

APPLICABLE FINAL TERMS

5 January 2017

ARION BANK HF

Issue of 160,000,000 ISK Fixed Rate Covered Bonds due December 2019 under the €1,000,000,000 Covered Bond Programme

PART A – CONTRACTUAL TERMS

Terms used herein shall be deemed to be defined as such for the purposes of the Conditions set forth in the Offering Circular dated 23 December 2016 which constitutes a base prospectus for the purposes of the Prospectus Directive (Directive 2003/71/EC) (the **Prospectus Directive**). This document constitutes the Final Terms of the Covered Bonds described herein for the purposes of Article 5.4 of the Prospectus Directive and must be read in conjunction with the Offering Circular. Full information on the Issuer and the offer of the Covered Bonds is only available on the basis of the combination of these Final Terms and the Offering Circular. The Offering Circular and the Final Terms are available for viewing at Borgartún 19, 105 Reykjavík, Iceland and on the Luxembourg Stock Exchange's website at www.bourse.lu and from the registered office of the Issuer and from the specified office of the Agent in London.

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| 1. | (a) | Series Number: | 7 |
| | (b) | Tranche Number: | 2 |
| | (c) | Series which Covered Bonds will be consolidated and form a single Series with: | ISK 160,000,000 Fixed Rate Covered Bonds due December 2019 issued on 11 January 2017 |
| | (d) | Date on which the Covered Bonds will be consolidated and form a single Series with the Series specified above: | 11 January 2017 |
| 2. | | Specified Currency or Currencies: | ISK |
| 3. | | Aggregate Nominal Amount: | |
| | – | Tranche: | 160,000,000 |
| | – | Series: | 1,700,000,000 |
| 4. | | Issue Price: | 100.3232% of the Aggregate Nominal Amount |
| 5. | (a) | Specified Denominations: | ISK 20,000,000 |
| | (b) | Calculation Amount | ISK 20,000,000 |
| 6. | (a) | Issue Date: | 11 January 2017 |
| | (b) | Interest Rate: | Fixed Interest Rate |

	(c) Interest Commencement Date:	Issue Date
7.	Maturity Date:	16 December 2019
8.	Extended Final Maturity Date:	16 December 2022
		If an Extended Final Maturity Date is specified and the Final Redemption Amount is not paid in full on the Maturity Date, payment of the unpaid amount will be automatically deferred until the Extended Final Maturity Date, provided that any amount representing the Final Redemption Amount due and remaining unpaid on the Maturity Date may be paid by the Issuer on any Interest Payment Date occurring thereafter up to (and including) the relevant Extended Final Maturity Date. See Condition 8.1
9.	Interest Basis:	See paragraph 17 below
10.	Redemption/Payment Basis:	
		Subject to any purchase or cancellation or early redemption, the Covered Bonds will be redeemed on the Maturity Date at 100 per cent. of their nominal amount.
11.	Change of Interest Basis:	Not applicable
12.	Put/Call Options:	Not Applicable
13.	Date Board approval for issuance of Covered Bonds obtained:	16 November 2016
14.	Method of distribution:	Non-syndicated
15.	Name and address of the Calculation Agent	Arion Bank hf. Borgartún 19, 105 Reykjavík, Iceland

PROVISIONS RELATING TO INFLATION LINKED COVERED BONDS

16.	Inflation Linked Covered Bond Provisions	Not Applicable
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PROVISIONS RELATING TO INTEREST (IF ANY) PAYABLE

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| 17. Fixed Rate Covered Bond Provisions | Applicable |
| (a) Rate(s) of Interest: | 5.50% per annum payable semi-annually in arrear. |
| (b) Interest Payment Date(s): | 16 December and 16 June in each year up to and including the Maturity Date of the Extended Final Maturity Date as applicable |
| (c) Fixed Coupon Amount | Not Applicable |
| (d) Broken Amount(s): | Not Applicable |
| (e) Day count fraction: | 30/360 |
| (f) Determination Date(s): | Not applicable |
| 18. Floating Rate Covered Bond Provisions | Not Applicable |
| 19. Zero Coupon Covered Bond Provisions | Not Applicable |
| 20. Inflation Linked Non-Amortising Covered Bond Provisions | Not Applicable |
| (a) Rate(s) of Interest: | |
| (b) Interest Payment Date(s): | |
| (c) Base Index: | |
| (d) Day Count Fraction: | |

