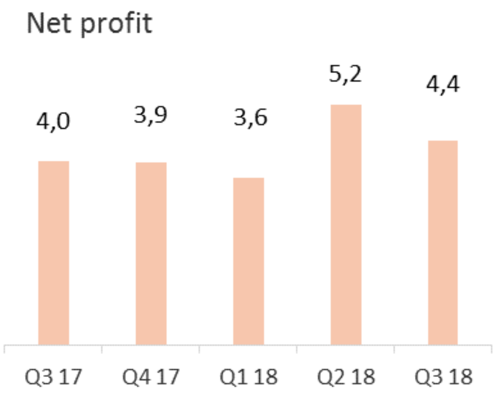
# Interim Report January – September 2018 Summary of Results

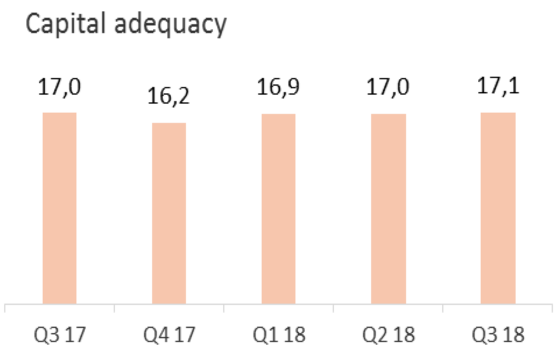
**Q3 2018 in comparison with Q2 2018**

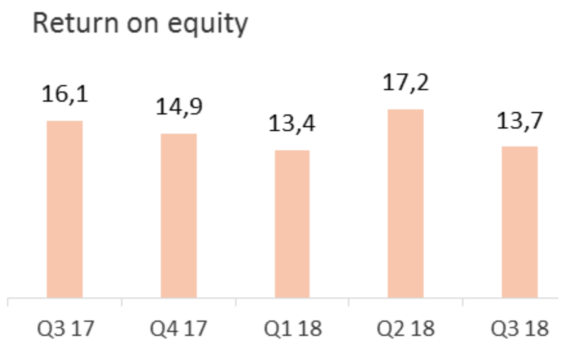
- Net profit EUR 4.4 m (EUR 5.2 m), of which EUR 3.9 m (EUR 4.7 m) is attributable to owners of the parent
- Net income EUR 13.1 m (EUR 13.7 m)
- Operating expenses EUR 6.3 m (EUR 6.3 m)
- Loan provisions EUR 1.9 m (EUR 1.6 m)
- Income tax expenses EUR 0.5 m (EUR 0.6 m)
- Return on equity 13.7% (17.2%)
- Capital adequacy 17.06% (17.0%)




**Q3 2018 in comparison with Q3 2017**

- Net profit EUR 4.4 m (EUR 4.0 m), of which EUR 3.9 m (EUR 3.6 m) is attributable to owners of the parent
- Net income EUR 13.1 m (EUR 10.1 m)
- Operating expenses EUR 6.3 m (EUR 5.0 m)
- Loan provisions EUR 1.9 m (EUR 1.1 m)
- Income tax expenses EUR 0.5 m (EUR 0 m)
- Return on equity 13.7% (16.1%)
- Capital adequacy 17.06% (17.0%)



Return on equity ratios is based on the profit attributed to the shareholders and equity of AS LHV Pank and do not include non-controlling interest.

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# Business activites

In Q3, the number of new customers at the bank increased by more than 7,300 and the total number of clients exceeded the threshold of 150,000. New record levels were achieved in customer activity. During the quarter, the bank's deposit volume grew by EUR 97 million and the loan volume by EUR 35 million. The growth of the deposit and loan base was very strong. The deposits of regular customers grew by EUR 56 million and those of the financial intermediaries by EUR 41 million. Corporate loans grew by EUR 15 million and retail loans by EUR 20 million.

The quarterly profit before taxes was EUR 4.9 million and net profit EUR 4.4 million. As at the end of the quarter, the net profit exceeded the financial plan by EUR 0.6 million. A positive contribution to the profit came from the EUR 1.5 million bigger than planned fee and commission income and a negative contribution from the EUR 1.2 million higher than planned specific provision of loans.

A cooperation agreement was concluded at the beginning of the quarter with deposit marketplace Raisin, the aim of which is to involve more longer-term deposits. In the middle of the quarter, the Youth Bank offer was launched, consisting of a debit card with purchase insurance and partner benefits, state student loan and microinvestments. A low value payment was launched, where a private client can make up to five consecutive payments in the amount of up to EUR 30 without entering PIN2 and with a possibility to withdraw cash at the stores together with making a purchase. At the end of the quarter, the bank started e-identification, which enables adult private persons to open a bank account in the internet bank with an ID-card, Mobile-ID or Smart-ID. With e-identification, a legally required monthly limit of EUR 15,000 applies to using the money.

Due to BREXIT Bank initiated the activity of reregistring the branch from European Union branch to third country branch. The process was started both with Estonian and United Kingdom's FSA.

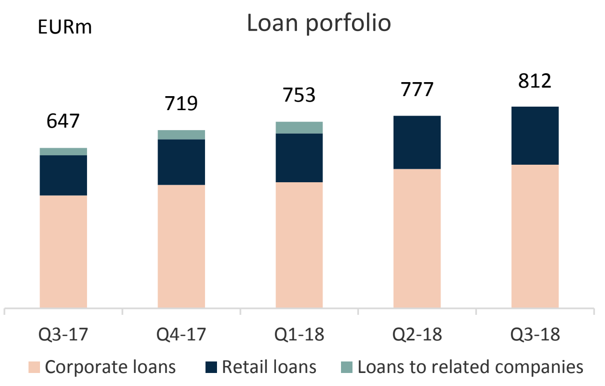
# Financial Summary

Q3 was successful in terms of business volumes. LHV Bank generated EUR 9.7 million in net interest income and EUR 2.6 million in net fee and commission income. In total, the bank's net income amounted to EUR 12.3 million, expenditure to EUR 6.3 million and loan provisions to EUR 1.9 million. Financial income was 0.1 million in Q3. LHV Pank is accounting from Q2 14% advance income tax, which generated corporate income tax in amount of 0.5 million euro. Banks Q3 protit was 4.4 million EURt, which is 15% more than in Q2 2018 (5.2) and 11% more than Q3 2017 (4.0).

Securities brokerage fees, transaction fees and fees from cards are greatest contributor to fee and commission income.

The increase in net interest income stems from the growth in business volumes. By the end of Q3, the total volume of the bank's loan portfolios amounted to EUR 812 million (Q2: EUR 777 million). The volume of portfolios grew 5% over the quarter.

Retail loans portfolio grow 9% within quarter and has reached EUR 237 million (Q2 2018: EUR 218 million). Loan portfolio increased by EUR 35 million in Q3 (Q2 2018: EUR 23 million).




Banks deposits decreased 6% within a quarter and reached EUR 1 652 million by end of September (Q2 EUR 1 555 million). Financial intermediates deposits decreased by EUR 41 million. EUR 1 523 million were demand deposits and EUR 129 million were term deposits. Private individuals deposits reached EUR 405 million increasing 8% q-t-q. Outstanding bond portfolio was EUR 41 million, decreasing 11% comparing to end of Q2.

| **Business volumes**<br>EUR million | **Q3 2018** | **Q2 2018** | **Quarter over quarter** | **Q3 2017** | **Year over year** |
|---|---|---|---|---|---|
| Net interest income | 9,65 | 9,60 | 0% | 7,93 | 22% |
| Net fee and commission income | 2,59 | 3,80 | -32% | 2,14 | 21% |
| Other financial income | 0,05 | 0,25 | -78% | 0,03 | 116% |
| Total net operating income | 12,29 | 13,65 | -10% | 10,10 | 22% |
| Other income | 0,77 | 0,03 | 2 384% | 0,00 | - |
| Operating expenses | -6,32 | -6,29 | 1% | -5,04 | 25% |
| Loan losses | -1,86 | -1,60 | 16% | -1,10 | 69% |
| Income tax expenses | -0,50 | -0,63 | -21% | 0,00 | - |
| Net profit | 4,38 | 5,16 | -15% | 3,96 | 11% |

| **Business volumes**<br>EUR million | **30.09.2018** | **31.12.2017** | **Change** |
|---|---|---|---|
| Loan portfolio | 812,0 | 719,4 | 13% |
| Financial investments | 41,0 | 50,0 | -18% |
| Deposits of customers | 1 652,0 | 1 551,0 | 7% |
| incl. deposits of financial intermediates | 511,4 | 607,0 | -16% |
| Equity (including minority interest) | 120,0 | 99,5 | 21% |

