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Risk and Capital Management 2023

Landsbankinn hf. Pillar III risk report 31.12.2023

Landsbankinn hf. in brief

Landsbankinn hf. (hereinafter referred to as the 'Bank' or 'Landsbankinn') was founded on 7 October 2008. The Bank is a limited liability company incorporated and domiciled in Iceland. The Bank operates in accordance with Act No. 161/2002 on Financial Undertakings. The Bank is subject to supervision of the Financial Supervisory Authority of the Central Bank of Iceland (FSA) in accordance with Act No. 87/1998, on Official Supervision of Financial Activities.

The registered address of the Bank's office is Reykjastræti 6, Reykjavík. Landsbankinn operates an extensive branch network in Iceland, comprised of 34 branches and service points at year-end 2023. The Bank's primary lines of business are corporate and personal banking, markets, asset management and other related financial services. The Group operates solely in Iceland.

The National Treasury of Iceland holds 98.2% of shares in the Bank. The Bank itself owns 1.6% of shares and other shareholders own 0.2% of shares in the Bank.

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1 Introduction

Introduction

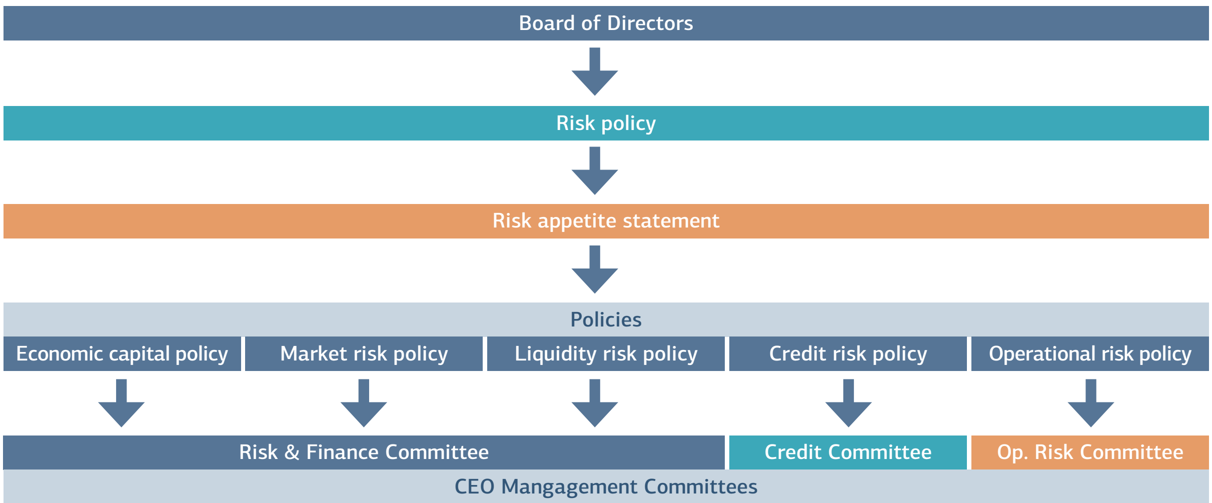
1.1 Declaration of the Board

Risk is inherent in the Bank's activities. It is managed through a process of on-going identification, measurement, management and monitoring, subject to internal limits and controls. Risk identification involves finding the origins and structures of possible risk factors in the Bank's operations and undertakings. Risk measurement entails measuring identified risk for management and monitoring purposes. Controls and limits promote compliance with rules and procedures, as well as adherence with the Bank's risk appetite.

The objective of the Bank's risk policies and procedures is to ensure that the risks in its operation are detected, measured, monitored and effectively managed, and that exposure to risk is managed to ensure that it remains within limits. Risk management policy is implemented through risk appetite, business strategy, and internal policies and limits that comply with the regulatory framework of the financial market.

The Board of Directors has reviewed the adequacy of the Bank's risk management arrangements, providing assurance that the risk management systems put in place are adequate with regard to the Bank's profile and strategy, in accordance with Article 435 of CRR.

Figure 1.1: Risk policy structure



1.2 Risk statement

The following statement has been approved by the Board of Directors and describes the Bank's overall risk profile. For key ratios and figures, refer to section 1.7 in this chapter, and for the interaction of the Bank's risk profile with risk tolerances set by the Board via the Bank's risk appetite, refer to section 2.4.

1.2.1 Executive summary

A strong capital position, robust credit portfolio and a healthy funding profile makes Landsbankinn well placed to tackle challenges through the economic cycle. The Bank's consolidated profit amounted to ISK 33 billion in 2023 and the return on equity was 11.6%, an increase of 5.3 percentage points from the previous year.

The credit quality in the Bank's credit portfolio remains high, the Bank's liquidity position is strong and the Bank's market risk is comfortably within its risk appetite. The Bank's credit rating is at BBB/A-2 and with a positive outlook as of November 2023.

In general, the Bank's risk measurements and assessment of material risk factors are positive with a stable outlook for most risk factors. Loans past due in the Bank's portfolio remain very low, its capital ratio is strong and all key risk factors are generally within risk appetite at year-end 2023, having developed positively.

1.2.2 Capital position

The Bank's capital position remains strong at year-end 2023. The total capital ratio decreased by 1.1 percentage points in 2023 and was 23.6% at year end. The Bank's minimum capital requirement, as determined by the FSA, is the sum of Pillar I and Pillar II-R requirements. The Pillar I requirement is 8% and the Pillar II-R requirement of 2.8% is based on the FSA's 2023 Supervisory Review and Evaluation Process (SREP). The effective capital buffer requirement was 9.4% at year-end 2023. In March 2024, the Central Bank of Iceland (CBI) will raise the countercyclical buffer in Iceland from 2.0% to 2.5%. Taking effective capital buffers into account, the total capital requirement for the Bank was 20.2%. As the Bank's management has set a capital target of $\geq$22%, there is an implied management buffer of 1.8% and, as a result, excess capital of 1.6%, or ISK 20 billion.

The Bank's risk-weighted exposure amount (RWEA) was ISK 1,279 billion at year-end 2023 and increased by ISK 91 billion, or 7.7%, for the year. The increase was primarily due to lending growth. Credit risk remains the single largest risk factor, amounting to 89% of total RWEA.

1.2.3 Credit risk

Credit risk increased in 2023 in line with increased lending to customers while key credit risk metrics were all within the Bank's risk appetite at year end. RWEA for credit risk increased by ISK 73 billion or 6.9%.

Lending to customers increased by ISK 87 billion or 5.6% in 2023. Carrying amount of loans to corporations increased by ISK 57 billion, driven by increased lending to real estate and construction companies. Lending to individuals increased by ISK 29 billion or 3.7% mainly due to an increase in mortgages. Rising interest rates have decreased demand for new mortgages while mortgages past due have only increased slightly in 2023. Individuals with mortgages with variable interest rates have largely been able to meet rising interest payments or have been able to refinance their mortgages to lower their monthly payments. Non-indexed mortgages amounting to ISK 213 billion, or 26% of the mortgage portfolio, have fixed interest rates that are due to change in 2024 or 2025. Of the ISK 19 billion of mortgages that had fixed interest rates change in 2023, only 1.1% were past due at year end. This gives some indication that customers have capabilities to meet rising interest payments or have opportunities to refinance their mortgages to adjust monthly payments. The robustness of the mortgage portfolio is largely due to a conservative indebtedness of customers as indicated by the weighted average loan-to-value ratio of 51% for the portfolio.

Expected loss in the credit portfolio remained unchanged at 0.3% at year-end 2023. Weighted average PD decreased slightly in 2023 from 1.8% to 1.5% at year end. The Bank's internal rating models and PD estimates for corporations and individuals were updated in 2023 using updated historical data based on the current default definition in line with the EBA guidelines implemented in 2021. Default rates remained low in 2023, or 0.8% weighted by exposures. At year-end 2023, the ratio of gross carrying amount of loans in default, or stage 3, was 1.4% or 0.1 percentage points higher than at year-end 2022. The ratio of loans more than 90 days past due remained stable at 0.3% at year-end 2023.

In 2023, net impairment charges on loans and advances were just under ISK 3.0 billion, as opposed to a release of ISK 2.4 billion in 2022. The main drivers of impairment in 2023 were defaults and post-model adjustments in response to the natural disaster on the Reykjanes peninsula.

Concentration risk decreased slightly in 2023 as reflected by the decrease in large exposures. At year-end 2023, the ratio of large exposures to Tier 1 capital was 9.4% compared to 32.3% at year-end 2022. Other measures of concentration risk remained relatively stable in 2023 and are in line with the Bank's risk appetite.

1.2.4 Market risk

The Bank's total market risk has fluctuated somewhat in 2023, and was 1.6% at year-end 2023 compared to 1.7% year-end 2022, measured as the ratio of risk-weighted assets to total RWEA. The most significant change in market risk was due to a lower net FX balance at year-end 2023 compared to year-end 2022. Exposure in the equity trading book rose steadily from the second quarter and was higher at year-end 2023 than year-end 2022. Interest rate risk in trading book fluctuated over the year but was unchanged between year-end 2022 and 2023. Despite unstable market conditions this year the Bank has effectively managed its market risk, which has remained comfortably within the defined risk appetite.

The Bank's total CPI indexation balance increased rapidly in 2023 and amounted to ISK 75 billion at year end, or 25% of total equity, as compared to ISK 8 billion at year-end 2022. The increase is most notable in the fourth quarter and is mainly due to CPI-linked mortgages, which increased by ISK 64 billion in 2023.

1.2.5 Liquidity risk and funding

Liquidity risk is one of the Bank's key risk factors and the Bank's policy is to sustain strong liquidity position in the near- and long term. The Bank's total liquidity coverage ratio (LCR) at year-end 2023 was 181%, LCR ISK was 129% and 1,499% in EUR, well above regulatory requirements and the Bank's internal limits. The Bank's total net stable funding ratio was 123% (145% in foreign currencies), above regulatory limits and the Bank's risk appetite.

The Bank's funding rests on three main pillars: equity, deposits from customers and funding through borrowing. The largest part of the Bank's funding are deposits from customers, amounting to ISK 1,049 billion at year end, increasing by 81 billion in 2023.

In January 2023, the Bank signed an agreement with Nordic Investment Bank (NIB), providing for a USD 40 million loan relating to the Bank's new headquarters. In August 2023, the Bank issued 2-year bonds under the Bank's EMTN programme, amount of NOK 1,000 million and SEK 450 million. In addition, the Bank issued green 3.5-year bonds for EUR 300 million in September and finalised a 7-year loan agreement with NIB, amounting to USD 75 million, in December. At year-end 2023, unsecured bond issuance in foreign currency amounted to ISK 241 billion, increasing by ISK 13 billion during the year.

In March, the Bank issued European Covered Bonds (Premium) in euros, the first from an Icelandic bank, in the amount of 300 million for 5 years. The bond issuance further increased the Bank's funding sources. Regular auctions of covered bonds were held in 2023 where previously issued series were tapped in addition to issuance of a new non-indexed series, LBANK CB 29. At year-end 2023, outstanding covered bonds amounted to ISK 268 billion, increasing by ISK 45 billion in the year.

In March, the Bank issued subordinated bonds in the amount of ISK 12 billion for 10 years, callable in 5 years. The issuance counts as Tier 2 capital. Subordinated bond issuance under the Bank's debt issuance programme amounted to ISK 20 billion at year-end, decreasing by ISK 2 billion from the previous year.

The Bank's credit rating is at BBB/A-2 and with a positive outlook as of November 2023.

1.2.6 Operational risk

In 2023, the number of operational incidents was stable. There were no major operational incidents, but one major credit loss incident related to external fraud. The operational risk profile remains stable. The number of attempts of fraud and cybercrime targeting the Bank's customers continues to grow. International cooperation, such as Nordic Financial CERT, continues to be an integral part of fighting cybercrime along with the support of the Icelandic CERT-IS. Part of the Bank's response to cybercrime has been the implementation of strong customer authentication in line with legal requirements and customer protection, as well as continued training and education. One of the main pillars of the Bank's control of operational risk and security of information assets is continued ISO 27001 certification. In 2023, the Bank was recertified in accordance with the standard for the 16th year.

1.2.7 Economic outlook

A steady cooling of the economy took place last year. Preliminary figures from Statistics Iceland show that GDP grew by 1.1% in the third quarter of 2023 as compared to the same quarter in 2022. Private consumption fell by 1.7% and investment fell by 4.7%. As domestic demand has slowed down and tourism has reached pre-pandemic heights, third quarter economic growth was driven by a decrease in imports. Landsbankinn Economic Research expects final figures for economic growth in 2023 to be around 3.1% and forecasts a slower growth of 2.1% in 2024.

Inflation has been above the Central Bank's inflation target since May 2020. Inflation peaked at 10.2% in February 2023, but had decreased to 7.7% in December 2023. While Landsbankinn Economic Research expects the inflation rate to continue to decrease as 2024 progresses, it will stay above target next years.

The Monetary Policy Committee of the Central Bank began a rate hike cycle in May 2021 and has since raised its key interest rate from 0.75 to 9.25%. Landsbankinn Economic Research expects that the Central Bank will begin rate cuts around mid-2024. In addition to uncertainty stemming from ongoing collective bargaining negotiations, volcanic and seismic activity on the Reykjanes peninsula has fuelled uncertainty in relation to inflation and public finance.

Unemployment measured 3.6% in December and has increased steadily since falling below 3% last summer. Landsbankinn Economic Research expects the unemployment rate this year to slightly outpace 2023 as high interest rates continue to cool the labour market. Wages rose by 9.8% in 2023, with purchasing power increasing by 1%.

1.3 Regulatory background

The Basel III Accord, implemented in the European Union through the Capital Requirements Directive (CRD 2013/36/EU (the 'Directive')) establishes a revised regulatory capital framework across Europe, governing the amount and nature of capital that must be maintained by credit institutions. Parts of the Directive have been implemented into Icelandic law by amendments to the Act on Financial Undertakings (Act. No. 57/2015 and Act No. 69/2016, amending Act No. 161/2002 on Financial Undertakings). The amendments to Icelandic law incorporate, among other things, the CRD IV capital buffer requirements, disclosure requirements, minimum leverage ratio, supervisory review and evaluation process and capital definitions.

The Basel framework consists of three 'Pillars':

- Pillar I defines the minimum capital amount that meets the firm's credit, market and operational risk;
- Pillar II requires the firm to assess whether its Pillar I capital is adequate to meet its risks (Internal Capital / Liquidity Adequacy Assessment Process, ICAAP/ILAAP) and is subject to annual review by the FSA in the Supervisory Review and Evaluation Process (SREP);
- Pillar III requires disclosure of specified information about the underlying risk management controls and capital position.

This publication, Risk and Capital Management 2023, reviews the Bank's organisation and processes relating the identification and management of the risk type characteristic of a financial group with its type of business concept. It also describes the Bank's risk position based on the requirements under Pillar III.

1.4 Disclaimer

This report is presented solely to explain the basis for preparation and disclosure of certain capital requirements and provide information about the management of certain risks. The report does not constitute any form of audited financial statement. The information it contains should not form the basis for any judgements about the Bank. The disclosures herein will only be subject to external verification to the extent that they are equivalent to those made under accounting requirements.

In the interest of simplifying text, Landsbankinn Group, which consists of the parent entity, Landsbankinn and its subsidiaries, is referred to as the 'Bank' in the disclosures. Where necessary, a distinction is made in the report between the group and the parent. For further information, see Note No. 83.1 – Basis of consolidation in the Bank's Consolidated Financial Statements for 2023 and Template EU LI3 in the Pillar III additional disclosures.

This publication, Risk and Capital Management 2023, has not been audited by external auditors. It does include information from the audited Consolidated Financial Statements 2023 and has been verified internally and approved by the Board of Directors. This publication has also been presented to and reviewed by the Board's Risk Committee. There may be some discrepancies between this report and financial information in the Consolidated Financial Statements 2023, as the report has been prepared for the purpose of Article 18 of Act No. 161/2002, on Financial Undertakings, cf. Article 11 of Act No. 96/2016, and the provisions of Directive 36/2013/EU (CRD IV) and Regulation (EU) No. 575/2013 (CRR) as amended by Regulation (EU) 2019/876 (CRR II), incorporating the Basel Pillar III disclosure requirements, rather than in accordance with IFRS.

All amounts are in ISK million unless otherwise stated.

1.5 Disclosure policy

In accordance with the Directive, the Bank has adopted a formal disclosure policy in that it will comply with the requirement to publicly disclose relevant information.

The rules state that one or more of the required disclosures may be omitted if it is believed that the information is immaterial. Materiality is based on the criteria that the omission or misstatement of material information would be likely to change or influence the assessment or decision of a user relying on that information for the purposes of making economic decisions. If a disclosure is considered immaterial, it will be stated in the relevant section.

One or more of the required disclosures may be omitted if the information is regarded as proprietary or confidential. Proprietary information is that which, if it were shared, would undermine a competitive position. Information is considered confidential if there are obligations binding the Bank to confidentiality with customers and counterparties. If information is omitted for either of these reasons, it will be stated in the relevant section along with the rationale. Further general information on required disclosures will be published where appropriate.

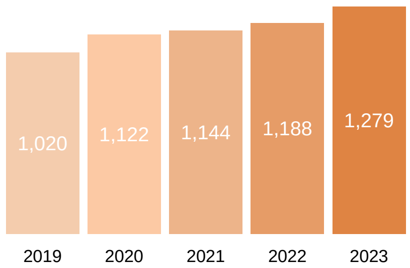
The disclosures are published annually on the Bank's website.

1.6 Additional disclosures

Additional Pillar III disclosures required under CRR are included as an appendix to this report in the form of a spreadsheet. Table 10.1 in the appendix to this report lists the relevant templates included in the additional disclosures. The additional disclosures can be downloaded here: https://corporate.landsbankinn.com/en/the-bank/investor-relations/reports-and-financials.

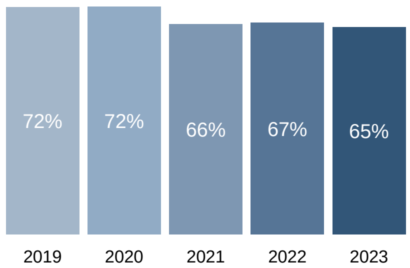
1.7 Risk metrics overview

Risk-weighted exposure amount (RWEA)



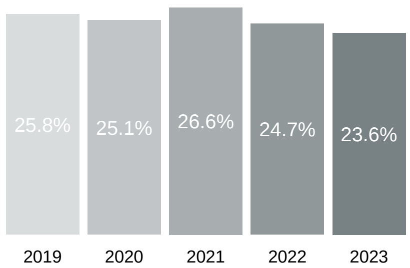
1,279 ISK bn

RWEA to total assets



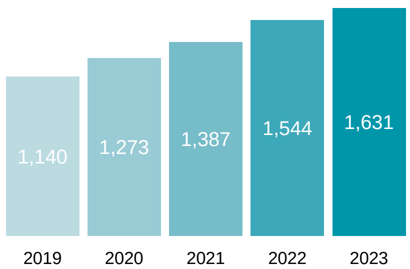
65%

Total capital ratio



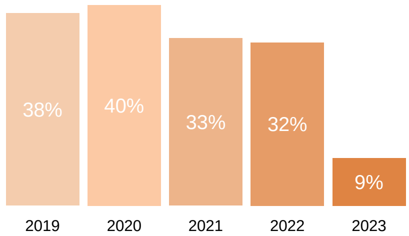
23.6%

Loans and advances to customers



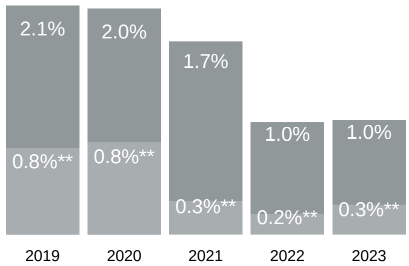
1,631 ISK bn

Large exposures to tier 1 capital*



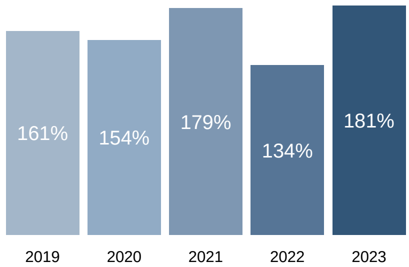
9%

Stage 3 loans



1.0%

Liquidity coverage ratio total



181%

* Up to and including 2020, large exposures were measured as a % of eligible capital.
** Of which 90 days past due.

2 Risk management

Risk management

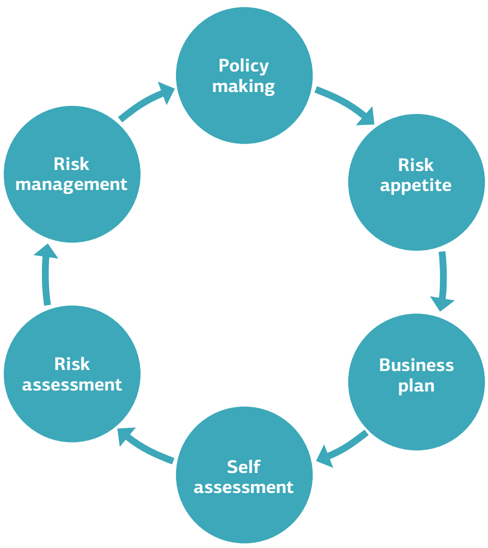
Risk management involves the identification, assessment and control of risk in the Bank's operation. The Bank adopts detailed risk rules and develops an effective internal governance structure to ensure a clear division of responsibility, management of risks and compliance to internal and external rules and regulations.

All pertinent risks in the operation are considered, both financial and non-financial. The Bank's management structure defines authorisations regarding decision making, risk taking, follow-up and monitoring.

The Board of Directors approves the Bank's risk appetite, which defines target levels for risk in the Bank's operation and is utilised for the management of risk taking within the Bank. Risk appetite shall be reviewed at least annually, or as needed, so that it reflects the Bank's targets regarding risk taking at any given time.

Risk management entails a process in which the Bank's risk appetite and business plan are intertwined. That process includes self assessment and risk assessment which are followed by further analysis and management of risk. The Bank's strategic planning takes risk appetite and risk management into account, making risk policy an integral part of its operation. Risk management is an ongoing process, the implementation of which is an integral part of a sound risk culture.

Figure 2.1: Risk management process



2.1 Risk policy

The Bank's risk policy is as follows:

The Bank's operations, risk diversification and decisions shall be in accordance with its risk appetite, sound business practices, financing, liquidity and equity position. The Bank seeks to ensure diversified and sound financing, high asset quality, and a sustainable risk profile. The Bank has set internal limits with the aim of maintaining a strong capital and liquidity position which, along with active risk management, are important to achieve long-term profitability and strong standing. In this manner, the Bank aims to minimise fluctuation in its operations and promote resilience.

Risk appetite defines the type and extent of risk that management is willing to take to meet the Bank's business objectives. In pursuit of its goals, the Bank only takes on risks that it understands and can measure, evaluate and manage.

The Bank seeks to maintain solid business relationships, having regard for its own position as well as that of its customers at all times, and with due regard to any internal connections between customers. The Bank pursues long-term business relationships and aims to minimise and contain reputational risk.

The Bank is obligated to comply with relevant laws and regulations in all its operations. The main focus areas within the Bank's risk culture are adherence to rules, integrity, ethical behaviour, professionalism and the promotion of risk awareness throughout the organisation.

2.2 Risk identification

The Bank defines material risk as any risk large enough to substantially impact the success of the enterprise, risk described in its risk appetite and/or amounting to more than 2.5% of its capital base.

The Bank is exposed to the following material risks:

- Credit risk
- Market risk
- Liquidity risk
- Operational risk

Table 2.1 provides a link between the Bank's business units and the material risks that they are exposed to. The risk significance is assessed within the context of the Bank as a whole and is measured based on allocation of capital within the Bank.

For each of these risk factors, several material risk subfactors are defined. There are also several risk factors, such as concentration risk, sustainability risk and conduct risk, that can act as amplifiers on one or more of the Bank's material risk factors. These are covered in detail in the subsequent chapters.

Table 2.1: Relative allocation of capital due to material risks to the Bank's business units

Material risk	**Personal Banking**	**Corporate Banking**	**Asset Management & Capital Markets**	**Treasury & Market Making**
Credit risk	High	High	Low	Low
Market risk	Low	Low	Medium	High
Liquidity risk	n/a	n/a	n/a	High
Operational risk	Medium	Medium	High	Medium

2.3 Risk management structure

The Bank aims to operate in line with international best practice and guidelines on risk management. The Bank devotes substantial resources to developing and maintaining its risk management systems and operations.

The Bank's risk management is based on policies and governance determined by the Board of Directors. These policies are implemented by the Bank's CEO through key risk management bodies and committees.

2.3.1 Risk committees

The Bank's risk management governance structure at year-end 2023 is shown in Tables 2.2 and 2.3.

Table 2.2: Sub-committees of the Board of Directors

Supervision by the Board of Directors and its sub-committees
Audit Committee
Remuneration Committee
Risk Committee
Sustainability Committee

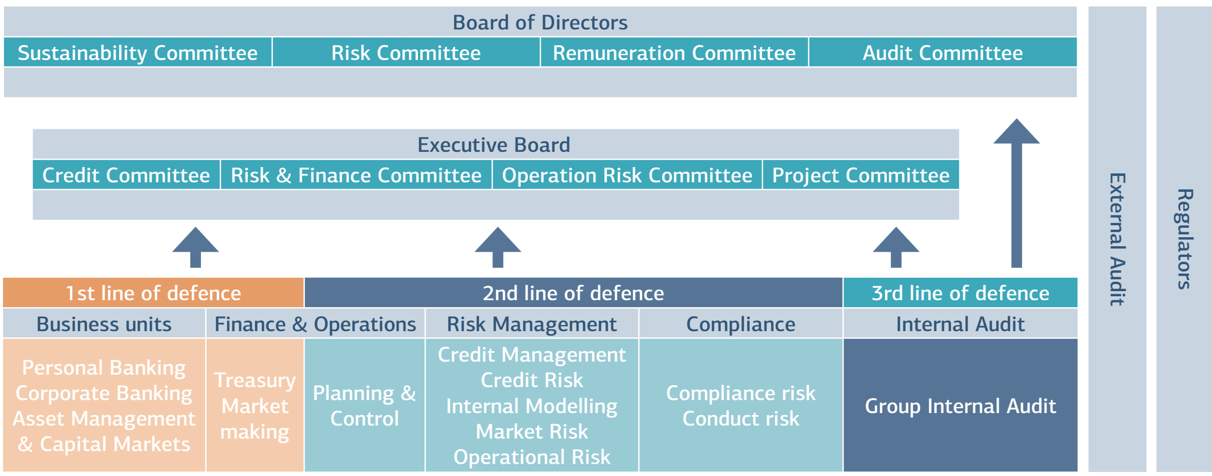
Table 2.3: Key risk management bodies and committees

Committee	Chair	Other members
Executive Board	CEO	Managing Directors
Risk & Finance Committee	CEO	CFO, CRO, Head of Legal Services
Credit Committee	CEO	CRO, MD of Corporate Banking
Operational Risk Committee	CRO	MD of Personal Banking, MD of IT, Chief Compliance Officer, Head of Operations, Head of Operational Risk
Project Committee	CEO	Managing Directors

The Board of Directors has overall responsibility for the establishment and oversight of the risk management framework, risk appetite, and setting risk limits. The CEO is responsible for the effective implementation of the framework and risk appetite through the corporate governance structure and committees.

Sub-committees of the Board of Directors provide important preparation for Board meetings. The purpose of sub-committees is to facilitate discussion and in-depth analysis of issues addressed by the Board and increase its efficacy. There are currently four sub-committees: Risk Committee, Audit Committee, Sustainability Committee and Remuneration Committee. The Risk Committee serves as advisor to the Board of Directors on the development of the Group's risk strategy and risk appetite. The Audit Committee's role is to ensure the quality of the Group's financial statements and other financial information, as well as the independence of its auditors. The Sustainability Committee's role is to review the Bank's policy making regarding sustainability, review the status and development of sustainability metrics and

Figure 2.2: Risk management governance structure



to review the publication of information regarding sustainability from the Bank. The Remuneration Committee's role is to provide guidance to the Board of Directors and CEO on salary and benefits for key executives and to advise the Board on the remuneration policy.

The Executive Board serves as a forum for discussion about business opportunities and challenges, approves funding for larger projects, and serves as a decision-making platform on matters that do not fall within the remit of other committees. The main role of the Executive Board is to ensure compliance of the Group's operation with laws, regulations, business plans and policies of the Bank at any given time. There are four sub-committees at the Executive Board level; Credit Committee, Risk & Finance Committee, Operational Risk Committee and Project Committee. The Credit Committee's main role is to ensure that the Group's loan portfolio and credit risk remain in compliance with its credit risk policy and risk appetite. The Credit Committee is responsible for significant credit decisions, credit limits for customers, credit quality and large exposures. The Risk & Finance Committee primarily provides governance oversight of market and liquidity risk as well as formulating risk limits for these factors for the Board of Directors. The committee also has oversight of counterparty risk, reviews various rules and policies regarding risk, reviews ICAAP methodology and scenarios, and reviews the Group's market risk, liquidity risk and economic capital policies. The Operational Risk Committee is a forum for discussion and decisions on operational risk issues and review of the effective implementation of the operational risk policy of the Bank. The Project Committee selects, prioritises, oversees and supports the Group's major projects and digital transformation projects as well as promoting their success.

