Return on equity | **11.7%** | 10.2% | 14.2% | 15.7% | 11.6% |
| | Net interest margin (of total assets) | **2.9%** | 2.6% | 2.4% | 2.4% | 2.4% |
| | Cost-to-income ratio[1] | **42.7%** | 47.6% | 45.3% | 39.4% | 49.9% |
| | Cost of risk[2] | **(0.20%)** | (0.17%) | (0.23%) | (0.64%) | (0.42%) |

| | | **30.6.22** | 31.3.22 | 31.12.21 | 30.9.21 | 30.6.21 |
|---|---|---|---|---|---|---|
| **BALANCE SHEET** | Loans to customers, ISKm | **1,153,677** | 1,107,893 | 1,086,327 | 1,081,418 | 1,089,723 |
| | Total assets, ISKm | **1,437,253** | 1,446,355 | 1,428,821 | 1,456,372 | 1,446,860 |
| | Risk exposure amount, ISKm | **992,883** | 945,321 | 901,646 | 917,764 | 924,375 |
| | Deposits from customers, ISKm | **756,862** | 761,471 | 744,036 | 754,442 | 765,614 |
| | Customer loans to customer deposits ratio | **152%** | 145% | 146% | 143% | 142% |
| | Non-performing loans (NPL) ratio[3] | **1.8%** | 1.8% | 2.0% | 2.0% | 2.1% |
| **LIQUIDITY** | Net stable funding ratio (NSFR), for all currencies | **118%** | 123% | 122% | 121% | 122% |
| | Liquidity coverage ratio (LCR), for all currencies | **147%** | 195% | 156% | 225% | 187% |
| **CAPITAL** | Total equity, ISKm | **203,662** | 197,201 | 203,710 | 197,381 | 190,355 |
| | CET 1 ratio[4] | **18.2%** | 18.8% | 21.3% | 20.6% | 20.1% |
| | Tier 1 ratio[4] | **19.2%** | 19.9% | 22.5% | 21.8% | 20.1% |
| | Total capital ratio[4] | **21.5%** | 22.5% | 25.3% | 24.7% | 22.9% |
| | Leverage ratio[4] | **12.5%** | 12.4% | 13.6% | 13.2% | 12.4% |

1.Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund – One-off items) / (Total operating income – One-off items). 2. Negative cost of risk means that there is a net release of impairments. 3. Stage 3, loans to customers, gross carrying amount. 4. Including 3Q21 profit for 30.9.21 and 1Q22 profit for 31.3.22.

# Income growth of 16% YoY driven by NII and NFCI

## Robust profitability in 2Q22 built on a solid platform

| Income statement, ISKm | 2Q22 | 2Q21 | Δ% | 1H22 | 1H21 | Δ% | 2021 |
|---|---|---|---|---|---|---|---|
| Net interest income | **10,254** | 8,417 | 22% | **19,463** | 16,607 | 17% | 34,043 |
| Net fee and commission income | **3,434** | 2,907 | 18% | **6,498** | 5,769 | 13% | 12,849 |
| Net financial income (expense) | **208** | 619 | (66%) | **113** | 912 | (88%) | 2,499 |
| Net foreign exchange gain | **75** | 95 | (21%) | **241** | 225 | 7% | 479 |
| Other operating income | **59** | 82 | (28%) | **324** | 204 | 59% | 302 |
| **Total operating income** | **14,030** | 12,120 | 16% | **26,639** | 23,717 | 12% | 50,172 |
| Salaries and related expenses | **(3,396)** | (3,594) | (6%) | **(6,818)** | (7,168) | (5%) | (13,397) |
| Other operating expenses | **(2,597)** | (2,894) | (10%) | **(5,009)** | (5,172) | (3%) | (9,799) |
| **Administrative expenses** | **(5,993)** | (6,488) | (8%) | **(11,827)** | (12,340) | (4%) | (23,196) |
| Contribution to the Depositor's and Investors' Guarantee Fund | 0 | (162) | (100%) | **(165)** | (344) | (52%) | (688) |
| Bank tax | (412) | (451) | (9%) | **(842)** | (861) | (2%) | (1,683) |
| **Total operating expenses** | **(6,405)** | (7,101) | (10%) | **(12,834)** | (13,545) | (5%) | (25,567) |
| Net impairment on financial assets | **575** | 1,140 | (50%) | **1,058** | 622 | 70% | 3,018 |
| **Profit before tax** | **8,200** | 6,159 | 33% | **14,863** | 10,794 | 38% | 27,623 |
| Income tax expense | **(2,331)** | (769) | 203% | **(3,794)** | (1,805) | 110% | (5,119) |
| **Profit for the period from continuing operations** | **5,869** | 5,390 | 9% | **11,069** | 8,989 | 23% | 22,504 |
| Discontinued operations held for sale, net of income tax | **11** | 41 | (73%) | **(2)** | 57 | (104%) | 1,221 |
| **Profit for the period** | **5,880** | 5,431 | 8% | **11,067** | 9,046 | 22% | 23,725 |

**Key ratios**

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Net Interest Margin (NIM) | **2.9%** | 2.4% | | **2.7%** | 2.4% | | 2.4% |
| Cost-to-income ratio (C/I) | **42.7%** | 49.9% | | **45.0%** | 50.6% | | 46.2% |
| Return on Equity (ROE) | **11.7%** | 11.6% | | **10.9%** | 9.7% | | 12.3% |
| Cost of risk (COR) | **(0.20%)** | (0.42%) | | **(0.19%)** | 0.12% | | (0.28%) |

# Balance sheet reflects a balanced loan and funding profile

## Conservative mix of assets and stable funding

### Assets

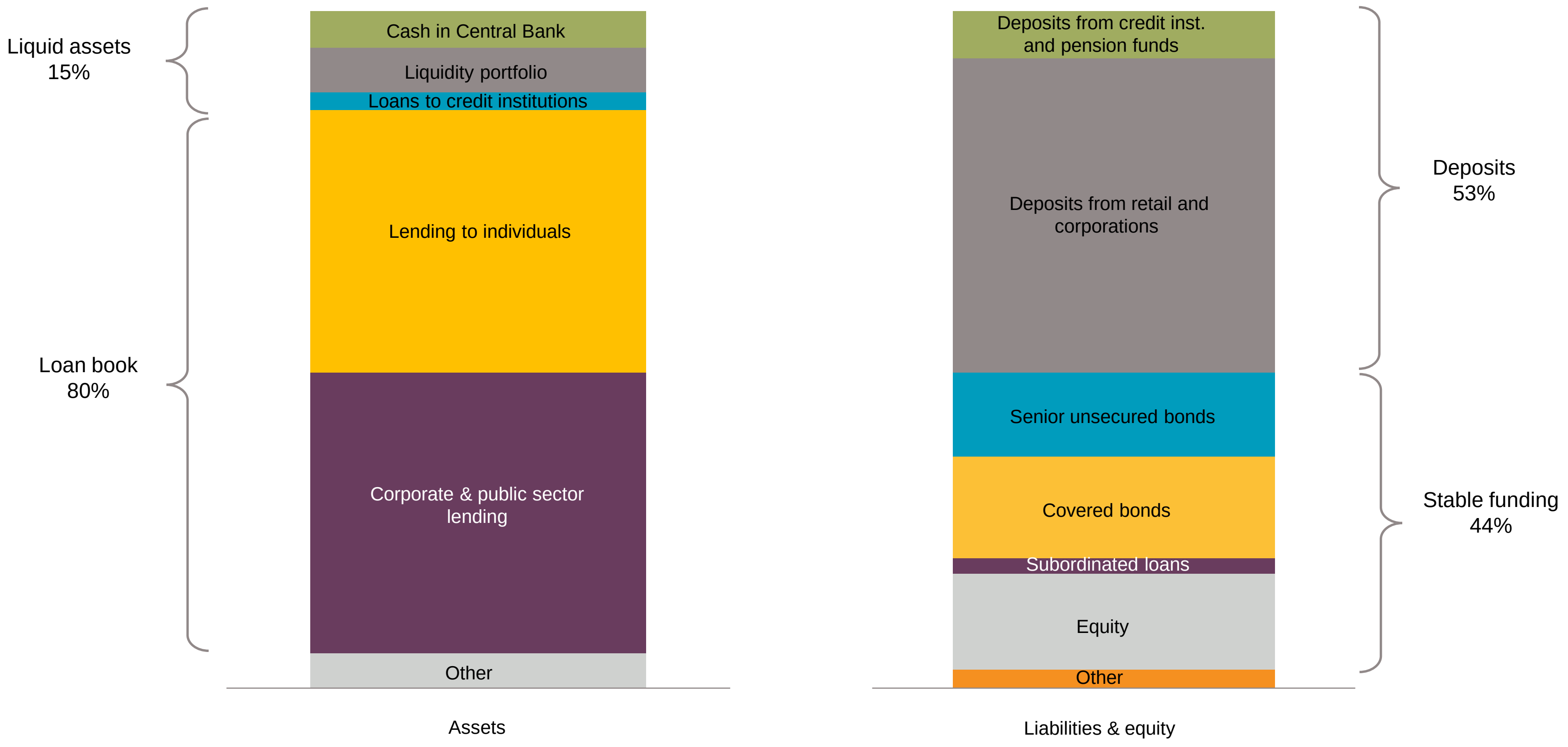
- Vast majority of assets consist of lending to both retail and corporates
- Strong liquidity portfolio is a consistent factor in balance sheet management
- Very limited exposure to non-liquid or non-lending assets

