

FINANCIAL STATEMENTS
30.09.2014

INVESTOR PRESENTATION



HIGHLIGHTS IN Q3 2014

STABLE OPERATION WITH POSITIVE RESULTS

- **Good quarter**
- **All income items on or above budget**
- **Continued increase in Commission income**
- **Operating expenses relatively modest during the period as customary in Q3**
- **Increased loans and loan commitments**
- **More focus on liquidity management**
- **Capital base continues to grow**



HIGHLIGHTS OF THE THIRD QUARTER OF 2014

FINANCIALLY ROBUST BANK WITH STABLE CORE BUSINESS

- Solid financial results
 - Return on equity 19.9%
 - Capital ratio 24.6%
- Regular operations remain stable
 - Commission income up 22% YoY
 - Interest income unchanged and net interest margin remains same at 2.9%
 - Cost-to-income ratio 48.7%
- Irregular items have positive impact on financial results
- Income tax and bank levy amounted to ISK 6.5 billion
- Arion Bank and Norwegian shipping company Havila Shipping ASA signed agreement on loan from Bank worth NOK 300 million
- Arion Bank and United Silicon signed an agreement on the Bank's funding of a silicon plant at Helguvík

HIGHLIGHTS OF THE THIRD QUARTER OF 2014 CONTD.

- Startup Reykjavík event was held for third time
 - The ten companies presented themselves and their ideas to investors
- Customers given the option of ordering foreign currency via the Bank's website
- Arion Research published its report on the tourist industry in Iceland
- The Bank participated in the Icelandic Fisheries Exhibition held in Kópavogur
- Arion's vehicle financing unit celebrated its second birthday in September and moved into Borgartún 18
- Internal Audit completed external quality audit
 - It confirmed the sound procedures and working practices in place at the Bank
- Arion Bank football tournament held for 4th time in Reykjavík
 - Total of 2,400 children took part
- A number of meetings, courses, conferences, lectures and art exhibitions were held at the Bank during the period



HIGHLIGHTS OF 9M 2014

FINANCIAL HIGHLIGHTS



INCOME STATEMENT



INCOME STATEMENT

EXCELLENT RESULTS FOR 9M 2014

Substantial increase in Net commission income mostly due to excellent performance in Cards and Investment Banking

Increase in net financial income mainly due to HB Grandi shares

Successful restructuring efforts resulting in positive net valuation changes

	9M 2014	9M 2013	Diff	Diff%
Net interest income	18,309	18,313	(4)	(0%)
Net commission income	10,119	8,284	1,835	22%
Net financial income	5,861	954	4,907	514%
Other income	3,963	4,035	(72)	(2%)
Operating income	38,252	31,586	6,666	21%
Salaries and related expense	(10,026)	(9,439)	(587)	6%
Other operating expenses	(8,598)	(8,744)	146	(2%)
Net change in valuation	2,877	(119)	2,996	-
Net earnings before taxes	22,505	13,284	9,221	69%
Income tax	(4,456)	(2,851)	(1,605)	56%
Bank levy	(2,008)	(300)	(1,708)	569%
Net gain from disc. operations	6,592	(3)	6,595	-
Net earnings	22,633	10,130	12,503	123%