Governance pertaining to specific risks is discussed in the relevant sections.

2.3.2 Managing directors

Managing directors are responsible for the implementation of risk appetite and risk culture in their units based on the Bank's risk policy and business plan. Managers are responsible for risk-taking and risk management and for ensuring that risk within their units is assessed and measured, and information escalated to the relevant parties. Managers shall contribute to the development and maintenance of a healthy risk culture in their units, present the risk policy and ensure that employees are familiar with the rules that apply to their duties.

2.3.3 Risk Management

Risk Management is responsible for measuring, monitoring and reporting on all risk within the Bank. Subsidiaries of the Bank have their own risk management functions and Risk Management receives information on exposures from the subsidiaries and collates them into Group exposure. Risk Management is also responsible for comprehensive risk reporting on risk positions to various internal departments and committees and supervisory authorities.

The Risk Management division comprised six departments at year-end 2023:

- Credit Management reviews and approves or vetos credit decisions made by the Bank's business units when credit applications exceed the business unit's limits. Confirmation by Credit Management implies that Credit Management has reviewed the credit application and does not exercise its veto rights. Credit applications exceeding the confirmation limits of Risk Management are referred to the Bank's Credit Committee. The department also oversees regular updates of the Bank's credit policies and other rules related to the credit process.

- Credit Risk is responsible for measuring and monitoring credit risk as well as for providing the Bank with systems and processes to measure, monitor and control credit risk in credit and policy decisions. Credit Risk is responsible for assessment, analysis and reporting on credit risk, economic capital and impairment. Credit Risk is also responsible for rules and procedures regarding credit risk, such as procedures for impairment measurement, credit mitigation and forbearance.

- Market Risk is responsible for measuring, monitoring and reporting on market risk, liquidity risk and interest rate risk in the banking book along with limit monitoring and reporting. The department develops and maintains the Bank's market risk models and maintains the Bank's Market Risk Policy and Liquidity Risk Policy, as well as implementing processes to measure and monitor market risk and liquidity risk within the Bank. Market Risk is also responsible for monitoring all derivatives trading the Bank enters into, both for hedging and trading purposes, securities financing transactions as well as FX balance monitoring for the Bank.

- Operational Risk is responsible for ensuring centralised management of operational risk other than compliance and conduct risk. The department assists in mapping the Bank's operational risk in a comprehensive risk assessment and in executive assessment and analysis of operational and loss events. Operational Risk is involved in the design and testing of the Group's continuity plans. The department is responsible for ensuring compliance with the ISO 27001 standard for information security.

- Internal Risk Models provides the Bank with IRB and EC models and related processes to estimate credit risk and link the risk to equity and provides support during the implementation of those models and processes within the Bank. The department develops models for pre-approved limits in order to facilitate the automation of lending processes.

- Risk Solutions develops and operates external solutions used by Risk Management and maintains the IT reporting and development environment for Risk Management. The department is also responsible for monitoring and maintaining periodic executions of code by the division and reporting to supervisory parties. The department is responsible for effective risk data aggregation and risk reporting, in accordance with BCBS 239.

2.3.4 Compliance

Compliance is an independent control function which reports directly to the CEO and operates in accordance with a letter of appointment from the Board of Directors.

Compliance is part of the Bank's second level control and is responsible for monitoring compliance and coordinating measures against money laundering and terrorist financing and personal data processing.

Compliance informs management on the impact of regulatory changes on the Bank's operations, and advises on actions necessary to ensure that the Bank operates in accordance with regulatory requirements and proper and sound business practices.

2.3.5 Internal Audit

Internal Audit is an independent, objective assurance and consulting activity that is a part of the Bank's organisational chart and an element of its internal control system. The Board of Directors has oversight of Internal Audit and appoints the Chief Audit Executive. The role of Internal Audit is to improve and protect the Bank's value with risk-based and objective verification, consultation and insight. Internal Audit evaluates and improves the risk management framework, control and governance processes through systematic and disciplined practices, thus supporting the Bank in accomplishing its objectives. The Chief Audit Executive is responsible for ensuring that Internal Audit works in accordance with laws, recommendations from the FSA no. 3/2008, and standards and guidelines cited therein, including the benchmarks of the Institute of Internal Auditors (IIA).

2.3.6 General staff

All employees are responsible for carrying out their duties in accordance with external laws and rules, risk appetite, risk policy, rules and the Bank's procedures and ensure compliance with them at all times. Employees shall report any suspected breaches to their superior. Employees need to be familiar with the purpose and nature of the control measures they carry out. They must be mindful of the proper functionality of control measures and inform management should they consider control measures insufficient or control inadequate to support the Bank's objectives.

2.4 Risk measurement

The Bank regularly monitors and assesses its current risk profile. The risk appetite framework considers key risks relevant to the Bank's business activities by setting limits and target levels for risk. In addition, the Bank measures and monitors other risk indicators to support the management of key risk factors.

The Bank's risk appetite for 2023 has been reviewed, revised and implemented. Table 2.4 lists the risk appetite metrics, year-end values for the past three years and the status of the metrics in relation to tolerance levels set by the Board. A green status indicates that the value is in line with tolerance levels, yellow status indicates that the value is outside tolerance levels but within external limits and red status indicates that the value is outside of external limits. Monitoring and reporting on the Bank's risk appetite has been aligned with monitoring and reporting of recovery plan indicators according to the Bank Recovery and Resolution Directive (BRRD).

2.4.1 Stress testing and sensitivity analysis

Stress testing and sensitivity analysis are important tools used to quantify risk in severe, unlikely but plausible scenarios. This section provides an overview of stress testing and sensitivity analysis for different risk types within the Bank.

2.4.1.1 Capital and liquidity

Stress testing is an important part of the Bank's capital and liquidity planning process. Internal stress tests are used as an important risk management tool to determine how severe, unlikely but plausible changes in the business and macro environment affect the Bank's capital need and liquidity position. Stress tests reveal how the capital need and liquidity ratios vary during a stressed scenario, where impact on financial statements, regulatory capital requirements and capital ratios are tested. The stress testing process is divided into the following steps:

- Scenario development and approval
- Scenario translation
    - Translation model to determine loan loss
    - Translation method to determine the effect on financial statements
    - Translation model to determine internal capital requirements
- Calculation

Table 2.4: Overview of risk appetite metrics

Risk category	Risk type	Metric	31.12.2023	31.12.2022	31.12.2021
Credit risk	Credit quality	Expected loss (% of total loans)	0.3%	0.3%	0.4%
		Probability of default	1.6%	1.8%	2.2%
	Single name concentration	Large exposures (% of Tier 1 capital)*	9.4%	32.3%	33.1%
Market risk	Market risk	Total market risk (% of RWEA)	1.6%	1.7%	0.9%
Liquidity risk	Liquidity risk	Liquidity coverage ratio - Total	180.9%	133.6%	178.8%
		Liquidity coverage ratio - FX	447.1%	351.0%	555.8%
		Liquidity coverage ratio - EUR	1,499.6%	-	-
		Liquidity coverage ratio - ISK	128.6%	99.2%	120.1%
Funding risk	Funding	Net stable funding ratio - Total	123.0%	116.6%	121.0%
Capital risk	Capital adequacy ratio	Capital adequacy ratio	23.6%	24.7%	26.6%
Profitability	Profitability	Return on equity after taxes	11.6%	6.3%	10.8%
Operational risk	Change in RWEA	12-month change in RWEA	-0.3%	-5.5%	-2.8%

*In addition to monitoring large exposures as a % of Tier 1 capital, the Bank also monitors the largest single exposure as a % of Tier 1 capital. The goal is <18% and as at 31.12.2023, the largest exposure is well below that goal. External regulation mandates a ratio of <25%.

- Analysis and reporting
- Management actions

The Bank aims to develop dynamic, forward-focused scenarios that simultaneously cover key aspects of the Bank's operations, including system-wide interaction and feedback effects.

These scenarios, which include a baseline scenario, assume developments of key macro indicators over a three-year period. The scenarios demonstrate an alternative development of key economic variables induced by various shocks compared to the baseline macroeconomic forecast of the Bank's Economic Research department. Idiosyncratic events are also defined within the scenarios to stress specific asset classes or operations of the Bank.

The Bank uses a loan loss model which incorporates macroeconomic variables and produces probability of default (PD), default rates, as well as loss given default (LGD), which can be translated into loan losses for a given scenario. In addition to the loan loss model results, expert judgement is applied for loan loss on selected large exposures by industries affected within each scenario.

Scenario results are compared with the Bank's current business plan, risk appetite, and the Bank's solvency.

The effect on financial statements is translated and calculated with a resulting impact on the capital base and liquidity position. Capital assessment for the Bank is calculated for each scenario, as well as various risk metrics within the Bank's risk appetite. If the risk appetite constraints are violated, management actions are required within the scenario.

2.4.1.2 Credit risk

Stress testing is an important part of the Bank's capital planning process. Stress testing for credit risk is mainly applied as part of capital planning and focuses on measuring potential credit losses and effects on capital.

2.4.1.3 Market risk

The Bank conducts stress tests and sensitivity analysis pertaining to market risk on a regular and ad-hoc basis. Comprehensive market risk stress testing is conducted as part of the Bank's ICAAP/ILAAP once a year with a time horizon of three years. Other stress tests and sensitivity analyses of the Bank's trading and non-trading portfolios with regard to equity and interest rate risk and currency risk are made on a case-by-case basis.

2.4.1.4 Liquidity risk

Various stress tests have been constructed to try to efficiently model how different scenarios affect the Bank's liquidity position and liquidity risk. The stress tests are based on the Bank's balance sheet mixture and take the Bank's current operating environment into account. Key liquidity metrics are also mapped onto annual internal stress tests that are used as an important risk management tool in order to determine how severe, unlikely but plausible changes in the business and macro environment affect the capital need and liquidity position of the Bank. The Bank also performs other internal stress tests that may vary from time to time.

2.5 Risk monitoring

The Bank allocates considerable resources to ensure on-going adherence with approved risk limits and for risk monitoring. The risk monitoring process combines active monitoring of risks, exposures and adherence to the Bank's risk framework and extensive risk reporting. The Bank has set guidelines for reporting to relevant management bodies, including the Board of Directors, Executive Board and all relevant committees on developments in risk measures and risk appetite.

The Bank has implemented a policy on risk data in compliance with BCBS 239 (Basel Committee on Banking Supervision's guideline 239). The policy defines which reports should be submitted where, the frequency of those submissions, and who is responsible for them.

Figure 2.3: Overview of risk reporting within the Bank

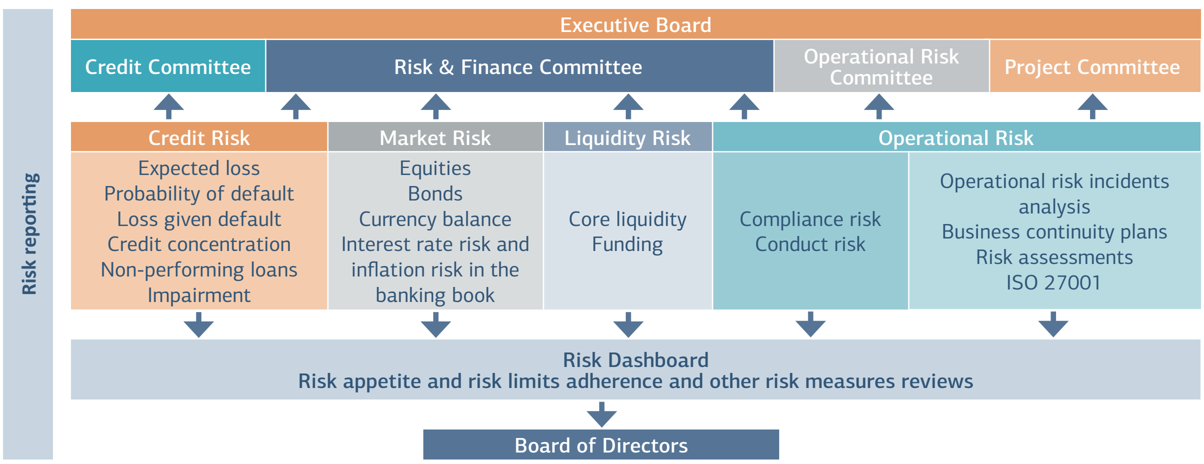


Table 2.5: Principal reporting to the Board of Directors

Annual	
Risk and capital management report	Pillar III disclosures.
ICAAP/ILAAP report	Evaluation of the risk profile and solvency need. The report contains conclusions drawn from stress testing, including the effect of various scenarios on expected losses and capital needs. The ICAAP/ILAAP report is subject to the FSA's Supervisory Review and Evaluation Process (SREP).
Recovery plan	The recovery plan focuses on measures to protect and restore the Bank's financial position, following a significant deterioration. It includes governance and decision-making processes, continuity of critical economic functions and core business lines, specification of trigger points to activate recovery options and internal and external communications.
Compliance report	Annual assessment of the role, independence, authorisations and work of Compliance and whether Compliance has sufficient funding to perform its duties. The report contains an assessment of compliance risk and conduct risk as well as an AML report and a data protection report.
Semi-annual	
Credit risk report	Thorough risk report providing analysis of such issues as development in risk appetite, past due loans, average exposure-weighted probability of default (PD), default rate vs. PD, distribution of loan portfolio in rating categories and migration analysis and other analysis of credit risk aspects.
Market & liquidity risk report	Thorough risk report summarising the Bank’s liquidity risk and market risk exposures and any concerns regarding liquidity and/or market risk.
Operational risk report	Thorough risk report providing analysis of operational risk aspects.
Monthly	
Risk report	An aggregated report containing information on the Group’s risk appetite and material from the credit, market, liquidity and operational risk reports.
Executive management report	An aggregated report containing risk related material such as risk appetite, internal capital and RAROC.
Bi-weekly or more frequently	
Market & liquidity risk report*	Market and liquidity risk report highlighting the Bank’s market risk exposures, risk appetite, market risk limit utilisation and liquidity risk and any concerns regarding liquidity and/or market risk.

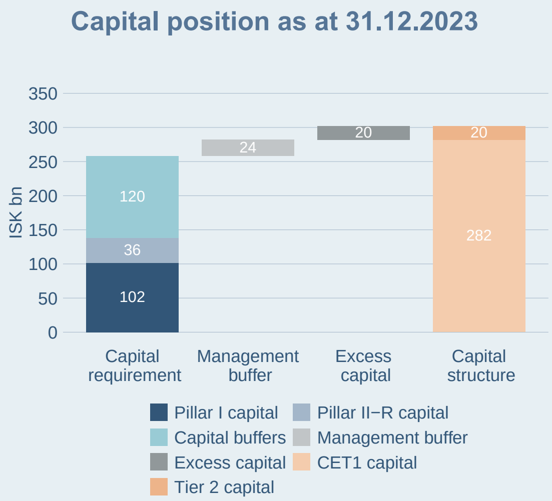
*Daily during adverse conditions

3 Capital management

Capital management

The purpose of the Bank's capital management is to support the Bank's strategy and ensure that it has sufficient capital to cover its risk at all times.

- The Bank's total capital ratio decreased by 1.1 percentage points in 2023, to 23.6%.
- A regular dividend payment of ISK 0.36 per share in the total amount of ISK 8.5 billion was made in 2023.
- The Bank's Pillar II-R capital requirement decreased in the latest SREP, but remains in excess of the Bank's internal assessment of capital.
- Compared to the total capital requirement of 20.2%, and an implied management buffer of 1.8%, the Bank's excess capital was 1.6 percentage points or ISK 20 billion.



3.1 Capital management framework

The purpose of the Bank's capital management framework is to support the Bank's strategy and ensure that it has sufficient capital to cover its risks. The capital management framework of the Bank is comprised of four interdependent activities: capital assessment, risk appetite/capital target, capital planning, and reporting/monitoring.

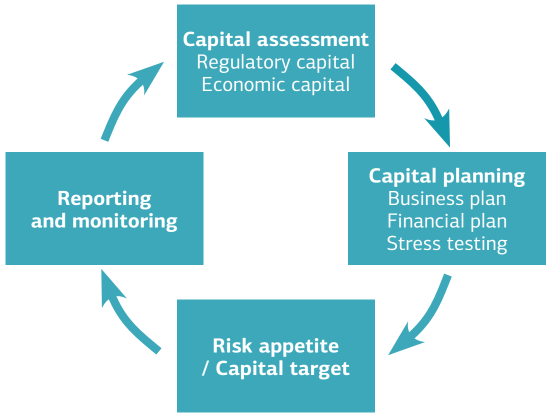
The Bank uses standardised approaches in measuring the regulatory capital requirement for Pillar I risks and economic capital (EC) for capital management purposes.

The Bank's capital management governance structure at year-end 2023 is as follows:

Board of Directors

The Board of Directors of Landsbankinn is responsible for reviewing and approving the Bank's business strategy and policy on aggregate exposure and determines the Bank's risk appetite. The Board of Directors approves the Bank's current funding programme and subordinated borrowings. The Board of Directors shall be actively involved in the design and implementation of stress tests and ensure that they are based on robust and efficient governance and methodology.

Figure 3.1: Capital management framework



CEO, Risk & Finance Committee

The CEO is responsible for implementation of the capital structure policy. The CEO has formed the Risk & Finance Committee to manage and oversee the implementation. The Committee is responsible for ensuring compliance with the policy in the development of the Bank's business and financial plans. The Risk & Finance Committee is responsible for the design and presentation of stress tests and scenarios.

Finance

The CFO is responsible for the day-to-day capital management and funding of the Bank and reports to the Risk & Finance Committee. The Finance division is tasked with monitoring the risk-weighted asset base, the capital base and capital position at any given time. Finance is responsible for the design and presentation of scenarios and implementation of stress testing of the Bank's capital structure. The division is also responsible for the Bank's recovery plan which is to ensure that banks are prepared to restore their viability in a timely manner even in periods of severe financial stress.

Treasury, a department within Finance, is responsible to the Risk & Finance Committee for the management of the Bank's funding, both in ISK and foreign currency.

Risk Management

The CRO is responsible for risk assessment and monitoring of risk factors and reports to the Risk & Finance Committee. Risk Management is also responsible for the EC framework and measurement, the Pillar III risk report and the ICAAP and ILAAP report.

Managing directors

The managing directors shall comply with the capital structure policy in their activities. This means, *inter alia*, that business decisions taken by these divisions shall comply with the business plan and budget, risk appetite and the Bank's current profitability target.

Internal Audit

Internal Audit shall regularly review and comment on the framework and work procedures related to the capital structure policy and, thereby, help ensure that the policy extends to and is proportional to the nature, scope and risk inherent in the Bank's operation.

3.2 Capital policy

The Bank has a policy on capital structure, the objective of which is to ensure appropriate management, efficiency and economic utilisation of the Bank's equity, while additionally ensuring that the Bank fulfils regulatory capital requirements. With active capital management, the Bank ensures that dividend payments are based on its dividend policy and do not exceed set limits, and that the Bank can at all times meet increased risk in its operating environment.

The total capital ratio target is reviewed annually. When setting the target, EC, Pillar I and II capital requirements, MREL requirements, regulatory capital buffers, the management capital buffer, risk appetite, and strategic objectives are considered. The Bank's aim is to maintain a capital ratio above the CBI's total capital requirement at any given time, plus a management buffer specified in the Bank's risk appetite. The Bank also aims to be in the highest category for risk-adjusted capital ratio, as determined and measured by the relevant credit rating agencies.

The Bank aims to pay regular dividends to shareholders, amounting to around 50% of the previous year's profit. In addition, and in line with the Bank's target capital and liquidity ratios, the aim is also to make special dividend payments to optimise the Bank's capital structure. The Bank paid a regular dividend of ISK 8.5 billion in 2023.

When determining the amount of dividend payments, the Board needs to maintain the Bank's strong financial position. The Board needs to consider internal and external risk, growth prospects and the maintenance of a long-term, robust equity and liquidity position, as well as compliance with regulatory requirements.

3.3 Capital position

The Bank's equity increased by ISK 24.7 billion in 2023 and amounted to ISK 303.8 billion as at 31 December 2023 (2022: ISK 279.1 billion). The capital adequacy ratio is calculated in accordance with Article 84 of Act No. 161/2002, on Financial Undertakings. The Bank's total capital ratio decreased by 1.1 percentage points in 2023, remaining strong at 23.6% as at 31 December 2023 (2022: 24.7%).

The capital base consists of 22.0% CET1 based on core equity only and 1.6% of Tier 2 capital, with two instruments in the form of subordinated liabilities: First, an ISK 5.5 billion fixed-rate inflation-linked instrument (carrying amount ISK 7.1 billion) with final maturity in December 2029 but callable in December 2024, and second, an ISK 12.0 billion fixed-rate inflation-linked instrument (carrying amount ISK 13.1 billion) with final maturity in March 2033 but callable in March 2028 and on each subsequent interest payment date.

On 4 May 2020, regulation No. 452/2020 transposed into Icelandic law Regulation (EU) 2017/2395 of the European Parliament and of the Council amending Regulation (EU) No. 575/2013, as regards, *inter alia*, transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds. The Financial Supervisory Authority (FSA) has granted permission for the Bank to apply IFRS 9 transitional arrangements in accordance with the aforementioned regulations. The effect of the arrangements on the Bank's CET1 capital was positive by ISK 0.6 billion in 2023 (2022: ISK 0.7 billion).

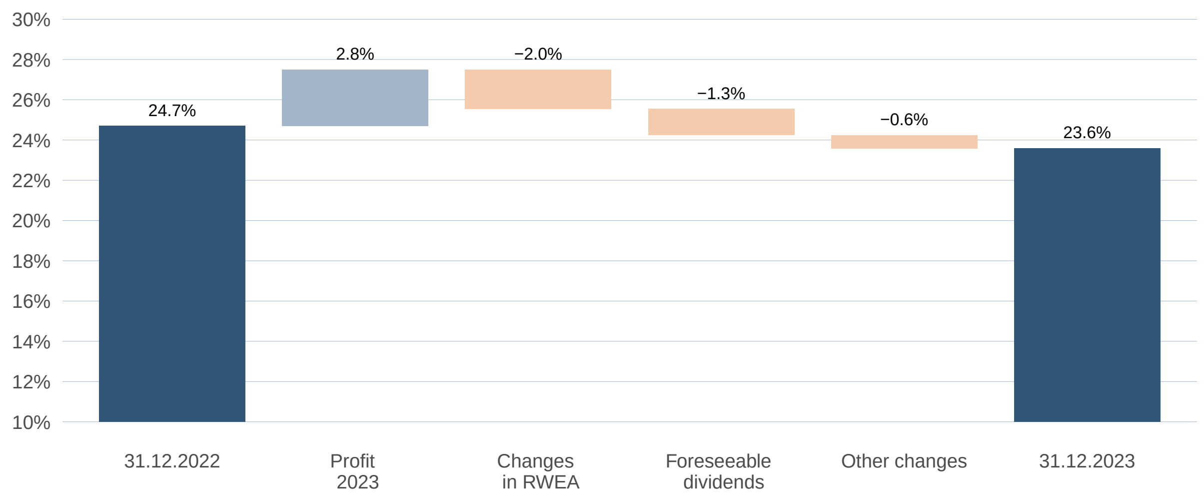
CRR dictates that institutions shall determine the applicable amount of insufficient coverage for non-performing exposures to be deducted from CET1 capital, as determined in Article 47c of CRR. The deduction is applicable for exposures originated after April 2019. The effect of this deduction on the Bank's CET1 capital at year-end 2023 was ISK 1.3 billion.

Table 3.1: Breakdown of the capital base (ISK m)

	31.12.2023	31.12.2022
Share capital	23,621	23,621
Share premium	120,593	120,593
Reserve	11,432	11,986
Retained earnings	148,108	122,891
Total equity attributable to owners of the Bank	**303,754**	**279,091**
Intangible assets	-7	-10
Foreseeable dividends*	-16,584	-8,498
Fair value hedges	-4,669	320
Adjustment under IFRS 9 transitional arrangements	595	727
Insufficient coverage for non-performing exposures	-1,291	0
CET1	**281,798**	**271,630**
Non-controlling interests	0	0
Tier 1 capital	**281,798**	**271,630**
Subordinated liabilities	20,176	21,753
Tier 2 capital	**20,176**	**21,753**
Capital base	**301,974**	**293,383**
Risk exposure amount (RWEA)		
Credit risk	1,144,477	1,071,091
Market risk	20,559	19,618
Operational risk	114,400	97,716
Total RWEA	**1,279,436**	**1,188,425**
CET1 ratio	**22.0%**	**22.9%**
Total capital ratio	**23.6%**	**24.7%**

*The Board of Directors intends to propose that the annual general meeting (AGM) approve a dividend of ISK 16.6 billion, or 0.70 per share, to be paid to shareholders in 2024. The Bank's capital and capital ratio has been reduced by an amount equivalent to the dividend payment as foreseeable dividends in the consolidated financial statements for the year 2023.

Figure 3.2: Changes in the Bank's total capital ratio in 2023



3.3.1 CET1 capital - statutory deductions and transitional arrangements

CET1 capital consists of core equity less statutory deductions according to requirements of the FSA based on Chapter 10 of Act No. 161/2002.[1] The Bank makes deductions in order to determine its CET1 capital where applicable.

- Carrying amounts of intangible assets
- Deferred tax assets
- Capital holdings in other credit and financial institutions amounting to more than 10% of their capital
- Foreseeable dividends in next year's operations

Further to CET1 statutory deductions, the Bank makes transitional arrangements by mitigating the impact of the introduction of IFRS 9 on own funds based on regulation 452/2020 and deducts from CET1 capital due to insufficient coverage for non-performing exposures in accordance with Article 47c in CRR.

Further quantitative information regarding the Bank's capital position can be found in templates CC1, CC2 and CCA in the additional disclosures accompanying this report.

3.4 Capital assessment

3.4.1 Pillar I capital requirement

The regulatory minimum capital requirement under Pillar I of the Directive is 8% of risk-weighted exposure amount for credit risk, market risk and operational risk. The Bank uses the standardised approach in measuring Pillar I capital requirements for credit risk and market risk. For counterparty credit risk, the Bank uses the original exposure method and for operational risk, it uses the basic indicator approach.

The Bank's risk-weighted exposure amount (RWEA) was ISK 1,279 billion at year-end 2023 and increased by ISK 91 billion, or 7.6%, for the year. The increase is largely due to credit growth. Accordingly, the Pillar I capital requirement for the Bank was ISK 102.4 billion at year-end 2023 (2022: ISK 95.1 billion). Credit risk is the single largest risk type or 89.5% of total RWEA. Further quantitative information regarding the Bank's RWEA can be found in templates OV1, CR4-5, CCR1-3, MR1 and OR1 in the additional disclosures accompanying this report.

Table 3.2: Pillar I capital requirement and RWEA (ISK m)

	31.12.2023		31.12.2022	
	Pillar I	**RWEA**	**Pillar I**	**RWEA**
Credit risk	91,558	1,144,477	85,687	1,071,091
Market risk	1,645	20,559	1,569	19,618
Operational risk	9,152	114,400	7,817	97,716
Total capital requirement and RWEA	**102,355**	**1,279,436**	**95,074**	**1,188,425**

3.4.2 Pillar II capital requirement

The Bank's Pillar II-R requirement is determined via the CBI's Supervisory Review and Evaluation Process (SREP). The Pillar II-R requirement decreased from 3.4% to 2.8% in the 2023 SREP. The CBI can also issue a non-binding additional capital guidance based on stress test results (Pillar II-G). The result of the 2023 SREP did not yield a Pillar II-G guidance. The total Pillar II capital requirement was therefore 2.8% or ISK 36 billion at year-end 2023.

[1] See https://www.althingi.is/lagas/nuna/2002161.html

The Internal Capital Adequacy Assessment Process (ICAAP) is the Bank's own assessment of its capital need. The Bank uses internal models for the calculation of economic capital (EC) for material risk factors, for ICAAP, as well as using stress tests. For credit risk, which is the biggest risk factor in the Bank's operation, the Bank primarily uses the internal rating based (A-IRB) approach to assess its capital need. The total Pillar II requirement as calculated by the Bank's internal models in 2023 is lower than the requirement set by the SREP. The difference lies in the assessment of the capital need for credit risk. ICAAP and SREP form the foundation for the Bank's capital planning, including the business and financial plan for the next 3 years. Table 3.3 shows the results of the 2023 SREP compared to 2022.

Table 3.3: SREP results

		2023 % RWEA	2022 % RWEA
Pillar I	Credit risk	7.2%	7.2%
	Market risk	0.1%	0.1%
	Operational risk	0.7%	0.7%
	Minimum capital requirement	**8.0%**	**8.0%**
Pillar II	Credit, counterparty and concentration risk	1.2%	1.8%
	Market risk and IRRBB	1.4%	1.4%
	Other risk	0.2%	0.2%
	Additional P-II R	**2.8%**	**3.4%**
	Additional P-II G	**0.0%**	**0.0%**
	Minimum requirement under Pillar I and Pillar II-R	**10.8%**	**11.4%**

3.4.3 Capital buffers

CRD IV introduced a combined buffer requirement that applies in addition to the solvency need ratio. The combined buffer consists of a countercyclical buffer, a capital conservation buffer, O-SII buffer and a systemic risk buffer. Capital buffers must be funded with CET 1 capital.

