

## CREDIT OPINION

21 July 2022

Update



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### RATINGS

#### Arion Bank

Domicile	Iceland
Long Term CRR	A3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Not Assigned
Long Term Deposit	A3
Type	LT Bank Deposits - Fgn Curr
Outlook	Positive

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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## Arion Bank

New issuer - Arion Bank assigned A3 deposit and Baa1 issuer ratings, outlook positive

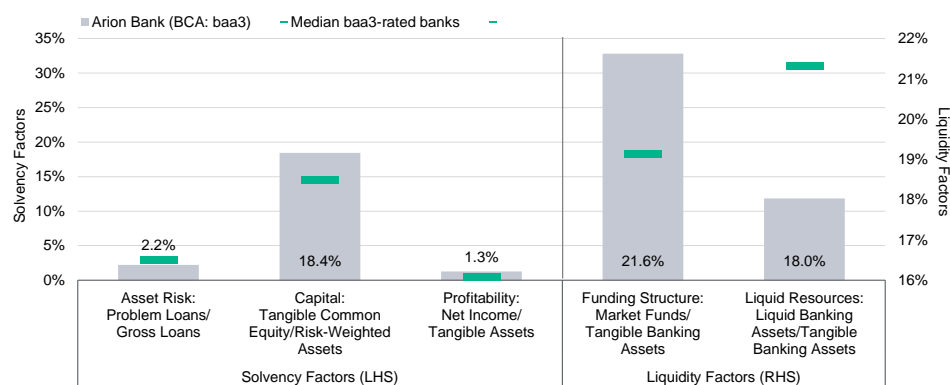
### Summary

Arion Bank's (Arion) foreign and local currency banks deposit ratings of A3/Prime-2 and issuer ratings of Baa1 are driven by the bank's baa3 baseline credit assessment (BCA); and three notches and two notches of rating uplift, respectively, under our forward-looking Advanced Loss Given Failure (LGF) analysis, which takes into accounts the risks faced by the bank's different liabilities should Arion enter into resolution.

Arion's BCA of baa3 reflects its robust capitalisation coupled with satisfactory core profitability and adequate liquidity balanced against single name and high geographical concentration, market related risks driven by the bank's market making operations and reliance on market funding.

Exhibit 1

### Rating Scorecard - Key Financial Ratios as of end-March 2022



These represent our [Banks](#) methodology scorecard ratios, whereby asset risk and profitability reflect the weaker of either the three year average and the latest annual figure. Capital ratio is the latest reported figure. Funding structure and liquid resource ratios reflect the latest fiscal year-end figures.

Source: Moody's Investors Service

## Credit strengths

- » Low levels of non-performing loans which have improved in recent years and compare favorably to global peers
- » Strong capitalisation supported high capital requirements and improving profitability
- » Diversified revenue stream compared to domestic peers
- » Adequate liquidity buffers

## Credit challenges

- » Geographical and single-name concentration as well as low levels of provisioning result in significant tail risks in the loan book
- » Non-credit related risks driven by market making operations
- » Increasing reliance on market funding, with an increasing amount of FX-debt, exposes the bank to changes in investor sentiment

## Outlook

The positive outlook on Arion's long-term deposit and issuer ratings reflects the bank's improved performance during the past 18 months in terms of asset quality metrics and overall risk profile. The outlook also incorporates Moody's expectation that the bank will exhibit lower earnings volatility going forward, reflective of the successful disposal of some of the discontinued operations, tighter underwriting criteria and further integration of the insurance operations in the bank's activities.

## Factors that could lead to an upgrade

The positive outlook could transform into a rating upgrade in the next 12-18 months, provided that Arion continues to demonstrate resilience in its financial performance while sustaining strong asset quality and capitalisation while it successfully disposes of its remaining discontinued operations currently held for sale.

For the issuer ratings, upward rating pressure could also develop because of a larger cushion of loss absorbing obligations protecting creditors in case of failure.

## Factors that could lead to a downgrade

Downward pressure could emerge if Arion's (1) asset quality and risk profile was to deteriorate, for example as a result of increased exposures to more volatile sectors and/or increased single name concentrations; (2) risk profile increases driven by non-credit related risks such as market risk and fx risk (3) the bank's recurring profitability weakens significantly limiting the bank's internal capital generation (4) financing conditions were to become more difficult or (4) the macroeconomic environment deteriorates significantly leading to a lower Macro Profile.