Amounts are in ISK millions

INCOME STATEMENT

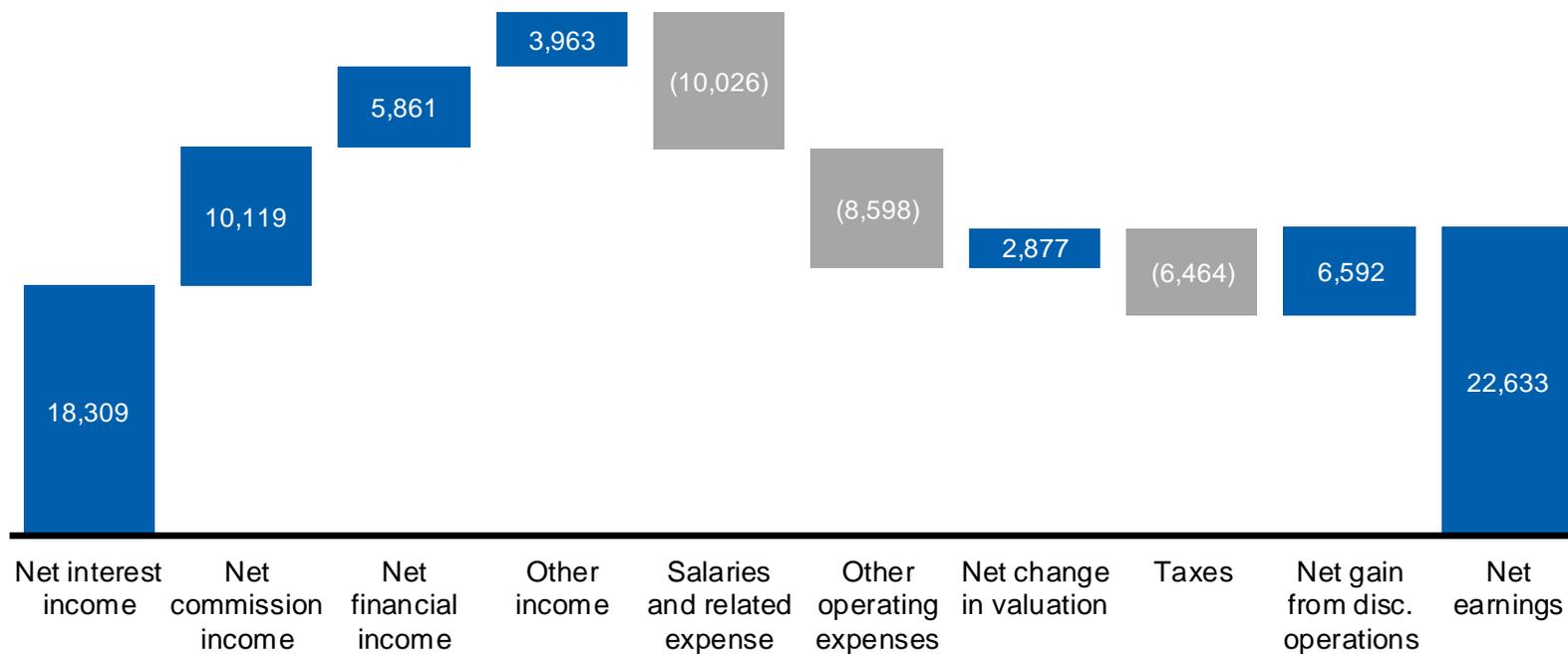
CONTINUED SOLID PERFORMANCE

	Q3 2014	Q2 2014	Q1 2014	9M 2014
Higher inflation in Q2 and Q3 resulting in higher net interest income				
Continued growth in net commission income				
Decrease in other income due to the sale of Landfestar, a subsidiary specializing in commercial real estate				
Lower effective income tax rate in Q2 compared to other quarters due to tax exemption relating to appreciating share prices				
Net interest income	6,343	6,483	5,483	18,309
Net commission income	3,526	3,445	3,148	10,119
Net financial income	1,994	4,439	(572)	5,861
Other income	689	2,356	918	3,963
Operating income	12,552	16,723	8,977	38,252
Salaries and related expense	(2,862)	(3,714)	(3,450)	(10,026)
Other operating expenses	(2,787)	(3,064)	(2,747)	(8,598)
Net change in valuation	876	34	1,967	2,877
Net earnings before taxes	7,779	9,979	4,747	22,505
Income tax	(1,989)	(1,152)	(1,315)	(4,456)
Bank levy	(633)	(715)	(660)	(2,008)
Net gain from disc. operations	67	6,433	92	6,592
Net earnings	5,224	14,545	2,864	22,633

Amounts are in ISK millions

INCOME STATEMENT

BREAKDOWN OF NET EARNINGS IN 9M 2014



Amounts are in ISK millions

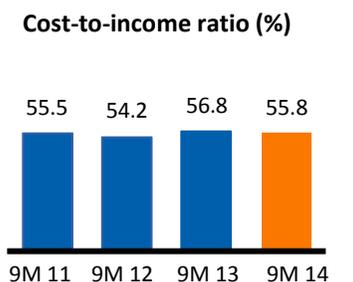
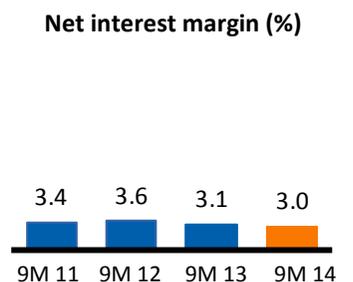
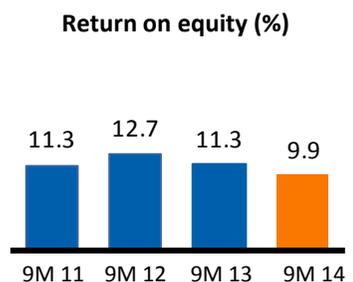
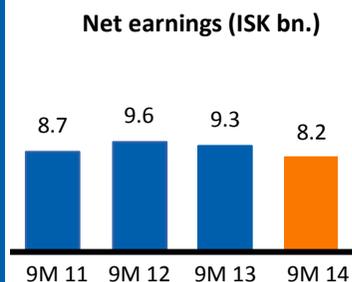
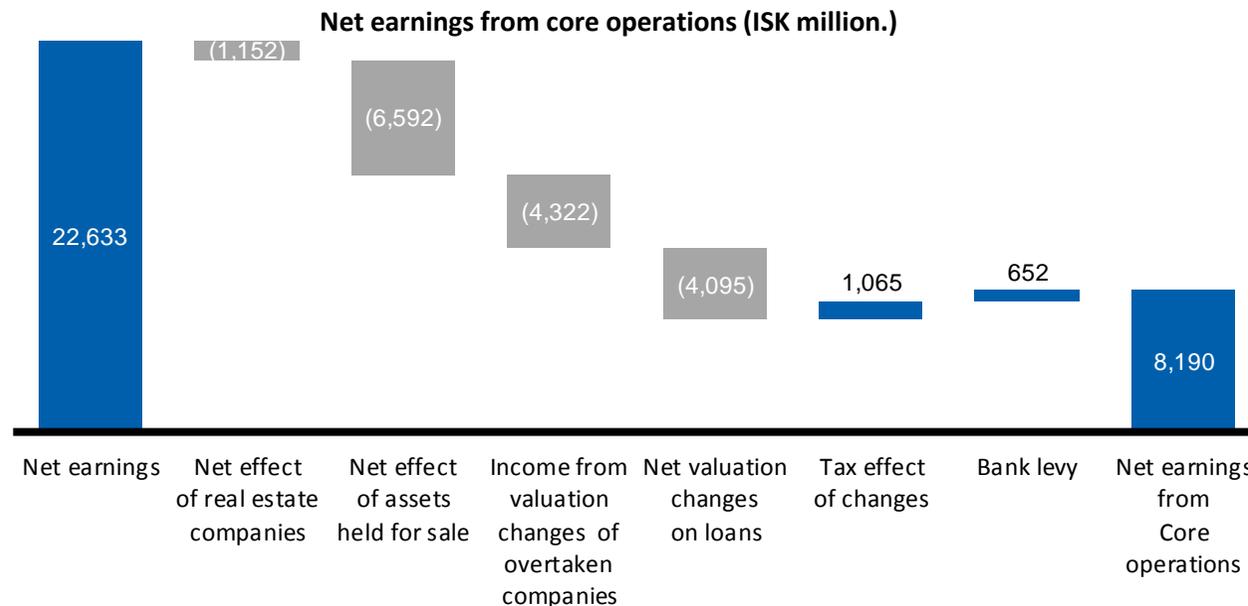
CORE INCOME

INCREASED CHALLENGE TO DEFINE CORE VS. NON CORE EARNINGS AS THE BANK DEVELOPS

Increased equity has a major effect on returns

Irregular items have great effect on outcome from core operation

No expenses have been deducted in core income calculation even if they partially relate to irregular operations



