

Earnings Press Release, 5 May 2021

Arion Bank's Q1 2021 financial results

- Arion Bank reports net earnings of ISK 6,039 million in Q1 2021
- The results represent a significant improvement from Q1 2020 and are better than could be expected in the challenging economic environment
- Return on equity in Q1 was 12.5%, compared with a negative 4.6% in Q1 2020
- Net interest margin was 2.7% in a low interest rate environment, compared with 2.8% in Q1 2020
- Core revenues increased by 4.2%, compared with Q1 2020
- The Bank's total assets increased by 0.7% from year-end 2020, with mortgage lending up 3.7%
- Considerable activity on the corporate lending side albeit a small reduction in the Bank's corporate loan book due to the syndication and sale of corporate loan exposures to institutional investors
- Dividend payment and share buy-backs amounted to ISK 14.8 billion
- The Bank's capital ratio was 26.9% and the CET1 ratio was 22.4%
- The Bank is very well positioned to distribute capital and meet funding requirements of our customers

Arion Bank reported net earnings of ISK 6,039 million in the first quarter with 12.5% return on equity. Return on equity, assuming 17% CET1 ratio, was 16.0% for the quarter.

Total assets amounted to ISK 1,181 billion at the end of the period, compared with ISK 1,173 billion at the end of 2020. Loans to customers increased by 1.7%, primarily mortgage lending, but there was a slight decrease in liquid assets, partially due to share buy-backs and dividend payments during the quarter. On the liability side deposits increased by 4.2%. Total equity amounted to ISK 189 billion at the end of the period. Total equity increased due to the reported net earnings but decreased by ISK 14.8 billion due to dividend paid and the share buy-backs.

The Bank's capital ratio was 26.9% and the CET1 ratio was 22.4% at the end of March 2021, assuming 50% dividend payments of net earnings in line with the dividend policy, and outstanding buy-back of ISK 3 billion, compared with 27.0% and 22.3% respectively at year end 2020. The Group's capital ratio, as calculated under the Financial Undertakings Act No. 161/2002, was 26.5% and the CET1 ratio was 22.0%. The Bank's capital ratios comfortably exceed the requirements set by law and the Financial Supervisory Authority of the Central Bank.

Benedikt Gíslason, CEO of Arion Bank

"We are pleased with the Bank's performance in the first quarter. All our key financial targets were met and we believe we have successfully navigated the Bank through the challenging conditions created by the global pandemic. Core revenues, i.e. net interest income, net commission income and net insurance income increased by more than 4% year-over-year. We have also managed to further reduce costs. Impairments and financial income improved substantially between years, since there was great uncertainty surrounding the first quarter results in 2020. Although the route out of the pandemic is still far from clear, there is cause for optimism now that a successful vaccination program is being rolled out, both in Iceland and in many of the countries vital for the tourist industry. We are happy to see so many of our customers getting ready for better times ahead.

A key focus in recent years has been to make banking more convenient for our customers, offering user-friendly digital solutions to make complex actions straightforward. One of our latest products allows people to access their pensions in the Arion app. This solution recently won an award at the annual Icelandic Web Awards for its ability to gather complex information from numerous sources and present it in a way that people can easily understand. We are immensely proud of this achievement as we think it is vital that people fully understand their pensions – both young people who are just starting to save for the future and older people approaching retirement age.

There have been significant changes among the shareholders so far this year. The major international shareholders who participated in the Bank's IPO three years ago have largely sold their stakes and been replaced by Icelandic investors. Today the Bank has more than 8,000 shareholders, with Icelandic shareholders holding approximately 90% of share capital. Pensions funds own almost 50% of the Bank and other domestic investors hold around 40%. Interestingly, although international shareholders only own around 10% in the Bank, they number around 5,000 and are therefore the majority of shareholders in terms of numbers."



