Q2 results 2022

Investor presentation 27 July 2022

Key results Q2 and H1 2022

Eventful H1 with strong core income generation

- Strong 21.8% ROE in the quarter and 16.9% for the year
- Driven by ongoing positive momentum in Core Income in combination with successful divestments of HFS assets
- Countered by challenging market conditions, impacting financial income in the quarter
- Core operating income increased 23.5% from Q2 2021 (19.9% increase vs. 6M 2021), mainly due to net interest income
- Strong capital and liquidity position. New share buyback program awaiting regulatory approval
- Good progress towards achieving medium term targets

Key results	Q2 2022	H1 2022	Medium term targets
Return on equity	21.8%	16.9%	Exceed 13%
Operating income / REA[1]	6.1%	6.6%	Exceed 7.3%
Insurance premium growth (YoY)	11.4%	10.2%	Premium growth (net of reinsurance) to exceed the growth of the domestic market by more than 3%[2]
Loan growth	3.5%	7.9%	In line with nominal economic growth[3]
Cost-to-income ratio	50.1%	46.3%	Below 45%
CET1 ratio[1]	19.7%	19.7%	~17%
Dividend payout ratio[4]	-	-	50%

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

1 Including full impact of Valitor sale
2 Premium growth in the domestic insurance market in Q1 2022 was 8.0% from Q1 2021
3 Arion Bank forecasts economic growth of 12.5% in 2022
4 Pay-out ratio of approximately 50% of net earnings attributable to shareholders through either dividends or buy-back 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 buffe

Number of milestones in the quarter – further enhancing customer value and experience

The sale of Valitor completed

Rapyd | VALITOR

Digital registration of title for car loans

which greatly shortens the lending process

New rating from Moody's and updated rating from S&P

S&P Global Ratings
Moody's

The Markets division delivers strong performance despite challenging markets

- Strong net inflow in assets under management in Q2
- Broker fees up 57% YoY in Q2
- Stefnir Dividend Fund and Stefnir Equities Fund delivering the strongest performance among mutual equity funds in Iceland over the last 12 months[1]

Arion Bank receives the Covered Bond Report Award for Excellence

Digital strategy and bancassurance progressing

- A broader offering of insurance products introduced within the Arion app
- Open banking platform launched, enabling 3rd party collaboration through APIs
- An AI driven chatbot implemented servicing automatically approx. 60% of requests through our webchat channel

Strong activity in Corporate & Investment Banking with public listing of Alvotech and Nova Telecom

alvotech NOVA

New communication strategy introduced

Solid ESG rating from Sustainalytics

SUSTAINALYTICS
a Morningstar company
RATED

1. www.keldan.is

New communication strategy

In the spring of 2021, we began the process of a comprehensive brand review. This included our brand message, tone of voice, identity and the foundations on which we will build our brand going forward.

- The objectives of this work were to:
  - Be more engaging in our communications with customers, employees and other stakeholders.
  - Communicate the core values of the bank and our services in a more compelling way.
  - Support integrated communications and be more consistent across all channels

The outcome of this work is the creative concept „Þinn árangur“. A literal translation would be something like "Your success", but „árangur“ is a big Icelandic word that has multiple meanings; results, achievement, accomplishment, progress, improvement, success.

Thus, in Icelandic, the sentence becomes a commitment to the long term success of our customers in all its different forms and the thought it expresses is more in the vein of: "We will help you achieve your goals and ambitions."

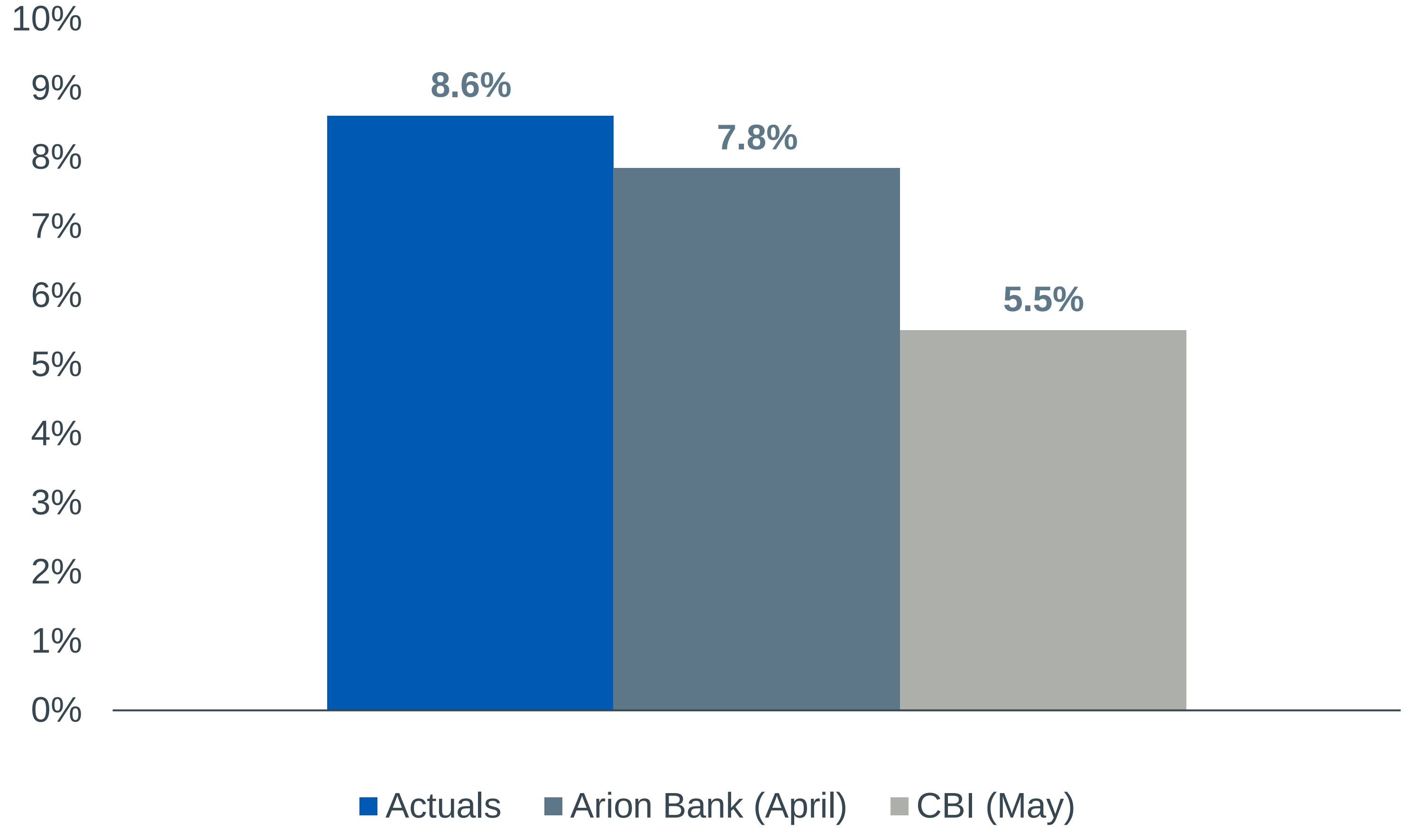
In the launch campaign, people are asked simply what "árangur" means to them and their incredibly varied answers - from startup success to further education to more family time - confirm this idea.

Macroeconomic environment

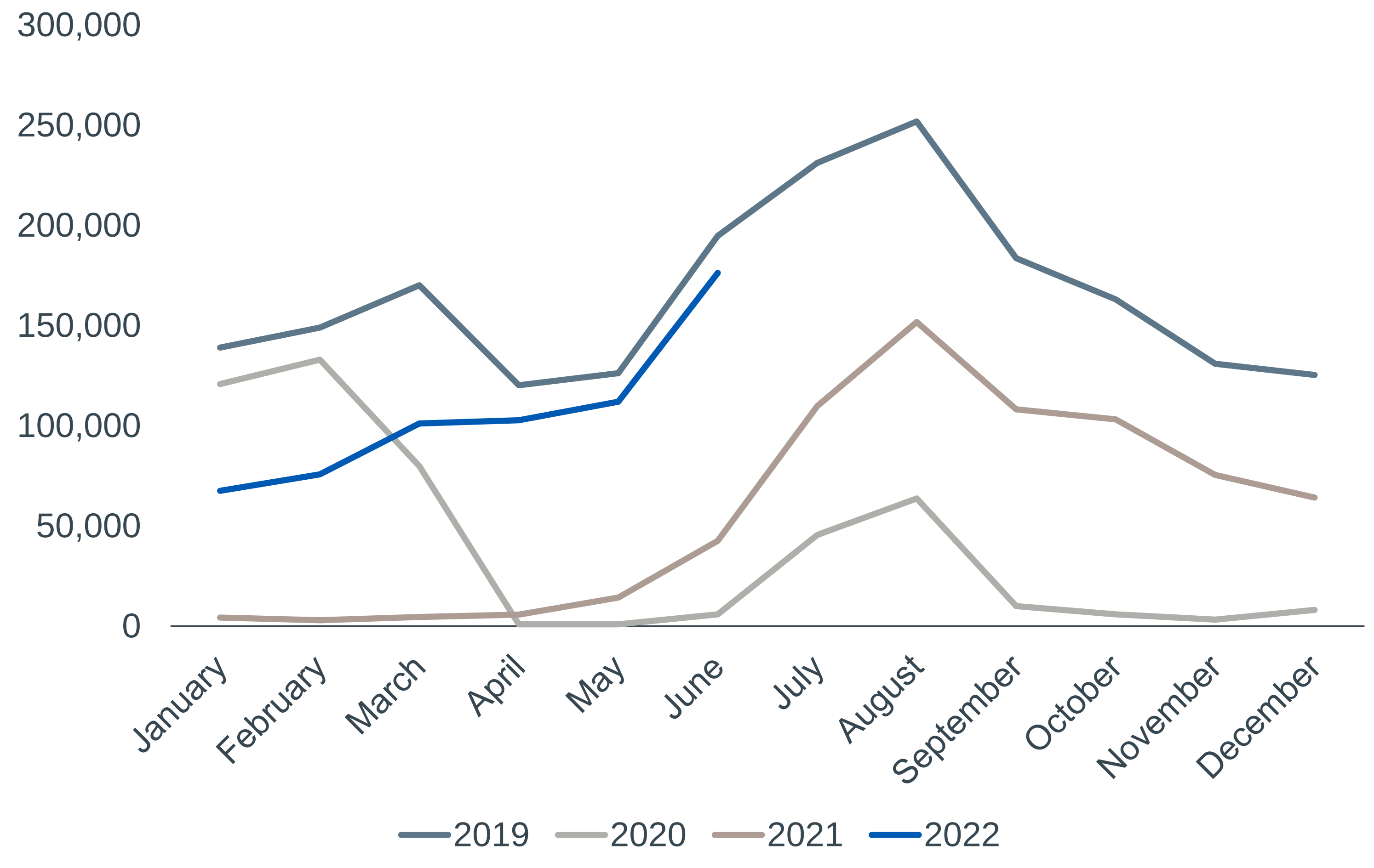
Strong economic growth in growing global uncertainty

GDP increased by 8.6% YoY in Q1, a result that was well above analysts' expectations. Growth was driven by record-breaking private consumption and increased growth in tourism. Robust domestic economic activity is reflected in large current account deficit, falling unemployment rate and rising inflation.

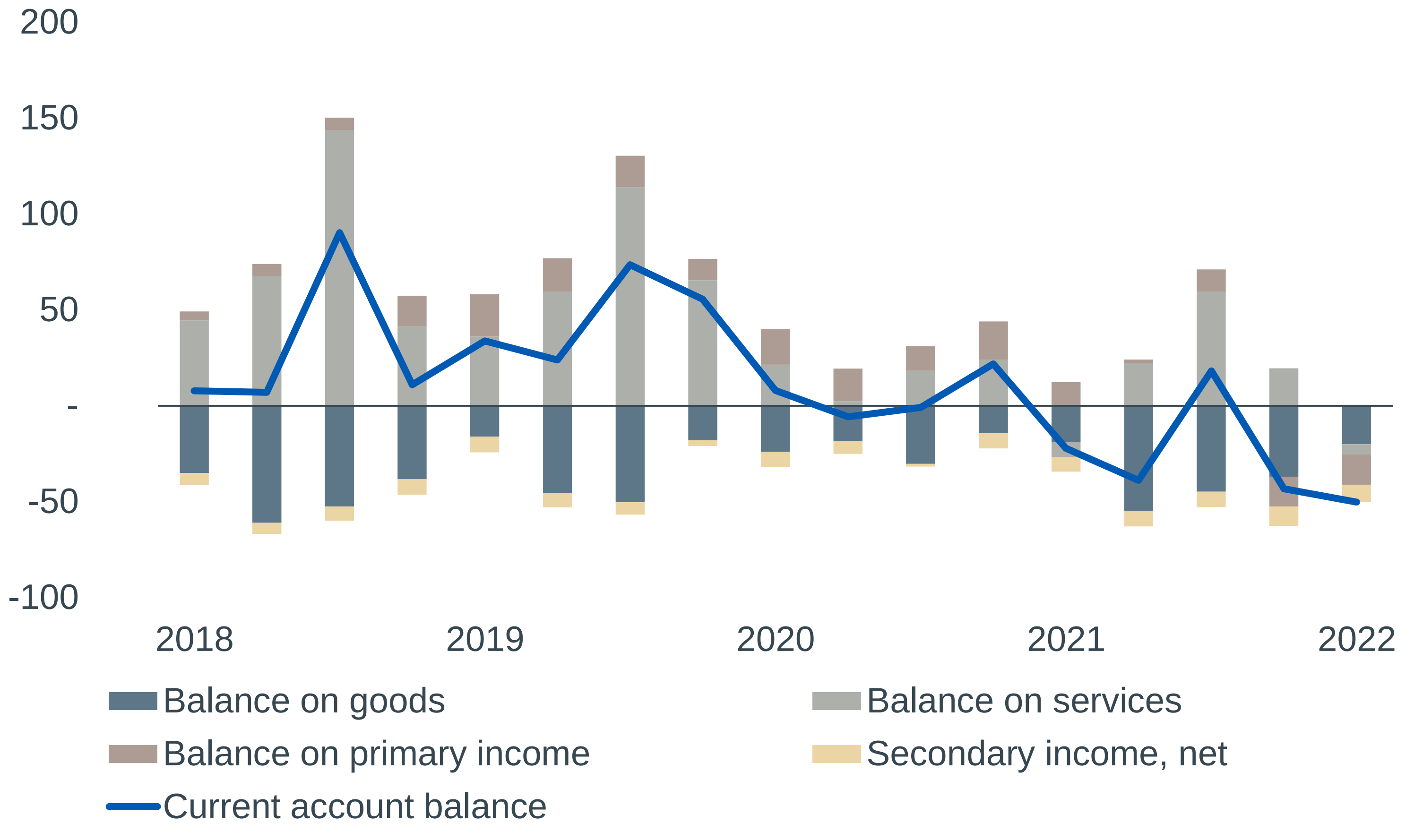
GDP in Q1 2022
- comparison between forecast and actual results



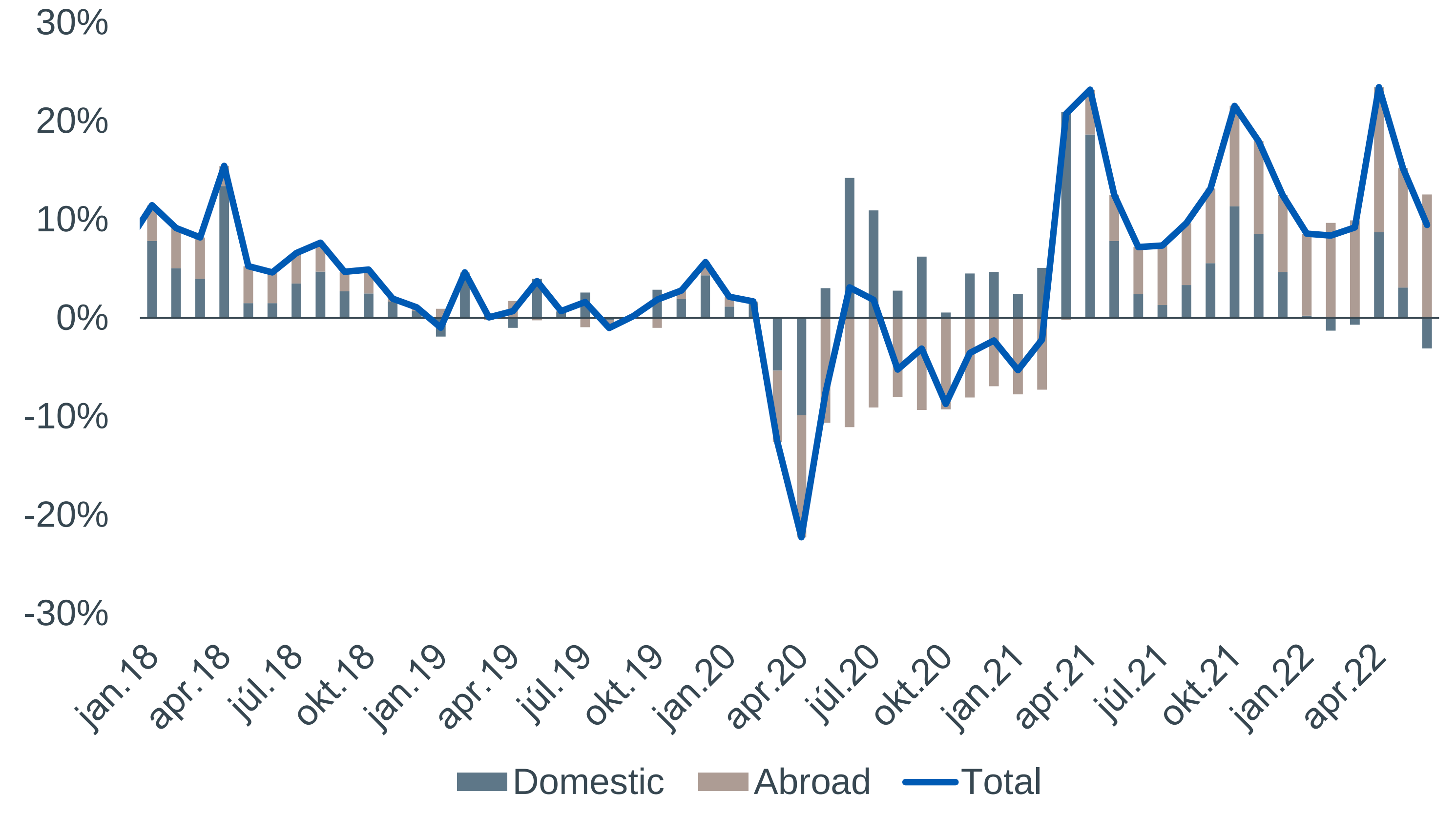
Tourist arrivals via Keflavik International Airport



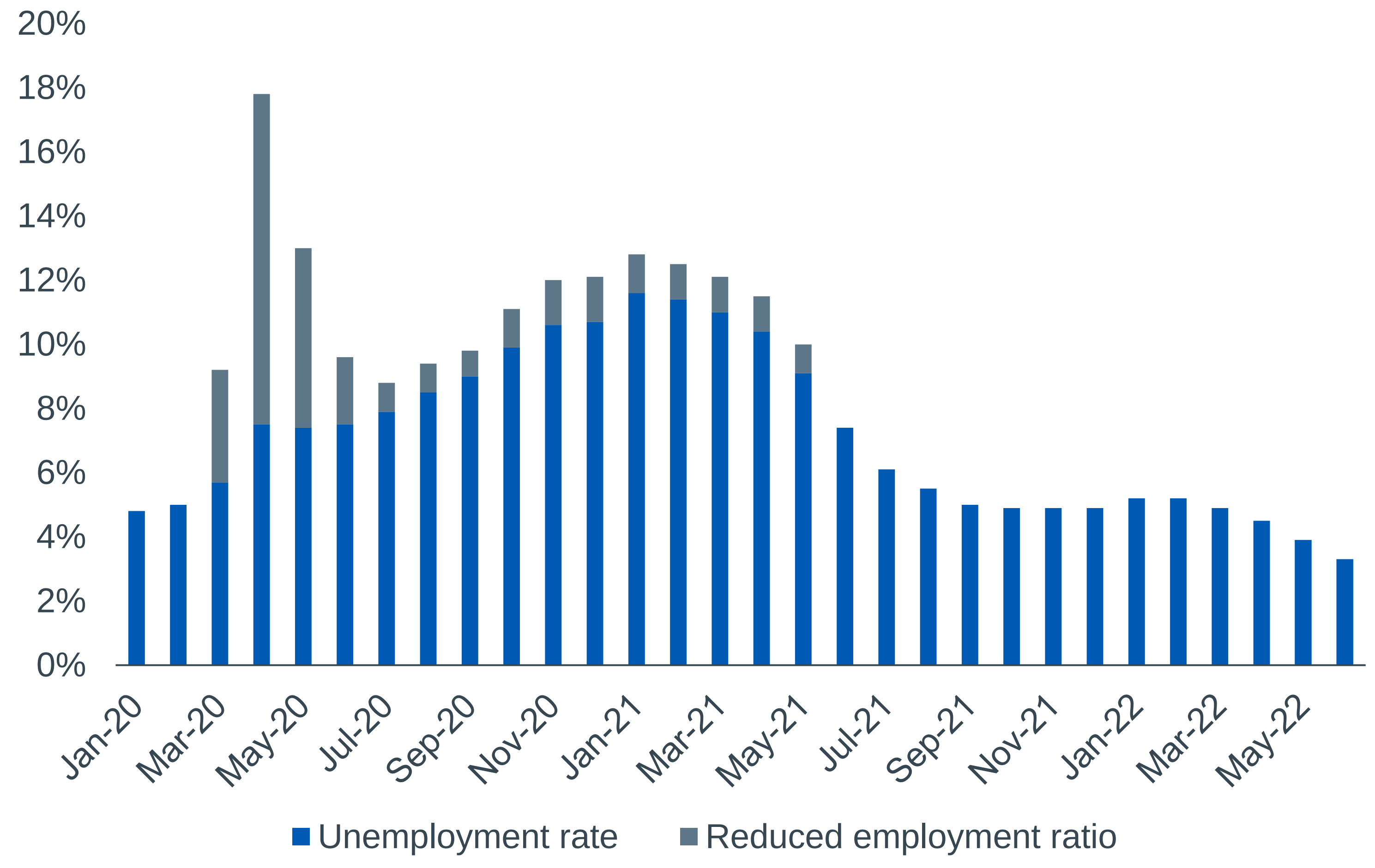
Current account balance
- bn. ISK at constant exchange rate



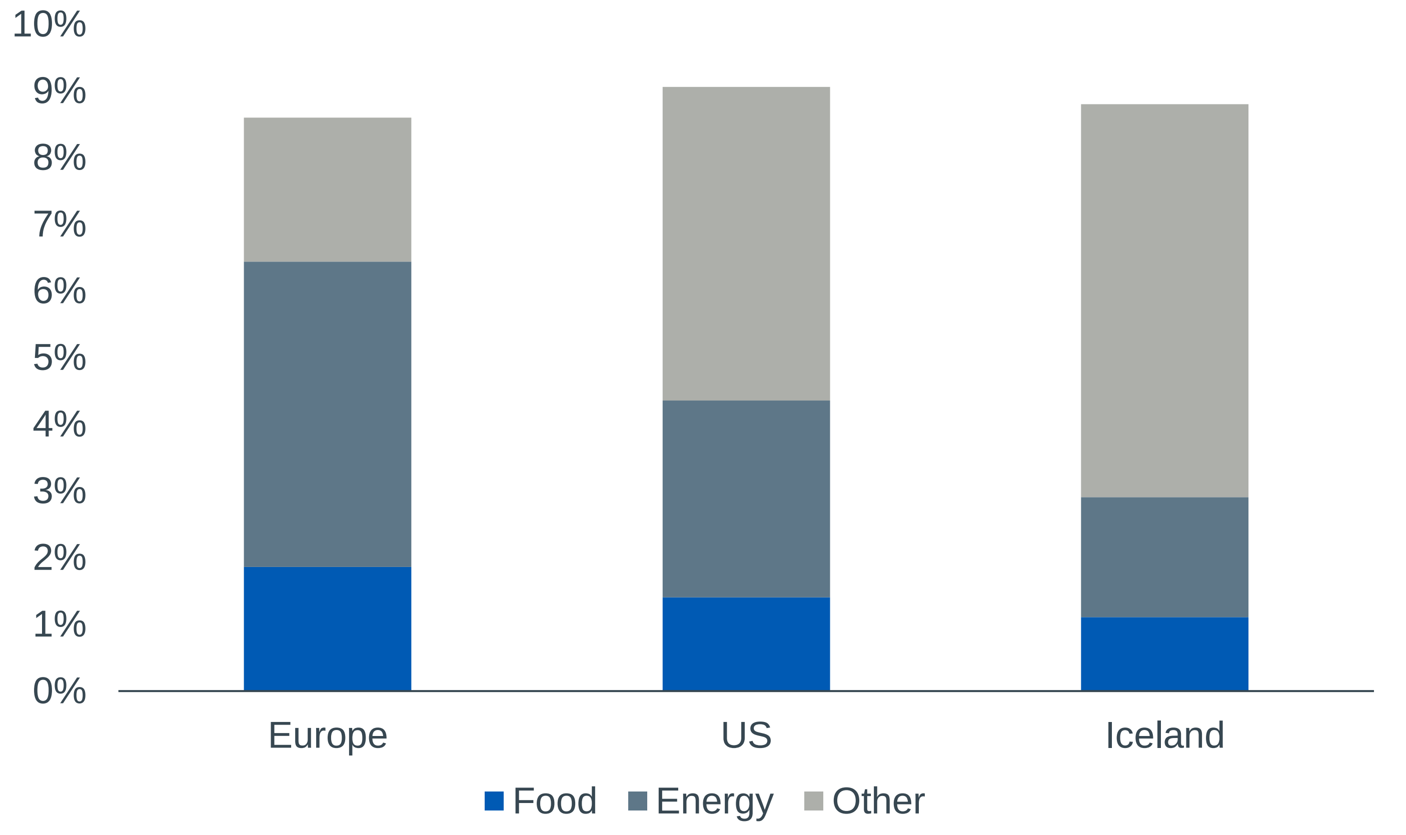
Payment card turnover
- YoY growth, growth contributions of underlying components



The composition of registered unemployment



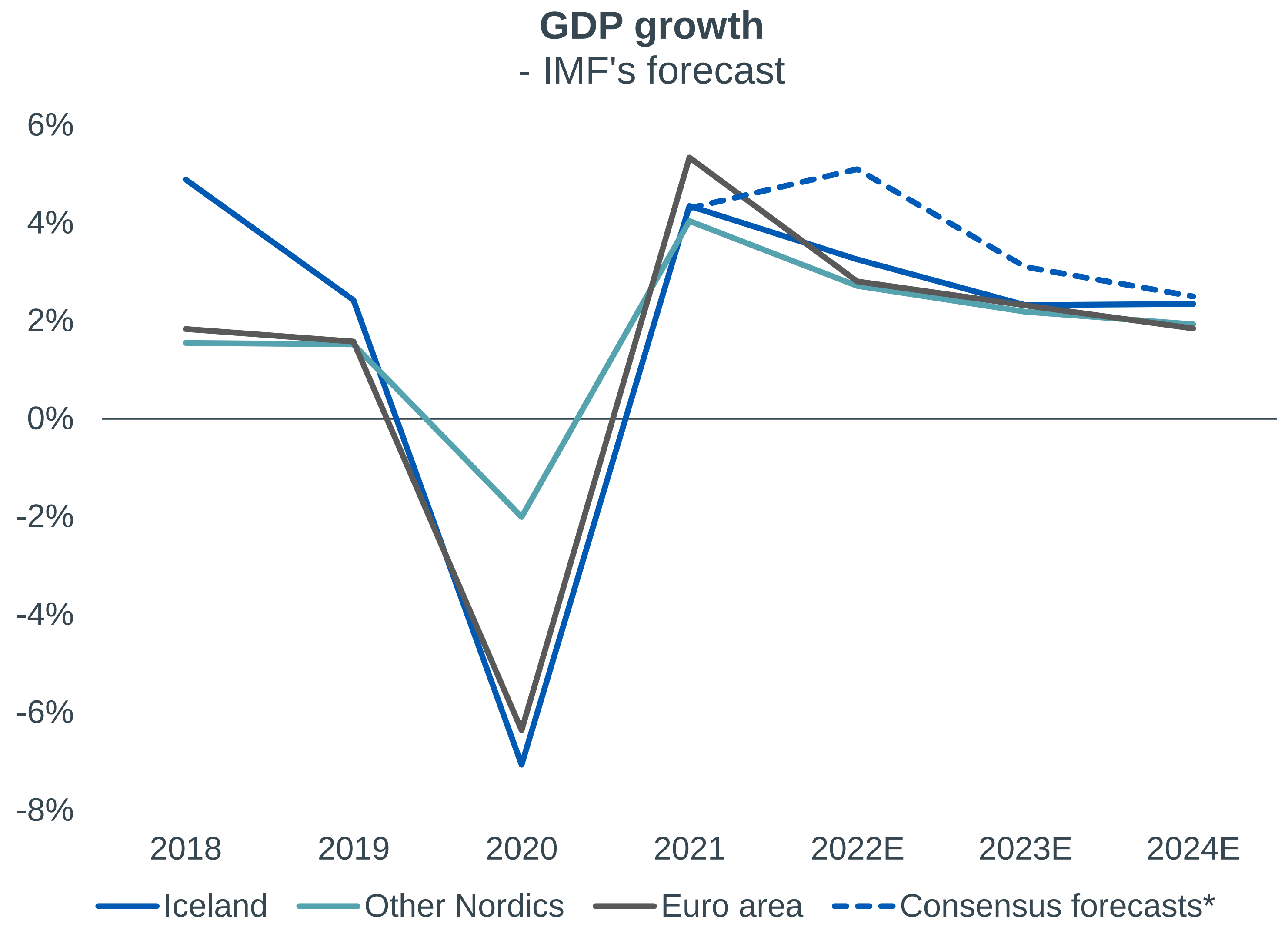
Contribution to annual inflation rate
- June

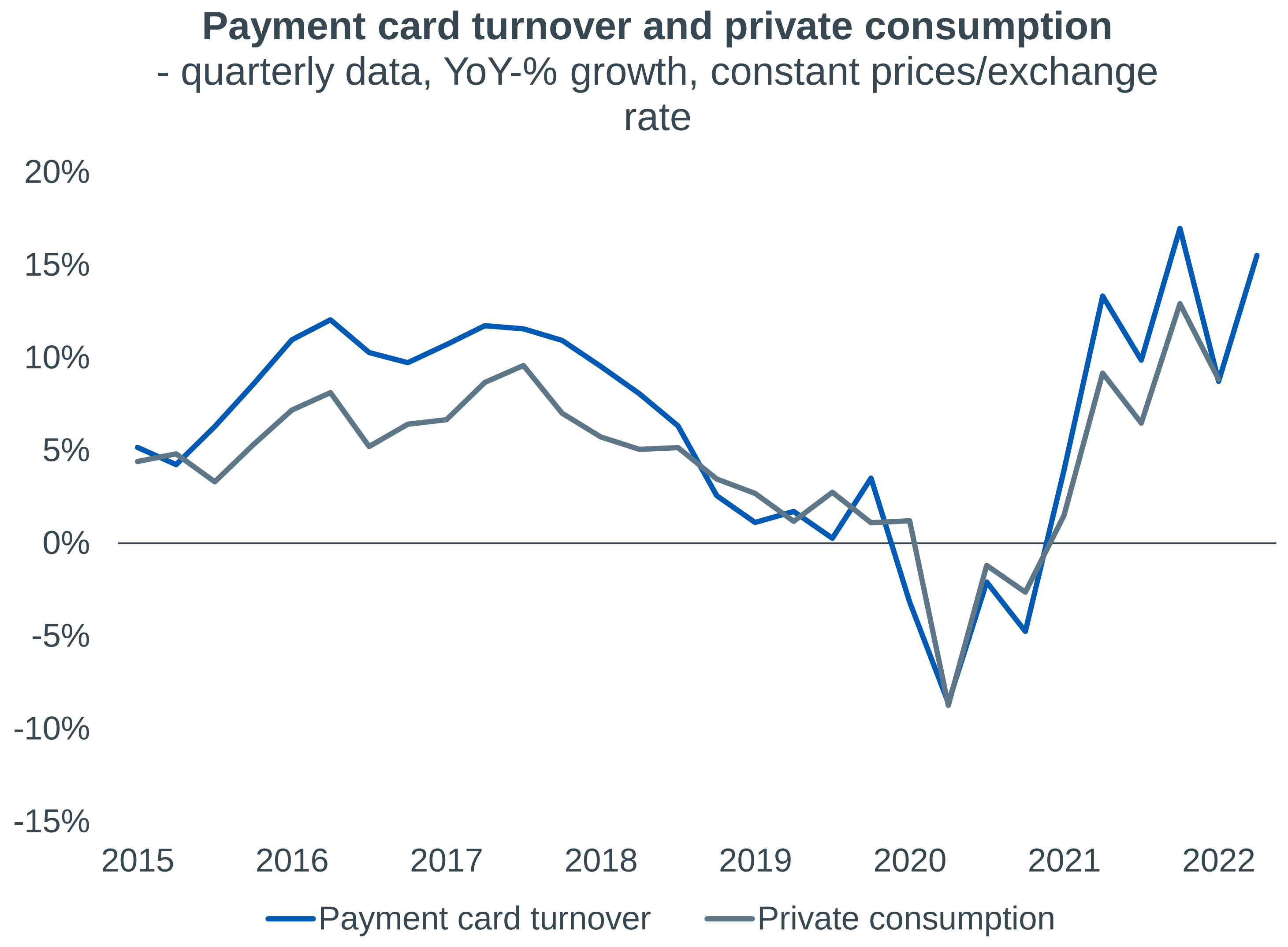


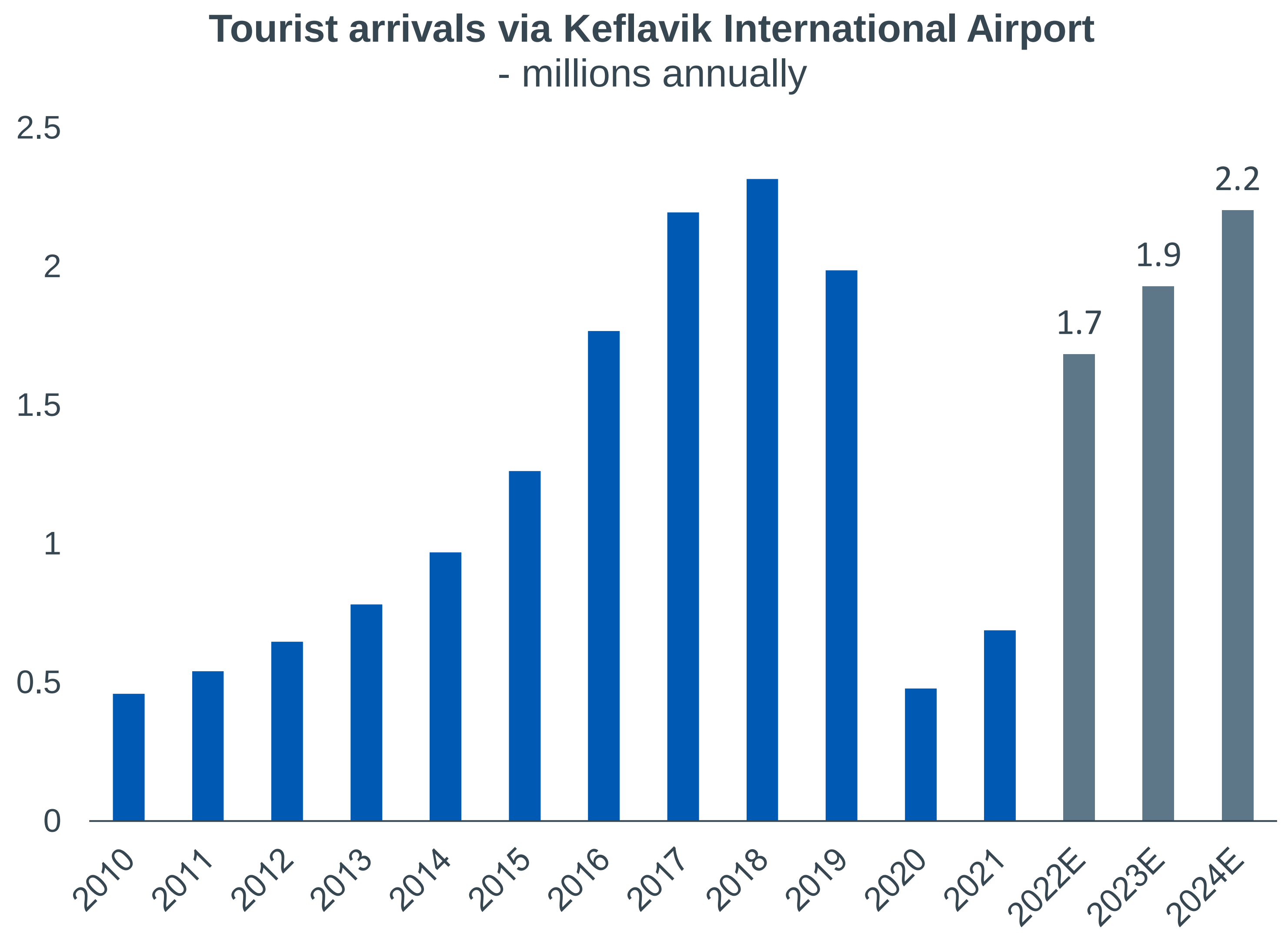
Sources: Statistics Iceland, Central Bank of Iceland, Arion Bank