| | | | |
|---|---|---|---|
| Assets managed by bank | 153 893 | 133 655 | 15% |

| **Ratios** mln eurot | **Q3 2018** | **Q2 2018** | **Quarter over quarter** | **Q3 2017** | **Year over year** |
|---|---|---|---|---|---|
| Net profit | 4,4 | 5,2 | -0,8 | 4,0 | 0,4 |
| Net profit attributable to owners of the parent | 3,9 | 4,7 | -0,8 | 3,6 | 0,3 |
| Average equity | 114,4 | 109,8 | 4,6 | 88,9 | 25,5 |
| Return on equity (ROE), % | 13,7 | 17,2 | -3,5 | 16,1 | -2,4 |
| Return on assets (ROA), % | 0,89 | 1,05 | -0,16 | 1,12 | -0,23 |
| Net interest income | 9,6 | 9,6 | 0,0 | 7,9 | 1,7 |
| Interest-bearing assets, average | 1 766,4 | 1 791,8 | -25,4 | 1 171,2 | 595,2 |
| Net interest margin (NIM) % | 2,18 | 2,14 | 0,04 | 2,27 | -0,09 |
| Price spread (SPREAD) % | 2,15 | 2,12 | 0,03 | 2,20 | -0,05 |
| Cost/income ratio % | 48,4 | 46,0 | 2.4 | 49,9 | -1,5 |

**Explanations to ratios** (quarterly ratios have been expressed on an annualised basis)

Average equity (attributable to owners of the parent) = (equity as at the end of the reporting period + equity as at the end of the previous reporting period) / 2

Return on equity (ROE) = net profit for the quarter (share of owners of the parent) / average equity (attributable to owners of the parent) *100

Return on assets (ROA) = net profit for the quarter (share of owners of the parent) / average assets*100

Net interest margin (NIM) = net interest income / interest-bearing assets, average * 100

Price spread (SPREAD) = interest yield from interest-bearing assets – cost of external capital

Interest yield from interest-bearing assets = interest income / interest-bearing assets, average * 100

Cost of external capital = interest expenses / interest-bearing liabilities, average * 100

Cost/income ratio = total operating cost / total income * 100

# The Group's Liquidity, Capitalisation and Asset Quality

The Group's liquidity coverage ratio (LCR), as defined by the Basel Committee, stood at 130.8% as at the end of September (31 December 2017: 121.1%). Banks liquidity situation remained same in Q3, change in LCR levels are related to significantly higher financial intermediates deposits what Bank covers 100% with liquid assets. Excluding the financial intermediates deposits the Groups LCR in 237.9%. The Group recognises cash and bond portfolios as liquidity buffers. These accounted for 55% of the balance sheet (31 December 2017: 58%). The ratio of loans to deposits stood at 49% as at the end of the third quarter (31 December 2017: 46%).

Bank runs every you internal liquidity assesment process (ILAAP), which is done both on statical and dynamical balance sheet modelling.

In assessment bank follows both regulative and internal liquidity ratios dynamics and fulfillment of limits. In dynamic assessment bank is following its own risk scenario.

Banks own funds at end of September were EUR 128.4 million (31.12.2017 EUR 113.9 million).

Bank is adequately capitalized at end of the reporting periood, capital adequacy was 17.06% (31.12.2017: 16.75%), calculated according to CRR IV directive. Banks capital adequacy exceeds internal capital targets, which is 15.06%.

Both AS LHV Pank and its subsidiary AS LHV Finance are included into capital adequacy calculation.

Bank uses standard methodology for calculating credit and market risk capital charges and basic indicator approach calculating operational risk capital requirement. Bank has fulfilled all capital requirement in current reporting periood.

Each year, an internal capital adequacy assessment process (ICAAP) is performed, the goal of which is to identify potential capital needs in addition to regulatory capital requirements.

| **Capital bases** *(in thousands of euros)* | **30.09.2018** | **31.12.2017** |
|---|---|---|
| Paid-in share capital | 69 500 | 59 500 |
| Statutory reserves paid in from net profit | 2 121 | 1 528 |
| Accumulated profit/deficit | 31 442 | 19 891 |
| Intangible assets (subtracted) | -1 271 | -951 |
| Net profit for the reporting period | 8 122 | 13 909 |
| Other adjustments | -1 629 | 0 |
| **Total Tier 1 capital** | **108 355** | **93 877** |
| Subordinated debt | 20 000 | 20 000 |
| **Total Tier 2 capital** | **20 000** | **20 000** |
| **Net own funds for capital adequacy** | **128 355** | **113 877** |
| **Capital requirements** | | |
| Central governments and central bank under standard method | 922 | 945 |
| Credit institutions and investment companies under standard method | 6 608 | 5 886 |
| Companies under standard method | 495 049 | 465 202 |
| Retail claims under standard method | 128 390 | 107 197 |
| Public sector under standard method | 303 | 185 |
| Housing real estate under standard method | 32 424 | 20 039 |
| Overdue claims under standard methods | 16 380 | 20 915 |
| Other assets under standard method | 11 685 | 10 169 |
| **Total capital requirements for covering the credit risk and counterparty credit risk** | **691 761** | **630 539** |
| Capital requirement against foreign currency risk under standard method | 286 | 409 |
| Capital requirement against interest position risk under standard method | 83 | 412 |
| Capital requirement against equity portfolio risks under standard method | 562 | 585 |
| Capital requirement against credit valuation adjustment risks under standard method | 96 | 15 |
| Capital requirement for operational risk under base method | 59 434 | 47 754 |
| **Total capital requirements for adequacy calculation** | **725 222** | **679 714** |
| **Capital adequacy (%)** | **17,06** | **16,75** |
| **Tier 1 capital ratio (%)** | **14,40** | **13,81** |

# CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

## Condensed Consolidated Interim Statement of Profit or Loss and Other Comprehensive Income

| *(in thousands of euros)* | Note | Q3 2018 | 9M 2018 | Q3 2017 | 9M 2017 |
|---|---|---|---|---|---|
| Interest income | | 11 355 | 33 425 | 9 097 | 25 728 |
| Interest expense | | -1 709 | -4 985 | -1 170 | -2 975 |
| **Net interest income** | 7 | **9 646** | **28 440** | **7 927** | **22 753** |
| Fee and commission income | | 4 615 | 14 152 | 3 273 | 9 515 |
| Fee and commission expense | | -2 028 | -5 514 | -1 130 | -3 745 |
| **Net fee and commission income** | 8 | **2 587** | **8 638** | **2 143** | **5 770** |
| Net gains/losses from financial assets measured at fair value | | -23 | 166 | 42 | 389 |
| Foreign exchange gains/losses | | 77 | 71 | -17 | 771 |
| **Net gains from financial assets** | | **54** | **237** | **25** | **1 160** |
| Other income/(expense) | | 770 | 828 | 1 | -35 |
| **Total other income** | | **770** | **828** | **1** | **-35** |
| Staff costs | 9 | -3 279 | -10 068 | -2 643 | -8 208 |
| Administrative and other operating expenses | 9 | -3 039 | -8 633 | -2 396 | -6 797 |
| **Total expenses** | | **-6 318** | **-18 701** | **-5 039** | **-15 005** |
| **Profit before impairment losses on loans and advances** | | **6 739** | **19 442** | **5 057** | **14 643** |
| Income tax expense | | -501 | -1 970 | 0 | 0 |
| Impairment losses on loans and advances | | -1 859 | -4 337 | -1 098 | -3 050 |
| **Net profit for the reporting period** | | **4 379** | **13 135** | **3 959** | **11 593** |
| **Other comprehensive income** | | | | | |
| Items that may be reclassified subsequently to profit or loss: | | | | | |
| Available-for-sale investments: | | | | | |
| Revaluation of available-for-sale financial assets | | 76 | -36 | 19 | 82 |
| **Total profit and other comprehensive income for the reporting period** | | **4 455** | **13 099** | **3 978** | **11 675** |
| **Total profit of the reporting period attributable to:** | | | | | |
| Owners of the parent | | 3 924 | 12 046 | 3 569 | 10 405 |
| Non-controlling interest | | 455 | 1 089 | 390 | 1 188 |
| **Total profit for the reporting period** | | **4 379** | **13 135** | **3 959** | **11 593** |
| **Total comprehensive income attributable to:** | | | | | |
| Owners of the parent | | 4 000 | 12 010 | 3 588 | 10 487 |
| Non-controlling interest | | 455 | 1 089 | 390 | 1 188 |
| **Total comprehensive income for the reporting period** | | **4 455** | **13 099** | **3 978** | **11 675** |

