



Report of the Board of Directors

19 April 2024

LANDSBANKINN HF. | Reg. No. 471008 0280 | LANDSBANKINN.IS

Report of the Board of Directors

19 April 2024

Dear shareholders and other guests,

I will now deliver the report of the Board of Directors for the year 2023. Afterwards, our CEO, Lilja Björk Einarsdóttir, will review the Bank's operation in the previous year.

It is tempting to look back on this occasion, as I am now stepping down from the Board of Directors. I have been a Director of the Board since 2013 and Chairman since 2016.

During this time, the Bank's total assets have grown by around 70% and currently amount to almost ISK 2,000 billion. Customer deposits have doubled and lending has grown by around 140%, or by almost ISK 1,000 billion. Alongside growth in equity by over ISK 62 billion, the Bank has paid dividends in the amount of ISK 192 billion, counting this year's dividend payment. Tax payments have also been considerable. Paid income tax in the period amounts to ISK 81.8 billion. The Bank has in total paid ISK 57.9 billion in special financial administration tax, often referred to as the bank tax, and ISK 9.9 billion in social security tax. The Bank's total tax contribution is even higher.

Major digital advances and fantastic app

During this time, the Bank's service platform has undergone major changes. In 2013, the Bank had first-rate online banking but no app - now the app has long since overtaken online banking in terms of use. Landsbankinn's app is leading among the domestic banking apps, both in terms of available features and the user experience. Alongside renewal of the Bank's core systems and setting out on a journey that would lead to major digital advances, we ensured that Landsbankinn continues to provide personal service around the country. This strategy has been warmly received by customers. The Bank's market share continues to grow and satisfaction with its services is high, as evidenced by the Bank topping the Customer Satisfaction Index in the banking market for 5 years running.

The Bank's operation has been exceedingly sound by all measurements. Its cost to income ratio has decreased and, in 2023 - the best operating year since the Bank's restoration - it was only 33.7%, among the lowest values in the banking market. And despite a growing customer base and expanding service platform, positional values are down by 30%, from just over 1,180 at year-end 2013 to just under 820 at the end of 2023.

These changes have allowed us to move the Bank's operation from facilities and buildings that have become too large and impractical. We have sold the old Landsbankinn buildings in Akureyri, Ísafjörður and Selfoss and have downsized significantly elsewhere. The most notable change occurred last year, when we moved from the Landsbankinn building in Austurstræti 11 and 13 other houses in Kvosin and Borgartún to join forces under one roof in Reykjastræti. The move was a success and has revitalised the Bank. Since 2017, when the decision to build new headquarters was taken, total square metres occupied by the Bank have decreased by almost 40%, from over 40,000 to around 25,000 square metres.

It has been a great privilege to be a part of the extensive changes to the Bank during this decade. The Board of Directors is proud and pleased with these fantastic results and the Bank's employees, who are to be commended for their ambition and professionalism, should certainly be so as well.

Support for Grindavík

Looking back at our successes, it can be easy to forget that success is the result of hard work and that there have also been challenges. There was no lack of challenges in 2023 yet the Icelandic economy even so showed both resilience and drive. While economic growth has slowed, the outlook for 2024 remains fine, provided inflation can be brought under control and conditions created for rate cuts.

The collective bargaining agreements that have been concluded are promising. International warfare contributes to increased uncertainty and the economic ramifications of seismic and volcanic activity on the Reykjanes peninsula remain unclear. The people of Grindavík have been in all of our thoughts here at Landsbankinn. Many of our valued customers hail from Grindavík, both individuals and companies, as well as important members of our team. Landsbankinn has supported the inhabitants of Grindavík in various ways and my hope is that all issues will be resolved as soon as possible.

Landsbankinn's position is strong

Landsbankinn showed positive results in 2023. The Bank's profitability was 11.6%, in line with its target 10% long-term profitability. The Bank's funding was also successful. Foreign currency issuances were well received and the same can be said for issuances on the domestic bond market.

