Earnings Press Release, 26 October 2022

Arion Bank's Q3 2022 financial results

- Arion Bank reports net earnings of ISK 4,863m in Q3, compared with ISK 8,238m in Q3 2021
- Return on equity in Q3 was 10.5%, compared with 17.0% in Q3 2021
- Earnings per share in ISK of 3.26 in Q3, compared with 5.23 in Q3 2021
- Net interest margin of 3.2%, compared with 2.7% in Q3 2021
- Core income increased by 19.2% compared with Q3 2021
- Challenging market conditions impact financial income in the quarter
- Cost-to-income ratio in Q3 was 41.8%, compared with 37.5% in Q3 2021
- The Bank's total capital ratio was 23.1% and the CET1 ratio was 19.3% on 30 September 2022

Arion Bank reported net earnings of ISK 4,863m in the third quarter and ISK 20,393m during the first nine months of the year. Return on equity was 10.5% for the quarter and 14.8% for the first nine months.

Total assets amounted to ISK 1,428bn at the end of the period, compared with ISK 1,314bn at the end of 2021. Loans to customers increased by 11.6% from year-end 2021. The increase was 15.6% in corporate lending and 8.5% in loans to individuals. Total equity amounted to ISK 186bn at period end. Total equity decreased from year-end due to a capital release of ISK 28.9bn which was partly offset by net earnings for the period.

The Bank's total capital adequacy ratio was 23.1%, and the CET1 ratio was 19.3% at the end of September. The ratios are determined on the basis of the unaudited net earnings in the quarter, with a deduction of 50% of net earnings as foreseeable dividends in line with the Bank's dividend policy and foreseeable buybacks of ISK 2.8 billion. The Group's capital ratio, as calculated under the Financial Undertakings Act No. 161/2002, was 22.8% and the CET1 ratio was 19.0%. These ratios comfortably exceed the requirements made by the Financial Supervisory Authority of the Central Bank of Iceland (FSA) and Icelandic law.

Benedikt Gíslason, CEO of Arion Bank

"We are quite pleased with the Bank's financial results for the third quarter. Core income increased by 19% between years and the trajectory is generally very positive throughout our business. The challenging securities markets over the past few months have, however, impacted the Group's financial income during the quarter. The Bank remains strongly capitalized and a ISK 5 billion share buyback program is currently underway, and the regulatory authorities have approved the repurchase of a further ISK 5 billion. All in all, we are well on the way towards achieving our financial goals this year.

Our capital markets and asset management businesses are performing strongly despite market turbulence. In terms of turnover on Nasdaq Iceland, Arion Bank's brokerage had the highest market share in both equities and fixed income during the first nine months of the year.

The Bank's funding position is excellent following a €300 million senior issuance in September. This funding was partly used to pay off loans maturing next year. As a result, the Bank has a light maturity profile through to the end of next year. The Bank's liquidity position is also robust and allows us to utilize opportunities in terms of capital and balance sheet management.

In many respects Iceland is in an enviable position at the moment, particularly compared to many of our neighbours. Following Russia's invasion of Ukraine, many of Iceland's neighbouring countries are dealing with high inflation, not least as a consequence of rising energy prices. We are fortunate to have our geothermal energy and hydropower, both sustainable resources, and this has proven invaluable to us. In addition to lower inflation, there are a lot of positives in our environment and we expect solid GDP growth this year and low unemployment. We can therefore afford to be reasonably optimistic about our environment this coming winter."

Income Statement

In ISK millions	Q3 2022	Q3 2021	Δ	Δ %	9M 2022	9M 2021	Δ	Δ %
Net interest income	10,421	7,937	2,484	31%	29,753	23,295	6,458	28%
Net commission income	4,002	3,755	247	7%	12,093	10,594	1,499	14%
Net insurance income	690	992	(302)	(30%)	1,781	2,577	(796)	(31%)
Net financial income	(1,332)	1,366	(2,698)	-	(3,252)	5,069	(8,321)	(164%)
Other operating income	103	840	(737)	(88%)	1,283	1,456	(173)	(12%)
Operating income	**13,884**	**14,890**	**(1,006)**	**(7%)**	**41,658**	**42,991**	**(1,333)**	**(3%)**
Salaries and related expenses	(3,100)	(2,899)	(201)	7%	(10,483)	(9,745)	(738)	8%
Other operating expenses	(2,710)	(2,689)	(21)	1%	(8,177)	(8,263)	86	(1%)
Operating expenses	**(5,810)**	**(5,588)**	**(222)**	**4%**	**(18,660)**	**(18,008)**	**(652)**	**4%**
Bank levy	(444)	(486)	42	(9%)	(1,253)	(1,171)	(82)	7%
Net impairment	42	718	(676)	(94%)	(267)	2,610	(2,877)	-
Net earnings before income tax	**7,672**	**9,534**	**(1,862)**	**(20%)**	**21,478**	**26,422**	**(4,944)**	**(19%)**
Income tax expense	(2,803)	(1,920)	(883)	46%	(7,994)	(5,194)	(2,800)	54%
Net earnings from cont. operations	**4,869**	**7,614**	**(2,745)**	**(36%)**	**13,484**	**21,228**	**(7,744)**	**(36%)**
Discontinued operations, net of tax	(6)	624	(630)	-	6,909	865	6,044	-
Net earnings	**4,863**	**8,238**	**(3,375)**	**(41%)**	**20,393**	**22,093**	**(1,700)**	**(8%)**

