Q2 results 2023

Investor presentation
26 July 2023

Arion Bank

Key results in Q2

Arion Bank continues momentum with strong quarter

- 15.5% ROE in the quarter and 14.5% YTD
- Key medium-term targets exceeded
- Robust capital, liquidity and funding position

Arion Bank will host its Capital Markets Day in Q1 2024

- Update on strategy and direction of the Group
- Medium-term targets under review
  - Review will reflect impact of evolving external operational environment and business plan which will be finalized in autumn
  - Impact of IFRS17 implementation on "Core operating income" reconciliation

Key results	Medium-term targets	Q2 2023		6M 2023	
Return on equity	Exceed 13%	✓	15.5%	✓	14.5%
Core operating income[4] / REA	Exceed 6.7% on core income	✓	7.5%	✓	7.2%
Insurance premium growth (YoY)	Premium growth (net of reinsurance) to exceed the growth of the domestic market by more than 3%[1]	✓	12.3%	✓	10.1%
Cost-to-core income[4] ratio	Below 48% on core income	✓	39.4%	✓	43.0%
CET1 ratio	150-250 bps management buffer[2]	•	400 bps	•	400 bps
Dividend payout ratio[3]	50%	✓	50% of net profit deducted from CET1	✓	50% of net profit deducted from CET1

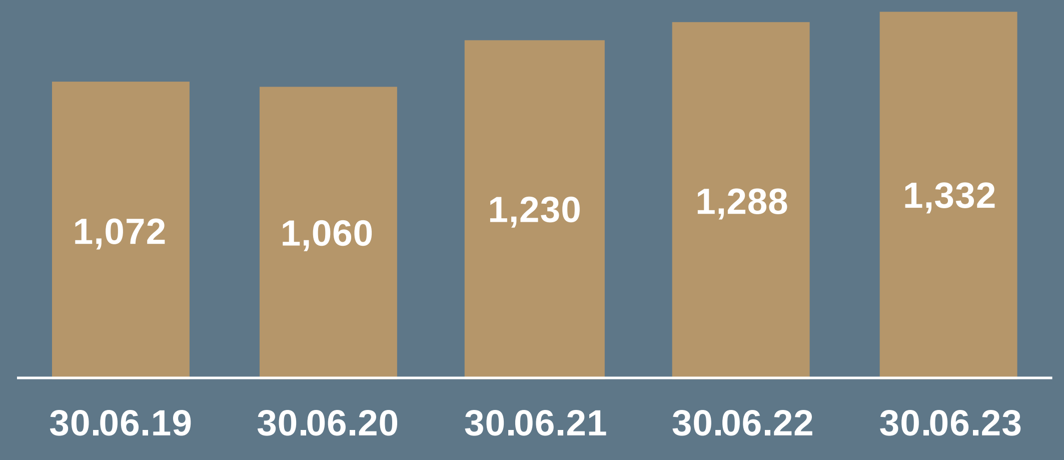
Medium-term targets are reviewed annually, and the underlying horizon is up to 3 years

1 Premium growth in the domestic insurance market in Q1 2023 was 9.3% and 7.5% in full year 2022
2 Approx.16.4 - 17.4% based on current capital requirements.
3 Pay-out ratio of approximately 50% of net earnings attributable to shareholders through either dividends or buyback of the Bank's shares or a combination of both. Additional distributions will be considered when Arion Bank's capital levels are above the minimum requirements set by the regulators in addition to the Bank's management buffer
4 Core income: Net interest income, net fee and commission income and insurance service results (excluding opex)

Key operational highlights in Q2

Pillar 2 capital requirement for the Bank reduced to 2.1% of REA.
A decrease of 1.4 percentage points YoY

Strong AuM development despite challenging markets (ISK bn)



Ongoing activity in Corporate & Investment Banking, advised on the sole listing in Q2

HAMPIÐJAN

Successful launch of new deposit accounts
First of its kind CPI linked 90-day term deposits

Proactive engagement with customers with upcoming interest rate resets of their fixed nominal mortgages

The Bank is well prepared to support its customers by offering various products and solutions to manage mortgage debt service

Bancassurance strategy progressing

- Bancassurance ratio for individuals to 34.4% vs. 32.7% in Q2 2022
- Bancassurance ratio for corporates to 24.9%. vs 21.8% in Q2 2022

Arion supporting growth companies

Empowering the development of Iceland's 4th export pillar and fostering Iceland's economic resilience

- By leveraging merchant banking expertise, and utilizing a robust balance sheet, Arion offers advisory and tailored financial solutions to support growth companies
- Support comes mainly through CIB finding potential investors and in some cases funding with potential upside for Arion Bank, such as:
  - Convertible bonds, where the Bank can exchange the corporate bonds for common stock in the issuing company
  - Warrant bonds, the warrant entitles the Bank to buy shares in the issuing company at a predetermined exercise price
  - Equity kickers, Arion either gets equity stake in the company or paid in cash after the transaction has materialized
  - Funding participation, Arion can support growth companies by participating in placement rounds it advises on

Examples of Arion's merchant banking activities with Icelandic growth companies

Kerecis

- Kerecis recently announced a takeover bid from Coloplast A/S for all share capital in the company, with a valuation above USD 1.2bn (approx. ISK 175bn) making it an Icelandic Unicorn
- Arion is working closely with Kerecis to finalize the financial aspect of the takeover
- Arion aligned its interests with the company's largest shareholders with a warrant bond in early 2021
- In addition to recognized ~ISK 330m in 2021/2022, unrealized profit from Kerecis warrants amount to approx. ISK 560m (Q3 2023)

Controlant

- Arion has worked closely with Controlant throughout the past few years, supporting the company during its leading growth period
- Arion advised the company on a convertible bond placement in early 2020 and to cement its commitment to the company, Arion participated in the private placement and was the largest single bondholder
- Arion refinanced the bond with a senior loan and is still a shareholder, currently holding a 1.58% stake in the company

Amaroq Minerals

- Arion corporate finance advised the company on a private placement round and its listing process on the First North Stock Exchange in 2022
- Arion supported the company by participating in the placement but has since then divested its stake through the stock exchange with a positive upside for both companies
- Arion is still an active shareholder through its market making agreement with the company

Positive progress in the development of Blikastadir

Ambitious project which can strongly support future housing supply in the capital region

- Draft of new master plan published by the municipality in June
- One of the largest undeveloped plots of land in the capital area
- Land covers 93.31 hectares, estimated 3,500 – 3,700 residences and total construction estimated at 430,000 m2
  - Of which commercial property 40-60,000 m2
- Partnership agreement with municipality includes a CPI linked ISK 6bn payment, spread out over the construction period for construction rights and an ISK 1bn contribution to development of sports facilities in the area

Valuation increased to reflect updated position

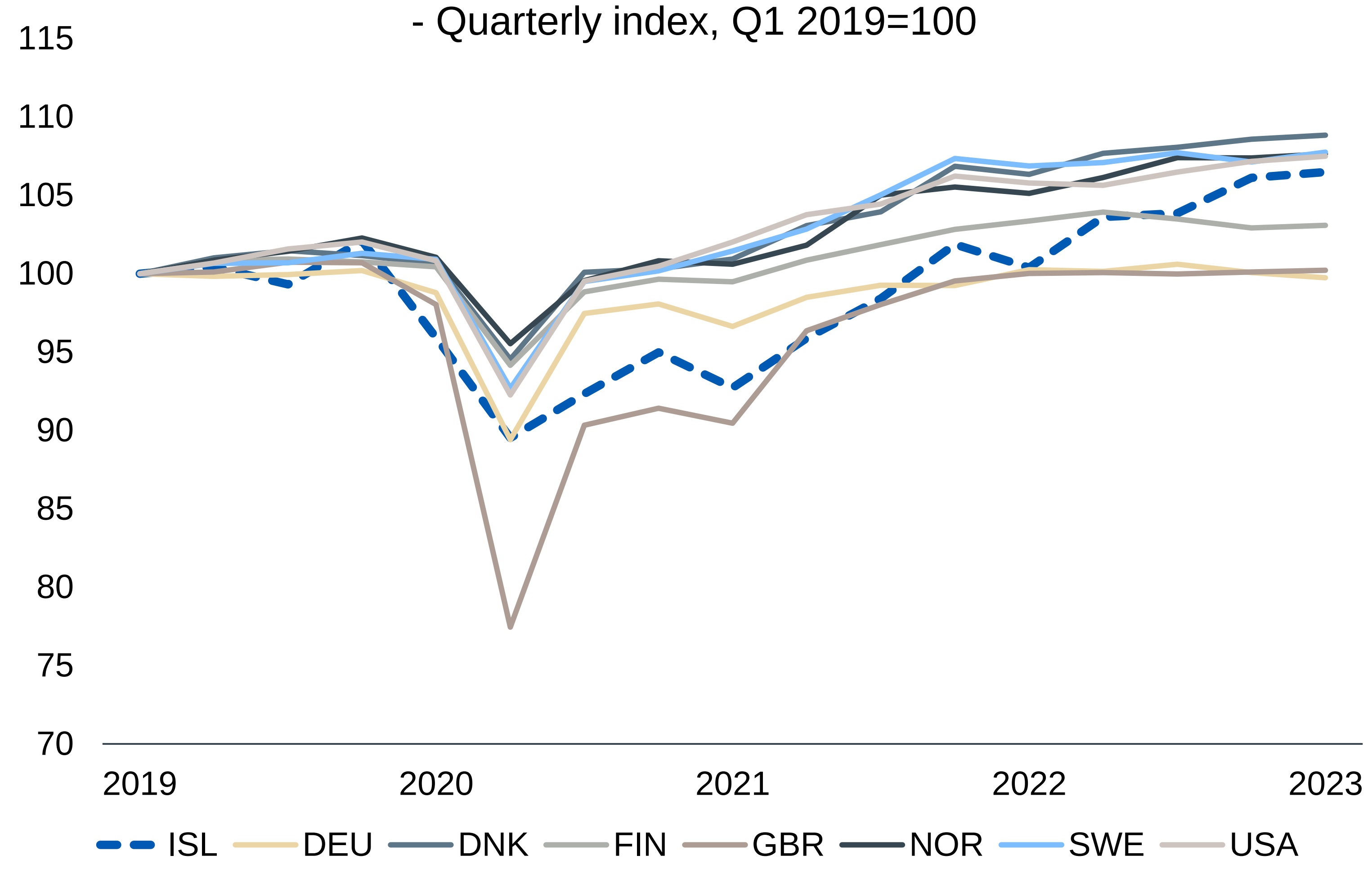
- Updated book value of ISK 6.7bn
- Reduced uncertainty regarding the project's timeline. Valuation model assumes a 16-year timeline, likely to be divided into 4-5 phases.
- WACC decreased to ~20% to reflect reduced uncertainty, while project is still subject to execution uncertainties which are reflected in its valuation assumptions

Macroeconomic environment

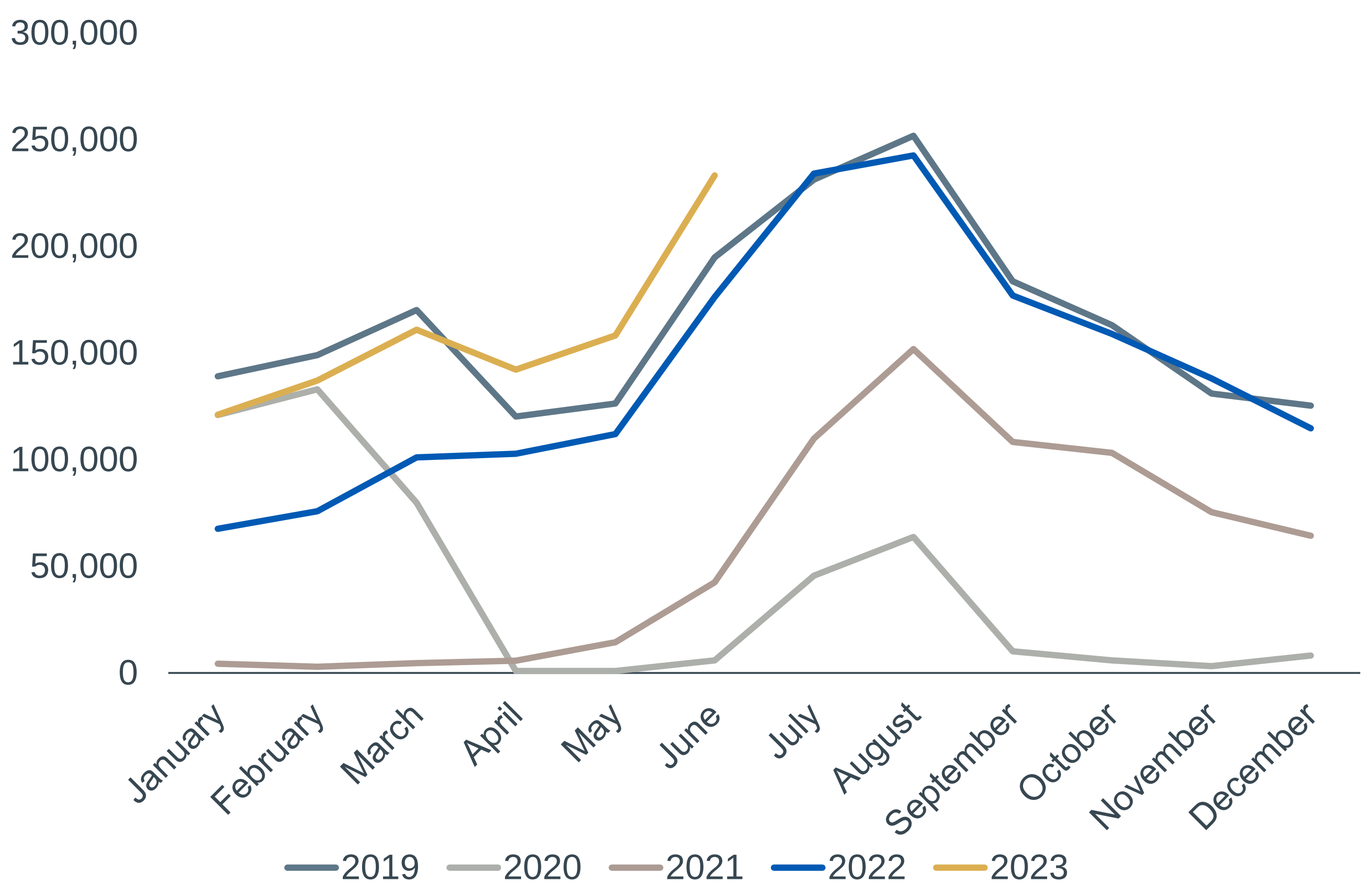
Tourism driven growth amid slowing private consumption

GDP growth of 7% in Q1 2022. Strong growth albeit lower than Arion Research anticipated. Since May, evidence of cooling domestic demand has gradually emerged but many other sectors, most importantly tourism, have flourished. The number of tourists in June, 233,000, matched the record year of 2018.

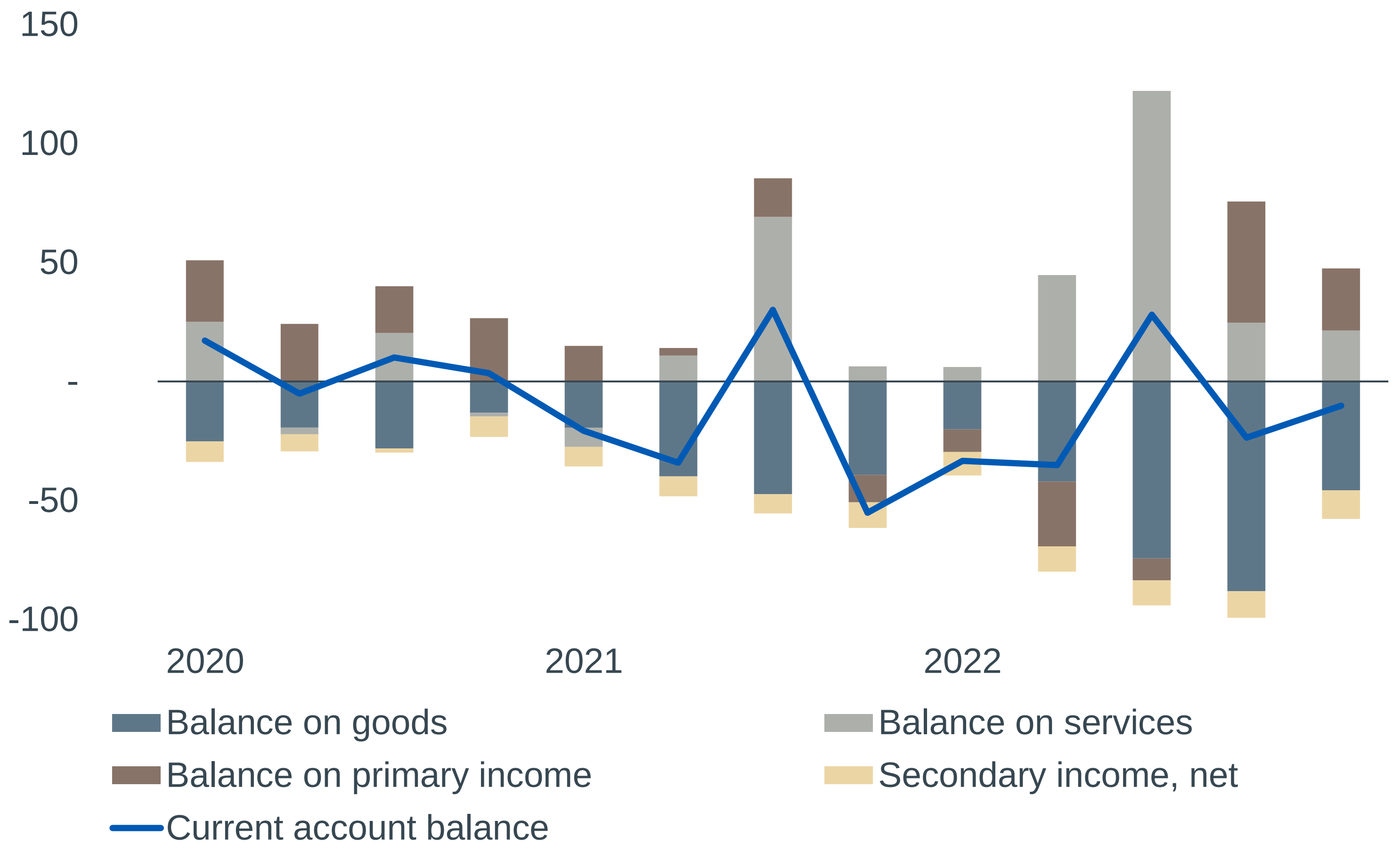
GDP
- Quarterly index, Q1 2019=100



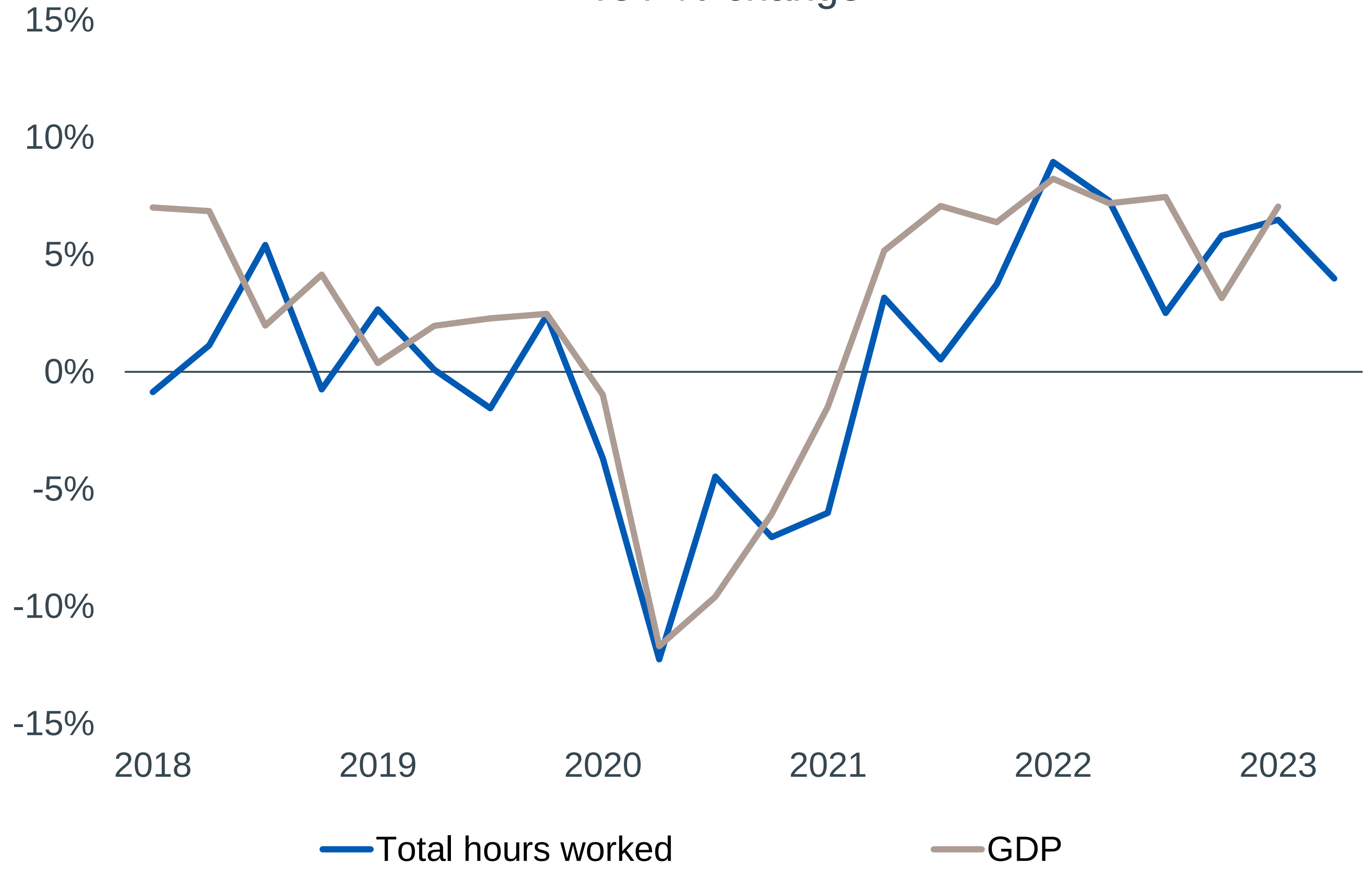
Tourist arrivals via Keflavík International Airport



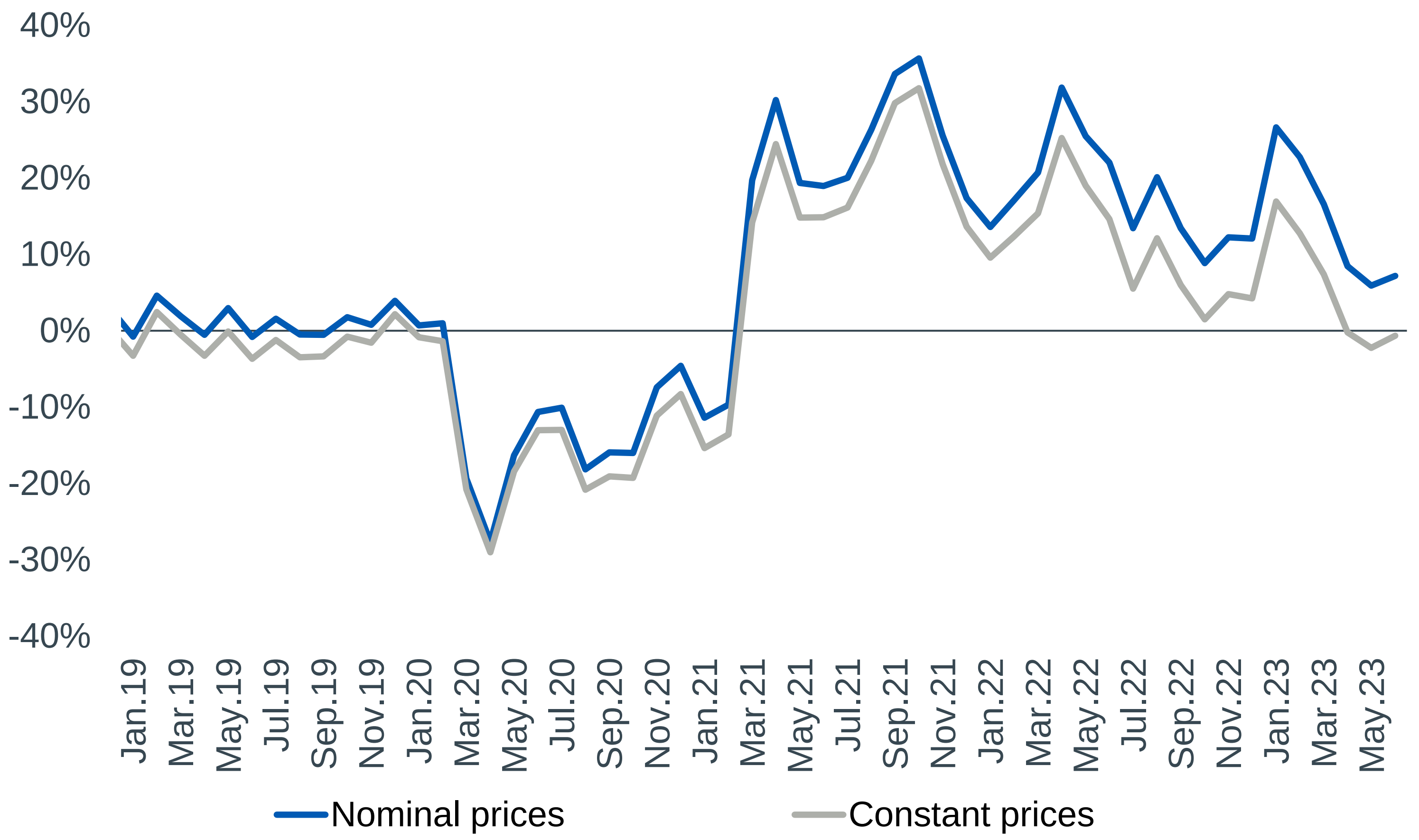
Current account balance
- bn. ISK at constant exchange rate,



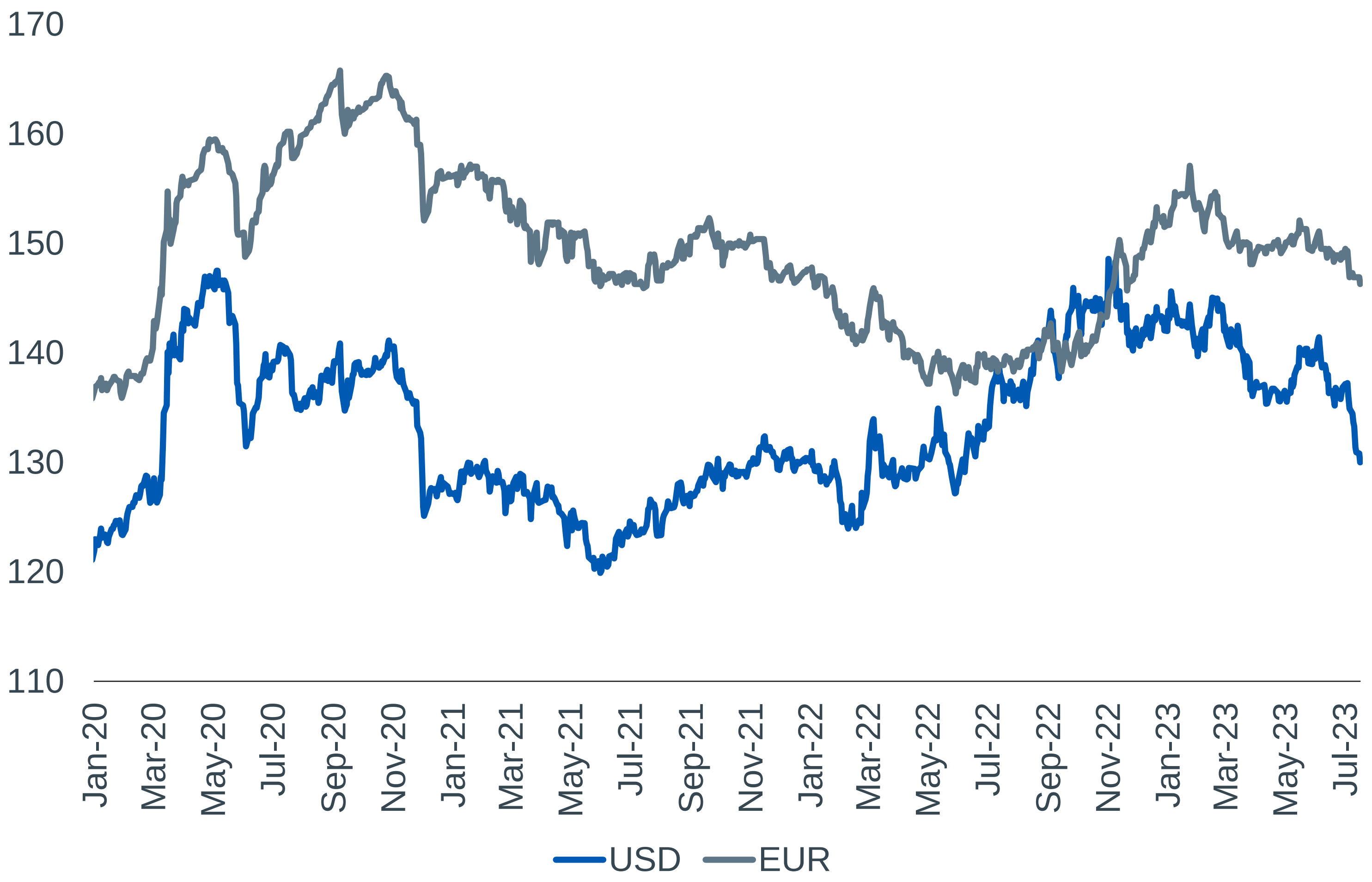
Employment and GDP
- YoY %-change



Payment card turnover in Iceland
- foreign and domestic cards, YoY %-change



The ISK against major trade currencies

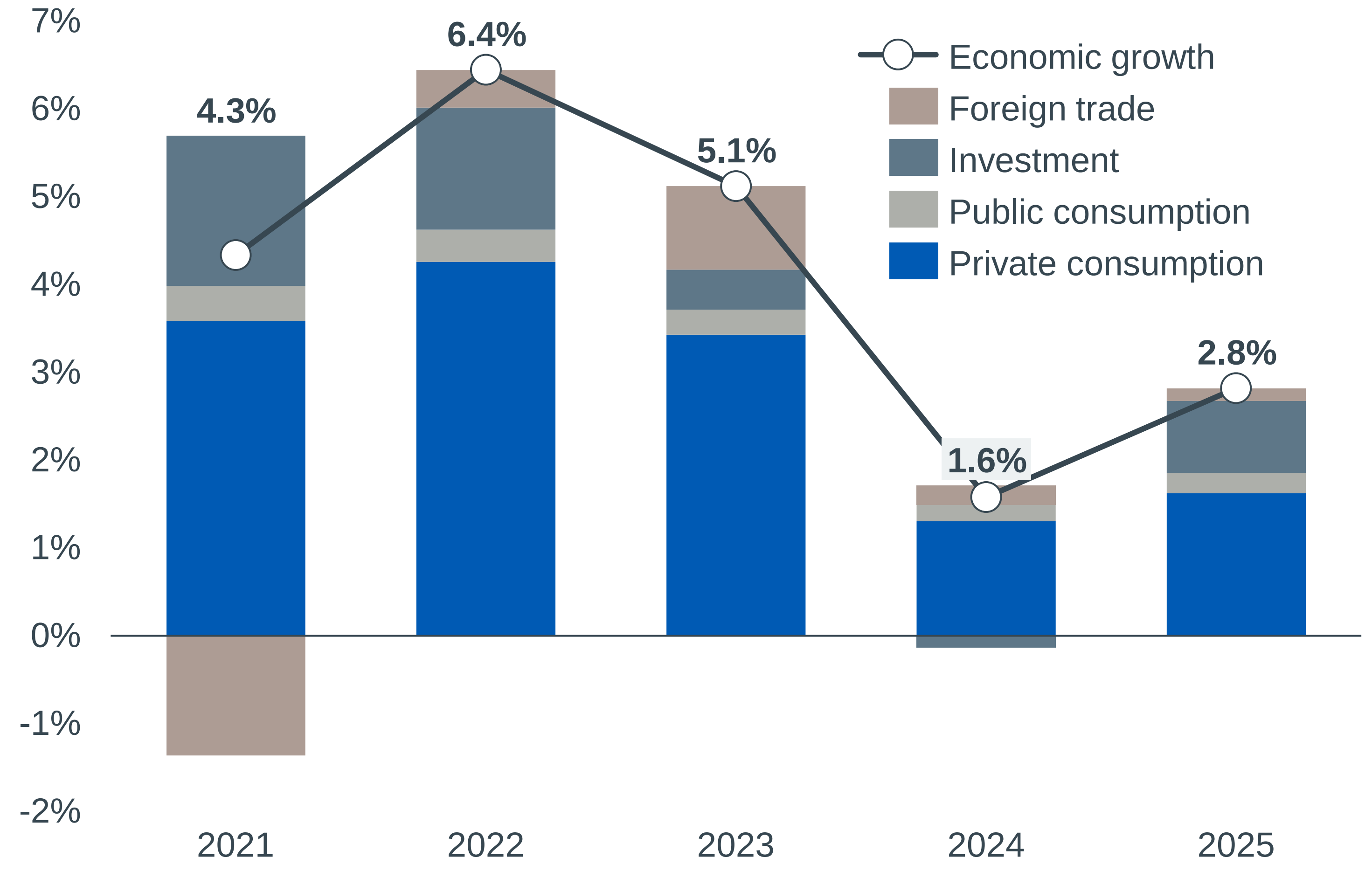


Sources: OECD, Statistics Iceland, Central Bank of Iceland, Icelandic Tourist Board, Arion Research