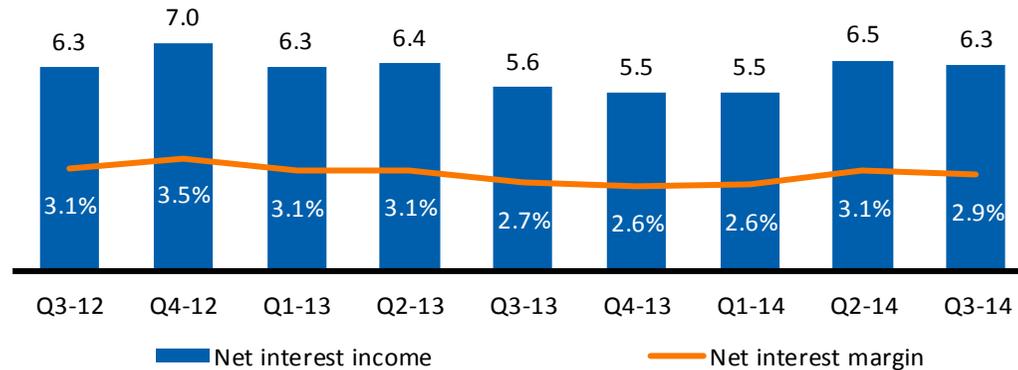
NET INTEREST INCOME

NET INTEREST INCOME AT NORMAL LEVELS AFTER A SLIGHT DEPRESSION IN PRIOR QUARTERS

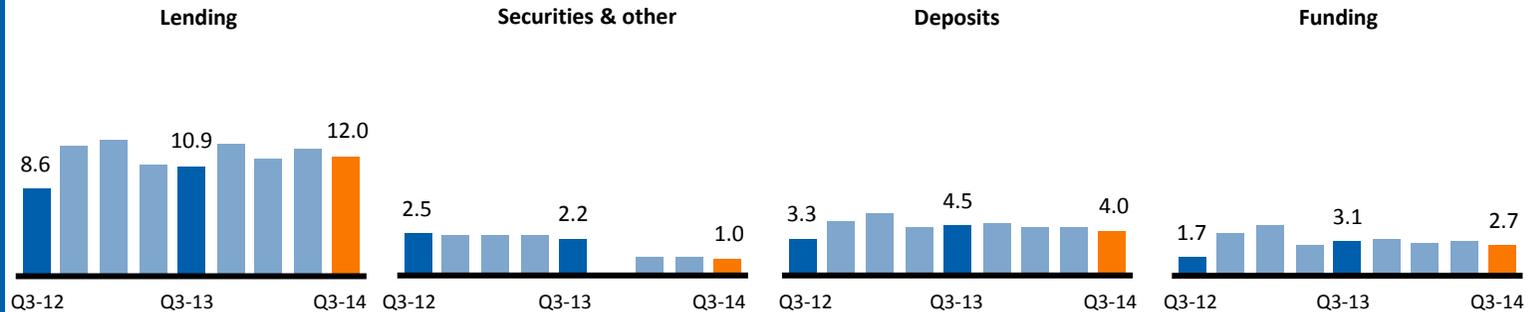
Increase in Net interest income in Q2 and Q3 mainly explained by higher inflation and better performance in liquidity management

Challenge to maintain Net interest margin in a highly competitive environment

By quarters from Q3 2012 – Q3 2014 (ISK bn.)



Interest income by type (ISK bn.)



NET COMMISSION INCOME

CONTINUED GROWTH IN Q3

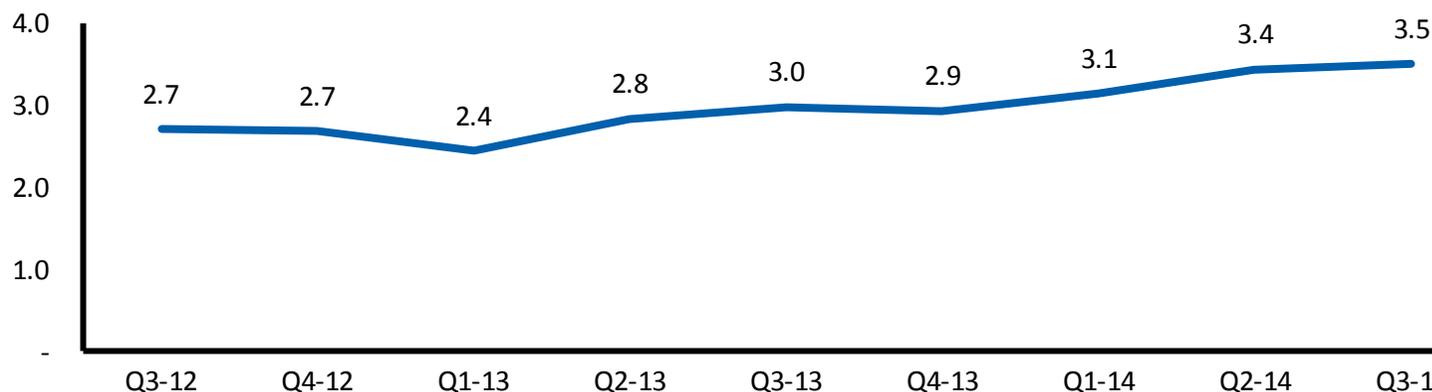
Growth expectations are materializing, Net commission income has increased by 22% from 9M 2013

Net commission income from cards increased by 27% from 9M 2013

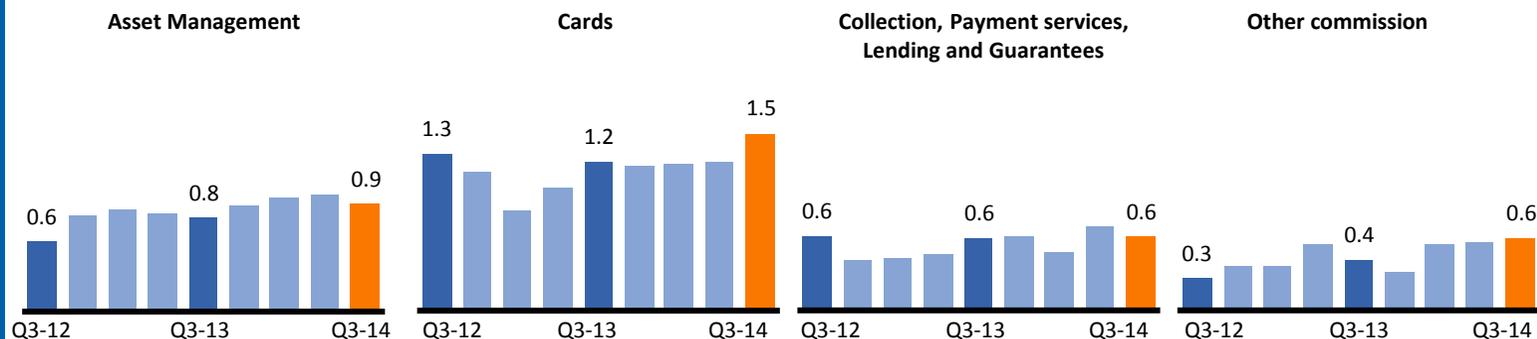
Excellent performance in Investment Banking

Asset management continues to perform well

Net commission income from Q3 2012 – Q3 2014 (ISK bn.)



By type from Q3 2012 – Q3 2014 (ISK bn.)



