



ÍSLENSKA  
ÁNÆGJUÞOGIN  
2013

ÍSLENSKA  
ÁNÆGJUÞOGIN  
2014

ÍSLENSKA  
ÁNÆGJUÞOGIN  
2015

ÍSLENSKA  
ÁNÆGJUÞOGIN  
2016

17 August 2017

# 1H2017 Financial Results



**The Banker**  
Bank of the Year 2014  
ICELAND

**The Banker**  
Bank of the Year 2016  
ICELAND

# Forward Looking Statements

## Important information

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# Table of Contents

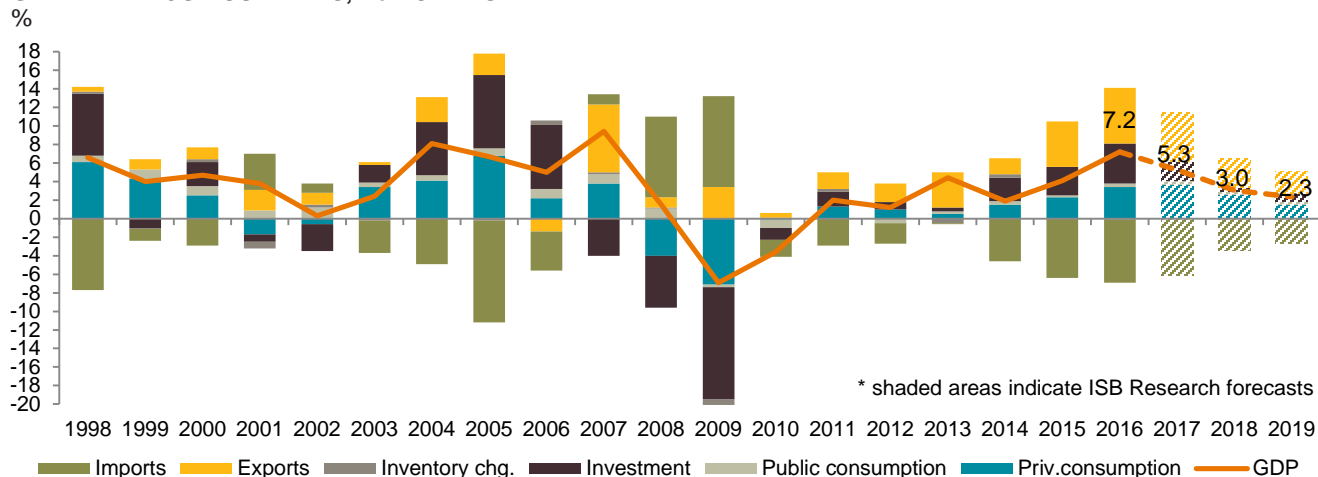
1. Icelandic economy update
2. Overview
3. Income Statement
4. Assets
5. Liabilities, Liquidity & Capitalisation
6. Financial targets and key points

# 1. Icelandic economy update

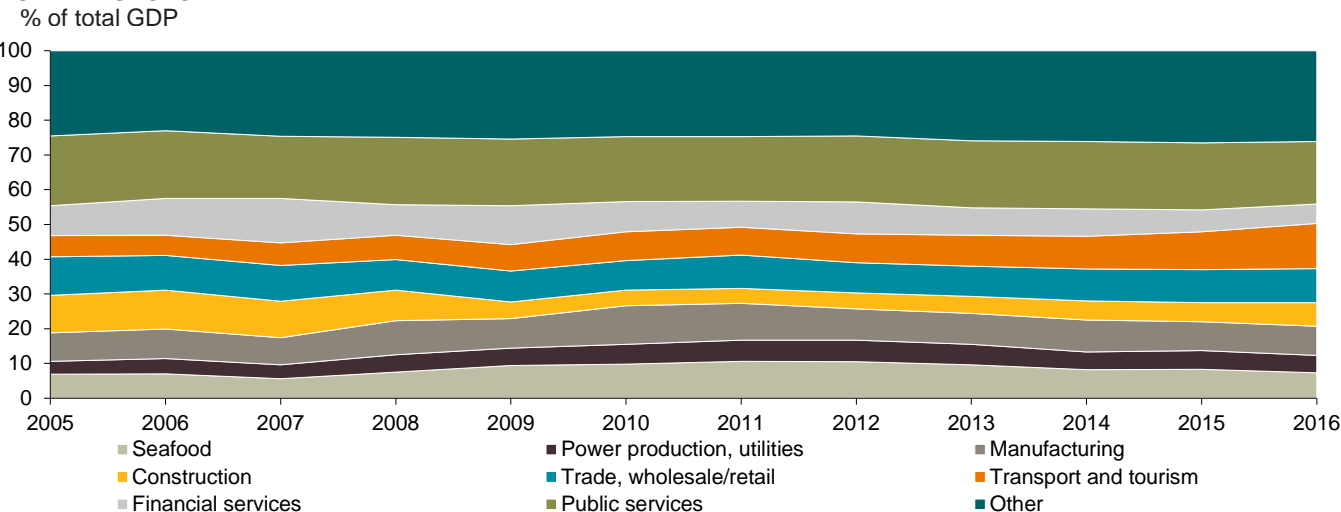
# Outlook for continuing robust GDP growth

Economic growth to moderate in coming quarters

GDP AND MAJOR SUBITEMS, YoY CHANGE\*



GDP BY SECTOR



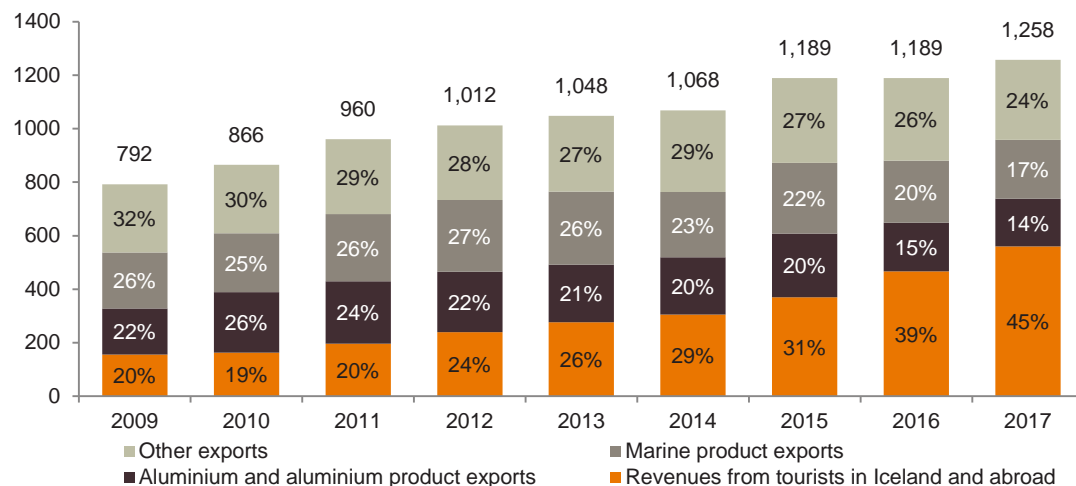
- 5.0% GDP growth in Q1 2017, following 7.2% full-year growth in 2016
- Outlook for 5.1% GDP growth in 2017, 3.0% growth in 2018 and 2.3% growth in 2019
- Services exports, private investment and private consumption main contributors to growth in 2017
- Slower growth in coming years due to minimal growth in investment and slower growth in private consumption and exports
- Stronger fundamentals for sustainable growth than in previous business cycles
- Share of tourism and transport in GDP has doubled in a decade, from 6.5% in 2007 to 13% in 2016

# Tourism sector growth moderating

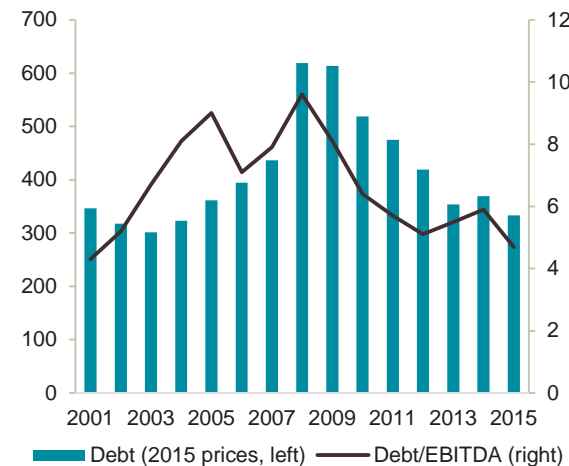
## Fishing industry on sound footing

### EXPORT REVENUES BY SECTOR

(ISK bn)

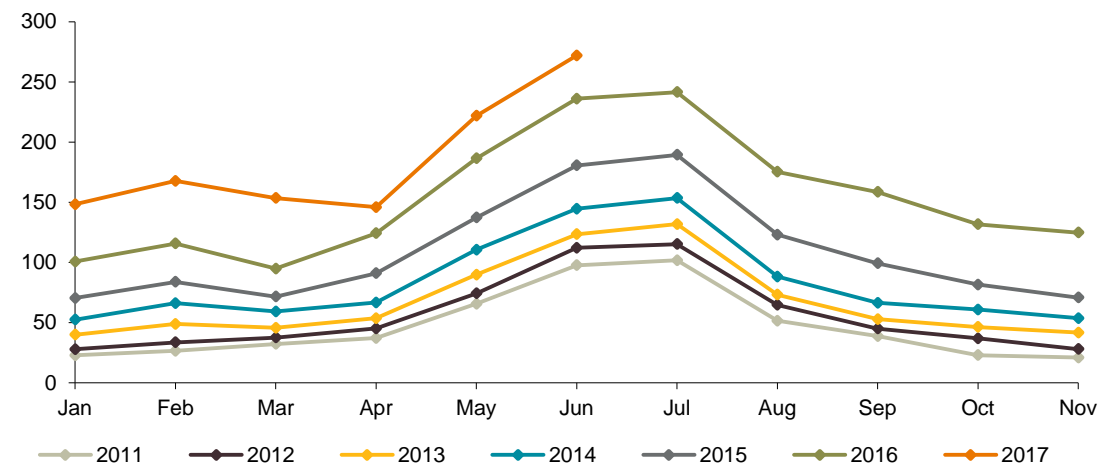


### FISHING COMPANIES' DEBT POSITION

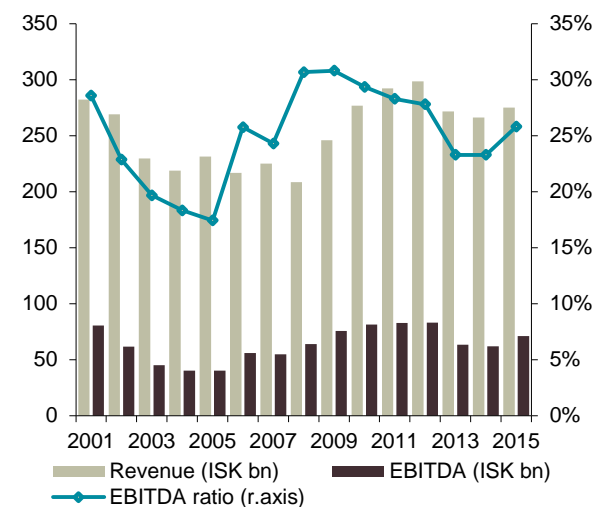


### FOREIGN TOURISTS DEPARTING FROM ICELAND BY AIR

(thous.)