Sound and profitable operation allows the Bank to pay dividends that benefit the entire community and is also vital to the Bank itself. Only through profitable operation can the Bank continue to invest, to develop and to counter increased competition with full force by offering its customers exemplary service.

Continue to lead

In recent years, financial services and the financial market have undergone significant and rapid change, both internationally and in Iceland. Several companies now offer financial services and competition has grown stiffer in certain services. In an increasingly competitive environment, the Bank benefits from having in recent years invested extensively in IT and development of digital services. As a result, the Bank is more agile and can be quicker to respond to technical innovations and legal requirements. It is no less dynamic when it comes to implementing new and interesting ideas.

The Bank has also responded to growing competition by adding income streams and new services. A good example is the merchant acquiring service that is off to a great start.

To ensure continued success, the Bank must continue to add income streams that strengthen its operation and allow it to offer even more diverse and better financial services. It was with this in mind that the Board of Directors initially began evaluating the possibility of adding insurance to the Bank's broad service platform. I will return to the topic of TM tryggingar later in my speech.

Service charges and interest margin fund exemplary service

Alongside the Bank's significant investment in the development of financial infrastructure and new technology, the interest margin for households has decreased, as have service fees, in real terms. Public debate does not often mention that the interest margin and service fees fund both comprehensive and complex service as well as higher tax levies than what is common in our neighbouring countries. A comparison of service fees and interest margins, published in a report from a work group under the auspices of the Minister of Business Affairs last year, was favourable for Landsbankinn and an encouragement to do even better.

Complicated regulatory environment

The demand banks face to implement new rules and legislation is not often discussed either. The legal requirements we must comply with are extensive and complex, originating for a large part in European regulations that are built around companies operating in much larger markets. Complying with these demands can be a costly and time-consuming undertaking.

Trust, professionalism and sound risk culture

Landsbankinn places great emphasis on complying with new rules in a prompt and professional manner and on ensuring effective training and education to ensure that they are followed in full.

Last year, the Financial Supervisory Authority (FSA) of the Central Bank of Iceland published the outcome of two comprehensive reviews of the Bank's activities, on the one hand on measures to combat money laundering and terrorist financing, and on the other hand, on Landsbankinn's involvement in the public offering of the State's 22.5% stake in Íslandsbanki in 2022. The FSA remarked on certain aspects of the Bank's measures to combat money laundering and terrorist financing. The Bank agreed with the FSA's findings and has put in place necessary improvement measures. The FSA did not see reason to fine or otherwise penalise the Bank in either case.

The Bank's successes speak for themselves. The work done here is guided by professionalism and the interest of both the Bank and its customers. A sound risk culture characterises the Bank's entire activity.

About Landsbankinn's purchase of TM

Dear guests.

I have now reviewed the position and performance of Landsbankinn in the past few years, both of which are very good. In recent weeks, these excellent results have sadly been overshadowed by relentless criticism from Icelandic State Financial Investments (ISFI) on the Bank's purchase of TM tryggingar. The Board of Directors published a detailed memorandum on 22 March, setting out the course of events and reasons for the acquisition. The memorandum is detailed and I refer you to that document. But there is full reason to review the main aspects of this matter here at the AGM.

Events leading up to the purchase

The Board of Directors considers making a bid for TM a sound business decision, as the company represents an eligible investment opportunity for Landsbankinn.

The Board has long considered the possibility of adding insurance to the Bank's service platform. We consider insurance and banking service to align. Other banks, both domestic and international, agree. Arion Bank owns an insurance company and, as we know, Íslandsbanki also made an offer to purchase TM, alongside Landsbankinn. In Norway, DNB Bank which is one-third owned by the Norwegian State, is a major actor in the insurance market.

Landsbankinn could either build its insurance operation organically or acquire an established insurance company. Neither option is without flaws and one of the issues that we considered was the time frame; the lengthy time it would take to build a profitable insurance operation from the ground up. When it became clear last summer that Íslandsbanki and Kvika Bank would not merge, the Board asked the CEO to examine the option of acquiring TM from Kvika Bank. As detailed in the Board's memorandum from 22 March, we informed ISFI that we had approached Kvika Bank to discuss the purchase of TM in summer of 2023. These negotiations did not lead to a transaction.