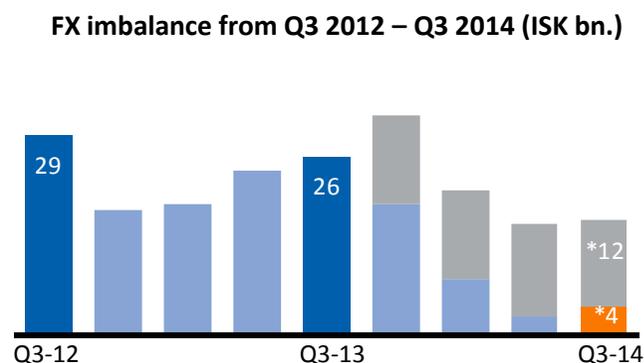
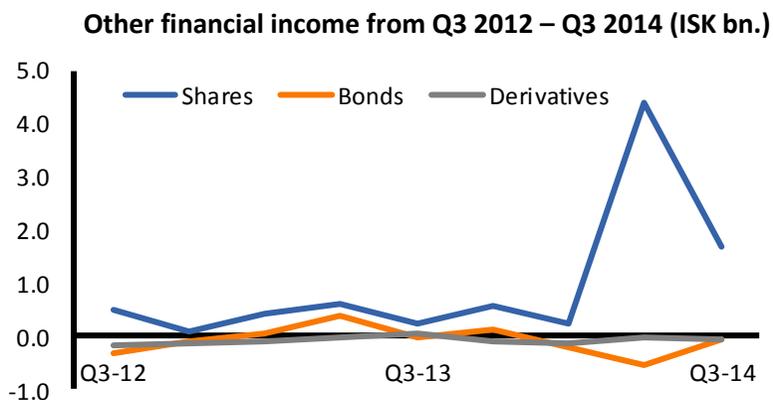
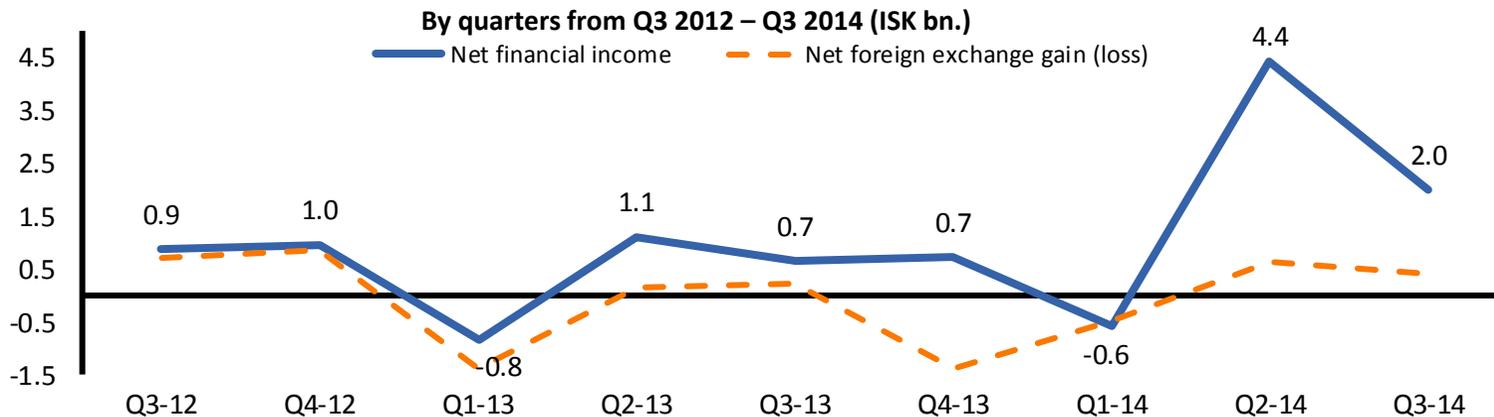
NET FINANCIAL INCOME

REDUCED VOLATILITY DUE TO DECREASED FX IMBALANCE

Positive outcome from shares mainly related to listed shares in HB Grandi and Hagar

The bond market has been unfavorable

Successful decrease in FX-imbalance and more focus on FX management resulting in FX gain



*Arion Bank has ISK 4.2 bn. and subsidiaries ISK 12.4 bn. in FX imbalance

OTHER INCOME

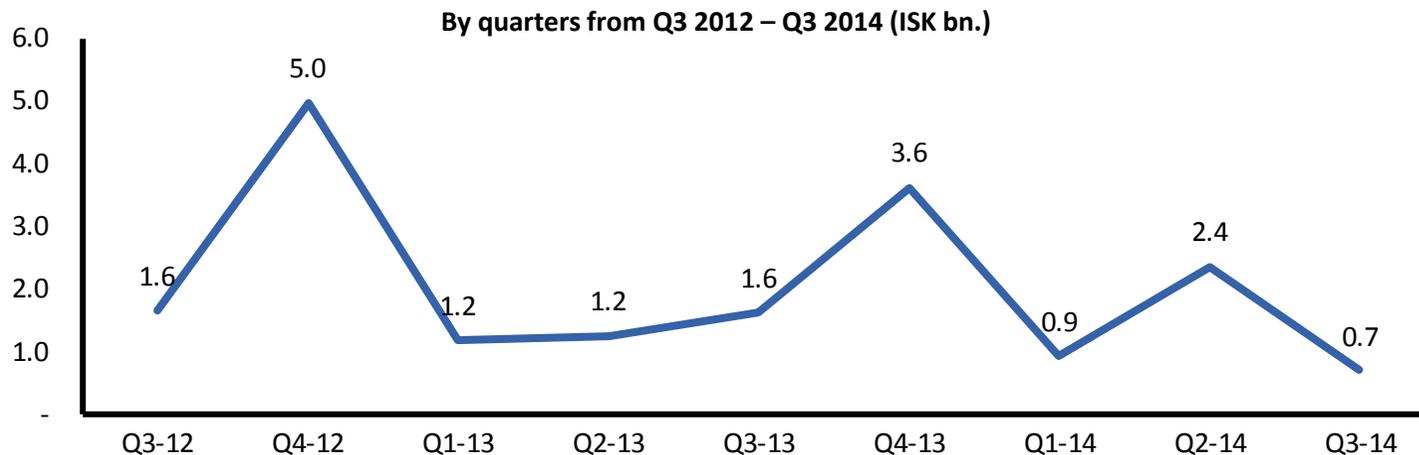
DECREASE IN OTHER INCOME DUE TO THE SALE OF LANDFESTAR AS PREVIOUSLY INDICATED

Decrease in rental income from investment property due to the sale of Landfestar, rental income now immaterial