The combined capital buffer requirement as determined by the Icelandic Financial Stability Committee (FSC) for SIFIs was 9.5% of RWEA at year-end 2023.

Table 3.4: Regulatory capital buffers

	19.3.2020	29.9.2022	16.3.2024	Effective capital buffers at year-end 2023
Systemic risk buffer	3.00%	3.00%	3.00%	2.90%
O-SII buffer	2.00%	2.00%	2.00%	2.00%
Countercyclical buffer	0.00%	2.00%	2.50%	2.00%
Capital conservation buffer	2.50%	2.50%	2.50%	2.50%
Combined capital buffer requirement	**7.50%**	**9.50%**	**10.00%**	**9.40%**

In March 2023, the FSC announced its intention to raise the countercyclical buffer from 2.0% to 2.5% in March 2024. In the announcement, the FSC stated that Icelandic banks are well equipped to meet increased capital requirements while maintaining credit availability. Further, the FSC stated that the countercyclical buffer is an important part in maintaining the robustness of the Icelandic banking system, and the decision to increase it is due to increased risk in the system.

The capital buffers are expressed as a proportion of consolidated RWEA. However, the systemic risk buffer only applies to domestic RWEA, meaning that the effective requirement for the buffer is slightly lower than defined by the financial authorities, or 2.9% instead of 3.0%. The effective countercyclical capital buffer is determined using the weighted average of the prevailing capital buffer level in the countries where the Bank has exposure. The buffer is currently 2.0% in Iceland. Countercyclical buffers for foreign exposures, can raise or lower the effective buffer for the portfolio, based on their respective values. The effective countercyclical buffer was 2.0% at year-end 2023. Further quantitative information regarding the countercyclical capital buffer can be found in templates CCyB1 and CCyB2 in the additional disclosures accompanying this report.

The effective total regulatory capital buffer for the Bank at year-end 2023 was 9.4% of consolidated RWEA. Therefore, the Bank's total capital requirement at year-end 2023 is 20.2% of consolidated RWEA.

Table 3.5: Capital requirement

31.12.2023	CET1	Tier 1	Total
Pillar I	4.5%	6.0%	8.0%
Pillar II-R	1.6%	2.1%	2.8%
Minimum requirement under Pillar I and Pillar II-R	**6.1%**	**8.1%**	**10.8%**
Systemic risk buffer	2.9%	2.9%	2.9%
Capital buffer for systematically important financial institutions	2.0%	2.0%	2.0%
Countercyclical capital buffer	2.0%	2.0%	2.0%
Capital conservation buffer	2.5%	2.5%	2.5%
Combined buffer requirement	**9.4%**	**9.4%**	**9.4%**
Total capital requirement	**15.5%**	**17.5%**	**20.2%**

3.4.4 Capital target

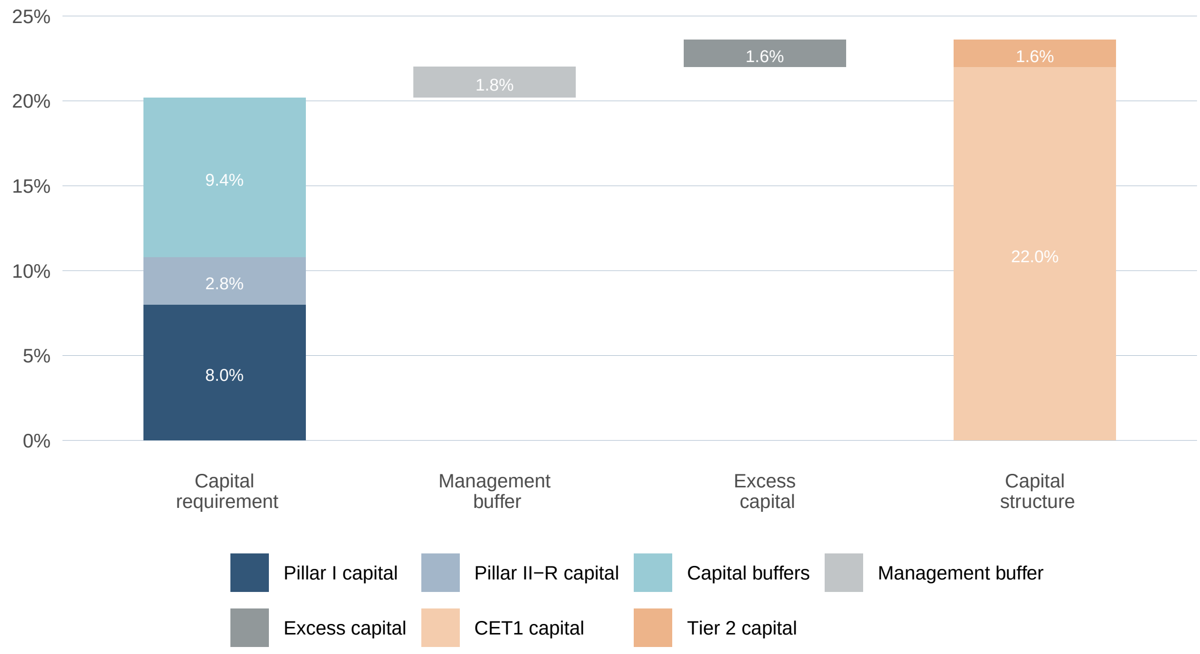
The Bank's capital target is based on the current regulatory capital requirement of 15.5% CET1 and 20.2% total capital ratio (TCR). In addition, the Bank defines a management buffer for the purpose of targeting and managing its capital position comfortably above the overall regulatory capital requirement. Determination of the management buffer is based on various current and forward-looking factors such as the economic and funding outlook, competitive issues, risk profile and business plan.

As shown in Table 3.6, the Bank's total target capital ratio is $\geq$ 22% and $\geq$ 18% for the CET1 ratio. Given the 20.2% TCR requirement, the Bank's current implied management buffer is 1.8%. The total capital ratio at year-end 2023 was 23.6%, hence the implied Bank's excess capital was 1.6% of RWEA, or ISK 20 billion.

Table 3.6: Capital ratio

	Target	2023	2022	2021	Comment
Total capital ratio	$\geq$22.0%	23.6%	24.7%	26.6%	Long-term goal
Common equity Tier 1	$\geq$18.0%	22.0%	22.9%	24.8%	Long-term goal
Dividend pay-out ratio	Around 50%	50%	71%	43%	The target dividend pay-out ratio is around 50% of the previous year's profit.

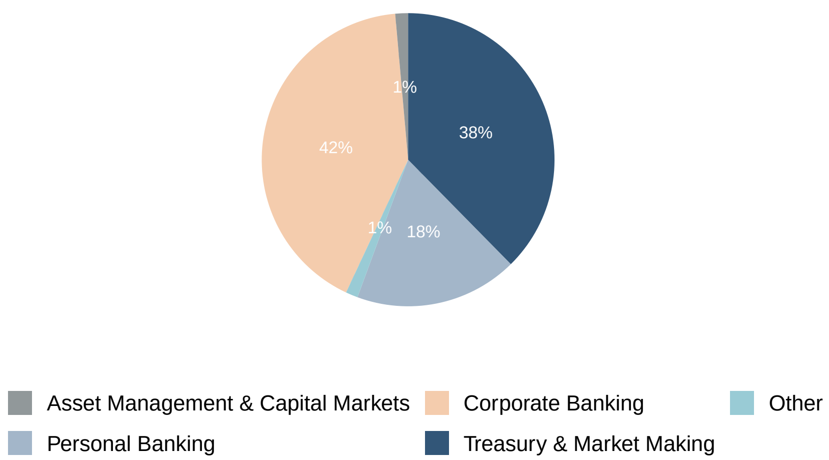
Figure 3.3: Capital structure (% RWEA) as at 31.12.2023



3.4.5 Capital allocation to business lines

The Bank makes an internal capital allocation across business divisions on the basis of each unit's contribution to the Bank's total risk as estimated by the Bank's EC model. Capital exceeding the Bank's minimum capital target and the management buffer is allocated to Treasury. Allocated capital plus retained earnings per business unit at year-end 2023 is shown in Figure 3.4.

Figure 3.4: Capital allocation per business line 31.12.2023



3.4.6 Risk-adjusted return on capital

To analyse the Bank's risk-adjusted profit and profitability, i.e. including the cost of risk, the measures risk-adjusted profit (RAP) and risk-adjusted return on capital (RAROC), are reported monthly to senior management. The objective of these metrics is to assess shareholder value creation and profitability in relation to the equity capital needed to cover the undertaken risks, i.e., the economic capital. The measures enable risk-based pricing, increase incentives to measure and manage risk appropriately, focus on long-term profit, and support the assessment of the Bank's optimal capital structure. These measures have been implemented throughout the Bank and are used in individual credit decisions for large corporate customers, as well as to determine the pricing of loan products for smaller corporate customers and individuals.

3.5 Leverage ratio

The Capital Requirements Regulation (CRR), as part of the Basel III framework, requires banks to measure, report and monitor their leverage ratios. The ratio is defined as CET1 capital as a percentage of total leverage exposure (see Table 3.7) and acts as a credible supplementary measure to the risk-based capital requirements.

A credible leverage ratio is one that ensures broad and adequate capture of both the on and off-balance sheet sources of the Bank's leverage, aimed at revealing hidden leverage on the Bank's balance sheets. The ratio reinforces the risk-based requirements with a simple non-risk based 'backstop' measure and is intended to restrict the build-up of leverage in the banking sector. The leverage ratio minimum requirement is 3%.

At year-end 2023, the Bank's leverage ratio was 13.6%. Figures 3.5 and 3.6 show the Bank's leverage ratio for the past five years. Despite trending downwards in this period, the ratio is still around 4.5 times the minimum 3% requirement.

Table 3.7: Leverage ratio

	2023	**2022**
Tier 1 capital	281,799	271,628
Leverage exposure		
- On balance sheet exposure (excluding derivatives)	1,942,770	1,772,743
- Derivatives instrument exposure	21,757	9,482
- Securities financing transaction exposures	11,598	12,325
- Off balance sheet exposure	118,051	97,338
- Regulatory adjustments to Tier 1 capital	-20,664	-7,463
Total leverage exposure	**2,073,512**	**1,884,426**
Leverage ratio	**13.6%**	**14.4%**

In theory, if the Bank would want to decrease its leverage ratio and aim for the minimum of 3%, it would not be able to do so without breaching other regulated, or internal risk appetite ratios first. Furthermore, off-balance sheet exposures and derivative instrument exposures are not significant factors of the Bank's leverage ratio. The risk of excessive leverage is thus not considered a significant risk factor for the Bank. Leverage ratio is nevertheless a part of the Bank's risk appetite and is considered a relevant risk indicator both in the Bank's ICAAP/ILAAP, as well as within BRRD. The Bank has management actions in place to meet scenarios that would adversely affect the Bank's leverage ratio. Further quantitative information regarding the Bank's leverage ratio can be found in templates LR1, LR2 and LR3 in the additional disclosures accompanying this report.

Figure 3.5: Leverage ratio

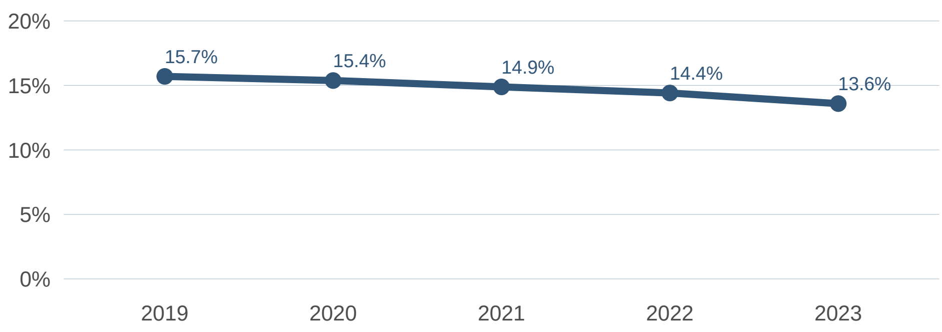
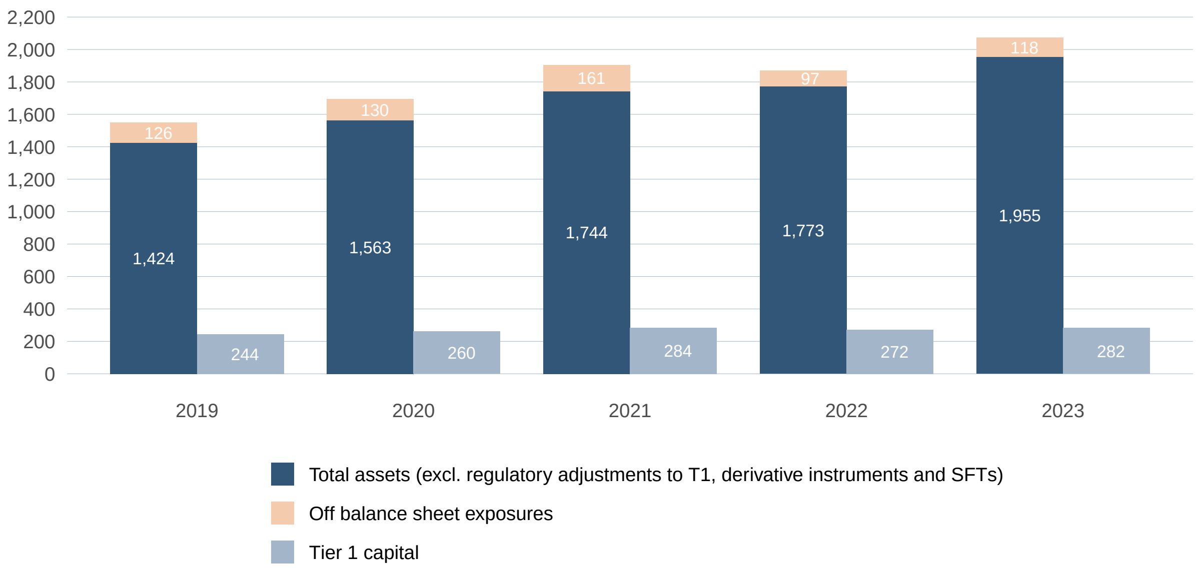


Figure 3.6: Leverage ratio breakdown (ISK bn)



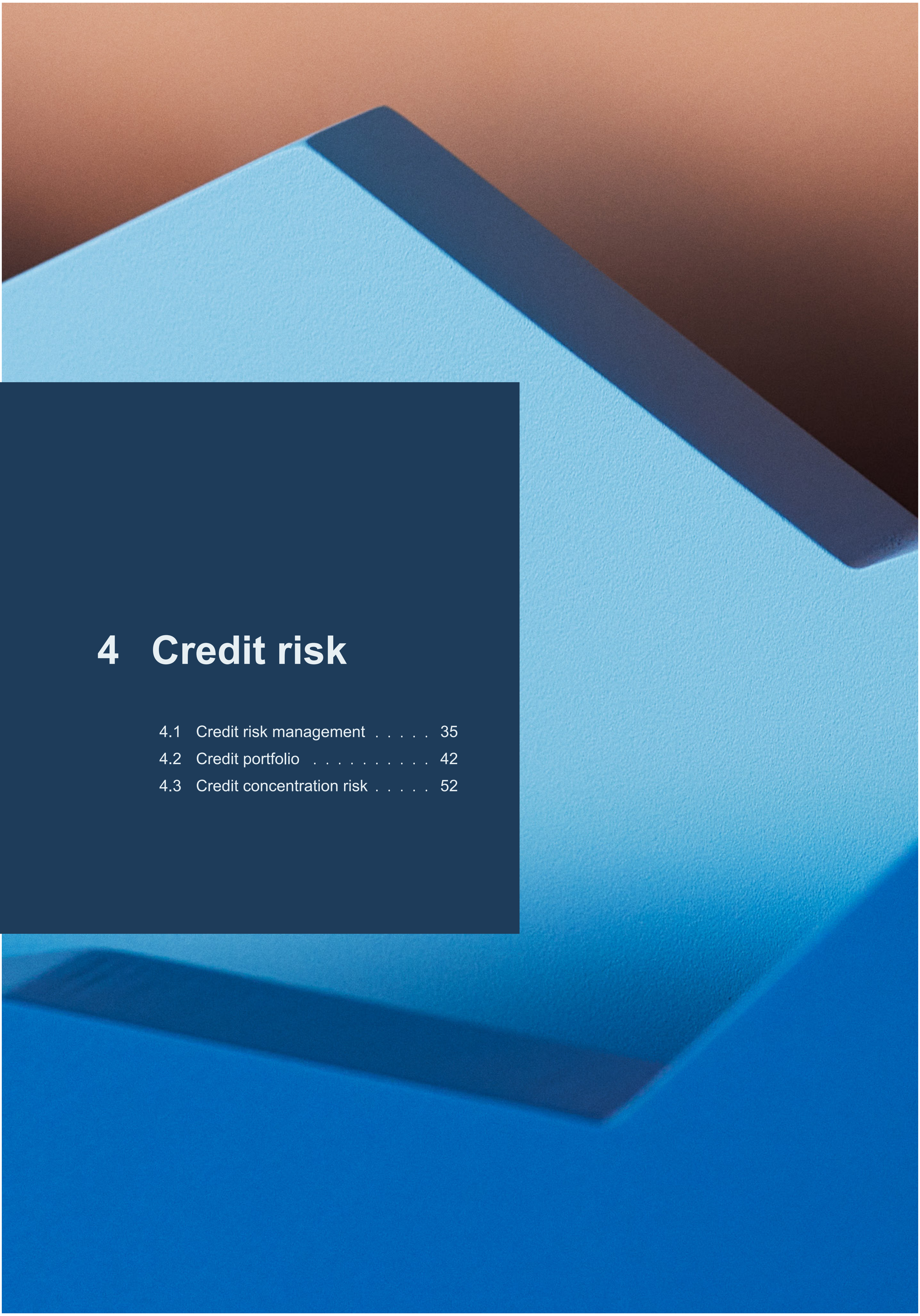
3.6 Minimum requirement for own funds and eligible liabilities (MREL)

Under the Act on Recovery and Resolution of Credit Institutions and Investment Firms, No. 70/2020, companies that fall under the scope of the Act shall at all times satisfy minimum requirements for own funds and eligible liabilities (MREL). On 17 October 2023, the CBI's Resolution Authority announced its latest MREL decision for the Bank. The MREL decision entails that the Bank must satisfy a 21.6% MREL requirement, as a percentage of total RWEA. MREL must be met without regards to the combined buffer requirement (CBR), which must be separately fulfilled alongside MREL. The Bank must also maintain a minimum of 6.0% of MREL funds, as a percentage of the Bank's Total Exposure Measure (TEM), which is equal to two times the Bank's minimum leverage ratio. The Bank also expects the Resolution Authority to introduce a 13.5% Subordination Requirement in the second half of 2024.

The MREL maximum distributable amount (M-MDA) is the maximum amount that the Bank is allowed to distribute via various actions, including dividend payments to shareholders, buy-back of own shares and payments of variable remuneration. These MREL restrictions are in addition to other own funds requirements.

Table 3.8: Minimum requirements for own funds and eligible liabilities (MREL)

Own funds and eligible liabilities as at 31.12.2023	**Amount**	**Percentage of RWEA**
Common Equity Tier 1 (CET1)	281,798	22.0%
Additional Tier 1 capital (AT1)	-	0.0%
Tier 2 capital	20,176	1.6%
Eligible liabilities	182,851	14.3%
Sum of own funds and eligible liabilities	**484,825**	**37.9%**
Less: Recurring MREL requirement	-276,358	-21.6%
Less: Combined buffer requirement (CBR)	-120,267	-9.4%
Sum of MREL and CBR	**-396,625**	-31.0%
MREL Maximum Distributable Amount (M-MDA)	**88,200**	**6.9%**



4 Credit risk

Credit risk

Credit risk is defined as the risk of loss if customers fail to fulfil their agreed obligations and the estimated value of pledged collateral does not cover existing claims.

- The Bank's total risk-weighted exposure to credit risk was ISK 1,144 billion at year-end 2023, increasing by 6.9% from the previous year. Loans and advances to customers carry the most credit risk of the Bank's assets.
- Total credit exposure from lending to customers increased by 6% in 2023 and amounted to ISK 1,631 billion at year end.
- Probability of default, weighted by gross carrying amount, decreased to 1.5% at year-end 2023 (2022: 1.8%).
- Total expected credit loss was ISK 11.9 billion at year-end 2023 (2022: ISK 10.6 billion).
- Default rates in the credit portfolio remain at low levels.

4.1 Credit risk management

The Bank offers loans, credits, guarantees and other credit-related products as part of its business model and thus takes on credit risk. Regular risk reporting enables the on-going monitoring of the Bank's credit risk position relative to its risk appetite.

The credit risk appetite is converted by the business units to their specific key performance indicators (KPIs) in collaboration with Risk Management. Monitoring functions determine whether credit facilities are granted in accordance with the risk appetite. Risk Management monitors and challenges the performance and reports the progress to the Executive Board and the Board of Directors.

Credit risk is primarily managed through the credit process and the Bank's credit risk models which include PD, LGD and EAD modelling. The models are used for various purposes, such as in provisioning, internal assessment of capital and management reporting.

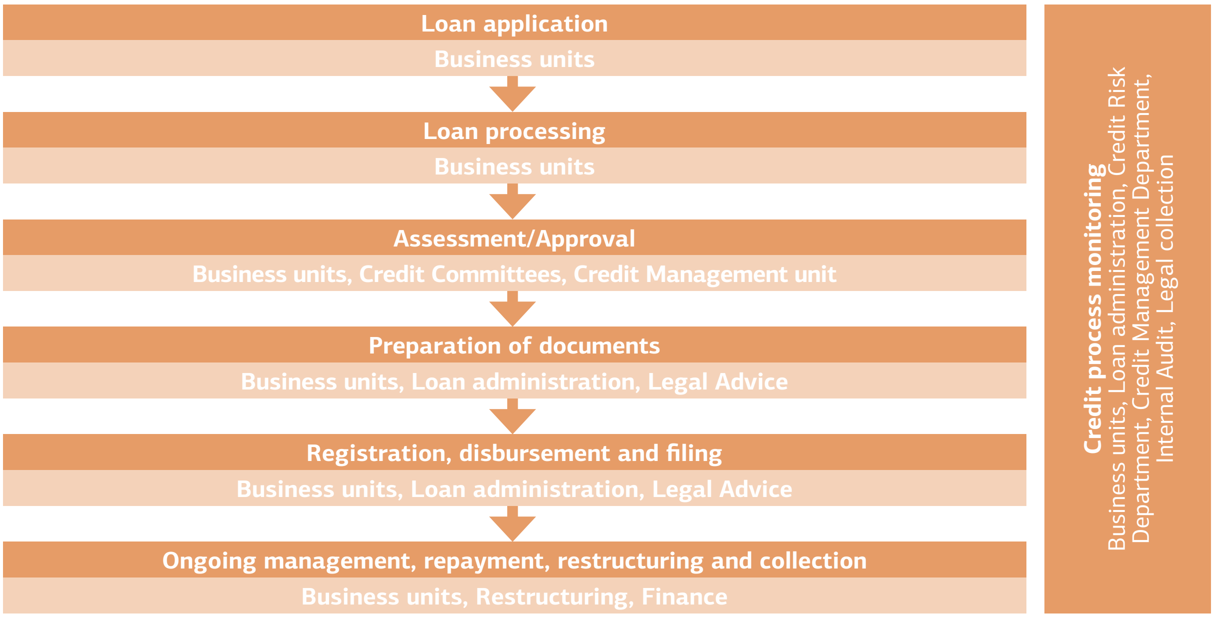
4.1.1 Identification

Credit risk is defined as the risk of loss if customers fail to fulfil contractual obligations and the estimated value of pledged collateral does not cover existing claims.

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of an entity to honour its obligation to deliver cash, securities or other assets as contractually agreed. Settlement risk is deemed immaterial in the Bank's operations.

Credit risk is the greatest single risk faced by the Bank and arises principally from loans and advances to customers, but also from loans and advances to financial institutions, investments in bonds and debt instruments, investments in equity and equity instruments, commitments, guarantees and documentary credits, counterparty credit risk in derivatives contracts, and the aforementioned settlement risk along with other assets.

Figure 4.1: The credit process



4.1.2 Assessment

Credit risk is primarily measured in three main dimensions: probability of default (PD), loss given default (LGD) and exposure at default (EAD). To measure PD, the Bank has developed an internal rating system, including internally developed rating models. The objectives of the rating system are to provide a meaningful assessment of obligor characteristics; a meaningful differentiation of credit quality; and accurate and consistent quantitative estimates of default risk, i.e., probability of default (PD). Internal ratings and associated PD values are essential in the risk management and decision-making process, and in the credit approval and corporate governance functions.

The rating system has an obligor rating scale which exclusively reflects quantification of the risk of obligor default, or credit quality. The obligor rating scale has 10 rating grades for non-defaulted obligors from 1 to 10, with 10 indicating the highest credit quality, and the grade 0 for defaulted obligors. The Bank's default definition is aligned with EBA's Guidelines on the application of the definition of default under Article 178 of Regulation (EU) No 575/2013 (EBA/GL/2016/07).

The internal rating system is used to assign ratings and calculate risk-weighted exposure amounts for the majority of the Bank's customers for economic capital. The PD assignment is supported by PD models, where information such as industry classification, financial accounts and payment behaviour is considered. The PD models were recalibrated in 2023 to accurately reflect the default risk under EBA/GL/2016/07. Additionally, external ratings from Standard & Poor's, Moody's and Fitch, are used for foreign credit institutions, and ratings from Creditinfo for new retail customers.

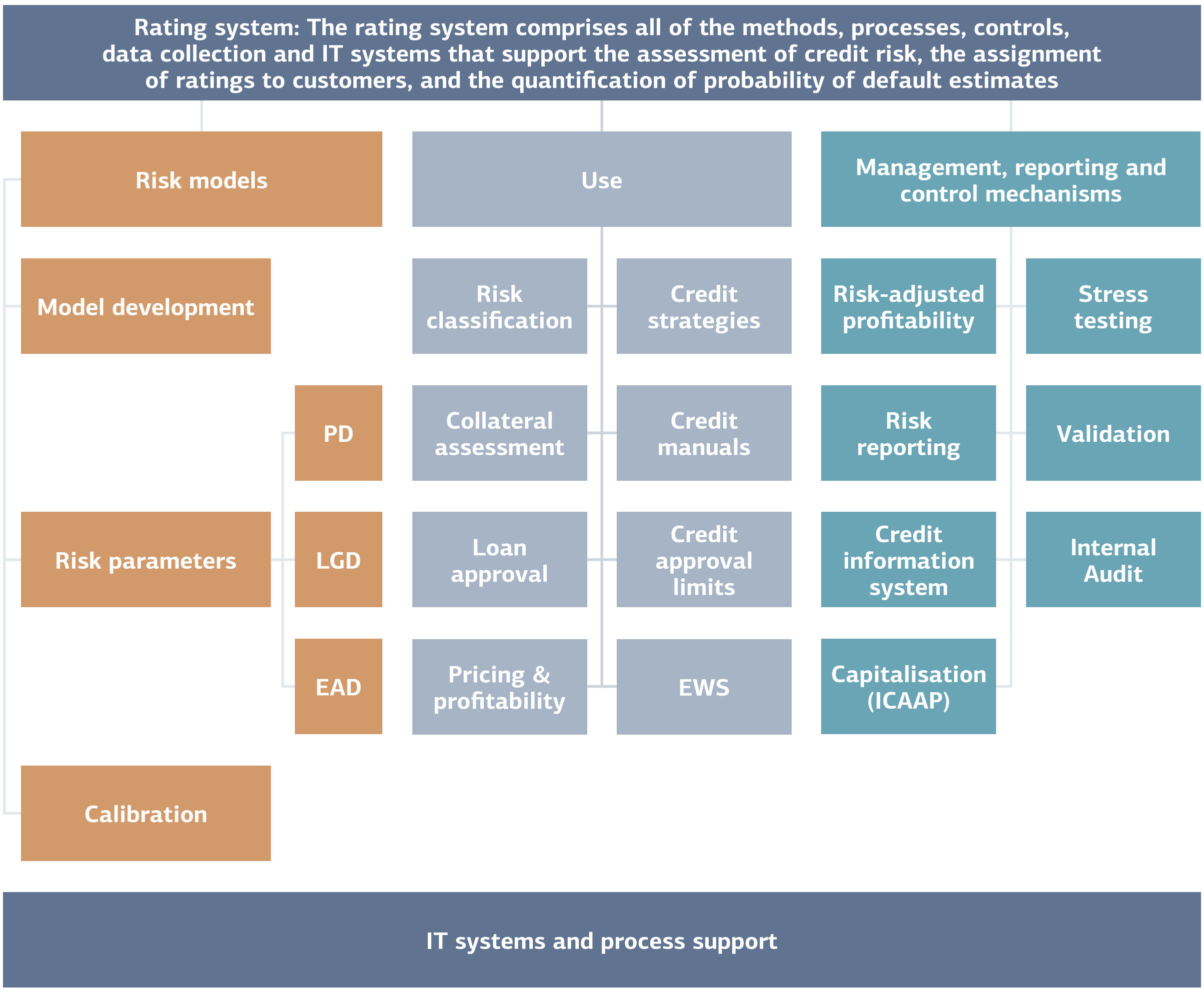
The rating assignment and approval is an integrated part of the credit approval process and assignment is updated at least annually, or when material information regarding the obligor or exposure becomes available.