PROVISIONS RELATING TO REDEMPTION

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| 21. Issuer Call | Not Applicable |
| 22. Investor Put: | Not Applicable |
| 23. Final Redemption Amount of each Covered Bond | ISK 20,000,000 per Covered Bond of ISK 20,000,000 Specified Denomination |
| 24. Early Redemption Amount of each Covered Bond payable on redemption for taxation reasons: | Not applicable |
| 25. Relevant Percentage: | Not applicable |

GENERAL PROVISIONS APPLICABLE TO THE COVERED BONDS

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| 26. Form of Covered Bonds: | ISD Covered Bonds |
| | ISD Covered Bonds issued in uncertificated and dematerialised book entry form. See further item 7 of Part B below. |

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| 27. | New Global Covered Bond: | No |
| 28. | Additional Financial Centre(s): | Not Applicable |
| 29. | Talons for future Coupons or Receipts to be attached to definitive Covered Bonds in bearer form (and dates on which such Talons mature): | No. |
| 30. | Details relating to Instalment Covered Bonds; amount of each instalment, date on which each payment is to be made: | Not Applicable |
| 31. | Redenomination: | Redenomination not applicable |

DISTRIBUTION

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| 32. | (a) If syndicated, names of Managers: | Not Applicable |
| | (b) Date of Subscription Agreement: | Not Applicable |
| | (c) Stabilising Manager(s) (if any): | Not Applicable |
| 33. | If non-syndicated, name of Dealer: | Arion Bank hf. |
| 34. | U.S. Selling Restrictions: | Reg. S Category 2; TEFRA C |

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PART B – OTHER INFORMATION

- 1. LISTING AND ADMISSION TO TRADING** Application has been made by the Issuer (or on its behalf) for the Covered Bonds to be admitted to trading on the NASDAQ Iceland hf. (the Icelandic Stock Exchange) and listing on the Regulated Market of the NASDAQ Iceland hf. with effect from or prior to the first Interest Payment Date.
- Estimate of total expenses related to admission to trading: ISK 115,000
- 2. RATINGS**
- Ratings: The Covered Bonds to be issued have not been rated.
- 3. INTERESTS OF NATURAL AND LEGAL PERSONS INVOLVED IN THE ISSUE**
- Save for any fees payable to the Dealer, so far as the Issuer is aware, no person involved in the issue of the Covered Bonds has an interest material to the offer. The Dealer and its affiliates have engaged, and may in the future engage, in investment banking and/or commercial banking transactions with, and may perform other services for, the Issuer and its affiliates in the ordinary course of business.
- 4. REASONS FOR THE OFFER, ESTIMATED NET PROCEEDS AND TOTAL EXPENSES**
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| (i) Reasons for the offer | As set out in "Use of Proceeds" in the Prospectus |
| (ii) Estimated net proceeds: | ISK 160,402,120 |
| (iii) Estimated total expenses: | ISK 115,000 |
- 5. YIELD (FIXED RATE COVERED BONDS ONLY)**
- Indication of yield: 5.50 % per annum
- 6. PERFORMANCE OF FORMULA/CPI, EXPLANATION OF EFFECT ON VALUE OF INVESTMENT AND ASSOCIATED RISKS AND OTHER INFORMATION CONCERNING THE UNDERLYING (*INFLATION LINKED COVERED BONDS AND INFLATION LINKED NON AMORTISING COVERED BONDS ONLY*)** Not applicable
- 7. OPERATIONAL INFORMATION**
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| (i) ISIN Code: | IS0000028132 |
| (ii) Common Code: | Not Applicable |
| (iii) Any clearing system(s) other than Euroclear Bank S.A./N.V. and Clearstream Banking, société anonyme (together with the address of each such clearing system) and the relevant identification number(s): | Nasdaq CDS Iceland Laugavegur 182, 105 Reykjavík, Iceland. |

- (iv) Delivery: Delivery free of payment
- (v) Names and addresses of additional Paying Agent(s) (if any) or, in the case of ISD Covered Bonds, the ISD Agent: Arion Bank hf.
Borgartún 19, 105 Reykjavík, Iceland
- (vi) Deemed delivery of clearing system notices for the purposes of Condition 14 (*Notices*): Any notice delivered to Covered Bondholders through the clearing systems will be deemed to have been given on the second business day after the day on which it was given to Euroclear, and Clearstream, Luxembourg and ISD.
- (vii) Intended to be held in a manner which would allow Eurosystem eligibility: No.

Signed on behalf of the Issuer:

By: Eiríkur M. Jensen

Duly authorised signatory