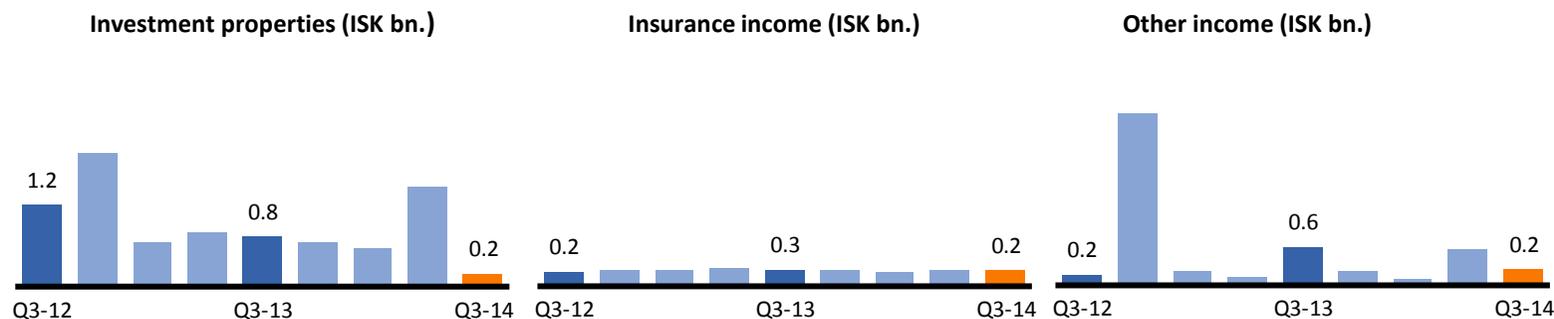
No material FV changes on investment property in Q3

Realized gain on investment property in Landey ISK 138 million in Q3

Very stable insurance income from Okkar líf



Other income by type from Q3 2012 – Q3 2014



TOTAL OPERATING EXPENSES

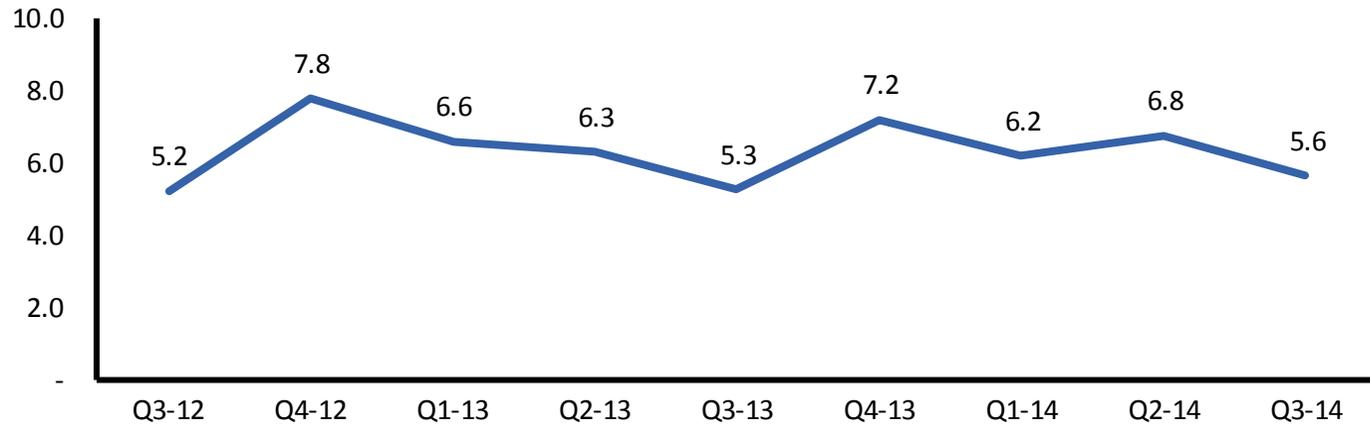
CONTINUED FOCUS ON OPERATING EFFICIENCY

Increase in salaries from 9M 2013, mainly due to the Banks's performance plan

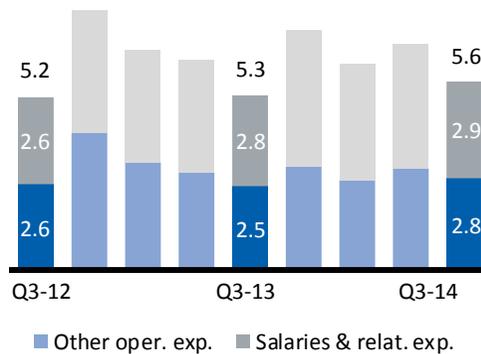
Slight decrease in other operating expenses compared to 9M 2013

Favorable cost to income ratio mainly related to increase in operating income

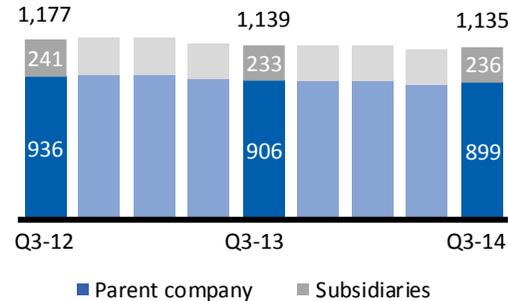
By quarters from Q3 2012 – Q3 2014 (ISK bn.)



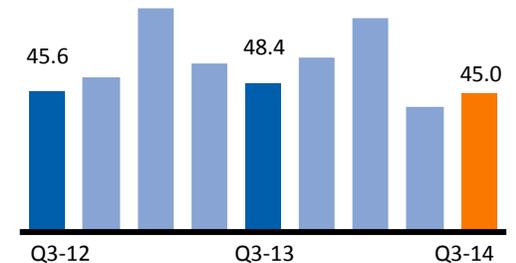
By type (ISK bn.)



Total employees



Cost-to-income ratio (%)





BALANCE SHEET

BALANCE SHEET

THE BANK IS WELL PREPARED FOR THE LIFTING OF CAPITAL CONTROLS

Increase in Loans to customers related to loans to individuals and corporates in seafood, real-estate and industry

Other changes from June mainly related to liquidity management

Strong platform for future growth

Assets					
Billion ISK	30.09.2014	30.06.2014	Diff%	31.12.2013	Diff%
Cash & balances with CB	33	17	92%	38	(12%)
Loans to credit institutions	109	140	(22%)	102	6%
Loans to customers	653	637	2%	636	3%
Financial assets	99	99	(0%)	87	15%
Investment property	3	6	(52%)	29	(90%)
Other assets	45	49	(8%)	48	(5%)
Total assets	942	949	(1%)	939	0%

Liabilities and Equity					
Billion ISK	30.09.2014	30.06.2014	Diff%	31.12.2013	Diff%
Due to credit institutions & CB	21	29	(28%)	28	(25%)
Deposits from customers	483	474	2%	472	2%
Other liabilities	56	60	(7%)	58	(3%)
Borrowings	192	200	(4%)	205	(6%)
Subordinated loans	31	31	0%	32	(2%)
Equity	160	155	3%	145	10%
Total liabilities and equity	942	949	(1%)	939	0%