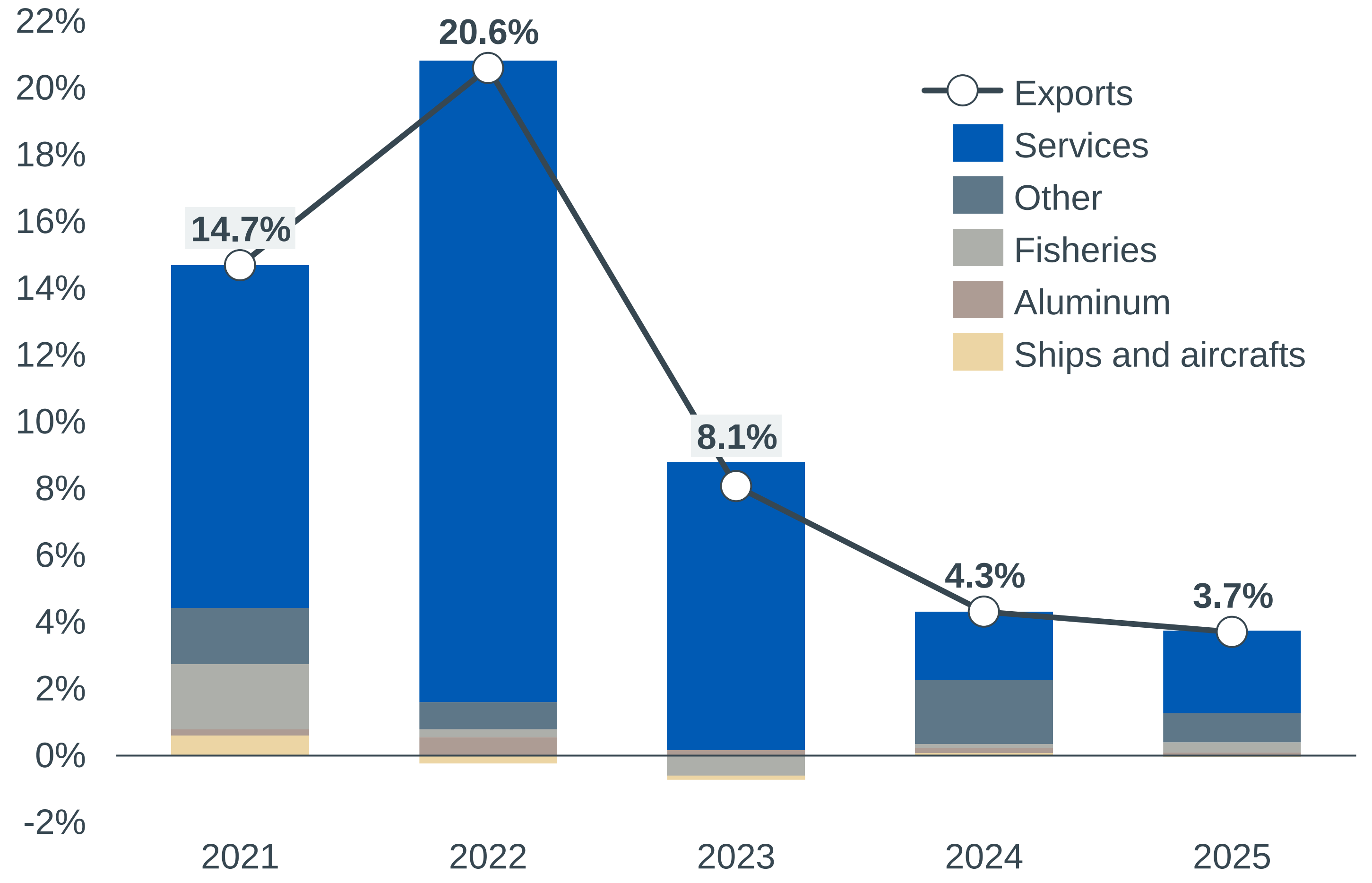
The outlook remains positive

- The Icelandic economy is set for strong growth in 2023, despite the rocky global environment but next year could be challenging with slower growth
- Private consumption has slowed faster than Arion Research anticipated as is evident in the recent real decline in payment card turnover. However, income continues to rise and household balance sheets remain robust, which is underlined by the fact that recent consumption growth has to some extent been driven by reduced savings
- However, tourism appears to be outperforming forecasts as recent figures are matching or exceeding the record year of 2018
- Other exports are set for moderate growth. Meanwhile, “other” exports, i.e., not tourism, aluminum, and fisheries but including health care products and aquaculture could exceed the forecast

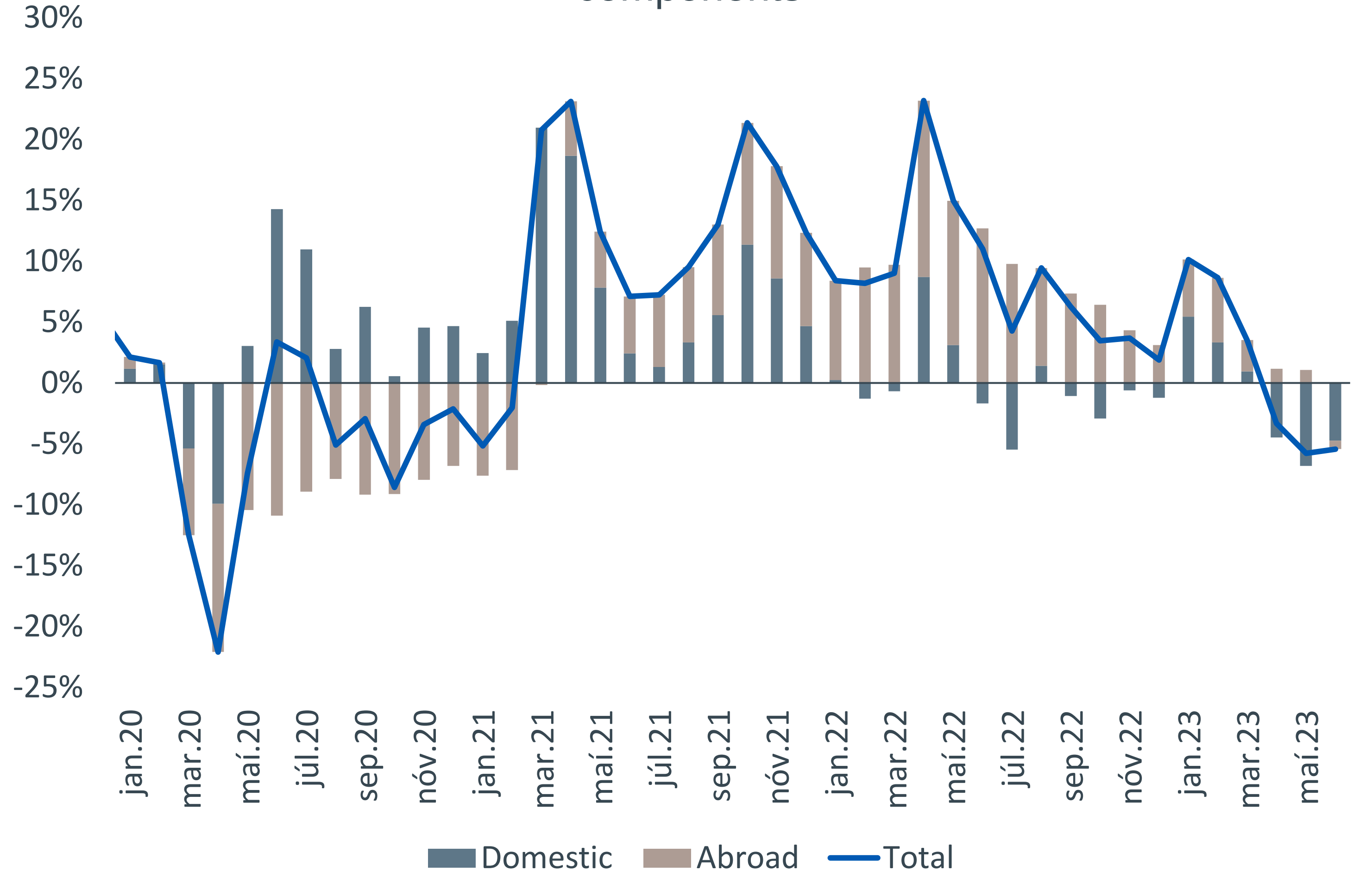
GDP Growth
- contribution of GDP components



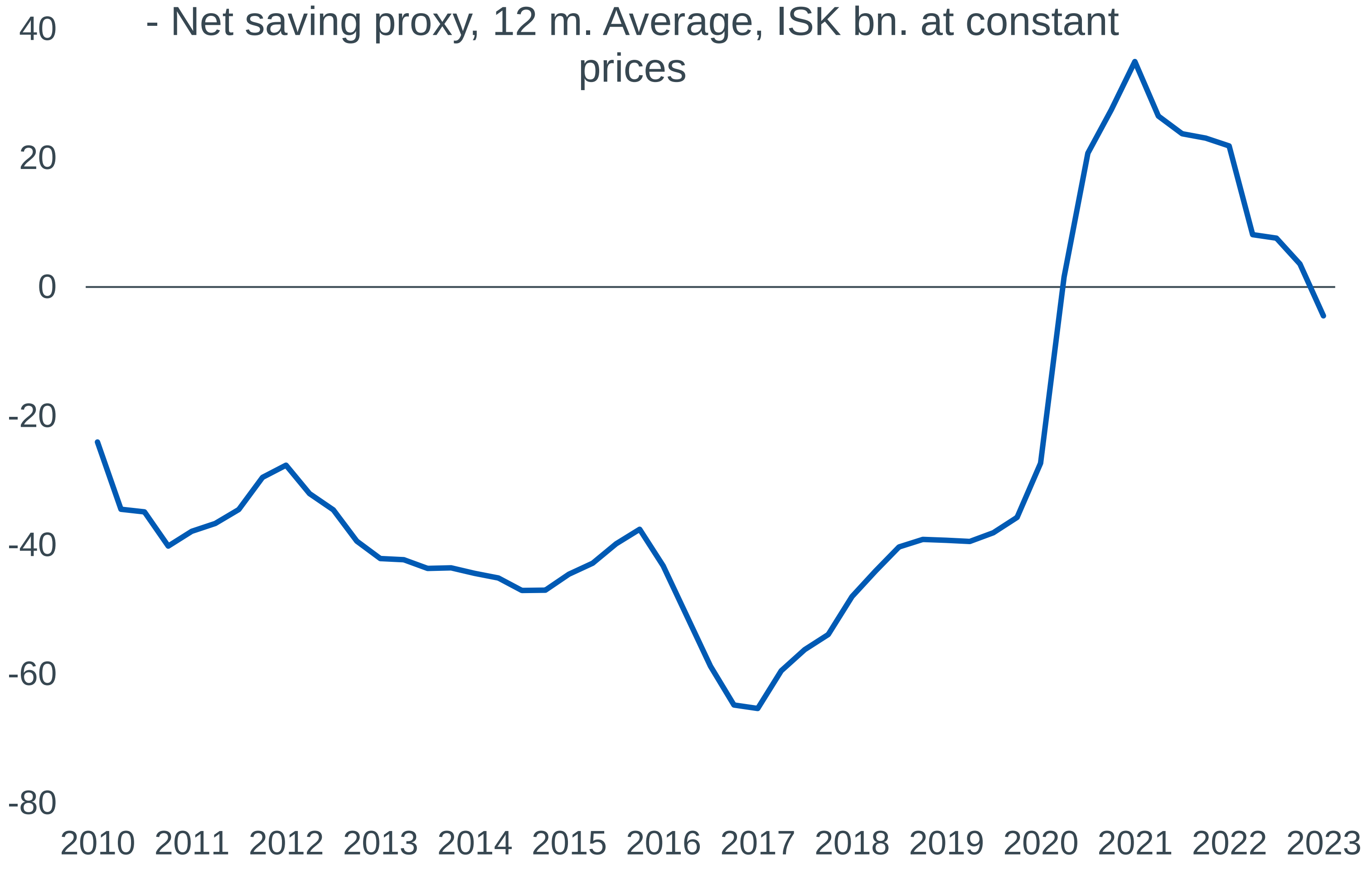
Exports
- growth contribution of components



Household payment card turnover
- YoY growth, growth contributions of underlying components



Household disposable income less consumption
- Net saving proxy, 12 m. Average, ISK bn. at constant prices

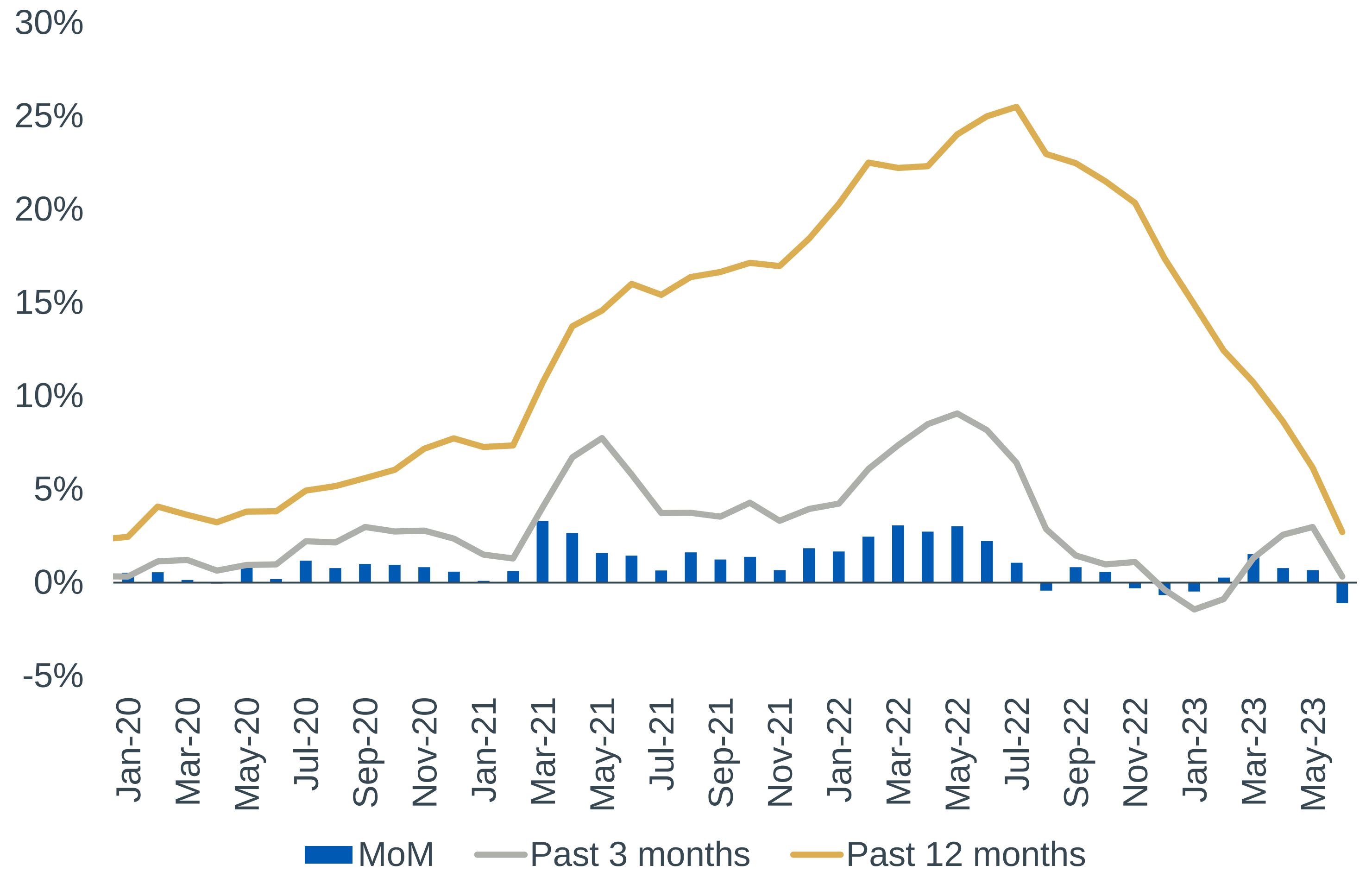


Sources: IMF, Central Bank of Iceland, Statistics Iceland, Icelandic Tourist Board, ISAVIA, Arion Research

Mixed signals in the housing market

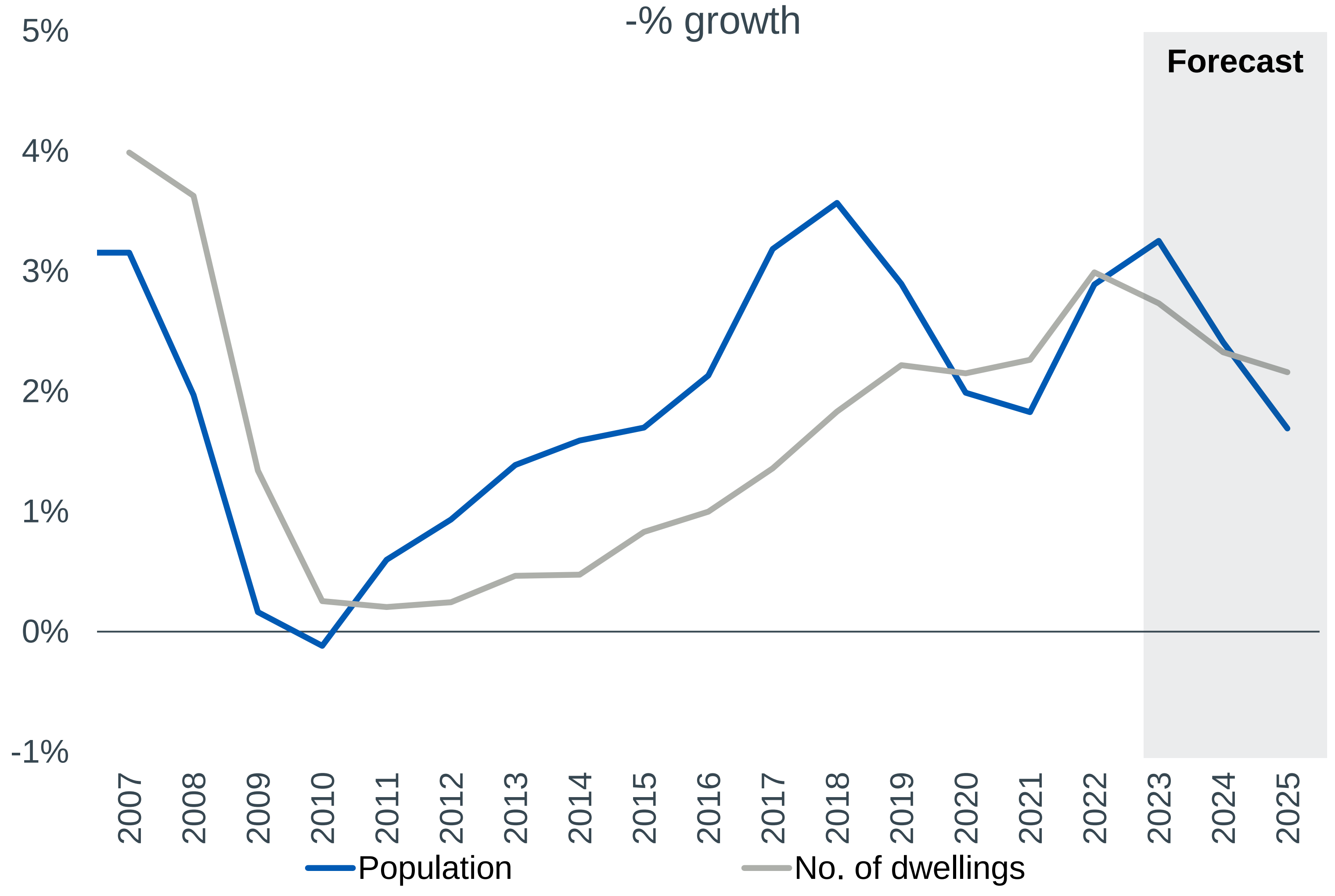
- Recent price movements in the housing market have been giving mixed signals. There was an unexpected surge in prices in March through May. But in June, prices in the Capital area fell by 1.1%. Arion Research expects housing prices to decrease slightly until the end of this year before recovering in 2024
- It's fitting that signals are mixed as key market drivers are moving in opposite directions. On one hand rising interest rates and tighter lending conditions are reducing demand. On the other hand, unprecedented population growth is likely to be rapidly contributing to housing shortage
- Households have a cushion in historically high debt but some adjustment might be needed. As the need for housing is likely to increase, Arion Research expects the adjustment to occur primarily through falling real prices, as set out in the latest Economic Outlook

Housing price index in the Capital area
- % change

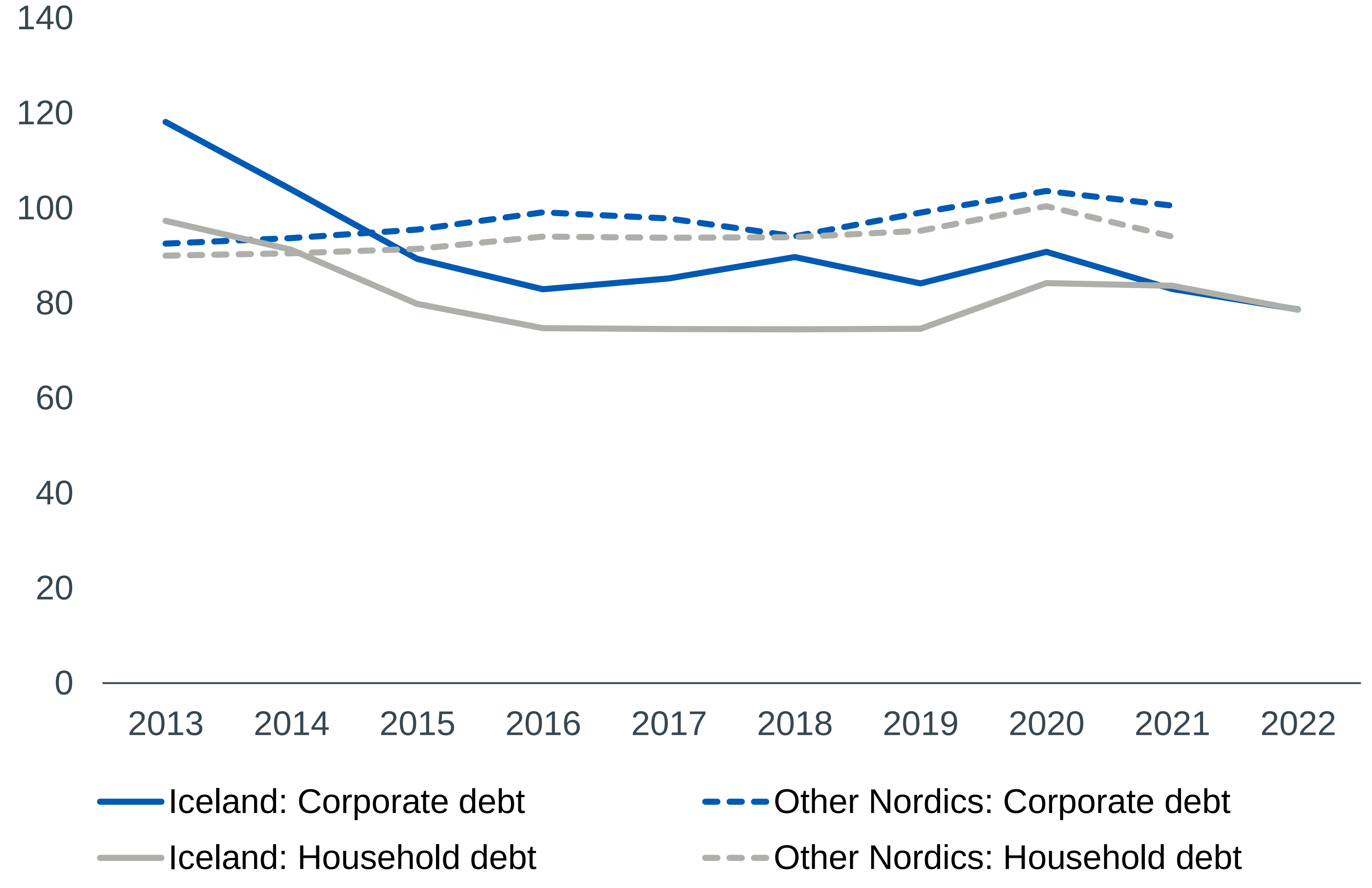


Housing investment
- bn. ISK at 2022 prices

Housing and population growth
-% growth



Private debt
-% of GDP

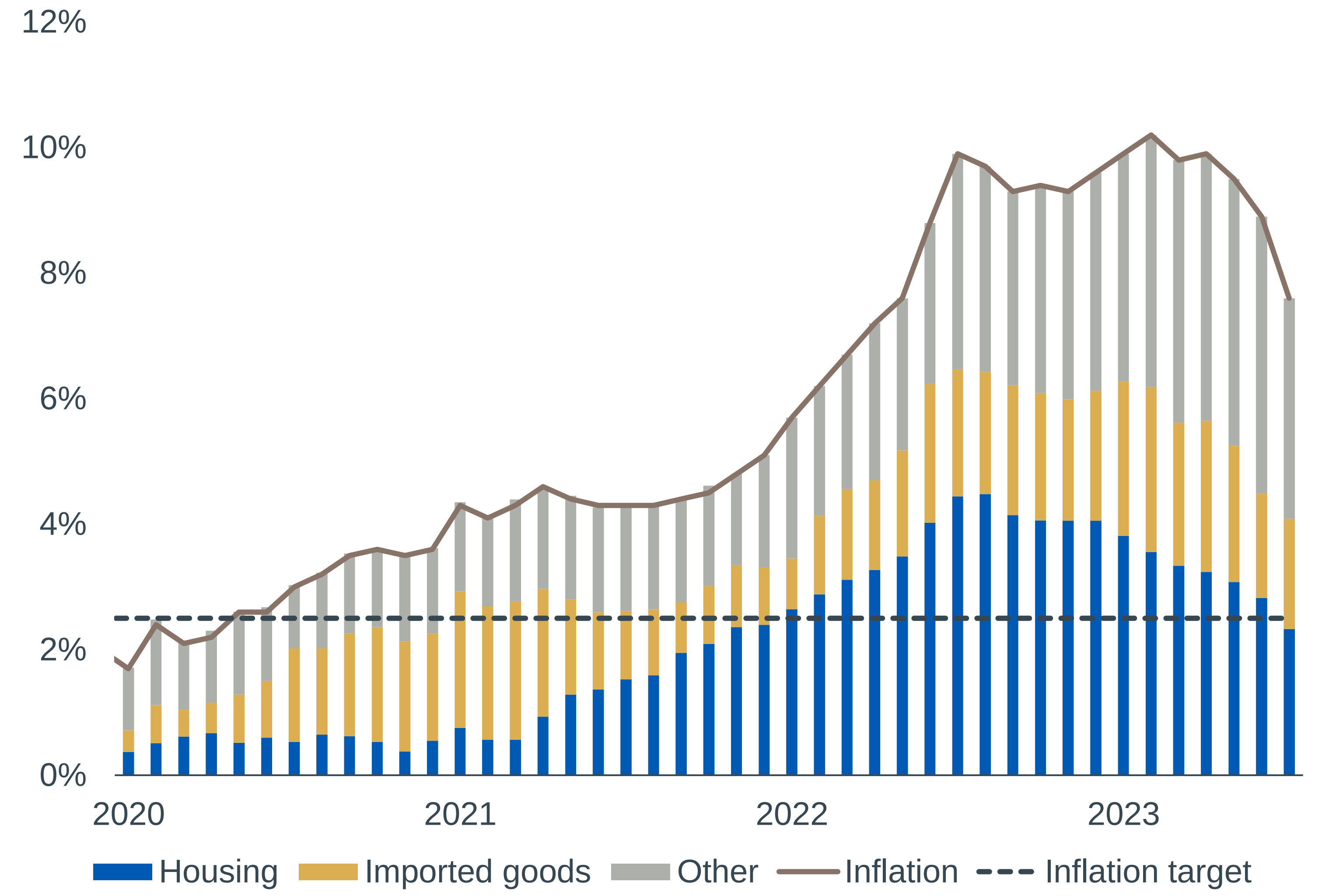


Sources: Central Bank of Iceland, Statistics Iceland, HMS, Arion Research

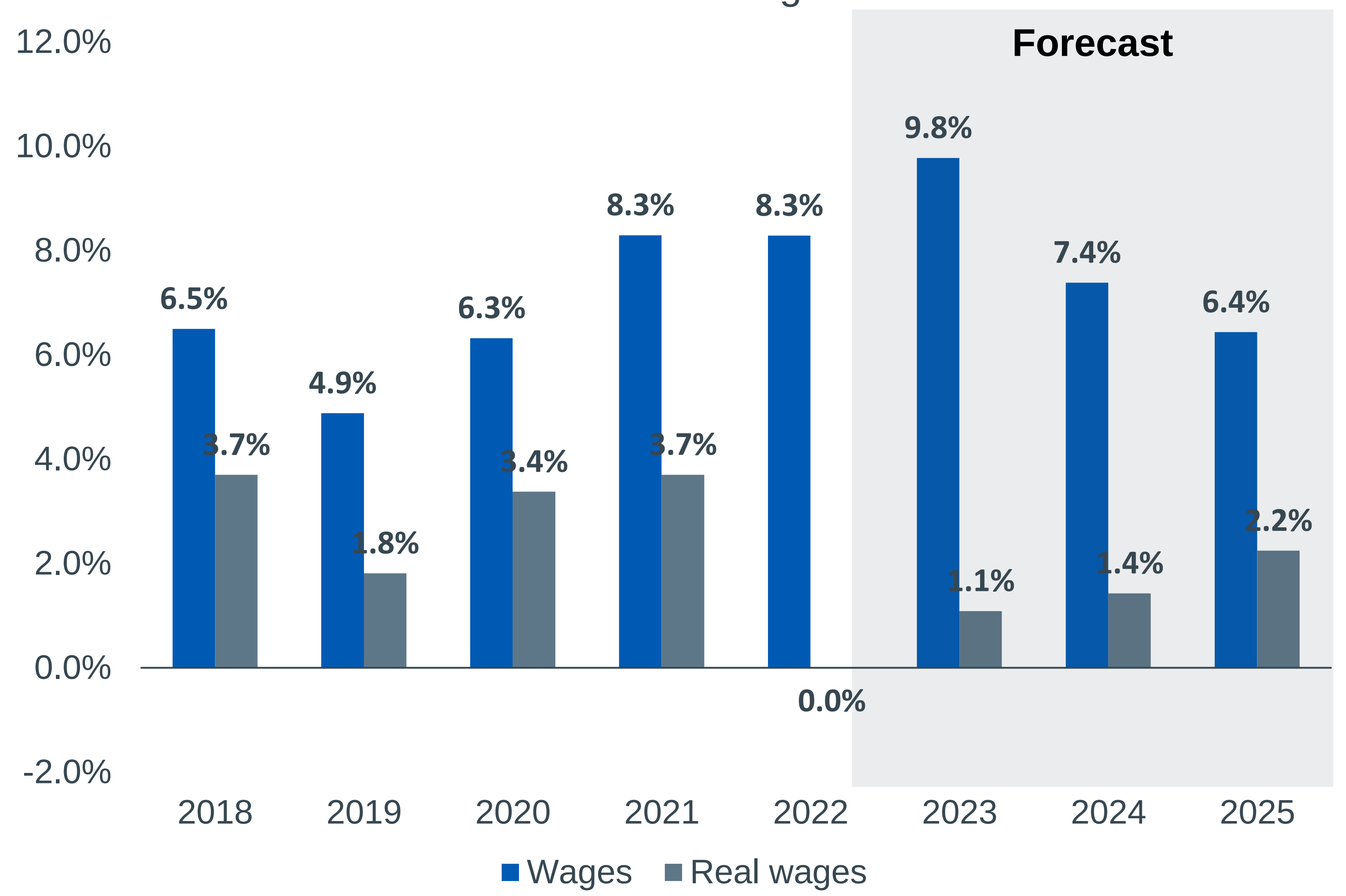
Inflation declining. Terminal rates in sight?

