Íslandsbanki

# Condensed Consolidated Interim Financial Statements

Third quarter 2021

Unaudited

# Contents

# Factsheet 3Q21

Íslandsbanki

## Our profile

With a history that dates from 1875, Íslandsbanki is an Icelandic universal bank with a strong customer focus. The Bank believes in moving Iceland forward by empowering its customers to succeed – reflecting a commitment to run a solid business that is a force for good in society.

Driven by the ambition to be #1 for service, Íslandsbanki's banking model is led by three business divisions that build and manage relationships with its customers. Íslandsbanki maintains a strong market share with the most efficient branch network in the country, supporting at the same time its customers' move to more digital services.

The Bank operates in a highly attractive market and, with its technically strong foundations and robust balance sheet, is well positioned for the opportunities that lie ahead.

Íslandsbanki has a BBB/A-2 rating from S&P Global Ratings.

The Bank's shares are listed on the Nasdaq Iceland Main Market.

## The Bank

**12** branches

**730** number of FTEs at Íslandsbanki at period end

## Sustainability 3Q21

Íslandsbanki became a supporter of Grænvangur, a collaboration forum on climate issues and green solutions

Íslandsbanki oversaw the sale of a social bond for Reykjavik University and green/blue bond for seafood company Brim

Íslandsbanki was recognised for Excellence in Corporate Governance for the eighth year in a row

## Digital milestones 3Q21

An English version of the app was released in September

Push notifications in app enables easy flow of relevant information to customers

Customers can now estimate their carbon footprint based on their spending profile via the app

## Market share[1]

**29%** retail customers

**38%** SMEs

**35%** large companies

## Ratings and certifications

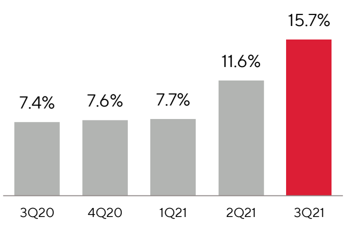
S&P Global Ratings

**BBB/A-2**
Stable outlook

EQUAL PAY CERTIFICATE 2018 - 2021

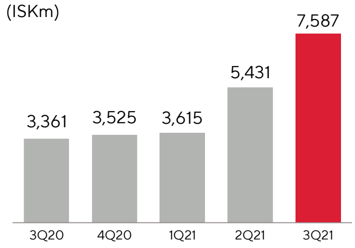
EXEMPLARY IN CORPORATE GOVERNANCE

## Return on equity

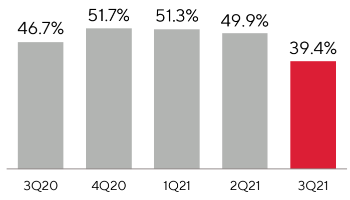



## Profit after tax

(ISKm)

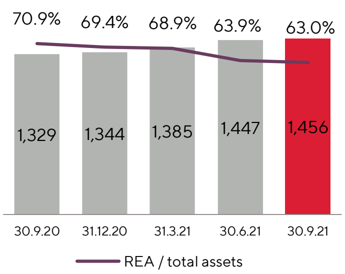



## Cost-to-income ratio[2]



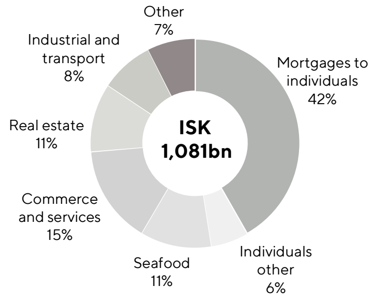

## Total assets

(ISKbn)



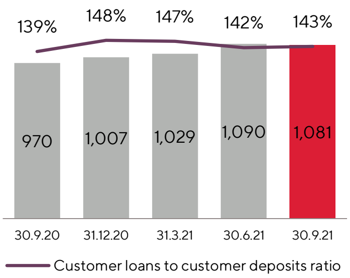

## Loans to customers

(Sector split as of 30.9.21)

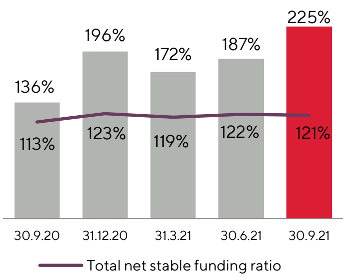



## Loans to customers

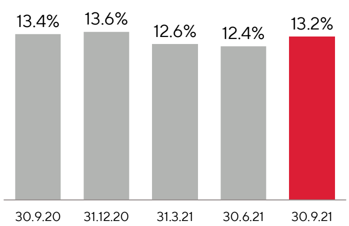
(ISKbn)



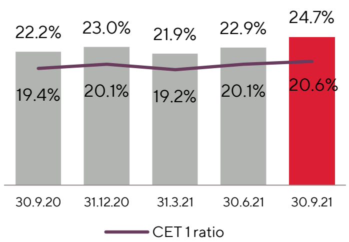

## Total liquidity coverage ratio




## Leverage ratio[3]




## Total capital ratio[3]




The information above has not been reviewed or audited by the Bank's auditor.
1. Based on Gallup surveys regarding primary bank. 2021 average for retail customers and SMEs and 2020 average for large companies.
2. IPO costs in 1Q21 were not adjusted for in the 1Q21 results.
3. Including third quarter profit.

# Directors' Report

These are the condensed consolidated interim financial statements for the period 1 January to 30 September 2021 ("the interim financial statements") of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") and its subsidiaries (together referred to as "the Group").

## Operations in the reporting period

Íslandsbanki is a universal bank offering comprehensive financial services to households, corporations, and institutional investors in Iceland. The Group is one of Iceland's largest banking and financial services groups, with a strong domestic market share.

The Group's profit from operations for the reporting period amounted to ISK 16,633 million. At the end of the reporting period, the Group employed 763 full-time members of staff, including 730 within the Bank itself.

Net interest income increased by 1.1% between years, as balance sheet growth outweighed the lower interest rate environment. The net interest margin did however reduce from 2.6% to 2.4%. Net fee and commission income rose by 20.1%, with strong performances in all business units. Salaries and related expenses were up by 6.1% between years due to general wage agreement increases in Iceland, one-off costs relating to the Bank's Initial Public Offering ("IPO") and redundancy costs. Other operating expenses rose by 2.4% due to one-off costs relating to the IPO of the Bank. The Bank's cost to income ratio fell from 55.3% to 46.6% between years. Net impairment reversals amounted to ISK 2,379 million as the tourism sector has started to recover from the COVID-19 pandemic and economic conditions have improved.

The Group's loan book grew by 7.4% in the period as the demand for new mortgages and refinancing continued at a strong pace. However, demand for new loans declined in the third quarter and some large corporate customers used favourable conditions in the bonds market to refinance existing bank debt. The Bank's ratio of non-performing loans fell from 2.9% at year-end 2020 to 2.0% due to both partial and full repayment of loans. Stage 2 loans under IFRS 9 remain at 13.0% of the loan book as loans to the tourism industry are still deemed to show signs of increased credit risk. Loans that have been subject to forbearance will remain in Stage 2 until 12 months have passed since repayments recommence. That said, the outlook for the tourism sector has improved substantially in the past few months resulting in a net positive impairment in the reporting period.

## Capital and funding

Customer deposits had at the end of September risen by 11.0% from year-end 2020, mainly due to a strong increase in Business Banking. The Bank continues to be a steady issuer of covered bonds, issuing ISK 4.4 billion in the third quarter. In September the Bank issued its inaugural Additional Tier 1 notes as a part of its effort to optimise its capital structure. The issue of SEK 750 million perpetual notes with a 5-year call was placed with investors across Scandinavia and continental Europe and was considerably oversubscribed. The liquidity position of the Bank remains robust with all liquidity ratios well above both internal and regulatory requirements.

The Bank is very well capitalised, with a total capital ratio of 24.7% at the end of the period, compared with the current 17.8% regulatory requirement, and a CET1 ratio of 20.6%. The total capital ratio increased by 1.8 percentage points in the third quarter due to the strong earnings in the period, the AT1 notes issued in September and a reduction in the risk exposure amount ("REA"), due to net repayments in the corporate loan book.

The implementation of EU regulation 2019/876 ("CRR II") in Iceland caused a fall in REA in the second quarter, contributing in turn to a 60bp rise in the capital ratios. As a result, the ratio of REA/total assets fell sharply. The most material effect was the amendment of the SME supporting factor, lowering the REA by ISK 35bn.

In September, the Central Bank of Iceland ("CBI") decided to restore the countercyclical capital buffer from 0% back to the pre-pandemic level of 2% of the risk base for financial institutions' domestic exposures. The increase will take effect at the end of September 2022. In the CBI's opinion, the combination of rapidly rising asset prices and increased household debt has already raised cyclical systemic risk to at least the pre-pandemic level. As a result, the CBI is of the view that the scope granted to financial institutions in March 2020, with the reduction in the buffer, is no longer needed.

Íslandsbanki retains its long-term total capital target of 19.5-21.0%, assuming a long-term capital requirement of 19.0%. The Bank therefore continues to be substantially over capitalised and has plans to release some of the excess capital along with the regular annual dividend payment in early 2022.

## Outlook

There are stronger signs of economic recovery in Iceland as the impact of the pandemic fades. Unemployment has halved year-to-date, from 12.8% in January to 5.0% in September. GDP rebounded in second quarter 2021 following the pandemic-induced recession as GDP grew by 7.3% year-on-year. Consumer sentiment and corporate expectations have shown a firm upward trend as private consumption and business investment are once more growing at a healthy pace. Export recovery is also underway and is expected to gather pace in coming quarters as global tourism recovers. However, inflation has proven more persistent than expected, with a rapid rise in house prices (14.7% year-on-year as of September) increasingly contributing to headline inflation that measured 4.4% in September. The Central Bank has responded to improving economic prospects and persistent inflation by raising its main policy rate from 0.75% as of end-April to the current 1.50%.

# Directors' Report

For 2022, the Bank's Chief Economist expects GDP growth to measure 3.6% as tourism rebounds and domestic economic activity normalises following a fading pandemic impact. However, a recent windfall in the proposed capelin quota could boost export revenues significantly and push GDP growth above 4.0% in 2022. Unemployment is expected to continue declining throughout the year and reach pre-pandemic levels by year-end. A stronger ISK, moderating pace of house prices increases and fading impact of global supply disruptions, combined with increasing monetary restraint by the Central Bank, will likely combine to bring inflation to the Central Bank's target in the fourth quarter next year.

The outlook for the Bank's operations remains robust as the economy recovers from the COVID-19 pandemic and economic forecasts point towards strong economic growth in the near term. The Bank continues to support its clients in the tourism industry and is optimistic for the future of that industry in Iceland.

The Bank is well on its way to reach its profitability targets. Interest income has held up well and is expected to grow with the balance sheet and a higher rates environment. Fee income growth has been very strong during the reporting period and the Bank is on target with its cost reduction plans. Impairments were positive in the period, which is a substantial change from the year before. Impairments will continue to fluctuate with the economic environment. Lastly, the issuance of AT1 notes in September supports the Bank's ambitions to optimise its capital structure to enhance profitability.

## Ownership

The Bank had a successful IPO in June 2021. On 30 September 2021 the number of shareholders of the Bank numbered over seventeen thousand, which is the largest shareholder base of any listed company in Iceland. The Icelandic Government is the largest shareholder, representing 65% of the outstanding shares and votes, those shares are administered by the ISFI in accordance with Act no. 88/2009 on Icelandic State Financial Investments. Other shareholders include pension funds, asset management funds, and private individuals. For further information on the Bank's shareholders see Note 37.

## Statement by the Board of Directors and the CEO

The interim financial statements for the period 1 January to 30 September 2021 have been prepared on a going concern basis in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting as adopted by the European Union; the Act on Annual Accounts, no. 3/2006; the Act on Financial Undertakings, no. 161/2002; and rules on accounting for credit institutions, where applicable.

To the best of our knowledge, these interim financial statements provide a true and fair view of the Group's operating profits and cash flows in the reporting period and its financial position as of 30 September 2021. Furthermore, in our opinion the financial statements and the Director's report give fair view of the main operational developments and achievements and describe the principal risks and uncertainties that the Group faces in its operations.

The Board of Directors and the CEO have today discussed and approved the Condensed Consolidated Interim Financial Statements for the period 1 January to 30 September 2021.

Kópavogur, 28 October 2021

**Board of Directors:**

Hallgrímur Snorrason, Chairman

Heiðrún Jónsdóttir, Vice-Chairman

Anna Þórðardóttir

Árni Stefánsson

Frosti Ólafsson

Guðrún Þorgeirsdóttir

Jökull H. Úlfsson

**Chief Executive Officer:**

Birna Einarsdóttir

# Consolidated Interim Income Statement

| | Notes | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|---|
| Interest income* | | 42,455 | 42,418 | 14,318 | 13,820 |
| Interest expense | | ( 17,056) | ( 17,305) | ( 5,526) | ( 5,515) |
| **Net interest income** | 5 | 25,399 | 25,113 | 8,792 | 8,305 |
| Fee and commission income | | 10,776 | 9,178 | 3,940 | 3,793 |
| Fee and commission expense | | ( 1,580) | ( 1,518) | ( 513) | ( 931) |
| **Net fee and commission income** | 6 | 9,196 | 7,660 | 3,427 | 2,862 |
| Net financial income (expense) | 7 | 1,853 | ( 2,174) | 941 | ( 255) |
| Net foreign exchange gain | 8 | 320 | 364 | 95 | 101 |
| Other operating income | 9 | 286 | 134 | 82 | 44 |
| **Other net operating income** | | 2,459 | ( 1,676) | 1,118 | ( 110) |
| **Total operating income** | | 37,054 | 31,097 | 13,337 | 11,057 |
| Salaries and related expenses | 10 | ( 10,121) | ( 9,536) | ( 2,953) | ( 2,842) |
| Other operating expenses | 11 | ( 7,307) | ( 7,137) | ( 2,135) | ( 2,268) |
| Contribution to the Depositors' and Investors' Guarantee Fund | | ( 517) | ( 525) | ( 173) | ( 50) |
| Bank tax | | ( 1,294) | ( 1,174) | ( 433) | ( 416) |
| **Total operating expenses** | | ( 19,239) | ( 18,372) | ( 5,694) | ( 5,576) |
| **Profit before net impairment on financial assets** | | 17,815 | 12,725 | 7,643 | 5,481 |
| Net impairment on financial assets | 12 | 2,379 | ( 6,987) | 1,757 | ( 1,058) |
| **Profit before tax** | | 20,194 | 5,738 | 9,400 | 4,423 |
| Income tax expense | 13 | ( 3,703) | ( 2,238) | ( 1,898) | ( 1,350) |
| **Profit for the period from continuing operations** | | 16,491 | 3,500 | 7,502 | 3,073 |
| Discontinued operations held for sale, net of income tax | 14 | 142 | ( 270) | 85 | 288 |
| **Profit for the period** | | 16,633 | 3,230 | 7,587 | 3,361 |
| Profit attributable to shareholders of Íslandsbanki hf. | | 16,638 | 3,533 | 7,588 | 3,362 |
| Loss attributable to non-controlling interests | | ( 5) | ( 303) | ( 1) | ( 1) |
| **Profit for the period** | | 16,633 | 3,230 | 7,587 | 3,361 |
| **Earnings per share from continuing operations** | | | | | |
| Basic and diluted earnings per share attributable to the shareholders of Íslandsbanki hf.** | 15 | 8.25 | 1.90 | 3.75 | 1.54 |

*Of which interest income amounting to ISK 40,905 million (2020: ISK 40,762 million) is calculated using the effective interest method.
**The calculation for earnings per share for comparative periods have been restated (see Note 15).

The notes on pages 11 to 57 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

# Consolidated Interim Statement of Comprehensive Income

| | 2021 | 2020 | 2021 | 2020 |
|---|---|---|---|---|
| | 1.1-30.9 | 1.1-30.9 | 1.7-30.9 | 1.7-30.9 |
| Profit for the period | 16,633 | 3,230 | 7,587 | 3,361 |
| Net gain (loss) on financial assets | ( 39) | ( 798) | - | 115 |
| Net gain (loss) on financial liabilities | ( 858) | 586 | ( 138) | ( 233) |
| **Items that will not be reclassified to the income statement** | ( 897) | ( 212) | ( 138) | ( 118) |
| Foreign currency translation | 5 | ( 112) | 14 | ( 112) |
| **Items that may subsequently be reclassified to the income statement** | 5 | ( 112) | 14 | ( 112) |
| **Other comprehensive expense for the period, net of tax** | ( 892) | ( 324) | ( 124) | ( 230) |
| **Comprehensive income for the period** | 15,741 | 2,906 | 7,463 | 3,131 |
| Comprehensive income attributable to shareholders of Íslandsbanki hf. | 16,108 | 3,424 | 7,459 | 3,000 |
| Comprehensive income (expense) attributable to non-controlling interests | ( 367) | ( 518) | 4 | 131 |
| **Comprehensive income for the period** | 15,741 | 2,906 | 7,463 | 3,131 |

The notes on pages 11 to 57 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

# Consolidated Interim Statement of Financial Position

| | Notes | 30.9.2021 | 31.12.2020 |
|---|---|---|---|
| **Assets** | | | |
| Cash and balances with Central Bank | 20 | 110,233 | 78,948 |
| Loans to credit institutions | 21 | 81,117 | 89,920 |
| Bonds and debt instruments | 16 | 123,599 | 128,216 |
| Derivatives | 22 | 2,374 | 6,647 |
| Loans to customers | 23 | 1,081,418 | 1,006,717 |
| Shares and equity instruments | 16 | 31,456 | 14,851 |
| Investments in associates | 25 | 952 | 775 |
| Property and equipment | 26 | 7,082 | 7,341 |
| Intangible assets | | 3,249 | 3,478 |
| Other assets | 27 | 13,954 | 4,125 |
| Non-current assets and disposal groups held for sale | 28 | 938 | 3,173 |
| **Total Assets** | | 1,456,372 | 1,344,191 |
| **Liabilities** | | | |
| Deposits from Central Bank and credit institutions | 29 | 20,409 | 39,758 |
| Deposits from customers | 30 | 754,442 | 679,455 |
| Derivative instruments and short positions | 22 | 10,869 | 6,936 |
| Debt issued and other borrowed funds | 32 | 397,672 | 387,274 |
| Subordinated loans | 33 | 36,923 | 27,194 |
| Tax liabilities | | 6,256 | 5,450 |
| Other liabilities | 35 | 32,420 | 11,920 |
| **Total Liabilities** | | 1,258,991 | 1,157,987 |
| **Equity** | | | |
| Share capital | | 10,000 | 10,000 |
| Share premium | | 55,000 | 55,000 |
| Reserves | | 5,738 | 6,181 |
| Retained earnings | | 126,653 | 113,529 |
| **Total Shareholders' Equity** | | 197,391 | 184,710 |
| Non-controlling interests | | ( 10) | 1,494 |
| **Total Equity** | | 197,381 | 186,204 |
| **Total Liabilities and Equity** | | 1,456,372 | 1,344,191 |

The notes on pages 11 to 57 are an integral part of these Condensed Consolidated Interim Financial Statements.

Financial Statements third quarter 2021 7 Amounts are in ISK million

# Consolidated Interim Statement of Changes in Equity

| | Share capital | Share premium | Statutory reserve | Restricted reserves | Fair value reserve | Liability credit reserve | Foreign currency translation reserve | Retained earnings | Total shareholders' equity | Non-controlling interests | Total equity |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Equity as at 1.1.2021** | 10,000 | 55,000 | 2,500 | 3,556 | 572 | ( 238) | ( 209) | 113,529 | 184,710 | 1,494 | 186,204 |
| Profit (loss) for the period ............................................ | | | | | | | | 16,638 | 16,638 | ( 5) | 16,633 |
| Net gain (loss) on financial assets ................................ | | | | | ( 572) | | | 900 | 328 | ( 367) | ( 39) |
| Net loss on financial liabilities ....................................... | | | | | | ( 858) | | | ( 858) | | ( 858) |
| Foreign currency translation ......................................... | | | | | | | | | - | 5 | 5 |
| **Comprehensive income (expense) for the period** | - | - | - | - | ( 572) | ( 858) | - | 17,538 | 16,108 | ( 367) | 15,741 |
| Dividends paid ............................................................. | | | | | | | | ( 3,400) | ( 3,400) | | ( 3,400) |
| Restricted due to capitalised development costs .......... | | | | ( 218) | | | | 218 | - | | - |
| Restricted due to fair value changes ............................ | | | | 1,126 | | | | ( 1,126) | - | | - |
| Restricted due to associates ........................................ | | | | 79 | | | | ( 79) | - | | - |
| Changes in non-controlling interests ............................ | | | | | | | | (27) | (27) | (1,137) | ( 1,164) |
| **Equity as at 30.9.2021** | 10,000 | 55,000 | 2,500 | 4,543 | - | ( 1,096) | ( 209) | 126,653 | 197,391 | ( 10) | 197,381 |
| **Equity as at 1.1.2020** | 10,000 | 55,000 | 2,500 | 3,525 | 1,432 | ( 392) | - | 105,569 | 177,634 | 2,428 | 180,062 |
| Profit (loss) for the period ............................................ | | | | | | | | 3,533 | 3,533 | ( 303) | 3,230 |
| Net loss on financial assets .......................................... | | | | | ( 372) | | | ( 212) | ( 584) | ( 214) | ( 798) |
| Net gain (loss) on financial liabilities ............................. | | | | | | 631 | | ( 45) | 586 | | 586 |
| Foreign currency translation ......................................... | | | | | | | (32) | (79) | (111) | (1) | ( 112) |
| **Comprehensive income (expense) for the period** | - | - | - | - | ( 372) | 631 | ( 32) | 3,197 | 3,424 | ( 518) | 2,906 |
| Restricted due to capitalised development costs .......... | | | | ( 218) | | | | 218 | - | | - |
| Restricted due to fair value changes ............................ | | | | 170 | | | | ( 170) | - | | - |
| Restricted due to subsidiaries and associates .............. | | | | 14 | | | | ( 14) | - | | - |
| Other changes due to IFRS 15 ..................................... | | | | | | | | (115) | (115) | | (115) |
| Changes in non-controlling interests ............................ | | | | | | | | (302) | (302) | (42) | ( 344) |
| **Equity as at 30.9.2020** | 10,000 | 55,000 | 2,500 | 3,491 | 1,060 | 239 | ( 32) | 108,383 | 180,641 | 1,868 | 182,509 |

Authorised share capital of the Bank is ISK 10,000 million ordinary shares, divided into 2,000 million outstanding shares of ISK 5 each. At 30 September 2021 paid up share capital totalled ISK 65,000 million which is the total stated share capital of the Bank. The Bank has one class of ordinary shares which carry no right to fixed income. The Annual General Meeting ("AGM") for the operating year 2020 was held on 18 March 2021. At the AGM shareholders approved the Board's proposal to pay dividends to shareholders amounting to ISK 3,400 million which is equivalent to ISK 1.70 per share (2020: none). The dividends were paid on 30 March 2021. It was also approved that the Board may convene a special shareholder meeting later in the year where a proposal regarding payment of dividends of profit for previous fiscal years could be suggested.

