AS LHV Pank
Group Annual Report 2022

(Translation of the Estonian original)

Consolidated Annual Report **1 January 2022 – 31 December 2022**

Legal name	**AS LHV Pank**
Commercial Registry no.	**10539549**
Legal address	**Tartu mnt 2, 10145 Tallinn**
Phone	**(372) 6800400**
Fax	**(372) 6800410**
E-mail	**lhv@lhv.ee**
Main activities	**Banking** **Leasing and other lending** **Financial advisory** **Security brokerage**
Financial year	**1 January – 31 December**
Management Board	**Kadri Kiisel (Chairman)** **Andres Kitter** **Indrek Nuume** **Jüri Heero** **Meelis Paakspuu** **Martti Singi**
Supervisory Board	**Madis Toomsalu** **Rain Lõhmus** **Andres Viisemann** **Tiina Mõis** **Raivo Hein** **Heldur Meerits**
Auditor's legal name	**KPMG Baltics OÜ**
Auditor's Commercial Registry no.	**10096082**
Auditor's legal address	**Narva mnt. 5, 10117 Tallinn, Estonia**

Company's consolidated financial statements in pdf-format without European Single Electronic Format (ESEF) markups.
The link to original document: https://investor.lhv.ee/en/reports/

Mandatory elements of the basic taxonomy of the ESEF

Name of reporting entity or other means of identification	**AS LHV Pank**
Explanation of change in name of reporting entity or other means of identification from end of preceding reporting period	**No changes**
Domicile of entity	**Tartu mnt 2, Tallinn, 10145, Republic of Estonia**
Legal form of entity	**Public Limited Company**
Country of incorporation	**Republic of Estonia**
Address of entity's registered office	**Tartu mnt 2, Tallinn, 10145, Republic of Estonia**
Principal place of business	**Republic of Estonia**
Description of nature of entity's operations and principal activities	**Banking, leasing and other lending, financial advisory, security brokerage**
Name of parent entity	**AS LHV Group**
Name of ultimate parent of group	**AS LHV Group**

Table of contents

Management report

Business overview

Our vision is encouraging people and businesses think big and act big.

Our mission is to provide better access to financial services and capital.

LHV's values are simple, supportive, and effective.

AS LHV Pank ('the Bank' or 'LHV Pank') is the largest domestic bank in Estonia. We focus on active and independent customers with an entrepreneurial mindset. Our services for private customers include management of daily financial affairs and home loans. Our competitive edge is the best customer experience and offering customers the best options for growing their money. Our services for business customers include flexible and tailored financing solutions and management of daily financial affairs, and our services for financial intermediaries include a single banking platform for both EUR and GBP payments. LHV Pank's products and services are simple, transparent, and relevant. We communicate with customers mainly through modern digital channels and use the resulting cost savings for the benefit of our customers by keeping the prices of everyday banking services affordable.

With a market share of more than 15% in the Estonian daily banking, deposit, and business loan segments, LHV Pank is currently the third largest bank in the daily banking and deposit segments. Estonia is our home market where we wish to be as strong as possible. Our long-term goal is to become the largest and most profitable bank in Estonia, while focusing on efficiency, innovation and best-in-class service. By offering the best market expertise, a proactive approach and services that are innovative and the fastest in the market, we make an impact on entrepreneurship and people's financial behaviour. The Bank defines itself as a local bank offering the full range of services to customers that keep their funds at the Bank and actively use the Bank's services.

The Bank has offices in Tallinn, Tartu, Pärnu and a branch in London. Pärnu office was opened in March 2022. The Bank's consolidated financial statements comprise the accounts of the Bank and its 65% subsidiary AS LHV Finance ('LHV Finance'), which specialises in consumer financing (together referred to 'the Group' or 'LHV').

1. Business activities

2022 was largely impacted by the war in Ukraine and the impact it had on already increasing inflation rate. For first two quarters of the year the Bank was adjusting with the new reality and economic conditions. New environment impacted plans towards increasing volumes and fees from investment and forex services, but second half of the year was largely impacted by the changes in European Central Bank's decisions regarding interest rates that effected positively net interest fees from loan portfolio. New challenges arose after numerous new sanctions packages were introduced in a short period of time and affected screening and monitoring systems and processes, resulting in increased number of staff.

Still, the Bank continued to grow in 2022. The number of customers increased by 57,000 to 378,000, i.e., by 18%. The growth in customer activity and business volumes was broad-based. The Bank's UK branch number of customers is approximately 200 financial intermediaries, who in turn have over 10 million end-customers across the world.

2. Development activities

Several new products and improvements were introduced during the year. Since the beginning of the year, the Bank started offering virtual cards to customers leading the way towards plastic free everyday banking solutions. More focus was set to merchants offering them payment collection services and overdraft. In March we opened a brand-new office space and branch in Pärnu, building a larger presence in the western region of Estonia. In cooperation with Bitstamp the Bank also started offering customers the opportunity to trade with crypto assets.

Several improvements were made to existing products and processes to improve convenience and speed as the main foundation of great customer experience. Customers can get almost instant offer to a car leasing application and fractional shares were added to growth account product range. From academic year that started on 2022, the conditions of the national student loan were changed, and banks have more flexibility in offering the product. The Bank used the opportunity and improved the product, processes and experience resulting in record growth in the student loan portfolio and market share. The user interface of the Internet bank was updated with a modern look and biometric identification was added to authentication solutions. During 2022 LHV further strengthened the real-time payments product portfolio. In addition to the SEPA real-time payments, LHV customers can take advantage of the euro TIPS real-time payments. In the UK we connected to the local BACS payment scheme.

The increasing financial crime requires constant investments into effective tools, better industry-wide data-sharing, and data quality. LHV has launched multiple risk management initiatives, such as the Confirmation of Payee and MITS. But above all, the engineering and product teams focused on building the LHV UK infrastructure. At the beginning of the year the Bank launched a new intelligence sharing platform Salv Bridge which helps exchanging sensitive AML intelligence easily, securely, and almost instantly with different peers.

3. Organisation

The Bank is divided into eight functional areas, each with its own departments. Business areas include retail banking, corporate banking and financial intermediation. Support areas include IT, financial management and support services, risk management, product management and credit risk management. Human resource management, marketing and communication, compliance and ESG are bank-wide activities. The Bank's UK branch is part of the financial intermediation area.

In 2022, the number of the Group' employees increased by 163 to 785, including inactive and part-time staff and the 24 employees of LHV Finance. The number of active staff converted to the full-time equivalent was 719

The year brought several awards and accolades. Once again, LHV Pank was named the bank with the best customer service in Estonia in a survey conducted by the market research company Dive. The Bank ranked first in the Most Attractive Employers survey conducted by the job portal CVKeskus.ee and first in financial sector and top-of-mind category in the TOP Employer survey conducted by the job portal CV-Online Estonia. The Bank also received several high rankings in the employer reputation survey conducted by employer branding agency Instar by being the most attractive employer among economics students and experienced employees. The Bank’s staff satisfaction survey Q12 reflected continuously a very high level of satisfaction. City Plaza building, where the Bank’s Tallinn office is established, has a BREEAM (Building Research Establish Environmental Assessment Method) certificate. Both Euromoney and The Banker magazine of the Financial Times named LHV Pank the best bank in Estonia, for the fifth and fourth year in a row, respectively.

4. Sustainability at LHV Pank

LHV supports the national climate strategy and makes an effort in reducing our environmental impact. In LHV, we understand the central role which the financial sector plays in the shift of the economy – through lending and investing banks can channel capital flows into sustainable activities that support the transition to a climate-neutral economy. Since 2020, LHV Group has been a member of the United Nations Environment Programme Finance Initiative (UNEP FI), which is a single framework for sustainable banking developed through a partnership between banks worldwide and the United Nations.

The Principles for Responsible Banking (PRB) set out the banking industry’s role and responsibility in shaping a sustainable future and in aligning the banking sector with the objectives of the UN Sustainable Development Goals and the Paris Climate Agreement. They also enable banks to embed sustainability across all business lines, identity the main impact areas of the bank as well as set targets.

In 2022, the Bank moved a considerable step closer to our sustainability goals regarding metrics, regulatory understanding as well as ESG governance, credit portfolio analysis and risk management processes. From the beginning of 2023, we will hold monthly ESG Steering Committee meetings for our bank management to further enhance sustainability governance. We have continued with integrating ESG principles into our credit decision-making process by developing an ESG risk score model, as well as updated our sustainability-related questionnaire of the credit application. We started measuring and disclosing the climate impact of our loan portfolio and will continue to improve the data quality to report more accurate findings. Based on the analysis, we can determine the most emission-intensive sectors and take further actions to reduce emissions within these areas.

LHV is committed to its positive social impact and responsibility. This year we were recognised as the most attractive employer in Estonia and have taken seriously our focus on organisational development and employee well-being even through the uncertainties and physical limitations the past few years have brought about. Where possible, the Bank supports enterprises and initiatives that contribute to the development of the Estonian society. In leading the discussions on inclusive economies and supporting various culturally and socially important initiatives, LHV continues to contribute to the pursuit of innovative ideas and projects which improve life in Estonia.

Business environment

The keyword for 2022 in the global economy was certainly price increase. No major economic region was left untouched. In both Europe and the US, consumer prices rose by just under 10% on average over the year, while the price increase was somewhat slower in Asia. Particularly worrying is the situation in Europe, where, in addition to rapid price rises, the issue of security of energy supply has become a serious concern and many large companies are making plans to downsize or even relocate. In the context of the global economy, the biggest drag on growth is China, which struggles with corona pandemic and continues to deal with problems in the over-leveraged real estate sector.

Europe's economy has remained surprisingly strong despite rapid price increases. The strong impact of the lifting of corona restrictions and the easing of supply chain constraints supported the economy until early autumn, when reduced confidence and weaker export performance became more apparent. Although growth slowed in Q3, the economy grew by 5.4% YoY in the first nine months of the year. The year was not the most successful for Estonia's main trading partners, as both Finland and Latvia were more exposed than average to supply chains from Russia, and Sweden's overheated construction and real estate markets reacted strongly to monetary policy changes.

The labour market situation in the euro area remains strong and the economic slowdown has not had much impact yet. The unemployment rate was a record low 6.5% in October. Unemployment levels vary across countries, reaching close to 12% in Greece and Spain and just over 2% in the Czech Republic. The difference is even greater when looking at unemployment levels by age. In Spain, around a third of young people (up to 25 years old) are unemployed, compared to just 5% in the Czech Republic and Germany. Estonia is at the same level as the European average, at around 15%.

Annual inflation in the euro area slowed to 10% in November. It also meant that price growth slowed for the first time since June 2021. The impact of energy prices on price increases has gradually started to diminish, as global commodity prices have fallen. At the same time, Europe is still going through the peak of food price rises, which means there is no reason to expect a rapid dissipation of inflation. Core inflation, i.e., consumer price inflation excluding energy and food, remained stable at 5% at the end of the year.

Against a backdrop of rapid inflation, the European Central Bank has taken decisive monetary policy steps to bring price rises back under control. Since July, base rates have been raised in total by 2.5% in four consecutive meetings. The heads of the European Central Bank expect interest rates to continue to rise and, once they have reached the necessary level, to remain higher than normal for a longer period. In addition to raising interest rates, the first decisions were taken last year to overhaul the asset purchase programme. From March 2023, the volume of securities held will be reduced by 15 billion euros per month. The tactics of the Central Bank have also clearly recognised the high indebtedness of some euro area countries, which is why it remains flexible in reducing the size of its asset purchase portfolio and responds to market needs.

Changes in monetary policy were also reflected in market interest rates, which jumped in the second half of last year. By the end of the year, the 6-month Euribor rate reflected in the majority of loan agreements had risen to 2.7%, which is comparable to the average Euribor level if the period of negative interest rates (since 2015) is excluded from the reference period. According to market expectations, the 6-month Euribor rate will rise to 3.5–4% by the summer of 2023 and then start to gradually decline.

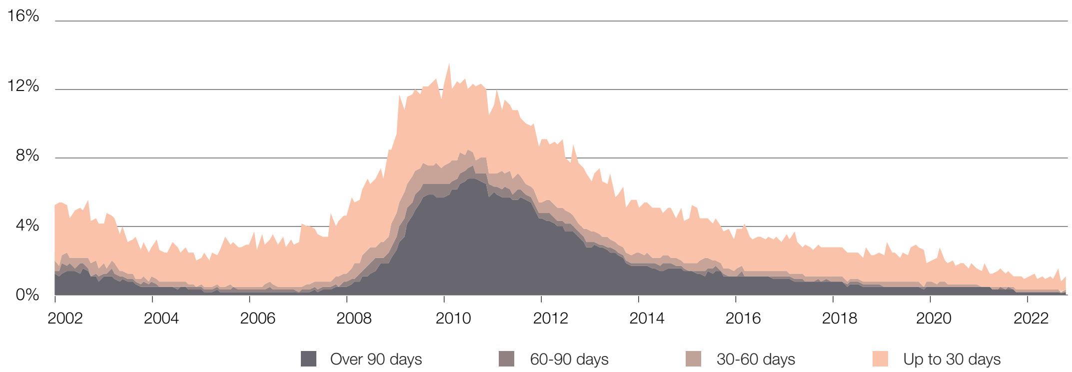
Estonia's growth already came to a standstill at the beginning of 2022, and from then on, the quarter-on-quarter comparison only showed a decline. While Estonia's economy was one of the best performers in Europe in 2021, last year was the opposite. As a result of the loss of confidence brought about by the war, and the general uncertainty about energy security and prices, companies were less willing to make prudent investments, putting many expansion plans on hold and consolidating the activities where possible. While in the first half of the year there were still sufficient orders from across the border, in the second half of the year external demand weakened significantly.

In terms of activities, the economy was mainly supported by services and domestic demand. In the first nine months of the year, professional, scientific, and technical activities grew by 24%, transport and storage by 6%, construction by 7%, and information and communication by 8%. The accommodation and food services sector, which had been hit by the pandemic, managed to make a clear recovery, growing above pre-pandemic levels. At the same time, industrial growth remained at a few percent. A peculiar contradiction emerged in the energy sector, which could have been very successful in the face of high energy prices and possible energy shortages, but according to official statistics, the value added generated in the first nine months of the year was 21% lower than in 2021.

Price growth in Estonia was just under 20% last year. With such rapid price growth, Estonia was clearly in the lead among European countries. Slightly less than half of the increase came from housing-related costs, while just under a fifth came from higher food and transport costs. Towards the end of the year, the share of energy costs started to decline as energy commodity prices fell somewhat from their peak and stabilised. At the same time, food price inflation, which had not yet shown signs of easing by the end of the year, started to contribute more. Both types of expenditure account for a very large share of the average Estonian consumer basket, which is one of the reasons why price growth in Estonia was so much higher than the European average.

Despite rapid price increases and a cooling economy, household finances remained strong in 2022. In the second half of the year, the volume of deposits started to fall gradually, as consumers had to start using savings to cope with rising prices. At the end of the year, however, household deposits were at the same level as a year earlier. The loan balance in the economy as a whole increased by 10% (including loans to households by 9% and business loans by 10%) and credit quality remained good, with the share of overdue loans in the loan portfolio declining year-on-year.

Market average share of overdue loans in loan portfolio, %



Source: Bank of Estonia

Various forecasts show that Estonia's gross domestic product in 2022 will remain at the same level as in the previous year or decline slightly. Growth is also projected to be essentially zero in 2023, as rapid inflation has reduced household purchasing power and private consumption cannot continue to grow at its previous pace. A broader economic recovery could start in the second half of 2023, with prices gradually easing, and reach a growth rate of 3.1% by 2024.

Key economic indicators of Estonia* **Bank of Estonia forecast**

	2016	2017	2018	2019	2020	2021	2022E	2023E	2024E	2025E
Nominal GDP (EUR billion)	21.8	23.8	25.8	27.7	26.8	31.4	36.1	38.4	40.2	42.8
GDP volume**	3.2%	5.8%	4.1%	4.1%	-3.0%	8.1%	-0.5%	0.4%	3.1%	4.4%
Private consumption expenditures***	4.5%	2.5%	4.3%	4.1%	-2.5%	6.9%	2.8%	-1.1%	2.1%	4.4%
Government consumption expenditures	2.5%	1.9%	1.0%	3.0%	3.0%	3.9%	0.4%	3.9%	-2.9%	-0.2%
Fixed capital formation	5.1%	13.9%	-0.1%	6.1%	19.9%	7.0%	-15.9%	-0.5%	5.1%	5.6%
Exports	4.8%	4.8%	3.9%	6.5%	-5.0%	20.0%	4.1%	-0.1%	2.8%	3.4%
Imports	6.5%	4.0%	5.7%	3.8%	0.9%	21.3%	4.2%	-5.4%	1.5%	2.6%
CPI	0.1%	3.4%	3.4%	2.3%	-0.4%	4.6%	19.4%	9.3%	2.8%	2.2%
Unemployment rate (% of the labour force)	6.8%	5.8%	5.4%	4.4%	6.9%	6.2%	5.7%	8.5%	8.7%	7.6%
Current account (% of GDP)	1.9%	3.3%	1.8%	2.0%	-0.3%	-1.8%	0.3%	1.4%	0.1%	0.6%
Budget balance (% of GDP) ****	-0.3%	-0.4%	-0.5%	0.1%	-5.6%	-2.4%	-1.9%	-4.6%	-3.8%	-3.1%

* The figures reported are annual changes in percentage terms unless otherwise indicated; ** GDP and its components are chain-linked; *** Including NPISH; **** The budget balance forecast considers only those measures on which sufficient information was available at the date of the forecast.

Sources: Bank of Estonia, Statistics Estonia

Financial results

Deposits from customers decreased by 15% to EUR 4,957 million. Deposits from ordinary customers grew by 2% to EUR 3,675 million and deposits from financial intermediaries decreased by 43% to EUR 1,281 million. Modest growth in ordinary customers deposits resulted from the changes in the economic environment where increased prices started effecting customers savings buffers. Decrease in financial intermediaries' deposits is the opposite effect of surge taken please in Q4 2021 due to volatility in the prices of virtual currencies. In 2022, the Bank did not actively raise funds through deposit platforms as there was no need. Deposit balances of deposit platforms decreased to almost non-existent.

The Group's loan portfolio grew by 19% to EUR 3,187 million during the year. Corporate loans grew by 17% to EUR 1,731 million and retail loans by 22% to EUR 1,365 million. The breakdown of the retail loan portfolio was as follows: home loans 81%, leases 11% and other loans 8%.

The Group's total assets decreased by 11% to EUR 6,057 million in 2022. The main factor behind the decrease has been a decrease in financial intermediaries' deposits and the volatile growth in 2021 was rather an anomaly. Balances have grown for all other customer groups and loans portfolios.

The Group's net profit for the year grew by 26% to EUR 80.9 million. Total income grew by 26%, total expenses grew by 31%. Net interest income increased through growth in corporate and home loan portfolios, but great positive impact arose from European Central Bank positive interest rate decisions to tackle high inflation rates in Europe. The rise in net fee and commission income was modest 4%. It was mainly impacted by the changes in the economic environment resulting in lower fees than planned from investment services and financial intermediaries' forex services. Credit losses increased by EUR 3 million over the year but were over EUR 6 million less than initially planned. Credit portfolio maintained historically highest quality and the share of non-performing loans was extremely low. Results for the year include also deferred tax expense for 2022 of EUR 13.3 million payable on the expected future dividend payment, which must be recognised in accordance with the IFRS (EU) accounting rules (IAS 12.40). The Group's performance indicators were solid: return on equity (on net profit attributable to shareholders) was 24.9%, the cost/income ratio was 39.9% and risk cost ratio was 0.1%.

Financial results

EUR million	2022	2021	change
Net interest income	129.49	97.66	33%
Net fee and commission income	32.41	31.17	4%
Net gain/loss from financial assets	-0.42	-1.54	-73%
Total net operating income	161.47	127.29	27%
Other income	0.20	0.60	-66%
Operating expenses	-64.55	-49.34	31%
Income tax expense	-13.26	-10.56	26%
Credit losses	-3.00	-3.95	-24%
Net profit	**80.87**	**64.05**	**26%**

Key figures, %

EUR million	2022	2021	change
Return on equity (ROE)	24.0	25.6	-6%
Return on assets (ROA)	1.3	1.1	15%
Net interest margin (NIM)	2.0	1.7	21%
Spread	2.0	1.6	22%
Cost / Income ratio	39.9	38.6	3%

Volumes

EUR million	31 Dec 2022	31 Dec 2021	change
Loan portfolio	3,187	2,677	19%
Deposits	4,957	5,847	-15%
Equity	388	280	39%
Number of bank customers (thousands)	378	321	18%

Liquidity and capitalisation

The Bank is mainly funded by deposits. Customer deposits are complemented by covered bonds, unsecured bonds and secured funding from the European Central Bank's TLTRO facility.

Liquidity

The Bank runs a conservative liquidity risk profile. The main liquidity risk inherent in the Bank's business is the risk of deposit outflows in LHV Pank. The Group monitors a number of internally defined and regulatory liquidity risk metrics on a regular basis.

The liquidity coverage ratio (LCR) of the Bank stood at 136% at the end of December (31 Dec 2021: 141%), well exceeding the regulatory 100% requirement. The Bank's liquid assets accounted for 47% of the balance sheet total (31 Dec 2021: 55%). The Bank's loan-to-deposit ratio at the end of 2022 was 64% (31 Dec 2021: 46%).

The Bank has a relatively low loan-to-deposit ratio and a high share of liquid assets out of total statement of financial position. This reflects the fact that the deposits collected from financial intermediaries are matched with a liquidity buffer (primarily composed of central bank deposits) and are not used for the lending business. The volume of deposits declined during 2022, mainly driven due to lower volumes of deposits received from financial intermediaries.

The Bank's regulatory net stable funding ratio (NSFR) equalled 145% as at the end of December 2022 (31 Dec 2021: 164%), illustrating the Bank's solid funding base.

Capitalisation

The Bank is well capitalised as at the end of the reporting period.

Bank's common equity was increased by EUR 30 million in 2022, as a contribution from the sole shareholder.

LHV Group issued EUR 20 million of AT1 subordinated bonds in the fourth quarter of 2022, out of which EUR 15 million was passed to the Bank. Also, the Bank has strong internal capital generation through profits.

The Bank's level of net own funds amounted to EUR 451.7 million as at 31 Dec 2022 (31 Dec 2021: EUR 352,8 million).

Total capital adequacy level was as at the end of the reporting period of 20.38% (31 Dec 2021: 18.66%). The Bank's internal target for total capital adequacy was changed in December 2022 by Supervisory Board and stands now at 19.2% (was 16.5%). The Bank uses the standard method for the calculation of credit risk and market risk capital requirements and the basic indicator approach for the calculation of operational risk capital requirements. The Bank has complied with all capital requirements during the financial year and in previous year.

The Bank's leverage ratio stood at 6.27% as at the end of 2022 (31 Dec 2021: 4.04%). The Bank is not subject to MREL requirements on an individual basis.

Capital base *EUR thousand*	31 Dec 2022	31 Dec 2021
Paid-in share capital	141,500	111,500
Legal reserves transferred from net profit	8,736	5,648
Accumulated profit	147,685	91,126
Intangible assets (subtracted)	-2,881	-1,243
Profit for accounting period (COREP)	43,966	61,761
Deductions	-759	-4,028
Tier 1 capital	**338,247**	**264,764**
Additional Tier 1 capital	53,000	38,000
Total Tier 1 capital	**391,247**	**302,764**
Subordinated debt	60,500	50,072
Total Tier 2 capital	**60,500**	**50,072**
Net own funds for capital adequacy calculation	**451,747**	**352,836**

Capital requirements		
Central governments and central bank under standard method	0	0
Credit institutions and investment companies under standard method	11,355	10,390
Companies under standard method	1,202,058	1,141,853
Retail claims under standard method	218,342	212,860
Public sector under standard method	6	6
Housing real estate under standard method	506,767	291,338
Overdue claims under standard method	8,004	19,331
Other assets under standard method	86,279	82,510
Total capital requirements for covering the credit risk and counterparty credit risk	**2,032,805**	**1,758,288**
Capital requirement against foreign currency risk under standard method	7,167	3,489
Capital requirement against interest position risk under standard method	0	0
Capital requirement against equity portfolio risks under standard method	740	2,079
Capital requirement against credit valuation adjustment risks under standard method	2,228	1,211
Capital requirement for operational risk under base method	173,468	125,729
Total capital requirements for adequacy calculation	**2,216,408**	**1,890,796**
Capital adequacy (%)	**20.38**	**18.66**
Tier 1 Capital Ratio (%)	**17.65**	**16.01**

Management and compensation policy

LHV Pank is a public limited company and its governing bodies are the General Meeting of shareholders, the Supervisory Board and the Management Board.

1. General Meeting

The General Meeting of shareholders is the highest governing body of LHV Pank where shareholders invoke their rights.

The primary duties of the General Meeting of shareholders are amendment of the articles of association, increase and decrease of share capital, decisions on issuance of convertible bonds, election and extension of terms of Supervisory Board members, premature removal of Supervisory Board members, approval of the annual report and profit allocation, determining the number of auditors, appointment and recall of auditors and other decisions that are within the powers of the General Meeting of shareholders pursuant to law.

The Management Board calls General Meetings of shareholders. The annual General Meeting of shareholders for approval of the annual report is held at least once per annum.

The sole shareholder of LHV Pank is LHV Group. The shareholders with significant influence in LHV Group are Rain Lõhmus and persons related to him, who hold 21.8% of share capital in aggregate and Andres Viisemann and persons related to him, who hold 11.3% of share capital in aggregate.

2. Supervisory Board

The Supervisory Board is the governing body of LHV Pank that plans the activities of LHV Pank, organises the management of LHV Pank and supervises the activities of the Management Board. The Supervisory Board determines and regularly reviews the strategy, general plan of action, risk management policies and the annual budget of LHV Pank. The Supervisory Board consists of five to seven members. Supervisory Board members have terms of up to five years. Members of the Supervisory Board elect the Chairman of the Supervisory Board from among themselves who organises the Supervisory Board's activities.

The Supervisory Board of LHV Pank has six members. The Supervisory Board is comprised of Madis Toomsalu, Rain Lõhmus, Andres Viisemann, Tiina Mõis, Heldur Meerits and Raivo Hein.

3. Management Board

The Management Board is the governing body of LHV Pank that represents and manages LHV Pank. The Management Board has three to seven members. Management Board members have term of up to five years. The Chairman of the Management Board organises the work of the Management Board. The company may be represented by two Management Board members jointly.

The Management Board of LHV Pank has six members from January 2021. Until January 2021 the Management Board had seven members, comprising of Erki Kilu, Andres Kitter, Indrek Nuume, Jüri Heero, Meelis Paakspuu, Kadri Kiisel and Martti Singi. Starting from January 2021 Erki Kilu was recalled from the Management Board and Kadri Kiisel elected as the new Chairman of the Management Board.

4. Committees

The Supervisory Board of LHV Pank has formed one committee on the LHV Pank level, the aim of which is to advise the Supervisory Board of LHV Pank in matters described below. The Supervisory Board of LHV Group, the sole shareholder of LHV Pank, has formed additional three committees on the LHV Group level, the aim of which is to advise the Supervisory Board of LHV Group in matters described below concerning all of the group companies.

4.1 Risk and Capital Committee

The Risk and Capital Committee, which has been formed at the level of LHV Pank, is a functional body responsible for advising the Supervisory Board and Management Board of LHV Pank in matters related to risk management principles and risk tolerance, assessing the risks taken by LHV and monitoring implementation of the risk policy at the group companies. The Risk and Capital Committee has at least three members who are elected from among the members of the Supervisory Board of LHV Pank.

4.2 Audit Committee

The Audit Committee is above all an advisory body to the Supervisory Board of LHV Group in the fields of accounting and reporting, audit, risk and capital management, internal control system and internal audit as well as legal and regulatory compliance. The Audit Committee has at least three members, who are appointed for a term of three years. The duties of the Audit Committee are to monitor and analyse the processing of financial information to the extent necessary for preparing quarterly and annual financial statements, effectiveness of risk management and internal control, the audit process of financial statements or consolidated financial statements and the independence of the auditor and independent auditor who represents it on the basis of law and compliance of its activities with provisions of the Auditors Activities Act. The Audit Committee is responsible for making proposals to the Supervisory Board of LHV Group and provide recommendations for the appointment or removal of the auditor, appointment or removal of the internal auditor, prevention or elimination of problems or ineffectiveness in the organisation and compliance with legislation and good professional practice.

4.3 Nomination Committee

The purpose of the Nominating Committee is to support the Supervisory Boards of LHV Group, LHV Pank and LHV Finance in issues concerning the selection process and fit-and-proper requirements. The Nominating Committee is comprised of at least three members, who are selected from among the matching members of LHV Group and LHV Pank Supervisory Boards.

4.4 Remuneration Committee

The Remuneration Committee is a body established by the Supervisory Board of LHV Group, LHV Pank, LHV Finance and LHV Kindlustus for the development, implementation and supervision of a remuneration strategy for the employees and members of the Management Board of the group companies. One of the tasks of the Remuneration Committee is to evaluate the impact of any remuneration-related decision on compliance with the requirements established for the management of risks, own funds and liquidity. The Remuneration Committee consists of at least three Supervisory Board members of LHV Pank.

5. Remuneration policy

The policy of compensating members of the Management Board and employees of LHV Pank is set and its implementation is evaluated by the Remuneration Committee established on the level of LHV Group. A monthly base salary is paid to members of the Management Board and employees of LHV Pank. The Supervisory Board determines the base salaries of members of the Management Board and the Management Board determines the base salaries of employees. Management board member agreements have been concluded with the Management Board members; everyone else is employed under employment contracts. LHV Pank has made no major severance payments nor significant non-cash compensations.

6. Share options

LHV shareholders have approved two share option programmes (LTI plans) that were relevant in 2022. The share option programme for the Management Board members and key employees that was approved in 2014 was implemented until 2019, hence the share options that were exercised in 2022 were granted in 2019 for the results of 2018 based on that option programme. In 2020 a new result-based share option programme for Management Boards and equivalent staff as well as key employees of LHV and the group companies was adopted to be implemented from 2020 until 2024. In 2022 the recipients and amounts of share options to be granted for the results for 2021 were determined based on the new programme.

The aim of issuing share options is to create conditions where the long-term objectives and interests of the management and equivalent staff as well as key employees of LHV and the group companies would be harmonised with the long-term interests of the shareholders of LHV. Another objective is to offer a system of compensation on the labour market that is equal to competitors.