Income Statement

<i>In ISK millions</i>	Q1 2021	Q1 2020	Δ	Δ %
Net interest income	7,342	7,253	89	1%
Net commission income	3,277	3,076	201	7%
Net insurance income	671	501	170	34%
Net financial income (loss)	1,500	(2,000)	3,500	-
Other operating income	307	146	161	110%
Operating income	13,097	8,976	4,121	46%
Salaries and related expenses	(3,271)	(3,130)	(141)	5%
Other operating expenses	(2,777)	(3,077)	300	(10%)
Operating expenses	(6,048)	(6,207)	159	(3%)
Bank levy	(330)	(331)	1	(0%)
Net impairment	1,080	(2,860)	3,940	-
Net earnings (loss) before income tax	7,799	(422)	8,221	-
Income tax expense	(1,866)	(860)	(1,006)	117%
Net earnings (loss) from cont. operations	5,933	(1,282)	7,215	-
Discontinued operations, net of tax	106	(889)	995	-
Net earnings (loss)	6,039	(2,171)	8,210	-
KFI's				
Return on equity (ROE)	12.5%	(4.6%)		
Return on equity, continuing operations	12.3%	(2.7%)		
Return on equity assuming 17% CET 1	16.0%	(6.1%)		
Return on total assets (ROA)	2.1%	(0.8%)		
Earnings per share (in ISK)	3.61	(1.25)		
Cost to income ratio (C/I)	46.2%	69.2%		
Net interest margin (NIM)	2.7%	2.8%		
Operating income / REA	7.0%	5.0%		

Net interest income increased slightly, compared with the first quarter of 2020. The net interest margin (NIM) as a percentage of average interest-bearing assets was 2.7% during the quarter, compared with 2.8% for the same period in 2020. The Bank aims to maintain NIM in the range of 2.6% - 2.8%, whilst the base rate remains at current levels. The loan book increased from same period in 2020, mainly mortgage lending, but the lower interest rate environment is weighing in on the net interest income.

Net commission income increased by 7%, compared with the first quarter of 2020. Corporate Finance had a very robust quarter as M&A activities have returned. The forming of CIB from the previously separate Corporate Banking and Investment Banking divisions has been successful and is supporting the business on both sides. Income from lending and guarantees continues to be strong, supported by an increased focus on capital velocity as opposed to loan growth, whereas volume-related fees, which are expected to grow again, have decreased due to the pandemic.

Insurance premiums earned at the insurance company Vördur have been increasing, but volatility in *net insurance income* is mainly due to seasonal fluctuations in the claim rate. The combined ratio for the first quarter of 2021 was 98.5%, compared with 103.5% for the same period in 2020, and is highly competitive in the domestic market.

Net financial income was very strong with a profit of ISK 1,500 million, compared with a significant loss in the first quarter of 2020. Equity holdings performed well during the quarter due to favorable market conditions and active management.

Other operating income increased in the first quarter of 2021, compared with the same period in 2020. Profit from the sale of assets was the main source of income in both quarters.

Operating expenses decreased by 3% compared with the first quarter of 2020. Salaries and related expenses increased slightly, whereas other operating expenses decreased by 10%. At the end of March the number of full-time equivalent positions (FTEs) was 772 at the Group and 641 at the Bank, a 5% decrease at Group level, compared with the same period in prior year. Other operating expenses have been trending down, partly due to Covid-19, except for IT expenses which have increased. With the new Sopra core banking system now operational the Bank has opportunities to rationalize.

Net impairment is positive in the first quarter of 2021 as the Bank is reversing a part of its impairments. Previously impaired loans have been partially recovered, either through payments or due to an increase in collateral value. IFRS models remain unchanged as the expectation is that the worst is behind us in terms of the economy. Uncertainty does though persist regarding the valuation of assets due to the pandemic.

Income tax, as reported in the financial statements, comprises 20% income tax on earnings and a special 6% financial tax on the earnings of financial undertakings of more than ISK 1 billion. The effective income tax rate was 23.9% for the first quarter, compared with a negative effective income tax rate in the first quarter of 2020, due to a



significant loss from equity holdings. In general, the combination of income is the main driver behind the fluctuation in the effective tax rate.

Discontinued operations held for sale comprise the operating results of the subsidiary Valitor hf. and valuation changes of the underlying assets of the subsidiaries Stakksberg ehf. and Sólbjarg ehf.