The notes on pages 11 to 57 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

# Consolidated Interim Statement of Cash Flows

| | 2021 | 2020 |
|---|---|---|
| | 1.1-30.9 | 1.1-30.9 |
| Profit for the period | 16,633 | 3,230 |
| Non-cash items included in profit for the period* | 13,012 | 22,083 |
| Changes in operating assets and liabilities* | ( 16,797) | ( 42,894) |
| Dividends received | 54 | 30 |
| Paid income tax, special financial activities tax, and bank tax | ( 4,517) | ( 4,383) |
| **Net cash provided by (used in) operating activities** | 8,385 | ( 21,934) |
| Net investment in a subsidiary and an associate | 568 | ( 2,486) |
| Proceeds from sales of property and equipment | 25 | 24 |
| Purchase of property and equipment | ( 124) | ( 492) |
| Purchase of intangible assets | ( 183) | ( 158) |
| **Net cash provided by (used in) investing activities** | 286 | ( 3,112) |
| Proceeds from borrowings | 70,543 | 15,255 |
| Repayment and repurchases of borrowings | ( 54,199) | ( 31,543) |
| Repayment of lease liabilities | ( 315) | ( 293) |
| Dividends paid | ( 3,400) | - |
| Subsidiary's capital decrease and share buyback paid to non-controlling interests | ( 1,130) | - |
| **Net cash provided by (used in) financing activities** | 11,499 | ( 16,581) |
| Net increase (decrease) in cash and cash equivalents | 20,170 | ( 41,627) |
| Effects of foreign exchange rate changes | 19 | 224 |
| Cash and cash equivalents at the beginning of the year | 115,668 | 152,481 |
| **Cash and cash equivalents at the end of the period** | 135,857 | 111,078 |

| **Reconciliation of cash and cash equivalents** | Notes | | |
|---|---|---|---|
| Cash on hand | 20 | 3,775 | 3,965 |
| Cash balances with Central Bank | 20 | 106,458 | 91,057 |
| Bank accounts | 21 | 34,555 | 25,554 |
| Mandatory reserve, special restricted and pledged balances with Central Bank | 20 | ( 8,931) | ( 9,498) |
| **Cash and cash equivalents at the end of the period** | | 135,857 | 111,078 |

*For further breakdown see the following page.

Interest received from 1 January to 30 September 2021 amounted to ISK 40,111 million (2020: ISK 36,657 million) and interest paid in the same period 2021 amounted to ISK 12,190 million (2020: ISK 13,994 million). Interest is defined as having been paid when it has been deposited into the customer account and is available for the customer's disposal.

The notes on pages 11 to 57 are an integral part of these Condensed Consolidated Interim Financial Statements.

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# Consolidated Interim Statement of Cash Flows

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 |
|---|---|---|
| Depreciation, amortisation, and write-offs | 1,033 | 1,380 |
| Share of profit and reversal of impairment of associates | ( 146) | ( 20) |
| Accrued interest and fair value changes on debt issued and subordinated loans | 10,508 | 9,857 |
| Net impairment on financial assets | ( 2,124) | 6,857 |
| Foreign exchange gain | ( 358) | ( 300) |
| Net gain from sales of property and equipment | ( 14) | ( 427) |
| Unrealised fair value (gain) loss recognised in profit or loss | ( 760) | 1,392 |
| Discontinued operations, net of income tax | ( 142) | ( 131) |
| Bank tax | 1,294 | 1,174 |
| Income tax expense | 3,703 | 2,238 |
| Other changes | 18 | 63 |
| **Non-cash items included in profit for the period** | **13,012** | **22,083** |

| | | |
|---|---|---|
| Mandatory reserve, special restricted and pledged balances with Central Bank | 618 | 5,781 |
| Loans to credit institutions | ( 2,835) | 5,099 |
| Bonds and debt instruments | 4,735 | ( 93,823) |
| Loans to customers | ( 76,354) | ( 53,510) |
| Shares and equity instruments | ( 16,550) | ( 681) |
| Other assets | ( 9,852) | ( 13,769) |
| Non-current assets and liabilities held for sale | 2,342 | ( 857) |
| Deposits from Central Bank and credit institutions | ( 19,028) | 4,061 |
| Deposits from customers | 75,821 | 66,221 |
| Derivative instruments and short positions | 3,754 | 7,845 |
| Other liabilities | 20,552 | 30,739 |
| **Changes in operating assets and liabilities** | **( 16,797)** | **( 42,894)** |

**Non-cash transactions 1 January to 30 September 2021**

During the period the Group did not have any significant non-cash transactions.

**Non-cash transactions 1 January to 30 September 2020**

During the period Íslandsbanki sold its 63.5% stake in Borgun hf. ISK 726 million of the sale price is due in 2021. Prior to the sale, shares in Borgun-VS ehf. a company holding series C preferred shares in Visa Inc., which were not part of the sale of Borgun, were transferred to the old owners of Borgun.

During the period the Bank sold an office building for the price of ISK 100 million with ISK 85 million outstanding at the end of the period.

The notes on pages 11 to 57 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

# Notes to the Condensed Consolidated Interim Financial Statements

## 1. Corporate information

Íslandsbanki hf., the parent company, was incorporated on 8 October 2008 and is a limited liability company domiciled in Iceland. The registered office is at Hagasmári 3, 201 Kópavogur, Iceland.

The condensed consolidated interim financial statements for the period 1 January to 30 September 2021 ("the interim financial statements") comprise the financial statements of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") and its subsidiaries (together referred to as "the Group").

The interim financial statements were approved and authorised for issue by the Board of Directors and the CEO of Íslandsbanki hf. on 28 October 2021.

## 2. Basis of preparation

The interim financial statements have been prepared in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting, as adopted by the European Union and additional requirements in the Act on Annual Accounts no. 3/2006, the Act on Financial Undertakings no. 161/2002 and rules on accounting for credit institutions.

The interim financial statements do not include all the information required for annual financial statements and should be read in conjunction with the audited consolidated financial statements of the Group for the year ended 31 December 2020, as well as the unaudited Pillar 3 Report for the year 2020. Both are available on the Bank's website: www.islandsbanki.is.

The accounting policies and the basis of measurement are unchanged from those set out in Notes 3 and 67 in the consolidated financial statements for the year 2020 except for the changes presented in Note 3 in these interim financial statements.

The interim financial statements are presented in Icelandic króna ("ISK"), which is the functional currency of Íslandsbanki hf. All amounts presented in ISK have been rounded to the nearest million, except when otherwise indicated. At 30 September 2021 the exchange rate of the ISK against the USD was 130.32 and for the EUR 150.90 (at year-end 2020: USD 127.21 and EUR 156.10).

The Group's management has made an assessment of the Group's ability to continue as a going concern and is satisfied that the Group has the resources to continue in business for the foreseeable future. Therefore, the interim financial statements have been prepared on a going concern basis.

### Significant accounting estimates and judgements

The preparation of the interim financial statements requires management to make judgements, estimates, and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income, and expenses recognised. Actual results may differ from those estimates.

Estimates and underlying assumptions are under constant review. Changes in accounting estimates are recognised when they occur.

As described in Note 3 in the consolidated financial statements for the year 2020, key sources of estimation uncertainty include the allowance for credit losses, the determination of fair value of financial instruments, and intangible assets.

#### Impairment of financial assets, changes from year-end 2020

Note 67.4 in the consolidated financial statements for the year 2020 contains a description of the Group's accounting policies for the impairment of financial assets.

At the end of the third quarter of 2021, the following changes have been made.

The Group's Chief Economist provided a new macroeconomic forecast on 21 September 2021 which takes into account the effects of the COVID-19 pandemic. The table below shows macroeconomic indicators from the new forecast.

| **Change in economic indicators %** | Estimate 2020 | Forecast 2021 | Forecast 2022 | Forecast 2023 | Forecast 2024 |
|---|---|---|---|---|---|
| Economic growth | ( 6.5) | 4.2 | 3.6 | 3.0 | 2.4 |
| Housing prices in Iceland | 6.4 | 11.3 | 6.9 | 3.4 | 3.5 |
| Purchasing power | 3.5 | 3.6 | 1.4 | 1.9 | 1.6 |
| ISK exchange rate index | 11.1 | ( 3.6) | ( 5.1) | ( 0.9) | - |
| Policy rate, Central Bank of Iceland | 1.5 | 1.0 | 2.2 | 3.2 | 3.5 |
| Inflation | 2.8 | 4.4 | 3.0 | 2.5 | 2.4 |
| Capital formation | ( 8.7) | 7.5 | 2.3 | 2.0 | 3.5 |
| thereof capital formation in industry | ( 14.2) | 9.5 | 0.9 | 2.2 | 3.5 |

# Notes to the Condensed Consolidated Interim Financial Statements

2. Cont'd

The Group continues to make temporary changes to the impairment model due to the COVID-19 pandemic.The Group's impairment process allows for temporary changes to the impairment model to account for circumstances when it becomes evident that existing or expected risk factors have not been appropriately considered in the credit risk rating or modelling process. The COVID-19 pandemic has created such circumstances for the tourism industry and therefore an adjustment is warranted. To account for the material uncertainty in the operating environment of companies in the tourism industry, not reflected in their current risk class, they have been further classified into four impact groups as described in Note 46. Where the increase was found to be significant (groups 2 - 4), the exposure was transferred to Stage 2. In addition, an overlay factor was applied to the expected credit losses, comparable to an increase in up to three risk classes, and a higher haircut was applied to value of collateral for the higher impact groups in the more severe scenarios. The common risk factor in tourism was found to apply to loans to customers with a gross carrying amount of ISK 103,315 million resulting in a expected credit losses of ISK 5,619 million, thereof the cumulative effect of the stage transfer and credit loss overlay is estimated to be around ISK 2.8 billion.

A new model for the risk assessment of loans to individuals was introduced in the third quarter of 2021. The new model utilises new data from the semi-automatic lending process for mortgages, which enhances the model's diagnostic ability. This leads to a general shift to better risk classes and an overall reduction in probability of default. Furthermore, the Group was able to reduce the margin of conservatism following the commissioning of the new model. As a consequence, the expected credit losses and the impairment allowance for loans to individuals fell by ISK 0.5 billion.

The All Risk Committee determined that it was appropriate to adjust the weights of the scenarios due to the COVID-19 pandemic, generally the scenarios are weighted 25%-50%-25% (good, base, bad) but it was determined appropriate to set the weights at 15%-50%-35%, as this would best represent the probability-weighted average over all possible scenarios. When deciding on the appropriate weights for the three scenarios, management used sensitivity analysis that indicated that a shift of 5% weight from the baseline to the pessimistic scenario would increase the impairment allowance by ISK 600 million while a 5% shift from the baseline to the optimistic scenario would decrease the allowance by ISK 200 million.

Substantial uncertainty remains with regards to the impact of the COVID-19 pandemic on the credit quality of the Group's credit exposures in future periods and therefore the assessment of expected credit losses.

## 3. Changes to accounting policies

The accounting policies in the interim financial statements are consistent with those applied in the consolidated financial statements for the year 2020, except for amendments related to the Phase 2 of the Interest Rate Benchmark Reform as described in Note 4 in the consolidated financial statements for the year 2020. The amendments did not have a significant impact on the interim financial statements.

# Notes to the Condensed Consolidated Interim Financial Statements

## 4. Operating segments

Segment information is presented in accordance with the Group's management and internal reporting structure. The segments' operating result are reported to the Board of Directors and the Chief Executive Officer, who are responsible for allocating resources to the reportable segments and assessing their financial performance.

An operating segment is a distinguishable component of the Group, for which discrete financial information is available, that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. Each operating segment is engaged in providing products or services which are subject to risk and return that are different from those of other operating segments. The accounting policies for the reportable segments are in line with the Group's accounting policies. The Group operates mainly in the Icelandic market.

The Bank has three main business segments: Personal Banking, Business Banking, and Corporate & Investment Banking. Operating segments pay and receive interest to and from Treasury to reflect the allocation of capital, funding costs, and the relevant risk premium. Capital allocation to the business units is based on the pillar 1 regulatory capital requirement, the pillar 2-R capital requirement calculated according to the Bank's ICAAP and the combined buffer requirement as stipulated in the Act on Financial Undertakings. Income tax and bank tax with breakdown for each segment is according to the current tax rates.

The Group comprises the following operating segments:

### Personal Banking

Personal Banking provides comprehensive financial services to individuals, such as lending, savings and payments. Íslandsbanki's customers are increasingly taking care of their day-to-day banking via digital solutions such as apps, the online bank and the secure web chat. Customers can also visit the Bank's efficient branch network for comprehensive consultancy services and contact the contact centre.

### Business Banking

Business Banking provides small and medium-sized enterprises (SMEs) with comprehensive financial services and Ergo, the Bank's asset financing service, is also part of the division. Business Banking serves customers in business centres and branches close to their business. Via online banking and app, customers have full overview of their business and day-to-day operations are easy to manage.

### Corporate & Investment Banking

Corporate & Investment Banking provides universal banking services to large companies, municipalities, institutional investors, and affluent individuals. Services include customised products and services to customers including lending and advisory, risk management, brokerage, and private banking services. The division is sector-focused, building and maintaining relationships with key customer segments within Iceland. Outside of Iceland, Íslandsbanki has a special focus on the North Atlantic seafood industry, leveraging its expertise in the domestic market and global contacts.

### Treasury and Proprietary Trading

Treasury is responsible for funding the Bank's operations and for managing the internal pricing framework. It is also responsible for the Bank's balance sheet management and for relations with investors, financial institutions, stock exchanges, and rating agencies. Equity that is not allocated to business units sits within Treasury. Proprietary Trading includes equity and debt investments in the trading book and the banking book.

### Cost centres

Cost centres comprise the CEO's office (Human Resources, Marketing & Communications, Strategy, and Legal), IT, Risk Management, Compliance and Finance excluding Treasury and Proprietary Trading. Group Internal Audit is also included in cost centres, however, it is independent from the Bank and the Chief Audit Executive reports directly to the Bank's Board of Directors.

### Subsidiaries, eliminations and adjustments

Subsidiaries include Íslandssjóðir hf., Allianz Ísland hf. and other less significant subsidiaries (see Note 25).

Assets and liabilities of subsidiaries, that are classified as non-current assets and disposal groups held for sale, are included in the column “Other subsidiaries".

All inter-company eliminations are included in the column “Eliminations & adjustments".

Following is an overview showing the Group's performance with a breakdown by operating segments.

# Notes to the Condensed Consolidated Interim Financial Statements

4. Cont'd

| **1 January to 30 September 2021** | Personal Banking | Business Banking | Corporate & Investment Banking | Treasury & Proprietary Trading | Cost centres | The Bank total | Subsidiaries, eliminations & adjustments | The Group total |
|---|---|---|---|---|---|---|---|---|
| Net interest income | 8,835 | 7,884 | 6,788 | 2,015 | ( 135) | 25,387 | 12 | 25,399 |
| Net fee and commission income | 2,739 | 1,590 | 3,358 | ( 88) | ( 62) | 7,537 | 1,659 | 9,196 |
| Other net operating income | 182 | 53 | 634 | 2,089 | 147 | 3,105 | ( 646) | 2,459 |
| Total operating income | 11,756 | 9,527 | 10,780 | 4,016 | ( 50) | 36,029 | 1,025 | 37,054 |
| Salaries and related expenses | ( 1,858) | ( 1,339) | ( 1,232) | ( 189) | ( 4,926) | ( 9,544) | ( 577) | ( 10,121) |
| Other operating expenses | ( 1,796) | ( 754) | ( 624) | ( 188) | ( 3,591) | ( 6,953) | ( 354) | ( 7,307) |
| Contribution to the Depositors' and Investors' Guarantee Fund | ( 405) | ( 101) | ( 11) | - | - | ( 517) | - | ( 517) |
| Bank tax | ( 542) | ( 258) | ( 387) | ( 97) | ( 10) | ( 1,294) | - | ( 1,294) |
| Net impairment on financial assets | 495 | 1,994 | ( 179) | 70 | - | 2,380 | ( 1) | 2,379 |
| Cost allocation | ( 3,358) | ( 2,361) | ( 2,339) | 237 | 7,821 | - | - | - |
| Profit (loss) before tax | 4,292 | 6,708 | 6,008 | 3,849 | ( 756) | 20,101 | 93 | 20,194 |
| Income tax expense | ( 1,257) | ( 1,811) | ( 1,663) | 1,024 | 193 | ( 3,514) | ( 189) | ( 3,703) |
| **Profit (loss) for the period from continuing operations** | 3,035 | 4,897 | 4,345 | 4,873 | ( 563) | 16,587 | ( 96) | 16,491 |
| Net segment revenue from external customers | 19,157 | 10,986 | 14,926 | ( 9,076) | 36 | 36,029 | 1,025 | 37,054 |
| Net segment revenue from other segments | ( 7,401) | ( 1,459) | ( 4,146) | 13,092 | ( 86) | - | - | - |
| Fee and commission income | 3,984 | 1,607 | 3,425 | 96 | 2 | 9,114 | 1,662 | 10,776 |
| Depreciation, amortisation, and write-offs | ( 124) | ( 44) | ( 11) | - | ( 847) | ( 1,026) | ( 7) | ( 1,033) |
| **At 30 September 2021** | | | | | | | | |
| Loans to customers | 495,179 | 234,771 | 351,379 | 89 | - | 1,081,418 | - | 1,081,418 |
| Other assets | 3,463 | 2,197 | 4,595 | 355,019 | 9,583 | 374,857 | 97 | 374,954 |
| **Total segment assets** | 498,642 | 236,968 | 355,974 | 355,108 | 9,583 | 1,456,275 | 97 | 1,456,372 |
| Deposits from customers | 335,054 | 238,816 | 149,483 | 33,589 | - | 756,942 | ( 2,500) | 754,442 |
| Other liabilities | 1,174 | 1,309 | 9,562 | 485,768 | 5,656 | 503,469 | 1,080 | 504,549 |
| **Total segment liabilities** | 336,228 | 240,125 | 159,045 | 519,357 | 5,656 | 1,260,411 | ( 1,420) | 1,258,991 |
| Allocated equity | 36,652 | 34,578 | 63,878 | 59,698 | 1,058 | 195,864 | 1,517 | 197,381 |
| Risk exposure amount | 244,100 | 216,980 | 388,169 | 61,568 | 6,512 | 917,329 | 435 | 917,764 |

The individual segment balance sheet positions are with external customers, and exclude internal transactions thus explaining the differences in total assets, and total liabilities and equity.