### Liabilities

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

### Simplified balance sheet structure

30.6.2022, ISK 1,437bn



# Growth in loans to customers continues

## Steady mortgage growth supported by a strong capital base

| Assets, ISKm | 30.6.22 | 31.3.22 | Δ | Δ% | 31.12.21 | Δ | Δ% |
|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank | **77,884** | 77,799 | 85 | 0% | 113,667 | (35,783) | (31%) |
| Loans to credit institutions | **37,226** | 73,220 | (35,994) | (49%) | 43,988 | (6,762) | (15%) |
| Bonds and debt instruments | **108,477** | 130,700 | (22,223) | (17%) | 132,289 | (23,812) | (18%) |
| Derivatives | **6,193** | 4,245 | 1,948 | 46% | 2,445 | 3,748 | 153% |
| Loans to customers | **1,153,677** | 1,107,893 | 45,784 | 4% | 1,086,327 | 67,350 | 6% |
| Shares and equity instruments | **25,789** | 28,655 | (2,866) | (10%) | 31,677 | (5,888) | (19%) |
| Investment in associates | **3,836** | 767 | 3,069 | 400% | 939 | 2,897 | 309% |
| Property and equipment | **6,846** | 6,911 | (65) | (1%) | 7,010 | (164) | (2%) |
| Intangible assets | **3,304** | 3,327 | (23) | (1%) | 3,351 | (47) | (1%) |
| Other assets | **12,126** | 11,170 | 956 | 9% | 5,784 | 6,342 | 110% |
| Non-current assets and disposal groups held for sale | **1,895** | 1,668 | 227 | 14% | 1,344 | 551 | 41% |
| **Total Assets** | **1,437,253** | 1,446,355 | -9,102 | (1%) | 1,428,821 | 8,432 | 1% |
| **Key ratios** | | | | | | | |
| Risk Exposure Amount (REA) | **992,883** | 945,321 | 47,562 | 5% | 901,646 | 91,237 | 10% |
| Non-performing loans (NPL) ratio[1] | **1.8%** | 1.8% | | | 2.0% | | |

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

# Diversified funding base

## Deposits are the largest source of funding

| Liabilities & Equity, ISKm | 30.6.22 | 31.3.22 | Δ | Δ% | 31.12.21 | Δ | Δ% |
|---|---|---|---|---|---|---|---|
| Deposits from Central Bank and credit institutions | **11,437** | 10,949 | 488 | 4% | 13,384 | (1,947) | (15%) |
| Deposits from customers | **756,862** | 761,471 | (4,609) | (1%) | 744,036 | 12,826 | 2% |
| Derivative instruments and short positions | **11,410** | 11,013 | 397 | 4% | 9,467 | 1,943 | 21% |
| Debt issued and other borrowed funds | **393,754** | 406,845 | (13,091) | (3%) | 402,226 | (8,472) | (2%) |
| Subordinated loans | **32,181** | 34,139 | (1,958) | (6%) | 35,762 | (3,581) | (10%) |
| Tax liabilities | **8,498** | 6,980 | 1,518 | 22% | 6,432 | 2,066 | 32% |
| Other liabilities | **18,498** | 16,802 | 1,696 | 10% | 12,848 | 5,650 | 44% |
| Non-current liabilities and disposal groups held for sale | **951** | 955 | (4) | (0%) | 956 | (5) | (1%) |
| Total Liabilities | **1,233,591** | 1,249,154 | (15,563) | (1%) | 1,225,111 | 8,480 | 1% |
| Total Equity | **203,662** | 197,201 | 6,461 | 3% | 203,710 | (48) | (0%) |
| **Total Liabilities and Equity** | **1,437,253** | 1,446,355 | (9,102) | (1%) | 1,428,821 | 8,432 | 1% |

| Key ratios | 30.6.22 | 31.3.22 | 31.12.21 |
|---|---|---|---|
| Customer loans to customer deposits ratio | **152%** | 145% | 146% |
| REA/total assets | **69.1%** | 65.4% | 63.1% |
| Net stable funding ratio (NSFR) | **118%** | 123% | 122% |
| Liquidity coverage ratio (LCR) | **147%** | 195% | 156% |
| Total capital ratio[1] | **21.5%** | 22.5% | 25.3% |
| Tier 1 capital ratio[1] | **19.2%** | 19.9% | 22.5% |
| Leverage ratio[1] | **12.5%** | 12.4% | 13.6% |

1. Including first quarter profit for 31.3.22.

# Appendix II – Icelandic economy update

October 2022

# Moderate GDP growth on the cards after an impressive surge

## Exports take over from demand as the main driver

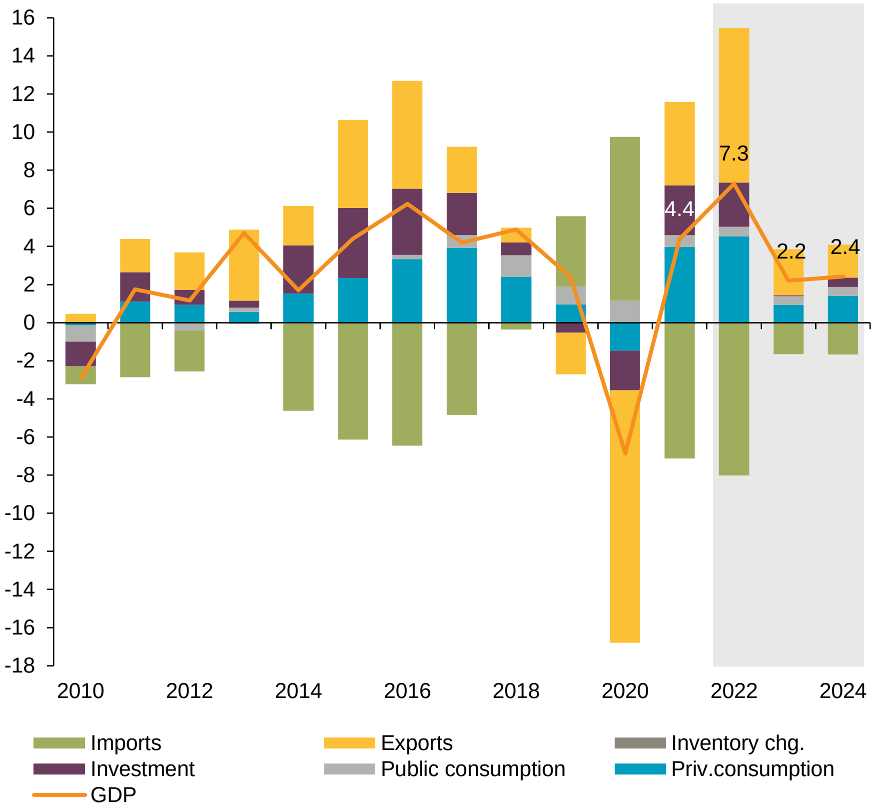


### Highlights

- After a 6.9% contraction in 2020, the Icelandic economy picked up strongly in 2021, with GDP growth measuring 4.4%
- Growth was driven mainly by domestic demand. Exports also picked up strongly, albeit outpaced by import growth
- ISB Research (forecast published in Sept-2022) expects GDP growth at 7.3% in 2022, the fastest growth rate in 15 years
- Exports take over from domestic demand as the mainstay of growth, with a rapid recovery of tourism and an increase in other exports. Growing consumption and investment also fuel GDP growth in 2022
- For 2023, GDP growth is forecast to measure 2.2%, with exports once again the main driver, although growth in exports as well as domestic demand will ease year-on-year
- For 2024, GDP growth is projected at 2.4%. By then, export growth will have eased and consumption and investment will have started picking up again
- External risk factors include the war in Ukraine, the effects of high inflation and rising interest rates on trading partner demand, and the ambiguous outlook for China

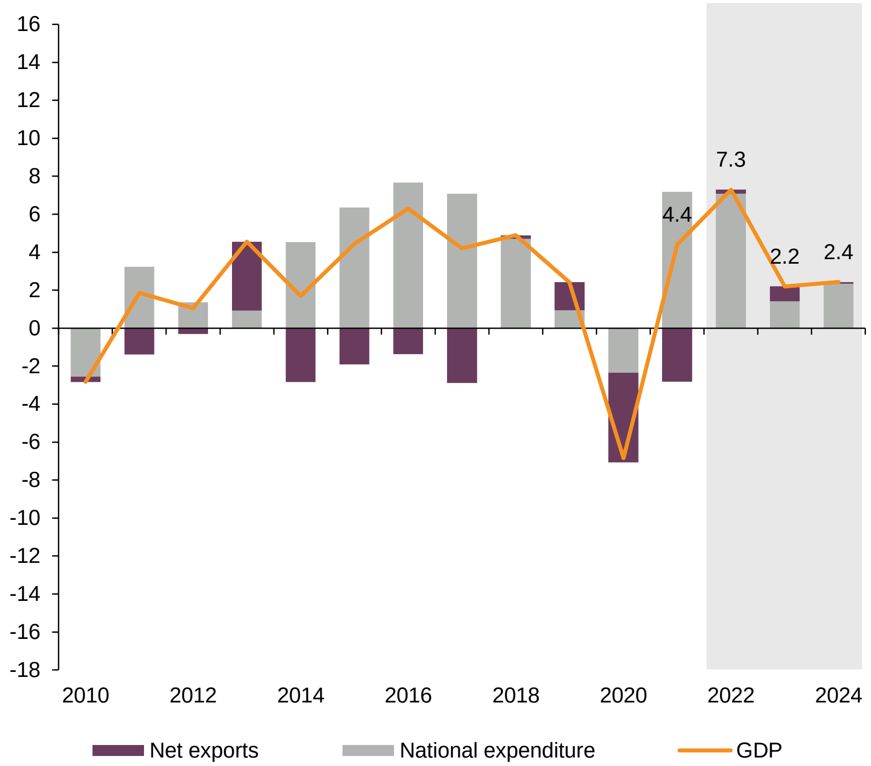
### GDP and contribution of its subcomponents

Volume change from prior year (%)




### GDP, domestic demand, and external trade

Volume change from prior year (%)




Sources: Statistics Iceland, ÍSB Research.