Synergies

In early November 2023, Kviká Bank announced the formal sale process of TM which began on 16th of that month. What followed was detailed and extensive preparatory work. The outcome was, based on the price offered by the Bank and the most conservative synergy scenario, that the investment in TM was estimated to return an 18% internal rate of return to Landsbankinn. Taking advantage of additional synergy opportunities would make the investment even more attractive. Following publication of the memorandum, the Board offered an even more in-depth presentation to ISFI, an offer the institution did not accept.

About the State Ownership Policy

Criticism of the Bank's acquisition of TM has not least been based on its supposed opposition with the State Ownership Policy. The Board of Directors disagrees. To the contrary, the purchase of TM aligns with the objectives and purpose of the Policy. To quote the State Ownership Policy from 2020: "The state does not aim to hold a majority in financial undertakings in the private sector in the longer term. It is therefore important that administration of these holdings is done professionally, soundly and on market principles, in part to maximise their sales value and dividends to taxpayers". At its core, the transaction aims to maximise the value of the State's holding in Landsbankinn in accordance with the Policy.

The Policy also mentions the importance of fostering robust and healthy competition and of having regard for the State's key aim, to reduce public debt. Regular and acceptable dividend payments from and/or the sale of equities in financial undertakings are said to be key to achieve this objective. The Board worked to further these Policy objectives as it considers clear that the acquisition of TM will in the long term result in increased profitability and enhance the Bank's dividend capacity.

Operates on market principles

Despite being almost wholly owned by the State, Landsbankinn shall according to the State Ownership Policy operate on market principles and must as such participate fully in competition in the financial market, hereafter as heretofore. If the intent of the Bank is not to operate as any other company on a competitive market, the risk is that it will slowly but surely lag further and further behind its competitors who are not similarly restricted. If shareholders are of the opinion that Landsbankinn's role should be different and that it should not participate fully on the financial market and based on market principles, this should be stated as a formal policy and with changes to the company's purpose as it is set forth in its Articles of Association, or with the decision of a shareholders' meeting.

Communication with ISFI

Criticism has also been directed at the purchase being in opposition with the will of the Minister of Finance and Economic Affairs and the government platform. ISFI has referred to the stated will of the then Minister of Finance and Economic Affairs in a podcast in February 2024, which ISFI apparently made special note of in its minutes on 8 February. ISFI saw now reason to make the Board of Directors aware of this statement by the Minister. In a meeting between the then Minister and the Bank's management, held later in February, the same opinion was stated. It should be noted that such meetings are generally held yearly with the Bank's management to review operations in general and the operating environment. The meetings are not a forum designed to affect the governance and strategy of the banks. The arm's length principals in the State Ownership Policy and the agreement with ISFI provide that communication is to be directed through ISFI. I would also like to point out that remarks were forthcoming from ISFI following this interaction.

Clear framework

The framework providing for the the Bank's operation and communication protocol is clear in order to preserve the arm's-length principal, consideration for competition and transparency. We informed ISFI in accordance with protocol and received no remarks. Remember that in summer 2023, we informed ISFI that the Bank has entered into negotiations with Kvika Bank for the purchase of TM. In December of last year, we notified of the Bank's indicative offer for TM. In neither instance did ISFI express its opinion that the potential purchase of TM by the Bank contravened the State Ownership Policy. Nor did ISFI advance any other comments, request further documentation or a certain method of moving forward until after the bid process had concluded.

There is no disagreement that the decision to make an offer for TM was the prerogative of the Board of Directors and within its remit according to the laws and rules that apply to the Board. It is also clear that the Board considers the transaction to accord with the State Ownership Policy, despite external disagreement on that point. This does not alter the fact that the decision was the Board's prerogative and the Board is responsible for that decision. The Board reiterates that, according to the laws and rules governing the Bank, and as provided for in the State Ownership Policy, the Board of Directors shall be independent in its decisions.