Amounts are in ISK billions

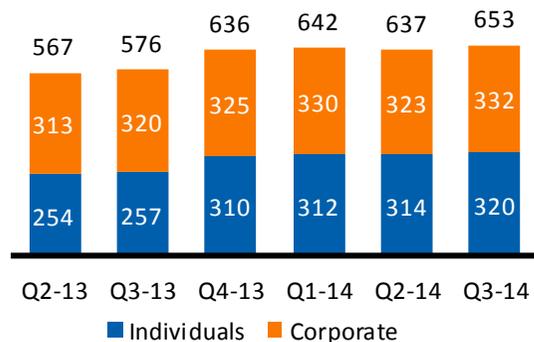
LOANS TO CUSTOMERS ARE WELL DIVERSIFIED

INCREASE IN LOANS TO BOTH CORPORATES AND INDIVIDUALS

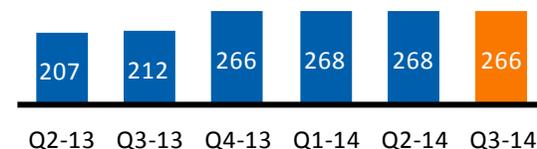
Increased lending to new export revenue generating industries

It is the strategic objective of the Bank to maintain a well diversified loan portfolio in all corporate sectors

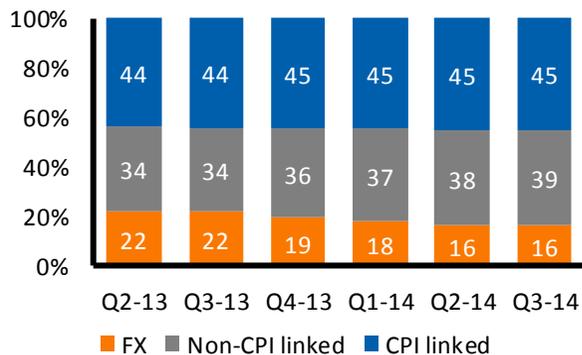
Development (ISK bn.)



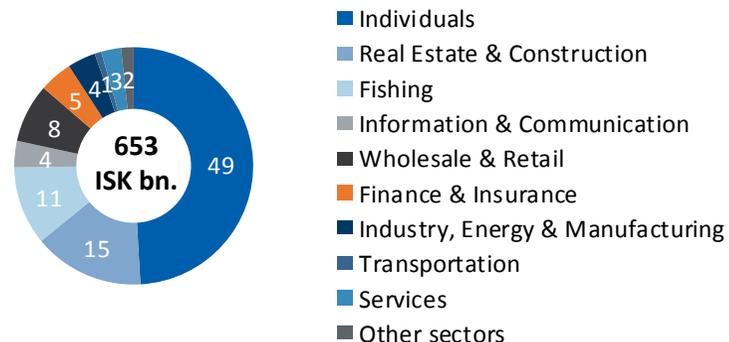
Mortgage loans (ISK bn.)



By type 30.09.2014 (%)



By sectors 30.09.2014 (%)



IMPROVING ASSET QUALITY

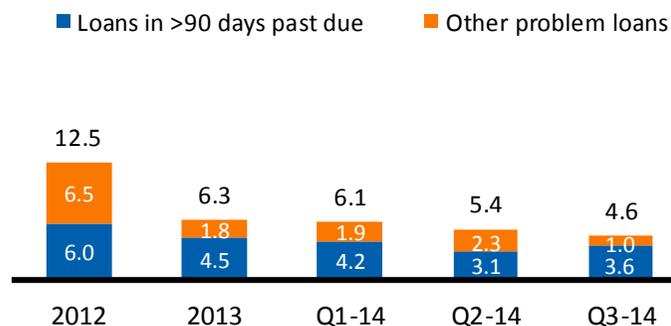
GOOD PROGRESS IN PROBLEM LOANS DURING Q3 2014

The Bank has already reached its year end goal to be below 5%

Problem loans as a percentage of equity are now starting to resemble those of other Nordic Banks

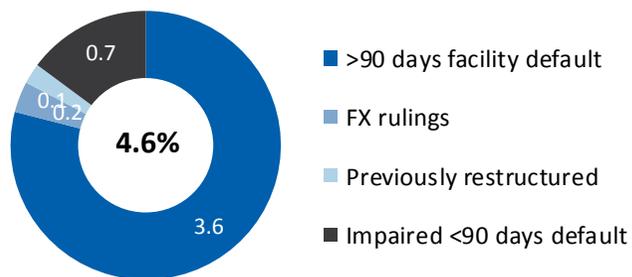
Improving asset quality will continue to be a focus point for the Bank

Development of problem loans (%)

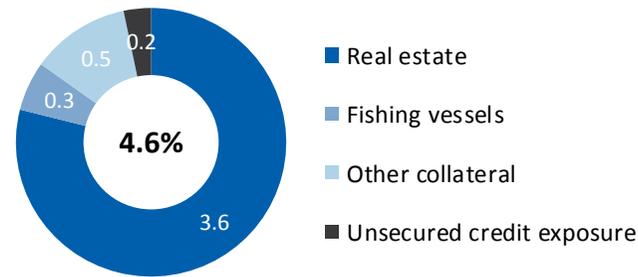


The Bank defines problem loans as book value of loans (i.e. net of impairment) that are either individually impaired or are over 90 days past due and not impaired as % of total book value of loans to customers

Problem loans by status (%)



Collateral behind problem loans (%)



STRONG FUNDING PROFILE

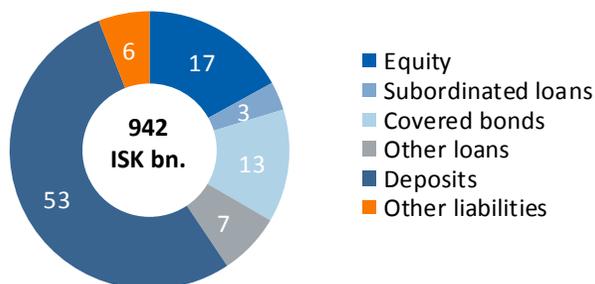
WELL BALANCED FUNDING PROFILE

Strong long-term funding and limited need for refinancing

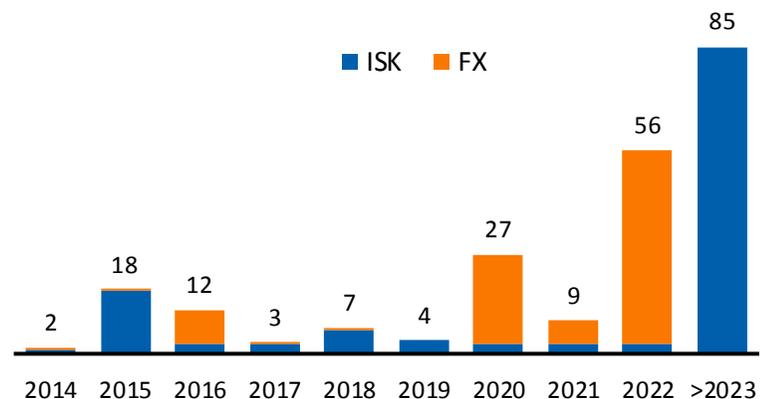
Long term financing mostly due 2020 or later