# Tourism industry bouncing back after the pandemic

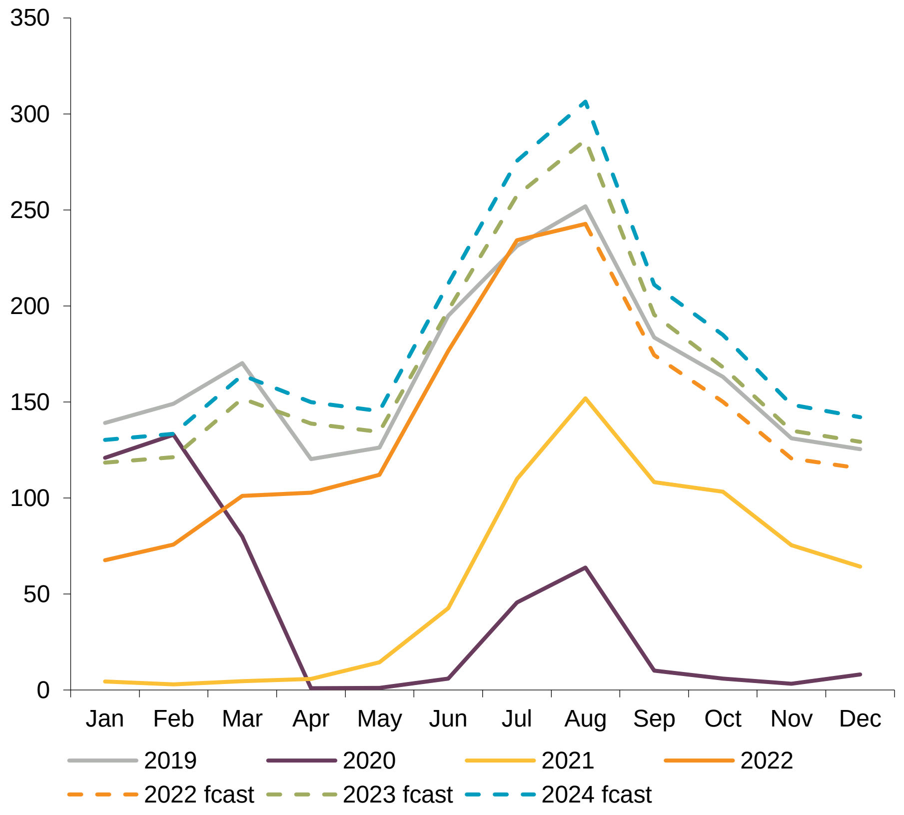
## 1.7 million tourists expected to visit Iceland in 2022, followed by 2 million in 2023

### Highlights

- After two punishing years dominated by the pandemic, prospects for the tourism sector have improved rapidly
- Just over 1.1 million tourists visited Iceland in the first eight months of 2022, the largest total for this period since 2019
- The outlook for coming quarters is quite good despite significant near-term uncertainty about matters in the UK and mainland Europe
- ISB Research expects 1.7 million tourists this year, about the same number as in 2016
- Tourist numbers are assumed to rise to 2.0 million in 2023 and 2.2 million in 2024
- The slower increase later in the horizon is due in part to the ambiguous economic outlook on both sides of the Atlantic, as well as to the higher real exchange rate
- The total head count is not the only determinant of revenue generation, either: the length of each visitor's stay and the amount each spends on goods and services while in the country are also important factors which fortunately appear to be on a positive trend in Iceland

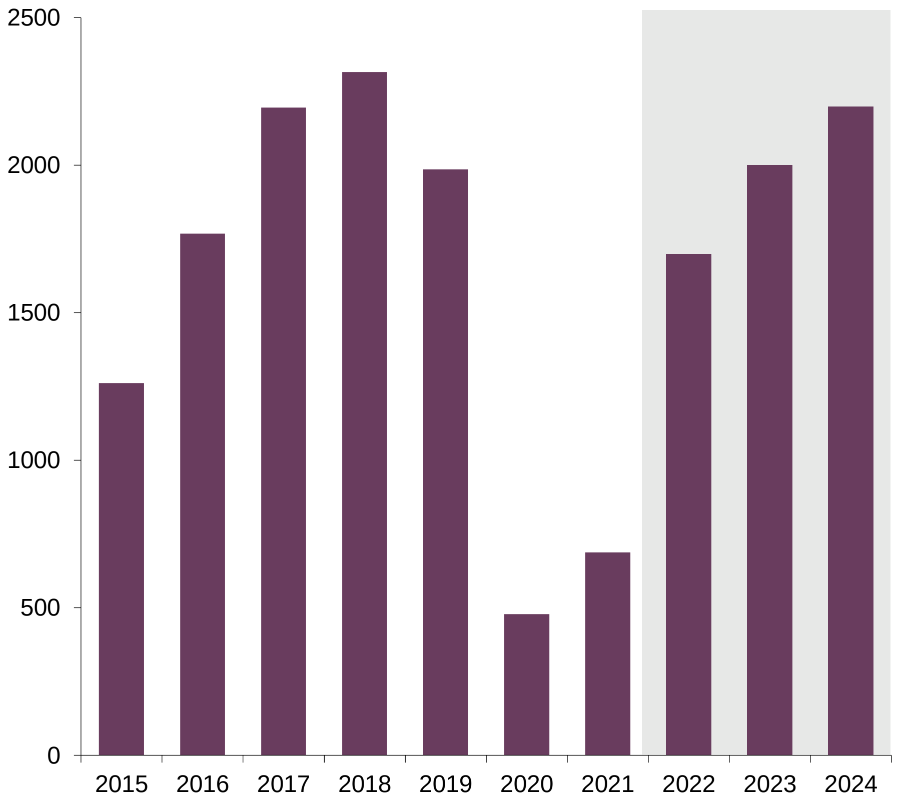
### Number of foreign tourists, by month

thousands




### Number of foreign tourists, by year

thousands




Sources: Icelandic Tourist Board, ÍSB Research.

# Current account flips from deficit to surplus

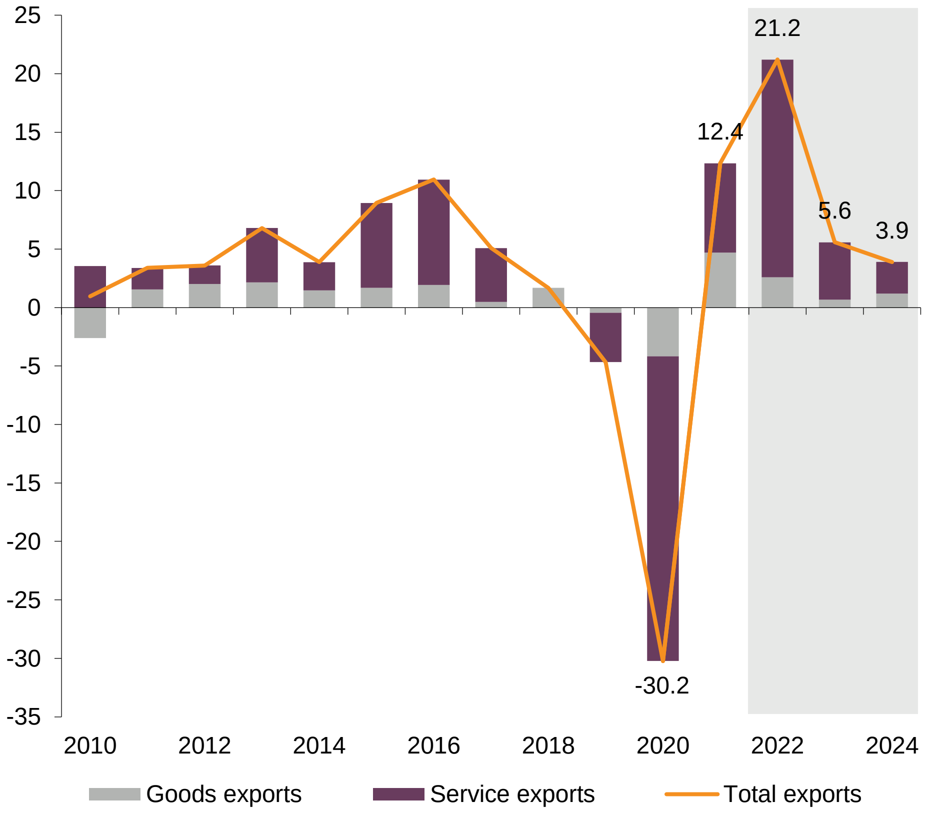
## Export growth and reduced demand growth push the current account back into positive territory

### Highlights

- The return of tourism as Iceland's key export sector explains most of the 21% export growth forecasted for 2022 as well as the more moderate growth expected in 2023-2024
- Furthermore, the outlook is for modest growth in goods exports. This is due to booming exports of capelin, farmed fish, and silicon metals as well as a modest increase in exports of aluminium and manufactured goods, offset by a contraction in exports of groundfish, particularly cod
- Last year's ISK 52bn (1.6% of GDP) current account deficit reflects the fact that domestic demand picked up faster than exports in the wake of the pandemic
- Following a sizeable deficit in H1 2022, the current account is expected to return to surplus in H2
- The current account surplus is expected to measure 1% of GDP in 2023 and 2.4% of GDP in 2024
- Iceland's net external assets currently total just under ¼ of GDP. Headwinds in global securities markets have adversely impacted the external asset position but a recovery is likely in the medium term