- Slower increases in housing prices or actual declines are helping to reduce inflationary pressure. Less imported inflation is also helping to bring down the inflation rate. Inflation was 7.6% in July after a year at the 9%-10% mark. However, analysts don’t expect inflation to go much lower over the next 3 months and some inflationary pressures still persist
- Other domestic inflation will be a key uncertainty in the next few years. Recent wage hikes have pushed up prices and with major collective agreements expiring in January 2024 the Central Bank’s Monetary Policy Committee (MPC) has made it clear that it intends to reduce inflation as much as possible before then. Arion Research expects inflation to be around 6% then
- The key interest rate rose by 1.25 bps in May and now stands at 8.75%. The MPC is expected to raise rates again at its next meeting in August but it is uncertain that any further increases will be made after that. Arion Research's most recent Economic Outlook projected a terminal rate of 9% and forecasts that rates will gradually decrease from the second half of 2024

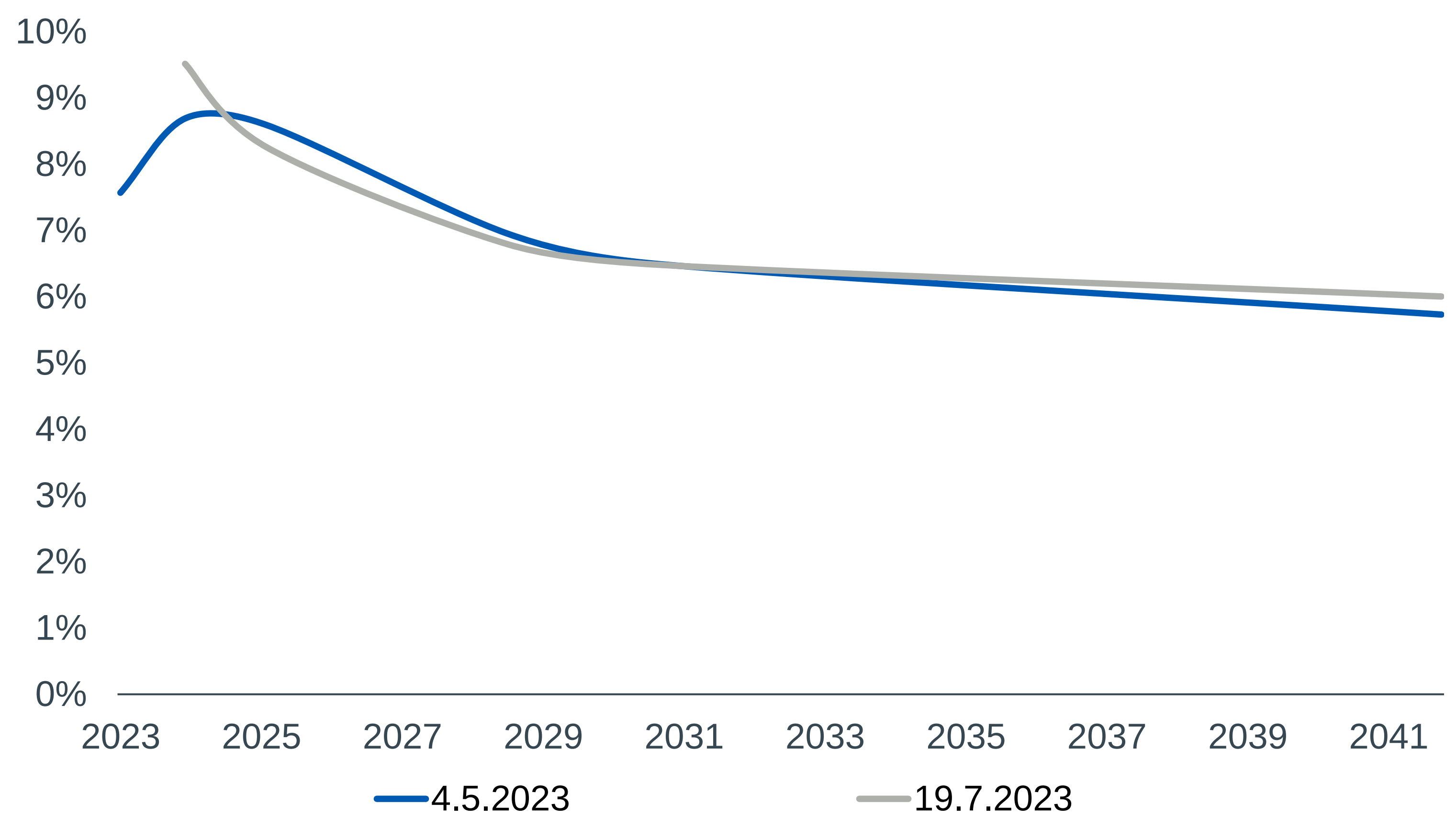
CPI by expenditure groups



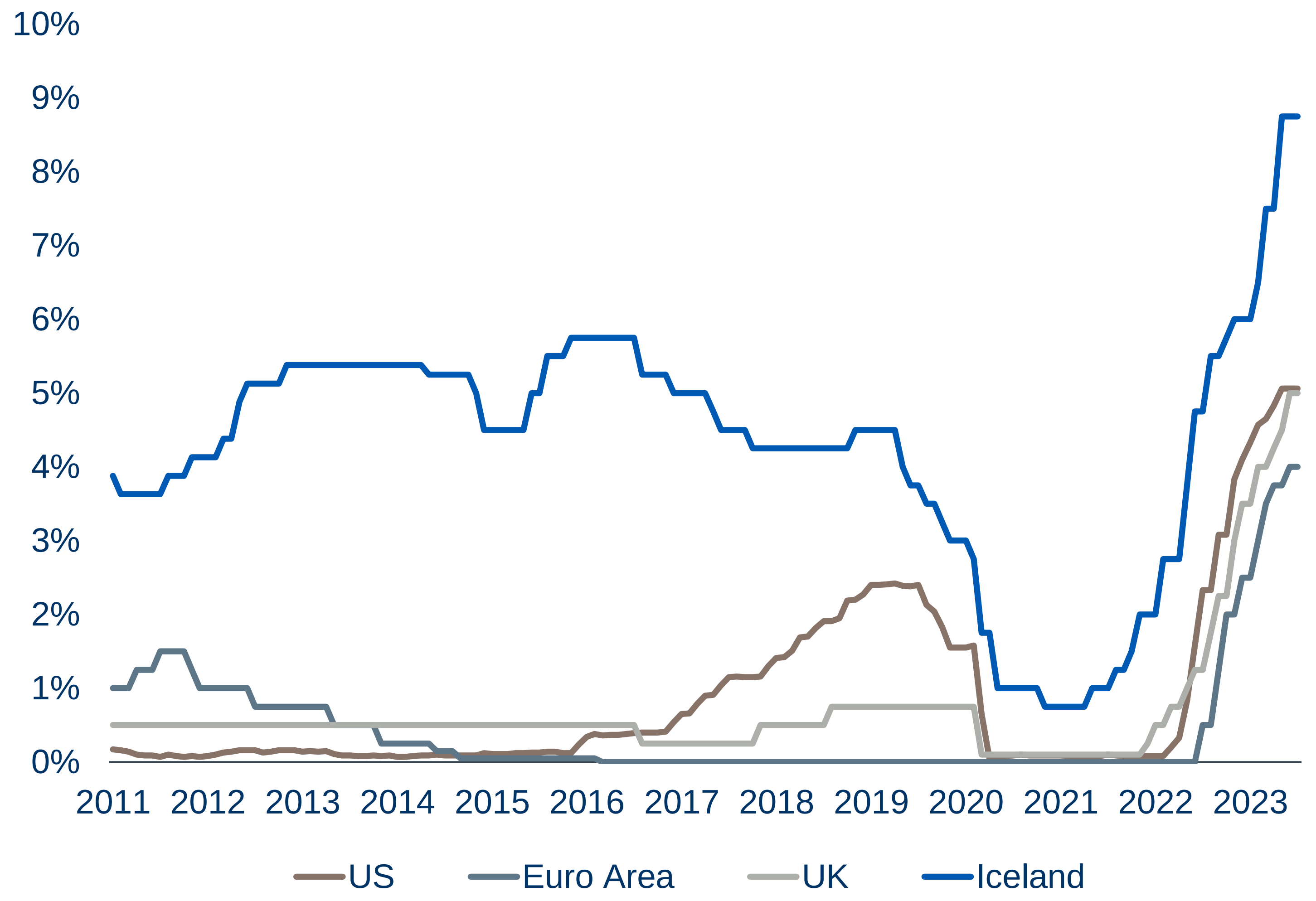
Wages and real wages
- YoY %-change



Treasury bill yield curve



Key interest rates



Sources: Statistics Iceland, Central Bank of Iceland, BoE, ECB, Federal Reserve, Arion Research

Financials

Key takeaways in Q2 2023

Operational performance *Solid momentum*	▸ Strong quarter with net profit of ISK 7.1bn resulting in ROE of 15.5% ▸ While loan growth is slowing, operational development across the Group remains robust ▸ Prudent loan loss provisioning despite risk indicators of credit quality remaining at healthy levels, albeit with signs of turning cycle
Blikastadir *Valuation updated*	▸ Positive traction in planning process of Blikastadir land development subsidiary ▸ Valuation increased by ISK 1.6bn to ISK 6.7bn considering enhanced clarity around timeline and other key valuation drivers
Balance sheet *Robust position*	▸ Pillar II capital requirements reduced from 3.5% to 2.1%, which is expected to increase regulatory capital and MREL buffers ▸ Capital position strong with a CET1 ratio of 18.9% or 400bps above regulatory minimum ▸ Diversified and seasoned deposit base continued to grow in the quarter and light wholesale funding maturity profile ▸ Liquidity position strong with an LCR of 163%. Average duration of liquidity bond portfolio within one year and no HTM accounting
IFRS 17 *Change in presentation of insurance operation*	▸ Implementation of IFRS 17 impacts the presentation of key line items of the insurance operation ▸ Operating expenses, net commissions and net interest related to insurance operation now all included in “insurance service results" ▸ Immaterial impacts on net results of the Group, mainly transfer between line items that affect previous quarter comparisons and KPIs

[1] Net interest income, net fee and commission income and insurance service results (excluding opex)

Income statement Q2 2023

- Net profit of ISK 7.1bn resulting in ROE of 15.5%
- Core income* increases 8% YoY and 10% from Q1
- Continued increase in NII following policy rate increases and lending growth
- Slight decrease in NCI, mainly from lending activities which were high in Q1 2023 and in Q2 last year
- Strong operation in insurance business, with premium increase of 12% between years. (*Presentation of line items impacted by IFRS17 implementation)*
- Challenging quarter in net financial income impacted by market volatility
- Updated Blikastadir valuation of ISK 1.6bn accounted for in Other income
- Operating expense decreased by 1% YoY, and 7% from last quarter. When Opex of insurance operation is included, the increase was 1.5% YoY
- Net impairments mainly due to prudent changes to IFRS9 model assumptions
- High effective income tax rate of 31.3% due to combination of income

	Q2 2023	**Q2 2022**	**Diff**	**Q1 2023**	**Diff**
Net interest income	11,426	9,745	17%	10,994	4%
Net commission income	4,187	4,582	(9%)	4,451	(6%)
Insurance service results	762	924	(18%)	(721)	-
Net financial income	(617)	(2,878)	(79%)	796	-
Other operating income	1,586	732	117%	19	-
Operating income	**17,344**	**13,105**	**32%**	**15,539**	**12%**
Operating expenses	(6,009)	(6,056)	(1%)	(6,470)	(7%)
Bank levy	(457)	(416)	10%	(449)	2%
Net impairment	(568)	186	-	(52)	-
Net earnings before taxes	**10,310**	**6,819**	**51%**	**8,568**	**20%**
Income tax expense	(3,226)	(3,588)	(10%)	(2,287)	41%
Net earnings from continuing operations	**7,084**	**3,231**	**119%**	**6,281**	**13%**
Discontinued operations net of tax	7	6,819	-	10	-
Net earnings	**7,091**	**10,050**	**(29%)**	**6,291**	**13%**
Return on equity	15.5%	22.6%		13.7%	
Core income*	17,116	15,844	8%	15,528	10%

* Core income: Net interest income, net fee and commission income and insurance service results (excluding opex)

 All amounts in ISK m

Income statement H1 2023

- Net profit of ISK 13.4bn resulting in ROE of 14.5%
- Core income* increases 13% YoY
- Strong increase in NII YoY, mainly due to increased base rate and 11% growth in loans to customers from the same period last year
- Continuing positive NCI development
- Insurance premium grew by 10.5% YoY but at the same time claims increased by 9.8%
- Net financial income below expectations during the first half of the year
- Positive result in other income is mainly from revaluation of the investment property Blikastadir
- Operating expense increased by 7% YoY but taking into account the opex connected to insurance operation there was an increase of ISK 1.2bn or 9.1%

	H1 2023	H1 2022	Diff
Net interest income	22,420	19,221	17%
Net commission income	8,638	8,138	6%
Insurance service results	41	360	(89%)
Net financial income	179	(1,758)	-
Other operating income	1,605	1,164	38%
Operating income	**32,883**	**27,124**	**21%**
Operating expenses	(12,479)	(11,633)	7%
Bank levy	(906)	(809)	12%
Net impairment	(620)	(309)	101%
Net earnings before taxes	**18,878**	**14,374**	**31%**
Income tax expense	(5,513)	(5,304)	4%
Net earnings from continuing operations	**13,365**	**9,070**	**47%**
Discontinued operations net of tax	17	6,915	(100%)
Net earnings	**13,382**	**15,985**	**(16%)**
Return on equity	14.5%	17.4%	
Core income*	32,644	28,946	13%

*Core income: Net interest income, net fee and commission income and insurance service results (excluding opex)

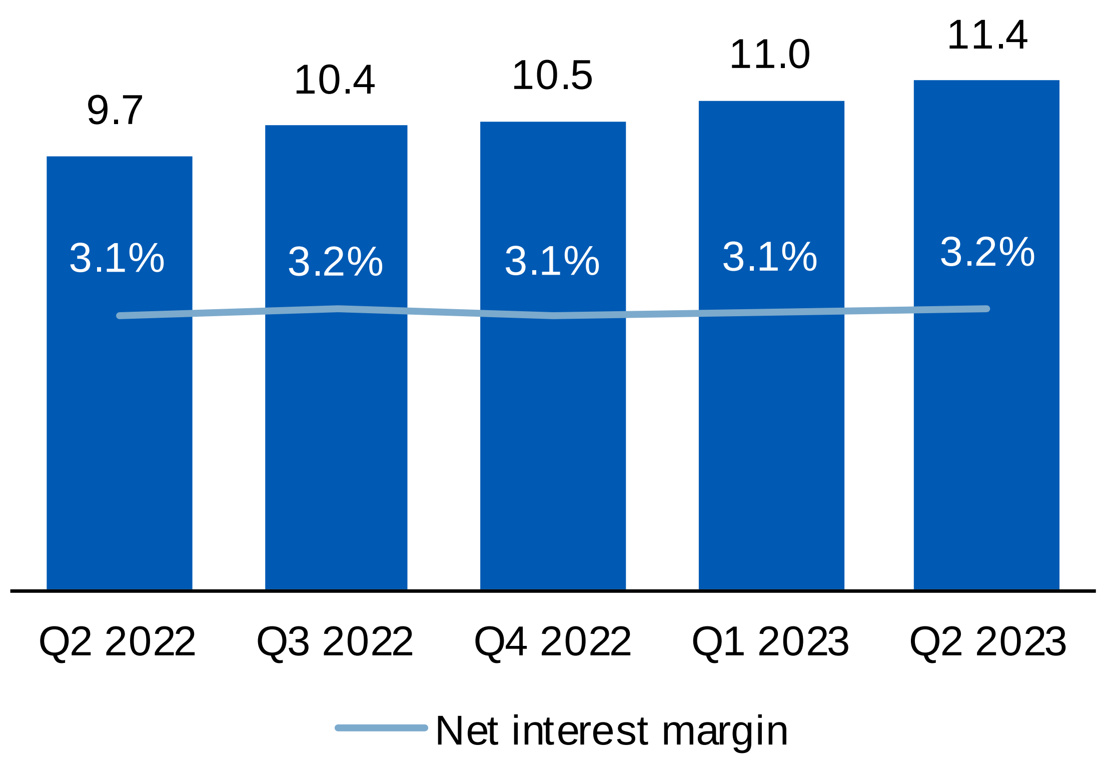
 All amounts in ISK m

Net interest income

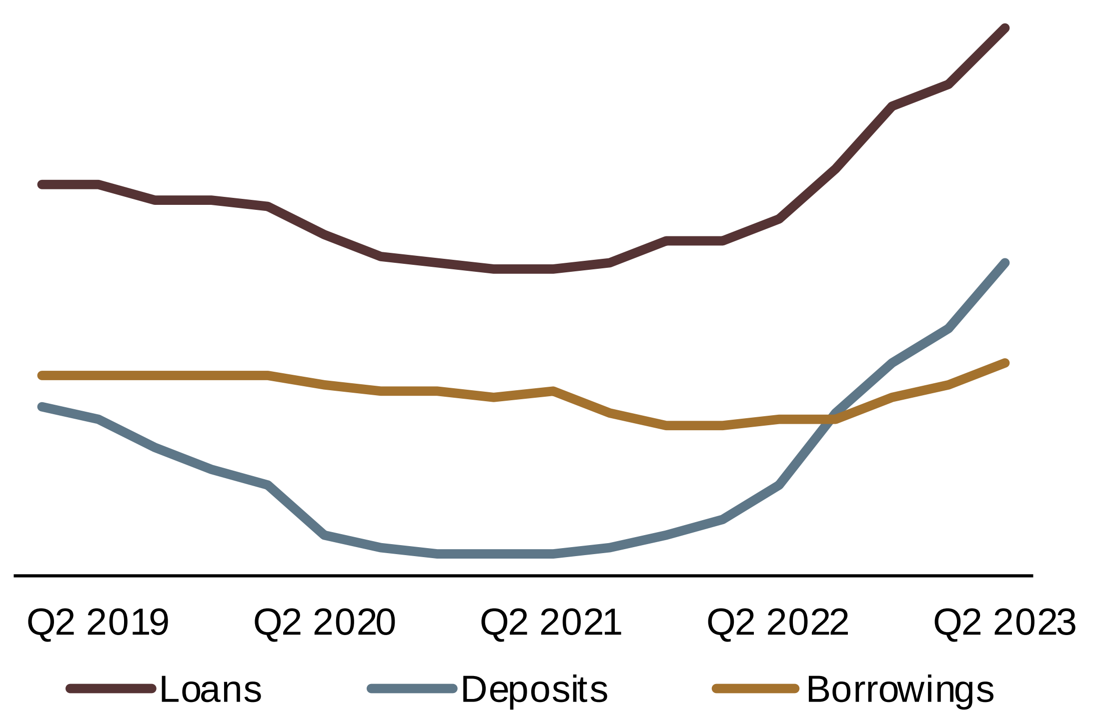
Robust margin but rate sensitivity slowing as expected

- Net interest income in Q2 increased by 17% from Q2 2022 and 4% between quarters from Q1 2023
- Policy rate increased from 2.75% at the beginning of Q2 2022 to 8.75% at the end of Q2 2023. In late May there was a hike of 125 bps
- Rate sensitivity slowing as interest expense increasing on both deposits and wholesale funding. Forward guidance for NIM continues to be around 3% level
- Reset of interest of ISK 152bn fixed rate nominal mortgage portfolio which will start in autumn, with most of these being reset over the next couple of years
  - The Bank is well prepared to support its customers by offering various products and solutions to manage mortgage debt service
- Average interest-bearing assets increased in Q2 by 9.2% from Q2 2022 and by 2.0% from Q1 2023

Net interest income

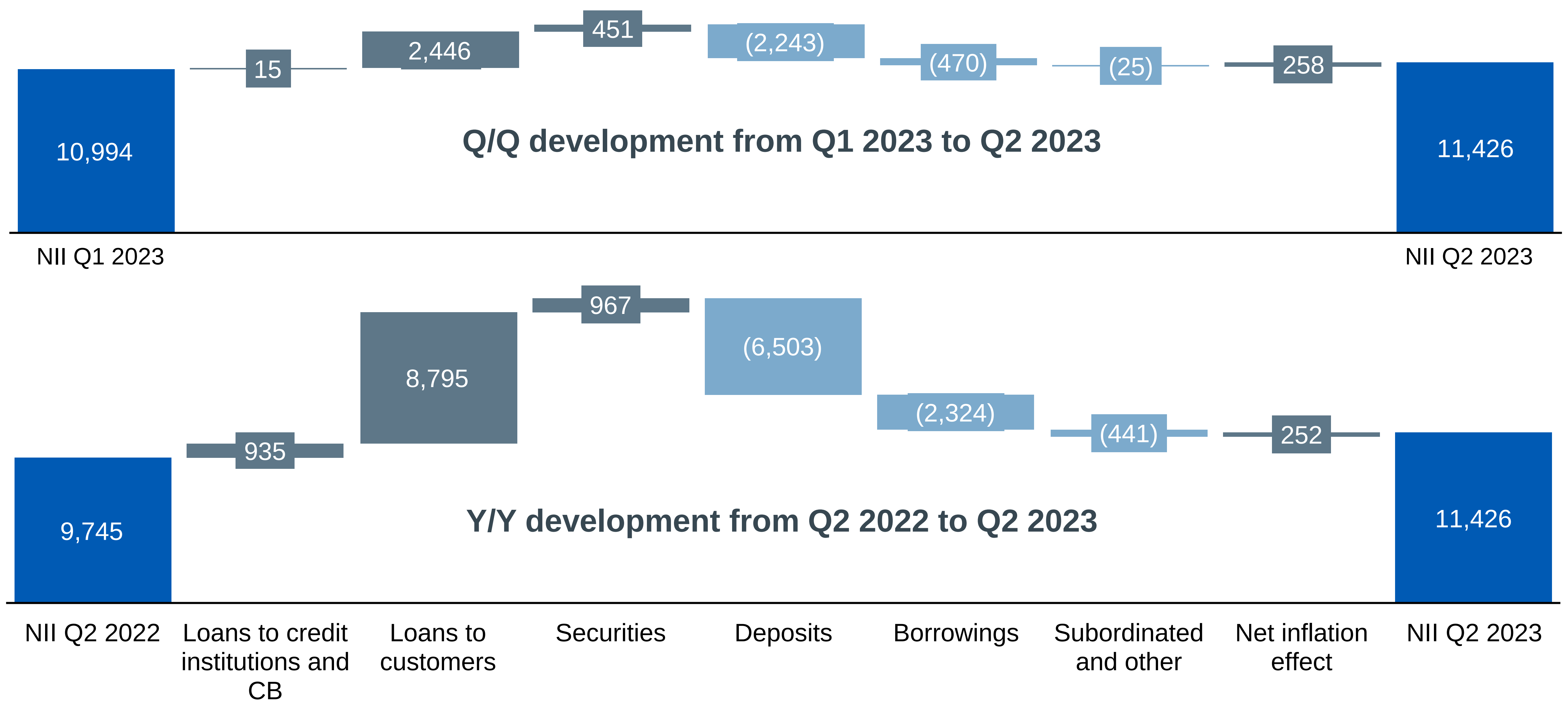


Main interests* (%)



*Excluding net inflation effect

Net interest income development (ISK m)

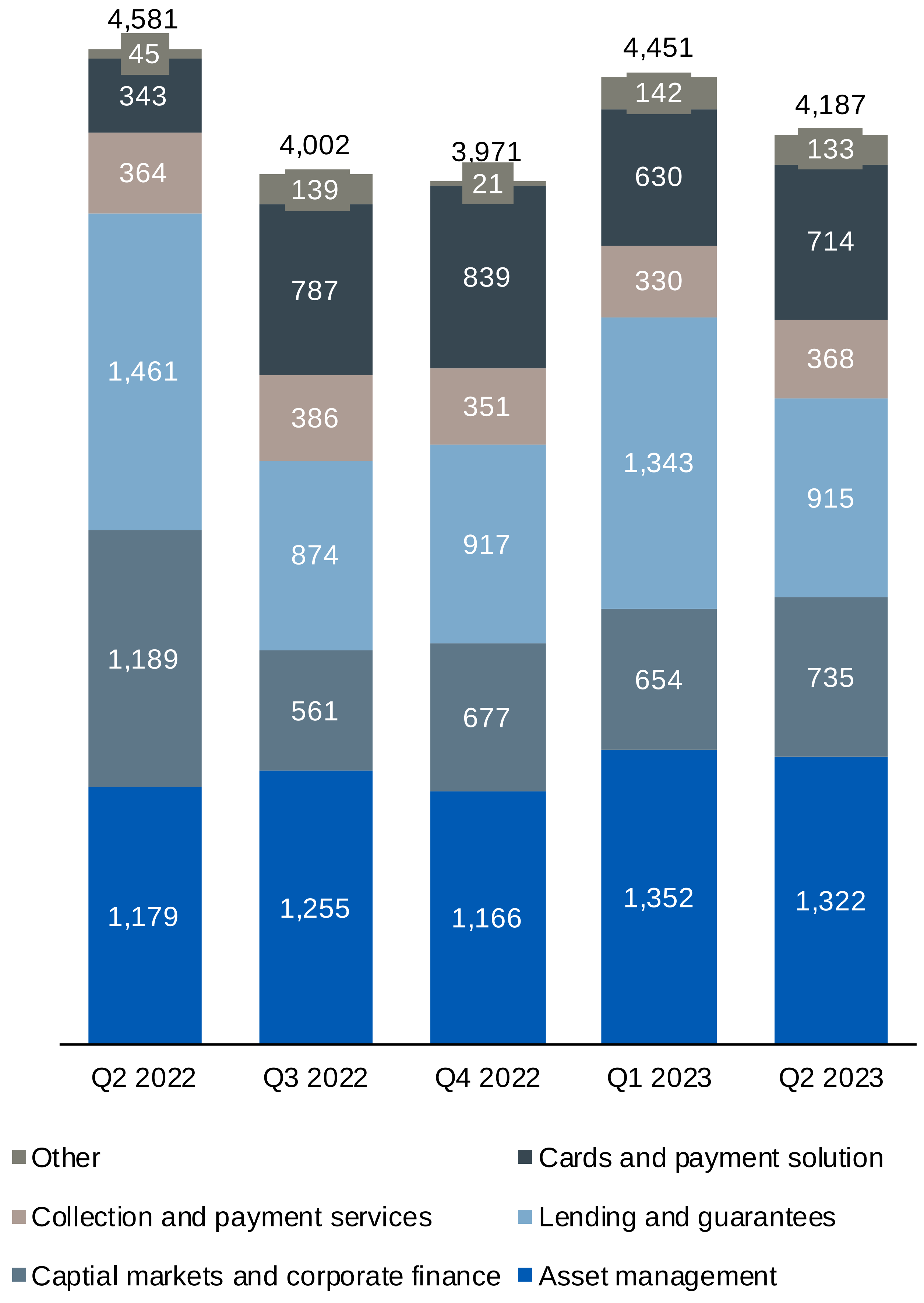


Net fee and commission income

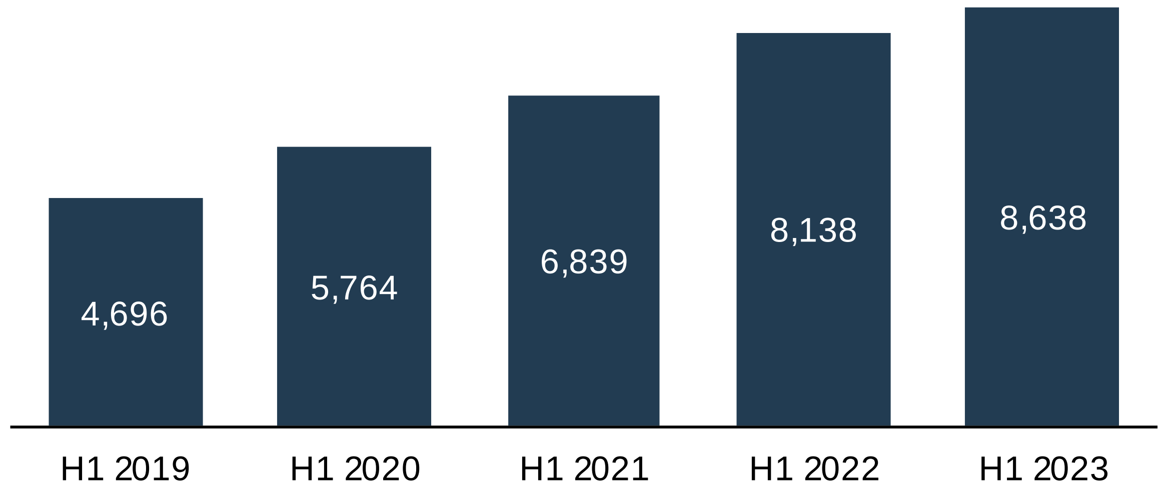
Diversified fee businesses support continued strong fee generation

- Solid quarter in all fee generating businesses with total fees of ISK 4.2bn
- Lending fees down from Q1 and lower than Q2 2022 as both these quarters were high relating to large transactions closing
- Continued strong and stable income from asset management, despite challenging market conditions. Assets under management continue to rise and end the quarter at ISK 1,332bn
- Net fee and commissions income covers 62% of total operating expenses, up from 35% for the first half of 2019

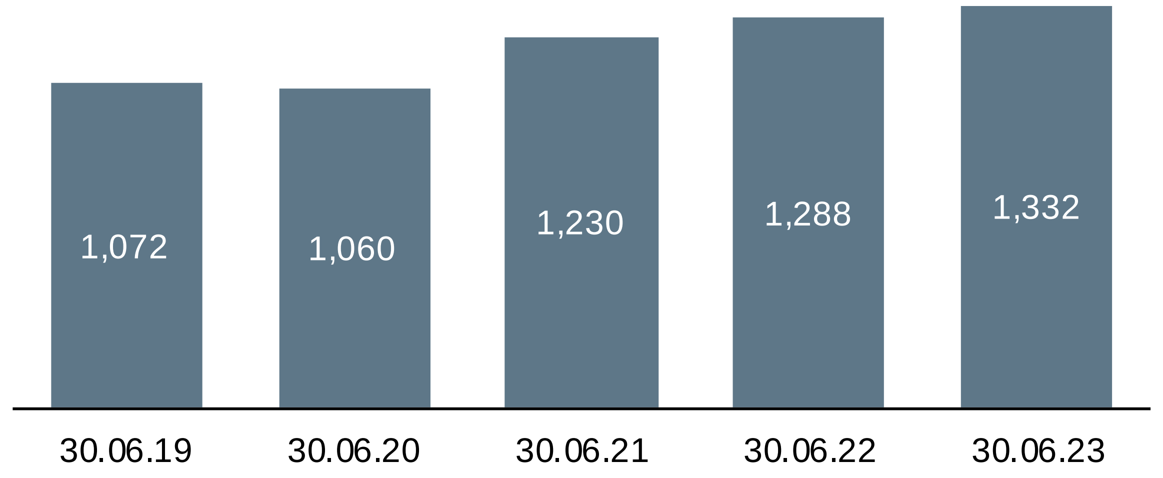
Net fee and commission income (ISK m)



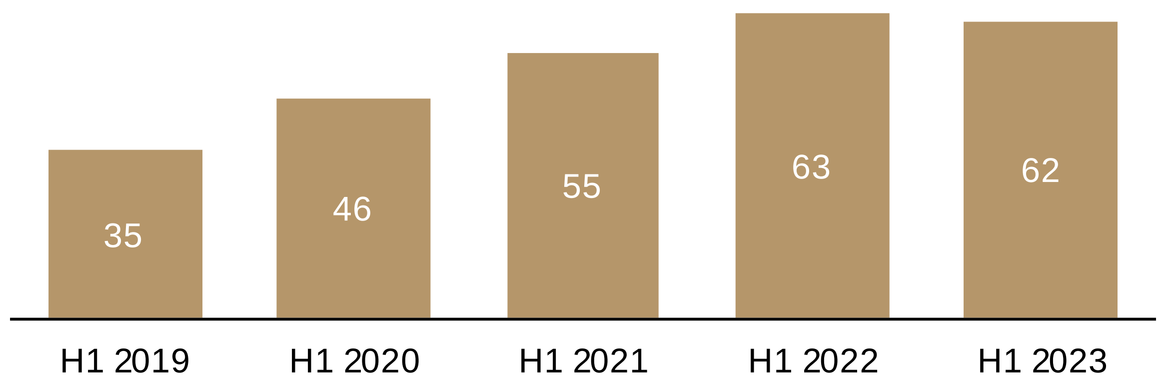
Net fee and commission income (ISK m)



Assets under management (ISK bn)



Net fee and commission income / Total operating expenses* (%)



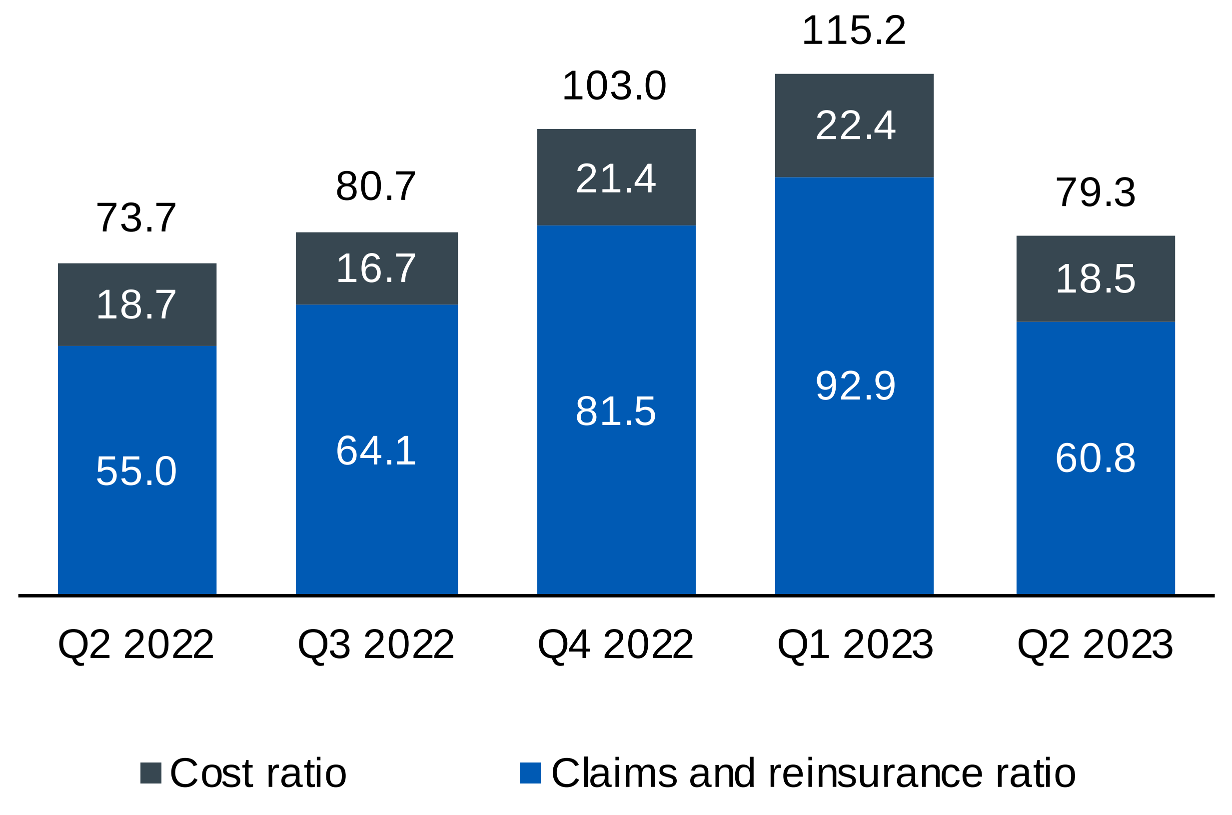
*Operating expenses from insurance operation included in H1 2022 and H1 2023 figures for comparative purposes

Insurance service results

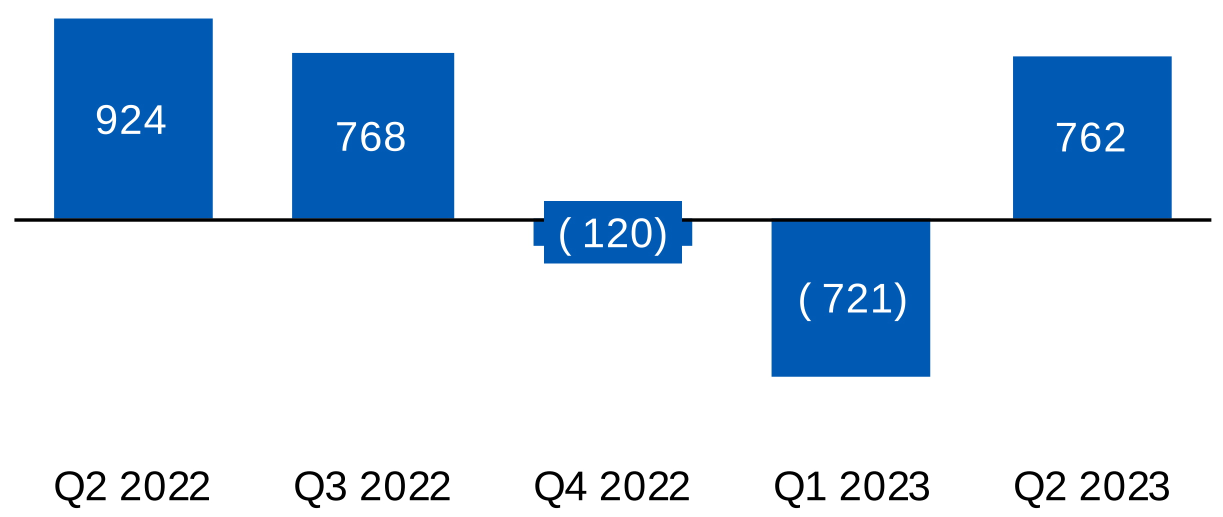
Positive traction in bancassurance journey