Furthermore, a reduction in the rating uplift as a result of our LGF analysis triggered by structural funding changes to the bank's balance sheet could lead to downward rating pressure.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

## Key indicators

Exhibit 2

### Arion Bank (Consolidated Financials) [1]

	03-22 <sup>2</sup>	12-21 <sup>2</sup>	12-20 <sup>2</sup>	12-19 <sup>2</sup>	12-18 <sup>2</sup>	CAGR/Avg. <sup>3</sup>
Total Assets (ISK Billion)	1,341.0	1,313.9	1,172.7	1,081.9	1,164.3	4.4 <sup>4</sup>
Total Assets (USD Million)	10,507.1	10,085.3	9,192.3	8,941.7	9,992.9	1.6 <sup>4</sup>
Tangible Common Equity (ISK Billion)	163.2	175.9	180.0	174.3	181.5	(3.2) <sup>4</sup>
Tangible Common Equity (USD Million)	1,278.5	1,350.1	1,411.0	1,440.8	1,557.4	(5.9) <sup>4</sup>
Problem Loans / Gross Loans (%)	1.6	1.9	2.6	2.7	2.6	2.3 <sup>5</sup>
Tangible Common Equity / Risk Weighted Assets (%)	18.4	21.0	23.3	23.9	22.5	21.8 <sup>6</sup>
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	9.4	9.8	11.4	11.4	11.5	10.7 <sup>5</sup>
Net Interest Margin (%)	3.0	2.7	2.8	2.9	2.7	2.8 <sup>5</sup>
PPI / Average RWA (%)	3.6	3.9	3.4	2.3	2.0	3.0 <sup>6</sup>
Net Income / Tangible Assets (%)	1.7	2.2	1.1	0.1	0.7	1.2 <sup>5</sup>
Cost / Income Ratio (%)	46.2	47.1	50.7	63.2	64.3	54.3 <sup>5</sup>
Market Funds / Tangible Banking Assets (%)	21.5	21.6	21.1	22.4	28.7	23.1 <sup>5</sup>
Liquid Banking Assets / Tangible Banking Assets (%)	14.1	18.0	18.9	15.8	17.5	16.9 <sup>5</sup>
Gross Loans / Due to Customers (%)	144.8	144.0	146.9	158.9	180.0	154.9 <sup>5</sup>

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; IFRS. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.

Sources: Moody's Investors Service and company filings

## Profile

Arion bank was founded following the default of its predecessor Kaupthing, which had roots tracing back to 1930. Following the collapse of Kaupthing in 2009, a new, state-owned entity named New Kaupthing was established and assumed control of the bank's domestic assets and liabilities. The entity later changed its name to Arion Banki and in 2018 the government sold its final stake through a double-listing of the bank on Nasdaq Iceland and Nasdaq Stockholm.

Arion is a full-service commercial bank in Iceland that provides retail, corporate, investment and private banking services, asset management services through its Stefnir subsidiary, as well as insurance offerings through its Vördur subsidiary. It operates through a network of 15 branches in Iceland.

Arion is the third largest bank in Iceland with total assets of around ISK1,341 billion as of end-March 2022 and had market shares of around 27% for both loans and deposits in the Icelandic banking system. The bank is listed on Nasdaq Iceland and is privately owned.

## Recent developments

### Macroeconomic developments

Russia's invasion of Ukraine has significantly altered the global economic backdrop through three main channels. First, the spike in commodities prices driven by existing and expected supply shortages is creating risks of damagingly high input costs and consumer inflation over an extended period. Second, financial and business disruption poses risks to the highly integrated global economy. Third, heightened security and geopolitical risks will exert economic costs and weigh on the economy by denting sentiment. We have lowered our baseline growth forecasts to capture these shifts in the global economic environment. We now [expect](#) the advanced G-20 economies to expand 2.6% in 2022 and emerging market countries will grow 3.8%, down from our March forecast of 3.2% and 4.2%, respectively. Russia is the only G-20 economy that we forecast will contract this year.

## Detailed credit considerations

### Arion's operations are supported by its "Strong-" weighted macro profile

Arion operates mostly in Iceland, with a small international exposure in the Arctic region amounting to less than 5% of the group's assets. This is reflected in Arion's assigned Weighted Macro Profile of 'Strong -'. Iceland's 'Strong -' [Macro Profile](#) balances the country's small size and associated history of economic boom and bust episodes with very high wealth levels and strong competitiveness. Iceland further benefits from high institutional and government strength, combined with a low susceptibility to political event risk.