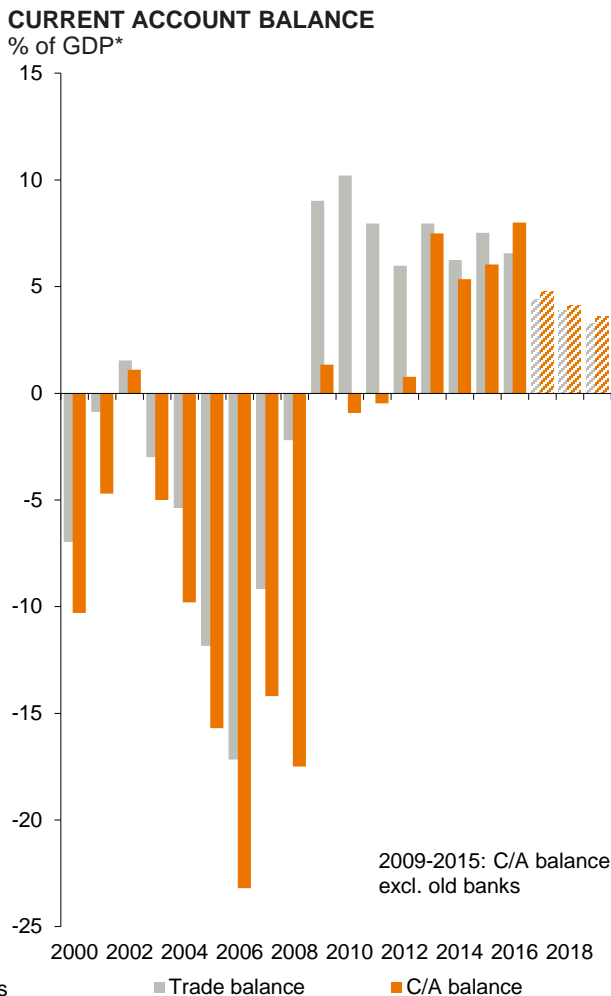
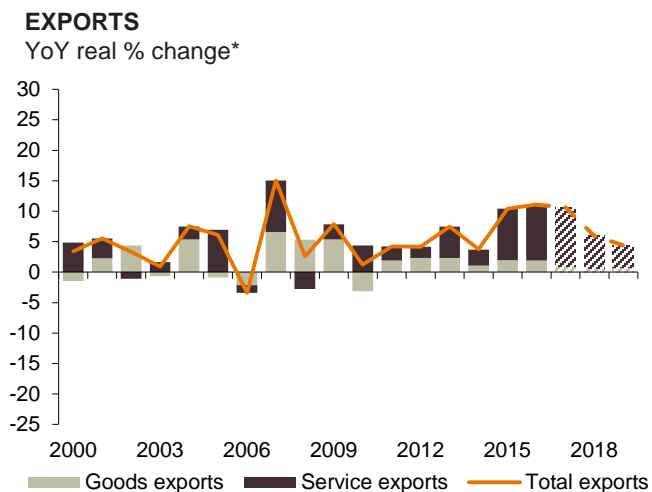
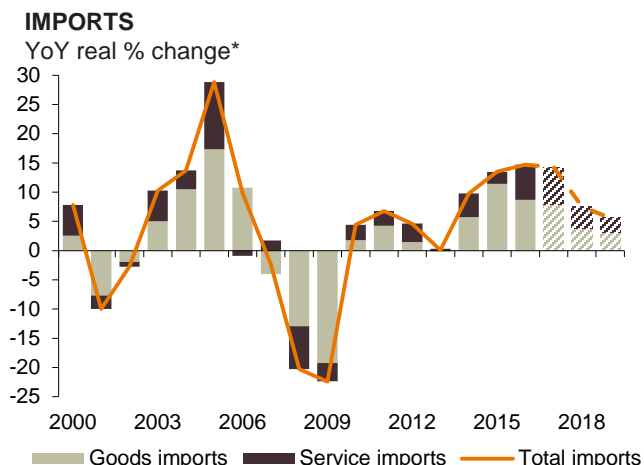


### FISHING INDUSTRY REVENUES AND EBITDA



# Trade surplus to narrow in coming years

Service exports play a key role in maintaining C/A surplus



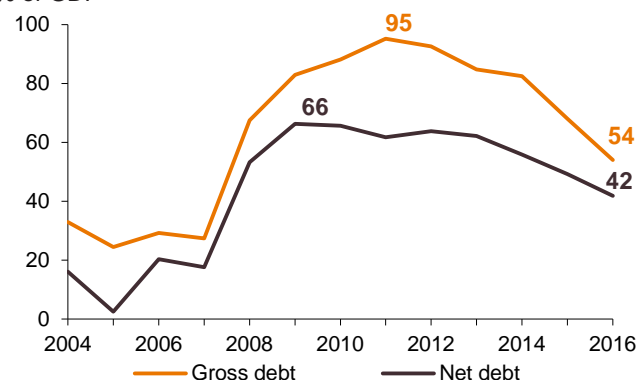
- Rapid growth in tourism is the main source of export growth in recent years, explaining 80% of total export growth in 2016
- Services will continue to lead export growth in coming quarters, although goods exports will also rise moderately
- Goods and services look set to contribute evenly to import growth in coming quarters
- Sizeable current account surplus in recent years, peaking at 7.9% of GDP in 2016
- More moderate C/A surplus in coming quarters as tourism growth slows and imports rise, delining from 4.8% of GDP in 2017 to 3.6% in 2019
- The C/A surplus, coupled with other factors, has resulted in a vast improvement in Iceland's external position
- At end-Q1 2017, external assets net of external liabilities amounted to 3.7% of GDP

\* shaded areas indicate ISB Research forecasts

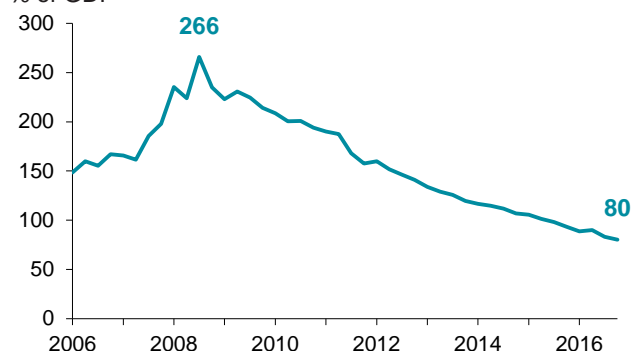
# Domestic balance sheets strong

Substantial deleveraging by both public and private sectors in recent years

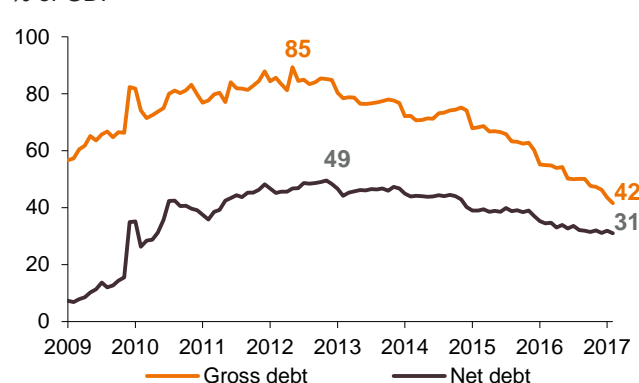
**GENERAL GOVERNMENT DEBT**  
% of GDP



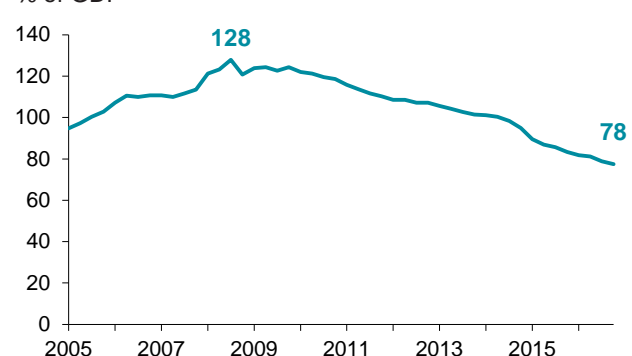
**CORPORATE DEBT**  
% of GDP



**CENTRAL GOVERNMENT DEBT**  
% of GDP



**HOUSEHOLD DEBT**  
% of GDP



- Gross public debt has decreased from 95% of GDP to 54% of GDP over the past 5 years
- Private sector credit-to-GDP ratio has fallen steadily throughout the decade, due to deleveraging and, more recently, also GDP growth
- In recent years, corporate investment has largely been financed by equity, but the share of credit financing is growing
- Average LTV ratio of real estate has fallen from 55% in 2010 to around 35% by end-2016 due to a combination of deleveraging and rising house prices
- According to the Central Bank's recent Financial Stability Report, households have seldom been as resilient against external shocks

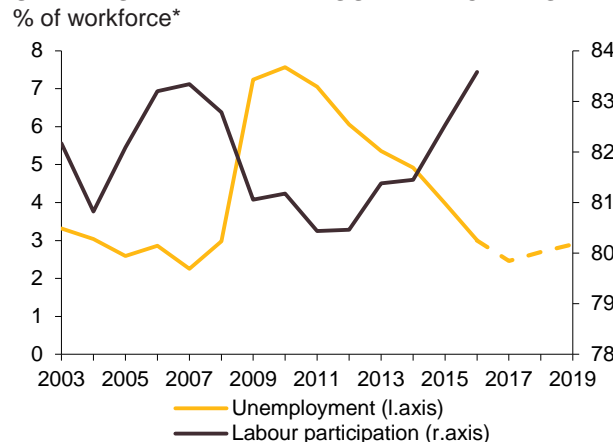


# Households' financial conditions favourable

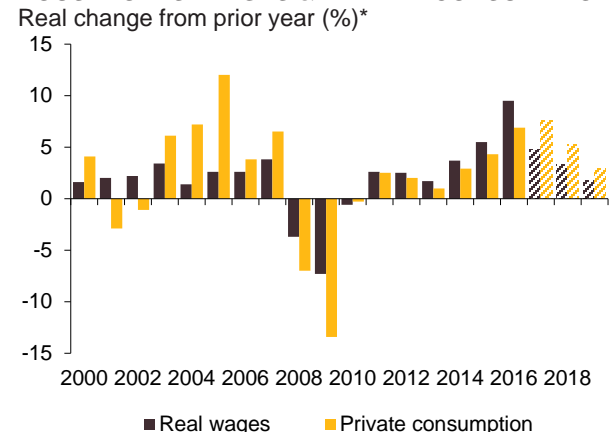
Purchasing power and consumption growing, but housing market conditions are challenging

- Labour market beginning to show strains, with low unemployment and high labour force participation
- Real wage growth has moderated but remains relatively rapid
- Private consumption growth in line with increasing purchasing power of wages
- Housing market conditions challenging, with significant gap between demand and supply pushing real prices upward
- Supply of new housing expected to rise in coming years
- New housing supply and demand could reach balance by 2019

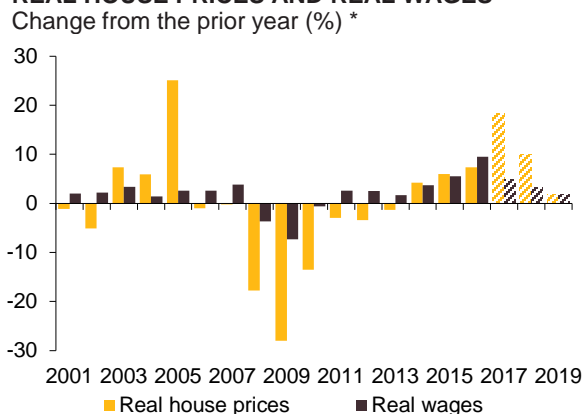
**UNEMPLOYMENT AND LABOUR PARTICIPATION**



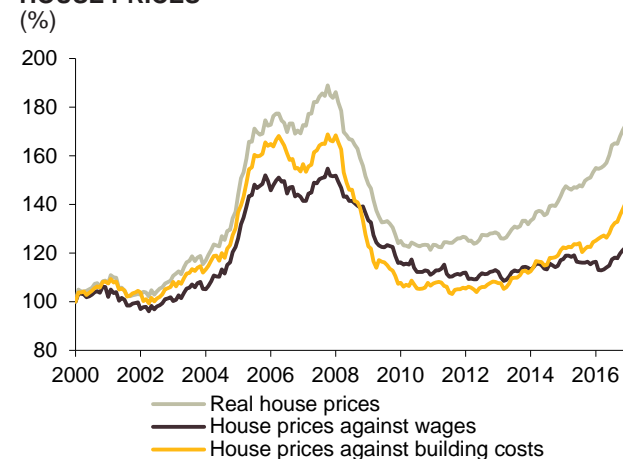
**HOUSEHOLDS' WAGES & PRIVATE CONSUMPTION**