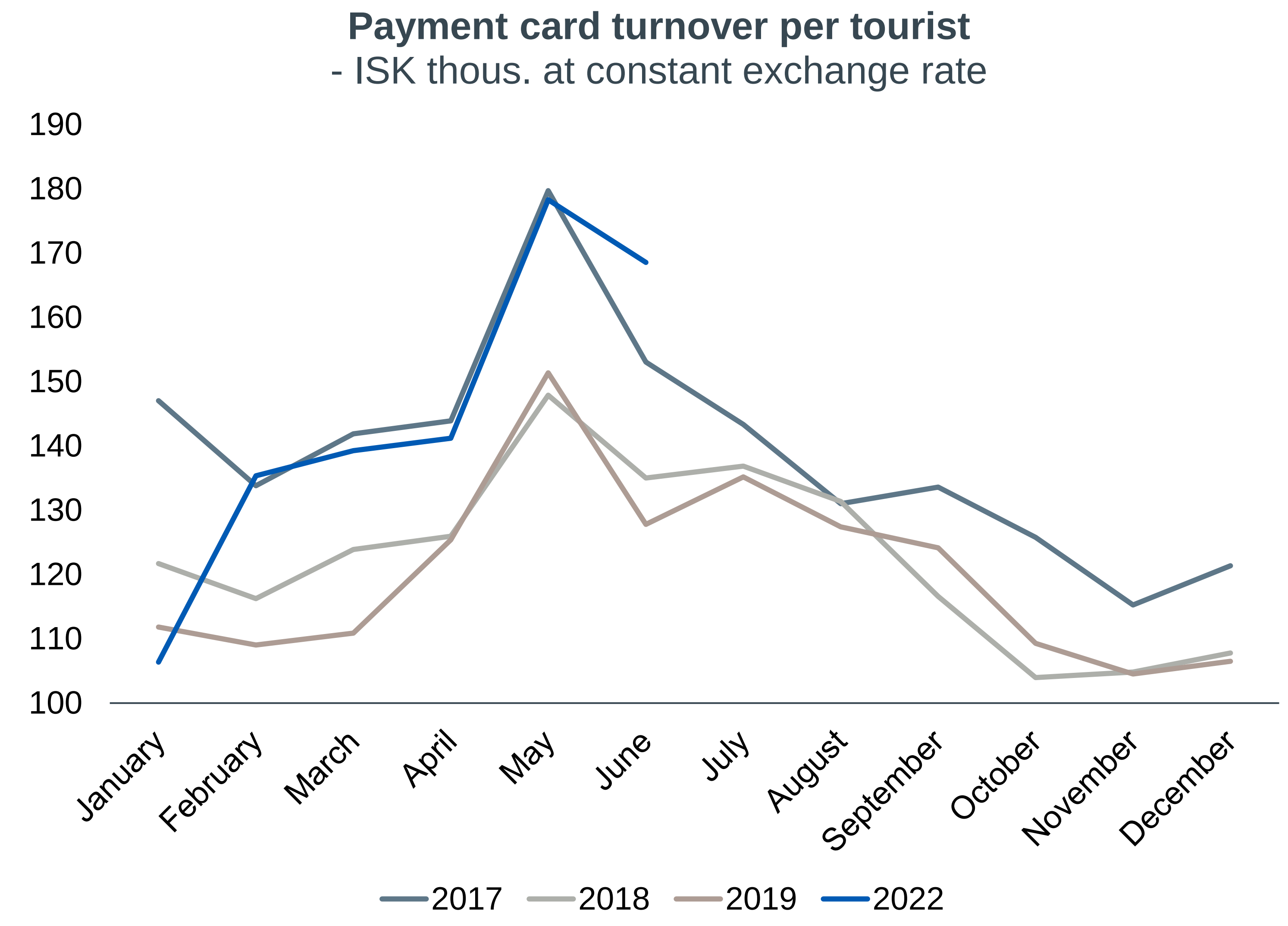
Relatively positive outlook

- Despite the highly uncertain global economic outlook the Icelandic economy is set for strong growth in 2022, driven by tourism, business investment and household consumption
- While the IMF expects the Icelandic economy to grow in line with other Nordics, domestic analysts are more optimistic, with the consensus at 5.1% growth in 2022
- Household consumption has surprised analysts, reaching unprecedented heights in the past quarters. This trend is set to continue in Q2 as payment card turnover increased by 16% YoY
- Tourism has almost regained its former strength, with tourist arrivals in June reaching 90% of June 2019. More importantly, each tourist is spending much more than pre-covid, despite high inflation on both sides of the Atlantic









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

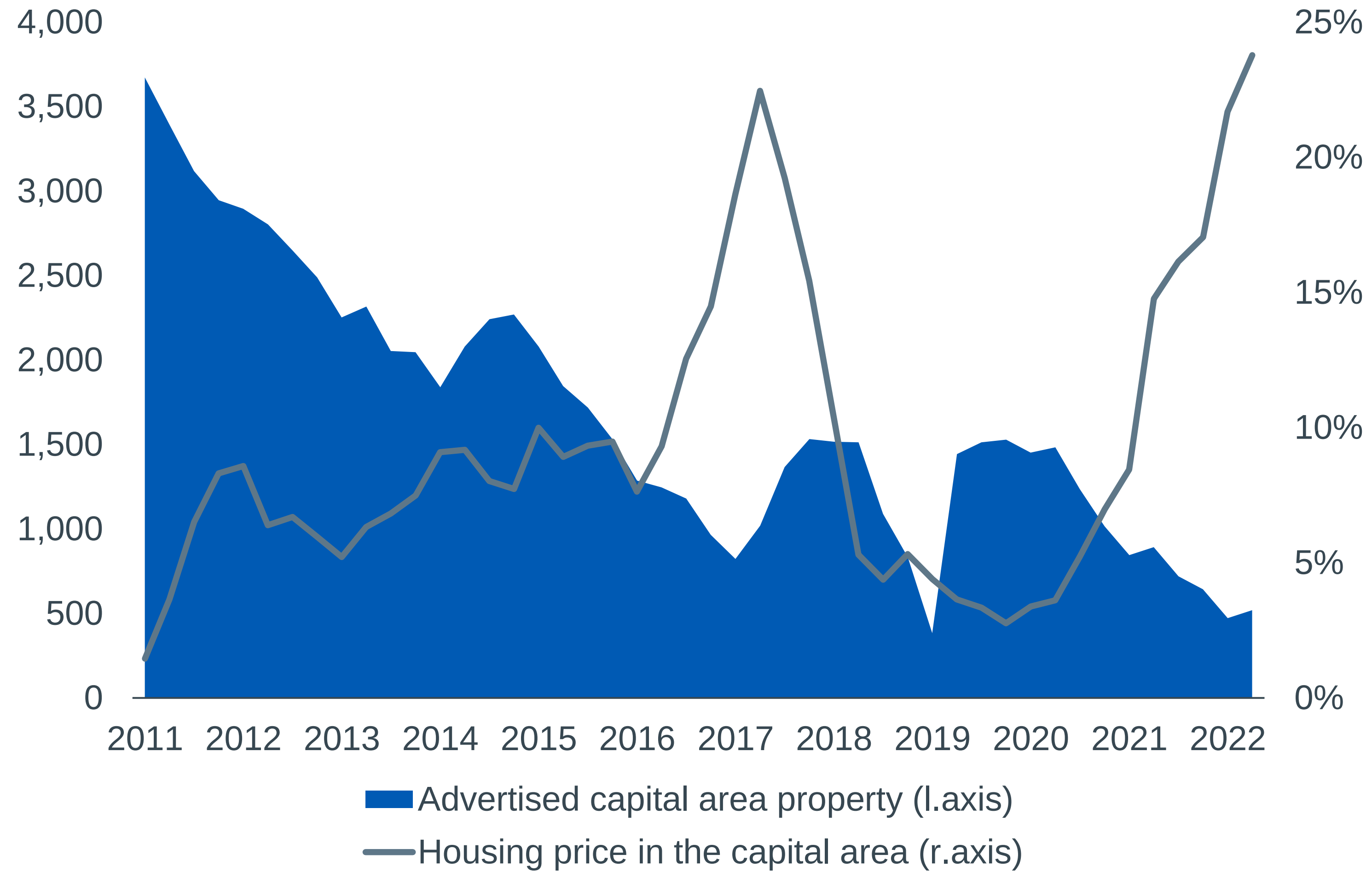
Taming the housing market

- House prices rose sharply in Q2, increasing by 24% YoY. In the first half of this year, an average of 500 properties were advertised for sale monthly in the capital area, the lowest number ever recorded

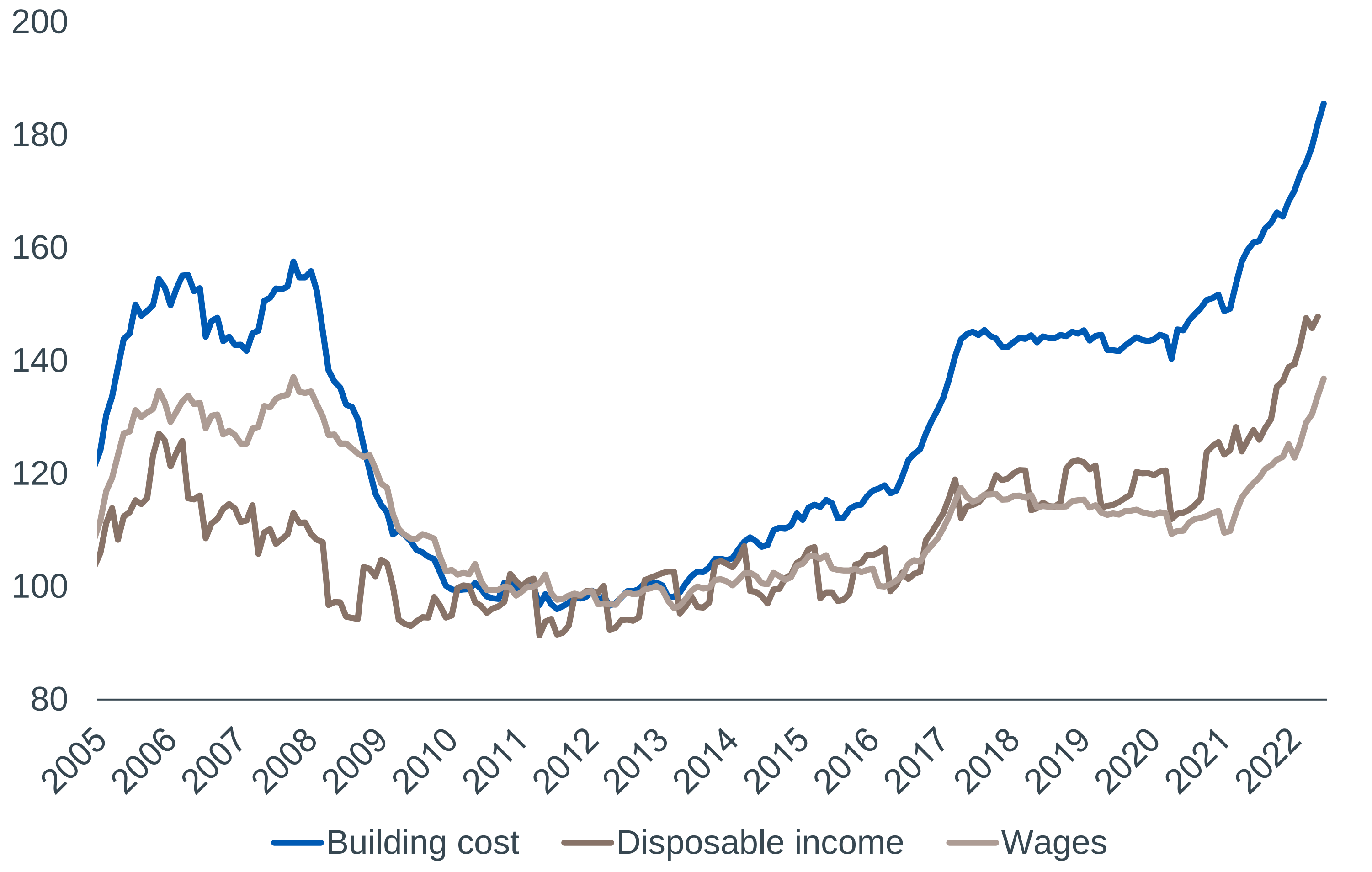
- Housing prices have risen at a considerably quicker rate than wages, and especially disposable income, over the past year, leading to growing imbalances

- In response to the current circumstances, the Financial Stability Committee of the Central Bank decided to lower the maximum loan-to-value for first time buyers, from 90% to 85%, and established a reference interest rate for the calculation of debt service, setting the rate at 3% for indexed mortgages and 5.5% for non-indexed mortgages

Advertised capital area property and housing price
- quarterly data, no. and YoY %-change

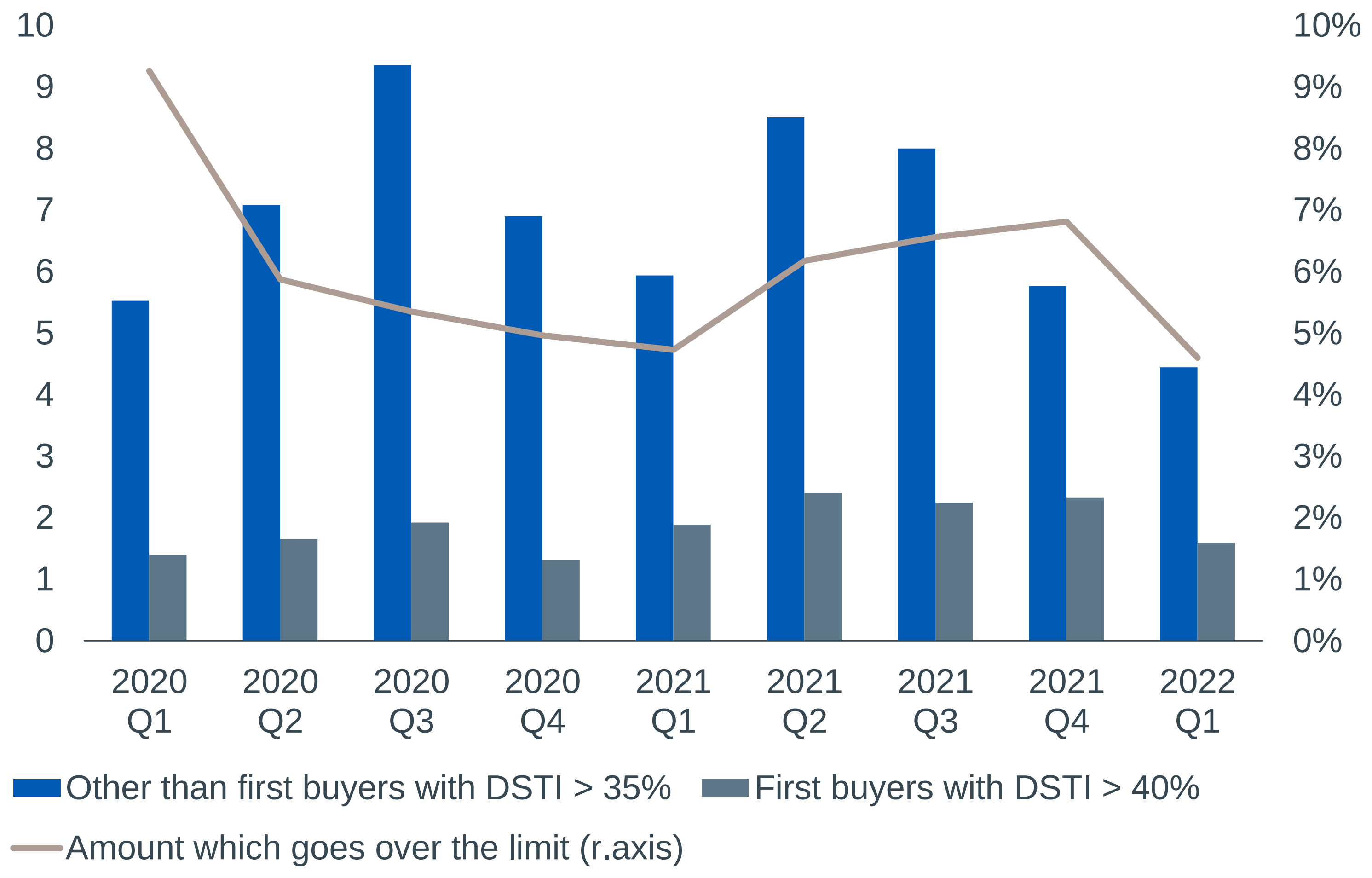


House prices relative to fundamentals
- indices, January 2011 = 100



Arion Bank´s mortgage rates

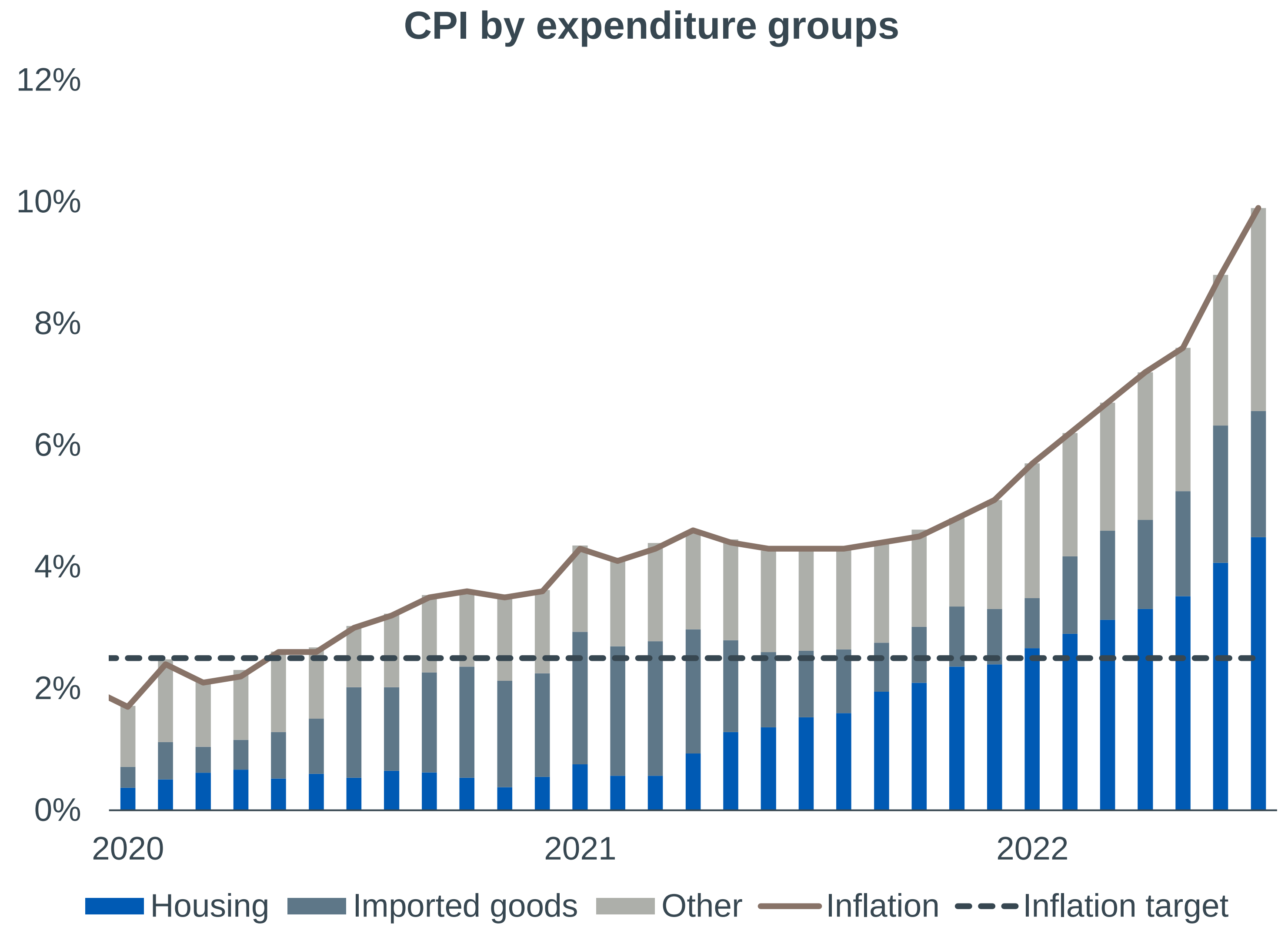
Impact of rules on maximum debt service-to-income
- bn. ISK and % of total amount of new loans

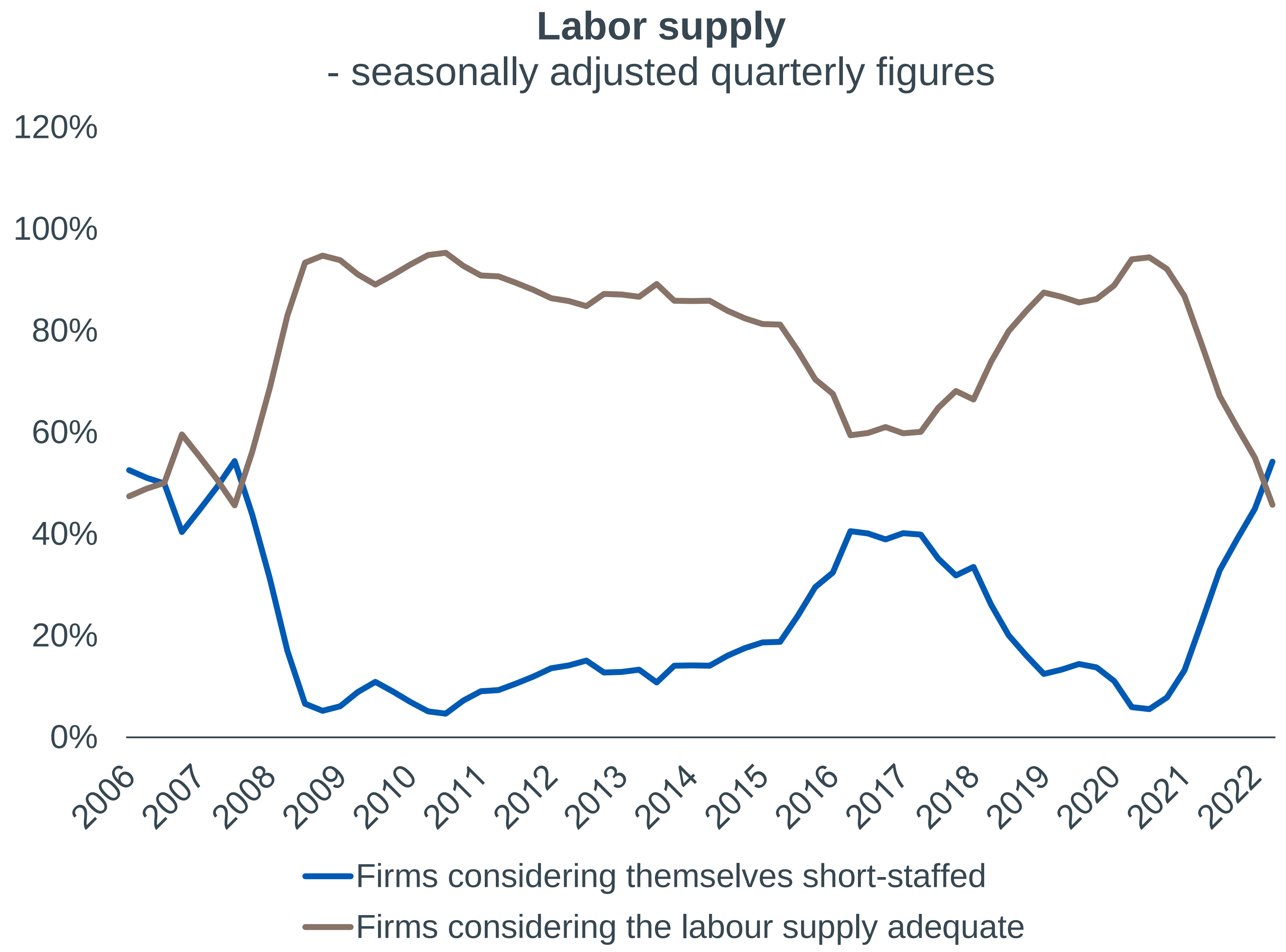


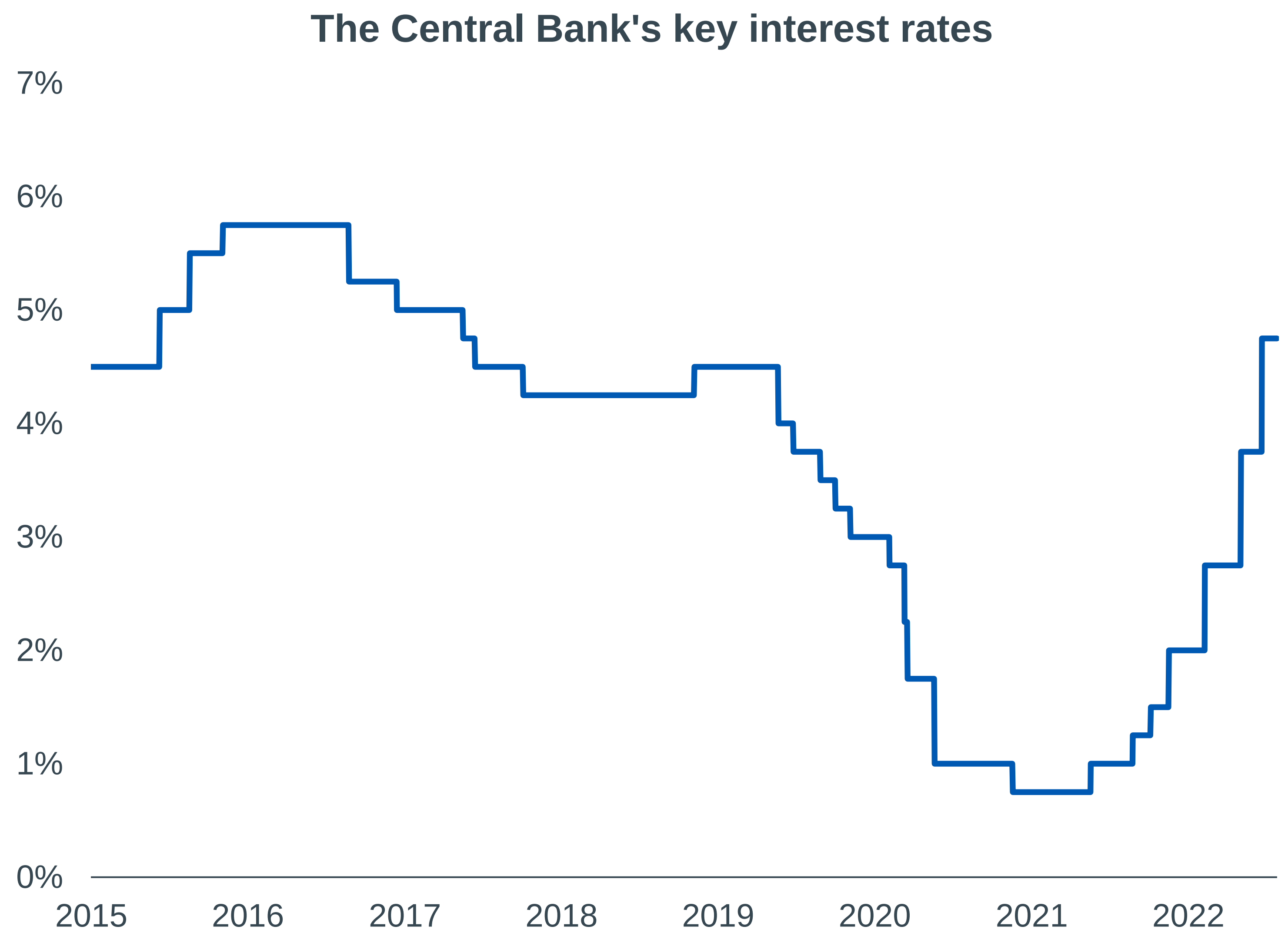
Sources: Registers Iceland, Central Bank of Iceland, Statistic Iceland, Einar Jón Erlingsson *Þróun á húsnæðismarkaði og virkni lánþegaskilyrða,* Arion Bank.