- Change in presentation of insurance results due to adoption of IFRS 17. Comparative historical information has been restated
- Strong growth of 14.4% in premiums written YoY and 12.6% insurance revenue
  - Corporate sales have increased considerably following the transition of the corporate insurance team to Arion Bank’s CIB division. Strong synergies provide early bancassurance benefits
  - Sales through the Arion app and web are picking up and will gain further momentum through product and service development over coming years
- Claims seasonally volatile but showing signs of normalizing post challenging quarters
- Cost ratio which was impacted by one-off items in recent quarters also stabilizing
- Combined ratio was 96.7% in H1 2023 compared with 94.4% in H1 2022

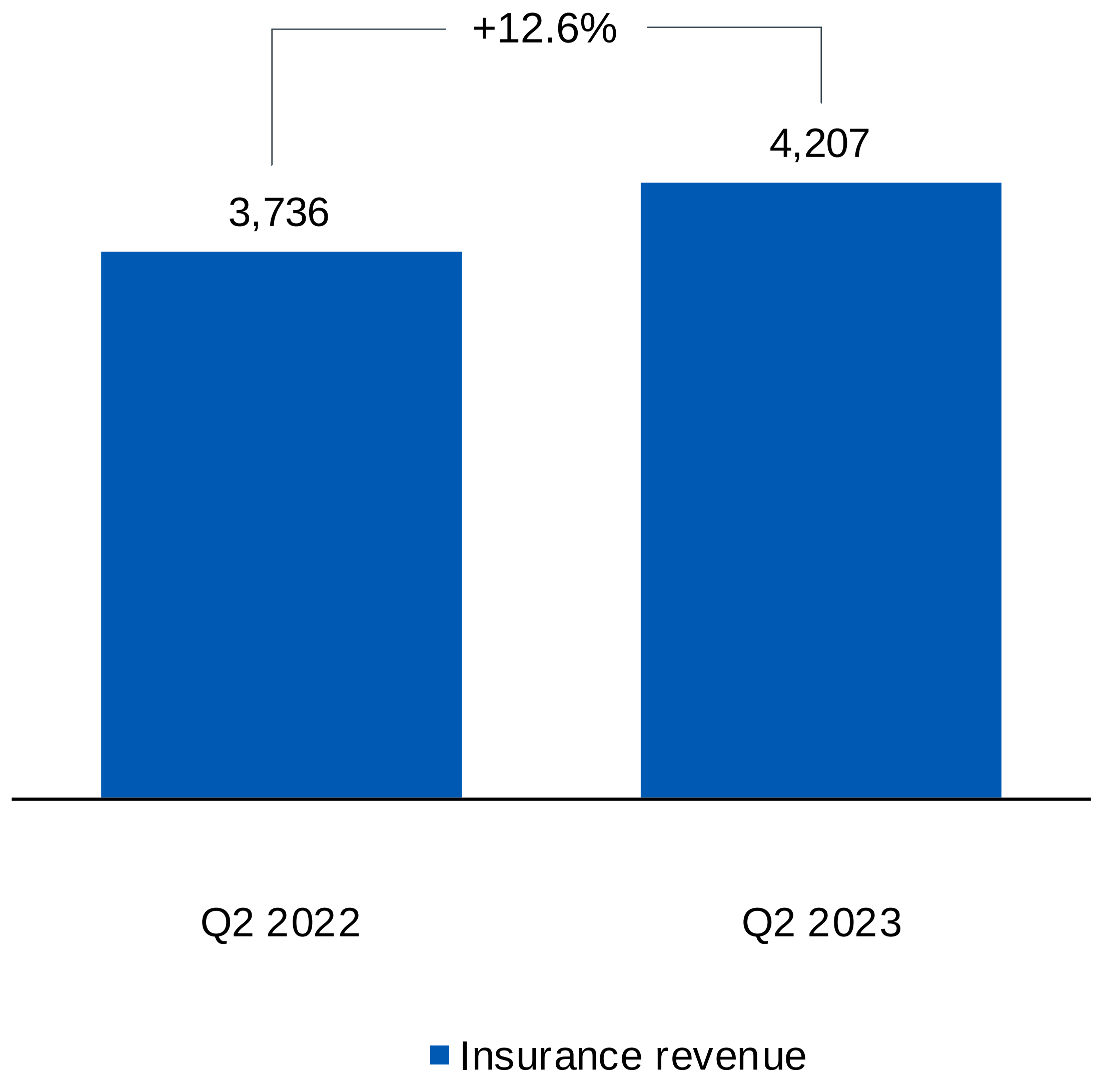
Combined ratio (%)



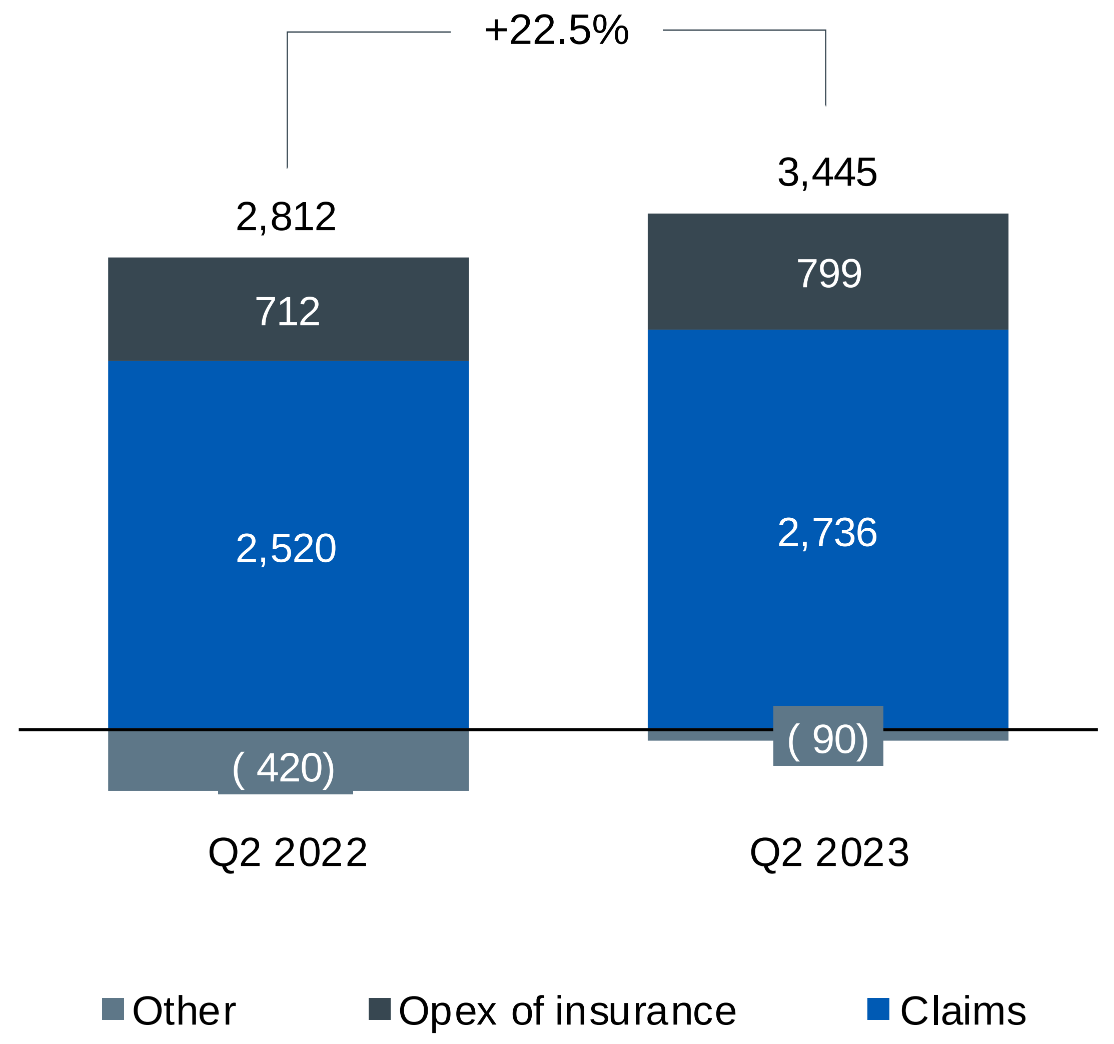
Insurance service results



Insurance revenue



Insurance service expenses net of reinsurance



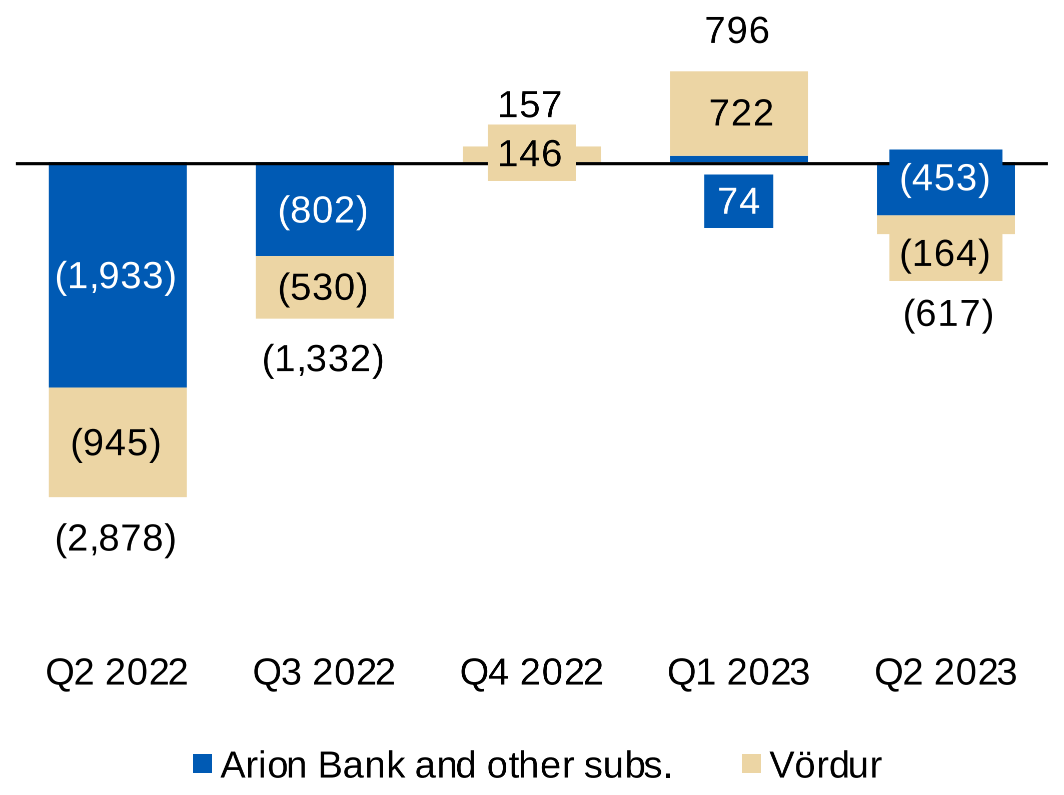
 All amounts in ISK m

Net financial income

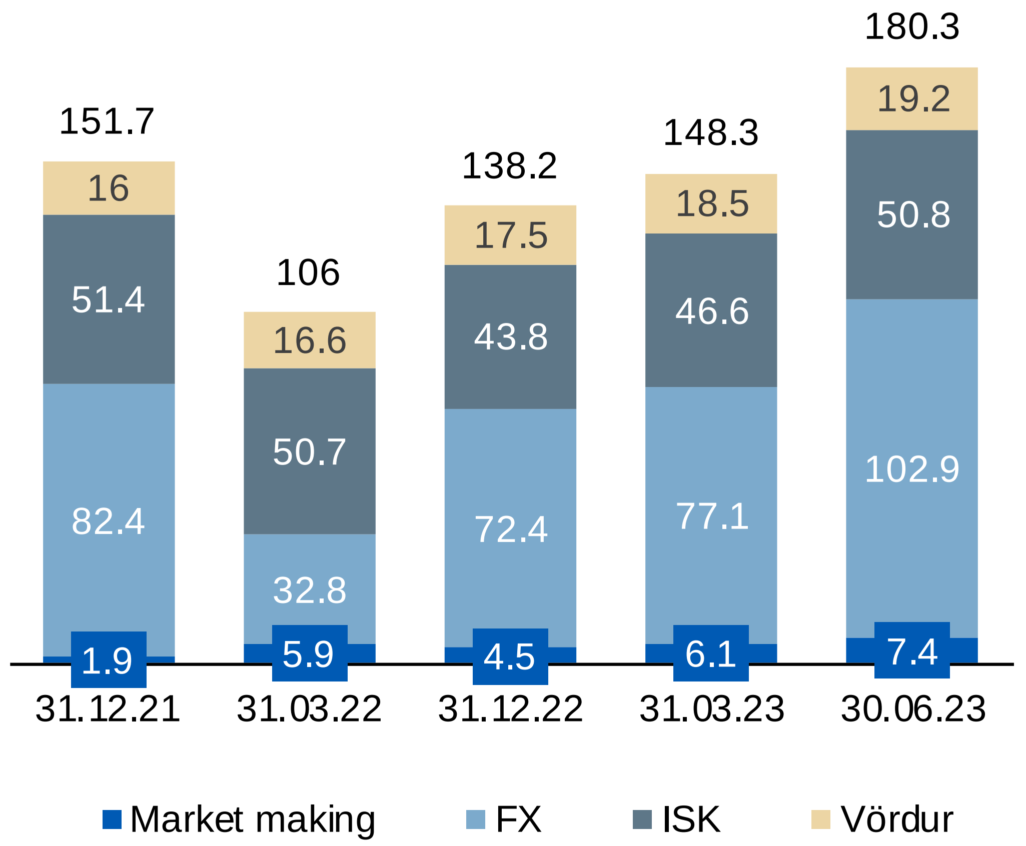
Continued market volatility impacts results while equity holdings at Bank level are reduced

- Another challenging quarter, especially for equity positions with total financial loss of ISK 617m
- Bond holdings fluctuate between quarters in line with liquidity management
  - No held-to-maturity (HTM) accounting within bond portfolio, with all market value changes incorporated in capital position
  - Average duration of liquidity portfolio within one year
- Total investment portfolio of Vördur is ISK 26.3bn; ISK 19.2bn of bonds and ISK 7.3bn in equity instruments, yielding a loss of ISK 164m in the quarter
- Largest unlisted equity holdings currently held at Bank level are Controlant hf., Ísfélag hf. (previously Rammi hf.) and Carbon Recycling International (CRI hf.)
- The Bank expects to realize profit in Q3 from Kerecis warrants amounting to approximately ISK 560m

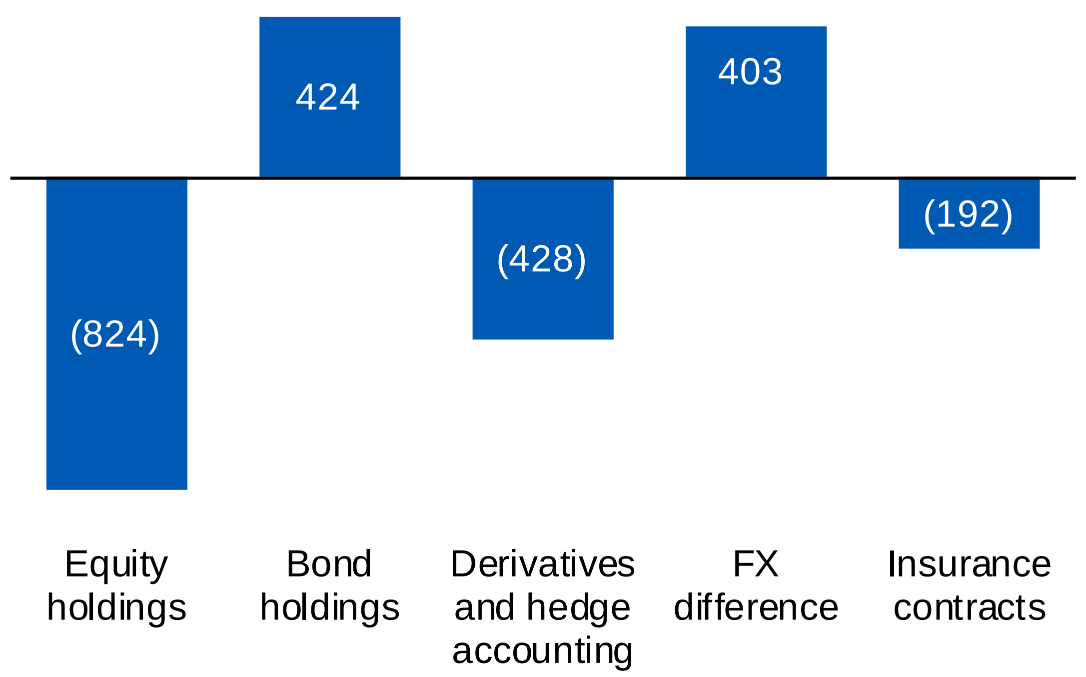
Net financial income (ISK m)



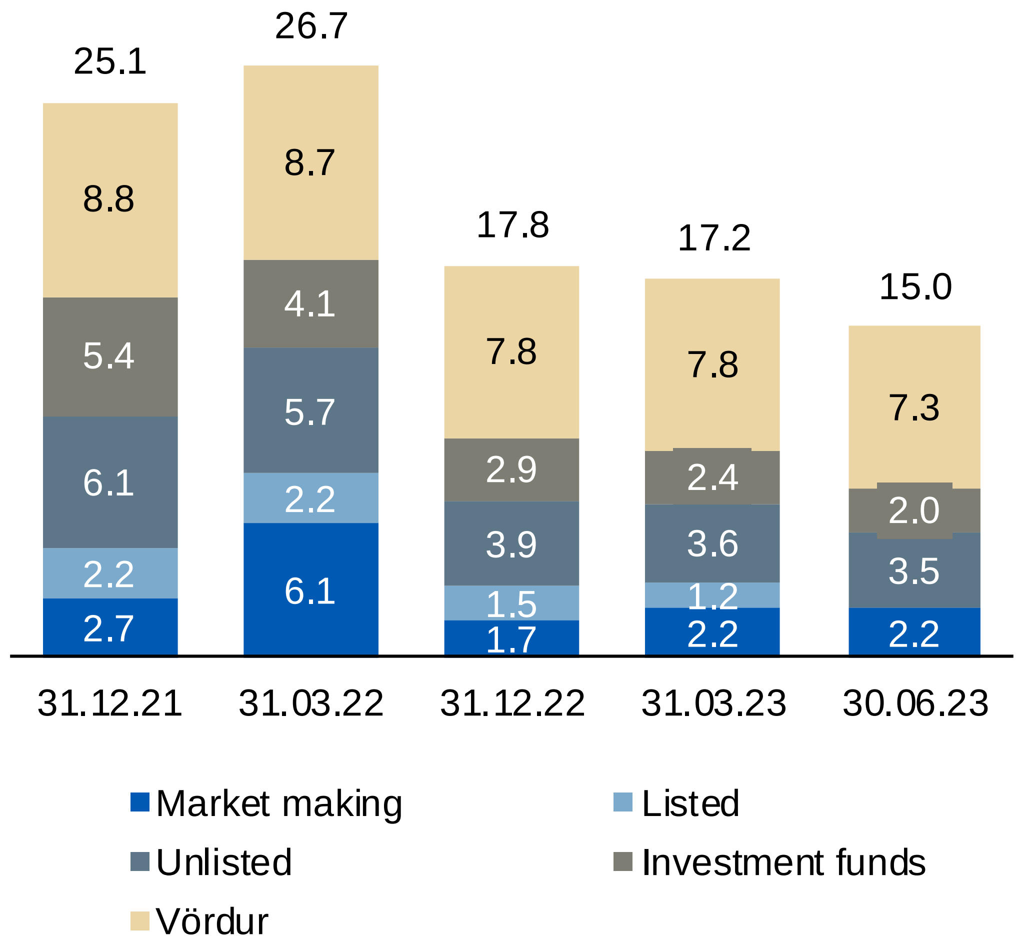
Bond holdings



Net financial income by type Q2 2023 (ISK m)



Equity holdings



 All amounts in ISK bn

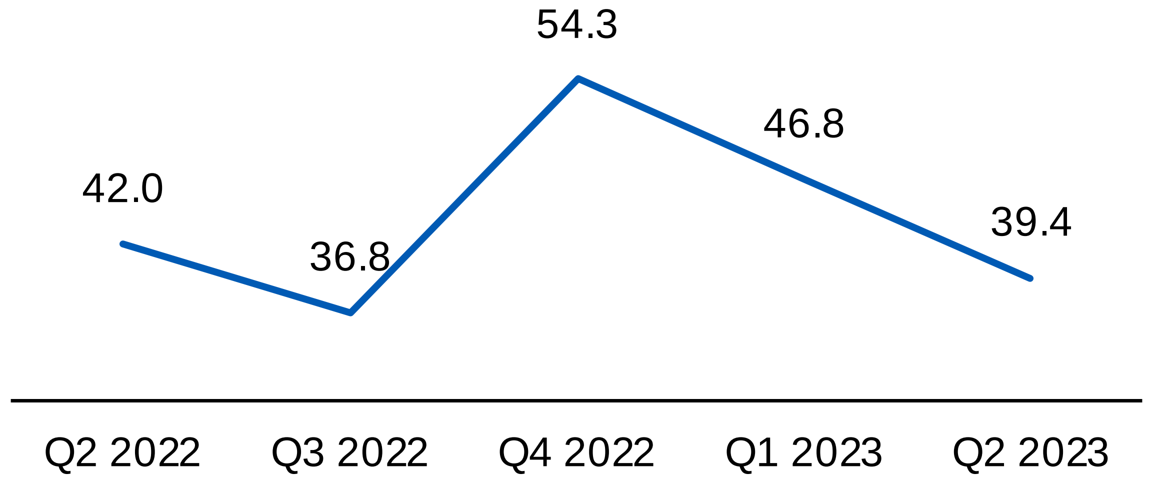
Operating expenses*

A return to a more normalized quarter following Q1 which was impacted by one-off items

- Total operating expenses outlined here include costs related to insurance business which is accounted for through insurance service results post IFRS17
- Ongoing focus on OPEX and efficiency
  - Cost-to-core income for Q2 was 39.4% compared with 42.0% in Q2 2022 and 46.8% in Q1 2023
  - Core income per employee has been increasing steadily in recent years
- Q1 2023 expenses were impacted by several one-off items
- Salary expense increases between years mainly due to new labor agreements and increased number of FTE's, mostly in IT

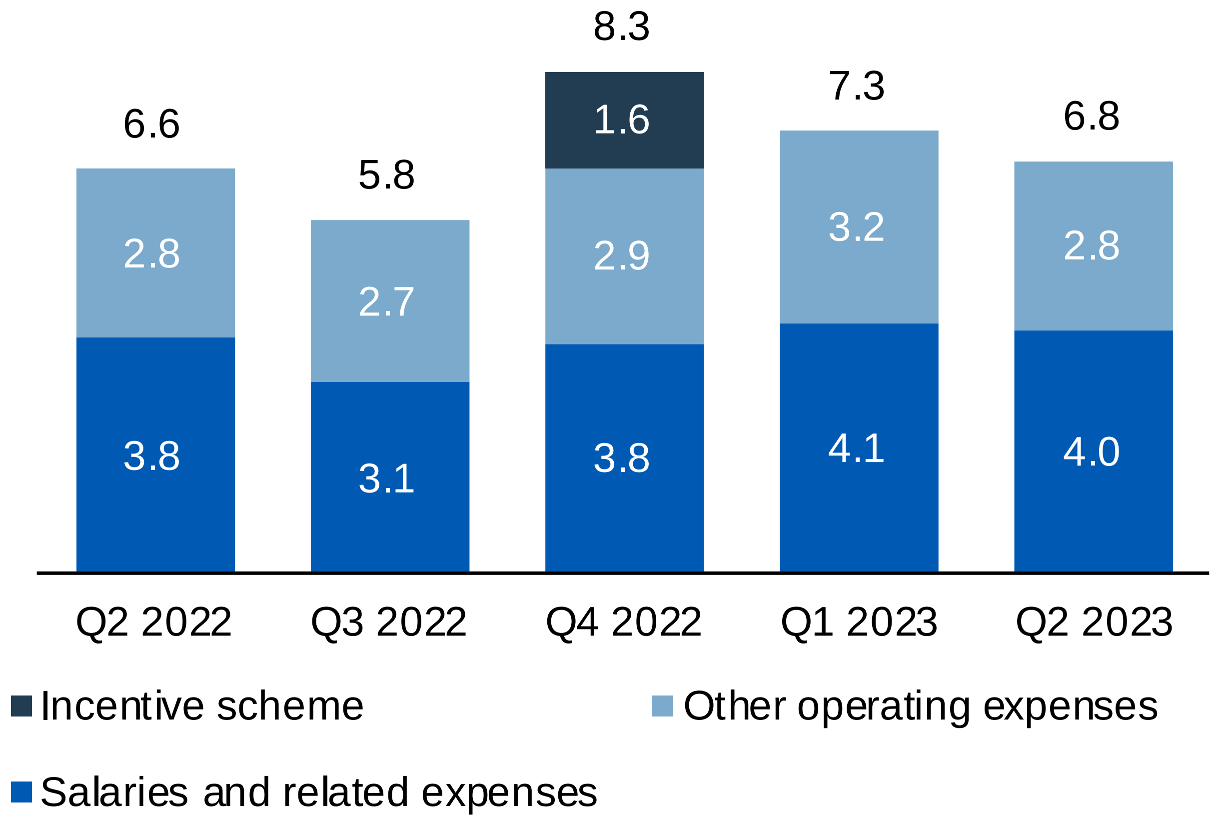
*Operating expenses from insurance operations are included in all figures for comparative purposes

Cost-to-Core income ratio** (%)

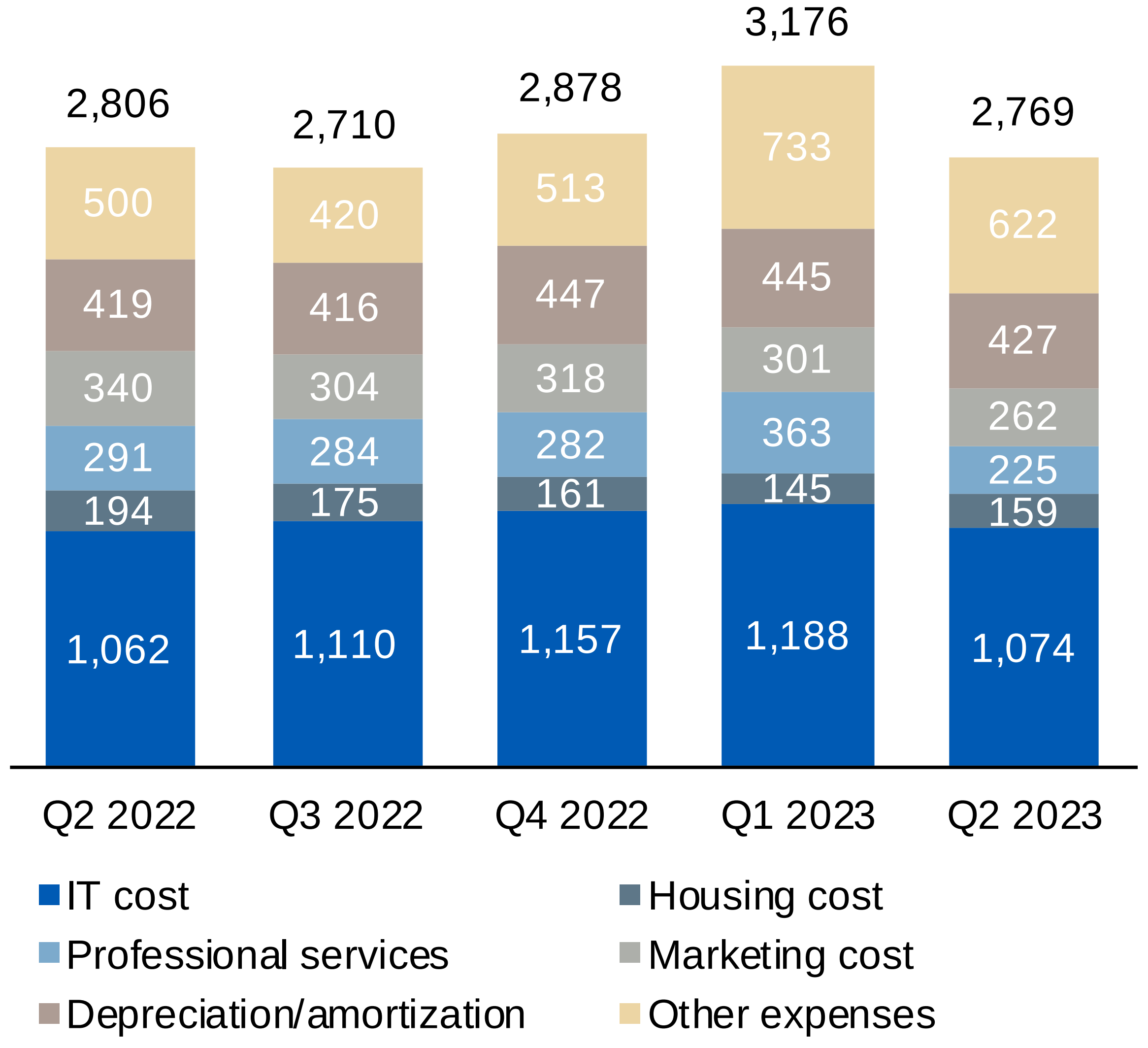


** Cost-to-core income ratio in Q4 2022 excluding incentive scheme was 43.8%

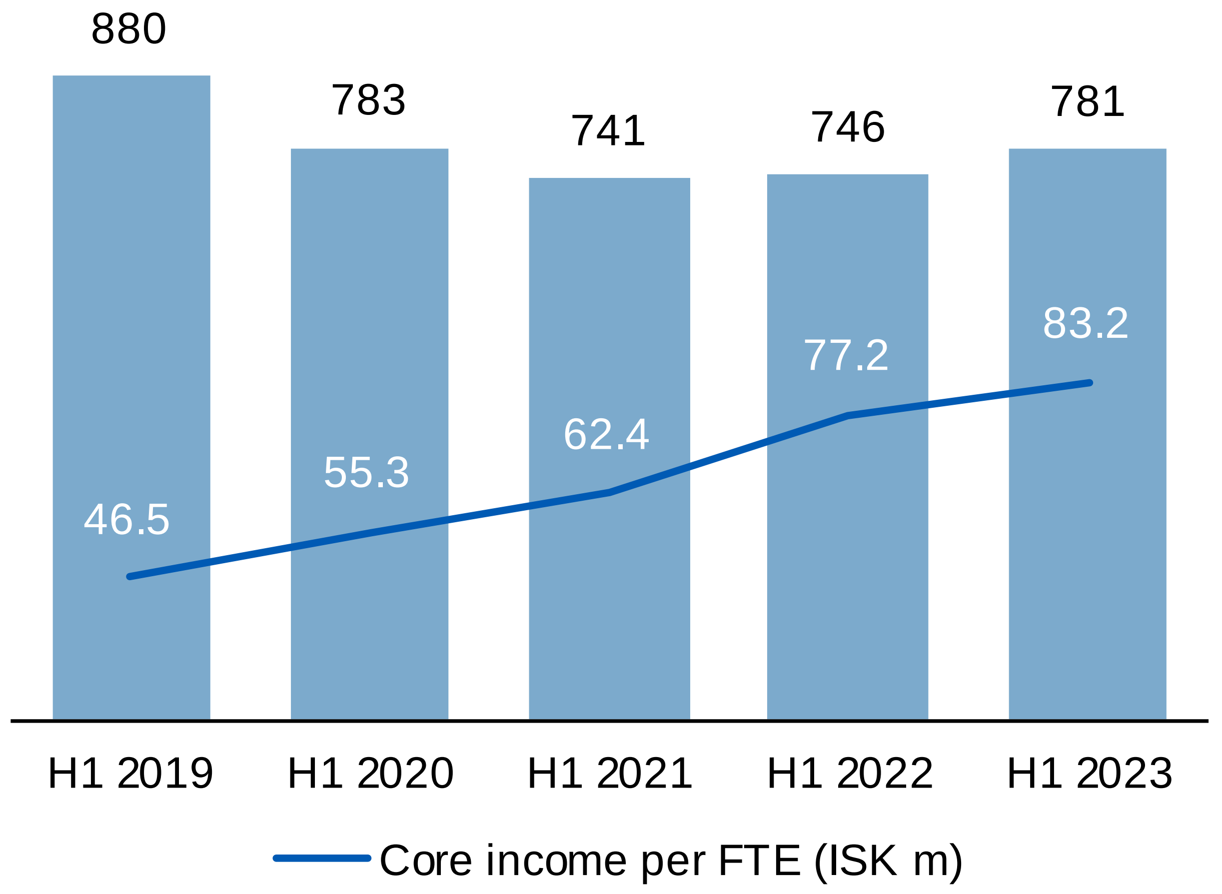
Total operating expenses



Other operating expenses (ISK m)



Core income per FTE



Balance sheet

Deposit position supports lending growth

- Robust and relatively simple balance sheet
- Loan growth supported by ongoing strong deposit position
  - Loans to customers increased by 1.9% in Q2
  - Deposits increased by 0.8% in Q2
- Liquidity position remains strong:
  - Liquidity coverage ratio (LCR) of 163% (106% in ISK)
  - Net stable funding ratio (NSFR) of 118%

Assets	**30.06.2023**	**31.03.2023**	**Diff.**	**31.12.2022**	**Diff.**	**30.06.2022**	**Diff.**
Cash & balances with CB	76	80	(5%)	114	(33%)	78	(2%)
Loans to credit institutions	43	63	(31%)	46	(5%)	40	8%
Loans to customers	1,135	1,114	2%	1,085	5%	1,011	12%
Financial assets	226	205	10%	193	17%	204	11%
Other assets	38	38	(1%)	28	36%	51	(25%)
Total Assets	**1,518**	**1,501**	1%	**1,466**	4%	**1,383**	10%