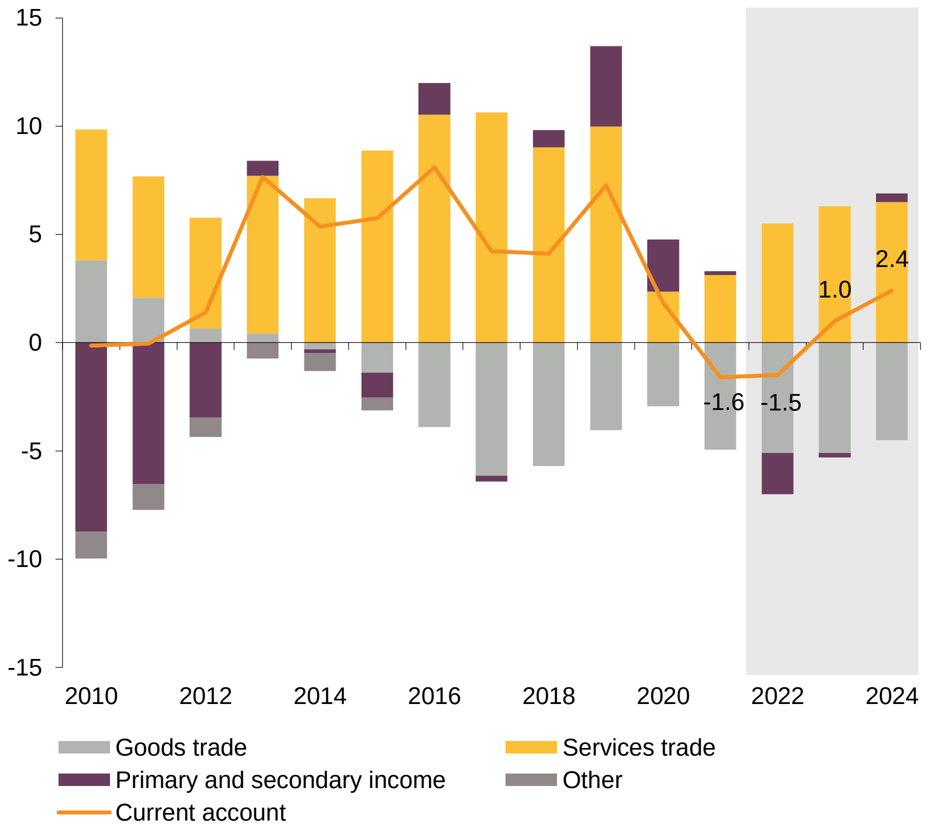
### Exports and contribution from subcomponents

% change




### Current account balance and GDP growth

% of GDP and % change YoY



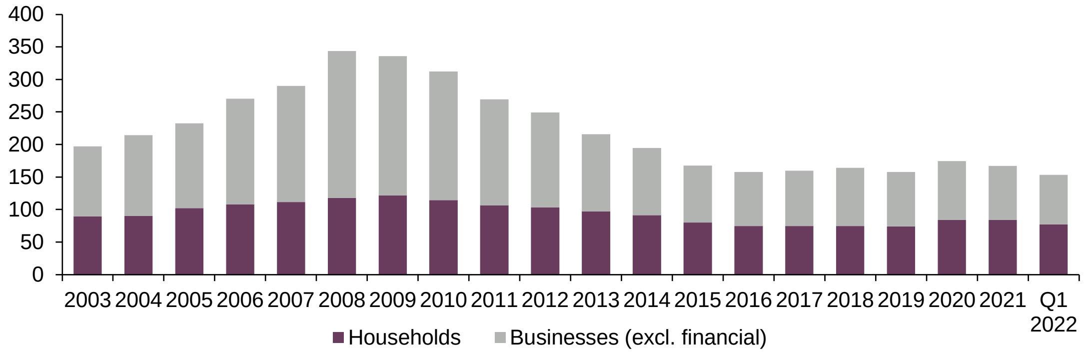

Sources: Statistics Icelandic, Central Bank of Iceland, ÍSB Research.

# Domestic balance sheets still healthy

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

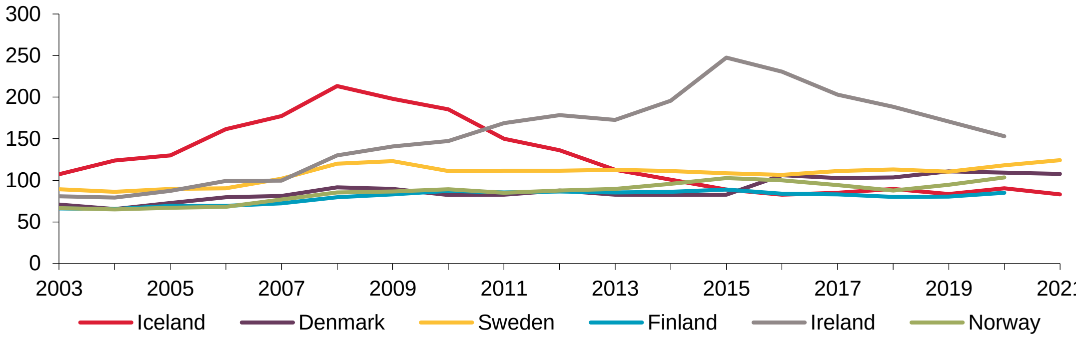
### Private sector debt

% of GDP



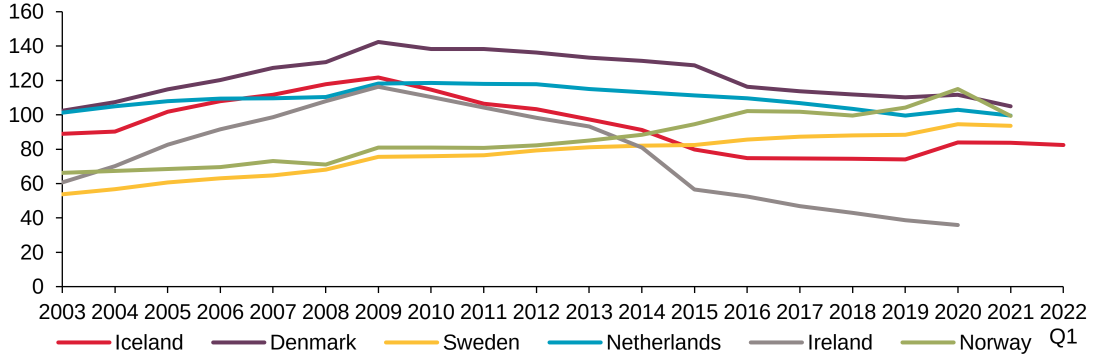

### Corporate debt

% of GDP



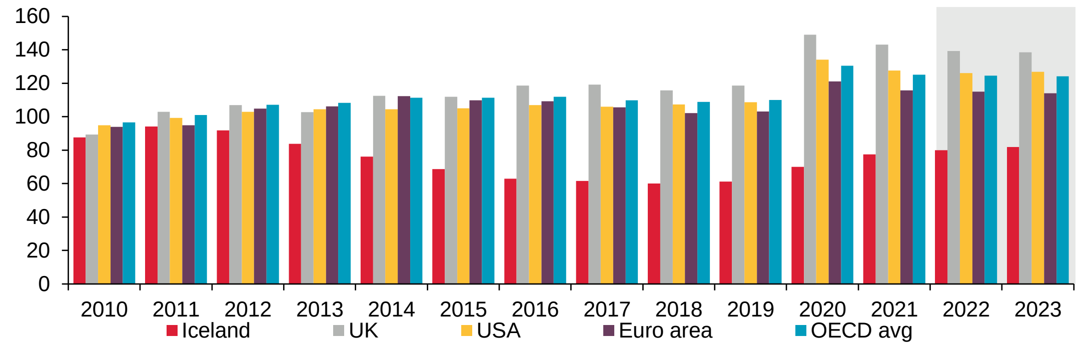

### Household debt

% of GDP




### General government gross financial liabilities

% of GDP




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

# Investment growth strong in 2022 but slower further ahead

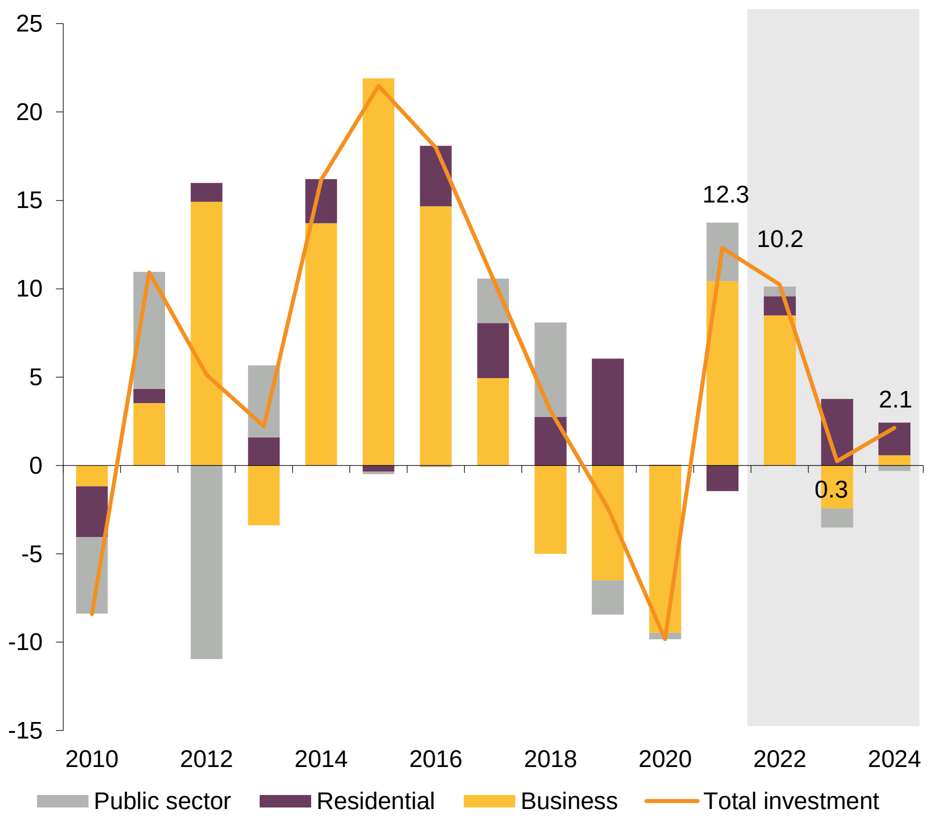
## Residential investment to take over from business investment as the driver of growth

### Highlights

- After a two-year contraction, investment spiked in 2021, with growth measuring just over 12%, its fastest pace in five years
- Business investment and public investment grew markedly, while residential investment contracted by over 5%
- Business investment grew by 12% in H1, and indicators imply that the trend will continue through the year-end. Residential investment is also picking up after contracting in H1, and growth is expected to be positive for the year as a whole.
- In 2023, residential investment will likely be the sole driver of growth, as business investment looks set to contract because of rising interest rates and bleaker expectations about firms' operating environment
- 2024 will probably see moderate growth in private sector investment coupled with a marginal contraction in public investment
- ISB Research forecasts that total investment will grow by over 10% in 2022, remain virtually flat in 2023, and grow by just over 2% in 2024.
- The investment-to-GDP ratio will therefore taper off gradually, although investment will be reasonably strong in historical context