As part of the programme, there is an annual performance pay added to basic salary, the amount or issue of which depends on the fulfilment of individual and LHV objectives. The objectives of the programme are:

- ensuring a competitive remuneration, to be attractive in the labour market;
- keeping and motivating key personnel through creating a relationship of ownership;
- reconciling the interests of shareholders and employees;
- increasing company value through performance management.

The instruments of performance pay under the option programme are 100% equity options. The term of share options is 3 years from the moment the options were granted. An additional criterion has been applied to options issued from 2018 onwards for Management Boards' members – they are not allowed to sell these shares for another year after executing the rights under option. The three-year vesting period before issuance of shares gives the opportunity to evaluate the results in the long run. It is not possible to receive the specified amount in cash in lieu of share options. Share options are issued annually in the amount of up to 2% of the total number of LHV shares. LHV has the right to refuse to exercise and issue equity options to the entitled person, in whole or in part, if:

- LHV General Meeting or the Supervisory Board under instructions from the General Meeting does not adopt the decision on the increase of LHV share capital and issuance of shares;

- the Management Board member agreement or the employment relationship of the person entitled to receive options has ceased at the initiative of the person entitled to receive options or pursuant to § 88 of the Employment Contracts Act or, if the Employment Contracts Act is amended, on an analogous basis. However, based on the decision of the Supervisory Board it is possible to make exceptions to the applicability of this paragraph;
- the financial results of LHV or its relevant subsidiary have substantially deteriorated compared to the previous period;
- the person entitled to receive options no longer meets the performance criteria or does not meet the requirements imposed by law on the management or employees of a credit institution or a fund management company;
- LHV or its relevant subsidiary no longer meets the prudential regulations or the company's business risks are not adequately covered by own funds;
- the issuance of options has been determined based on information which has proven to be materially misstated or incorrect.

The share options have been issued annually from 2015 to 2022. In 2022, the options issued in 2019 were fully exercised. The next share options issue could be in 2023 based on the Supervisory Board's decision.

The granting and size of share options granted in 2022 was dependent upon the successful achievement of operational targets of the overall company and the targets of individual Management Board members and employees. In 2022 in LHV Pank, share options were granted to seven Management Board members (6 from LHV Pank AS and 1 from LHV Finance AS) and 132 employees in the amount of EUR 5,172 thousand. In 2021, share options were granted to six Management Board member and 119 employees in the amount of EUR 2,764 thousand.

The share options issued in 2020 can be exercised between the period from 1 April 2023 to 30 April 2023 and shares with the nominal value of EUR 0.1 can be acquired for EUR 0.596 per share. The share options issued in 2021 can be exercised between the period from 1 April 2024 to 30 April 2024 and shares with the nominal value of EUR 0.1 can be acquired for EUR 0.923 per share. The share options issued in 2022 can be exercised between the period from 1 April 2025 to 30 April 2025 and shares with the nominal value of EUR 0.1 can be acquired for EUR 2.182 per share.

The members of the Management Board and employees cannot receive a specified amount of cash in lieu of the share options. Share options cannot be exchanged, sold, pledged, or encumbered. Share options can be inherited. The contract on share options expires upon early termination of the employment or board member contract on the initiative of the employee or board member, for which exceptions can be made by the Supervisory Board of AS LHV Group or the Remuneration Committee based on the decision of the Supervisory Board, and upon extraordinary termination of the employment or board member contract by the employer due to reasons resulting from the employee or board member. According to the Credit Institutions Act, the Supervisory Board of AS LHV Group can reduce the number of share options granted or cancel the share options if the overall financial results of the company have significantly deteriorated compared to the previous period, the member of the Management Board or employee no longer meets the performance criteria, the company no longer meets the prudential regulations, the company's business risks are not adequately covered by the company's own funds or the performance fee has been determined based on information, which has subsequently proven to be materially misstated or incorrect.

7. Wages and salaries

The table below provides wages, salaries paid, and the number of employees who received salaries and wages during the year (including trainees).

Calculated gross salaries and wages

EUR thousand	Base salary	Incentive salary	Total	Number of employees
Retail banking	6,388	0	6,388	362
Private and corporate banking	2,245	0	2,245	75
Financial intermediates	2,135	0	2,135	75
Support services	7,604	0	7,604	286
Information technology	5,440	0	5,440	178
Total	**23,812**	**0**	**23,812**	**979**

Sustainability report

1. Sustainability at LHV

Sustainability mission statement

Sustainability is a constant learning process in which we engage stakeholders and external experts to better understand the consequences of our decisions and create long-term value. We aim to strategically enhance in-house competence, develop sustainable financial products and services, improve our business processes, and develop sector-wide partnerships to work toward more responsible business operations.

- We realise how our business decisions affect society and the environment, and we focus on measuring and managing these impacts.
- We aim to be a leader in sustainable development in the financial world by striving toward initiating systemic change and adopting innovative and sustainable solutions.
- We are aligning our operations with the UN Sustainable Development Goals and the Paris Agreement.
- We operate transparently and disclose our progress and in voluntary and regulatory sustainability reports and through our corporate communication channels. We are continually improving our know-how on sustainability reporting standards and comply with GRI (Global Reporting Initiative) reporting standards in our annual sustainability reports.
- We are committed to creating the conditions for adhering to our sustainability strategy. This is achieved both by internal capacity building and constant integration of ESG considerations into decision making, business operations and practices.

The aim of sustainability report is to provide an insight to how LHV integrates sustainability matters into its business activities to increase its positive impact on the environment and society. While the following sustainability report has been assessed by an external party, it has not been reviewed or audited.

2. Global sustainability frameworks

2.1 United Nations Environment Programme Finance Initiative Principles for Responsible Banking

The United Nations Environment Programme Finance Initiative (UNEP FI) is a global partnership established between the United Nations Environment Program (UNEP) and the financial sector. The UNEP FI Principles for Responsible Banking (UNEP FI PRB) provide banks with a framework for sustainable operations. We joined the initiative in 2021 to show our commitment to the UN Sustainable Development Goals and to align our activities with the goals of the Paris Climate Agreement.

We take part in international cooperation in the financial sector and in sharing best practices.

The 6 principles (indicated below) provide a framework for developing and maintaining a sustainable banking system. They were designed to help the industry make a positive contribution to society. We are currently in progress of setting targets based on our impact areas.

Principle 1
Alignment

We will align our business strategy to be consistent with and contribute to individuals' needs and society's goals, as expressed in the Sustainable Development Goals, the Paris Climate Agreement and relevant national and regional frameworks.

Principle 2
Impact & target setting

We will continuously increase our positive impacts while reducing the negative impacts on, and managing the risks to, people and environment resulting from our activities, products and services. To this end, we will set and publish targets where we can have the most significant impacts.

Principle 3
Clients & customers

We will work responsibly with our clients and our customers to encourage sustainable practices and enable economic activities that create shared prosperity for current and future generations.

Principle 4
Stakeholders

We will proactively and responsibly consult, engage and partner with relevant stakeholders to achieve society's goals.

Principle 5
Governance & culture

We will implement our commitment to these Principles through effective governance and a culture of responsible banking.

Principle 6
Transparency & accountability

We will periodically review our individual and collective implementation of these Principles and be transparent about and accountable for our positive and negative impacts and our contribution to society's goals.

2.2 Partnership for Carbon Accounting Financials

At the end of 2021, we joined the Partnership for Carbon Accounting Financials (PCAF) initiative. While we have measured our scope 1, 2 and 3 emissions at the operational level since 2019, joining PCAF helps us disclose our scope 3 emissions (category 15, investments) which are relevant in understanding our full climate impact.

The PCAF standard, which is in line with the GHG protocol, provides a consistent methodology for measuring and disclosing emissions from business activities, including those associated with corporate/business loans, commercial real estate loans, residential mortgages, motor vehicle loans, project finance and even the equity and bond positions that banks hold on their statements of financial position. This year we have estimated our climate impact in four asset classes: business loans, motor vehicle loans, commercial real estate loans and mortgages.

These results give us a valuable starting point and help us set emission reduction targets that enable us to reach alignment with the Paris Agreement. For us, this is a big step forward in not only understanding our own climate impact but also a step towards in estimating our customers' environmental performance and working with them on reducing our impact to the environment.

3. ESG strategy

3.1 Material ESG and sustainability topics

Our goal is to make an actual impact through the sustainability efforts we make. We devote our resources to addressing the environmental, social and governance (ESG) sustainability matters most affected by our business decisions. With the help of UNEP FI Portfolio Impact Analysis Tool, we have identified our potential positive and negative environmental and social impacts arising from our business activities. Through engaging both internal and external stakeholder groups, as well as applying proper ESG management approach, we have determined the areas on which LHV has significant impact through its products and services.

Materiality and impact analysis findings

The results of the materiality and impact analysis were validated by the management team during the ESG strategy development process. As an outcome, we identified two environmental and two socioeconomic impact areas where LHV could achieve the most significant impact on sustainable development through its core work across the value chain and portfolio:

- Climate and biodiversity
- Circular economy
- Inclusive and cohesive economy
- Financial literacy and economic security

In addition, an internally relevant material aspect was identified – honest and transparent organisational culture (covering both social and governance aspects).

Based on these impact areas, we have built our sustainability strategy to address the issues by setting KPIs, targets, as well as developing sustainable financing products. Moreover, we ensure that our sustainability strategy contributes to the development needs and targets set by the United Nations Sustainable Development Goals (SDGs).

4. Management of ESG

The core of our ESG strategy is specified in our ESG policy and KPI roadmap, which sets the goals, ambitions, and approaches for our sustainability efforts in all the subsidiaries of the group. The ESG policy sets a high-level structure and responsibilities for group-wide ESG governance. The Head of ESG is responsible for all everyday ESG matters, Group CEO as a governing body member is ultimately responsible for ESG supervision, all Heads of LHV Group's subsidiaries are responsible for supervision over everyday ESG matters and ESG activities in their respective subsidiaries, and Communications Manager is responsible for external communication related to environmental and social matters and serves as a contact person for all sustainability-related public enquiries.

Since 2020, we have a dedicated ESG team who reports directly to the Bank CEO. Over the past years, we have considerably increased and developed ESG competencies in-house, resulting in the growth of our ESG team as well as ESG-focused professionals in the Compliance, Credit, Risk and Asset Management Departments. The main aim of the group-wide management of ESG is the smooth integration of sustainability principles into all relevant business lines, processes, strategy building, and risk management.

In 2023, we will begin with holding monthly ESG Steering Committee meetings in LHV Pank, where specific focus will be put on integrating sustainability matter into business areas of our banking operations. The ESG Steering Committee of LHV Pank is comprised of the members of the management board of LHV Pank and the Head of ESG. We are currently setting up a proper ESG governance system within LHV, aiming to integrate ESG and sustainability matters into all relevant business functions and processes, and to involve all relevant managers in business units.

4.1 ESG risk management

We understand the need for assessing the risks related to ESG and being more transparent and accountable in our decision-making processes. We have published a list of business areas that are inconsistent with our credit policy and our goals for sustainability. In 2022 we have also finished building our ESG risk assessment/rating model for credit clients, which is used as a comprehensive analysis tool to understand our credit clients, their potential environmental and societal (E&S) risks, and hence, will give us more insight into how to integrate ESG and E&S risk criteria into business development 2023 and onward. We are firm believers in the approach that you can only manage what you can measure.

We also realise that an adequate ESG risk management framework is the core of responsible business operations. Hence, we will finalise the group wide ESG risk management framework in the beginning of 2023. In addition, we are looking thoroughly into ongoing legislative processes which will affect our sustainability efforts in the future. One of them is the EU Taxonomy. The implementation of the taxonomy is one of the current focuses and will be the foundation for our taxonomy alignment and ESG scoring criteria and methodology. Taxonomy implementation will not only influence our own ESG data analysis and scoring methodologies and processes but will help our corporate customers become more transparent in their sustainability efforts and knowledgeable in managing their ESG risks and disclosures.

5. Management of impact areas

5.1 Environmental impact

We understand our role as a financial institution as having a transformational capacity and influence to create positive change. To mitigate the negative impact on the environment, we strive for more sustainable ways of achieving growth and creating value. LHV constantly aims to operate sustainably, and as an Estonian company, we want to help the Estonian economy to adapt to meet the environmental and climate targets.

We have committed to achieving the goals of the Paris Climate Agreement as well as support the Estonia's national goal of attaining a climate-neutral economy by 2050. To do so, we carefully follow the green office principles by monitoring our annual footprint of own operations. In addition, we are now also measuring and taking steps to decrease the emissions of our investment and lending activities, which we refer to as financed emissions.

5.1.1 Green office operations

Even though our greatest environmental impact comes from financing and investing activities, it is no less important how we go about our daily business. One way of reducing our carbon footprint is to act to mitigate the negative impact coming from our office operations. Since 2019, we have a Green Office working group, who initiates sustainability projects aiming to increase employee's awareness regarding the impact each one of us can have through our daily activities.

The Green Office Principles have now been embedded throughout the teams in all our offices. During the previous years, we have reached considerable milestones and been awarded for our achievements. While the Tallinn City Plaza office has already received the Green Office certificate, in 2022 we also started the certification application process for our Tartu and Pärnu offices. In addition, the BREEAM certificate for building environmental performance for the City Plaza office was extended until the end of 2023.

Waste generation and utilisation is highly prioritised in LHV offices, and we have developed a solid waste sorting procedure. In cooperation with Nutriloop, we recycle our biowaste, which we use to grow plants on the balconies of our office building, as well as donate it to local farmers and gardeners. Employees are encouraged to recycle their waste both at work and at home, for example through allowing them to bring unwanted clothes or hazardous waste into collection boxes installed in the office.

5.1.2 Our carbon footprint

For setting an action plan and targets for emission reductions, it is first necessary to identify and measure the GHG emissions of our business activities and to follow a standardised methodology in the process. We calculate our footprint based on the methodology provided by the Greenhouse Gas (GHG) Protocol Corporate Accounting and Reporting Standard, an internationally recognised and the most widely used greenhouse gas accounting standard. The results are expressed in CO_2 equivalents, the universal greenhouse gas unit of measurement, indicating the potential for causing global warming.

Based on GHG Protocol, emissions are categorised into three scopes. Scope 1 relates to direct emissions that occur from sources that are controlled or owned by an organisation. Scope 2 emissions refer to indirect emissions associated with purchase of electricity, heating, and cooling. Scope 3 emissions includes all other indirect emissions accounting for emissions coming from our own operations and emissions that are financed through our financing and lending activities.

At the end of each year, we measure the carbon footprint of our office operations through collecting data about business travels, consumption of office buildings, ordered paper, fruits etc. Based on this, we make comparisons with previous years and introduce new activities in the Green Office action plan to further reduce our footprint. Our office activity generates emissions mostly due to the use of heating, power, employee commuting, and business travel.

To evaluate the impacts of employee commuting, a web survey was conducted among the employees, which inquired about the distance between home and work (direct route, without any interim stops) and the modes of transport ordinarily used. 58% of employees responded and the results were extrapolated to the number of employees working for the company.

The analysis covered the activities of LHV Group's Tallinn, Pärnu and Tartu offices. Similarly, to the assessments of the past years, the 2022 analysis did not consider LHV's UK office (due to limited availability of data). As the office in London is small, it is not expected to have a significant impact on the carbon footprint of LHV Group as a whole. To perform the calculation of intensity of carbon footprint per employee, the aggregate result was divided by the number of LHV Group's employees at the end of the reporting year.

In 2021, LHV's office activity had a greenhouse gas emission footprint of 1,444 tonnes of CO_2-equivalent, which was 2.3 tonnes per employee at the time of calculation (see table below for more detailed overview). For 2022 the results were 1.968 tonnes, or 2.5 tonnes per employee. The main reason for the increase in our operational level CO_2 footprint was due to increase in heating used for the Tallinn office as well as from the increase in plane trips taken for business purposes compared to the previous year where it was largely hindered due to the Covid-19 pandemic.

Emissions from own operations (GRI 305:2016)		2022	2021
	Scope 1	0	0
	Scope 2	567 tCO_2e	445 tCO_2e
	Scope 3 (excl. category 15)	1,400 tCO_2e	999 tCO_2e
	Total emissions from own operations	**1,968 tCO_2e**	**1,444 tCO_2e**
	GHG emissions intensity per FTE	2.48 tCO_2e	2.28 tCO_2e

		2022		2021	
	Type	tCO_2 e	Share %	tCO_2 e	Share %
Scope 1Direct emissions		-	-	-	-
Total Scope 1		-	-	-	-
2 - Indirect, emissions related to purchased electricity and heat	Electricity (renewable electricity): Tallinn office	0	0	0	0
	Electricity (renewable electricity): Tartu office	0	0	78	5
	Electricity (non-renewable electricity): Pärnu office	16	1	-	-
	Heating: Tallinn office	544	28	357	25
	Heating: Tartu office	5	0	9	1
	Heating: Pärnu office	1	0	-	-
Total Scope 2		**567**	**29**	**445**	**31**
3 - All other indirect emissions in the value chain	Outsourced materials (trading assets)	45	2	25	2
	Office furniture	35	2	29	2
	Office equipment	274	14	238	17
	Generated waste	28	1	16	1
	Water consumption	2	0	1	0
	Business travel: plane	158	8	54	4
	Business travel: train	5	0	1	0
	Business travel: bus	4	0	1	0
	Business travel: taxi	1	0	1	0
	Business travel: personal car	18	1	10	1
	Drive home to work: 2022 (795 employees)	425	22	308	22
	Home office (795 employees)	31	2	19	1
	Indirect energy and fuel effects				
	Electricity grid loss	26	1	5	0
	Heating grid loss	64	3	56	4
	Indirect impact related to heating production	282	14	237	17
	Grid loss from production of heating	1	0	-	-
Total Scope 3		**1,400**	**71**	**999**	**69**
Total emissions from own operations		**1,968**	**100**	**1,444**	**100**

Estimates of financed emissions

Since a large share of our emissions is related to our financing activities, in 2022 we began with assessing our emissions under scope 3 category 15 investments (as defined by the GHG Protocol Corporate Value Chain standard) using the PCAF methodology.

By the end of 2022, we managed to estimate the emissions for 96% of our credit portfolio in four asset classes (business loans, motor vehicle loans, commercial real estate loans and mortgages) totalling 562,506 tCO2 with an average emission intensity of 183.4 tCO2/mln EUR (see table below for more detailed overview).

The results of the emission estimations can vary to some extent depending on the quality of the input data used in the calculation models. We strive to improve the data quality by obtaining more specific information directly from our clients in the coming years to ensure more accurate results. At the same time, we are aware of the limitations of this methodology and acknowledge that fact that there are improvements to be made but also see this as an optimal starting point for gaining a better overview of our climate impact. Based on these findings we will be able to set emission reduction targets in the future.

Financed emissions			2022
Scope 3 (Category 15 – investments)	Type	tCO_2 e	tCO_2 e / EUR million
	Business loans*	388,757	275.9
	Mortgages	88,490	82.8
	Commercial real estate	77,879	159.1
	Motor vehicles**	7,380	74.3
Total Scope 3 (Category 15 – investments)		**562,506**	

* Due to uncertainty scope 3 information is not available
**Emissions from passenger cars, busses, and trucks

Offsetting our carbon footprint locally through innovation

While we have been taking considerable steps to reduce the carbon footprint of our office operations, it can be done only to a certain extent. Therefore, we are collaborating with eAgronom, who provides us a local solution helping us to achieve our first emissions related target. We are using eAgronom's newly developed solution to buy carbon credits from Estonian farmers who sequester carbon dioxide from the air into the soil and thereby improve the soil quality of their fields.

Working together with eAgronom helps us to understand the offset business much better, we can improve local soil quality, store more nutrients in the soil and increase water holding capacity while supporting local farmers in applying the new approach in their everyday farming habits.

In November 2022, we received our first carbon credits which enables to declare that we have reached Net-Zero at the operational level.

5.2 Sustainable products and services

LHV's influence in the Estonian financial sector is growing. As part of an industry that is vital for society, we, directly and indirectly, affect our surroundings and make our most significant contribution through investing and financing. That is why we have decided to channel cash flows from our core activities more concertedly to activities that support the transition to a climate-neutral and sustainable economy. We have developed unique green products that motivate our customers to make everyday consumer and investment decisions that are as environmentally responsible as possible. In this way, we do our part to support economic growth, while at the same time reducing greenhouse gas emissions, pollution, and waste generation.

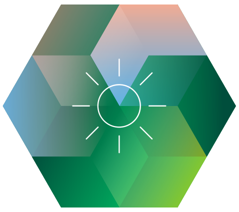
Green Home Loan

One of the most important consumer decisions a person will ever make – in terms of the financial cost and the environmental impact – is regarding purchasing their home. One-third of the average Estonian's annual CO2 footprint is related to their home – mostly deriving from energy used for heating and emissions arising from use of household electricity.

We would like to promote the building and buying of the most energy efficient homes, so we're offering our customers the possibility to leverage Estonia's first green home loan.

Green Loan for Housing Development

We aim to promote the purchase of energy-efficient vehicles. The most energy-efficient vehicle you can choose to drive is a fully electric car. But to be sure of its sustainability level, the energy needs to derive from renewable sources entirely. From 2026 onwards, only cars with zero CO_2 emissions per kilometer are considered clean vehicles. Only electric and hydrogen vehicles will meet this standard. We, therefore, offer car leasing for new fully electric vehicles purchased for general use. In line with a longer-term strategy and the desire to contribute to Estonia's climate objectives, LHV Pank has decided that LHV will no longer finance the purchasing of new diesel passenger cars from 2030 onwards.



Green hire-purchase

Renewable energy sources are undeniably an investment for the future. Using solar panels for generating energy and heating homes and household water with geothermal energy is a smart choice. Instead of driving vehicles that run on fossil fuels, we want our customers to try considering electric monowheels or two-wheeled vehicles. We want to make it easier to make energy-efficient choices.

Green Investment Loan for Companies

The Estonian economy is very carbon-intensive. Therefore, investing in lower energy consumption, production of renewable energy, or daily resource efficiency is very profitable and will increase any company's competitive advantage.

5.3 Social

While banks and financial institutions play an integral part in driving economic growth, they also have the power to impact individual lives and communities' overall wellbeing. Our business is always conducted with integrity, transparency, and ethics in mind, with the utmost emphasis on fair dealing and respect towards our partners, customers, and employees.

By acknowledging our role and societal influence at the local level, we do following:

- maintain a budget to support music or arts, education, sports, and community events;
- support external movements and partners to promote the cultural and economic development of local communities;
- stand for equal opportunities for people and companies;
- build the trust of our customers in LHV as a non-discriminatory financial services provider;
- encourage financial literacy and the share of economic knowledge;
- continuously improve our competencies in the field of ESG to further advance social cohesion. The prosperity and welfare of our people is at the core of our business operations.

We realise that good business results and growth cannot be achieved without people who create value, are well taken care of and engaged in their personal and collective mission and feel highly valued.

5.3.2 Financial literacy

Since its establishment, LHV has been part of the Estonian investor community. As a market leader in investment services and as a listed enterprise that values investor relations, we actively contribute to educating investors. In our relations with more than 10,000 shareholders, we are open, transparent, and inclusive.

- We organise free seminars as part of the Investment School, where 19,262 people participated in 2022 (2021: 8,200).
- We also carry out the annual stock market game Börsihai. This year, the number of participants reached 5,415.
- We continue to organise campaigns on financial literacy, as well as targeting the mostly Russian-speaking youth in Estonia, with insightful videos on money management on our social media platforms.
- In cooperation with 5 other companies, we initiated the "Lae end" program that brings together the brightest teachers of Estonian schools, start-ups in the educational landscape as well as representatives of the physics teacher community with the aim of improving the study materials used in physics classes.
- We participated in projects for improving financial literacy organised by the Estonian Banking Association.
- We supported the Investor Toomas conference organised by Äripäev, the Investment Festival carried out by the Investment Club, the Women's Investment Club, and stock training.

5.3.3 Sponsorships

Within its means, LHV supports activities that contribute to the development of Estonian society. In our sponsorship projects, we prefer long-term and substantial cooperation. In 2022 one of our biggest contributions was a donation of EUR 500,000 to the Estonian Refugee Council to help the refugees of the war in Ukraine. Our other sponsorship contributions are described below.

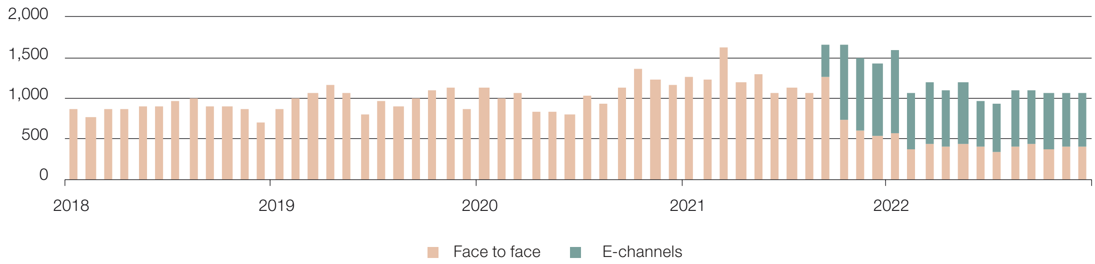
5.3.4 Social impact through channels and customer experience

For LHV, uncompromising customer experience and quality of e-channels has always been a top priority. While for the past few years, we have been more focusing on making banking services available online, especially to private customers, we are now working on wider segments and product portfolio, but also better communication and customer service tools online. For LHV, it is continually essential to develop our internet bank and mobile app in a way, that will support the growing product offering and make our e-channels available for wider audience including insurance customers, pension funds and consumer credit product users.

In 2022, we have onboarded an average of 5,100 new customers every month. Close to 70% of our new private customers open their bank accounts through our e-channels, either directly online or combining e-channels with face-to-face meeting with the bank representative. We have seen the percentage growing steadily in previous years, but 2022 has proven that most of our customers can use our services remotely and online.

Since September 2021, when we first introduced digital onboarding to our legal customers, the percentage of bank accounts opened by legal customers in e-channels has been growing steadily from 20% to an average of 60% in Q4 2022. We will continue working on expanding the possibilities for legal customers, as currently only simple company structures are allowed, and many compliance and risk measures are additionally applied for online onboarding.

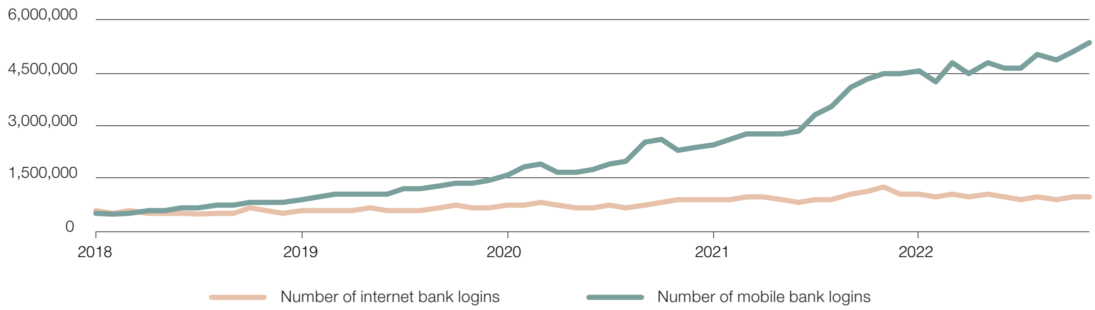
Identification upon onboarding of legal entities



2022 was the first year when we witnessed the monthly usage of our mobile bank exceeding internet bank usage. Our mobile bank app has been rapidly gaining popularity among both, private and legal customers. Even when the statistics of unique monthly users are in the same ballpark for both channels, mobile bank app shows approximately 5 times higher monthly activity rates than internet bank.

We have been working on improving the usability and look & feel of our electronic channels and making user experience as seamless as possible. The percentage of new customers logging into the electronic channels in Q4 2022 has reached 74% for mobile bank and up to 90% for internet bank. This means that customers are taking advantage of our electronic channels even more than before.

LHV internet bank and mobile bank usage activity



Opening a bank account online for underage children through our internet bank or mobile app has kept popularity among our customers. Currently, child's ID card, passport, or residence permit card issued in Estonia is required in addition to customer data and agreement of the parent opening the account. We are planning to redesign the flow and requirements to make it even more simple and allow to set up child accounts without signing the customer agreement with the parent.

5.3.5 Our societal impact as an employer

LHV, as a large employer and an important part of the society, is responsible for its actions, words, and ways of working. LHV is using leverage to promote high ethical standards and inclusive approach in all customer, investor, and employee relations. We aim to be a responsible organisation, and we also hope to contribute to systematic change towards a more sustainable approach and inclusive society in general.

In 2020 we introduced a new employee engagement survey – Gallup's Q12. This is an international format developed to measure employee engagement. The survey consists of 12 questions, which all measure factors that are influencing employee engagement. The format has been proven internationally to bring out greater performance and facilitate communication between managers and employees. We have concluded two surveys this year, in April and in November. The results were very high, in both we got 4.5 out of 5 in average. In addition to the results, the surveys have brought up the same topics about growth, communication, caring, friendships, etc within teams and the whole organisation.

Equality and non-discrimination

LHV is an equality-driven, fair, and inclusive employer. We foster and maintain non-discriminatory business and HR practices. In the leadership and recruitment processes, we are guided by the highest ethical standards, human rights, and equal opportunities. In line with our personnel policy, we take a gender-neutral, non-discriminatory approach in all recruitment and promotion decisions, and base the decisions on equal, measurable qualities, such as experience, education, skills and, if necessary, requirements set by applicable regulations.

It is important for LHV not to discriminate against any minorities. In recruitment processes we choose the best person for the given role, not considering nonrelated factors, such as race, disabilities, political views, sexual orientation, etc. If the person is fit for the job, no other aspects will play a role. Currently, the physical office space is unfortunately not yet adapted to all the needs of people with physical disabilities but working remotely is offered as an alternative.

The remuneration policy sets the guidelines for determining the renumeration. The decision must be objective and unaffected by the person. If required, compliance with legislations is checked. In 2021, LHV set a process for equal pay calculation. We are using the analytical job evaluation method created and developed by Fontes and based on the method recommended by the ILO. It is used in all three Baltic States for market benchmarking. LHV has used Fontes' benchmarking method since 2011 for yearly evaluation. In this method jobs are evaluated based on education and professional experience, work characteristics and accountability. The analytical job evaluation method is universal and is applicable in every organisation and with all jobs. Fontes's analytical job evaluation points scale and job family classification scale are compatible. This ensures that we compare similar value jobs with each other. In 2022, we continued with the same methodology. This year the analysis showed that in specialist categories, where the job requirements and the work are more comparable, the women/men salary ratio ranged from 1.09 to 0.86. In the manager categories the range was slightly higher, from 1.25 to 0.75, but these roles are often more specific, incomparable with each other. We have seen a step up from 2021 in all categories. Still the situation is not perfect, and we are moving on with a focus on improvement within all categories needed.