Amounts are in ISK million

4. Cont'd

| 1 January to 30 September 2020 | Personal Banking | Business Banking | Corporate & Investment Banking | Treasury & Proprietary Trading | Cost centres | The Bank total | Subsidiaries, eliminations & adjustments | The Group total |
|---|---|---|---|---|---|---|---|---|
| Net interest income | 8,021 | 7,913 | 6,465 | 2,847 | ( 166) | 25,080 | 33 | 25,113 |
| Net fee and commission income | 2,231 | 1,484 | 2,939 | ( 272) | 5 | 6,387 | 1,273 | 7,660 |
| Other net operating income | 305 | 48 | 813 | ( 2,079) | 215 | ( 698) | ( 978) | ( 1,676) |
| Total operating income | 10,557 | 9,445 | 10,217 | 496 | 54 | 30,769 | 328 | 31,097 |
| Salaries and related expenses | ( 1,793) | ( 1,463) | ( 1,161) | ( 211) | ( 4,348) | ( 8,976) | ( 560) | ( 9,536) |
| Other operating expenses | ( 1,937) | ( 888) | ( 640) | ( 217) | ( 3,110) | ( 6,792) | ( 345) | ( 7,137) |
| Contribution to the Depositors' and Investors' Guarantee Fund | ( 361) | ( 132) | ( 31) | ( 1) | - | ( 525) | - | ( 525) |
| Bank tax | ( 403) | ( 260) | ( 409) | ( 90) | ( 12) | ( 1,174) | - | ( 1,174) |
| Net impairment on financial assets | ( 479) | ( 4,571) | ( 1,959) | 22 | - | ( 6,987) | - | ( 6,987) |
| Cost allocation | ( 3,407) | ( 2,089) | ( 2,190) | 262 | 7,424 | - | - | - |
| Profit (loss) before tax | 2,177 | 42 | 3,827 | 261 | 8 | 6,315 | ( 577) | 5,738 |
| Income tax expense | ( 671) | ( 79) | ( 1,101) | ( 306) | ( 5) | ( 2,162) | ( 76) | ( 2,238) |
| **Profit (loss) for the period from continuing operations** | 1,506 | ( 37) | 2,726 | ( 45) | 3 | 4,153 | ( 653) | 3,500 |
| Net segment revenue from external customers | 15,421 | 11,218 | 15,260 | ( 11,296) | 166 | 30,769 | 328 | 31,097 |
| Net segment revenue from other segments | ( 4,864) | ( 1,773) | ( 5,043) | 11,792 | ( 112) | - | - | - |
| Fee and commission income | 3,500 | 1,507 | 3,002 | ( 79) | 6 | 7,936 | 1,242 | 9,178 |
| Depreciation, amortisation, and write-offs | ( 261) | ( 138) | ( 14) | - | ( 861) | ( 1,274) | ( 6) | ( 1,280) |
| **At 30 September 2020** | | | | | | | | |
| Loans to customers | 362,175 | 236,530 | 371,494 | 110 | - | 970,309 | - | 970,309 |
| Other assets | 8,172 | 2,231 | 4,347 | 331,439 | 11,353 | 357,542 | 873 | 358,415 |
| **Total segment assets** | 370,347 | 238,761 | 375,841 | 331,549 | 11,353 | 1,327,851 | 873 | 1,328,724 |
| Deposits from customers | 309,836 | 196,849 | 146,909 | 47,678 | - | 701,272 | ( 2,662) | 698,610 |
| Other liabilities | 4,415 | 2,502 | 8,121 | 425,805 | 5,687 | 446,530 | 1,075 | 447,605 |
| **Total segment liabilities** | 314,251 | 199,351 | 155,030 | 473,483 | 5,687 | 1,147,802 | ( 1,587) | 1,146,215 |
| Allocated equity | 30,692 | 38,835 | 63,690 | 45,914 | 918 | 180,049 | 2,460 | 182,509 |
| Risk exposure amount | 213,292 | 241,386 | 408,780 | 61,621 | 6,227 | 931,306 | 11,033 | 942,339 |

Amounts are in ISK million

## Notes to the Condensed Consolidated Interim Financial Statements

4. Cont'd

**Subsidiaries, eliminations & adjustments**

| **1 January to 30 September 2021** | Íslands-sjóðir hf. | Allianz Ísland hf. | Other subsidiaries | Eliminations & adjustments | Total |
|---|---|---|---|---|---|
| Net interest income | - | 4 | 10 | ( 2) | 12 |
| Net fee and commission income | 1,189 | 512 | ( 23) | ( 19) | 1,659 |
| Other net operating income | 273 | 14 | 10 | ( 943) | ( 646) |
| Total operating income | 1,462 | 530 | ( 3) | ( 964) | 1,025 |
| Salaries and related expenses | ( 435) | ( 142) | - | - | ( 577) |
| Other operating expenses | ( 147) | ( 309) | ( 1) | 103 | ( 354) |
| Net impairment on financial assets | - | - | - | ( 1) | ( 1) |
| Profit (loss) before tax | 880 | 79 | ( 4) | ( 862) | 93 |
| Income tax expense | ( 175) | ( 2) | - | ( 12) | ( 189) |
| **Profit (loss) for the period from continuing operations** | 705 | 77 | ( 4) | ( 874) | ( 96) |
| Net segment revenue from external customers | 1,657 | 504 | - | ( 1,136) | 1,025 |
| Net segment revenue from other segments | ( 195) | 26 | ( 3) | 172 | - |
| Fee and commission income | 1,554 | 512 | - | ( 404) | 1,662 |
| Depreciation, amortisation, and write-offs | - | ( 1) | - | ( 6) | ( 7) |
| **At 30 September 2021** | | | | | |
| Total assets | 2,617 | 1,118 | 5,797 | ( 9,435) | 97 |
| Total liabilities | 415 | 676 | 37 | ( 2,548) | ( 1,420) |
| Total equity | 2,202 | 442 | 5,760 | ( 6,887) | 1,517 |

| **1 January to 30 September 2020** | Íslands-sjóðir hf. | Allianz Ísland hf. | Other subsidiaries | Eliminations & adjustments | Total |
|---|---|---|---|---|---|
| Net interest income | 11 | 10 | 14 | ( 2) | 33 |
| Net fee and commission income | 881 | 514 | ( 23) | ( 99) | 1,273 |
| Other net operating income | 41 | 12 | 5 | ( 1,036) | ( 978) |
| Total operating income | 933 | 536 | ( 4) | ( 1,137) | 328 |
| Salaries and related expenses | ( 419) | ( 141) | - | - | ( 560) |
| Other operating expenses | ( 141) | ( 310) | ( 1) | 107 | ( 345) |
| Profit (loss) before tax | 373 | 85 | ( 5) | ( 1,030) | ( 577) |
| Income tax expense | ( 76) | ( 17) | - | 17 | ( 76) |
| **Profit (loss) for the period from continuing operations** | 297 | 68 | ( 5) | ( 1,013) | ( 653) |
| Net segment revenue from external customers | 1,144 | 425 | - | ( 1,241) | 328 |
| Net segment revenue from other segments | ( 211) | 111 | ( 4) | 104 | - |
| Fee and commission income | 1,237 | 514 | - | ( 509) | 1,242 |
| Depreciation, amortisation, and write-offs | - | - | - | ( 6) | ( 6) |
| **At 30 September 2020** | | | | | |
| Total assets | 2,101 | 1,406 | 8,607 | ( 11,241) | 873 |
| Total liabilities | 307 | 633 | 335 | ( 2,862) | ( 1,587) |
| Total equity | 1,794 | 773 | 8,272 | ( 8,379) | 2,460 |

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

## 5. Net interest income

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Cash and balances with Central Bank | 556 | 1,645 | 298 | 235 |
| Loans to credit institutions | 103 | 200 | 61 | 16 |
| Loans to customers | 40,246 | 38,917 | 13,272 | 12,985 |
| Financial assets mandatorily at fair value through profit or loss | 1,544 | 1,653 | 684 | 583 |
| Other assets | 6 | 3 | 3 | 1 |
| **Interest income** | 42,455 | 42,418 | 14,318 | 13,820 |
| Deposits from Central Bank and credit institutions | ( 254) | ( 612) | ( 63) | ( 192) |
| Deposits from customers | ( 4,520) | ( 6,324) | ( 1,400) | ( 1,625) |
| Debt issued and other borrowed funds designated as at FVTPL | ( 547) | ( 446) | ( 183) | ( 150) |
| Debt issued and other borrowed funds at amortised cost | ( 9,966) | ( 8,353) | ( 3,219) | ( 2,979) |
| Subordinated loans | ( 518) | ( 570) | ( 179) | ( 211) |
| Other liabilities* | ( 1,251) | ( 1,000) | ( 482) | ( 358) |
| **Interest expense** | ( 17,056) | ( 17,305) | ( 5,526) | ( 5,515) |
| **Net interest income** | 25,399 | 25,113 | 8,792 | 8,305 |

*Thereof is lease liabilities' interest expense amounting to ISK 63 million (2020: ISK 65 million).

## 6. Net fee and commission income

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Asset management | 2,129 | 1,746 | 705 | 576 |
| Investment banking and brokerage | 2,399 | 1,831 | 1,050 | 684 |
| Payment processing | 3,339 | 3,297 | 1,240 | 1,697 |
| Loans and guarantees | 1,604 | 1,324 | 540 | 514 |
| Other fee and commission income | 1,305 | 980 | 405 | 322 |
| **Fee and commission income** | 10,776 | 9,178 | 3,940 | 3,793 |
| Brokerage | ( 317) | ( 233) | ( 91) | ( 67) |
| Clearing and settlement | ( 1,255) | ( 1,285) | ( 420) | ( 864) |
| Other fee and commission expense | ( 8) | - | ( 2) | - |
| **Fee and commission expense** | ( 1,580) | ( 1,518) | ( 513) | ( 931) |
| **Net fee and commission income** | 9,196 | 7,660 | 3,427 | 2,862 |

Fee and commission income by segment is disclosed in Note 4.

## 7. Net financial income (expense)

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Net gain (loss) on financial assets and financial liabilities mandatorily at FVTPL | 1,323 | ( 1,688) | 718 | ( 140) |
| Net gain (loss) on financial liabilities designated as at FVTPL | 522 | ( 487) | 220 | ( 115) |
| Net gain on fair value hedges | 8 | 1 | 3 | - |
| **Net financial income (expense)** | 1,853 | ( 2,174) | 941 | ( 255) |

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

## 8. Net foreign exchange gain

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Cash and balances with Central Bank | ( 19) | 224 | 54 | 48 |
| Loans at amortised cost | ( 3,624) | 36,681 | 9,318 | 7,230 |
| Financial assets mandatorily at fair value through profit or loss | ( 4,632) | 8,464 | 553 | 2,628 |
| Other assets | ( 6) | 12 | - | 1 |
| **Net foreign exchange gain (loss) for assets** | ( 8,281) | 45,381 | 9,925 | 9,907 |
| Deposits | 1,155 | ( 15,528) | ( 3,377) | ( 2,299) |
| Debt issued and other borrowed funds designated as at FVTPL | 3,141 | ( 9,671) | ( 2,678) | ( 2,573) |
| Debt issued and other borrowed funds at amortised cost | 3,075 | ( 15,712) | ( 3,113) | ( 3,982) |
| Subordinated loans | 1,230 | ( 4,106) | ( 662) | ( 952) |
| **Net foreign exchange gain (loss) for liabilities** | 8,601 | ( 45,017) | ( 9,830) | ( 9,806) |
| **Net foreign exchange gain** | 320 | 364 | 95 | 101 |

## 9. Other operating income

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Share of profit of associates, net of income tax | 86 | 19 | 41 | - |
| Reversal of impairment for an associate | 60 | - | - | - |
| Gain from sale of property and equipment | 18 | 2 | 7 | - |
| Legal fees | 56 | 63 | 20 | 23 |
| Rental income | 30 | 30 | 10 | 10 |
| Other net operating income | 36 | 20 | 4 | 11 |
| **Other operating income** | 286 | 134 | 82 | 44 |

## 10. Salaries and related expenses

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Salaries | 7,794 | 7,341 | 2,268 | 2,183 |
| Contributions to pension funds | 1,206 | 1,102 | 354 | 334 |
| Social security charges and financial activities tax* | 1,042 | 1,039 | 323 | 323 |
| Other salary-related expenses | 79 | 54 | 8 | 2 |
| **Salaries and related expenses** | 10,121 | 9,536 | 2,953 | 2,842 |

*Financial activities tax calculated on salaries is 5.5% (2020: 5.5%).

## 11. Other operating expenses

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Professional services | 1,674 | 1,125 | 348 | 365 |
| Software and IT expenses | 3,129 | 3,301 | 980 | 1,071 |
| Real estate and office equipment | 392 | 413 | 115 | 138 |
| Depreciation, amortisation, and write-offs | 1,033 | 1,280 | 346 | 394 |
| Other administrative expenses | 1,079 | 1,018 | 346 | 300 |
| **Other operating expenses** | 7,307 | 7,137 | 2,135 | 2,268 |

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## 12. Net impairment on financial assets

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Expected credit losses, on-balance sheet items* | 2,316 | ( 6,812) | 1,747 | ( 1,069) |
| Expected credit losses, off-balance sheet items | 63 | ( 175) | 10 | 11 |
| **Net impairment on financial assets** | 2,379 | ( 6,987) | 1,757 | ( 1,058) |

*The main reasons for the reduced expected credit loss allowance are: a decrease related to the COVID-19 pandemic, mostly due to more favourable outlook in the tourism industry (ISK 946 million), a further reduction due to a more favourable economic environment (ISK 266 million) and a decrease related to a new model for risk assessment of loans to individuals (ISK 500 million). For further information see Note 2.

## 13. Income tax expense

Recognised income tax is based on applicable tax laws. The income tax rate for legal entities in 2021 is 20% (2020: 20%). Special financial activities tax is calculated as 6% of the Bank's taxable profit exceeding ISK 1 billion in accordance with the Act on Financial Activities Tax no. 165/2011. The effective income tax rate in the Group's income statement for the third quarter 2021 is 18.4% (2020: 39.0%).

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 |
|---|---|---|
| Current tax expense excluding discontinued operations | 3,208 | 2,909 |
| Special financial activities tax | 846 | 776 |
| Difference in prior year's calculated income tax | 2 | 12 |
| Changes in deferred tax assets and deferred tax liabilities | ( 353) | ( 1,459) |
| **Income tax recognised in the income statement** | 3,703 | 2,238 |
| **Income tax recognised in other comprehensive income** | - | ( 16) |

| | 2021<br>1.1-30.9 | | 2020<br>1.1-30.9 | |
|---|---|---|---|---|
| Profit before tax | 20,194 | | 5,738 | |
| 20% income tax calculated on the profit for the period | 4,039 | 20.0% | 1,148 | 20.0% |
| Special financial activities tax | 846 | 4.2% | 776 | 13.5% |
| Expenses (income) not subject to tax | ( 1,436) | ( 7.1%) | 75 | 1.3% |
| Non-deductible expenses | 259 | 1.3% | 235 | 4.1% |
| Other differences | ( 5) | ( 0.02%) | 4 | 0.1% |
| **Effective income tax expense** | 3,703 | 18.4% | 2,238 | 39.0% |

The Bank is taxed jointly with its subsidiary Íslandssjóðir hf.

## 14. Discontinued operations held for sale, net of income tax

| | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 | 2021<br>1.7-30.9 | 2020<br>1.7-30.9 |
|---|---|---|---|---|
| Net profit (loss) from foreclosed assets | 15 | ( 6) | ( 17) | 30 |
| Net profit (loss) from disposal groups held for sale | 130 | ( 705) | 99 | ( 167) |
| Net profit from sale of a subsidiary | - | 427 | - | 427 |
| Income tax expense | ( 3) | 14 | 3 | ( 2) |
| **Discontinued operations held for sale, net of income tax** | 142 | ( 270) | 85 | 288 |

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# Notes to the Condensed Consolidated Interim Financial Statements

## 15. Earnings per share

| | Continued operations | | Profit for the period | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| | 1.1-30.9 | 1.1-30.9 | 1.1-30.9 | 1.1-30.9 |
| Profit attributable to shareholders of the Bank | 16,496 | 3,803 | 16,638 | 3,533 |
| Weighted average number of outstanding shares* | 2,000 | 2,000 | 2,000 | 2,000 |
| **Basic earnings per share** | 8.25 | 1.90 | 8.32 | 1.77 |

The Group's basic and diluted earnings per share are equal as the Group has not issued any options, warrants, convertibles, or other financial instruments that dilute earnings per share (2020: none).

* In 2021 the share capital of ISK 10,000 million was divided into 2,000 million outstanding shares of ISK 5 each. As a result the calculation for earnings per share for comparative periods have been restated.

## 16. Classification of financial assets and financial liabilities

| **At 30 September 2021** | Mandatorily at FVTPL | Held for hedging | Designated as at FVTPL | Amortised cost | Carrying amount |
|---|---|---|---|---|---|
| Cash and balances with Central Bank | - | - | - | 110,233 | 110,233 |
| Loans to credit institutions | - | - | - | 81,117 | 81,117 |
| Listed bonds and debt instruments | 84,491 | - | - | - | 84,491 |
| Listed bonds and debt instruments used for economic hedging | 39,050 | - | - | - | 39,050 |
| Unlisted bonds and debt instruments | 58 | - | - | - | 58 |
| Derivatives | 1,749 | 625 | - | - | 2,374 |
| Loans to customers | - | - | - | 1,081,418 | 1,081,418 |
| Listed shares and equity instruments | 3,237 | - | - | - | 3,237 |
| Listed shares and equity instruments used for economic hedging | 24,407 | - | - | - | 24,407 |
| Unlisted shares and equity instruments | 3,812 | - | - | - | 3,812 |
| Other financial assets | - | - | - | 13,009 | 13,009 |
| **Total financial assets** | 156,804 | 625 | - | 1,285,777 | 1,443,206 |
| | | | | | |
| Deposits from Central Bank and credit institutions | - | - | - | 20,409 | 20,409 |
| Deposits from customers | - | - | - | 754,442 | 754,442 |
| Derivative instruments and short positions | 10,869 | - | - | - | 10,869 |
| Debt issued and other borrowed funds | - | 46,013 | 91,882 | 259,777 | 397,672 |
| Subordinated loans | - | - | - | 36,923 | 36,923 |
| Other financial liabilities | - | - | - | 30,889 | 30,889 |
| **Total financial liabilities** | 10,869 | 46,013 | 91,882 | 1,102,440 | 1,251,204 |

Amounts are in ISK million

## 16. Cont'd

| At 31 December 2020 | Mandatorily at FVTPL | Held for hedging | Designated as at FVTPL | Amortised cost | Carrying amount |
|---|---|---|---|---|---|
| Cash and balances with Central Bank | - | - | - | 78,948 | 78,948 |
| Loans to credit institutions | - | - | - | 89,920 | 89,920 |
| Listed bonds and debt instruments | 90,603 | - | - | - | 90,603 |
| Listed bonds and debt instruments used for economic hedging | 37,468 | - | - | - | 37,468 |
| Unlisted bonds and debt instruments | 145 | - | - | - | 145 |
| Derivatives | 5,639 | 1,008 | - | - | 6,647 |
| Loans to customers | - | - | - | 1,006,717 | 1,006,717 |
| Listed shares and equity instruments | 2,933 | - | - | - | 2,933 |
| Listed shares and equity instruments used for economic hedging | 9,109 | - | - | - | 9,109 |
| Unlisted shares and equity instruments | 2,809 | - | - | - | 2,809 |
| Other financial assets | - | - | - | 3,692 | 3,692 |
| **Total financial assets** | 148,706 | 1,008 | - | 1,179,277 | 1,328,991 |
| Deposits from Central Bank and credit institutions | - | - | - | 39,758 | 39,758 |
| Deposits from customers | - | - | - | 679,455 | 679,455 |
| Derivative instruments and short positions | 6,936 | - | - | - | 6,936 |
| Debt issued and other borrowed funds | - | 48,032 | 94,438 | 244,804 | 387,274 |
| Subordinated loans | - | - | - | 27,194 | 27,194 |
| Other financial liabilities | - | - | - | 9,721 | 9,721 |
| **Total financial liabilities** | 6,936 | 48,032 | 94,438 | 1,000,932 | 1,150,338 |

## 17. Fair value information for financial instruments

### Financial instruments carried at fair value

The fair value of a financial instrument is the transaction price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Where a market price is not readily available, the Group applies valuation techniques based on estimates and assumptions that are consistent with that which market participants would use in setting a price for the financial instrument.

The following table shows financial instruments carried at fair value at 30 September 2021 categorised into three levels of fair value hierarchy that reflect the type of inputs used in making the fair value measurements. The different levels have been defined as follows:

Level 1: Inputs that are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Group can access at the measurement date.

Level 2: Valuation techniques based on observable inputs other than the quoted prices included in Level 1, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Valuation techniques based on significant unobservable inputs, e.g. internal assumptions.

| At 30 September 2021 | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Bonds and debt instruments | 123,541 | - | 58 | 123,599 |
| Derivatives | - | 2,374 | - | 2,374 |
| Shares and equity instruments | 27,580 | - | 3,876 | 31,456 |
| **Total financial assets** | 151,121 | 2,374 | 3,934 | 157,429 |
| Short positions | 2,097 | - | - | 2,097 |
| Derivative instruments | - | 8,772 | - | 8,772 |
| Debt issued and other borrowed funds designated as at FVTPL | 91,882 | - | - | 91,882 |
| **Total financial liabilities** | 93,979 | 8,772 | - | 102,751 |

Amounts are in ISK million

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| **At 31 December 2020** | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Bonds and debt instruments | 128,071 | - | 145 | 128,216 |
| Derivatives | - | 6,647 | - | 6,647 |
| Shares and equity instruments | 11,931 | 30 | 2,890 | 14,851 |
| Non-current assets and disposal groups held for sale | - | - | 1,266 | 1,266 |
| **Total financial assets** | 140,002 | 6,677 | 4,301 | 150,980 |
| | | | | |
| Short positions | 737 | - | - | 737 |
| Derivative instruments | - | 6,199 | - | 6,199 |
| Debt issued and other borrowed funds designated as at FVTPL | 94,438 | - | - | 94,438 |
| **Total financial liabilities** | 95,175 | 6,199 | - | 101,374 |

| **Changes in Level 3 assets measured at fair value** | Bonds and debt instruments | Shares and equity instruments | Non-current assets |
|---|---|---|---|
| Fair value at 1 January 2021 | 145 | 2,890 | 1,266 |
| Purchases | 32 | 155 | - |
| Sales | ( 116) | - | ( 1,201) |
| Net gain (loss) on financial instruments recognised in profit or loss | ( 3) | 831 | - |
| Net loss on financial instruments recognised in other comprehensive income | - | - | ( 65) |
| **Fair value at 30 September 2021** | 58 | 3,876 | - |

| | Bonds and debt instruments | Shares and equity instruments | Non-current assets |
|---|---|---|---|
| Fair value at 1 January 2020 | 1,348 | 6,016 | - |
| Purchases | 18 | 7 | - |
| Sales | - | - | ( 2,028) |
| Net loss on financial instruments recognised in profit or loss | ( 1,256) | ( 2) | - |
| Net gain on financial instruments recognised in other comprehensive income | - | - | 114 |
| Transfer to "Non-current assets and disposal groups held for sale" | - | ( 3,180) | 3,180 |
| Other changes | 35 | 49 | - |
| **Fair value at 31 December 2020** | 145 | 2,890 | 1,266 |

At the end of each reporting period the Group determines whether transfers have occurred between levels in the hierarchy, by reassessing categorisation based on the lowest level input that is significant to the fair value measurement as a whole. No transfers between levels took place during the period.

*Valuation process*

The responsibility for the valuation of the fair value of financial instruments lies with the relevant business units. Each quarter, the business units present a valuation report to the Investment Committee for approval. The report and its assumptions are reviewed by Risk Management.

*Valuation techniques*

Where applicable, fair values are determined using quoted prices in active markets for identical assets and liabilities. In other cases, where there is no active market, the fair value is estimated using valuation techniques such as net present value and discounted cash flow models; comparison with similar instruments for which observable market data exists; net asset value (NAV) for investment fund units or expected recovery for distressed bonds. These valuation techniques are based on various assumptions and inputs such as risk-free rate, expected revenue growth and credit and liquidity spreads. In some cases, where significant inputs into these models are not observable, expert judgement and estimation for these inputs are required.

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# Notes to the Condensed Consolidated Interim Financial Statements

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*Level 1: Fair value established from quoted market prices.*
Financial instruments at this level are financial assets and financial liabilities containing actively traded bonds and equities that are listed either domestically or abroad.