**REAL HOUSE PRICES AND REAL WAGES**



**HOUSE PRICES**

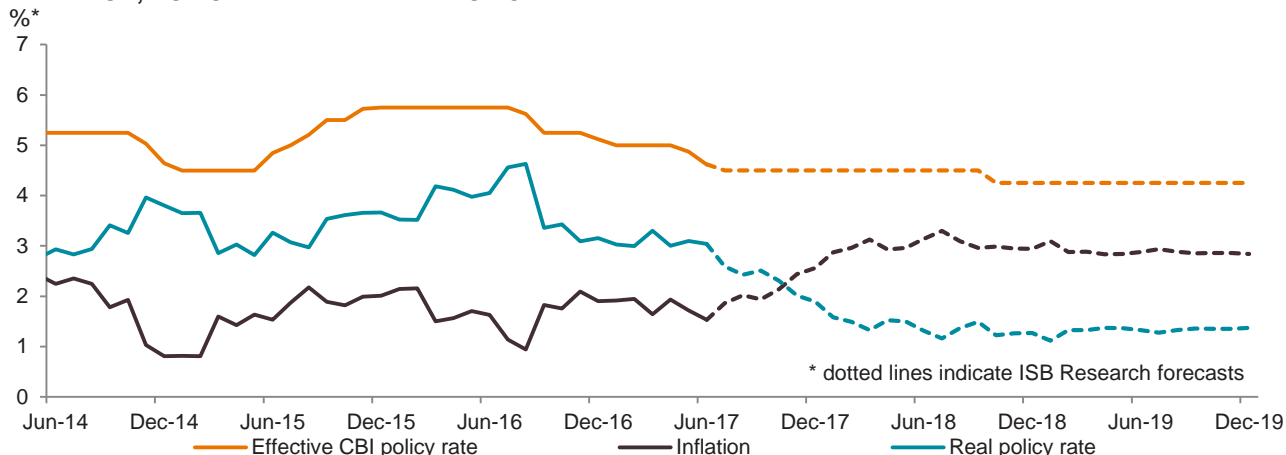


\* shaded areas/dotted lines indicate ISB Research forecasts

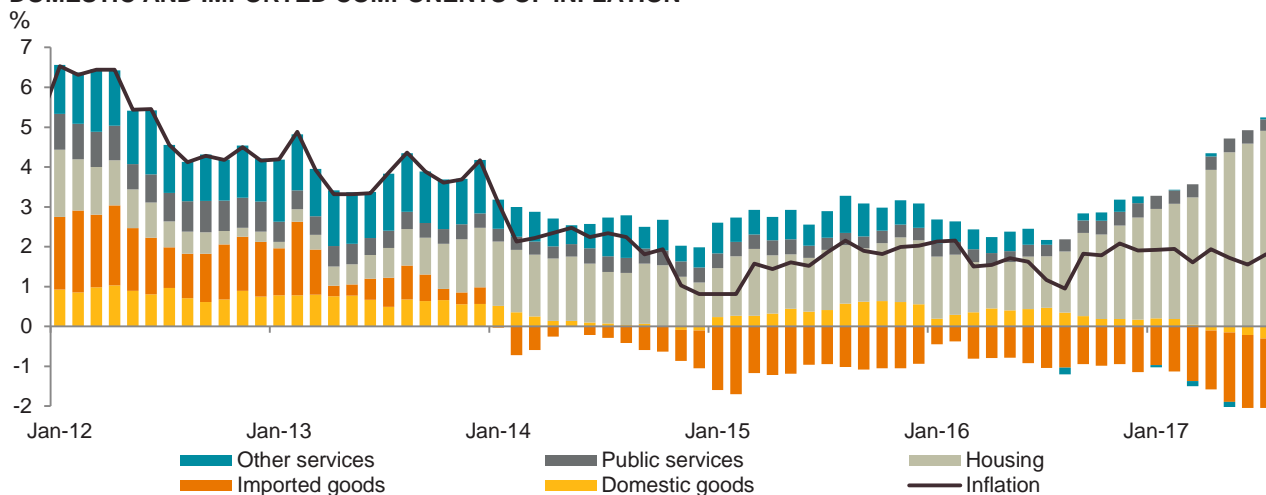
# Inflation to rise above CBI target

CBI expected to keep rates close to current levels near-term

INFLATION, POLICY RATE AND REAL POLICY RATE



DOMESTIC AND IMPORTED COMPONENTS OF INFLATION



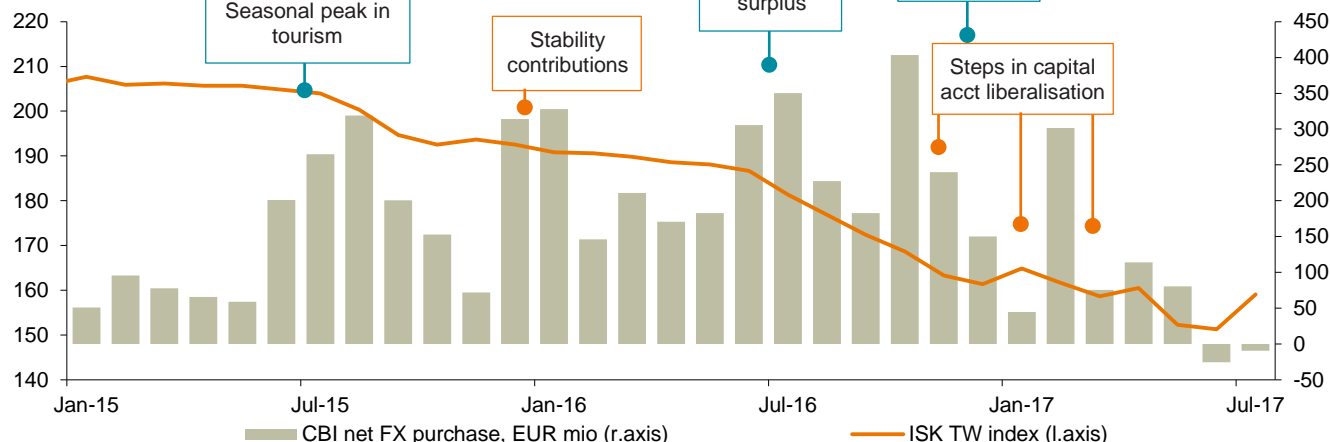
Source: Statistics Iceland, Central Bank of Iceland and ISB Research

- Inflation below CBI target since Q1 2014, largely due to ISK appreciation, imported deflation in the period
- Inflation to overtake the Central Bank's (CBI) 2.5% inflation target around year-end 2017 and then remain close to 3.0% throughout 2019
- Rising inflation due to less imported deflation and continued domestic cost pressures
- CBI policy rate currently 4.5% following a 50bp decrease in H1 2017
- A lower policy rate supported by ongoing low inflation, inflation expectations near 2.5% target
- ISB Research forecasts unchanged policy rate throughout H2 2018
- Slower growth and stable inflation may lead to moderate rate cuts in coming years

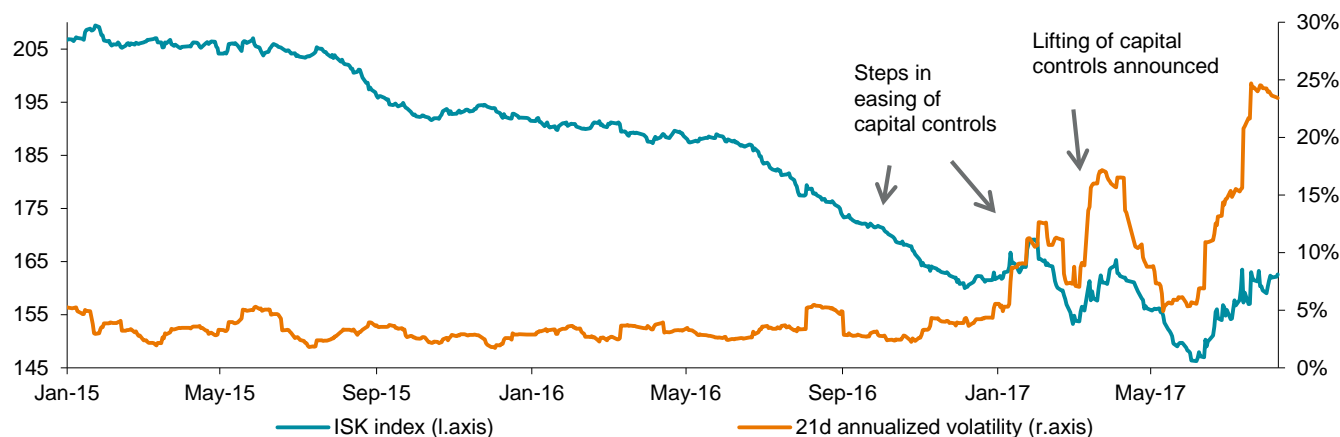
# ISK appreciation trend has halted

The Central Bank's net FX reserves have grown to almost  $\frac{1}{4}$  of GDP

## CBI NET FX PURCHASE AND ISK TW INDEX



## ISK TW INDEX AND VOLATILITY



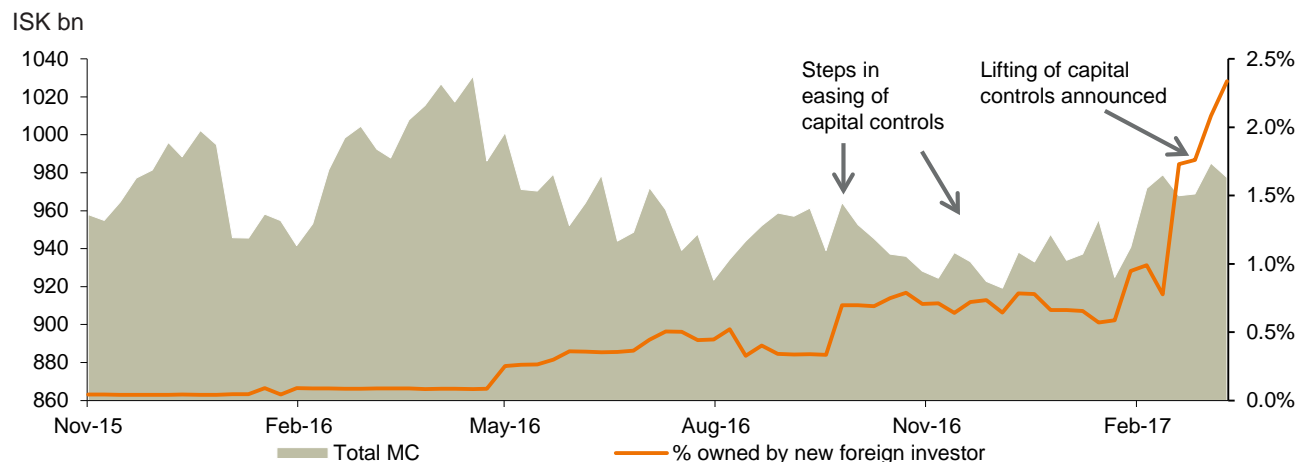
- Following considerable appreciation in 2016, the ISK exchange rate has fluctuated in 2017
- ISK volatility has increased sharply following lifting of capital controls in March, whereas appreciation trend has halted
- The CBI accumulated substantial FX reserves while leaning against the appreciation in 2015-2016
- Net FX reserves currently stand at EUR 4.9bn, around 23% of GDP
- Present real exchange rate closer to sustainable medium-term levels

# 120 days since lifting of capital controls

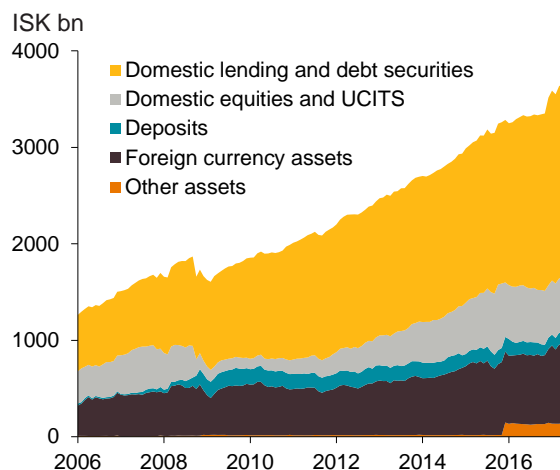
Capital account liberalisation in March has made FX market more forward-looking

- Lifting of capital controls in mid-March widely seen as successful end to 8 years of capital controls
- Moderate impact on ISK, largely due to underlying trade surplus inflows and ample CBI FX reserves
- FX market increasingly driven by more factors than just trade flows since lifting of controls
- Foreign investors currently own 16% of the Icelandic stock market
- Pension funds currently have 22% of total assets in foreign assets. They want to increase foreign assets to 30-40% of total in coming years
- Rating agencies have viewed the lifting of controls favourably

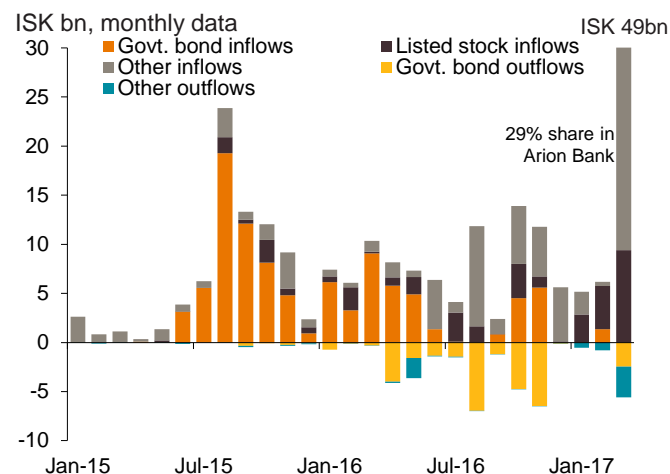
## MARKET CAP OF STOCK MARKET AND % OWNED BY NEW FOREIGN INVESTORS



## PENSION FUND ASSETS



## NEW INVESTMENTS BY FOREIGNERS

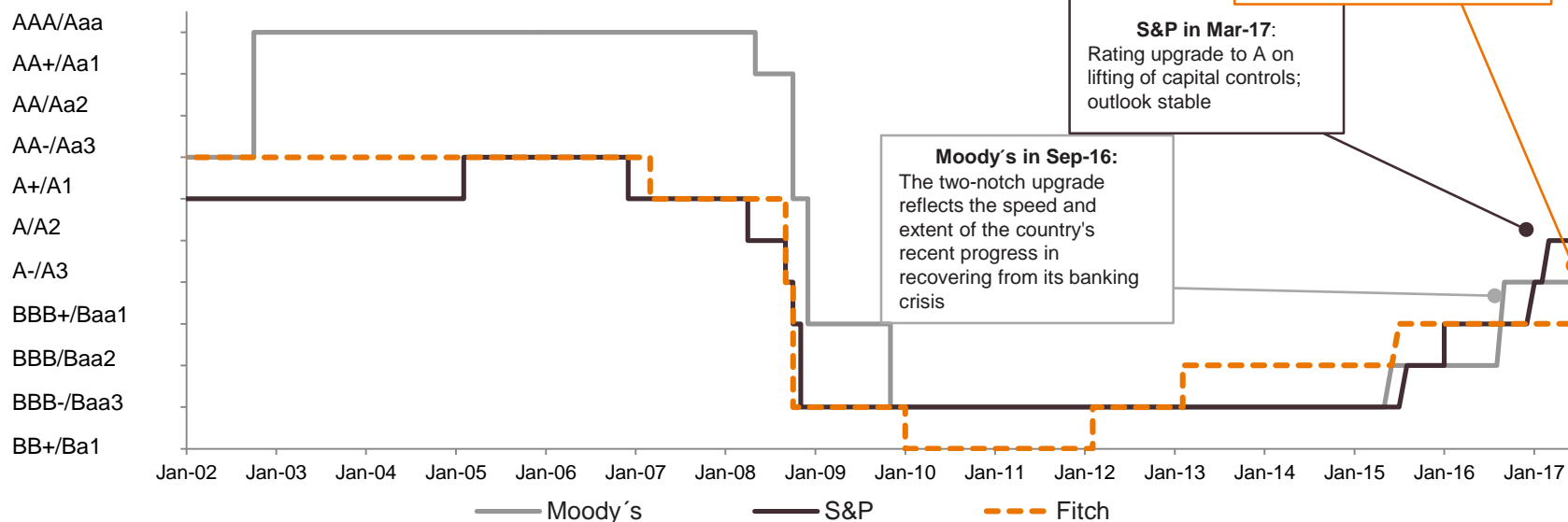


# Iceland's credit rating improves further

Iceland now rated a single-A economy by all 3 major rating agencies

## DEVELOPMENT OF SOVEREIGN CREDIT RATING

Moody's, Fitch and SP Global



### MOODY'S IN SEPTEMBER 2016

- The two-notch upgrade to A3' from 'Baa2' of Iceland's government rating reflects the speed and extent of the country's recent progress in recovering from its 2008 banking crisis.