In 2021 Iceland's real GDP grew by 4.3% compared to a contraction of 7.1% in 2020 following the pandemic's impact on the tourism industry. The real GDP is expected to grow by 4.7% in 2022 as tourism continues to rebound, with some further support from high prices and strong demand on fish exports. The growth could be hampered by Russia's invasion of Ukraine as the economic impact on trade partners could result in spillover effects on commodity prices and global inflation, which could erode terms of trade and push domestic inflation upwards. However, Icelandic households have high levels of savings and Iceland has minimal direct exposure to Russia both in terms of trade and within the banking system.

The main risks to Iceland's banking system stem from the small size and volatility of the economy, the substantial amount of CPI-indexed loans on banks' loan books, and risk of contagion within the banking sector. These risks are somewhat offset by low levels of household debt combined with strong savings, a shift towards non-indexed loans and the banks' very strong capital and leverage ratios.

### Asset quality has been improving but geographical and single name concentration as well as non credit related risk weigh on the bank's risk profile

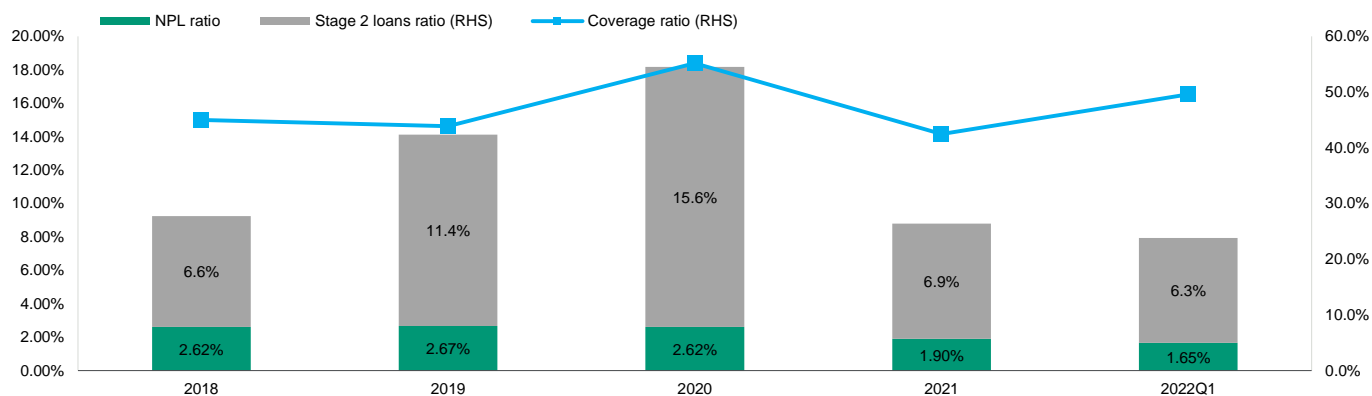
Arion bank's asset quality has improved with a reported non-performing loans (NPL) ratio (stage 3 loans to gross loans) of 1.6% at end March 2022, from its peak of 2.7% in 2019, while the ratio remained broadly unchanged at 2.6% during 2020 despite the coronavirus outbreak. Arion's declining NPL ratio is reflective of the market as a whole, where overall NPL ratios have improved in recent years as the effect of the pandemic wears off.

Stage 2 loans have also improved significantly. Arion bank had a higher level of Stage 2 loans entering the pandemic, compared to its other 2 domestic peers, owing to its exposures to the travel industry and the turbulence in the travel sector during 2018/2019 following the bankruptcy of Primera air. As of 1Q 2022, Stage 2 loans account for 6.3% of gross loans relating mostly to exposures to the service and tourism sector, down from 16.7% at its peak during 2Q20. Forborne loans account for 4.7% of the bank's gross loans and have also demonstrated improving trends in recent quarters (the vast majority of which are in tourism related sectors). It is also worth noting that 44% of the forborne loans are classified as stage 1 at end March 2022 and only 20% are stage 3.

We expect the bank's asset quality metrics to remain stable broadly stable assuming that the tourism sector continues its recovery. However, despite Iceland not being directly affected by the war in Ukraine due to self-sufficiency in terms of energy, there are downside risks related to potential negative impacts to the tourism and export sectors stemming from potentially prolonged inflationary pressure and recession risks for key trading partners.