Inclusive workplace

It is important to us that our employees' ideas, thoughts, and statements are heard and taken into considerations. We believe that great success comes from working together and using our collective brain. It is important that employees feel free to have a say and that their words reach up to the top management. LHV has included all employees in the process of setting goals for each team. This is done as a team effort.

While we encourage our employees to express their thoughts daily, the subject is very much in focus at least twice a year, during our engagement survey Q12. In the 7th question in the survey, the respondents must agree or disagree with the statement 'At work, my opinions seem to count'. This year we have seen a small decrease in this result as it has gone down from 4.6 out of 5 to 4.5 out of 5 in both April and November survey. As the format also includes one-on-one conversations for every team member with their manager, the subject is discussed, and actions proposed, if anything needs to be improved. This has been shared as one of focus subjects from HR to the team leaders.

Professional and personal development is part of LHV culture as we strive to innovate and be better at providing smarter solutions to our customers. The ideas for the solutions should come from our employees, and therefore developing one's skills is part of the daily job. The training approach is guided by the individual needs, motivation and goals as well as regulative guidelines for professional development. In addition to professional trainings, we have contributed to team training with the aim of helping teams work better together. We have also focused more intensely on leadership development with a set leadership training programme. This year the focus has been mapping employee's strengths through Gallup's Clifton Strengths Finder test, more that 35% of our teams and employees have done the tests and have an overview of their biggest strengths.

Our employee engagement survey measures employees' satisfaction with their development. There are three questions focused on professional growth: is there someone at work who encourages your development; has anyone talked to you about you progress, and have you had opportunities to learn and grow in the past year? In the latest survey, from November 2022, 89% of our employees replied with a 4 or a 5 to all these questions. This is a slight decrease from last year in the first 2 questions, but the same time still 96% of the employees say that they have opportunities to learn and grow in the past year in their role.

Work-life balance

It is very important to us that our employees have a well-balanced life. An unbalanced life will affect both private and work life. Therefore, LHV does not encourage working overtime and offers flexible working hours. We have however this year seen an increase of working overtime. Having analysed the reasons, it is mostly done during rapidly changing situations, for example many teams had to react quickly when the war started in Ukraine and sanctions were put in place. Still the general company culture supports a balanced work life. During the pandemic we implemented a hybrid-workplace solution, which is still in place. Although many of our employees prefer to work from the office, there is always option to work from home and we have set flexibility in all roles, where possible.

Promotion of employees' health

To keep our employees healthy, LHV has an extensive occupational health package. We contribute to the physical and mental health of our employees. As well as keeping the balance between work and private life, it is important to ensure a supportive mental and physical working environment. LHV provides employees with healthy snacks at the office, promotes physical activity during the working day and offers an allowance for sports and recreation as well as a personal budget to use for your mental health.

A recognised employer

While attractive employer awards have never been a goal for LHV they are still a great acknowledgement. In the past few years LHV has gained (an increasingly growing/a growing) reputation for being a desirable employer. Our goal has been to offer our employees opportunities for professional growth and an inspiring company culture. This year we have had many possibilities to share our experience and our leadership culture in various podcasts, at conferences, in schools and universities. All of this has helped in being noticed. We have received acknowledgements in CV-Online's TOP Employer Survey, being named the 1st choice in both financial sector as well as Top-of-Mind employer in Estonia. Also, CV Keskus ranked LHV as the most desirable employer. We were also recognised as an attractive employer by students and experienced employees in Instar's survey.

Such recognition helps us attract talented people to join the company, especially in today's highly competitive labour market. This year we have had the chance to communicate with almost 5,000 applicants from whom we have hired 4.4%. In addition to job offerings, we have continued with our internship programme and promoted job-shadowing and rotation. In the summer of 2022, we had a record breaking 50 interns, 44% of whom continued as employees.

5.4 Governance

LHV is committed to always acting with integrity and in good faith and ensuring that our management policies, business mechanisms, and structures are transparent and reflect accountability, equality, and the highest ethical standards. We manage carefully all potential conflicts of interest, avoid bribery, money-laundering, unlawful behaviour, and corruption. To encourage the sustainability mindset across all management levels and the organisation, we:

- maintain a flat, non-hierarchical organisational structure to emphasise the importance of employees taking individual responsibility;
- continuously enhance the integration of ESG factors into our everyday work, management style, recruitment processes, and strategy building;
- focus on engagement and cooperation;
- recognise the integration of ESG factors into our business processes as a change management effort and understand the importance of collaboration to achieve our set goals;
- work toward better analysing and reporting our ESG activities and progress and appropriately disclosing our metrics and achievements to regulators, partners, and the public;
- in order to ensure a transparent management culture, we follow the Good Corporate Governance Practices recommended by the EFSA and the Nasdaq Tallinn Stock Exchange;
- report regularly on the UNEP FI Principles of Responsible Banking;
- have integrated ESG targets into the executive compensation programme.

5.5 Sustainability reporting

We continuously work towards improving our sustainability reporting and strive to be transparent in reporting our ESG metrics. Over the past years, we have joined several voluntary non-financial disclosure initiatives (Nasdaq Environmental and Social Disclosure Form, PCAF, UNEP FI). In 2022, we submitted our second report to UNEP FI regarding our progress of implementing the UNEP FI Principles of Responsible Banking and continue to do so in the upcoming years while also taking into account the feedback received from UNEP FI. We continue to align our ESG reporting practices with GRI requirements as well as the Nasdaq Reporting Guide for Nordic & Baltic Market.

Below in the GRI content index, we have also reported on both GRI as well as voluntary ESG indicators.

5.5.1 ESG metrics

Working towards our goals of more sustainable business development, we comprehend the challenges of ESG governance, impact measurement and setting KPIs to sustainability goals. To manage our impacts, we need to be able to measure them. We have updated our list of key indicators to all our impact areas and are working on setting specific targets for each KPI. We are also developing a new ESG roadmap for 2024-2030 that will help us move closer to our goals in a more structured manner. Incorporating ESG in all our business decisions and business lines will need to go hand in hand with comprehensive mechanisms for measuring our impact across the board and reporting on it correctly. This will be one of the key ESG-related goals for LHV moving forwards. The goal of 2023 and onward would be to establish a more specific target setting plan for these metrics and start setting business specific ESG targets which are tangible and aligned with both our ambition as well as the global goals.

5.5.2 Taxonomy reporting

Article 8 of the EU Taxonomy Regulation No 2020/852 (the TR or Taxonomy Regulation) obligates any undertaking subject to an obligation to publish non-financial information pursuant to Article 19a or Article 29a of Directive 2013/34/EU (the NFRD companies) to include in its non-financial statements or consolidated non-financial statements information on how and to what extent the undertaking's activities are associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the TR. The disclosure pursuant to Article 8 is further specified in Commission Delegated Regulation 2021/2178 (the Disclosures Delegated Act (DDA)). It is important to note here that the DDA will enter into force in several stages in 2022-2026.

LHV Pank's taxonomy eligibility

As the Bank is treated as a financial undertaking based on the DDA, the Bank must disclose the following information in 2023 (Article 10 (3 of the DDA):

- the proportion in their total assets of exposures to taxonomy non-eligible and taxonomy-eligible economic activities;
- the proportion in their total assets of the exposures referred to in Article 7, paragraphs 1 and 2 of the DDA (exposures to central governments, central banks and supranational issuers, and derivative instruments);
- the proportion in their total assets of the exposures referred to in Article 7(3) of the DDA (exposures to undertakings that are not obliged to publish non-financial information pursuant to Article 19a or 29a of Directive 2013/34/EU, referred to as non-NFRD companies);
- the qualitative information referred to in Annex XI of the DDA.

Regarding portfolio management, portfolios are not included in total assets in the meaning of Article 10 (3) of the DDA. Therefore, these assets are not subject to disclosure at this stage.

The table below shows the eligibility of exposures against the EU taxonomy environmental goals of climate change mitigation and climate change adaptation as specified in Commission Delegated Regulation No. 2021/2139 (the Climate Delegated Act (CDA)):

LHV Pank EU taxonomy reporting

EUR thousand			Taxonomy eligible	Taxonomy non-eligible	Coverage %
Art 10	3a	Total assets	1,126,107	2,431,618	31.7%
		Of which trading portfolio and on demand interbank loans in total assets	-	363,638	10.2%
	3b	Exposure to governments & central banks	-	2,478,335	41.1%
		Total exposure to derivatives	-	40	0.0%
	3c	Total exposure to non-NFRD companies	-	2,012,316	33.3%

Clarifications regarding LHV Pank EU taxonomy reporting

Eligible assets of LHV Pank include loans to households collateralised by residential property and car loans to households as specified in the DDA. In addition to that, eligible assets include exposures to NFRD companies. Where the use of proceeds for a particular exposure is unknown, the share of eligible exposures to NFRD companies is calculated on the basis of the most recent taxonomy eligibility data disclosed in annual reports. Exposures to non-NFRD companies, derivatives, trading portfolio and on demand interbank loans are not considered in the assessment of eligibility according to the DDA and are therefore regarded as non-eligible.

Exposures to central governments, central banks and supranational issuers are excluded from the total assets under 3a and therefore also excluded from the coverage ratios under 3a. Coverage ratios of items under 3b and 3c are provided as a proportion of total on assets of the statement of financial position.

5.5.3. ESG Key Performance Indicators (KPIs)

Table below depicts our defined ESG Key Performance Indicators (KPIs) that help us better understand the environmental, social and governance impact of our business. These KPIs have been selected based on the areas where LHV has most impact through our business activities.

Within the impact area of climate and environment, we have committed to phasing out the financing of new diesel cars by 2030 and have additionally set a target to gradually decrease the average CO2 emissions of our vehicle leasing portfolio over the upcoming years. We understand that our main climate impact comes from our loan portfolio, which is why we have set a target to increase the share of renewable energy projects in our energy sector portfolio to 90% by 2030. In addition, we have defined a goal that by 2030, at least 50% of our annually signed mortgage contracts will be done for A and B energy class housing. Our intention for 2023 is to set science-based emission reduction targets for carbon-intensive sectors in our loan portfolio.

In LHV, we acknowledge our role in the society when it comes to improving the financial resilience of our clients. We believe that educating society about responsible borrowing and financial habits will eventually improve their possibilities of gaining access to financing. We have therefore set a target to increase the coverage rate of investment services contracts among young (up to 26 years old) clients to reach 60% by 2030.

Since gender pay gap is a major concern within the financial sector, we have decided to be transparent regarding our gender pay gap across all levels and set a target to completely abolish gender pay gap in LHV by 2030. In addition, we aim to improve our employee satisfaction score to reach 5 (maximum score) by 2030.

ESG key performance indicators in LHV Group

1. Climate and biodiversity (E)	2022	2021	2020
Contract value for new renewable energy projects added to the corporate loan portfolio (EUR million)	107.1	41.4	53.9
Number of new energy class A apartments financed annually through housing developments	532	-	-
Share of annually signed mortgage contracts for A and B energy class housing in the mortgage portfolio	29.8%	-	-
Average CO2 emissions in Group’s car leasing portfolio (gCO2/km)	122.3	134.9	140.9

2. Inclusive and cohesive economy (S)	2022	2021	2020
Use of digital channels among private customers*	59.4%	59.3%	58.8%
Use of digital channels among private customers with native language other than Estonian*	66.2%	64.3%	62.8%
Use of digital channels among private customers older than 65*	40.8%	39.2%	35.7%
Share of retail customer base outside big cities (Tallinn, Tartu, Pärnu)	32.7%	32.4%	31.6%

* logging in at least once a month

3. Financial literacy and economic sense of security (S)	2022	2021	2020
Share of young people (up to 26 years old) with an investment services contract	46.1%	45.7%	29.8%
Share of private clients with an investment services contract	40.8%	41.1%	30.8%
Share of female private clients with an investment services contract	36.3%	36.0%	24.6%
Number of microloans granted	1068	1001	948
Share of LHV Pank customers with 2nd pillar pension	35%	-	-
Total number of Investment School attendees	19 262	12 000	7 420

4. Honest and transparent organisational culture (G)	2022	2021	2020
Confirmed incidents of corruption and actions taken	0	0	0
Customer satisfaction level	95.7%	95.8%	94.9%
Number of legal proceedings pending against the company as of end of year	1	1	0
Proportion of female employees in LHV Group	57.6%	63%	60%
Percentage of female employees in leadership positions	48.4%	46.1%	44.8%
The ratio of the CEO's salary to median FTE salary at LHV	5.26	5.26	5.26
Gender pay-gap	0.92	0.87	-
Employee satisfaction indicator (on a 5-point scale)	4.5	4.5	4.6

Consolidated financial statements

Risk management

Risk is defined as a potential negative deviation from the expected financial results. LHV encounters several risks in its day-to-day operations. The objective of risk management at LHV is to recognise these risks, to measure them appropriately, to manage and to report them. More broadly, the aim of risk management is to increase the value of LHV by minimising losses and reducing the volatility of results. Risk management at LHV is based on a strong risk culture and follows the principle of three lines of defence. The first line of defence, the business units, is responsible for taking risk and for day-to-day risk management. The second line of defence is responsible for the ownership, continuous review, and implementation of a robust risk management framework in the Group, including ownership of the relevant methodologies defined in the policies, and for holistically ensuring that risk identification, assessment, measurement, management, mitigation, monitoring, and reporting is well executed in the Group.

The third line of defence, the internal audit, exercises independent supervision over the entire Group. Risk management principles, requirements and areas of responsibility are described in the risk management policy. The principles and objectives of capital management are described in internal documents (the capital management policy and capital objectives). More detailed risk management processes are described in the policies of the respective fields.

Under the initiative of the independent risk management unit, LHV has developed a group-wide risk appetite framework, approved by the Supervisory Board. LHV's risk appetite reflects its readiness to take specific risks. The larger the risk appetite, the more risk can be assumed. The risk appetite is set in line with the desired risk profile, reflecting the nature of LHV's business model.

Risk framework

Risk management principles, roles and responsibilities

- Risk management and control principles
- Ethics principles
- Remuneration principles
- Organizational structure
- Roles and responsibilities

Goals, measures and controls

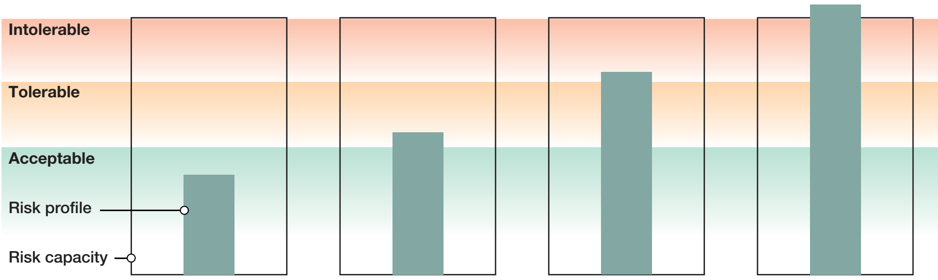
- Risk tolerance levels
- Measurement of risks
- Rights and limits

Internal and external reporting

Risk appetite has been defined in risk appetite statement for all risks LHV is materially exposed to. Risk appetite is determined in terms of both qualitative guidance and quantitative limits, considering the following principles:

- Qualitative guidance is worded simply and adopts the terminology commonly used in the organisation and in the business plan.
- Quantitative limits are set at a level that is sufficiently detailed to capture all key risk categories and sub-categories, but at the same time sufficiently aggregated to maintain each metric of relevance to the group-wide risk profile of LHV. Where quantification is possible, the acceptable, tolerable and intolerable amounts of risk are defined as follows:
  - acceptable – the amount of risk allowed to be taken under normal business conditions;
  - tolerable – the amount of risk that gives a warning signal: the increase of risk must be properly assessed, and an action plan defined to return to the acceptable area; the assessment results and the action plan must be reported at least to the Management Board of LHV;
  - intolerable – a hard limit violation, the level of risk LHV does not wish to exceed under any circumstances: immediate action must be taken to return at least to the tolerable area; the violation, assessment results and an action plan must be reported to the Supervisory Board of LHV.

Risk appetite framework



The actual risk profile is inside the acceptable range. Risk profile is under control and no specific action needed.

The actual risk profile is inside the tolerable range which indicates an early warning signal. An action plan must be submitted to the management.

The actual risk profile is inside the intolerable range. An action plan has been launched to reduce the risk profile.

The actual risk profile exceeds LHV risk capacity. Financial recovery plan has been launched.

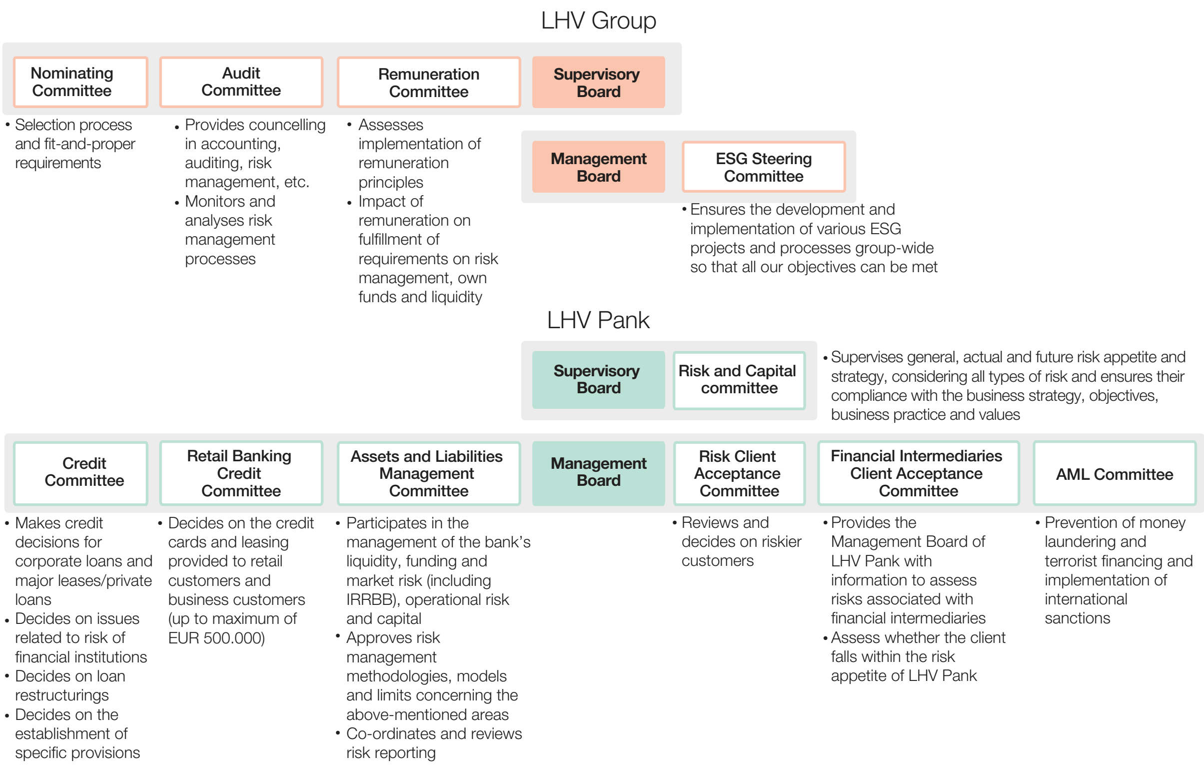
Risk capacity – the maximum amount of risk LHV is capable to take given its capital base, its risk management and control capabilities, and its regulatory constraints.

Risk appetite – the aggregate level and types of risk LHV is willing to assume within its risk capacity, in line with its business model, to achieve its strategic objectives.

Risk profile – combination of the real risks of LHV resulting from the nature, scale and complexity of LHV activities and operation environment.

As seen from the figure, if the actual risk profile remains within the acceptable risk appetite range, it is a foreseeable situation, and no further action is needed. If the actual risk profile is within the tolerable risk appetite range, it is an early warning signal: an action plan must be put in place to reduce the risk profile. It is also necessary to inform the Management Board in this case. If the actual risk profile exceeds the tolerable level, an action plan must be put in place to reduce the risk profile. It is also necessary to inform the Supervisory Board in this case. The first line of defence is responsible for managing LHV's risk profile and ensuring it stays within the risk appetite limits, while independent monitoring and reporting is the responsibility of the Risk Management Department. Within the framework of the financial recovery plan, LHV has developed early warning indicators with thresholds and corresponding measures.

In accordance with the risk management policy, quantitative risk appetite levels must be specified at least for capital risk, credit risk, market risk, operational risk, liquidity risk and money laundering risk. The risk appetite limits are defined in each of the respective risk policies, which are approved by the Supervisory Board. The policies also provide detailed instructions and guidelines. LHV has a system of committees and decision-making competencies. The functions of the main committees are shown in the figure below.



As part of the risk policy framework, LHV has developed a risk reporting process. The table below gives an overview of the main reports prepared by the Risk Management Department, which are presented to the governing bodies, and the reporting frequency.

Governing body	Members	Title of the report	Report frequency	Coverage of risks
Supervisory board of the LHV Group	All the members of the supervisory board of the Group	Risk report	Quarterly	Credit risk, market risk, interest risk, liquidity risk, operational risk, anti-money laundering risk, monitoring of legislation
		Compliance overview	Monthly	Compliance risk
		ICAAP report, ICAAP macro scenario, SREP report	Once a year	All the risks
Supervisory board of the Bank	All the members of the supervisory board of the Bank	Risk report	Monthly	Credit risk, market risk, interest risk, liquidity risk, operational risk, anti-money laundering risk, monitoring of legislation
		Risk management overviews	Once a year	All the risks
		ICAAP report, ICAAP macro scenario, SREP report	Once a year	All the risks
Risk and Capital Committee of the Bank	Rain Lõhmus, Andres Viisemann, Tiina Mõis Madis Toomsalu	Risk report	Quarterly	Credit risk, market risk, interest risk, liquidity risk, operational risk, anti-money laundering risk, monitoring of legislation
		Problematic loan customers	Quarterly	Credit risk
Audit committee	Kristel Aarna, Urmas Peiker, Tauno Tats	Risk report	Quarterly	Credit risk, market risk, interest risk, liquidity risk, operational risk, anti-money laundering risk, monitoring of legislation
CEO of the Group, Chairman of the Supervisory Board of the Bank	Madis Toomsalu	Risk report	Monthly	Credit risk, market risk, interest risk, The liquidity risk, operational risk, anti-money laundering risk, compliance risk, monitoring of legislation
Asset and Liability Committee of the Bank	Management board members of the Bank, Head of Treasury	Risk report	Monthly	Credit risk, market risk, interest risk, liquidity risk, operational risk, anti-money laundering risk, compliance risk, monitoring of legislation
		Business continuity test and planning	After every test	Operational risks
		Risk self-assessment	After assessment	Operational risks
Management Board of the Bank	Management board members of the Bank	Compliance overview	Once in a year	Compliance risks
		Anti-money laundering overview	Once in a year	Anti-money laundering risks
		Monitoring of legislation	Monthly	Compliance risks
		Compliance audit	After every audit	Compliance risks
		ICAAP report, ICAAP macro scenario, SREP report	Once a year	All the risks

LHV has established a risk management policy, which sets the risk management framework. Separate policies are set for major risk categories. The risks are analysed and monitored and reported to different levels of management on a monthly and quarterly basis. The monthly risk report presents information by type of risk. The risk report also includes information on capital adequacy. It provides a regular overview of all the important risks at the company level, allowing to monitor risk development, identify bottlenecks, and react promptly.

Within the overall risk management framework, specific risk types are managed via dedicated frameworks. As LHV's business model and the external environment are continuously developing, the type and size of LHV's risk exposures are constantly changing, and the risk management framework is adapted accordingly.

In developing the risk management framework, we have considered the relative materiality of current and estimated future exposures, as illustrated in the risk heat map below. The risk types with material exposures, i.e., where potential losses are substantial and the likelihood of such losses materialising is higher, are managed more closely. The specific framework elements, including methodology, processes, tools, people, and perimeter of application, reflect the specific nature of these risks.

The frameworks for addressing the main risk types the Group is more significantly exposed to, including solvency risk, credit risk, market risk, liquidity risk, and operational risk, are described in detail in the following sections.

Within the overall risk management framework, special attention is given also to ESG risk management, i.e., managing the risk of losses resulting from current or prospective impacts from environmental, social and/or governance factors. LHV recognises the growing materiality of this risk going forwards and is strengthening its risk management framework accordingly.

Risk management framework

This includes, similarly to all material risk categories, defining risk appetite and ensuring the Group stays within the risk appetite limits. Where appropriate, the ESG perspective is included in the aspects of the risk management framework directly addressing credit, market, operational, liquidity and funding, and strategic risks. Defining a common taxonomy and considering emerging regulations and best practices are parts of strengthening this framework. LHV maintains a no-go list of industries and types of transactions that are not eligible for financing due to their negative environmental or social impact.

1. Capital management

The net capital of a credit institution must be at all times equal to or exceed the minimum amount of share capital prescribed in the Credit Institutions Act. The capital of banks and investment firms in the European Union is subject to a legal framework (Capital Requirements Directive IV (CRD IV) / capital requirements regulation), largely based on the Basel III framework, as agreed in the Basel Committee on Banking Supervision. The objective of the framework is to strengthen the resilience of the financial sector to adverse economic shocks and thereby ensure adequate and sustainable financing of the economy. Significant changes implemented by the new requirements include the requirement for credit institutions to maintain a higher level and quality of capital than before and a unified framework for designing liquidity buffers. The CRD IV also defines measures for macro-prudential supervision that member states can use to mitigate the procyclical behaviour of credit institutions and to alleviate risks arising from market structure. Every year smaller changes have been implemented in the regulations. Due to the COVID-19 pandemic, the implementation of CRD V has been partially postponed and completely updated regulations will become effective in 2025.

The goals of the Group's capital management are:

- to ensure the Group's business continuity and ability to generate return for its shareholders;
- to maintain a strong capital base supporting business development;
- to comply with capital requirements as established by supervisory authorities.

The Group considers net own funds, as defined in the capital adequacy regulation, as capital. Its own funds consist of Common Equity Tier 1 (CET1) capital, Additional Tier 1 capital and Tier 2 capital. The amount of net own funds that the Group managed as at 31 December 2022 was EUR 451,747 thousand (31 December 2021: EUR 352,837 thousand). The goals of the Group's capital management are set based on both regulative requirements and additional internal buffer requirements.

The Group follows these general principles in its capital management:

- The Group must be adequately capitalised at all times, to ensure economic sustainability and enable financing new profitable growth opportunities.

- The main focus of the capital management is on Core Tier 1 own funds, because only Core Tier 1 own funds can absorb losses. All other capital layers in use are dependent on the volume of these funds.
- The Group's capital is divided into: 1) regulated minimum capital; 2) capital buffer held by the Group and 3) qualifying liabilities for MREL.
- MREL ratios can be met with suitable liabilities instead of own funds.

To reach its long-term economic goals, the Group must strive towards a proportional lowering of the regulated minimum capital (through risk minimisation and high transparency). At the same time, the Group must strive towards a sufficient and conservative capital reserve, which will ensure economic sustainability even in the event of a severe negative risk scenario.

The risk appetite set by the Group is an important input to capital management planning and capital goal setting. Larger risk appetite requires maintaining a higher capital buffer.

The capital requirements regulation, which is directly applicable in the member states, obligates all credit institutions operating in the European Union (including their consolidating holding companies) and investment firms to maintain a CET 1 capital ratio of 4.5% (the Common Equity Tier 1 capital as a percentage of the total risk-weighted assets) and a Tier 1 capital ratio of 6% (the Tier 1 capital as a percentage of the total risk-weighted assets).The overall Capital Adequacy Requirement (CAD), including both Tier 1 and Tier 2 capital, remains at the current level of 8.0%.

In addition to the main requirements based on uniform rules, the directive defines the principles for forming capital buffers.

First EFSA sets Pillar 2 capital charge, which is credit institution based capital requirement. Base capital requirement and Pillar 2 capital charge layers together form SREP capital requirement, the minimum capitalisation level credit institution must fulfil to retain the licence.

In addition to SREP capital buffers there are set several additional buffers that banks need to cover. Credit institutions have been subjected to capital maintenance and systemic risk buffers called capital conservation buffer of 2.5% imposed by the EFSA; other systematically important institutions buffers set individually to larger institutions of 2.0% (imposed by the Bank of Estonia); the countercyclical capital buffer set by the Bank of Estonia is set to 1.0%. Only systemic risk buffer is currently set at 0.0% (imposed by Bank of Estonia).

Breaching capitalisation levels triggers different actions from the regulator's side. These actions start with limitations for dividend payments and increase in different steps until losing the licence.

LHV received the SREP report in December 2022 and internal capital targets have been adjusted based on that. Overview of capital requirements based on the report is provided in the table below:

Capital requirements of LHV Group	CET1	Tier 1	CAD
Base capital requirement	4.50%	6.00%	8.00%
Pillar 2 capital charge	1.91%	2.55%	3.40%
Total SREP capital requirement	**6.41%**	**8.55%**	**11.40%**
Capital conservation buffer	2.50%	2.50%	2.50%
Other systematically important institutions buffer	2.00%	2.00%	2.00%
Systemic risk buffer	0.00%	0.00%	0.00%
Countercyclical buffer	1.00%	1.00%	1.00%
Capital requirements total	**11.91%**	**14.05%**	**16.90%**

In addition to the capital requirement, the EFSA has set Pillar 2 guidance for LHV at 2.00% on each capitalisation level. LHV meets this requirement as part of internal buffers.

LHV has kept a conservative approach in capital management and keeps additional internal buffers beyond the regulatory ones. Capitalisation requirements have been increased mainly due to the Bank's increasing market share and weaker macro-economic situation.

Starting from 2022, the LHV Group is also subject to the minimum requirement for own funds and eligible liabilities (MREL) which is a building block of the resolution plan. LHV has to maintain sufficient own funds and qualifying liabilities which can be used to cover losses in resolution planning. There are two separate MREL ratios which have to be complied with on the consolidation group level for LHV Group. MREL-TREA is calculated based on total risk weighted assets. MREL-LRE is calculated based on total assets. The final targets for the MREL ratios have been applied with a transitional period until 1st of January 2024. The final target levels of the ratios have been set at 24.57%

for MREL-TREA and 5.91% for MREL-LRE. The interim targets have been set at 19.08% for MREL-TREA and 5.91% for MREL-LRE which became effective on 1st January 2022. To distribute earnings, additional buffers must be applied on top of the abovementioned targets. Each year the EFSA will recalibrate the MREL requirements.