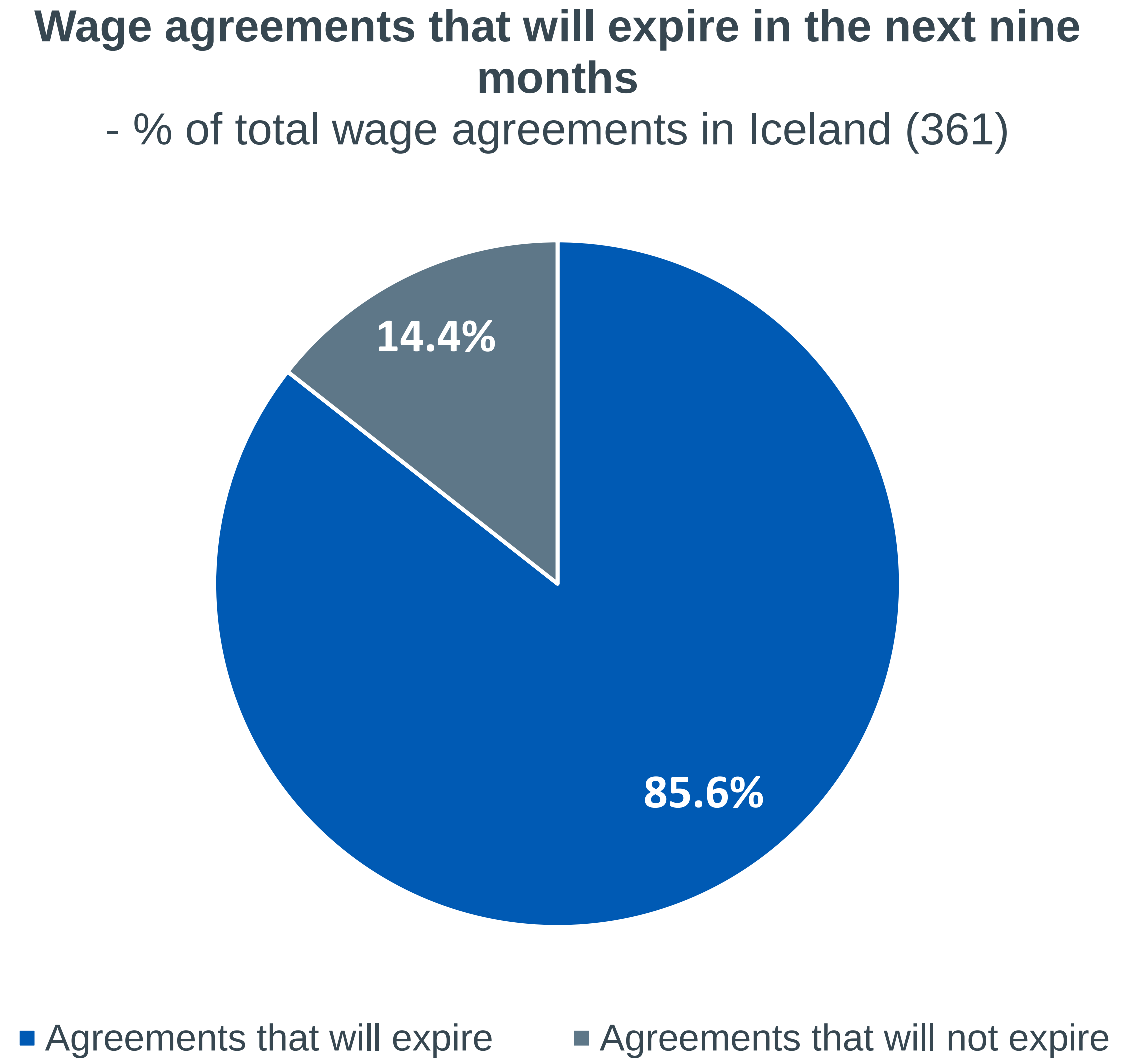
Challenging times

- Climbing housing prices, imported inflation and domestic demand pressures have stoked inflation, which has proven to be much more persistent than previously forecast
- Most analysts expect inflation to be around 10% over the next months, before trickling down. The CBI's inflation target will however not be reached in the foreseeable future
- Persistent inflation, strong domestic economic activity and fear over de-anchoring of inflation expectations has compelled the CBI to raise interest rates by 400 bps. since May last year
- Further rate hikes will largely depend on the decisions taken in the labor market, where over 85% of wage agreements expire in the next nine months. The labor market is currently tight, with 3.3% unemployment rate, staffing shortages and increased pressure on wages



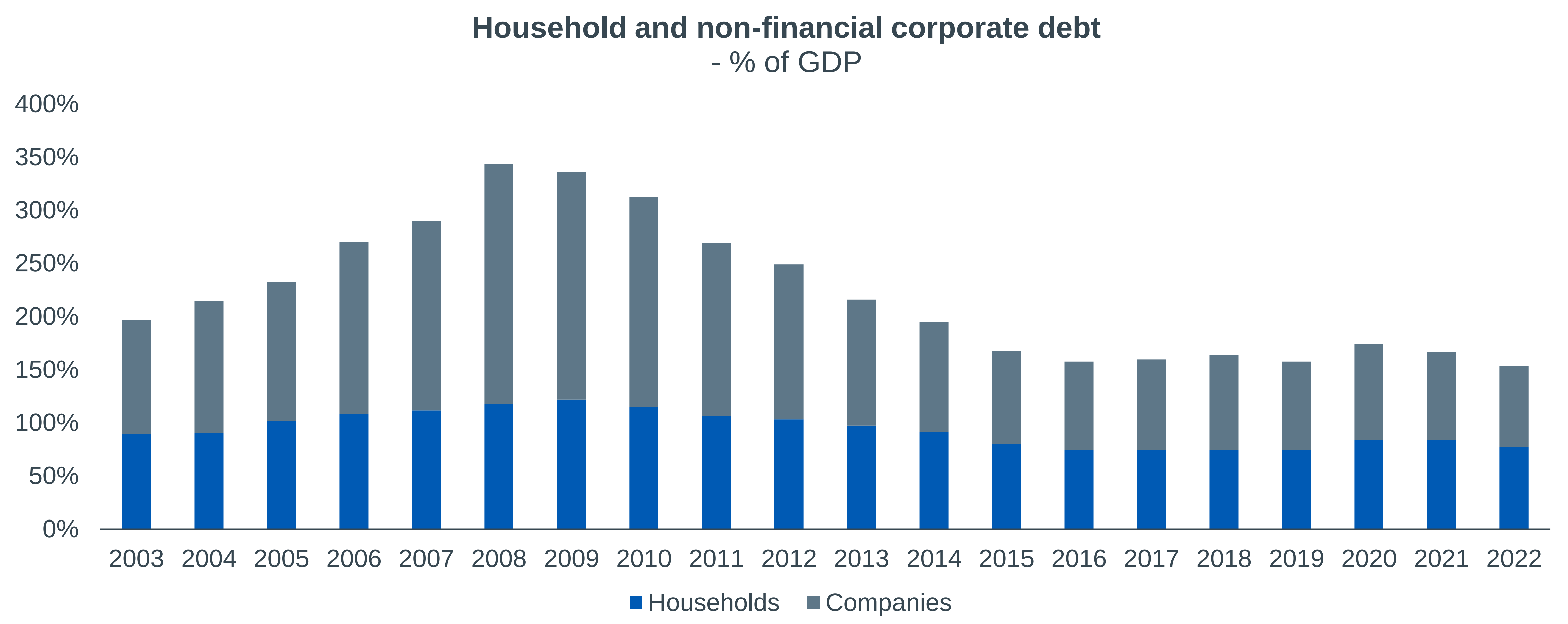


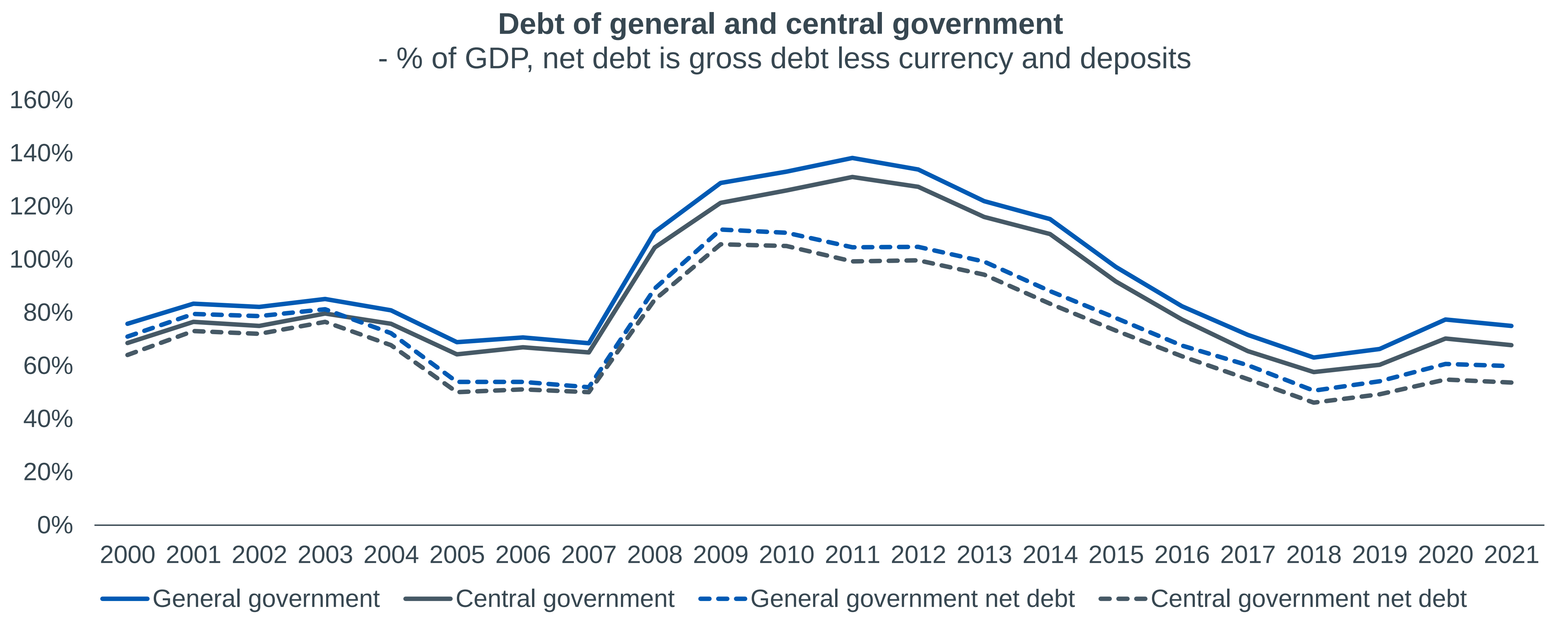


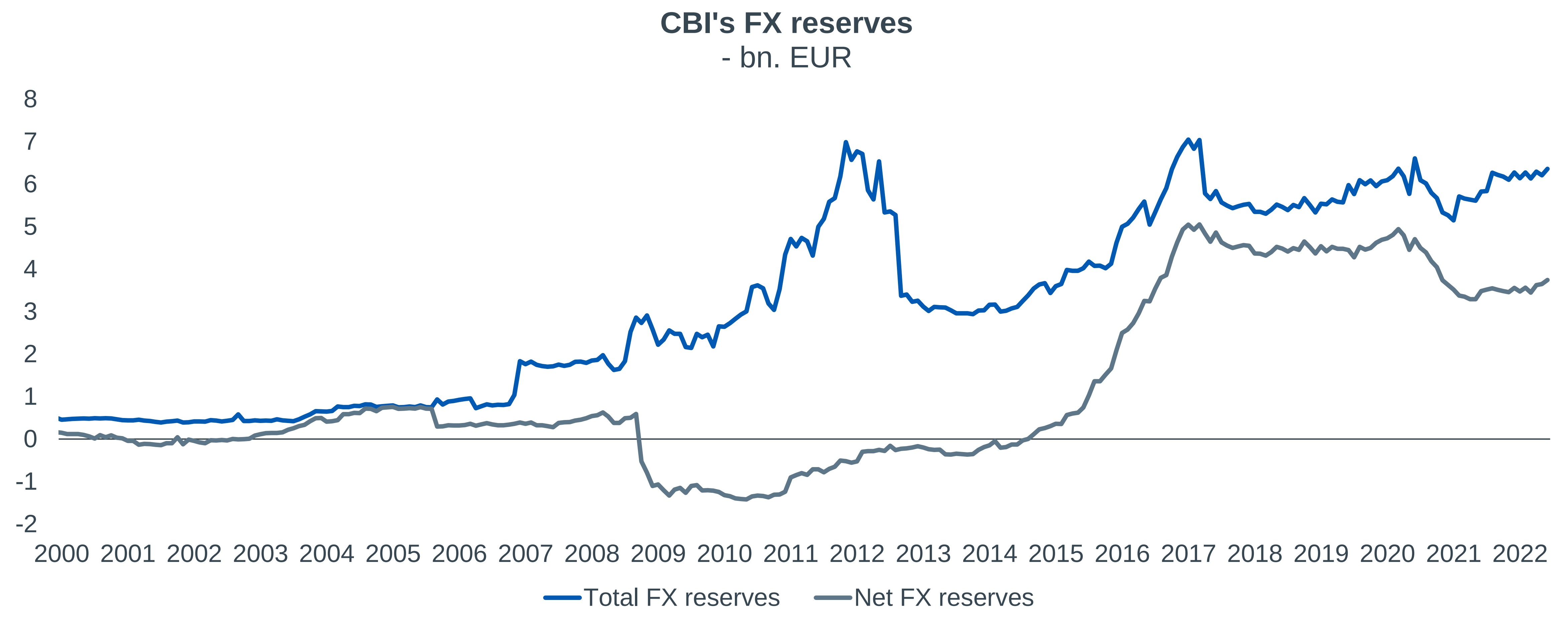


Sources: Statistics Iceland, Central Bank of Iceland, The State Conciliation and Mediation Officer, Arion Bank

Small economy, strong foundations







 Sources: Central Bank of Iceland, Arion Bank

Financials

Key takeaways in Q2 2022

Profitability *Eventful quarter*	▸ Net profit of 9.7bn and ROE of 21.8% in the quarter ▸ Momentum in Core Income[1], increasing by 23.5% YoY, countered somewhat by loss on financial assets and high effective tax rate ▸ Strong pipeline and positive momentum across our businesses, while external environment retains level of uncertainty
Valitor and Sólbjarg *Milestones in HFS line*	▸ Sale of Valitor completed and fully accounted for in the quarter. Total proceeds of ISK 14.6bn (USD 112.5m) with net profit of ISK 5.6bn ▸ Capital release from sale of ISK 13.8bn ▸ Additional recoveries within Sólbjarg resulting in earnings of ISK 0.5bn
Net commissions *Record quarter*	▸ Net commissions of ISK 4.5bn represents the highest in a single quarter for the Bank, driven by strong activity in CIB ▸ Pipeline remains strong but activity near term will be impacted by market dynamics ▸ Sale of Valitor anticipated to support card fee income going forward
Net interest income *Strong NIM retained*	▸ Net interest income increases 22% YoY and 3% from last quarter ▸ Net interest margin holding at a strong level of 3.1% with rate sensitivity slowing somewhat mainly from liability side impact
Capital and liquidity *Robust position*	▸ Capital and liquidity positions remain robust and allows for optionality in terms of capital and balance sheet management ▸ Moody's rating and ECB repo window accessibility further support funding options ▸ A new buy-back program pending regulatory approval

[1] Net interest income, net fee and commission income and net insurance income

Income statement Q2 2022

- Core income (NII, NCI and net insurance income) increases 23.5% YoY and 17.9% from last quarter
- Strong growth in NII YoY, mainly due to increased base rate and 20% growth in the loan book from Q2 2021
- Continuing strong NCI growth across the Bank
- Stronger performance in net insurance income following a weak Q1
- Negative Net financial income due to difficult market conditions and reclassification from OCI equity reserve
- Operating expense increased by 4% YoY, significantly below inflation of 7% YoY
- Positive effect from impairments, largely due to recovery on loans previously written off
- Income tax rate unusually high due to unfavorable combination of income
- Profit form sale of Valitor of ISK 5.6bn. Profit of ISK 0.5bn from sale of assets within Sólbjarg

	Q2 2022	Q2 2021	Diff	Q1 2022	Diff
Net interest income	9,804	8,016	22%	9,528	3%
Net commission income	4,539	3,562	27%	3,552	28%
Net insurance income	1,086	914	19%	5	-
Net financial income	(2,911)	2,203	-	991	-
Share of profit of associates	23	25	(8%)	203	(89%)
Other operating income	719	284	153%	235	206%
Operating income	**13,260**	**15,004**	**(12%)**	**14,514**	**(9%)**
Salaries and related expense	(3,843)	(3,575)	7%	(3,540)	9%
Other operating expenses	(2,806)	(2,797)	0%	(2,661)	5%
Operating expenses	**(6,649)**	**(6,372)**	**4%**	**(6,201)**	**7%**
Bank levy	(416)	(355)	17%	(393)	6%
Net impairment	186	812	(77%)	(495)	-
Net earnings before taxes	**6,381**	**9,089**	**(30%)**	**7,425**	**(14%)**
Income tax expense	(3,488)	(1,408)	148%	(1,703)	105%
Net earnings from continuing operations	**2,893**	**7,681**	**(62%)**	**5,722**	**(49%)**
Discontinued operations net of tax	6,819	135	-	96	-
Net earnings	**9,712**	**7,816**	**24%**	**5,818**	**67%**
Return on equity	21.8%	16.3%		12.7%	

 All amounts in ISK m

Income statement H1 2022

- Core income (NII, NCI and net insurance income) increases 19.9% YoY
- Very strong increase in NII YoY, mainly due to increased base rate and 20% growth in loans to customers from Q2 last year
- Continuing strong NCI growth across the Bank
- Weak first quarter in net insurance income mainly due to high claim rate but insurance premiums have increased by 10% from H1 2021
- Negative Net financial income partly due to reclassification from OCI equity reserve
- Operating expense increased by 3% YoY, significantly below inflation during the period
- Impairments lower than through the cycle expectations of 21bps
- Income tax rate unusually high due to unfavorable combination of income
- The profit from sale of Valitor is ISK 5.6bn, the operating results of Valitor and positive outcome from sale of assets at Sólbjarg of ISK 0.5bn is the main contributor

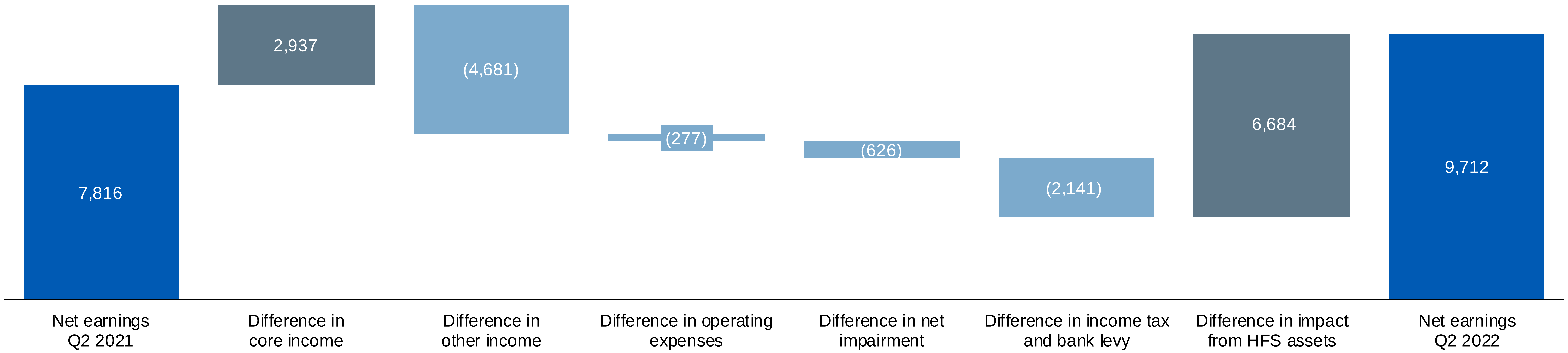
	H1 2022	H1 2021	Diff
Net interest income	19,332	15,358	26%
Net commission income	8,091	6,839	18%
Net insurance income	1,091	1,585	(31%)
Net financial income	(1,920)	3,703	-
Share of profit of associates	226	26	-
Other operating income	954	590	62%
Operating income	**27,774**	**28,100**	**(1%)**
Salaries and related expense	(7,383)	(6,846)	8%
Other operating expenses	(5,467)	(5,574)	(2%)
Operating expenses	**(12,850)**	**(12,420)**	**3%**
Bank levy	(809)	(685)	18%
Net impairment	(309)	1,892	-
Net earnings before taxes	**13,806**	**16,887**	**(18%)**
Income tax expense	(5,191)	(3,274)	59%
Net earnings from continuing operations	**8,615**	**13,613**	**(37%)**
Discontinued operations net of tax	6,915	241	-
Net earnings	**15,530**	**13,854**	**12%**
Return on equity	16.9%	14.3%	

 All amounts in ISK m

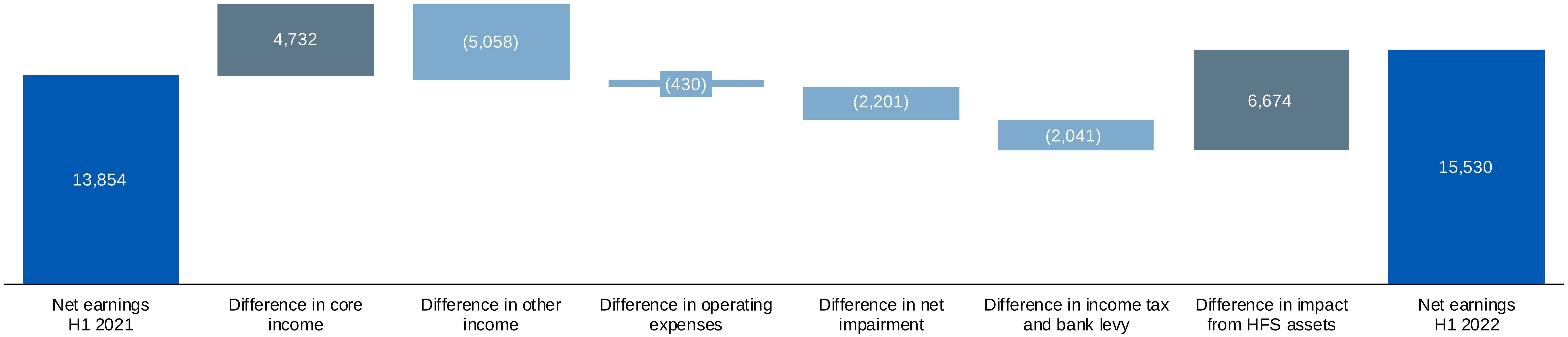
Sale of Valitor and core income support earnings growth

Negative net financial income affects other income

Q2 2021 vs. Q2 2022



H1 2021 vs. H1 2022



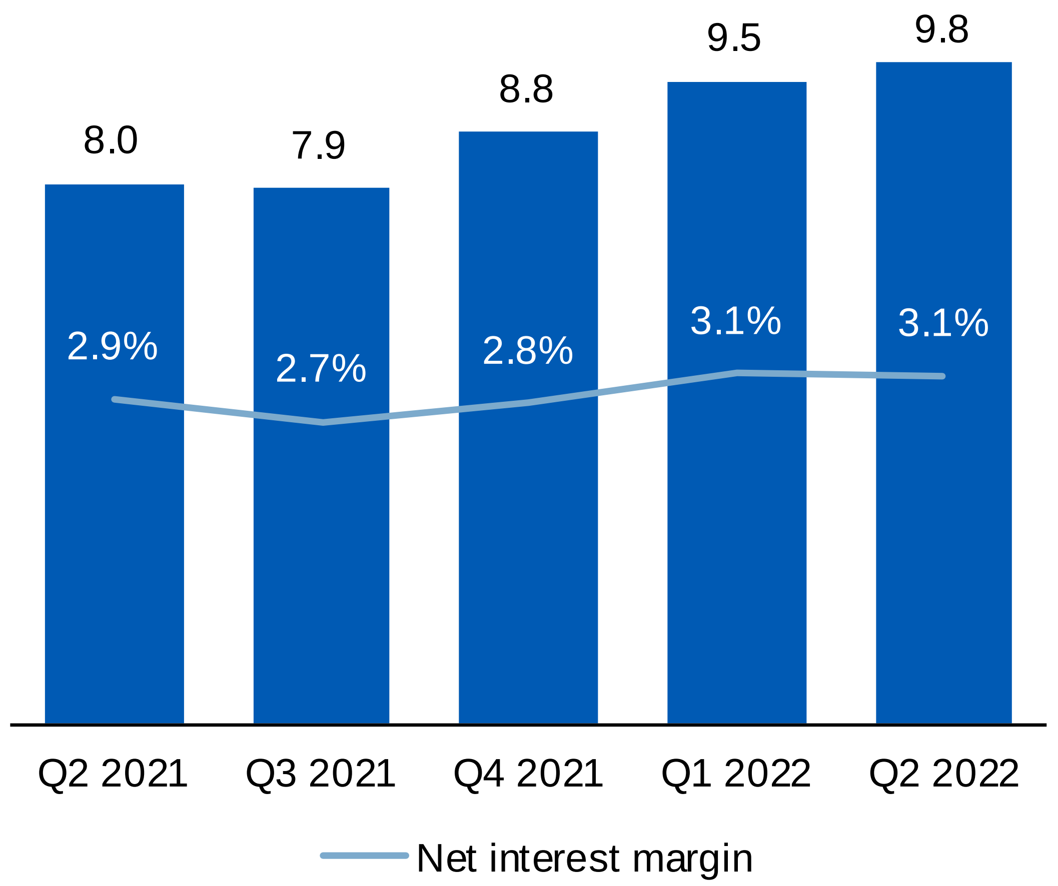
 All amounts in ISK m

Net interest income

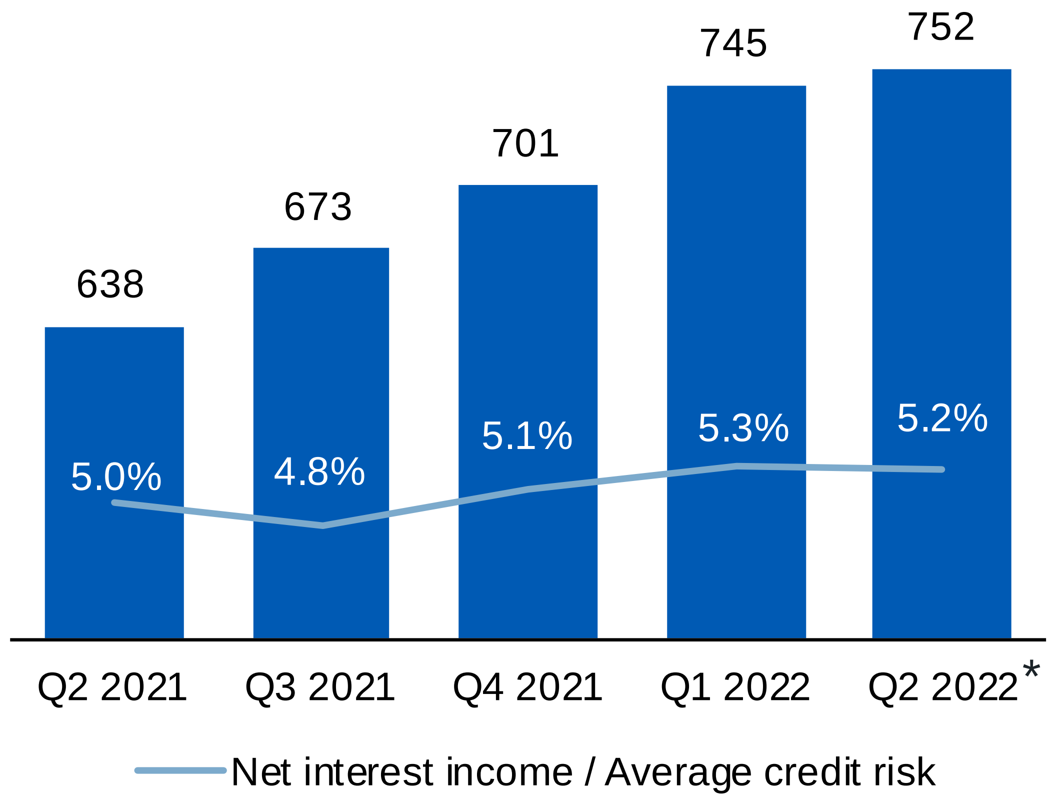
Strong 3.1% NIM retained from first quarter

- Net interest income increased by 22% from Q2 2021 whilst average interest bearing assets increased by 5%, mainly loans to customers but interest bearing liabilities increased by 4% YoY, mainly deposits
- Base rate has increased from 0.75% at the beginning of Q2 2021 to 4.75% in June 2022. During the quarter there were two rate hikes of a 100 bps each in May and at the end of June
- Net interest income / average credit risk continues at strong levels – stable around 5% and significantly up from previous years
- Evolution of borrowings has had a positive effect on NII, with similar funding cost on 20% higher borrowings

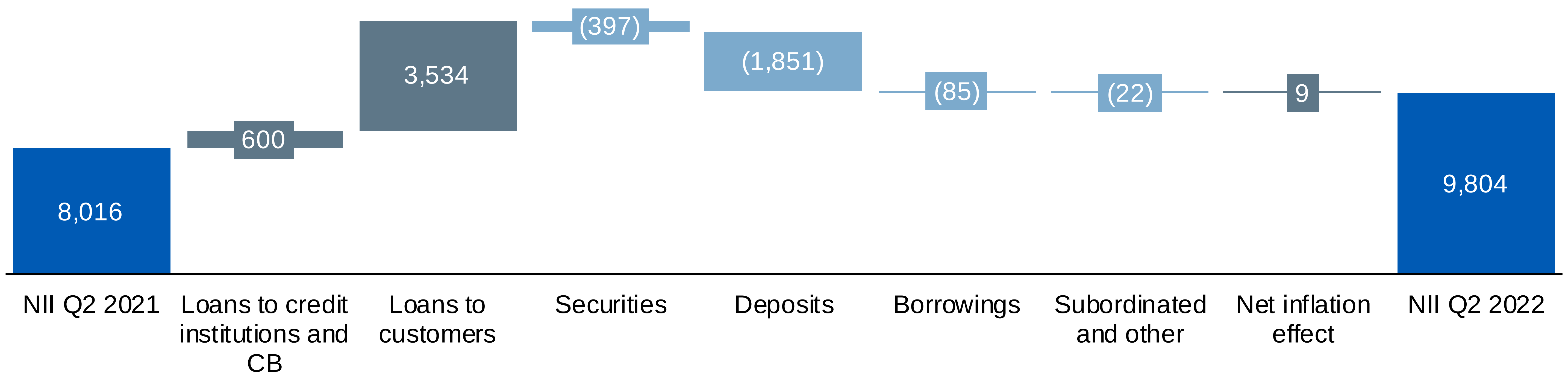
Net interest income



Credit risk



Net interest income Q2 2021 vs. Q2 2022 (ISK m)



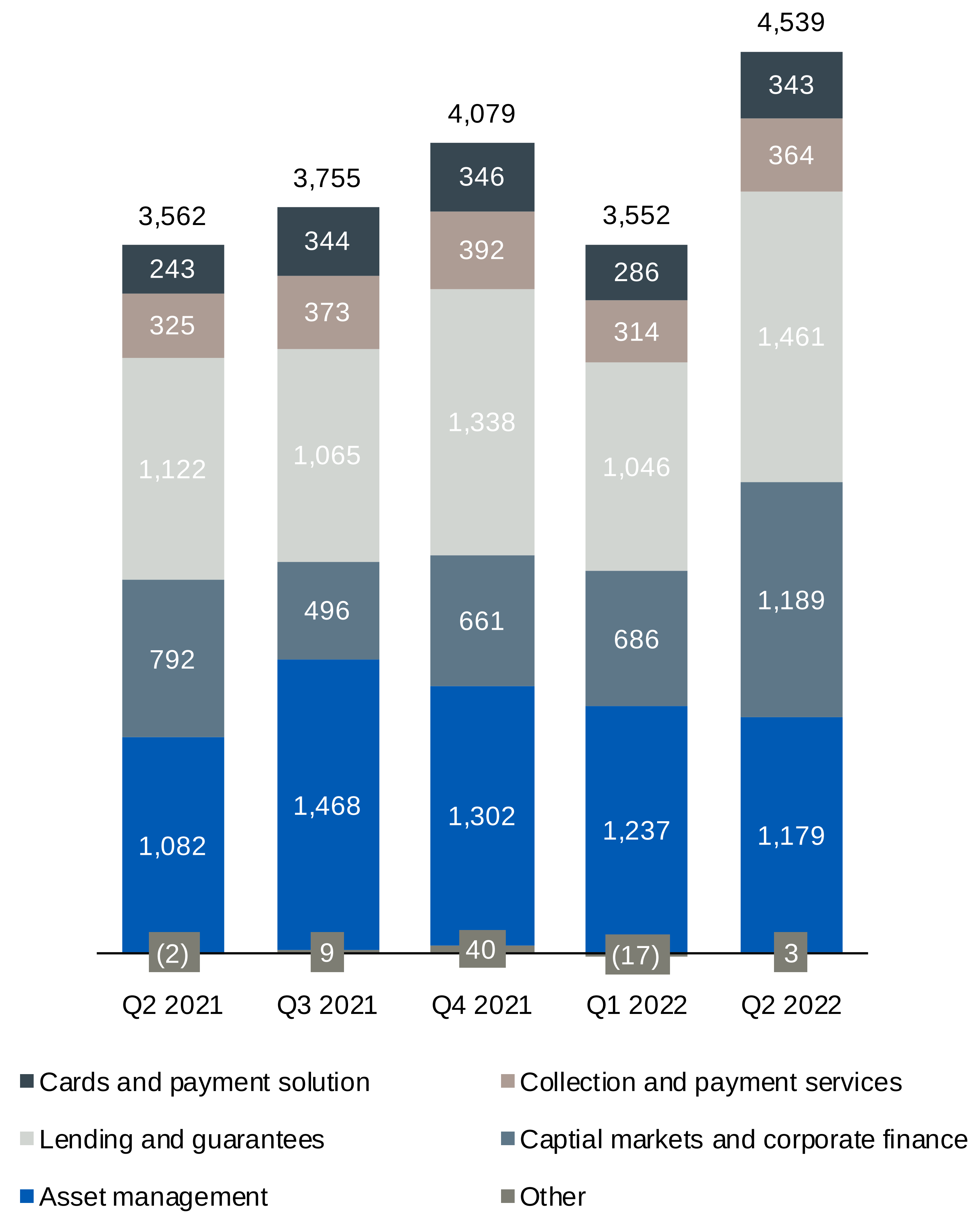
*Including full impact of Valitor sale

Net fee and commission income

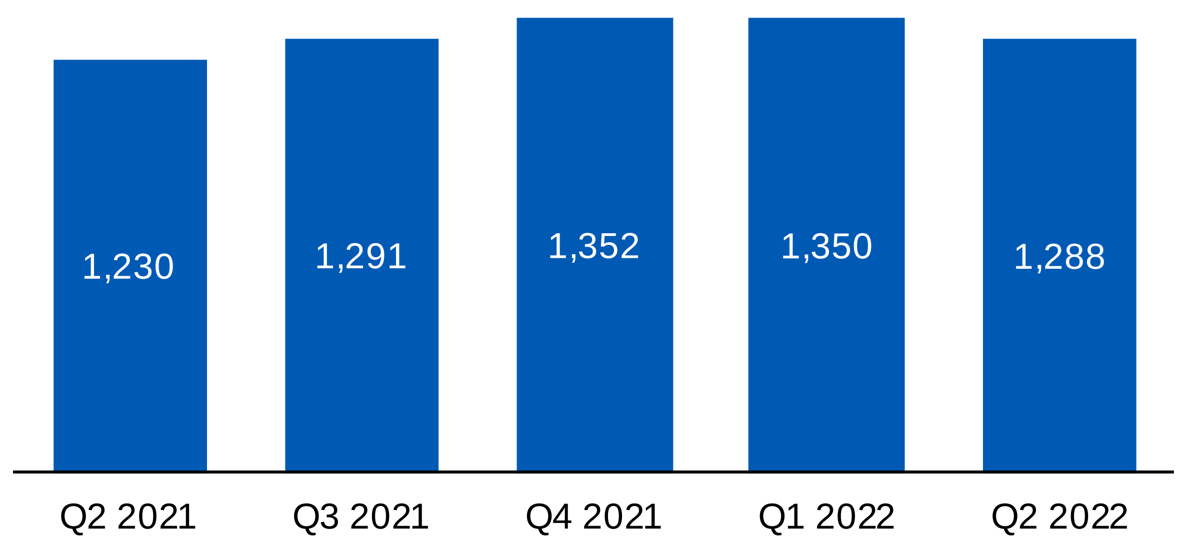
YoY growth in all fee generating businesses

- Strong income from lending and guarantees, partly due to performance based fees
- Robust result from capital markets transactions, with the Bank number one in bond trading and number two in equity trading in the Icelandic market
- Corporate finance with strong quarter, including listing of Nova and Alvotech
- Income from asset management increased slightly in Q2 2022 compared with Q2 2021. Strong net inflow in asset management but AuM impacted by market volatility Q2
- Sale of Valitor anticipated to support card fee income going forward

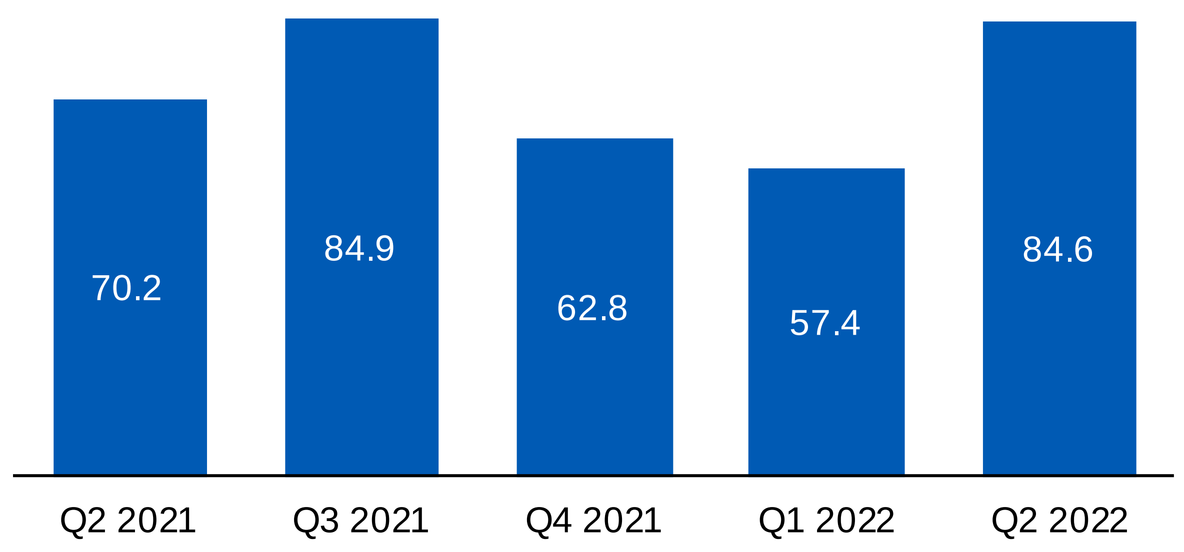
Net fee and commission income (ISK m)