Liabilities and Equity							
Due to credit institutions & CB	22	24	(10%)	12	86%	5	371%
Deposits from customers	781	775	1%	755	3%	727	7%
Other liabilities	77	84	(8%)	71	9%	72	7%
Borrowings	406	391	4%	393	3%	363	12%
Subordinated liabilities	46	47	(0%)	47	(2%)	33	39%
Total Liabilities	**1,332**	**1,321**	1%	**1,278**	4%	**1,200**	11%
Equity	186	180	4%	188	(1%)	183	2%
Total Liabilities and Equity	**1,518**	**1,501**	1%	**1,466**	4%	**1,383**	10%

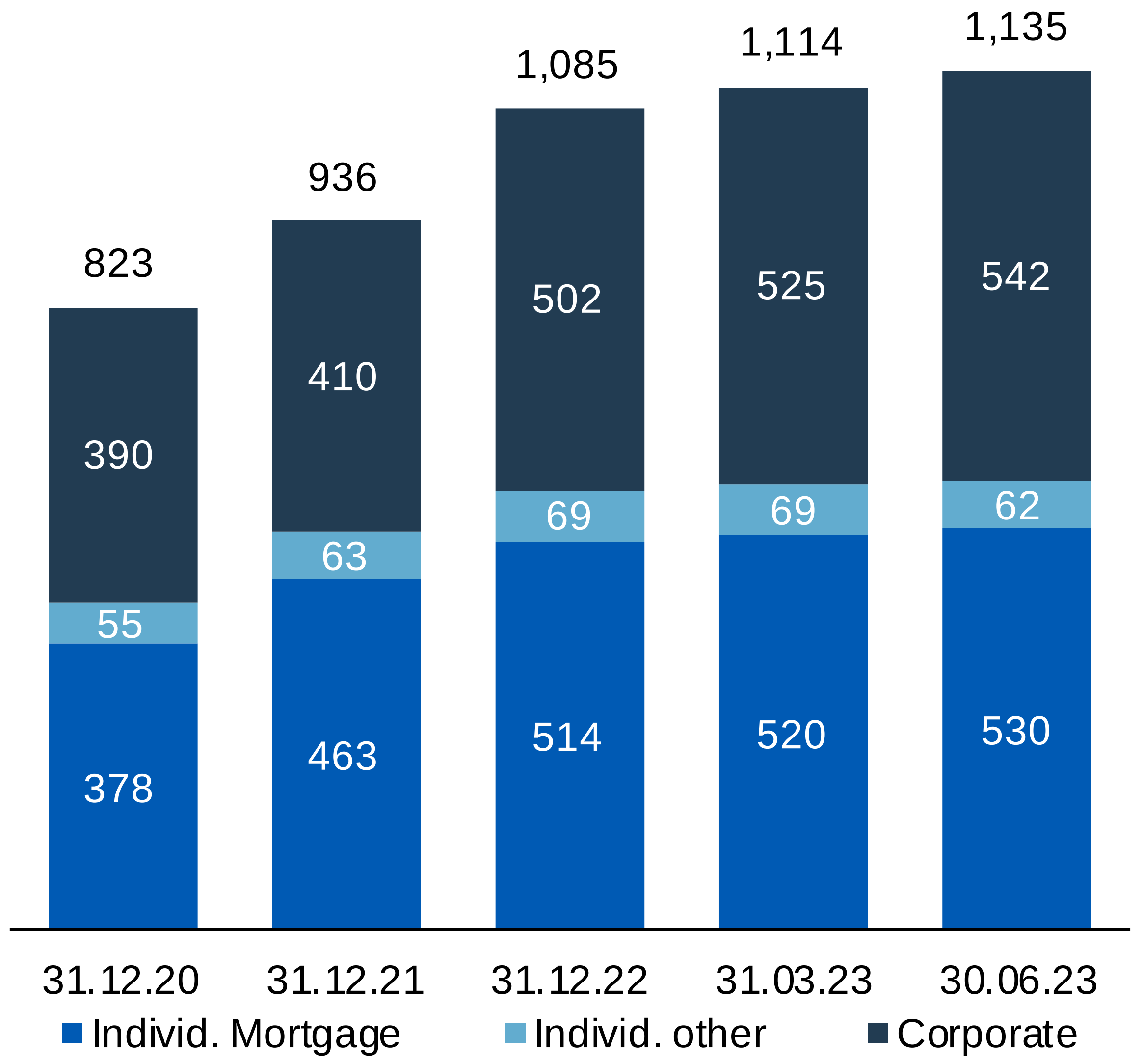
 All amounts in ISK bn

Loans to customers

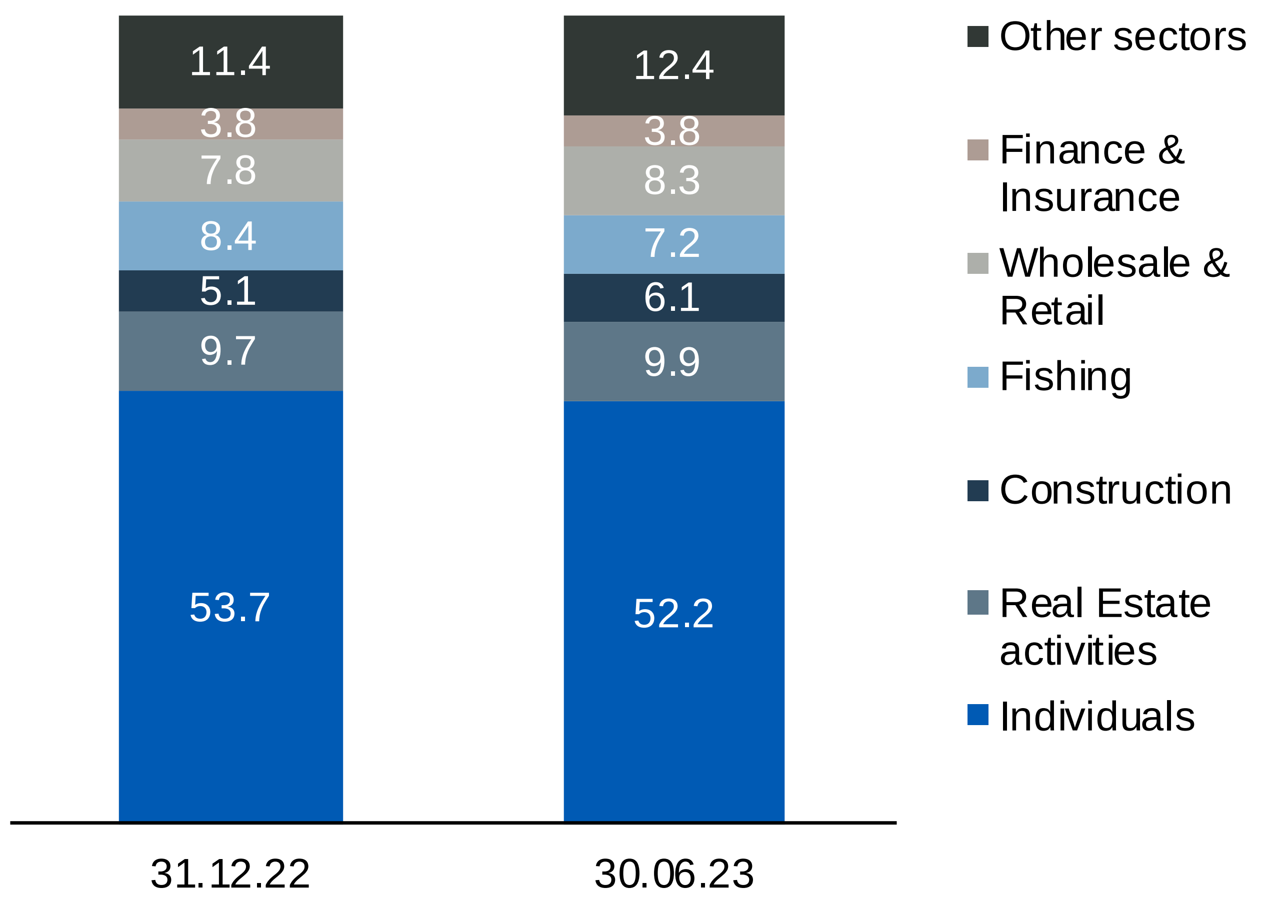
Combination of factors resulting in reduced loan growth over past quarters

- Loans to customers increased by ISK 20.5bn or 1.8% during the quarter
    - Loans to corporates by ISK 17bn or 3.2% and loans to individuals by ISK 3 bn or 0.6%
    - Total loans increased by ISK 8.9bn due to inflation, of which ISK 7.1bn mortgage lending. FX loans decreased by ISK 0.6bn during the quarter due to stronger ISK, primarily corporate loans
- The diversification of the corporate loan book continues to be good and in line with the Bank's credit strategy

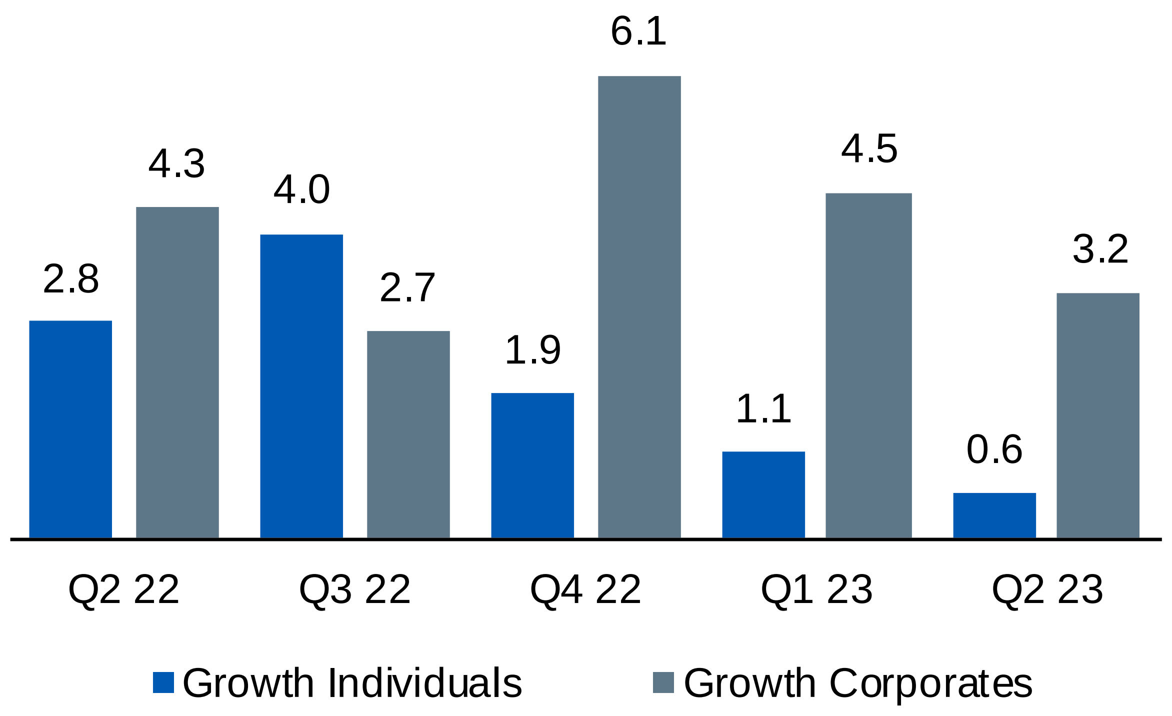
Loans to customers



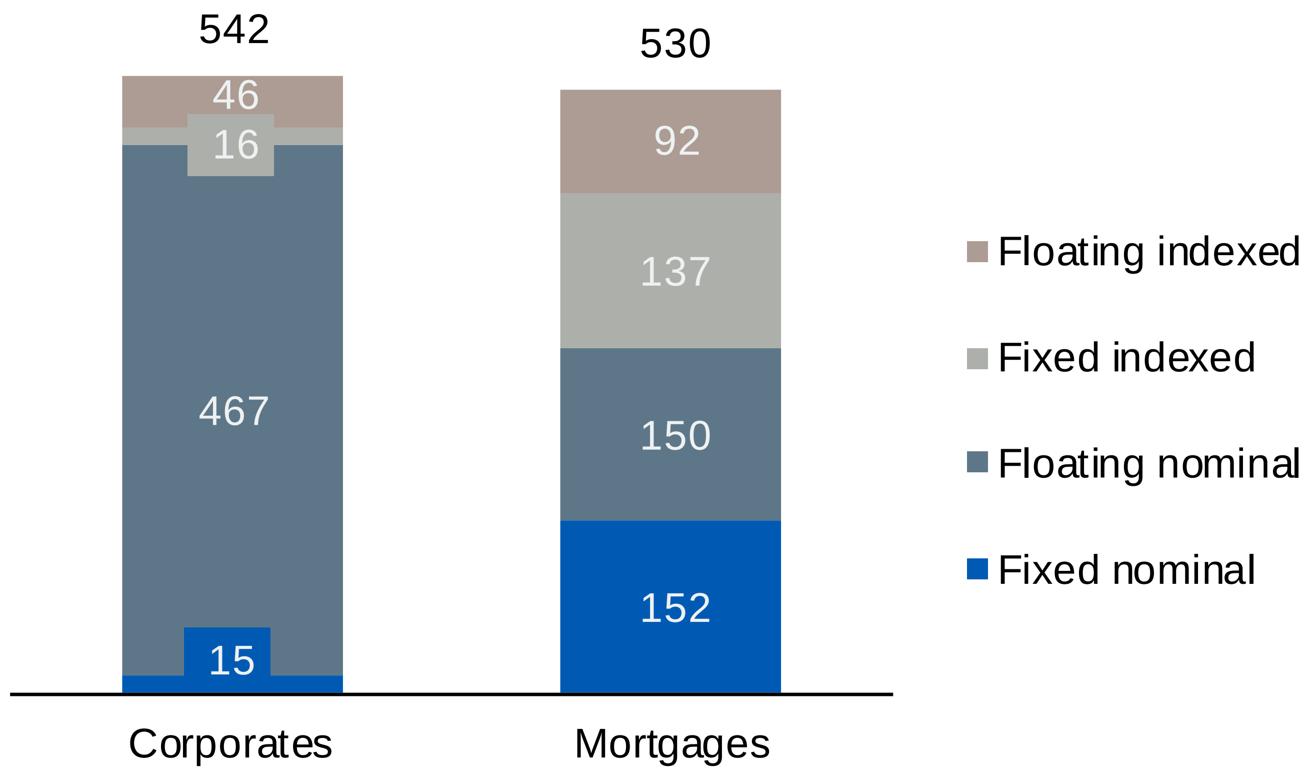
Loans to customers by sector (%)



Loan growth (%)



Loans to customers by interest rate type at period end



Residential mortgages

Low default rates and comfortable LTV levels, but rising costs for borrowers

Macroprudential measures:

- Loan-to-value capped at 80% (85% for first-time buyers, which was already applied by Arion)
- Debt service-to-income < 35% (40% for first-time buyers). In June 2022, the Central Bank introduced prescribed minimum interest rates for debt-service which primarily affects indexed loans.
- Affects mostly first-time buyers and higher loan applications

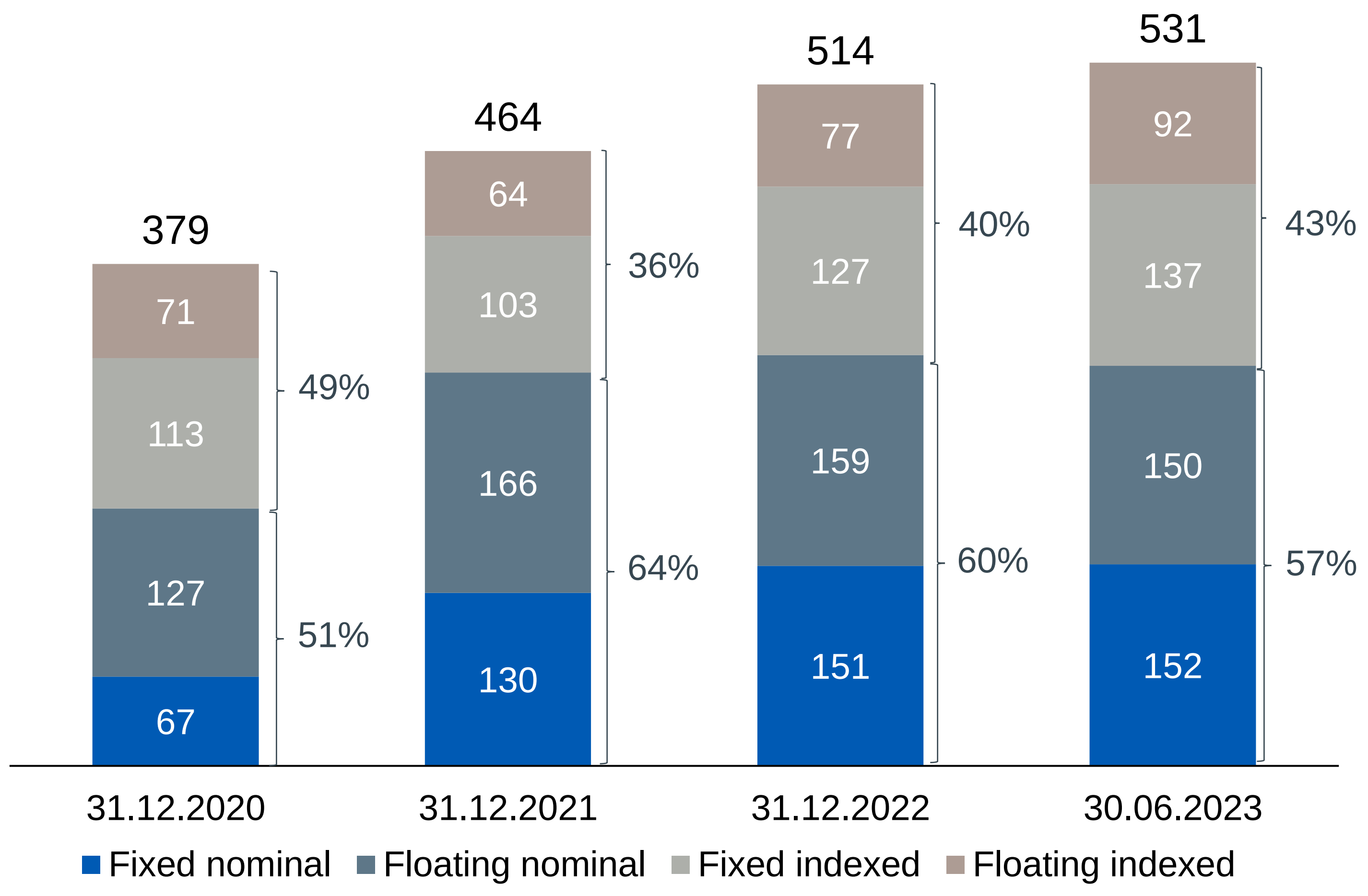
Furthermore, the Bank has adjusted its criteria for household expenditures in its payment assessment, taking into account rising cost of living.

Internal stress test of fixed nominal portfolio shows that if interest rates remain high into 2025, up to one third of borrowers need to seek lower monthly payments, e.g., through refinancing to indexed loans.

- In this stress test floating nominal rates reach a maximum of 10.7%
- The stress test reveals that, following refinancing to lower debt servicing, further measures may be needed for 0.5-1% of borrowers

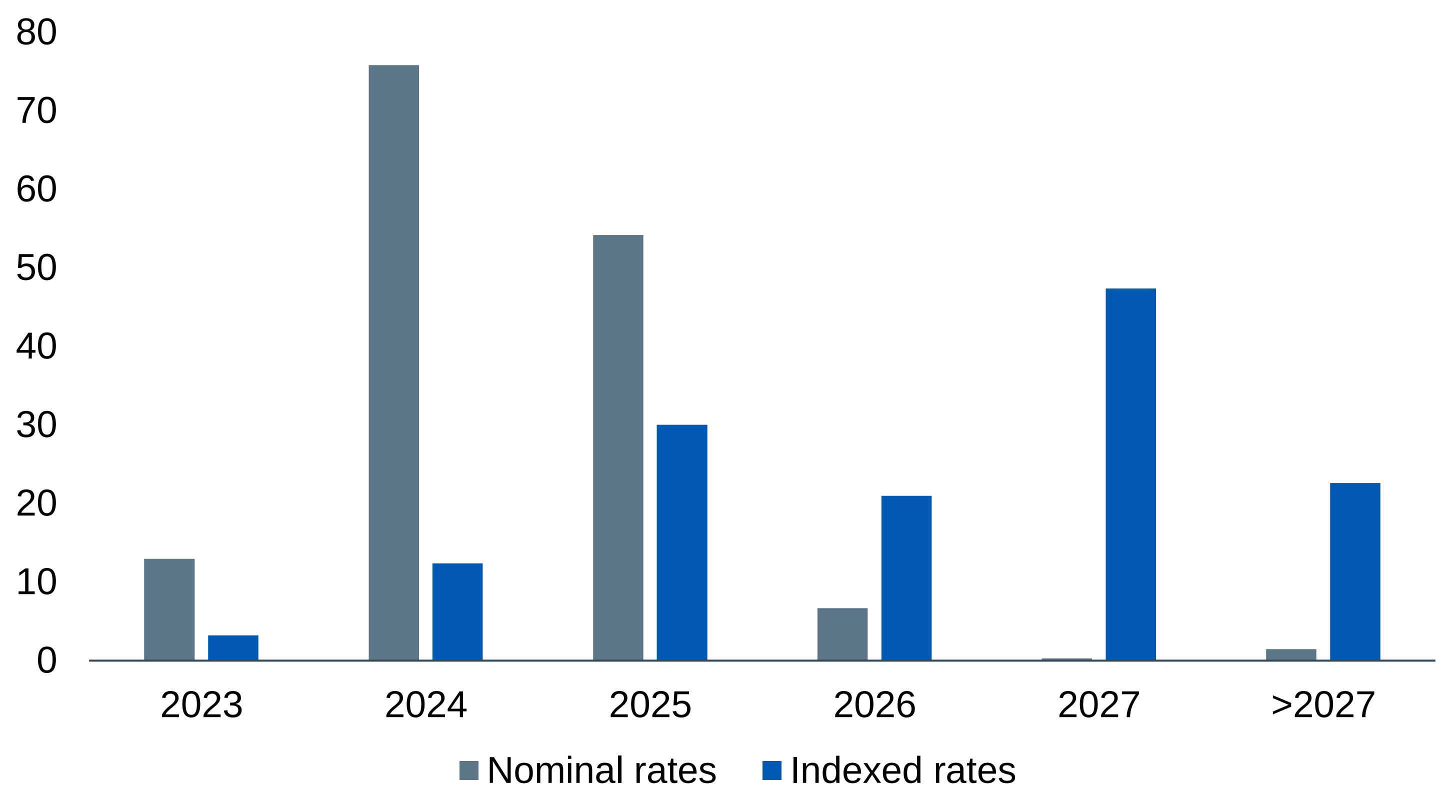
Residential mortgages by interest rate type (ISK bn)

Nominal rate loans are 57% of the mortgage portfolio at end of Q2 2023. Demand for indexed loans is picking up again.



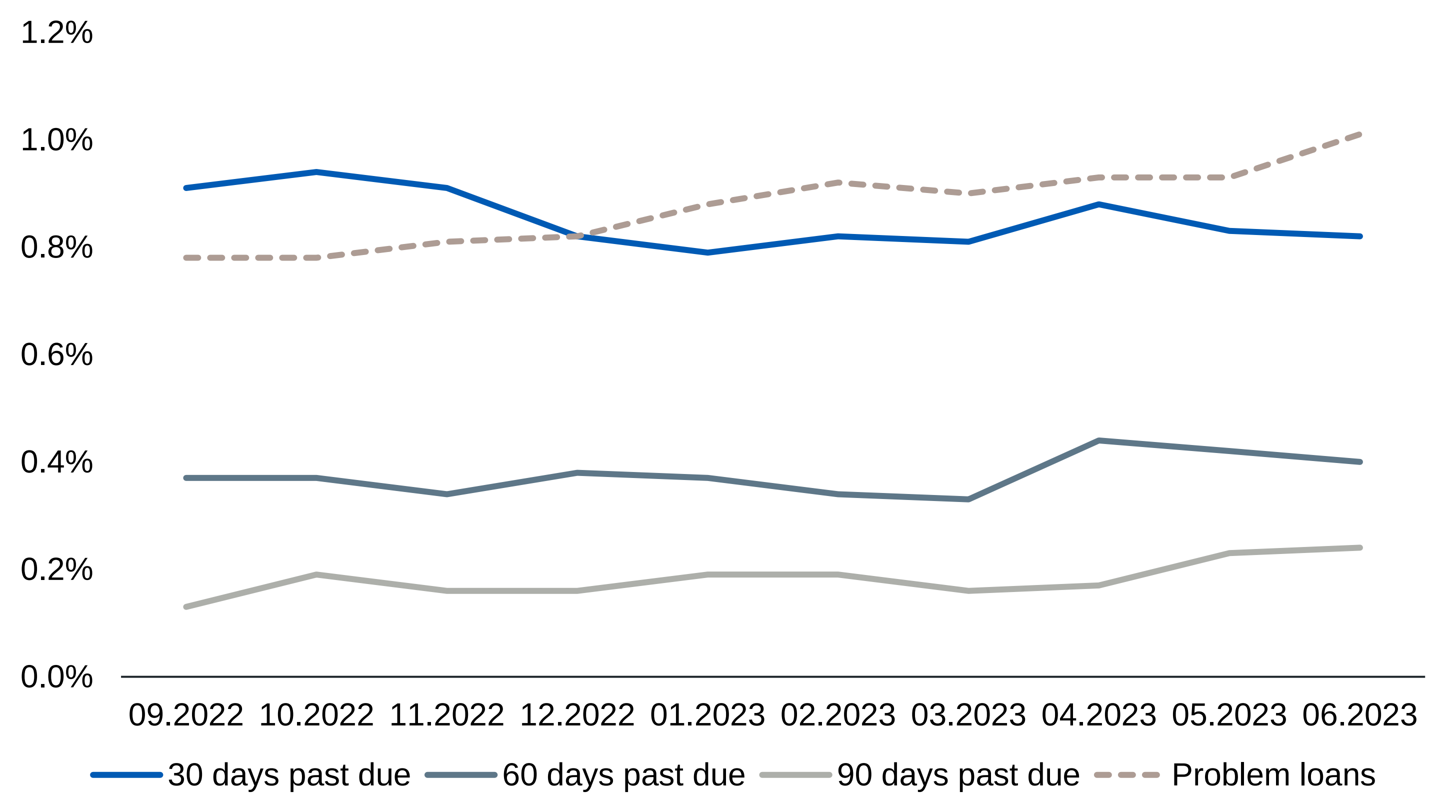
Interest rate reset profile for fixed rate mortgages (ISK bn)

The bulk of fixed nominal rate loans are reset in 2024 and 2025.



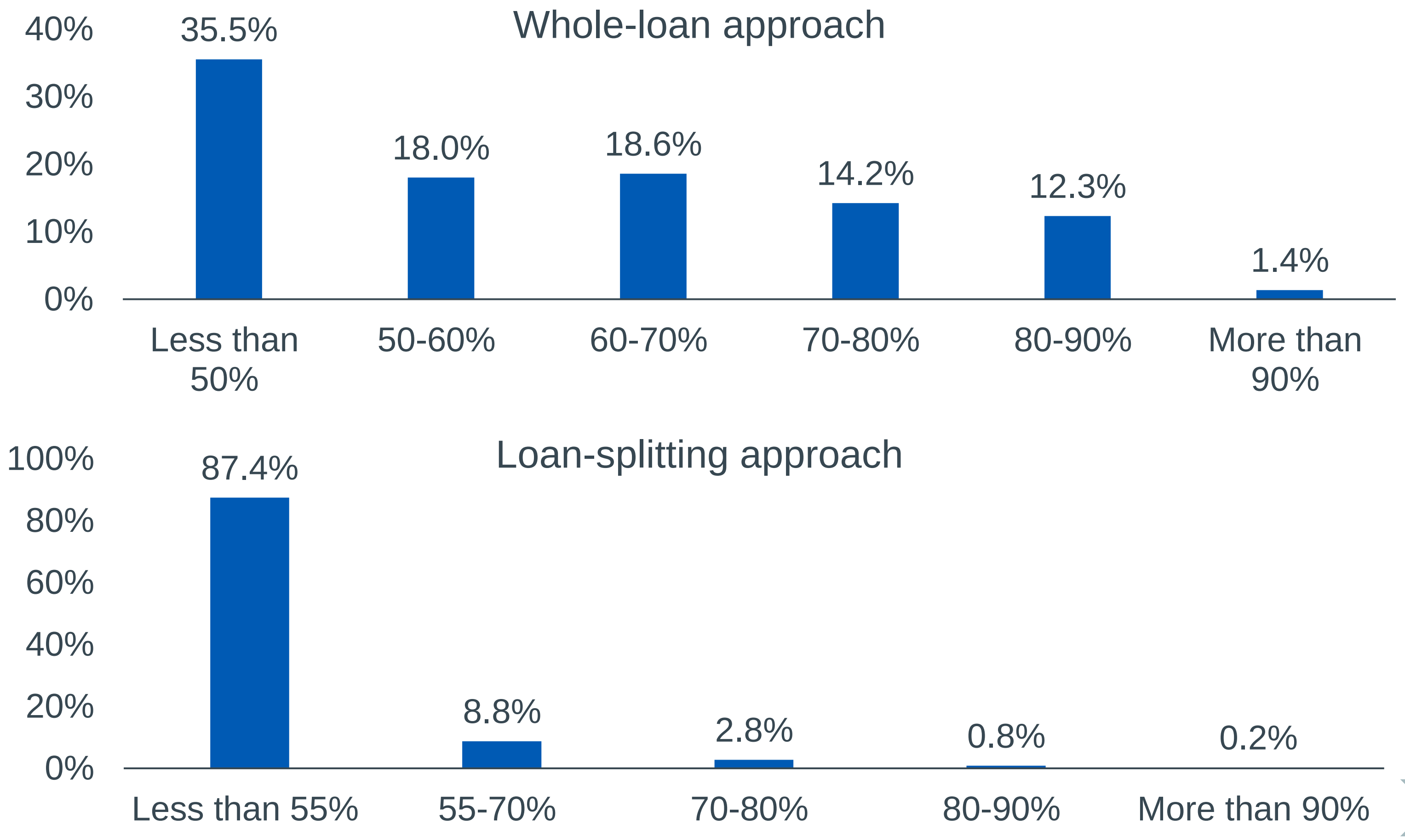
Rate of defaults and payments past due

Non-performing loans are 1.0% of the mortgage portfolio with a slight trend upwards from YE 2022.



Loan to value distribution

Loan-to-value below 80% accounts for 86% of the mortgage portfolio (whole-loan approach).