Internal capital adequacy targets as at 31 Dec 2022 are as follows:

Internal capitalisation targets of LHV Group	%
Core Tier 1 capital adequacy	14.20%
Tier 1 capital adequacy	16.35%
Total capital adequacy	19.20%
MREL-TREA (until 2024)	19.50%
MREL-TREA (starting from 2024)	24.57%
MREL-LRE	6.20%
Leverage ratio	3.50%

The Group uses the standard method for calculating capital requirements for credit and market risk and basic indicator approach calculating operational risk capital requirement. The Group and its subsidiaries have complied with all the capital requirements during the financial year and in previous years. LHV Group is planning to start using the internal model based capitalisation (IRB) in future and has been preparing the internal processes. LHV Group expects to apply for IRB licence in 2023 and hopefully will receive the licence year later.

Capital adequacy and the use of regulatory capital are managed by the Finance Department based on regular prudential reporting on capital requirements.

Each year, the LHV Group's Supervisory Board approves the goals of capitalisation and the target level of capital adequacy to cover potential risks arising from financial plan for next five years.

In addition to these, capitalisation situation is forecasted on monthly bases based on the actual performance and economic outlook; and if needed adjustments are made to capital plans. Risk Management Department is separately preparing several stress scenarios all affecting the capitalisation and which are taken into account in planning phase.

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

The Bank follows both regulatory requirements and capitalisation targets in daily capital management.

2. Credit risk

Credit risk is the risk of suffering financial loss, should any of the Group's customers or market counterparties fail to fulfil their contractual obligations to the Group. Credit risk arises from cash and cash equivalents, derivatives and deposits with banks and other financial institutions and debt securities, but mainly from credit exposures to customers, including outstanding loans, issued guarantees, other receivables, and commitments.

Credit risk is one of the largest risks for the Group's business; management therefore carefully manages its exposure to credit risk. A central principle for LHV is that each of LHV´s credit business units have full responsibility for their credit risks, that credit decisions adhere to the credit process and decisions are in line with LHV`s business and credit strategies. The credit risk management and control are distributed across the three lines of defence, with responsibilities concentrated in a dedicated independent Credit Risk Management Department, which reports regularly to the Management Board and Supervisory Board. As from 1 January 2022 the dedicated Credit Risk Management Department directly reports to the CEO of LHV Pank. The responsibilities of the dedicated Credit Risk Management Department include debt and risk assets management, real estate collateral assessment, corporate (exposure to LHV > EUR 500 thousand) credit risk analysis and first-line credit control and monitoring units.

Depending on the size and nature of each loan the credit process is performed based on the principle that low-risk loans can be approved through a more cost-efficient and faster process, while for riskier and larger exposures more in-depth analysis and process are carried out. Accordingly, the lending decisions are made by the Credit Committee (exposures > EUR 500 thousand), by the Retail Banking Credit Committee or at a lower decision level which includes decisions made by credit officers or fully automated decisions made by the system for small financing. For credit decisions either rating or scoring systems are used to assess customer credit risk (see subsection 2.1 Credit risk measurement and distribution). In the credit decision-making process LHV takes into account the principles of responsible lending and sustainability, including environmental considerations, social responsibility, and business ethics (see also subsection 'General ESG principles' of this section).

For an early identification of significant increase in credit risk a continuous monitoring is carried out after issuing the loan. Quarterly monitoring is performed based on the customer´s financial position for corporate customers (exposure to LHV > EUR 500 thousand). In addition, information from external sources like credit bureaus, the tax office and other public registers are used. At least annually all ratings of corporate customers, financial institutions and sovereigns are individually reviewed. Customers with a significant increase in credit risk are included in a watchlist. The financial position, liquidity, and collateral value of watchlist customers is thoroughly monitored and a monthly overview is given to the Credit Committee. For retail business, after the date of initial recognition, the borrower's payment behaviour is monitored on a periodic basis to develop a behavioural score. Any other known information about the borrower which impacts their creditworthiness – such as unemployment and previous delinquency history – is also incorporated into the behavioural score. Customers with increased credit risk in retail portfolio are generally managed based on the customer´s payment behaviour.

The Group employs a range of policies and practices for mitigating credit risk. The Group has internal policies on the acceptability of specific classes of collateral or credit risk mitigation.

Impact from COVID-19 and cooling economy

LHV used a conservative approach in credit risk measurement on the onslaught of the COVID-19 crises back in year 2020. LHV decided not to use any temporary regulatory measures exempting from changing the risk treatment of the customers to whom payment holiday was granted under public payment moratorium. This means that most of these customers were classified as forborne or default (distressed restructuring) exposures, which had a significant impact on the increase in the share of items classified to Stage 2 under IFRS 9. Even though almost all customers have returned to scheduled repayments without having any difficulties in servicing their obligations, the minimum probation period of forborne exposures is 2 years after the end of payment holiday. Consequently, the reclassification of these exposures back to Stage 1 continues throughout 2022 and 2023 depending on the initial length of the payment holiday (3–12 months). This decision was based on the fact that LHV's shares are listed and it would have made it more difficult for investors to understand the actual financial results.

The escalated conflict in Ukraine in early 2022, did not have direct impact to LHV credit portfolio, because of historical restrictive lending to customers exposed to risks outside EU. However, increasing energy prices need to be considered, when issuing credits both to corporates and retail clients going forward. For example, some business models need to change and both commercial and residential buildings need to become more energy efficient.

During the second half of the year 2022, the Estonian economy has entered a mild recession. So far, the cooling economy has had no negative impact on the credit portfolio quality. As opposite, both the forborne and the overdue portfolio have been continuously shrinking throughout the year 2022. LHV is continuously monitoring credit portfolio quality and is in close dialog with customers, so that in case of a need, potential risks could be mitigated.

ESG risks in credit risk

As there is growing evidence that ESG factors may affect credit risk, ESG considerations have become increasingly important in the Bank's credit risk decision processes including risk appetite principles, policies, and procedures.

ESG risks are defined in the context of this chapter as risks of any negative financial impact on the group stemming from the current or prospective impacts of ESG factors on its counterparties or invested assets. Environmental risk drivers are categorised as physical risks and transition risks. Physical risks are direct negative impacts from climate change and environmental degradation, which could result in reduced production capacity, increased raw material costs, asset impairment, increased labour and capital costs, etc. Transition risks refer to the uncertainty related to the timing and speed of the process of adjustment to an environmentally sustainable economy. This process may be affected by three drivers: policy, technology, and consumer preferences. The main changes in this field are happening in carbon-intensive sectors (e.g., climate-related policy actions may have an impact on asset prices). Social risks involve social factors that may have a positive or negative impact on the financial performance or solvency of a counterparty, such as the rights, well-being and interests of people and communities including (in)equality, health, inclusiveness, labour relations, workplace health and safety, human capital, and community life.

ESG risks can materialise in two ways, reflecting their potential double materiality. Financial institutions can be impacted by (outside-in perspective) ESG risks through their counterparties and invested assets, as these may be impacted by (outside-in perspective) or have an impact on (inside-out perspective) ESG factors. For example, a counterparty's environmentally harmful business activities (negative inside-out impact on environmental factors) might make it more vulnerable to the implementation of transition policies targeting environmental degradation (negative outside-in impact of environmental factors).

Considering the impact of its business activity, LHV has set a goal to promote an environmentally and socially sustainable and responsible economy and expedite progress toward solutions to key environmental and climate problems, by motivating customers to make more sustainable choices in their business activities and investment decisions.

LHV will refrain from knowingly offering credit products to customers whose activities bear clear evidence of human rights violations and serious environmental harm. Based on the principles of sustainable and responsible activity, it is against credit policy to credit customers whose volume of credit products from LHV exceeds EUR 500 thousand and whose operations are related to any of the areas listed in exclusion list in the table below.

Restricted fields of activity	**Description**
Forestry	• Those engaged in illegal logging
Well-being of endangered plant and animal species, animals	• Those engaged in trading in endangered or Red List plant and animal; • Those engaged in illegal animal testing as defined by European Union legal acts; • Activities related to the forcible feeding of ducks and geese; • Keeping of animals for the purpose of fur production
Arms industry	• Those whose area of activity is the production or distribution of weapons or weapons components prohibited under international law (cluster bombs, infantry mines, biological and chemical weapons, nuclear weapons, laser weapons designed to cause permanent blindness)
Energy industry	• Coal and oil shale mining and generation of electricity from them; • Activities in the preliminary phase of the oil production chain
Hazardous materials	• Asbestos mining and production, marketing and use of asbestos fibres and products and compounds containing these fibres; • Export of mercury and mercury compounds and the production, export and import of many mercury containing products
Tobacco	• Distribution of tobacco products or e-cigarettes if it is the primary area of activity of the company (>50% of revenue)
Fishing	• Practising ecologically unsustainable fishing methods, such as drifting nets, deep sea bottom trawls, use of explosives or cyanide
Transport	• Transport of oil or other hazardous materials on ships that do not meet the requirements of the International Maritime Organization; • Financing new diesel-powered passenger cars in 2030 or later

General ESG principles

In addition to exclusion list of certain sub-sectors, LHV has also adopted the general ESG principles, which restrict crediting of activities like:

- production and trading of all goods that are illegal under the laws and regulations of the Republic of Estonia or international conventions and agreements;
- use of forced labour or human rights violations;
- facilitation of prostitution or production of pornographic material;
- distribution of prohibited substances and trading without required export or import licences;
- activities that have a negative impact on UNESCO World Heritage sites;
- activities that have a negative impact on national parks and natural protection areas or wetlands covered by the Ramsar Convention;
- activities prohibited under the legal acts of the Republic of Estonia or international conventions related to protection of biological diversity resources or cultural heritage;
- illegal forced expulsion of persons, groups of communities

In the lending process ESG risks are taken into consideration in loan reviews. A detailed ESG risks analysis is done for corporate loan applications of over EUR 0.5 million. For other customers, a basic assessment of ESG factors is made based on the nature and complexity of the loan product and the customer's field of activity. To identify borrowers that are exposed, directly or indirectly, to increased risk associated with ESG factors, a comprehensive heat map of ESG risks for individual economic (sub)sectors was developed in cooperation with environmental and social field experts. The heat map highlights environmental and social risks assessment for each individual economic sector, taking into account the corresponding risk classifications of rating agencies and international financial institutions, as well as local and EU regulations and Estonian national dimension where relevant.

Overview of LHV credit portfolio by environmental and social risks classification of economic sectors is given in the following table.

Credit portfolio distribution by risk classification

	Risk level	2022	2021
Environmental and climate change risk (E)	High	10.5%	14.0%
	Medium	56.3%	51.2%
	Low	33.1%	34.8%
Social risk (S)	High	10.6%	14.8%
	Medium	57.5%	56.1%
	Low	32.0%	29.2%

Development of the Bank's ESG analysis procedures and tools for corporate customers took place during the year and is expected to continue next year.

2.1 Credit risk measurement and distribution

The Group classifies the financial assets exposed to credit risk in the following key categories:

a) due from central banks and credit institutions (referred to as 'banks' in the tables) and investment companies

b) debt securities and derivatives

c) loans to legal entities

d) loans to individuals

a) Due from banks and investment companies

Management estimates that the credit risk exposure from cash and cash equivalents, held at the central bank, other correspondent banks and investment institutions is inherently low. Loans and advances to central banks, credit institutions and investments companies are generally unsecured. The funds of the Group are assessed according to ratings given by Standard & Poor's or equivalent (central banks are without a rating). In case there are ratings available from more than one rating agency, the average, or the most conservative rating is used.

If Estonian local credit institutions do not have external ratings and they are subsidiaries of large EU banks, the rating of the parent company is used. Management has assessed that the expected credit loss (ECL) from credit institutions' and investment companies' exposures is immaterial due to the strong ratings of the counterparties and as the Group holds only very liquid positions with them.

b) Debt securities and derivatives

The Credit Committee sets limits on taking credit risk associated with debt securities considering the issuer's rating.

No principal and accrued interest receivables arising from debt securities are overdue. The bonds have no collateral.

c) Loans to legal entities

Loan portfolio of legal entities includes credit to companies, local governments, non-profit associations (incl. apartment associations) etc., including the following products:

- corporate loans (corporate lending)
- leasing
- overdraft (corporate lending)
- trade finance (corporate lending)
- leveraged loans (investment financing)
- credit cards and hire-purchase (consumer financing)
- apartment association loans (corporate lending)
- credit letters (consumer financing)

Credits to legal entities (except apartment association loans) with total exposure to LHV of more than EUR 500 thousand are evaluated on an individual basis. Each customer is assigned a credit rating between 1 and 13, where 1 means the lowest probability of default (PD) and 13 indicates insolvency. Credit rating is assigned to a customer considering a combination of the customer's financial status and business risk. The specific financial ratios and business risk aspects considered depend on the rating model used: corporate, commercial real estate, residential development, local government, and commodity. Credit rating is assigned by a credit analyst and confirmed by Head of the Credit Analysis Department, but the final decision of risk taking is the unanimous decision by the Credit Committee. After issuing the loan, follow-up monitoring is performed usually at least on a quarterly basis for each customer's financial position. At least annually all customer ratings are reviewed. Customers with significant increase in credit risks are listed in watchlist. The financial position, liquidity, and collateral value of watchlist customers is thoroughly monitored more frequently.

Credits below EUR 500 thousand to legal entities and loans to apartment associations irrespective of the loan amount are analysed with a more time-efficient scoring process. The scoring process is carried out at the time of submission of the loan application, and it is one of the criteria for issuing the loan. The probability of default (PD) is calculated by reference to the customer's financial data and payment behaviour. The structure of assets and liabilities as well as the profitability and cash flow ratios are also taken into account.

d) Loans to private individuals

The loan portfolio to private individuals includes secured and unsecured credit and leasing products to private individuals, including the following products:

Credit products to private individuals	Explanation
mortgage loans (private lending)	secured loan for acquiring an apartment or house (home loan)
private loans (private lending)	secured loan for free use (investment activity, renovation, etc.)
consumer loans (consumer financing)	unsecured consumer loan (issuer: subsidiary AS LHV Finance)
hire-purchase (consumer financing)	unsecured instalment payment product offered by merchants (issuer: subsidiary AS LHV Finance)
leasing	leasing for the purchase of vehicles
leveraged loans (investment financing)	loan against the collateral of publicly traded securities
credit card loans (consumer financing)	unsecured credit card loan
overdraft (private lending)	unsecured overdraft
study loan (private lending)	loan to students with a state guarantee
real estate leasing (private lending)	mortgage loan (property is owned by LHV)

Credits to private individuals are also analysed with a time-efficient scoring process (for more information on the inputs for the PD models used, see the subsection 'Credit risk grading'). The scoring process is carried out at the time of loan application and it is one of the criteria for issuing the credit. Credit decisions are made by the Retail Banking Credit Committee or at a lower decision level. Consumer financing products to private individuals are offered through the subsidiary LHV Finance in Estonia.

Credit risk measurement

For all issued credit products LHV uses either rating or scoring systems to assess customer credit worthiness, as outlined in the table below. For credit decisions in the corporate segment (exposure to LHV > EUR 500 thousand) expert-based rating model is used and in retail application scoring statistical PD models are used, while portfolio scoring PD models have been developed for the existing contracts. There are also separate models to cover the dimensions of Loss Given Default (LGD) and Credit Conversion Factor (CCF).

Models used for credit worthiness assessment

Portfolio	Segment	Definition	PD	LGD	CCF/EAD
Corporate	Corporate exposures	Loans to companies with total exposure to LHV > EUR 500 thousand	Rating models	Model	Model
Retail	SME, incl. micro enterprises	Loans to companies with total exposure to LHV <= EUR 500 thousand, loans to apartment association irrespective of total exposure to LHV	Scoring models		
	Private mortgage	All mortgage loans to private individuals	Scoring models		
	Private non-mortgage	All consumer financing products and car leasing to private individuals	Scoring models		

Credit risk grading

The Group uses internal credit risk grading that reflect the assessment of the PD of individual counterparties. The Group use internal rating or scoring models tailored to various categories of counterparties. Different risk characteristics are used for different types of exposures to assess the borrower's credit risk:

- obligor risk characteristics
- for corporate exposures: financial statements, management experience, support from parent company, etc.
- for retail exposures: financial statements or personal income information, socio-demographic information, behavioural information, etc.
- transactional risk characteristics – type of product, remaining balance, etc.
- delinquency characteristics from internal and external sources.

In addition, the rating models enable expert judgement from the Credit Risk Officer to be fed into the final internal credit rating for each counterparty. This allows to include considerations which may not be captured as part of other data inputs.

The credit grades are calibrated so that the risk of default increases exponentially at each higher risk grade. For example, the difference in the PD between rating grade 4 and 5 is smaller than the difference in the PD between grades 7 and 8.

The following are additional considerations for each type of portfolio held by the Group:

- **Retail**

In retail portfolio, risk assessment is done at the credit facility level and the final scoring is mapped to PD. After the date of initial recognition, for retail business, the payment behaviour of the borrower is monitored on a periodic basis to develop a behavioural score. Any other known information about the borrower which impacts their creditworthiness – such as unemployment and previous delinquency history – is also incorporated into the behavioural score.

- **Corporate**

For corporate business, the rating is determined at the borrower level. A credit analyst will incorporate any updated or new information/credit assessments into the credit system on an ongoing basis. In addition, the analyst will update information about the creditworthiness of the borrower at least annually from sources such as public financial statements. This will determine the updated internal credit rating and PD.

- **Treasury**

For debt securities in the Treasury portfolio, the credit standing of the security is determined based on the ratings of external rating agencies. These ratings are continuously monitored and updated. The PDs associated with each rating are mapped to LHV's rating scale.

- **Credit risk ratings**

The Group's rating method used for evaluating the PD of corporate loans consists of a total of 13 credit ratings where 1 stands for the lowest and 13 for the highest credit risk (default). Ratings 1 and 2 are attributed only to international enterprises, organisations, local governments, and countries whose solvency has been confirmed by the rating agencies with their investment grade rating. The rating classes 3-13 are also partly based on the evaluation of rating agencies, although this category includes mainly Estonian enterprises that do not have an international rating.

Internal rating scale for corporate loans and mapping of external ratings

LHV rating	LHV description	PD%	S&P	Moody's
1		0.03	AAA	Aaa
2		0.05	AA+	Aa1
3		0.10	AA, AA-	Aa2, Aa3
4		0.20	A+,A,A-	A1,A2,A3
5	Investment grade	0.30	BBB+	Baa1
6		0.40	BBB	Baa2
7		0.50	BBB-	Baa3
8		1.00	BB+,BB	Ba1,Ba2
9		2.50	BB-	Ba3
10	Non-investment grade	5.00	B+	B1
11	(including special monitoring)	10.00	B,B-	B2,B3
12		30.00	CCC/C	Caa
13	Default	100.00	D	C

The rating methods are subject to annual validation and recalibration so that they reflect the latest projections in the light of all actually observed defaults.

Ratings are divided into three groups: investment grade, non-investment grade and default. Investment grade is allocated when the counterparty is not overdue as at the reporting date. Special monitoring status is allocated when the rating of the counterparty is 10-13. Rating 13 (default status) is based on the definition of default.

Collateral

Even though the Group only issues credits to creditworthy customers from payment ability perspective, LHV also employs a range of policies and practices to mitigate credit risk. The Group has internal policies on the acceptability of specific classes of collateral or credit risk mitigation.

The Group prepares a valuation of the collateral obtained as part of the loan origination process. This assessment is reviewed periodically. The valuations of the market value of collaterals are based on the principle of conservatism, which takes into account the type of collateral, its location, the likelihood of realisation and liquidity.

Expert evaluations are used to evaluate immovables. To ensure that market values are up to date, the individual valuations of commercial real estate are updated at least once a year. In the case of residential and other homogeneous types of real estate, statistical indexation models are also used for regular re-evaluation.

The main collateral types for loans and advances are:

- Mortgage
- Commercial pledge
- Commodity pledge
- Deposit
- Credit insurance
- Marketable securities
- Unlisted securities
- Pledge over the right of claim
- Guarantee of KredEx Fund, the Rural Development Foundation, or the European Investment Fund
- Letter of credit
- Surety of a private person or legal entity
- Vehicle, machinery, aircraft, equipment etc.

The Group prefers collateral in the case of which there is no strong correlation between the customer's default risk and the value of the collateral. In general, the pledged assets need to be insured, the life of the collateral needs to be longer than the due date of the loan and the market value of the collateral needs to exceed the outstanding loan balance.

Unsecured loans can be issued to private customers up to a specified amount. For corporate customers this is only allowed when the cash flow forecast shows stable and significantly strong cash flows and/or the customer's credit risk is low.

Collaterals for leveraged loans are monitored daily and, if collateral value is falling, immediate measures are taken to avoid credit losses. Consumer loans and credit card loans are issued without collateral and risk is mitigated by regular monitoring of customers' payment behaviour. Leasing and mortgage loans are all over-collateralised. Regarding leasing, hire purchase, mortgage loans and overdraft to private individuals, the Group monitors customers in arrears on a regular basis.

In relation to under-collateralised corporate loans, it should be taken into consideration that the Group has assessed the market value of certain collaterals conservatively (personal sureties, commercial pledges). Under-collateralised loans are mainly considered to bear higher risk, for which the Group carries out monthly monitoring in the Credit Committee, to mitigate potential credit losses.

2.2 Expected credit loss measurement

IFRS 9 outlines a three-stage model for impairment based on changes in credit quality since initial recognition as summarised below:

A financial instrument that is not credit-impaired on initial recognition is classified to 'Stage 1' and its credit risk is continuously monitored by the Group.

If a significant increase in credit risk (SICR) since initial recognition is identified, the financial instrument is moved to Stage 2 but is not yet deemed to be credit-impaired. Please refer to subsection 2.2.1 'Significant increase in credit risk' for a description of how the Group determines whether a significant increase in credit risk has occurred.

If the financial instrument is credit-impaired, the financial instrument is moved to Stage 3. Please refer to subsection 2.2.2 'Definition of default and credit-impaired assets' for a description of how the Group defines 'credit-impaired' and 'default'.

For financial instruments in Stage 1, the ECL is measured at an amount equal to the portion of lifetime ECLs that results from default events possible within the next 12 months. For instruments in Stages 2 or 3, the ECL is measured based on ECLs on a lifetime basis. Please refer to subsection 2.2.3 'Measuring ECL – Explanation of inputs, assumptions, and estimation techniques' for a description of inputs, assumptions and estimation techniques used in measuring the ECL.

A pervasive concept in measuring the ECL in accordance with IFRS 9 is the consideration of forward-looking information. Subsection 2.2.4 'Forward-looking information incorporated in the ECL model' includes an explanation of how the Group has incorporated this in its ECL models.

Purchased or originated credit-impaired financial assets are those financial assets that are credit-impaired on initial recognition. Their ECL is always measured on a lifetime basis (Stage 3).

The following diagram summarises the impairment requirements under IFRS 9 (other than purchased or originated credit-impaired financial assets):

Change in credit quality since initial recognition

Stage 1	Stage 2	Stage 3
(Initial recognition)	(Significant increase in credit risk since initial recognition)	(Credit-impaired assets)
12-month expected credit losses	Lifetime expected credit losses	Lifetime expected credit losses

The key judgements and assumptions adopted by the Group in addressing the requirements of the standard are discussed below.

2.2.1 Significant increase in credit risk

The Group considers a financial instrument to have experienced a significant increase in credit risk (SICR) when one or more of the following quantitative or backstop criteria have been met:

Quantitative criteria

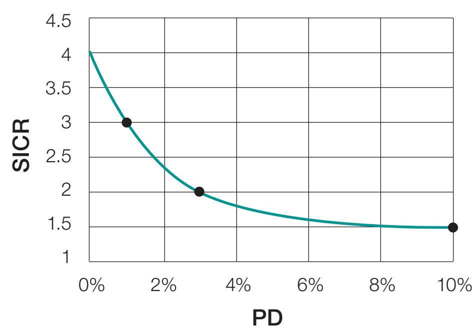
The remaining lifetime PD at the reporting date has increased, compared to the lifetime PD expected at the reporting date when the exposure was first recognised, if it exceeds the relevant threshold per the table below:

Retail portfolio

Lifetime PD band at initial recognition	Increase in Lifetime PD at reporting date which is considered significant
X%	≥100 bps
And	Current PD_life/Initial PD_life > 1.4885+exp(0,9549-54,173*Initial PD_life)

To illustrate the formula, see the SICR curve graphic below. In addition to the curve, the PD increase has to be at least 100 bps. The SICR curve shows the relation between the origination PD and the significance threshold (PD increase in number of times) for identifying significant increase in default risk

To illustrate the application of these thresholds, take for example a 3-year retail business loan agreement initiated on 13th February 2018, which at initial recognition had a lifetime PD of 3.36 % and was expected to have a residual lifetime PD of 2.76% ten months later at the current reporting date. If at the current reporting date the loan has a current lifetime PD of 8.86% then this exceeds the expected PD of 2.76% by more than the threshold shown above. Therefore, a SICR has occurred.



These thresholds have been determined by assessing how the lifetime PD moves prior to an instrument becoming delinquent. The lifetime PD movements on instruments which do not subsequently become delinquent have also been assessed, to identify the natural movement in the lifetime PD, which is not considered indicative of a SICR. The average maturity of the corporate portfolio is short at 2.5 years.

Backstop

A backstop is applied and the financial instrument considered to have experienced a SICR if the borrower is more than 30 days past due on contractual payments.

Low credit risk exemption

The Group has used a low credit risk exemption for cash and nostro accounts fulfilling the liquidity portfolio criteria in the years ended 31 December 2022 and 31 December 2021.

2.2.2 Definition of default and credit-impaired assets

The Group defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

Quantitative criteria

The borrower has breached the materiality threshold in 90 consecutive days.

Qualitative criteria

The following circumstances are considered as indicators that the customer may not be able to pay the debt in full:

- there are indications of unlikeliness to pay, which show that the borrower is in significant financial difficulty
- distressed restructuring has occurred
- additional forbearance measures have been applied on the probation period for existing forbearance measures
- the contract is terminated.

The criteria above have been applied to all financial instruments held by the Group and are consistent with the definition of 'default' used for internal credit risk management purposes. The definition has been applied consistently to model the PD, EAD and LGD throughout the Group's expected loss calculations.

In applying the default status, a customer-based approach is used for the corporate portfolio and a contract-based approach is used for the retail portfolio.

An instrument ceases to be in default when it no longer meets any of the default criteria throughout the probation period. The probation period should not be shorter than 3 months from the moment that the default criteria cease to exist.

Loans under distressed restructuring are considered to require particular attention in the reclassification to non-defaulted status because the assessment of days past due is based on the modified payment arrangement and the exposure cannot stop being restructured until the time it is fully repaid. Therefore, the probation period for these loans is defined as at least 1 year from the latest of:

- the moment of extending the restructuring measures;
- the moment when the exposure has been classified as defaulted;
- other end of grace period included in the restructuring arrangements.

2.2.3 Measuring ECL – Explanation of inputs, assumptions, and estimation techniques

The aim of the ECL model is to calculate the 12-month and lifetime expected credit losses that:

- are unbiased, i.e., do not include any conservatism or optimism;
- are probability-weighted amounts that are determined by evaluating three provisioning scenarios (base scenario, upside scenario and downside scenario);
- reflect the time value of money;
- use reasonable and supportable information about past events, current conditions, and forecasts of future economic conditions.

The Group's ECL model follows the widely accepted sum of marginal losses approach, whereby ECLs are calculated as the sum of the marginal losses occurring in each period (month) from the reporting date. The marginal losses are derived from individual risk parameters (PD, LGD, EAD) that estimate exposures and losses in the case of default and the marginal PD for each period (the probability of default between time periods t and t+1.

ECL calculations are based on four components:

- PD is an estimate of the likelihood of default over a given time horizon.
- EAD is an estimate of the exposure at a future default date, taking into account the expected changes in the exposure after the reporting date, including repayments of principal and interest, and expected drawdowns on committed facilities.
- LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that LHV would expect to receive, including from any collateral. LGD is expressed as a percentage of EAD.
- Discount factor is used to discount an expected loss to a present value at the reporting date.

Mathematically, the ECL amount for the prediction horizon T (12 months or lifetime, depending on whether 12-month or lifetime ECL estimates are calculated) is expressed as follows:

$$ECL_T = \sum_{t=1}^{T} PD_t * LGD_t * EAD_t * d_t$$

Where:

t = 0

T – a one-month period within the prediction horizon T;

for a 12-month ECL estimate

T = 12 months; for a lifetime ECL estimate

T = expected life of the lending exposure

PDt – marginal PD for month t

LGDt – LGD as estimated for month t

EADt – exposure amount, incl. expected

drawdowns of undrawn commitments, at month t

dt – discount factor for month t

The discount rate represents the effective interest rate (EIR) for the financial instrument or an approximation thereof.

A simplified example of the calculation logic is given in the table below. Note that in this example for secured loans, LGD is directly derived from the collateral value and as a simplification, fair value is assumed to be constant. However, the actual ECL model takes into account the possible decrease of collateral fair value over time through different scenarios.

ECL (EUR)	31 Jan 2023	28 Feb 2023	31 Mar 2023	30 Apr 2023	31 May 2023	30 Jun 2023	31 Jul 2023	31 Aug 2023	30 Sep 2023
(1) Exposure (EAD)	4,000	3,500	3,000	2,500	2,000	1,500	1,000	500	0
(2) Marginal PD, %	0.40%	0.38%	0.36%	0.34%	0.32%	0.30%	0.28%	0.26%	0.24%
(3) Collateral value	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000
(4) Potential loss amount [Max(0:1-3)]	2,000	1,500	1,000	500	0	0	0	0	0
(5) Expected marginal loss [2*4]	8.00	5.70	3.60	1.70	0.00	0.00	0.00	0.00	0.00
(6) Expected marginal loss, discounted	7.97	5.65	3.56	1.67	0.00	0.00	0.00	0.00	0.00
Lifetime ECL at 31/12/2022 [Sum (6)]	18.85								

Note. Discounting is done, assuming the current reporting date 31 December 2022 and a 5% discount rate.

For the defaulted exposures, ECL is computed as:

$$ECL_T \sum_{t=1}^{T} LGD_t * Exposure_t * d_t$$

Each of the risk dimensions (PD, LGD, EAD) is covered with internally developed rating and scoring models. These models have been developed for business and credit management.

The key issue in ECL modelling is to transform the available risk parameter values into forward-looking point-in-time (PiT) estimates and feed them into the expected credit loss calculation formula.