### FITCH IN JULY 2017

- The Outlook is Positive.
- The main factors that could lead to an upgrade are:
  - Resilience of the economy to external shocks, in the context of a more open capital account.
  - Continued economic growth without excessive macroeconomic imbalances.
  - Continued falls in the public debt ratio, supported by prudent fiscal policy.

### S&P IN JUNE 2017

- S&P Global Ratings affirmed its 'A/A-1' long- and short-term foreign and local currency sovereign credit ratings on the Republic of Iceland.
- The stable outlook balances the potential for improvements in Iceland's fiscal position against risks of the economy overheating during the next two years.

## 2. Overview

# Íslandsbanki today

A leader in financial services in Iceland, Íslandsbanki is a universal bank with a proven strategy

## RECOGNITION



Driven by the **vision to be #1 for service**, our business model is based on three business divisions that manage and **build relationships** with our customers, simplify our product offering and unify our objectives with society at large – or as we like to say it - how we **multiply, simplify and unify**.

## KEY FIGURES 1H 2017

ROE (Regular operations) **11.2%**

Cost / Income **59.2%**

CET1 **23.3%**

Total Assets **EUR 8.9bn**

## EMPLOYEES



**858**

Number of FTE's for parent company at end of June 2017, excluding summer employees

**4** training courses a year per **employee**



**95%** **Job satisfaction** among Íslandsbanki's employees

## MARKET SHARE

retail market share

**+30%**



**35%**

market share in **SMEs**

market share in **31%** **large companies**

## WAYS TO BANK

**59.000** **APP** **USERS**



**1**

Self-service branch

**57** **ATMs**



**14** **branches**



users **107,000** **online banking**



## CREDIT RATINGS

**BBB/A-2** Positive outlook

**S&P Global** Ratings

**BBB/F3**

**Fitch Ratings**

Stable outlook

## RELATIONSHIP BANKING

### Personal banking

Provides customers with comprehensive banking services through digital channels and a modern nationwide branch network

**130,000 individuals**

## MULTIPLY – SIMPLIFY – UNIFY

### Business banking

Responsible for service to SMEs in the Bank's branches, as well as Ergo, Íslandsbanki's asset based financing unit

**10,800 SMEs**

### Corporate and Investment banking

provides comprehensive financial services to investors and large companies, including lending, securities and currency brokerage, corporate advisory services, private banking services, and sales of hedging instruments

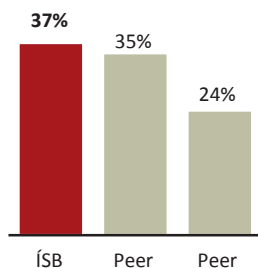
**575 large corporates**

# Leading customer perception in key segments

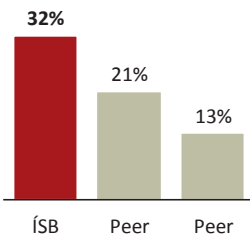
Opportunity to transform positive market perception to market share

## CONSIDERED THE LEADING BANK FOR:

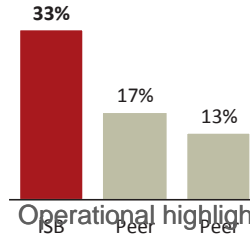
### INDIVIDUALS<sup>1</sup>



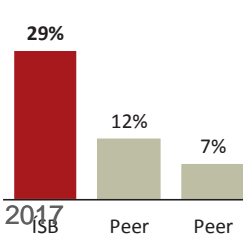
### SMEs<sup>4</sup>



### LARGE COMPANIES<sup>2</sup>



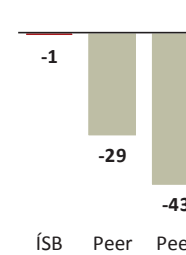
### CORPORATE FINANCE<sup>6</sup>



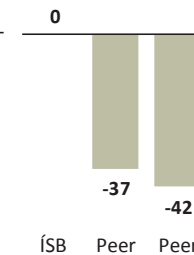
Operational highlights 1H 2017

## #1 for SERVICE

### NPS SMEs<sup>4</sup>

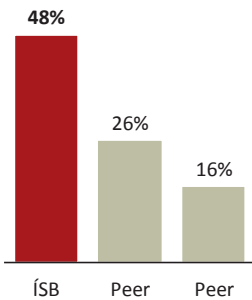


### NPS LARGE COMPANIES<sup>2</sup>

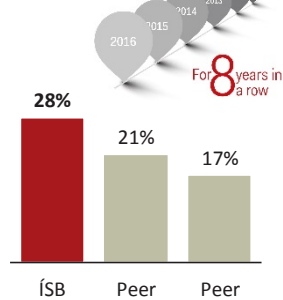


## MOST PROFESSIONAL:

### SMEs<sup>4</sup>

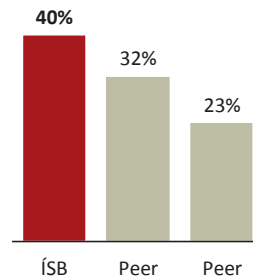


### LARGE COMPANIES

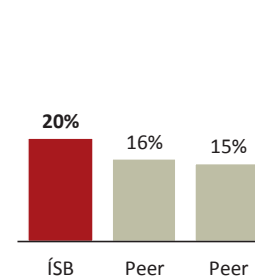


## FIRST CHOICE FOR:

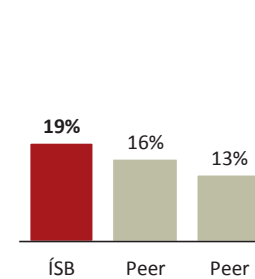
### ASSET FINANCING<sup>5</sup>



### ASSET MANAGEMENT<sup>3</sup>



### MUTUAL FUNDS INVESTMENT<sup>3</sup>



1. Gallup: 6-month rolling average of monthly tracking survey among individuals in July 2017.

2. Gallup: Survey among 300 largest corporates in Iceland according to Frjáls Verslun, an Icelandic Business Magazine, December 2016.

3. Gallup: Survey, market position in the savings market in May 2016.

4. Gallup: Survey amongst small and medium enterprises in December 2016.

5. Gallup: Ergo corporate market, survey conducted in November 2016

6. Gallup: Survey amongst corporate finance in December 2016.



# Operational highlights 1H2017

A few examples of how our strategy lends colour to our operations and daily activities



## MULTIPLY

We are the banking partner of:

- 2 of Iceland's largest energy companies
- 4 of Iceland's 5 largest seafood companies
- 1 of Iceland's 2 largest shipping companies





**ergo**  
New website launched

### Corporate ADVISORY mandates

Icelandic Gadus  
Seachill  
Grayline  
Iceland Travel  
Ölgerðin  
Lífland  
Íslandshótel

### Strengthening the client relationship

-  **8,522** proactive calls to individuals
-  **2,000** proactive visits to corporates

**Retail banking service**  
**Net promoter score**  
Highest score since **2009**



Foreign currency ATM opened



**ÍSLANDSSJÓÐIR**

New fund  
**IS EQUUS equity fund**



## SIMPLIFY



All head office operations to be consolidated in the new HQ in 2017  
**4 → 1**

### Covered bonds offerings

Total issuance in Q1 2017 amounted to ISK 30.6 bn

Implementation of SOPRA, a centralised core banking system for deposits and payment system is progressing well



### MOVING TOWARDS A PAPERLESS BANK

Bank statements only available on digital format and all loan documents stored electronically



## UNIFY



### Helping Hand

Íslandsbanki employee a part of the project "Digital Divide Initiative" in Malawi, Burundi and Tanzania

In Iceland over 120 employees have donated a full day's work to a charity of their choice

New customer centred organisational structure introduced in May



Education matters  
13 students grants issued

### Publications



**ICELANDIC MUNICIPALITIES**  
A new sector report

# Financial highlights from 1H 2017

Solid recurring revenues and resilient ROE based on high capital levels

## 1. MACRO

- Outlook for 5.1% growth in 2017, 3.0% in 2018 and 2.3% growth in 2019\*
- Full capital account liberalisation in March 2017
- Sovereign rating upgrades from all three rating agencies

## 2. PROFITABILITY

- Net profit of 8.0bn and ROE of 9.2%
- Reg. ROE of 11.2% based on normalised CET1 15%

## 3. STRONG RECURRING REVENUES

- NIM at 2.9%, slight drop due to lower interest rate environment
- NFC up 2% in 1H17, mainly due to increased activity in the corporate and investment banking division
- Slight increase in regular underlying costs in the short term, rendering a C/I ratio of 59.2%

## 4. SOUND BALANCE SHEET

- Balanced growth of loan portfolio of 4.9%, ISK 108bn in new lending since YE2016
- Asset quality continues to improve, NPL was 1.2%, compared to 1.8% at YE16
- Positive impairments due to favourable economic environment

## 5. BBB RATINGS AND SOLID LIQUIDITY POSITION

- Fitch upgrade to BBB/F3 rating with stable outlook in Jan '17 and S&P rating upgrade in Oct '16 to BBB/A-2 on positive outlook
- Total capital ratio 23.5% (CET1 23.3%) and leverage ratio of 15.7%
- Group's liquidity coverage ratio (LCR) was 171% and NSFR 119%
- The AGM in March approved a dividend payment of ISK 10bn to the Bank's shareholders for 2016 profits in line with dividend policy
- A proposal for an extraordinary dividend on previous operational years was also authorised allowing for further capital optimisation

# Overview

## Key figures & ratios

		1H17	1H16	2Q17	2Q16	2016
<b>PROFITABILITY</b>	ROE 15% CET1 (regular operations)*	<b>11.2%</b>	11.3%	<b>11.8%</b>	13.3%	10.7%
	ROE (after tax)	<b>9.2%</b>	12.9%	<b>11.3%</b>	19.1%	10.2%
	Net interest margin (of total assets)	<b>2.9%</b>	3.1%	<b>3.0%</b>	3.3%	3.1%
	Cost to income ratio**	<b>59.2%</b>	55.8%	<b>58.3%</b>	52.8%	56.9%
	After tax profit, ISK m	<b>8,041</b>	13,017	<b>4,997</b>	9,507	20,158
	Earnings from regular operations, ISK m***	<b>7,365</b>	8,017	<b>3,862</b>	4,508	15,138

		30.6.2017	31.3.2017	31.12.2016	31.12.2015
<b>CAPITAL</b>	Total equity, ISK m	<b>175,928</b>	170,765	178,925	202,227
	Tier 1 capital ratio	<b>23.3%</b>	22.8%	24.9%	28.3%
	Total capital ratio	<b>23.5%</b>	23.1%	25.2%	30.1%
	Leverage ratio	<b>15.7%</b>	15.5%	16.0%	18.1%
<b>BALANCE SHEET</b>	Total assets, ISK m	<b>1,047,221</b>	1,028,808	1,047,554	1,045,769
	Risk exposure amount, ISK m	<b>736,310</b>	730,120	704,177	699,693
	Loans to customers, ISK m	<b>721,820</b>	703,447	687,840	665,711
	Total deposits, ISK m	<b>581,769</b>	578,739	599,109	618,876
	Total deposit / loan ratio	<b>78.0%</b>	78.4%	84.9%	88.3%

\*Return from regular operations on normalized CET1 of 15%, adjusted for risk free interest on excess capital

\*\*Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund - One off items) / (Total operating income – one off items)

\*\*\*Earnings from regular operations is defined as earnings excluding one-off items e.g. bank tax, fair value gain deriving from changes in classification of assets, costs associated with one-off costs, and net earnings from discontinued operations

## 3. Income Statement

# Income statement

Strong recurring revenues with stable growth in NII and NFCI contributing 97% of total operating income