The Bank's estimation and validation process includes quality controls to assess the performance of models, procedures and systems, and is designed to ensure the accuracy of risk parameters through adjustments where necessary.

Table 4.1: Internal mapping from internal rating grade to external rating agencies

Internal rating grade	Standard & Poor's and Fitch	Moody's	Lower PD	Upper PD
10	AAA/AA+/AA/AA-	Aaa/Aa1/Aa2/Aa3	0.00%	0.04%
9	A+/A/A-	A1/A2/A3	0.04%	0.10%
8	BBB+	Baa1	0.10%	0.21%
7	BBB/BBB-	Baa2/Baa3	0.21%	0.46%
6	BB+/BB	Ba1/Ba2	0.46%	0.99%
5	BB-	Ba3	0.99%	2.13%
4	B+	B1	2.13%	4.54%
3	B	B2	4.54%	9.39%
2	B-	B3	9.39%	18.42%
1	CCC/C	Caa1/Caa2/Caa3/Ca/C	18.42%	99.99%

Figure 4.2: Rating system overview



Internal rating models are validated annually, both quantitatively and qualitatively. The quantitative validation includes statistical tests of the models' discriminatory power, i.e. the models' ability to distinguish default risk, and absolute accuracy, i.e. the ability to predict default levels.

The PD parameters are validated annually by a quantitative and qualitative assessment, and re-estimated when the validation deems it necessary. PD estimates are based on long-term observed default frequency in available internal data and adjusted through an add-on. The adjustment for the length of internal data available is embedded in the margin of conservatism which also includes an add-on to compensate for statistical uncertainty in the estimation.

LGD is measured using an internal LGD model for the internal assessment of capital and provisioning. The LGD model takes into account more types of collateral and is more sensitive to the collateralisation level than calculations defined in the Basel framework, under the standardised method, and is calibrated to internal historical loss data.

EAD is an estimate of the amount outstanding (drawn amounts plus likely future drawdowns of yet undrawn lines) in case the borrower defaults. The Bank uses the standard approach for estimating RWEA and internal assessment of capital but uses internal models for provisioning.

4.1.3 Management and policy

The Bank's credit risk management objective is to ensure compliance with the Bank's credit policy, which entails that the only risk taken is one that the Bank understands, can evaluate, measure and manage.

The Bank's credit risk management is based on active monitoring by the Board of Directors, the CEO, the Risk & Finance Committee, the Credit Committee, the credit departments within the Risk Management division and the business units. The Bank manages credit risk according to its risk appetite statement, credit policy and industry policies, approved by the Board of Directors, as well as detailed credit policies approved by the CEO. The risk appetite, credit policy and industry policies include limits on large exposures to individual borrowers or groups of borrowers, concentration of risk and exposure to certain industries. The CEO ensures that the risk policy is reflected in the Bank's internal framework of regulations and guidelines. The Bank's Managing Directors are responsible for ensuring that the Bank's business units execute the risk policy appropriately and the CEO is responsible for oversight of the entire process.

Figure 4.3: Credit risk management framework

Incremental credit authorisation levels are defined based on size of units, types of customers and the lending experience of credit officers. Credit decisions exceeding authorisation levels of business units are subject to approval by Credit Management. The Corporate Banking Credit Committee has authorisation levels exceeding that of individual business unit managers and meets regularly to make credit decisions. Credit Management has veto powers over the decisions of the Corporate Banking Credit Committee and the Executive Credit Committee. Credit decisions exceeding the authorisation levels of the Corporate

Banking Credit Committee are subject to approval by the Bank's Credit Committee. Credit decisions exceeding the limits of the Credit Committee are subject to approval by the Board of Directors, which holds the highest credit authorisation within the Bank.

4.1.4 Mitigation

Mitigating risk in the credit portfolio is a key element of the Bank's credit policy, as well as an inherent part of the credit-decision process. Securing loans with collateral is the main method of mitigating credit risk, whereas for some loan products collateral is required by legislation, as in the mortgage finance market, or is standard market practice.

The most important types of collateral are real estate, vessels and financial assets (shares or bonds).

The amount and type of collateral required depends on an assessment of the credit risk associated with the counterparty. Valuation parameters and the acceptability of different types of collateral are defined in the Bank's credit policy. Credit extended by the Bank may be secured on residential or commercial property, land, listed and unlisted securities, transport vessels, fishing vessels together with their non-transferable fishing quotas, etc. The Bank also secures its loans by means of receivables, inventory and operating assets, such as machinery and equipment. Residential mortgages involve the underlying residential property. Less stringent requirements are set for securing short-term personal loans, such as overdrafts and credit card borrowings.

The Bank regularly assesses the market value of received collateral. The Bank estimates the value as the market value less a haircut. A haircut in this context is a discount factor which represents a conservative estimate of the costs to sell in a forced sale. Costs to sell include maintenance costs during the period the asset is held for sale, external fees and loss in value. For listed securities, haircuts are calculated with an internal model based on variables, such as price volatility and marketability.

The Bank monitors the market value of mark-to-market collateral and may require additional collateral in accordance with the underlying loan agreements.

In order to further limit the credit risk arising from financial instruments, the Bank enters into netting agreements, under which the Bank is able to set off all contracts covered by the netting agreement against the debt in cases of default. The arrangements generally include all market transactions between the Bank and the customer.

Generally, collateral is not held over loans and advances to financial institutions, nor is it usually held against bonds and debt instruments.

The Bank includes all collateral to which a value is assigned in accordance with its internal procedures. Guarantees are included if they imply lower risk weights than the original exposure. In addition, collateral is volatility-adjusted (by means of a haircut) in order to take price volatility and the expected costs of repossession and sale of the pledge into account.

4.1.4.1 Counterparty credit risk

Counterparty credit risk (CCR) is the risk arising from the possibility that the counterparty may default on amounts owned on derivative financial instruments and securities financing.

In order to mitigate this risk, the Bank chooses the counterparties for derivatives and margin trading based on stringent requirements. The Bank also enters into standard International Swaps and Derivatives Association (ISDA) master netting agreements and similar general netting agreements with financial counterparties. In the case of derivatives, amounts due to and from the Bank are offset when the Bank has a legally enforceable right to set off a recognised amount and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Collateral and margin requirements are in place for all derivative contracts and securities financing transactions the Bank enters into. Collateral management and monitoring are performed daily, and derivative contracts with customers are usually fully hedged.

The Bank's supervision system monitors both exposure and collateral value and calculates an intraday credit equivalent value for each derivative. It also issues margin calls and manages netting agreements.

In the case of derivatives, amounts due to and from the Bank are offset when the Bank has a legally enforceable right to set off a recognised amount and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Information on CCR can be found in templates CCRA and CCR1-CCR6 in the additional disclosures accompanying this report.

4.1.5 Control and monitoring

The Bank has set limits for large exposures as well as policies for exposure ratio for different portfolios to control the credit risk in the Bank's credit portfolio and ensure risk diversification. The credit risk decision process is controlled with limits set in the Bank's Credit rules approved by the Board of Directors. The rules set the limit for each credit decision party within the Bank where the credit approval authority is based on the underlying credit risk measured by exposure size, credit rating and colour classification code.

The credit risk monitoring process is based on regular reporting, monitoring systems and other manual monitoring. There is increased monitoring for significant exposures and for customers with indications of financial difficulties. One of the integral parts of the credit risk monitoring process is the early warning system.

The Bank monitors exposures to identify signs of weakness in customer earnings and liquidity, or other issues that could increase the Bank's credit risk, as soon as possible. To monitor customers, the Bank uses an early warning system, which is supplemental to ratings and classifies credit exposures to four credit risk groups (green, yellow, orange and red). The colour classification is as follows:

- The customer is considered as performing without signs of financial difficulties
- The customer shows indication of deteriorating financial strength, which could lead to financial difficulties
- The customer is or has been in financial difficulties or default
- The customer is in default and in legal collection and/or restructuring

The Credit Risk department within Risk Management and the Bank's business units are responsible for the colour classification of customers.

4.1.6 Impairment process

The Bank uses the three-stage expected credit loss model under IFRS 9. Allowance is calculated as the 12-month expected credit loss (ECL) or the lifetime expected credit loss.

The Bank recognises loss allowances for ECL on the following financial instruments that are not measured at fair value through profit or loss:

- Cash and balances with Central Bank
- Bonds and debt instruments
- Loans and advances to financial institutions
- Loans and advances to customers
- Other assets

Off-balance sheet exposures:

- Financial guarantees and underwriting commitments
- Undrawn loan commitments
- Undrawn overdraft/credit card facilities

When measuring ECL, the Bank uses a forward-focused model in compliance with IFRS 9. This requires considerable judgement over how changes in economic factors affect ECL. ECL reflects the present value of cash shortfalls due to possible default events either over the following twelve months or over the expected life of a financial instrument, depending on credit deterioration from origination.

The Credit Risk Department is responsible for assessing impairment on loans and receivables and a Valuation Team, comprised of the CEO, the managing directors of Finance, Risk Management, Corporate Banking and Personal Banking, reviews and approves the assessment.

In general, all impairment charges are loan-specific based on the aforementioned ECL models. If needed, the Valuation Team can assess and issue additional general impairment charges.

In 2023, updated PD Point-in-Time (PD PIT) models were developed and implemented. The updated models were developed using updated historical default data, in line with the Bank's updated definition of default, implemented in 2021.

For further information on the Bank's impairment process, see Note 83.11(g) in the Bank's Annual Financial Statement 2023.

4.2 Credit portfolio

4.2.1 Risk-weighted exposure amount

The Bank's risk-weighted exposure amount (RWEA) for credit risk was ISK 1,144 billion at year-end 2023, which is an increase of 6.9% from the previous year. The increase is mostly due to increased corporate and mortgage lending. Table 4.2 shows the RWEA for credit risk at year-end 2022 and 2023, broken down by exposure classes. Further quantitative information regarding RWEA for credit risk can be found in templates CR4 and CR5 in the additional disclosures accompanying this report.

Table 4.2: RWEA and Pillar I capital requirement for credit risk by exposure classes

	31.12.2023		31.12.2022	
	Pillar I	**RWEA**	**Pillar I**	**RWEA**
Central governments or central banks	3	43	3	42
Regional governments or local authorities	230	2,878	185	2,315
Public sector entities	221	2,758	222	2,781
Institutions	1,135	14,183	572	7,144
Corporates	51,571	644,640	46,634	582,922
Retail	7,767	97,091	8,450	105,631
Secured by mortgages on immovable property	24,007	300,086	22,357	279,464
Exposures in default	1,646	20,581	1,486	18,573
Items associated with particular high risk	2,816	35,206	3,720	46,499
CIUs	65	818	48	597
Equities and equity instruments	34	422	60	752
Other items	2,062	25,770	1,950	24,372
Credit risk	**91,558**	**1,144,477**	**85,687**	**1,071,091**

4.2.2 Credit exposure

The Bank's credit exposure is defined as balance sheet items and off-balance sheet items that carry credit risk. For on-balance sheet loans and advances, the exposure is calculated net of accumulated ECL for exposures measured at amortised cost, otherwise at fair value. Off-balance sheet amounts are the maximum amounts the Bank might have to pay out in guarantees, loan commitments in their full amount, and undrawn overdraft and credit card facilities.

At year-end 2023, 89.5% of the Bank's RWEA was due to credit risk, most of which comes from lending activities. On the same date, total loans and advances amounted to ISK 1,685 billion (2022: ISK 1,573 billion), with ISK 1,631 billion coming from lending activities (2022: ISK 1,544 billion) and ISK 54 billion from loans and advances to financial institutions (2022: ISK 29 billion).

The maximum on-balance exposure to credit risk was ISK 1,935 billion at year-end 2023. ISK 1,631 billion was derived from loans and advances to customers, ISK 75 billion from cash and balances with the Central Bank, and ISK 130 billion from bonds and debt instruments. The total off-balance exposure at year-end 2023 was ISK 291 billion. ISK 183 billion was derived from undrawn loan commitments, ISK 80 billion from undrawn overdraft/credit card facilities and ISK 28 billion from financial guarantees and underwriting commitments. Further quantitative information regarding the Bank's credit portfolio can be found in templates CR1, CR1-A, CR2, CQ1, CQ3, CQ5, CQ7 and CR3 in the additional disclosures accompanying this report.

4.2.2.1 Credit exposure from lending activities

At year-end 2023, the Bank's total credit exposure from lending activities amounted to ISK 1,631 billion, increasing by 6% from ISK 1,544 billion at year-end 2022.

The total average PD weighted by gross carrying amount was 1.5% at year-end 2023 (2022: 1.8%). Excluding loans to financial institutions, the average PD was 1.6% (2022: 1.9%). The average PD for individuals was 0.8% (2022: 1.4%) and the average PD for corporates was 2.4% (2022: 2.3%). The decrease in average PD for individuals is largely attributed to updated rating models, based on updated historical default data. Credit quality in the corporate portfolio remained stable in 2023, with updated rating models for corporates not having the same effect on PD values as observed for individuals.

At year-end 2023, the total average LGD weighted by gross carrying amount, excluding loans to financial institutions, was 10.4% (2022: 13.2%). The average LGD for individuals was 7.4% (2022: 7.8%) and the average LGD for corporates was 13.5% (2022: 18.7%).

The carrying amount of loans in stage 3 net of accumulated ECL as a percentage of the total portfolio was 1.0% at year-end 2023 (2022: 1.0%). The ratio was 1.6% for corporates (2022: 1.8%) and 0.5% for individuals (2022: 0.2%).

The carrying amount of loans and advances to customers past due by 6-90 days increased slightly in 2023. The ratio of loans past due by 6-90 days was 1.0% at year-end 2023 (2022: 0.7%). For individuals, the ratio was 0.8% (2022: 0.5%) and for corporates, the ratio was 1.2% (2022: 0.9%).

Figure 4.4: Probability of default (PD)

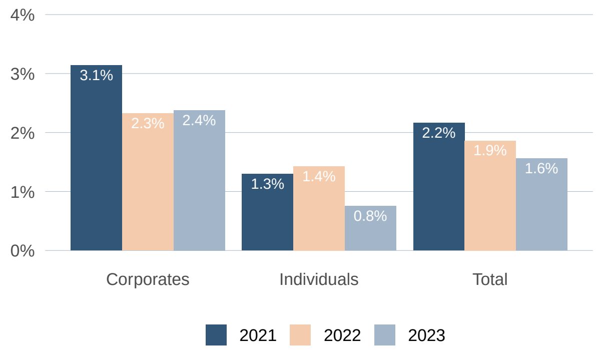


Figure 4.5: Loss given default (LGD)

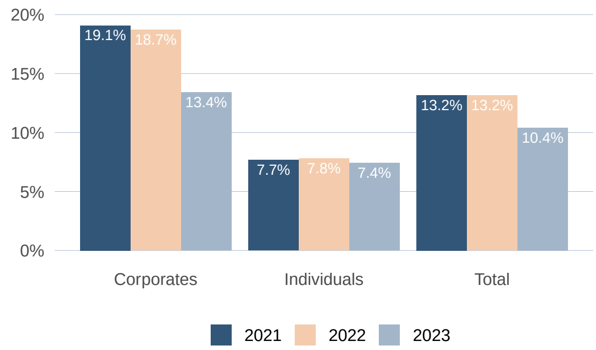


Figure 4.6: Stage 3 loans (% of total portfolio)

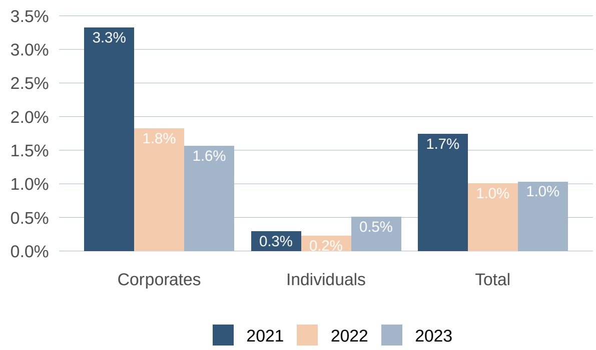
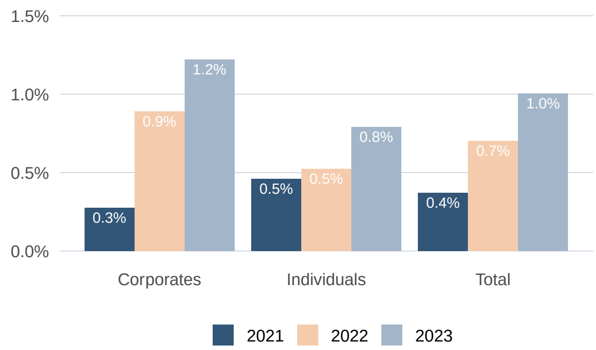


Figure 4.7: Ratio of loans past due 6-90 days



The ratio of the carrying amount of loans and advances to customers in stage 3 was 1.0% at year-end 2023 (2022: 1.0%). For individuals, the ratio increased in 2023 and was 0.5% at year end (2022: 0.2%) and for corporates, the ratio decreased in 2023 and was 1.6% at year end (2022: 1.8%). The ratio of the carrying amount of loans and advances to customers past due more than 90 days was 0.3% at year-end 2023 (2022: 0.2%).

Table 4.3 shows the carrying amount of loans and advances by industry sectors along with key risk metric values. PD and LGD averages in the table are weighted by gross carrying amount, other ratios with carrying amount. A more thorough description of the largest industry sectors follows.

4.2.2.2 Loans to corporates

The Bank's corporate loan portfolio is well diversified across sectors and is almost exclusively (97%) comprised of loans to domestic entities. The largest sectors are fisheries, real estate companies, construction companies and the travel industry.

The corporate portfolio grew by 8% in 2023 and loans and advances to corporate customers amounted to ISK 800 billion at year end. Corporate loans represent 49% of the Bank's loan portfolio. Credit quality in the corporate portfolio remained stable in 2023, with the average PD value increasing only slightly, from 2.3% to 2.4%. The average LGD value for corporate loans decreased in 2023 and was 13.5% at year end (2022: 18.9%). The ratio of corporate loans in stage 2 increased slightly in 2023 and was 6.5% at year end (2022: 4.8%), while the ratio of corporate loans in stage 3 decreased slightly and was 1.6% at year end (2022: 1.8%).

4.2.2.3 Loans to individuals

Loans to individuals comprise 50% of the Bank's loan portfolio. A majority of these loans are mortgages, secured by residential properties. Other loans to individuals include car loans, credit cards, overdrafts and other consumer loans.

4.2.2.3.1 Mortgages

The carrying amount of mortgages to individuals in the portfolio was ISK 731 billion at year-end 2023 (2022: ISK 705 billion). Non-indexed loans represented 67% of the carrying amount of the mortgage portfolio at year-end 2023 (2022: 75%). Fixed-rate, non-indexed mortgages amounted to ISK 317 billion at year-end 2023 (2022: ISK 297 billion). Customers can choose to fix rates on their mortgages for either a period of 3 or 5 years at a time. At year-end 2023, ISK 213 billion of fixed-rate, non-indexed mortgages had a repricing date in either 2024 or 2025. Indexed mortgages amounted to ISK 241 billion at year-end 2023 (2022: ISK 178 billion), of which ISK 200 billion were floating rate mortgages. Floating-rate, non-indexed mortgages amounted to ISK 173 billion at year-end 2023 (2022: ISK 230 billion).

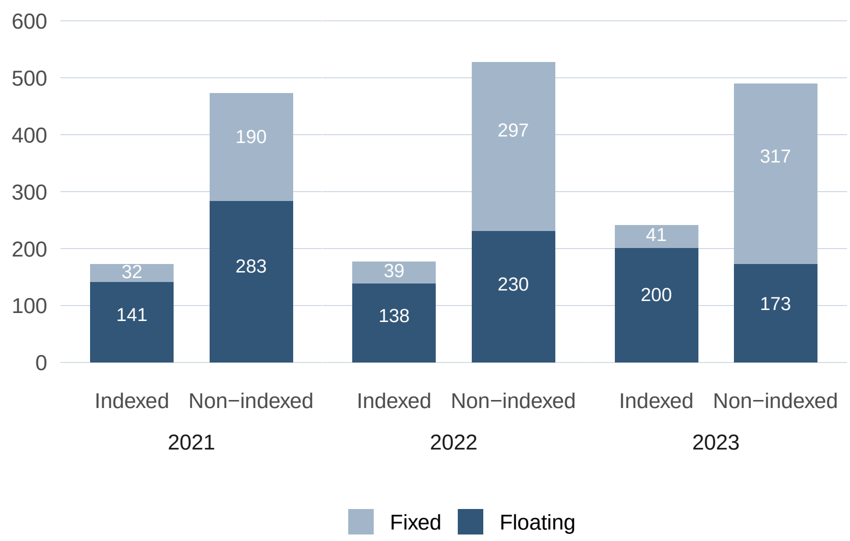
The increase in indexed mortgages along with the decrease in floating-rate, non-indexed mortgages is largely due to rising interest rates and the lower debt service of indexed mortgages. At year-end 2023, 1.1% of fixed-rate, non-indexed mortgages were past due. In 2023, ISK 19 billion of fixed-rate, non-indexed mortgages had their fixed-rate period expire. At year end, 1.1% of these mortgages were past due, the same ratio as for the entire portfolio of fixed-rate, non-indexed mortgages. This modest past due ratio in a challenging interest rate environment suggests a certain robustness of the mortgage portfolio, as a result of moderate leverage and the ability to decrease debt service by refinancing into indexed mortgages. The default rate for mortgages remains at low levels and was 0.3% in 2023, weighted by number of defaults.

Table 4.3: Overview of credit risk measures by industries

As at 31 December 2023	Carrying amount	PD	LGD	Past due 6-90 days	Stage 2 loans	Stage 3 loans	Total ECL
Public entities	11,449	0.6%	5.0%	0.0%	0.7%	0.0%	-4
Individuals	**819,151**	**0.8%**	**7.4%**	**0.8%**	**3.5%**	**0.5%**	**-2,382**
Mortgages	730,985	0.6%	4.3%	0.7%	2.4%	0.3%	-1,246
Other	88,166	2.1%	32.5%	1.2%	12.5%	1.9%	-1,136
Corporates	**800,294**	**2.4%**	**13.5%**	**1.2%**	**6.5%**	**1.6%**	**-8,988**
Fisheries	190,233	1.4%	8.2%	0.1%	0.3%	0.6%	-2,771
Real estate companies	176,428	2.3%	9.4%	1.3%	3.7%	1.2%	-930
Construction companies	132,177	2.8%	16.0%	0.1%	4.8%	1.5%	-1,172
Travel industry	107,693	3.3%	17.4%	4.9%	8.7%	4.9%	-2,498
Retail	64,178	1.5%	19.3%	0.2%	4.8%	0.4%	-330
Services and ITC*	62,100	3.8%	21.7%	2.8%	5.9%	0.9%	-725
Manufacturing and energy	32,536	2.5%	18.5%	0.3%	38.1%	0.4%	-382
Holding companies	27,739	4.0%	13.4%	0.1%	36.6%	4.1%	-164
Agriculture	7,210	0.5%	7.9%	0.0%	0.1%	0.0%	-16
Other	0	25.3%	50.1%	54.5%	9.3%	0.0%	0
Total loans to customers	**1,630,894**	**1.6%**	**10.4%**	**1.0%**	**4.9%**	**1.0%**	**-11,374**
Financial institutions	54,101	0.0%	30.0%	0.0%	0.0%	0.0%	0
Total loans including financial institutions	**1,684,995**	**1.5%**	**11.0%**	**1.0%**	**4.8%**	**1.0%**	**-11,374**
As at 31 December 2022	**Carrying amount**	**PD**	**LGD**	**Past due 6-90 days**	**Stage 2 loans**	**Stage 3 loans**	**Total ECL**
Public entities	10,519	1.3%	5.0%	0.0%	0.0%	0.0%	-6
Individuals	**790,238**	**1.4%**	**7.8%**	**0.5%**	**3.6%**	**0.2%**	**-1,327**
Mortgages	705,256	1.4%	5.0%	0.5%	3.1%	0.2%	-563
Other	84,982	2.0%	30.8%	1.0%	7.8%	0.6%	-763
Corporates	**743,604**	**2.3%**	**18.9%**	**0.9%**	**4.8%**	**1.8%**	**-8,662**
Fisheries	192,036	1.6%	11.2%	0.0%	1.2%	0.0%	-403
Real estate companies	139,509	2.5%	12.7%	1.0%	4.2%	1.1%	-989
Construction companies	102,394	3.5%	26.9%	1.0%	6.0%	2.4%	-1,553
Travel industry	110,843	3.2%	22.1%	3.3%	15.1%	5.5%	-3,450
Retail	64,585	1.3%	19.2%	0.2%	2.2%	0.4%	-925
Services and ITC*	60,334	1.9%	27.6%	0.8%	3.8%	0.2%	-366
Manufacturing and energy	38,971	1.1%	36.4%	0.0%	0.9%	8.2%	-778
Holding companies	28,168	3.6%	17.9%	0.1%	1.0%	0.1%	-177
Agriculture	6,764	2.2%	8.2%	0.0%	4.0%	0.1%	-20
Other	0	0.0%	50.1%	0.0%	100.0%	0.0%	0
Total loans to customers	**1,544,360**	**1.9%**	**13.2%**	**0.7%**	**4.2%**	**1.0%**	**-9,994**
Financial institutions	28,621	0.1%	30.0%	0.0%	0.0%	0.0%	0
Total loans including financial institutions	**1,572,981**	**1.8%**	**13.5%**	**0.7%**	**4.1%**	**1.0%**	**-9,995**

*ITC consists of corporations in the information, technology and communication sectors

Figure 4.8: Indexed vs. non-indexed mortgages (ISK bn)



All new mortgages must meet requirements for credit rating, payment capacity and collateralisation limits. These limits become more stringent as the loan amount increases. The Central Bank of Iceland has set rules on the maximum loan-to-value (LTV) ratio, i.e. the ratio of loan value to the value of the underlying collateral, of real estate loans to consumers. The current rules state that the maximum LTV for new mortgages is 80%, except for first-time buyers, where the maximum is 85%. The rules also include a payment capacity constraint, capping the monthly payment of mortgages to 35% of net monthly income (40% for first-time buyers). These limits were imposed to prevent unsustainable indebtedness for mortgage customers in the portfolio, in a market environment with high interest rates and rising housing prices.

The weighted average LTV of mortgage loans decreased in 2023 and was 50.7% at year-end (2022: 56.5%). The decrease in LTV is in line with rising housing prices, as the value of real estate underlying the calculation is largely based on official property valuation, which increased by an average of 19.9% for the market as a whole in 2023. If the LTV per customer is considered for the mortgage portfolio, 79% of the customers in the portfolio have an LTV of 70% and lower, and 97% have an LTV of 85% and lower. Figure 4.10 shows the gross carrying amount at year-end 2023 of indexed and non-indexed mortgages and the weighted-average LTV, as at year-end 2023, by year of loan origination. The figure shows the great demand for non-indexed mortgages during the period 2020-2022 due to favourable interest rates for non-indexed mortgages, and a resurgence of indexed loans in 2023. Demand for indexed mortgages increased in 2023 as variable interest rates on non-indexed mortgages have remained high. The figure also shows a high frequency of mortgage refinancing, made easier by favourable refinancing costs. This leads to a high ratio of the mortgage portfolio being recently issued loans. The weighted-average LTV was 57.5% for loans issued in 2023, around 55.8% for loans issued in 2022 and lower for older loans.

The average PD value for mortgages decreased in 2023 and was 0.6% at year end (2022: 1.4%). The decrease is largely due to a recalibration of PD models for individuals in 2023. Total ECL as a ratio of gross carrying amount for mortgages was 0.2% at year-end 2023 (2022: 0.1%). The default rate for mortgages, weighted by gross carrying amount, was 0.3% in 2023 (2022: 0.2%). Default rates and past due ratios have been very low in the mortgage portfolio for the past few years.