KFI's	Q3 2022	Q3 2021	9M 2022	9M 2021
Return on equity (ROE)	10.5%	17.0%	14.8%	15.2%
Return on total assets (ROA)	1.4%	2.6%	2.0%	2.4%
Earnings per share (in ISK)	3.26	5.23	13.60	13.68
Cost to income ratio (C/I)	41.8%	37.5%	44.8%	41.9%
Net interest margin (NIM)	3.2%	2.7%	3.1%	2.7%
Operating income / REA	6.4%	7.8%	6.5%	7.6%

Net interest income increased by 31.3%, compared with the third quarter of 2021. The net interest margin (NIM) as a percentage of average interest-bearing assets was 3.2% during the quarter, compared with 2.7% for the third quarter of 2021. The main reason for this sharp increase is the higher base rate, growth in loan book and a change in funding composition. Interest-bearing assets increased by 11.5% compared with the third quarter of 2021, mainly loans to customers, while interest-bearing liabilities increased by 13.7% for the same period, mainly deposits.

Net commission income increased by 6.6%, compared with the third quarter of 2021. Diversification in the fee based operation is a strength, with seasonally lower fee income in corporate finance and corporate lending but higher income from cards. There is robust income from asset management against a challenging market backdrop and a net AuM inflow. The Bank also ranks number one both in bond and equity trading in the Icelandic market during the first nine months 2022.

Insurance premiums earned at the insurance company Vördur have been increasing, but volatility in *net insurance income* is mainly due to an unusually high claims ratio, partially due to difficult weather conditions in Iceland. Insurance premiums for own account increased by 10.4% from the same period in the previous year, whereas claims for own account increased by 27.9%. The combined ratio for the third quarter of 2022 was 96.1%, compared with 85.5% for the same period in 2021. For the first nine months the combined ratio was 99.5%, compared with 91.7% for the first nine months of 2021.

Net financial income was negative by ISK 1.3bn for the quarter due to difficult market conditions, mainly driven by losses in equity holdings at the Bank and Vördur.

Operating expenses increased by 4.0% in the third quarter, compared with the third quarter of 2021. At the end of September, the number of full-time equivalent positions (FTEs) was 777. Salary expenses increased, compared with the third quarter of 2021, mainly due to the insourcing of IT operations and general wage increases. Other operating expenses remain relatively stable.

Net impairment was positive by ISK 42m in the third quarter of 2022, mainly due to the recovery of loans previously written off. Impairments are lower than through the cycle expectations, estimated at 20-25bps of the loan book on an annualized basis. The Bank has, however, changed its outlook in the IFRS9 impairment models, with more uncertainty in the global economic environment.

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 1bn. The effective income tax rate was unusually high for the quarter. In general, the combination of income is the main driver behind the fluctuation in the effective tax rate.

Balance sheet

The balance sheet increased by 8.7% from year-end 2021. The liquidity position remains very strong despite ISK 28.9bn capital distribution through dividends and buybacks of own shares during the first nine months and ISK 108.9bn increase in loans to customers.

Assets

In ISK millions	**30.09.2022**	**31.12.2021**	**Δ**	**Δ %**	**30.06.2022**	**Δ**	**Δ %**
Cash & balances with CB	68,149	69,057	(908)	(1%)	78,011	(9,862)	(13%)
Loans to credit institutions	52,643	30,272	22,371	74%	40,195	12,448	31%
Loans to customers	1,045,152	936,237	108,915	12%	1,010,666	34,486	3%
Financial instruments	223,142	225,657	(2,515)	(1%)	203,740	19,402	10%
Intangible assets	8,816	9,463	(647)	(7%)	9,038	(222)	(2%)
Assets and disposal groups HFS	2,152	16,047	(13,895)	(87%)	2,126	26	1%
Other assets	27,832	27,131	701	3%	39,585	(11,753)	(30%)
Total assets	**1,427,886**	**1,313,864**	**114,022**	**9%**	**1,383,361**	**44,525**	**3%**

KFI's							
REA / Total assets	60.8%	61.9%			62.1%		
Share of stage 3 loans, gross	1.4%	1.9%			2.6%		

Loans to customers increased by 11.6% from the end of 2021, with loans to corporates increasing by 15.6%, whereas loans to individuals increased by 8.5%. The medium-term growth outlook going forward is expected to be relatively balanced between corporates and individuals, while this will fluctuate between quarters. There continues to be a strong pipeline, especially on the corporate side in origination and syndications. Sales of loans are progressing well as the Bank follows the strategy of increasing capital velocity. In 2022 the Bank has sold corporate loans for ISK 19bn and further syndication is in process.