*Level 2: Fair value established using valuation techniques with observable market information.*
Financial instruments at this level are assets and liabilities containing domestic bonds, equities as well as derivatives. For interest rate derivatives contracts such as interest rate swaps (IRS) and cross-currency interest rate swaps (CIRS) the Group calculates the net present value of estimated future cash flows based on yield curves with key inputs such as interest swap rates and forward-rate agreements (FRAs) rates. Foreign-currency forwards and foreign-currency swaps are valued using the FX spot rate adjusted for forward pricing points that can be obtained from market sources. These products are classified as Level 2. Bond forwards and equity forwards are also classified as Level 2 as they are valued using standard models with key inputs observed from stock prices, estimated dividend rates and funding rates.

*Level 3: Fair value established using valuation techniques using significant unobservable market information.*
Financial instruments at this level contain primarily unlisted and illiquid equities and bonds. Unlisted equities and bonds are initially recorded at their transaction price but are revalued each quarter based on the models as described above.

At 30 September 2021 the Group's Level 3 shares amounted to ISK 3,876 million:

-These include shares in seven professional investment funds and investment companies investing in unlisted equities and specialised investments in Iceland totalling ISK 2,003 million. The Group receives information from fund managers which use valuation models for the valuation of these equities.

-Other Level 3 shares amount to ISK 1,873 million.

At 30 September 2021 the Group's Level 3 bonds amounted to ISK 58 million:

-The majority of the amount in Level 3 bonds is estimated by discounting cash flow where the yield is the contractual currency's base rate with a premium that is decided by expert judgement on projected risk and financing cost.

In April 2021 the Group sold Series C preferred shares in Visa Inc., classified as non-current asset held for sale, amounting to ISK 1,201 million.

*Sensitivity analysis for Level 3 assets*

The valuations of Level 3 assets are in general uncertain and subject to various factors. The favourable and unfavourable scenarios can be considered as being likely movements in valuation within a year. The very favourable and very unfavourable scenarios are considered less likely, but not impossible and are not worst-case scenarios for some of the assets.

The following table shows how profit (loss) and total comprehensive income would have been affected if one or more of the inputs for fair value measurement in Level 3 were changed.

| **At 30 September 2021**<br>**Effect on profit or (loss):** | Carrying amount | Very favourable | Favourable | Unfavourable | Very unfavour-able |
|---|---|---|---|---|---|
| Level 3 Bonds and debt instruments | 58 | 81 | 16 | ( 29) | ( 58) |
| Level 3 Shares and equity instruments | 3,876 | 1,139 | ( 71) | ( 1,634) | ( 2,035) |

| **At 31 December 2020**<br>**Effect on profit or (loss):** | Carrying amount | Very favourable | Favourable | Unfavourable | Very unfavour-able |
|---|---|---|---|---|---|
| Level 3 Bonds and debt instruments | 145 | 1,015 | 773 | ( 132) | ( 145) |
| Level 3 Shares and equity instruments | 2,890 | 1,897 | 539 | ( 571) | ( 878) |
| **Effect on comprehensive income:** | | | | | |
| Level 3 Non-current assets and disposal groups held for sale | 1,266 | 1,898 | 949 | ( 633) | ( 1,266) |

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

## 18. Financial instruments not carried at fair value

### Assets

The fair value of "Loans to customers" may differ from their net carrying amount because the interest rates they carry may not reflect the interest rates that similar new loans would carry. The fair value is estimated by subtracting from or adding to the net carrying amount of the loans the discounted interest rate difference calculated from the reporting date until the next interest reset or maturity, whichever comes first. Since the interest rate difference is estimated using internal models these assets are classified as Level 3.

For "Cash and balances with Central Bank" and "Other financial assets" the fair value is adequately approximated by the carrying amount as they are short-term in nature. They are thus classified as Level 2.

### Liabilities

The fair value of a financial liability with a demand feature, such as a demand deposit, is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid. Most deposits are on demand or carry floating interest rates and as such their carrying amount is considered a good approximation of their fair value. The fair value for longer term fixed rate deposits is calculated with a duration approach, using the difference in each liability's current interest rate from the rate that a similar deposit would carry today. All deposits are classified as Level 2 based on the use of observable market interest rates to estimate the fair value.

Observed market value is used for the fair value of "Debt issued and other borrowed funds" where it is available. Issued bonds and bills with quoted market prices are classified as Level 1. If there is no quoted market price the fair value of the debt is valued in the same manner as deposits if it carries a fixed rate. If the debt carries a floating rate its fair value is estimated by comparing the margin with the Group's current funding premium on similar debt. These liabilities are classified as Level 2. The funding premium is based on the interest margin in the Group's issued papers including covered bonds, commercial papers as well as foreign currency denominated bonds.

Other financial liabilities mainly include unsettled securities transactions and payments due to leasing contracts and they are classified as Level 2 since their value is not observable from active market prices. Due to the short-term nature of these liabilities their carrying amount is considered a good approximation of their fair value.

The following table shows the fair value measurement and classification of the Group's assets and liabilities not carried at fair value. The different levels are defined in Note 17.

| **At 30 September 2021** | Level 1 | Level 2 | Level 3 | Total fair value | Carrying amount |
|---|---|---|---|---|---|
| Cash and balances with Central Bank | - | 110,233 | - | 110,233 | 110,233 |
| Loans to credit institutions | - | 81,117 | - | 81,117 | 81,117 |
| Loans to customers | - | - | 1,083,476 | 1,083,476 | 1,081,418 |
| Other financial assets | - | 13,009 | - | 13,009 | 13,009 |
| **Total financial assets** | - | 204,359 | 1,083,476 | 1,287,835 | 1,285,777 |
| Deposits from Central Bank and credit institutions | - | 20,450 | - | 20,450 | 20,409 |
| Deposits from customers | - | 754,511 | - | 754,511 | 754,442 |
| Debt issued and other borrowed funds | 202,830 | 115,414 | - | 318,244 | 305,790 |
| Subordinated loans | - | 37,832 | - | 37,832 | 36,923 |
| Other financial liabilities | - | 30,889 | - | 30,889 | 30,889 |
| **Total financial liabilities** | 202,830 | 959,096 | - | 1,161,926 | 1,148,453 |

| **At 31 December 2020** | Level 1 | Level 2 | Level 3 | Total fair value | Carrying amount |
|---|---|---|---|---|---|
| Cash and balances with Central Bank | - | 78,948 | - | 78,948 | 78,948 |
| Loans to credit institutions | - | 89,920 | - | 89,920 | 89,920 |
| Loans to customers | - | - | 1,010,315 | 1,010,315 | 1,006,717 |
| Other financial assets | - | 3,692 | - | 3,692 | 3,692 |
| **Total financial assets** | - | 172,560 | 1,010,315 | 1,182,875 | 1,179,277 |
| Deposits from Central Bank and credit institutions | - | 39,827 | - | 39,827 | 39,758 |
| Deposits from customers | - | 679,607 | - | 679,607 | 679,455 |
| Debt issued and other borrowed funds | 194,849 | 112,165 | - | 307,014 | 292,836 |
| Subordinated loans | - | 26,003 | - | 26,003 | 27,194 |
| Other financial liabilities | - | 9,721 | - | 9,721 | 9,721 |
| **Total financial liabilities** | 194,849 | 867,323 | - | 1,062,172 | 1,048,964 |

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

## 19. Offsetting financial assets and financial liabilities

The following tables show reconciliation to the net amounts of financial assets and financial liabilities, which are subject to offsetting, enforceable master netting agreements and similar agreements.

| | Financial assets subject to netting arrangements | | | Amounts not set off but subject to master netting arrangements and similar agreements | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **At 30 September 2021** | Financial assets before netting | Netting with financial liabilities | Net financial assets | Financial liabilities | Cash collateral received | Financial instruments collateral received | Net amount after consideration of potential effect of netting arrangements | Assets outside the scope of offsetting disclosure requirements | Total financial assets recognised in the balance sheet |
| Reverse repurchase agreements .. | 89 | - | 89 | - | - | - | 89 | - | 89 |
| Derivatives .................................. | 2,374 | - | 2,374 | ( 834) | ( 484) | ( 209) | 847 | - | 2,374 |
| **Total assets** | 2,463 | - | 2,463 | ( 834) | ( 484) | ( 209) | 936 | - | 2,463 |
| **At 31 December 2020** | | | | | | | | | |
| Reverse repurchase agreements .. | 898 | - | 898 | - | - | - | 898 | - | 898 |
| Derivatives .................................. | 6,647 | - | 6,647 | ( 761) | ( 4,330) | ( 187) | 1,369 | - | 6,647 |
| **Total assets** | 7,545 | - | 7,545 | ( 761) | ( 4,330) | ( 187) | 2,267 | - | 7,545 |

| | Financial liabilities subject to netting arrangements | | | Amounts not set off but subject to master netting arrangements and similar agreements | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| **At 30 September 2021** | Financial liabilities before netting | Netting with financial assets | Net financial liabilities | Financial assets | Cash collateral pledged | Financial instruments collateral pledged | Net amount after consideration of potential effect of netting arrangements | Liabilities outside the scope of offsetting disclosure requirements | Total financial liabilities recognised in the balance sheet |
| Derivative instruments and short positions ............................. | 10,869 | - | 10,869 | ( 834) | ( 500) | - | 9,535 | - | 10,869 |
| **At 31 December 2020** | | | | | | | | | |
| Derivative instruments and short positions ............................. | 6,936 | - | 6,936 | ( 761) | ( 504) | - | 5,671 | - | 6,936 |

## 20. Cash and balances with Central Bank

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Cash on hand ........................................................................................................................................ | 3,775 | 3,814 |
| Balances with Central Bank ...................................................................................................................... | 97,527 | 65,585 |
| Balances with Central Bank subject to special restrictions ........................................................................ | - | 1,288 |
| **Included in cash and cash equivalents** | 101,302 | 70,687 |
| Cash and balances pledged as collateral to Central Bank ......................................................................... | 588 | 288 |
| Mandatory reserve deposits with Central Bank .......................................................................................... | 8,343 | 7,973 |
| **Cash and balances with Central Bank** | 110,233 | 78,948 |

Amounts are in ISK million

## 21. Loans to credit institutions

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Money market loans | 46,562 | 43,646 |
| Bank accounts | 34,555 | 46,269 |
| Other loans | - | 5 |
| **Loans to credit institutions** | 81,117 | 89,920 |

## 22. Derivative instruments and short positions

| **At 30 September 2021** | Assets | Notional values related to assets | Liabilities | Notional values related to liabilities |
|---|---|---|---|---|
| Interest rate swaps | 1,203 | 147,931 | 3,286 | 86,564 |
| Cross-currency interest rate swaps | - | - | 149 | 17,973 |
| Equity forwards | 144 | 3,688 | 3,991 | 17,501 |
| Foreign exchange forwards | 124 | 7,020 | 251 | 7,654 |
| Foreign exchange swaps | 647 | 21,631 | 1,044 | 66,889 |
| Bond forwards | 256 | 38,911 | 51 | 7,360 |
| **Derivatives** | 2,374 | 219,181 | 8,772 | 203,941 |
| Short positions in listed bonds | - | - | 2,097 | 1,362 |
| **Total** | 2,374 | 219,181 | 10,869 | 205,303 |

| **At 31 December 2020** | | | | |
|---|---|---|---|---|
| Interest rate swaps | 1,888 | 181,914 | 3,581 | 62,275 |
| Cross-currency interest rate swaps | 2,861 | 63,067 | 45 | 3,171 |
| Equity forwards | 7 | 813 | 1,488 | 6,702 |
| Foreign exchange forwards | 70 | 4,010 | 362 | 8,582 |
| Foreign exchange swaps | 1,738 | 32,227 | 435 | 24,101 |
| Foreign exchange options | - | - | 1 | 25 |
| Bond forwards | 83 | 10,907 | 287 | 29,596 |
| **Derivatives** | 6,647 | 292,938 | 6,199 | 134,452 |
| Short positions in listed bonds | - | - | 737 | 550 |
| **Total** | 6,647 | 292,938 | 6,936 | 135,002 |

The Group uses derivatives to hedge currency exposure, interest rate risk in the banking book as well as inflation risk. The Group carries relatively low indirect exposure due to margin trading with clients and the Group holds collaterals for possible losses. Other derivatives in the Group held for trading or for other purposes are insignificant.

Short positions are in Icelandic Government bonds and bonds issued by municipalities, banks, and public companies. As a primary dealer the Group has access to securities lending facilities provided by the Central Bank and other issuers. Majority of the securities lending facilities have a maturity of less than a year.

The Group applies hedge accounting only with respect to certain EUR denominated interest rate swaps, whereby the Group pays floating rate interest and receives fixed rate interest. The interest rate swaps are hedging the exposure of changes in the fair value of certain fixed-rate EUR denominated bonds (see Note 32) arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 30 September 2021 the total fair value of the interest rate swaps was positive and amounted to ISK 625 million (2020: ISK 1,008 million) and their total notional amount was ISK 45,270 million (2020: ISK 46,830).

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# Notes to the Condensed Consolidated Interim Financial Statements

## 23. Loans to customers

| **At 30 September 2021** | Gross carrying amount Stage 1 | Stage 2 | Stage 3 | Expected credit losses Stage 1 | Stage 2 | Stage 3 | Net carrying amount |
|---|---|---|---|---|---|---|---|
| Individuals | 500,151 | 9,945 | 5,560 | ( 1,217) | ( 259) | ( 625) | 513,555 |
| Commerce and services | 87,881 | 76,617 | 6,938 | ( 618) | ( 3,884) | ( 2,767) | 164,167 |
| Construction | 33,170 | 1,797 | 1,699 | ( 299) | ( 69) | ( 105) | 36,193 |
| Energy | 9,420 | 119 | - | ( 29) | ( 2) | - | 9,508 |
| Financial services | 2,025 | 1 | - | ( 1) | - | - | 2,025 |
| Industrial and transportation | 61,794 | 25,973 | 4,573 | ( 291) | ( 356) | ( 1,943) | 89,750 |
| Investment companies | 19,209 | 3,446 | 655 | ( 319) | ( 300) | ( 124) | 22,567 |
| Public sector and non-profit organisations | 9,874 | 59 | 2 | ( 15) | - | ( 1) | 9,919 |
| Real estate | 89,017 | 24,551 | 2,499 | ( 415) | ( 591) | ( 542) | 114,519 |
| Seafood | 119,212 | 200 | 88 | ( 209) | ( 9) | ( 67) | 119,215 |
| **Loans to customers** | 931,753 | 142,708 | 22,014 | ( 3,413) | ( 5,470) | ( 6,174) | 1,081,418 |

| **At 31 December 2020** | Gross carrying amount Stage 1 | Stage 2 | Stage 3 | Expected credit losses Stage 1 | Stage 2 | Stage 3 | Net carrying amount |
|---|---|---|---|---|---|---|---|
| Individuals | 423,570 | 9,011 | 7,561 | ( 1,608) | ( 254) | ( 903) | 437,377 |
| Commerce and services | 60,062 | 64,350 | 5,958 | ( 511) | ( 3,151) | ( 2,448) | 124,260 |
| Construction | 36,551 | 5,420 | 997 | ( 283) | ( 195) | ( 138) | 42,352 |
| Energy | 7,997 | 701 | - | ( 17) | ( 8) | - | 8,673 |
| Financial services | 1,539 | - | - | - | - | - | 1,539 |
| Industrial and transportation | 46,526 | 30,971 | 3,989 | ( 243) | ( 783) | ( 1,899) | 78,561 |
| Investment companies | 15,287 | 5,504 | 3,628 | ( 268) | ( 427) | ( 284) | 23,440 |
| Public sector and non-profit organisations | 10,869 | 58 | 1 | ( 17) | - | - | 10,911 |
| Real estate | 112,189 | 42,169 | 6,794 | ( 461) | ( 1,655) | ( 1,534) | 157,502 |
| Seafood | 120,845 | 1,365 | 319 | ( 237) | ( 9) | ( 181) | 122,102 |
| **Loans to customers** | 835,435 | 159,549 | 29,247 | ( 3,645) | ( 6,482) | ( 7,387) | 1,006,717 |

## 24. Expected credit losses

**Total allowances for expected credit losses**

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Cash and balances with Central Bank | 3 | - | - | 3 |
| Loans to credit institutions | 99 | - | - | 99 |
| Loans to customers | 3,413 | 5,470 | 6,174 | 15,057 |
| Other financial assets | 28 | 4 | - | 32 |
| Off-balance sheet loan commitments and financial guarantees | 497 | 358 | 137 | 992 |
| **At 30 September 2021** | 4,040 | 5,832 | 6,311 | 16,183 |
| Cash and balances with Central Bank | 2 | - | - | 2 |
| Loans to credit institutions | 109 | - | - | 109 |
| Loans to customers | 3,645 | 6,482 | 7,387 | 17,514 |
| Other financial assets | 15 | 4 | - | 19 |
| Off-balance sheet loan commitments and financial guarantees | 347 | 483 | 225 | 1,055 |
| **At 31 December 2020** | 4,118 | 6,969 | 7,612 | 18,699 |

Amounts are in ISK million

## 24. Cont'd

The following tables reconcile the opening and closing balances for accumulated expected credit losses for loans to customers, and off-balance sheet loan commitments and financial guarantees.

**Loans to customers**

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| At 1 January 2021 | 3,645 | 6,482 | 7,387 | 17,514 |
| Transfer to Stage 1 | 1,124 | ( 952) | ( 172) | - |
| Transfer to Stage 2 | ( 302) | 1,271 | ( 969) | - |
| Transfer to Stage 3 | ( 32) | ( 860) | 892 | - |
| Net remeasurement of loss allowance | ( 2,831) | ( 1,521) | ( 1,609) | ( 5,961) |
| New financial assets originated or purchased | 2,216 | 1,341 | 2,025 | 5,582 |
| Derecognitions and maturities | ( 407) | ( 288) | ( 1,151) | ( 1,846) |
| Write-offs | - | ( 3) | ( 798) | ( 801) |
| Recoveries of amounts previously written off | - | - | 255 | 255 |
| Foreign exchange | - | - | ( 5) | ( 5) |
| Unwinding of interest | - | - | 319 | 319 |
| **At 30 September 2021** | 3,413 | 5,470 | 6,174 | 15,057 |

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| At 1 January 2020 | 3,645 | 953 | 5,700 | 10,298 |
| Transfer to Stage 1 | 3,577 | ( 2,827) | ( 750) | - |
| Transfer to Stage 2 | ( 1,743) | 3,200 | ( 1,457) | - |
| Transfer to Stage 3 | ( 171) | ( 1,314) | 1,485 | - |
| Transfer to "Non-current assets and disposal groups held for sale" | ( 50) | ( 12) | ( 83) | ( 145) |
| Net remeasurement of loss allowance | ( 3,316) | 6,024 | 1,201 | 3,909 |
| New financial assets originated or purchased | 2,104 | 597 | 2,516 | 5,217 |
| Derecognitions and maturities | ( 401) | ( 139) | ( 404) | ( 944) |
| Write-offs | - | - | ( 1,498) | ( 1,498) |
| Recoveries of amounts previously written off | - | - | 159 | 159 |
| Foreign exchange | - | - | 37 | 37 |
| Unwinding of interest | - | - | 481 | 481 |
| **At 31 December 2020** | 3,645 | 6,482 | 7,387 | 17,514 |

**Off-balance sheet loan commitments and financial guarantees**

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| At 1 January 2021 | 347 | 483 | 225 | 1,055 |
| Transfer to Stage 1 | 71 | ( 54) | ( 17) | - |
| Transfer to Stage 2 | ( 10) | 46 | ( 36) | - |
| Transfer to Stage 3 | ( 1) | ( 12) | 13 | - |
| Net remeasurement of loss allowance | ( 369) | ( 148) | ( 45) | ( 562) |
| New loan commitments and financial guarantees | 522 | 126 | 25 | 673 |
| Derecognitions and maturities | ( 63) | ( 83) | ( 28) | ( 174) |
| **At 30 September 2021** | 497 | 358 | 137 | 992 |
| At 1 January 2020 | 403 | 55 | 231 | 689 |
| Transfer to Stage 1 | 230 | ( 146) | ( 84) | - |
| Transfer to Stage 2 | ( 74) | 252 | ( 178) | - |
| Transfer to Stage 3 | ( 11) | ( 53) | 64 | - |
| Net remeasurement of loss allowance | ( 466) | 269 | 103 | ( 94) |
| New loan commitments and financial guarantees | 376 | 166 | 128 | 670 |
| Derecognitions and maturities | ( 111) | ( 60) | ( 39) | ( 210) |
| **At 31 December 2020** | 347 | 483 | 225 | 1,055 |

Amounts are in ISK million

## 25. Investments in subsidiaries and associates

| Investments in subsidiaries | | 30.9.2021 | 31.12.2020 |
|---|---|---|---|
| Íslandssjóðir hf., a fund management company, Hagasmári 3, 201 Kópavogur | Iceland | 100% | 100% |
| Allianz Ísland hf., an insurance agent, Dalshraun 3, 220 Hafnarfjörður | Iceland | 100% | 100% |

In addition Íslandsbanki has control over ten other non-significant subsidiaries.

| Investments in associates | | 30.9.2021 | 31.12.2020 |
|---|---|---|---|
| Auðkenni ehf., an information security company, Borgartún 31, 105 Reykjavík* | Iceland | 23.8% | 23.8% |
| JCC ehf., a cash centre service company, Sundaborg 15, 108 Reykjavík | Iceland | 33.3% | 33.3% |
| Reiknistofa bankanna hf., an IT service centre company, Katrínartún 2, 105 Reykjavík | Iceland | 30.1% | 30.1% |

*On 1 July 2021 Íslandsbanki hf. signed an agreement to sell its 23.8% stake in Auðkenni ehf. to the Icelandic State Treasury. This sale is, however, subject to approval by the Icelandic Competition Authority. Therefore, the Group has not recognised the sale nor the resulting profit at the end of the reporting period.