Figure 4.9: Weighted average LTV - Mortgages

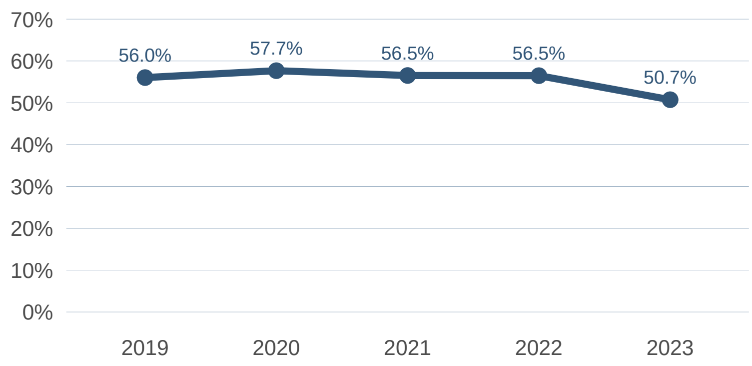


Figure 4.10: Gross carrying amount (ISK bn) and LTV of mortgages at 31.12.2023 by year of loan origination

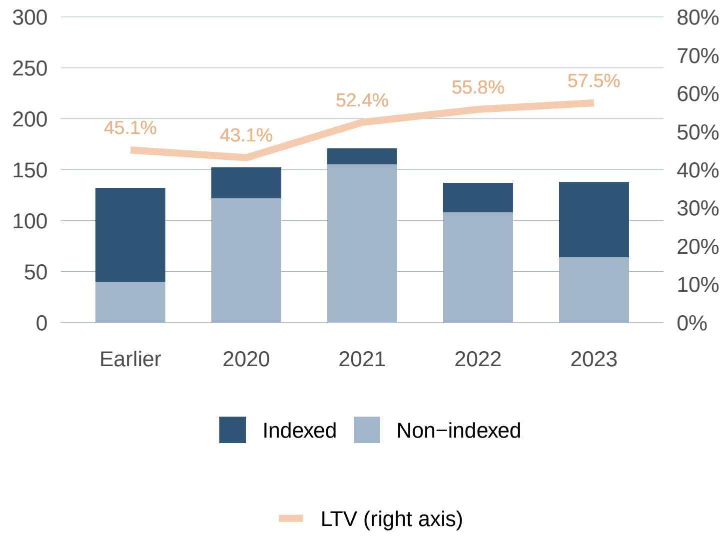
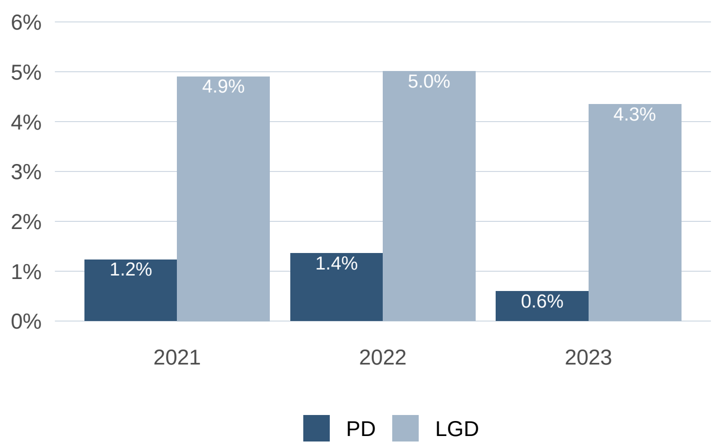


Figure 4.11: Average PD & LGD - Mortgages



4.2.3 Probability of default & migration analysis

Migration analysis in this section is based on the Bank's rating scale and PD estimates.

Figures 4.12 and 4.13 show the rating grade distribution of the loan portfolio for corporates and individuals.

Figure 4.12: Rating grade distribution - Corporates

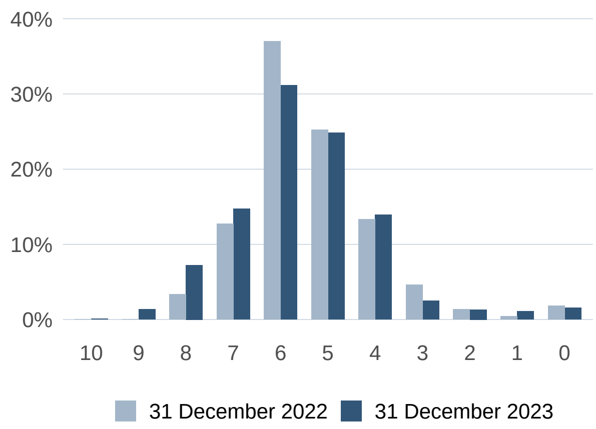
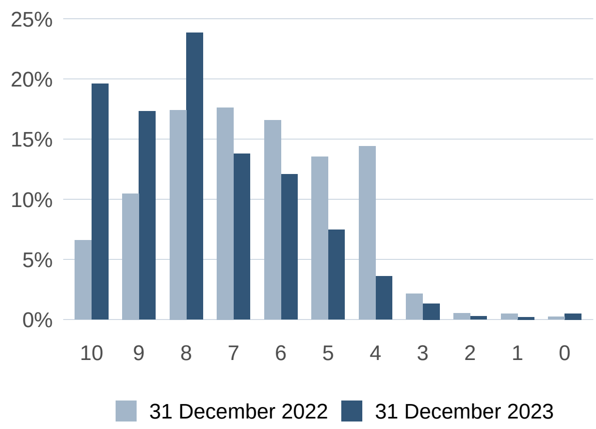


Figure 4.13: Rating grade distribution - Individuals



Figures 4.14 to 4.16 show the rating grade migration for corporates and individuals during 2023, based on existing customers at year-end 2022 and 2023.

Migration is shown both in terms of number of customers and exposure. Migration analysis does not include customers in default, i.e. customers with a credit rating of 0.

The rating and risk grade distribution changes primarily due to three factors: changes in rating grade for existing customers, or pure migration; different rating grade distribution of new customers and customers leaving the Bank compared to the rating grade distribution of existing customers during the comparison period, and; increased or decreased exposure per rating grade to existing customers. However, the recalibration of PD models to accurately reflect the default risk under EBA/GL/2016/07 is the largest factor in rating migrations in 2023.

Figure 4.14: Rating migration ratios in 2023

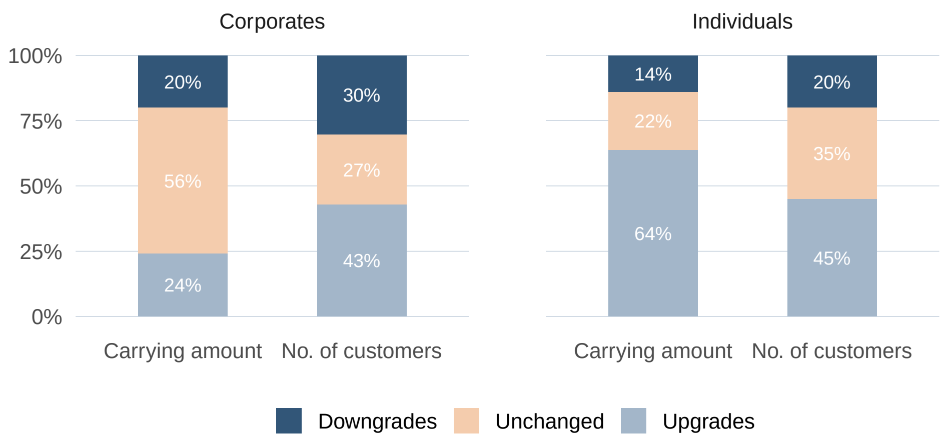


Figure 4.15: Rating migration of corporates in 2023

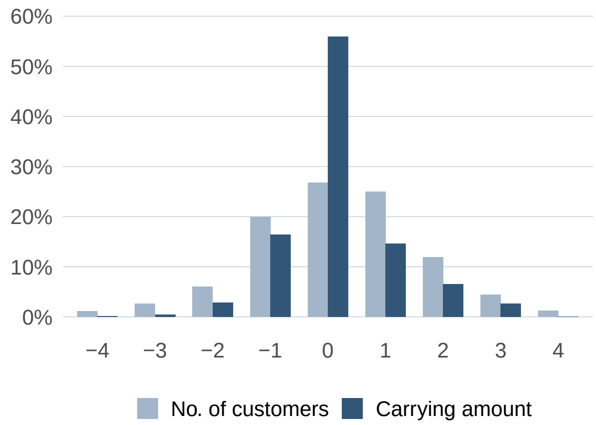
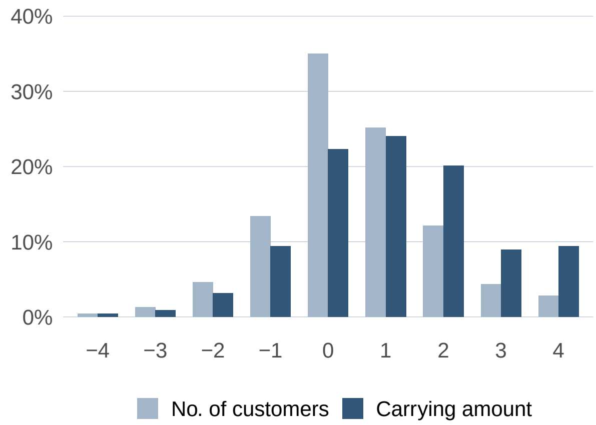
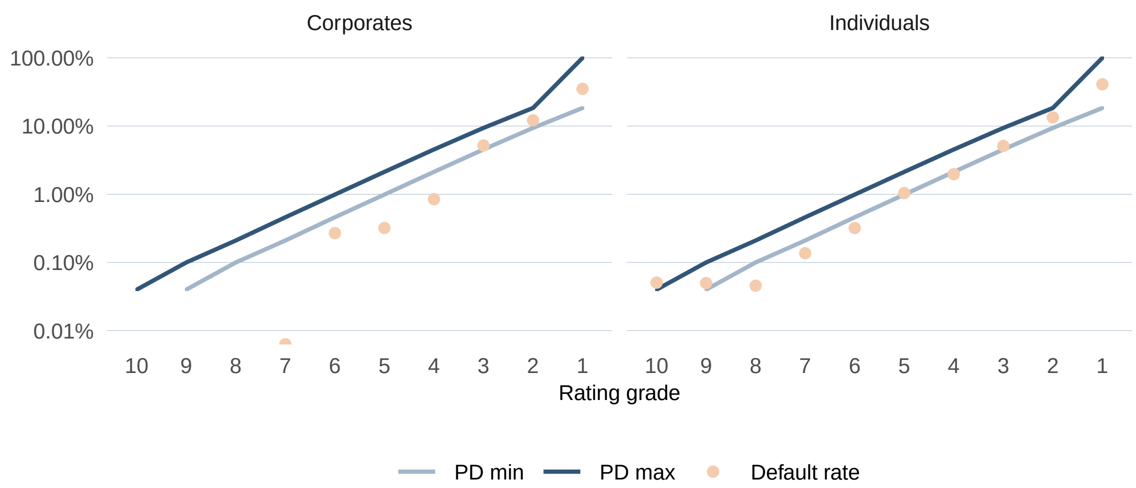


Figure 4.16: Rating migration of individuals in 2023



The default rate, measured by number of customers, was 1.6% for corporate customers in 2023, as compared to the estimated 3.4%. No corporate customers in rating grades 7-10 defaulted. The default rate of individuals for 2023 was 0.8% as compared to the estimated 1.1%. Estimated default rates are based on the average through-the-cycle (TTC) PD values for each rating category at the start of the year. For most rating grades, both for individuals and corporates, the default rate was below the PD bands. For individuals in rating grade 10, the default rate was slightly above the PD band. For all rating grades for corporate customers the default rate was below the PD band.

Figure 4.17: 12-month default rate vs. probability of default band



Figures 4.18 and 4.19 show a comparison between realised default rates and estimated PD values at the start of each year, weighted by gross carrying amount and number of customers, for both corporates and individuals. Realised default rates have been consistently below the estimated PD values both for corporates and individuals for the past four years.

Figure 4.18: Default rate vs. PD - Corporates

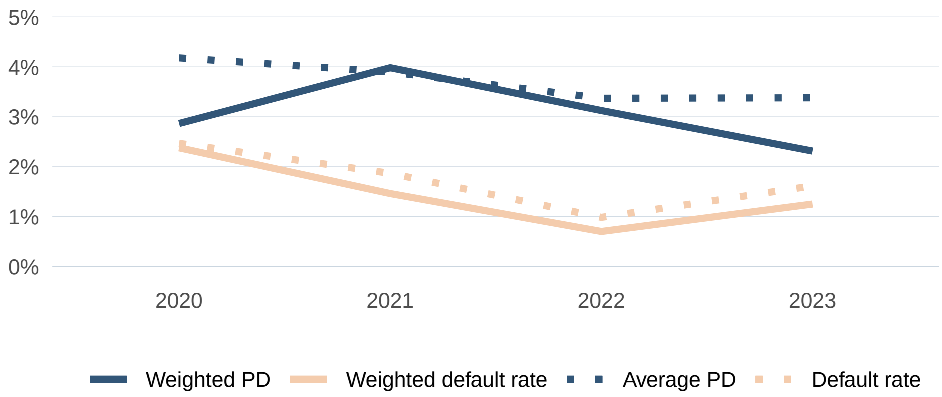
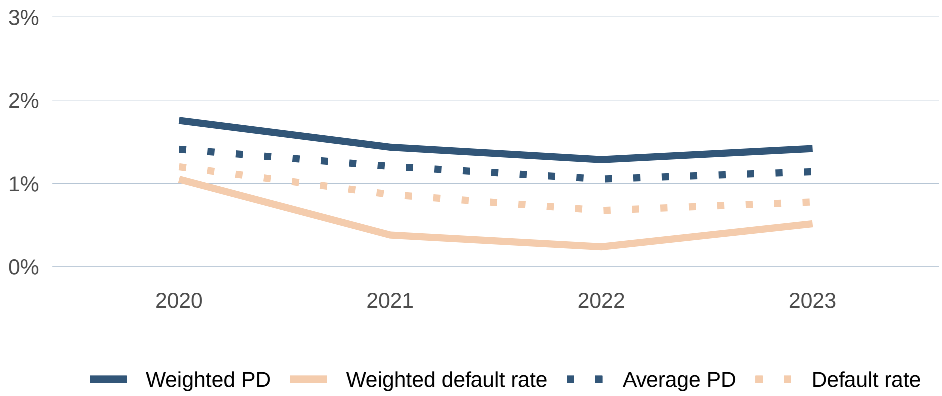


Figure 4.19: Default rate vs. PD - Individuals



4.2.4 Forbearance

The Bank adopts forbearance plans to assist customers in financial difficulty with the goal of protecting the Bank's long-term interests. Concessions granted to customers include interest-reduction schedules, interest-only schedules, temporary payment holidays, term extensions, cancellation of outstanding fees and settlements.

Forbearance plans must comply with the Bank's credit policy. They are used as an instrument to maintain long-term customer relationships for customers with financial difficulties if there is a realistic possibility that the customer will be able to meet obligations again and are used for minimising loss in the event of default.

The Bank has implemented EBA's definition of loans subject to forbearance measures. Table 4.4 is based on EBA's definition where exposures with forbearance measures are divided into performing and non-performing loans.

Total exposures subject to forbearance measures decreased from ISK 95 billion at year-end 2022 to ISK 46 billion at year-end 2023, which is a decrease from 6.1% to 2.8% of the total portfolio. This decrease is mainly due to discontinuation of forbearance classification of exposures that were granted COVID-related payment moratoria in 2021.

Further quantitative information regarding forborne exposures can be found in template CQ1 in the additional disclosures accompanying this report.

Table 4.4: Exposures subject to forbearance (ISK m)

	31.12.2023		31.12.2022	
	Performing	**Non-performing**	**Performing**	**Non-performing**
Modification	26,473	14,677	70,209	20,086
Refinancing	3,406	1,331	1,899	2,554
- of which: Under probation	7,337	0	4,897	0
Total	**29,878**	**16,008**	**72,108**	**22,640**

4.2.5 Loan impairment

Total expected credit loss (ECL) amounted to ISK 11.9 billion at year-end 2023 (thereof classified as deduction from gross carrying amounts: ISK 11.4 billion), as compared to ISK 10.6 billion at year-end 2022 (thereof classified as deduction from gross carrying amounts: ISK 10.0 billion). In 2023, a net impairment charge of ISK 3.0 billion was recognised in the Bank's income statement, as opposed to an ISK 2.4 billion released in 2022. Details on the development of ECL during the year can be found in note 60 in the Bank's annual financial statement for 2023.

ECL increased across all stages in 2023, mostly in stage 3. For individuals, the total ECL increased by ISK 1.1 billion while ECL in the corporate portfolio increased by ISK 326 million. The GCA of loans in stage 2 increased as well in 2023, as Figure 4.24 shows.

Figure 4.20: Expected credit loss by stage (ISK bn)

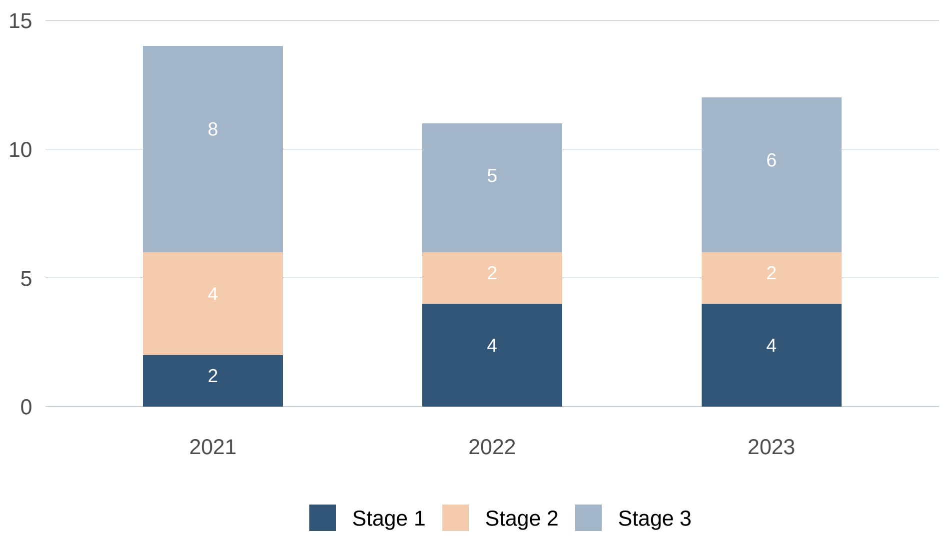


Figure 4.21: ECL to gross carrying amount - Stage 1

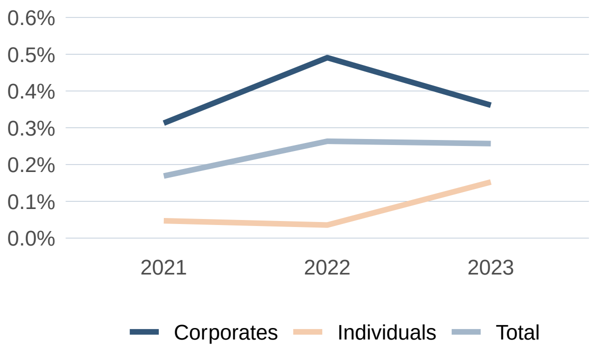


Figure 4.22: ECL to gross carrying amount - Stage 2

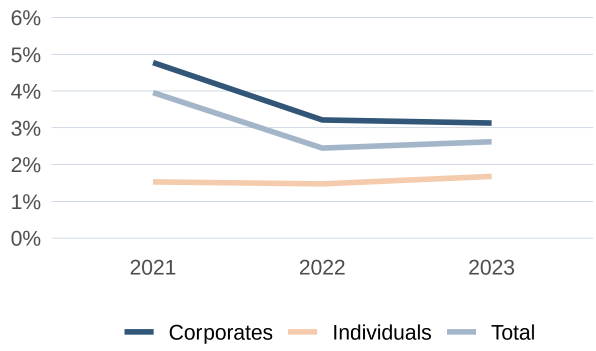


Figure 4.23: ECL to gross carrying amount - Stage 3

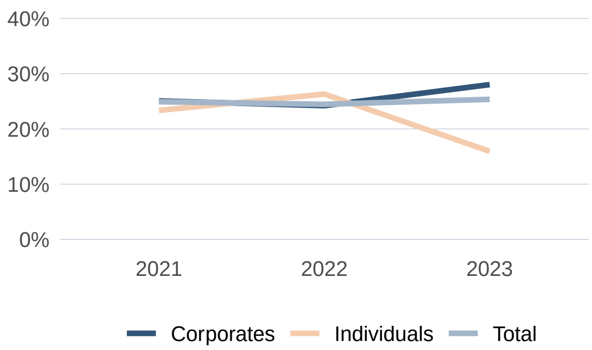
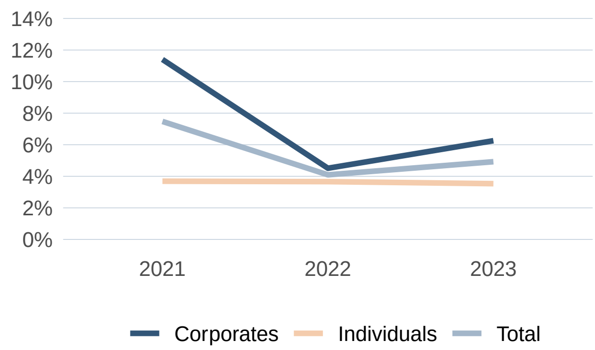


Figure 4.24: Gross carrying amount in stage 2



4.3 Credit concentration risk

Credit concentration risk includes (i) single name concentrations of large (connected) individual counterparties and (ii) significant exposures to groups of counterparties whose likelihood of default is driven by common underlying factors, e.g. sector, economy, geographical location, instrument type, or other.

Limit management for single name and segment concentrations is set, monitored and managed through the Bank's risk appetite and its limit management structure. The Bank's risk profile for concentration risk is reported monthly to the Executive Committee and the Board of Directors according to internal guidelines.

The Bank uses the identification of concentration risk in the credit portfolio as a credit risk management parameter. Concentration risk arises in the credit portfolio as an inevitable consequence of the Bank's business strategy. Concentration risk is credit risk related to the degree of diversification in the credit portfolio and includes both single name concentration risk and segment concentration risk.

According to CRR, exposures to a single customer or a group of related customers – after the deduction of particularly secure claims – may not exceed 25% of common equity tier 1 (CET1) capital. No exposure to a single customer or a group of related customers exceeded 25% in the year 2023 and, at year end, the largest single-customer exposure was well below 25%.

The Bank's risk profile for large exposures is monitored daily by Risk Management and reported monthly to Managing Directors and the Board of Directors.

As for single name concentration, the Bank's Board of Directors sets portfolio limits for segment concentration in the Bank's risk appetite.

At year-end 2023, lending to individuals represented 50% of the Bank's total credit exposure (2022: 51%). Most of the demand from individuals is for mortgages, and the Bank's lending to individuals is therefore mostly secured by real estate.

The Bank's credit exposures are primarily to Icelandic corporate customers. Companies in the fisheries, real estate, travel and construction sectors represent the largest exposure to single sectors.

Customers domiciled in Iceland accounted for 95% of the Bank's total credit exposure in 2023 (2022: 96%), excluding exposures to financial institutions. The majority of exposures to foreign counterparties relate to management of the Bank's foreign liquidity reserves and are classified as loans and advances to financial institutions.

The Bank estimates sector concentration risk as the difference between sector concentration for Iceland and the sector concentration in the Bank's portfolio. Figure 4.27 shows a comparison of industry concentration between the Bank's portfolio and the portfolios of all Icelandic banks. Data for Iceland is from the CBI. Note that this sector classification includes the travel industry as part of the services sector.

Figure 4.25: Exposures between 10% and 20% of Tier 1 capital

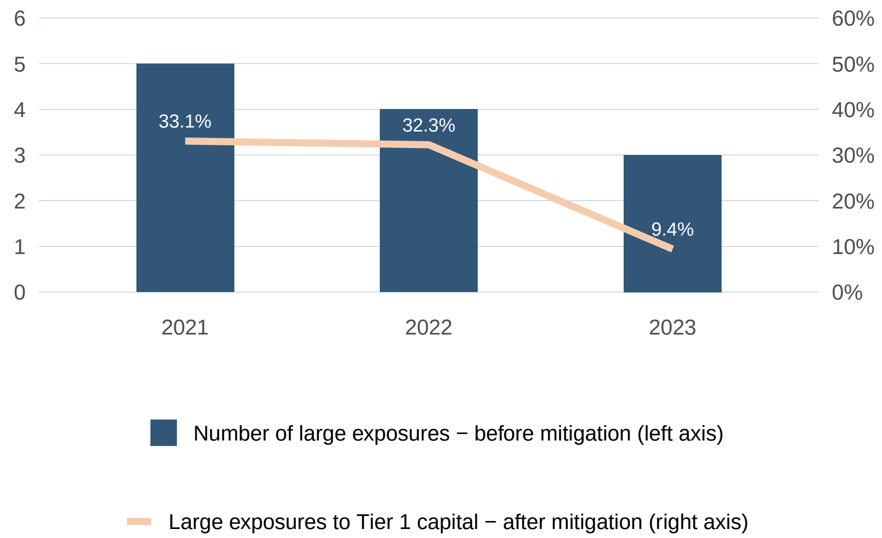


Figure 4.26: Loans and advances by geographical area (ISK bn)

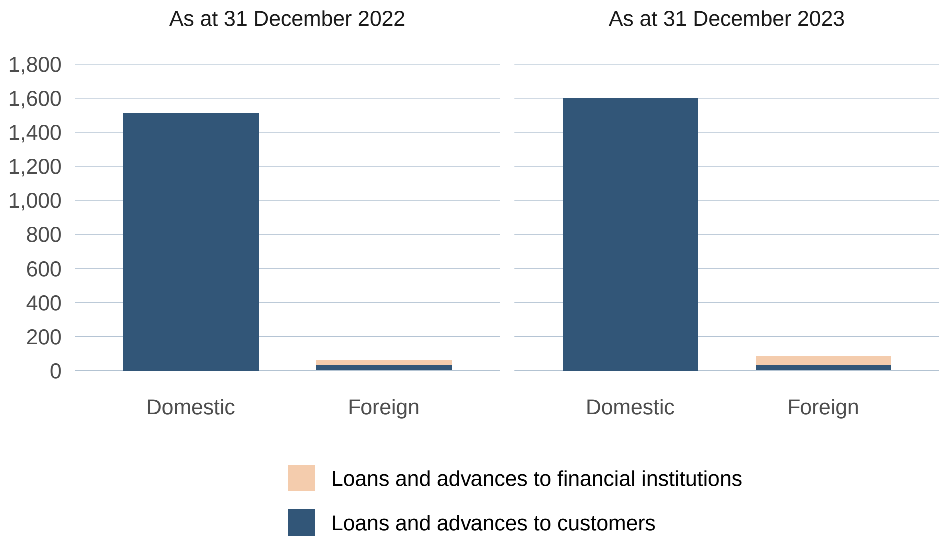
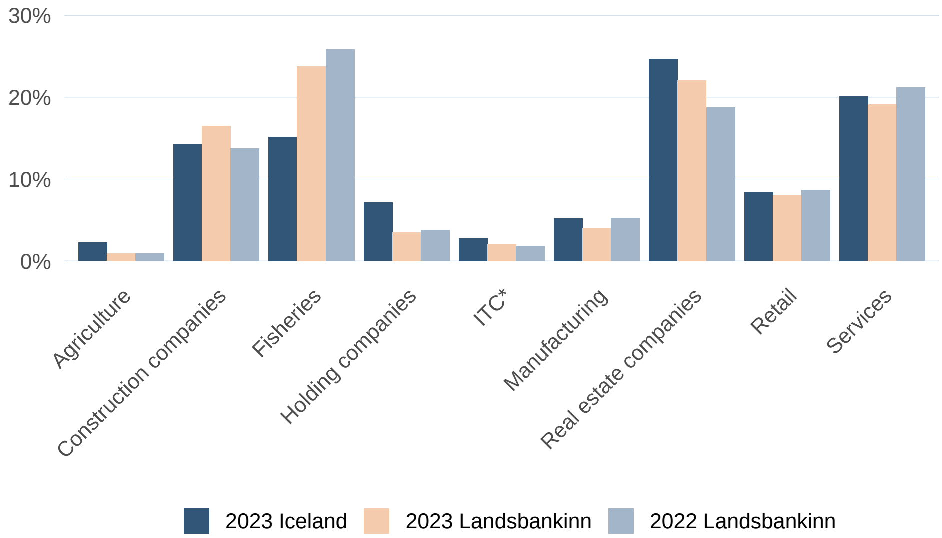


Figure 4.27: Industry concentration



*ITC consists of corporations in the information, technology and communication sectors

5 Market risk

Market risk

Market risk is the risk that changes in market prices will adversely impact the fair value of future cash flows of financial instruments. Market risk arises from open positions in currency, equities and interest rate products, all of which are exposed to general and specific market movements and changing volatility levels in market rates and prices, for instance in interest rates, inflation, foreign exchange rates and equity prices. Credit Valuation Adjustment (CVA), an adjustment to the fair value of derivative instruments to account for counterparty credit risk, also belongs to market risk.

- The Bank's market risk has fluctuated somewhat this year yet measures slightly lower at year-end 2023, or 1.6%, compared to 1.7% at year-end 2022, measured as the ratio of risk-weighted assets to total RWEA.
- The most significant change in market risk from year-end 2022 was due to a lower net FX balance at year-end 2023. Exposure in the equity trading book rose steadily from the second quarter and was higher at year-end 2023 than at year-end 2022. Interest rate risk in the trading book fluctuated over the year but was unchanged between year-end 2022 and 2023.
- Despite unstable market conditions this year, the Bank has effectively managed its market risk, which has remained comfortably within the defined risk appetite.

5.1 Market risk management and policy

The Board of Directors is responsible for determining the Bank's market risk appetite. The CEO and the Risk & Finance Committee are responsible for developing market risk management policies and procedures and setting market risk limits. Market risk is managed centrally by Treasury as well as within trading units, in accordance with the Bank's policies, limits and risk appetite. Together, the risk appetite of the Bank and the market risk policies set the overall limits for market risk management within the Bank in accordance with the Bank's three lines of defence principle.