Assets under management



Net fee and commission income and net insurance income / Operating expenses (%)

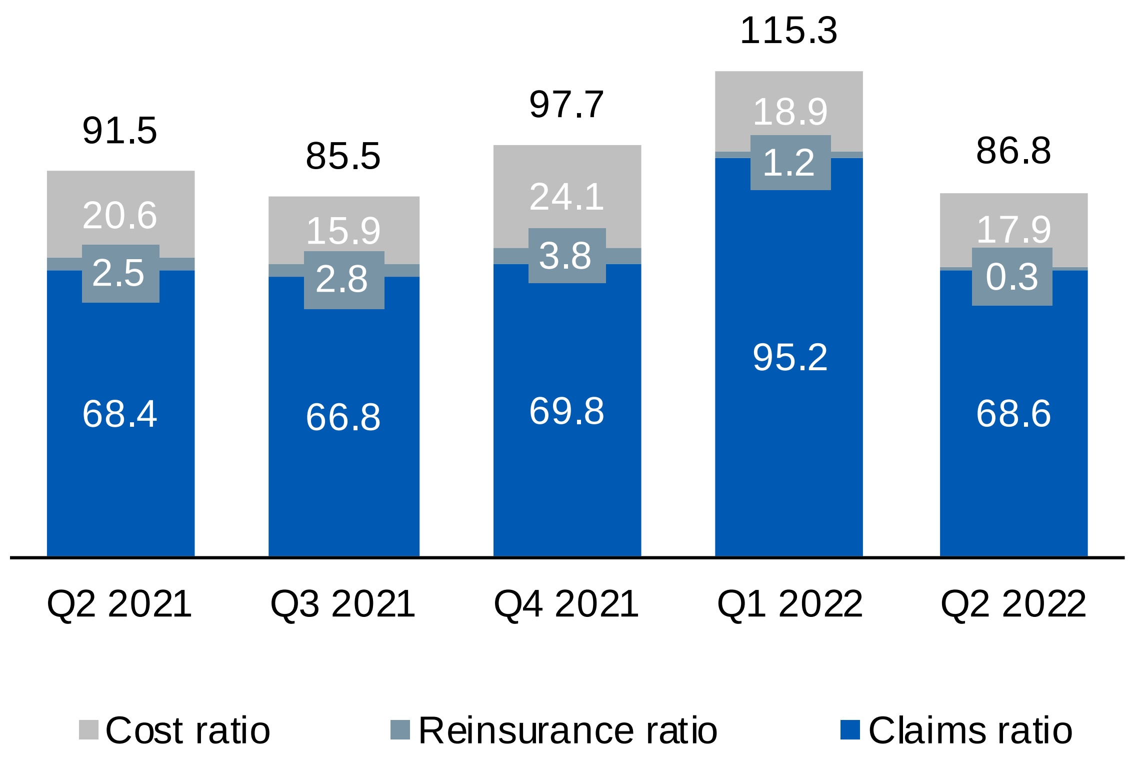


Net insurance income

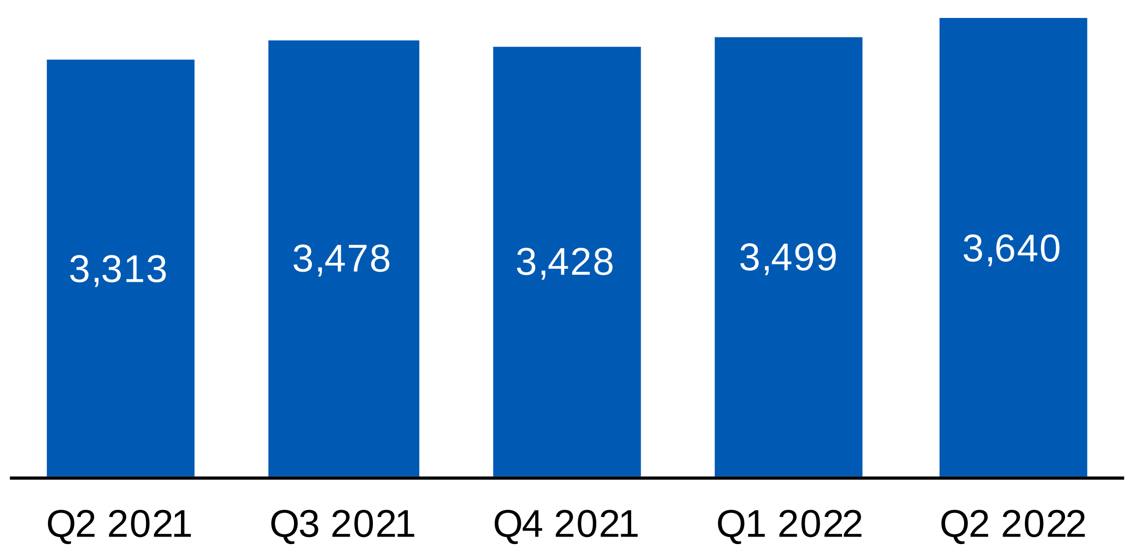
Strong improvement in the combined ratio from a difficult first quarter

- Combined ratio of 86.8% for the quarter and 101.1% in 6M 2022
- Earned premiums increased by 9.9% YoY and amounted to ISK 3,640m
- Strong growth in number of customers, especially corporates with 5.5% increase
- Net earnings for Vördur in the quarter was a loss of ISK 455m and a loss of ISK 535m for 6M 2022 driven by negative financial income
  - Investment income was ISK negative ISK 945m and negative ISK 517m in 6M 2022
- Arion Bank continues its integration with Vördur to create a combined product and service offering for customers

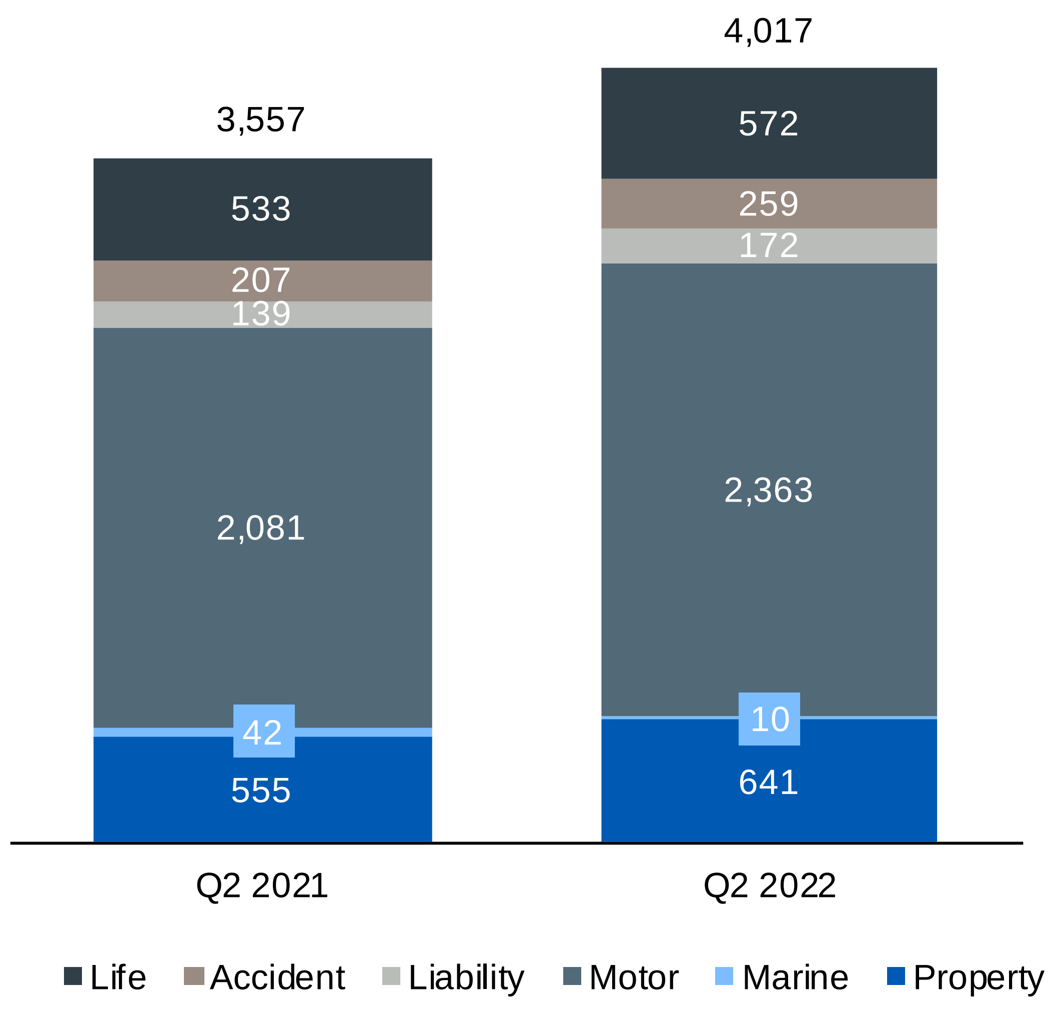
Combined ratio (%)



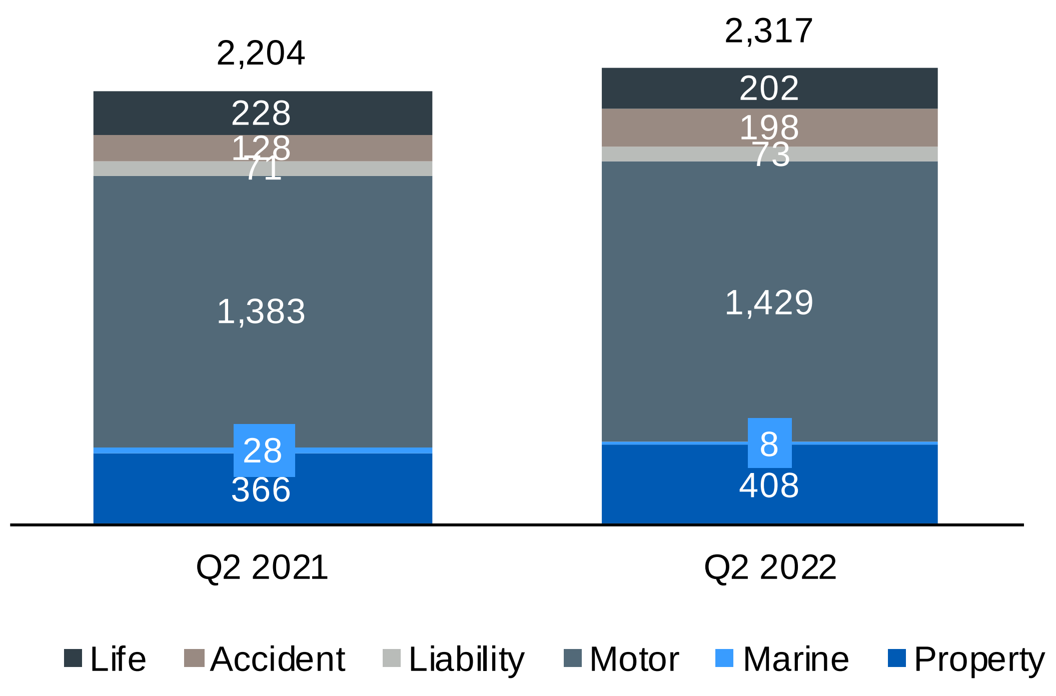
Earned premiums



Premiums written



Claims paid



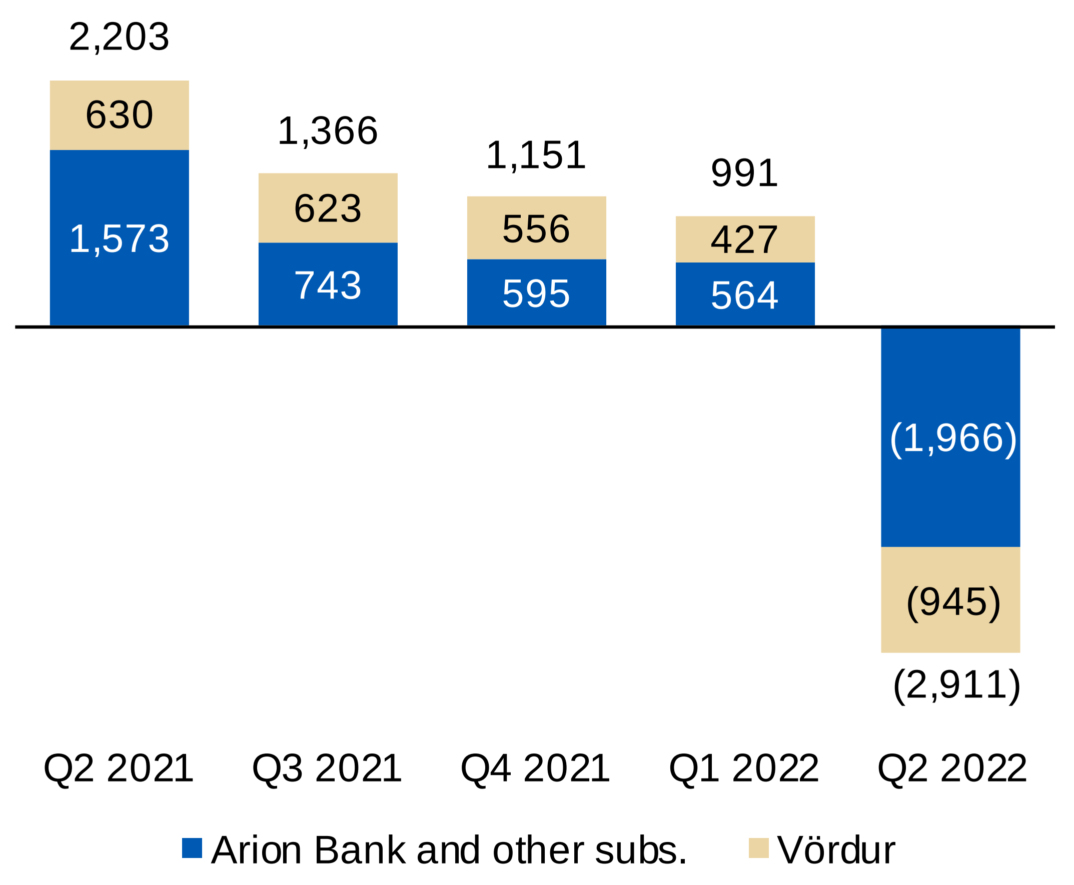
 All amounts in ISK m

Net financial income

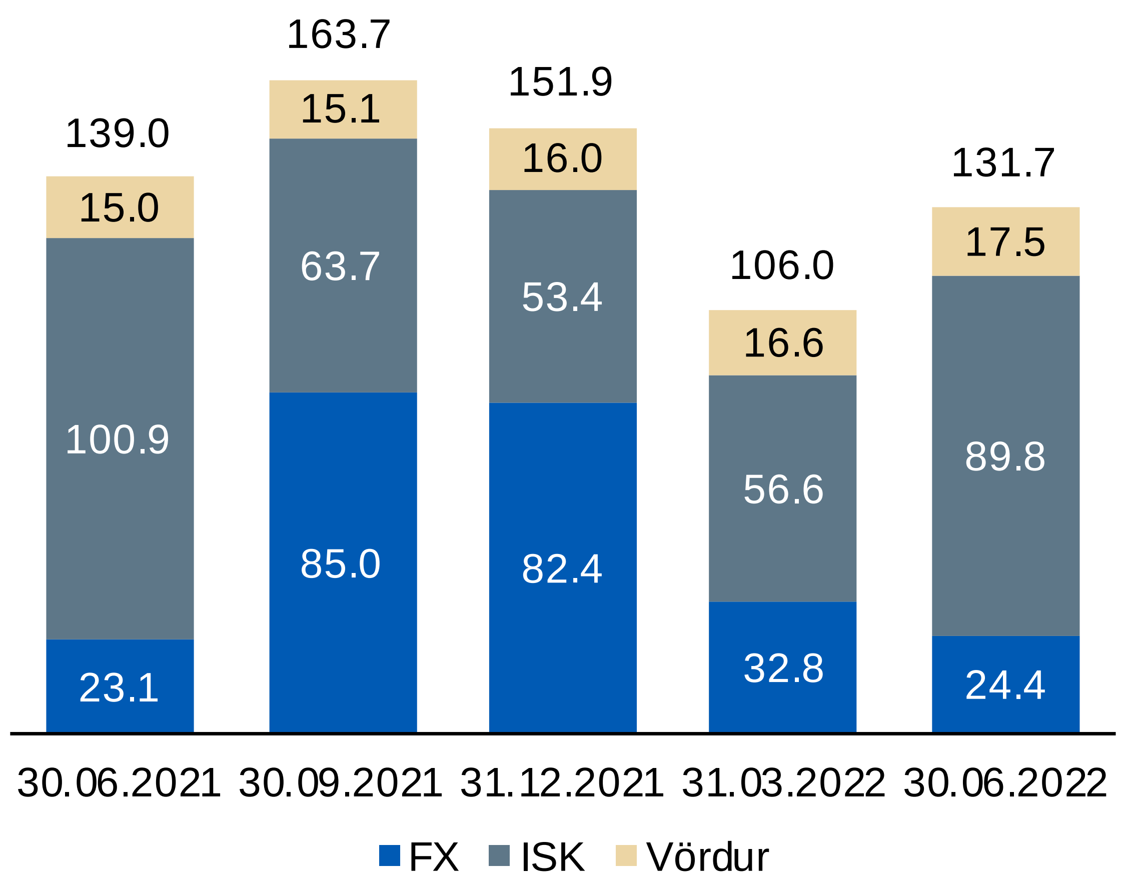
Challenging market conditions

- Negative net financial income in Q2 driven by loss in equity holdings at the Bank and at Vördur and one-off reclassification from OCI equity reserve of ISK 1.9bn[1]
- Equity holdings in market making business vary between quarters and are lowered by ISK 1.3bn from 31.03.2022
- Total investment portfolio of Vördur is ISK 25.2bn; ISK 17.5bn of bonds and ISK 7.7bn in equity instruments, yielding a total loss of ISK 945m in the quarter

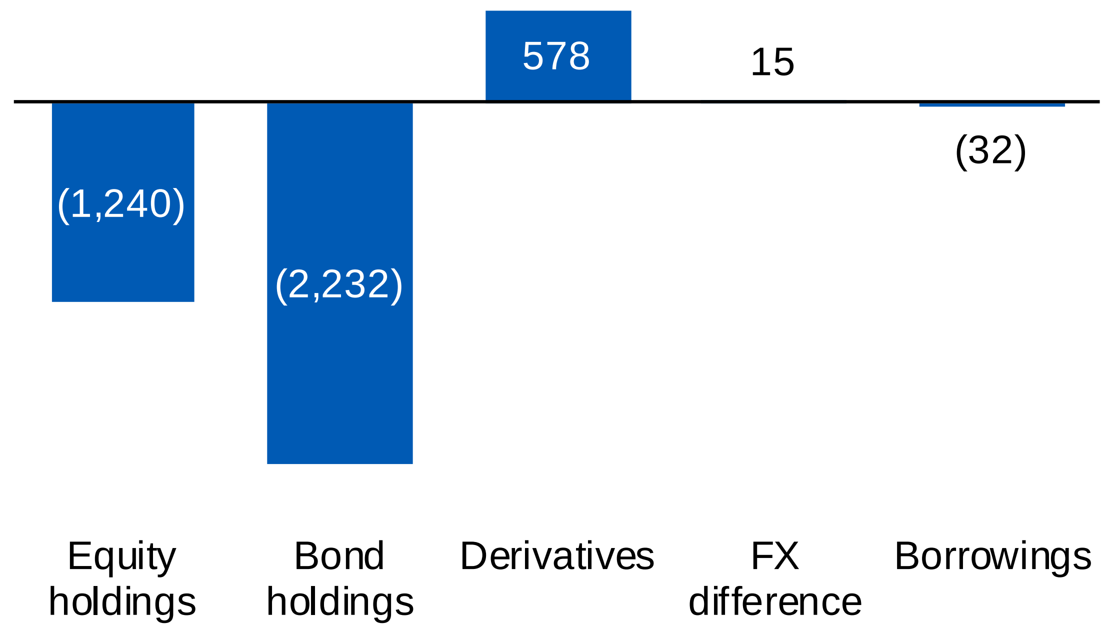
Net financial income (ISK m)



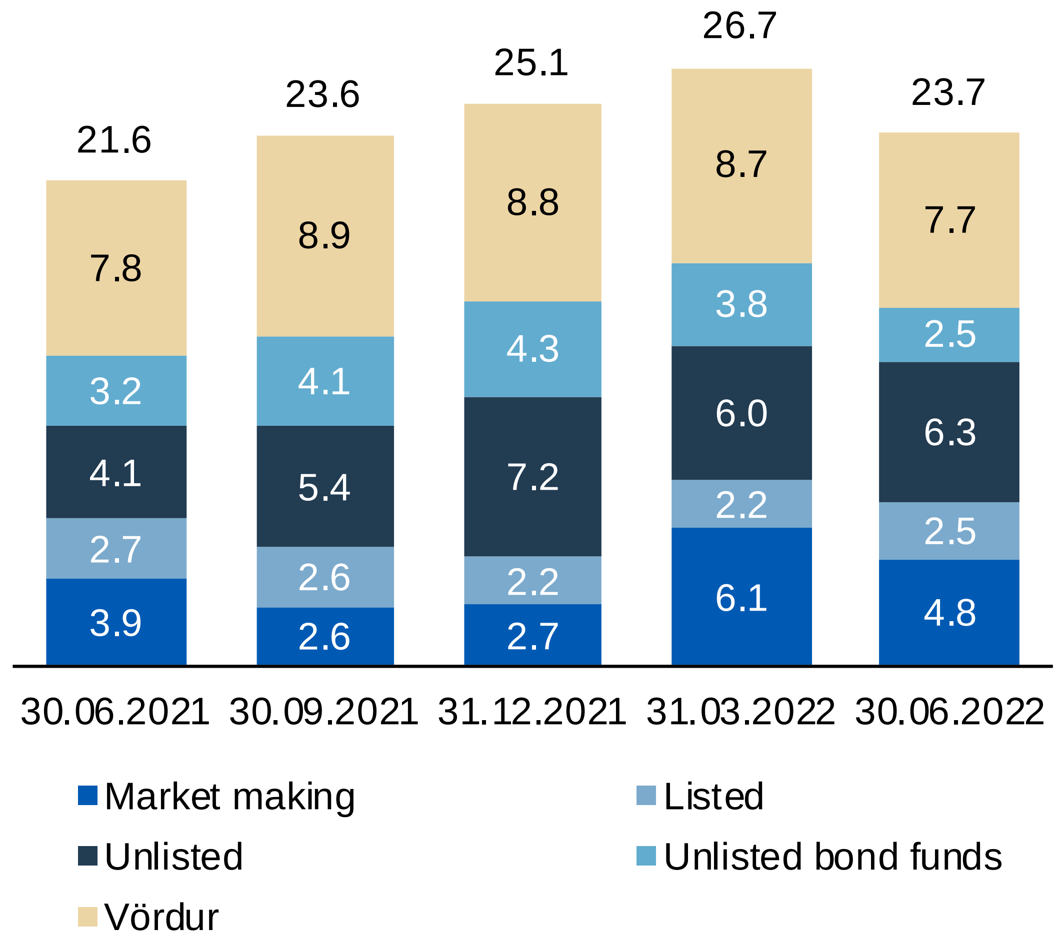
Bond holdings



Net financial income by type Q2 2022 (ISK m)



Equity holdings



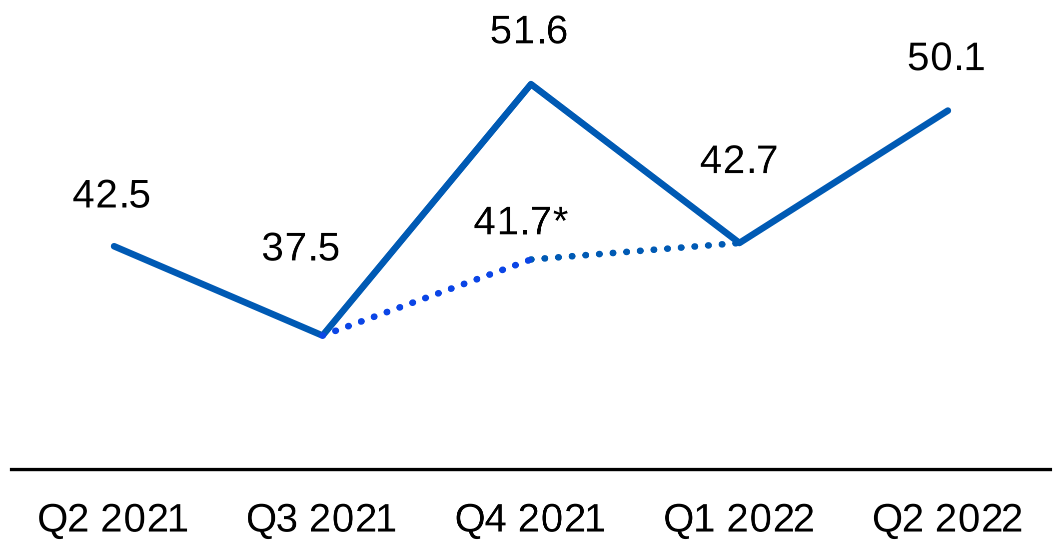
[1]See note 9 in Arion Bank's Condensed Consolidated Interim Financial Statements 30.06.2022

Total operating expense

Stable total OPEX despite high inflation

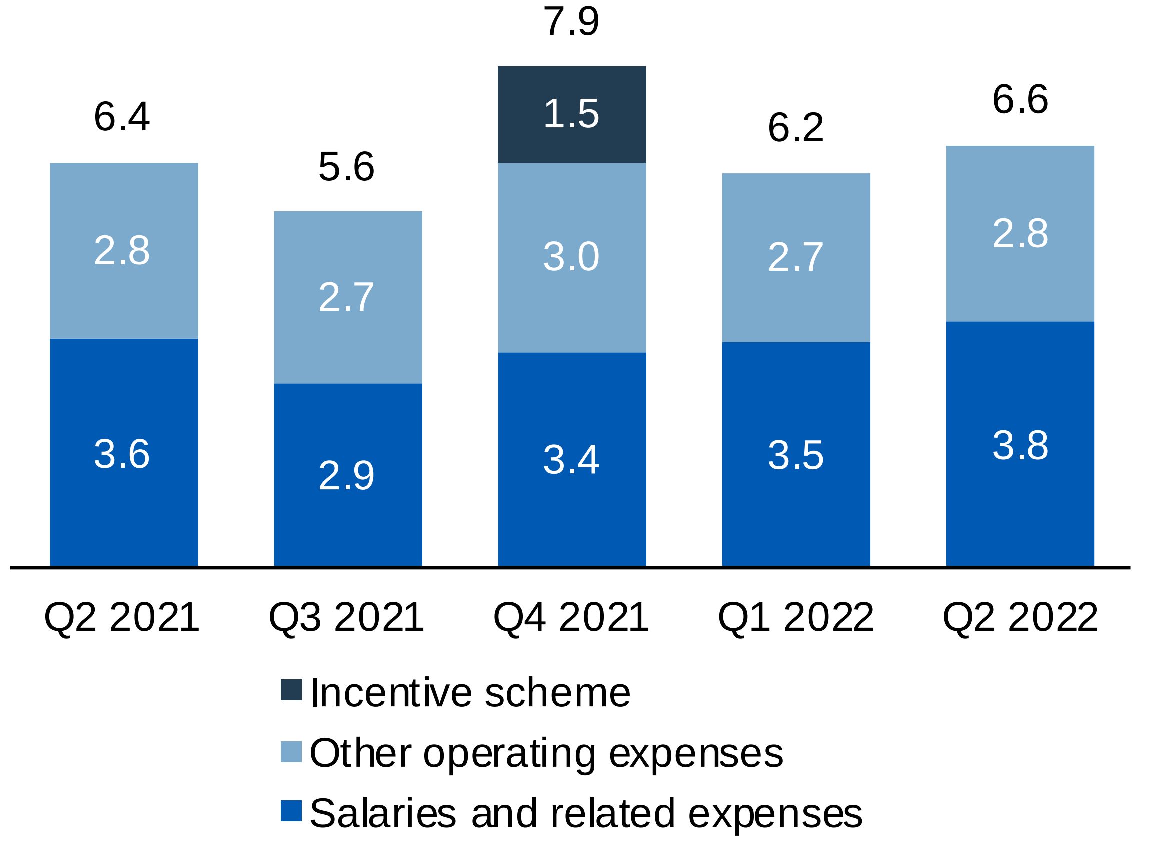
- Ongoing focus on opex and efficiency results in acceptable development
- Number of FTEs stable between quarters and YoY
- Salary expense in Q2 2022 increases, partly due to insourcing of IT operation
    - No accruals are recognized for incentive scheme during the quarter nor will be until Q4. Should all criterion be met at the end of the year the maximum total expense is estimated to be ISK 1.6bn including salary related expenses and would then be expensed in Q4
- Other OPEX stable YoY
    - IT expenses decreased partly due to more insourcing reflected in more FTEs and higher salary expenses in IT division
    - Due to amendments to the Act on the Depositors' Guarantee Fund no further charges from Q2 2022, approx. ISK 135m pr. Quarter
    - Marketing expense increases as new communication strategy is launched

Cost-to-income ratio (%)

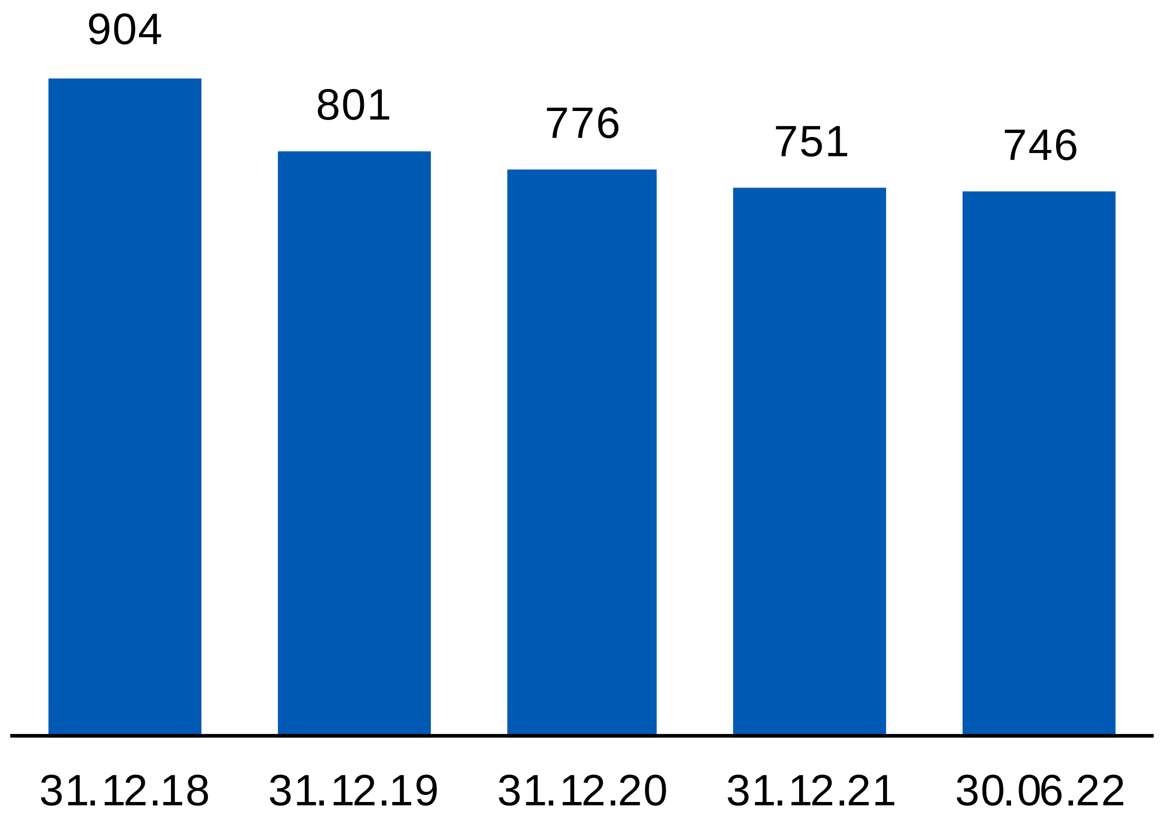


*Adjusted for incentive scheme expenses

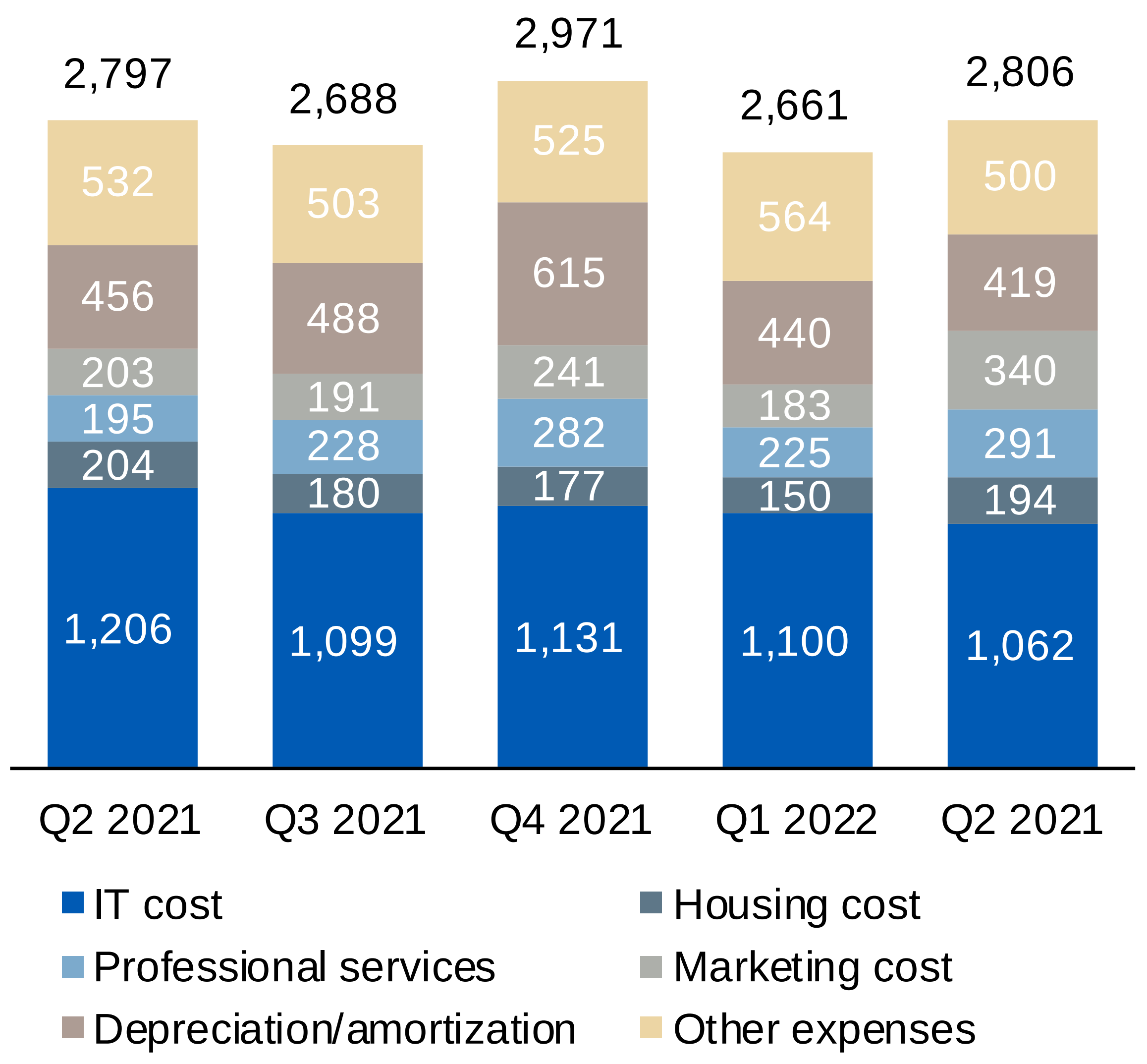
Total operating expenses



Number of employees



Other operating expenses (ISK m)