Exhibit 3

### Arion's NPL ratio has been decreasing in recent years along with stage 2 loans



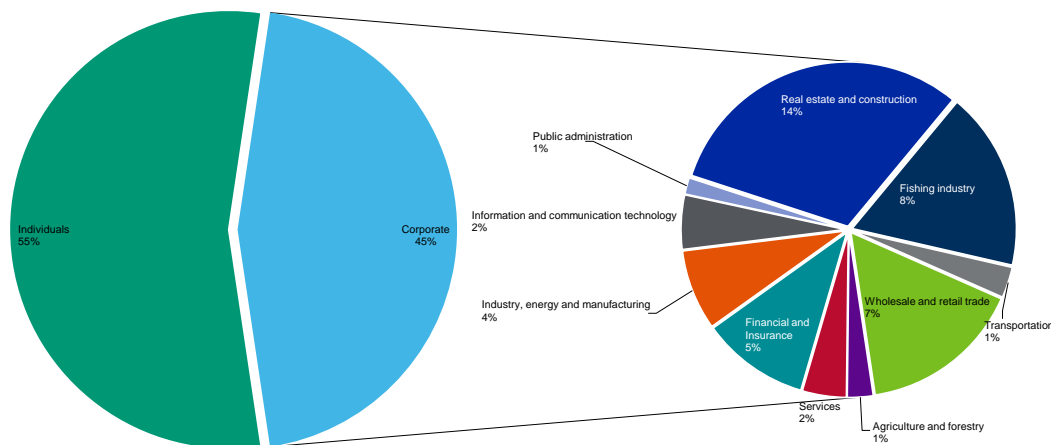
Source: Company reports, MIS

The bank's loan portfolio is evenly split between corporate and retail exposures, with retail exposures currently accounting for around 55% of the loan book as of end-March 2022 compared to 47.5% in 2019. The increased share of retail exposures is reflective of the favourable lending environment seen in Iceland in recent years following significant rate cuts and government measures to lessen the impact of the Covid-19 pandemic. This resulted in new lending being primarily in the form of non-indexed mortgages offered by commercial banks, as opposed to the historically more prevalent CPI-indexed mortgages. Furthermore a large share of indexed loans,

issued by pension funds, have been refinanced with non indexed products offered by commercial banks. However, during the first quarter of 2022, Arion's mortgage lending grew by 1% (21.9% in 2021) reflective of the steep interest rate increases by the Central Bank during 2022 and tighter underwriting rules.

Exhibit 4

#### Arion has a diverse asset mix, with a large share of corporate loans



Source: Company reports, MIS

Arion's corporate book is focused on real estate and construction, fishing and the wholesale and trade sector. During 2020 and the first half of 2021, corporate lending growth was in a negative territory reflective of the adverse economic conditions following the coronavirus outbreak. However, since Q3 21 corporate growth has been recovering and at in Q1 22 it was up by 13% yoy.

The corporate loan book also contains some client concentrations which in the past have lead to higher loan losses than peers and foreclosures of businesses (currently reported under discontinued operations). However, in the past years the bank has revised its risk framework limiting large exposures and sector concentrations, in addition a new KYC health risk appetite and statement metric was introduced and made part of the variable remuneration system which had a very positive impact.

The lending book also exhibits geographical concentrations, in line with the rest of the market, with contagion risks between various sectors given the small size of the economy. However it is worth noting that the bank is actively trying to increase its lending activities to the Arctic region albeit these operations remain small as a share of the whole portfolio.

Our assigned score also takes into consideration non-credit risks related to the bank's market making operations. The bank is still has equity exposures which are used for hedging forward contracts. While the derivative positions are hedged using the equity positions, there is still counterparty credit risks related to clients' margin positions. Counterparty credit risk amounted to ISK7.5 billion of the total risk-weighted exposure amount (REA) as of Q1 2022, down slightly from ISK7.8 billion in end-2021. This is also reflected in the bank's Pillar 2 requirements where market risk accounts for just over 40% of the total requirement.