The Bank separates its exposure to market risk into trading and non-trading portfolios, managing each separately. Trading portfolios include positions arising from market making, derivative sales and proprietary position taking. Non-trading portfolios include positions arising from the Bank's retail and commercial banking operations, proprietary position taking as part of asset and liability management, and funding transactions, managed by Treasury. Treasury is also responsible for daily liquidity management, which entails exposure to market risk.

Market risk mitigation reflects the Bank's overall risk appetite by identifying the target level for market risk factors and limiting exposure in line with the Bank's risk appetite. Other market risk mitigation plans are made on a case-by-case basis involving hedging strategies and risk reduction through diversification.

5.2 Control and monitoring

The aim of the market risk management process is to ensure that market risk levels are within the Bank's risk appetite and to mitigate the risk of loss while maintaining acceptable profitability. This entails quickly detecting and correcting deficiencies in compliance to policies, processes and procedures along with limit monitoring, handling limit breaches, risk modelling and reporting. The Bank monitors various indicators that can provide warning of an increased risk of future loss. Market risk indicators need to be concise, reported in a timely manner, give clear signals, highlight portfolio risk concentrations and reflect current risk positions. Risk reports show the Bank's total risk in addition to summarising risk concentration in different business units and asset classes, as well as across other attributes, as appropriate, pursuant to the Bank's activities.

Market risk arising from trading and non-trading activities is measured, monitored and reported on a daily, weekly and monthly basis. The market risk limits set by the Risk & Finance Committee are monitored by Market Risk, and exceptions and breaches of limits are reported on a regular basis to the Risk & Finance Committee and other relevant parties as necessary. Additional summarised reports highlighting market risk, risk appetite measurements and any concerns regarding market risk are sent to the Board of Directors on a regular basis.

5.3 Market risk exposure

Table 5.1 summarises the Bank's exposure to market risk at year-end 2023.

The Bank also faces counterparty credit risk arising from derivative contracts and securities financing transactions with customers and financial institutions. Counterparty credit risk is, however, very low compared to other credit risk and is mitigated through strict collateral requirements and limits. Further information about the Bank's exposure to counterparty credit risk can be found in the additional disclosures accompanying this document (see also 4.1.4.1).

Table 5.1: Total net exposure subject to market risk

	Net position at year-end	
	2023	**2022**
Equities and equity instruments in the trading book	2,605	2,146
Bonds and debt instruments in the trading book	14,447	15,715
FX balance	3,034	7,041
CVA risk exposure value	10,584	5,834

5.3.1 Banking book exposures

The banking book exposures of the Bank pertaining to market risk are exposures in equities and bonds. The equities are both unlisted and listed and are, in part, legacy positions obtained through corporate restructuring, or acquired when the Bank was established in 2008. The bond holdings in the banking book are comprised of strategic investments and liquidity management instruments. Capital reserved against these exposures is classified as credit risk.

5.4 Measuring market risk

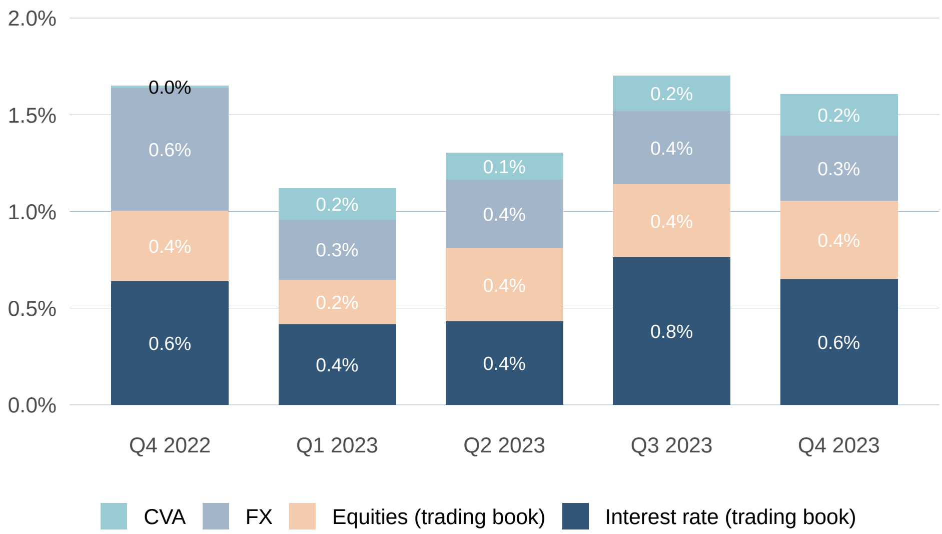
The Bank uses risk-weighted exposure amounts (RWEA) and economic capital (EC) as a common denominator for measuring risk across different asset classes, including those assets subject to market risk. RWEAs are determined by applying specific risk weights to the Bank's assets, according to capital requirement regulations. Several other indicators are used as measures of market risk as well, including value-at-risk (VaR), profit and loss analysis, delta positions and net positions across different attributes such as the currency and issuer. These risk measurements are supplemented by specific stress tests and scenario analyses as appropriate, taking the Bank's balance sheet composition and operating environment into account.

Total market risk, measured as the ratio of risk exposure amounts to total RWEA, was moderate, amounting to 1.6% at year-end 2023 (compared to 1.7% at year-end 2022), and well within the Bank's risk appetite.

Table 5.2: Total market risk (RWEA measure) at year-end

	2023		2022	
	RWEA	Ratio to RWEA	RWEA	Ratio to RWEA
Equity price risk in the trading book	5,219	0.4%	4,322	0.4%
Interest rate risk in the trading book	8,283	0.6%	7,587	0.6%
Foreign exchange risk	4,303	0.3%	7,562	0.6%
CVA risk	2,753	0.2%	147	0.0%
Total	**20,559**	**1.6%**	**19,618**	**1.7%**

Figure 5.1: Total market risk (ratio to total RWEA)



5.4.1 Equity price risk in the trading book

Equity price risk is the risk of equity value fluctuations due to open positions in equity-based instruments. The Bank's equity trading portfolio is comprised of proprietary trading positions and exposures from market making, including equity derivatives and hedging positions. All equity-based derivative contracts are usually fully hedged with regard to market risk and are subject to various, strict limit requirements.

5.4.2 Interest rate risk in the trading book

Interest rate risk is the risk of loss arising from the impact of adverse changes in market interest rates. The Bank's trading portfolios contain exposures due to market making and proprietary trading, highly concentrated on government-guaranteed bills/bonds, as well as covered bonds and fixed income derivatives. As with equity-based derivatives, all fixed income derivative contracts are usually fully hedged with regards to market risk and are subject to strict limit requirements.

5.4.3 Interest rate risk in the banking book

Interest rate risk in the banking book is the current or prospective risk to earnings and capital arising from adverse movements in interest rates. Changes in interest rates on the Bank's assets and liabilities impact its interest rate margin and/or the value of its equity. This risk is primarily the result of duration mismatch of assets and liabilities. Net positions of assets and liabilities in the banking book by the interest rate fixing period, at year-end 2023 and 2022, are shown in Table 5.3.

Table 5.3: Assets and liabilities in the banking book by interest rate fixing period

	Net position at year-end 2023				
	Up to 3 M	**3-12 M**	**1-5 Y**	**Over 5 Y**	**Total**
Total assets	1,310,081	261,452	329,297	20,419	1,921,249
Total liabilities	1,150,261	107,856	357,649	10,108	1,625,874
Net on-balance sheet position	159,821	153,596	-28,352	10,311	295,375
Effect of derivatives held for risk management	-90,054	0	90,054	0	0
Net off-balance sheet position	2,000	0	-2,000	0	0
Total interest repricing gap	**71,767**	**153,596**	**59,702**	**10,311**	**295,375**
	Net position at year-end 2022				
	Up to 3 M	**3-12 M**	**1-5 Y**	**Over 5 Y**	**Total**
Total assets	1,187,494	153,272	381,841	26,823	1,749,430
Total liabilities	1,041,946	118,767	259,455	64,137	1,484,306
Net on-balance sheet position	145,548	34,505	122,386	-37,314	265,124
Effect of derivatives held for risk management	-45,450	45,450	0	0	0
Net off-balance sheet position	2,000	0	-2,000	0	0
Total interest repricing gap	**102,098**	**79,955**	**120,386**	**-37,314**	**265,124**

The Bank employs a monthly stress test of the interest rate risk in the banking book by measuring the impact of shifting the relevant interest rates for every currency on the fair value of all interest-rate sensitive assets and liabilities in the banking book.

Table 5.4 summarises the sensitivity of the Bank's banking book fair value resulting from a flat 100 bp upward and downward shift of all yield curves at year end.

Table 5.4: Interest rate risk (fair value sensitivity) in the banking book at year-end

	2023		**2022**	
	+100 bps	**-100 bps**	**+100 bps**	**-100 bps**
ISK non-indexed	-4,141	4,405	-5,256	5,574
ISK indexed	1,629	-1,651	2,328	-2,458
EUR	1,089	-1,109	3,242	-3,355
SEK	4	-3	14	-14
USD	20	-20	-63	64
Other	23	-23	8	-8
Total	**-1,376**	**1,599**	**273**	**-197**

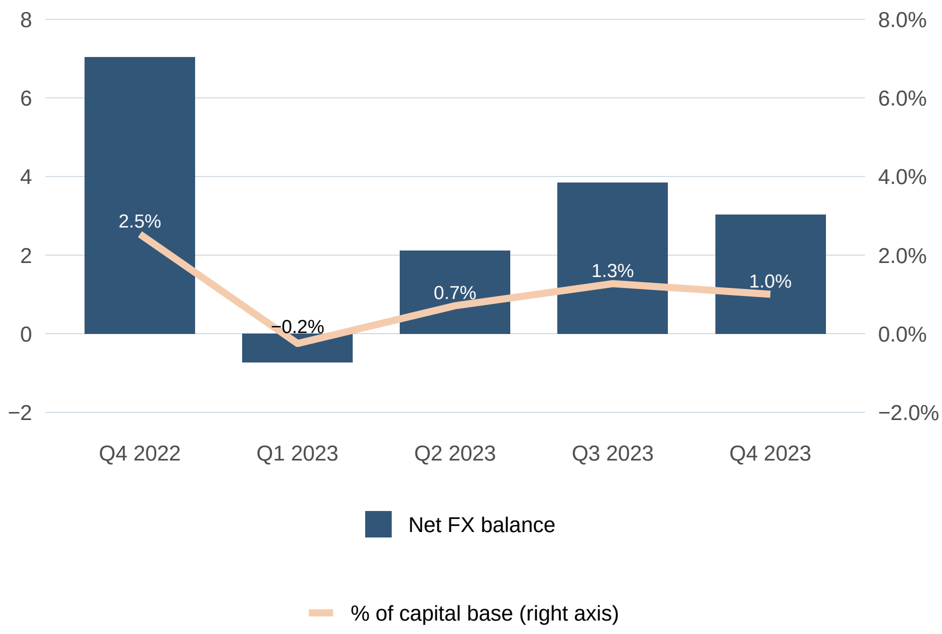
5.4.4 Foreign exchange risk

Foreign exchange risk (FX risk) is the risk of loss due to exchange rate fluctuations. Foreign exchange risk within the Bank may arise from holding assets in one currency and liabilities in another, from a spot or forward foreign exchange trade, currency swaps or other currency contracts that are not matched with an offsetting contract. The net FX balance at year-end 2023 and 2022 can be seen in Table 5.5.

Table 5.5: Net FX balance

	Net position at year-end	
	2023	**2022**
EUR	2,777	4,396
GBP	523	746
USD	-456	915
NOK	271	494
SEK	104	293
Other	-185	196
Total	**3,034**	**7,041**

Figure 5.2: Net FX balance (ISK bn)



5.4.5 Other market risk

Other market risk within the Bank is comprised of indexation risk and risk due to credit valuation adjustment (CVA).

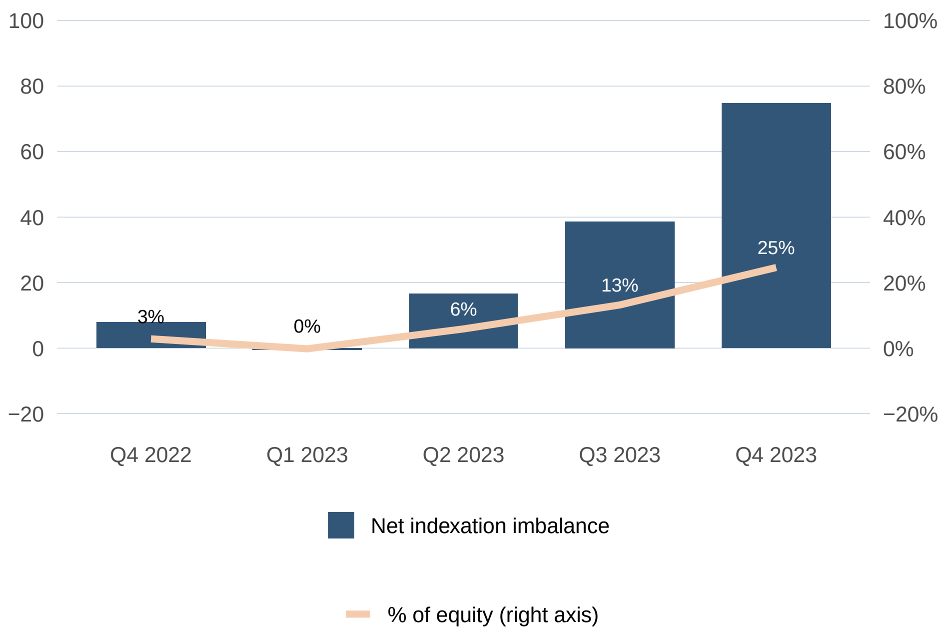
CVA is an adjustment to the fair value (or price) of derivative instruments to account for counterparty credit risk. CVA risk increased in the 2023 due to interest rate swap agreements that the Bank entered into. The Bank's derivative contracts that entail CVA risk are well collateralised, which reduces CVA risk. As a result, the Bank's CVA risk is considered immaterial.

Indexation risk is the risk that the fair value or future cash flows of CPI linked financial instruments may fluctuate due to changes in the Icelandic CPI. Mismatched CPI-linked assets and liabilities expose the

Bank to indexation risk. The Bank's total CPI indexation balance was ISK 75 billion at year-end 2023 as compared to ISK 8 billion at year-end 2022. The Bank's target is to keep the ratio below 80% of equity.

The balance increased rapidly over the past year, with loans and advances to customers growing by ISK 100 billion between year-end 2022 and 2023. Around ISK 64 billion thereof are from CPI-linked mortgages. CPI-linked borrowing increased by ISK 12 billion in 2023, subordinated liabilities by ISK 14 billion and customer deposits by ISK 19 billion. The most significant change to the balance occurred in the fourth quarter. Further information about the Bank's market risk can be found in template MR1 in the additional disclosures accompanying this report.

Figure 5.3: Indexation imbalance



6 Liquidity risk

Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting its financial liability obligations with cash or other financial assets or having to do so at excessive cost. This risk arises from earlier maturities of financial liabilities than financial assets.

- Liquidity risk is identified as one of the Bank's key risk factors and emphasis is placed on liquidity risk management within the Bank, which is reflected in both its risk appetite as well as in internal liquidity management policies and rules. The Bank's policy remains to sustain a strong liquidity position in the near- and longer-term as is reflected in the Bank's business plan.
- The Bank's liquidity position at year-end 2023 was well above regulatory requirements and the Bank's internal limits. The total liquidity coverage ratio was 181% at year-end 2023 (year-end 2022: 134%), the Bank's LCR in EUR was 1,499% (year-end 2022: 351%) and 129% in ISK (year-end 2022: 99%).
- The largest part of the Bank's funding is in the form of deposits from customers, which increased by ISK 81 billion in 2023 and amounted to ISK 1,049 billion at year end.
- In 2023, the Bank issued European Covered Bonds (Premium) in euros, the first from an Icelandic bank, in the amount of EUR 300 million for 5 years. The bond issuance further increased the Bank's funding sources.

6.1 Identification

The Board sets a liquidity management policy and the liquidity contingency plan for the Bank. Liquidity risk management refers to the internal policies and procedures containing quantitative and qualitative objectives, limits and reporting put in place. The policy describes how the Bank identifies, evaluates, measures, monitors, manages and reports its liquidity. The policy clearly outlines the structure, responsibilities and controls for managing liquidity risk within the Bank. The contingency plan provides a framework for detecting an upcoming liquidity event with predefined early warnings and actions for preventing temporary or longer-term liquidity disruptions.

6.2 Assessment

The Bank measures two key indicators, LCR and NSFR, to monitor and manage short-term liquidity risk and medium to long-term liquidity risk, respectively.

6.2.1 Liquidity coverage ratio

The Bank measures the liquidity coverage ratio (LCR) as a key indicator for short-term liquidity. The objective of the ratio is to promote short-term resilience by ensuring that the Bank has sufficient high-quality liquid assets to withstand a significant stress scenario lasting 30 calendar days. Quantitative information on the Bank's LCR at year-end 2023 can be found in the additional disclosures accompanying this document.

Table 6.1 shows the Bank's deposit base at year-end 2023. Run-off rates are used to estimate deposit outflows under stressed conditions for the next 30 calendar days and are set according to liquidity rules No. 266/2017. Figure 6.1 and Figure 6.2 show further breakdown of the Bank's deposit base.

Table 6.1: Total deposits by groups

As at 31 December 2023	Run off rate	0-30 days	Over 30 days	Guaranteed	Unguaranteed	Total
Individuals	5-100%	423,132	153,040	430,170	146,002	576,172
Small and medium sized corporates	5-100%	94,770	11,511	61,717	44,565	106,281
Operational deposits	5-25%	0	0	0	0	0
Large corporates	20-40%	174,958	57,620	12,238	220,341	232,578
Public entities	20-40%	51,204	6,608	0	57,812	57,812
Financial customers	100%	33,782	52,468	0	86,250	86,250
Pledged deposits		18,201	1,211	2,742	16,671	19,412
Total deposits		**796,047**	**282,458**	**506,866**	**571,640**	**1,078,506**

Figure 6.1: Total deposits by maturity

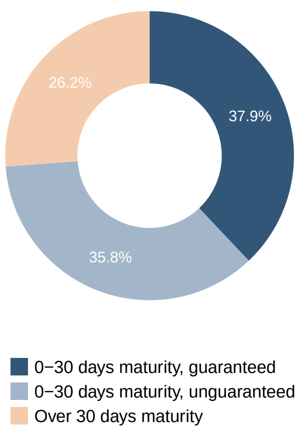
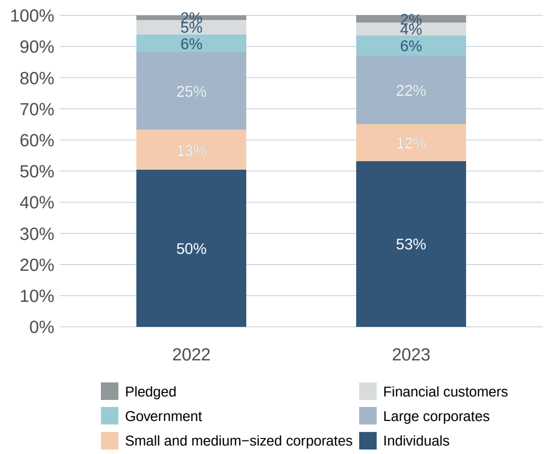


Figure 6.2: 0-30 days maturity deposits by groups*



*According to the Central Bank's Rules on Liquidity Coverage Requirements.

On January 1, 2023, new rules on the liquidity ratio of credit institutions no. 1520/2022, which introduced a minimum liquidity ratio in euros, 80%, for credit institutions that have 10% or more of their liabilities in euros. At the same time, a special minimum was imposed on other foreign currencies in total. Figure 6.4 shows the development of the Bank's LCR in EUR.

Figure 6.3: Liquidity coverage ratio (total)

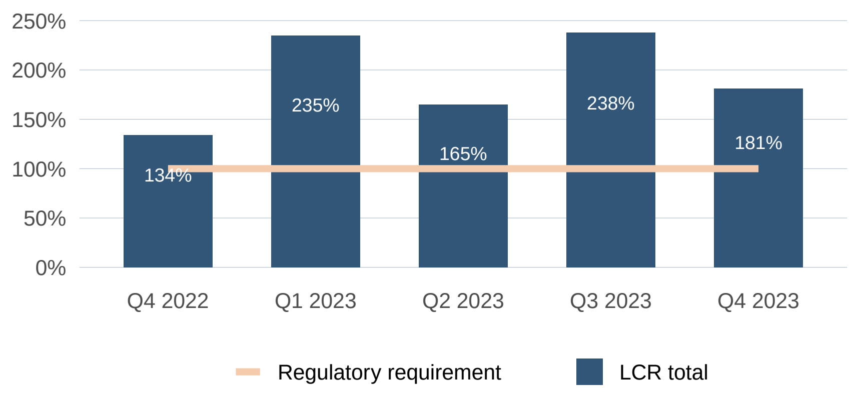


Figure 6.4: Liquidity coverage ratio (EUR)

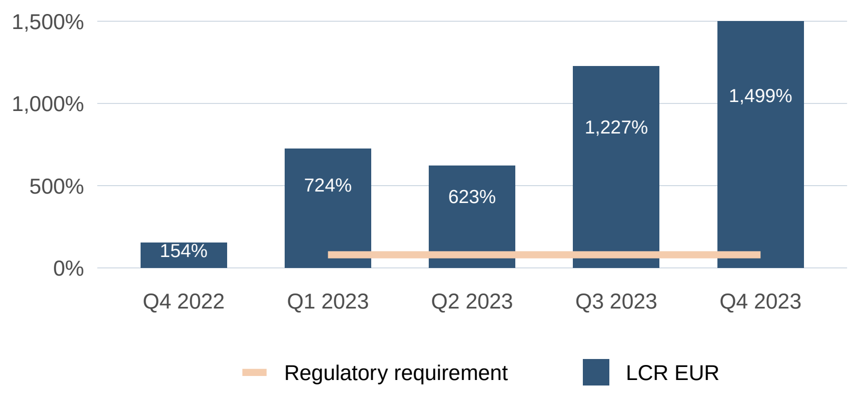
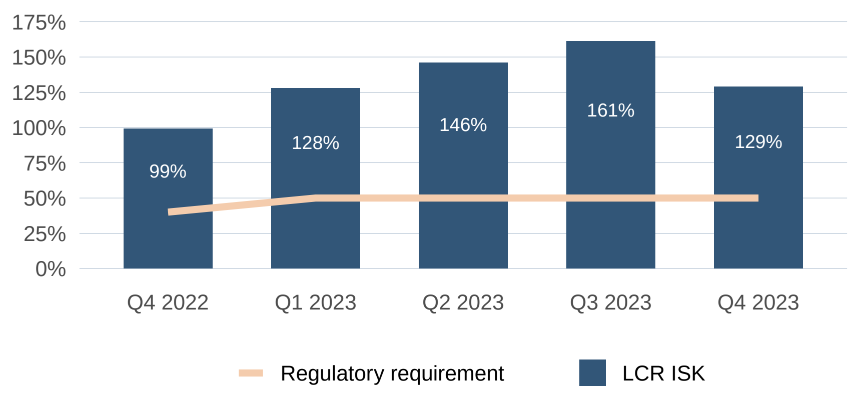


Figure 6.5: Liquidity coverage ratio (ISK)



6.2.2 Net stable funding ratio

The net stable funding ratio (NSFR) has a longer time horizon. Its objective is to capture structural issues in the balance sheet with the aim to provide a sustainable maturity structure of assets and liabilities. The aim of NSFR is to promote more medium and long-term funding. It establishes a minimum acceptable amount of stable funding based on the Bank's liquidity risk profile and limits over-reliance on short-term wholesale funding.

NSFR is defined as the ratio between the amount of available stable funding to the amount of required stable funding. Available stable funding is defined as the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR. The amount of such stable funding required of the Bank is a function of the liquidity characteristics and residual maturities of the various assets held by the institution, as well as those of its off-balance sheet (OBS) exposures. The Bank's total NSFR was 123% at year end (year-end 2022: 117%), and the NSFR in foreign currencies was 145% (year-end 2022: 132%).

Figure 6.6: Net stable funding ratio (total)

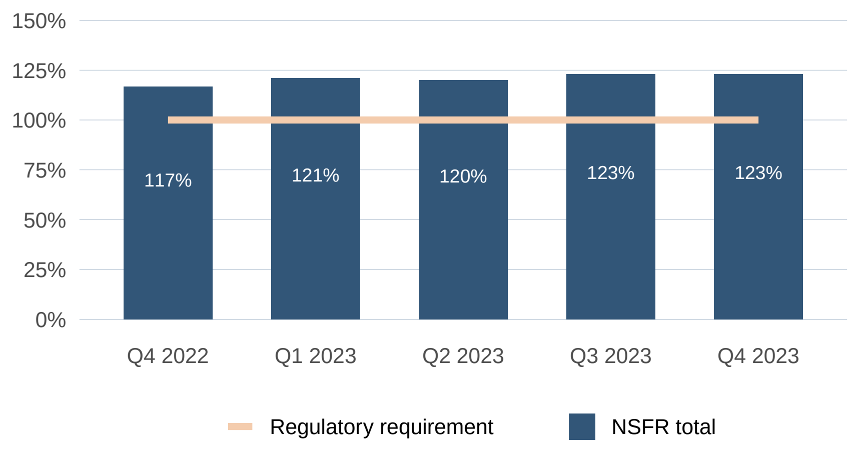
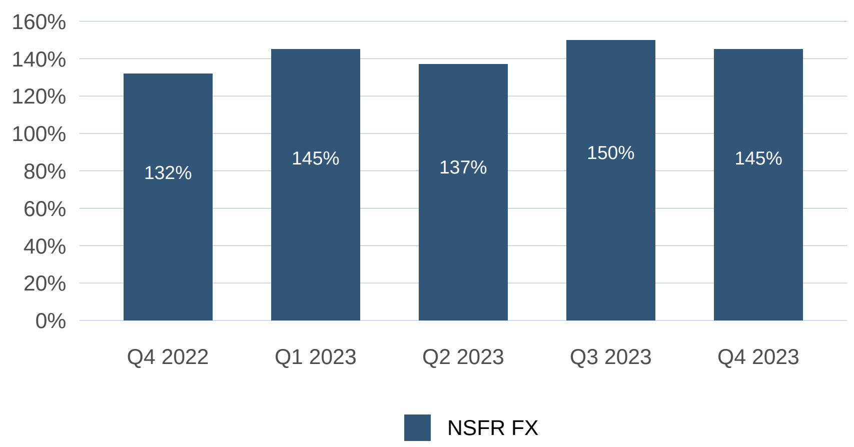


Figure 6.7: Net stable funding ratio (FX)



6.3 Management

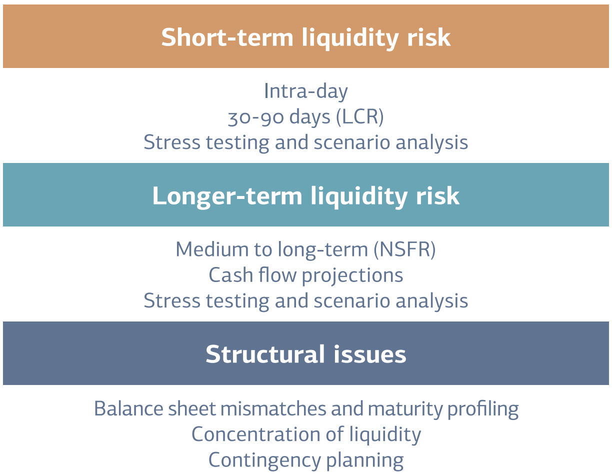
The objective of the liquidity management policy is to ensure that sufficient liquid assets and funding are available to meet financial obligations and sustain withdrawals of deposits in a timely manner and at a reasonable cost, even under stressed conditions.

The policy aims to ensure that the Bank does this by maintaining an adequate level of unencumbered, high-quality liquid assets that can readily be converted into cash. The Bank has also implemented stringent stress tests that have a realistic basis in the Bank's operating environment to further measure the Bank's ability to withstand different and adverse scenarios of stressed operating environments.

The Bank's liquidity risk is managed centrally by Treasury and is monitored and reported by Market Risk, allowing management to monitor and manage liquidity risk throughout the Bank. The Risk & Finance Committee monitors the Bank's liquidity risk, while the Bank's Internal Audit function assesses whether the liquidity management process is designed properly and is operating effectively.

The Bank's liquidity management process entails procedures, measurements, monitoring and reporting of both short-term and longer-term liquidity risk as well as structural issues in the balance sheet. An integral part of the management process is conducting forward-looking analysis to estimate future liquidity position, taking the Bank's commitments into account.

Figure 6.8: Liquidity management process



6.4 Control and monitoring

The Bank's Treasury department is responsible for day-to-day liquidity management, which entails closely monitoring current trends and potential market developments that may present significant and complex challenges for the Bank's liquidity strategy.

Liquidity risk is primarily controlled through limits set in the Bank's risk appetite and the Bank's liquidity management policy. Limit management is supplemented by regular monitoring and reporting of liquidity position under normal and stressed business conditions.