I have mentioned earlier that we notified ISFI of our negotiations with Kvika in summer 2023 and later of our involvement in the open sale process that began in November of that year. We were obligated to inform, which we did; we were not obligated to consult with ISFI on the decision at hand. Such consultation would in the opinion of the Board contravene both the Act on Public Limited Companies and the general principles of company law on equal treatment of shareholders.

Impact on capital ratio

The impact of the purchase on the Bank's equity position has been part of the discussion. As stated in the Board's memorandum to ISFI from 22 March, Landsbankinn's equity that would be tied up in the TM purchase amounts to ISK 18.7 billion. Prior to the purchase, the Bank's capital ratio is 23.6% and the regulatory requirement that applies to the Bank is 20.7%. The impact of the purchase is a 1.5 percentage point decrease, to a capital ratio of 22.1%. Countermeasures would raise this ratio back to 23.1%. The Bank aims to always maintain a ratio above the minimum requirement. The fact is that following the purchase of TM, with or without countermeasures, the Bank would at all times remain well above regulatory requirements.

Financing of the acquisition

I would like to take this opportunity to respond to criticism concerning the fact that the purchase offer was not submitted to a shareholders' meeting for approval. At the same time, I would like to reiterate that we, the Directors of the Board, take our responsibilities seriously. We have been entrusted with the management of Iceland's largest bank and the State's most important asset - the most important asset of the country's population. We have striven to uphold that responsibility.

Critique levelled at Landsbankinn for not making the offer subject to approval by a shareholders' meeting has referred to that proviso in Íslandsbanki's offer.

It is important to note that Íslandsbanki's offer provided for payment for TM through the issuance of new share capital, which is subject to the approval of a shareholders' meeting, as recently stated at the bank's AGM.

Landsbankinn does not intend to fund the purchase with the issuance of new shares; rather, the Bank intends to remit payment with cash on hand and issue a subordinated bond as a countermeasure. This funding avenue was selected so as not to curtail the Bank's capacity to pay dividends and as the method considered most favourable for the Bank and its owners. There is reason to note that banks frequently

utilise such borrowing to strengthen their capital ratios. Just in March of this year, we issued a subordinated bond in the total amount of ISK 15 billion that raises the Bank's excess capital base by the same amount.

It was the unanimous agreement of all parties involved in preparing the offer that a cash only payment would strengthen the Bank's offer. There was no need to issue new share capital as the Bank's capital ratios will remain well above the regulatory requirement. For this reason and this reason alone, the offer was not made contingent on the approval of a shareholders' meeting.

Dear guests.

The Board of Directors of Landsbankinn reiterates that both Directors and the Bank's employees worked on the TM offer with professionalism and integrity. We consider the purchase a sound investment for the Bank, designed to strengthen and empower it for the future. We regret that the transaction has become this debated and that the Chairman of the Board of Icelandic State Financial Investments has chosen to criticise the Board of Directors in the media in terms that can only be described as inflammatory. I urge ISFI to address this matter in a more responsible matter so as not to further harm the Bank.

I speak for the entire Board in saying that it has been an honour and a privilege to serve on the Board of Directors of Landsbankinn.

On behalf of the Board, I thank Lilja Björk Einarsdóttir, CEO, other executives and the Bank's employees for pleasant and effective collaboration in the past year. I extend our thanks to shareholders, ISFI, regulators and other stakeholders that we have collaborated with throughout the years. On a personal note, I am grateful for the exceedingly interesting and rewarding decade I have had at the Bank. I take my leave of Landsbankinn both grateful and proud, and look forward to seeing it continue to grow and advance. I will continue to follow the Bank closely and look forward to visiting its new Akureyri branch, scheduled to open this fall.

I congratulate new Directors on their election to the Board and wish them success in their work. You have an opportunity to work with an exceptional team and I hope that you will have the good fortune to resolve the TM transaction for the benefit of Landsbankinn and its shareholders.

Thank you.