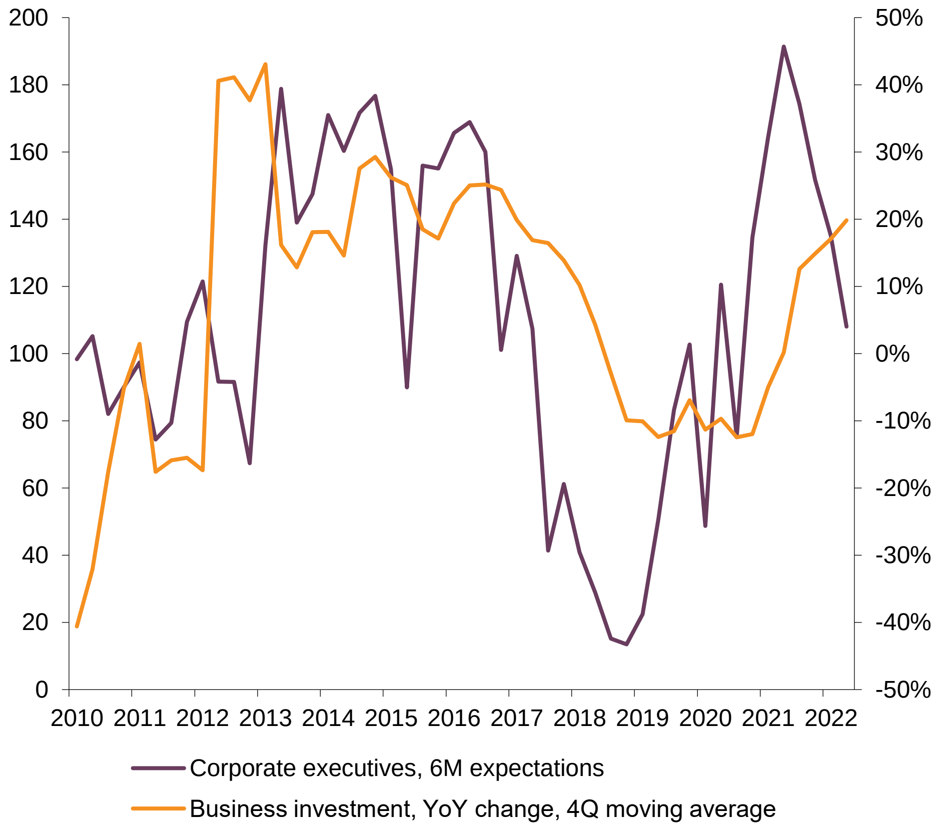
### Investment, real change, and contribution of subcomponents

%




### Executives' expectations and business investment

Index value (left) and % change year-on-year (right)




Source: Statistics Iceland, Gallup.

# Unemployment back to pre-pandemic level

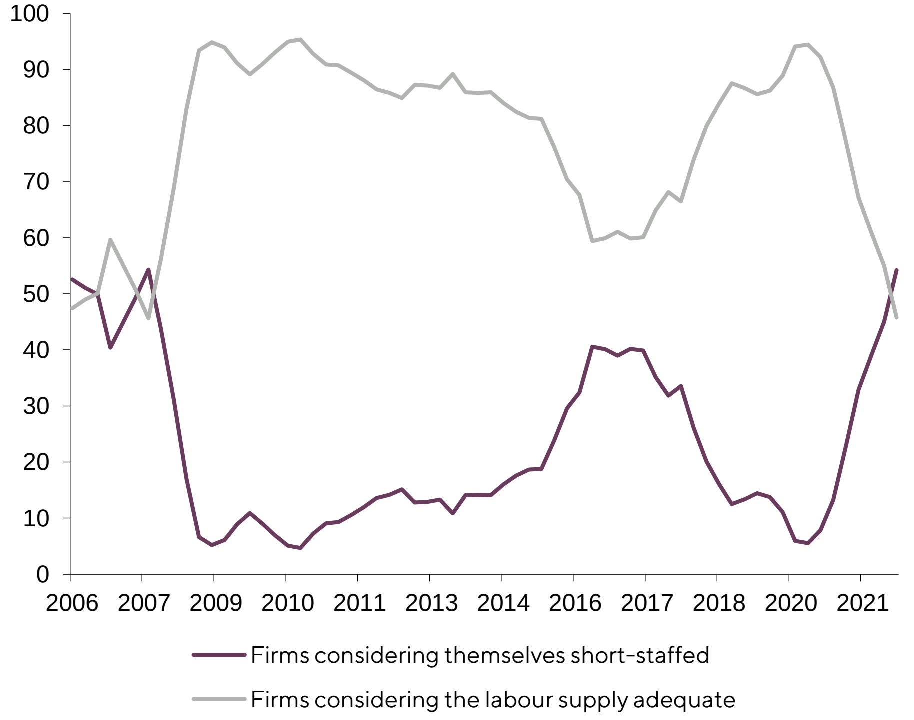
## Worker shortage at its second-highest ever

### Highlights

- Unemployment has fallen swiftly after peaking in January 2021as the relatively swift economic recovery in 2021 has fostered job growth
- Registered unemployment measures 3.1% in August 2022 and is now roughly where it was before airline WOW AIR folded in early 2019
- ISB Research forecasts average year-2022 unemployment at 3.8%
- According to a recent Gallup survey, 54% of company executives consider themselves short-staffed
- Construction and tourism companies in particular envision adding on staff
- As foreign workers have been prominent in these sectors, labour importation is likely to increase markedly this year
- Unemployment is already at its historical average, and we expect it to remain broadly at that level throughout the forecast horizon. We forecast average unemployment at 3.2% in 2023 and 3.6% in 2024

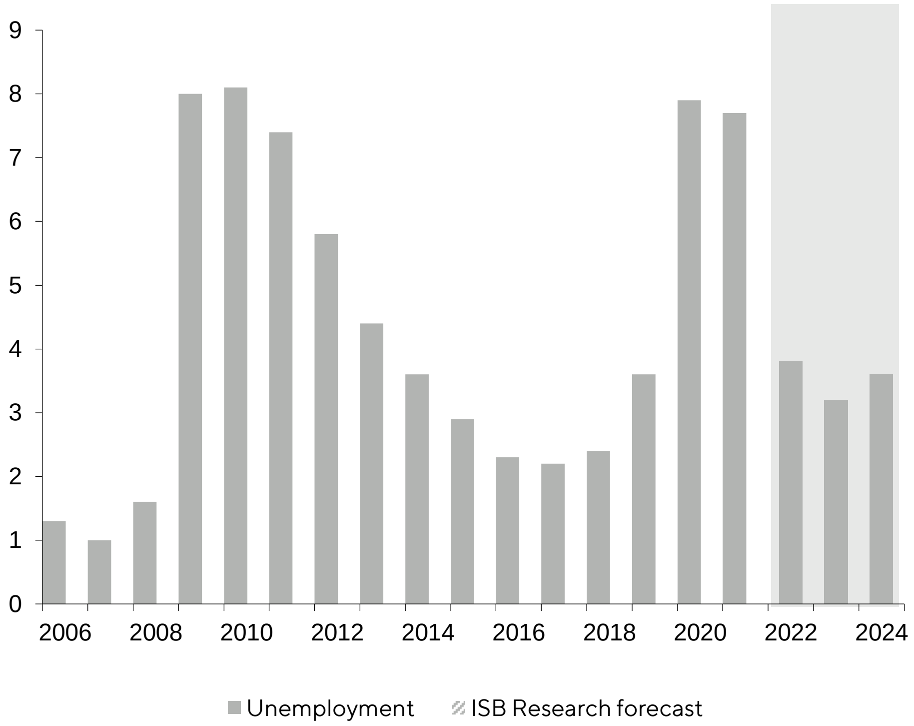
### Labour supply according to corporate executives

%




### Unemployment[1]

% of workforce, annual average






1. Excluding recipients of part-time unemployment benefits. Source: Statistics Iceland, The Central Bank of Iceland, Gallup.

# Private consumption growth eases after rising steeply

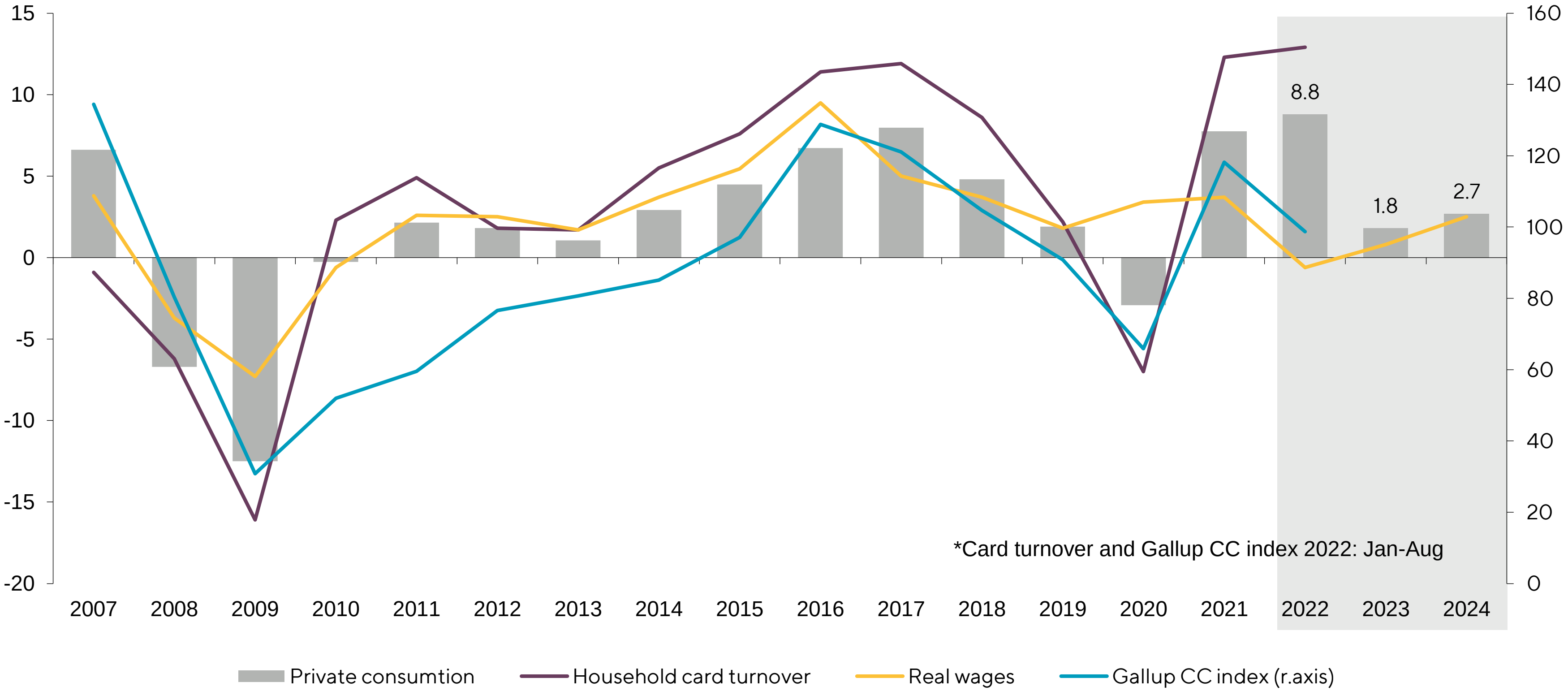
## Erosion of real wages will cut a hefty slice out of private consumption growth in the near term