ISK m	1H17	1H16	Δ	2Q17	2Q16	Δ
Net interest income	15,211	15,895	(684)	7,814	8,356	(542)
Net fee and commission income	6,813	6,659	154	3,543	3,515	28
Net financial income	109	6,666	(6,557)	97	6,062	(5,966)
Net foreign exchange gain (loss)	370	317	53	169	305	(136)
Other operating income	216	624	(409)	55	473	(418)
<b>Total operating income</b>	<b>22,718</b>	<b>30,161</b>	<b>(7,443)</b>	<b>11,678</b>	<b>18,711</b>	<b>(7,034)</b>
Salaries and related expenses	(7,768)	(7,636)	(132)	(4,109)	(3,697)	(412)
Other operating expenses	(5,498)	(6,480)	982	(2,739)	(3,902)	1,164
<b>Administrative expenses</b>	<b>(13,266)</b>	<b>(14,116)</b>	<b>850</b>	<b>(6,848)</b>	<b>(7,599)</b>	<b>751</b>
Depositors' and Investors' Guarantee Fund	(515)	(528)	13	(262)	(267)	5
Bank Tax	(1,472)	(1,407)	(64)	(752)	(716)	(36)
<b>Total operating expenses</b>	<b>(15,253)</b>	<b>(16,051)</b>	<b>797</b>	<b>(7,862)</b>	<b>(8,582)</b>	<b>720</b>
<b>Profit before net loan impairment</b>	<b>7,465</b>	<b>14,110</b>	<b>(6,645)</b>	<b>3,816</b>	<b>10,129</b>	<b>(6,313)</b>
Net loan impairment	440	369	71	200	689	(489)
<b>Profit before tax</b>	<b>7,905</b>	<b>14,479</b>	<b>(6,574)</b>	<b>4,016</b>	<b>10,818</b>	<b>(6,803)</b>
Income tax expense	(2,263)	(2,586)	323	(1,133)	(1,720)	588
<b>Profit for the period from continuing operations</b>	<b>5,642</b>	<b>11,893</b>	<b>(6,251)</b>	<b>2,883</b>	<b>9,098</b>	<b>(6,215)</b>
Profit from discontinued ops. net of income tax	2,399	1,124	1,275	2,114	409	1,704
<b>Profit for the period</b>	<b>8,041</b>	<b>13,017</b>	<b>(4,976)</b>	<b>4,997</b>	<b>9,507</b>	<b>(4,511)</b>

## HIGHLIGHTS

### Stable and strong recurring revenues

- Net interest income totalled ISK 15.2bn, a decrease of 4% from the previous year due to lower interest rate environment
- The net interest margin was 2.9%
- NFCI was up 2% over the period
- Comparison to 1H16 skewed due to sale of shares in VISA Europe within subsidiary Borgun under net financial income

### Continued focus on cost control

- The cost-to-income ratio was 59.3% and administrative expenses (excluding one-off extraordinary expenses) is at comparable levels to previous year
- Total salaries were ISK 7.8bn in 1H17, a 2% increase between years

### Positive impairments

- Positive impairments are a result of a favourable economic environment

### Consolidation effort

- Consolidation efforts continued adding front-end costs that are expected to be offset by future savings, this includes the four head office locations to be fully consolidated at new HQ in 2H17 and merger of two largest branches

# Earnings from regular operations

Excludes one-off items and ROE calculation is adjusted to normalised CET1 of 15%

## HIGHLIGHTS

### One off items 2017

- One off costs have greatly reduced and will have less impact on regular earnings in 2017
- 268m in one-off costs in 2Q17 are a result of organisational changes

### One off income 2016

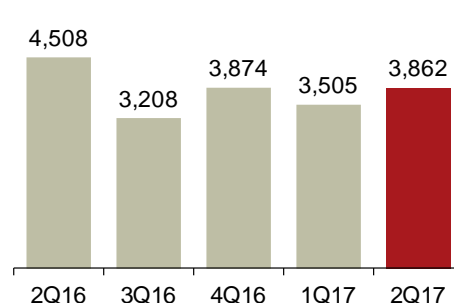
- The revenue excluded in 2016, was in connection with the sale of shares in VISA Europe within subsidiary Borgun which was recognised in June 2016 (ISK 6.2bn)

## RESILIENT ROE FROM REGULAR OPERATIONS

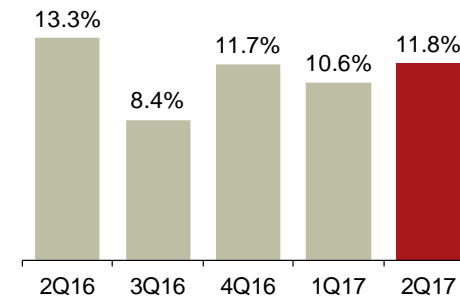
ISKm	1H17	1H16	Δ	2Q17	2Q16	Δ
Reported after tax profit	8,041	13,017	(4,976)	4,997	9,507	(4,511)
One-off revenue	0	(6,186)	6,186	0	(6,186)	6,186
One-off costs*	340	1,220	(880)	306	1,189	(883)
Bank tax	1,472	1,407	64	752	716	36
Profit (loss) from discontinued ops	(2,399)	(1,124)	(1,275)	(2,114)	(409)	(1,704)
Tax impact of adjustments	(88)	(317)	229	(80)	(309)	229
Earnings from regular operations**	7,365	8,017	(652)	3,862	4,508	(646)

ROE 15% CET1 (regular operations)***	11.2%	11.3%		11.8%	13.3%	
ROA from regular operations (after tax)	1.4%	1.6%		1.5%	1.8%	
Net interest margin adj. 15% CET1	2.7%	2.7%		2.8%	2.9%	
Cost / income ratio adj. 15% CET1	62.2%	60.6%		61.9%	67.8%	

### EARNINGS FROM REG. OPERATIONS (ISK m)



### ROE REG. OPERATIONS CET1 15% (%)



\* One-off costs include the impact of depreciation, maintenance expenses and pre-paid rent associated with Íslandsbanki's branches and previous headquarters

\*\* Earnings from regular operations is defined as earnings excluding one-off items e.g. fair value gain deriving from changes in accounting treatment, Bank tax, one off costs and net earnings from discontinued operations.

\*\*\* Return from regular operations and corresponding ratios on normalized CET1 of 15%, adjusted for risk free interest on excess capital

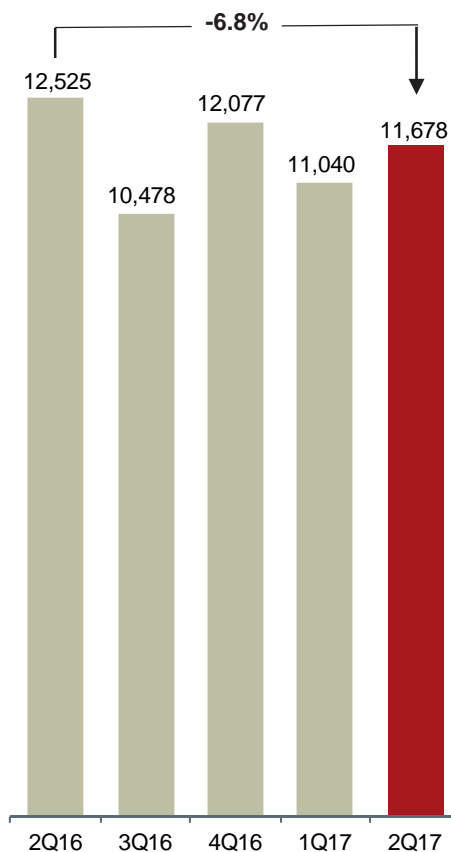
# Operating income

Core earnings, NII and NFCI, continue to generate majority of total income

## INCOME GROWTH

### TOTAL OPERATING INCOME

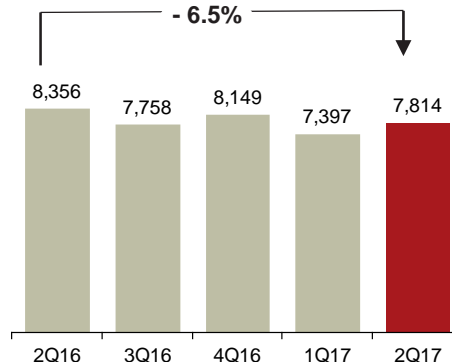
Excluding one-off income (ISKm)



## STRONG RECURRING REVENUES

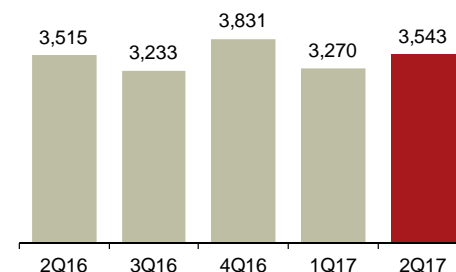
### NET INTEREST INCOME (NII)

(ISKm)



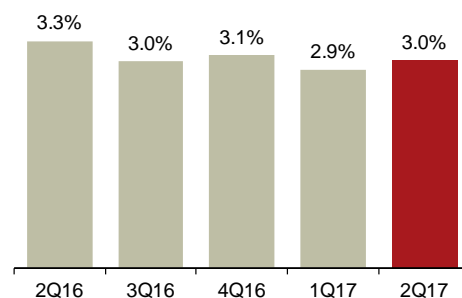
### NET FEE AND COMMISSION INCOME

(ISKm)



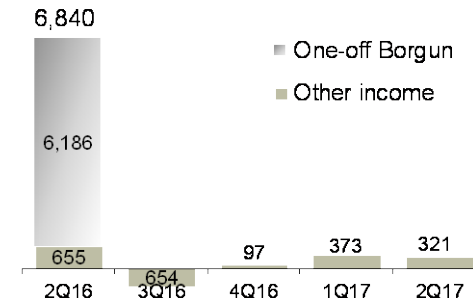
### NET INTEREST MARGIN (NIM)

(%)



### OTHER INCOME\*

(ISKm)



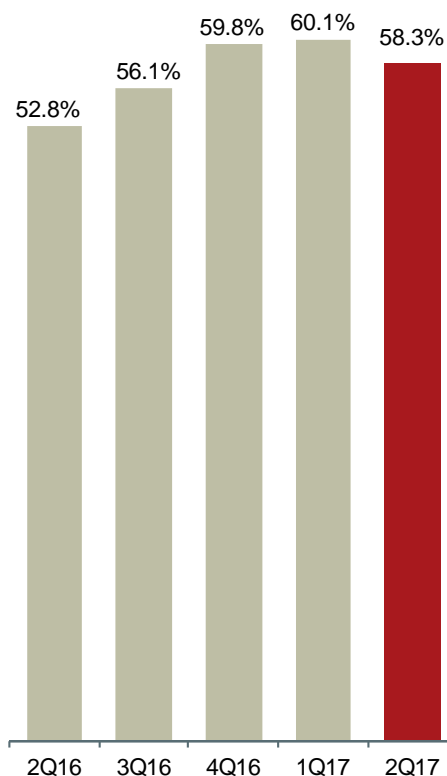
\* Diagonal column represents the sale of Borgun's share in Visa Europe which was recognized for ISK 6bn and is considered one-off

# Administrative expenses

Administrative expenses, excluding one-off expenses, is at comparable levels to previous year

## EFFICIENCY

### COST INCOME RATIO <sup>1</sup> (%)

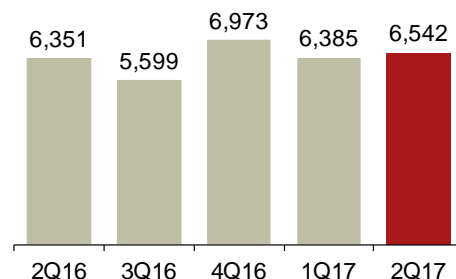


1. The cost-to-income ratio excludes Bank tax and one-off cost and revenue items.

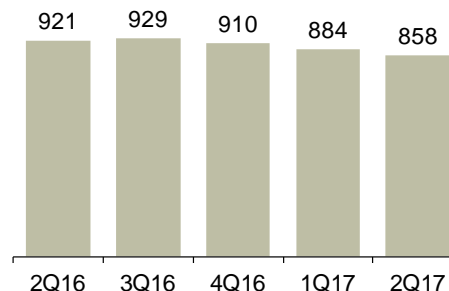
## COST STRUCTURE IMPROVING OVERALL

### ADMINISTRATIVE EXPENSES <sup>2</sup> (ISK m)

Real change in administrative expenses from 1H16 to 1H17: -1.2%



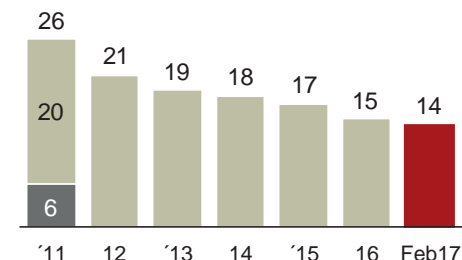
### PERIOD END FTE NUMBERS <sup>3</sup> (#, Parent company)