## 26. Property and equipment

| At 30 September 2021 | Land and buildings | Right-of-use assets: Buildings | Fixtures, equipment & vehicles | Total |
|---|---|---|---|---|
| Balance at the beginning of the year | 3,058 | 4,729 | 3,119 | 10,906 |
| Additions during the period | 30 | 133 | 96 | 259 |
| Disposals and write-offs during the period | - | - | ( 129) | ( 129) |
| Remeasurement | - | 115 | - | 115 |
| **Historical cost** | 3,088 | 4,977 | 3,086 | 11,151 |
| Balance at the beginning of the year | ( 1,340) | ( 906) | ( 1,319) | ( 3,565) |
| Depreciation during the period | ( 15) | ( 325) | ( 282) | ( 622) |
| Disposals and write-offs during the period | - | - | 118 | 118 |
| **Accumulated depreciation** | ( 1,355) | ( 1,231) | ( 1,483) | ( 4,069) |
| **Carrying amount** | 1,733 | 3,746 | 1,603 | 7,082 |

| At 31 December 2020 | Land and buildings | Right-of-use assets: Buildings | Fixtures, equipment & vehicles | Total |
|---|---|---|---|---|
| Balance at the beginning of the year | 4,096 | 4,634 | 4,068 | 12,798 |
| Additions during the year | 35 | - | 441 | 476 |
| Disposals and write-offs during the year | ( 120) | ( 69) | ( 583) | ( 772) |
| Remeasurement | - | 184 | - | 184 |
| Transfer to "Non-current assets and disposal groups held for sale" | ( 953) | ( 20) | ( 807) | ( 1,780) |
| **Historical cost** | 3,058 | 4,729 | 3,119 | 10,906 |
| Balance at the beginning of the year | ( 1,447) | ( 420) | ( 1,763) | ( 3,630) |
| Depreciation during the year | ( 19) | ( 421) | ( 398) | ( 838) |
| Disposals and write-offs during the year | 17 | ( 67) | 455 | 405 |
| Transfer to "Non-current assets and disposal groups held for sale" | 109 | 2 | 387 | 498 |
| **Accumulated depreciation** | ( 1,340) | ( 906) | ( 1,319) | ( 3,565) |
| **Carrying amount** | 1,718 | 3,823 | 1,800 | 7,341 |

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

## 27. Other assets

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Receivables | 1,303 | 1,767 |
| Unsettled securities transactions | 10,988 | 1,550 |
| Accruals | 246 | 200 |
| Prepaid expenses | 478 | 181 |
| Deferred tax assets | 826 | 259 |
| Other assets | 113 | 168 |
| **Other assets** | 13,954 | 4,125 |

## 28. Non-current assets and disposal groups held for sale

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Repossessed collateral: | | |
| Land and buildings | 635 | 1,548 |
| Industrial equipment and vehicles | 2 | 7 |
| Assets of disposal groups classified as held for sale | 301 | 1,618 |
| **Non-current assets and disposal groups held for sale** | 938 | 3,173 |

## 29. Deposits from Central Bank and credit institutions

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Deposits from credit institutions | 20,340 | 39,650 |
| Repurchase agreements with Central Bank | 69 | 108 |
| **Deposits from Central Bank and credit institutions** | 20,409 | 39,758 |

## 30. Deposits from customers

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Demand deposits and deposits with maturity up to 3 months | 671,017 | 582,746 |
| Term deposits with maturity of more than 3 months | 83,425 | 96,709 |
| **Deposits from customers** | 754,442 | 679,455 |

| **Deposits from customers specified by owners** | 30.9.2021 | | 31.12.2020 | |
|---|---|---|---|---|
| | Amount | % of total | Amount | % of total |
| Central government and state-owned enterprises | 13,364 | 2% | 8,145 | 1% |
| Municipalities | 10,878 | 1% | 7,561 | 1% |
| Companies | 384,275 | 51% | 326,799 | 48% |
| Individuals | 345,925 | 46% | 336,950 | 50% |
| **Deposits from customers** | 754,442 | 100% | 679,455 | 100% |

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

## 31. Pledged assets

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Financial assets pledged as collateral against liabilities | 286,759 | 236,901 |
| Financial assets pledged as collateral with the Central Bank | 7,824 | 5,088 |
| Financial assets pledged as collateral in foreign banks | 1,166 | 167 |
| **Pledged assets against liabilities** | 295,749 | 242,156 |

The Group has pledged assets against the issuance of covered bonds under Icelandic law, which are pledged on a pool of consumer mortgage loans. The Bank owns covered bonds for its own use which accounts for a portion of the pledged assets. The carrying amount of these bonds at 30 September 2021 was ISK 22,997 million.

The Group has also pledged assets with the Central Bank to ensure the clearing of the Icelandic payment system as well as other contracts with the Central Bank, moreover, it has pledged cash in foreign banks and financial institutions, mainly as collateral for trades under ISDA agreements to hedge market risk.

## 32. Debt issued and other borrowed funds

| | Issued | Maturity | | Interest | 30.9.2021 | 31.12.2020 |
|---|---|---|---|---|---|---|
| Covered bonds in ISK | 2019-2020 | 2021 | At maturity | Fixed rates | - | 5,076 |
| Covered bonds in ISK | 2015-2021 | 2023 | At maturity | Fixed rates | 40,718 | 29,496 |
| Covered bonds in ISK | 2020-2021 | 2027 | Amortising | Fixed rates | 20,837 | 5,386 |
| Covered bonds in ISK - CPI-linked | 2015-2017 | 2022 | At maturity | Fixed rates | 19,745 | 19,228 |
| Covered bonds in ISK - CPI-linked | 2012-2018 | 2024 | At maturity | Fixed rates | 37,420 | 36,797 |
| Covered bonds in ISK - CPI-linked | 2015-2018 | 2026 | At maturity | Fixed rates | 29,680 | 28,571 |
| Covered bonds in ISK - CPI-linked | 2019-2020 | 2028 | Amortising | Fixed rates | 23,129 | 25,606 |
| Covered bonds in ISK - CPI-linked | 2017-2018 | 2030 | At maturity | Fixed rates | 27,206 | 26,285 |
| **Covered bonds** | | | | | 198,735 | 176,445 |
| Senior unsecured bonds in SEK | 2018 | 2021 | At maturity | Fixed rates | - | 1,553 |
| Senior unsecured bonds in SEK | 2018-2019 | 2021 | At maturity | Floating rates | - | 6,630 |
| Senior unsecured bonds in SEK | 2018 | 2021 | At maturity | Floating rates | - | 14,832 |
| Senior unsecured bonds in EUR | 2019 | 2021 | At maturity | Floating rates | - | 1,795 |
| Senior unsecured bonds in SEK* | 2018 | 2022 | At maturity | Floating rates | - | 15,574 |
| Senior unsecured bonds in EUR** | 2019 | 2022 | At maturity | Fixed rates | 45,832 | 47,494 |
| Senior unsecured bonds in NOK | 2019 | 2022 | At maturity | Floating rates | 14,905 | 14,982 |
| Senior unsecured bonds in EUR*** | 2018 | 2024 | At maturity | Fixed rates | 46,013 | 48,032 |
| Senior unsecured bonds in NOK | 2019 | 2024 | At maturity | Fixed rates | 6,095 | 6,187 |
| Senior unsecured bonds in ISK | 2019 | 2024 | Amortising | Floating rates | 2,280 | 2,664 |
| Senior unsecured bonds in EUR** | 2020 | 2023 | At maturity | Fixed rates | 46,050 | 46,944 |
| Senior unsecured bonds in ISK | 2020-2021 | 2025 | At maturity | Fixed rates | 4,015 | 2,709 |
| Senior unsecured bonds in NOK | 2021 | 2024 | At maturity | Floating rates | 9,289 | - |
| Senior unsecured bonds in SEK | 2021 | 2024 | At maturity | Floating rates | 6,683 | - |
| Senior unsecured bonds in NOK | 2021 | 2025 | At maturity | Floating rates | 11,100 | - |
| Senior unsecured bonds in SEK | 2021 | 2025 | At maturity | Floating rates | 6,675 | - |
| **Bonds issued** | | | | | 198,937 | 209,396 |
| Bills issued | | | | | - | 1,433 |
| **Debt issued and other borrowed funds** | | | | | 397,672 | 387,274 |

Amounts are in ISK million

32. Cont'd

*The Bank repurchased own bonds during the period amounting to ISK 14,873 million.

**These bond issuances are classified as being designated as at fair value through profit or loss. At 30 September 2021 the total carrying amount of the bonds amounted to ISK 91,882 million and included in the amount are fair value changes amounting to ISK 1,005 million. The carrying amount of the bonds at 30 September 2021 was ISK 607 million higher than the contractual amount due at maturity.

***The Group applies hedge accounting to this bond issuance and uses certain EUR denominated interest rate swaps as hedging instruments (see Note 22). The interest rate swaps are hedging the exposure of the Group's changes in the fair value of this fixed-rate EUR denominated bond arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 30 September 2021 the total carrying amount of the bond issuance amounted to ISK 46,013 million and included in the amount are fair value changes amounting to ISK 470 million.

The Bank has issued additional covered bonds for its own use, for example for the purpose of securities lending with regards to market making agreements. These covered bond amounts are not included in the total.

## 33. Subordinated loans

| | Issued | Maturity | Callable | Interest | 30.9.2021 | 31.12.2020 |
|---|---|---|---|---|---|---|
| Subordinated loans in SEK ...................................... | 2017 | 2027 | 2022 | Floating, STIBOR + 2.0% | 11,125 | 11,646 |
| Subordinated loans in SEK ...................................... | 2018 | 2028 | 2023 | Floating, STIBOR + 2.5% | 7,412 | 7,775 |
| Subordinated loans in SEK ...................................... | 2019 | 2029 | 2024 | Floating, STIBOR + 3.9% | 7,386 | 7,773 |
| **Tier 2 subordinated loans** | | | | | 25,923 | 27,194 |
| Subordinated loans in SEK ...................................... | 2021 | Perpetual | 2026 | Floating, STIBOR + 4.75% | 11,000 | - |
| **Additional Tier 1 subordinated loans** | | | | | 11,000 | - |
| **Subordinated loans** | | | | | 36,923 | 27,194 |

## 34. Changes in liabilities arising from financing activities

| | | | Non-cash changes | | | |
|---|---|---|---|---|---|---|
| | 1.1.2021 | Cash flows | Interest expense | Foreign exchange | Fair value changes | 30.9.2021 |
| Covered bonds in ISK ............................................................... | 39,958 | 19,914 | 1,683 | - | - | 61,555 |
| Covered bonds in ISK - CPI-linked ........................................... | 136,487 | ( 6,353) | 7,046 | - | - | 137,180 |
| Senior unsecured bonds in ISK ................................................. | 5,373 | 795 | 127 | - | - | 6,295 |
| Senior unsecured bonds FX ...................................................... | 61,553 | ( 5,974) | 694 | ( 1,526) | - | 54,747 |
| Senior unsecured bonds FX at fair value .................................. | 94,438 | ( 513) | 547 | ( 3,141) | 551 | 91,882 |
| Senior unsecured bonds used for hedging ................................ | 48,032 | ( 526) | 409 | ( 1,549) | ( 353) | 46,013 |
| Other borrowed funds ................................................................ | 1,433 | ( 1,440) | 7 | - | - | - |
| Subordinated loans ................................................................... | 27,194 | 10,441 | 518 | ( 1,230) | - | 36,923 |
| **Total** | 414,468 | 16,344 | 11,031 | ( 7,446) | 198 | 434,595 |

Amounts are in ISK million

34. Cont'd

| | 1.1.2020 | Cash flows | Non-cash changes: Interest expense | Foreign exchange | Fair value changes | 31.12.2020 |
|---|---|---|---|---|---|---|
| Covered bonds in ISK | 24,088 | 14,400 | 1,470 | - | - | 39,958 |
| Covered bonds in ISK - CPI-linked | 125,975 | 2,532 | 7,980 | - | - | 136,487 |
| Senior unsecured bonds in ISK | 3,553 | 1,728 | 92 | - | - | 5,373 |
| Senior unsecured bonds FX | 58,892 | ( 7,093) | 1,013 | 8,741 | - | 61,553 |
| Senior unsecured bonds FX at fair value | 49,352 | 38,069 | 608 | 6,468 | ( 59) | 94,438 |
| Senior unsecured bonds used for hedging | 41,816 | ( 463) | 566 | 6,061 | 52 | 48,032 |
| Other borrowed funds | 2,705 | ( 1,330) | 58 | - | - | 1,433 |
| Subordinated loans | 22,674 | ( 738) | 763 | 4,495 | - | 27,194 |
| **Total** | 329,055 | 47,105 | 12,550 | 25,765 | ( 7) | 414,468 |

## 35. Other liabilities

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Accruals | 2,491 | 2,311 |
| Lease liabilities | 3,895 | 3,962 |
| Provision for effects of court rulings | 288 | 288 |
| Expected credit losses for off-balance sheet loan commitments and financial guarantees | 992 | 1,055 |
| Withholding tax | 483 | 915 |
| Unsettled securities transactions | 22,639 | 1,379 |
| Sundry liabilities | 1,603 | 1,983 |
| Non-current liabilities and disposal groups held for sale | 29 | 27 |
| **Other liabilities** | 32,420 | 11,920 |

## 36. Custody assets

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Custody assets - not managed by the Group | 3,264,900 | 2,863,328 |

## 37. Íslandsbanki's shareholders

| The following table shows the ten largest shareholders of the Bank. | 30.9.2021 | 31.12.2020 |
|---|---|---|
| The Icelandic Government | 65.00% | 100% |
| Capital Group | 4.32% | - |
| Live Pension Fund | 3.36% | - |
| Gildi Pension Fund | 3.34% | - |
| LSR Pension Fund | 2.92% | - |
| RWC Asset Management | 1.28% | - |
| Iceland Funds | 0.97% | - |
| Kvika banki hf. | 0.93% | - |
| Landsbankinn - Nominee account 1 | 0.84% | - |
| Almenni Pension Fund | 0.82% | - |
| Other shareholders with less than 0.82% shareholding | 16.22% | - |
| **Total** | 100% | 100% |

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## 38. Related party

Íslandsbanki has a related party relationship with the Icelandic Government as the largest shareholder with control over the Group. The shares are administered by the Icelandic State Financial Investments ("ISFI"). As a result, the Icelandic Government and the Icelandic State Financial Investments are defined as related parties. The Group has applied the partial exemption for government-related entities, as described in IAS 24.

The Board of Directors and key management personnel of the Bank, ISFI and subsidiaries of the Bank, close family members of individuals referred to herein and legal entities controlled by them, are defined as related parties.

The Group's associates are also defined as related parties.

The Group's products and services are offered to the Icelandic Government and government-related entities in competition with other vendors and under generally accepted commercial terms. In a similar manner the Group entities purchase products and services from government-related entities under generally accepted commercial terms. Transactions with related parties were made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third party counterparties.

Cash and balances with the Central Bank are disclosed under Note 20 and Deposits from the Central Bank are disclosed under Note 29.

All loans to employees are provided on general business terms of the Group and the balances do not reflect collaterals held by the Group.

| At 30 September 2021 | Assets | Liabilities | Net balance | Commitments, guarantees & overdrafts |
|---|---|---|---|---|
| Shareholders with control over the Group | - | - | - | 2 |
| Board of Directors, key management personnel and other related parties | 483 | 942 | ( 459) | 63 |
| Associated companies | 11 | 802 | ( 791) | 229 |
| **Balances with related parties** | 494 | 1,744 | ( 1,250) | 294 |

| 1 January - 30 September 2021 | Interest income | Interest expense | Other income | Other expense |
|---|---|---|---|---|
| Shareholders with control over the Group | - | - | 281 | - |
| Board of Directors, key management personnel and other related parties | 15 | 8 | 2 | 2 |
| Associated companies | 1 | 1 | 1 | 1,117 |
| **Transactions with related parties** | 16 | 9 | 284 | 1,119 |

| At 31 December 2020 | Assets | Liabilities | Net balance | Commitments, guarantees & overdrafts |
|---|---|---|---|---|
| Shareholders with control over the Group | - | - | - | 3 |
| Board of Directors, key management personnel and other related parties | 440 | 393 | 47 | 45 |
| Associated companies | 31 | 342 | ( 311) | 228 |
| **Balances with related parties** | 471 | 735 | ( 264) | 276 |

| 1 January - 30 September 2020 | Interest income | Interest expense | Other income | Other expense |
|---|---|---|---|---|
| Board of Directors, key management personnel and other related parties | 10 | 7 | 1 | - |
| Associated companies | - | 6 | 1 | 1,172 |
| **Transactions with related parties** | 10 | 13 | 2 | 1,172 |

At 30 September 2021 total of ISK 1 million (at year-end 2020: none) were recognised as Stage 1 expected credit losses. No share option programmes were operated during the period.

Amounts are in ISK million

## 39. Contingencies

### Contingent liabilities

#### Borgun hf. – Landsbankinn hf.

Borgun hf., (currently SaltPay IIB hf.) a former subsidiary of Íslandsbanki, is a payment acquirer and issuing processor. Landsbankinn hf. sold its 31.2% stake in Borgun hf. in late 2014. Landsbankinn claims that Borgun's management did not disclose all available information that might have affected the value of Borgun hf. during the sales process, namely the value of its stake in Visa Europe which was sold to Visa International shortly after the Borgun hf. sale. In order to reclaim the alleged loss, Landsbankinn filed a lawsuit against Borgun hf. and others on 12 January 2017, claiming the right to damages for having been deprived of the true value of the stake involved in the sale. Landsbankinn does not quantify the claim, but its estimate of the lost profit from having sold its shares in Borgun hf. is approximately ISK 1,930 million. Court appointed assessors presented their assessment in November 2019. A reassessment was demanded, and the senior assessors appointed by the court presented their reassessment in April 2021 which corroborates the previous assessment of Borgun's obligation to disclose. Further, the senior assessors estimated that Borgun's share in Visa as of 31 December 2013 would have amounted to at least ISK 387 million. The main hearing of the case is scheduled on 22 January 2022.

On 11 March 2020, the Bank signed an agreement to sell its 63.47% stake in Borgun hf. to Salt Pay Co Ltd. and concluded the sale on 7 July 2020. In the agreement the Bank undertook to reimburse 63.47% of losses incurred by Borgun hf. or the buyer as a result of an unfavourable outcome in the Landsbankinn case, however such reimbursement was never to exceed the Bank's share in the purchase price. The Group has not recognised a provision as a result of this event.

#### 105 Miðborg slhf. - ÍAV hf.

In March 2021 the professional investor fund 105 Miðborg slhf., operated by Íslandssjóðir (Iceland Funds), a wholly owned subsidiary of the Bank, terminated its contractor agreement with ÍAV hf., a contractor that had been retained for a real estate project at Kirkjusandur in the centre of Reykjavík. The main reason for the termination was the alleged and significant non-performance and delays in the construction of one building on the premises. The contractor, ÍAV hf., has claimed approximately ISK 3,829 million in damages plus late payment interest and legal costs from 105 Miðborg slhf. and Iceland Funds for the alleged unlawful termination. The case was filed on 11 May 2021 at the District Court of Reykjavík. In a written brief of dismissal, Iceland Funds opposed their involvement in the case on the basis that the contractual relationship was between ÍAV hf. and 105 Miðborg slhf. Further, the 105 Miðborg slhf. has issued a subpoena against ÍAV hf. claiming approximately ISK 3,878 million plus late payment interest and legal cost due to delay and significant breaches of contract. The Bank owns a 6.25% stake in the 105 Miðborg slhf. The Group has not recognised a provision in respect of this matter.

#### Threatened lawsuit by the Consumers' Association of Iceland

In September 2020 the Consumers' Association of Iceland sent a letter to Íslandsbanki hf., Arion Banki hf. and Landsbankinn hf. claiming that the method used to adjust variable interest rates on loans to consumers is illegal. The Consumers' Association considers the basis on which adjustments of such floating interest rates are made to be in violation of the loan agreements' provisions and not sufficiently transparent and intends to claim both an annulment of the relevant provision of the loan agreement and a repayment of overpaid interest. The Group has reviewed the contractual terms and processes for interest rate decisions and adjustments in light of these claims and has concluded that no changes were required and that the Consumers' Association's claim towards the Group are unfounded. On 19 May 2021 the Consumers' Association publicly announced that the association intends to initiate lawsuits against the Icelandic commercial banks and other loan institutions and called for participants in a possible class action lawsuit. The Group has received information requests from a legal firm representing over 1200 customers of Icelandic commercial banks and loan institutions. The Bank has commissioned an outside opinion on its legal position. The Group has not recognised a provision in respect of this matter.

## 40. Events after the reporting period

No events have arisen after the reporting period that require amendments or additional disclosures in the interim financial statements for the third quarter 2021.

# Notes to the Condensed Consolidated Interim Financial Statements

## 41. Risk management

### Risk governance

The Group is exposed to various risk factors and managing these risks is an integral part of its operations. More information about the Group's risk management and risk assessment processes is available in the unaudited Pillar 3 2020 Report, which is available on the Bank's website: www.islandsbanki.is.

## 42. Credit risk

Credit risk is defined as current or prospective risk to earnings and capital arising from an obligor's potential failure to meet the terms of any financial contract with the Group.

Credit concentration risk is the significantly increased risk that is driven by common underlying factors, e.g. industrial sector, economy, geographical location, type of financial instrument or due to connections or relations among counterparties. This includes exposures to parties under common control and significant exposures to groups of counterparties whose likelihood of default is driven by common underlying factors.

Credit risk arises principally from loans and advances to customers and other banks but also from balances with the Central Bank and off-balance sheet items such as financial guarantees, loan commitments and derivatives.

The Group has policies and procedures dedicated to accepting, measuring, and managing credit risk. The objective of the Group's credit risk management is to achieve an appropriate balance between risk and return and to minimise potential adverse effects of credit risk on the Group's financial performance.

A thorough analysis of the counterparty's financial standing, analysis of past and estimated future cash flows as well as the borrower's general ability to repay its obligations forms the basis for all credit decisions. The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, groups of borrowers, countries and industry segments. The Group measures and consolidates its credit risk for each counterparty or group of connected clients in accordance with internal and external criteria of connection between parties.

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security in borrower's assets. The principal collateral types for loans are properties, vehicles, equipment, vessels and securities. When applicable, other credit risk mitigants are employed.