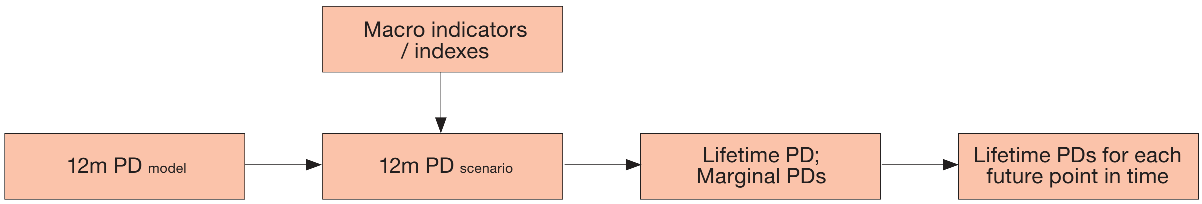
	IFRS 9 parameters
PD	• 12-month PD; lifetime PD broken down further into marginal probabilities for sub-periods • Forward looking PiT estimate, reflecting assessment of current and future economic conditions, and a range of possible future outcomes • No regulatory floors or margins of conservatism applied
LGD	• Neutral PiT projections • Consider current and future economic conditions, and a range of possible future outcomes • Recoveries discounted, using EIR as discount rate • No regulatory floors or margins of conservatism applied
CCF/EAD	• Reflects expected changes in the balance outstanding over the lifetime of the lending exposure, incl. scheduled loan payments and prepayments
ECL	• PV of cash shortfalls. For Stage 1 exposures, 12-month PD is used. For stage 2 exposures, lifetime PD is used. For Stage 3 exposures, PD = 100%

The following paragraphs outline how the existing underlying models are leveraged off for the ECL measurement. Each risk dimension in detail is discussed in the following chapters.

'Feeding' PDs from underlying rating and scoring models into ECL model

Instead of the historically based or long-run average 12-month PDs (model PDs), forward-looking 12-month and lifetime PiT estimates and marginal PDs are required for the expected credit loss calculation in accordance with IFRS 9.

The transformation of the model PD (PD model) is performed in the following flow:



Next, forward-looking 12-month PiT estimate is converted to lifetime PD and marginal PDs. This is done using the segment-specific standard default curve which gives the timing of the expected defaults for the remaining life of an exposure.

Lastly, lifetime PDs for each of the future points in time till the end of the expected life of the exposure are calculated.

Feeding LGDs from underlying models into ECL model

In the LGD dimension, the use of the underlying LGD models differs for secured and unsecured lending exposures.

The LGD for the secured part of the secured loan is estimated from fire-sale price of the collateral.

LGDs for the unsecured exposures and unsecured parts of the secured exposures rely on historical portfolio level statistics.

Further, macroeconomic scenarios are incorporated into both secured and unsecured LGDs as applicable for the defined provisioning scenarios.

Feeding CCF estimates from underlying models into ECL model

Internal CCF estimates feed directly into the ECL model and are used in the calculation of EAD. No further adjustments are needed for the CCF (because the internal estimates do not include margins of conservatism), through the cycle (TtC) nor downturn adjustments.

2.2.4 Forward-looking information incorporated in the ECL model

In order to incorporate forward-looking information into the ECL measurement and capture a range of possible outcomes for the future conditions, probability-weighted ECL amounts based on the three provisioning scenarios (base, upside and downside) are calculated. This approach enables to reflect non-linear relationships between alternative scenarios and the ECL.

Mathematically:

$$ECL = p_{base} * ECL_{base} + p_{up} * ECL_{up} + p_{down} * ECL_{down}$$

Where:

p_{base}, p_{up}, p_{down} – probabilities of the base, upside and downside scenarios, respectively

ECL_{base}, ECL_{up}, ECL_{down} – expected credit loss amounts calculated for each of the defined scenarios

ECLs for each of the defined scenarios are derived based on the general formula, using scenario specific risk parameter values.

Probability-weighted lifetime PD estimates for the purpose of assessing significant increase in credit risk are calculated in the same way:

$$PD = p_{base} * PD_{base} + p_{up} * PD_{up} + p_{down} * PD_{down}$$

Where:

PD_{base}, PD_{up}, PD_{down} – lifetime PD estimates corresponding to each of the defined scenarios

Selected indicators for private person credit portfolios

Selected macro indicators for private person credit portfolios and relative importance of each of the indicators are shown in table below:

	Mortgage	Consumer financing, fixed rate	Consumer financing, floating rate (incl. leasing)
Wage growth, %	17%	22%	18%
Unemployment rate, %	33%	44%	36%
House price index growth, %	8%	0%	0%
Inflation rate, %	8%	11%	9%
Euribor, 6m	17%	0%	18%
Bank lending margins	17%	22%	18%
Total	**100%**	**100%**	**100%**

Note. Relative importance of each of the indicators is calculated based on the indicator 'weights'.

Selected indicators for companies

A wide range of macroeconomic and sector-specific indicators was considered for companies. The analysis was conducted based on two industry breakdowns:

1) broad industry sector level based on letter codes of the NACE Rev.2 classification, and
2) sub-sectors based on lower-level numerical codes of the NACE Rev.2 classification.

The following conclusions were drawn from the analysis:

- All sectors have been affected by the same credit cycle and have experienced major sector-wide financial difficulties at the same time. Despite that, there are certain idiosyncratic differences between the industry sub-sectors, e.g., in manufacturing.
- There are only a few variables that work; the variables that have explanatory power tend to work similarly for most of the industry sectors:
    - GDP growth, which explains the general state of economy,
    - change in turnover,
    - change in number of persons employed.
- Change in an industry sector's profit/loss was also tested but it tends to be too volatile for drawing conclusions on substantial change in default risk.
- A few macro indicators are significant for certain industry sectors, sub-sectors and/or groupings of sub-sectors even if correlations are difficult to show due to low numbers of observations and/or because of a relatively short observation period. e.g.:
    - export conditions for export-oriented industries such as: metal products, chemical products, and electrical equipment,
    - population growth and income growth for residential real estate,
    - household consumption growth for industries that focus on internal consumption such as retail trade.
- In conclusion, the gross value added by industry sectors was selected as the indicator for companies, given several considerations:
    - observed correlation with the considered proxies for default rates;
    - GDP, which is a close indicator to the gross value added, is the preferred approach at the industry level;
    - it is easier to project for a macroeconomist than alternative indicators.

Economic variable assumptions

Macroeconomic scenarios (forecasts) with their indicators (incl. corporate portfolio PD and LGD estimates) are developed at least once a year internally in the Financial Risk Department that consults with the macro analysts and experts from credit management, business and finance units.

Macro developments are monitored on a quarterly basis as new macroeconomic data becomes available. Forecasts are updated as necessary to ensure timely inclusion of new forward-looking information into the ECL estimates.

The provisioning scenarios and significant updates to the scenarios are approved in the Risk and Capital Committee.

The most significant period-end assumptions used for the ECL estimate as at 31 December 2022 are set out below. The base, downside and upside scenarios were used for all portfolios.

Assumptions in companies ECL estimate, valid at 31 Dec 2022

	Base scenario		Downside scenario		Upside scenario	
General macro-financial indicators	**2023E**	**2024E**	**2023E**	**2024E**	**2023E**	**2024E**
Real GDP growth, %	**0.4%**	**3.1%**	**-3.5%**	**2.5%**	**1.0%**	**3.5%**
Household consumption, %	-1.1%	2.1%	-4.0%	2.0%	-0.5%	3.3%
Government consumption, %	3.9%	-2.9%	-2.0%	-1.0%	3.5%	0.5%
Gross fixed capital formation, %	-0.5%	5.1%	-5.0%	5.0%	0.0%	7.0%
Exports of goods and services, %	-0.1%	2.8%	-3.0%	3.2%	0.0%	4.0%
Imports of goods and services, %	-5.4%	1.5%	-0.5%	2.9%	-0.4%	3.8%
Nominal GDP, EUR million	38,486	40,353	37,985	39,324	38,569	40,997
GDP deflator, % change	5.8%	1.7%	8.1%	1.0%	5.4%	2.7%
Consumer price growth, %	9.3%	2.8%	12.0%	1.5%	7.0%	2.5%
Unemployment rate, %	7.4%	6.8%	9.0%	7.8%	7.0%	6.5%
Change in employment, %	-1.3%	1.0%	-0.5%	0.7%	-0.5%	1.2%
Net monthly wage growth, %	7.2%	6.5%	5.8%	4.2%	9.1%	7.6%
House price index growth, %	-10.0%	0.0%	-15.0%	-5.0%	-5.0%	6.0%
Euribor 6m	3.2%	3.0%	3.2%	3.0%	3.2%	3.0%
Bank lending margins on new loans (NFC)	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%

Nominal growth

	Base scenario		Downside scenario		Upside scenario	
Gross value added by sectors, YoY growth rates	**2023E**	**2024E**	**2023E**	**2024E**	**2023E**	**2024E**
Total - all NACE activities	**6.5%**	**5.1%**	**4.7%**	**3.8%**	**6.7%**	**6.5%**
Agriculture, forestry, and fishing	40.3%	24.5%	29.8%	17.3%	40.6%	26.2%
Industrial sector, except construction	5.2%	4.9%	1.5%	5.9%	5.5%	6.3%
Industrial sector, except construction and manufacturing (mostly energy related)	5.2%	2.8%	-0.3%	5.7%	5.5%	4.2%
Manufacturing	5.2%	5.7%	2.2%	6.0%	5.4%	7.1%
Construction	4.1%	4.9%	-2.4%	9.0%	4.3%	6.3%
Wholesale and retail trade, transport, accommodation, and food service activities	6.2%	5.5%	4.8%	4.1%	6.5%	6.9%
Information and communication	10.3%	7.6%	10.3%	4.2%	10.6%	9.1%
Financial and insurance activities	8.2%	7.5%	6.8%	6.2%	8.4%	9.0%
Real estate activities	1.0%	6.1%	-1.5%	6.0%	1.2%	7.6%
Professional, scientific, and technical activities; administrative and support service activities	3.5%	1.4%	2.1%	0.1%	3.7%	2.8%
Public administration, defence, education, human health and social work activities	10.4%	3.3%	11.3%	-0.1%	10.6%	4.8%
Arts, entertainment, and recreation; other service activities; activities of household and extra-territorial organisations and bodies	1.4%	6.3%	-1.3%	5.0%	1.6%	7.8%

The weightings assigned to each economic scenario on 31 December 2022 were as follows:

Valid at 31 Dec 2022

	Base scenario	Downside scenario	Upside scenario
Weights of economic scenarios	60%	25%	15%

The weightings assigned to each economic scenario on 31 December 2021 were as follows:

Valid at 31 Dec 2021

	Base scenario	Downside scenario	Upside scenario
Weights of economic scenarios	60%	25%	15%

The most significant period-end assumptions used for the ECL estimate as at 31 December 2021 are set out below. The base, downside and upside scenarios were used for all portfolios

Assumptions in companies ECL estimate, valid at 31 Dec 2021

	Base scenario		Downside scenario		Upside scenario	
General macro-financial indicators	**2022E**	**2023E**	**2022E**	**2023E**	**2022E**	**2023E**
Real GDP growth, %	**2.8%**	**3.9%**	**2.0%**	**3.0%**	**3.7%**	**4.1%**
Household consumption, %	4.0%	3.6%	3.5%	2.5%	6.0%	3.5%
Government consumption, %	-0.9%	-1.3%	0.0%	-0.4%	-1.2%	-0.8%
Gross fixed capital formation, %	-14.5%	6.9%	-15.0%	6.0%	-10.0%	8.0%
Exports of goods and services, %	4.9%	4.8%	3.0%	5.3%	6.5%	6.0%
Imports of goods and services, %	-0.9%	4.8%	-2.0%	5.3%	4.0%	4.2%
Nominal GDP, EUR million	33,020	35,480	32,681	34,941	33,068	35,595
GDP deflator, % change	5.8%	3.4%	5.5%	3.8%	5.0%	3.4%
Consumer price growth, %	6.9%	3.0%	6.5%	3.5%	6.0%	3.0%
Unemployment rate, %	5.5%	5.3%	6.0%	5.8%	5.5%	5.0%
Change in employment, %	1.1%	0.6%	0.5%	0.8%	1.5%	0.2%
Net monthly wage growth, %	8.3%	8.0%	6.7%	6.0%	8.5%	8.0%
House price index growth, %	8.5%	8.0%	3.0%	5.0%	8.8%	8.2%
Euribor 6m	-0.5%	-0.2%	-0.5%	-0.5%	-0.5%	-0.2%
Bank lending margins on new loans (NFC)	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%

Nominal growth

	Base scenario		Downside scenario		Upside scenario	
Gross value added by sectors, y-o-y growth rates	**2022E**	**2023E**	**2022E**	**2023E**	**2022E**	**2023E**
Total - all NACE activities	**8.7%**	**7.5%**	**7.6%**	**6.9%**	**8.9%**	**7.6%**
Agriculture, forestry, and fishing	8.0%	0.1%	6.9%	-0.4%	8.2%	0.3%
Industrial sector, except construction	8.9%	7.5%	7.8%	6.9%	10.4%	6.4%
Industrial sector, except construction and manufacturing (mostly energy related)	-0.1%	1.6%	-1.1%	1.1%	0.0%	1.8%
Manufacturing	11.8%	9.1%	10.6%	8.6%	13.6%	7.6%
Construction	5.4%	9.4%	4.3%	8.9%	5.5%	9.6%
Wholesale and retail trade, transport, accommodation, and food service activities	15.1%	7.5%	13.3%	7.5%	18.3%	4.9%
Information and communication	20.9%	10.0%	12.5%	11.0%	21.0%	12.8%
Financial and insurance activities	6.1%	7.5%	5.0%	6.9%	6.3%	7.6%
Real estate activities	10.0%	6.2%	8.9%	5.6%	10.2%	6.4%
Professional, scientific, and technical activities; administrative and support service activities	7.1%	7.5%	6.0%	6.9%	5.9%	9.0%
Public administration, defence, education, human health and social work activities	1.6%	7.5%	4.3%	3.0%	0.2%	9.3%
Arts, entertainment, and recreation; other service activities; activities of household and extra-territorial organisations and bodies	9.8%	7.5%	8.7%	6.9%	10.0%	7.6%

2.2.5 Loss allowance

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) in credit risk or becoming credit-impaired in the period, and the consequent step up (or step down) between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments derecognised in the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular update of model inputs;
- Impacts on the measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period (see subsection 2.2.6).

Allowances based on individual assessments

Allowances based on individual assessments are formed, using discounted cash flow approach. The amount of the loan loss allowance is measured as the difference between the lending exposure's carrying amount and the estimated future cash flows discounted at the effective interest rate. Individual loss allowances are assessed on a conservative basis for exposures of corporate customers classified as non-performing (default, rating 13) customers when the loan payments have not been collected by the due date and/or there is high uncertainty that expected cash flows from the realisation of collateral are not sufficient for covering the carrying amount of the loan principal and interest payments.

Minimum provisioning level for loans that become non-performing

All non-performing exposures originated later than 26 April 2019 should have following minimum provisioning levels (percentage of exposure):

	Years in default									
Type of contract	1	2	3	4	5	6	7	8	9	10
Unsecured exposure	0	0	35	100						
Secured (immovable property collateral)	0	0	0	25	35	55	70	80	85	100
Secured (other collateral)	0	0	0	25	35	55	80	100		
Export credit guarantee/insurance	0	0	0	0	0	0	0	100		

Where the terms and conditions of an exposure which was originated prior to 26 April 2019 are modified in a way that increases the exposure to the obligor, the exposure is considered as having been originated on the date when the modification applies.

In case non-performing exposure is only partly secured, the unsecured part of non-performing exposure is considered as unsecured exposure and the provision level of unsecured exposure should be used for this part of non-performing exposure.

2.2.6 Write-off policy

The Group writes off financial assets, in whole or in part, when it has exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a derecognition event.

Indicators that there is no reasonable expectation of recovery include (i) ceasing enforcement activity and (ii) where the Group's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovery.

If it is not feasible or economically reasonable for the Group to take measures to recover the claims that are being discounted, the claim is assessed as non-performing and is removed from the statement of financial position. If an irrecoverable claim is received subsequently, receipts are recognised as income.

At least one of the conditions has to be filled to declare a claim irredeemable based on the product class.

Credit cards, consumer loan and hire purchase

- There has been no significant contribution in 12 months since the customer's insolvency (default) and the court proceedings relating to arrears have terminated to the Group's detriment or the customer fails to comply with the court decision
- The customer has been declared bankrupt or insolvent

- The court has approved a debt restructuring plan (the claim recognised in the plan is less than the actual claim)
- Criminal proceedings have been initiated in relation to issued credit or fraud has been used to obtain credit
- The customer is dead and bankruptcy is declared after the inventory of the estate
- The customer associated with the claim handed over to the bailiff has a foreign address or none at all.

Leasing, private and business loans

- The customer does not voluntarily reimburse the Group's claim resulting from the difference between the original claim and the realisation of the collateral.

2.2.7 Modifications of financial assets

The Group sometimes modifies the terms of loans provided to customers due to commercial renegotiations, or for distressed loans, with a view to maximising recovery.

Such restructuring activities include extended payment term arrangements, payment holidays and payment forgiveness. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Restructuring is most commonly applied to term loans.

The risk of default of such assets after modification is assessed at the reporting date and compared with the risk under the original terms at initial recognition, when the modification is not substantial and so does not result in derecognition of the original asset. The Group monitors the subsequent performance of modified assets. The Group may determine that credit risk has significantly improved after restructuring, so that the assets are moved from Stage 3 or Stage 2 (lifetime ECL) to Stage 1 (12-month ECL). This is only the case for assets which have performed in accordance with the new terms for six consecutive months or more.

2.3 Credit risk exposure

The following tables contain an analysis of the credit risk exposure of financial instruments. The gross carrying amount of financial assets below also represents the Group's maximum exposure to credit risk on these assets. Information on how the ECL is measured and how the three stages are determined is included in subsection 2.2. 'Expected credit loss measurement'.

2.3.1 Risk concentration

Financial assets and liabilities by geographic region as at 31 Dec 2022

EUR thousand	Note	Estonia	Germany	Other EU	USA	UK	Other	Total
Due from banks and investment companies	7	1,935,474	0	329,496	24,727	189,442	101	**2,479,240**
Financial assets at fair value	8	62	7	308	21	3	6	**407**
Financial assets measured at amortised cost	8	236,130	4,966	123,134	0	0	0	**364,230**
Loans and advances to customers	9	3,162,295	612	17,867	622	900	4,693	**3,186,989**
Receivables from customers	10	9,253	0	0	0	0	0	**9,253**
Other financial assets	11	24	0	0	100	0	0	**124**
Total financial assets		**5,343,238**	**5,585**	**470,805**	**25,470**	**190,345**	**4,800**	**6,040,243**
Amounts owed to central banks (TLTRO)	13	147,841	0	0	0	0	0	**147,841**
Deposits from customers	13	3,656,847	5,292	794,101	14,891	452,415	33,385	**4,956,931**
Loans received and debt securities in issue	13	384,149	0	0	0	0	0	**384,149**
Subordinated debt	16	114,056	0	0	0	0	0	**114,056**
Accounts payable and other financial liabilities	14	54,838	0	0	0	0	0	**54,838**
Financial liabilities at fair value	8	3,850	0	0	0	0	0	**3,850**
Total financial liabilities		**4,361,581**	**5,292**	**794,101**	**14,891**	**452,415**	**33,385**	**5,661,665**

Financial assets and liabilities by geographic region as at 31 Dec 2021

EUR thousand	Note	Estonia	Germany	Other EU	USA	UK	Other	Total
Due from banks and investment companies	7	3,611,388	0	76,010	29,900	269,593	42	**3,986,933**
Financial assets at fair value	8	47,814	6	79,709	30	2	159	**127,720**
Loans and advances to customers	9	2,652,960	781	17,292	903	849	4,375	**2,677,160**
Receivables from customers	10	2,970	0	0	0	0	0	**2,970**
Other financial assets	11	117	0	0	2,119	0	0	**2,236**
Total financial assets		**6,315,249**	**787**	**173,011**	**32,952**	**270,444**	**4,576**	**6,797,019**
Amounts owed to central banks (TLTRO)	13	197,461	0	0	0	0	0	**197,461**
Deposits from customers	13	3,488,788	113,798	1,484,106	62,541	631,356	66,013	**5,846,602**
Loans received and debt securities in issue	13	349,063	0	0	0	0	0	**349,063**
Subordinated debt	16	88,989	0	0	0	0	0	**88,989**
Accounts payable and other financial liabilities	14	41,155	0	0	0	0	0	**41,155**
Financial liabilities at fair value	8	157	0	0	0	0	0	**157**
Total financial liabilities		**4,165,613**	**113,798**	**1,484,106**	**62,541**	**631,356**	**66,013**	**6,523,427**

2.3.2 Distribution of loans granted by industry

Distribution of loans granted by industry (net)

EUR thousand	31 Dec 2022	%	31 Dec 2021	%
Individuals	1,245,358	39.1%	1,009,927	37.7%
Agriculture	79,448	2.5%	68,459	2.6%
Mining and quarrying	1,630	0.1%	2,019	0.1%
Manufacturing	154,069	4.8%	151,638	5.7%
Energy	93,170	2.9%	58,504	2.2%
Water and utilities	29,129	0.9%	23,505	0.9%
Construction	108,401	3.4%	83,011	3.1%
Wholesale and retail	148,560	4.7%	131,630	4.9%
Transport and logistics	24,831	0.8%	28,752	1.1%
Hotels and restaurants	30,742	1.0%	28,680	1.1%
Information and communication	14,301	0.4%	10,878	0.4%
Financial services	127,950	4.0%	85,505	3.2%
Real estate	777,830	24.4%	654,325	24.4%
Professional, scientific, and technical activities	75,174	2.4%	44,669	1.7%
Administrative activities	116,551	3.7%	114,446	4.3%
Public management	79,145	2.5%	97,622	3.6%
Education	5,445	0.2%	4,328	0.2%
Health	11,542	0.4%	13,139	0.5%
Art and entertainment	55,271	1.7%	48,832	1.8%
Other servicing activities	8,442	0.3%	17,291	0.6%
Total (Note 9)	**3,186,989**	**100.0%**	**2,677,160**	**100.0%**

2.3.3 Loan portfolio by ratings

Distribution of legal entity financing by internal ratings

EUR thousand	31 Dec 2022	31 Dec 2021	Grading
3 low credit risk	0	0	Investment grade
4 low credit risk	34,069	49,031	
5 low credit risk	48,410	64,896	
6 low credit risk	365,287	277,748	
7 medium credit risk	433,152	369,284	
8 medium credit risk	591,503	479,112	
9 heightened credit risk	196,840	184,268	
10 high credit risk	39,252	32,516	Non-investment grade
11 high credit risk	55,843	48,780	(incl. special monitoring)
12 non-satisfactory rating	18,912	19,111	
13 insolvent	717	1,619	Default
Total corporates	**1,783,985**	**1,526,365**	
Retail SMEs	157,646	135,361	
Total	**1,941,631**	**1,661,726**	

Unused portions of corporate loans and financial guarantee limits are presented in the following table.

Credit quality of liabilities accounted for off the statement of financial position
(unused loan commitments for corporate loans and financial guarantees)

EUR thousand	31 Dec 2022	31 Dec 2021
3 low credit risk	100,000	100,000
4 low credit risk	35,000	32,091
5 low credit risk	10,078	8,425
6 low credit risk	106,057	80,577
7 medium credit risk	81,891	143,825
8 medium credit risk	143,622	192,424
9 heightened credit risk	109,119	80,244
10 high credit risk	7,742	4,491
11 high credit risk	3,346	6,833
12 non-satisfactory rating	1,718	103
13 insolvent	0	214
Non-rated (retail clients)	85,142	96,387
Total	**683,715**	**745,614**

2.4 Quality of credit portfolio

2.4.1 Distribution of loans by economic sectors and stages

Loans by economic sectors and stages as at 31 Dec 2022 (net)

EUR thousand	Stage 1	Stage 2	Stage 3	Allowance for credit losses	Total
Individuals	1,127,635	115,433	5,446	-3,156	1,245,358
Agriculture	76,817	2,743	0	-112	79,448
Mining and quarrying	1,039	519	122	-50	1,630
Manufacturing	126,670	28,626	81	-1,308	154,069
Energy	92,186	1,305	0	-321	93,170
Water and utilities	29,314	90	0	-275	29,129
Construction	104,812	5,243	58	-1,712	108,401
Wholesale and retail	142,811	6,599	69	-919	148,560
Transport and logistics	15,198	10,323	1	-691	24,831
Hotels and restaurants	8,775	23,446	43	-1,522	30,742
Information and communication	11,330	3,004	1	-34	14,301
Financial services	119,435	9,337	0	-822	127,950
Real estate	744,928	34,577	1,558	-3,233	777,830
Professional, scientific, and technical activities	68,002	7,313	30	-171	75,174
Administrative activities	115,072	4,563	32	-3,116	116,551
Public management	79,272	0	0	-127	79,145
Education	5,151	596	0	-302	5,445
Health	11,077	541	0	-76	11,542
Art and entertainment	27,619	30,225	15	-2,588	55,271
Other servicing activities	6,970	1,503	11	-42	8,442
Total	**2,914,113**	**285,986**	**7,467**	**-20,577**	
Allowance for credit losses	-10,874	-7,632	-2,071		
Total loan portfolio	**2,903,239**	**278,354**	**5,396**		**3,186,989**

Loans by economic sectors and stages as at 31 Dec 2021 (net)

EUR thousand	Stage 1	Stage 2	Stage 3	Allowance for credit losses	Total
Individuals	886,127	114,863	11,328	-2,392	1,009,926
Agriculture	63,843	4,809	21	-214	68,459
Mining and quarrying	923	1,114	0	-18	2,019
Manufacturing	125,985	26,328	255	-930	151,638
Energy	57,403	1,729	0	-627	58,505
Water and utilities	23,172	573	0	-240	23,505
Construction	80,323	3,990	477	-1,778	83,012
Wholesale and retail	126,082	5,186	848	-486	131,630
Transport and logistics	25,730	3,057	101	-136	28,752
Hotels and restaurants	5,526	25,036	159	-2,041	28,680
Information and communication	10,600	294	8	-24	10,878
Financial services	85,481	327	0	-303	85,505
Real estate	569,902	85,688	1,995	-3,260	654,325
Professional, scientific, and technical activities	39,062	5,344	482	-219	44,669
Administrative activities	113,860	3,698	155	-3,268	114,445
Public management	97,307	315	0	0	97,622
Education	4,035	275	31	-14	4,327
Health	9,766	3,441	3	-71	13,139
Art and entertainment	24,155	27,576	64	-2,963	48,832
Other servicing activities	16,463	856	38	-65	17,292
Total	**2,365,745**	**314,499**	**15,965**	**-19,049**	
Allowance for credit losses	-9,472	-7,444	-2,133		
Total loan portfolio	**2,356,273**	**307,055**	**13,832**		**2,677,160**

2.4.2 Distribution of loans by loan types and stages

The following tables explain the changes in the credit loss allowances as well as changes in stages by loan types between the beginning and the end of the reporting period due to factors described in subsection 2.2 of this section.

Loans by loan types and stages (net)

EUR thousand	Stage 1	Stage 2	Stage 3	Purchased or Initiated credit impaired	Allowance for credit losses	Total
Corporate lending	1,687,958	145,015	636	0	-15,435	1,818,174
Private lending	997,972	105,887	4,244	0	-1,014	1,107,089
Leasing	122,833	28,419	1,442	0	-2,008	150,686
Consumer financing	94,818	6,661	1,145	0	-2,107	100,517
Investment financing	10,532	4	0	0	-13	10,523
Total as at 31 Dec 2022	**2,914,113**	**285,986**	**7,467**	**0**	**-20,577**	**3,186,989**
Corporate lending	1,382,162	182,476	2,377	0	-15,288	1,551,727
Private lending	777,868	107,810	9,949	0	-1,062	894,565
Leasing	120,117	18,848	2,162	0	-1,250	139,877
Consumer financing	71,408	5,367	1,353	0	-1,320	76,808
Investment financing	14,189	0	123	0	-129	14,183
Total as at 31 Dec 2021	**2,365,744**	**314,501**	**15,964**	**0**	**-19,049**	**2,677,160**

Stage 1

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	1,382,153	510,402	-335,414	130,817	-9,762	1,678,196
Private lending	777,861	248,818	40,533	-69,240	-283	997,689
Leasing	120,141	55,079	-23,881	-28,506	-374	122,459
Consumer financing	71,419	54,373	-37,439	6,465	-442	94,376
Investment financing	14,189	1,865	10,173	-15,695	-13	10,519
Total	**2,365,763**	**870,537**	**-346,028**	**23,841**	**-10,874**	**2,903,239**

Stage 2

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	182,476	15,355	-28,157	-24,659	-5,371	139,644
Private lending	107,817	21,589	-16,141	-7,378	-577	105,310
Leasing	18,827	4,996	-3,741	8,337	-1,058	27,361
Consumer financing	5,367	3,110	-5,239	3,423	-626	6,035
Investment financing	0	0	-417	421	0	4
Total	**314,487**	**45,050**	**-53,695**	**-19,856**	**-7,632**	**278,354**

Stage 3

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	2,377	0	-1,430	-311	-302	334
Private lending	9,949	159	-2,124	-3,740	-154	4,090
Leasing	2,160	44	-158	-604	-576	866
Consumer financing	1,353	276	-804	320	-1,039	106
Investment financing	123	0	-472	349	0	0
Total	**15,962**	**479**	**-4,988**	**-3,986**	**-2,071**	**5,396**

2.4.3 Transfers between stages

The following table explains the changes in the loan stages between the beginning and the end of the reporting period due to factors described in subsection 2.2 of this section.

Inter-stage transfers in 2022 (gross)

EUR thousand	1 > 2	1 > 3	2 > 1	2 > 3	3 > 1	3 > 2
Corporate lending	48,492	37	67,256	292	0	389
Leasing	17,379	0	5,174	242	0	405
Private lending	34,925	93	53,085	654	0	4,705
Consumer financing	1,984	316	1,555	267	0	387
Investment financing	3	0	0	0	0	1
Total	**102,783**	**446**	**127,070**	**1,455**	**0**	**5,887**

2.4.4 Loans against collateral

In the tables below, collateral information of loans and advances is disclosed based on the collateral type and carrying amount or fair value (if lower) of the collateral held. The under-collateralised amount is presented as unsecured loans.