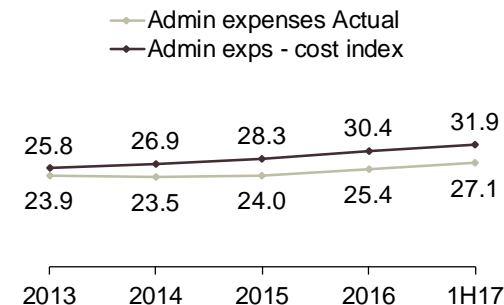
2. Excluding one off items

3. FTE numbers exclude summer employees.

### BRANCH NETWORK (#, Byr branches due to merger in dark grey)



### ADMIN. EXPENSE vs COST INDEX <sup>4</sup> (ISK bn, excl. one-off cost, parent company)



4. Administrative expense - cost index is calculated as 40% inflation and 60% salary index excluding one-off items.



## 4. Assets

# Assets

Total assets on par with year-end 2016, rose 1.8% in 2Q17

ISK m	30.6.2017	31.3.2017	31.12.2016
Cash and balances with CB	<b>227,189</b>	210,437	275,453
Bonds and debt instruments	<b>33,301</b>	35,678	31,256
Shares and equity instruments	<b>11,936</b>	12,128	10,626
Derivatives	<b>3,942</b>	2,322	1,953
Loans to credit institutions	<b>23,983</b>	35,142	17,645
Loans to customers	<b>721,820</b>	703,447	687,840
Investment in associates	<b>705</b>	705	450
Property and equipment	<b>6,663</b>	6,376	6,211
Intangible assets	<b>3,644</b>	3,024	2,672
Other assets	<b>10,103</b>	14,298	7,064
Non-current assets held for sale	<b>3,935</b>	5,251	6,384
<b>Total assets</b>	<b>1,047,221</b>	1,028,808	1,047,554

## Liquid assets

- The three line items, Cash and balances with CB, Bonds and debt instruments, and Loans to credit institutions, amount to about ISK 284bn, whereby ISK 269bn are considered to be liquid assets

## Loans to customers

- New lending amounted to ISK 108bn since year-end 2016
- The loan book has grown by 4.9% since year-end, despite ISK 76.7bn in loans being fully repaid
- Real estate remains Íslandsbanki's most important type of collateral. The weighted average loan-to-value (LTV) ratio for the residential mortgage portfolio was 61% at June 2017, compared to 69% at March 2017, mainly due to the new FMR valuation which generally raised housing valuations up 15.5% on average

## Other assets

- Decreased by ISK 4.2bn in the quarter which is a direct result of unsettled transactions; the date of settling fluctuates month by month causing the difference between quarters

## Non-current assets held for sale

- Contracted by ISK 2.4bn since year-end 2016; with the divestment of assets within the parent company (ISK 1.2bn) and assets in held for sale entities

## Asset encumbrance

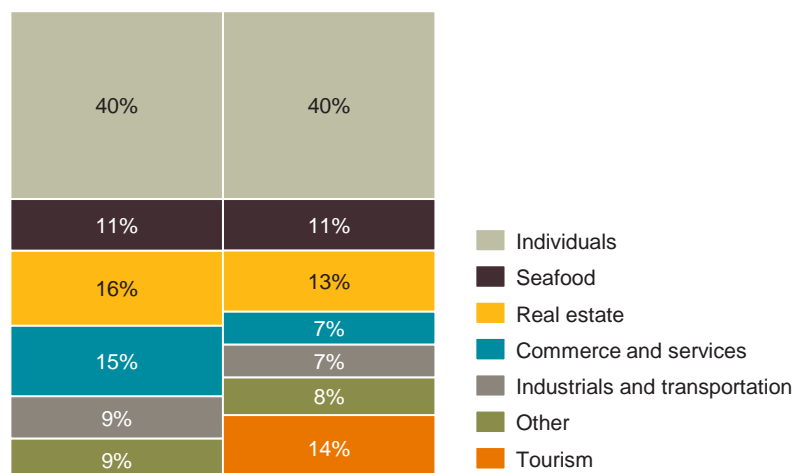
- The Bank's asset encumbrance ratio was 13.4% at end of June, compared to 14.2% at March 2017, the drop is primarily down to less restricted deposits at CBI, which were held against deposits from foreign investors

# Diversified loan portfolio

Loan portfolio grew by 4.9% in first half of 2017, largely reflecting economic activity in Iceland

## LOANS TO CUSTOMERS

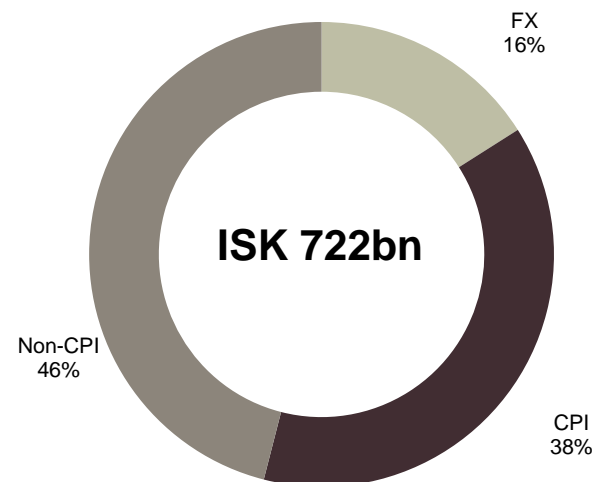
(ISK bn, by sector, consolidated)



Standard sectors Including tourism sector

## LOANS TO CUSTOMERS

(ISK bn, by currency, consolidated)



- The growth in Loans to customers is mainly due to diverse new lending to both new and existing customers
- The growth was balanced across lending units and especially strong in car leasing to individuals and companies

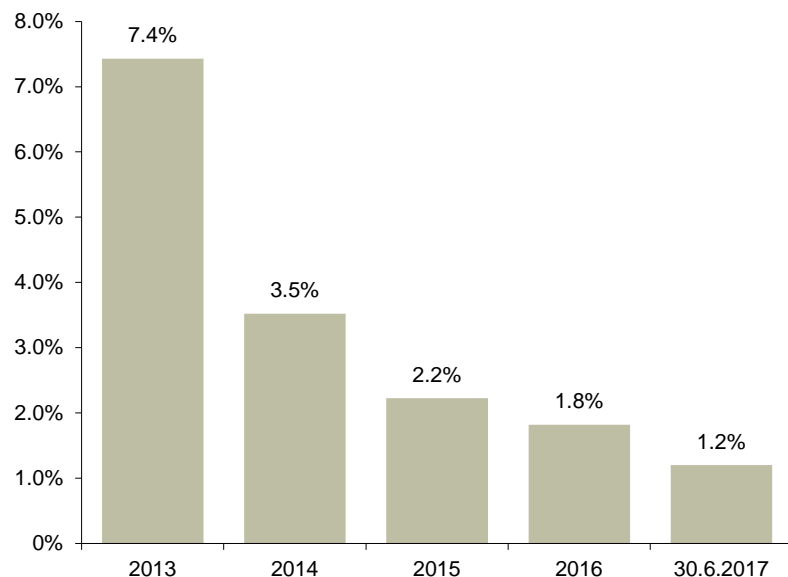
- Tourism continues to be growing sector in Iceland, but the Bank's loans to the tourism industry have been stable in the first half of year
- Outstanding loans to the tourism industry are 14% of the loan portfolio, most are in the real estate (hotels), commerce & service (car rentals, restaurants, tour operators) and industrials & transportation sectors (airport services)

# Non-performing loans

Asset quality continues to improve with a drop in NPL ratio to 1.2%, from 1.8% at year-end

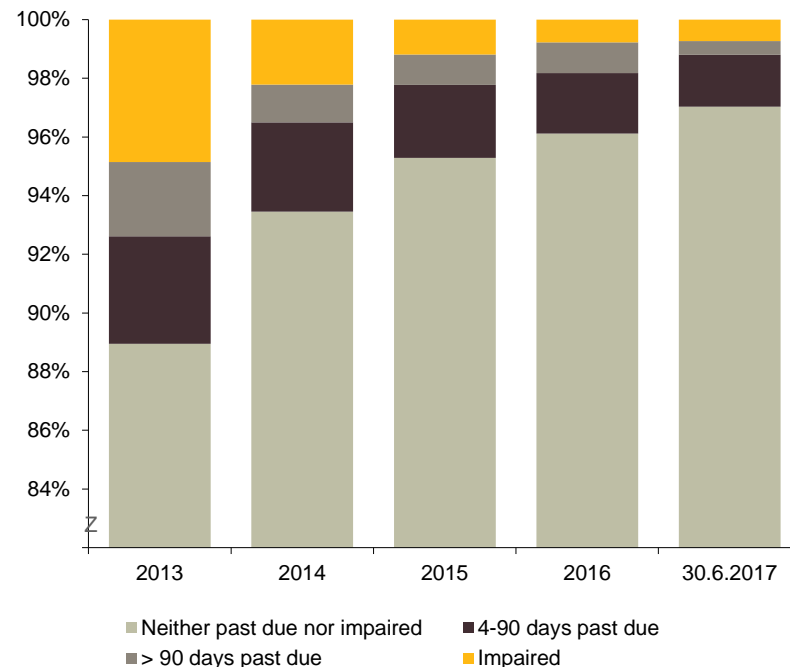
## NON-PERFORMING LOANS

(Impaired loans and past due (>90 days) loans and Loans to customers)



## PERFORMANCE OF LOANS TO CUSTOMERS

(Impaired, past due, and neither past due nor impaired loans)



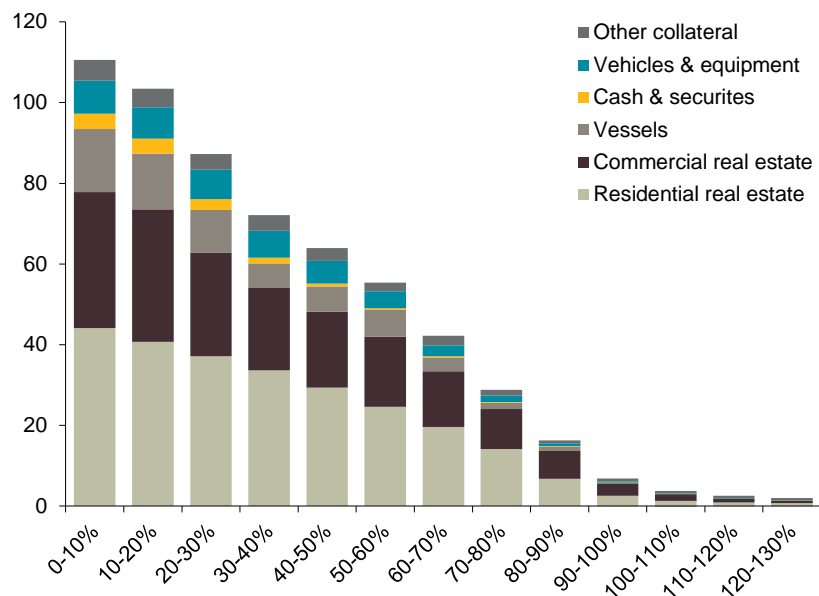
- The Bank's loan quality indicators have improved, with the ratio of non-performing loans decreasing from 1.8% to 1.2% from year-end 2016
- The observed default frequency is significantly lower than the long-term average
- As lower NPL levels are reached, the NPL ratio will decrease at a slower pace going forward

- This improvement reflects favourable economic conditions, prudence in lending operations and the successful restructuring of the loan portfolio
- More information on credit quality is available in the Bank's Pillar 3 Report

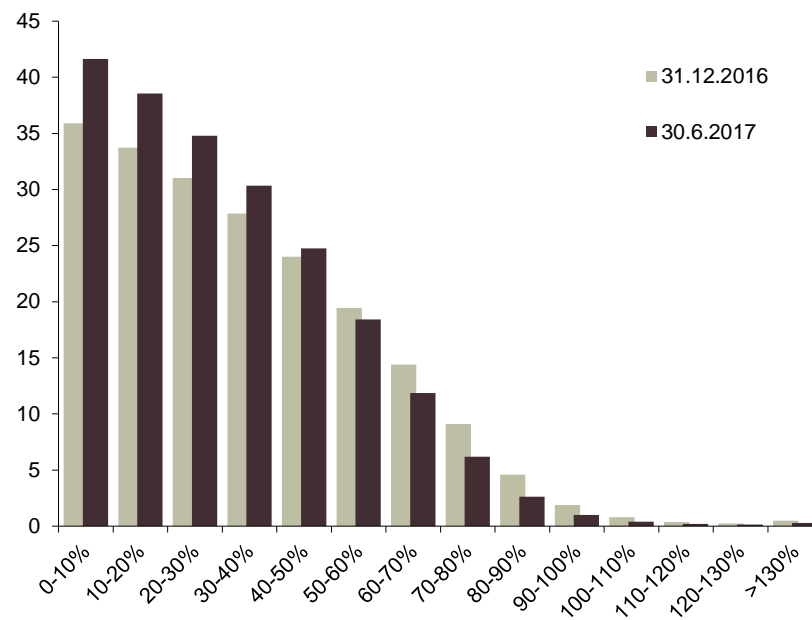
# LTV distribution of loan portfolio

Loans generally well covered by stable collateral, majority in residential and commercial real estate

**LTV DISTRIBUTION BY UNDERLYING ASSET CLASS**  
(ISK bn, by type of underlying asset, as of 30.06.2017)



**CONTINUOUS LTV DISTRIBUTION OF MORTGAGES TO INDIVIDUALS**  
(ISK bn, as of 30.06.2017 – average LTV 61% (67% 31.12.2016)\*)



- Most of the Bank's collateral is in the form of residential and commercial real estate
- The second most important collateral type is vessels, mostly fishing vessels

- The LTV distribution is calculated from tax value of properties which is published annually in June
- LTV has decreased significantly since year end 2016 which is mainly due to the newly published tax value of properties which raised housing valuations around 15.5% from its previous publication
- The Bank has exercised caution in its mortgage lending during rising real estate prices, and the Bank's underwriting standards for mortgages has tightened slightly in 2017

\* The average LTV can be calculated in many different ways and therefore the definition is important for comparison to other banks. The weight is Íslandsbanki's total amount outstanding on the property and the LTV used is the maximum LTV of all Íslandsbanki's loans of the property. The calculation is based on tax value.