# Condensed Consolidated Interim Statement of Financial Position

| *(in thousands of euros)* | Note | 30.09.2018 | 31.12.2017 |
|---|---|---|---|
| **Assets** | | | |
| Due from central bank | 10 | 926 047 | 920 714 |
| Due from credit institutions | 10 | 25 912 | 20 991 |
| Due from investment companies | 10 | 12 159 | 14 186 |
| Available-for-sale financial assets | | 220 | 775 |
| Financial assets at fair value through profit or loss | | 40 761 | 49 239 |
| Loans and advances to customers | 5 | 811 951 | 719 390 |
| Receivables from customers | | 6 260 | 7 357 |
| Other financial assets | | 2 687 | 2 289 |
| Other assets | | 627 | 836 |
| Tangible assets | | 1 242 | 1 225 |
| Intangible assets | | 1 271 | 952 |
| **Total assets** | | **1 829 137** | **1 737 954** |
| **Liabilities** | | | |
| Deposits of customers and loans received | 11 | 1 663 928 | 1 556 573 |
| Financial liabilities at fair value through profit or loss | | 2 | 2 |
| Accounts payable and other liabilities | | 25 253 | 61 858 |
| Subordinated debt | | 20 000 | 20 000 |
| **Total liabilities** | | **1 709 183** | **1 638 433** |
| **Owner's equity** | | | |
| Share capital | | 69 500 | 59 500 |
| Statutory reserve capital | | 2 191 | 1 492 |
| Other reserves | | 0 | 36 |
| Retained earnings | | 44 816 | 34 963 |
| **Total equity attributable to owners of the parent** | | **116 507** | **95 991** |
| Non-controlling interest | | 3 447 | 3 530 |
| **Total equity** | | **119 954** | **99 521** |
| **Total liabilities and equity** | | **1 829 137** | **1 737 954** |

# Condensed Consolidated Interim Statement of Cash Flows

| *(in thousands of euros)* | Note | Q3 2018 | 9M 2018 | Q3 2017 | 9M 2017 |
|---|---|---|---|---|---|
| **Cash flow from operating activities** | | | | | |
| Interest received | | 11 511 | 33 195 | 9 412 | 25 880 |
| Interest paid | | -1 971 | -4 731 | -1 178 | -3 258 |
| Fees and commissions received | | 4 615 | 14 152 | 3 276 | 9 522 |
| Fees and commissions paid | | -2 028 | -5 514 | -1 133 | -3 752 |
| Other income | | 770 | 827 | 1 | -35 |
| Staff costs paid | | -3 735 | -9 707 | -2 578 | -7 597 |
| Administrative and other operating expenses paid | | -2 709 | -7 790 | -2 177 | -6 154 |
| Income tax | | -631 | -1 469 | 0 | 0 |
| **Cash flow from operating activities before change in operating assets and liabilities** | | **5 822** | **18 963** | **5 623** | **14 606** |
| **Net increase/decrease in operating assets:** | | | | | |
| Net acquisition/disposal of trading portfolio | | -36 | -85 | 734 | 231 |
| Loans and advances to customers | | -37 969 | -95 788 | -53 578 | -123 928 |
| Mandatory reserve at central bank | | 92 | -994 | -2 580 | -4 950 |
| Security deposits | | -340 | -398 | -1 359 | -1 380 |
| Other assets | | 30 | 251 | -1 354 | -1 298 |
| **Net increase/decrease in operating liabilities:** | | | | | |
| Demand deposits of customers | | 83 173 | 99 289 | 279 475 | 524 308 |
| Term deposits of customers | | 13 802 | 1 768 | -20 837 | -28 294 |
| Loans received | | 6 250 | 6 250 | 0 | 0 |
| Repayments of loans received | | 0 | 0 | 0 | -779 |
| Financial liabilities held for trading at fair value through profit and loss | | -6 | -1 | 0 | -209 |
| Other liabilities | | 10 052 | -36 819 | -4 340 | -6 819 |
| **Net cash generated from/used in operating activities** | | **80 870** | **-7 564** | **201 784** | **371 488** |
| **Cash flow from investing activities** | | | | | |
| Purchase of non-current assets | | -205 | -1 171 | -264 | -736 |
| Proceeds from disposal of subsidiary | | 0 | 0 | 0 | 0 |
| Proceeds from disposal and redemption of investment securities available for sale | | 631 | 519 | 88 | 106 |
| Net change of investments at fair value through profit or loss | | 4 404 | 8 729 | -175 | 11 436 |
| **Net cash flow from investing activities** | | **4 830** | **8 077** | **-351** | **10 806** |
| **Cash flows from financing activities** | | | | | |
| Contribution in share capital | | 0 | 10 000 | 3 000 | 3 000 |
| Dividends paid | | 0 | - 3 350 | 0 | 0 |
| **Net cash from financing activities** | | **0** | **6 650** | **3 000** | **3 000** |
| **Effect of exchange rate changes on cash and cash equivalents** | | **77** | **71** | **-17** | **771** |
| **Net decrease/increase in cash and cash equivalents** | | **85 777** | **7 234** | **474 284** | **386 065** |
| Cash and cash equivalents at the beginning of the period | | 861 973 | 940 516 | 204 416 | 292 635 |
| **Cash and cash equivalents at the end of the period** | **10** | **947 750** | **947 750** | **678 700** | **678 700** |

# Condensed Consolidated Interim Statement of Changes in Equity

| *(in thousands of euros)* | Share capital | Statutory reserve capital | Other reserves | Accumulated deficit/ retained earnings | **Total equity attributable to owners of LHV Group** | Non-controlling interest | **Total equity** |
|---|---|---|---|---|---|---|---|
| **Balance as at 01.01.2017** | **56 500** | **888** | **-40** | **20 902** | **78 250** | **1 918** | **80 168** |
| Transfer to statutory reserve capital | 3 000 | 0 | 0 | 0 | 3 000 | 0 | **3 000** |
| Share options | 0 | 604 | 0 | -604 | 0 | 0 | **0** |
| Paid in share capital | 0 | 0 | 0 | 542 | 542 | 0 | **542** |
| *Profit for the year* | *0* | *0* | *0* | *10 405* | *10 405* | *1 188* | ***11 593*** |
| *Other comprehensive loss* | *0* | *0* | *82* | *0* | *82* | *0* | ***82*** |
| Total profit and other comprehensive income for the reporting period | 0 | 0 | 82 | 10 405 | 10 487 | 1 118 | **11 675** |
| **Balance as at 30.09.2017** | **59 500** | **1 492** | **42** | **31 245** | **92 279** | **3 106** | **95 385** |
| **Balance as at 01.01.2018** | **59 500** | **1 492** | **36** | **34 963** | **95 991** | **3 530** | **99 521** |
| Changes in accounting policies | 10 000 | 0 | 0 | 0 | 10 000 | 0 | **10 000** |
| Transfer to statutory reserve capital | 0 | 699 | 0 | -699 | 0 | 0 | **0** |
| Dividends paid | 0 | 0 | 0 | -2 179 | -2 179 | -1 172 | **-3 351** |
| Share options | 0 | 0 | 0 | 685 | 685 | 0 | **685** |
| *Profit for the year* | *0* | *0* | *0* | *12 046* | *12 046* | *1 089* | ***13 135*** |
| *Other comprehensive loss* | *0* | *0* | *-36* | *0* | *-36* | *0* | ***-36*** |
| Total profit and other comprehensive income for the reporting period | 0 | 0 | -36 | 12 046 | 12 010 | 1 089 | **13 099** |
| **Balance as at 30.09.2018** | **69 500** | **2 191** | **0** | **44 816** | **116 507** | **3 447** | **119 954** |

# Notes to the Condensed Consolidated Interim Financial Statements

## NOTE 1 Accounting Policies

The interim financial statements have been prepared in accordance with the international financial reporting standard IAS 34 "Interim Financial Reporting", as adopted in the European Union and accordance with International Financial Reporting Standards as adopted by European Union. The interim financial statements should be read in conjunction with the group's annual financial statements as at 31 December 2017. The accounting policies adopted are consistent with those of the previous financial year except for the financial reporting standards that are presented at the end of this report in Note 14.

The financial figures of the interim financial statements have been presented in thousands of euros, unless otherwise indicated. The interim financial statements have been consolidated and include the results of AS LHV Pank and its subsidiaries AS LHV Finance (65% interest).