## 43. Maximum credit exposure

The Group's credit risk exposure comprises both on-balance sheet and off-balance sheet items. Maximum exposure to credit risk for on-balance sheet assets is the net carrying amount as reported in the statement of financial position. The maximum exposure for off-balance sheet items is the amount that the Group might have to pay out against financial guarantees and loan commitments, less provisions that have been made because of these items. The maximum credit exposure for a derivative contract is calculated by multiplying the sum of potential future credit exposure and the positive market value of the contract by a factor 1.4. This multiplication factor along with a new method for calculating potential future credit exposure was introduced with the implementation of CRR II in Iceland, leading to an increase in maximum credit exposure due to derivatives.

The industry breakdown shows the credit exposure by industry classification. The breakdown follows an internal industry classification which is based on the Icelandic ISAT2008 that derives from the European NACE Rev. 2 classification standard. During the period, industry classification was changed for a number of customers in order to better reflect the underlying operations. This is most notable where certain companies previously in "Real estate" are now classified as "Commerce and services" or "Industrial and transportation". Comparative figures have not been restated.

43. Cont'd

The Government guarantee schemes issued in response to the COVID-19 pandemic are presented in the line item "Loans to customers". Of these, ISK 2,453 million are subject to 100% Government guarantee, ISK 1,195 million to 85% Government guarantee and ISK 558 million to 70% Government guarantee.

As a part of the agreement on the sale of Borgun hf. (currently SaltPay IIB hf.) in 2020 the Group took on certain guarantees with regards to chargeback risk that Borgun hf. is exposed to through its operations, which at 30 September 2021 amounted to about ISK 134 million. These guarantees are not included in the following table.

The Group's credit exposure, before taking account of any collateral held or other credit enhancements, is as follows:

| **At 30 September 2021** | Individuals | Central governments | Commerce and services | Construction | Energy | Financial services | Industrial and transportation | Investment companies | Public sector and non-profit organisations | Real estate | Seafood | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank ....... | - | 110,233 | - | - | - | - | - | - | - | - | - | 110,233 |
| Loans to credit institutions ......................... | - | - | - | - | - | 81,117 | - | - | - | - | - | 81,117 |
| Bonds and debt instruments ...................... | - | 99,391 | 642 | - | 444 | 20,550 | - | 8 | 1,410 | 1,154 | - | 123,599 |
| Derivatives ................................................ | 357 | 716 | 485 | - | 22 | 14,286 | 305 | 4,042 | - | 1,510 | 539 | 22,262 |
| Loans to customers: | 513,555 | - | 164,167 | 36,193 | 9,508 | 2,025 | 89,750 | 22,567 | 9,919 | 114,519 | 119,215 | 1,081,418 |
| Overdrafts ............................................... | 11,225 | - | 11,294 | 2,856 | 77 | 7 | 5,428 | 804 | 399 | 2,883 | 2,942 | 37,915 |
| Credit cards ............................................ | 15,398 | - | 1,495 | 276 | 7 | 23 | 383 | 32 | 110 | 74 | 45 | 17,843 |
| Mortgages ............................................... | 450,760 | - | - | - | - | - | - | - | - | - | - | 450,760 |
| Capital leases ......................................... | 6,079 | - | 27,822 | 3,235 | 21 | - | 7,967 | 110 | 36 | 225 | 176 | 45,671 |
| Government guarantee schemes ............ | 18 | - | 3,413 | 130 | - | - | 366 | 50 | - | 140 | 89 | 4,206 |
| Other loans ............................................. | 30,075 | - | 120,143 | 29,696 | 9,403 | 1,995 | 75,606 | 21,571 | 9,374 | 111,197 | 115,963 | 525,023 |
| Other financial assets ............................... | 725 | 2,444 | 222 | - | 4 | 9,160 | 37 | 203 | 10 | 186 | 18 | 13,009 |
| Off-balance sheet items: | 31,180 | - | 33,836 | 27,793 | 1,587 | 7,835 | 28,227 | 955 | 5,159 | 11,238 | 13,556 | 161,366 |
| Financial guarantees ............................... | 425 | - | 6,766 | 7,808 | 5 | 8 | 2,556 | 35 | 4 | 1,890 | 580 | 20,077 |
| Undrawn loan commitments ................... | - | - | 8,439 | 15,893 | 1,246 | 184 | 17,176 | 265 | - | 7,045 | 4,684 | 54,932 |
| Undrawn overdrafts ................................. | 8,444 | - | 14,001 | 3,216 | 302 | 7,391 | 7,426 | 449 | 3,852 | 1,987 | 8,098 | 55,166 |
| Credit card commitments ........................ | 22,311 | - | 4,630 | 876 | 34 | 252 | 1,069 | 206 | 1,303 | 316 | 194 | 31,191 |
| **Maximum credit exposure** | 545,817 | 212,784 | 199,352 | 63,986 | 11,565 | 134,973 | 118,319 | 27,775 | 16,498 | 128,607 | 133,328 | 1,593,004 |

Amounts are in ISK million

## 43. Cont'd

| At 31 December 2020 | Individuals | Central governments | Commerce and services | Construction | Energy | Financial services | Industrial and transportation | Investment companies | Public sector and non-profit organisations | Real estate | Seafood | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank ....... | - | 78,948 | - | - | - | - | - | - | - | - | - | 78,948 |
| Loans to credit institutions ......................... | - | - | - | - | - | 89,920 | - | - | - | - | - | 89,920 |
| Bonds and debt instruments ..................... | - | 107,502 | 22 | - | 1,257 | 18,192 | 116 | 7 | 191 | 929 | - | 128,216 |
| Derivatives ................................................ | - | 165 | 66 | - | - | 8,436 | 239 | 669 | - | 65 | 273 | 9,913 |
| Loans to customers: | 437,377 | - | 124,260 | 42,352 | 8,673 | 1,539 | 78,561 | 23,440 | 10,911 | 157,502 | 122,102 | 1,006,717 |
| Overdrafts ............................................... | 10,506 | - | 12,117 | 3,104 | 10 | 1,097 | 5,915 | 954 | 949 | 2,422 | 5,138 | 42,212 |
| Credit cards ............................................ | 14,942 | - | 1,170 | 247 | 6 | 14 | 318 | 23 | 77 | 62 | 29 | 16,888 |
| Mortgages ............................................... | 377,155 | - | - | - | - | - | - | - | - | - | - | 377,155 |
| Capital leases ......................................... | 5,612 | - | 26,236 | 2,742 | 16 | - | 7,328 | 153 | 38 | 1,058 | 176 | 43,359 |
| Government guarantee schemes ............ | 15 | - | 2,968 | 57 | - | - | 323 | 9 | - | 136 | 86 | 3,594 |
| Other loans ............................................. | 29,147 | - | 81,769 | 36,202 | 8,641 | 428 | 64,677 | 22,301 | 9,847 | 153,824 | 116,673 | 523,509 |
| Other financial assets ............................... | 437 | 645 | 110 | 10 | 6 | 2,285 | 29 | 39 | 88 | 35 | 8 | 3,692 |
| Off-balance sheet items: | 33,695 | - | 29,294 | 13,373 | 316 | 7,376 | 26,056 | 1,531 | 5,348 | 21,209 | 14,190 | 152,388 |
| Financial guarantees ............................... | 489 | - | 5,349 | 6,786 | - | 90 | 2,077 | 30 | 6 | 8,090 | 272 | 23,189 |
| Undrawn loan commitments ................... | - | - | 5,445 | 3,111 | - | - | 17,896 | 846 | - | 10,145 | 2,583 | 40,026 |
| Undrawn overdrafts ................................. | 9,722 | - | 13,826 | 2,679 | 286 | 7,051 | 4,901 | 446 | 4,026 | 2,664 | 11,145 | 56,746 |
| Credit card commitments ........................ | 23,484 | - | 4,674 | 797 | 30 | 235 | 1,182 | 209 | 1,316 | 310 | 190 | 32,427 |
| **Maximum credit exposure** | 471,509 | 187,260 | 153,752 | 55,735 | 10,252 | 127,748 | 105,001 | 25,686 | 16,538 | 179,740 | 136,573 | 1,469,794 |

## 44. Credit exposure covered by collateral

Collateral and other credit mitigants vary between types of obligors and credit facilities. For loans to individuals the principal collateral taken is residential property against mortgages. In the case of corporate entities the Group takes a charge over assets such as real estate, vessels, cash and securities as well as other collateral including accounts receivables, inventory, vehicles and equipment. Loans to government entities and to municipalities are more often than not unsecured. Derivative exposures are generally made under ISDA master agreements with Credit Support Annex or corresponding terms with pledged collateral in the form of cash and government bonds.

In some cases the Group uses guarantees as a credit enhancement but since guarantees effectively transfer credit risk from one counterparty to another they do not represent a reduction in maximum exposure to credit risk. Exception from this are Government guarantees issued in response to the COVID-19 pandemic which are shown under other collateral. Covenants in loan agreements are also an important credit enhancement but do not reduce maximum credit exposure.

Amounts are in ISK million

44. Cont'd

Valuation of collateral is based on market price, official valuation for tax purposes or expert opinion of the Group's employees, depending on availability. In the case of fishing vessels the associated fishing quota is included in the valuation. Collateral is allocated according to the gross carrying amount of loans and nominal off-balance sheet items, and is measured without including the effect of overcollateralisation. This means that if some loans have collateral values in excess of their gross carrying amount, then the excess is removed in order to reflect the Group's actual maximum exposure to credit risk. The total value of pledged assets can thus be higher than the cover indicates. The maximum credit risk exposure is measured on net carrying value basis, and therefore collateral allocation can in some instances be higher. For capital leases the Group remains the owner of the leased object. In total ISK 40,475 million of the collateral are leased objects.

The following table shows the maximum exposure to credit risk by class of financial asset and collateral held against those exposures. An overview of collateral held by the Group against credit exposure is shown below for exposures in Stages 1 and 2 (non credit-impaired) and exposures in Stage 3 (credit-impaired):

| **At 30 September 2021**<br>**Collateral held against non credit-impaired exposures** | Maximum exposure to credit risk | Residential real estate | Commercial real estate | Vessels | Cash & securities | Vehicles & equipment | Other collateral | Total credit exposure covered by collateral | Total credit exposure not covered by collateral | Associated ECL |
|---|---|---|---|---|---|---|---|---|---|---|
| Derivatives | 22,262 | - | - | - | 9,560 | - | - | 9,560 | 12,702 | - |
| Loans and commitments to customers: | 1,226,475 | 496,831 | 291,650 | 96,461 | 4,976 | 51,118 | 91,637 | 1,032,673 | 193,802 | 9,738 |
| Individuals | 539,756 | 450,479 | 9,802 | - | 241 | 15,578 | 222 | 476,322 | 63,434 | 1,529 |
| Commerce and services | 193,516 | 15,739 | 68,777 | 147 | 827 | 26,863 | 27,788 | 140,141 | 53,375 | 4,792 |
| Construction | 62,367 | 9,313 | 27,683 | 7 | 1,051 | 2,436 | 3,154 | 43,644 | 18,723 | 612 |
| Energy | 11,095 | 27 | 7,754 | - | 37 | 7 | 14 | 7,839 | 3,256 | 45 |
| Financial services | 9,860 | - | 1,395 | - | 1 | - | 834 | 2,230 | 7,630 | 3 |
| Industrial and transportation | 115,270 | 1,260 | 59,040 | 1,272 | 175 | 5,772 | 22,757 | 90,276 | 24,994 | 818 |
| Investment companies | 22,991 | 1,442 | 6,593 | - | 2,096 | 70 | 11,742 | 21,943 | 1,048 | 637 |
| Public sector and non-profit organisations | 15,077 | 92 | 784 | - | 4 | 26 | - | 906 | 14,171 | 17 |
| Real estate | 123,798 | 17,635 | 97,292 | - | 469 | 268 | 2,729 | 118,393 | 5,405 | 1,057 |
| Seafood | 132,745 | 844 | 12,530 | 95,035 | 75 | 98 | 22,397 | 130,979 | 1,766 | 228 |
| **Total** | 1,248,737 | 496,831 | 291,650 | 96,461 | 14,536 | 51,118 | 91,637 | 1,042,233 | 206,504 | 9,738 |
| **Collateral held against credit-impaired exposures** | | | | | | | | | | |
| Loans and commitments to customers: | 16,309 | 5,439 | 5,787 | 1,959 | 114 | 678 | 812 | 14,789 | 1,520 | 6,311 |
| Individuals | 4,979 | 4,041 | 321 | 19 | 2 | 120 | 3 | 4,506 | 473 | 652 |
| Commerce and services | 4,487 | 475 | 1,903 | 678 | - | 202 | 496 | 3,754 | 733 | 2,850 |
| Construction | 1,619 | 10 | 1,279 | - | 73 | 101 | 41 | 1,504 | 115 | 113 |
| Industrial and transportation | 2,707 | 375 | 402 | 1,252 | 14 | 242 | 270 | 2,555 | 152 | 1,960 |
| Investment companies | 531 | 13 | 502 | - | - | 5 | - | 520 | 11 | 124 |
| Public sector and non-profit organisations | 1 | - | - | - | - | - | - | - | 1 | 1 |
| Real estate | 1,959 | 518 | 1,368 | 5 | 25 | 8 | 2 | 1,926 | 33 | 543 |
| Seafood | 26 | 7 | 12 | 5 | - | - | - | 24 | 2 | 68 |
| **Total** | 16,309 | 5,439 | 5,787 | 1,959 | 114 | 678 | 812 | 14,789 | 1,520 | 6,311 |

Amounts are in ISK million

44. Cont'd

| At 31 December 2020 / Collateral held against non credit-impaired exposures | Maximum exposure to credit risk | Residential real estate | Commercial real estate | Vessels | Cash & securities | Vehicles & equipment | Other collateral | Total credit exposure covered by collateral | Total credit exposure not covered by collateral | Associated ECL |
|---|---|---|---|---|---|---|---|---|---|---|
| Derivatives | 9,913 | - | - | - | 5,318 | - | - | 5,318 | 4,595 | - |
| Loans and commitments to customers: | 1,136,660 | 398,644 | 307,452 | 95,947 | 11,869 | 49,504 | 102,673 | 966,089 | 170,571 | 10,957 |
| Individuals | 464,333 | 357,801 | 24,704 | 7 | 376 | 14,327 | 151 | 397,366 | 66,967 | 1,939 |
| Commerce and services | 149,751 | 14,754 | 46,856 | 157 | 659 | 25,444 | 32,211 | 120,081 | 29,670 | 4,029 |
| Construction | 54,812 | 7,036 | 34,293 | 11 | 1,297 | 2,108 | 2,249 | 46,994 | 7,818 | 570 |
| Energy | 8,989 | - | 6,545 | - | 1 | 14 | 14 | 6,574 | 2,415 | 25 |
| Financial services | 8,915 | 357 | 726 | - | 26 | - | 3,543 | 4,652 | 4,263 | 2 |
| Industrial and transportation | 102,499 | 1,174 | 38,576 | 12 | 178 | 7,088 | 29,500 | 76,528 | 25,971 | 1,127 |
| Investment companies | 21,626 | 1,054 | 5,849 | - | 1,891 | 79 | 11,125 | 19,998 | 1,628 | 709 |
| Public sector and non-profit organisations | 16,258 | 108 | 899 | - | 5 | 28 | - | 1,040 | 15,218 | 20 |
| Real estate | 173,328 | 16,122 | 133,869 | - | 7,424 | 343 | 1,157 | 158,915 | 14,413 | 2,280 |
| Seafood | 136,149 | 238 | 15,135 | 95,760 | 12 | 73 | 22,723 | 133,941 | 2,208 | 256 |
| **Total** | 1,146,573 | 398,644 | 307,452 | 95,947 | 17,187 | 49,504 | 102,673 | 971,407 | 175,166 | 10,957 |
| **Collateral held against credit-impaired exposures** | | | | | | | | | | |
| Loans and commitments to customers: | 22,445 | 8,469 | 6,175 | 1,556 | 2,704 | 725 | 917 | 20,546 | 1,899 | 7,612 |
| Individuals | 6,739 | 5,436 | 537 | 21 | 3 | 144 | 4 | 6,145 | 594 | 935 |
| Commerce and services | 3,803 | 417 | 1,289 | 691 | 3 | 232 | 780 | 3,412 | 391 | 2,573 |
| Construction | 913 | 111 | 519 | - | - | 87 | 50 | 767 | 146 | 151 |
| Industrial and transportation | 2,118 | 46 | 385 | 810 | 51 | 246 | 71 | 1,609 | 509 | 1,922 |
| Investment companies | 3,345 | 104 | 610 | - | 2,611 | 6 | - | 3,331 | 14 | 284 |
| Public sector and non-profit organisations | 1 | - | 1 | - | - | - | - | 1 | - | - |
| Real estate | 5,383 | 2,348 | 2,734 | 5 | 36 | 7 | 12 | 5,142 | 241 | 1,565 |
| Seafood | 143 | 7 | 100 | 29 | - | 3 | - | 139 | 4 | 182 |
| **Total** | 22,445 | 8,469 | 6,175 | 1,556 | 2,704 | 725 | 917 | 20,546 | 1,899 | 7,612 |

Amounts are in ISK million

## 45. Credit quality of financial assets

The following tables provide the gross carrying amount of loans and credit risk exposure on loan commitments and financial guarantees. Amounts are broken down by risk class and the method by which their respective credit loss allowances (ECL) are calculated, i.e. Stage 1, 2 and 3.

The Group uses internal rating models to assess the default probability of corporate and retail customers. The models assign each customer to one of ten risk classes. One risk class is for customers in default (risk class 10), and nine risk classes are for performing customers (risk classes 1-9). Risk classes are assigned on customer level and not facility level.

The rating of corporate customers is based on a company's most recent financial statements, together with a qualitative assessment of its management, market position and industry sector.

For retail customers the Group uses two different statistical rating models. One model is for individuals and another is for small companies with a total exposure to the Group of less than ISK 150 million. These models are behavioural scoring models and use information about a customer's payment history, amount of debt and deposits, and demographic variables to assess the probability that a customer will default on any of his obligations within 12 months of the rating assessment. A new risk assessment model for individuals was introduced in the third quarter of 2021. For further information see Note 2.

Risk classes 1-4 represent low risk, risk classes 5-6 moderate risk, risk classes 7-8 increased risk, risk class 9 high risk, and risk class 10 represents customers that are in default. Unrated are loans that are yet to be rated.

Further information on the risk classes, including the mapping from risk classes to the probability of default, can be found in Section 4.2.2 of the unaudited Pillar 3 2020 Report.

The same customer can have loans and off-balance sheet commitments in Stages 1 and 2 simultaneously. However, if a customer has an exposure in Stage 3 then all other loans and commitments are classified as Stage 3 as well.

**At 30 September 2021**

| Loans to customers: | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Risk class 1-4 ... | 395,105 | 2,121 | - | 397,226 |
| Risk class 5-6 ... | 335,241 | 63,924 | - | 399,165 |
| Risk class 7-8 ... | 186,219 | 63,761 | - | 249,980 |
| Risk class 9 ... | 13,960 | 12,126 | - | 26,086 |
| Risk class 10 ... | - | - | 22,014 | 22,014 |
| Unrated ... | 1,228 | 776 | - | 2,004 |
| | 931,753 | 142,708 | 22,014 | 1,096,475 |
| Expected credit losses ... | ( 3,413) | ( 5,470) | ( 6,174) | ( 15,057) |
| **Net carrying amount** | 928,340 | 137,238 | 15,840 | 1,081,418 |

| Off-balance sheet loan commitments and financial guarantees: | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Risk class 1-4 ... | 77,871 | 1,170 | - | 79,041 |
| Risk class 5-6 ... | 42,350 | 5,252 | - | 47,602 |
| Risk class 7-8 ... | 18,272 | 15,819 | - | 34,091 |
| Risk class 9 ... | 367 | 390 | - | 757 |
| Risk class 10 ... | - | - | 606 | 606 |
| Unrated ... | 103 | 158 | - | 261 |
| | 138,963 | 22,789 | 606 | 162,358 |
| Expected credit losses ... | ( 497) | ( 358) | ( 137) | ( 992) |
| **Total** | 138,466 | 22,431 | 469 | 161,366 |

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| At 30 September 2021 | Risk class 1-4 | Risk class 5-6 | Risk class 7-8 | Risk class 9 | Risk class 10 | Unrated | ECL | Total |
|---|---|---|---|---|---|---|---|---|
| Loans and commitments to customers: | | | | | | | | |
| Individuals | 230,646 | 195,384 | 105,433 | 10,109 | 5,341 | 3 | ( 2,181) | 544,735 |
| Commerce and services | 41,162 | 73,275 | 72,889 | 9,652 | 7,560 | 1,107 | ( 7,642) | 198,003 |
| Construction | 12,148 | 20,096 | 29,133 | 1,188 | 1,749 | 397 | ( 725) | 63,986 |
| Energy | 4,709 | 5,534 | 897 | - | - | - | ( 45) | 11,095 |
| Financial services | 7,560 | 1,748 | 540 | - | - | 15 | ( 3) | 9,860 |
| Industrial and transportation | 29,667 | 57,143 | 27,469 | 1,186 | 4,662 | 628 | ( 2,778) | 117,977 |
| Investment companies | 1,710 | 6,056 | 15,004 | 850 | 661 | 2 | ( 761) | 23,522 |
| Public sector and non-profit organisations | 13,396 | 1,399 | 273 | - | - | 28 | ( 18) | 15,078 |
| Real estate | 49,227 | 40,927 | 31,003 | 3,602 | 2,515 | 83 | ( 1,600) | 125,757 |
| Seafood | 86,042 | 45,205 | 1,430 | 256 | 132 | 2 | ( 296) | 132,771 |
| **Total** | 476,267 | 446,767 | 284,071 | 26,843 | 22,620 | 2,265 | ( 16,049) | 1,242,784 |

**At 31 December 2020**

| Loans to customers: | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Risk class 1-4 | 232,806 | 1,209 | - | 234,015 |
| Risk class 5-6 | 346,781 | 62,788 | - | 409,569 |
| Risk class 7-8 | 217,368 | 80,867 | - | 298,235 |
| Risk class 9 | 38,290 | 14,684 | - | 52,974 |
| Risk class 10 | - | - | 29,247 | 29,247 |
| Unrated | 190 | 1 | - | 191 |
| | 835,435 | 159,549 | 29,247 | 1,024,231 |
| Expected credit losses | ( 3,645) | ( 6,482) | ( 7,387) | ( 17,514) |
| **Net carrying amount** | 831,790 | 153,067 | 21,860 | 1,006,717 |

| Off-balance sheet loan commitments and financial guarantees: | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Risk class 1-4 | 64,781 | 1,341 | - | 66,122 |
| Risk class 5-6 | 51,169 | 6,461 | - | 57,630 |
| Risk class 7-8 | 10,852 | 16,227 | - | 27,079 |
| Risk class 9 | 1,142 | 553 | - | 1,695 |
| Risk class 10 | - | - | 809 | 809 |
| Unrated | 99 | 8 | - | 107 |
| | 128,043 | 24,590 | 809 | 153,442 |
| Expected credit losses | ( 347) | ( 483) | ( 225) | ( 1,055) |
| **Total** | 127,696 | 24,107 | 584 | 152,387 |

Amounts are in ISK million

## 45. Cont'd

| At 31 December 2020 | Risk class 1-4 | Risk class 5-6 | Risk class 7-8 | Risk class 9 | Risk class 10 | Unrated | ECL | Total |
|---|---|---|---|---|---|---|---|---|
| Loans and commitments to customers: | | | | | | | | |
| Individuals | 94,574 | 182,706 | 153,088 | 35,928 | 7,646 | 4 | ( 2,874) | 471,072 |
| Commerce and services | 25,813 | 62,494 | 58,182 | 7,121 | 6,402 | 144 | ( 6,602) | 153,554 |
| Construction | 4,809 | 22,332 | 26,078 | 2,130 | 1,064 | 33 | ( 721) | 55,725 |
| Energy | 5,006 | 3,338 | 670 | - | - | - | ( 25) | 8,989 |
| Financial services | 5,816 | 2,650 | 443 | - | - | 8 | ( 2) | 8,915 |
| Industrial and transportation | 15,557 | 56,578 | 28,547 | 2,895 | 4,039 | 50 | ( 3,049) | 104,617 |
| Investment companies | 868 | 5,171 | 14,695 | 1,599 | 3,628 | 2 | ( 993) | 24,970 |
| Public sector and non-profit organisations | 14,525 | 1,400 | 324 | 1 | 1 | 28 | ( 20) | 16,259 |
| Real estate | 46,297 | 82,945 | 42,299 | 4,057 | 6,950 | 8 | ( 3,845) | 178,711 |
| Seafood | 86,872 | 47,585 | 988 | 938 | 326 | 21 | ( 438) | 136,292 |
| **Total** | 300,137 | 467,199 | 325,314 | 54,669 | 30,056 | 298 | ( 18,569) | 1,159,104 |

## 46. Loans to customers in the tourism industry likely to be vulnerable to COVID-19 pandemic

Companies susceptible to the impact of COVID-19 pandemic were classified into four groups based on an assessment of how much of an increase in credit risk these companies face in the short, medium and long term. In addition, to account for the material uncertainty in the operating environment of companies in the tourism industry, not reflected in their current risk class, they are further classified into four groups based on an assessment of how vulnerable they are to various assumptions on when tourists can be expected to start visiting Iceland again. The base case assumes around 600,000 tourists in Iceland in 2021.