## 5. Liabilities, Liquidity & Capitalisation

# Liabilities

Deposits subtract from year-end due to end of capital controls, funding diversification continues

ISK m	30.6.2017	31.3.2017	31.12.2016
Deposits from CB and credit inst.	9,362	11,253	4,922
Deposits from customers	572,407	567,486	594,187
Derivatives and short positions	7,344	5,041	4,798
Debt issued and other borrowings	227,274	223,327	212,468
Tax liabilities	11,581	10,062	8,473
Other liabilities	43,209	40,606	43,456
Non-current liabilities held for sale	116	268	325
<b>Total liabilities</b>	<b>871,293</b>	<b>858,043</b>	<b>868,629</b>
<b>Total equity</b>	<b>175,928</b>	<b>170,765</b>	<b>178,925</b>
<b>Total liabilities and equity</b>	<b>1,047,221</b>	<b>1,028,808</b>	<b>1,047,554</b>

## Deposits

- Customer deposits decreased by ISK 21.8bn in 1H17; in major part due to withdrawals from foreign financial institutions and domestic mutual funds
- The deposit to loan ratio decreased slightly to 78.0%, compared to 78.4% at Mar17
- Customer term deposits now 35% of total customer deposits

## Debt issued and other borrowings

- Includes covered bonds, commercial paper and bonds in foreign currency

## Equity

- At end of June 2017, the total capital ratio was 23.5%, compared to 23.3% at March 2017, marginally above the Bank's short- to medium-term target of 23%
- The CET1 ratio was 23.3% at end of June 2017 compared to 22.8% at March 2017
- In March 2017, ISK 10bn in dividends were paid out, or equivalent to around 50% of 2016 net income in line with the Bank's dividend policy

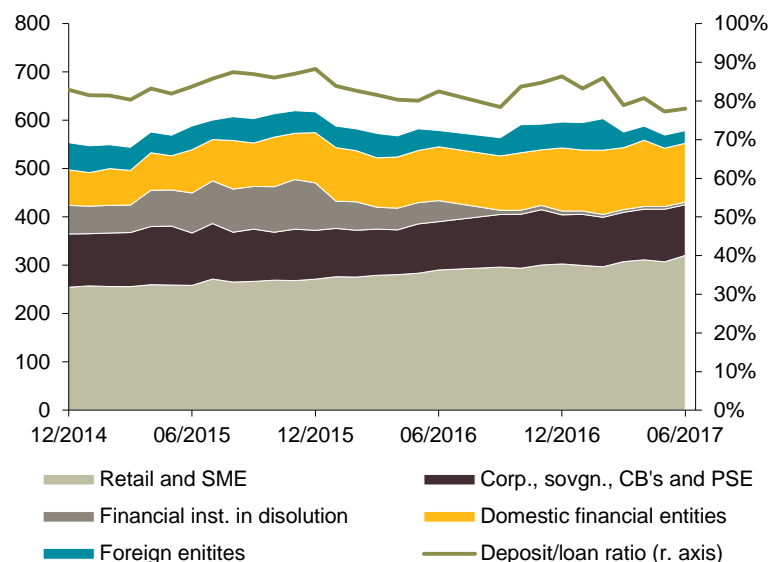
## Leverage

- The leverage ratio was 15.7% at the end of the period

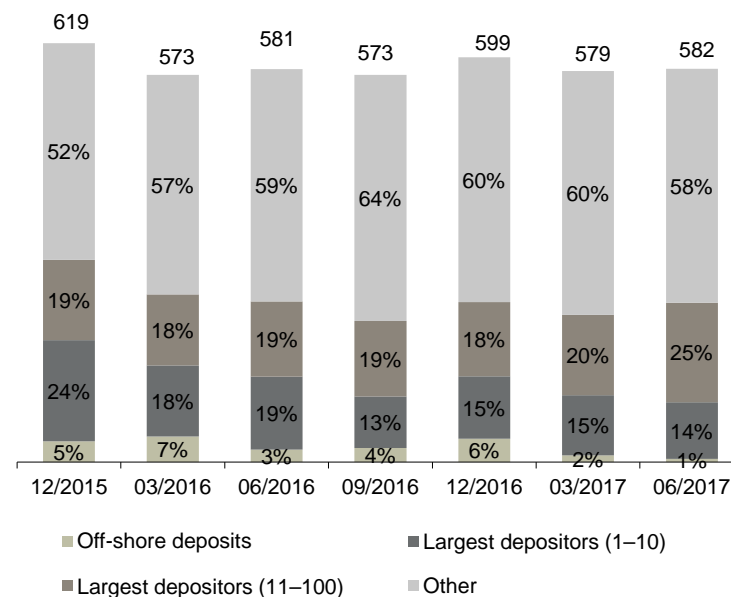
# Stable core deposits

Despite lifting of capital controls, deposits have remained mostly stable, 35% now customer term deposits

**DEPOSIT DEVELOPMENT AND DEPOSIT RATIO**  
ISK bn, consolidated



**DEPOSIT CONCENTRATION**  
ISK bn, consolidated



## Stable core deposit base

- Deposits remain the main funding source for the Bank and the deposit to loan ratio remains high

## Deposit concentration monitored closely

- At the end of 2Q17, 14% of the Bank's deposits belonged to the 10 largest depositors (excluding off-shore deposits)
- The ratio remains the same as at year-end 2016

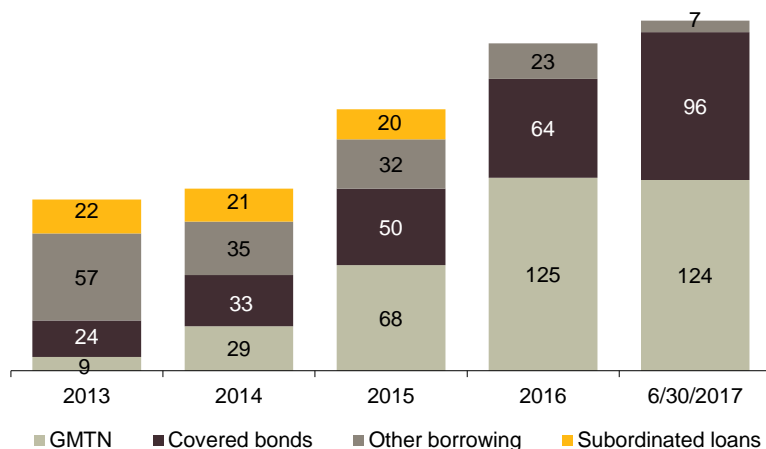


# Borrowings

Steady progress and good market access domestically and internationally

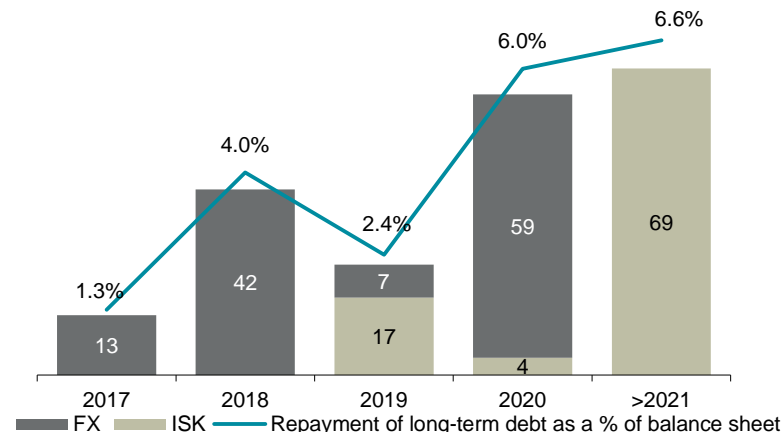
## BORROWING SOURCES

(ISK bn)



## MATURITY PROFILE OF LONG-TERM DEBT

(30.06.2017, ISK bn)

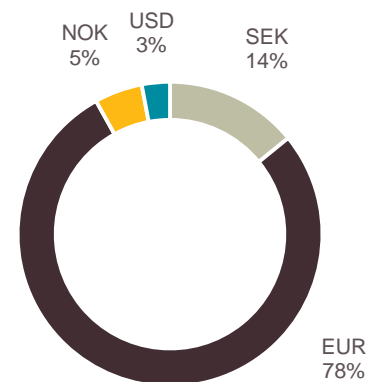


## Good market access and positive spread development

- Íslandsbanki is the largest issuer of covered bonds in the domestic market in 2017
  - A total of ISK 96bn in outstanding covered bonds at end of June
  - Total issuance in 1H 2017 amounted to ISK 30.6bn, primarily due to refinancing of an existing bond
  - Updated domestic issuance plan for 2017 estimates total issuance of ISK 35 – 45bn
- Total FX funding outstanding at 1H 2017 was ISK 123.8bn
  - Continued tightening on Icelandic FX secondary spreads

## FX BORROWING SPLIT BY CURRENCY

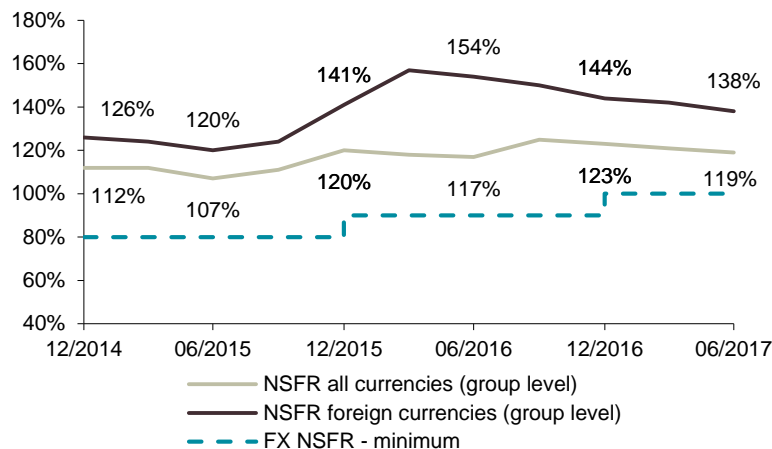
(%)



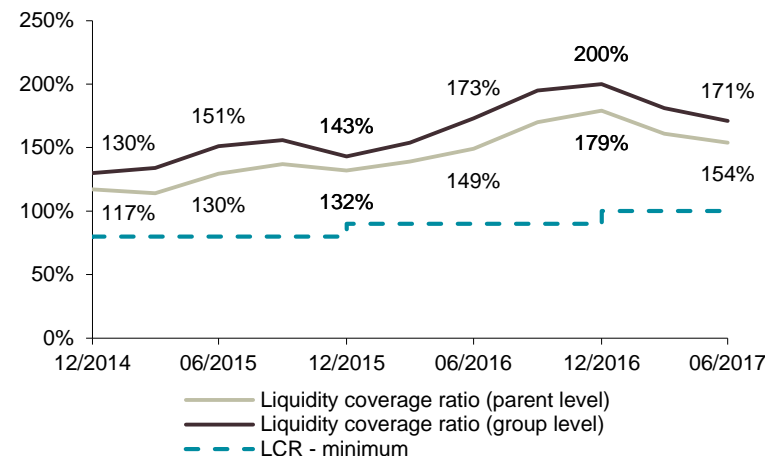
# Sound management of liquidity

Liquid assets of ISK 269bn above regulatory requirements and prudently managed

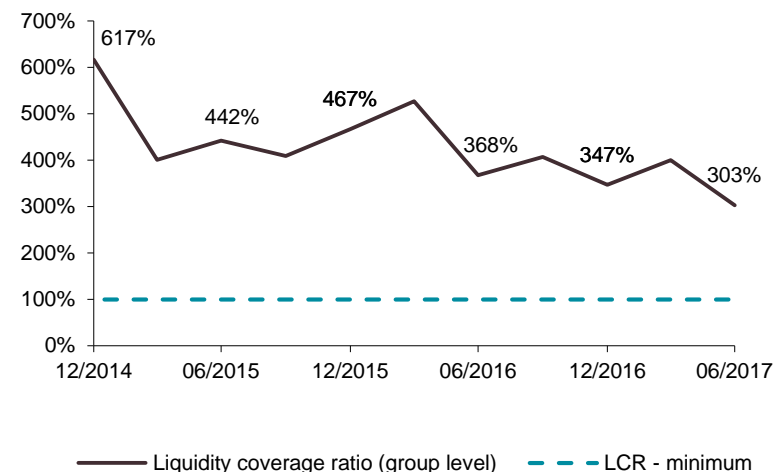
NET STABLE FUNDING RATIO (NSFR)



LIQUIDITY COVERAGE RATIO – ALL CURRENCIES



LIQUIDITY COVERAGE RATIO – FOREIGN CURRENCIES



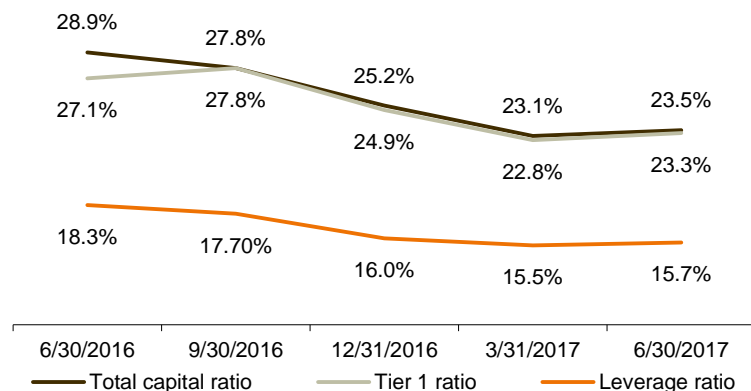
- All liquidity measures are above regulatory requirements
- FX liquid assets:
  - FX Government bonds have a minimum requirement of AA rating
  - FX cash placed with highly rated correspondent banks
- The Icelandic regulatory requirements for the NSFR currently only apply to foreign currency denominated assets and liabilities
- The liquidity ratios for all currencies have decreased slightly throughout 2Q17 in line with increased lending