The Market Risk department regularly evaluates the Bank's liquidity position and monitors internal and external events and factors that may affect the liquidity position.

6.4.1 Liquidity Contingency Plan

The Bank has a contingency plan in place, which is set to provide a framework for detecting an upcoming liquidity event with predefined early warning indicators and actions for preventing temporary or longer-term liquidity disruptions.

The Liquidity Contingency Plan stipulates the actions that shall be taken to monitor the likelihood or imminence of the occurrence of a liquidity event or a confidence crisis. It also includes a detailed action plan and procedures for managing a liquidity event along with various management actions aimed at resolving liquidity disruptions.

The contingency plan is supplemented by the monitoring of early warning indicators along with their defined warning and trigger levels to detect potential liquidity problems. These early warning indicators are either internal, such as changes in the Bank's balance sheet composition, decreasing liquidity ratios, deposit outflows or a downward trend in financial ratios, or external, such as rating downgrades, third party evaluations or market price fluctuations. The Bank determines up to four levels of stress for each early warning indicator. These four levels of stress are risk alert levels, and each level further indicates the increasing likelihood of funds leaving and increased likelihood of a liquidity event. The indicators are monitored weekly by the Risk & Finance Committee and reviewed at least annually by the Board of Directors.

6.5 Funding profile

The Bank is an active issuer on the domestic bond market with issuance of covered bonds each month in the year 2023 and was also active in the international market with a number of issuances of bonds in foreign currencies under its EMTN and Covered Bond Programme throughout the year.

The Bank's credit rating is at BBB/A-2 and with a positive outlook as of November 2023.

The Bank's covered bond program has been rated by S&P Global Ratings since January 2021. In November 2023 the covered bond rating was raised to A+ with a stable outlook.

6.5.1 Funding

The Bank's funding rests on three main pillars. Deposits from customers are the Bank's primary funding source but the Bank is also funded through borrowing in the form of bond issuance, both in the international markets in foreign currencies as well as in the domestic market in ISK. Furthermore, the Bank is funded with contributions from owners in the form of equity. Figure 6.9 shows the breakdown of the Bank's borrowings while Figure 6.10 shows the Bank's funding structure as of year-end 2023 and 2022.

Figure 6.9: Borrowings and subordinated liabilities (ISK bn)

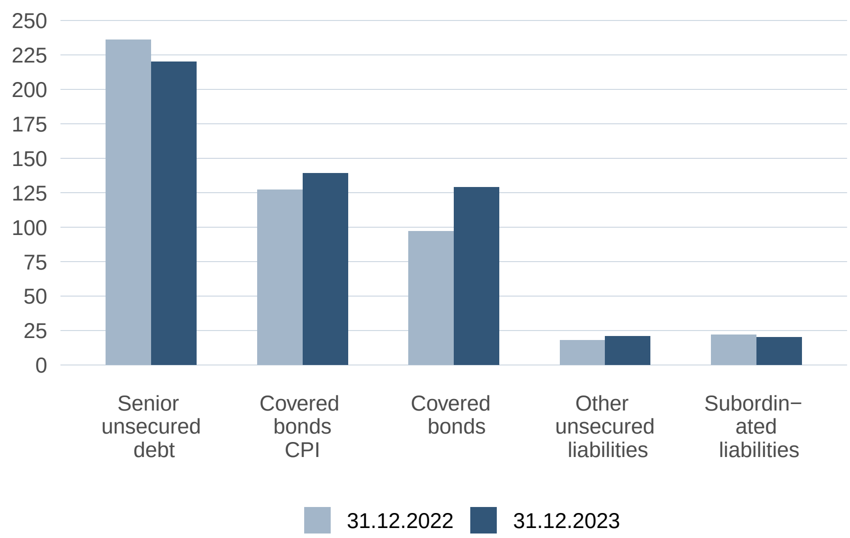
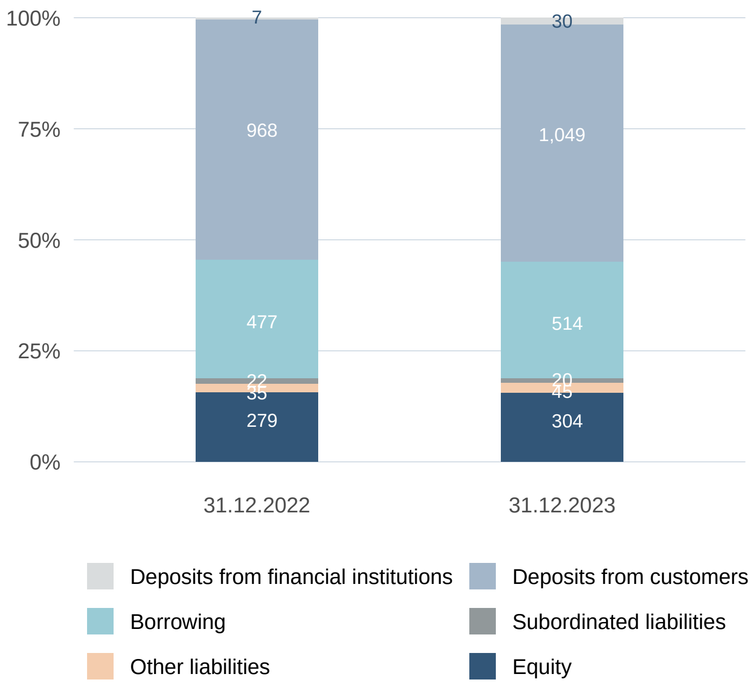


Figure 6.10: Funding profile (ISK bn)



6.5.2 Deposits from customers

The largest part of the Bank's funding is in the form of deposits from customers, which increased by ISK 81 billion in 2023 and amounted to ISK 1,049 billion at year end. Inflation-linked deposits amounted to ISK 180 billion at year-end 2023, increasing by ISK 19 billion from previous year.

6.5.3 Borrowings

6.5.3.1 EMTN Programme and other unsecured loans

Unsecured bond issuance in foreign currencies is the most important pillar in the Bank's market funding.

In January 2023, the Bank signed an agreement with Nordic Investment Bank (NIB), providing for a USD 40 million loan relating to the Bank's new headquarters.

In August, the bank issued 2-year bonds in the amount of NOK 1,000 million and SEK 450 million.

The Bank issued green 3.5-year bond for EUR 300 million in September. The bond was the Bank's third green bond issuance in euros. In conjunction with the issuance the Bank offered to tender outstanding bonds maturing in May 2024 resulting in a buyback of EUR 132 million.

A loan agreement with NIB was finalised in December amounting to USD 75 million for seven years.

At year-end 2023, unsecured bond issuance in foreign currency amounted to ISK 241 billion, increasing by ISK 13 billion during the year.

Table 6.2: EMTN Programme

As at 31 December 2023	Currency	Final maturity	Outstanding principal	Contractual interest rate
Senior unsecured				
LBANK FLOAT 01/24	SEK	19.01.2024	850	STIBOR + 0.65%
LBANK 0.5 5/24	EUR	20.05.2024	168	FIXED 0.5%
LBANK FLOAT 08/24	NOK	12.08.2024	300	NIBOR + 2.0%
LBANK FLOAT 01/25	NOK	20.01.2025	500	NIBOR + 0.79%
LBANK FLOAT 01/25	SEK	20.01.2025	850	STIBOR + 0.80%
LBANK 0.375 5/25	EUR	23.05.2025	300	FIXED 0.375%
LBANK FLOAT 08/25	NOK	18.08.2025	350	NIBOR + 2.35%
LBANK FLOAT 08/25	NOK	21.08.2025	1,000	NIBOR + 3.05%
LBANK FLOAT 08/25	SEK	25.08.2025	450	STIBOR + 3.5%
LBANK 0.75 5/26	EUR	25.05.2026	300	FIXED 0.75%
LBANK 6.375 3/27	EUR	12.07.2027	300	FIXED 6.375%
Subordinated				
LBANK T2I 29	ISK	11.12.2029	5,500	FIXED 3.85%, CPI-indexed
LBANK T2I 33	ISK	23.03.2033	12,000	FIXED 4.95%, CPI-indexed

6.5.3.2 Covered bonds

The size of the programme for covered bond issuance is EUR 2,500 million and was increased from ISK 250 billion in 2022. The programme was updated in 2022 to allow for covered bond issuance in foreign currency under the programme in addition to its listing on the Irish stock exchange, Euronext Dublin.

In March, the Bank issued European Covered Bonds (Premium) in euros, the first from an Icelandic bank, in the amount of EUR 300 million for 5 years. The bond issuance increased further the Bank's funding sources.

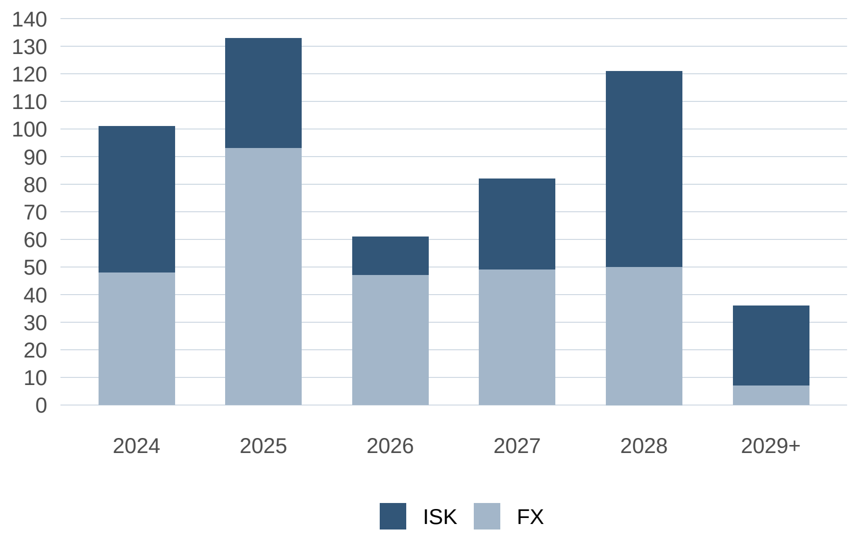
Regular auctions of covered bonds were held in 2023 where previously issued series were tapped and addition to issuance of a new non-indexed series, LBANK CB 29. The non-indexed series LBANK CB 23 matured in 2023. Agreements with market makers in the secondary market for covered bonds were renewed in the year.

At year-end 2023, outstanding covered bonds amounted to ISK 268 billion, increasing by ISK 45 billion during the year.

Table 6.3: Covered bonds

As at 31 December 2023	Currency	Final maturity	Outstanding principal	Contractual interest rate
Non-indexed				
LBANK CB 25	ISK	17.09.2025	39,660	3.40%
LBANK CB 27	ISK	20.09.2027	35,280	4.60%
LBANK CB 28	EUR	16.03.2028	47,945	4.25%
LBANK CB 29	ISK	27.09.2029	8,760	8.20%
Indexed				
LBANK CBI 24	ISK	15.11.2024	38,120	3.00%
LBANK CBI 26	ISK	20.11.2026	11,120	1.50%
LBANK CBI 28	ISK	04.10.2028	50,200	3.00%

Figure 6.11: Maturity profile (ISK bn)



6.5.3.3 Commerical paper

No commercial paper auctions were held in 2023 under the ISK 50 billion debt issuance programme. There was no outstanding issuance of commercial paper at year-end 2023.

6.5.3.4 Subordinated bond issuance

In March, the Bank issued subordinated bonds in the amount of ISK 12 billion for 10 years, callable in 5 years. The issuance counts as Tier 2 capital.

Call option on outstanding EUR 100 million subordinated bonds was exercised in September.

Subordinated bond issuance under the Bank's debt issuance programme amounted to ISK 20 billion at year-end, decreasing by ISK 2 billion from the previous year.

6.5.3.5 Equity

The Bank's equity amounted to ISK 304 billion at year-end 2023, increasing by ISK 25 billion over the course of the year. The Bank paid ISK 8,504 million in dividends to shareholders in 2023.

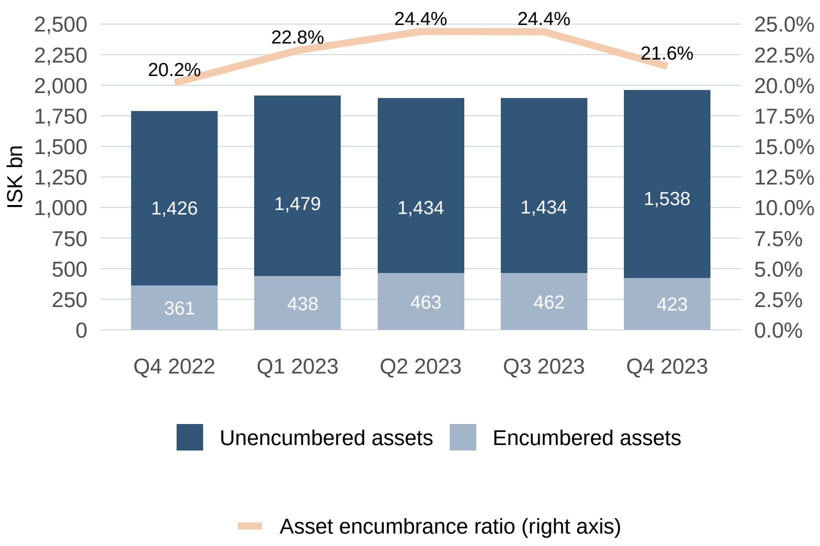
The Bank's total capital ratio was 23.6% at year-end 2023.

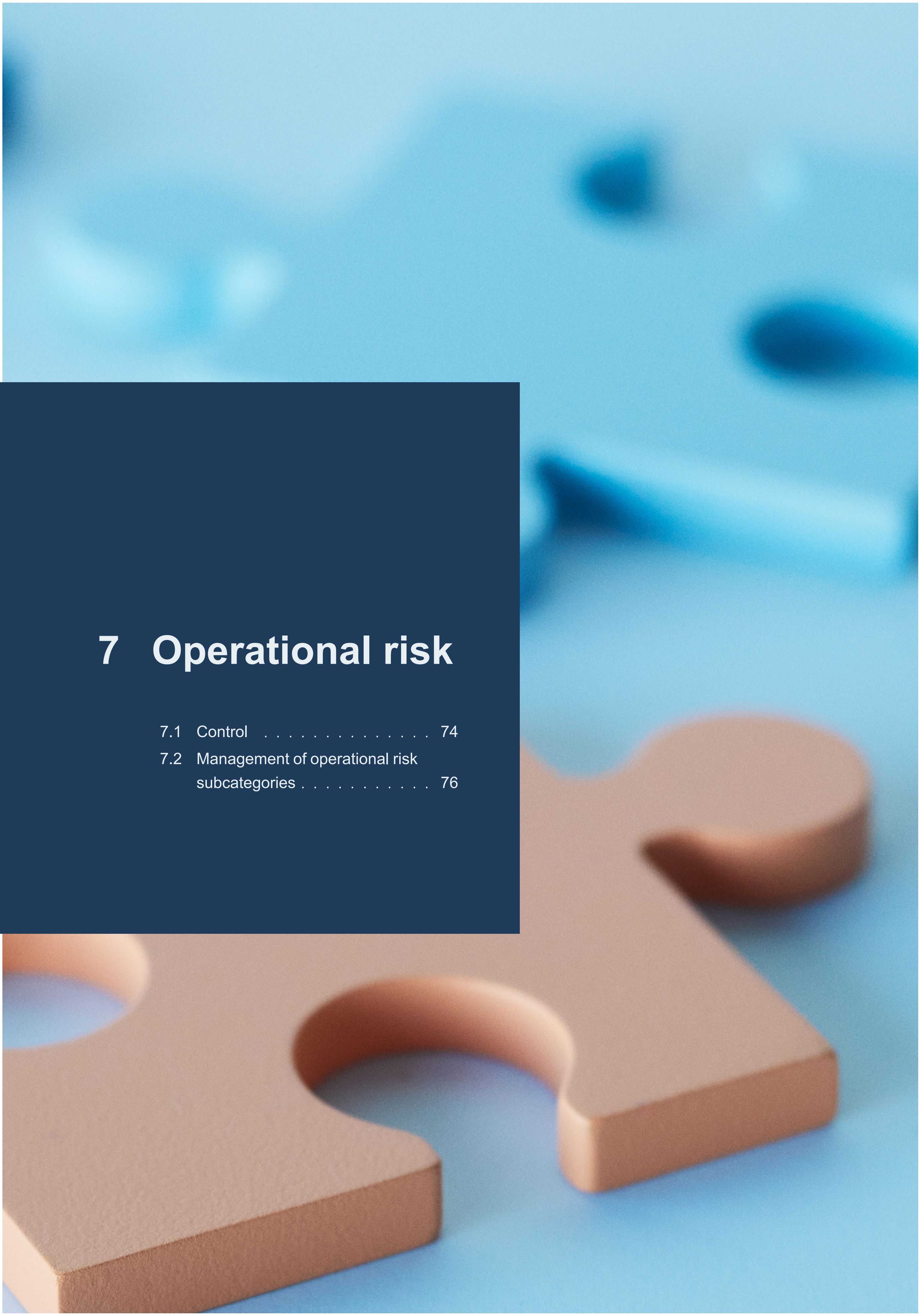
6.5.4 Asset encumbrance ratio

The Bank's liquidity and funding risk framework includes measures of encumbered assets as a ratio to total assets. Encumbered assets are primarily comprised of loans and advances which are pledged against covered bonds and secured bonds issued by the Bank. Other encumbered assets are pledged as collateral to the Central Bank, pledged as collateral to secure trading lines, and credit support for GMRA/ISDA master agreements and other pledges of similar nature. The Bank's asset encumbrance ratio remains low.

The Bank issues covered bonds in ISK and EUR for own use that can be sold later or used for securities lending and repurchase agreements. At year-end 2023, these bonds amounted to ISK 15 billion and EUR 250 million. Pledged assets against the bonds amounted to ISK 66 billion (2022: ISK 70.9 billion).

Figure 6.12: Asset encumbrance ratio





7 Operational risk

Operational risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

- The number of operational and loss incidents in 2023 was roughly equal compared to 2022.
- Continued emphasis on ICT risk by the Bank and regulators.

7.1 Control

The Bank is exposed to operational risk through its activities. Loss may result from inadequate or failed internal processes, people and systems, or from external events.

The Board of Directors sets the Bank's policy regarding operational risk and risk appetite. The policy outlines the roles and responsibilities of stakeholders within the Bank, and the operational risk tolerance in terms of limits. The Operational Risk Committee is responsible for overseeing all operational risk and for approving rules that fall within the remit of the Operational Risk Committee.

The Bank identifies the types of operational risk to which it is exposed in order to better understand its operational risk profile and assess its vulnerability to these risks. The aim is to identify and assess the operational risk inherent in all existing or new material products, activities, processes and systems. Effective operational risk identification and assessment processes are crucial in establishing a framework for operational risk monitoring and control.

Operational risk has been categorised by Landsbankinn into seven separate subcategories and responsibilities for managing the risks posed by them are divided between the Operational Risk department and the Compliance department.

Figure 7.1: Operational risk categories

Operational Risk Department	Compliance Department
ICT risk	**Compliance risk** is the exposure of the Bank to legal penalties and reputational damage if it fails to act in accordance with laws and regulations, internal policies and prescribed best practices.
Model risk	
Change management risk	
Physical security	**Conduct risk** involves the risk of financial loss due to human error, neglect or fraud in relation to the Bank's customers.
Outsourcing risk	

7.1.1 General methods to measure operational risk

In order to understand the effects of the exposures to operational risks in general, the Bank continually assesses its operational risk. A number of tools are used to identify and assess operational risk.

- Self-assessment. The Bank assesses its operations and activities against a menu of potential risk vulnerabilities. This is done annually, and more often if there are material changes in the operational risk environment in any particular business unit.
- Risk mapping. This process involves mapping all reported incidents by risk type and to business units.
- Risk assessments on important IT systems and as a part of project management.
- Key risk indicators (KRIs) are statistics and/or metrics, which can provide insight into the Bank's risk position.

In total there were 42 loss events in 2023. The category of execution, delivery and process management has the largest number of loss events; 38 in 2023, the next category 'External fraud' has 4 events.

The Bank categorises operational incidents into deviation from rules or processes, weakness in processes or systems, external circumstances, or security violations. The total number of incidents in 2023 was 195, 106 were due to transaction processing and 89 related to technology.

7.1.2 Mitigation

The Bank buys insurance to mitigate its operational risk. The insurance comprises of banker's comprehensive crime policy and cyber liability insurance policy.

Clear procedures are in place regarding the mitigating actions that result from self-assessment. There are separate procedures in place for how the Bank handles operational incidents and corrective and mitigating actions resulting from these incidents.

The architecture of the Bank's information systems is based on two mirrored data centres, primary and secondary, located in two different buildings linked with high-speed communication. This setup allows the Bank to run its core systems with access to mission critical data, even if one data centre (for instance the primary data centre) becomes unusable. In the event of a failure, core systems will automatically switch from one site (the failed one) to the other.

There are business continuity plans in place for all operations considered to be mission critical to the Bank. These plans are all tested on an annual basis, apart from the IT department's plan, which is tested more frequently.

7.1.3 Control and monitoring

Day-to-day management of operational risk is a part of every manager's responsibility, and they are further responsible for monitoring and controlling the operational risk in their departments. Managers evaluate operational risk through risk self-assessment, focusing on key risks identified with top-down management involvement.

Information security, physical security, education and training activities are important components of the management of operational risk, and close cooperation is maintained with the relevant departments involved in these processes. Internal Audit and Compliance are key functions in the framework that the Bank has established to monitor and control operational risk. The Bank is certified in accordance with ISO 27001, the international standard on information security.

Incident reporting, auditing and follow-up is an important part of operational risk management, as the identification and remedial action helps to limit losses resulting from inadequate and failed processes. The Operational Risk department is responsible for business continuity management and for overseeing the Bank's disaster recovery plans.

In identifying operational risk, the Bank examines both internal and external factors that could adversely affect its performance and prevent the achievement of its objectives, such as:

- Risk culture, human resource management practices, organisational changes, and employee turnover.
- The nature of the Bank's customers, products, contractors, and activities, including sources of business, distribution mechanisms and volume of transactions.
- The design, implementation, review and operation of the processes and systems involved in the operating cycle of the Bank's products and activities.
- The external operating environment and industry trends, including political, legal, technological, and economic factors, as well as the competitive environment and market structure.

Operational risk measurements are reported to the Board in a comprehensive manner as part of regular reporting.

7.2 Management of operational risk subcategories

7.2.1 ICT risk

The Bank manages ICT risk by minimising the risk of loss through breach of confidentiality, loss of integrity and/or unavailability of data and systems. The Bank's framework is based on an ISO 27001 certification, since 2007, and on adherence to Guidelines on ICT and security management by EBA. ICT risk includes the risk of breach of data confidentiality through attacking and exploiting vulnerabilities. Cyber defences are based on layered security. Every layer is monitored by more than one security system. A continuous vulnerability scan is performed by an external party. An internal scan is also performed on internal and external systems, associated ports, services and applications. Cultural awareness of cyber threats within the Bank is an important aspect and Workplace from Meta is used to share relevant material with employees. Finally, the Bank utilises knowledge from external parties, e.g. NF CERT, to gain insight into current threats with the aim to prevent them before they happen.

7.2.2 Conduct risk

The Bank manages conduct risk in accordance with its Operational Risk Policy. Based on the Policy, the Bank has set in place a variety of organisational and managerial actions, e.g.:

- Adopted suitable internal policies and procedures, e.g. Code of Conduct, Fraud Policy, Conflict of Interest Policy and Product Governance Rules.
- Adopted suitable work processes to minimise conduct risk, including robust complaints management procedures and procedures for managing conflicts of interest.
- Mandated management to promote a corporate culture that supports good conduct, e.g. to have an overview over possible conduct risk within each department and implement suitable measures to reduce the risk of human error, negligence or fraud, ensuring that employees are familiar with policies, procedures and processes relevant to their work and responsibilities and take appropriate action in response to conduct infringements.
- Training of management and employees.

- Reporting incidents and internal alerts procedures ('Whistleblowing').

The Compliance department has many responsibilities related to employee conduct and is responsible for monitoring the status of conduct risk within the Bank. However, due to its nature, monitoring conduct risk is not a simple matter and Compliance is continuously working towards improving this task and reviewing decisions on which parameters to watch in relation to conduct risk.

7.2.3 Model risk management

The Bank has a model risk management framework in place. A model inventory is used, where models that fulfil the Banks model definition are registered.

A risk assessment scorecard is used to categorise models into risk groups that controls the level of monitoring and controls applied to the models. The Operational Risk Committee approves the Bank's model rules and manages the Banks model risk.

7.2.4 Compliance risk

The Bank manages compliance risk in accordance with Operational Risk Policy. Based on the policy, the Bank has set in place a variety of organisational and managerial actions, e.g.:

- A process to monitor and implement regulatory changes.
- Adopted suitable internal rules and work processes to promote compliance.
- Mandated management to promote compliance e.g. by leading by example, ensuring that employees are familiar with policies, rules and procedures relevant to their work and responsibilities, and take appropriate action in response to compliance violations.
- Training of management and employees.
- Reporting incidents.

The Compliance department monitors compliance and submits a semi-annual report to the Risk Committee and an annual report to the Board of Directors.

7.2.5 Change management

The Bank has robust procedures in place to govern change management. Bank has a product approval process that is aligned with updated EBA guidelines on product governance. The updated version further strengthens the governance of new product approvals and has been fully implemented. The process includes provisions for life cycle management.

7.2.6 Physical security

The Bank's security manager is responsible for physical security in the Bank's operations. That includes integrating safety and security policies with the business operations. He is charged with evaluating safety and security plans for effectiveness and managing the emergency response team.

7.2.7 Outsourcing

The Bank has outsourcing rules that are in line with the EBA guidelines on outsourcing. This sets the standard for how the Bank manages outsourcing agreements and risks by identifying, assessing and controlling risks in relation to outsourcing.

8 Sustainability risk

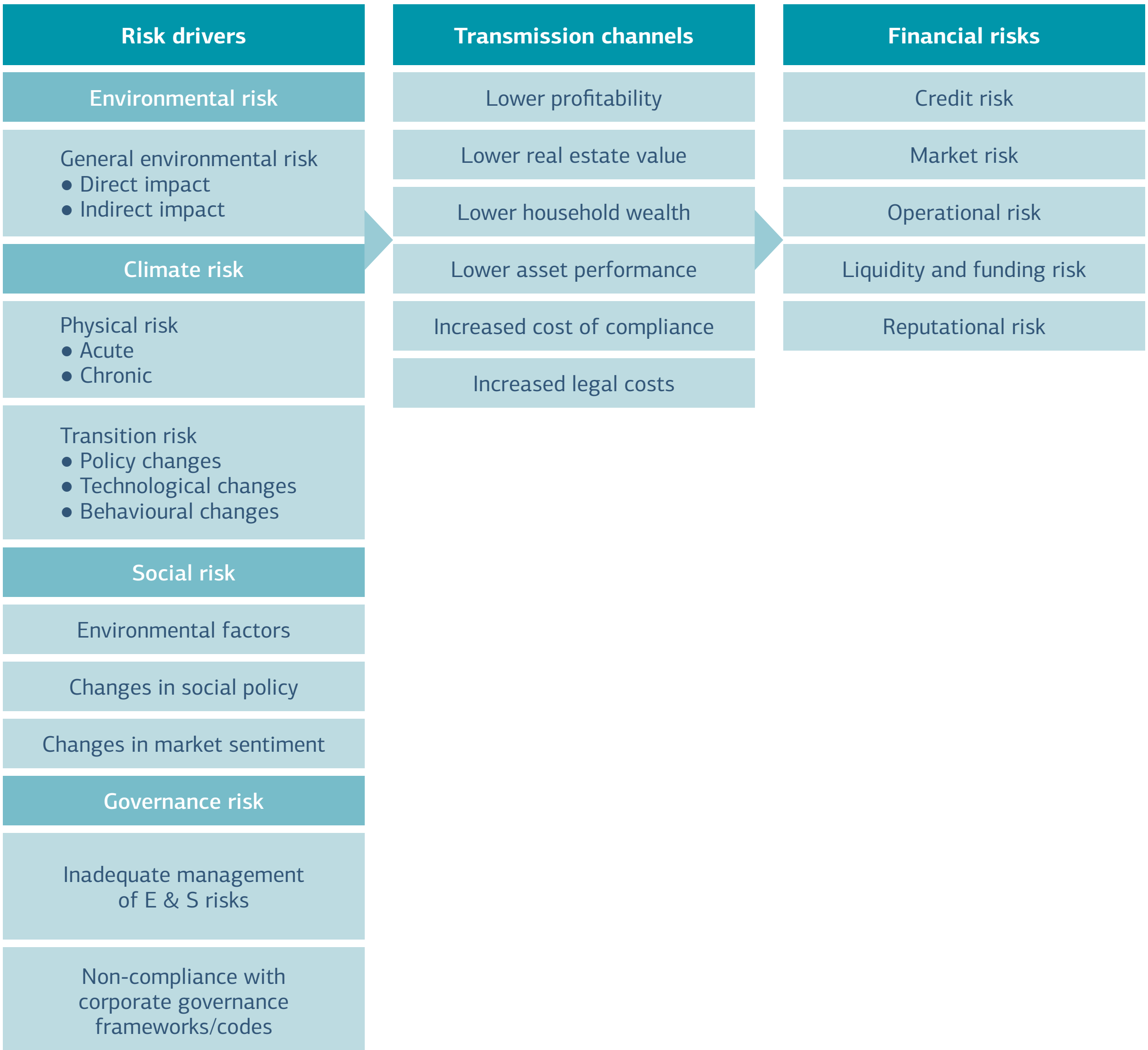
Sustainability risk

Sustainability risk is defined as risk that stems from the current or prospective impact of environmental, social and governance (ESG) factors on an institution's counterparties or invested assets. Sustainability risk materialises through the amplification of traditional categories of financial risks.