Balance sheet

The balance sheet increased by 1% from year-end 2020. The liquidity position remains very strong despite ISK 14.8 million capital distribution through dividends and the buy-back of own shares.

Assets

<i>In ISK millions</i>	31.03.2021	31.12.2020	Δ	Δ %	31.03.2020	Δ	Δ %
Cash & balances w ith CB	60,479	42,136	18,343	44%	118,174	(57,695)	(49%)
Loans to credit institutions	29,251	28,235	1,016	4%	33,797	(4,546)	(13%)
Loans to customers	837,162	822,941	14,221	2%	778,823	58,339	7%
Financial assets	197,216	227,251	(30,035)	(13%)	192,056	5,160	3%
Intangible assets	9,892	9,689	203	2%	8,826	1,066	12%
Assets and disposal groups HFS	16,271	16,811	(540)	(3%)	28,038	(11,767)	(42%)
Other assets	30,822	25,643	5,179	20%	28,106	2,716	10%
Total assets	1,181,093	1,172,706	8,387	1%	1,187,820	(6,727)	(1%)

KFI's

REA / Total assets	63.9%	63.6%	60.0%
Share of stage 3 loans, gross	2.9%	2.6%	2.9%

Loans to customers increased by 1.7% from the end of 2020, with mortgage lending increasing by 3.7%. Corporate lending is at a similar level to year-end 2020, with slight loan growth which is offset by the lower ISK value of FX loans, due to a stronger ISK. Lending activities remained robust during the quarter with significant sales of corporate credit exposures to institutional investors taking place. The loan book continues to be well balanced between individuals and corporates. Loans to individuals increased by 3.2% during the first quarter, with mortgages driving the growth with a 19% increase compared with the end of first quarter 2020. The importance of index-linked lending has been reduced as the indexation imbalance decreased by ISK 38 billion, or 53%, in one year.

Arion Bank has been supporting its customers and worked with the Icelandic authorities to develop government guaranteed loan facilities targeted at corporates that are going through temporary difficulties. At the end of March 1.67% of individual loans (by amount), predominantly mortgages, and 5.77% of corporate loans were in payment moratorium. At the end of March the Bank had made more than 338 loans with a government guarantee, amounting to ISK 4.2 billion.

The Bank's liquidity position is very strong with total LCR ratio at 192% and ISK LCR ratio at 153%. This is reflected in the strong position in *Cash and balances with Central Bank*, *Loans to credit institutions* and *Financial assets*, including bonds and debt instruments.

Assets and disposal groups held for sale comprise the subsidiaries Valitor ehf., Stakksberg ehf. and Sólbjarg ehf.

Liabilities and equity

<i>In ISK millions</i>	31.03.2021	31.12.2020	Δ	Δ %	31.03.2020	Δ	Δ %
Due to credit institutions & CB	9,525	13,031	(3,506)	(27%)	8,323	1,202	14%
Deposits from customers	592,540	568,424	24,116	4%	539,312	53,228	10%
Other liabilities	52,823	42,217	10,606	25%	75,142	(22,319)	(30%)
Borrowings	293,747	298,947	(5,200)	(2%)	322,470	(28,723)	(9%)
Subordinated liabilities	34,632	36,060	(1,428)	(4%)	35,837	(1,205)	(3%)
Liabilities associated w /disposal groups HFS	8,407	16,182	(7,775)	(48%)	22,857	(14,450)	(63%)
Total liabilities	991,674	974,861	16,813	2%	1,003,941	(12,267)	(1%)
Shareholders equity	189,245	197,672	(8,427)	(4%)	183,702	5,543	3%
Non-controlling interest	174	173	1	1%	177	(3)	(2%)
Total equity	189,419	197,845	(8,426)	(4%)	183,879	5,540	3%
Total liabilities and equity	1,181,093	1,172,706	8,387	1%	1,187,820	(6,727)	(1%)

KFI's

Loans to Deposits ratio	141.3%	144.8%	144.4%
CET1 ratio	22.4%	22.3%	22.5%
Capital adequacy ratio	26.9%	27.0%	27.5%

Deposits from customers remain the most important source of funding for Arion Bank and a greater focus on deposit funding has resulted in a significant increase. The increase is in all the main classes i.e. from individuals, corporates and public entities.