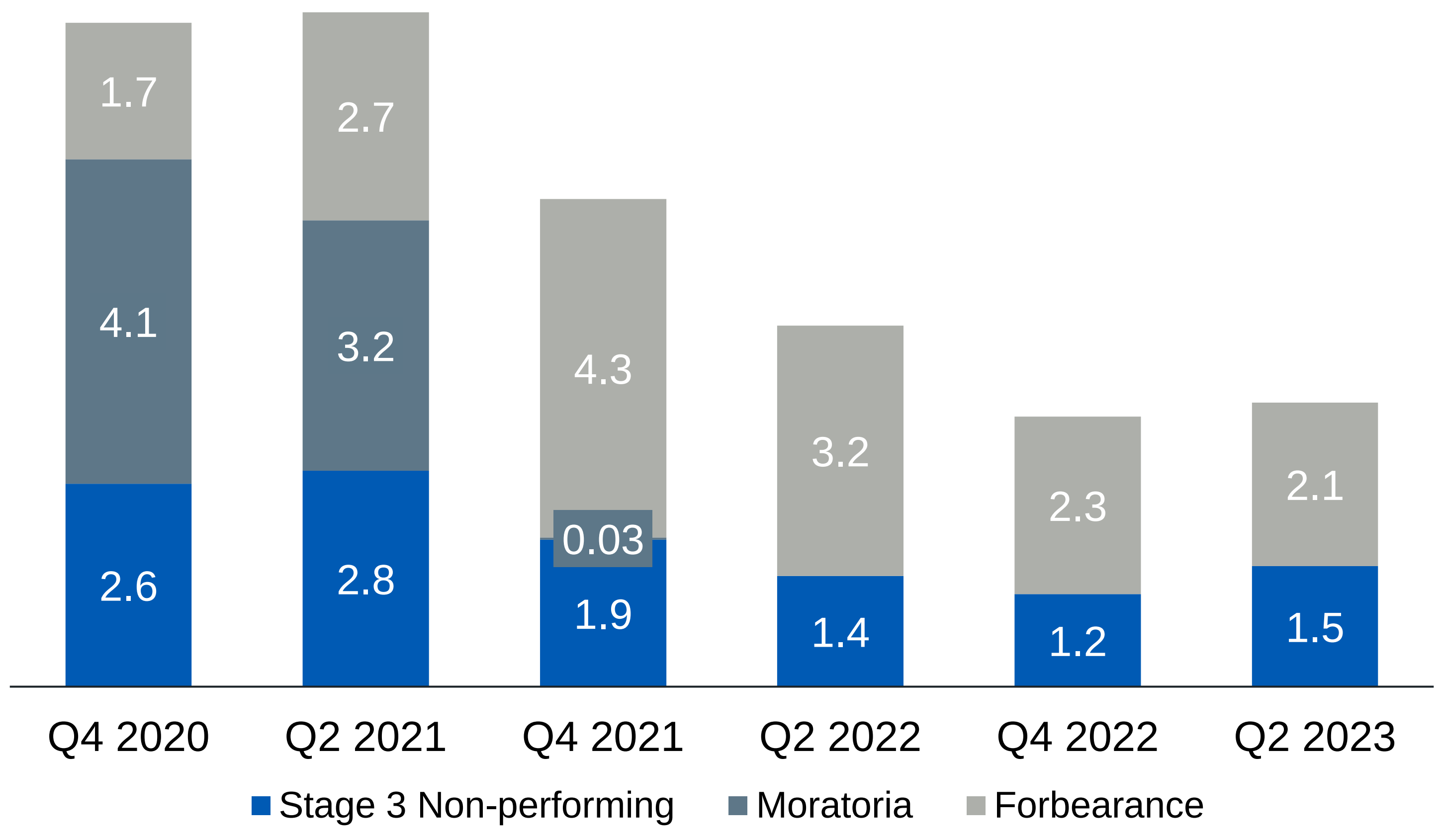


Risk profile

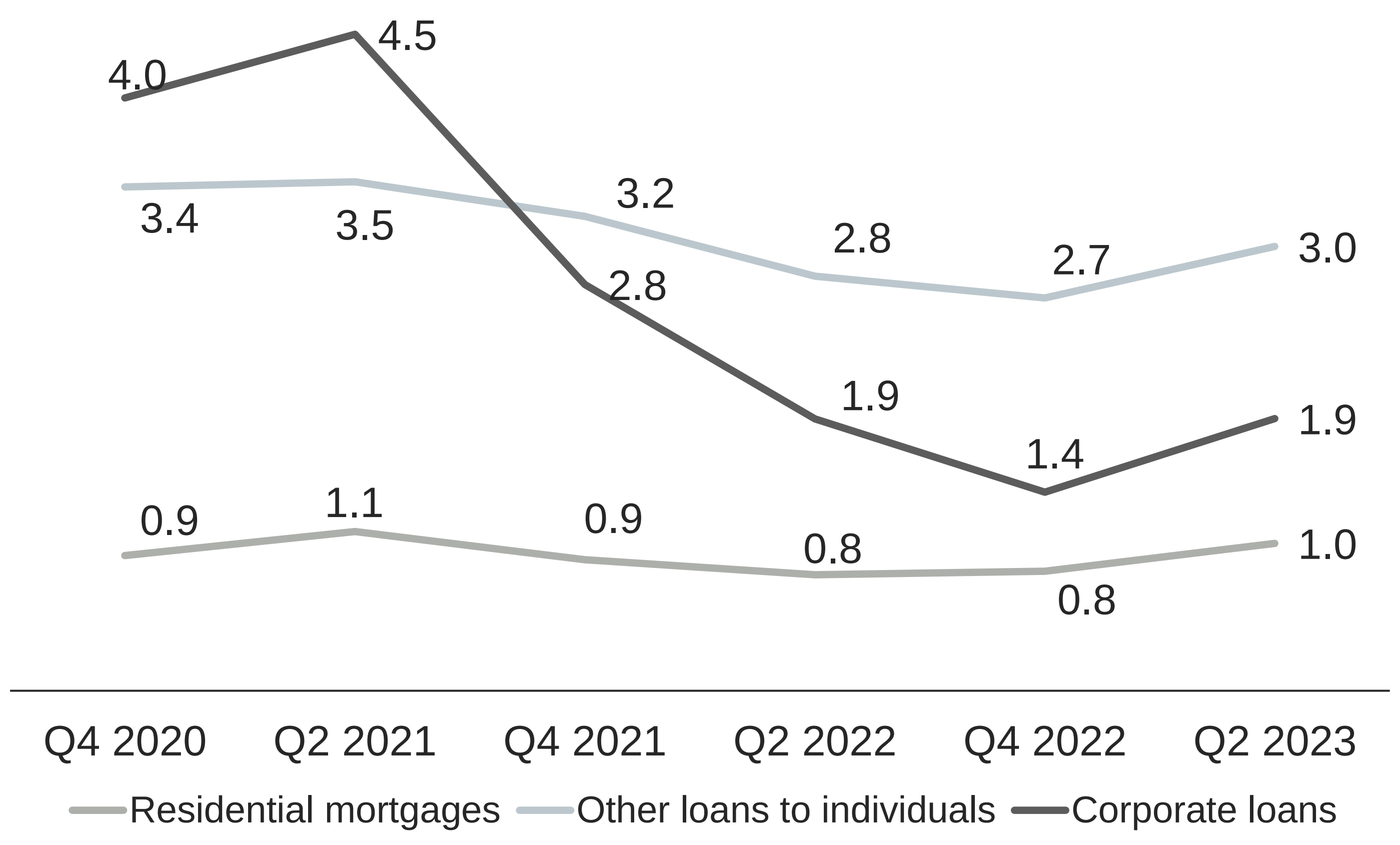
Strong credit quality indicators while a slight trend towards higher rate of payments past due observed

- Despite increased provisioning through management's forward looking macro-economic assumptions, risk indicators of credit quality remain at healthy levels.
- In H1 2023, the problem loans ratio increase for the first time since before Covid-19, especially for retail SME loans and loans to individuals. The ratios are however below long-term averages.
- Forborne exposures which are not in Stage 3 are 2.1% of loans to customers at 30.6.2023. The majority is in tourism related activities that are recovering from the impact of Covid-19.
- Total expected credit loss is expected to approach between 20-25bps in the long term based on current loan book composition. At the end of Q2 the expected 12-month credit loss ratio of 29bps reflects management's prudent view in the current economic conditions.
- Increased haircuts to real estate collateral results in increased provisions for residential mortgages.

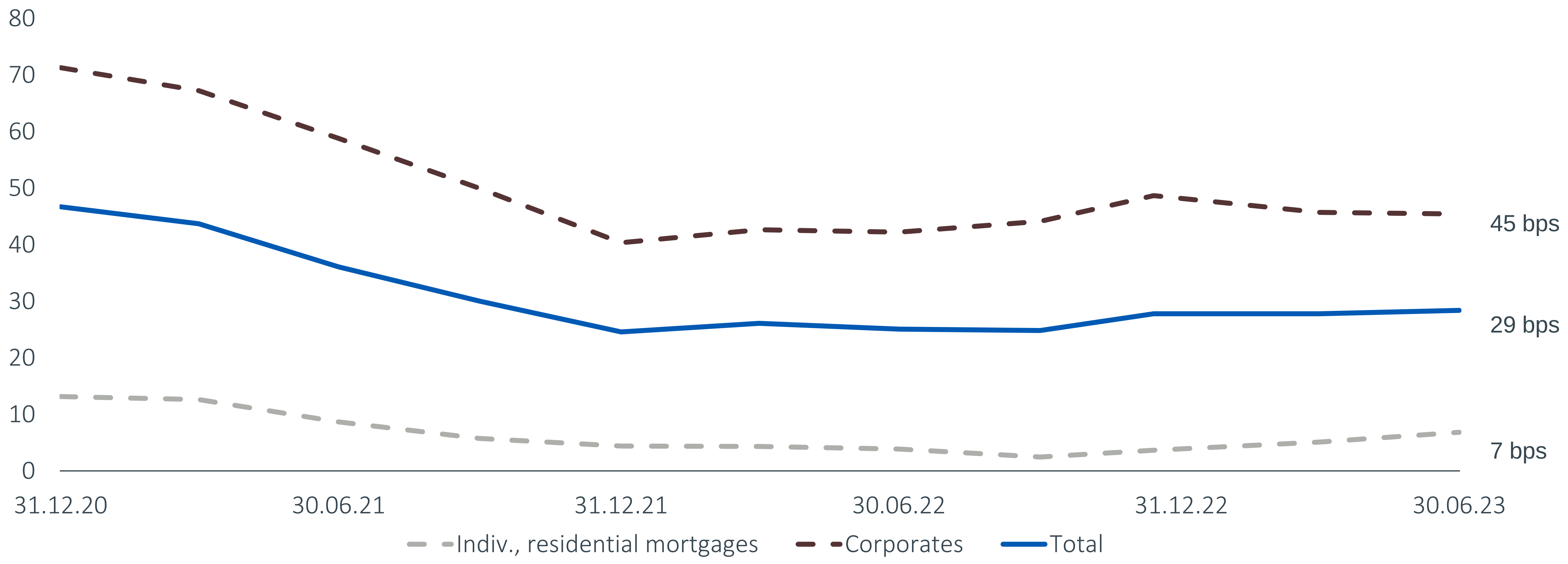
Development of non-performing loans, moratoria and forbearance (% of total loan book)



Development of problem loans ratio for loan portfolios
(% of relevant loan book)



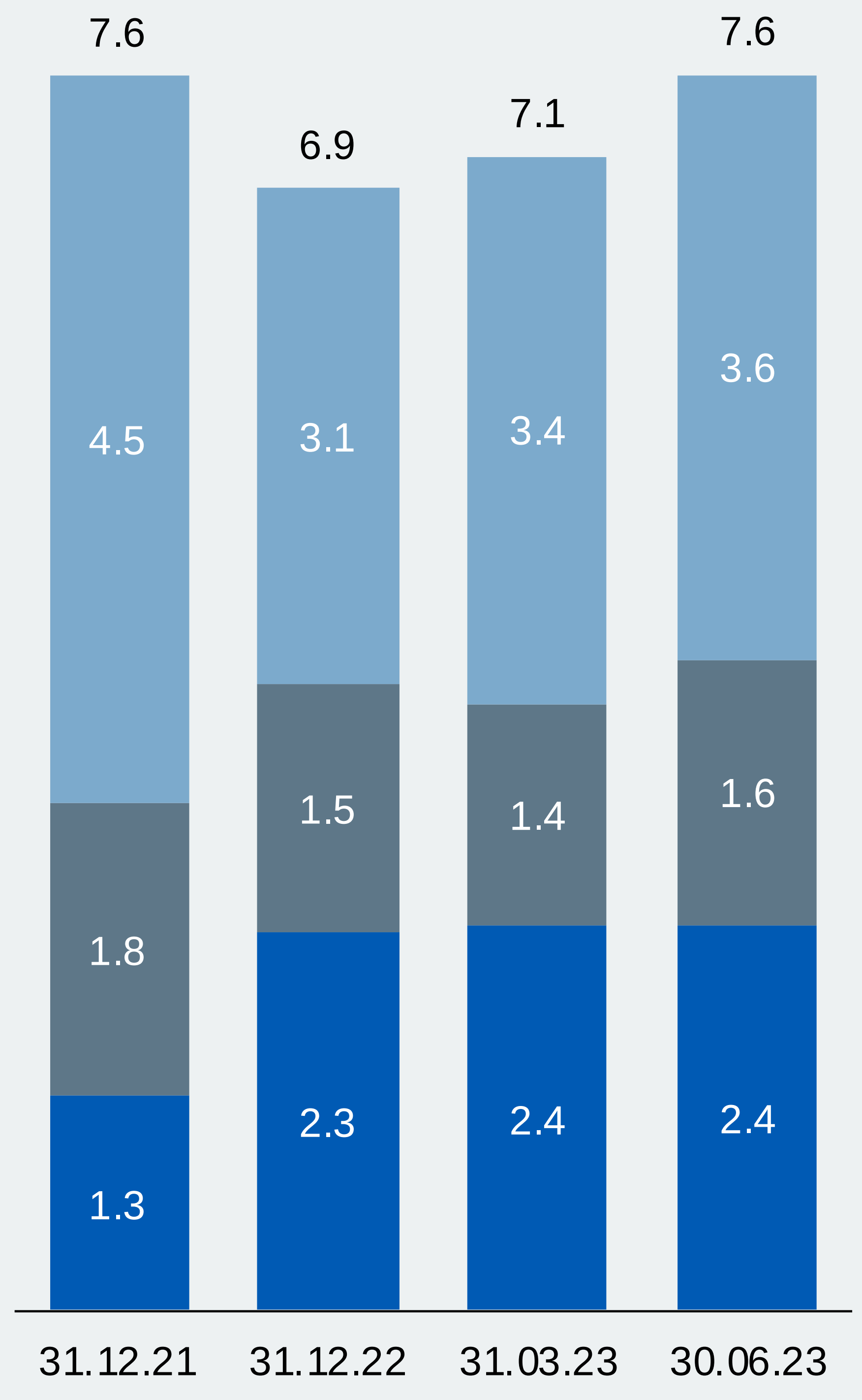
12-month expected credit loss for performing loans to customers (on balance sheet) (bps)



Loss allowance by IFRS 9 stages

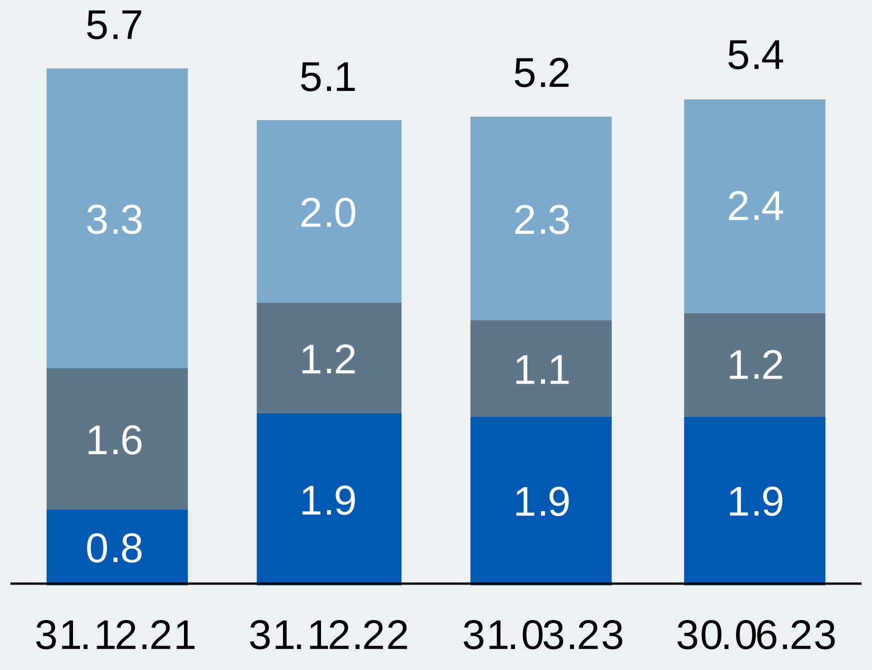
On loans to customers total

Loans to customers are 0.6% provisioned at period end



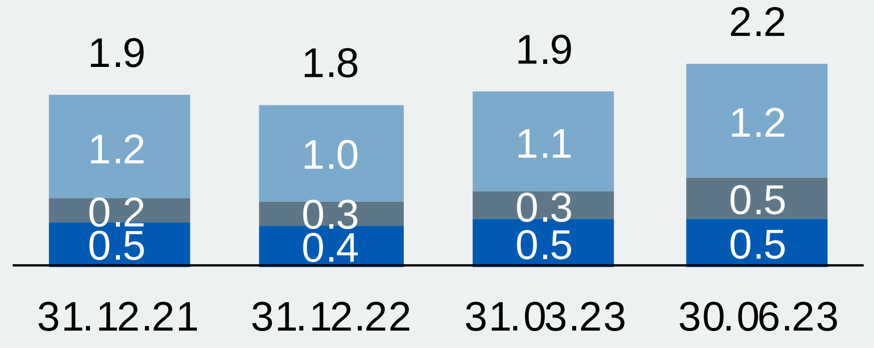
Thereof on loans to corporates

Loans to corporates are 1.0% provisioned at period end



Thereof on loans to individuals

Loans to individuals are 0.3% provisioned at period end



■ Stage 1 ■ Stage 2 ■ Stage 3

IFRS9 economic scenarios and assumptions

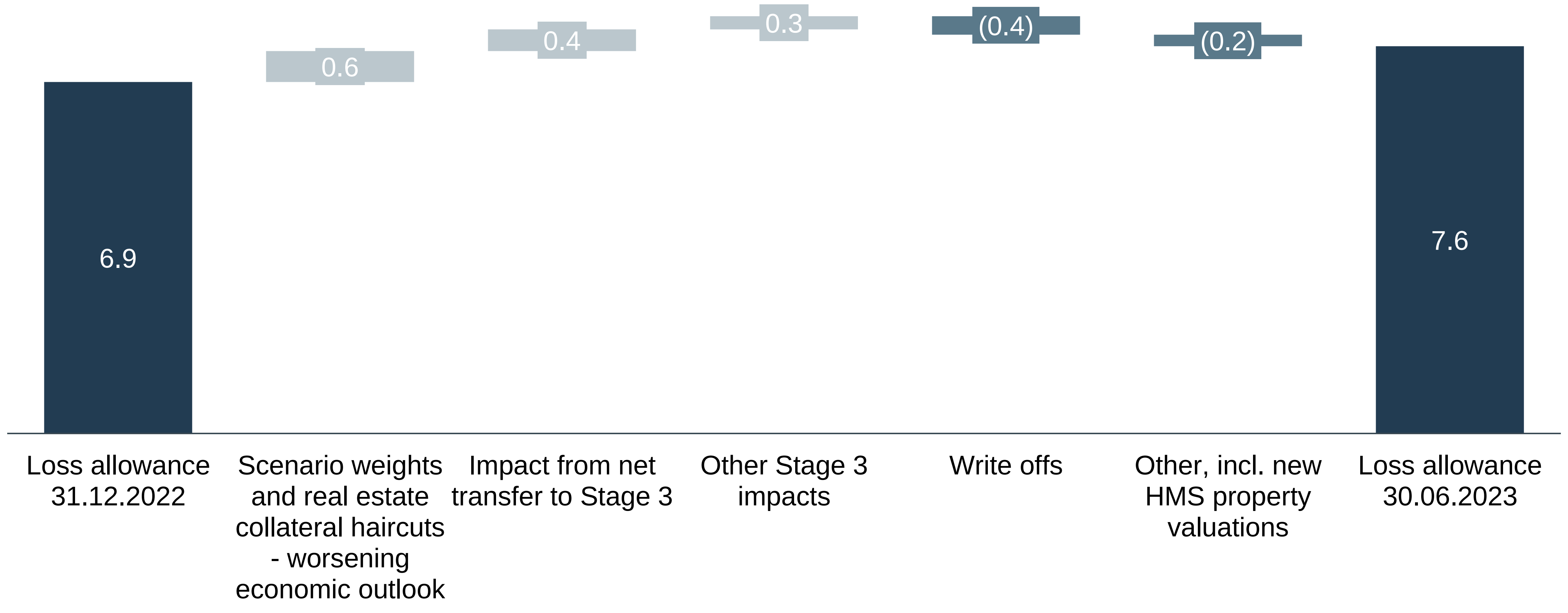
Worsening economic outlook is captured in a movement of weights from the optimistic case to the base and pessimistic case and 5% increase in haircut of real estate collateral in those scenarios.

IFRS9 scenario likelihood	YE 2021	YE 2022	Q2 2023
Optimistic	20%	10%	10%
Base case	60%	65%	60%
Pessimistic	20%	25%	30%

Real estate collateral haircut	Q1 2023 and prior		Q2 2023	
	Base case	Pessimistic	Base Case	Pessimistic
Residential	20%	35%	25%	40%
Commercial	30%	45%	35%	50%

Changes to loss allowance on loans to customers in H1

Included are FX changes and calculated interest on Stage 3 provision, which are not reflected in Net impairment line in the Income Statement. Off-balance impairments and effect of payments of loans previously written off are excluded from this analysis.



* Included are FX changes and calculated interests on Stage 3 provision, which are not reflected in Net impairment line in the Income Statement. Off-balance impairments and effect of payments of loans previously written off are excluded from this analysis.

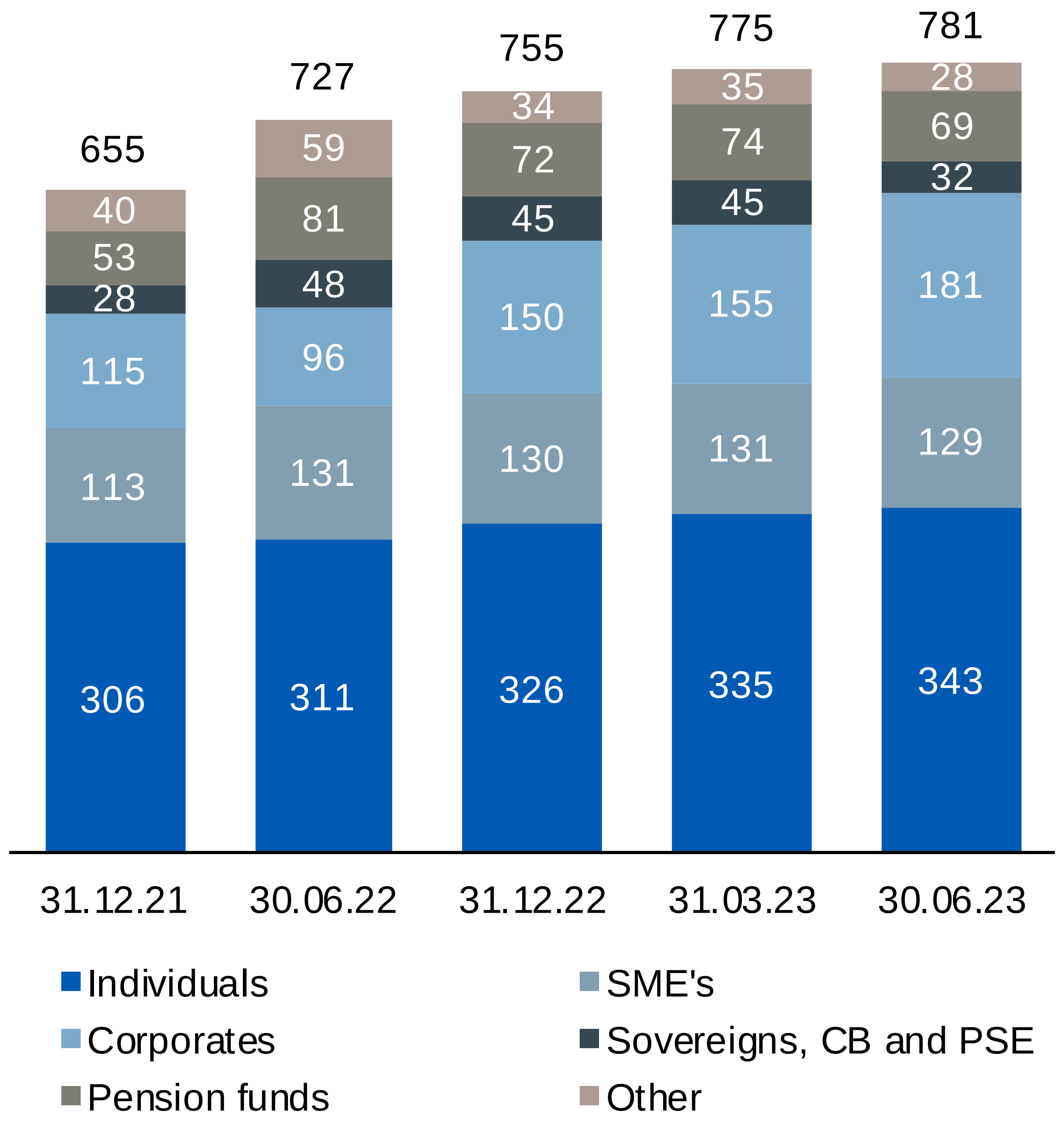
All amounts in ISK bn

Deposits from customers

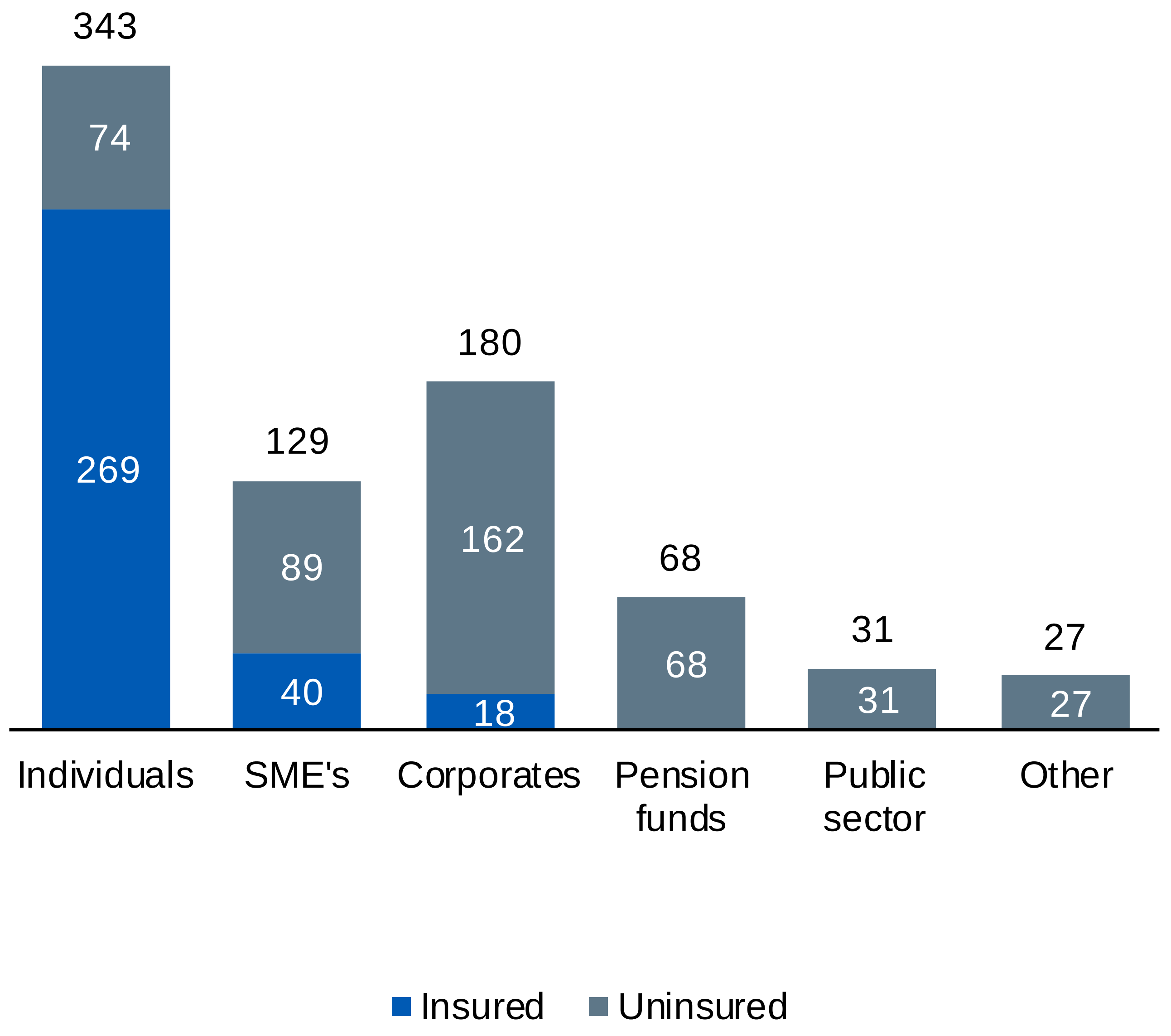
Robust position in competitive market

- Seasoned and diversified deposit base supports another quarter of growth in deposits
- Total deposits of ISK 781bn represent 59% of the Bank's total liabilities
- Growth in deposits from customers during the second quarter was 0.8% and 7.4% YoY
- Growth over past quarters has primarily been in "stable" LCR category and term deposits
- Loans to deposits ratio of 145% at the end of the quarter and has been stable over the last few years
- New CPI linked deposit product successfully launched in the quarter. Term deposits with minimum 90day withdrawal notice

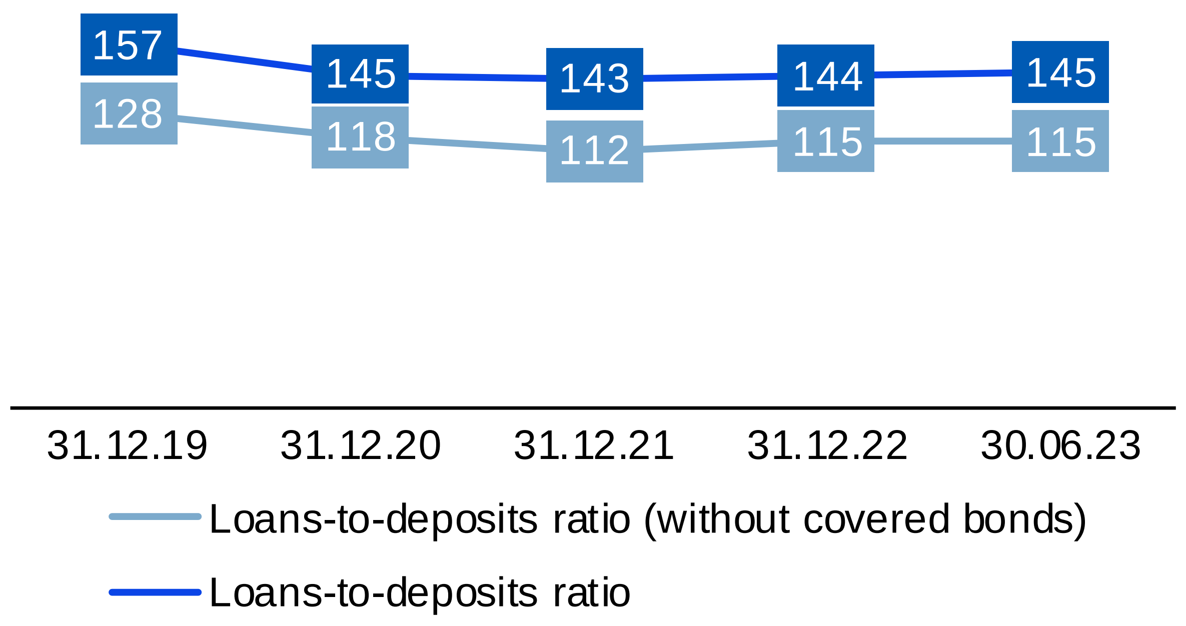
Deposits



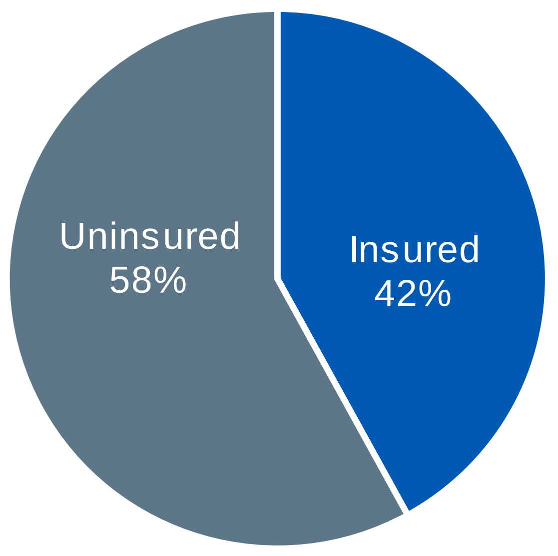
Deposits by insurance scheme



Loans to deposits ratio (%)



Total deposits by insurance scheme

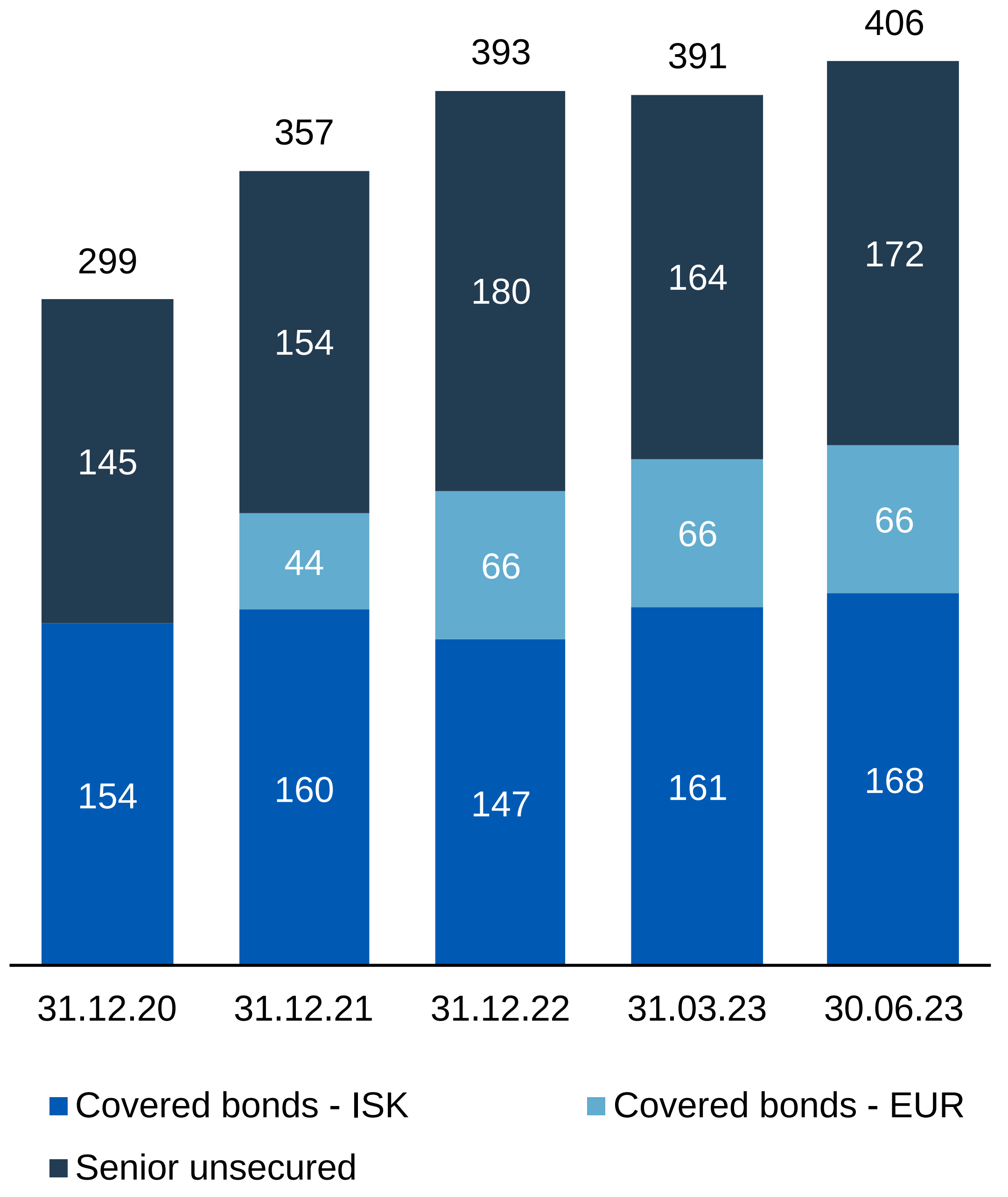


Borrowings

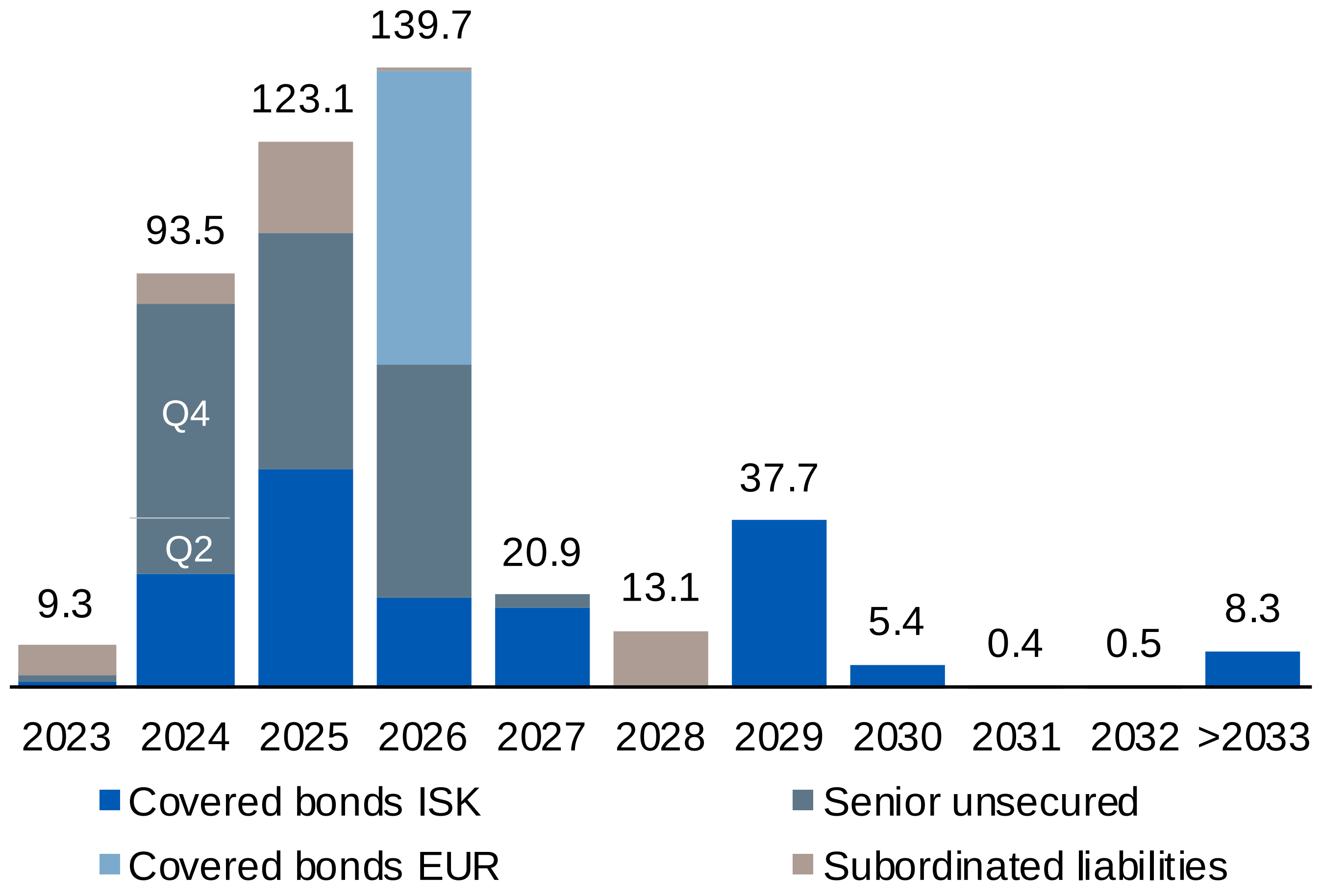
Conservative funding strategy with early financing of upcoming FX maturities