Impact group 1: viable even though significantly fewer tourists arrive in the year 2021
Impact group 2: viable with forbearance even though significantly fewer tourists arrive in the year 2021
Impact group 3: viable if the number of tourists in the year 2021 is similar to the base case
Impact group 4: viable if the year 2021 turns out to be better than the base case

Where the increase was found to be significant (groups 2-4), the exposure was transferred to Stage 2. In addition, an overlay factor was applied to the expected credit losses, comparable to an increase in up to three risk classes, and a higher haircut was applied to value of collateral for the higher impact groups in the more severe scenarios.

**At 30 September 2021**

| Loans to customers in the tourism industry: | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Group 1 | 4,575 | 20,151 | 246 | 24,972 |
| Group 2 | - | 51,858 | 1,518 | 53,376 |
| Group 3 | - | 21,120 | 1,202 | 22,322 |
| Group 4 | - | 346 | 2,299 | 2,645 |
| | 4,575 | 93,475 | 5,265 | 103,315 |
| Expected credit losses | ( 31) | ( 4,142) | ( 1,446) | ( 5,619) |
| **Net carrying amount** | 4,544 | 89,333 | 3,819 | 97,696 |

Off-balance sheet loan commitments and financial guarantees to customers in the tourism industry:

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Group 1 | 155 | 1,578 | - | 1,733 |
| Group 2 | - | 14,989 | 262 | 15,251 |
| Group 3 | - | 2,667 | 16 | 2,683 |
| Group 4 | - | 41 | 16 | 57 |
| | 155 | 19,275 | 294 | 19,724 |
| Expected credit losses | ( 1) | ( 285) | ( 61) | ( 347) |
| **Total** | 154 | 18,990 | 233 | 19,377 |

Amounts are in ISK million

## 46. Cont'd

**At 31 December 2020**

| Loans to customers in the tourism industry: | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Group 1 | 1,903 | 308 | - | 2,211 |
| Group 2 | - | 30,503 | 406 | 30,909 |
| Group 3 | - | 58,610 | 2,579 | 61,189 |
| Group 4 | - | 3,317 | 3,612 | 6,929 |
| | 1,903 | 92,738 | 6,597 | 101,238 |
| Expected credit losses | ( 24) | ( 4,483) | ( 2,529) | ( 7,036) |
| **Net carrying amount** | 1,879 | 88,255 | 4,068 | 94,202 |

Off-balance sheet loan commitments and financial guarantees to customers in the tourism industry:

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Group 1 | 50 | 2 | - | 52 |
| Group 2 | - | 13,416 | 51 | 13,467 |
| Group 3 | - | 5,118 | 163 | 5,281 |
| Group 4 | - | 429 | 17 | 446 |
| | 50 | 18,965 | 231 | 19,246 |
| Expected credit losses | ( 3) | ( 363) | ( 101) | ( 467) |
| **Total** | 47 | 18,602 | 130 | 18,779 |

## 47. Forbearance

When restructuring or modification measures are believed to be more appropriate than collection procedures, the Group offers several debt relief measures and restructuring frameworks for customers in financial difficulties. These forbearance measures include temporary payment holidays, extension of loan terms, capitalisation of arrears, and waiving of covenants.

The relationship between forbearance and stages is discussed in Note 67.4 in the consolidated financial statements for the year 2020.

Once an asset has been classified as forborne, it will remain forborne for a minimum 24-month probation period. In order for a loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:
- All of the customer's facilities have to be considered performing; and
- The customer does not have any contract that is more than 30 days past due; and
- The probation period of two years has passed from the date of the forbearance event; and
- Regular payments of more than an insignificant amount of principal or interest have been made during at least half of the probation period.

The tourism industry is an important economic sector in Iceland but due to the nature of tourism, its effects are not limited to hotels, car rentals, and tour guides. The Group therefore monitors the tourism industry internally as a quasi-sector instead of a new separate sector. Real estate companies that do not operate directly in the tourism sector but rely in part on rental income from such activities explain around half of the forbearance amount for companies not in tourism.

The following table provides a summary of the Group's forborne assets.

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## 47. Cont'd

| At 30 September 2021 | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Individuals | 1,686 | 6,623 | 1,530 | 9,839 |
| Companies | 5,471 | 88,842 | 10,794 | 105,107 |
| - In the tourism quasi-sector | - | 60,848 | 5,028 | 65,876 |
| - Other than the tourism quasi-sector | 5,471 | 27,994 | 5,766 | 39,231 |
| **Gross carrying amount** | 7,157 | 95,465 | 12,324 | 114,946 |

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Individuals | ( 13) | ( 131) | ( 168) | ( 312) |
| Companies | ( 27) | ( 3,667) | ( 3,945) | ( 7,639) |
| - In the tourism quasi-sector | - | ( 2,870) | ( 1,489) | ( 4,359) |
| - Other than the tourism quasi-sector | ( 27) | ( 797) | ( 2,456) | ( 3,280) |
| **Expected credit losses** | ( 40) | ( 3,798) | ( 4,113) | ( 7,951) |

| At 31 December 2020 | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Individuals | 932 | 5,249 | 2,068 | 8,249 |
| Companies | 209 | 104,523 | 13,608 | 118,340 |
| - In the tourism quasi-sector | - | 62,295 | 5,747 | 68,042 |
| - Other than the tourism quasi-sector | 209 | 42,228 | 7,861 | 50,298 |
| **Gross carrying amount** | 1,141 | 109,772 | 15,676 | 126,589 |

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Individuals | ( 10) | ( 127) | ( 176) | ( 313) |
| Companies | ( 1) | ( 4,114) | ( 4,147) | ( 8,262) |
| - In the tourism quasi-sector | - | ( 2,787) | ( 1,888) | ( 4,675) |
| - Other than the tourism quasi-sector | ( 1) | ( 1,327) | ( 2,259) | ( 3,587) |
| **Expected credit losses** | ( 11) | ( 4,241) | ( 4,323) | ( 8,575) |

## 48. Assets obtained by taking possession of collateral

Details of non-financial assets obtained by the Group during the period by taking possession of collateral held as security against loans.

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Property and land | 135 | 1,754 |
| Industrial equipment and vehicles | 67 | 86 |
| **Total** | 202 | 1,840 |

The Group pursues realisation of the collateral in an orderly manner. The Group does not generally use the non-cash collateral for its own operations.

Amounts are in ISK million

## 49. Write-offs

When the Group has no reasonable expectations of recovering a credit exposure or when it is uneconomical to pursue legal collection, the financial asset is written off. A write-off does not change the debt obligation which is therefore still subject to enforcement activity. Any recoveries of amounts previously written off are credited to the income statement.

| **Gross carrying amount written off and still subject to enforcement activity** | 2021<br>1.1-30.9 | 2020<br>1.1-30.9 |
|---|---|---|
| Individuals | 297 | 338 |
| Companies | 456 | 925 |
| **Total** | 753 | 1,263 |

## 50. Large exposures disclosure

When the Group's total exposure to a group of connected clients is 10% or higher of the Group's Tier 1 capital it is considered a large exposure. Note that the regulatory definition has changed since last reporting. Previously, exposures were considered large when the value of the exposure exceeded 10% of total capital base instead of Tier 1 capital. Both on-balance sheet and off-balance sheet items from all types of financial instruments are included in the exposure as defined by regulation no. 233/2017. The Group has internal criteria that define connections between clients. These criteria reflect the Group's interpretation of Article (1)(a) of the Act on Financial Undertakings no. 161/2002, where groups of connected clients are defined. Since the interim financial statements for the third quarter of the year are not audited, the official capital is based on reviewed own fund items at 30 June 2021.

The exposure is evaluated both before and after credit risk mitigating effects. After mitigating effects, the Group currently has two large exposures. The increase since last reporting is partly due to new definition of large exposures. No large exposure is above the maximum 25% large exposure limit set by the law.

The Group's largest exposure before eligible credit risk mitigating effects is the Icelandic Government. Biggest part of the exposure is due to Icelandic Government Bonds in the Group's liquidity portfolio.

The following table shows the Group's large exposures before and after eligible credit risk mitigating effects as a percentage of the Tier 1 capital as at 30 September 2021, and the Group's Total capital base as at 31 December 2020.

**At 30 September 2021**

| Groups of connected clients: | Before | After |
|---|---|---|
| Group 1 | 101% | 7% |
| Group 2 | 13% | 11% |
| Group 3 | 13% | 12% |

**At 31 December 2020**

| Groups of connected clients: | Before | After |
|---|---|---|
| Group 1 | 65% | - |
| Group 2 | 13% | 10% |

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## 51. Liquidity risk

The Group defines liquidity risk as the risk of not being able to fund its financial obligations or planned growth, or only being able to do so substantially above the prevailing market cost of funds.

The Group's main source of funding is customer deposits. Treasury is responsible for the Bank's funding and liquidity management in line with internal and regulatory limits and policies. Treasury manages the Bank's intraday liquidity. Risk Management, as the second line of defence, is responsible for independent reporting on the liquidity position to internal and external stakeholders and providing a holistic view on liquidity risk on a consolidated basis.

## 52. Liquidity coverage and Net stable funding ratio

Key measures for the assessment of liquidity risk are the Liquidity Coverage Ratio ("LCR") and Net Stable Funding Ratio ("NSFR"). The Central Bank of Iceland, which is the main supervisory authority regarding liquidity risk, has incorporated the LCR and the NSFR based on the CRD IV standards into the rules on liquidity ratio and the rules on funding ratio in foreign currencies. In addition, the Group complies with the Financial Supervisory Authority of the Central Bank's guidelines no. 2/2010 on best practices in liquidity management and liquidity coverage ratio rules no. 266/2017.

The following tables show the NSFR and the LCR for the Group at 30 September 2021 and at year-end 2020.

| **Net stable funding ratio** | 30.9.2021 | 31.12.2020 |
|---|---|---|
| For all currencies | 121% | 123% |
| Foreign currencies | 166% | 179% |

| **Liquidity coverage ratio** | 30.9.2021 | 31.12.2020 |
|---|---|---|
| For all currencies | 225% | 196% |
| ISK | 124% | 95% |
| Foreign currencies | 384% | 463% |

| **At 30 September 2021** | For all currencies | | ISK | | Foreign currencies | |
|---|---|---|---|---|---|---|
| | Unweighted | Weighted | Unweighted | Weighted | Unweighted | Weighted |
| Liquid assets level 1* | 190,046 | 190,046 | 161,482 | 161,482 | 28,564 | 28,564 |
| Liquid assets level 2 | 41,560 | 13,261 | 41,151 | 13,261 | 409 | - |
| **Total liquid assets** | 231,606 | 203,307 | 202,633 | 174,743 | 28,973 | 28,564 |
| Deposits | 617,271 | 174,565 | 544,215 | 149,069 | 73,056 | 25,496 |
| Debt issued | 1,385 | 1,385 | 1,282 | 1,282 | 103 | 103 |
| Other outflows | 93,726 | 31,469 | 66,828 | 27,299 | 26,898 | 4,170 |
| **Total outflows** | 712,382 | 207,419 | 612,325 | 177,650 | 100,057 | 29,769 |
| Short-term deposits with other banks** | 82,604 | 81,437 | 3,592 | 3,592 | 79,012 | 77,845 |
| Other inflows | 50,998 | 35,759 | 46,384 | 33,260 | 4,614 | 2,499 |
| Restrictions on inflows | - | - | - | - | ( 8,582) | ( 58,016) |
| **Total inflows** | 133,602 | 117,196 | 49,976 | 36,852 | 75,044 | 22,328 |
| **Liquidity coverage ratio** | | 225% | | 124% | | 384% |

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| At 31 December 2020 | For all currencies | | ISK | | Foreign currencies | |
|---|---|---|---|---|---|---|
| | Unweighted | Weighted | Unweighted | Weighted | Unweighted | Weighted |
| Liquid assets level 1* | 182,104 | 182,104 | 138,078 | 138,078 | 44,027 | 44,027 |
| Liquid assets level 2 | 14,648 | 2,941 | 14,470 | 2,941 | 178 | - |
| **Total liquid assets** | 196,752 | 185,045 | 152,548 | 141,019 | 44,205 | 44,027 |
| Deposits | 542,123 | 147,611 | 472,073 | 120,974 | 70,049 | 26,636 |
| Debt issued | 2,271 | 2,271 | 47 | 47 | 2,225 | 2,225 |
| Other outflows | 99,949 | 44,756 | 68,500 | 35,605 | 31,449 | 9,151 |
| **Total outflows** | 644,343 | 194,638 | 540,620 | 156,626 | 103,723 | 38,012 |
| Short-term deposits with other banks** | 88,495 | 88,328 | 2,077 | 2,077 | 86,419 | 86,252 |
| Other inflows | 29,842 | 11,981 | 21,342 | 6,221 | 8,500 | 5,760 |
| Restrictions on inflows | - | - | - | - | ( 17,126) | ( 63,503) |
| **Total inflows** | 118,337 | 100,309 | 23,419 | 8,298 | 77,793 | 28,509 |
| **Liquidity coverage ratio** | | 196% | | 95% | | 463% |

*Level 1 liquid assets include cash and balances with the Central Bank, domestic bonds and foreign government bonds in accordance with rules no. 266/2017 on liquidity ratio.

**Short-term deposits with other banks with maturity less than 30 days.

## Deposits by liquidity coverage ratio category

The Group's deposits are categorised by counterparty according to the Liquidity Coverage Ratio ("LCR") standard. The groups are listed in order of estimated stability and the respective LCR outflow weight. Deposits are also classified as stable if the customer has an established business relationship with the Bank and is covered by an effective insurance scheme.

| At 30 September 2021 | Deposits maturing within 30 days | | | | | |
|---|---|---|---|---|---|---|
| | Less stable | Weight (%) | Stable | Weight (%) | Term deposits | Total deposits |
| Retail | 130,854 | 13% | 265,124 | 5% | 74,303 | 470,281 |
| Operational relationships | 3,141 | 25% | - | 5% | - | 3,141 |
| Corporations | 107,262 | 40% | 2,921 | 20% | 28,763 | 138,946 |
| Sovereigns, Central Bank and public sector entities | 12,501 | 40% | 1,294 | 20% | 5,592 | 19,387 |
| Pension funds | 50,270 | 100% | - | - | 18,113 | 68,383 |
| Domestic financial entities | 40,674 | 100% | - | - | 21,811 | 62,485 |
| Foreign financial entities | 3,230 | 100% | - | - | 8,998 | 12,228 |
| **Total** | 347,932 | | 269,339 | | 157,580 | 774,851 |

| At 31 December 2020 | Deposits maturing within 30 days | | | | | |
|---|---|---|---|---|---|---|
| | Less stable | Weight (%) | Stable | Weight (%) | Term deposits | Total deposits |
| Retail | 120,510 | 14% | 247,625 | 5% | 75,971 | 444,106 |
| Operational relationships | 3,155 | 25% | - | 5% | - | 3,155 |
| Corporations | 77,705 | 40% | 1,959 | 20% | 24,965 | 104,629 |
| Sovereigns, Central Bank and public sector entities | 6,340 | 40% | 1,174 | 20% | 934 | 8,448 |
| Pension funds | 39,105 | 100% | - | - | 23,754 | 62,859 |
| Domestic financial entities | 38,284 | 100% | - | - | 41,647 | 79,931 |
| Foreign financial entities | 6,266 | 100% | - | - | 9,819 | 16,085 |
| **Total** | 291,365 | | 250,758 | | 177,090 | 719,213 |

Amounts are in ISK million

## 53. Maturity analysis of financial assets and financial liabilities

The following tables show the maturity profile of the Group's financial assets and the undiscounted cash flows of its financial liabilities. Maturity classification of assets is based on contractual maturity.

Bonds and debt instruments are based on contractual maturity and do not therefore represent the estimated liquidation time of the trading book.

The tables show undiscounted contractual payments of principal and interest for the Group's financial liabilities. Thus, the total figures for each liability class are higher than the respective balance sheet amount. Cash flows for payments of unknown nature, such as for floating rate, CPI-linked or foreign currency denominated instruments, are based on internal yield curves and forecasts.

For dated financial liabilities the amounts are grouped into maturity buckets according to contractual maturities of principal and estimated contractual payments of interest. For demand deposits or other non-dated liabilities, the figures are grouped according to the first possible required payment date.