The Bank received a revised credit rating from Standard & Poor's in October. The credit rating remains BB+ but outlook was changed from stable to positive which improves the Bank's possibilities for new funding and potential refinancing

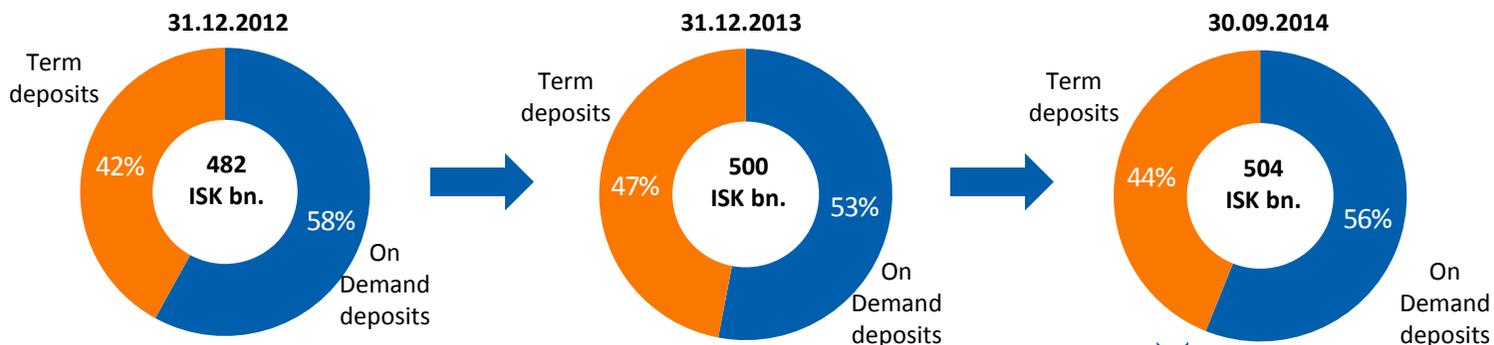
Breakdown of liabilities and equity (%)



Maturity of long-term funding 30.09.2014 (ISK bn.)



Development of total deposits by maturity



VERY SOLID CAPITAL BASE

INCREASE IN NEW LENDING AFFECTS THE CAPITAL RATIO

Arion Bank has maintained very solid levels of capitalization due to strong profit generation.

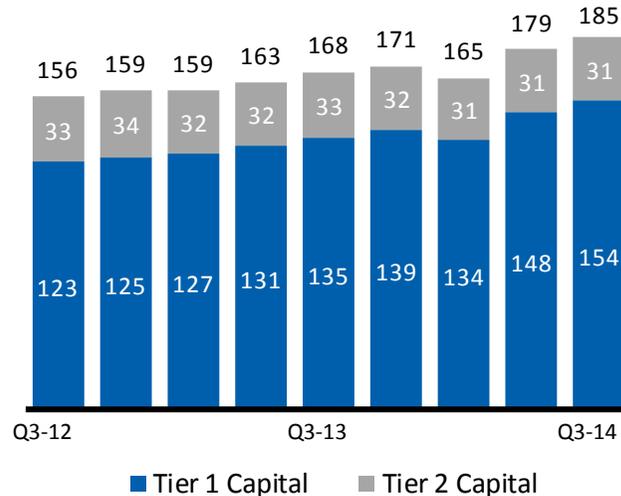
As Q3 is not audited the Bank cannot add Q3 net earnings to its capital base.

RWA increase due to new lending and commitments

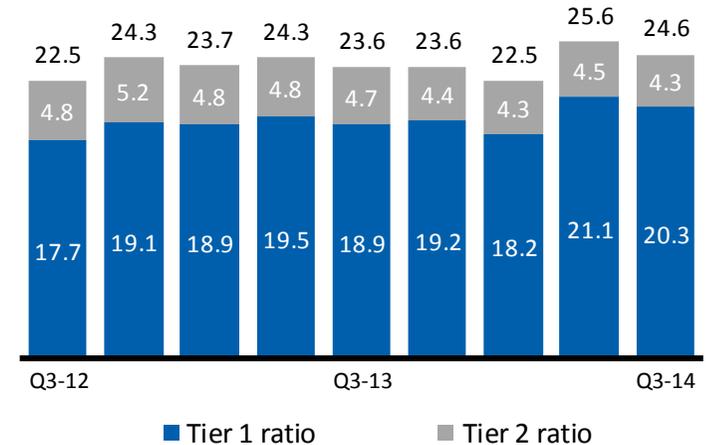
The Bank is using standardized approach calculating RWA.

RWA/Total Assets is approx. 77%.

Total capital base (ISK bn.)



Total capital ratio (%)

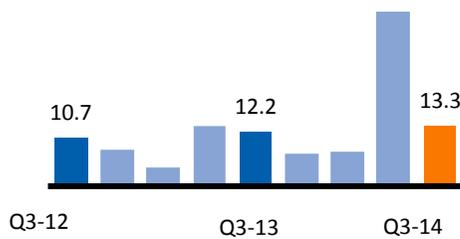


KEY FINANCIAL INDICATORS



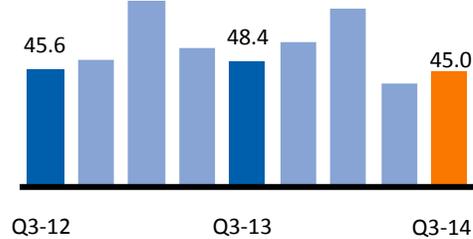
KEY FINANCIAL INDICATORS

Return on equity (%)

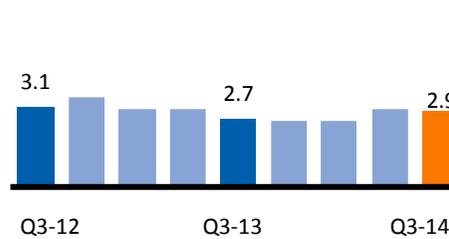


Cost-to-income ratio (%)