Balance sheet

Robust balance sheet further simplified with sale of HFS assets

- Loan growth supported by strong momentum in deposits
  - Loans to customers increased by 3.5% in Q2 and 7.9% from year end 2021
  - Deposits increased by 10.9% from YE 2021 and 20.3% from Q2 2021, partly due to the sale of Valitor from the Group
- Liquidity position remains strong despite ISK 26.7bn capital distribution through dividend and buy-back in Q1
  - Strong liquidity coverage ratio (LCR) of 163% (156% in ISK)
  - Net stable funding ratio (NSFR) of 115%
- Sale of Valitor reduces HFS assets to ISK 2bn, down from ISK 19bn at the end of the second quarter last year
- The Bank is very well positioned to meet the funding requirements of its customers in both ISK and FX and to distribute surplus capital
- Strong equity position and very high leverage ratio despite significant capital distribution

Assets	30.06.2022	31.03.2022	Diff.	31.12.2021	Diff.	30.06.2021	Diff.
Cash & balances with CB	78	64	21%	69	13%	70	12%
Loans to credit institutions	40	36	12%	30	33%	36	13%
Loans to customers	1,011	976	4%	936	8%	844	20%
Financial assets	204	186	10%	226	(10%)	214	(5%)
Assets and disposal groups held for sale	2	15	(86%)	16	(87%)	19	(89%)
Other assets	49	64	(24%)	37	33%	35	37%
Total Assets	**1,383**	**1,341**	3%	**1,314**	5%	**1,218**	14%
Liabilities and Equity							
Due to credit institutions & CB	5	4	8%	5	(8%)	8	(41%)
Deposits from customers	727	680	7%	655	11%	604	20%
Liabilities associated with disposal groups held for sale	-	15	-	17	(100%)	19	(100%)
Other liabilities	72	65	10%	50	43%	57	25%
Borrowings	363	370	(2%)	357	2%	301	21%
Subordinated liabilities	33	34	(1%)	35	(5%)	35	(3%)
Total Liabilities	**1,200**	**1,168**	3%	**1,119**	7%	**1,024**	17%
Equity	183	173	6%	195	(6%)	194	(5%)
Total Liabilities and Equity	**1,383**	**1,341**	3%	**1,314**	5%	**1,218**	14%

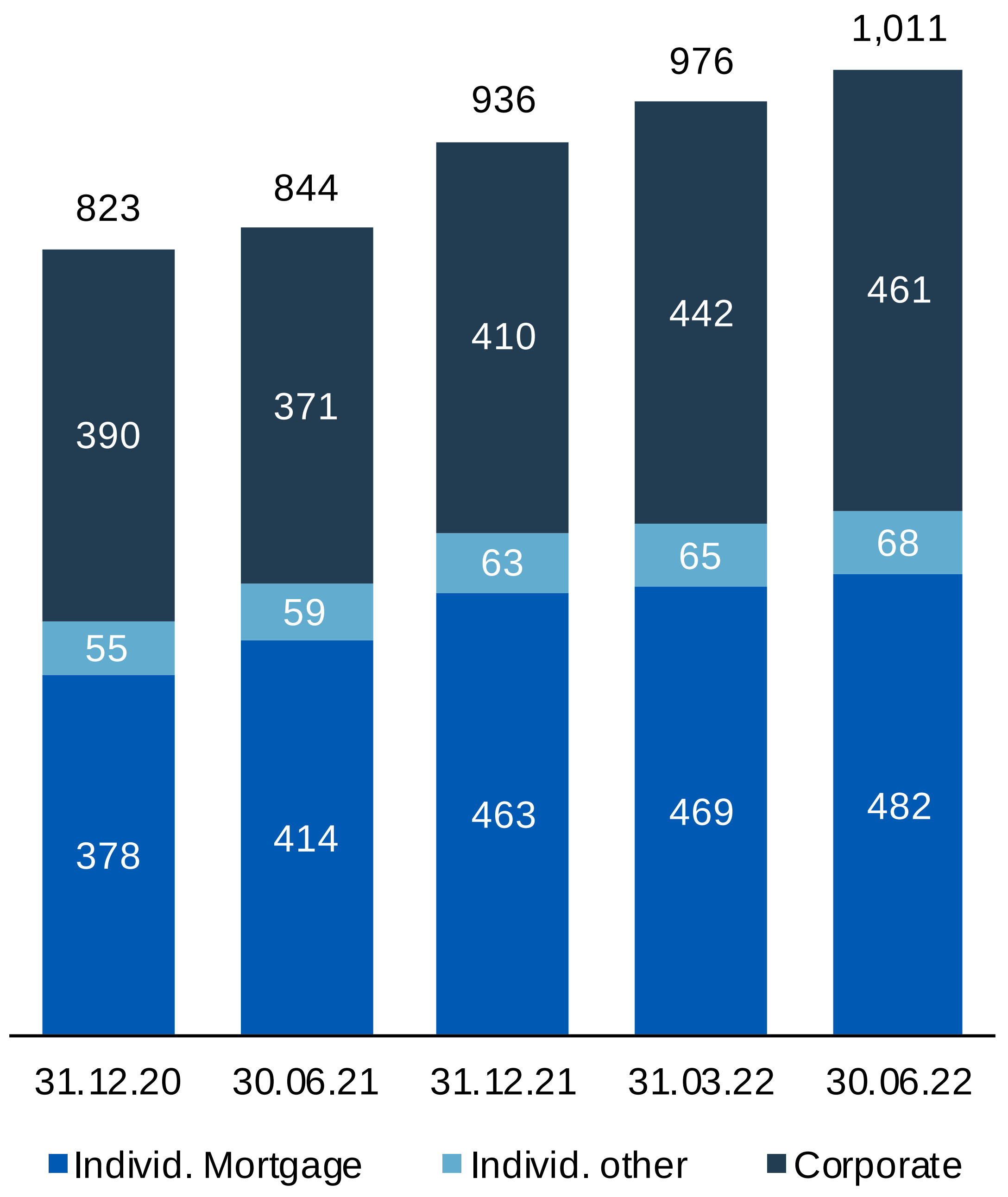
 All amounts in ISK bn

Loans to customers

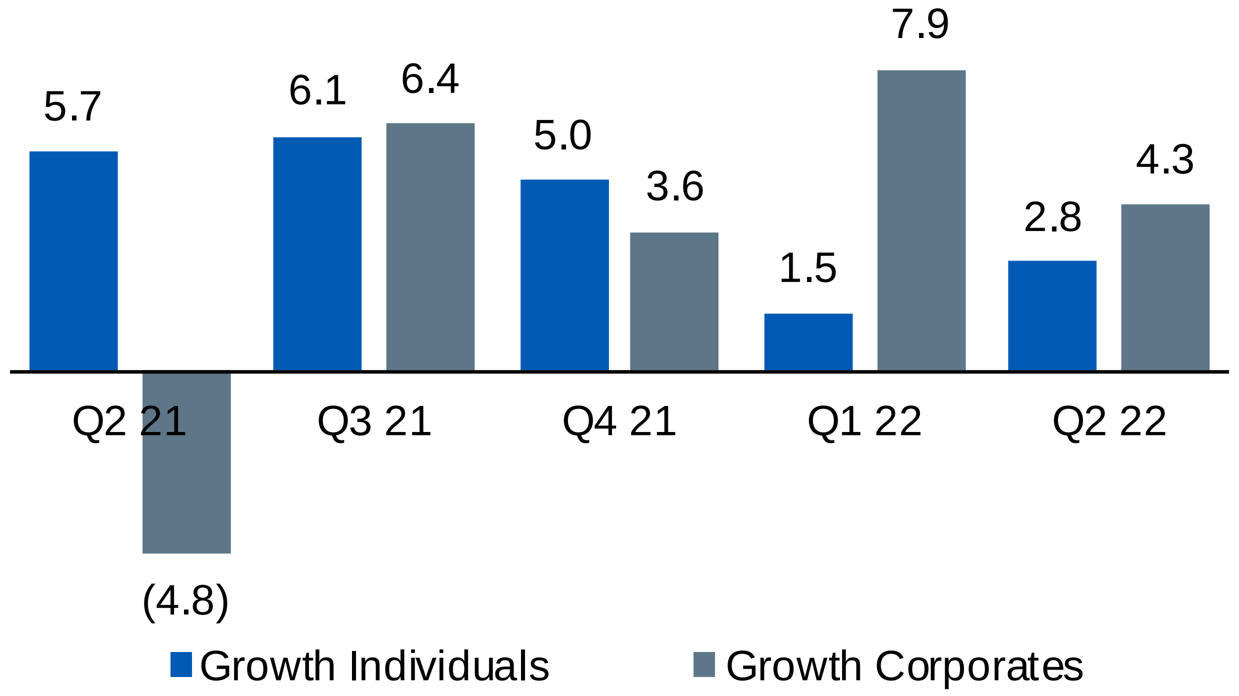
Balanced growth between corporates and individuals during the quarter

- Loans to customers increased by 3.5% during the quarter, loans to corporates 4.3% and loans to individuals 2.8%
- Strong pipeline combined with a robust capital and liquidity position allows for optionality for balance sheet management going forward
  - Near term growth and capital allocation to be managed carefully with a view of the external environment
- Continued CIB strategy of capital velocity
  - The Bank has sold corporate loans for ISK 14bn to institutional investors in 2022
- The diversification of the corporate loan book continues to be good and in line with the Bank’s credit strategy
- The growth in international loan portfolio has been significant – 28% during the quarter and 72% YoY, total of ISK 44.7bn

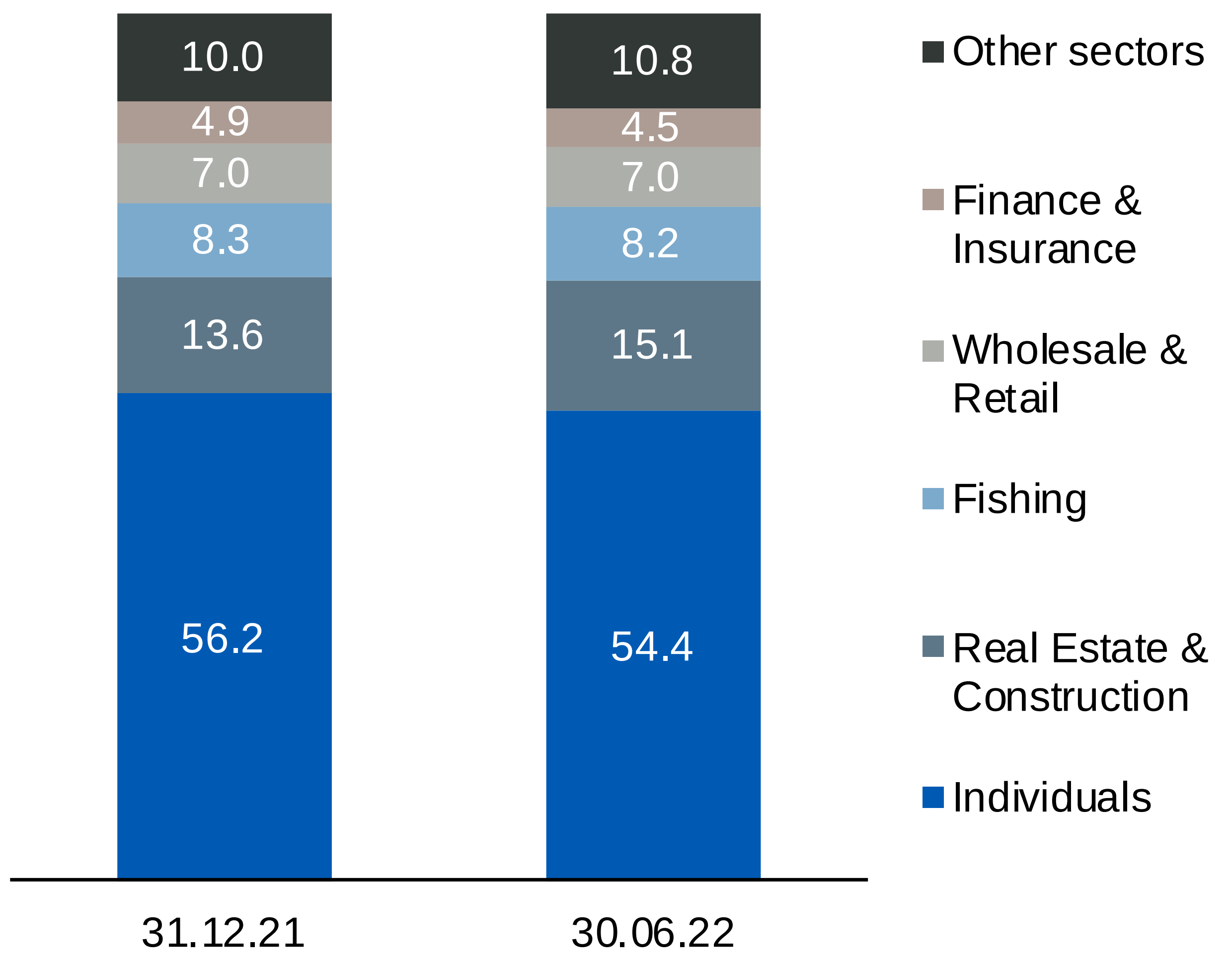
Loans to customers



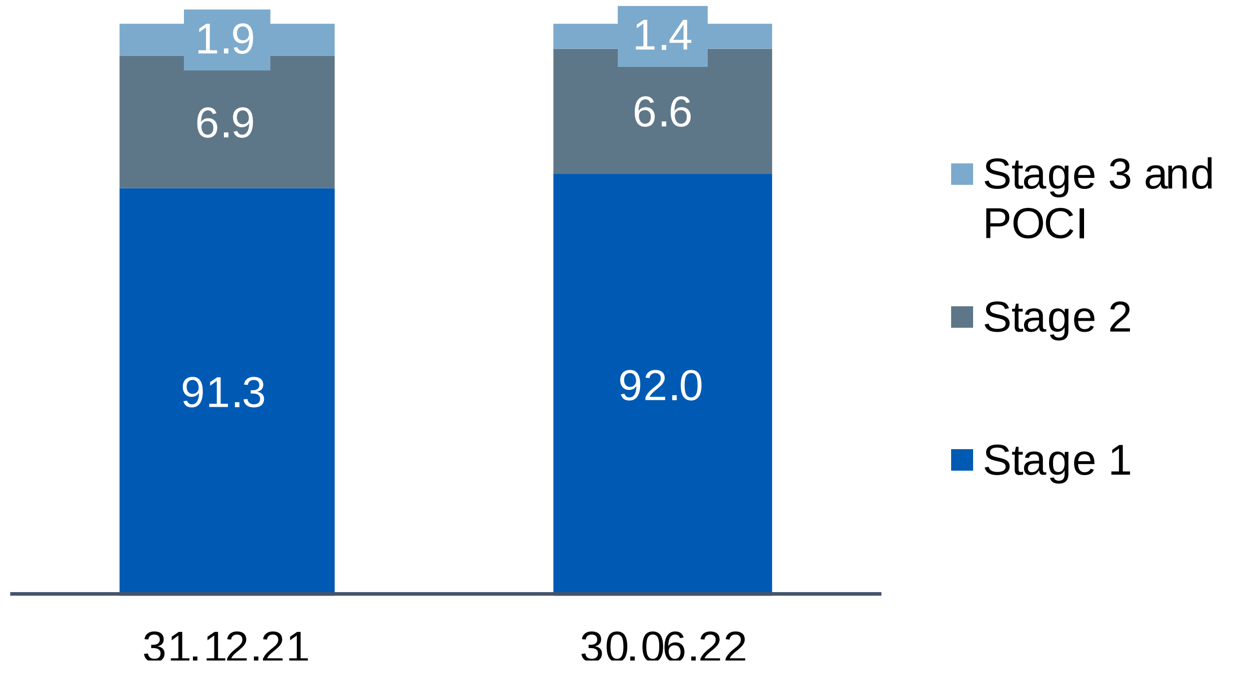
Growth in loans to customers (%)



Loans to customers by sector (%)



Loans to customers by stages (%)

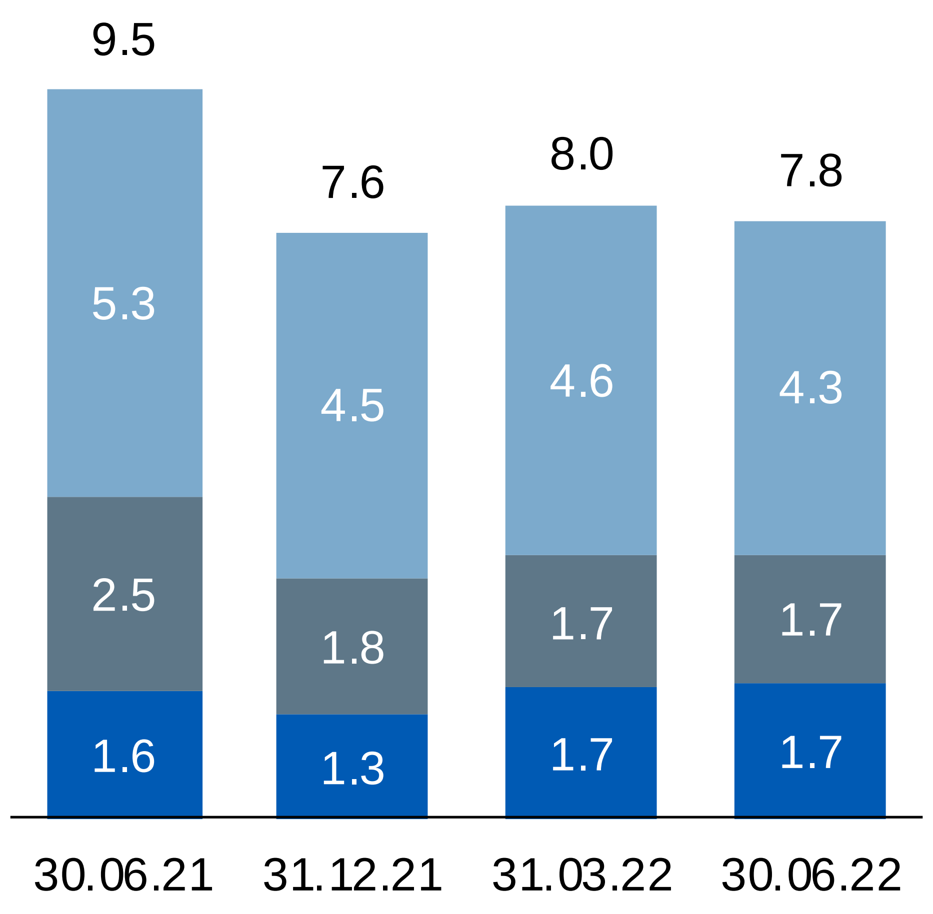


 All amounts in ISK bn

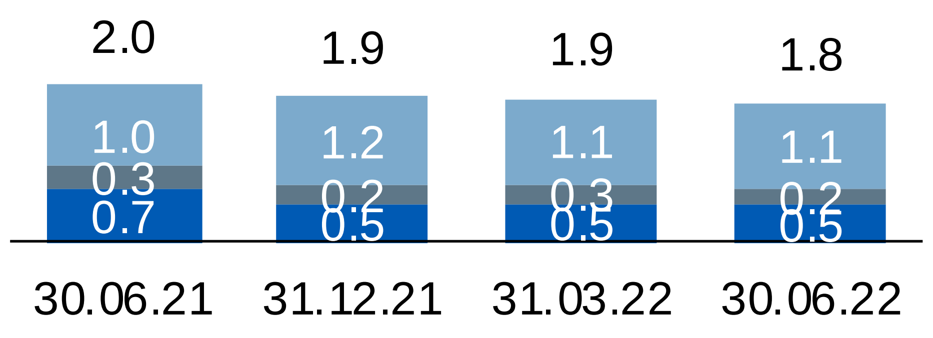
Loss allowance on loans to customers by IFRS 9 stages

Increase in H1 2022, mainly due to higher downside risk in IFRS scenarios and increase in corporate loans

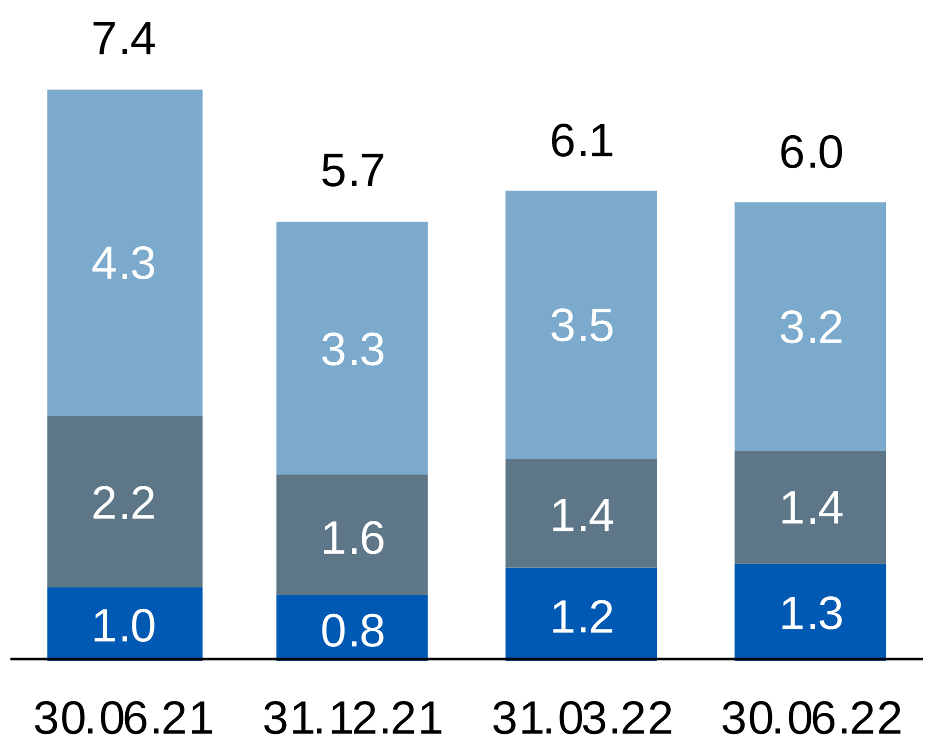
On loans to customers total



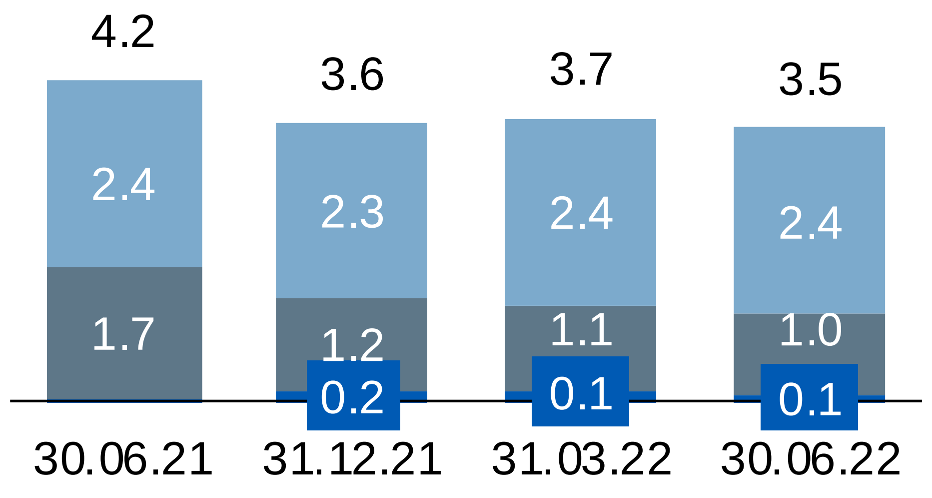
On individuals



On corporates



Thereof tourism exposure



■ Stage 1 ■ Stage 2 ■ Stage 3

- Total loss allowance as a percentage of face value of loans to customers was 0.7% at period end, compared to 0.8% year-end 2021 and 1.4% at year-end 2020
  - Reduction in loans in Stage 2 and 3 as a result of improved economic outlook following Covid-19, reduced moratoria, and problem loans which have been worked out
  - Coverage ratio for defaulted loans (Stage 3) was 30% at period end
- The war in Ukraine is not expected to have a significant effect on the Bank's financials. However, it is possible that secondary effects will impact the Icelandic economy and thus the Bank. This is accounted for in the loss allowance under IFRS 9 through adjustment of the probability weights of economic scenarios. Several corporate borrowers have been watchlisted in relation to the impact from the war without a determination of a significant increase in credit risk (Stage 2 trigger)

Scenario under IFRS9	YE 2021	Q2 2022
Optimistic	20%	10%
Base case	60%	65%
Pessimistic	20%	25%

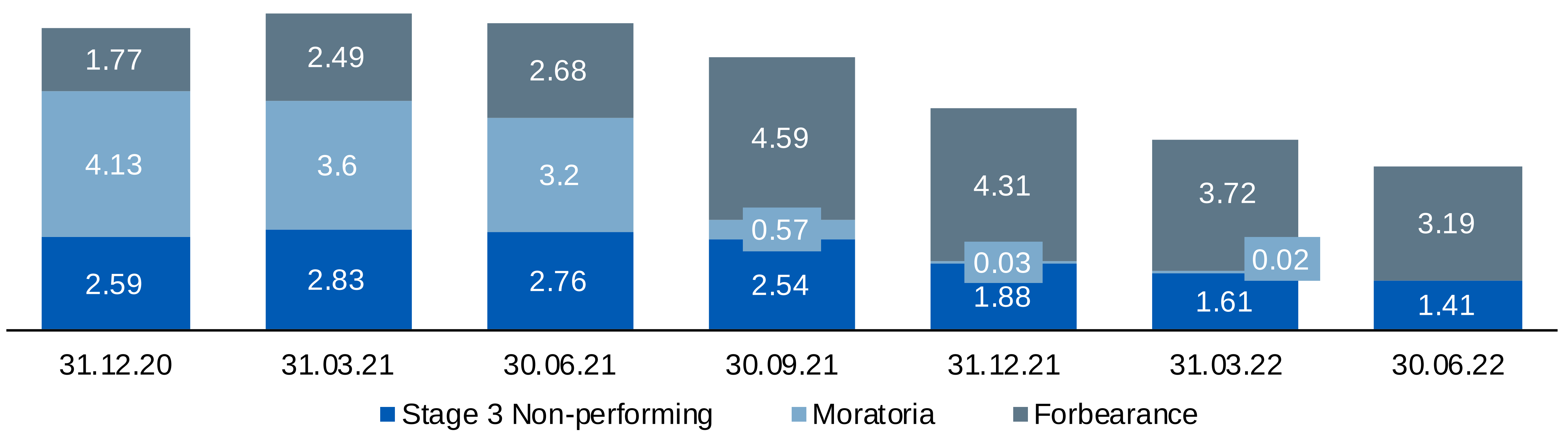
 All amounts in ISK bn

Risk profile

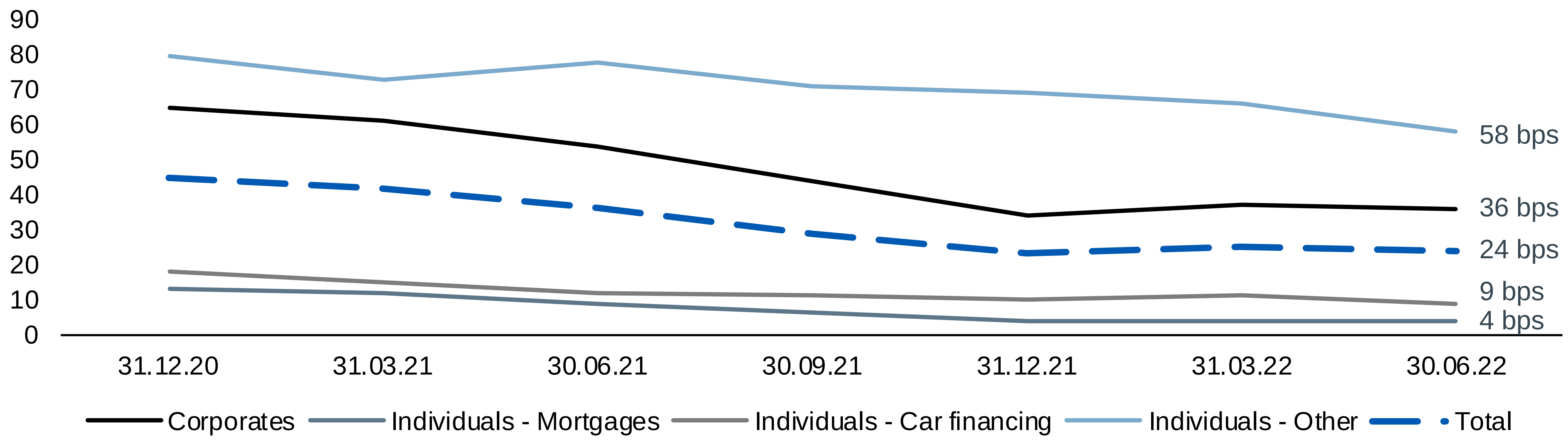
Increased portion of mortgages over the past couple of years reducing normalized Cost of Risk

- No material changes during Q2, with strong GDP, increase in asset value and low unemployment but higher interest rate level each other out
- In the medium term the expected credit loss ratios are likely to continue to approach their long-term average, around 3-4bps for mortgages to individuals and around 30-35bps for corporates.
- Total expected credit loss is therefore 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 was 24bps
- Loans with moratoria and forbearance measures which are not in stage 3 continue to decrease as the economy recovers from the effects of Covid-19. At the end of Q2 2022, they were 3.2% of the total loan book
- At period end about 48% of loans in default or subject to moratoria or forbearance are in the tourism sector

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



12-month expected credit loss for performing loans to customers



Residential mortgages

Comfortable position - proactive and dynamic management

Macroprudential measures:

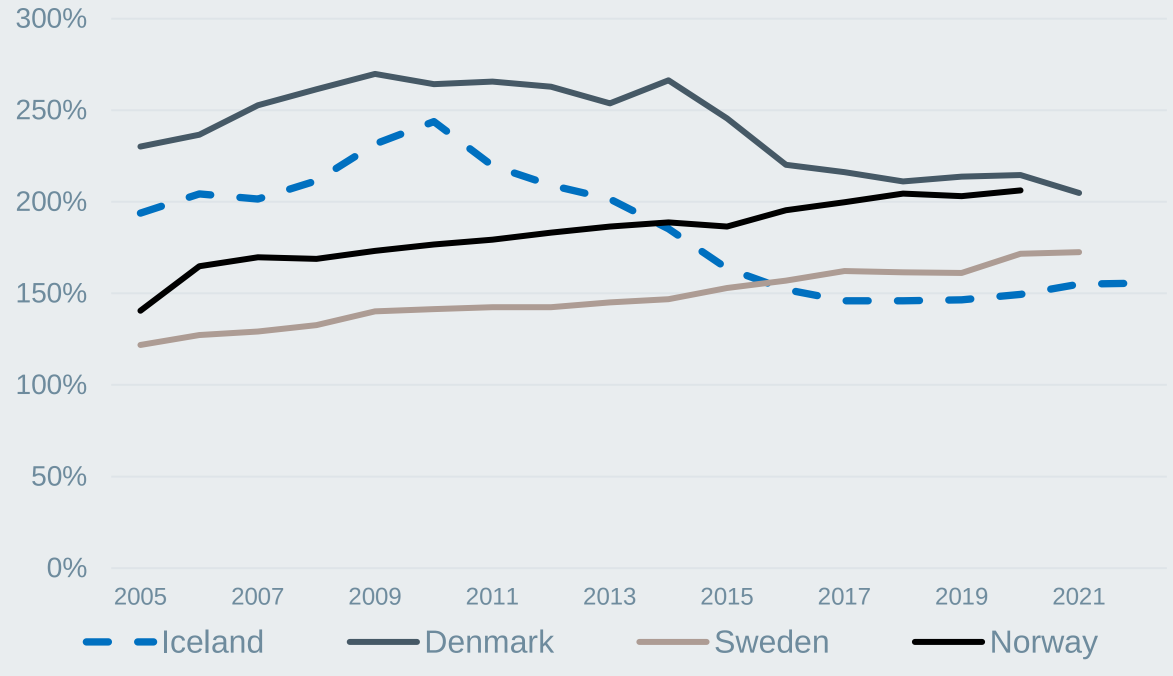
- Loan-to-value capped at 80% (85% for first-time buyers, lowered from 90% in June 2022)
- Debt service-to-income < 35% (40% for first-time buyers). In June 2022, the Central Bank introduced prescribed minimum interest rates for debt-service which primarily affects indexed loans.
- Affects mostly first time buyers and higher loan applications

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

- Energy prices in Iceland are stable as almost all houses are heated using local renewable energy.