Loans against collateral as at 31 Dec 2022 (net)

EUR thousand	Corporate lending	Consumer financing	Investment financing	Leasing	Private lending	Total
Listed securities	0	0	9,184	0	0	**9,184**
Unlisted equity securities	23,137	0	0	0	2,031	**25,168**
Mortgages, real estate	1,078,341	0	0	0	1,085,002	**2,163,343**
Guarantee of KredEx and Rural Development Foundation	37,543	0	0	0	2,521	**40,064**
Pledges of rights of claim	117,570	0	0	0	0	**117,570**
Deposits	3,361	0	818	0	2,000	**6,179**
Leased assets	0	0	0	84,054	0	**84,054**
Others	51,821	0	0	0	6159	**57,980**
Unsecured loans	506,401	100,517	521	66,632	9,376	**683,447**
Total	**1,818,174**	**100,517**	**10,523**	**150,686**	**1,107,089**	**3,186,989**

Loans against collateral as at 31 Dec 2021 (net)

EUR thousand	Corporate lending	Consumer financing	Investment financing	Leasing	Private lending	Total
Listed securities	0	0	14,183	0	0	**14,183**
Unlisted equity securities	22,593	0	0	0	2,003	**24,596**
Mortgages, real estate	835,391	0	0	0	871,814	**1,707,205**
Guarantee of KredEx and Rural Development Foundation	42,578	0	0	0	9,812	**52,390**
Pledges of rights of claim	91,211	0	0	0	0	**91,211**
Deposits	3,176	0	0	0	2,000	**5,176**
Leased assets	0	0	0	77,751	0	**77,751**
Others	72,998	0	0	0	1178	**74,176**
Unsecured loans	483,780	76,808	0	62,126	7,758	**630,472**
Total	**1,551,727**	**76,808**	**14,183**	**139,877**	**894,565**	**2,677,160**

Over and under-collateralised loans (net)

	Over-collateralised loans		Under-collateralised loans		Total	
EUR thousand	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral
31 Dec 2022	**1,740,958**	**2,825,209**	**1,446,033**	**762,610**	**3,186,989**	**3,587,819**
Corporate lending	732,786	1,075,592	1,085,388	579,012	1,818,174	1,654,604
Consumer financing	0	0	100,517	0	100,517	0
Investment financing	8,093	29,836	2,430	1,909	10,523	31,745
Leasing	17,684	30,171	133,002	66,370	150,686	96,541
Private lending	982,393	1,689,610	124,696	115,319	1,107,089	1,804,929
31 Dec 2021	**1,272,430**	**2,445,616**	**1,404,730**	**782,907**	**2,677,160**	**3,228,523**
Corporate lending	472,746	880,020	1,078,981	603,640	1,551,727	1,483,660
Consumer financing	0	0	76,808	0	76,808	0
Investment financing	14,183	150,842	0	0	14,183	150,842
Leasing	17,501	31,903	122,376	60,251	139,877	92,154
Private lending	**768,000**	**1,382,851**	**126,565**	**119,016**	**894,565**	**1,501,867**

Over and under-collateralised loans by stages as at 31 Dec 2022 (net)

	Over-collateralised loans		Under-collateralised loans		Total	
EUR thousand	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral
Stage 1	**1,573,313**	**2,572,693**	**1,329,926**	**691,963**	**2,903,239**	**3,264,656**
Corporate lending	665,681	984,695	1,012,514	532,506	1,678,195	1,517,201
Consumer financing	0	0	94,377	0	94,377	0
Investment financing	8,089	29,830	2,430	1909	10,519	31,739
Leasing	13,591	22,756	108,869	53,171	122,460	75,927
Private lending	885,952	1,535,412	111,736	104,377	997,688	1,639,789
Stage 2	**162,483**	**240,281**	**115,871**	**70,607**	**278,354**	**310,888**
Corporate lending	66,772	89,656	72,872	46,506	139,644	136,162
Consumer financing	0	0	6,035	0	6,035	0
Investment financing	3	6	1	0	4	6
Leasing	3,339	6,139	24,022	13,159	27,361	19,298
Private lending	92,369	144,480	12,941	10,942	105,310	155,422
Stage 3	**5,161**	**12,235**	**235**	**41**	**5,396**	**12,276**
Corporate lending	335	1,241	0	0	335	1,241
Consumer financing	0	0	105	0	105	0
Investment financing	0	0	0	0	0	0
Leasing	753	1,276	112	41	865	1,317
Private lending	4,073	9,718	18	0	4,091	9,718

2.4.5 ECL sensitivity analysis

The following tables show the impact of changing the PD (retail) or rating (corporate) thresholds for SICR on the ECL allowance as at 31 December 2022 and 31 December 2021. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognised.

Loan portfolio as at 31 Dec 2022

EUR thousand	Effect on impairment
+10% change in SICR (retail)	-50
-10% change in SICR (retail)	73
SICR with 0.5% threshold (retail)	1
SICR with 1.5% threshold (retail)	-3
+1 rating in SICR threshold (corporate)	-116
-1 rating in SICR threshold (corporate)	1,680

Loan portfolio as at 31 Dec 2021

EUR thousand	Effect on impairment
+10% change in SICR	-158
-10% change in SICR	482
SICR with 0.5% threshold	1
SICR with 1.5% threshold	-1

As evidenced by the tables, changing SICR by +/- 10% or changing the 100bps threshold to 50bps or 150bps have limited impact on the overall ECL of the Group. When changed by 1 rating, SICR threshold used for corporate segment would have larger impact.

However, the most significant assumptions affecting the ECL allowance are as follows:

Retail portfolio

- Unemployment rate
- Wage growth
- Euribor
- Bank lending margins
- GDP

Corporate portfolio

- Estimated portfolio PiT PD values for each scenario

The purpose of the sensitivity tests is to show the effect of changing the weights of positive and negative scenarios. Thus, in the sensitivity tests, the weight of the baseline scenario is retained, and two tests have been carried out, where the weights of the positive and negative scenarios have been changed by +/- 5%, respectively.

The table below illustrates the impact of changing scenario weights of positive and negative scenarios to the portfolio as it was on 31 December 2022 and 31 December 2021.

31 Dec 2022

EUR thousand	**60-10-30** (base/up/down)	**60-20-20** (base/up/down)
Change in scenario weights	896	-896

31 Dec 2021

EUR thousand	**65-5-30** (base/up/down)	**65-15-20** (base/up/down)
Change in scenario weights	671	-724

Set out below are the changes to the ECL as at 31 December 2022 and 31 December 2021 that would result from reasonably possible changes in these parameters compared with the actual values used in the Group's economic variable assumptions (for example, the impact on ECL of increasing the estimated unemployment rate by X% in each of the base, upside, downside scenarios):

Impact on ECL, 31 Dec 2022

EUR thousand	Impact of increase	Impact of decrease
Unemployment rate +/-1%	135	-156
Wage growth +/- 1%	-36	22
Euribor +/-0.5%	9	-20
Bank lending margins +/-0.5%	168	-256
Consumer price growth +/-1%	-25	24
House price index +/- 5%	-12	8
Gross value added by sectors, YoY growth rates +/- 5%	-177	228

Impact on ECL, 31 Dec 2021

EUR thousand	Impact of increase	Impact of decrease
Unemployment rate +/-1%	115	-84
Wage growth +/- 5%	-112	111
Euribor +/-0.5%	26	-15
Bank lending margins +/-0.5%	165	-136
Consumer price growth +/-1%	-12	32
House price index +/- 2%	-5	3
Gross value added by sectors, YoY growth rates +/- 5%	-109	139

The Group has performed scenarios where both PD and LGD estimates where modified. Within ECL, the downside scenario specific adjustment for recoveries was larger in 2022 compared to 2021. The impact of these stress tests on impairment is aggregated in the table below. The table includes loans, which are assessed for impairment collectively and which have material balances and potential impact.

2022

EUR thousand	Impact on credit loss allowances
LGD negative 0.80	803
LGD negative 0.90	-608
Average PiT PD -0.5%	-3,527
Average PiT PD +0.5%	3,369

2021

EUR thousand	Impact on credit loss allowances
LGD negative 0.85	603
LGD negative 0.95	-686
Average PiT PD -0.5%	-3,042
Average PiT PD +0.5%	3,321

3. Market risk

Market risk is the risk of losses caused by adverse movements in market prices, including the market prices of foreign currencies, interest rates, and securities. Market risk arises from items accounted for on and off the statement of financial position and can arise from both banking and trading book positions. The purpose of market risk management in the Bank is to correctly identify and quantify market risk and ensure that risk-conscious decisions are taken on market risk.

Among others, market risk must be managed as originating from the following sources:

- Foreign exchange risk from the Bank's net open positions in foreign currencies;
- Price risk from the Bank's positions in securities and derivatives, including those taken for the purposes of investment, risk management and brokerage;
- Interest rate risk from interest rate sensitive instruments in the banking book.

The Bank's market risk management is governed by the market risk management policy of LHV Group, the market risk management rules of LHV Pank and other internal rules, which set out the Bank's risk appetite for foreign currency risk, price risk and interest rate risk in the banking book. Based on the market risk management policy, the Group's appetite for market risk is low.

The Treasury Department of LHV Pank, the Assets and Liabilities Management Committee (ALCO) formed in the Bank have key roles in managing market risk as the first line of defence. The Risk Control Department and the Internal Audit Department are responsible for the second line of defence and the third line of defence functions, respectively.

3.1 Foreign currency risk

Foreign currency risk arises from the mismatch of the Bank's foreign currency assets and liabilities. Most items in the Bank's statement of financial position are denominated in euros but a mismatch could result from the foreign currency transactions of the Bank's customers.

Foreign currency risk is measured by estimating the potential loss to the Bank from its net open foreign currency position in a stress scenario. The loss from foreign currency risk should not exceed a prescribed level of the Bank's net own funds.

In addition to the risk appetite levels approved at the LHV Group level, the Bank's ALCO has implemented additional risk limits for various types of market risks in the Bank. Foreign currency risk limits in the Bank are fixed as maximum nominal net open position limits in euro equivalent for each currency. If the open currency position exceeds the limits set by the ALCO, measures must be implemented to close or reduce such positions.

A sensitivity analysis has been performed to show the effect of movements in foreign exchange rates on the statement of profit or loss, with the assumption of other conditions remaining constant. The sensitivity has been measured against a potential exchange rate movement of +/- 7% which is in line with the stress scenario used by the Group for measuring foreign currency risk of its net open positions. The Bank's foreign currency risk exposure is very low.

Impact on statement of profit or loss

EUR thousand	2022	2021
USD exchange rate +/- 7%	+/- 375	+/- 204
SEK exchange rate +/- 7%	+/-2	+/-6
GBP exchange rate +/- 7%	+/-68	+/-17
CHF exchange rate +/- 7%	+/-4	+/-0

Open currency exposures

The following tables present the risks arising from open currency exposures. Assets and liabilities denominated in foreign currencies have been presented in euro equivalent in respective columns, according to the exchange rate prevailing at the end of the reporting period. Derivatives reported at fair value in the statement of financial position have been included at contractual amounts under assets and liabilities accounted for off the statement of financial position. Open currency exposure and the volume of financial assets and liabilities of the Bank at the end of the reporting period do not significantly differ from the average exposure during the year. Foreign exchange forwards are shown in the table at their full contractual cash flow amounts as assets and liabilities accounted for off the statement of financial position. The table does not include the assets (tangible and intangible assets) and liabilities (provisions) not bearing currency risk, or equity.

It can be seen based on the table that as mentioned above, the majority of the Bank's business is conducted in euro currency.

Currency risk exposures as at 31 Dec 2022

EUR thousand	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Financial assets bearing currency risk								
Due from banks and investment companies	7	2,252 513	1,466	197,147	2,538	17,806	7,769	**2,479,240**
Investments in debt and equity securities	8	364,567	0	2	1	26	42	**364,637**
Loans and advances to customers	9	**3,180,990**	**74**	**232**	**385**	**5,068**	**241**	**3,186,989**
Receivables from customers	10	14,099	5	751	241	-4,512	-1,330	**9,253**
Other financial assets	11	124	0	0	0	0	0	**124**
Total financial assets bearing currency risk		**5,812,293**	**1,545**	**198,132**	**3,164**	**18,388**	**6,721**	**6,040,243**
Financial liabilities bearing currency risk								
Amounts owed to central banks (TLTRO)	13	147,841	0	0	0	0	0	**147,841**
Deposits from customers	13	4,590,049	5,323	193,442	10,968	148,058	9,089	**4,956,931**
Loans received and debt securities in issue	13	384,149	0	0	0	0	0	**384,149**
Financial liabilities at fair value	8	0	0	0	0	3,849	1	**3,850**
Accounts payable and other financial liabilities	14	41,563	19	4,006	172	8,987	91	**54,838**
Subordinated debt	16	114,056	0	0	0	0	0	**114,056**
Total financial liabilities bearing currency risk		**5,277,658**	**5,343**	**197,448**	**11,140**	**160,895**	**9,181**	**5,661,665**
Open gross position derivative assets at contractual value		9,403	3,757	0	8,001	148,162	2,371	**171,694**
Open gross position derivative liabilities at contractual value		162,291	0	0	0	0	0	**171,694**
Open foreign currency position		**381,747**	**-40**	**684**	**25**	**-3,748**	**-89**	378,578

Currency risk exposures as at 31 Dec 2021

EUR thousand	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Financial assets bearing currency risk								
Due from banks and investment companies	7	3,686,878	1,367	277,043	1,075	18,433	2,137	**3,986,933**
Investments in debt and equity securities	8	127,677	0	1	0	37	4	**127,720**
Loans and advances to customers	9	2,669,321	18	463	396	6,616	346	**2,677,160**
Receivables from customers	10	1,036	0	491	226	167	1,050	**2,970**
Other financial assets	11	117	0	0	0	2,119	0	**2,236**
Total financial assets bearing currency risk		**6,485,029**	**1,385**	**277,998**	**1,697**	**27,372**	**3,538**	**6,797,019**
Financial liabilities bearing currency risk								
Amounts owed to central banks (TLTRO)	13	197,461	0	0	0	0	0	**197,461**
Deposits from customers	13	5,448,088	5,037	271,784	7,837	101,149	12,708	**5,846,602**
Loans received and debt securities in issue	13	349,063	0	0	0	0	0	**349,063**
Financial liabilities at fair value	8	0	0	0	16	123	18	**157**
Accounts payable and other financial liabilities	14	28,269	218	6,456	217	5,676	319	**41,155**
Subordinated debt	16	88,989	0	0	0	0	0	**88,989**
Total financial liabilities bearing currency risk		**6,111,870**	**5,254**	**278,240**	**8,070**	**106,948**	**13,045**	**6,523,427**
Open gross position derivative assets at contractual value		0	3,872	0	6,454	82,496	9,026	**101,848**
Open gross position derivative liabilities at contractual value		101,848	0	0	0	0	0	**101,848**
Open foreign currency position		**271,311**	**3**	**-242**	**81**	**2,920**	**-481**	273,592

3.2 Price risk

Price risk arises from securities held by the Bank in the liquidity portfolio, trading portfolio and investment portfolios (Note 8, 9).

Price risk is measured by estimating the potential loss that can be incurred by the Bank in a stress scenario. The loss from price risk in the stress scenario should not exceed a prescribed percentage of the Bank's net own funds. The ALCO has set additional limits on the size of the trading and investment portfolios. There are criteria in place for acceptable credit ratings as well as other parameters of the debt securities that can be held by the Bank.

A sensitivity analysis has been performed to show the effect of movements in securities prices on the net result of the Bank. The potential securities price movements used in the sensitivity analysis are in line with the stress scenarios used by the Bank for measuring price risk and have been derived from actual historical volatility of the instruments included in the relevant portfolios. In case of the Bank's liquidity portfolio, two different stress scenarios are assumed: 0.5% price movement for securities with a maturity of up to 1 year, and 2% for securities with a maturity of over one year.

Impact on statement of profit or loss (profit after tax)

EUR thousand	2022	2021
Equity securities and fund units +/-25%	+/-92	+/-92
Debt securities +/-0.5% and +/-2.0%	+/-0	+/-2,547

It can be seen that the majority of the Bank's price risk results from the debt securities held in the Bank's liquidity portfolio. However, most of these securities are valued at amortised cost, so the materialisation of the price risk would not result in an immediate impact on the statement of profit or loss. The Bank does not hold significant amounts of equity securities (see Note 8), accordingly the sensitivity to change in the market price of these positions is marginal.

3.3 Interest rate risk

Interest rate risk arises from the mismatch of the term structure of interest rate sensitive assets and liabilities (gap risk), mismatch of base rates (basis risk), the optionality inherent in the interest rate sensitive instruments (option risk) and the change in credit spreads (credit spread risk). Interest rate risk can arise both from items accounted for on and off the statement of financial position.

Interest rate risk in the banking book is measured by estimating the change of net interest income (NII) and the economic value of equity (EVE) in a number of stress scenarios compared to the base scenario. The Group's risk appetite prescribes that the negative impact on NII or EVE in stress scenarios should not exceed a certain level of the Bank's net own funds.

The Bank's ALCO has approved the stress scenarios and other inputs and methodologies for calculating the change in NII and EVE. Market-implied interest rate curve is used as the base scenario. Six stress scenarios are used:

- parallel shock up;
- parallel shock down;
- steepener shock (short rates down and long rates up);
- flattener shock (short rates up and long rates down);
- short rates shock up; and
- short rates shock down.

Interest rate floors are applied for deeply negative rates where applicable based on regulatory guidance.

The analysis of the change in the economic value of equity (change in EVE) aims to assess the change in the economic value of the assets, liabilities, and equity in different interest rate scenarios. The measure of interest rate risk is the change in EVE in interest rate shock scenario compared to the base scenario. In order to calculate the change in EVE, the net present value of the cash flows arising from the banking book assets, liabilities and items accounted for off the statement of financial position is found under each scenario. The cash flows are calculated on a run-off balance sheet basis by applying the assumptions detailed below. All cash flows from the assets, liabilities and items accounted for off the statement of financial position are discounted using the same interest rate curve (swap curve depending on the scenario).

The analysis of the change in net interest income (change in NII) assesses the impact of interest rate changes on net interest income in the next 12-month period. In order to calculate the change in NII, all interest-bearing assets, liabilities and items accounted for off the statement of financial position are split into different time buckets according to their repricing date. Following repricing dates, interest-sensitive assets and liabilities are assumed to reprice at new interest rates specific to the scenario and change in NII in different scenarios can be determined. The NII analysis is performed on a constant statement of financial position.

The main assumptions for the calculation of the change in EVE and change in NII are as follows:

- The repricing terms of demand deposits of households and non-financial corporations vary between 1 day and 5 years, depending on their interest rate sensitivity.
- For deposits of financial institutions, immediate repricing is assumed.
- A 0% interest rate floor is applied to deposits of retail customers.
- For term deposits, contractual maturities are used.
- For loans, contract-specific interest rate floors are used.
- Conditional prepayment rate is used in the assessment of the early repayment of loans.

In the case of items accounted for off the statement of financial position (e.g., loan commitments and credit limits), the credit conversion factor is included in the model, and it is assumed that the use of the limit will increase on a straight-line basis until the expiry date.

The following table presents the changes in EVE and next 12 months' NII that have been estimated in the six stress scenarios compared to the base scenario. There was a significant change in the interest environment in reporting period which has an impact on the results of the following stress tests.

Stress tests scenarios impacts, valid at 31 Dec 2022

EUR thousand	Change in the economic value of equity	Change in the next 12 months' net interest income
Parallel shock up	19,955	22,911
Parallel shock down	-20,787	-22,901
Steepener shock	775	-7,477
Flattener shock	2,552	11,448
Short rates shock up	8,038	17,619
Short rates shock down	-8,778	-17,609

Stress tests scenarios impacts, valid at 31 Dec 2021

EUR thousand	Change in the economic value of equity	Change in the next 12 months' net interest income
Parallel shock up	85,367	33,935
Parallel shock down	23,806	-1,522
Steepener shock	-14,461	-1,519
Flattener shock	57,061	17,489
Short rates shock up	66,572	28,568
Short rates shock down	4,338	-1,523

The table below shows the structure of the interest-bearing assets and interest-bearing liabilities of the Bank grouped by the recalculation dates of interest rates at the principal amounts of receivables and liabilities.

Interest rate sensitivity gap as at 31 Dec 2022

EUR thousand	Note	Up to 3 months	3-12 months	1-5 years	Over 5 years	Subtotal	Accrued interest	Impair-ments	Total
Financial assets									
Due from banks and investment companies	7	2,479,240	0	0	0	2,479,240	0	0	2,479,240
Financial assets at fair value (debt securities)	8	0	17		390	407	0	0	407
Financial assets measured at amortised cost (debt securities)	8	236,130	4,965	122,671	0	363,766	555	-91	364,230
Loans and advances to customers	9	1,454,057	1,622,589	90,799	31,931	3,199,376	8,190	-20,577	3,186,989
Total		**4,169,427**	**1,627,571**	**213,470**	**32,321**	**6,042,789**	**8,745**	**-20,668**	**6,030,866**
Financial liabilities									
Amounts owed to central banks (TLTRO)	13	0	0	150,000	0	150,000	-2,159	0	147,841
Deposits from customers	13	3,829,982	306,833	819,419	0	4,956,234	697		4,956,931
Loans received and debt securities in issue	13	0	0	384,000	0	384,000	149	0	384,149
Subordinated debt16		0	0	10,000	103,500	113,500	556	0	114,056
Total		**3,829,982**	**306,833**	**1,363,419**	**103,500**	**5,603,734**	**-757**	**0**	**5,602,977**
Net interest sensitivity gap		**339,445**	**1,320,738**	**-1,149,949**	**-71,179**	**439,055**			

Interest rate sensitivity gap as at 31 Dec 2021

EUR thousand	Note	Up to 3 months	3-12 months	1-5 years	Over 5 years	Subtotal	Accrued interest	Impair-ments	Total
Financial assets									
Due from banks and investment companies	7	3,986,933	0	0	0	3,986,933	0	0	3,986,933
Financial assets at fair value (debt securities)	8	46,000	3,350	77,218	0	126,568	781	0	127,349
Loans and advances to customers	9	1,214,410	1,375,207	85,595	15,869	2,691,081	5,128	-19,049	2,677,160
Total		**5,247,343**	**1,378,557**	**162,813**	**15,869**	**6,804,582**	**5,909**	**-19,049**	**6,791,442**
Financial liabilities									
Amounts owed to central banks (TLTRO)	13	0	0	200,000	0	200,000	-2,539	0	197,461
Deposits from customers	13	2,288,647	101,744	3,457,466	0	5,847,857	-1,255	0	5,846,602
Loans received and debt securities in issue	13	0	0	350,000	0	350,000	-937	0	349,063
Subordinated debt16		0	0	0	88,500	88,500	489	0	88,989
Total		**2,288,647**	**101,744**	**4,007,466**	**88,500**	**6,486,357**	**-4,242**	**0**	**6,482,115**
Net interest sensitivity gap		**2,958,696**	**1,276,813**	**-3,844,653**	**-72,631**	**318,225**			

3.4 Credit valuation adjustment risk

Credit valuation adjustment (CVA) risk can be defined as the risk of losses arising from changing CVA values in response to movements in counterparty credit spreads and market risk factors that drive prices of derivative transactions. The Bank applies the standardised approach to calculate the capital charge for CVA risk. The Bank's capital requirement for CVA risk as of 31 Dec 2022 amounted to EUR 178 thousand (2021: EUR 97 thousand).

4. Liquidity risk

Liquidity risk is the risk that the Group is unable to fund increases in the Group's assets as envisaged in its business plan or pay its liabilities as they fall due, without incurring material losses or disrupting its normal business operations. Liquidity risk arises from items accounted for both on and off the statement of financial position. The purpose of the Group's liquidity risk management is to correctly identify, measure, control and monitor liquidity risk, and to ensure timely decisions can be taken so that sufficient liquidity with adequate margin can be always maintained.

According to the risk management policy of LHV Group, the Bank assesses liquidity risk from the following separate perspectives:

- Funding risk is the risk that the Bank is unable to attract funding in a timely way, in necessary amount and at acceptable cost without a negative impact to its daily activities or financial position. Funding risk also encompasses the risk related to liquidity outflows from withdrawal of deposits or redemption of wholesale funding. Intraday liquidity risk is also evaluated in this perspective.
- Market liquidity risk is the risk that it is not possible to execute a transaction such as selling of a security or pledging of an asset in a timely manner without incurring unacceptable losses, due to low trading activity, market disruption or limitations set by other market participants.
- Asset encumbrance risk is the risk that due to an excessive share of assets being encumbered as collateral the Group harms its ability to attract further unsecured or secured funding, due to unsecured creditors becoming effectively subordinated or due to the shortage of assets available to be pledged as collateral.

Liquidity risk is highly relevant for LHV Pank as the largest share of the Bank's funding is raised through collecting deposits that are used for funding long term loans which generally have a longer term than the deposits.

The Bank manages its liquidity risk in accordance with the LHV Group's liquidity risk management policy, group funding policy, liquidity risk management rules and other internal rules, which set out the LHV Group's and the Bank's funding strategy and liquidity risk appetite, early warning indicators and various internal procedures such as reporting routines and contingency plans. The Treasury Unit and the Assets and Liabilities Management Committee (ALCO) have key roles in managing liquidity risk as the first line of defence. Risk Control Unit and the Internal Audit Unit are responsible for the second line of defence and third line of defence functions, respectively.

The key quantitative metrics which are used for limiting the Bank's liquidity risk appetite include:

- Liquidity Coverage Ratio (LCR),
- Net Stable Funding Ratio (NSFR),
- Asset encumbrance ratio.

Limits have been set for each of the above risk appetite metrics with buffers over regulatory requirements (if applicable). First two are defined as regulatory requirements and third is internal. These metrics are calculated and reported on a monthly basis.

In addition to the regulatory and risk appetite metrics, additional liquidity risk indicators such as survival period in stress scenarios are calculated, limited and monitored.

The regulatory LCR and the internally defined minimum survival period in stress scenarios both assess the risk of liquidity outflows in a relatively short-term time horizon. To survive the stress scenario and the expected deposit outflows, the Bank keeps a counterbalancing buffer of liquid high-quality assets that can be used in either a market-wide or idiosyncratic stress scenario. The liquidity buffer of the Bank consists of cash and deposits with the central bank and liquid securities, which can be readily sold or used as collateral in funding operations. For calculating the survival horizon, behavioural assumptions are used for modelling liquidity outflows and inflows.

NSFR is used for assessing longer-term structural funding risk. The Bank should have an appropriate funding structure where long-term assets are matched with sufficient stable and well-diversified funding sources. Encumbrance ratio is observed to ensure that the Bank is not exposed to excessive asset encumbrance that could limit its access to funding markets.

The following table presents the values of the LCR and NSFR ratios in comparison to regulatory thresholds. It can be seen that both ratios exceeded regulatory requirements with a healthy buffer characterising the Group's conservative approach to managing liquidity risk.

Ratio	Regulatory requirement	Actual 31 Dec 2022	Actual 31 Dec 2021
LCR	Minimum 100%	135.6%	140.6%
NSFR	Minimum 100%	144.5%	164.2%

As set out in the LHV Group's funding policy, diversification of the funding profile is an important element of the Bank's liquidity risk management framework. The Banks's most stable funding source is retail deposits from its Estonian customers. Other deposits and wholesale unsecured and secured funding are used as additional sources of funding. The Bank has issued covered bonds to raise targeted funding for its residential mortgage loans portfolio. The LHV Group has also issued unsecured bonds which are used for both funding and for complying with the regulatory MREL requirement. The Bank has also used the TLTRO facility offered by the European Central Bank.

To manage longer-term funding risk, Treasury Department drafts funding plans as part of the LHV Group's financial planning cycle. The funding plan presents a longer-term view of the funding required to support the LHV Group's business along with key liquidity metrics for the LHV Group.

The following tables present the distribution of financial assets and liabilities, excl. derivatives, by due dates and by future contractual undiscounted cash flows. The carrying amounts are disclosed in a separate column. In the maturity analysis, the cash flows are split into the maturity buckets in which the cash flows occur (including interest cash flows).

Financial assets and liabilities by maturities 31 Dec 2022

EUR thousand	Note	On demand	Up to 3 months	3-12 Months	1-5 Years	Over 5 years	Total	Carrying amount
Liabilities by contractual maturity dates								
Amounts owed to central banks (TLTRO)	13	0	0	0	150,082	0	**150,082**	**147,841**
Deposits from customers	13	4,699,726	95,807	143,740	18,082	0	**4,957,355**	**4,956,931**
Loans received and debt securities in issue	13	0	0	6,790	396,890	0	**403,680**	**384,149**
Subordinated debt	16	0	2,311	16,932	118,843	0	**138,086**	**114,056**
Accounts payable and other financial liabilities	14	0	54,838	0	0	0	**54,838**	**54,838**
Unused loan commitments	19	0	601,093	0	0	0	**601,093**	**0**
Financial guarantees by contractual amounts	19	0	52,577	0	0	0	**52,577**	**0**
Foreign exchange derivatives (gross settled)		0	171,694	0	0	0	**171,694**	**0**
Financial liabilities at fair value	8	0	3,850	0	0	0	**3,850**	**3,850**
Total liabilities		**4,699,726**	**982,170**	**167,462**	**683,897**	**0**	**6,533,255**	**5,661,665**
Assets held for managing liquidity risk by contractual maturity dates								
Due from banks and investment companies	7	2,479,240	0	0	0	0	**2,479,240**	**2,479,240**
Financial assets at amortised cost (debt securities)	8	0	236,130	4,966	123,225		**364,321**	**364,637**
Loans and advances to customers	9	0	186,547	487,298	2,095,373	1,258,430	**4,027,648**	**3,186,989**
Receivables from customers	10	0	9,253	0	0	0	**9,253**	**9,253**
Other financial assets	11	124	0	0	0	0	**124**	**124**
Foreign exchange derivatives (gross settled)		0	171,694	0	0	0	**171,694**	**0**
Total assets held for managing liquidity risk		**2,479,364**	**603,624**	**492,264**	**2,218,598**	**1,258,430**	**7,052,280**	**6,040,243**
Maturity gap from assets and liabilities		**-2,220,362**	**-378,546**	**324,802**	**1,534,701**	**1,258,430**	**519,025**	

Financial assets and liabilities by maturities 31 Dec 2021

EUR thousand	Note	On demand	Up to 3 months	3-12 Months	1-5 Years	Over 5 years	Total	Carrying amount
Liabilities by contractual maturity dates								
Amounts owed to central banks (TLTRO)	13	0	0	0	197,000	0	**197,000**	**197,461**
Deposits from customers	13	5,687,287	55,271	101,784	2,288	0	**5,846,630**	**5,846,602**
Loans received and debt securities in issue	13	0	0	1,140	352,538	0	**353,678**	**349,063**
Subordinated debt	16	0	1,748	10,208	95,810	0	**107,766**	**88,989**
Accounts payable and other financial liabilities	14	0	41,155	0	0	0	**41,155**	**41,155**
Unused loan commitments	19	0	679,579	0	0	0	**679,579**	**0**
Financial guarantees by contractual amounts	19	0	49,409	0	0	0	**49,409**	**0**
Foreign exchange derivatives (gross settled)		0	101,848	0	0	0	**101,848**	**0**
Financial liabilities at fair value	8	0	157	0	0	0	**157**	**157**
Total liabilities		**5,687,287**	**929,167**	**113,132**	**647,636**	**0**	**7,377,222**	**6,523,427**
Assets held for managing liquidity risk by contractual maturity dates								
Due from banks and investment companies	7	3,986,933	0	0	0	0	**3,986,933**	**3,986,933**
Financial assets at fair value (debt securities)	8	0	46,047	3,387	77,915	0	**127,349**	**127,720**
Loans and advances to customers	9	0	173,534	431,582	1,661,341	924,419	**3,190,876**	**2,677,160**
Receivables from customers	10	0	2,970	0	0	0	**2,970**	**2,970**
Other financial assets	11	2,236	0	0	0	0	**2,236**	**2,236**
Foreign exchange derivatives (gross settled)		0	101,848	0	0	0	**101,848**	**0**
Total assets held for managing liquidity risk		**3,989,169**	**324,399**	**434,969**	**1,739,256**	**924,419**	**7,412,212**	**6,797,019**
Maturity gap from assets and liabilities		**-1,698,118**	**-604,768**	**321,837**	**1,091,620**	**924,419**	**34,990**	

The following table presents the distribution of assets and liabilities by classification of current and non-current.