### Highlights

- Private consumption has rebounded strongly after plummetng at the beginning of the pandemic. In 2021 it grew by 7.7% YoY in real terms and was above 2019 level
- In H1/2022 private consumption grew by an even more rapid 11%, including 13.5% in Q2, the swiftest pace seen in 17 years
- Payment card turnover for July and August suggest robust growth in Q3 as well. As yet, there are no signs that erosion of real wages has affected private consumption growth
- Real wages have indeed begun to deteriorate. In July, they fell YoY for the second month in a row, after a continuous growth spurt dating back to 2010
- This trend is likely to continue in the near term – or at least until inflation truly loses steam. We forecast the real wages will deteriorate by 0.6% in 2022, but then grow by 1.0% in 2023 and 2.5% in 2024
- Given how strongly private consumption has grown in the recent term, a slowdown is inevitable, and we expect it to start as soon as Q4/2022
- We project year-2022 private consumption growth at 8.8%. For the next year, we expect a growth rate of 1.8% and 2.7% in 2024 as inflation eases and real wage growth gains pace.

**Private consumption and related indicators***

% change year-on-year (left) and index value (right)

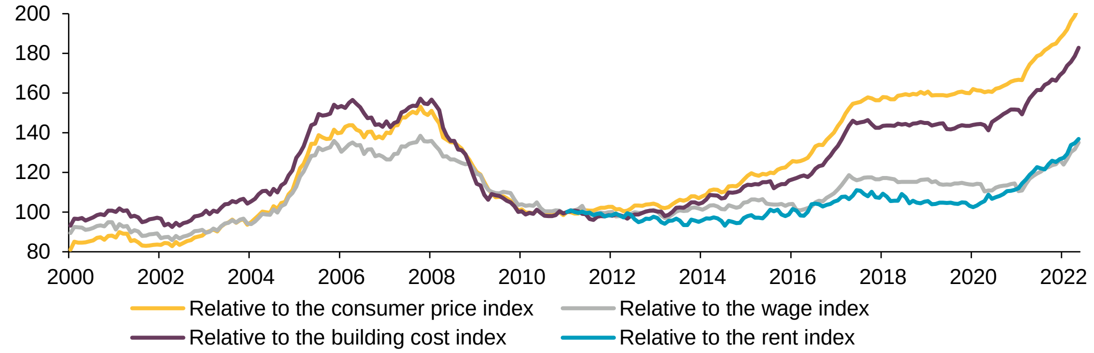



Sources: Central Bank of Iceland, Gallup, Statistics Iceland, ÍSB Research.

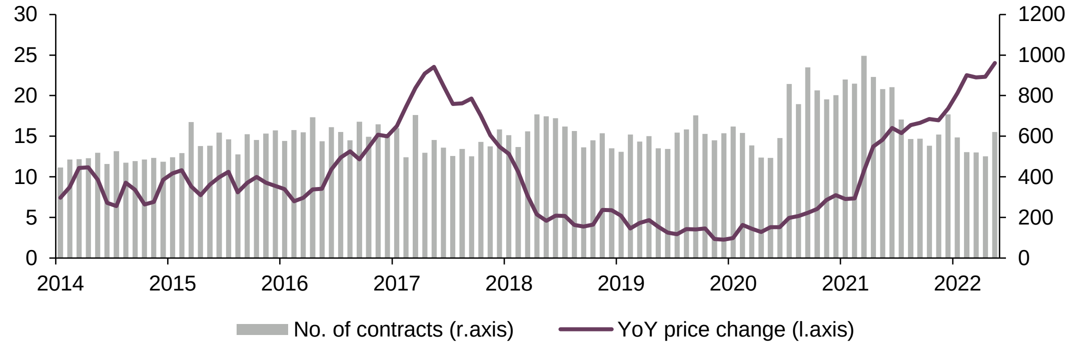
# Real estate markets still buoyant

## Commercial property prices rising again while residential house price rises have gained steam

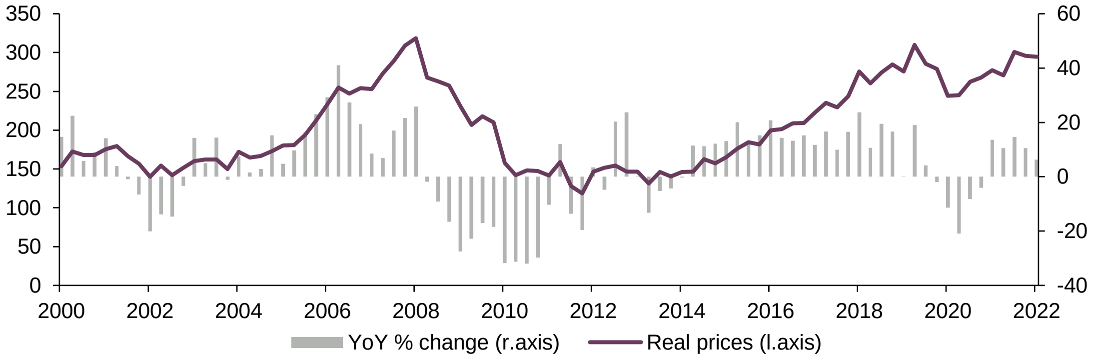
### Capital area house prices relative to macroeconomic fundamentals
Index, January 2011=100



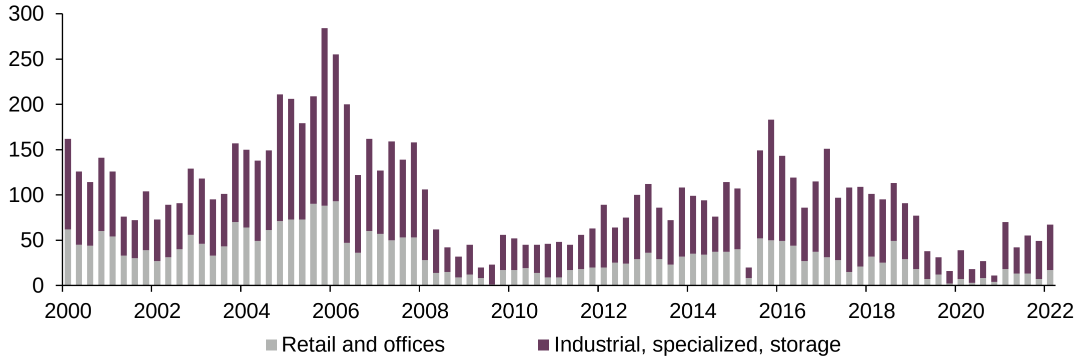

### Residential house prices and turnover in greater Reykjavik
% change (l.axis) and number (r.axis)




### Commercial property real prices in greater Reykjavik
Index, 1995=100 (l.axis) and % change (r.axis)




### Commercial real estate market activity
No. of registered purchase agreements




Source: The Central Bank of Iceland.

# Inflation has peaked

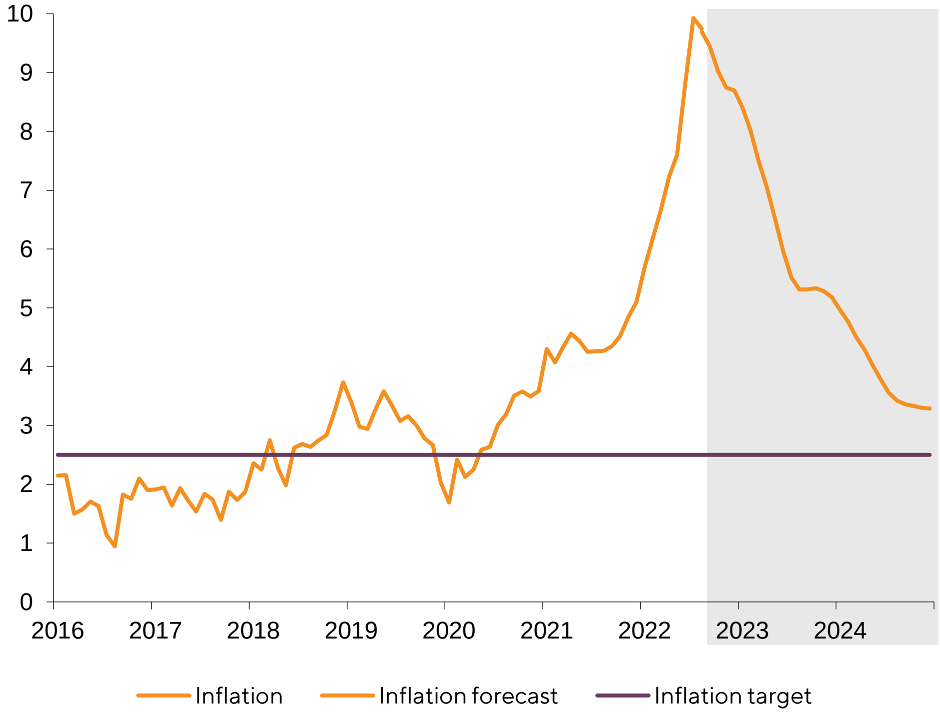
## Inflation set to subside rather quickly in the coming term