## NOTE 2 Breakdown of Financial Assets and Liabilities by Countries

| **30.09.2018** | **Estonia** | **Latvia** | **Lithuania** | **Finland** | **The Netherlands** | **Germany** | **Other EU** | **USA** | **Other** | **Total** |
|---|---|---|---|---|---|---|---|---|---|---|
| Due from banks and investment companies | 940 871 | 0 | 0 | 0 | 0 | 0 | 8 703 | 11 990 | 2 554 | **964 118** |
| Financial assets at fair value | 348 | 784 | 17 204 | 0 | 0 | 1 | 22 615 | 29 | 0 | **40 981** |
| Loans and advances to customers | 773 780 | 86 | 16 858 | 1 261 | 1 | 1 | 18 561 | 176 | 1 227 | **811 951** |
| Receivables from customers | 6 254 | 1 | 5 | 0 | 0 | 0 | 0 | 0 | 0 | **6 260** |
| Other financial assets | 112 | 0 | 0 | 0 | 0 | 0 | 0 | 2 575 | 0 | **2 687** |
| **Total financial assets** | **1 721 365** | **871** | **34 067** | **1 261** | **1** | **2** | **49 879** | **14 770** | **3 781** | **1 825 997** |
| Deposits of customers and loans received | 1 067 201 | 10 217 | 754 | 4 377 | 1 205 | 5 681 | 535 382 | 2 308 | 36 803 | **1 663 928** |
| Subordinated debt | 20 000 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **20 000** |
| Accounts payable and other financial liabilities | 2 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **2** |
| Financial liabilities at fair value | 22 596 | 0 | 4 | 27 | 0 | 0 | 13 | 3 | 0 | **22 643** |
| **Total financial liabilities** | **1 109 799** | **10 217** | **758** | **4 404** | **1 205** | **5 681** | **535 395** | **2 311** | **36 803** | **1 706 573** |

Unused loan commitments in the amount of EUR 269 215 thousand are for the residents of Estonia.

| **31.12.2017** | **Estonia** | **Latvia** | **Lithuania** | **Finland** | **The Netherlands** | **Germany** | **Other EU** | **USA** | **Other** | **Total** |
|---|---|---|---|---|---|---|---|---|---|---|
| Due from banks and investment companies | 916 853 | 0 | 0 | 0 | 0 | 0 | 3 051 | 28 152 | 7 835 | **955 891** |
| Financial assets at fair value | 846 | 779 | 17 456 | 0 | 0 | 29 867 | 1 064 | 2 | 0 | **50 014** |
| Loans and advances to customers | 650 871 | 42 | 37 218 | 998 | 91 | 42 | 26 580 | 45 | 3 503 | **719 390** |
| Receivables from customers | 7 351 | 1 | 5 | 0 | 0 | 0 | 0 | 0 | 0 | **7 357** |
| Other financial assets | 109 | 0 | 0 | 0 | 0 | 0 | 0 | 2 180 | 0 | **2 289** |
| **Total financial assets** | **1 576 030** | **822** | **54 679** | **998** | **91** | **29 909** | **30 695** | **30 379** | **11 338** | **1 734 941** |
| Deposits of customers and loans received | 862 286 | 5 024 | 825 | 2 717 | 12 505 | 632 | 639 608 | 2 855 | 30 121 | **1 556 573** |
| Subordinated debt | 20 000 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **20 000** |
| Accounts payable and other financial liabilities | 2 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | **2** |
| Financial liabilities at fair value | 60 079 | 0 | 4 | 27 | 0 | 0 | 13 | 3 | 0 | **60 126** |
| **Total financial liabilities** | **942 367** | **5 024** | **829** | **2 744** | **12 505** | **632** | **639 621** | **2 858** | **30 121** | **1 636 701** |

Unused loan commitments in the amount of EUR 168 228 thousand are for the residents of Estonia and in the amount of EUR 3 300 thousand for the residents of Lithuania.

## NOTE 3 Breakdown of Assets and Liabilities by Contractual Maturity Dates

| 30.09.2018 | On demand | 0-3 months | 3-12 months | 1-5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| **Liabilities by contractual maturity dates** | | | | | | |
| Deposits from customers and loans received | 1 522 621 | 43 893 | 80 848 | 11 956 | 5 129 | **1 664 447** |
| Subordinated debt | 0 | 341 | 1 023 | 5 455 | 22 443 | **29 262** |
| Accounts payable and other financial liabilities | 0 | 22 643 | 0 | 0 | 0 | **22 643** |
| Unused loan commitments | 0 | 269 215 | 0 | 0 | 0 | **269 215** |
| Financial guarantees by contractual amounts | 0 | 10 055 | 0 | 0 | 0 | **10 055** |
| Foreign exchange derivatives (gross settled) | 0 | 34 278 | 0 | 698 | 0 | **34 976** |
| Financial liabilities at fair value | 0 | 2 | 0 | 0 | 0 | **2** |
| **Total liabilities** | **1 522 621** | **380 427** | **81 871** | **18 109** | **27 572** | **2 030 600** |
| **Financial assets by contractual maturity dates** | | | | | | |
| Due from banks and investment companies | 964 118 | 0 | 0 | 0 | 0 | **964 118** |
| Financial assets at fair value (debt securities) | 0 | 60 | 23 329 | 15 668 | 2 084 | **41 141** |
| Loans and advances to customers | 0 | 26 048 | 158 039 | 602 441 | 127 479 | **914 007** |
| Receivables from customers | 0 | 6 260 | 0 | 0 | 0 | **6 260** |
| Other financial assets | 2 687 | 0 | 0 | 0 | 0 | **2 687** |
| Foreign exchange derivatives (gross settled) | 0 | 34 276 | 0 | 700 | 0 | **34 976** |
| **Total financial assets** | **966 805** | **66 644** | **181 368** | **618 809** | **129 563** | **1 963 189** |
| **Maturity gap from financial assets and liabilities** | **-555 816** | **-313 783** | **99 497** | **600 700** | **101 991** | **-67 411** |

| 31.12.2017 | On demand | 0-3 months | 3-12 months | 1-5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| **Liabilities by contractual maturity dates** | | | | | | |
| Deposits from customers and loans received | 1 423 306 | 37 104 | 90 332 | 3 335 | 2 864 | **1 556 941** |
| Subordinated debt | 0 | 341 | 1 022 | 5 455 | 23 466 | **30 284** |
| Accounts payable and other financial liabilities | 0 | 60 126 | 0 | 0 | 0 | **60 126** |
| Unused loan commitments | 0 | 171 528 | 0 | 0 | 0 | **171 528** |
| Financial guarantees by contractual amounts | 0 | 5 999 | 0 | 0 | 0 | **5 999** |
| Foreign exchange derivatives (gross settled) | 0 | 11 825 | 0 | 661 | 0 | **12 486** |
| Financial liabilities at fair value | 0 | 2 | 0 | 0 | 0 | **2** |
| **Total liabilities** | **1 423 306** | **286 925** | **91 354** | **9 451** | **26 330** | **1 837 366** |
| **Financial assets by contractual maturity dates** | | | | | | |
| Due from banks and investment companies | 955 891 | 0 | 0 | 0 | 0 | **955 891** |
| Financial assets at fair value (debt securities) | 0 | 180 | 30 952 | 17 005 | 2 084 | **50 221** |
| Loans and advances to customers | 0 | 45 720 | 149 634 | 505 058 | 95 517 | **795 929** |
| Receivables from customers | 0 | 7 357 | 0 | 0 | 0 | **7 357** |
| Other financial assets | 2 289 | 0 | 0 | 0 | 0 | **2 289** |
| Foreign exchange derivatives | 0 | 11 825 | 0 | 661 | 0 | **12 486** |
| **Total financial assets** | **958 180** | **65 082** | **180 586** | **522 724** | **97 601** | **1 824 173** |
| **Maturity gap from financial assets and liabilities** | **-465 126** | **-221 843** | **89 232** | **513 273** | **71 271** | **-13 193** |

It is possible to take a short-term loan from the central bank against the security of the majority of instruments in the bond portfolio.
All cashflows from financial assets and –liabilities except derivatives include all contractual cash flows.