#### Capitalisation is expected to remain strong, albeit a slightly lower levels

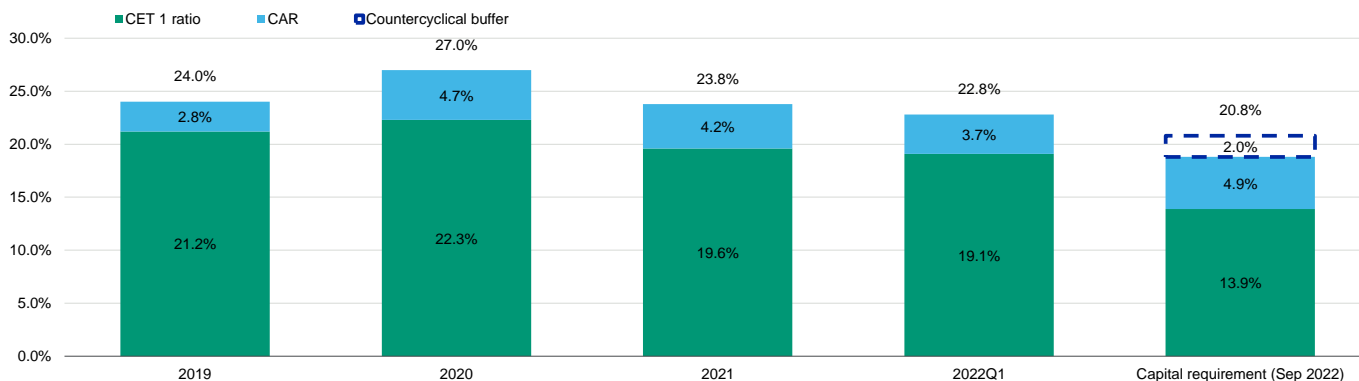
Arion enjoys a strong capital position as well as a very strong leverage ratio, reflective of the use of the standardised method for the calculation of capital requirements. The bank's reported common equity Tier 1 (CET1) ratio was 19.1% as of end-March 2022, down from 19.6% in 2021 (see Exhibit), compared to a CET1 requirement of 13.6%. The bank further had a total capital adequacy ratio (CAR) of 22.8% in end-March 2022 (23.8% in end-2021) compared to a minimum required CAR of 18.5%.

The CET1 requirement is expected to increase to 15.9% from September 2022 following the Central Bank's decision to re-instate the countercyclical capital buffer to 2% from 0%, combined with Arion's new Pillar 2 requirements of 3.5% (up by 0.3% from July 1, 2022), as communicated by the FSA in the latest Supervisory Review and Evaluation Process (SREP) report.

The strong capitalization is further supported by a strong leverage ratio of 12.5% as of end-March 2022, which is significantly above the European average leverage ratio of around 6%.

Exhibit 5

### Arion's capital buffer is on a declining trend but remains substantial



Source: Company reports, MIS

The bank is targeting a CET1 ratio of 17%, and a CAR of 21.9%, as it optimises its capital structure. Arion utilizes its 50% dividend policy, combined with share buy-backs and extra dividends in recent years, to reach its target capital level. Extra dividends could also arise from the sale of Valitor (which was finalised at end June 2022) which is expected to result in net proceeds of approximately ISK14.3 billion. The significant volumes of capital release are balanced by Arion's equity capital market access on the Nasdaq Iceland stock exchange and its stable shareholder base consisting to a large degree of Icelandic pension funds with a long-term and stable investing horizon.

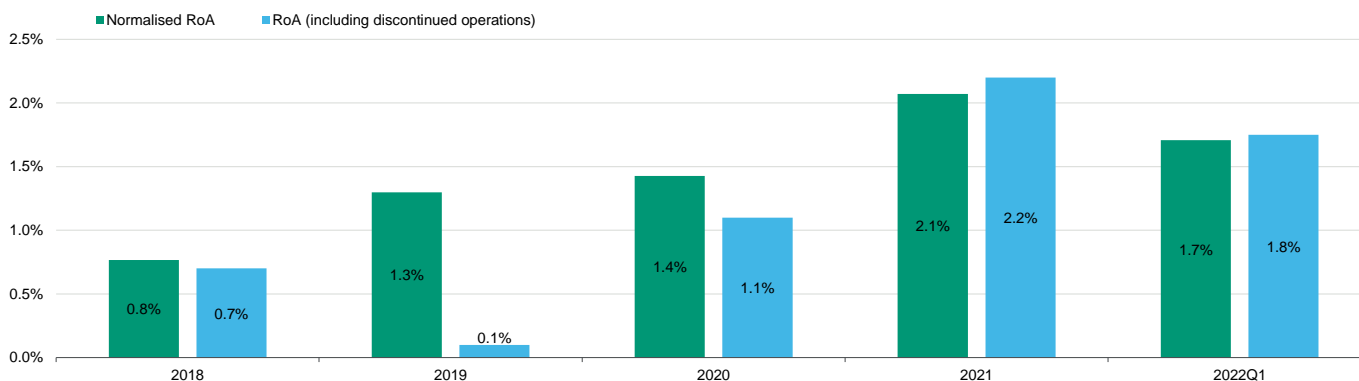
Our assigned capital score reflects Arion's strong capital metrics, strong leverage ratio and its access to equity capital markets combined with a stable ownership structure.

