

Ladies and gentlemen,

Thank you all for taking the time to be here with us today.

Arion Bank is a universal bank which provides customers with a diverse range of financial services. The Bank occupies a strong position in all key markets, its revenue streams are diverse and the Bank is fee driven. Operations are well balanced and this results in a moderate risk profile. Digital solutions play an ever increasing role and Arion Bank is a leader in this field. Numerous new solutions were launched in 2016 and more are in the pipeline.

We have at our disposal a dedicated team of employees, a strong infrastructure and a loyal customer base. The economic environment in Iceland has improved considerably in recent years and the conditions for continued growth are excellent. Arion Bank has a strong balance sheet and surplus capital that can be paid out over time in a controlled manner. At the end of 2016, the capital ratio was 27.1% and the leverage ratio was 18%, very strong indeed.

For us here at Arion Bank the year 2016 differed from previous years in many respects, not least to 2015 which was characterized by the divestment of acquired assets and which was one of the most profitable years in the Bank's history – a true landmark year. By selling the Bank's largest remaining assets in unrelated businesses, the Bank drew a line under the chapter relating to its legacy assets.

The year 2016 on the other hand was all about optimism for the future and investments in the tasks which matter most to the future development of the Bank as a universal financial institution. During the year Arion Bank's acquisition of the insurance company Vördur, one of Iceland's most popular insurers, was completed. The company has over 12% of the market share in non-life insurance in Iceland and will be an excellent addition to Arion Bank's range of products.

In the spring of 2016 Arion Bank opened a new branch at Keflavík International Airport and is the only bank with a presence at the airport. We see this as a great opportunity to provide first-class services to the huge number of tourists passing through Iceland. Our subsidiary Valitor continued to invest in its Danish and UK operations.

The Bank also invested heavily in digital solutions and it's fair to say that Arion Bank is at the forefront in this field in Iceland. Digital channels play a key role in Arion Bank's future vision. Approximately 70% of Arion Bank customers use online banking services and 35% are active users of the Arion app. The number of app users increased by 30% in 2016. The Bank launched five new digital solutions in 2016 and continued in the same vein at the beginning of 2017.

New digital solutions that have been launched include payment plans for credit cards which can be set up in just a few seconds using the app. Customers can also get a confirmed credit appraisal for buying a house in just a few minutes online and can finalize an application to get a mortgage. All the necessary documentation is obtained digitally and signatures are made using eID.

Our goal is to make our services even better and more convenient for our customers. We can see that these innovations are proving popular, with more than twice as many customers obtaining a credit appraisal in February 2017 than in February 2016.

So, in the year 2016 we invested in the future which we feel is full of opportunities and promise.

Arion Bank has led the way in Iceland by actively seeking funding on the international credit markets and 2016 was no exception. The Bank issued bonds in euros to a broad group of investors on two occasions during the year. At the beginning of 2017 the Bank tapped the second issue, bringing the issue to 500 million euros. The Bank's terms on this market have improved markedly recently, clear testament to the growing confidence of bond investors in the Bank and the Icelandic economy. The progress made by the Bank and the improved performance of the Icelandic economy, as well as the vital steps towards lifting the capital controls all have a lot to say in this regard. These factors led Standard & Poor's to upgrade the Bank's credit rating from BBB- to BBB during the year, with positive outlook.

In 2016 the board of directors of Arion Bank adopted a new policy on sustainable banking. One of the objectives is to increase the number of non-financial goals and key performance indicators. The strategy also calls for more prominence to sustainability in the Bank's reporting. The first steps in this direction are being taken in this year's annual report, now available on-line. This is a response to the UN Global Compact and also the guidelines made by the World Federation of Exchanges which set out which information listed companies should highlight in their reporting. Arion Bank has collaborated closely on this with the Icelandic innovation company Klappir. In 2017 the Bank will continue the implementation of its new strategy on sustainability.

In recent years the Bank's infrastructure and internal controls have been reinforced and the Bank has been recognized for good corporate governance. The Bank holds training programmes for employees to ensure that people are familiar with the legislation and regulations which apply to our business. In 2016 a special campaign was launched at the Bank, raising employees' awareness of their roles in risk management and internal controls at the Bank. This effort will continue in 2017. Each and every employee has an important role to play in this respect, no less than the board and the management. It is imperative that we do the right things and that we do them right.

A central component of Arion Bank's strategy and business model is to offer its customers a wide range of financial services – to be a universal bank. Crucial in this respect is to offer investment banking services. Unfortunately there is still talk in Iceland of separating retail and investment banking.

The type of investment activity which we saw conducted by the banks in the years leading up to the financial crisis means that investment banking is considered a risk-seeking industry in Iceland. It is important to remember that the situation with regard to giant international European and US banks is hardly applicable to Icelandic banks which are actually very small in comparison. We also need to consider that since the financial crisis, sweeping changes have been made to legislation and supervision in Iceland – which renders the need for separation essentially unnecessary. The main concerns have already been addressed and the risks averted. Any debate on the separation of activities has to be measured, informed, free of prejudice and based on the available facts.

It became clear in 2016 that Icelandic banks would still be expected to pay a tax which is not imposed on other Icelandic sectors or international banks. I am referring here to the so-called bank levy, which is charged on the liabilities of financial institutions. This is a specific tax which makes it difficult for banks to compete, both on the domestic mortgage market and with international banks when funding Iceland's largest companies.

Naturally the banks have to fund the bank levy by having a higher interest margin, higher commission income or reducing expenses. As a result the bank levy

unfortunately increases costs for customers of the banks and it pushes up interest rates in Iceland. The effects have been limited so far since the levy was only supposed to be a temporary measure. The arguments for extending the bank levy are weak. It is important that this form of taxation be reviewed.

The ownership of Arion Bank is well known to all present here today. Kaupthing ehf, owns 87% through its subsidiary Kaupskil ehf; and the Icelandic government, owns the remaining 13% through the Icelandic State Financial Investments. As stated in an announcement from Kaupthing and Arion Bank in June 2016, the possibilities regarding Kaupthing's ownership of Arion Bank are being appraised. An IPO is one of the options, although it should be stressed that no decision has been taken on timing or how this would be carried out.

It has been clear from the outset that the current ownership structure was not a long-term arrangement and it will be interesting to see how things develop in 2017. It is clearly very important that this is done successfully, not only for the Bank but also for the Icelandic financial system as a whole.

Arion Bank has adhered to the strategy adopted by the board of directors in 2010. This strategy builds on the relationship banking model and the desire to offer customers comprehensive financial services. Our subsidiaries play a vital role in this regard. These include Iceland's foremost payment services and asset

management companies, as well as the insurance company Vördur which is a key addition to the Bank's product offering.

Arion Bank is today financially robust and occupies a strong position on its chosen markets. The year 2016 was a positive year in which important steps were taken towards consolidating the Bank's future.

I would like to thank the management and our employees for their outstanding contribution to what we have accomplished.

Thank you.

*Monica Caneman*

*Chairman of the Board of Directors of Arion Bank*