The decrease in *borrowings* from the end of 2020 is primarily due to the strengthening of the ISK against foreign currencies. There are limited refinancing needs over the next few quarters but the remaining EUR 200 million maturity in Q4 2021 is the next foreseeable target.

Shareholders' equity decreased due to the dividend payment and purchase of own shares, in total ISK 14.8 billion, which is partly offset by the financial results for the period. In February 2021 the Board of Directors authorized the Bank to launch a share buy-back program for up to ISK 15 billion at market value. At the end of March ISK 3 billion were outstanding. The buy-back program concluded on 15 April. The leverage ratio was 14.7% at the end of March, compared with 15.1% at the end of 2020, which is very high in international comparison. At the end of the period the Group had ISK 67 billion of CET1 capital in excess of regulatory requirements and ISK 41 billion in excess of the Group's target CET1 ratio of 17%, in addition to the foreseeable ISK 6 billion equity reduction.

For further information on the accounts please visit Arion Bank's [website](#).

Financial targets

Return on Equity	Exceed 10%
Revenues / RWA's	Exceed 6.7%
Cost to Income Ratio	Reduce to 45%
Loan growth	The loan book will grow in line with economic growth, with growth in mortgage lending expected to outpace corporate lending.
CET 1 Ratio	Reduce to 17%
Dividend policy / Share buy-back	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 buffer.

Investor webcast on 6 May at 10:30 CET (8:30 GMT)

Arion Bank will be hosting a webcast on Thursday 6 May at 10:30 CET (8:30 GMT) where CEO Benedikt Gíslason, CFO Stefán Pétursson, Deputy CFO Eggert Teitsson and Head of Investor Relations Theodór Fridbertsson will present the results and answer questions from participants. The webcast will take place in English and will be streamed live.

The webcast will be accessible live on financialhearings.com and a link will also be made available on the Bank's website under [Investor Relations](#).

To participate in the webcast via telephone and ask questions please call in using the relevant number indicated below before the start of the webcast:

Sweden	+46 850 558 368
UK	+44 333 300 9034
USA	+1 833 526 8396
Iceland	+354 800 7520

For further information please contact Theodór Fridbertsson, [Head of IR](#), tel.+354 856 6760, and for media enquiries Haraldur Gudni Eidsson, [Head of Corporate Communications](#), tel. +354 856 7108.

Financial calendar

The Bank's Financial Statements are scheduled for publication as stated below. The calendar may be subject to change.

Q2 2021 Financial results	28 July 2021
Q3 2021 Financial results	27 October 2021
Q4 / 12M 2021 Financial results	9 February 2022
AGM 2022	16 March 2022

This is information that Arion Bank hf. is obliged to make public pursuant to the EU Market Abuse Regulation. The information was submitted for publication through the agency of the contact persons set out above.

Forward-looking statements

This release contains forward-looking statements that reflect management's current views with respect to certain future events and potential financial performance. The information in the release is based on company data available at the time of the release. Although Arion Bank believes that the expectations reflected in such forward-looking statements are reasonable, no assurance can be given that such expectations will prove to have been correct. Accordingly, results could differ materially from those set out in the forward-looking statements as a result of various factors. The most important factors that may cause such a difference for Arion Bank include, but are not limited to: a) the macroeconomic development, b) change in inflation, interest rate and foreign exchange rate levels, c) change in the competitive environment and d) change in the regulatory environment and other government actions. This release does not imply that Arion Bank has undertaken to revise any forward-looking statements, beyond what is required by applicable law or applicable stock exchange regulations if and when circumstances arise that will lead to changes after the date when this release was made. Arion Bank assumes no responsibility or liability for any reliance on any of the information contained herein. It is prohibited to distribute or publish any information in this release without Arion Bank's prior written consent.