- In 2023, the Bank continued to develop its sustainability risk framework.
- The Board of Directors established a Sustainability Committee under its auspices.
- The implementation of the EU Taxonomy regulation into Icelandic law means that for the first time, the Bank discloses a green asset ratio (GAR).
- The Bank has implemented sustainability risk into its risk appetite for 2024.
- The Bank is in the process of setting science-based targets for carbon emissions.

Sustainability risk drivers can affect and amplify traditional financial risk factors such as credit and market risk via various transmission channels as shown in Figure 8.1.

Figure 8.1: Sustainability risk drivers



The Bank has assessed the impact and materiality of different sustainability risk factors on other material financial risk factors in its operations. The assessment underpins further implementation of sustainability-related assessments, measures and mitigants in the Bank's risk framework.

Development and integration of sustainability risk assessment within the Bank's risk framework will continue in 2024. The main challenges the Bank faces in that regard are the definition of relevant measures, identification of necessary data to apply those measures as well as the collection of identified data.

8.1 Management and policy

In 2023, a new sub-committee of the Board of Directors was formed. With this step, the Bank has integrated sustainability in its strategy as the Committee's main responsibilities are to formulate a sustainability strategy, develop and standardise sustainability metrics, disclosure and publication of sustainability data, compliance with laws and rules on sustainability, and ensuring continuous education of the Board on sustainability concerns. The Sustainability Committee is created for a temporary period of 1-2 years and has completed its work when clear sustainability metrics have been implemented for the Bank and when it has become clear in what manner Directive (EU) 2022/2464, as regards corporate sustainability reporting (CSRD), will be transposed into Icelandic law and how the resulting requirements will be met by the Bank.

The Bank's Sustainability Policy sets out aims for sustainability and describes the Bank's methods of implementing these in its operation. The Board of Directors approves the Policy and the CEO is responsible for its implementation and realisation. The CEO is also responsible for monitoring implementation of the Policy and reports to the Board of Directors annually. Authority to approve and amend key points and principles lies with the Executive Board. The Managing Director of Finance is responsible for shaping, maintaining and presenting the Sustainability Policy. The Policy was reviewed and updated in 2023. The Bank has set itself eight sustainability goals based on its Sustainability Policy. For further information regarding the Policy, the Bank's sustainability goals and other sustainability issues, refer to the Bank's Sustainability Report for 2023.

Climate risk has been defined as a relevant risk factor in the Bank's Risk Policy. The Risk Management division is responsible for assessing, measuring and developing risk measures for relevant risk factors in the Policy. The Bank has implemented sustainability risk into its risk appetite for 2024.

The Bank's Risk & Finance Committee has formed a Sustainability Group under its auspices. The Group's role is to oversee the Bank's sustainability framework and compliance of the Bank's green financing schemes to the framework. The Bank produces annual public reports on various sustainability-related factors, such as carbon emissions (PCAF and Pillar III additional disclosures) and the Bank's progress on sustainability in a report to the Global Reporting Initiative (GRI).

Information about the governance structure for remuneration is presented in the Bank's Remuneration report in chapter 9. For further information on the Bank's governance as regards sustainability, refer to the Bank's Sustainability Policy and the Bank's corporate governance statement.

8.2 Control and monitoring

In 2023, the Bank continued to develop its sustainability risk framework. The Bank assessed greenhouse gas (GHG) emissions from its credit portfolio, using the methodology of the Partnership for Carbon Accounting Financials (PCAF). The Bank is in the process of setting science-based targets for carbon emissions and has committed to reaching carbon neutrality by 2040, in tandem with targets set by the Icelandic government. The Bank aims to reach this target in cooperation with its customers, assisting them in their sustainability journey, rather than directing business away from larger emitters. The Bank has published a PCAF report for the year 2022, disclosing information on total GHG emissions from the Bank's operation.

For corporate lending, the Bank has set itself sustainability guidelines. These guidelines influence the assessment of risk and compliance with the Bank's sustainability goals in credit decisions, applying both generally to corporate customers and specifically to certain sectors. These guidelines cover issues such as sound business practises, choice of suppliers, effect of climate change, waste management and more.

The Bank has established a green financing framework and included the ratio of eligible green assets, according to the framework, in the Bank's risk appetite for 2024.

8.3 Assessment

The Bank has assessed sustainability risk in relation to other material risks for the Bank. The largest impact of sustainability risk is on credit risk, funding risk and operational risk. In 2024, the Bank will continue to develop and implement sustainability risk management within its overall risk framework based on this assessment.

The effect of sustainability risk on financial risk factors, regarding capital and liquidity, is assessed in the Bank's Internal Capital/Liquidity Adequacy Assessment Process (ICAAP/ILAAP). No additional capital was allocated due to sustainability risk in the Bank's operation at year-end 2023.

8.3.1 Environmental risk

Environmental risk is the risk of any negative financial impact on the Bank stemming from the current or prospective impact of environmental factors, such as natural disasters or climate change and other forms of environmental degradation, on its counterparties or invested assets. In this section, environmental risk is divided into general environmental risk, which comprises volcanic activity, earthquakes, landslides, avalanches or any other type of natural disaster, and climate risk, which comprises physical risk and transition risk. Physical risk can be further divided into acute and chronic physical risk.

8.3.1.1 General environmental risk

General environmental risk events are not uncommon in Iceland. The recent and ongoing seismic and volcanic activity on the Reykjanes peninsula is the latest such event, but other recent events include avalanches and landslides in East Iceland.

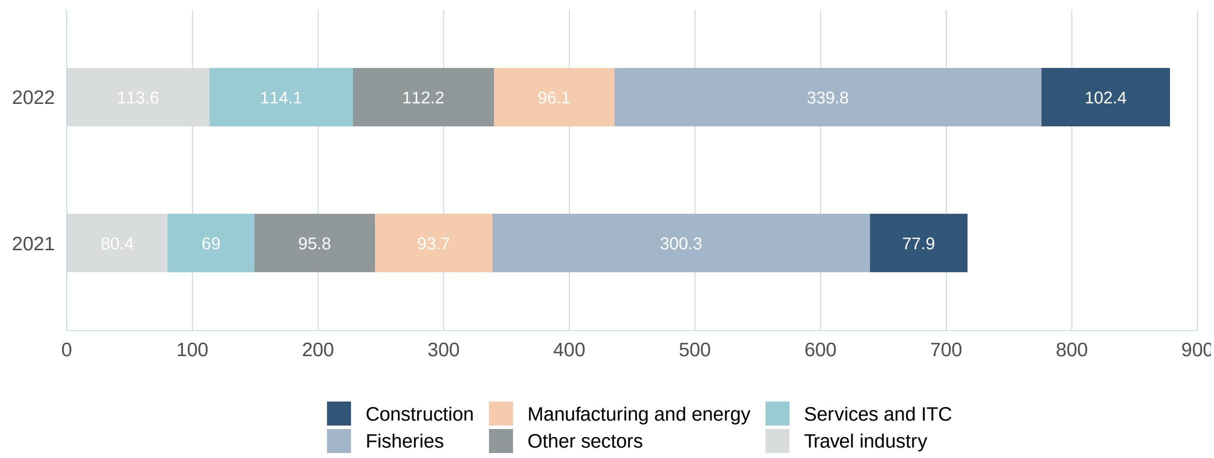
The biggest direct impact of general environmental risk events on the Bank is realised through damage to collateralised property. Due to the commonality of these events in Iceland, real estate is generally well insured against damages, both through regular insurance and via the National Catastrophe Insurance of Iceland (NTI).

Indirect impacts of environmental risk events can entail more uncertainty for the Bank and its customers. For example, temporary or permanent relocation of individuals from their primary residence or temporary loss of income for individuals and corporates due to operational challenges as a result of such risk events. These impacts of natural disasters can have a substantial impact on the Bank's customers and on the Bank, particularly via increased credit risk.

8.3.1.2 Climate risk

Total GHG emissions from the Bank's credit portfolio amounted to 878 kilotons of CO_2 equivalent ($ktCO_2e$) in 2022 (2021: 717 $ktCO_2e$). Of the total GHG emissions, 247 $ktCO_2e$ were scope 1 and scope 2 emissions, and 631 $ktCO_2e$ were scope 3 emissions. Note that emissions from the previous year have been updated in line with updated data from PCAF. The increased emissions are largely due to increased economic activity after the COVID-19 pandemic. Figure 8.2 shows a breakdown of emissions by sector.

Figure 8.2: GHG emissions from the loan portfolio in $ktCO_2e$



8.3.1.3 Acute physical risk

Acute physical risk, as a subcategory of climate risk, arises from particular events, especially weather-related events such as storms, floods, fires or heatwaves or other environmental hazards that may damage production facilities and disrupt value chains, potentially having a negative financial impact on the Bank, its counterparties or invested assets.

An increase in acute physical events due to climate change would potentially impact credit risk for the Bank through the effect on collateral. Real estate is the single largest category of collateral in the Bank's portfolio, all of which is located in Iceland. Another plausible impact on credit risk is that physical risk events could lead to negative economic effects and/or direct negative effects on distinct counterparties or groups of counterparties of the Bank, leading to an increase in default rates.

Should the effects of acute physical events increase in commonality and seriousness, they might negatively impact asset prices and put increased pressure on the Bank's liquidity profile if individuals and corporates need to access cash as a response to physical catastrophes.

Acute physical events can impact the Bank's operational risk via potential damages to property and equipment, injuries to staff and system disruptions. The Bank utilises data centres in various locations to mitigate this risk. Acute physical events also impact the Bank's suppliers, increasing the importance of supplier monitoring.

The negative impact on the Bank's collateral of acute physical events increasing in commonality and seriousness is already partly mitigated through strong insurance coverage. The overall impact and materiality of acute physical risk on the Bank's credit risk is therefore considered low. Figure 8.3 shows the sectors of the Bank's credit portfolio where acute physical risk is considered non-trivial, according to the Bank's risk assessment. While the potential effect of increased frequency of acute physical events on asset prices and liquidity is not currently mitigated, market risk is a small part of the Bank's overall risk profile and the impact and materiality of acute physical risk on the Bank's market and liquidity risk is as result considered low. The impact and materiality of acute physical risk on the Bank's operational risk is considered low.

8.3.1.4 Chronic physical risk

Chronic physical risk arises from longer-term trends such as temperature changes, rising sea levels, reduced water availability, biodiversity loss and changes in land and soil productivity. Such trends can potentially have a negative financial impact on the Bank, its counterparties or invested assets.

Through its exposure to the fisheries industry, the largest sector in the Bank's credit portfolio, the Bank is potentially exposed to chronic physical risk from the negative effect of rising temperatures and acidification on the marine ecosystem around Iceland. Rising sea levels can also potentially impact economic activity and/or real estate close to sea level.

The impact and materiality of chronic physical risk on the Bank's credit, market and liquidity risk is considered low in the short-term, but medium in the long-term. Figure 8.3 shows the sectors of the Bank's credit portfolio where chronic physical risk is considered non-trivial, according to the Bank's risk assessment.

8.3.1.5 Transition risk

Transition risk is the risk of any negative financial impact on the Bank stemming from the current or prospective impact of the transition to an environmentally sustainable economy on its counterparties or invested assets. In a report on the management and supervision of ESG risks published in 2021, the European Banking Authority (EBA) states that transition risk is most affected by three drivers; policy, technology and consumer behaviour. First, climate-related policy action or potentially disordered mitigation strategies could have an impact on asset prices in carbon-intensive sectors. Second, technological changes may, for instance, make existing technologies obsolete or uncompetitive, changing their affordability and affecting the relative pricing of alternative products. Third, changes in the preferences and behaviour of consumers and investors could affect institutions.

Operational conditions in certain sectors of the economy can be sensitive to change in laws and regulations, market conditions and market sentiment. Carbon-heavy sectors, such as manufacturing or transportation, are examples of this, where potentially increased costs due to the rising price of carbon emission certificates can impact the operation of companies significantly. As Iceland is committed to reaching carbon neutrality by 2040, regulatory changes, increased taxes for carbon-heavy sectors or other measures that contribute to this national target can be expected.

This could potentially affect the Bank's credit and liquidity risk, as well as operational risk via conduct risk. As a result, the impact and materiality of transition risk on the Bank's credit, liquidity and operational risk is considered medium. The impact and materiality of transition risk on the Bank's market risk is considered low. Figure 8.3 shows the sectors of the Bank's credit portfolio where transition risk is considered non-trivial, according to the Bank's risk assessment. The assessment is based on the underlying materiality of each sector, i.e. the total exposure and total GHG emissions of each sector, the likelihood of each risk factor materialising and the effect and severity of the risk factor on each sector.

Figure 8.3: Sustainability risk drivers

			Transition risk			Physical risk	
Sector	% of portfolio	% of CO_2	Policy	Technology	Behaviour	Acute	Chronic
Construction	8.1%	11.7%					
Fisheries	11.8%	38.7%					
Motor vehicle loans to individuals	1.0%	0.9%					
Travel industry	6.7%	12.9%					
Services and ITC	3.8%	13.0%					
Agriculture	0.4%	4.9%					
Manufacturing and energy	2.0%	10.9%					
Mortgages	44.8%	0.2%					
Other sectors	21.3%	6.8%					

Minimal	
Low	
Moderate	
High	

8.3.2 Social risk

Social risk is the risk of any negative financial impact on the Bank stemming from the current or prospective impact of social factors on its counterparties or invested assets.

These social risk factors include but are not limited to activities towards the community and society, employee relationships and labour standards, customer protection and product responsibility and human rights. The Bank's risk policy states that 'the Bank seeks to maintain sound business relationships, having regard for its own position as well as that of customers at each time, and with due regard for any internal connections between customers. The Bank pursues long-term business relationships and aims to avoid being linked to transactions that might damage its reputation.'

As previously mentioned, the Bank has set itself sustainability benchmarks for corporate lending, some of which pertain to social risk factors, such as:

- Considering potential risk factors in the counterparties' operational environment regarding inappropriate business practices, such as tax evasion, market dumping, competition infringements or other deviations from sound business practises.
- Human resource issues, such as equality, turnover of staff and number of staff in relation to the scope of operations.
- The collection of personal data, and security of such data.

The Bank can also be exposed to social risk in its own operation via reputational and conduct risk if it were to fail to adhere to laws, regulations and best practises regarding gender equality, inclusiveness, and health and safety in the workplace. Social conditions in Iceland rank among top conditions in the world in most areas and the Bank is well positioned as regards social issues. The Bank has implemented rules on gender ratios among managers, it has equal pay certification, and contributes to society through partnerships and charitable donations. The impact and materiality of social risk on the Bank's material risk factors in considered low.

8.3.3 Governance risk

Governance risk is the risk of any negative financial impact on the Bank stemming from the current or prospective impact of governance factors on its counterparties or invested assets.

These governance factors include but are not limited to ethical considerations, strategy and risk management, inclusiveness, transparency, management of conflict of interest and internal communication of critical concerns. The credit assessment of corporate customers includes a qualitative assessment of various governance factors for the customer, such as the experience, competence and integrity of executives, finances and planning, and disclosure of information to the Bank. The Bank can also be exposed to governance risk in its own operation via reputational and conduct risk. The Bank has a sound governance structure, with an established three lines of defence setup of risk governance, strong internal audit and compliance departments, a clear remuneration policy and sustainability policy. The greatest potential impact governance risk could have on the Bank is via reputational risk and conduct risk.

The impact and materiality of governance risk on the Bank's material risk factors in considered low.

8.4 Additional disclosures

Further quantitative information regarding sustainability can be found in templates ESG1-10 in the additional disclosures accompanying this report. Regulation (EU) No. 2020/852 (EU Taxonomy) entered into effect in Iceland 1 June 2023, and the Bank for the first time at year-end 2023 discloses information on its green asset ratio (GAR) which is based on the EU Taxonomy. With the regulation coming into effect in 2023, no data regarding the EU Taxonomy classification of the Bank's counterparties was available at year-end 2023. Therefore, the Bank's GAR for year-end 2023 is 0%. This conclusion is supported by an announcement by the Icelandic Financial Statement Registry, stating that Icelandic financial institutions are not obligated to disclose information where data is incomplete or unavailable. [1]

Furthermore, in template ESG2, all exposures are grouped in column O 'Without EPC label of collateral', due to the relevant regulations regarding EPC labels not being in effect in Iceland. In template ESG5, exposures are only allocated to column b, i.e., no exposures are categorised as being sensitive to climate change physical events. This is in spite of the Bank having completed analyses of the sensitivity of its exposures to physical risk. This is due to Iceland not being part of the Nomenclature of Territorial Units (NUTS), upon which template ESG5 is based, and the fact that the Bank's assessment of sensitivity to physical risk is subject to change upon further analysis. The conclusions regarding templates ESG2 and ESG5 are supported by consultation with the CBI regarding Pillar III additional disclosures on sustainability.

[1] See https://www.skatturinn.is/fyrirtaekjaskra/arsreikningaskra/ifrs-tilkynningar/yfirlysing-arsreikningaskrar-vegna-birtingar-upplysinga-sbr.-akvaedi-8.-gr.-flokkunarreglugerdar-evropusambandsins

9 Remuneration report

Remuneration report

The Bank emphasises hiring and employing exceptional personnel. The aim of its remuneration policy is to make the Bank a desirable workplace for qualified employees to ensure the Bank's competitiveness, continued development and acceptable profitability. The remuneration policy shall support sound operations in the long term and not encourage unreasonable risk taking. It is the Bank's aim that the terms of employment of executives and other employees are competitive but modest and not market leading. In determining terms of employment, responsibility and performance shall be taken into account, as well as equal rights perspectives. The remuneration policy applies to the Board of Directors, the Bank's Executive Board, and all employees of the Bank. The subsidiary of Landsbréf has its own remuneration policy and Remuneration Committee.

9.1 Governance

The remuneration policy of the Bank is approved by its Board of Directors and submitted to the Bank's Annual General Meeting for approval or rejection. The remuneration policy is reviewed annually, and any amendments shall be submitted to a shareholders' meeting for approval. The remuneration policy serves as an indicative guideline for the Bank and the Board of Directors. The Board of Directors shall note any deviations from the remuneration policy and substantiation thereof in the Board minutes. Deviations shall be presented to the Bank's next AGM.

The Remuneration Committee of the Bank is comprised of three Directors. The role of the Remuneration Committee is to provide guidance to the Board of Directors and CEO on salary and benefits for key executives and to advise the Board on the remuneration policy. The Committee reviews that the terms of employment of the Bank's executives are within the framework provided by the remuneration policy and report on its implementation yearly in connection with the Bank's AGM. The Committee shall monitor the developments of collective bargaining agreements, trends in salary expenses and number of employees. The Board of Directors has issued Rules of Procedure for the Committee, setting out its role and duties.

The Remuneration Committee members are the Chairman of the Board, which also chairs the Remuneration Committee and two other Directors of the Board. In 2023, the Remuneration Committee held 9 meetings. The Committee reviewed the remuneration policy in preparation for the 2023 AGM and made no significant changes.

9.2 Remuneration policy for the Bank's Board of Directors and CEO

Board members shall receive set monthly remuneration in accordance with the decision of the AGM each year, as provided for in Article 79 of Act No. 2/1995, on Public Limited Companies. In determining the remuneration amount, consideration shall be had for hours spent on the job, the responsibilities borne by Directors of the Board and the Company's performance. The Remuneration Committee presents the Board of Directors with a substantiated proposal for remuneration to Directors in the coming operating year. The Board of Directors deliberates on the Committee's proposal and submits a final proposal on remuneration to the AGM. The Bank reimburses Directors domiciled outside the capital region for travel expenses. Board members may not conclude severance agreements with the Bank.

The Board of Directors appoints the Bank's CEO and determines remuneration in accordance with the remuneration policy.

The CEO hires the Bank's key executives in accordance with the remuneration policy. The Bank publishes remuneration for Directors and key executives in its Annual & Sustainability Report. The Bank intends to achieve and maintain a gender balance of at least 60/40 at all levels of management. There are currently five male and two female Managing Directors, and the CEO is female. Members of the Bank's management body hold a total of 11 directorships in other entities.

Most employees in the Bank receive a fixed salary. The salary is evaluated regularly, mainly through collective bargaining. Mandatory pension contributions are made for all employees who also receive paid vacation as provided for by law, collective agreements and general market terms.

The Bank does not offer variable remuneration or bonuses in accordance with its remuneration policy. Any decision to implement a variable remuneration scheme must be presented to a shareholders' meeting for approval.

In 2013, the Bank offered a one-off employee incentive scheme in an agreement made by the Minister of Finance on behalf of the State, Landsbankinn hf. and Landsbanki Íslands hf. dated 15 December 2009. The scheme was compliant with FSA rules on performance-linked remuneration by financial undertakings. As a result, employees appear on the list of shareholders in the Bank.

The Remuneration Committee performs an annual comparison with market data on the Bank's remuneration to ensure remuneration is in accordance with the remuneration policy. Further quantitative information regarding the Bank's remuneration can be found in templates REM1, REM2 and REM5 in the additional disclosures accompanying this report.

10 Appendix

Table 10.1: List of additional disclosures

Template name	Template code	Type	Disclosure frequency	Reference chapter
Risk management				
Institution risk management approach	OVA	Qualitative	Annual	Chapter 2
Disclosure on governance arrangements	OVB	Qualitative	Annual	Chapter 2
Key metrics and risk-weighted exposure amounts				
Overview of RWEAs	OV1	Quantitative	Quarterly	Chapter 3
Key metrics template	KM1	Quantitative	Quarterly	Chapter 1
ICAAP information	OVC	Qualitative	Annual	Chapter 3
Own funds				
Composition of regulatory own funds	CC1	Quantitative	Semi-annual	Chapter 3
Reconciliation of regulatory own funds to balance sheet in the audited financial statements	CC2	Quantitative	Semi-annual	Chapter 3
Main features of regulatory own funds instruments and eligible liabilities instruments	CCA	Quantitative	Annual	Chapter 3
Comparison of institutions' own funds and capital and leverage ratios with and without the application of transitional arrangements for IFRS 9 or analogous ECLs	IFRS 9-FL	Quantitative	Quarterly	Chapter 3
Countercyclical capital buffers				
Geographical distribution of credit exposures used in the countercyclical capital buffer	CCyB1	Quantitative	Semi-annual	Chapter 3
Amount of institution-specific countercyclical buffer	CCyB2	Quantitative	Semi-annual	Chapter 3
Scope of application				
Differences between the accounting scope and the scope of prudential consolidation and mapping of financial statement categories with regulatory risk categories	LI1	Quantitative	Annual	Chapter 3
Main sources of differences between regulatory exposure amounts and carrying values in financial statements	LI2	Quantitative	Annual	Chapter 3
Outline of the differences in the scopes of consolidation (entity by entity)	LI3	Quantitative	Annual	Chapter 3
Explanations of differences between accounting and regulatory exposure amounts	LIA	Qualitative	Annual	Chapter 3

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Table 10.1 - Continued from previous page

Template name	Template code	Type	Disclosure frequency	Reference chapter
Other qualitative information on the scope of application	LIB	Qualitative	Annual	Chapter 3
Leverage ratio				
LRSum - Summary reconciliation of accounting assets and leverage ratio exposures	LR1	Quantitative	Semi-annual	Chapter 3
LRCom - Leverage ratio common disclosure	LR2	Quantitative	Semi-annual	Chapter 3
LRSpl - Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)	LR3	Quantitative	Semi-annual	Chapter 3
Disclosure of LR qualitative information	LRA	Qualitative	Annual	Chapter 3
Liquidity requirements				
Liquidity risk management	LIQA	Qualitative	Annual	Chapter 6
Quantitative information of LCR	LIQ1	Quantitative	Quarterly	Chapter 6
Qualitative information on LCR, which complements template EU LIQ1	LIQB	Qualitative	Quarterly	Chapter 6
Net Stable Funding Ratio (NSFR)	LIQ2	Quantitative	Semi-annual	Chapter 6
Credit risk quality				
General qualitative information about credit risk	CRA	Qualitative	Annual	Chapter 4
Additional disclosure related to the credit quality of assets	CRB	Qualitative	Annual	Chapter 4
Performing and non-performing exposures and related provisions	CR1	Quantitative	Semi-annual	Chapter 4
Maturity of exposures	CR1-A	Quantitative	Semi-annual	Chapter 4
Changes in the stock of non-performing loans and advances	CR2	Quantitative	Semi-annual	Chapter 4
Credit quality of forborne exposures	CQ1	Quantitative	Semi-annual	Chapter 4
Credit quality of performing and non-performing exposures by past due days	CQ3	Quantitative	Semi-annual	Chapter 4
Credit quality of loans and advances to non-financial corporations by industry	CQ5	Quantitative	Semi-annual	Chapter 4
Collateral obtained by taking possession and execution processes	CQ7	Quantitative	Semi-annual	Chapter 4
Credit risk mitigation techniques				
Qualitative disclosure requirements related to CRM techniques	CRC	Qualitative	Annual	Chapter 4
CRM techniques overview - Disclosure of the use of credit risk mitigation techniques	CR3	Quantitative	Semi-annual	Chapter 4
Use of the standardised approach				

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Table 10.1 - Continued from previous page

Template name	Template code	Type	Disclosure frequency	Reference chapter
Qualitative disclosure requirements related to standardised approach	CRD	Qualitative	Annual	Chapter 4
Standardised approach - credit risk exposure and Credit Risk Mitigation (CRM) effects	CR4	Quantitative	Semi-annual	Chapter 4
Standardised approach	CR5	Quantitative	Semi-annual	Chapter 4
Counterparty credit risk				
Qualitative disclosure related to CCR	CCRA	Qualitative	Annual	Chapter 5
Analysis of CCR exposure by approach	CCR1	Quantitative	Semi-annual	Chapter 5
Transactions subject to own funds requirements for CVA risk	CCR2	Quantitative	Semi-annual	Chapter 5
Standardised approach - CCR exposures by regulatory exposure class and risk weights	CCR3	Quantitative	Semi-annual	Chapter 5
Composition of collateral for exposures to CCR	CCR5	Quantitative	Semi-annual	Chapter 5
Credit derivatives exposures	CCR6	Quantitative	Semi-annual	Chapter 5
Market risk				
Qualitative disclosure requirements related to market risk	MRA	Qualitative	Annual	Chapter 5
Market risk under the standardised approach	MR1	Quantitative	Semi-annual	Chapter 5
Operational risk				
Qualitative information on operational risk	ORA	Qualitative	Annual	Chapter 7
Operational risk own funds requirements and risk-weighted exposure amounts	OR1	Quantitative	Annual	Chapter 7
Encumbered assets				
Encumbered and unencumbered assets	AE1	Quantitative	Annual	Chapter 6
Collateral received and own debt securities issued	AE2	Quantitative	Annual	Chapter 6
Sources of encumbrance	AE3	Quantitative	Annual	Chapter 6
Accompanying narrative information	AE4	Quantitative	Annual	Chapter 6
Remuneration				
Remuneration policy	REMA	Qualitative	Annual	Chapter 9
Remuneration awarded for the financial year	REM1	Quantitative	Annual	Chapter 9
Special payments to staff whose professional activities have a material impact on the instituions' risk profile	REM2	Quantitative	Annual	Chapter 9
Information on remuneration of identified staff	REM5	Quantitative	Annual	Chapter 9
Interest rate risk of non-trading book activities				

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Table 10.1 - Continued from previous page

Template name	Template code	Type	Disclosure frequency	Reference chapter
Qualitative information on interest rate risks of non-trading book activities	IRRBBA	Qualitative	Annual	Chapter 5
Interest rate risk of non-trading book activities	IRRBB1	Quantitative	Semi-annual	Chapter 5
Environmental, social and governance risk				
Environmental risk	ESGA	Qualitative	Semi-annual	Chapter 8
Social risk	ESGB	Qualitative	Semi-annual	Chapter 8
Governance risk	ESGC	Qualitative	Semi-annual	Chapter 8
Climate change transition risk: Credit quality of exposures by sector, emissions and residual maturity	ESG1	Quantitative	Semi-annual	Chapter 8
Banking book - Climate change transition risk: Loans collateralised by immovable property - Energy efficiency of the collateral	ESG2	Quantitative	Semi-annual	Chapter 8
Banking book - Climate change transition risk: Exposures to top 20 carbon-intensive firms	ESG4	Quantitative	Semi-annual	Chapter 8
Banking book - Climate change physical risk: Exposures subject to physical risk	ESG5	Quantitative	Semi-annual	Chapter 8
Summary of GAR KPIs	ESG6	Quantitative	Semi-annual	Chapter 8
Mitigating actions: Assets for the calculation of GAR	ESG7	Quantitative	Semi-annual	Chapter 8
GAR (%)	ESG8	Quantitative	Semi-annual	Chapter 8