### Profitability has been improving, reflective of the balance sheet clear out and focus on profitable growth

Arion's core profitability is strong and has been improving. The bank reported return on assets (RoA) of 1.8% at end-March 2022 and 2.2% in 2021 while it maintained a strong performance during 2020, despite the coronavirus outbreak and losses from discontinued operations, with a RoA of 1.1%. This is a great improvement from the 0.7% and 0.1% recorded in 2018 and 2019 which was primarily driven by the negative impact from discontinued operations that were held for sale. Nevertheless, the bank has taken active steps to dispose the operations in the past years, with Valitor's sale being finalised in the end of June 2022, which accounts for approximately 80% of the discontinued operations and should result in lower earnings volatility going forward.

Exhibit 6

### Arion's profitability has been improving supported by the balance sheet clear out

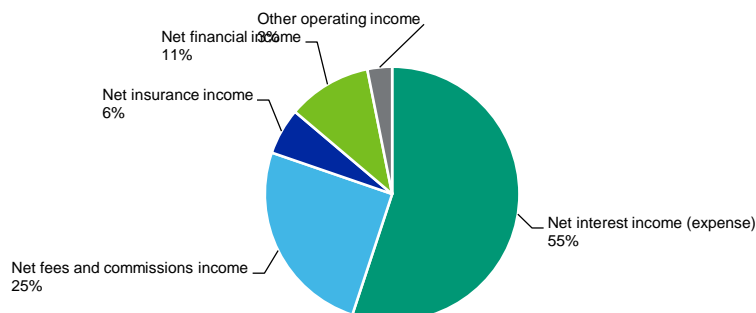


Source: Company reports, MIS

Arion's earnings benefit from a diverse revenue stream in the form of, net interest income from both retail and corporates, investment banking operations, asset management fees, and insurance and financial income through its Vördur subsidiary (see Exhibit below). The bank has actively diversified revenue stream recently through pursuing a bancassurance model with increased focus on the Vördur product offering, as well as increased digitalization to enable cross-selling and cost efficiencies. Arion bank also benefits from good cost control with a cost-to-income of 42.7% in Q1 2022, down from 44.4% in 2021 and 48.1% in 2020, reflective of a cost-conscious strategy in terms of digitalization and branch management.

Exhibit 7

#### Arion benefits from a diverse range of income streams



Arion's income mix as of 31 December 2021  
Source: Company reports, MIS

Net interest income accounted for 55% of Arion's income at end-2021, while net interest margin (NIM) stood at 2.7% and increased further to 3% in 1Q 22. We expect the net interest margin to benefit from an increasing share of mortgages being non-indexed, leading to potentially higher earnings in a higher-key-rate environment, and eased competitive pressure from pension funds. In the home market of Iceland, the Central Bank raised key policy rates by 4% since mid-2021, with the rate currently being 4.75%, in line with the Central Bank's inflation targeting policy, and further rate hikes are expected going forward. As interest rates increase competition from pension funds could re-emerge as they can offer competitive pricing in the absence of capital requirements, however, we expect a limited impact on Arion's NIM as the bank has reached critical mass on the retail market allowing it to focus on profitable growth going forward. In Q1 2022, the net interest margin strengthened to 3.1% supported by increased loan growth in the corporate market evident of the improved economic environment.

Net fee and commission income (NFCI) constituted 25% of Arion's earnings base during 2021 and is primarily driven by lending and guarantees as the bank builds on its strategy of capital velocity mainly focused on sale and syndication of corporate loans and income from its asset management business. In Q1 2022, NFCI increased by 8.4% year-on-year driven by a 21% increase in asset management fee as a result of strong market performance combined with AuM inflows amounting to 14%, albeit somewhat constrained by a weak performance in the investment banking segment where income from lending activities decreased by 10% year-on-year. There was further support to the NFCI from capital markets activities, which increased to ISK686m in Q1 2022 compared to ISK575m in Q1 2021.

Vördur's operations is a general insurance company offering both life and non-life products. Net insurance income accounted for 6% of 2021 earnings, supported by a strong performance during the year. However, during the first quarter of 2022 insurance income has decreased significantly as a result of unusually adverse weather conditions leading to a surge in claims frequency with the combined ratio increasing to 115.3% as of Q1 2022, compared to 93.2% in end-2021.

We expect the bank's profitability to be at lower levels than the 2.2% return on tangible assets reported in 2021, due to a muted earnings outlook for the insurance business for 2022 and 2023, lower financial income and return to a normalised cost of risk but still at a higher level than the historical average of 0.6%, during 2018-2020, reflective of the bank's balance sheet clear out and new strategic focus on profitable growth.