- EUR 300 million senior preferred issue during the quarter to prefund maturity in May 2024
  - Tender offer on May 2024 maturity, 73.5% of EUR 300 million were accepted
  - Leaves no significant FX maturities until December 2024
- During the quarter S&P affirmed Arion Bank's issuer rating and revised the outlook from stable to negative. S&P then revised the outlook from stable to positive on the Bank's covered bond rating
- The Bank will continue to regularly issue in the domestic market and opportunistically access the international markets

Borrowings by type



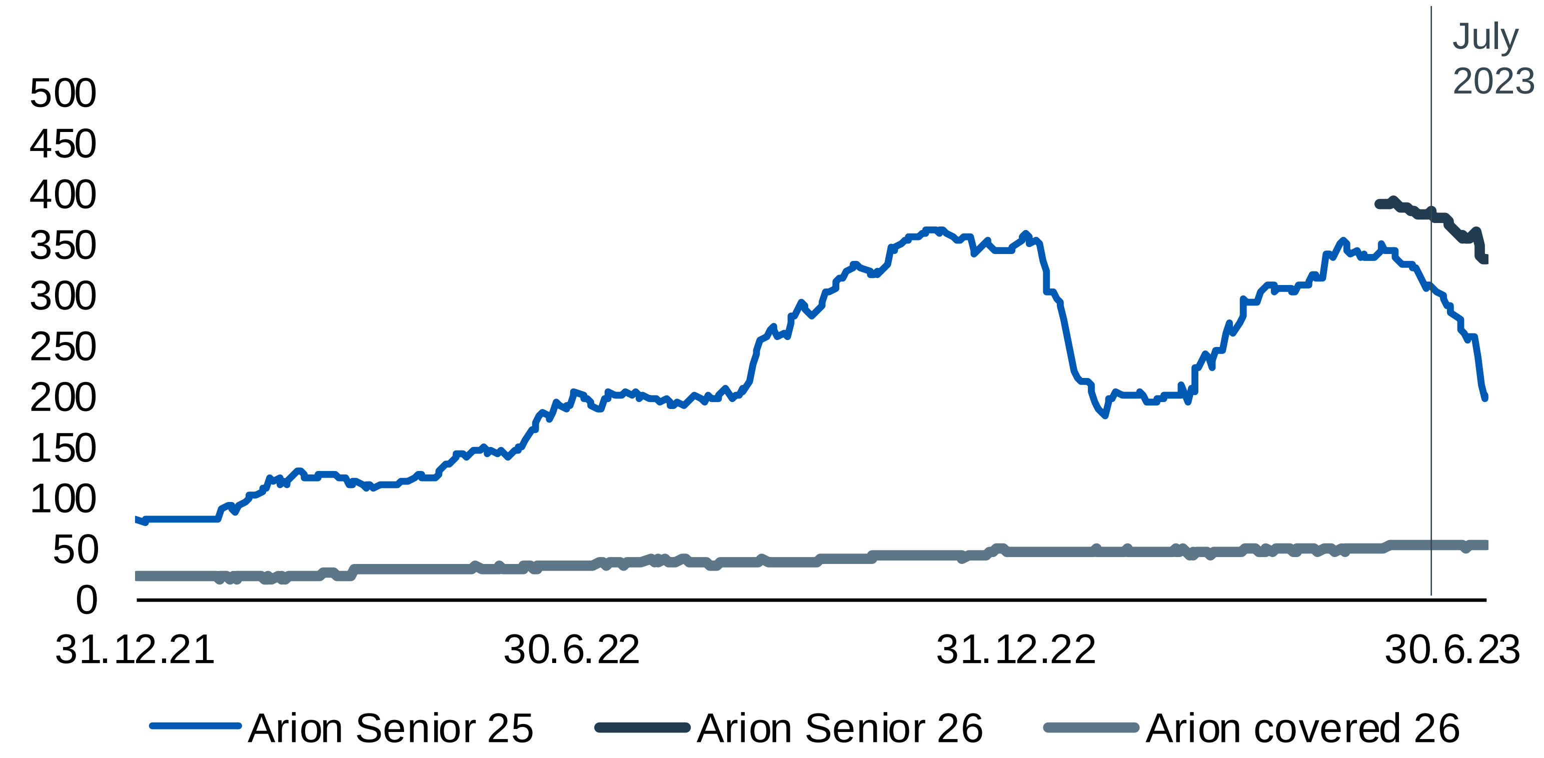
Maturities of borrowings and call dates on subordinated liabilities



Ratings

S&P		
Long term	BBB	A
Covered bond	A	N/A
Short term	A-2	A-1
Outlook	Negative	Positive
Moody's		
Deposits - long term	A3	N/A
Issuer - long term	Baa1	A2
Outlook	Positive	Positive

Development of EUR funding spreads (bps)



Source: Bloomberg

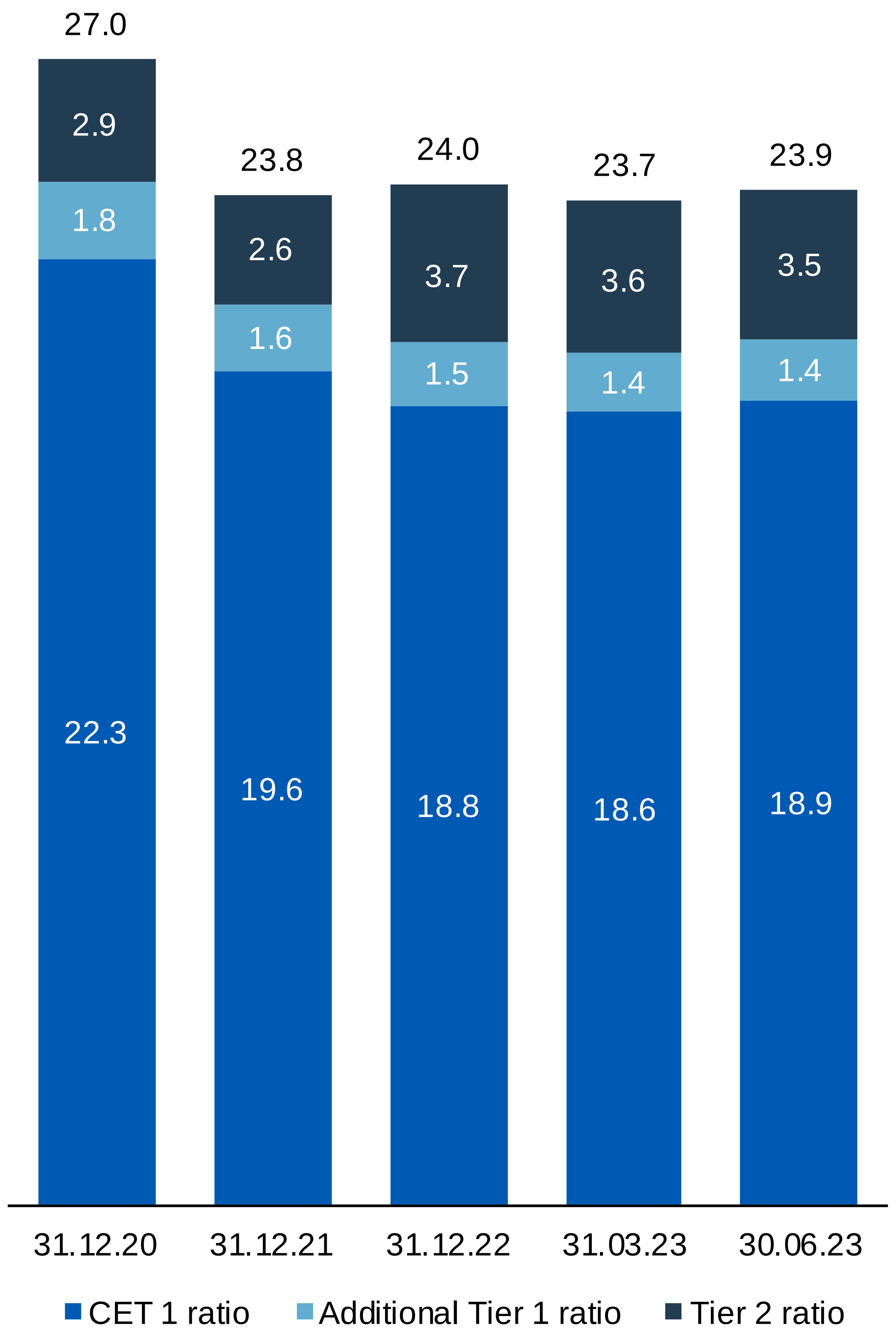
 All amounts in ISK bn

Own funds

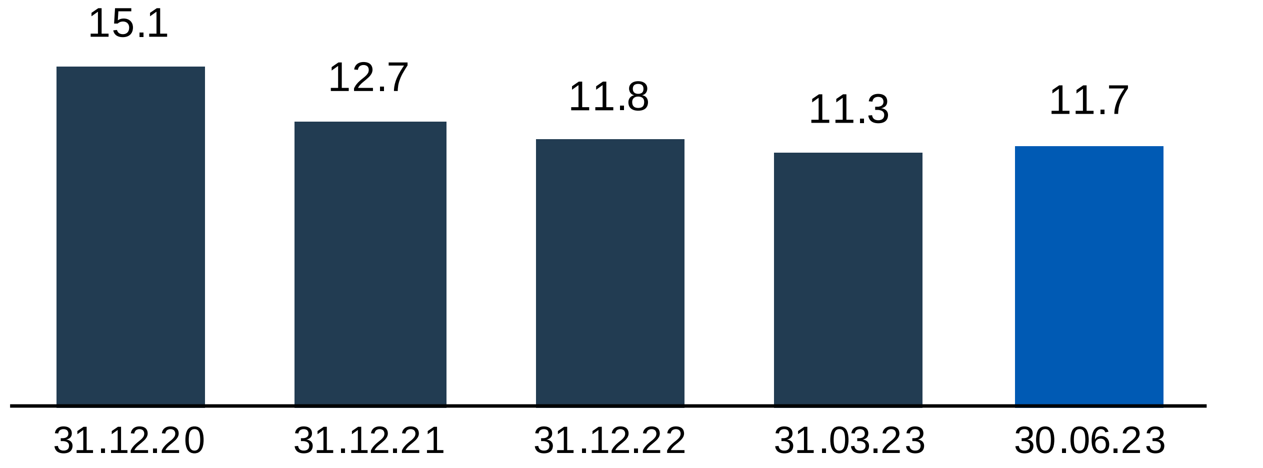
Strong capital position

- Capital position increases between quarters with CET1 ratio increasing by 30 bps to 18.9%
- CET1 position 400 bps above regulatory requirements
- REA increased by 0.5% in Q2 to ISK 912bn. The increase is mainly in credit risk from lending activities
- Leverage ratio of 11.7% significantly above most international peers

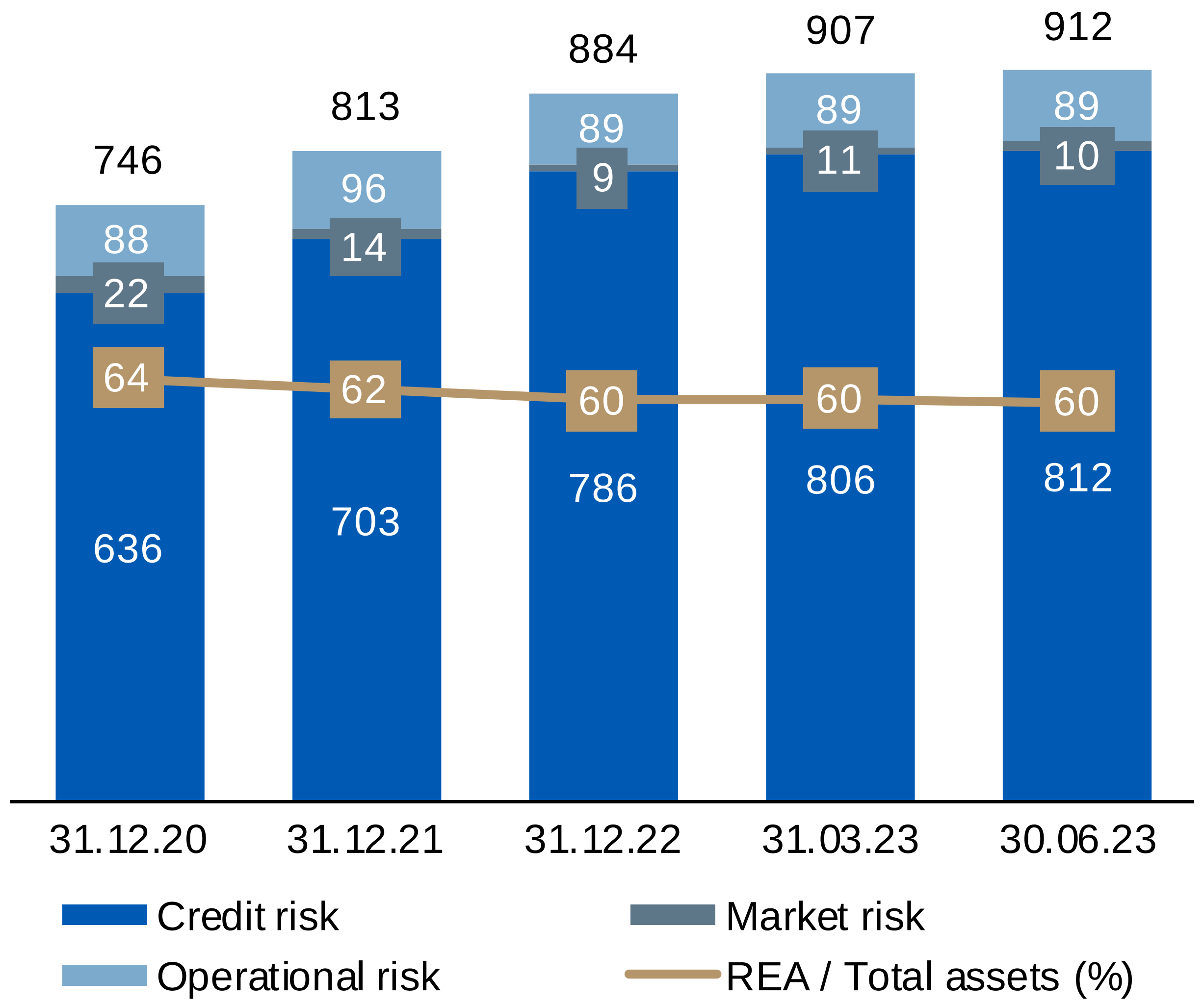
Capital ratio (%)



Leverage ratio (%)



Risk-weighted exposure amount



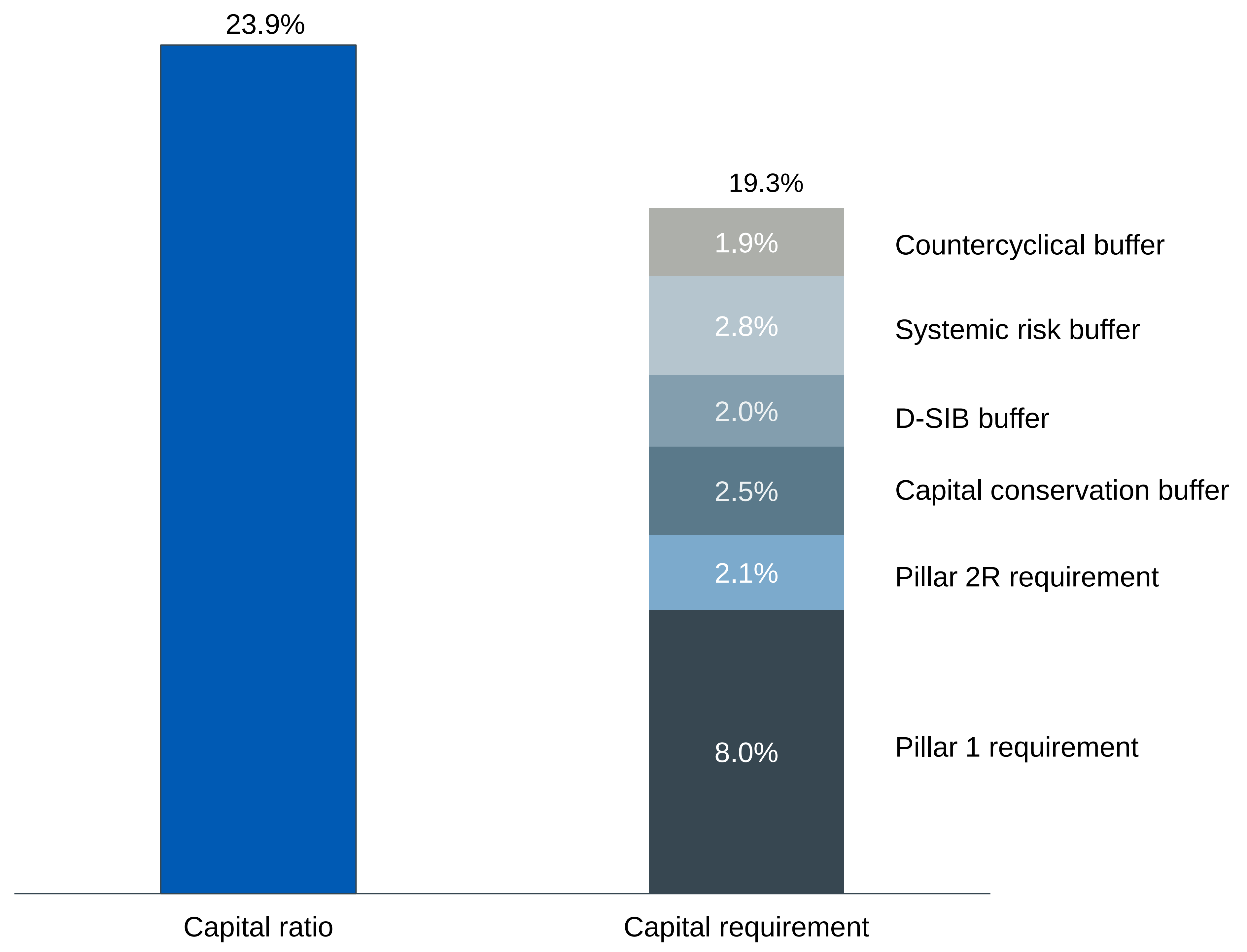
 All amounts in ISK bn

Own funds

Capital ratios comfortably above regulatory requirements – considerable reduction of Pillar 2 capital requirement

- The FME has published a revised Pillar 2 requirement for the Bank at 2.1% of REA, based on year-end 2022 financials, a decrease of 1.4 percentage points from the previous result
- The countercyclical capital buffer in Iceland will increase from 2.0% to 2.5% in March 2024, bringing the total capital requirement to 19.8%
- Capital ratios account for foreseeable dividend that corresponds to 50% of profits in accordance with the Bank's dividend policy
- The medium-term capital management buffer target is 150-250bps
- Considering the raised countercyclical buffer to 2.5%, the Bank has ISK 37bn of surplus capital over regulatory requirement
- The management buffer range implies surplus capital in the range from ISK 15bn to ISK 24bn. Note however rating considerations on the next page, which impact capital management near term
- The solvency ratio of Vördur insurance is 140.8%

Own funds and capital requirements (%)

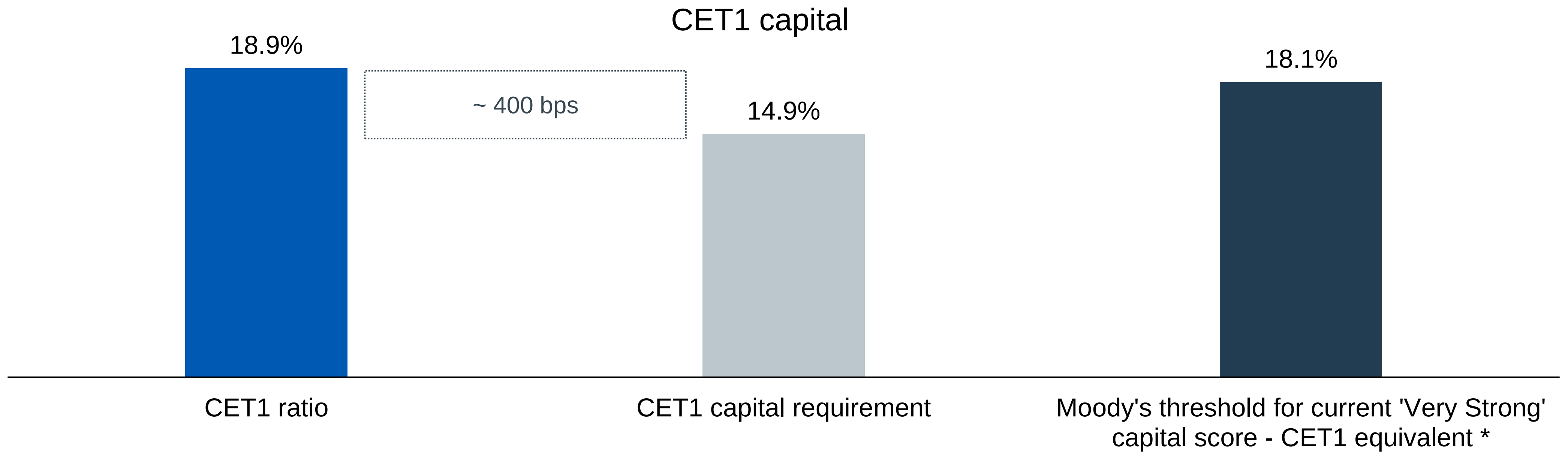


Own funds

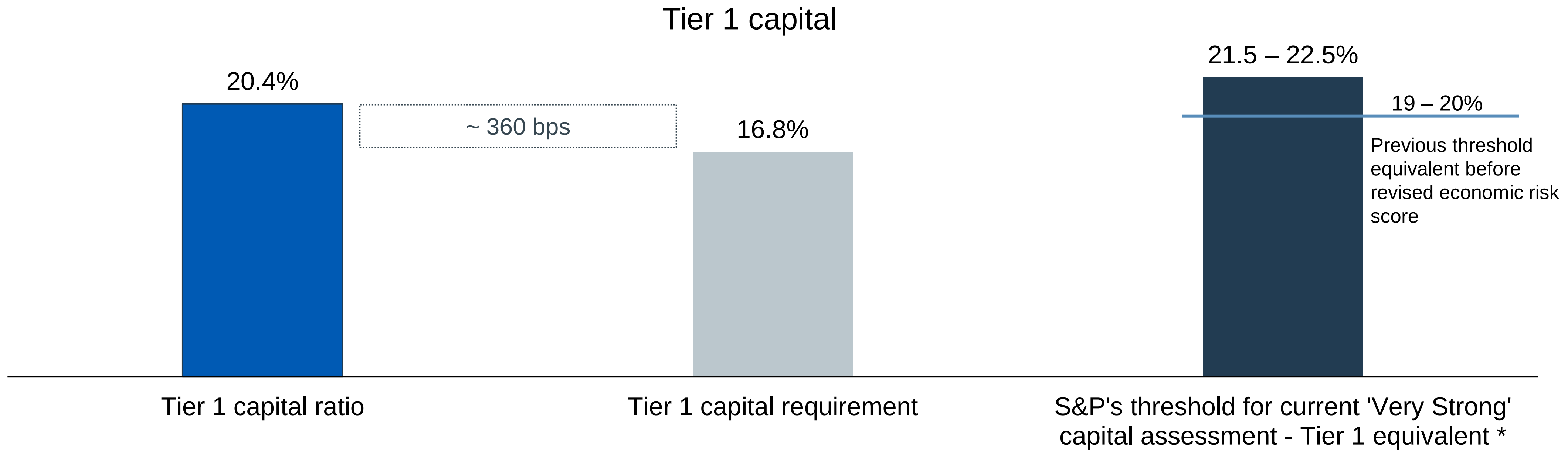
Rating considerations impact capital management in the near-term

- The Bank’s issuer ratings from S&P and Moody’s are BBB (negative outlook) and Baa1 (positive outlook), respectively.
- Both rating agencies’ assessment of the Bank’s capital position is ‘Very Strong’ as per the different methodologies.
- S&P’s capital assessment was significantly impacted by its elevated economic risk assessment for the Icelandic banking sector which was confirmed in a report early this year. Tier 1 capital threshold from this perspective increased from around 19 - 20% to 21.5 - 22.5%
- The Bank’s risk-adjusted capital ratio is currently below S&P’s revised threshold, which prompted a change to negative outlook in May.
- Moody’s measures capital through a ratio of tangible common equity over REA. Based on current "Very Strong" categorization this corresponds to a CET1 threshold of around 18%.
- The Bank will adhere to capital thresholds of the rating agencies in the near term, which implies raising the Tier 1 management buffer to 400-500bps. The expectation is however that constructive economic developments and/or positive impact of other rating factors will result in convergence of capital thresholds over the medium term.

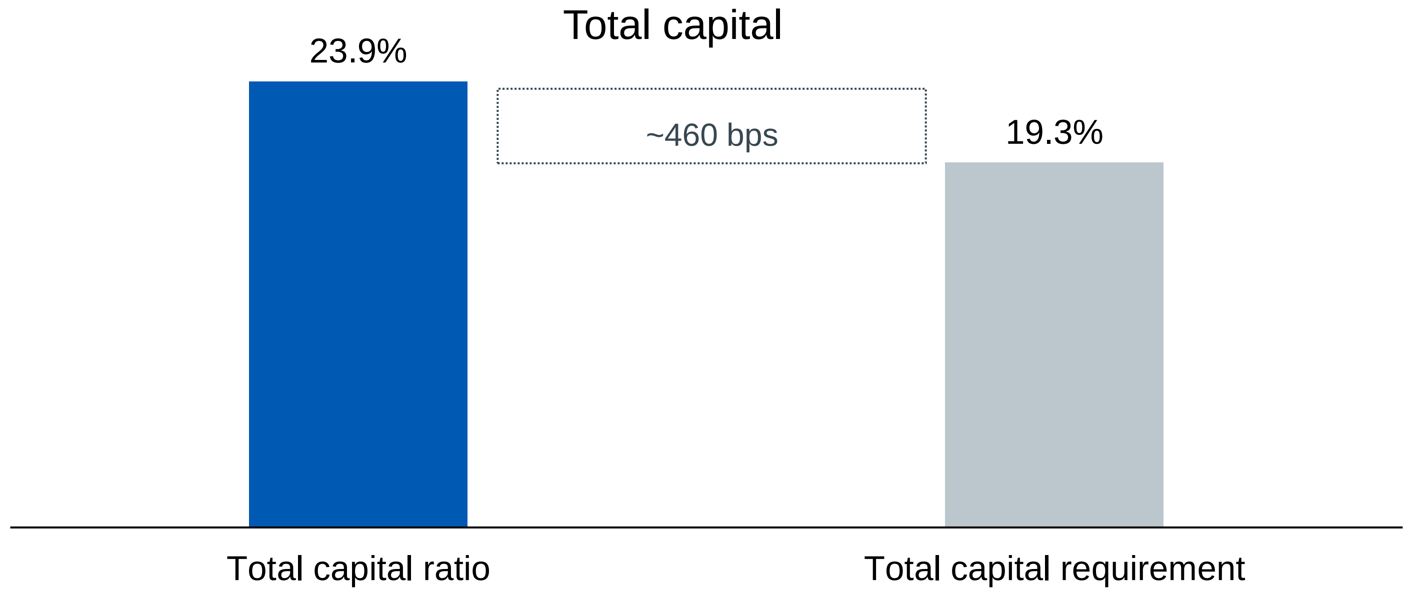
Own funds: capital requirements and rating benchmarks (%)



* Moody's capital benchmark ratio is tangible common equity over REA, with REA add-on of 20% risk-weight for sovereign exposures. The threshold for the current 'Very Strong' score for capital is 18%, which corresponds to 18.1% CET1 capital given fixed REA.



* S&P's risk-adjusted capital ratio (RAC) is total adjusted capital over S&P's own risk-weighted assets, where the risk-weights are a function of Iceland's economic risk score and banking industry country risk assessment (BICRA) score. The benchmark for 'Very Strong' capital assessment is a RAC ratio above 15% which roughly corresponds to a Tier 1 ratio of 22.4% but is a function of balance sheet composition, especially unlisted equity holdings.

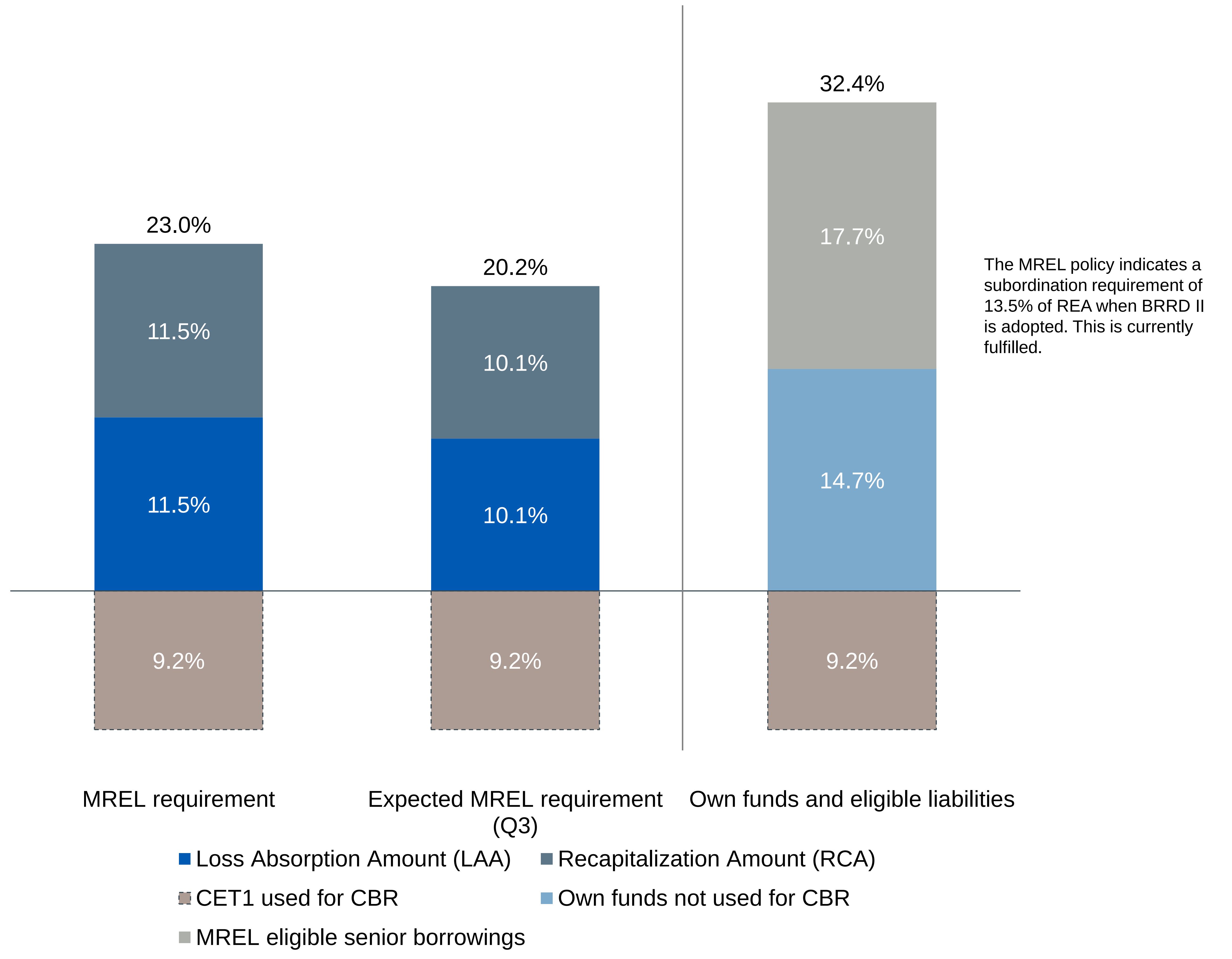


MREL requirement

Comfortably exceeding MREL requirements

- The BRRD I approach to MREL has been codified in Icelandic law
- Senior unsecured debt is MREL eligible unless it is excluded from the scope of bail-in
- The Icelandic Resolution Authority (IRA) has published its MREL policy
  - Both Loss Absorption Amount (LAA) and Recapitalization Amount (RCA) equal Pillar 1 plus Pillar 2, currently 11.5% of REA
  - Based on the SREP results for 31.12.2022 and in line with the MREL policy, the LAA and RCA are expected to be set at 10.1% of REA in Q3 2023
  - No Market Confidence Charge (MCC) because of the high level of combined buffer requirement (CBR), currently 9.2% of REA
  - No subordination requirement under BRRD I
- The primary legislation codifying BRRD II into Icelandic law has been passed. However, the details of the implementation of the MREL requirement in accordance with BRRD II will be introduced in secondary legislation which is expected to be published in the second half of 2023
- The Senior Non-Preferred (SNP) rank has been introduced into Icelandic law, but the Bank does not see a need to issue SNP debt in the coming year
- The graph shows
  - MREL requirement for Arion Bank 23.0% of REA in addition to the CBR
  - The expected MREL requirement at the end of Q3 2023 is 20.2% which corresponds to a 12.2% buffer based on current position
  - Own funds and MREL eligible senior borrowings (>1yr to maturity)

MREL requirement as % of REA*



*According to BRRD I, MREL requirement should be expressed in terms of total liabilities and own funds (TLOF) but % of REA is more relevant for determining the size of the requirement. Actual requirement is 14.7% TLOF which corresponds to 24.2% REA at 30.6.2023

Going forward

Positive momentum and conservative balance sheet management

Operating momentum has continued with a positive first half of the year where key medium-term targets are exceeded. Clear strategy and customer focus support outlook.