The following tables also show the contractual cash flow of the Group's derivative liabilities, i.e. derivatives that have a negative and a positive carrying amount at the reporting date. For derivatives settled on a gross basis, the cash flow for both legs of the derivative is shown, since netting cannot be applied upon settlement.

| **At 30 September 2021** | Carrying amount | On demand | Up to 3 months | 3-12 months | 1-5 years | Over 5 years | No maturity | Total |
|---|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank | 110,233 | 35,456 | 74,775 | 2 | - | - | - | 110,233 |
| Loans to credit institutions | 81,117 | 33,372 | 47,745 | - | - | - | - | 81,117 |
| Bonds and debt instruments | 123,599 | - | 31,061 | 28,835 | 58,016 | 5,687 | - | 123,599 |
| Loans to customers | 1,081,418 | 5,444 | 78,359 | 104,776 | 323,803 | 569,036 | - | 1,081,418 |
| Shares and equity instruments | 31,456 | - | - | - | - | - | 31,456 | 31,456 |
| Other financial assets | 13,009 | 12,526 | 352 | 131 | - | - | - | 13,009 |
| **Total financial assets** | 1,440,832 | 86,798 | 232,292 | 133,744 | 381,819 | 574,723 | 31,456 | 1,440,832 |
| | | | | | | | | |
| Deposits from CB and credit institutions | 20,409 | 7,075 | 8,140 | 3,258 | 1,994 | - | - | 20,467 |
| Deposits from customers | 754,442 | 621,160 | 73,413 | 43,984 | 24,962 | 27,541 | - | 791,060 |
| Debt issued and other borrowed funds | 397,672 | - | 2,946 | 99,317 | 308,374 | 55,791 | - | 466,428 |
| Subordinated loans | 36,923 | - | 311 | 731 | 17,173 | 28,358 | - | 46,573 |
| Other financial liabilities: | 30,889 | 24,269 | 1,435 | 1,132 | 1,843 | 1,959 | - | 30,638 |
| Lease liabilities | 3,895 | - | 130 | 387 | 1,811 | 1,959 | - | 4,287 |
| Other liabilities | 26,994 | 24,269 | 1,305 | 745 | 32 | - | - | 26,351 |
| **Total financial liabilities** | 1,240,335 | 652,504 | 86,245 | 148,422 | 354,346 | 113,649 | - | 1,355,166 |

| | On demand | Up to 3 months | 3-12 months | 1-5 years | Over 5 years | No maturity | Total |
|---|---|---|---|---|---|---|---|
| **Gross settled derivatives** | | | | | | | |
| Inflow | - | 23,714 | 15,805 | 13,300 | - | - | 52,819 |
| Outflow | - | ( 22,077) | ( 14,036) | ( 11,230) | - | - | ( 47,343) |
| Total | - | 1,637 | 1,769 | 2,070 | - | - | 5,476 |
| Net settled derivatives | - | 392 | - | - | - | - | 392 |
| **Total derivative financial assets** | - | 2,029 | 1,769 | 2,070 | - | - | 5,868 |
| **Gross settled derivatives** | | | | | | | |
| Inflow | - | 69,347 | 17,376 | 36,891 | - | - | 123,614 |
| Outflow | - | ( 77,662) | ( 19,801) | ( 40,263) | - | - | ( 137,726) |
| Total | - | ( 8,315) | ( 2,425) | ( 3,372) | - | - | ( 14,112) |
| Net settled derivatives | - | ( 3,881) | ( 1) | - | - | - | ( 3,882) |
| **Total derivative financial liabilities** | - | ( 12,196) | ( 2,426) | ( 3,372) | - | - | ( 17,994) |
| **Total net financial assets and financial liabilities** | ( 565,706) | 160,272 | ( 10,484) | 32,915 | 461,074 | 31,456 | 109,528 |

Amounts are in ISK million

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| **At 31 December 2020** | Carrying amount | On demand | Up to 3 months | 3-12 months | 1-5 years | Over 5 years | No maturity | Total |
|---|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank | 78,948 | 29,600 | 48,060 | - | - | 1,288 | - | 78,948 |
| Loans to credit institutions | 89,920 | 46,102 | 43,818 | - | - | - | - | 89,920 |
| Bonds and debt instruments | 128,216 | - | 38,169 | 34,776 | 48,047 | 7,224 | | 128,216 |
| Loans to customers | 1,006,717 | 2,562 | 81,090 | 96,084 | 334,520 | 492,461 | - | 1,006,717 |
| Shares and equity instruments | 14,851 | - | - | - | - | - | 14,851 | 14,851 |
| Other financial assets | 3,692 | 2,483 | 560 | 643 | 6 | - | - | 3,692 |
| **Total financial assets** | 1,322,344 | 80,747 | 211,697 | 131,503 | 382,573 | 500,973 | 14,851 | 1,322,344 |
| | | | | | | | | |
| Deposits from CB and credit institutions | 39,758 | 6,073 | 20,044 | 10,278 | 3,368 | - | - | 39,763 |
| Deposits from customers | 679,455 | 539,932 | 65,532 | 56,764 | 23,409 | 27,016 | - | 712,653 |
| Debt issued and other borrowed funds | 387,274 | - | 12,677 | 31,569 | 327,003 | 93,434 | - | 464,683 |
| Subordinated loans | 27,194 | - | 176 | 477 | 3,096 | 29,903 | - | 33,652 |
| Other financial liabilities: | 9,721 | 3,570 | 1,453 | 1,227 | 1,783 | 2,123 | - | 10,156 |
| Lease liabilities | 3,962 | - | 123 | 369 | 1,783 | 2,123 | - | 4,398 |
| Other liabilities | 5,759 | 3,571 | 1,330 | 858 | - | - | - | 5,759 |
| **Total financial liabilities** | 1,143,402 | 549,575 | 99,882 | 100,315 | 358,659 | 152,476 | - | 1,260,907 |

| | On demand | Up to 3 months | 3-12 months | 1-5 years | Over 5 years | No maturity | Total |
|---|---|---|---|---|---|---|---|
| **Gross settled derivatives** | | | | | | | |
| Inflow | - | 41,288 | 46,627 | 39,643 | - | - | 127,558 |
| Outflow | - | ( 38,823) | ( 45,090) | ( 36,516) | - | - | ( 120,429) |
| Total | - | 2,465 | 1,537 | 3,127 | - | - | 7,129 |
| Net settled derivatives | - | 90 | - | - | - | - | 90 |
| **Total derivative financial assets** | - | 2,555 | 1,537 | 3,127 | - | - | 7,219 |
| | | | | | | | |
| **Gross settled derivatives** | | | | | | | |
| Inflow | - | 29,311 | 18,714 | 29,943 | - | - | 77,968 |
| Outflow | - | ( 30,236) | ( 20,113) | ( 33,957) | - | - | ( 84,306) |
| Total | - | ( 925) | ( 1,399) | ( 4,014) | - | - | ( 6,338) |
| Net settled derivatives | - | ( 1,752) | - | - | - | - | ( 1,752) |
| **Total derivative financial liabilities** | - | ( 2,677) | ( 1,399) | ( 4,014) | - | - | ( 8,090) |
| | | | | | | | |
| **Total net financial assets and financial liabilities** | ( 468,828) | 117,047 | 34,124 | 31,055 | 348,497 | 14,851 | 76,746 |

Amounts are in ISK million

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### Off-balance sheet liabilities

The following table shows the amount of contractual obligations of off-balance sheet liabilities that the Group has taken towards customers, either by committing to lend out money in the future or as third party guarantees. The amounts shown reflect the maximum amount, not taking into account the Group's ability to reduce overdraft or credit card limits before the current undrawn amount is fully utilised by the customer. These obligations all fall into the first time bucket since contractually, on a case-by-case basis, the Group could be required to fulfil these obligations instantaneously.

| At 30 September 2021 | On demand | Up to 3 months | 3-12 months | 1-5 years | Over 5 years | No maturity | Total |
|---|---|---|---|---|---|---|---|
| Financial guarantees | 20,077 | - | - | - | - | - | 20,077 |
| Undrawn loan commitments | 54,932 | - | - | - | - | - | 54,932 |
| Undrawn overdrafts | 55,166 | - | - | - | - | - | 55,166 |
| Credit card commitments | 31,191 | - | - | - | - | - | 31,191 |
| **Total off-balance sheet liabilities** | 161,366 | - | - | - | - | - | 161,366 |
| **At 31 December 2020** | | | | | | | |
| Financial guarantees | 23,189 | - | - | - | - | - | 23,189 |
| Undrawn loan commitments | 40,026 | - | - | - | - | - | 40,026 |
| Undrawn overdrafts | 56,746 | - | - | - | - | - | 56,746 |
| Credit card commitments | 32,427 | - | - | - | - | - | 32,427 |
| **Total off-balance sheet liabilities** | 152,388 | - | - | - | - | - | 152,388 |

## 54. Market risk

The Group defines market risk as the current or prospective risk to earnings and capital arising from adverse movements in the level or volatility of prices of market instruments, such as those that arise from changes in interest rates, foreign exchange rates, equity prices, CPI-indexation, and commodity prices. Sources of market risk are imbalances in the Group's balance sheet and open positions in bonds, currencies and equities. Derivative contracts are also potential sources of market risk.

Market risk within the Group can broadly be split into two categories, trading book and banking book. The trading book includes market risk exposures related, directly or indirectly, to the Group's short- and medium-term trading in securities, currencies and other capital market instruments and derivatives. All financial assets and liabilities in the trading portfolio are recognised at fair value and all resulting changes are immediately reflected in the income statement. The banking book includes market risk exposures related to securities held for long-term investment purposes, unlisted securities or holdings in subsidiaries or affiliates. A large part of the banking book market risk is due to mismatches in the composition of assets and liabilities, for example with respect to currencies, interest rates, CPI-indexation or other factors that can affect the Group's earnings or earnings volatility. These mismatches are reported to management and are subject to internal and regulatory limits.

## 55. Interest rate risk

Interest rate risk is defined as the current or prospective risk to earnings or capital arising from adverse movements in interest rates. Sensitivity measures like Basis Point Value ("BPV") are used to measure and manage risk arising from its fixed income exposures. The BPV measures the effect of a 0.01 percentage point upward parallel shift in the yield curve on the fair value of these exposures.

Amounts are in ISK million

## 55. Cont'd

### Interest rate risk in the trading book

The fixed income trading unit invests mainly in government bonds, bonds issued by the Housing and Construction Authority which are guaranteed by the Icelandic Government, domestic municipality bonds, and covered bonds issued by other Icelandic banks. Bonds and bills in the Group's liquidity portfolio are also categorised in the trading book. In the following table the total market value ("MV") of long and short positions may not be the same as reported in Note 16 since netting between short and long positions is not applied here.

| | 30.9.2021 | | | 31.12.2020 | | |
|---|---|---|---|---|---|---|
| **Trading bonds and debt instruments, long positions** | MV | Duration | BPV | MV | Duration | BPV |
| Indexed | 732 | 5.43 | ( 0.40) | 4,103 | 1.87 | ( 0.77) |
| Non-indexed | 84,648 | 0.73 | ( 6.17) | 86,829 | 0.66 | ( 5.70) |
| **Total** | 85,380 | 0.77 | ( 6.57) | 90,932 | 0.71 | ( 6.47) |
| **Trading bonds and debt instruments, short positions** | | | | | | |
| Indexed | 201 | 11.00 | 0.22 | 224 | 6.00 | 0.12 |
| Non-indexed | 563 | 3.00 | 0.18 | 351 | 5.00 | 0.17 |
| **Total** | 764 | 5.10 | 0.40 | 575 | 5.39 | 0.29 |
| **Net position of trading bonds and debt instruments** | 84,616 | 0.73 | ( 6.17) | 90,357 | 0.68 | ( 6.18) |

### Interest rate risk in the banking book

Interest rate risk in the banking book arises from the Group's core banking activities. The main source of this type of interest rate risk is the risk of loss from fluctuations in future cash flows or fair value of financial instruments as interest rates change over time, reflecting the fact that the Group's assets and liabilities are of different maturities and are priced relative to different interest rates.

The following table shows the interest sensitivity of the Group's banking book from a parallel 100 basis points change in all yield curves, with all other variables held constant, categorised by the date of next interest rate reset.

**Sensitivity analysis for interest rate risk in the banking book**

**At 30 September 2021**

| Currency | 0-3 months | 3-12 months | 1-2 years | 2-5 years | 5-10 years | Over 10 years | Total |
|---|---|---|---|---|---|---|---|
| ISK, indexed | 5 | 178 | ( 99) | ( 2,245) | 2,802 | ( 839) | (198) |
| ISK, non-indexed | ( 7) | ( 19) | ( 96) | ( 1,559) | 668 | ( 35) | (1,048) |
| EUR | 23 | ( 49) | ( 621) | 721 | - | - | 74 |
| SEK | 32 | - | - | - | - | - | 32 |
| USD | 11 | ( 6) | - | - | - | - | 5 |
| Other | 36 | ( 2) | - | ( 7) | - | - | 27 |
| **Total** | 100 | 102 | ( 816) | ( 3,090) | 3,470 | ( 874) | ( 1,108) |

**At 31 December 2020**

| Currency | 0-3 months | 3-12 months | 1-2 years | 2-5 years | 5-10 years | Over 10 years | Total |
|---|---|---|---|---|---|---|---|
| ISK, indexed | - | ( 108) | 236 | ( 2,554) | 4,388 | ( 1,232) | 730 |
| ISK, non-indexed | ( 13) | ( 28) | ( 43) | ( 945) | ( 218) | ( 4) | ( 1,251) |
| EUR | 60 | ( 58) | ( 34) | 123 | - | ( 1) | 90 |
| SEK | ( 5) | - | - | - | - | - | ( 5) |
| USD | 27 | - | - | - | - | ( 1) | 26 |
| Other | ( 2) | ( 12) | - | ( 8) | - | ( 6) | ( 28) |
| **Total** | 67 | ( 206) | 159 | ( 3,384) | 4,170 | ( 1,244) | ( 438) |

Amounts are in ISK million

## 56. Currency risk

Currency risk is the risk that earnings or capital may be negatively affected from the fluctuations of foreign exchange rates, due to transactions in foreign currencies or due to a mismatch in the currency composition of assets or liabilities.

The analysis of the Group's foreign currency exposure presented below is based on the contractual currency of the underlying balance sheet items. Additionally, there are off-balance sheet items that carry currency risk and are included in the total currency imbalance. The off-balance sheet amounts below represent the notional amounts of derivatives and unsettled spot agreements.

| At 30 September 2021 | EUR | USD | GBP | CHF | JPY | SEK | NOK | DKK | CAD | Other foreign currencies | Total foreign currencies |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank | 418 | 388 | 161 | 38 | 15 | 60 | 77 | 83 | 31 | 208 | 1,479 |
| Loans to credit institutions | 12,944 | 42,319 | 178 | 292 | 650 | 8,606 | 13,379 | 176 | 235 | 193 | 78,972 |
| Bonds and debt instruments | 9,827 | 3,910 | 40 | - | - | 2,973 | 10,375 | - | - | - | 27,125 |
| Loans to customers | 126,369 | 39,085 | 1,094 | 995 | 3,030 | 66 | 3,410 | 2,737 | 3,861 | 22 | 180,669 |
| Shares and equity instruments | 150 | 294 | 342 | - | - | 298 | - | - | - | - | 1,084 |
| Other assets | 41 | 15 | - | - | - | 15 | - | 8 | - | - | 79 |
| **Total assets** | 149,749 | 86,011 | 1,815 | 1,325 | 3,695 | 12,018 | 27,241 | 3,004 | 4,127 | 423 | 289,408 |
| Deposits from credit institutions | 7,838 | 1,209 | 4 | - | - | - | 8 | 2 | - | - | 9,061 |
| Deposits from customers | 35,506 | 31,140 | 4,204 | 409 | 627 | 1,108 | 3,005 | 1,889 | 357 | 33 | 78,278 |
| Derivative instruments and short positions | 1 | - | - | - | - | 9 | - | - | - | - | 10 |
| Debt issued and other borrowed funds | 136,611 | - | - | - | - | 13,357 | 41,390 | - | - | - | 191,358 |
| Subordinated loans | - | - | - | - | - | 36,923 | - | - | - | - | 36,923 |
| Other liabilities | 30 | 10 | 833 | - | - | 9 | 67 | - | - | - | 949 |
| **Total liabilities** | 179,986 | 32,359 | 5,041 | 409 | 627 | 51,406 | 44,470 | 1,891 | 357 | 33 | 316,579 |
| **Net on-balance sheet position** | ( 30,237) | 53,652 | ( 3,226) | 916 | 3,068 | ( 39,388) | ( 17,229) | 1,113 | 3,770 | 390 | ( 27,171) |
| **Net off-balance sheet position** | 29,871 | ( 52,545) | 3,204 | ( 906) | ( 3,066) | 39,373 | 17,264 | ( 1,057) | ( 3,755) | ( 383) | 28,000 |
| **Net position** | ( 366) | 1,107 | ( 22) | 10 | 2 | ( 15) | 35 | 56 | 15 | 7 | 829 |

Amounts are in ISK million

56. Cont'd

| At 31 December 2020 | EUR | USD | GBP | CHF | JPY | SEK | NOK | DKK | CAD | Other foreign currencies | Total foreign currencies |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank | 779 | 281 | 148 | 45 | 17 | 54 | 56 | 101 | 31 | 119 | 1,631 |
| Loans to credit institutions | 28,586 | 44,519 | 1,301 | 422 | 248 | 880 | 9,487 | 415 | 375 | 100 | 86,333 |
| Bonds and debt instruments | 25,052 | 3,932 | 7 | - | - | 3,894 | 11,195 | - | - | - | 44,080 |
| Loans to customers | 127,317 | 31,584 | 1,160 | 521 | 3,330 | 84 | 3,215 | 2,788 | 7,468 | 29 | 177,496 |
| Shares and equity instruments | 32 | 1,551 | 338 | - | - | 152 | 32 | - | - | - | 2,105 |
| Other assets | 606 | 124 | - | - | - | 34 | - | - | 3 | - | 767 |
| **Total assets** | 182,372 | 81,991 | 2,954 | 988 | 3,595 | 5,098 | 23,985 | 3,304 | 7,877 | 248 | 312,412 |
| Deposits from credit institutions | 10,958 | 788 | 23 | - | - | - | 1 | - | - | - | 11,770 |
| Deposits from customers | 26,757 | 30,607 | 3,917 | 517 | 386 | 1,017 | 3,132 | 2,277 | 392 | 20 | 69,022 |
| Derivative instruments and short positions | - | - | - | - | - | 9 | - | - | - | - | 9 |
| Debt issued and other borrowed funds | 143,255 | - | - | - | - | 38,589 | 21,169 | - | - | - | 203,013 |
| Subordinated loans | - | - | - | - | - | 27,194 | - | - | - | - | 27,194 |
| Other liabilities | 415 | 114 | - | - | - | 19 | - | 29 | 1 | - | 578 |
| **Total liabilities** | 181,385 | 31,509 | 3,940 | 517 | 386 | 66,828 | 24,302 | 2,306 | 393 | 20 | 311,586 |
| **Net on-balance sheet position** | 987 | 50,482 | ( 986) | 471 | 3,209 | ( 61,730) | ( 317) | 998 | 7,484 | 228 | 826 |
| **Net off-balance sheet position** | 463 | ( 46,840) | 920 | ( 484) | ( 3,198) | 61,672 | 268 | ( 829) | ( 7,468) | ( 276) | 4,228 |
| **Net position** | 1,450 | 3,642 | ( 66) | ( 13) | 11 | ( 58) | ( 49) | 169 | 16 | ( 48) | 5,054 |

Amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

## 57. Inflation risk

The Group is exposed to inflation risk since the value of CPI-linked assets exceeds CPI-linked liabilities. The value of these assets and liabilities changes according to changes in the CPI at any given time and all changes in the CPI affect profit and loss. A 1% rise in the index would lead to an ISK 106 million increase in the balance sheet and a 1% fall would lead to a corresponding decrease, other risk factors held constant.

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| Bonds and debt instruments | 1,193 | 4,684 |
| Loans to customers | 254,325 | 268,062 |
| **Total CPI-linked assets** | 255,518 | 272,746 |
| Deposits from customers | 91,739 | 90,353 |
| Debt issued and other borrowed funds | 137,180 | 136,487 |
| Off-balance sheet exposures | 15,993 | 19,725 |
| **Total CPI-linked liabilities** | 244,912 | 246,565 |
| **CPI imbalance** | 10,606 | 26,181 |

## 58. Derivatives

The Group uses derivatives to hedge currency exposure, interest rate risk in the banking book as well as inflation risk. However, the Group is subject to indirect exposure through customers' margin trading. Margin trading is subject to continuous monitoring and collateral requirements. Other derivatives held for trading or for other purposes are insignificant.

## 59. Capital management

The following tables show the capital base, the risk exposure amount (“REA"), the resulting capital ratios, and the leverage ratio for the Group at 30 September 2021 and 31 December 2020.

The Group's regulatory capital requirement is calculated according to CRD IV as implemented through the Act on Financial Undertakings no. 161/2002 and regulation no. 233/2017 on prudential requirements for financial undertakings. Capital requirement calculations for credit risk and market risk are based on the standardised approach whereas the capital requirement calculations for operational risk are based on the basic indicator approach. EU regulation 2019/876 was implemented in Iceland 28 June 2021 by amending regulation no. 233/2017. The most material effect was the amendment of the SME supporting factor, which relaxes the conditions for obligors to be classified as small or medium sized enterprises allowing the supporting factor to be applied to a larger part of the Bank's loan portfolio, lowering the REA. Another material amendment was the change in methodology for calculating the exposure amount for counterparty credit risk, which lead to an increase in the REA.

The Bank is currently reviewing the methodology for calculating REA for operational risk. Changing from the basic indicator approach to the standardised approach could reduce the REA and offer some relief in the Pillar 1 requirement.

The Group aims at managing its capital position and the corresponding capital ratios above the overall regulatory capital requirement. According to the latest SREP report from the Financial Supervisory Authority of the Central Bank, the Bank shall as of 30 September 2021 maintain an additional capital requirement of 2.5% of risk exposure amount. The Bank’s overall capital requirement, taking into account capital buffers, is 17.8%. In September 2022 a countercyclical capital buffer of 2% will be reintroduced, increasing from it's current level of 0%. The Group's capital target includes a 0.5-2.0% management buffer on top of the overall capital requirement.

The minimum leverage ratio for Icelandic financial institutions is 3%.

Amounts are in ISK million

59. Cont'd

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| **Own funds** | | |
| Ordinary share capital | 10,000 | 10,000 |
| Share premium | 55,000 | 55,000 |
| Reserves | 5,738 | 6,181 |
| Retained earnings | 126,653 | 113,529 |
| Third quarter profit | ( 7,587) | - |
| Non-controlling interests | ( 10) | 1,494 |
| IFRS 9 reversal due to transitional rules | 3,239 | 5,164 |
| Fair value changes due to own credit standing | 1,096 | 238 |
| Target dividend payment* | ( 4,523) | - |
| Tax assets | ( 826) | ( 259) |
| Intangible assets | ( 3,249) | ( 3,478) |
| **CET1 capital** | 185,531 | 187,869 |
| Additional Tier 1 capital | 11,000 | - |
| **Tier 1 capital** | 196,531 | 187,869 |
| Tier 2 capital | 25,923 | 27,194 |
| **Total capital base** | 222,454 | 215,063 |

*Target dividend payment is based on target dividend payout ratio of c. 50% of the first half 2021 results which were reviewed by the Bank's auditor.

| | 30.9.2021 | 31.12.2020 |
|---|---|---|
| **Risk exposure amount** | | |
| - due to credit risk | 818,932 | 830,141 |
| - due to market risk | 12,659 | 16,626 |
| Market risk, trading book | 11,408 | 11,306 |
| Currency risk | 1,251 | 5,320 |
| - due to credit valuation adjustment | 1,147 | 1,728 |
| - due to operational risk | 85,026 | 85,026 |
| **Total risk exposure amount** | 917,764 | 933,521 |
| **Capital ratios** | | |
| CET 1 ratio | 20.2% | 20.1% |
| Tier 1 ratio | 21.4% | 20.1% |
| Total capital ratio | 24.2% | 23.0% |
| **Capital ratios including third quarter profit** | | |
| CET 1 ratio | 20.6% | 20.1% |
| Tier 1 ratio | 21.8% | 20.1% |
| Total capital ratio | 24.7% | 23.0% |
| **Leverage ratio** | | |
| **Exposure amount** | | |
| On-balance sheet exposures | 1,445,652 | 1,333,807 |
| Off-balance sheet exposures | 48,005 | 41,067 |
| Derivative exposures | 22,646 | 9,922 |
| **Leverage ratio total exposure measure** | 1,516,303 | 1,384,797 |
| Tier 1 capital | 196,531 | 187,869 |
| **Leverage ratio** | 13.0% | 13.6% |
| **Leverage ratio including third quarter profit** | 13.2% | 13.6% |

Amounts are in ISK million

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