### Reliance on market funding balanced against adequate liquidity

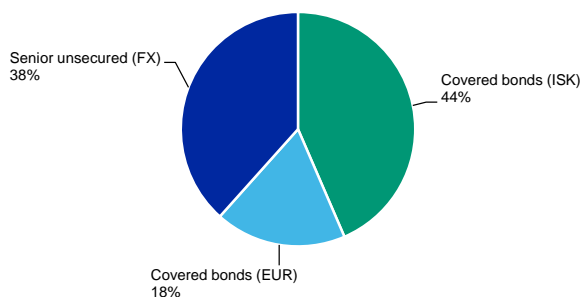
Arion's liability structure consisted of approximately 59% deposits in Q1 2022 (compared to 59% and 58% in 2021 and 2020, respectively) following a year-on-year growth in deposits of 15%. Core deposits, consisting of retail and SME deposits, have proven resilient over the years and grew by 23.3% from Q1 2021 until Q1 2022 following significant inflows as a result of pandemic-related restrictions. Going forward, inflows of deposits are expected to normalise as the effects of the pandemic lessen, however, green deposits are expected to maintain momentum in the near term, as evidenced by strong growth of 67% in the first quarter of 2022.

The bank's funding mix is balanced between senior unsecured and covered bond, as well as between FX and domestic issuances (see Exhibit below). Senior debt accounts for almost 40% of debt outstanding and all issued in foreign currency which provides access to a wider investor base. However, high reliance in foreign investors also exposes the bank to changes in investor sentiment in times of market stress. Furthermore, Arion has issued a total of ISK51.7 billion in green bonds amounting to 14% of total debt instruments, up from ISK47.7 billion as of year-end 2021, with a target of 20% of the loan book being committed to green projects by 2030.

Covered bonds account for around 60% of market funding, which we consider to be a more stable source of funding, and is primarily issued in local currency. During 2022 the bank started also issuing in the international markets, which although it provides diversification in its investor base it also increases somewhat the FX risk due to the absence of international counterparties to provide currency swaps for these issuances. FX debt issuances broadly match FX lending needs and the net position is closely monitored and managed to zero.

Exhibit 8

#### Arion's funding mix contains a diverse range of currency exposures



Source: Company reports, MIS

Our assigned market funding score reflects our view that Arion's use of market funding will increase over the next 12-18 months as deposit inflows normalise. The score further reflects Arion's good market access in international markets and their resilient core deposits, albeit offset by risks related to changes in investor sentiments.

Arion benefits from adequate liquidity, with liquid assets accounting for 18.0% tangible banking assets in December 2021. The bank further benefits from a very strong Basel III LCR ratio of 195% as of Q1 2022, (203% in 2021 and 189% in 2020), well above the regulator's minimum requirements of a total LCR and LCR in FX of 100%, and for a minimum LCR ISK of 40% (50% from January 2023). The liquid pool of assets consists mostly of cash and deposits with the central bank and government bonds.

### Source of facts and figures cited in this report

Unless noted otherwise, the bank specific figures originate from bank's reports and Moody's Banking Financial Metrics. All figures are based on our own chart of accounts and may be adjusted for analytical purposes. Please refer to the document [Financial Statement Adjustments in the Analysis of Financial Institutions](#), published on 9 August 2018.

### ESG considerations

We consider Arion Bank to have a low exposure to Environmental risks in line with how we view the banking sector. See our Environmental risks [Environmental heatmap](#) for further information.



The most relevant Social risks for banks arise when they interact with their customers. Social risks are particularly high in the area of data security and customer privacy which is partly mitigated by sizeable technology investments. Fines and reputational damage due to product mis-selling or other types of misconduct is a further social risk. Societal trends are also relevant in a number of areas, such as shifting customer preferences towards digital banking services, increasing information technology cost, aging population concerns, which is relevant to Iceland, impacting demand for financial services or socially driven policy agendas that may translate into regulation that affects banks' revenue base.

We regard the coronavirus outbreak as a social risk under our ESG framework, given substantial implications for public health and safety. Overall, we consider banks, including Arion Bank, to face moderate social risks. See our Social risks [Social heatmap](#) for further information.

Governance is highly relevant to Arion Bank's creditworthiness. Corporate governance weaknesses can lead to a deterioration in a company's credit quality, while governance strengths can benefit its credit profile. Governance risks are largely internal rather than externally driven, and for Arion Bank, we do not highlight any particular governance issue. Nonetheless, corporate governance remains a key credit consideration and requires ongoing monitoring.

## Support and structural considerations

### Loss Given Failure

The European Union's BRRD has been transposed into Icelandic law, applicable from 1 September 2020, which confirmed our current assumptions regarding the LGF analysis. We assume a residual tangible common equity of 3% and post-failure losses of 8% of tangible banking assets, a 25% run-off in junior wholesale deposits, a 5% run-off in preferred deposits, in line with our standard assumptions.