Prudent balance sheet management with light wholesale maturity profile. Loan provisioning also prudent despite risk indicators of credit quality at healthy levels, albeit with signs of turning cycle.

The Group is in a good position to navigate the current external operational environment with diverse and seasoned businesses and conservative and agile balance sheet management.

Strong capital position with buffer of 400bps over CET1 requirements. S&P recent elevation of economic risk assessment and resulting higher capital thresholds drive short-term capital management.

We are starting to see signs of inflation subsiding and recent Icelandic sovereign positive rating outlook upgrades from S&P and Moody's are a testament to the relative strength of the economy.

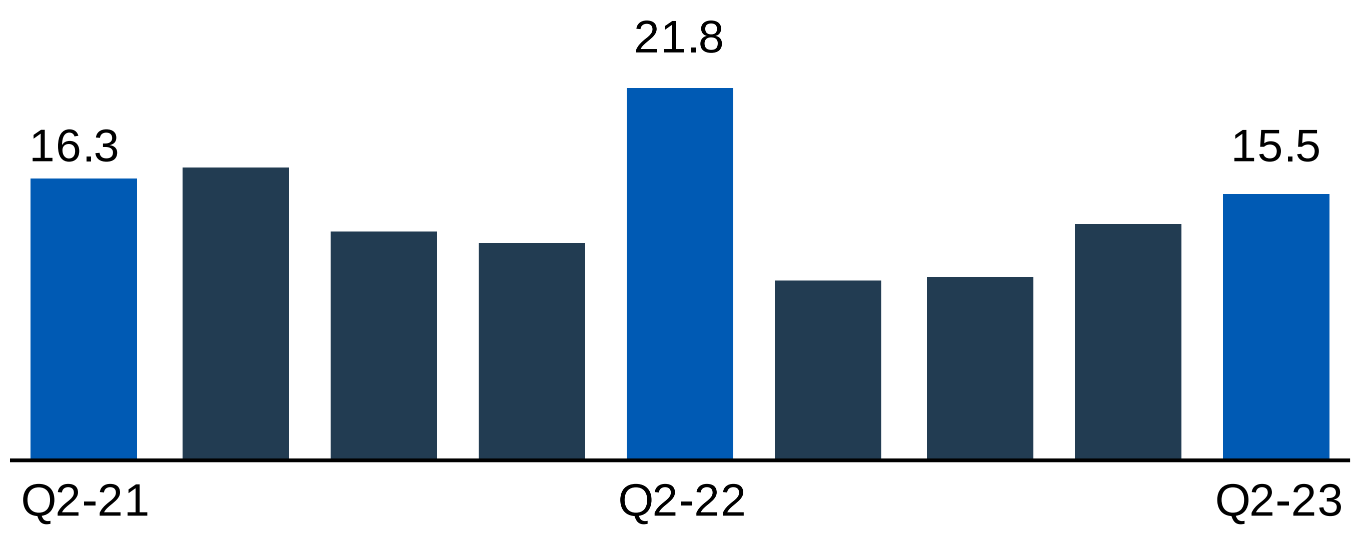
Medium-term targets under review with evolving external environment and operational development.

Capital Markets day planned for Q1 2024 to present revised plan and targets.

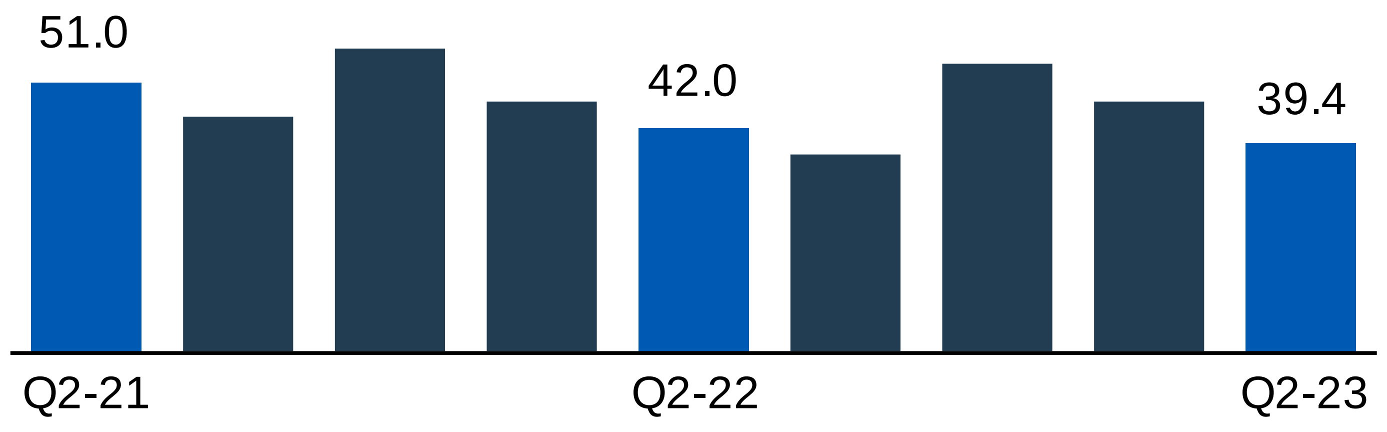
Appendix

Key financial indicators - quarter

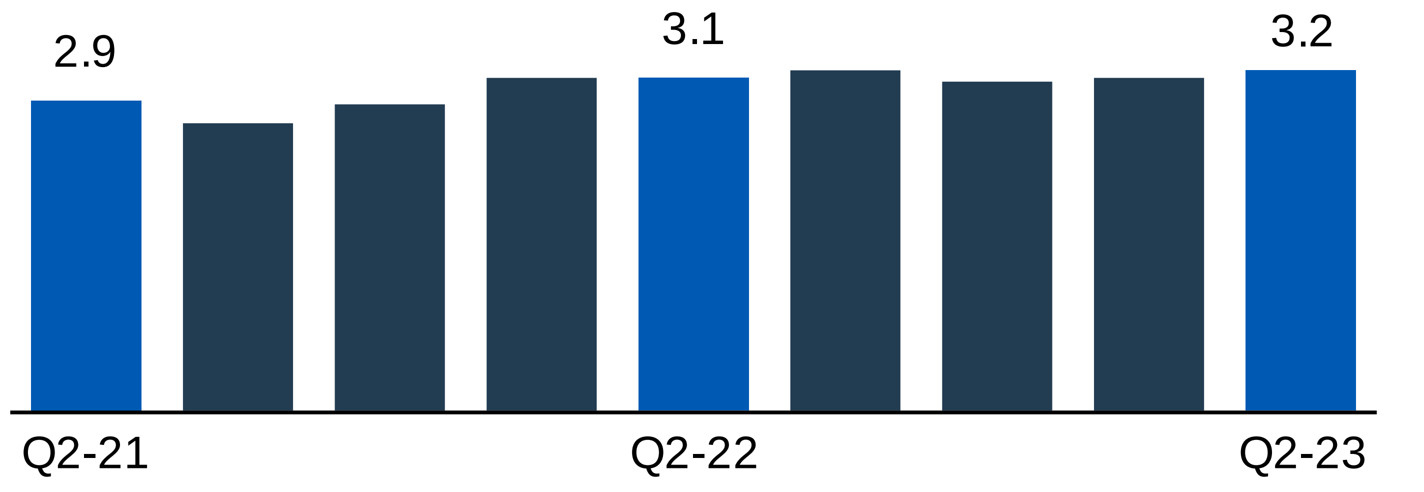
Return on equity (%)



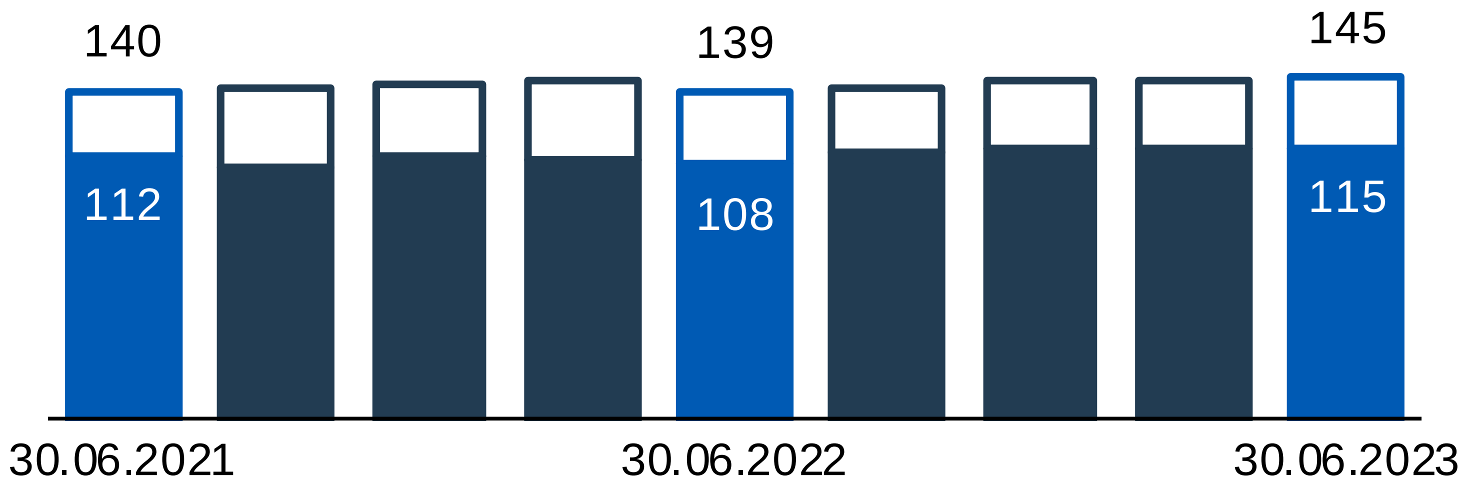
Cost-to-Core income ratio (%)*



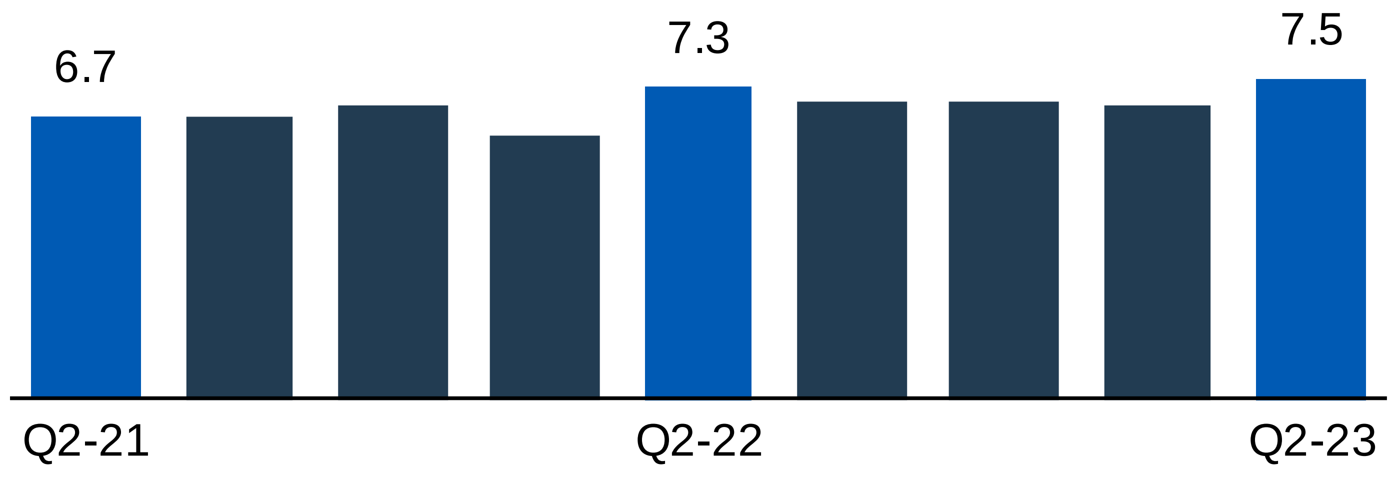
Net interest margin (%)



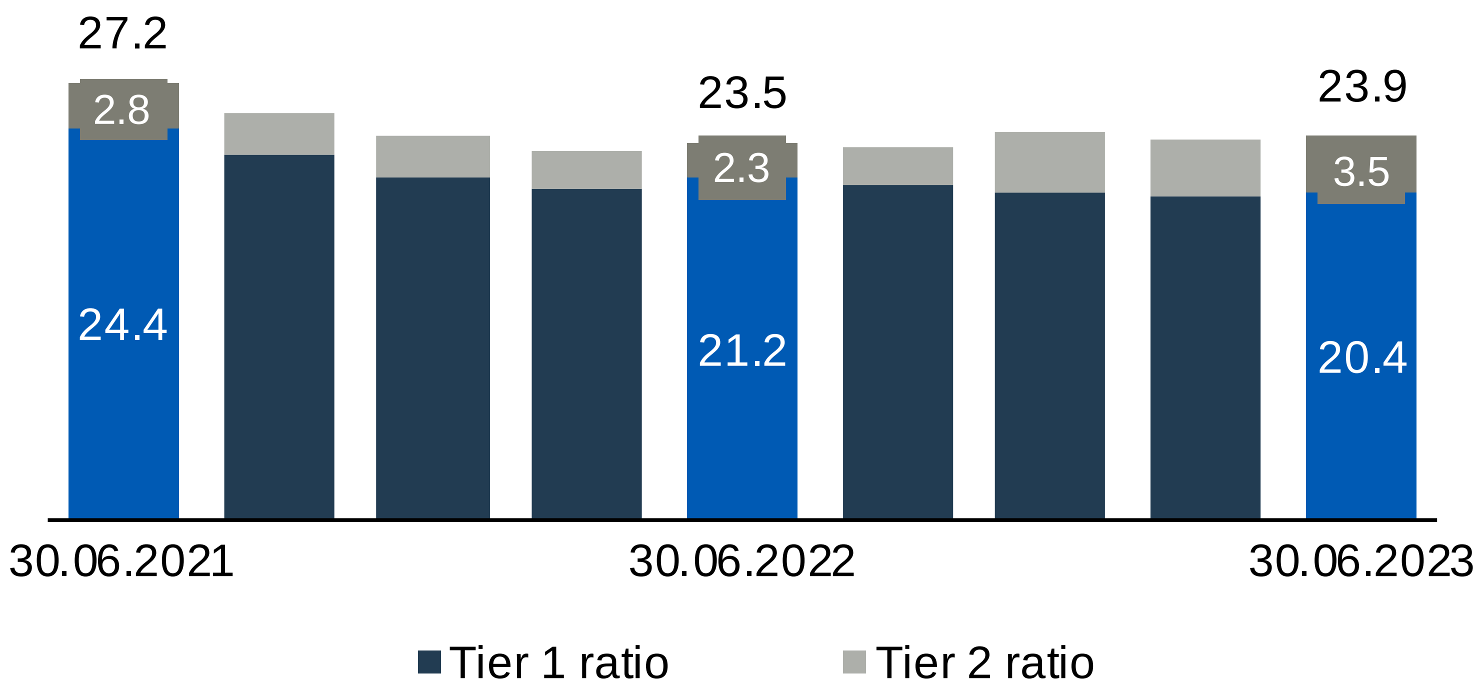
Loans-to-deposits ratio (%)
(without loans financed by covered bonds)



Core operating income / REA (%)*



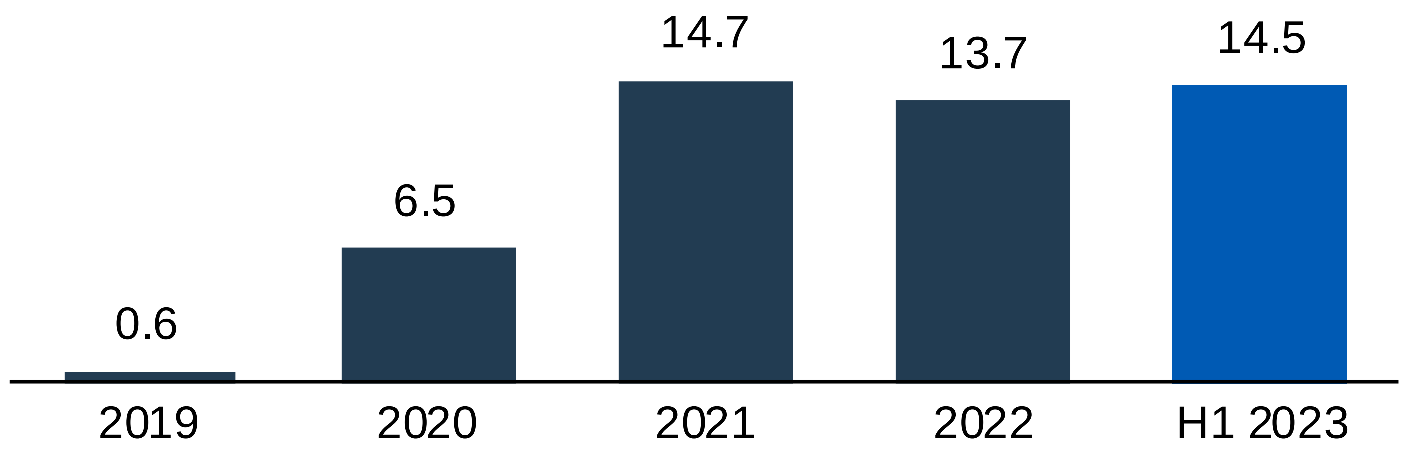
Capital ratio (%)



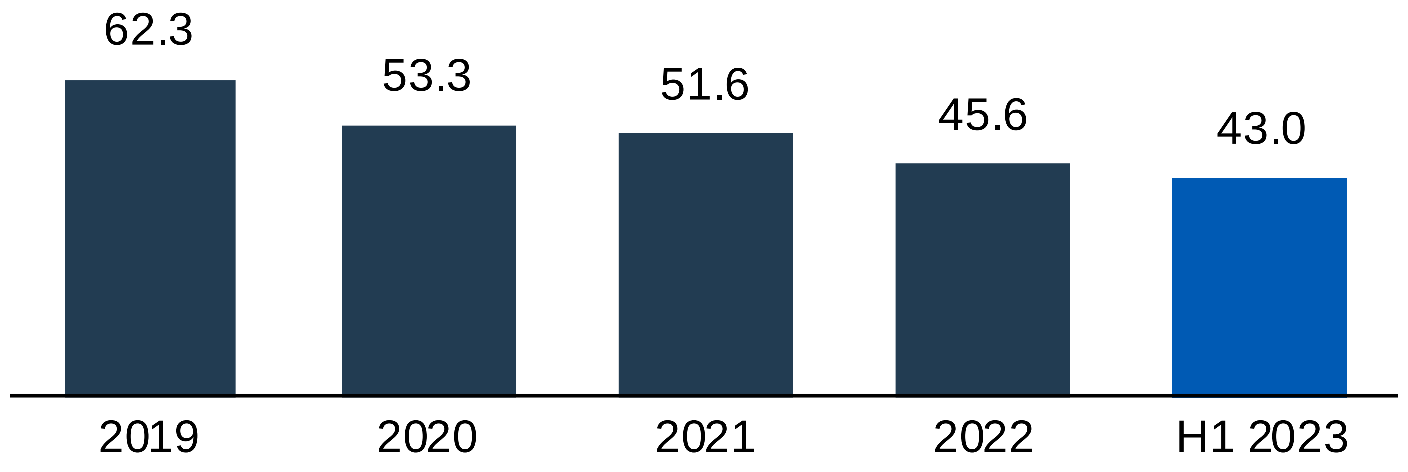
*Figures for periods prior to Q1 2023 have not been adjusted to IFRS 17 apart from Q1 and Q2 2022

Key financial indicators - annual

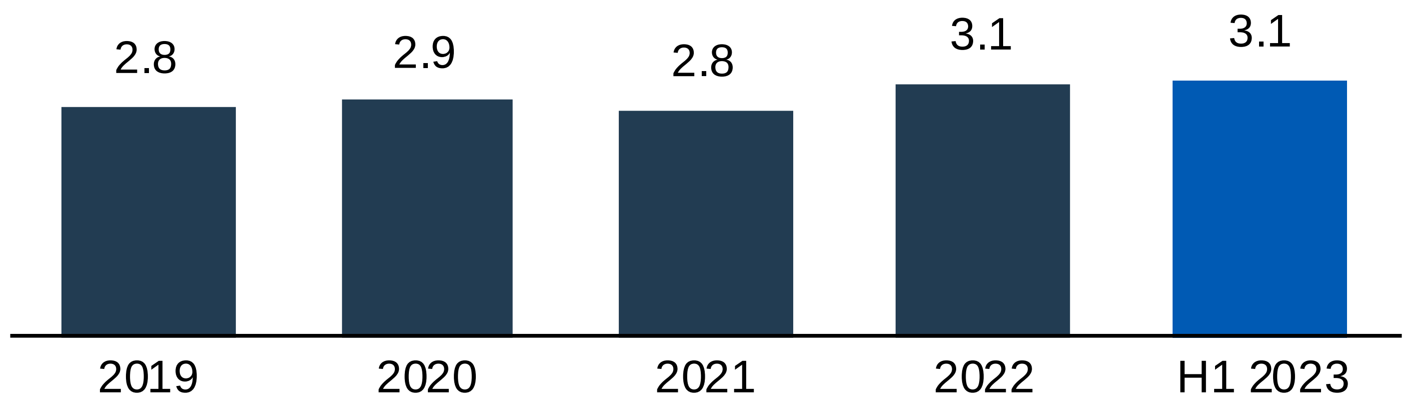
Return on equity (%)



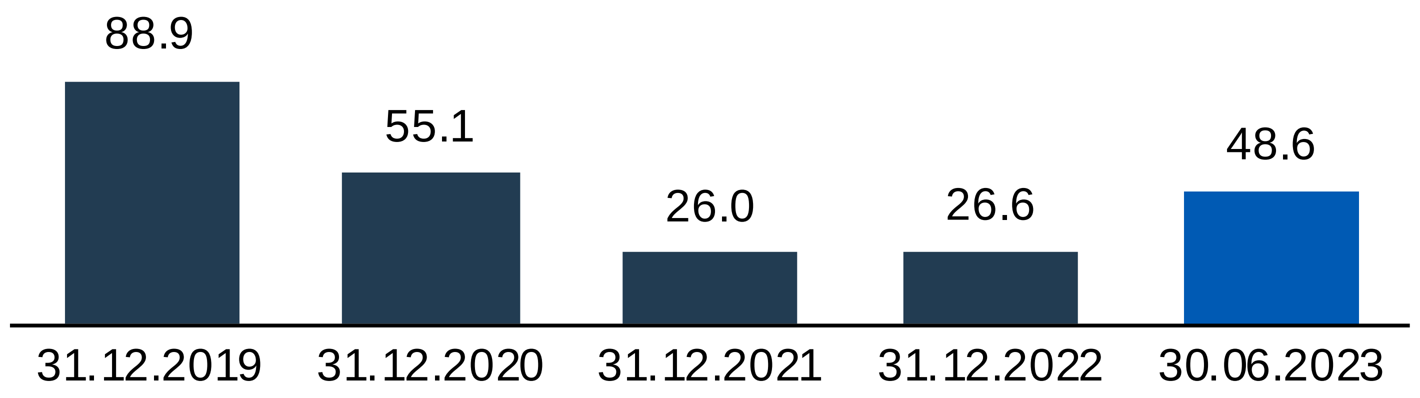
Cost-to-Core income ratio (%)*



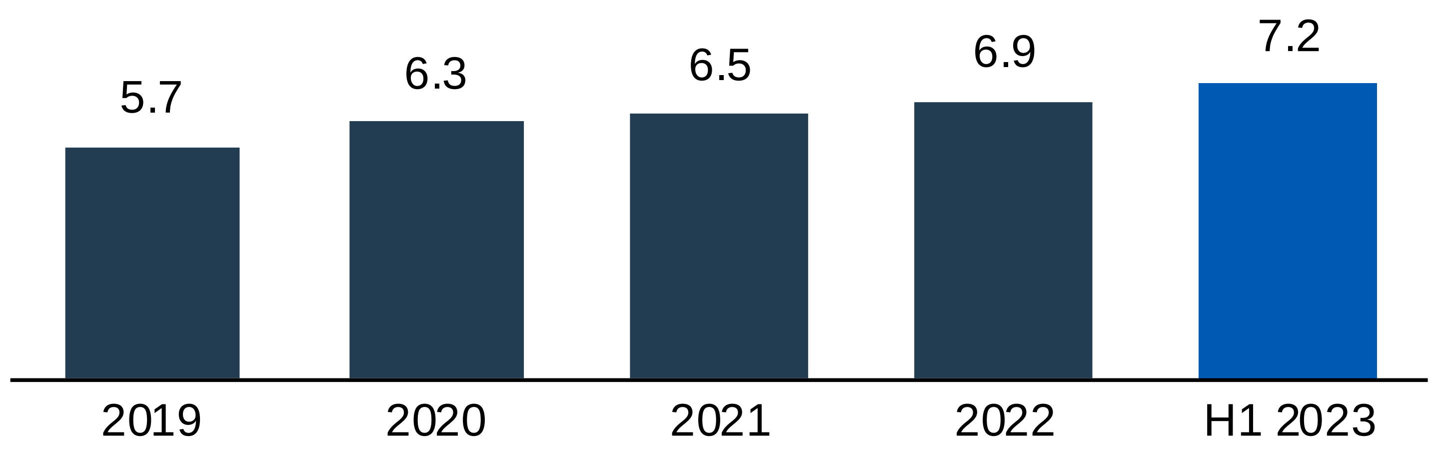
Net interest margin (%)



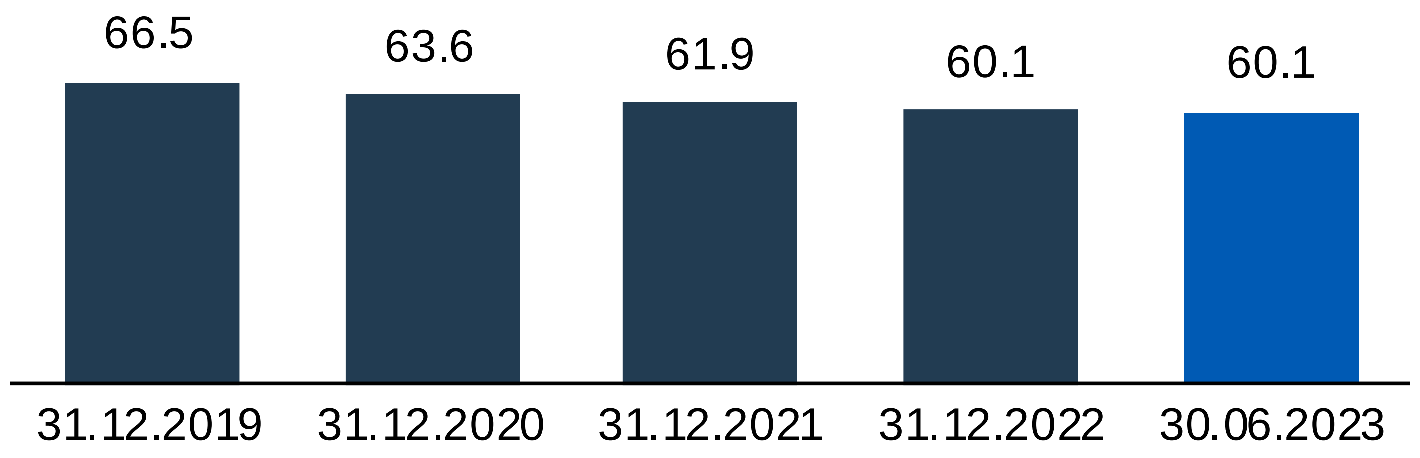
CPI imbalance (ISK bn)



Core operating income / REA (%)*



Risk exposure amount / Total assets (%)



*Figures for periods prior to Q1 2023 have not been adjusted to IFRS 17 apart from Q1 and Q2 2022

Key figures*

Operations	H1 2023	H1 2022	H1 2021	H1 2020	H1 2019	Q2 2023	Q1 2023	Q4 2022	Q3 2022	Q2 2022
Net interest income	22,420	19,221	15,358	15,110	15,242	11,426	10,994	10,524	10,421	9,745
Net commission income	8,638	8,138	6,839	5,764	4,696	4,187	4,451	3,972	4,002	4,582
Operating income	32,883	27,125	28,101	23,039	23,928	17,344	15,539	15,540	13,884	13,105
Operating expenses	(12,479)	(12,850)	(12,420)	(12,602)	(13,480)	(6,009)	(6,470)	(8,251)	(5,810)	(6,649)
Net earnings	13,382	15,985	13,857	2,741	3,114	7,091	6,291	5,023	4,863	10,050
Return on equity	14.5%	17.4%	14.3%	2.9%	3.2%	15.5%	13.7%	10.7%	10.5%	21.8%
Net interest margin	3.1%	3.1%	2.8%	2.9%	2.8%	3.2%	3.1%	3.1%	3.2%	3.1%
Return on assets	1.8%	2.3%	2.3%	0.5%	0.5%	1.9%	1.7%	1.4%	1.4%	2.9%
Cost-to-core income ratio	43.0%	44.4%	52.2%	56.9%	64.1%	39.4%	46.8%	54.3%	36.8%	42.0%
Cost-to-income ratio	37.9%	46.3%	44.2%	54.7%	56.3%	34.6%	44.5%	53.1%	41.8%	50.1%
Cost-to-total assets	1.7%	1.9%	2.1%	2.2%	2.2%	1.6%	2.0%	2.3%	1.7%	2.0%

Balance Sheet	30.06.2023	31.12.2022	31.12.2021	31.12.2020	31.12.2019	30.06.2023	31.03.2023	31.12.2022	30.09.2022	30.06.2022
Total assets	1,518,227	1,465,609	1,313,864	1,172,706	1,081,854	1,518,227	1,500,645	1,465,609	1,427,886	1,383,362
Loans to customers	1,134,621	1,084,757	936,237	822,941	773,955	1,134,621	1,114,128	1,084,757	1,045,152	1,010,666
Mortgages	595,896	574,029	504,877	409,641	333,406	595,896	576,861	574,029	562,617	536,610
Share of stage 3 loans, gross	1.6%	1.2%	1.9%	2.6%	2.7%	1.6%	1.4%	1.2%	1.4%	1.4%
REA/ Total assets	60.1%	60.1%	61.9%	63.6%	66.5%	60.1%	60.4%	60.1%	60.8%	117.4%
CET 1 ratio	18.9%	18.8%	19.6%	22.3%	21.2%	18.9%	18.6%	18.8%	19.3%	19.7%
Leverage ratio	11.7%	11.8%	12.7%	15.1%	14.1%	11.7%	11.3%	11.8%	12.0%	12.7%
Liquidity coverage ratio	162.9%	158.5%	202.8%	188.5%	188.3%	162.9%	173.6%	158.5%	189.3%	163.2%
Loans to deposits ratio	145.2%	143.6%	142.8%	144.8%	157.0%	145.2%	143.8%	143.6%	141.2%	139.0%

*Figures for periods before H1 2022 have not been restated according to IFRS 17

 All amounts in ISK m

Vördur adopted IFRS 17 Insurance contracts

IFRS 17 standard

The insurance subsidiary Vördur adopted IFRS 17 Insurance contracts 1 January 2023 when the standard came into effect. The standard sets out new principles for recognition, measurement, presentation and disclosures of insurance contracts and mainly results in a few reclassifications within the Consolidated Financial Statement

The goal of IFRS 17 is to ensure consistent accounting for all insurance contracts, increase comparability between insurance companies and to drive more detailed disclosures

Main changes in presentation and amounts

A shift of insurance service expenses (both salary expenses and other opex) from *Operating expenses* to *Insurance service results*

Minor shifts of financial income, commission income and interest income to *Insurance service results* as all revenues and expenses related to insurance contracts are now classified as *Insurance service results*

Net impact on the total equity of the Group a decrease of ISK 917m as of 1 January 2022, corresponding to ISK 375m as of 1 January 2023

Insurance contract liability decreases

- Liabilities for incurred claims increase due to changes in the calculation of the liability, with main changes in risk adjustment, discounting, and claims handling cost
- Liabilities for remaining coverage decrease to reflect prepaid premiums only, with similar deduction applied to accounts receivables

Comparative figures for the year 2022 have been restated

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