# Sound capital position

The capital ratio remains above target and leverage is moderate

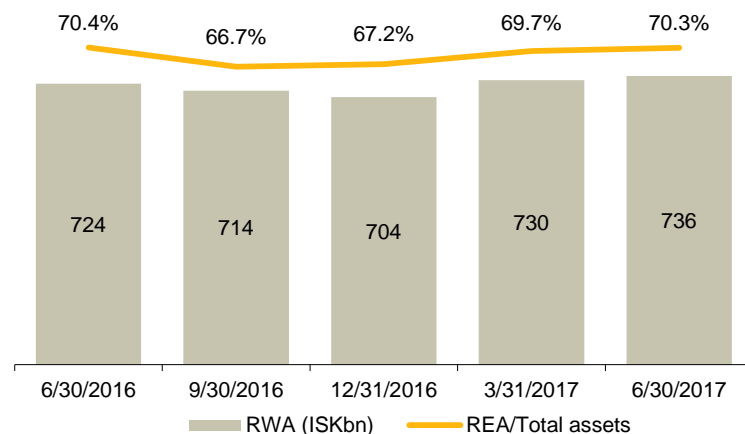
## CAPITAL RATIOS

%



## RISK Exposure Amount (REA)

ISK bn, %



## Capital ratios

- Total capital base was ISK 173bn at 30.06.2017, compared to ISK 177bn at YE2016, where the decrease is mainly due to a dividend payment of ISK 10bn
- The leverage ratio was 15.7% compared to 16.0% at YE2016

## Risk exposure amount (REA)

- REA was ISK 736bn at 30.06.2017, compared to ISK 704bn at YE2016, whereby the increase is mainly due to a rise in the loan portfolio
- The ratio of REA of total assets increased from 67.2% to 70.3%

## Capital target

- The long-term capital target assumes the Bank maintains a management buffer of about 0.5–1.5%, on top of the capital requirement according to SREP results, to cover FX fluctuations, and other volatility in earnings and REA
- Based on last year's SREP results of 19.2%, this translates to a long-term target total capital ratio of around 20% and a minimum CET1 ratio of around 15%

## Dividends

- The bank paid ISK 10bn in dividend in the first half, in line with the Bank's dividend policy of 40-50% of after-tax profit be paid out in dividends
- The Bank aims to continue with its capital optimisation process and expects to cautiously manage its capital ratios towards the long-term target in the short to medium term

# BBB ratings from both Fitch and S&P

Fitch upgrade in January 2017 to BBB/F3 and S&P in October 2016 to BBB/A-2 with positive outlook

## FITCH BBB/F3 STABLE OUTLOOK

Press Release 27 January 2017

- “The upgrade reflects the continuous strengthening of the **Icelandic operating environment** following extended robust economic growth and an improved external position. Fitch recently revised the Outlook on Iceland's rating to Positive (see “Fitch Revises Outlook on Iceland to Positive; Affirms at 'BBB+’”, dated 17 January 2017).
- Iceland has taken significant steps in reducing its external vulnerabilities and **removing capital controls**.
- The upgrade also reflects the **successful rebuilding by Íslandsbanki of a solid balance sheet** in the wake of Glitnir's collapse in 2008, including successfully restructuring a large share of its loan book and managing down legacy funding and trapped deposits in an orderly fashion.
- Íslandsbanki's ratings are underpinned by the bank's **leading Icelandic universal banking franchise**, with domestic market shares of about 30% in lending and deposits, continuously improving asset quality, a stable liquidity position and high reported capital ratios.[...] The bank's concentration in a small market is a rating constraint, as its size makes it more vulnerable to domestic and international shocks.”

## S&P BBB/A-2 POSITIVE OUTLOOK

Press release 25 October 2016

- “Operating conditions for Icelandic banks are improving, in our view, with falling private-sector leverage and improved access to foreign debt capital markets. We expect to see a continued stabilization of Íslandsbanki's credit risk from the strong economic performance in Iceland and lower private-sector debt. The positive outlook reflects **positive trends in the Icelandic banking sector** and the potential that improved clarity of future capital and ownership could lead to an upgrade in the coming two years.
- Íslandsbanki's capital levels are the **highest among Icelandic peers**, however, we see uncertainty as to future levels due to preparation for a possible sale or IPO.
- The improved anchor for the Icelandic banking sector and the bank's capital metrics result in a two-notch improvement in our assessment of Íslandsbanki's SACP to 'bbb+' from 'bbb-'. [...], we apply a one-notch negative adjustment to Íslandsbanki's 'bbb+' stand-alone credit profile (SACP) [...], given our expectation that banks might look to optimize their capital bases, given their **very high leverage ratios versus international peers**, and to have more attractive returns on equity for potential investors”

## ÍSLANDSBANKI

	S&P	FITCH
Long-term	BBB	BBB
Short-term	A-2	F3
Outlook	Positive	Stable
Rating action	Oct 2016	Jan 17

## ICELANDIC SOVEREIGN

	S&P	FITCH	MOODY'S
Long-term	A	A-	A3
Short-term	A-1	F1	P-2
Outlook	Stable	Positive	Stable
Rating action	Jun 2017	Jul 2017	Sept 2016

## 6. Financial targets and key points

# Financial targets

Medium and long term strategies structured around achieving key financial targets

	TARGET	1H17	2016	2015	Guidance
ROE REGULAR OPERATIONS <sup>1</sup>	9-11%	✓ 11.2%	✓ 10.7%	✓ 13.2%	<ul style="list-style-type: none"> <li>As the Bank retains a large pool of liquid assets, interest rate level in Iceland can have a substantial impact on ROE levels</li> <li>The bank tax, excluded thus far from target returns, will have an impact on profitability if kept at current high levels</li> <li>Target ROE from regular operations in the range of 8-10% in 2017</li> </ul>
COST / INCOME RATIO <sup>2</sup>	<55.0%	59.2%	56.9%	56.2%	<ul style="list-style-type: none"> <li>This is a medium to long term target, C/I ratios can be expected to be higher in the near term</li> <li>Headcount and non-headcount related cost control programmes in place</li> </ul>
CET1	>15% LT	✓ 23.3%	✓ 24.9%	✓ 28.3%	<ul style="list-style-type: none"> <li>Based on the regulatory SREP requirement with 50-150bp management buffer</li> </ul>
TOTAL CAPITAL RATIO	> 20.0% LT > 23.0 ST	✓ 23.5%	✓ 25.2%	✓ 30.1%	<ul style="list-style-type: none"> <li>Current target of &gt;23% for the short term and &gt;20% for the long term</li> <li>Short term target of 23% was set due to risks due to lifting of capital controls and IFRS9. Both of those risk factors are becoming less relevant and therefore this target is likely to be adjusted in the coming months.</li> </ul>
DIVIDEND PAYOUT RATIO	40-50%	✓ 50% <sup>3</sup>	✓ 50%	✓ 40%	<ul style="list-style-type: none"> <li>Dividend pay-out ability will be impacted if the bank tax will be kept at current high levels</li> </ul>

1. Return from regular operations on normalized CET1 of 15%, adjusted for risk free interest on excess capital. Results 2014-15 based on CET1 14%. Earnings from regular operations is defined as earnings excluding one-off items e.g. net loan impairment before collective impairment, fair value gain deriving from changes in accounting treatment, Bank tax, one off costs and net earnings from discontinued operations

2. Calculated as (Administrative expenses + Contribution to the Depositors' and Investors' Guarantee Fund – One off items) / Total operating income

3. The AGM decided that dividends be paid in 2017 in the amount of ISK 10bn on 2016 profits

# Key points

Delivering responsible growth driven by the vision to be **#1 for service**

1

Stable operating environment following **full liberalisation of capital controls** for individuals and businesses resulting in **Sovereign upgrades** M:A3 / F:A- / SP:A

2

Proven business strategy of being **#1 for service** renders high satisfaction scores, strong recurring revenues, and **resilient ROE**

3

**Solid balance sheet**, successful restructuring and all holdings in non-related business divested - asset quality continues to improve with **NPLs 1.2%**

4

Sound capital and liquidity ratios that compare very well with peers – 15.7% leverage ratio and **capital optimisation process** continued with 10bn dividend in March 2017

5

Good market access to international funding markets - **benchmark EUR 500m** issue performing well in aftermarket, lowest coupon since 2008 and largest in size at time of issuance

6

Fitch **upgrade** to BBB/F3 stable outlook in Jan17 and S&P **upgrade** to BBB/A-2 on positive outlook in Oct16

**GDP**  
5.3% **2017**

Net profit	8.0bn
ROE (Regular operations)	11.2%
Capital Ratio	23.5%
Loan growth	4.9%

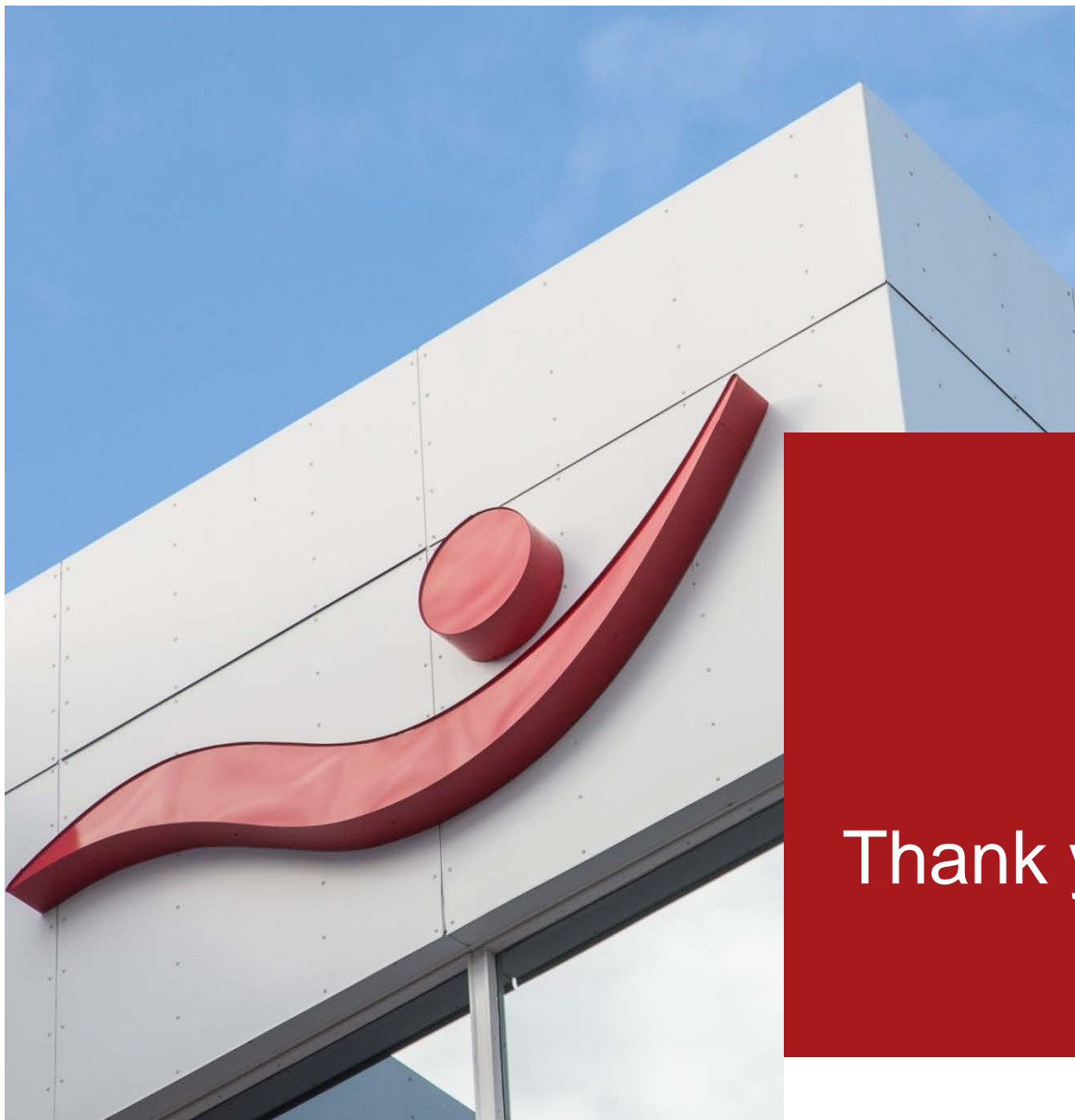
**NPLs**  
1.2%

**BBB**  
ratings

LCR	171%
NFSR	119%
Leverage ratio	15.7%



Above information is based on the Bank's 1H17 financials and forecasts by Íslandsbanki Research.



Thank you