The Bank's liquidity position is very strong with the total LCR ratio at 189% and the ISK LCR ratio at 141%. 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 Stakksberg ehf. and Sólbjarg ehf., following the conclusion of sale of Valitor in Q2.

Liabilities and equity

In ISK millions	**30.09.2022**	**31.12.2021**	**Δ**	**Δ %**	**30.06.2022**	**Δ**	**Δ %**
Due to credit institutions & CB	5,099	5,000	99	2%	4,604	495	11%
Deposits from customers	739,969	655,476	84,493	13%	726,948	13,021	2%
Other liabilities	85,902	50,131	35,771	71%	71,731	14,171	20%
Borrowings	376,540	356,637	19,903	6%	363,375	13,165	4%
Subordinated liabilities	34,089	35,088	(999)	(3%)	33,392	697	2%
Liabilities associated w/disposal groups HFS	0	16,934	(16,934)	-	0	0	-
Total liabilities	**1,241,599**	**1,119,266**	**122,333**	**11%**	**1,200,050**	**41,549**	**3%**
Shareholders equity	185,607	193,925	(8,318)	(4%)	182,625	2,982	2%
Non-controlling interest	680	673	7	1%	686	(6)	(1%)
Total equity	**186,287**	**194,598**	**(8,311)**	**(4%)**	**183,311**	**2,976**	**2%**
Total liabilities and equity	**1,427,886**	**1,313,864**	**114,022**	**9%**	**1,383,361**	**44,525**	**3%**

KFI's							
Loans to Deposits ratio	141.2%	142.8%			139.0%		
CET1 ratio	19.3%	19.6%			19.7%		
Capital adequacy ratio	23.1%	23.8%			23.5%		

Deposits from customers remain the most important source of funding for Arion Bank, with 60% of total liabilities in deposits. The increase from year-end 2021 is mainly in SMEs but also in deposits from individuals and institutional investors.

The increase in *borrowings* from year-end 2021 is mainly due to the Bank's issuance in the domestic market of ISK 18bn and issuance for the equivalent of ISK 81bn in EUR, NOK and SEK, which is partly offset by payment maturities and prepayments during the first nine months.

Shareholders' equity decreased due to dividend payments and the purchase of own shares, in total ISK 28.9bn, which is partly offset by the net earnings for the first nine months of ISK 20.4bn. The leverage ratio was 12.0% at the end of September, compared with 12.7% at the end of 2021, which is very high in international comparison. At the end of September, the Group had ISK 9.2bn to ISK 17.9bn in excess of the Group's target capital structure of 150-250 bps management buffer or approximately 17.2-18.2% based on current capital requirement.

For further information on the accounts please visit Arion Bank's website.

Medium-term financial targets

Return on equity	Exceed 13%
Operating income / REA	Exceed 7.3%
Insurance premium growth	Premium growth (net of reinsurance) to exceed the growth of the domestic market by more than 3 percentage points
Loan growth	In line with nominal economic growth
Cost-to-income ratio	Below 45%
CET1 ratio	150-250 bps management buffer approx 17.2-18.2% based on current capital requirement
Dividend payout ratio	50%

Investor meeting / webcast in English on 27 October at 10:30 CEST / 9:30 BST / 8:30 GMT

Arion Bank will be hosting a meeting / webcast at the Bank's headquarters in Borgartún 19, Reykjavík, on Thursday 27 October at 10:30 CEST / 9:30 BST / 8:30 GMT where CEO Benedikt Gíslason and CFO Ólafur Hrafn Höskuldsson will present the results and Chief Economist Erna Björg Sverrisdóttir will give an update on the economic environment. The meeting will take place in English and will be streamed live.

The webcast will be accessible live on financialhearings.com and a link is also available on the Bank's website under Investor Relations.

Participants attending virtually will be able to ask questions during the meeting through a message board, located below the video feed. Answers will be provided by presenters at the end of the webcast.

For any further information please contact Theodór Fridbertsson, Head of IR, tel.+354 856 6760, or Haraldur Gudni Eidsson, Head of Corporate Communications, tel. +354 856 7108.

Financial calendar

Arion Bank's financial calendar is available on the Bank's website.

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.