### Highlights

- Inflation has risen sharply in the recent term. It peaked in July at 9.9%, its highest in nearly 13 years
- Inflation eased to 9.7% in August and looks set to keep falling. ISB Research expect it to fall rather quickly in the near future
- The main reasons inflation is likely to fall in the near future are that housing market has started cooling rather quickly and imported inflation looks set to be somewhat lower
- There is long road ahead, and considerable ground to cover before it reaches the CBI's 2.5% target
- ISB Research expect inflation to average 8.1% in 2022, 6.3% in 2023, and 3.9% in 2024. Thus it will not align with the target during the forecast horizon
- The main assumptions underlying our forecast are a calm housing market, a slowdown in imported inflation, and an ISK appreciation strong enough to contain import prices
- A key uncertainty in our forecast is the upcoming round of wage negotiations

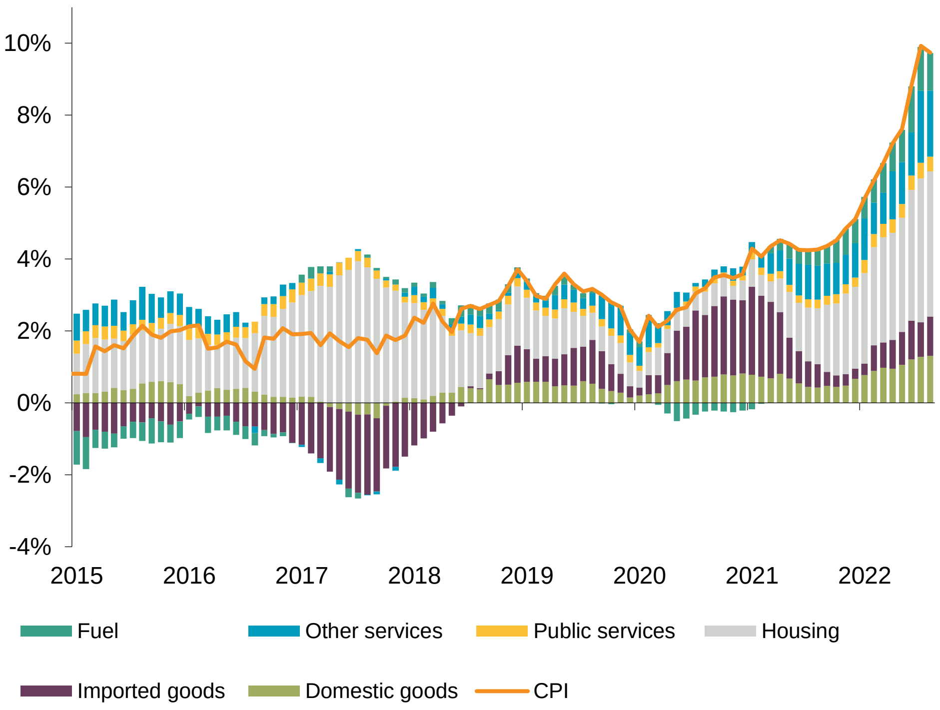
### Inflation and the CBI inflation target

%




### Inflation by contribution of main categories

%




Sources: Statistics Iceland, ÍSB Research.

# Monetary tightening phase probably well advanced

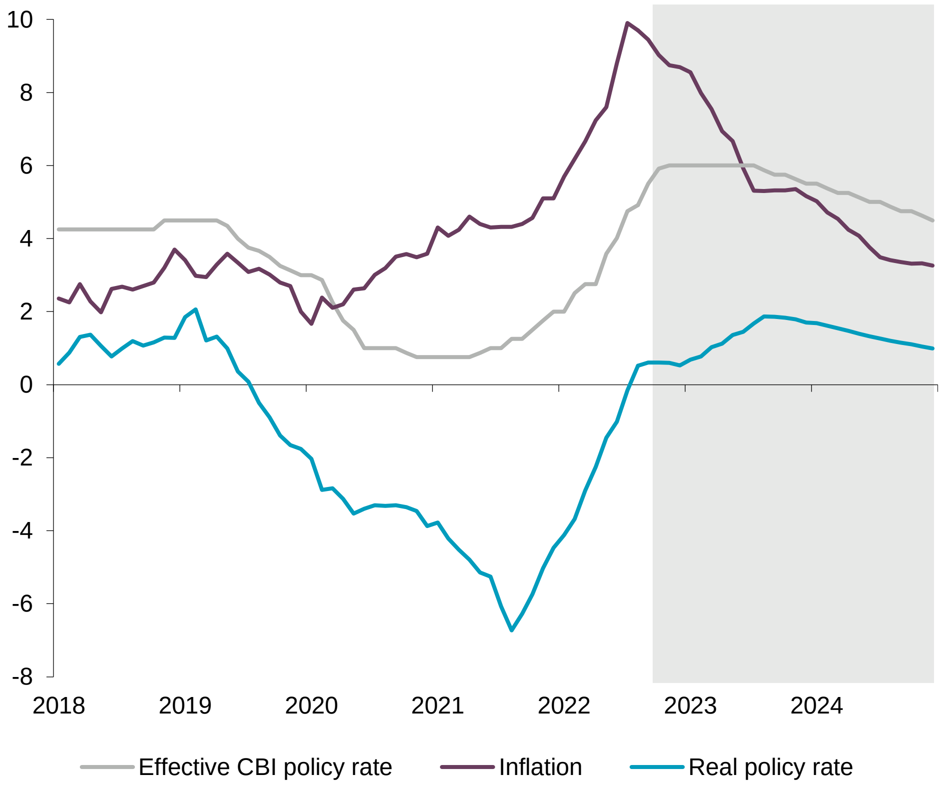
## Gradual easing further ahead; equilibrium rate in sight by the end of the horizon

### Highlights

- The CBI began raising interest rates in spring 2021, in response to the worsening inflation outlook and improving economic outlook. The policy rate is now 5.5%, after being raised by 3.5 percentage points in 2022 to date
- The real policy rate is still low by all measures, however, and negative by some of them
- Further rate hikes are expected in Q4 2022, so as to rein inflation in, keep inflation expectations under wraps, and push the real policy rate higher
- Inflation and inflation expectations have eased since the CBI's last interest rate decision, however
- ISB Research predicts that the policy rate will peak at 6% by end-2022 before declining gradually from 2H2023 onwards
- Long term nominal rates are likely to remain elevated during the policy rate hike cycle, then decrease moderately
- Long term real rates, currently just under the 2% mark, are expected to decline gradually as the economy cools and inflation subsides

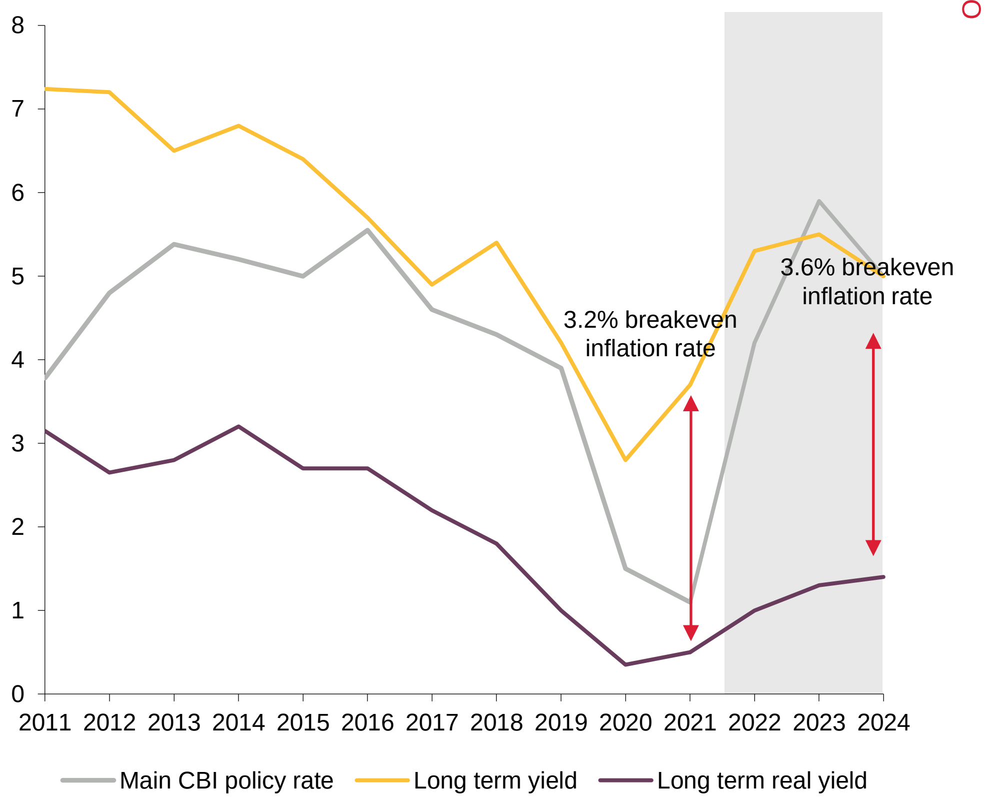
### Policy rate and inflation

%, Real policy rate in terms of average expected policy rate and inflation over the coming 12 months