Assets and liabilities by classification of current and non-current

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Current assets			
Due from central bank	7	2,390,964	3,874,284
Due from credit institutions	7	84,885	106,461
Due from investment companies	7	3,391	6,188
Financial assets at fair value through profit or loss	8	407	127,720
Financial assets measured at amortised cost	8	241,005	0
Loans and advances to customers	9	508,795	455,929
Receivables from customers	10	9,253	2,970
Other assets	11	2,866	2,446
Total current assets		**3,241,566**	**4,575,998**
Non-current assets			
Financial assets measured at amortised cost	8	123,225	0
Loans and advances to customers	9	2,678,194	2,221,231
Other financial assets	11	124	2,236
Tangible assets	12	10,960	8,139
Intangible assets	12	2,881	1,243
Total non-current assets		**2,815,384**	**2,232,849**
Total assets	**5**	**6,056,950**	**6,808,847**
Liabilities			
Current liabilities			
Deposits from customers	13	4,939,370	5,844,321
Amounts owed to central banks (TLTRO)	13	147,841	0
Financial liabilities at fair value through profit or loss	8	3,850	157
Accounts payable and other liabilities	14	62,457	47,105
Subordinated debt	16	10,000	0
Total current liabilities		**5,153,518**	**5,891,583**
Non-current liabilities			
Amounts owed to central banks (TLTRO)	13	0	197,461
Deposits from customers	13	17,561	2,281
Loans received and debt securities in issue	13	384,149	349,063
Subordinated debt	16	103,500	88,500
Total non-current liabilities		**502,210**	**637,305**
Total liabilities	**5**	**5,668,728**	**6,528,888**

5. Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, and systems or from external events. Operational risk includes legal risk, ICT risk and reputational risk, but excludes strategic risk. Operational risk is inherent in all products, activities, processes, and systems.

Each manager in LHV is responsible for managing operational risk within their responsibility area. Risk Division is acting as the second line of defence and providing both proper trainings and guidance to implement the operational risk framework, as well as oversight to ensure that the risk profile is within the desired level as described in risk appetite statements.

The operational risk framework is described in the operational risk policy, the operational resilience policy and in other relevant operational risk management documents. The main processes and tools to manage, i.e., to identify, assess, mitigate, and monitor operational risks are as follows.

Risk and control self-assessment

There is a unified process and method across LHV to assess operational risks of all products and processes. The regularity of self-assessment depends on the criticality level of the product and the process and must ensure that all managers are aware of the risks they are responsible for and apply relevant mitigating and monitoring measures to keep the risk profile within the desired risk level.

Change management and approval process in case of new or significantly changed products, IT systems, processes, organisation, partners (incl. outsourcing), or in case of exceptional transactions

Change management and approval process is designed to ensure all significant changes in products, IT systems, processes, organisation, partners (incl. outsourcing) or significant exceptional transactions are managed with due care and no change is approved before all risk considerations have been taken into account. To achieve this, pre-described risk management rules are implemented, accompanied by independent opinions from the Risk and Compliance Divisions.

Operational risk event and business continuity management

The objective of the operational risk event management is to ensure all events are managed in a proper manner, as well as to learn from the events and use the lessons to prevent similar cases from happening in the future.

Event management activities depend on the event type and severity level. For critical processes business continuity plans are in place and will be activated in case there is a disruption in a critical process. Critical IT systems have recovery plans in place for the same reasons. If needed, crisis management will be applied, steered by the Crisis Committee.

Business continuity plans are regularly reviewed and tested to ensure they are up-to-date and applicable in the event of critical process disruptions.

All events must be reported centrally and registered in a central database for further analysis conducted by the Risk Division. The event data is also used for capital calculation purposes within the ICAAP.

Key risk indicators

Key risk indicators (KRI) are the main tools to monitor if risks are at desired level and controls are working effectively. KRIs are used to monitor risks at different levels, i.e., across LHV as well as at the level of specific units. Action plans will be implemented if KRIs indicate undesired changes in risk level or deficiencies in existing controls.

Capital calculation

The operational risk capital charge is calculated based on the basic indicator approach and amounts to EUR 13,877 thousand as at 31 December 2022 (31 December 2021 EUR 9,024 thousand).

ICT and information security risk management

One of our main goals is to be a trustworthy banking partner to our customers with the focus on providing customer-friendly, secure and resilient digital banking services. Secure and resilient IT systems are key to this objective.

In addition to the general operational risk framework, dedicated ICT and information security risk management tools and methods are applied to protect the information and customers' assets and ensure the IT systems are available. For example:

- reasonable conservatism is being applied when implementing new configurations to products and services
- regular security monitoring
- vulnerability management process
- security controls in the software development lifecycle
- training of our personnel to increase awareness and prevent actions that may cause security incidents on IT systems and services
- up-to-date information about developments in the security scene to understand potential weaknesses.

We take seriously and react to all malicious attacks targeted at our own infrastructure, the customer data in our possession, and our customers.

6. Compliance risk

The number of regulatory requirements and their constant changes make compliance risk a significant operational risk, the realisation of which can lead to both financial and reputational damage.

The task of compliance function is to manage the compliance risk through various activities. The compliance covers the entire activity of LHV and is not limited to specific areas. However, LHV has separated the AML compliance function from the general compliance function.

In addition to the tasks set out in the regulatory requirements, compliance function is involved in maintaining and developing the culture of the organisation to promote a culture that supports compliance.

In order to perform its tasks efficiently, the compliance function, among other things, constantly assesses the need for resources and makes proposals for enhancing and developing the function, where appropriate.

In the coming period, the transition to the direct supervision of the ECB and the registration of the holding company of the LHV Group as a financial holding company will undoubtedly have a significant impact on compliance risk management and the compliance function.

7. Anti-money laundering (AML)

7.1. AML/CTF governance

The internal governance of LHV is based on the three lines of defence model. Since January 2022, the Bank`s AML internal governance has been organised fully to reflect clear demarcation lines between the first and the second line of defence. The AML Department was reorganised into the AML Compliance Department which is reporting to CRO (until 1 December 2022 to CEO). The KYC (know your customer) and EDD (enhanced due diligence) functions, as well as initial investigation on screening and monitoring are now located within business units' relevant organisational units.

AML Compliance is the second line of defence which is established to ensure the first line of defence (i.e., operational, including operational risk, management) is properly designed, in place, and operating as intended. As management functions, they provide framework and guidance for developing and modifying risk management governance, methodologies and applying ongoing compliance controls.

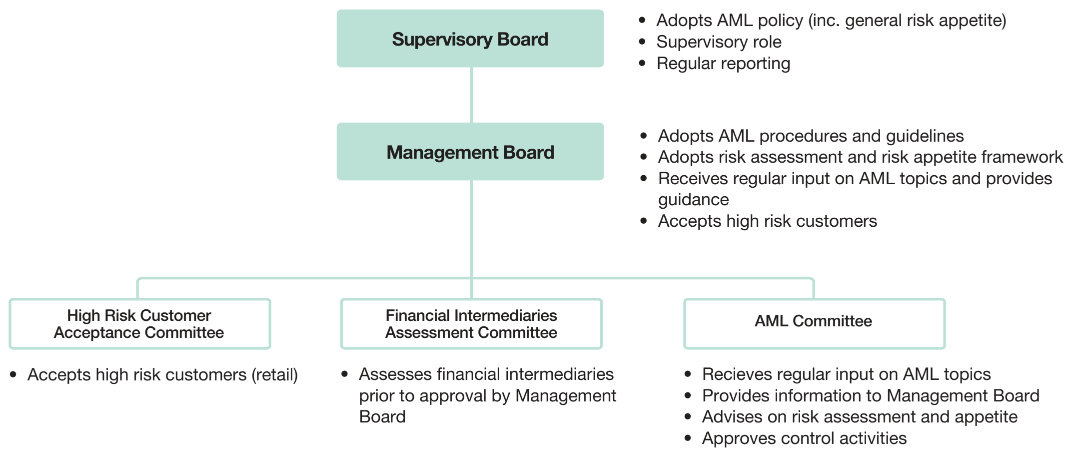
All lines of defence follow a risk-based approach in assessing products, services, customers, and countries. Proper risk mitigating measures, including customer due diligence (CDD) and EDD), are applied on the basis of risk-based screening and monitoring activities and defined risk levels. A high level of awareness and commitment towards risk management and AML issues is the foundation of a strong AML culture which is further supported by continuous activities of awareness raising, information and dissemination, networking and exchange of best practices, training, and reporting.

The Management Board and the Supervisory Board of LHV Group and LHV Pank have a strong commitment towards implementing, maintaining and developing AML/KYC regime across all the group entities. The policies and procedures for AML and CTF (counter-terrorism financing) are updated yearly.

During 2022 the AML screening and monitoring software developed and supported by OÜ Salv Technology was fully implemented, lastly, taking over Estonian customer base transaction monitoring and risk scoring.

In addition to the investments in IT systems, the number of employees directly and indirectly involved in AML has significantly increased. New positions were created in both the AML Compliance Department and the business units' AML functions, respectively.

7.2 AML governance structure



First line of defence		Second line of defence	Third line of defence
Customer relations	**Business units' AML departments**	**AML compliance**	**Internal audit**
• Implementation onboarding and on-going KYC	• Responsibility of onboarding of higher risk clients • Performs EDD, incl. AML monitoring and screening • Improves measures related to risk clients in accordance with the regulations • Cooperates with the AML compliance, ensuring their implementation • Ensures customer data quality	• Coordinates AML procedures and processes • Evaluates the risks of higher risk customers, countries and services • Advises first line of defence • Exercises assessment and scrutiny over first line activities • Performs AML inspections and compliance audits • Raises awareness on AML and conducts trainings • Assess AML compliance risks associated with new services and processes • Reports to governing bodies • Reports to the FIU	• Exercises assessment and scrutiny over first and second line activities • Carries out independent assessment of AML measures • Reports to Supervisory Board and Audit Committee

7.3 AML/KYC measures

The main AML/CTF measures (incl. KYC) in LHV are as follows:

- comprehensive risk assessment and risk segmentation;
- strong onboarding CDD supported by the customer acceptance principles;
- regular CDD and EDD;
- risk-based on-line and off-line customer and transactions monitoring;
- screening customers and transactions against international financial sanctions lists and other similar lists (incl. UN and EU lists, but also US OFAC list and UK HM Treasury list);
- strong commitment of the senior and middle managers;
- regular training of employees;
- ongoing communication and cooperation with the Financial Intelligence Unit (FIU) and other relevant stakeholders;
- active participation in setting up industry best practices.

LHV has implemented a four-level decision making process for customer acceptance at the onboarding stage. Depending on the risk indicators of the customer, the decision is made at the following level:

- Customer Relationship Manager
- Customer Relationship Manager together with a Senior Manager (the 4-eyes principle)
- High Risk Customer Acceptance Committee
- The Management Board

In addition to the conservative and risk-based approach and procedures followed at the onboarding stage, risk-based monitoring and screening activities are implemented and regular KYC updates are carried out.

7.4 Banking Services

LHV provides services to fintech companies that in turn provide financial services to their own customers. Compared to servicing other types of clients, this presents a different portfolio of financial crime risks due to LHV being exposed to the customers of our clients. As such, LHV has carefully considered the risks associated with this client population and has applied additional risk-based measures to mitigate risks associated with servicing fintech clients. LHV employs dedicated Client Relationship Managers to this sector, alongside specific first-line and second-line units that monitor and manage the financial crime risks arising from these clients. Enhanced Due Diligence is applied to the fintech client base to reflect the correspondent risk that is posed, including assessing the financial crime programme that we expect to be both commensurate with our own and suitable for the client's own business. During the onboarding and periodic review processes, LHV assesses the business model, ownership structure, leadership, AML/KYC measures, technical capabilities for screening and monitoring, target market, and customer and jurisdiction risk segmentation as part of its assessment of the client. LHV undertakes a programme of period on-site visits to assess AML framework of clients. LHV employs a transaction monitoring programme designed to identify characteristics in client behaviour that indicate financial crime. In the event that LHV identifies risk associated with one of its clients that falls outside of its appetite, remediation actions are taken to address the risk, up to and including termination of the relationship.

7.5 Estonian AML system and the outlook

The most important event for the AML area this year at the national level was the evaluation visit of the European Commission's expert committee Moneyval in April-May, which will result in an assessment report scrutinising the effectiveness of the design and functioning of the AML/CFT system over the past five years. The final report of the evaluation was published on 27 January 2023, and the decision has a significant potential impact on Estonia's reputation. Globally, Estonia's financial system, including LHV, was affected by Russia's and Belarusian-backed aggression against Ukraine, which began in February. The scale of the various sanctions imposed on the aggressor states has historically been unprecedented. As a result, the increased attention of supervisory authorities towards different actors in the financial sector remains the same to minimise the risk of using the Estonian financial system for money laundering, terrorism financing or evading sanctions.

To ensure the effective implementation of due diligence measures, like other major market participants, LHV has essentially stopped mediating payments with credit institutions in Russia and Belarus. We have significantly strengthened the scope of the control measures to be implemented to avoid the risks of circumvention of sanctions.

8. Other risks

8.1 Strategic and business risk

Strategic risk arises mainly from wrong strategic decisions. It is mitigated through well-considered business plans and analyses. In addition, members of management in Group and subsidiaries (both the Management Board and the Supervisory Board) have long-term experience in the banking sector and/or entrepreneurship. Prior to entering new markets and sectors, professionals in the field will always be involved and a thorough analysis will be carried out.

8.2 Country risk

Similarly to reputation risk, country risk usually materialises through other risks (operational risk, credit risk, strategic risk). In addition to Estonia, LHV conducts its business in the United Kingdom.

Consolidated statement of profit or loss and other comprehensive income

EUR thousand	Note	2022	2021
Interest income		152,168	124,637
incl interest income based on EIR		145,992	118,990
Interest expense		-22,679	-26,973
Net interest income	**4**	**129,489**	**97,664**
Fee and commission income		52,889	48,711
Fee and commission expense		-20,481	-17,538
Net fee and commission income	**5**	**32,408**	**31,173**
Net gains from financial assets measured at fair value	8	-1,829	-1,515
Foreign exchange rate gains/losses		1,407	-26
Net loss from financial assets		**-422**	**-1,541**
Other income		199	599
Staff costs	6	-36,129	-26,721
Administrative and other operating expenses	6	-28,416	-22,619
Profit before credit losses		**97,129**	**78,555**
Impairment losses on financial instruments measured at amortised cost		-2,996	-3,948
Profit before income tax		**94,133**	**74,607**
Income tax expense	24	-13,260	-10,557
Net profit for the year		**80,873**	**64,050**
Total comprehensive income for the year		**80,873**	**64,050**
Total comprehensive income attributable to:			
Owners of the parent		78,658	61,759
Non-controlling interest		2,215	2,291
Total comprehensive income for the year		**80,873**	**64,050**

Notes on pages 89 to 109 are an integral part of the consolidated financial statements.

Consolidated statement of financial position

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Assets			
Due from central bank	7	2,390,964	3,874,284
Due from credit institutions	7	84,885	106,461
Due from investment companies	7	3,391	6,188
Financial assets at fair value through profit or loss	8	407	127,720
Financial assets measured at amortised cost	8	364,230	0
Loans and advances to customers	9	3,186,989	2,677,160
Receivables from customers	10	9,253	2,970
Other financial assets	11	124	2,236
Other assets	11	2,866	2,446
Tangible assets	12	7,947	4,182
Right-of-use assets	12	3,013	3,957
Intangible assets	12	2,881	1,243
Total assets		**6,056,950**	**6,808,847**
Liabilities			
Loans received from central banks (TLTRO)	13	147,841	197,461
Deposits from customers	13	4,956,931	5,846,602
Loans received and debt securities in issue	13	384,149	349,063
Financial liabilities at fair value through profit or loss	8	3,850	157
Accounts payable and other liabilities	14	61,901	46,616
Subordinated debt	16	114,056	88,989
Total liabilities		**5,668,728**	**6,528,888**
Equity			
Share capital	17	141,500	111,500
Legal reserve	17	8,736	5,648
Retained earnings		231,805	156,745
Total equity attributable to owners of the parent		**382,041**	**273,893**
Non-controlling interest		6,181	6,066
Total equity		**388,222**	**279,959**
Total liabilities and equity		**6,056,950**	**6,808,847**

Notes on pages 89 to 109 are an integral part of the consolidated financial statements.

Consolidated statement of cash flows

EUR thousand	Note	2022	2021
Cash flows from operating activities			
Interest received		148,992	124,688
Interest paid		-20,545	-29,539
Fees and commissions received	5	52,889	48,711
Fees and commissions paid	5	-20,481	-17,538
Other income received		199	599
Staff costs paid		-32,080	-24,181
Administrative and other operating expenses paid		-23,902	-19,186
Income tax paid		-11,639	-9,556
Cash flows from operating activities before change in operating assets and liabilities		**93,433**	**73,998**
Net increase/decrease in operating assets:			
Net decrease in financial assets at fair value through profit or loss		-35	-140
Loans and advances to customers		-518,254	-475,118
Mandatory deposit at central bank	7	8,609	-16,045
Security deposits	11	2,112	-164
Other assets		4,874	2,586
Net increase/decrease in operating liabilities:			
Demand deposits of customers	13	-989,318	2,031,748
Term deposits of customers	13	97,695	-324,019
Repayments of loans received	13	-49,216	-21,764
Debt securities issued		65,000	99,633
Debt securities redeemed		-31,000	0
Financial liabilities at fair value through profit or loss		3,693	-64
Other liabilities		6,697	20,097
Net cash from/used in operating activities		**-1,305,710**	**1,390,748**
Cash flows from investing activities			
Purchase of tangible and intangible assets	12	-7,548	-4,673
Net changes of investment securities at fair value through profit or loss and amortised cost	8	-234,810	193,835
Net cash from/used in investing activities		**-242,358**	**189,162**
Cash flows from financing activities			
Paid in share capital	17	30,000	5,000
Proceeds from subordinated debt	16	30,000	0
Subordinated loans redeemed		-5,000	0
Dividends paid		-6,000	-6,000
Repayment of principal of lease liabilities		-1,423	-1,254
Net cash from/used in financing activities		**47,577**	**-2,254**
Effect of exchange rate changes on cash and cash equivalents		**1,407**	**-26**
Net increase/decrease in cash and cash equivalents		**-1,499,084**	**1,577,630**
Cash and cash equivalents at the beginning of the year	7	**3,929,635**	**2,352,005**
Cash and cash equivalents at the end of the year	7	**2,430,551**	**3,929,635**

Notes on pages 89 to 109 are an integral part of the consolidated financial statements.

Consolidated statement of changes in equity

EUR thousand	Share capital	Legal reserve	Retained earnings	Total	Non-controlling interest	Total equity
Balance as at 1 Jan 2021	**106,500**	**4,022**	**98,285**	**208,807**	**5,875**	**214,682**
Transfer to legal reserve (Note 19)	0	1,626	-1,626	**0**	0	**0**
Paid in share capital (Note 17)	5,000	0	0	**5,000**	0	**5,000**
Dividends paid	0	0	-3,900	**-3,900**	-2,100	**-6,000**
Share options (Note 17)	0	0	2,227	**2,227**	0	**2,227**
Profit for the year	0	0	61,759	**61,759**	2,291	**64,050**
Total comprehensive income for 2021	0	0	61,759	**61,759**	2,291	**64,050**
Balance as at 31 Dec 2021	**111,500**	**5,648**	**156,745**	**273,893**	**6,066**	**279,959**
Balance as at 1 Jan 2022	**111,500**	**5,648**	**156,745**	**273,893**	**6,066**	**279,959**
Transfer to legal reserve (Note 19)	0	3,088	-3,088	**0**	0	**0**
Paid in share capital (Note 17)	30,000	0	0	**30,000**	0	**30,000**
Dividends paid	0	0	-3,900	**-3,900**	-2,100	**-6,000**
Share options (Note 17)	0	0	3,390	**3,390**	0	**3,390**
Profit for the year	0	0	78,658	**78,658**	2,215	**80,873**
Total comprehensive income for 2022	0	0	78,658	**78,658**	2,215	**80,873**
Balance as at 31 Dec 2022	**141,500**	**8,736**	**231,805**	**382,041**	**6,181**	**388,222**

Additional information on equity is provided in Note 17.

Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented and to all the consolidated group entities, unless otherwise stated.

1. Basis of preparation

The Group's consolidated financial statements for 2022 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted in European Union. The financial statements have been prepared under the historical cost convention. As an exception, some financial assets and liabilities, including derivatives, are stated at their fair values as described in the accounting policies below.

The preparation of consolidated financial statements in accordance with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 2.

The financial year started at 1 January 2022 and ended at 31 December 2022. The financial figures have been presented in thousands of euros (EUR) unless otherwise indicated.

1.1 Changes in used accounting policies

During the reporting period there was a change in liquidity management. The treatment of liquidity portfolio was changed. Before the change, the liquidity portfolio was measured at fair value in the statement of financial position. After the change, the liquidity portfolio is measured at amortised cost.

1.2 Summary of significant accounting policies

A number of new standards, interpretations and amendments are effective for annual periods beginning on or after 1 January 2022 but do not have a material impact on the Group's financial statements.

New currently effective requirements

Annual improvements to IFRS standards 2018-2020 (Effective for annual periods beginning on or after 1 January 2022. Early application is permitted.) These amendments are not yet endorsed by the EU.

Improvements to IFRS (2018-2020) include three amendments to the standards:

- The amendments to IFRS 9 Financial Instruments clarify that, when assessing whether an exchange of debt instruments between an existing borrower and lender is on terms that are substantially different, the fees to include together with the discounted present value of the cash flows under the new terms include only fees paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf.
- The amendments to IFRS 16 Leases remove illustrative example 13 accompanying IFRS 16, which in practice creates confusion in accounting for leasehold improvements for both the lessee and the lessor. The purpose of the amendment is to remove the illustrative example that creates confusion.
- The amendments to IAS 41 Agriculture remove the requirement to use pre-tax cash flows to measure the fair value of agriculture assets. Previously, IAS 41 had required an entity to use pre-tax cash flows when measuring fair value but did not require the use of a pre-tax discount rate to discount those cash flows.

The Group does not expect the amendments to have a material impact on its financial statements when initially applied.

Amendment to IFRS 16 COVID-19-Related Rent Concessions beyond 30 June 2021 (Effective for annual periods beginning on or after 1 April 2021.)

The pronouncement amended IFRS16 Leases to provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification.

Forthcoming requirements

The following new standards, interpretations and amendments were not yet effective for the annual reporting period ended 31 December 2022 and have not been applied in preparing these consolidated financial statements. The Group plans to adopt these pronouncements when they become effective.

Amendments to IAS 1 Presentation of Financial Statements (Effective for annual periods beginning on or after 1 January 2023; to be applied retrospectively. Early application is permitted.) These amendments are not yet endorsed by the EU.

The amendments clarify that the classification of liabilities as current or non-current is based solely on the entity's right to defer settlement at the end of the reporting period. The entity's right to defer settlement for at least 12 months from the reporting date need not be unconditional but must have substance. The classification is not affected by management's intentions or expectations about whether and when the entity will exercise its right. The amendments also clarify the situations that are considered settlement of a liability.

The Group does not expect the amendments to have a material impact on its financial statements when initially applied.

Accounting Policies, Changes in Accounting Estimates and Errors – Amendments to IAS 8 Effective for annual periods beginning on or after 1 January 2023. Early application is permitted)

The amendments introduce a new definition for accounting estimates: clarifying that they are monetary amounts in the financial statements that are subject to measurement uncertainty. The amendments also clarify the relationship between accounting policies and accounting estimates by specifying that a company develops an accounting estimate to achieve the objective set out by an accounting policy.

The amendments are not expected to have a material impact on the Group.

Income Taxes - Amendments to IAS 12 (Effective for annual periods beginning on or after 1 January 2023. Early application is permitted)

The amendments clarify the accounting for deferred tax on transactions that involve recognising both an asset and a liability with a single tax treatment related to both.

The Group does not expect the amendments to have a material impact on its financial statements when initially applied.

Lease Liability in a Sale and Leaseback – Amendments to IFRS 16 (Effective for annual periods beginning on or after 1 January 2024)

Leases impact how a seller-lessee accounts for variable lease payments that arise in a sale-and-leaseback transaction. The Group is currently assessing the impact of the standard on its financial statements.

Classification of Liabilities as Current or Non-current – Amendments to IAS 1 (Effective for annual periods beginning on or after 1 January 2024)

Amendment clarifies the requirements for the presentation of liabilities in the statement of financial position. The Group is currently assessing the impact of the standard on its financial statements.

2. Consolidation

The consolidated financial statements for 2022 comprise the financial statements of AS LHV Pank (parent company) and its subsidiary LHV Finance. AS LHV Pank holds a 65% interest in LHV Finance.

Subsidiaries are entities which are controlled by the Group. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Acquisitions of subsidiaries and businesses are accounted for using the acquisition method (except for business combinations of entities under common control). The cost of an acquisition is measured as the acquisition-date fair value of the assets acquired, equity instruments issued, and liabilities incurred or assumed.

Transaction costs incurred on issuing equity instruments are deducted from equity; transaction costs incurred on issuing debt instruments are deducted from their carrying amounts and all other transaction costs associated with the acquisition are expensed. According to the acquisition method, the identifiable assets, liabilities, and contingent liabilities of the acquired subsidiary are recognised at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest.

The Group measures a non-controlling interest that represents a present ownership interest and entitles the holder to a proportionate share of net assets in the event of liquidation on a transaction by transaction basis, either at: (a) fair value, or (b) the non-controlling interest's proportionate share of the net assets of the acquiree. Non-controlling interests that are not present ownership interests are measured at fair value.

Goodwill is measured by deducting the net assets of the acquiree from the aggregate of the consideration transferred for the acquiree, the amount of any non-controlling interest in the acquiree and the fair value of the acquirer's previously held interest in the acquiree. Any negative amount (bargain purchase gain) is recognised in profit or loss, after management reassesses whether it has identified all the assets acquired and all liabilities and contingent liabilities assumed, and reviews the appropriateness of their measurement.

Intragroup transactions, balances, and unrealised profits on transactions between group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred.

The revenues and expenses of subsidiaries acquired during the financial year are consolidated in the Group's statement of profit or loss and other comprehensive income from the date of acquisition to the end of the financial year. The results of operations of subsidiaries disposed of during the financial year are consolidated in Group's statement of profit or loss and other comprehensive income from the beginning of the financial year to the date of disposal.

Consistent with the Accounting Act of the Republic of Estonia, the primary financial statements of the consolidating entity (the parent company) have to be disclosed in the notes to the consolidated financial statements. In preparing the primary financial statements of the parent, the same accounting policies have been used as in preparing the consolidated financial statements, except for investments in subsidiaries, which in the parent's separate primary financial statements (see Note 24) are accounted for at cost less any impairment losses. A non-controlling interest is that part of the net results and net assets of a subsidiary, which is not attributable, directly or indirectly, to the parent company. A non-controlling interest forms a separate component of the Group's equity. A non-controlling interest in the consolidated statement of financial position is disclosed separately from the equity attributable to the owners of the parent company. In the consolidated statement of profit or loss and other comprehensive income, a non-controlling interest's share of profit or loss and total comprehensive income is disclosed separately from that of the owners of the parent.

3. Associates

An associate is an entity over which the Group has significant influence but which it does not control. Generally, significant influence is assumed to exist when the Group holds between 20% and 50% of the voting rights. The Group did not have any associate as at 31 December 2022 and 31 December 2021.

In the consolidated financial statements, investments in associates are accounted for using the equity method. Under this method, the investment is initially recognised at cost, which is thereafter adjusted for post-acquisition changes in the investor's share of the investee's equity (changes both in the profit or loss as well as other equity items of the associate), depreciation of depreciable assets and amortisation of the differences between the fair values and carrying amounts of the investee's assets, liabilities and contingent liabilities as determined in the purchase price allocation. Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the assets.

When the Group's share of losses in the associate accounted for under the equity method exceeds the carrying amount of the associate, the carrying amount of the investment is reduced to zero and such long-term loans granted to the associate that in substance form a part of the investment are written down. Further losses are accounted for off the statement of financial position. When the Group has guaranteed or incurred obligations on behalf of the associate, the respective liability as well as the loss under the equity method are recognised in the statement of financial position. Other receivables from the associate are measured at amortised cost.

An investment in the assets and liabilities of the acquired associate as well as any goodwill that arose on acquisition is presented as a net amount in the statement of financial position within investments in associates.

At the end of each reporting period, it is assessed whether there is any indication that the recoverable amount of the investment has fallen below its carrying amount. If any such indications exist, an impairment test is performed. To determine the recoverable amount of the investment, the principles described in 'Summary of significant accounting policies' section 10. are used.

4. Foreign currency translation

4.1 Functional and presentation currency

The functional and presentation currency of entities in the Group is euro.