## NOTE 4 Open Foreign Currency Positions

| 30.09.2018 | EUR | CHF | GBP | SEK | USD | Other | Total |
|---|---|---|---|---|---|---|---|
| **Assets bearing currency risk** | | | | | | | |
| Due from banks and investment companies | 942 494 | 2 588 | 4 123 | 2 715 | 1 002 | 11 196 | **964 118** |
| Financial assets at fair value | 14 738 | 0 | 19 | 1 | 26 203 | 19 | **40 981** |
| Loans and advances to customers | 795 806 | 4 | 14 821 | 700 | 599 | 21 | **811 951** |
| Receivables from customers | 5 294 | 0 | 666 | 41 | 119 | 140 | **6 260** |
| Other financial assets | 614 | 0 | 0 | 0 | 2 073 | 0 | **2 687** |
| **Total assets bearing currency risk** | **1 758 946** | **2 591** | **19 629** | **3 457** | **29 997** | **11 377** | **1 825 997** |
| **Liabilities bearing currency risk** | | | | | | | |
| Deposits from customers and loans received | 1 568 513 | 2 588 | 45 406 | 5 953 | 34 136 | 7 332 | **1 663 928** |
| Accounts payable and other financial liabilities | 13 811 | 6 | 284 | 412 | 210 | 7 920 | **22 643** |
| Interest rate swaps | 0 | 0 | 0 | 0 | 2 | 0 | **2** |
| Subordinated debt | 20 000 | 0 | 0 | 0 | 0 | 0 | **20 000** |
| **Total liabilities bearing currency risk** | **1 602 324** | **2 594** | **45 690** | **6 365** | **34 348** | **15 252** | **1 706 573** |
| Open gross position derivative assets at contractual value | 698 | 0 | 25 921 | 2 912 | 5 128 | 3 575 | 38 234 |
| Open gross position derivative liabilities at contractual value | 37 536 | 0 | 0 | 0 | 698 | 0 | 38 234 |
| **Open foreign currency position** | **119 784** | **-2** | **-140** | **4** | **79** | **-300** | **119 424** |

| 31.12.2017 | EUR | CHF | GBP | SEK | USD | Other | Total |
|---|---|---|---|---|---|---|---|
| **Assets bearing currency risk** | | | | | | | |
| Due from banks and investment companies | 917 110 | 2 587 | 28 237 | 892 | 1 359 | 5 707 | **955 891** |
| Financial assets at fair value | 15 378 | 0 | 0 | 4 | 34 603 | 28 | **50 014** |
| Loans and advances to customers | 717 512 | 0 | 4 | 14 | 1 832 | 28 | **719 390** |
| Receivables from customers | 6 914 | 7 | 204 | 11 | 145 | 76 | **7 357** |
| Other financial assets | 288 | 0 | 0 | 0 | 2 001 | 0 | **2 289** |
| **Total assets bearing currency risk** | **1 657 202** | **2 594** | **28 445** | **921** | **39 940** | **5 839** | **1 734 941** |
| **Liabilities bearing currency risk** | | | | | | | |
| Deposits from customers and loans received | 1 471 237 | 2 534 | 33 134 | 3 558 | 42 646 | 3 464 | **1 556 573** |
| Financial liabilities at fair value | 56 909 | 66 | 260 | 82 | 54 | 2 775 | **60 146** |
| Interest rate swaps | 0 | 0 | 0 | 1 | 1 | 0 | **2** |
| Subordinated debt | 20 000 | 0 | 0 | 0 | 0 | 0 | **20 000** |
| **Total liabilities bearing currency risk** | **1 548 146** | **2 600** | **33 394** | **3 641** | **42 701** | **6 239** | **1 636 721** |
| Open gross position derivative assets at contractual value | 699 | 0 | 4 959 | 2 763 | 3 615 | 450 | 12 486 |
| Open gross position derivative liabilities at contractual value | 11 787 | 0 | 0 | 0 | 699 | 0 | 12 486 |
| **Open foreign currency position** | **97 968** | **-6** | **10** | **43** | **155** | **51** | **98 220** |

## NOTE 5 Breakdown of Loan Portfolio by Economic Sectors

| | 30.09.2018 | % | 31.12.2017 | % |
|---|---|---|---|---|
| Individuals | 188 550 | 22,9% | 141 199 | 19,4% |
| Real estate activities | 204 923 | 24,9% | 197 695 | 27,2% |
| Financial activities | 84 771 | 10,3% | 114 888 | 15,8% |
| Manufacturing | 89 089 | 10,8% | 68 251 | 9,4% |
| Professional, scientific and technical activities | 21 028 | 2,6% | 13 948 | 1,9% |
| Wholesale and retail trade | 24 516 | 3,0% | 21 081 | 2,9% |
| Other service activities | 9 570 | 1,2% | 15 480 | 2,1% |
| Arts and entertainment | 34 665 | 4,2% | 29 289 | 4,0% |
| Transportation and storage | 7 456 | 0,9% | 5 869 | 0,8% |
| Agriculture | 18 335 | 2,2% | 8 717 | 1,2% |
| Administrative and support service activities | 41 524 | 5,0% | 33 941 | 4,7% |
| Construction | 34 891 | 4,2% | 19 414 | 2,7% |
| Education | 2 192 | 0,3% | 2 217 | 0,3% |
| Information and communication | 4 485 | 0,5% | 8 430 | 1,2% |
| Other sectors | 56 701 | 6,9% | 45 871 | 6,3% |
| **Total** | **822 696** | **100%** | **726 290** | **100%** |
| Provision | -10 745 | | -6 900 | |
| **Total loan portfolio** | **811 951** | **100%** | **719 390** | **100%** |

Loans to related parties were 30.09.2018 EUR 3 378 thousand (31.12.2017: 39 594). At 31.12.2017 outstanding balance of loans given to related parties was EUR 36 775 thousand given to other subsidiaries of parent company AS LHV Group. Loans have been given out on market terms.

## NOTE 6 Fair Value of Financial Assets and Liabilities

The Management Board of the Group has determined the fair value of assets and liabilities recognised at amortised cost in the balance sheet. To determine the fair value, future cash flows are discounted based on the market interest curve.

The below table provides an overview of the assessment techniques, which depend on the hierarchy of assets and liabilities measured at fair value:

| | Level 1 | Level 2 | Level 3 | 30.09.2018 | Level 1 | Level 2 | Level 3 | 31.12.2017 |
|---|---|---|---|---|---|---|---|---|
| **Financial assets at fair value through profit and loss** | | | | | | | | |
| Shares and fund units | 145 | 0 | 0 | **145** | 71 | 0 | 0 | **71** |
| Available-for-sale bonds and shares | 0 | 0 | 220 | **220** | 555 | 0 | 220 | **775** |
| Bonds at fair value through profit and loss | 40 575 | 0 | 0 | **40 575** | 49 138 | 0 | 0 | **49 138** |
| Interest rate swaps and foreign exchange forwards | 0 | 41 | 0 | **41** | 0 | 30 | 0 | **30** |
| **Total financial assets** | **40 720** | **41** | **220** | **40 981** | **49 984** | **30** | **0** | **50 014** |
| **Financial liabilities at fair value through profit and loss** | | | | | | | | |
| Interest rate swaps and foreign exchange forwards | 0 | 2 | 0 | **2** | 0 | 2 | 0 | **2** |
| **Total financial liabilities** | **0** | **2** | **0** | **2** | **0** | **2** | **0** | **2** |

Hierarchy levels:

1. Level 1 – the price quoted on active market
2. Level 2 – a technique which uses market information as input (rates and interest curves of arms-length transactions)
3. Level 3 – other methods (e.g. discounted cash flow method) with estimations as input

Interest rate swaps are instruments, where the fair value is determined via the model-based approach by using the inputs available on the active market. The fair value of such non-market derivatives is calculated as a theoretical net present value (NPV), by using independent market parameters and without assuming the presence of any risks or uncertainties. The NPV is discounted by using the risk-free profitability rate available on the market.

Loans are issued in the bank's business segments on market conditions. Therefore, the fair value of loans does not materially differ from their carrying amount as at 30 June 2018 and 31 December 2017. In determining the fair value of loans, considerable management judgements are used (discounted cash flow method with current market interest is used for the valuation). Loans issued are thus categorised under hierarchy level 3.

Other receivables from customers, along with accrued expenses and other current receivables have been generated in the course of ordinary business and are subject to payment over a short period of time. Their fair value does not thus differ from the carrying amount. These receivables and payables do not bear any interest. The fair value of accounts payable, accrued expenses and other payables is determined based on hierarchy level 3.

Customer deposits with fixed interest rates are mostly short-term with the deposits priced pursuant to market conditions. The fair value of the deposits determined via discounting future cash flows does not thus materially differ from the carrying amount. In determining the fair value of customer deposits, considerable management judgements are used. Customer deposits are thus categorised under hierarchy level 3.