### Interest rates

%




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

# ISK set to strengthen further in the coming term

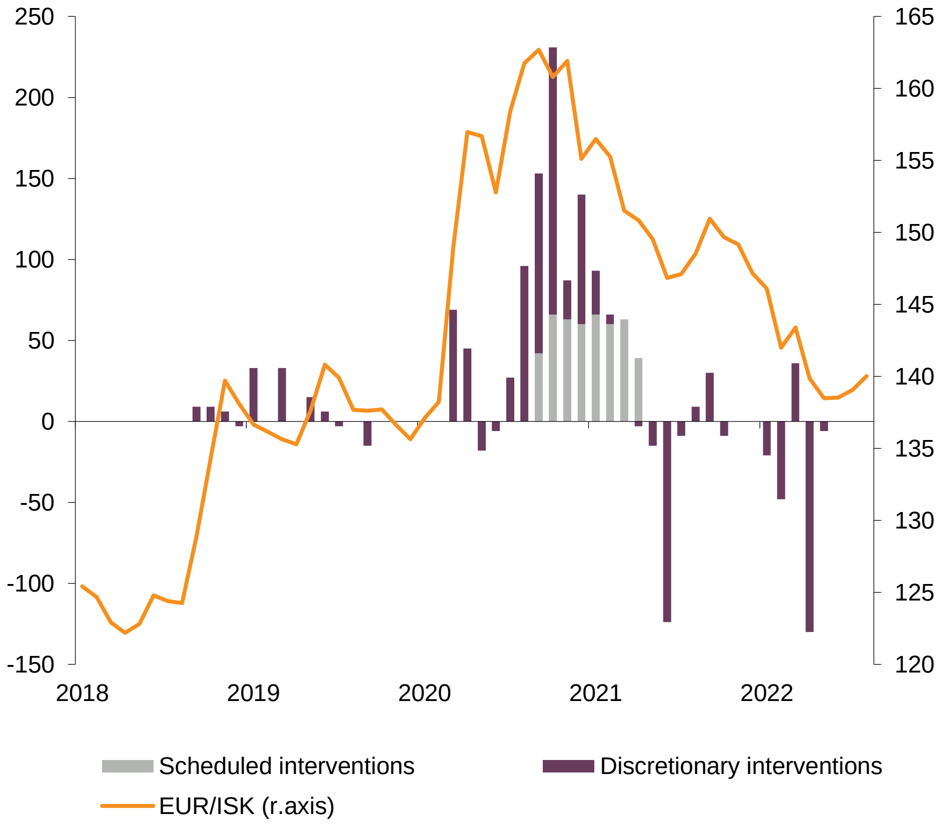
## More favourable CA balance and investment inflows offset pension funds' foreign investments

### Highlights

- Following nearly 3% appreciation in 2021, the ISK continued to strengthen in trade-weighted terms by just over 7% over the first five months of 2022
- However, in June through August it depreciated by 5%
- Increased position-taking with the ISK via forward contracts probably played a role in the appreciation early in the year despite the hefty current account deficit
- Consequently, part of the appreciation that would otherwise accompany FX inflows later this year has already materialised
- The near-term outlook for the current account has dimmed somewhat recently and the tailwinds supporting the ISK will probably be weaker in the coming term than previously anticipated
- Even so, a current account surplus is in the cards further ahead and a positive interest rate differential, strong external position, relatively favourable growth prospects, and low non-residents' securities holdings should also support the ISK in the medium term
- ISB Research forecasts that the ISK will be some 6% stronger at the end of the forecast horizon than at end-August 2022. The real exchange rate in terms of relative consumer prices will then be broadly as in 2018-2019

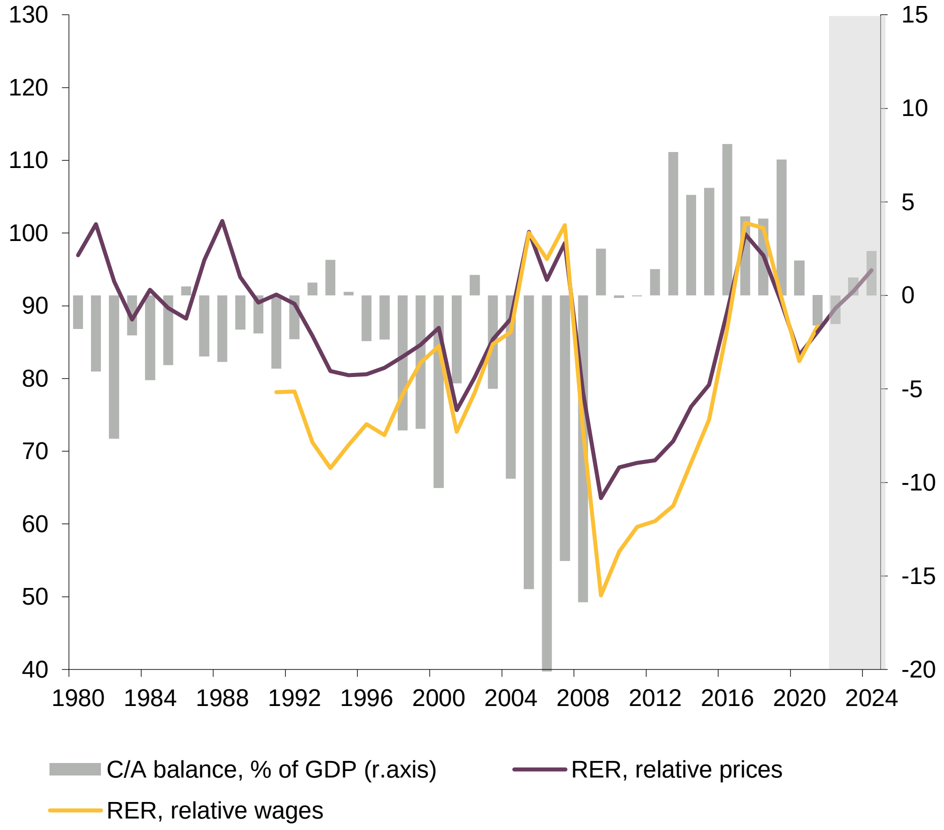
### ISK exchange rate and CBI FX market intervention

EUR m (left) and EURISK (right)




### Real exchange rate and current account balance

Index and % of GDP

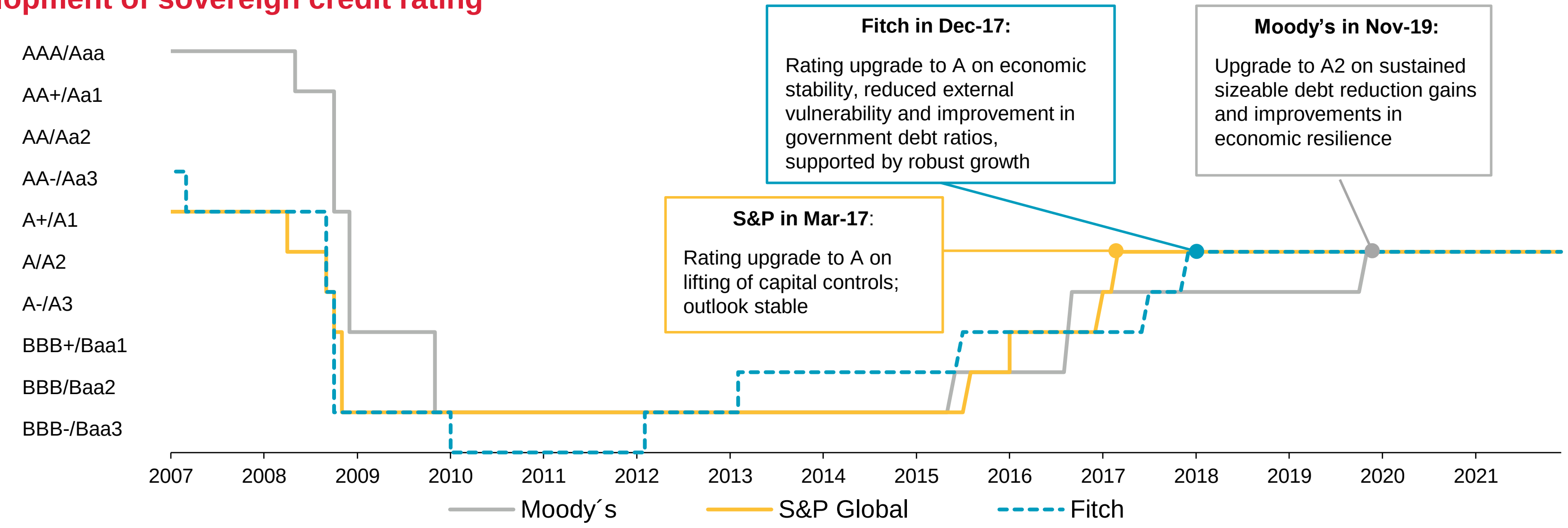



Source: Statistics Iceland, The Central Bank of Iceland, ISB Research.

# Iceland's credit rating has remained at A

## Rating companies acknowledge the flexibility of the economy and resilience to the pandemic shock

### Development of sovereign credit rating




**MOODY'S IN AUGUST 2021**

- "The credit profile of Iceland is supported by its wealthy and flexible economy with favourable demographics that support its long-term growth prospects. Current-account surpluses have contributed to a net external creditor position and large foreign-currency reserves."
- "The credit profile is mainly constrained by the economy's small size and concentration in a limited number of sectors, which increase its vulnerability to shocks and cause volatility in growth."

**FITCH IN APRIL 2022**

- Rating affirmed at A with a stable outlook
- "Iceland's 'A' rating is driven by its very high income per capita, very strong governance, human development and doing business indicators that are more consistent with those of 'AAA' and 'AA' rated countries"
- "The revision of the Outlook to Stable reflects the resilience shown by the Icelandic economy to the pandemic shock and Fitch Ratings' expectation of a sustained growth recovery, which should facilitate a fiscal deficit and debt reduction over time."

**S&P IN MAY 2022**

- "The stable outlook indicates S&P's expectation that Iceland's economy will continue to recover and remain relatively unaffected by the war in Ukraine."
- "The agency believes fiscal deficits will continue to decrease over the next few years, stabilizing the debt to GDP ratio net of liquid assets."
- "At the same time, ample foreign reserves will enable the CBI to deal with external pressures or exchange-rate volatility, should they occur."

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

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