The Icelandic legislation has established full depositor preference over senior unsecured creditors. Therefore, we assign a 100% probability to deposits being preferred to senior unsecured debt.

For Arion's short-term and long-term deposit ratings and issuer ratings we have considered the likely impact on loss given failure from the combination of their own volume and the amount of debt subordinated to them. This results:

» for the deposit ratings in a Preliminary Rating Assessment of A3/Prime-2, three notches above the BCA, reflecting an extremely low loss given failure.

» for the issuer ratings in a Preliminary Rating Assessment of Baa1, two notches above the BCA, reflecting a very low loss given failure.

### Government support

Despite Arion's significant deposit market share of 27% and its systemically important status, we assume a low probability of government support for its deposit, CRA, and CRR ratings reflecting Iceland's implementation of the EU's Bank Recovery and Resolution Directive (BRRD) and the country's past track record on providing no support to the financial sector during the 2008 financial crisis.

### Counterparty Risk Ratings (CRR)

#### Arion's CR Assessment is A3(cr)/Prime-2(cr)

For Arion, the preliminary CR Assessment is three notches above the entity's baa3 Adjusted BCA, reflecting the buffer against default provided to more junior obligations represented by the CR Assessment. To determine the CR Assessment, we focus purely on subordination, taking no account of the volume of the instrument class. Finally, the bank's CR Assessment does not benefit from any government support uplift.

### Counterparty Risk (CR) Assessment

#### Arion's CRR is A3/Prime-2

The CRR, before government support, is three notches above the Adjusted BCA of baa3, reflecting a moderate loss given failure from the volume of instruments that will be subordinated to CRR liabilities. Further, Kvika's CRR does not benefit from any rating uplift based on government support, in line with our support assumptions on senior debt.

### About Moody's bank scorecard

Our Scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment is expressed. As a result, the output of our Scorecard

may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The Scorecard output and the individual scores are discussed in rating committees and may be adjusted up or down to reflect conditions specific to each rated entity.

## Rating methodology and scorecard factors

Exhibit 9

### Arion Bank

<b>Macro Factors</b>							
<b>Weighted Macro Profile</b>		<b>Strong - 100%</b>					
<b>Factor</b>	<b>Historic Ratio</b>	<b>Initial Score</b>	<b>Expected Trend</b>	<b>Assigned Score</b>	<b>Key driver #1</b>	<b>Key driver #2</b>	
Solvency							
Asset Risk							
Problem Loans / Gross Loans	2.2%	a3	↔	ba2	Single name concentration	Geographical concentration	
Capital							
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	18.4%	aa3	↔	aa3	Risk-weighted capitalisation		
Profitability							
Net Income / Tangible Assets	1.3%	a3	↓	baa2	Expected trend		
Combined Solvency Score		a2		baa1			
Liquidity							
Funding Structure							
Market Funds / Tangible Banking Assets	21.6%	baa3	↓	ba1	Market funding quality		
Liquid Resources							
Liquid Banking Assets / Tangible Banking Assets	18.0%	ba1	↔	ba1	Stock of liquid assets		
Combined Liquidity Score		baa3		ba1			
Financial Profile							
Qualitative Adjustments				Adjustment			
Business Diversification				0			
Opacity and Complexity				0			
Corporate Behavior				0			
Total Qualitative Adjustments				0			
Sovereign or Affiliate constraint							
BCA Scorecard-indicated Outcome - Range				baa1 - baa3			
Assigned BCA				baa3			
Affiliate Support notching				0			
Adjusted BCA				baa3			
<b>Instrument Class</b>	<b>Loss Given Failure notching</b>	<b>Additional notching</b>	<b>Preliminary Rating Assessment</b>	<b>Government Support notching</b>	<b>Local Currency Rating</b>	<b>Foreign Currency Rating</b>	
Counterparty Risk Rating	3	0	a3	0	A3	A3	
Counterparty Risk Assessment	3	0	a3 (cr)	0	A3(cr)		
Deposits	3	0	a3	0	A3	A3	
Senior unsecured bank debt	2	0	baa1	0	Baa1	Baa1	

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

## Ratings

Exhibit 10

Category	Moody's Rating
<b>ARION BANK</b>	
Outlook	Positive
Counterparty Risk Rating	A3/P-2
Bank Deposits	A3/P-2
Baseline Credit Assessment	baa3
Adjusted Baseline Credit Assessment	baa3
Counterparty Risk Assessment	A3(cr)/P-2(cr)
Issuer Rating	Baa1

Source: Moody's Investors Service

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