From all the subordinated loans are received in 2014-2016. From all the subordinated loans were received in October 2015 and the rest in 2014. Subordinated loans were issued on market terms and considering the movements in loan and interest market, we can say that the market conditions are similar as they were when issuing the subordinated loans so that the fair value of the loans does not materially differ from their net book value. In determining the fair value of loans, considerable management judgements are used. Loans issued are thus categorised under hierarchy level 3.

## NOTE 7 Net Interest Income

| **Interest income** | **Q1 2018** | **9M 2018** | **Q3 2017** | **9M 2017** |
|---|---|---|---|---|
| Business loans | 7 073 | 19 905 | 5 986 | 16 579 |
| including loans between related parties | 8 | 22 | 7 | 21 |
| Hire purchase | 999 | 3 026 | 1 015 | 3 161 |
| Leasing | 543 | 1 841 | 437 | 1 402 |
| including loans between related parties | 1 | 3 | 1 | 4 |
| Leverage loans and lending of securities | 111 | 353 | -12 | 47 |
| Bonds | 32 | 105 | 47 | 164 |
| Creditcard loans | 194 | 568 | 180 | 511 |
| Consumer loans | 1 377 | 3 820 | 1 063 | 2 858 |
| Balances with credit institutions and investment companies | 45 | 103 | 8 | 18 |
| Other loans | 981 | 3 704 | 373 | 988 |
| including loans between related parties | 8 | 21 | 7 | 19 |
| **Total** | **11 355** | **33 425** | **9 097** | **25 728** |

| **Interest expense** | | | | |
|---|---|---|---|---|
| Deposits of customers and loans received | -483 | -1 283 | -314 | -890 |
| Balances with the central bank | -886 | -2 682 | -514 | -1 058 |
| Subordinated liabilities | -340 | -1 020 | -342 | -1 027 |
| **Total** | **-1 709** | **-4 985** | **-1 170** | **-2 975** |
| **Net interest income** | **9 646** | **28 440** | **7 927** | **22 753** |

| Interest income on loans by customer location (interest on bank balances and bonds excluded): | Q3 2018 | 9M 2018 | Q3 2017 | 9M 2017 |
|---|---|---|---|---|
| Estonia | 11 278 | 32 694 | 8 825 | 24 850 |
| Lithuania | 0 | 523 | 217 | 696 |
| **Total** | **11 278** | **33 217** | **9 042** | **25 546** |

## NOTE 8 Net Fee and Commission Income

| Fee and commission income | Q3 2018 | 9M 2018 | Q3 2017 | 9M 2017 |
|---|---|---|---|---|
| Security brokerage and commissions paid | 597 | 3 152 | 566 | 2 472 |
| Asset management and similar fees | 576 | 1 827 | 424 | 1 203 |
| Currency conversion revenues | 449 | 1 111 | 163 | 665 |
| Fees from cards and payments | 2 406 | 6 354 | 1 716 | 4 244 |
| Other fee and commission income | 587 | 1 708 | 404 | 931 |
| **Total** | **4 615** | **14 152** | **3 273** | **9 515** |
| **Fee and commission expense** | | | | |
| Security brokerage and commissions paid | -142 | -417 | 214 | 169 |
| Expenses related to cards | -699 | -1 911 | -487 | -1 425 |
| Expenses related to acquiring | -759 | -2 014 | -225 | -1 102 |
| Other fee and commission expense | -428 | -1 172 | -632 | -1 387 |
| **Total** | **-2 028** | **-5 514** | **-1 130** | **-3 745** |
| **Net fee and commission income** | **2 587** | **8 638** | **2 143** | **5 770** |

| Fee and commission income by customer location: | Q3 2018 | 9M 2018 | Q3 2017 | 9M 2017 |
|---|---|---|---|---|
| Estonia | 4 615 | 14 152 | 3 273 | 9 438 |
| Latvia | 0 | 0 | 0 | 0 |
| Lihuania | 0 | 0 | 0 | 77 |
| **Total** | **4 615** | **14 152** | **3 273** | **9 515** |

## NOTE 9 Operating Expenses

| | Q3 2018 | 9M 2018 | Q3 2017 | 9M 2017 |
|---|---|---|---|---|
| Wages, salaries and bonuses | 2 463 | 7 712 | 1 988 | 6 286 |
| Social security and other taxes* | 816 | 2 356 | 655 | 1 922 |
| **Total personnel expenses** | **3 279** | **10 068** | **2 643** | **8 208** |
| IT expenses | 487 | 1 352 | 367 | 999 |
| Infoteenused ja pangateenused | 130 | 413 | 112 | 384 |
| Marketing expenses | 441 | 1 156 | 423 | 1 040 |
| Office expenses | 127 | 389 | 96 | 309 |
| Transportation and communication expenses | 50 | 141 | 47 | 133 |
| Staff training and business trip expenses | 144 | 431 | 109 | 237 |
| Other outsourced services | 466 | 1 530 | 376 | 1 151 |
| Other administrative expenses | 518 | 1 378 | 353 | 1 101 |
| Depreciation of non-current assets | 323 | 842 | 219 | 641 |
| Operational lease payments | 275 | 813 | 234 | 671 |

| | | | | |
|---|---|---|---|---|
| Other operating expenses | 78 | 188 | 60 | 131 |
| **Total other operating expenses** | **3 039** | **8 633** | **2 396** | **6 797** |
| **Total operating expenses** | **6 318** | **18 701** | **5 039** | **15 005** |

**lump-sum payment of social, health and other insurances*

## NOTE 10 Balances with the Central Bank, Credit Institutions and Investment Companies

| | **30.09.2018** | **31.12.2017** |
|---|---|---|
| Term deposits with maturity less than 3 months* | 38 071 | 35 177 |
| Legal reserve with the central bank | 16 368 | 15 375 |
| Other receivables from central bank* | 909 679 | 905 339 |
| **Total** | **964 118** | **955 891** |
| *Cash and cash equivalents in the Statement of Cash Flows | 947 750 | 940 516 |

The breakdown of receivables by countries has been presented in Note 2. Demand deposits include receivables from investment companies in the total amount of EUR 12 159 thousand (31 December 2017: EUR 14 186 thousand). All other demand and term deposits are held with credit institutions and the central bank.

The minimum reserve requirement as at 30 September 2018 was 1% (31 December 2017: 1%) of all financial resources (customer deposits and loans received). The reserve requirement is to be fulfilled as a monthly average in euros or in the foreign financial assets approved by the central bank.

## NOTE 11 Deposits of Customers and Loans Received

| **Deposits/loans by type** | **Individuals** | **Financial intermediates** | **Legal entities** | **Public sector** | **30.09.2018** |
|---|---|---|---|---|---|
| Demand deposits | 352 320 | 511 407 | 651 361 | 7 425 | 1 522 513 |
| Term deposits | 52 753 | 0 | 70 493 | 5 634 | 128 880 |
| Loans received | 0 | 0 | 12 250 | 0 | 12 250 |
| Accrued interest liability | 171 | 0 | 108 | 6 | 285 |
| **Total** | **405 244** | **511 407** | **734 212** | **13 065** | **1 663 928** |

| **Deposits/loans by type** | **Individuals** | **Financial intermediates** | **Legal entities** | **Public sector** | **31.12.2017** |
|---|---|---|---|---|---|
| Demand deposits | 278 430 | 606 600 | 531 990 | 6 203 | 1 423 223 |
| Term deposits | 51 075 | 0 | 70 221 | 5 816 | 127 112 |
| Loans received | 0 | 0 | 6 000 | 0 | 6 000 |
| Accrued interest liability | 144 | 0 | 87 | 7 | 238 |
| **Total** | **329 649** | **606 600** | **608 298** | **12 026** | **1 556 573** |

LHV Pank signed an unsecured 10-year loan agreement with the European Investment Fund (EIF) in the amount of EUR 12.5 million to increase the borrowing possibilities of small and medium-sized enterprises. As at 30.09.2018, the Bank had utilized 12 250 thousand euros of the loan amount. The nominal interest rate of the deposits of customers and loans granted equals to their effective interest rate, as no other significant fees have been implemented.