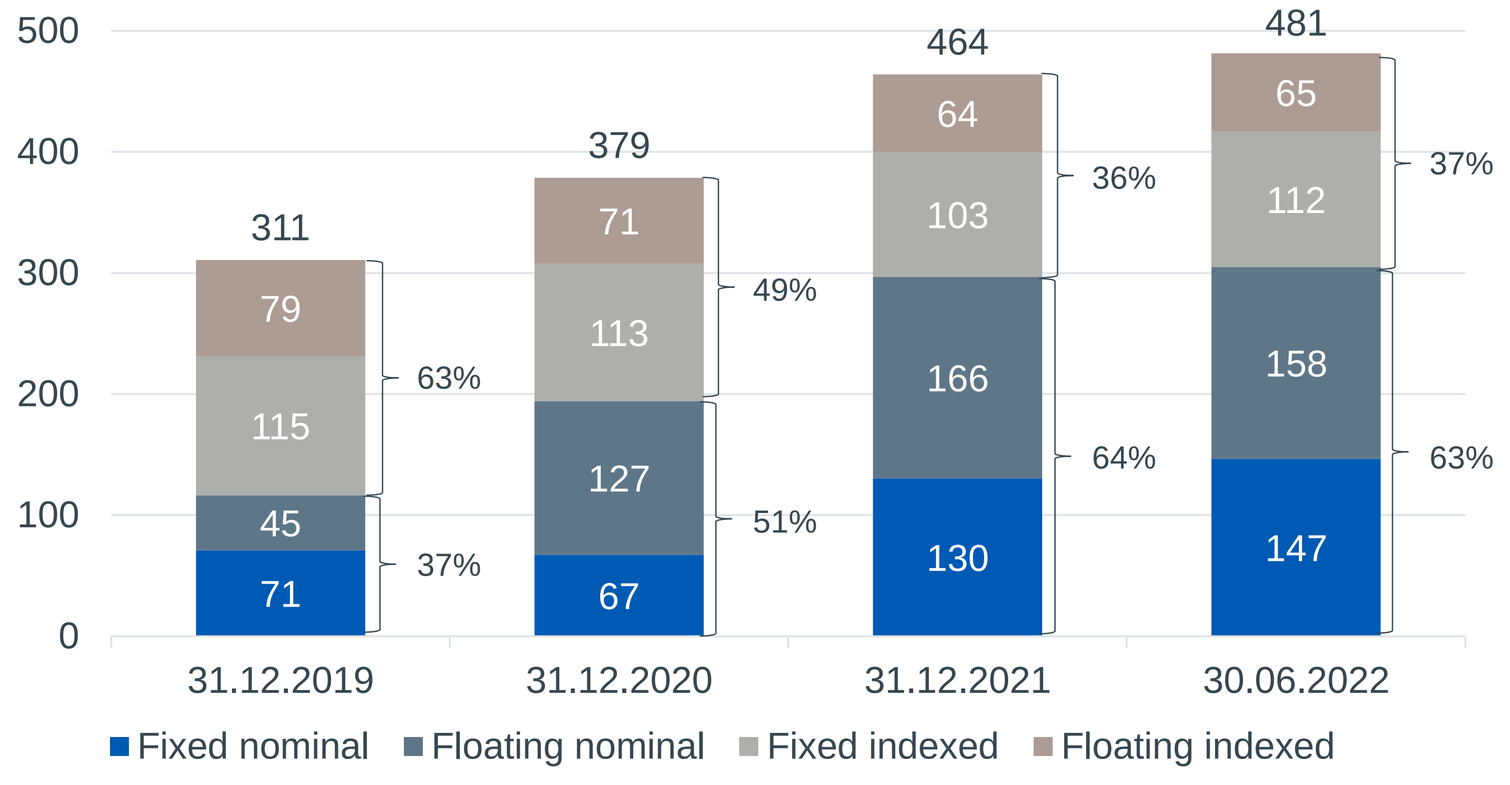
Total gross debt of Icelandic households 155% of disposable income[2]

Household debt to disposable income[2]



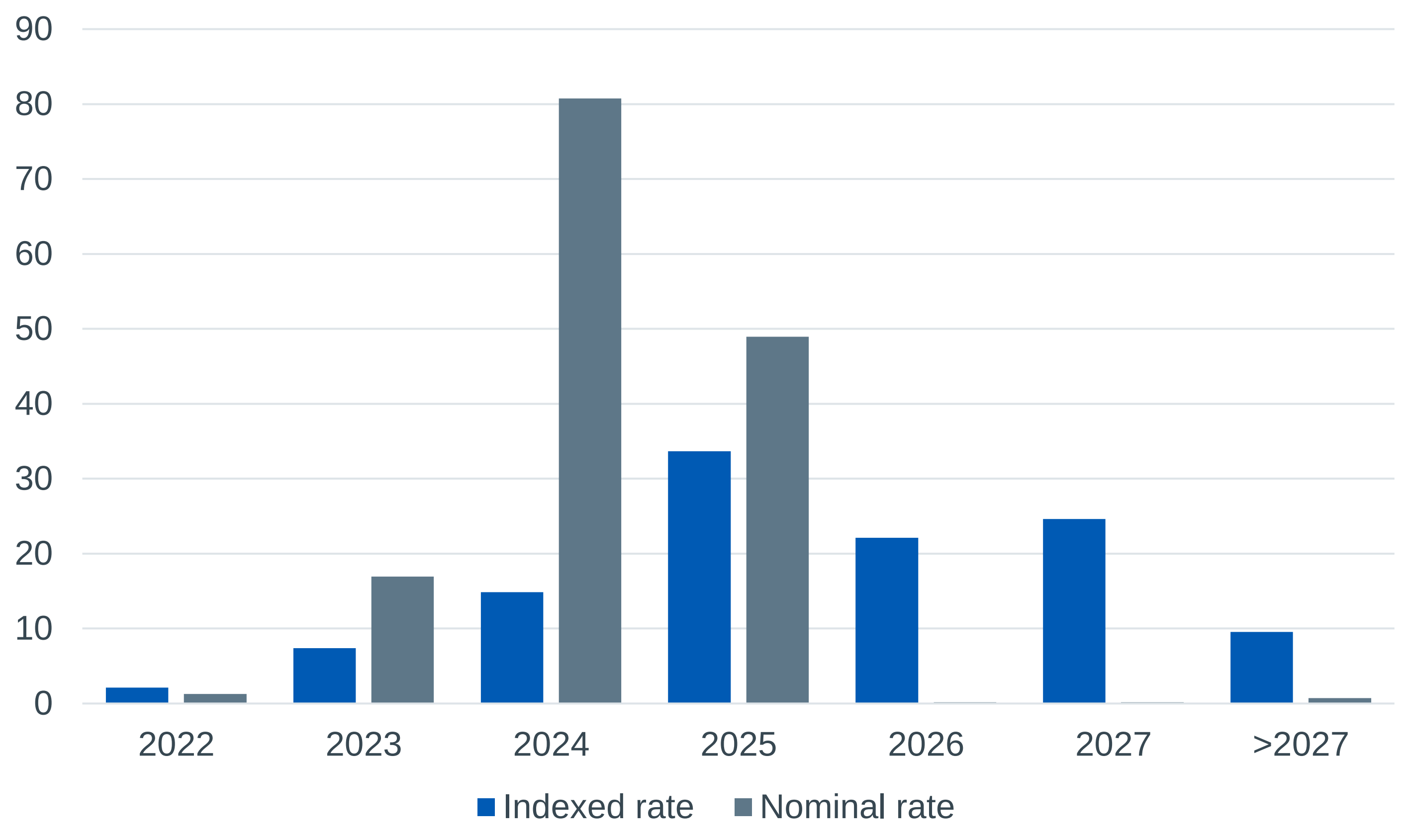
Residential mortgages by interest rate type (ISK bn)

The share of indexed vs. nominal rate mortgages has been reversed since YE 2019. Nominal rate loans are 63% of the mortgage portfolio at 30 June 2022



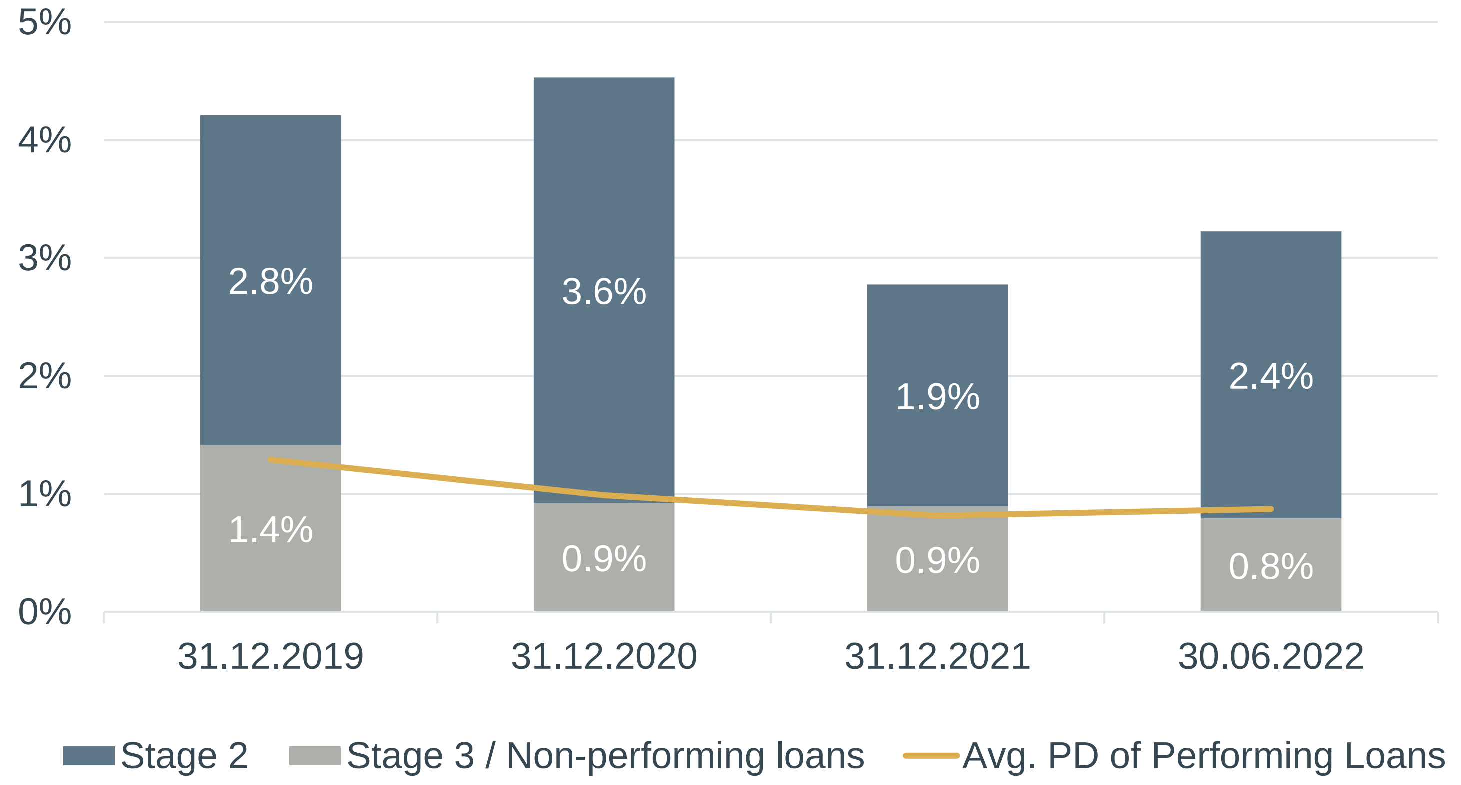
Interest rate reset profile for fixed rate mortgages (ISK bn)

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



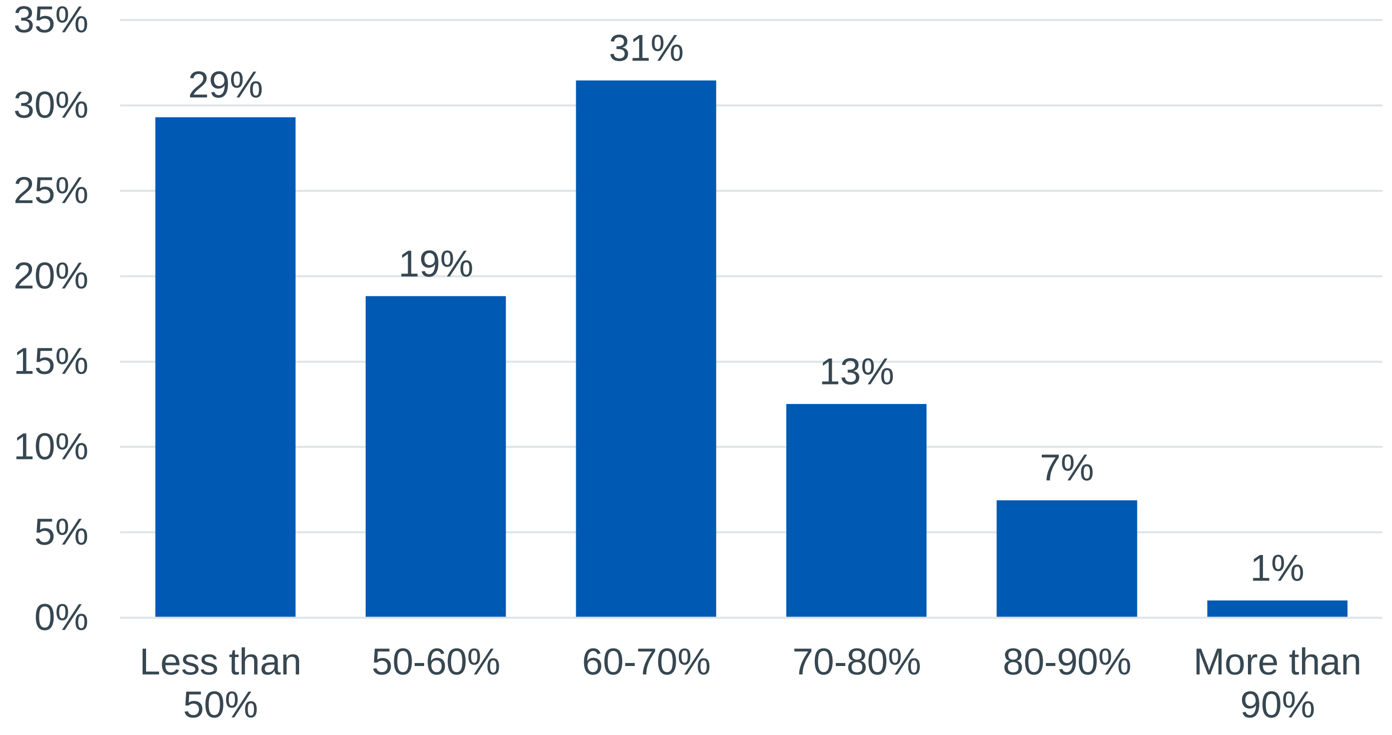
Stage allocation and probability of default

Non-performing loans are 0.8% of the loan book.



Loan to value distribution[1]

Loan-to-value below 80% accounts for 92% of the mortgage portfolio.



1. Total exposure of a loan is in one bracket
2. Central Bank of Iceland, Financial Stability Report

Real Estate and Construction sector

Exposures to real estate companies (excl. construction) 24% of corporate loan book. Internal risk limit at 25%.

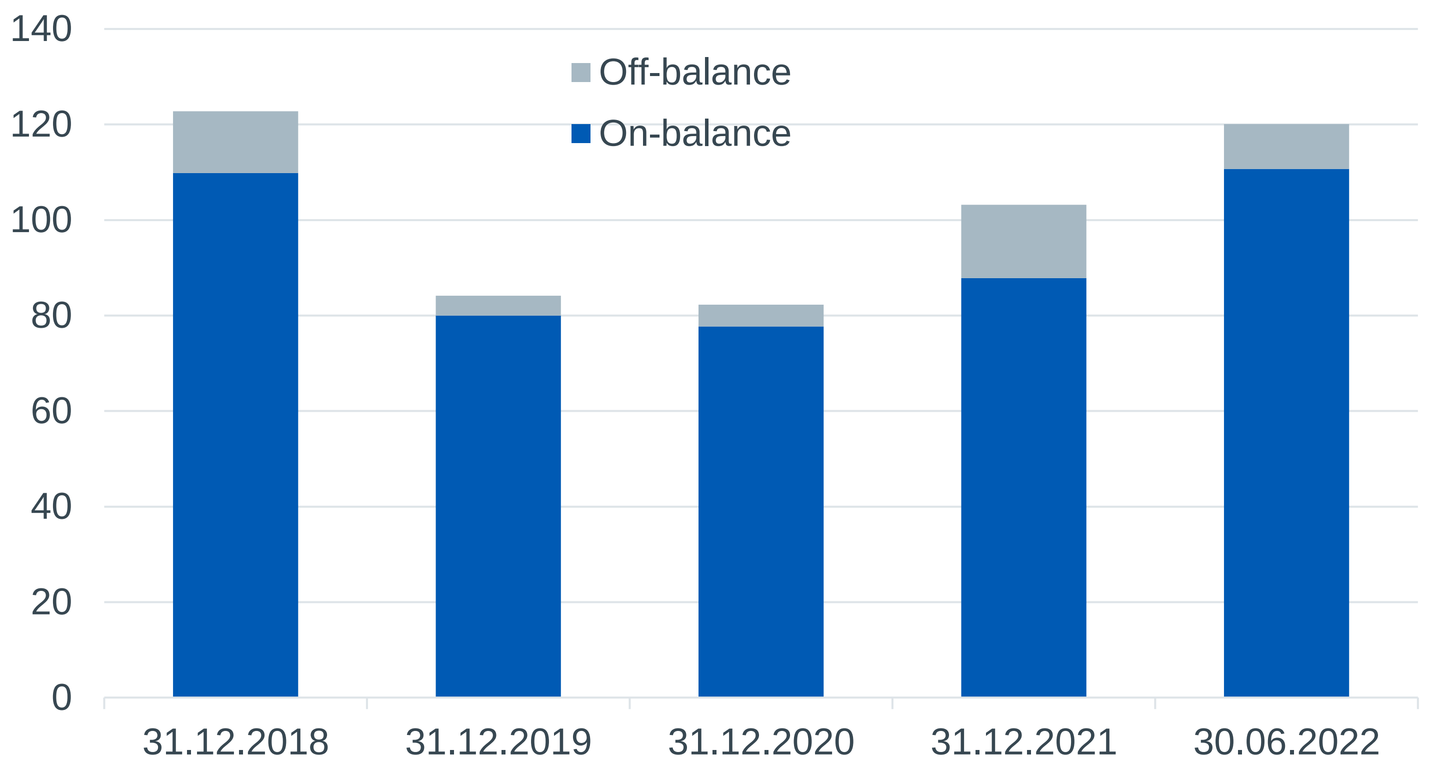
- Debt service being tested in the sector with rising interest rates. A slowdown or recession would lead to higher vacancies, hampering the ability to pass inflationary pressure to tenants.
- Disciplined origination with average LTV ratio at 66%. The Bank's debt service criteria has accounted for rising rates. Median range Net debt / EBITDA 7-11x for commercial real estate and 10-16x for residential real estate.
- Largest exposure in sector 5.1% of Tier 1 capital. Top 10 exposures 36% of total sector exposure.

The construction portfolio is in a renewal phase – moving from relatively large high-end projects to diversified residential property development. Construction phases are evenly spread out in time.

- The demand for housing expected to remain high due to population increase and net migration.
- Residential property development roughly 80% of the construction portfolio. The Blikastaðir development project expected to commence in 2023.
- Rising cost of production. Financial covenants include cost-overrun headroom to counter the current market risk.

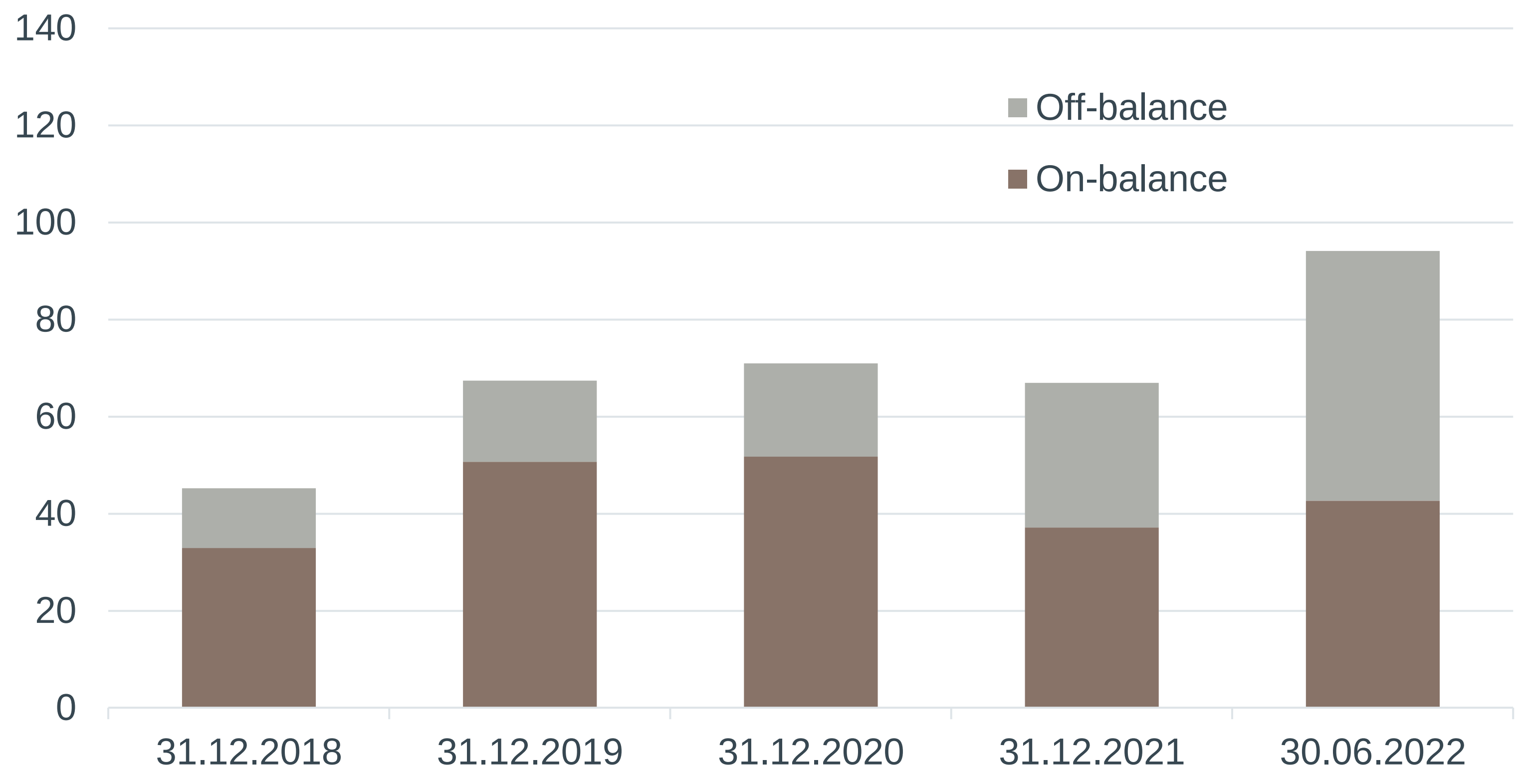
Development of exposures to real estate activities (ISK bn)

Average LTV 66% for exposures to real estate companies



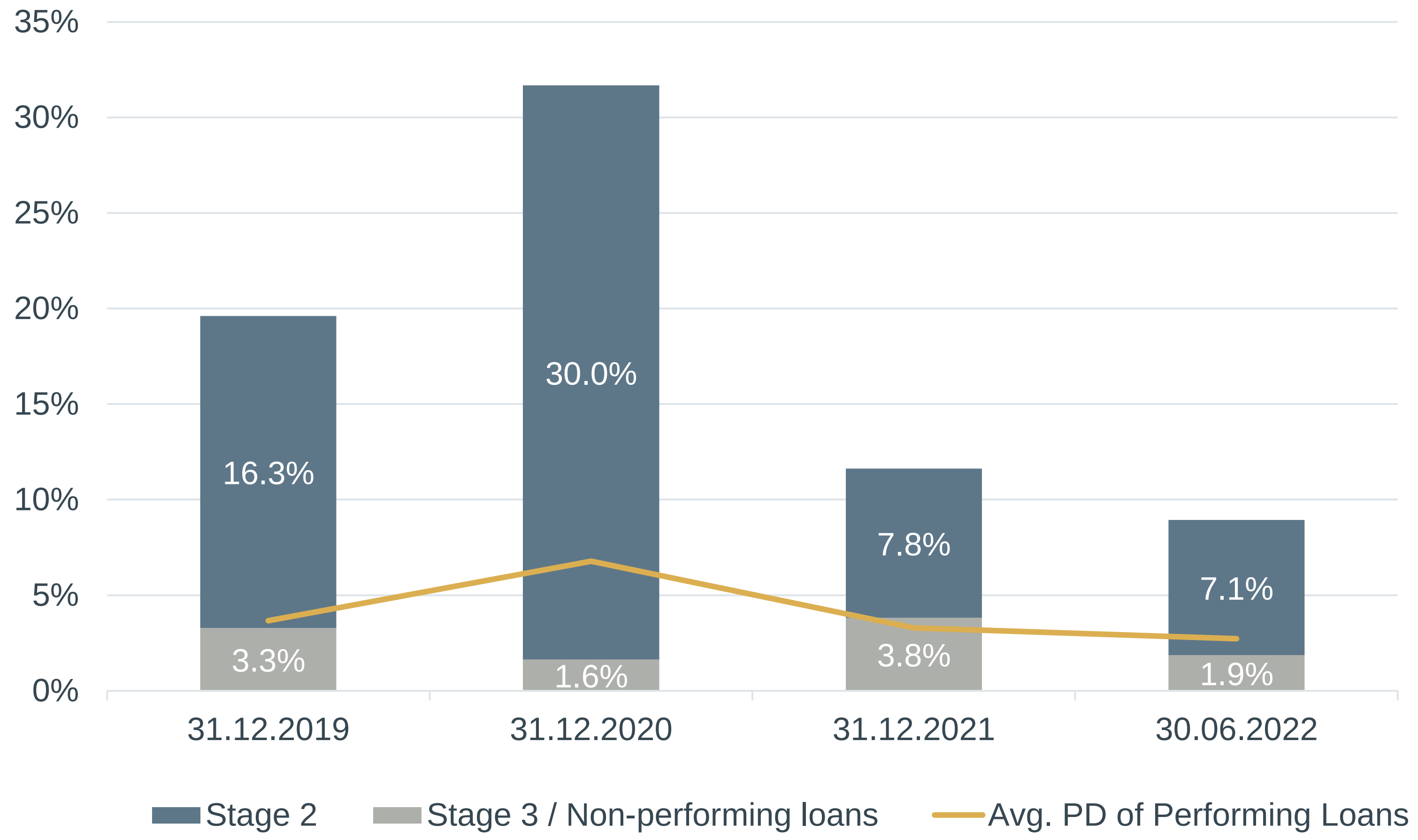
Development of construction exposures (ISK bn)

Focus on increasing exposure to diverse housing development projects. Internal risk limits allow for considerable growth.



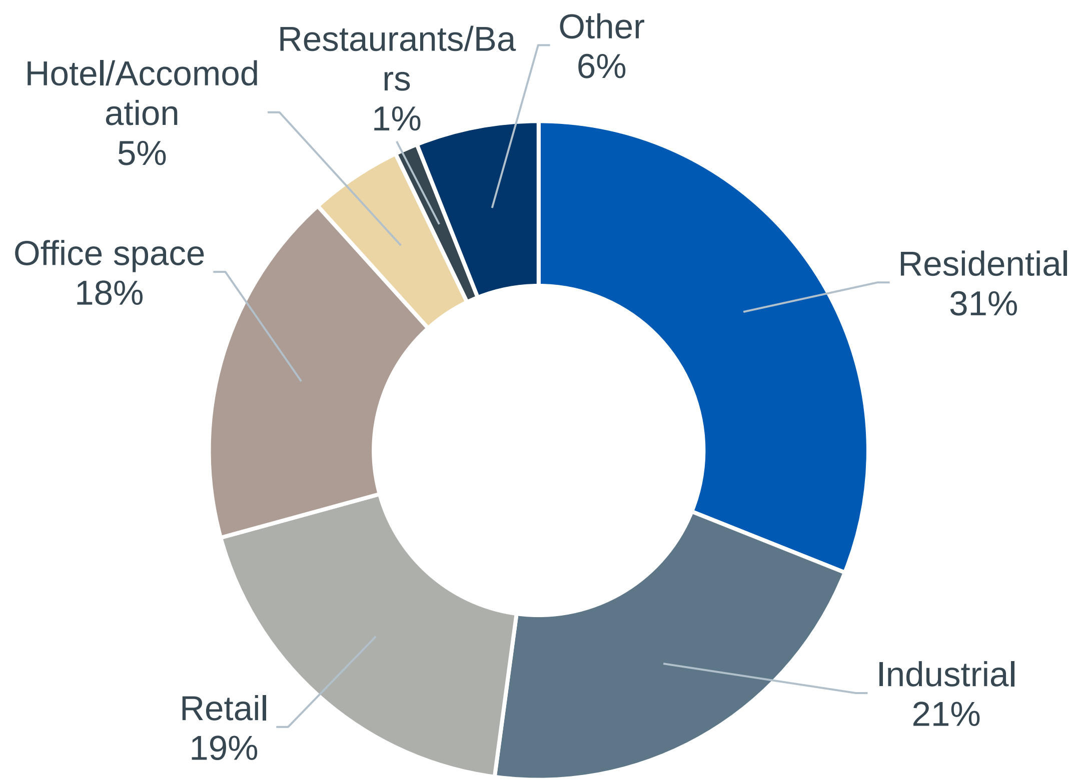
Real estate activities: stage allocation and probability of default

Reduction in Stage 2 loans following Covid-19. Returns under pressure due to inflation. Considerable downside risk in a recession.



Real estate collateral by type[1]

Well diversified collateral in terms of real estate type



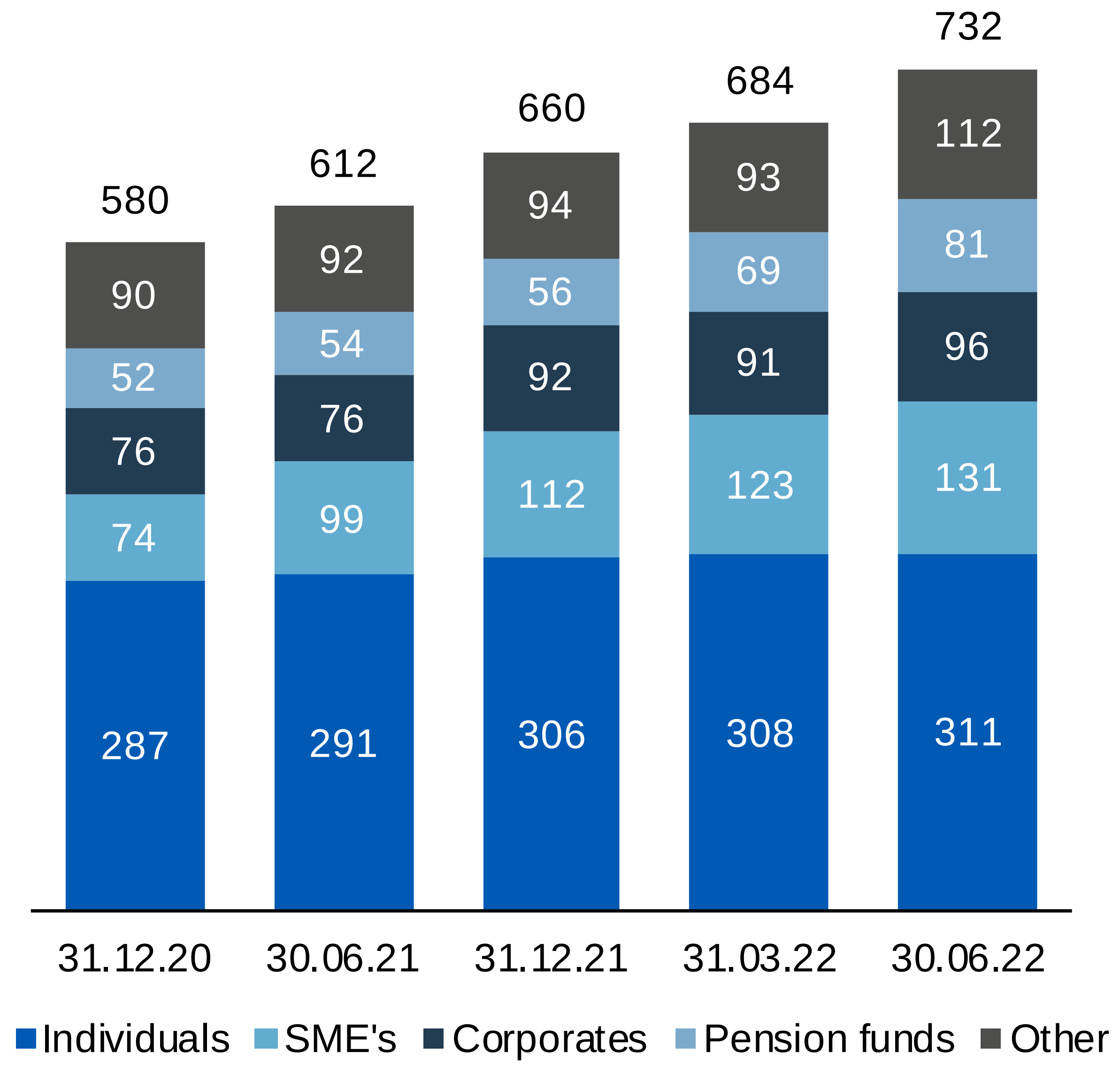
1. For real estate sector only.