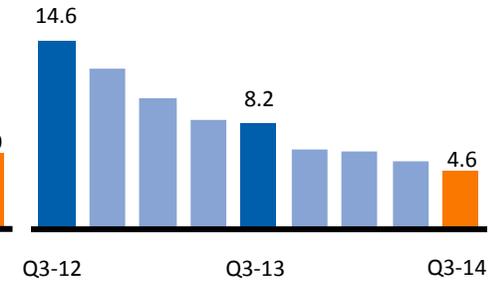
without net valuation change



Net interest margin (%)

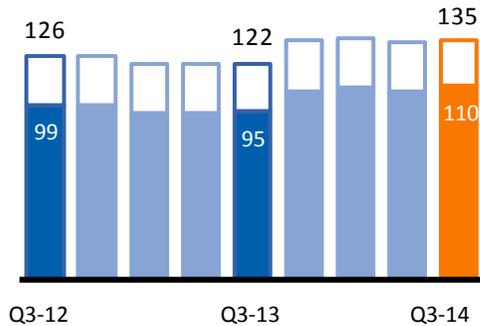


Problem loans* (%)

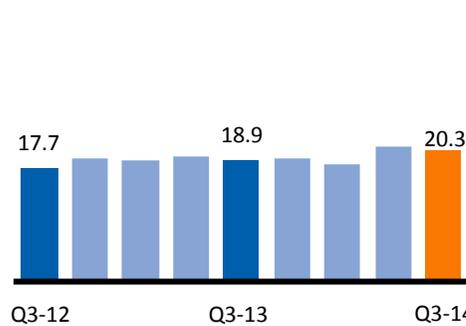


Loans-to-deposits ratio (%)

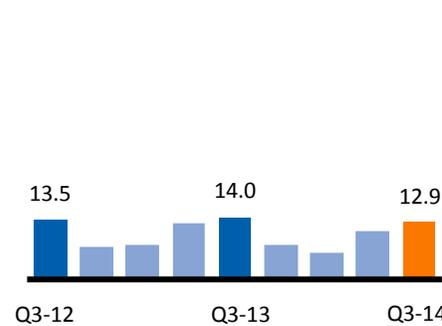
without loans financed with covered bonds



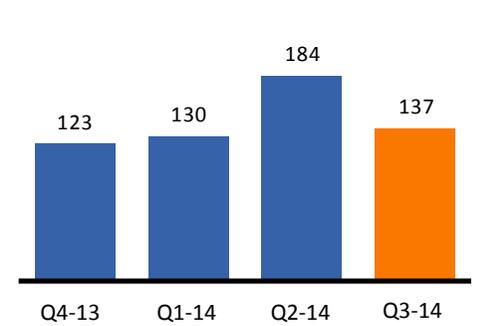
Tier 1 ratio (%)



Core return on equity (%)



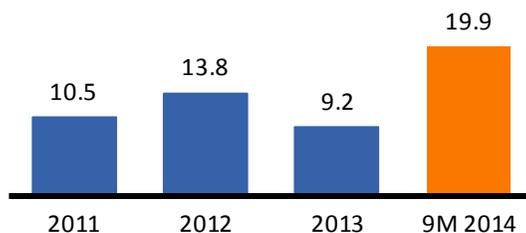
Liquidity coverage ratio (LCR) (%)



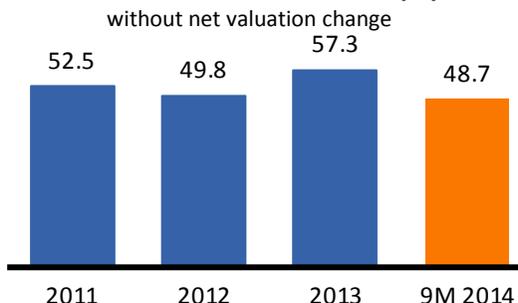
* Problem loans (past due but not impaired loans over 90 days + individually impaired loans) as % of loans to customers

KEY FINANCIAL INDICATORS

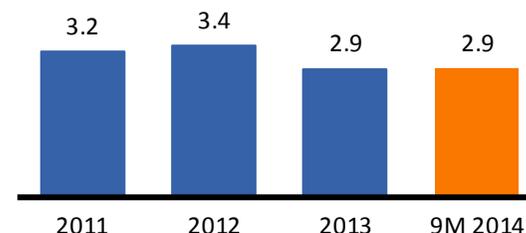
Return on equity YTD (%)



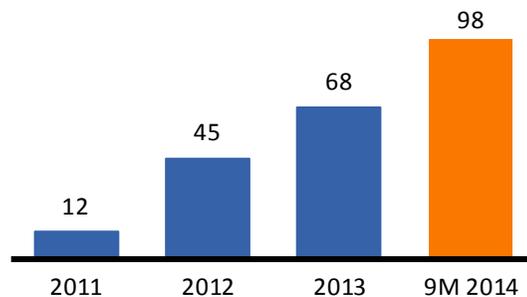
Cost-to-income ratio YTD (%)



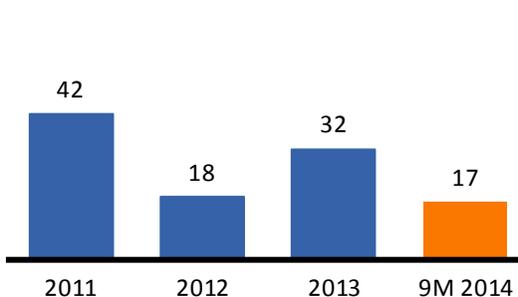
Net interest margin YTD (%)



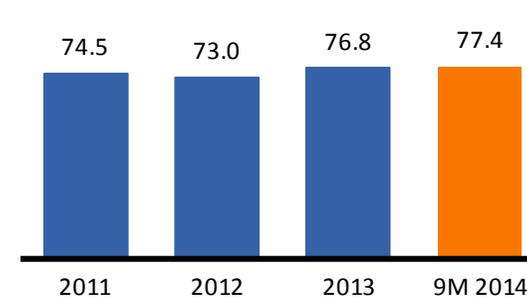
CPI Imbalance – ISK bn.



FX Imbalance – ISK bn.



Risk weighted assets/Total assets (%)





Arion banki

Arion banki

Arion banki

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ER BESTUR
ÞÁ SEM



YOU DON'T KNOW
ICELANDIC? DON'T
WORRY. THIS ONE
HERE SPEAKS WITH A
VERY NICE
ACCENT.



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