## NOTE 12 Assets Under management

| AS LHV Pank, operating as an account manager for its customers, has custody of or intermediates the following customer assets: | **30.09.2018** | **31.12.2017** |
|---|---|---|
| Cash balance of customers | 9 905 | 10 266 |
| Securities of customers | **1 406 561** | **1 277 535** |
| *Incl. parent company* | *93 100* | *84 300* |

| | | |
|---|---|---|
| *Incl. shareholders of the parent company and related entities* | *180 171* | *168 637* |
| **Total** | **1 416 466** | **1 287 801** |

## NOTE 13 Contingent Liabilities

| Irrevocable transactions | Performance guarantees | Financial guarantees | Letter of credit | Unused loan commitments | Total |
|---|---|---|---|---|---|
| Liability in the contractual amount as at 30 September 2018 | 11 530 | 10 055 | 85 | 269 215 | **290 885** |
| Liability in the contractual amount as at 31 December 2017 | 10 129 | 5 999 | 51 | 171 528 | **187 707** |

## NOTE 14 Changes in accounting policies

**FINANCIAL ASSETS AND LIABILITIES**
**Financial assets**

Financial assets are recognised on the statement of financial position when the Group becomes a party to the contractual provisions of the instrument and are measured at fair value on initial recognition. Transaction costs are included in the fair value on initial recognition except for financial assets at fair value through profit or loss where transaction costs are expensed in profit or loss. Financial assets are derecognised when the rights to receive cash flows have expired, the Group has transferred substantially all risks and rewards and upon substantial modification. Transfers of financial assets with retention of all or substantially all risks and rewards include for example repurchase transactions and securities lending transactions. Financial assets at fair value are recognised on the statement of financial position on trade date. Financial assets measured at amortised cost are recognised on trade date. The Group classifies and subsequently measures its financial assets in the following categories: financial instruments at fair value through profit or loss; fair value through other comprehensive income and amortised cost. The classification will depend on if the financial asset is a debt instrument, an equity instrument or a derivative.

Debt instruments (Loans and debt securities)

The classification is based on a combination of assessing the business model for managing the financial assets and whether the contractual cash flows consist of solely payments of principal and interest ('SPPI'). The business model assessment is performed for homogenous portfolios/products identified based on how the business is managed in the divisions of the Group. The assessment is based on reasonable scenarios taking into consideration how the portfolio is evaluated and reported to management; the risks affecting the performance of the portfolio and how these risks are managed; how managers are compensated; and the frequency, value and timing of sales including the reasons for the sales. In determining if the cash flows consist solely of principal and interest, the principal is defined as the fair value of the debt instrument at initial recognition, which can change over the life if there are repayments or capitalisation of interest. Interest cash flows are consistent with components per a basic lending arrangement including consideration for time value of money, credit risk, liquidity risk as well as administrative costs and profit margin. If there are contractual features introducing an exposure to other risks or volatility, it is not considered to consist of solely payments of principal and interest. SPPI tests are performed as a part of new product approval tests. In implementation of IFRS 9 SPPI was applied to 22 larger products carried at amortised cost. All products exept one remained in accounting with same treatment. With remaining one – margin loan, the product conditions were changed so that one functionality was taken out of the product and then product passed SPPI. All the LHV products remained with same accounting treatment as before.

Debt instruments are presented in the statement of financial position line items: Due from central banks, credit institutions and investment companies; Loans and advances to customers; Available-for-sale financial assets; Financial assets at fair value through profit or loss; Receivables from customers and Other financial assets, and include instruments in the following measurement categories.

Fair value through profit or loss: Debt instruments are classified in this category if not meeting the criteria for amortised cost or fair value through other comprehensive income. This is the case if the business model is held for trading; where financial assets are considered held for trading if they are held with the intention to be sold in the short-term and for the purpose of generating profits. Debt instruments are mandatorily measured at fair value through profit or loss if the assets are managed and evaluated on a fair value basis or the assets are held with an intention to sell, or alternatively, if the cash flows do not consist of solely payments of principal and interest.

Fair value through other comprehensive income: Debt instruments are classified in this category if both of the following criteria are met (a) the business model objective is to both hold assets to collect contractual cash flows and to sell the assets (b) the contractual cash flows consist of solely payments of principal and interest. The assets are measured at fair value and gains and losses arising from changes in fair value are reported in other comprehensive income and accumulated in equity. The cumulative gain or loss is reclassified from equity to profit or loss upon derecognition of the debt instrument. Interest is calculated by applying the effective interest method on interest-bearing financial assets and expected credit losses are recognised in profit or loss.

Amortised cost: Debt instruments are classified in this category if both of the following criteria are met (a) the business model objective is to hold assets to collect contractual cash flows and (b) the contractual cash flow characteristics consist of solely payments of principal and interest. The gross carrying amount of these assets is measured using the effective interest method and adjusted for expected credit losses.

Equity instruments

Equity instruments are per default classified as financial assets at fair value through profit or loss. An irrevocable election can be made on initial recognition to classify equity instruments (not held for trading) at fair value through other comprehensive income.

Derivatives

Derivatives are classified as fair value through profit or loss (held for trading).

**Modification**

The Group may renegotiate loans and modify contractual terms. If the new terms are substantially different from the original terms, the Group derecognises the original financial asset and recognises a new asset. The Group also assesses whether the new financial asset is credit-impaired at initial recognition. If the terms are not substantially different, the modification does not result in derecognition and the Group recalculates the gross carrying amount based on the new cash flows using the original effective interest rate of the financial asset and recognises a modification gain or loss.

**Reclassification**

In rare circumstances debt instruments (financial assets) excluding those designated at fair value through profit or loss on initial recognition, can be reclassified if there has been a change in the business model for managing the financial asset.

**Financial liabilities**

Financial liabilities are measured at fair value on initial recognition. In case the financial liabilities are measured at fair value through profit or loss, transaction costs directly attributable to the acquisition or the issuance of the financial liability are recognised in profit or loss. For other financial liabilities direct transaction cost are recognised as a deduction from the fair value.

Financial liabilities are derecognised when extinguished, that is, when the obligation is discharged, cancelled or expired.

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss are either classified as held for trading or designated as fair value through profit or loss on initial recognition (fair value option).

Financial liabilities held for trading are primarily derivatives not designated as hedging instruments.

Other financial liabilities

The category other financial liabilities primarily include the Group's short-term and long-term borrowings. After initial recognition other financial liabilities are measured at amortised cost, using the effective interest method. The statement of financial position line items Deposits from customers and loans received, Accounts payable and other liabilities and Subordinated debt are included in this category.

**Offsetting financial assets and liabilities**

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legal right to offset transactions and an intention to settle net or realise the asset and settle the liability simultaneously.

**Embedded derivatives**

Some combined contracts contain both a derivative and a non-derivative component. In such cases, the derivative component is termed an embedded derivative. If the host contract is a financial asset in scope of IFRS 9 the contract is assessed for classification in its entirety and the embedded derivative is not separated.

**Repurchase agreements**

When the Group borrows or purchases securities subject to a commitment to resell them (a 'reverse repo'), the securities are not included in the statement of financial position. Payments made are recognised as Loans and advances to customers. Reverse repurchase agreements are measured at amortised cost.

**REVENUES AND EXPENSES**

**Interest income and interest expense**

The effective interest method is applied to recognise interest income and interest expenses in profit or loss for financial assets and financial liabilities measured at amortised cost.

The effective interest method is a method of calculating the gross carrying amount of a financial asset or the amortised cost of a financial liability and of allocating interest income and interest expenses. The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial instrument. When calculating future payments, all payments included in the terms and conditions of the contracts, such as advance payments, are taken into consideration. The calculation of the effective interest rate includes fees that are an integral part of the effective interest rate. However, expected credit losses are not taken into account.

If a financial asset subsequently has become credit impaired the interest income is recognised applying the effective interest rate to the amortised cost, i.e. gross carrying amount adjusted for the loss allowance. In case a financial asset is credit-impaired at initial recognition, the expected credit losses are included in the estimated cash flows to calculate a credit adjusted effective interest rate which then is applied to recognise the interest income.

**Fee and commission income**

The recognition of revenue from contracts with customers is reported as fee and commission income. This does not apply for revenue from leasing contracts or financial instruments and other contractual obligations within the scope of IFRS 9 Financial Instruments.

Fees that are included in the calculation of the effective interest rate of a financial instrument measured at amortised cost, such as loan origination fees, are allocated over the expected tenor of the instrument applying the effective interest method and presented in Net interest income.

Fee and commission income is recognised to depict the transfer of promised services to the customers in an amount that reflects the consideration to which LHV expects to be entitled in exchange for the service. The major types of fees are described below.

Fee and commission income for asset custody and asset management to customers is recognised as revenue over the period in which the services are provided. Performance based fees are recognised when it is highly probable that a significant reversal of recognised revenue will not occur, which is most often when the performance criteria are fulfilled.