Deposits

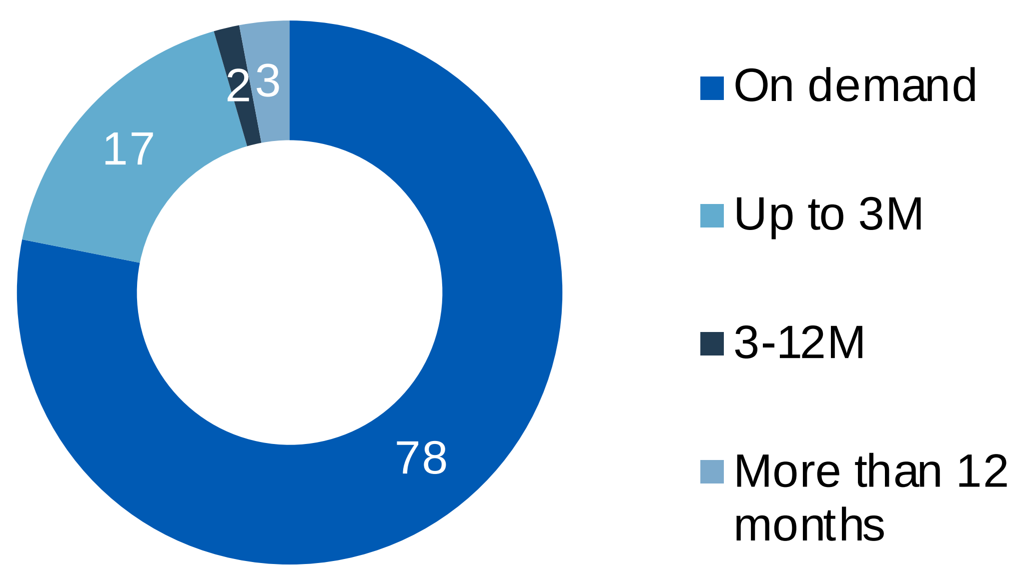
Growth backed by continued focus on competitive position with core clients

- Deposits represent 61% of the Bank's total liabilities, was 59% at year-end 2021.
- Growth of 5.6% in core deposits from YE 2021 and 15.7% YoY
  - Core deposits are from individuals, SME's and corporates
- Loans to deposits ratio has decreased significantly over the last few years with stronger deposit base
- Green deposits continue to grow at a strong pace and are up 169% from YE 2021 (ISK 22.0bn at 30.06.2022)

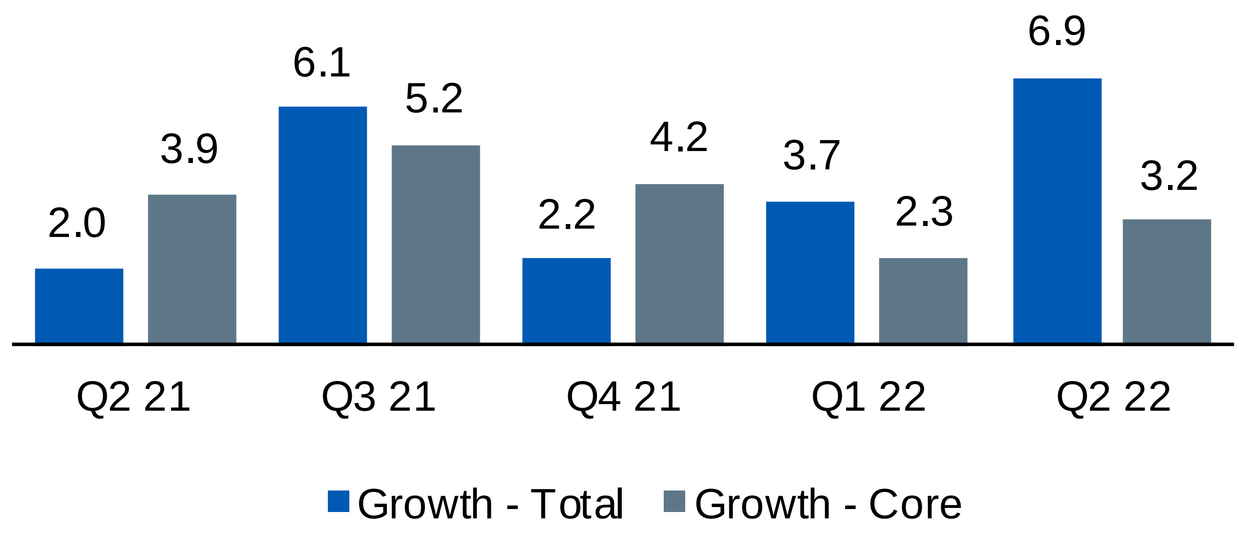
Deposits*



Maturity of deposits (%)

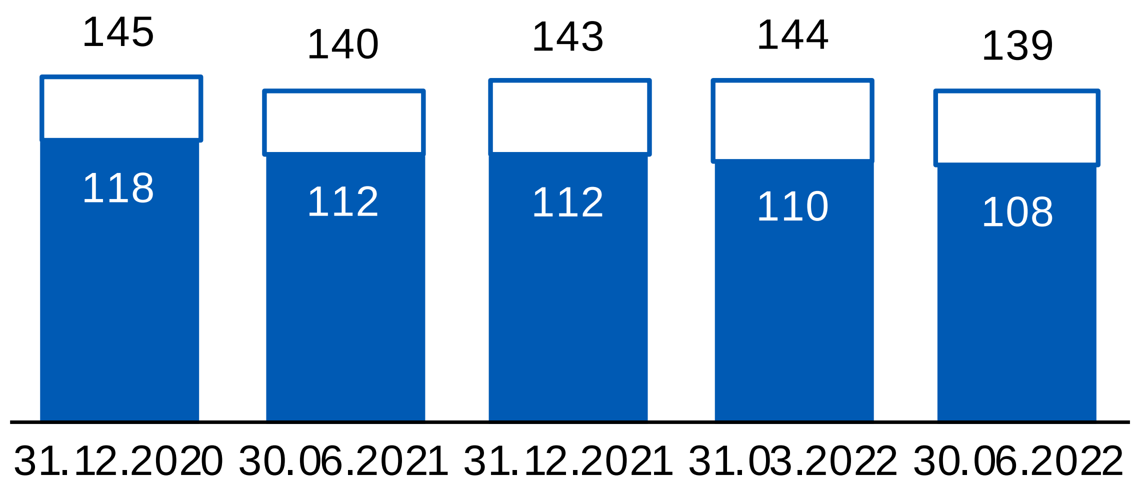


Growth in deposits (%)



Loans to deposits ratio (%)

(Without loans financed by covered bonds)



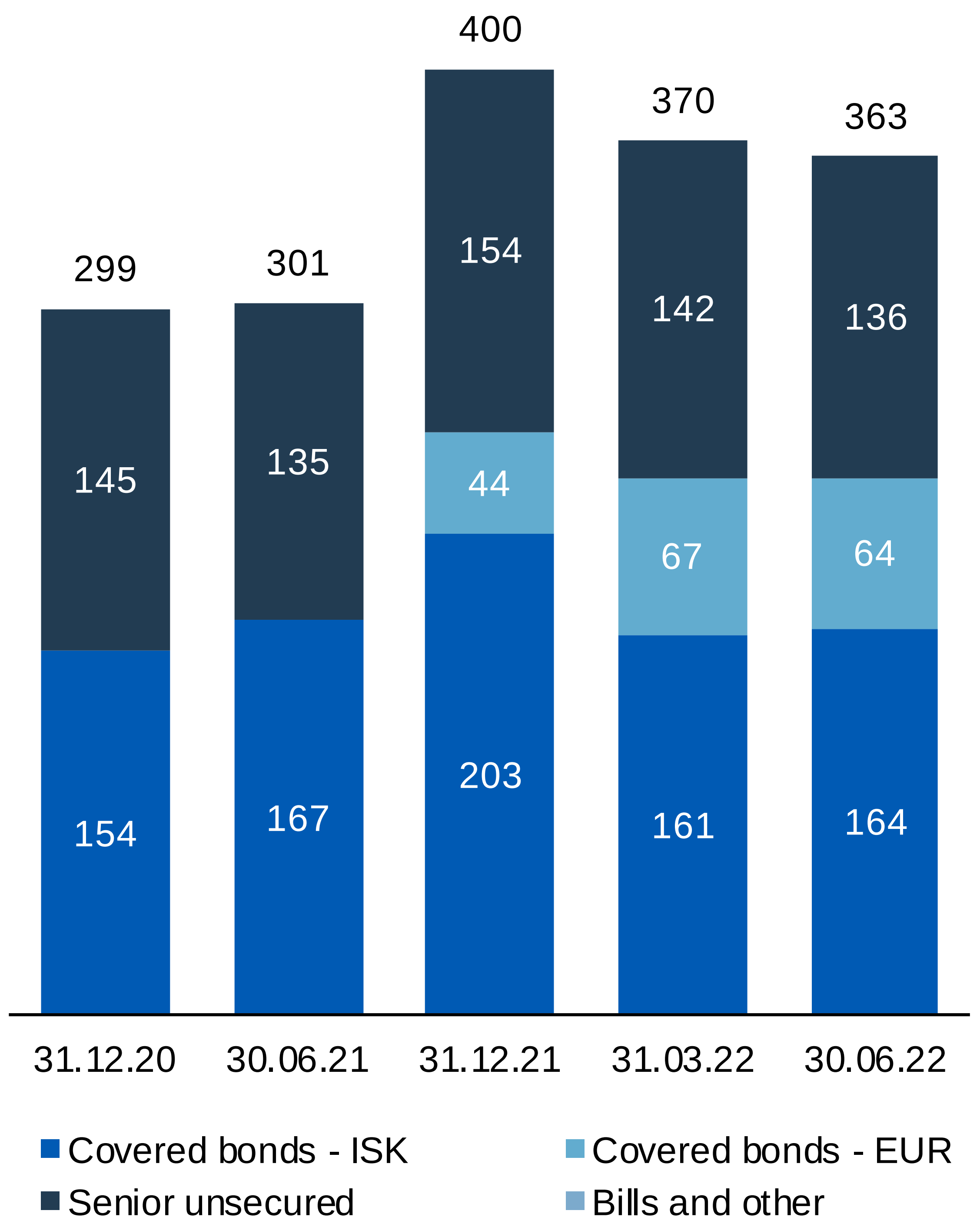
*Includes due to credit institutions and Central Bank

Borrowings

Balanced maturity profile with broad funding options

- Diverse funding options further supported in the quarter with added Moody's rating and access to ECB repo window
- Broadening of funding sources in recent years is a key strength in what is a challenging market backdrop
- Arion Bank issued EUR 250 million of ECB repo eligible covered bonds in July that are retained on balance sheet. This further broadens funding options and can be utilized especially while markets remain volatile
- Moody´s assigned A3 deposit and Baa1 issuer rating with positive outlook
- Covered bond maturity in autumn prefunded with regular issues over the year
  - Total issuance of ISK 9.2bn in the quarter and ISK 15.4bn from year-end
- The Bank will continue to regularly issue in the domestic market and opportunistically access the international markets throughout the year

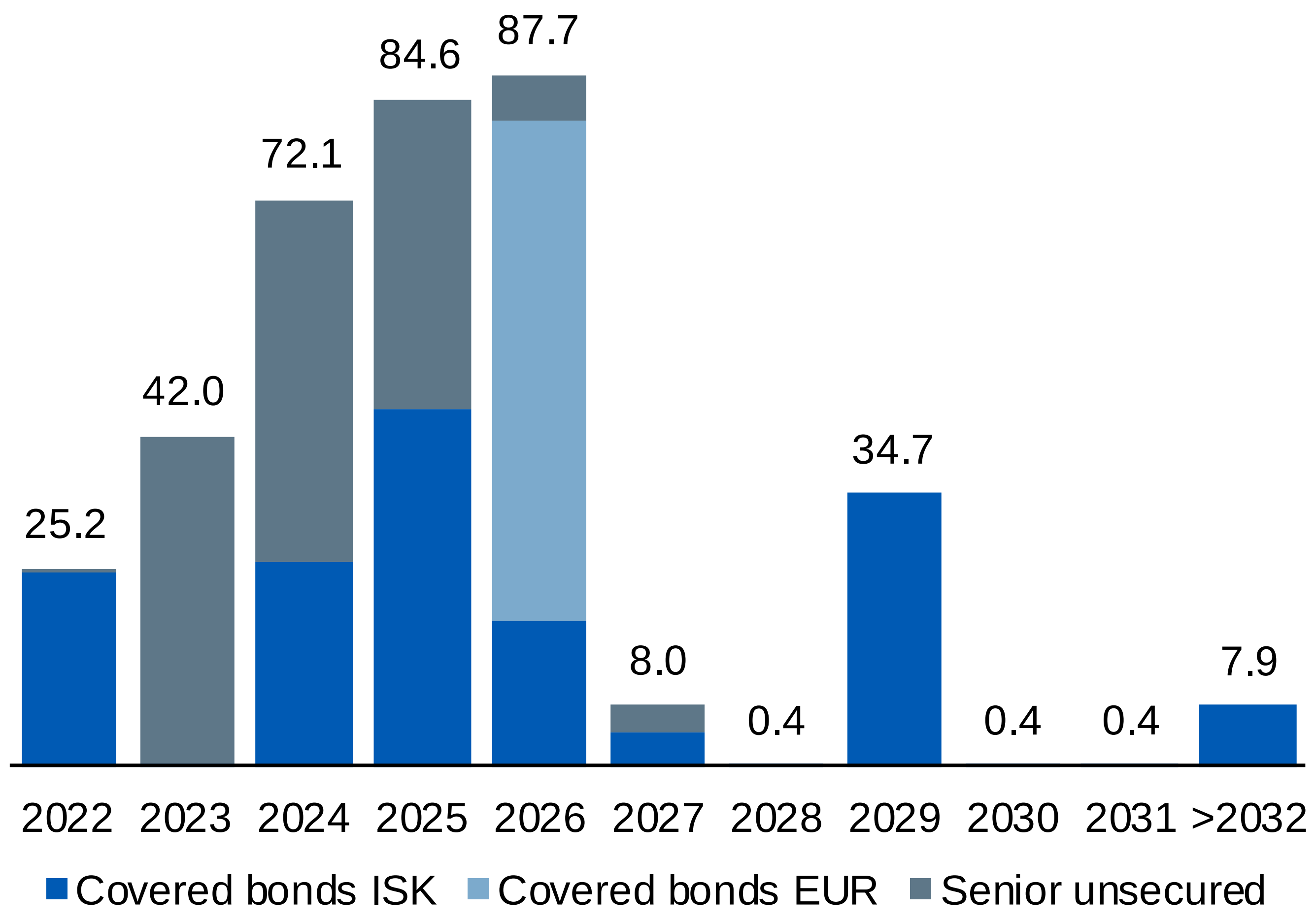
Borrowings by type



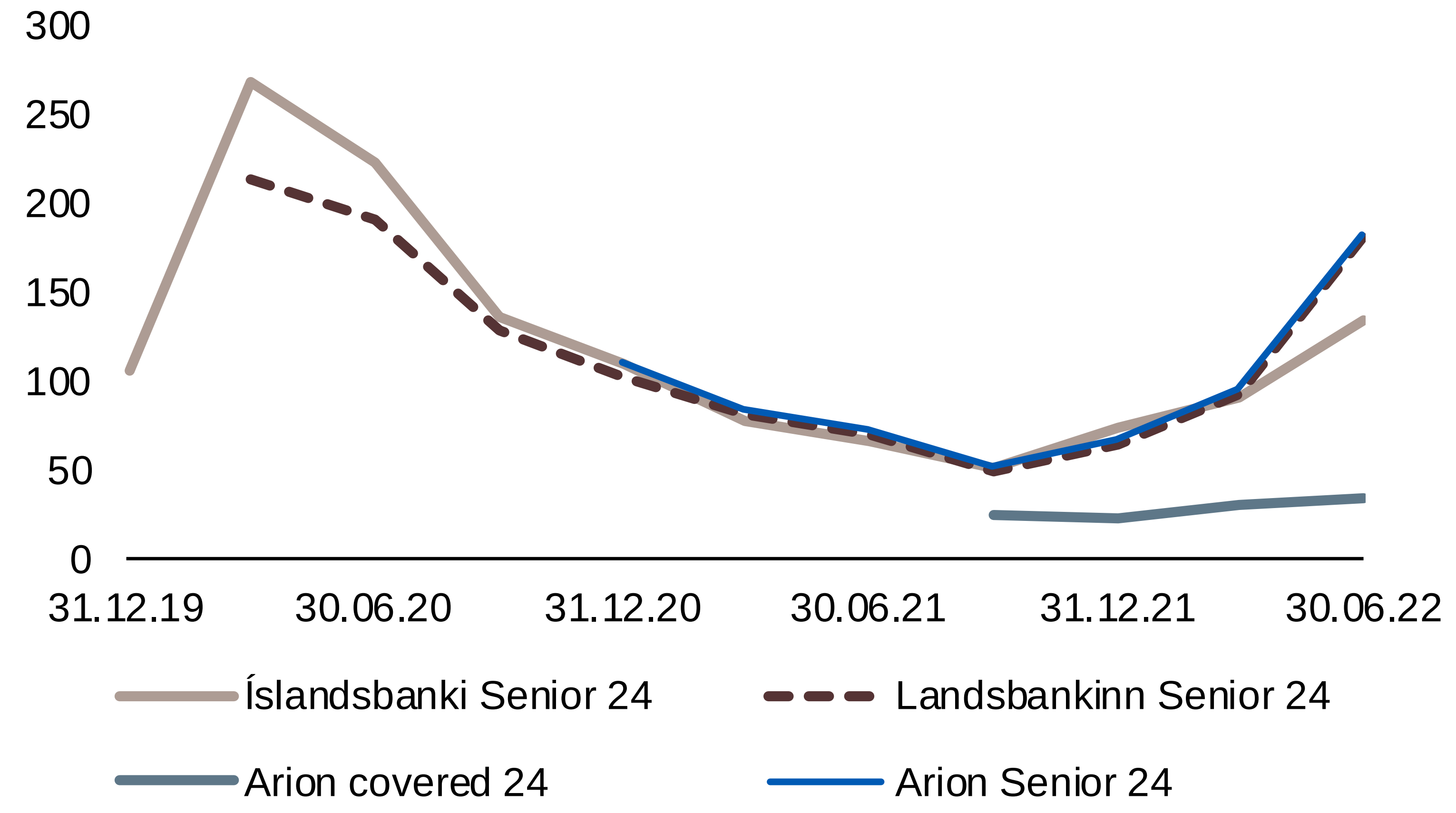
Ratings

S&P		
Senior unsecured	BBB	A
Covered bond	A-	N/A
Short term debt	A-2	A-1
Outlook	Stable	Stable
Moody's		
Long-term	Baa1	A-2
Outlook	Positive	Stable

Maturities of borrowings



Development of funding spreads (bps)



Source: Bloomberg

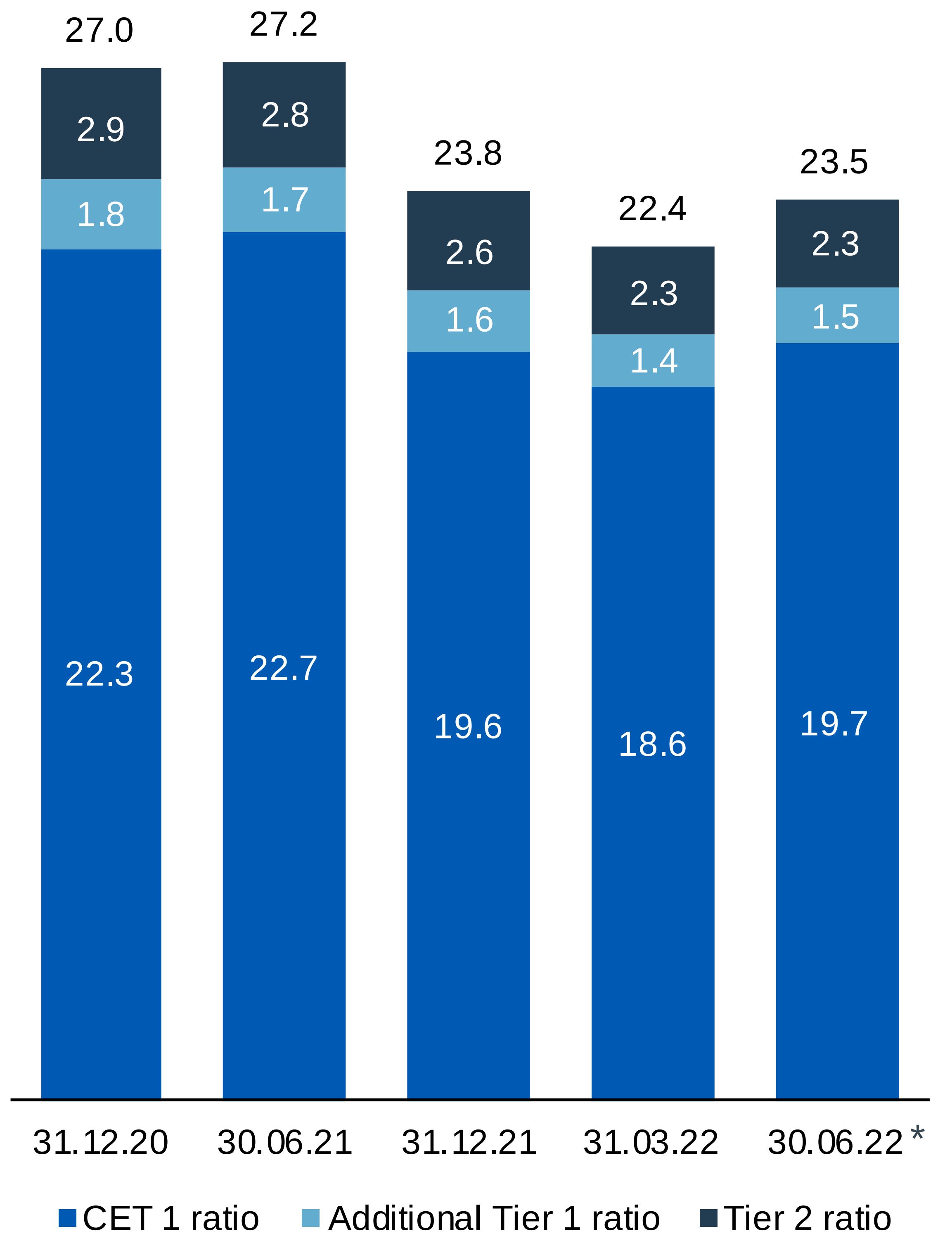
 All amounts in ISK bn

Own funds

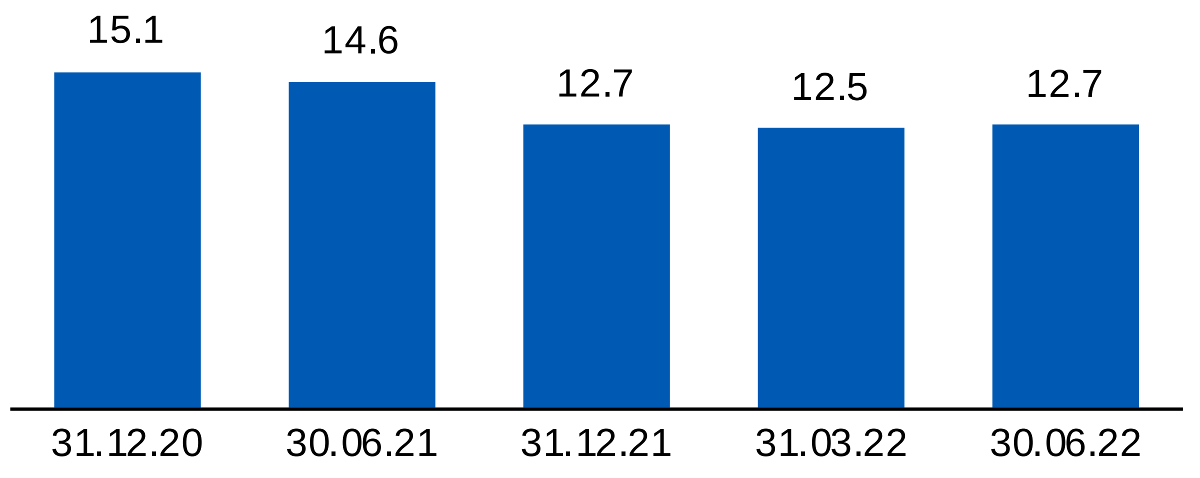
Very strong capital ratios while capital optimalization continues

- The sale of Valitor has a positive capital impact of ISK 12.7bn when profits from the sale and REA reduction are both accounted for (ISK 13.8bn including effect of capital released due to reduced FX imbalance created in relation to the transaction)
- The CET1 increased by 0.6% in Q2, mainly due to effect from the sale of Valitor
- REA decreased by 1.4% in Q2, mainly due to the sale of Valitor and lower market risk but lending growth increased credit risk by 1.1%
- REA of ISK 13.6bn for settlement risk related to the sale of Valitor not included here because the settlement took place on 1 July. This allows the full impact of the Valitor sale to be seen.
- Leverage ratio of 12.7% significantly above international competitors despite release of total ISK 58.3bn capital from beginning of 2021

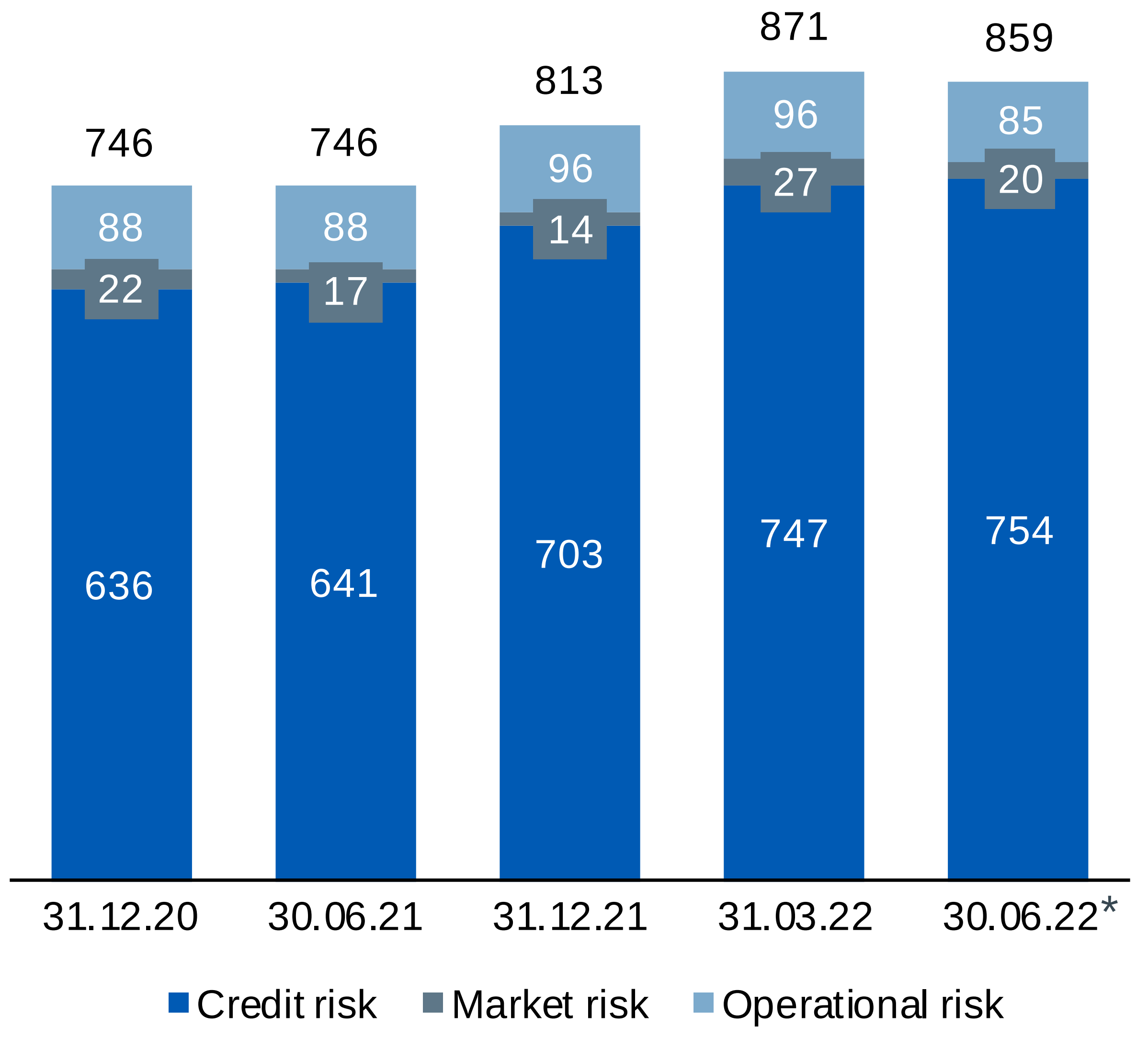
Total capital ratio (%)



Leverage ratio (%)



Risk-weighted exposure amount



*Including full impact of Valitor sale

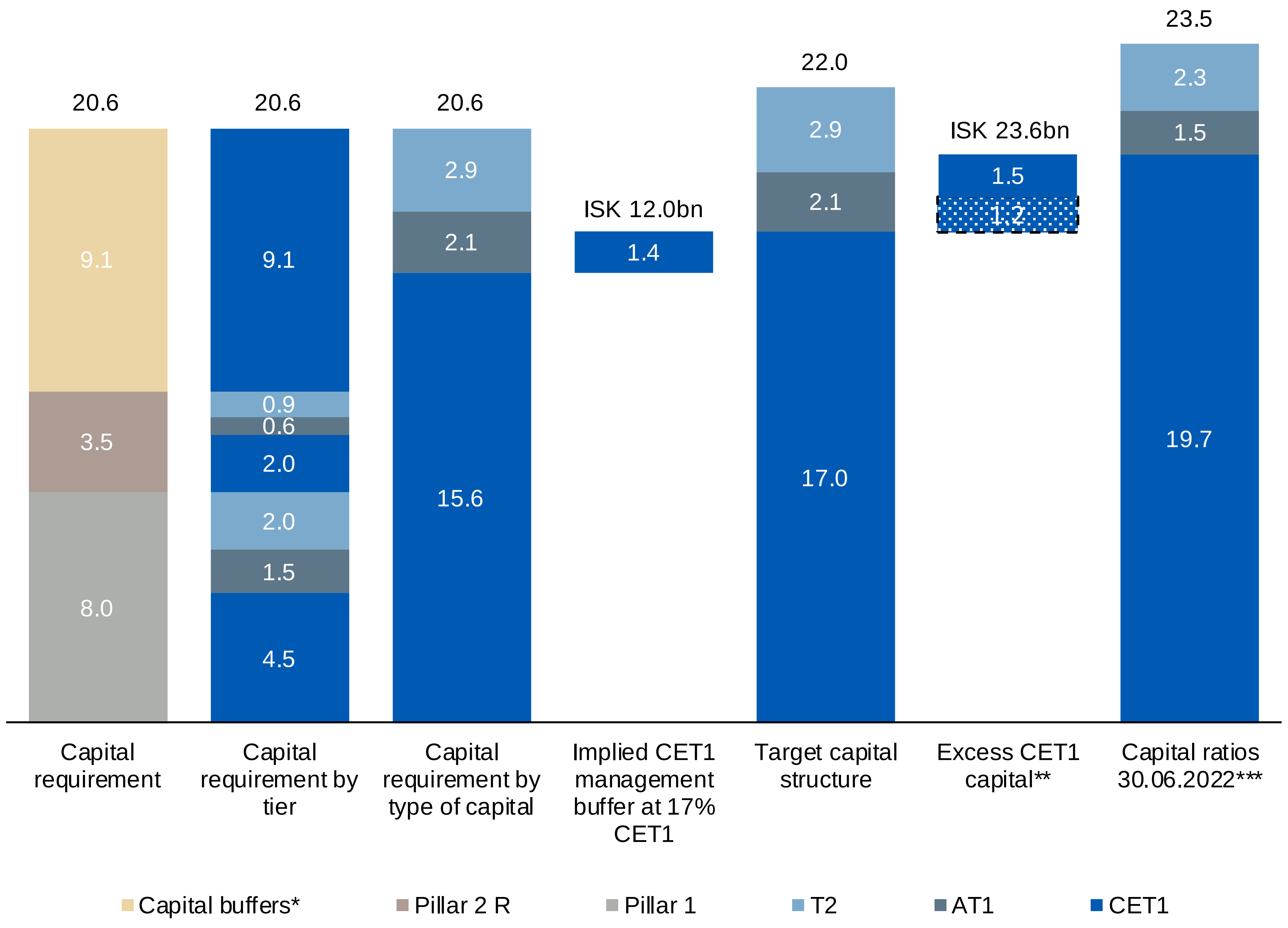
 All amounts in ISK bn

Own funds

ISK 23.6bn surplus capital partially contingent on further subordinated issue

- ISK 22.5bn of dividends paid out in March 2022
- H1 profits of ISK 15.5bn and corresponding foreseeable dividends of ISK 7.8bn included in the capital ratios
- The Pillar 2 requirement is 3.5% as a result of the SREP process based on year-end 2021 financials.
- The Financial Stability Council has announced that the countercyclical buffer will be increased to 2% as of 29 September 2022 from its current level of 0%
- Target CET1 ratio remains unchanged at 17%
  - Implied 1.4% CET1 management buffer (ISK 12.0bn) which is the difference between the target CET1 ratio and regulatory CET1 requirement when the foreseeable increase in the countercyclical buffer is included
  - CET1 capital of ISK 23.6bn in surplus of target capital structure, however since currently the Bank does not make the optimal use of the AT1 and T2 capital items then a portion of the surplus CET1 is used to make up that shortfall. The remaining CET1 surplus is ISK 13.0bn
- The solvency ratio of Vördur insurance is 161%

Own funds and capital requirements (%)



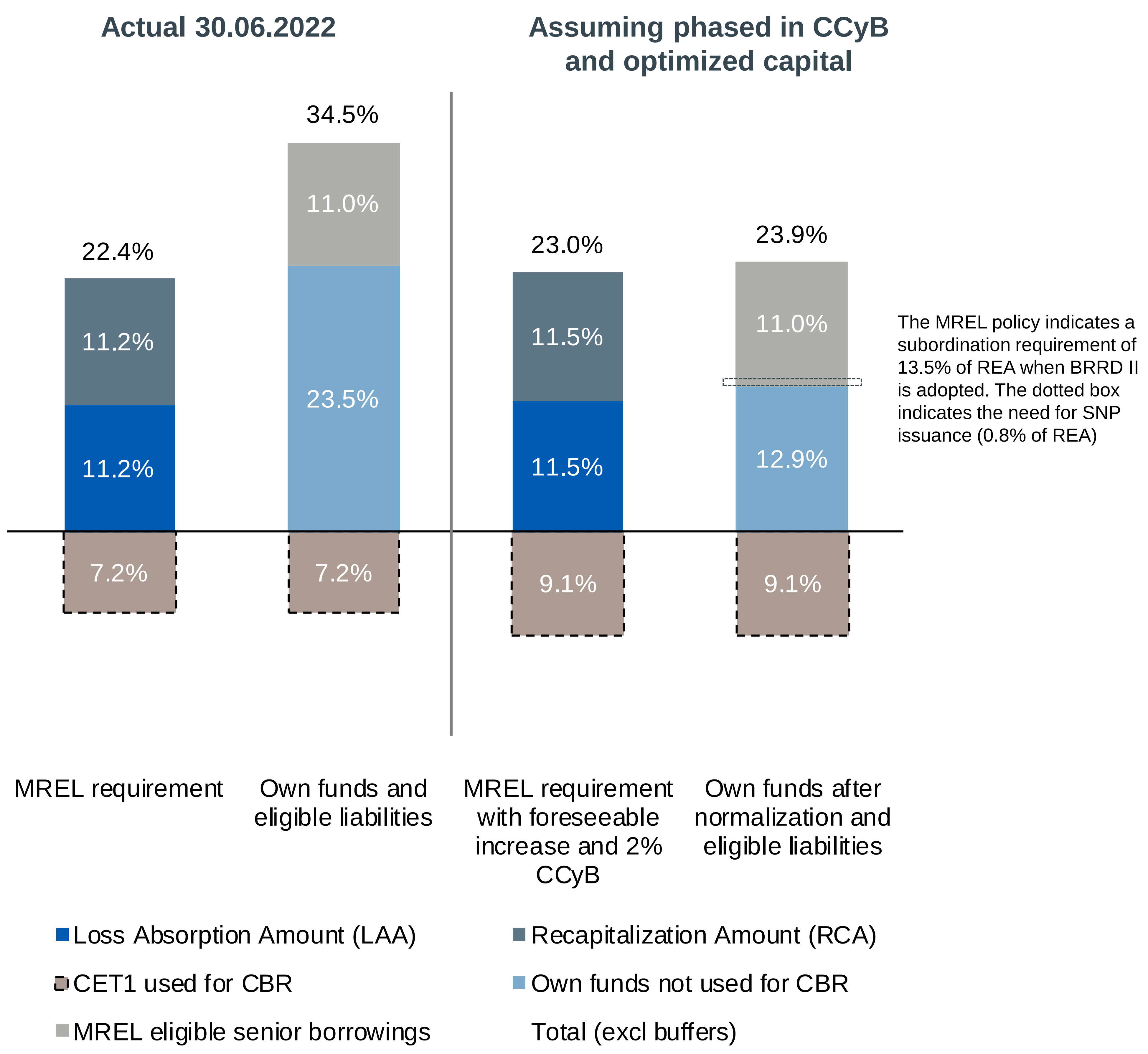
* Capital buffers include the announced increase in the countercyclical buffer in Iceland to 2%, effective 29 September 2022
** A portion of the surplus CET1 capital must be used to make up for the AT1 and T2 shortfall. This portion is shown in a chequered pattern
*** Including full impact of Valitor sale

MREL requirement

The Icelandic Resolution Authority has published its MREL policy

- 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 11.2% of REA, expected to rise to 11.5% of REA based on most recent SREP results
  - No Market Confidence Charge (MCC) because of the high level of combined buffer requirement (CBR), currently 7.2% of REA and expected to increase to 9.1% of REA on 30 September 2022
  - No subordination requirement
- Iceland is obligated to introduce the BRRD II approach at some point but the timeline is uncertain
- Some steps towards BRRD II have been taken
  - The Senior Non-Preferred (SNP) rank has been introduced into Icelandic law
  - The IRA MREL Policy discusses the key differences in MREL between BRRD I and BRRD II but does not state any firm decisions regarding their approach under the BRRD II regime
- Arion Bank has updated the terms of senior unsecured borrowings so that new issuances will be MREL eligible (senior preferred, SP) according to BRRD II
- The graph shows
  - MREL requirement for Arion Bank 22.4% of REA in addition to the CBR
  - 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 14.2% TLOF which corresponds to 21.9% REA at 31.03.2022

Going forward

Strong position to navigate the current operating environment

Underlying business dynamics are strong, with a healthy net interest margin and good trajectory in non-interest income, supported by clear strategy and operational discipline

Robust capital and liquidity positions further strengthened by sale of Valitor. The sale also reduces operational complexity going forward while supporting the momentum in fee income

Key theme for the coming months is to utilize this strong position and retain optionality in the current environment in terms of capital and balance sheet management

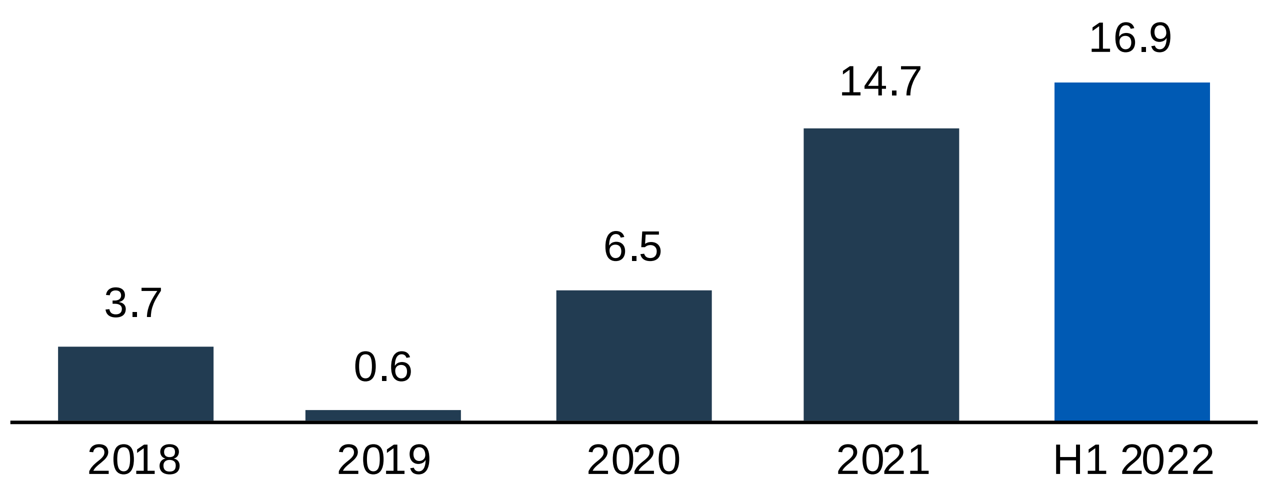
The external environment is complicated but there can be scope for optimism as agility in supply and demand dynamics and efficient flow of information means that the global economy could adjust quicker than historical precedents might suggest

The Icelandic economy is in many ways in a relatively strong position. One key strength in recent years has been stability and consistency in the regulatory, fiscal, and political environment

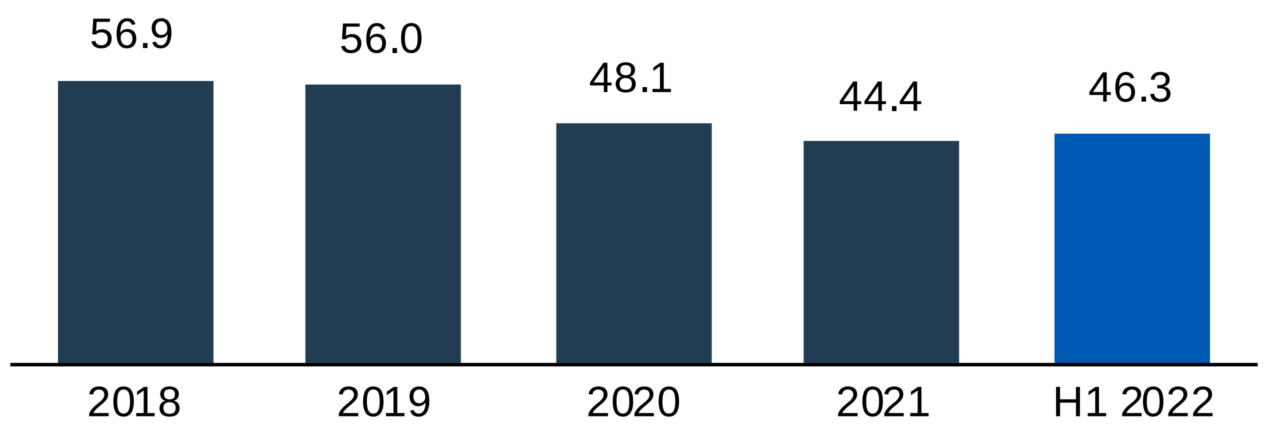
The Group is in a strong position to navigate the current environment, with diverse and profitable businesses, broad funding options and robust capital and liquidity positions

Key financial indicators - annual

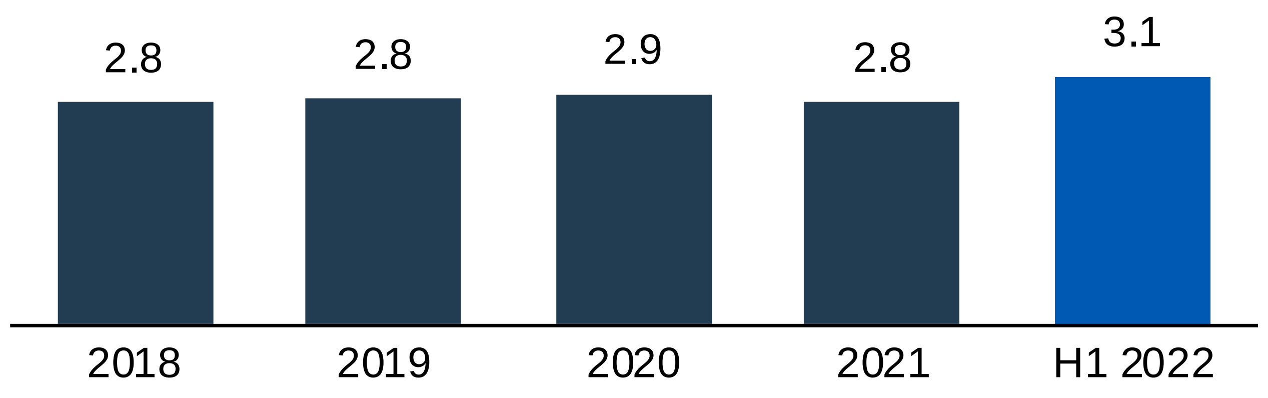
Return on equity (%)



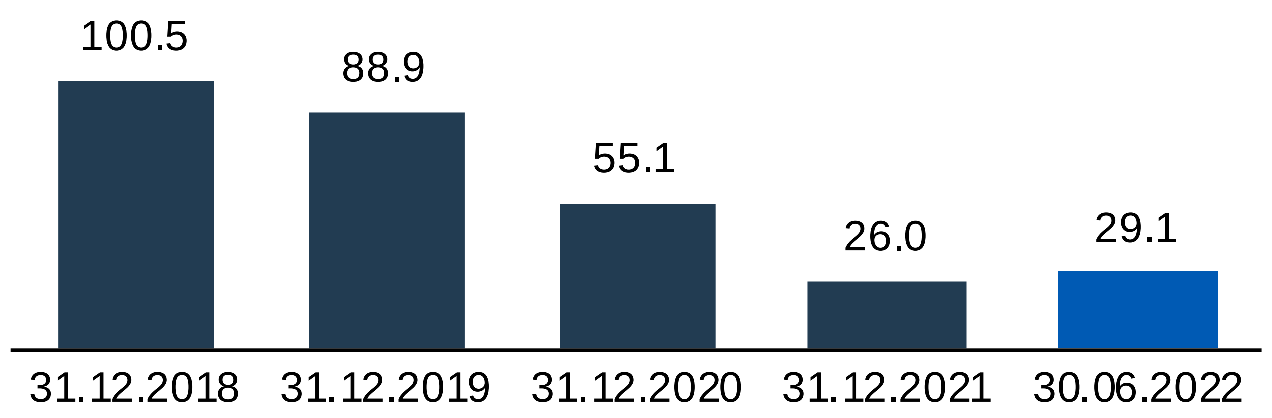
Cost-to-income ratio (%)



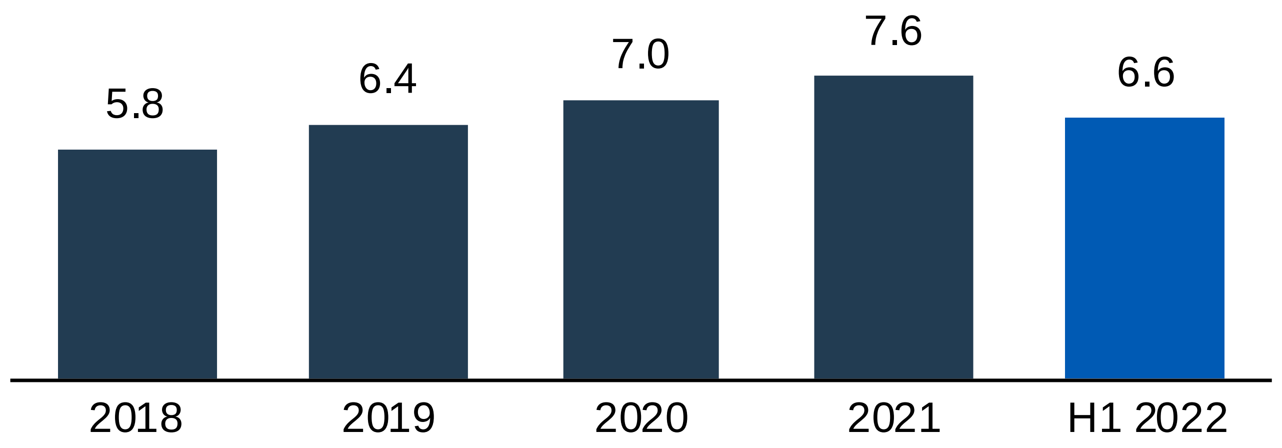
Net interest margin (%)



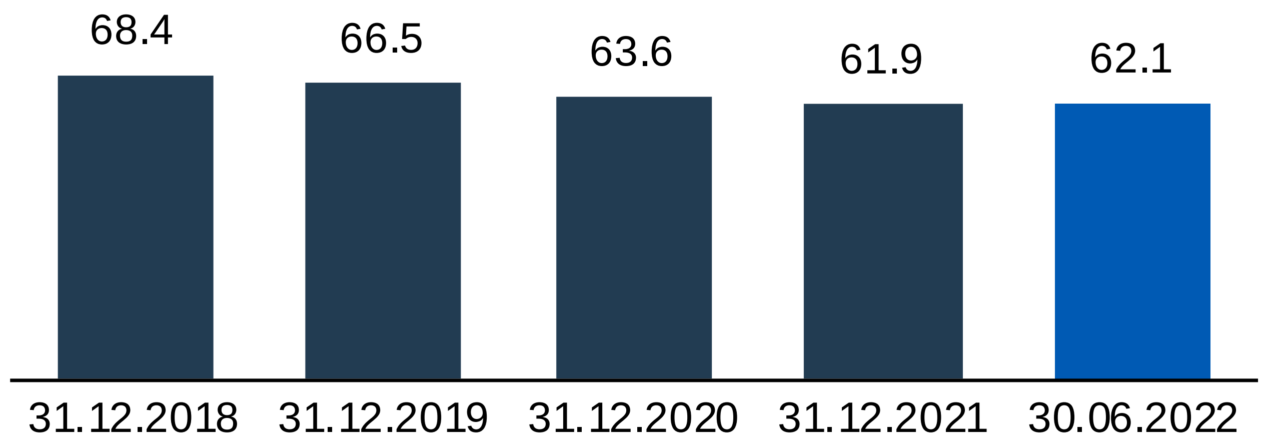
CPI imbalance (ISK bn)



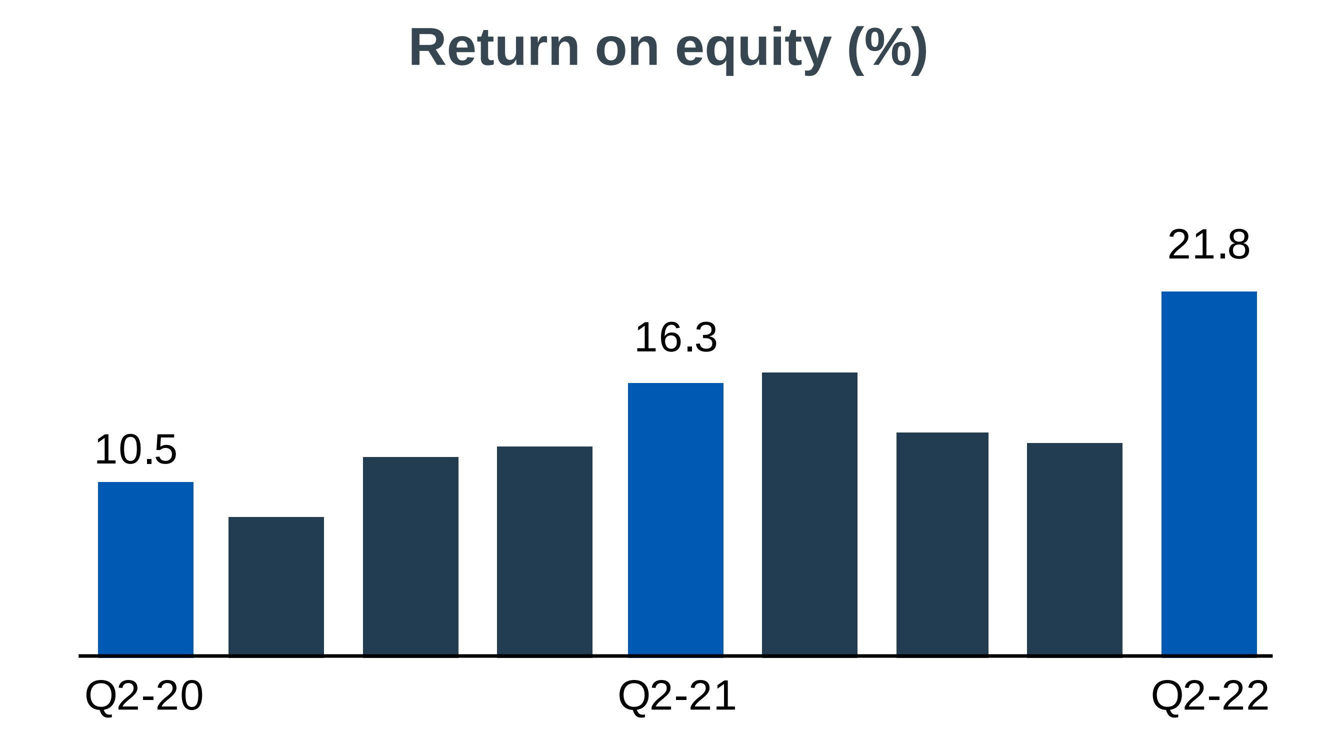
Operating income / REA (%)

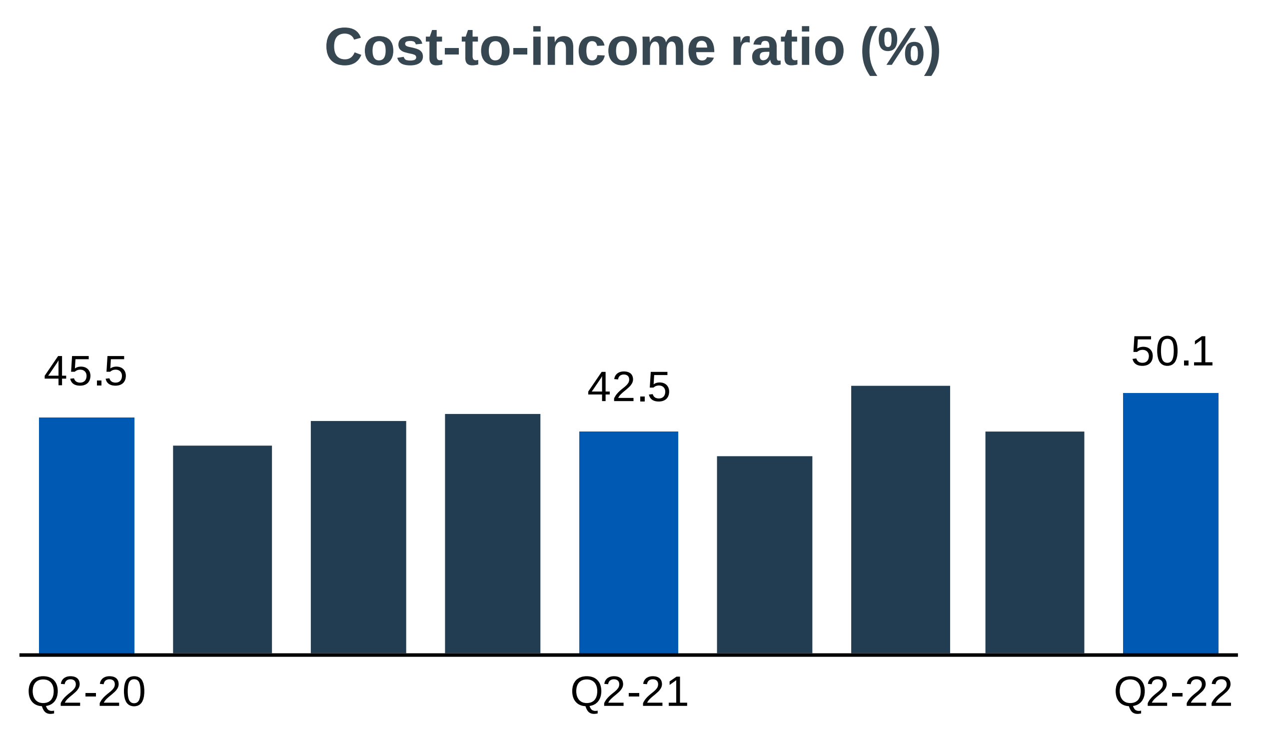


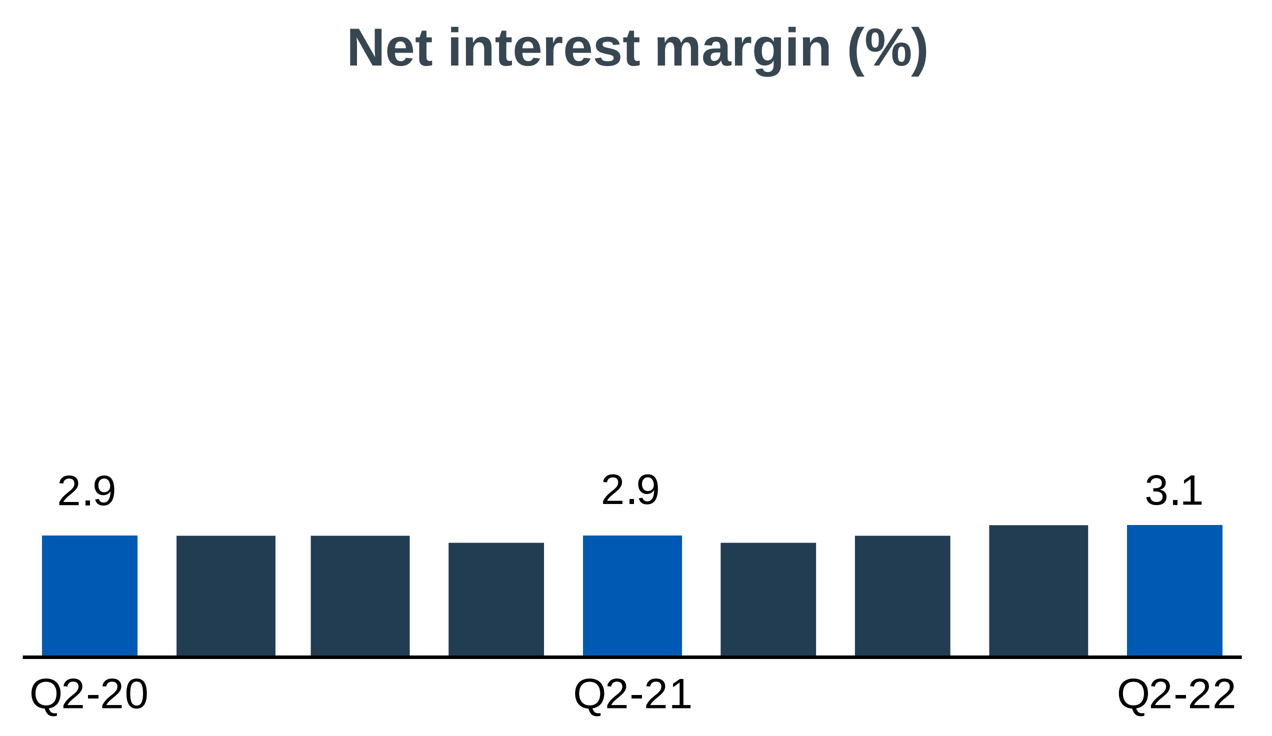
Risk exposure amount / Total assets (%)

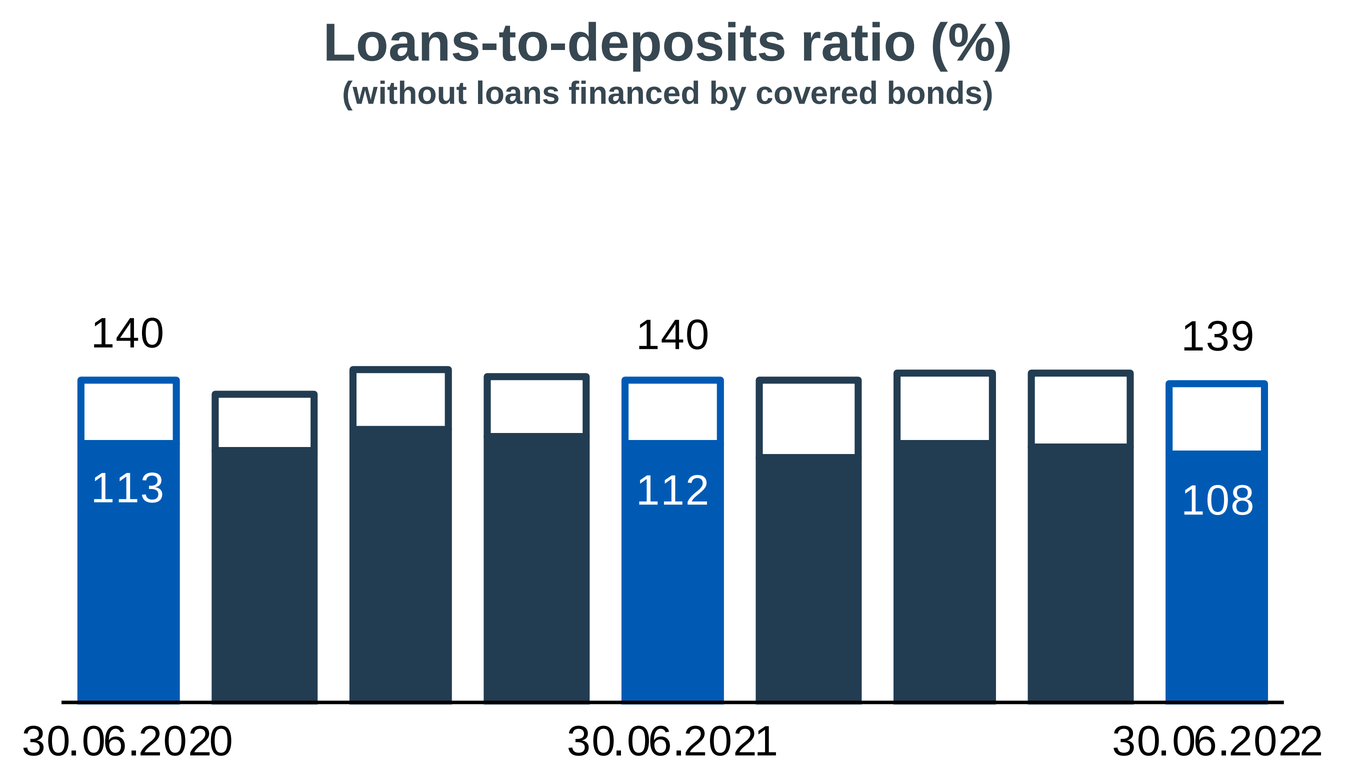


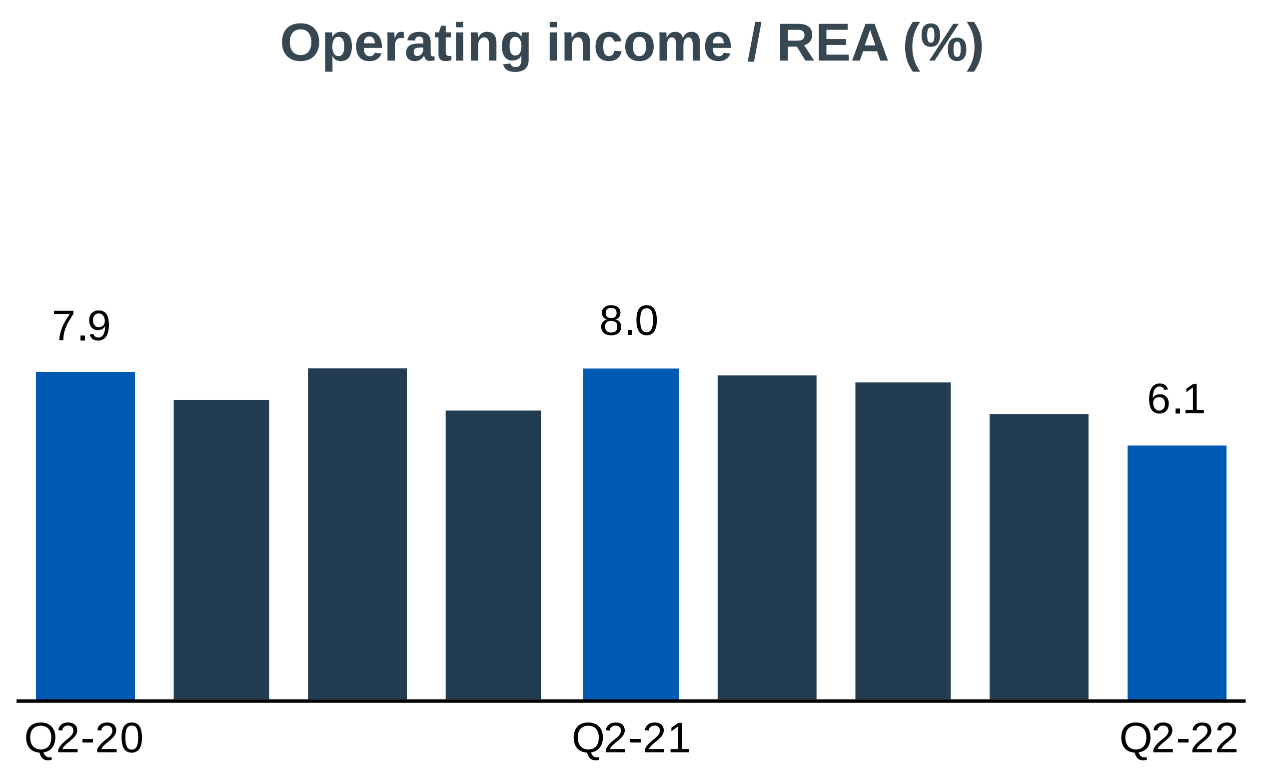
Key financial indicators - annual

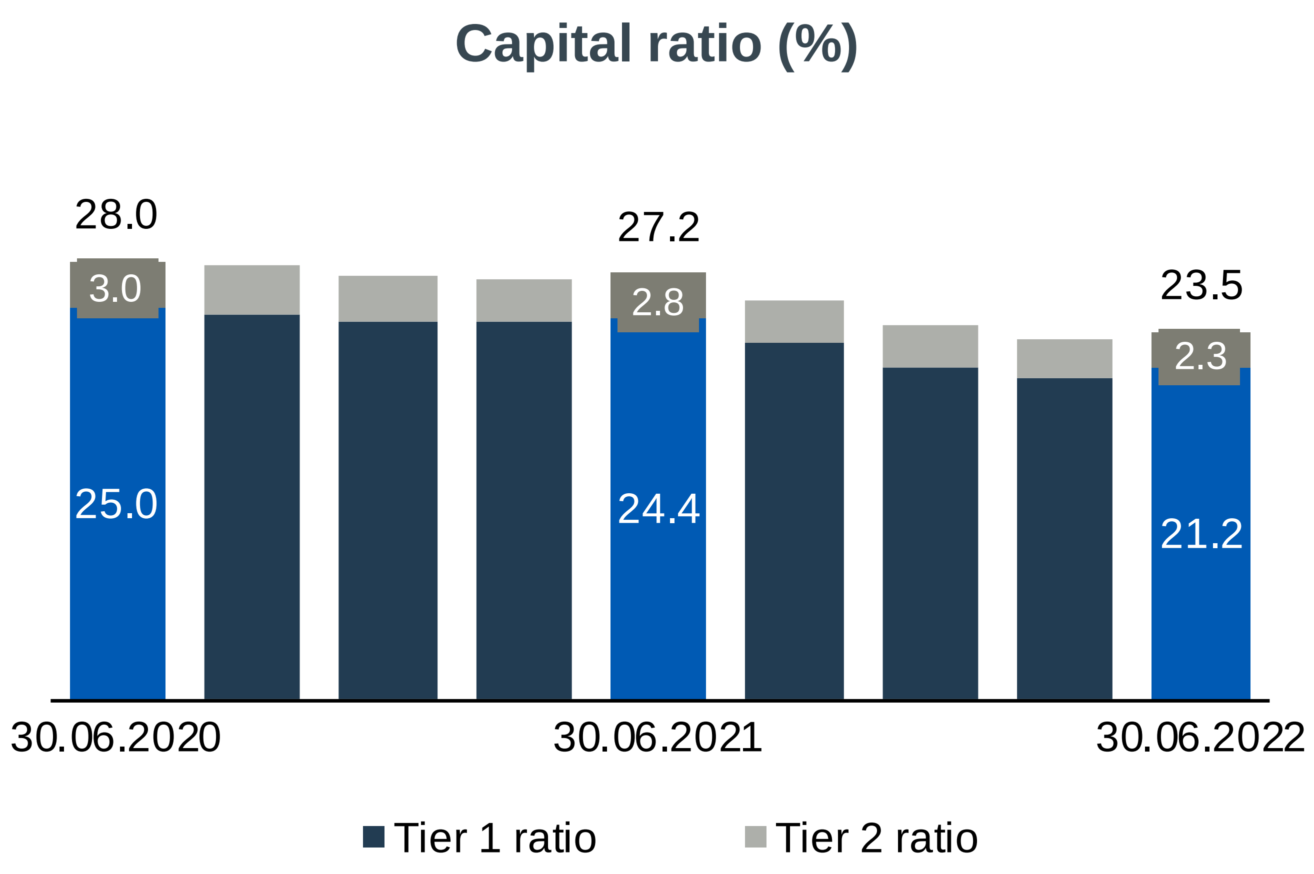












Key figures

Operations	H1 2022	H1 2021	H1 2020	H1 2019	H1 2018	Q2 2022	Q1 2022	Q4 2021	Q3 2021	Q2 2021
Net interest income	19,332	15,358	15,110	15,242	14,141	9,804	9,528	8,768	7,937	8,016
Net commission income	8,091	6,839	5,764	4,696	4,917	4,539	3,552	4,079	3,755	3,562
Operating income	27,774	28,101	23,039	23,928	23,315	13,260	14,514	15,234	14,890	15,004
Operating expenses	12,850	12,420	12,602	13,480	13,686	6,649	6,201	7,867	5,588	6,372
Net earnings	15,530	13,855	2,744	3,113	5,011	9,712	5,818	6,522	8,238	7,816
Return on equity	16.9%	14.3%	2.9%	3.2%	4.7%	21.8%	12.7%	13.4%	17.0%	16.3%
Net interest margin	3.1%	2.8%	2.9%	2.8%	2.7%	3.1%	3.1%	2.8%	2.7%	2.9%
Return on assets	2.3%	2.3%	0.5%	0.5%	0.9%	2.9%	1.8%	2.0%	2.6%	2.6%
Cost-to-income ratio	46.3%	44.2%	54.7%	56.3%	58.7%	50.1%	42.7%	51.6%	37.5%	42.5%
Cost-to-total assets	1.9%	2.1%	2.2%	2.2%	2.4%	2.0%	1.9%	2.4%	1.7%	2.1%

Balance Sheet	30.06.2022	31.12.2021	31.12.2020	31.12.2019	31.12.2018	30.06.2022	31.03.2022	31.12.2021	30.09.2021	30.06.2021
Total assets	1,383,362	1,313,864	1,172,706	1,081,854	1,164,326	1,383,362	1,341,014	1,313,864	1,346,092	1,217,921
Loans to customers	1,010,666	936,237	822,941	773,955	833,826	1,010,666	976,383	936,237	896,940	843,988
Mortgages	536,610	504,877	409,641	333,406	365,820	536,610	515,760	504,877	483,514	452,881
Share of stage 3 loans, gross	1.4%	1.9%	2.6%	2.7%	2.6%	1.4%	1.6%	1.9%	2.6%	2.8%
REA/ Total assets	62.1%	61.9%	63.6%	66.5%	68.4%	62.1%	64.9%	61.9%	58.0%	61.3%
CET 1 ratio	19.7%	19.6%	22.3%	21.2%	21.2%	19.7%	19.1%	19.6%	20.9%	22.7%
Leverage ratio	12.7%	12.6%	15.1%	14.1%	14.2%	12.7%	12.5%	12.6%	12.4%	14.6%
Liquidity coverage ratio	163.2%	202.8%	188.5%	188.3%	164.4%	163.2%	195.4%	202.8%	221.0%	215.1%
Loans to deposits ratio	139.0%	142.8%	144.8%	157.0%	178.9%	139.0%	143.6%	142.8%	139.9%	139.6%

 All amounts in ISK m