Brokerage fees, commission and fees from negotiating a transaction for a third party, such as arrangement of acquisitions or purchase or sale of a business, are recognised on completion of the transaction.

Expenses that are directly related to the generation of fee and commission income are recognised as fee and commission expense.

**Net financial income**

Gains and losses arising from changes in fair value of financial assets and liabilities measured at fair value through profit or loss are reported under the item Net financial income. For financial liabilities designated at fair value through profit or loss the change in fair value relating to change in own credit risk is accounted for in other comprehensive income.

**Dividend income**

Dividends are recognised when the entity's legal right to receive payment is established.

**EXPECTED CREDIT LOSS**

**Measurement**

The impairment requirements are based on an expected credit loss (ECL) model. The guiding principle of the ECL model is to reflect the general pattern of deterioration or improvement in the credit quality of financial instruments.

All financial assets measured at amortised cost and fair value through other comprehensive income, as well as lease receivables, financial guarantees contracts, contract assets and certain loan commitments are in scope for expected credit loss.

ECLs on financial assets measured at amortised cost and lease receivables are presented as allowances, i.e., as an integral part of the measurement of those assets in the statement of financial position. The allowance reduces the gross carrying amount. ECLs on loan commitments and financial guarantee contracts are presented as provisions, i.e., as a liability, in the statement of financial position. Adjustment to the loss allowance and provision due to changes in ECLs is recognised in the statement of profit or loss as net expected credit losses.

The assessment of credit risk, and the estimation of ECL, shall be unbiased and probability-weighted, and shall incorporate all available information which is relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. LHV uses both models and expert based individual assesments for calculating ECLs.

The ECL model has a three-stage approach based on changes in the credit risk. A 12-month ECL (Stage 1) applies to all items, unless there is a significant increase in credit risk since initial recognition. For items where there is a significant increase in credit risk (Stage 2) or in default (Stage 3), lifetime ECL applies.

**Significant increase in credit risk**

At the end of each reporting period the Group performs an assessment of whether credit risk has increased significantly since initial recognition. The assessment of whether there has been a significant change in credit risk is based on quantitative and qualitative indicators. Indicators include payments that are past due >30 days and <90 days and financial assets that have been classified as watch-list or with forbearance measures (loans whose contractual terms have been revised due to the customer's financial difficulties). A quantitative indicator is calculated based on the change in lifetime probability of default (PD) by comparing the scenario-weighted lifetime PD at the reporting date with the scenario-weighted lifetime PD at initial recognition. In case there has been a significant increase in credit risk since initial recognition, an allowance for lifetime ECL shall be recognised and the financial instrument is transferred to Stage 2. The approach is symmetrical, meaning that in subsequent reporting periods, if the credit quality of the financial instrument improves such that there is no longer a significant increase in credit risk since initial recognition, the financial assets moves back to Stage 1.

**Definition of default**

Financial instruments in default are in Stage 3. LHV applies a definition of default for accounting purposes that is consistent with how it is defined in the capital requirements regulation, which includes financial assets past due more than 90 days. All financial assets in Stage 3 are considered credit-impaired.

**Modelling**

The ECL is calculated as a function of the probability of default (PD), the exposure at default (EAD) and the loss given default (LGD), as well as the timing of the loss. The Group's IFRS 9 methodology for ECL measurement is based on existing internal scoring and rating models.

PD represents the likelihood that a loan will not be repaid and will go into default in either a 12-month or lifetime horizon. The expected PD for each individual instrument incorporates a consideration of past events, current market conditions and reasonable and supportable information about future economic conditions. LHV uses existing scoring and rating models that are adjusted according to specific IFRS 9 requirements. The models are calibrated based on a combination of assets class and product type.

EAD represents an estimate of the outstanding amount of credit exposure at the time a default may occur. For off-balance sheet amounts, EAD includes an estimate of any further amounts to be drawn at the time of default. LGD is the amount that may not be recovered in the event of default. LGD takes into consideration the amount and quality of any collateral held. LHV uses existing LGD models adjusted to meet IFRS 9 requirements. When measuring ECL, LHV uses the maximum contractual period during which LHV is exposed to risk.

**Forward-looking information**

The Group uses internally developed macroeconomic forecasts as the basis for the forward-looking information incorporated in the ECL measurement. In order to ensure an unbiased estimation of credit losses under IFRS 9, at least three scenarios shall be used. One of the scenarios shall be the base case scenario, representing the most likely outcome, which is also applied in the regular financial planning and budgeting process, while other case scenarios shall represent more optimistic or pessimistic outcomes.

Forecasts are developed internally in the Credit Management Department that consults with the experts from Risk Control Unit, business and finance. As available without undue cost, external experts and externally developed ‘benchmark forecasts’ should be consulted. The referred benchmark forecasts include but are not limited to World Economic Outlook by the IMF, European Economic Forecasts by the European Commission and Economic Forecasts by Bank of Estonia. The scenarios shall be approved by the Risk and Capital Committee.

Scenarios should be developed for a time horizon over which reliable projections can be made, typically for a time horizon of 3 years. At minimum, selected macro indicators have to be forecasted for a period of two years following the current year. In general, scenarios shall be reviewed on a quarterly basis. In case of significant changes in the macroeconomic environment and outlook, the scenarios shall be updated.

**Individual assesments and Management´s judgement**

The Group uses both models and expert based judgement in order to determine ECLs. The degree of judgement that is required to estimate ECL depends on the model outcome, materiality and the availability of detailed information. The model provides guidance and transparency as to how economic events could affect the impairment of financial assets. Expert based judgement may be applied to the modelled outcome to incorporate an estimated impact of factors not captured by the model. Such individual ECL assesments may be applied to significant exposures at a counterparty level. These assesments are decided by the Credit Committee. In addition there may be a need for adjustments at a portfolio level, which is decided by the Risk and Capital Committee.

**New and amended critical judgements for IFRS 9 and IFRS 15 from 2018**

**EXPECTED CREDIT LOSS MODEL**

When calculating expected credit loss (ECL) there are a number of key concepts that require a high level of judgement. Estimating expected credit loss is, by its very nature, uncertain and the accuracy of these estimates depends on many factors, e.g. macroeconomic forecasts and involves complex modelling and judgements. The assessment of significant increase in credit risk is a new concept under IFRS 9 Financial Instruments and will require significant judgement. At the end of each reporting period the Group shall perform an assessment of whether credit risk has increased significantly since initial recognition by considering the change in the risk of default occurring over the remaining life of the financial instrument, using key risk indicators that are used in the Group’s existing risk management processes. Another area requiring significant judgement is the incorporation of forward-looking information and macroeconomic scenarios. IFRS 9 requires an unbiased and probability-weighted estimate of credit losses by evaluating a range of possible outcomes that incorporates forecasts of future economic conditions. LHV uses internally developed macroeconomic forecasts as the basis for the forward-looking information in the ECL measurement. LHV uses both models and expert based judgement in order to determine ECLs. The objective of applying expert based judgement is to incorporate the estimated impact of factors not captured in the modelled ECL. The degree of judgement that is required to estimate expected credit losses depends on the outcome from calculations, materiality and the availability of detailed information. The models, assessment and assumptions are regularly reviewed by the risk organisation of the Group and approved by the Group Risk Committee.

**FEE AND COMMISSION INCOME**

In recognising fee and commission income LHV makes judgements to determine the amount and timing of revenue from contracts with customers.

When LHV performs e.g. custody, asset management or administration of clients investment policies the fees are based on the time period the service is provided and/or on the amounts of underlying assets. LHV’s judgement is that the customer simultaneously receives and consumes the service and LHV’s obligations are therefore satisfied over the time the service is provided.

When LHV performs e.g. brokerage, negotiations of transactions for third parties such as arrangement of acquisitions or purchase or sale of businesses or acts as an arranger in loan syndications LHV’s judgement is that the customer obtains control of the asset and LHV’s obligations are satisfied at the time of the completion of the transaction.

When fees are based on LHV’s performance LHV recognise revenue based on judgements when it is highly probable that a significant reversal of recognised revenue will not occur, which is most often when the performance criteria are fulfilled.

**ASSETS RECOGNISED FROM THE COSTS TO OBTAIN OR FULFIL A CONTRACT, DEFERRED ACQUISITION COSTS**

LHV recognise as an asset, costs to obtain contracts that would not have incurred if the contract had not been obtained, mainly sales commissions to obtain investment contracts.

The amortisation period for the asset is based on assumptions about average lifetime of the contracts including assumptions about surrenders and lapses.

# General information

| | |
|---|---|
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