4.2 Foreign currency transactions and balances

Foreign currency transactions are recorded on initial recognition based on the foreign exchange rates of the European Central Bank prevailing at the dates of the transactions. At the end of each reporting period, foreign currency monetary items are translated into euros using the foreign exchange rates of the European Central Bank prevailing at the reporting date. Non-monetary items that are measured at fair value in a foreign currency are translated into euros using the foreign exchange rates of the European Central Bank prevailing at the date the fair value was measured. Gains and losses on the translation of monetary assets and liabilities are recognised in profit or loss within foreign exchange gains/losses. Translation differences on non-monetary items, such as equities at fair value through profit or loss, are reported as part of the fair value gain or loss in profit or loss within net gain/loss from financial assets measured at fair value.

5. Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, demand deposits with central and other banks and investment companies, and term deposits with original maturities of three months or less that are available for use without any restrictions and subject to an insignificant risk of changes in value.

6. Financial assets

6.1 Initial recognition and derecognition

Financial assets are recognised in the statement of financial position when the Group becomes a party to the contractual provisions of the instrument and measured at fair value on initial recognition. Transaction costs are included in the initial fair value except for financial assets at fair value through profit or loss whose transaction costs are recognised in profit or loss. Financial assets measured at fair value and financial assets measured at amortised cost are recognised in the statement of financial position on the trade date.

Financial assets are derecognised when (a) the assets are redeemed or the rights to the cash flows from the assets otherwise expire or (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all the risks and rewards of ownership, but not retaining control.

Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

6.2 Subsequent measurement

The Group classifies its financial assets as subsequently measured at fair value through profit or loss, fair value through other comprehensive income or amortised cost. The classification depends on whether the financial asset is a debt instrument, an equity instrument or a derivative.

6.3 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 are 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 Group's divisions. 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 contractual cash flows are solely payments of principal and interest, principal is defined as the fair value of the debt instrument at initial recognition. The principal amount can change over the life of the instrument if there are repayments of principal or interest is capitalised. Interest cash flows are consistent with the components of a basic lending arrangement including consideration for the time value of money, credit risk, liquidity risk as well as administrative costs and a profit margin. If there are contractual terms introducing exposure to other risks or volatility, the cash flows are not considered to be solely payments of principal and interest. SPPI tests are performed as a part of new product approval tests.

Debt instruments are presented in the statement of financial position within due from central banks, due from credit institutions, due from investment companies, loans and advances to customers, financial assets at fair value through profit or loss, financial assets at amortised cost, receivables from customers and other financial assets and they include instruments in the following measurement categories.

Fair value through profit or loss: Debt instruments are classified into this category if they do not meet the criteria for amortised cost or fair value through other comprehensive income. This is the case if the instrument is held for trading. Financial assets are held for trading if they are held for the purpose of selling in the short term and profit-taking. Debt instruments are measured at fair value through profit or loss if they are managed and measured on a fair value basis or held with the intention to sell, or if their cash flows are not solely payments of principal and interest.

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

Amortised cost: Debt instruments are classified into this category if both of the following criteria are met. (a) the business model objective is to hold the assets to collect contractual cash flows and (b) the contractual cash flows are 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.

6.4 Equity instruments

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

6.5 Derivatives

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

6.6 Modification

The Group may renegotiate loans and modify contractual terms. If the new terms are substantially different from the original ones, 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.

6.7 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 affected financial assets.

6.8 Write-off

The Group writes off financial assets, in whole or in part, when it has exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a derecognition event.

Indications of no reasonable expectation of recovery include (i) ceasing of debt collection activities and (ii) where the Group's recovery method is foreclosing on collateral, determining that the value of the collateral is such that there is no reasonable expectation of recovery.

If it is not feasible or economically reasonable for the Group to take measures to recover a receivable, the receivable is classified into non-performing and removed from the statement of financial position. At least one of the conditions has to be filled to classify a receivable into non-performing.

If a receivable which has been written off as uncollectable is subsequently collected, the amount received is recognised as income.

IFRS 9 measurement category		Asset class		31 Dec 2022	31 Dec 2021
Financial assets	Amortised cost	Due from banks and investment companies		2,479,240	3,986,933
		Loans and advances to customers	Loans to legal entities	1,941,632	1,667,234
			Loans to individuals	1,245,357	1,009,926
		Debt securities		364,230	0
		Receivables from customers		9,253	2,970
		Other financial assets		124	2,236
	Fair value through profit or loss	Shares and fund units		367	367
		Listed bonds		0	127,349
		Derivatives		40	4
Financial liabilities	Amortised cost	Amounts owed to central banks (TLTRO)		147,841	197,461
		Deposits from customers		4,956,931	5,846,602
		Loans received and debt securities in issue		384,149	349,063
		Accounts payable and other liabilities		54,838	41,155
		Subordinated debt		114,056	88,989
	Fair value through profit or loss	Derivatives		3,850	157

7. Impairment of financial assets

7.1 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 the recognition of ECLs.

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 liabilities, in the statement of financial position. Adjustment to the loss allowances and provisions due to changes in ECLs is recognised in profit or loss as net expected credit losses.

The assessment of credit risk, and the estimation of the ECL must be unbiased and probability-weighted and 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 calculates ECLs using both models and individual assessments which are based on input from experts.

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

7.2 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. The indicators include payments that are >30 days and <90 days past due and financial assets that have been classified as on the 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 the 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. If there has been a significant increase in credit risk since initial recognition, an allowance for lifetime ECL is recognised and the financial instrument is transferred to Stage 2. The approach is symmetrical, meaning that if the credit quality of the financial instrument subsequently improves, such that there is no longer a significant increase in credit risk since initial recognition, the financial asset moves back to Stage 1.

7.3 Definition of default

The Group defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

1) Quantitative criteria

The borrower is more than 90 days and over EUR 10 past due on the contractual payments. The threshold of EUR 10, which is set out in debt management procedures, is a trigger for debt collection activities and also indicated as the materiality threshold in the definition of default.

2) Qualitative criteria

The borrower meets the unlikeliness to pay criteria, which indicate that the borrower is in significant financial difficulty. The following circumstances are considered as indicators for the customer is unlikely to settle the debt in full:

- non-accrued status of the contract;
- specific credit adjustments have been made due to the decline in the credit quality;
- sale of the credit obligation with an economic loss exceeding 5%;
- distressed restructuring measures have been applied to the contract resulting in the decrease of the financial obligation by more than 1%;
- it is becoming probable that the borrower will enter or has filed for bankruptcy;
- the customer's cash flows are no longer sufficient to meet the instalment payments;
- the Group has called in any collateral, if any, including a guarantee.

The above criteria are applied to all financial instruments held by the Group and are consistent with the definition of default used for internal credit risk management purposes. Financial instruments in default are in Stage 3. All financial assets in Stage 3 are considered credit impaired.

7.4 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 over 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 the asset class and the product type.

EAD represents an estimate of the outstanding amount of credit exposure at the time a default may occur. For amounts accounted for off the statement of financial position, 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, which have been adjusted to meet IFRS 9 requirements. When measuring ECL, LHV uses the maximum contractual period during which LHV is exposed to risk.

7.5 Forward-looking information

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

Forecasts are developed internally in the Credit Management Department, which consults with the Risk Control Department and business and finance experts. If possible, without undue cost, external experts should be consulted and externally developed benchmark forecasts should be taken into account. The benchmark forecasts include but are not limited to the World Economic Outlook by the IMF, European Economic Forecasts by the European Commission and Economic Forecasts by the Bank of Estonia. The scenarios must be approved by the Risk and Capital Committee.

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

7.6 Individual assessments and management´s judgement

The Group uses both models and judgement based on the input of experts 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. Experts' opinions may be applied to the modelled outcome to incorporate an estimated impact of factors not captured by the model. Such individual ECL assessments may be applied to significant exposures at a counterparty level. The assessments 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.

8. Tangible fixed assets

Tangible fixed assets (tangible assets) are non-current assets used in the Group's operating activities that have a useful life of over one year. A tangible asset is initially recognised at its cost, which consists of the purchase price (incl. customs duties and other non-refundable taxes) and any directly attributable expenditure on bringing the asset to its operating condition and location. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repair and maintenance costs are charged to operating expenses during the reporting period in which they are incurred.

A tangible asset is carried in the statement of financial position at cost less any accumulated depreciation and any accumulated impairment losses. Depreciation is calculated on a straight-line basis. The annual depreciation rate for computers, furniture and fixtures is 33%. Improvements of rental space are either depreciated at the rate of 20% per year or over the lease term, depending on which is shorter. Depreciation is calculated starting from the month of acquisition until the carrying amount decreases to the residual value of the asset. When the residual value is greater than the carrying amount of the asset, depreciation ceases.

The depreciation methods used, and the residual values and useful lives of assets are reviewed, and adjusted if appropriate, at the end of each reporting period. The Group performs an impairment test when there are circumstances which indicate impairment. Where an asset's carrying amount is greater than its estimated recoverable amount (the higher of an asset's fair value less costs of disposal and its value in use), the asset is immediately written down to its recoverable amount by recognising an impairment loss in the statement of profit or loss for the reporting period. Gains and losses on disposals are determined by comparing the disposal proceeds with the carrying amount of the asset. The gains and losses are included in other income and operating expenses, respectively, in the statement of profit or loss for the reporting period.

9. Intangible assets

Intangible assets are identifiable non-monetary assets without physical substance. An intangible asset is initially measured at cost, comprising of its purchase price and any directly attributable expenditure on preparing the asset for its intended use. After initial recognition, an intangible asset is carried at its cost less any accumulated amortisation and any accumulated impairment losses. Amortisation is calculated on a straight-line basis. The annual amortisation rate for purchased licenses is 33%.

The appropriateness of amortisation rates, methods and residual values is assessed at the end of each reporting period. The Group reviews intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's fair value less costs to sell and value in use.

10. Impairment of non-financial assets

Assets that have indefinite useful lives (including goodwill) are not subject to amortisation. Instead, they are tested annually for impairment by comparing their carrying amounts with their recoverable amounts.

Assets with an unlimited useful life and depreciable assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. In the event of such circumstances, the recoverable amount of the asset is assessed and compared with its carrying amount.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating unit).

Impairment losses are recognised in profit or loss.

At the end of each following reporting period, assets that have been written down are assessed to determine whether their recoverable amount has increased (except for impairment losses of goodwill that are not reversed). If the impairment test indicates that the recoverable amount of an asset or asset group (cash-generating unit) has increased above its carrying amount, the previous impairment loss is reversed up to the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years. Reversals of impairment losses are recognised in profit or loss as a reduction of the impairment loss.

11. Loan commitments, financial guarantees and performance guarantees

The Group issues commitments to provide loans. These commitments are irrevocable or revocable only in response to a material adverse change. Such commitments are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight-line basis over the life of the commitment, except for commitments to originate loans if it is probable that the Group will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At the end of each reporting period, the commitments are measured at (i) the remaining unamortised balance of the amount at initial recognition, plus (ii) the amount of the loss allowance determined based on the expected credit loss model, unless the commitment is to provide a loan at a below market interest rate, in which case the measurement is at the higher of these two amounts. The carrying amount of the loan commitments represents a liability. For contracts that include both a loan and an undrawn commitment and where the Group cannot separately distinguish the ECL on the undrawn loan component from the loan component, the ECL on the undrawn commitment is recognised together with the loss allowance for the loan. To the extent that the combined ECLs exceed the gross carrying amount of the loan, they are recognised as a liability.

The Group issues financial guarantees. Financial guarantees represent irrevocable assurances to make payments if a customer fails to make payment to third parties and carry the same credit risk as loans. Financial guarantees are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight-line basis over the life of the financial guarantee. At the end of each reporting period, the financial guarantees are measured at the higher of (i) the amount of the loss allowance for the guaranteed exposure determined based on the expected loss model and (ii) the remaining unamortised balance of the amount at initial recognition. In addition, an ECL allowance is recognised for fees receivable that are recognised in the statement of financial position as an asset.

Performance guarantees are contracts that provide compensation if another party fails to perform a contractual obligation. Such contracts do not transfer credit risk. Performance guarantees are initially recognised at their fair value, which is normally evidenced by the amount of fees received. This amount is amortised on a straight-line basis over the life of the contract. At the end of each reporting period, the performance guarantee contracts are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the contract at the end of each reporting period, discounted to present value. Where the Group has the contractual right to revert to its customer for recovering amounts paid to settle the performance guarantee contracts, such amounts will be recognised as loans and receivables upon transfer of the loss compensation to the guarantee's beneficiary.

12. Financial liabilities

The Group classifies financial liabilities either:

a) financial liabilities measured at fair value through profit or loss
b) financial liabilities measured at amortised cost
c) financial guarantee contracts and loan commitments

Derivatives are classified as financial liabilities at fair value through profit or loss as disclosed in 'Summary of significant accounting policies' section 6. All other financial liabilities are subsequently measured at amortised cost using the effective interest method. Transaction costs are included in the calculation of the effective interest rate. The difference between the proceeds (less transaction costs) and redemption value are recognised in profit or loss during the term of the instrument using the effective interest rate. Interest expense is reported in profit or loss within interest expense.

Deposits from customers are initially recorded on their settlement date at their fair value less transaction costs and are subsequently measured at amortised cost using effective interest method. Deposits from customers are reported in the statement of financial position within deposits from customers and loans received. Accrued interest liabilities are included in the same item.

Loans received, debt securities issued, and similar subordinated debts are initially recognised at fair value less transaction costs (cash received less transaction costs). Subordinated debts are those liabilities which in case of the liquidation of a credit institution or declaration of bankruptcy are settled after the satisfaction of the justifiable claims of other creditors. Other financial liabilities (trade payables, accrued expenses and other borrowings) are initially recognised at fair value less transaction costs and are subsequently carried at amortised cost.

LHV entered into one new type of funding transaction in 2021:

- preferred bonds;

These instruments are accounted for as other loans received using effective interest rates, similarly to the year 2020 new fundings TLTRO III and covered bonds. Covered bonds are secured by the mortgage book and the issues are rated by Moody's and listed on the Euronext Dublin. TLTRO III is secured by mortgage bonds and loans provided to local governments. Preferred bonds are issued with a four-year maturity, which includes the option to call back the transaction after the third year. The issue received a Baa3 rating and was listed on Euronext Dublin.

TLTRO III has a conditional interest rate, which depends on the fulfilment of conditions. LHV has taken a conservative approach and calculates the effective interest without taking the potential positive uplift of interest into account. When the conditions are fulfilled, LHV will recalculate interest income and recognise the difference in the current period without restating the previous accounting periods.

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled, or expires).

13. Payables to employees

Payables to employees include unpaid salary accruals and a vacation pay accrual calculated in accordance with employment contracts and the laws in force in the employee's country of residence at the end of the reporting period. The accrued vacation pay liability together with related social security and unemployment insurance charges is included within current liabilities in the statement of financial position and recognised as staff costs in profit or loss.

The social security tax includes payments to the state pension system. The group has no existing legal nor constructive obligations to make pension or similar payments supplementary to the social security tax.

14. Share-based payments

AS LHV Group operates a share-based option programme, under which the company receives services from Group's employees as consideration for the equity instruments (options) of LHV Group. The fair value of the employee services received in exchange for the grant of the options is recognised during the shared-based compensation program as the Group's staff costs and as an increase in equity (other reserves). The total amount to be expensed is determined by the fair value at the time of issuing the options. The fair value of the options granted is determined by:

- including any market-based performance conditions (market conditions) that influence the option price (e.g., the LHV Group share price);
- excluding the impact of any service and non-market conditions (vesting conditions other than market conditions) e.g., profitability, sales growth targets and remaining an employee of the Group over a specified period).

At the end of each reporting period, the Group revises its estimates of the number of options that are expected to vest based on the vesting conditions (other than market conditions). It recognises the impact of the revision to original estimates, if any, in profit or loss, with a corresponding adjustment to equity.

When the options are exercised, LHV Group issues new shares.

The grant by LHV Group of options to acquire its equity instruments to the employees of subsidiary undertakings is treated as a capital contribution. The fair value of employee services received, measured by reference to the grant date fair value, is recognised over the vesting period as an increase in investments in subsidiary undertakings, with a corresponding credit to equity in the parent entity accounts. According to the law, there are no social security charges when the options are exercised after a 3-year period.

15. Provisions and contingent liabilities

A provision is recognised when the Group has a liability of uncertain timing or amount arising from an obligating event before the end of the reporting period that has either a legal basis or has arisen from the Group's current operating practice (a legal or constructive obligation), it is probable (more likely than not) that an outflow of resources will be required to settle the obligation and the amount of the obligation can be estimated reliably. Provisions are recognised based on the management's estimates regarding the amount and timing of the expected outflows. A provision is recognised in the statement of financial position in the amount which according to management is necessary to settle the obligation at the end of the reporting period or to transfer it to a third party at that time. Expenditure on the recognition of provisions and changes in the carrying amounts of provisions are recognised as an expense in the reporting period. Provisions are not recognised for future operating losses. In case the provision is decreased the change is recognised as a reduction of expense in the reporting period.

When it is probable that a provision will be realised later than 12 months after the end of the reporting period, it is recorded at discounted value (present value of expected outflows) unless the effect of discounting is immaterial.

Contingent obligations (guarantees, excluding financial guarantees, and other commitments) whose realisation is less probable than non-realisation or amount cannot be estimated reliably but which may transform into obligations in certain circumstances, are disclosed in the notes to the financial statements as contingent liabilities. Contingent liabilities may develop in a way not initially expected. Therefore, they are assessed continually to determine whether an outflow of resources embodying economic benefits has become probable on a portfolio basis. If it becomes probable that an outflow of future economic benefits will be required for an item or a portfolio of items previously classified as a contingent liability, a provision is recognised in the financial statements of the period in which the change in probability occurs (except in the extremely rare circumstances where no reliable estimate can be made).

16. Distinction between current and non-current assets and liabilities

Assets from which resources are expected to flow to the Group within 12 months are recognised as current assets. The portion of assets with expected inflows later than 12 months after the end of the reporting period is recognised as non-current assets (see the disclosures in the 'Risk management' section, subsection 4).

Liabilities are treated as current when they are due to be settled within 12 months after the end of the reporting period or if the Group does not have an unconditional right to defer settlement for more than 12 months after the end of the reporting period. Loans received with a due date within 12 months after the end of the reporting period which are refinanced as non-current after the end of the reporting period but before the financial statements are authorised for issue are treated as current. Loans received that the lender has the right to call in at the end of the reporting period due to breaches of contractual terms are also treated as current.

17. Revenues and expenses

17.1 Interest income and expenses

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 or debt investments measured at fair value through other comprehensive income.

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 gross carrying amount of the financial asset or the amortised cost of a financial liability. 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 becomes credit-impaired, interest income is recognised by applying the effective interest rate to the amortised cost, i.e. the gross carrying amount is adjusted for the loss allowance. If 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 is then applied to recognise interest income.

17.2 Fee and commission income and expenses

Fee and commission income comprises revenue from contracts with customers. It does not include revenue from lease 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 by 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 customers in an amount that reflects the consideration to which LHV expects to be entitled in exchange for the service.

Fee and commission income is recognised over time on a straight-line basis as the services being rendered, when the customer simultaneously receives and consumes the benefits provided by the Group's performance. Variable fees are recognised only to the extent that management determines that it is highly probable that a significant reversal will not occur.

Other fee and commission income is recognised at a point in time when the Group satisfies its performance obligation, usually upon execution of the underlying transaction. The amount of fee or commission received or receivable represents the transaction price for the services identified as distinct performance obligations.

The main types of fees are described below.

Fee and commission income for asset custody and asset management provided 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 the purchase or sale of a business, are recognised on the completion of the transaction.

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

17.3 Financial income and cost

Gains and losses arising from changes in the fair values of financial assets and liabilities measured at fair value through profit or loss are reported within net gain/loss from financial assets. 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.

17.4 Dividend income

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

18. Asset management services

The Group provides asset management services (Note 18). Assets managed by the Group that belong to third parties are accounted for off the statement of financial position. The Group derives service fees from the holding and management of such assets. The services do not involve any credit or market risks for the Group.

19. Leases - Group as the lessee

Lessees are required to recognise:

(a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and

(b) depreciation of lease assets separately from interest on lease liabilities in the income statement.

The Group leases various properties. Rental contracts are typically made for fixed periods of up to 5 years but include, as a rule, extension, and termination options. Lease terms are negotiated on an individual basis and may contain a wide range of different terms and conditions.

The Group recognises a right-of-use asset and a corresponding lease liability at the date at which the leased asset is available for use.

In the periods presented, lease liabilities are recognised at the present value of the lease payments. Right-of use assets are measured at amounts equal to the lease liabilities, as no adjustments to right-of-use assets were necessary. Each lease payment is allocated between the reduction of the lease liability and finance cost. The finance cost is charged to profit or loss over the lease term to produce a constant periodic rate of interest on the remaining balance of the liability. The right-of-use asset is depreciated on a straight-line basis over the shorter of its useful life and the lease term.

Lease liabilities include the net present value of the following lease payments:

- fixed payments, less any lease incentives receivable;
- variable lease payment that are based on an index or rate (for example inflation, Euribor);
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option.

Lease payments are discounted using the interest rate implicit in the lease, if it is readily determinable, or the Group's incremental borrowing rate. The incremental borrowing rate is the rate of interest that a lessee would have to pay to borrow, over a similar term and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment.

Short-term leases are leases with a lease term of 12 months or less. Low-value assets comprise IT-equipment and small items of office furniture. In determining the lease term, management considers all facts and circumstances that create an economic incentive to exercise an extension option or not to exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended (or not terminated). Management reviews the assessment if a significant event or a significant change in circumstances occurs that is within the control of management and affects whether the Group is reasonably certain to exercise an option not previously included in the determination of the lease term or not to exercise an option previously included in the determination of the lease term.

According to the contracts, the Group has not granted any residual value guarantees.

20. Taxation and deferred income tax

20.1 Corporate income tax in Estonia

Estonian companies generally do not pay corporate income tax on profit earned in a financial year. Income tax is paid on profit distributions, both direct (dividends, other distributions from equity) and indirect ones (non-business expenses, transfer price adjustments, certain payments to tax havens, etc.). The income tax rate for dividends and other profit distributions is 20% (the amount of tax payable is calculated as 20/80 of the net distribution). Starting from 2019, the income tax rate for regular dividend distributions is 14% (the amount of tax payable is calculated as 14/86 of the net distribution). The lower tax rate applies to a dividend distribution to the extent of the three preceding years' average dividend distribution on which tax has been paid. Corporate income tax arising from dividend distributions is recognised as a liability and income tax expense when the dividend is declared. Income tax must be paid by the 10th day of the month following the distribution of the dividend.

Starting from Q2 2018 credit institutions have to make advance payments of income tax at the rate of 14% of their quarterly profits (Note 24). The tax has to be paid by the 10th day of the third month following the quarter. Advance income tax payments are non-refundable and thus recognised as an expense but they can be used to reduce the income tax payable on future dividend distributions. LHV is a growing company and cannot utilise the paid advance income tax in the foreseeable future. Therefore, the tax is recognised as an expense.

20.2 Deferred tax

Deferred tax is calculated on all significant temporary differences between the tax bases and carrying amounts of assets and liabilities. The main temporary differences arise from depreciation and tax loss carry-forwards. Deferred tax items are measured at the tax rates that are expected to apply to the period when the temporary differences reverse or the tax loss carry-forwards are utilised, based on tax rates enacted or substantively enacted by the end of the reporting period. Deferred tax assets and liabilities are offset only when they relate to the same taxable entity. Deferred tax assets for deductible temporary differences and tax loss carry-forwards are recognised only to the extent that it is probable that future taxable profit will be available against which the assets can be utilised. Deferred tax is recognised for all taxable temporary differences associated with investments in subsidiaries, except to the extent that the Group is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The contingent income tax liability reflecting the tax obligation that would arise if all the Group's unrestricted equity were distributed as dividends is not recognised in the statement of financial position. The maximum amount of income tax payable on the distribution of the entire retained earnings as dividends is disclosed in Note 17 to the financial statements.

21. Offsetting

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously. More detailed information is presented in the Risk management section.

22. Legal reserve

The legal reserve is a mandatory capital reserve which is formed using annual net profit transfers to comply with the requirements of the Estonian Commercial Code. Each financial year, at least one-twentieth of net profit has to be transferred to the legal reserve, until the reserve reaches one-tenth of share capital. The legal reserve may be used to cover losses or to increase share capital. It may not be used to make distributions to shareholders.

Notes to the consolidated financial statements

NOTE 1 General information

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as adopted in European Union for the year ended 31 December 2022 for AS LHV Pank (hereinafter the Bank or LHV Pank, including branch in UK) and its subsidiary AS LHV Finance (together hereinafter: the Group or LHV). AS LHV Pank holds 65% interest in AS LHV Finance.

AS LHV Pank provides banking, financial advisory and securities brokerage services to customers in Estonia and in UK. There are offices for client servicing in Tallinn, Tartu and also London branch was opened in 2018. LHV is a limited liability company incorporated and domiciled in Estonia. The address of its registered office is Tartu mnt. 2, Tallinn. As at 31 Dec 2022, the Group employed 765 people, including 45 non-active employees (31 Dec 2021: 611 people, 40 non-active employees). LHV Finance offers hire-purchase services to merchants and consumer loans.

The Management Board approved the consolidated annual report (incl. financial statements) on 16 February 2023. The consolidated annual report will be presented for approval to the sole shareholder AS LHV Group. Rain Lõhmus, who owns 21.8% of the voting rights and Andres Viisemann, who owns 11.3% of the voting rights (see also Note 17), have significant influence over AS LHV Group.

The consolidated annual report approved by the Management Board shall be authorised for approval by the Supervisory Board and shareholders. The shareholders have the right not to approve the consolidated annual report while the Supervisory Board does not have that right.

NOTE 2 Significant management estimates and assumptions

Consistent with IFRS, management makes estimates and assumptions which affect the amounts reported in the financial statements. Although the estimates are based on management's best knowledge and judgement, actual outcomes may differ from these estimates. Management's estimates have been applied to valuation of loans, receivables and investments (Risk management section 2, Notes, 8, 9 and 10).

Estimates and judgments are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable in the circumstances. Changes in management's estimates are recognised prospectively.

The most significant management estimates and assumptions are related with the financial instrument standard IFRS 9, namely the criteria for a significant increase in credit risk (SICR), the calculation of probability of default (PD) and loss given default (LGD), the business model and solely payments of principal and interest (SPPI) assessment for the classification of financial assets. Please see more information in the 'Risk management' section, subsection 2 and below.

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 concept under IFRS 9 Financial Instruments and requires significant judgement. At the end of each reporting period the Group performs 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 judgements based on the input of experts to determine ECLs.

The objective of making judgements based on the input of experts is to incorporate the estimated impact of factors not captured in the modelled ECL. The degree of judgement that is required to estimate ECLs depends on the outcome of the calculations, materiality, and the availability of detailed information. The models, assessments and assumptions are regularly reviewed by the risk organisation.

NOTE 3 Offsetting assets and liabilities

The Bank has offset the following assets and liabilities.

As at 31 Dec 2022	Gross amount before offsetting in the statement of financial position	Offsetting	Net exposure presented in the statement of financial position	Related arrangements not set off in the statement of financial position: Financial instruments	Related arrangements not set off in the statement of financial position: Cash collateral received	Net amounts
Assets						
Derivatives	40	0	40	0	0	0
Liabilities						
Derivatives	3,850	0	3,850	0	0	0
As at 31 Dec 2021						
Assets						
Derivatives	4	0	4	0	0	0
Liabilities						
Derivatives	157	0	157	0	0	0

NOTE 4 Net interest income

Net interest income

EUR thousand	Note	2022	2021
Interest income using effective interest calculation			
Corporate loans		78,909	62,213
incl. loans to related parties	20	78	54
incl. stage 3 interest*		63	303
Hire purchase		3,338	3,409
Consumer loans		9,607	8,156
Leveraged loans and lending of securities		1,629	1,742
Credit card loans		836	834
From balances with credit institutions and investment companies		3,664	281
Mortgage loans		28,144	21,441
incl. loans to related parties	20	42	41
Private loans		2,450	2,299
incl. loans to related parties	20	7	6
From balances with central bank		8,594	2,283
Other loans		8,821	16,332
Subtotal		**145,992**	**118,990**
Other similar interest income			
Leasing		6,407	6,000
incl. leases to related parties	20	11	9
From debt securities		-231	-353
incl. debt securities at fair value through profit or loss	8	-342	-353
Subtotal		**6,176**	**5,647**
Total		**152,168**	**124,637**
Interest expense			
Deposits from customers and loans received		-5,696	-5,245
From balances with central bank		-7,661	-14,171
Subordinated debt	16, 20	-9,322	-7,557
Total		**-22,679**	**-26,973**
Net interest income		**129,489**	**97,664**

Interest income of loans by customer location (interest from bank balances and debt securities not included):

Estonia	140,141	121,461
United Kingdom	0	965
Total	**140,141**	**122,426**

*As most of the stage 3 loans are sold to debt collectors, the stage 3 interests are marginal in all loan portfolios except corporate loans.

NOTE 5 Net fee and commission income

Fee and commission income

EUR thousand	Note	2022	2021
Security brokerage and commission fees		4,329	6,159
Asset management and related fees		5,807	5,354
Currency exchange fees		8,462	8,617
Fees from cards and settlements		27,498	23,635
Other fee and commission income		6,793	4,946
Total	23	**52,889**	**48,711**
Fee and commission expense			
Security brokerage and commission fees paid		-2,386	-1,856
Expenses related to cards		-6,312	-5,904
Expenses related to card payments		-7,344	-7,104
Fees related to consumer loans and hire-purchase paid		-830	-667
Other fee expense		-3,609	-2,007
Total	23	**-20,481**	**-17,538**
Net fee and commission income	23	**32,408**	**31,173**

Fee and commission income by customer location:	2022	2021
Estonia	45,537	41,414
United Kingdom	7,352	7,297
Total	**52,889**	**48,711**

NOTE 6 Operating expenses

EUR thousand	2022	2021
Wages, salaries and bonuses	27,654	20,356
Social security and other taxes*	8,475	6,365
Total staff costs	**36,129**	**26,721**
IT expenses	4,943	3,890
Information services and banking services	1,297	1,288
Marketing expenses	2,583	1,936
Office expenses	1,358	815
Transportation and communication costs	492	292
Training and travelling expenses of employees	1,073	407
Other outsourced services	5,343	3,452
Other administrative expenses	6,964	6,749
Depreciation and amortisation	3,091	2,668
Rental payments	293	526
Other operating expenses	979	596
Total other operating expenses	**28,416**	**22,619**
Total operating expenses	**64,545**	**49,340**

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

The average number of employees working for the Group in 2022 was 710 (2021: 573).

NOTE 7 Due from central bank, credit institutions and investment companies

EUR thousand	31 Dec 2022	31 Dec 2021
Demand and term deposits with maturity of less than 3 months*	88,276	112,649
Statutory reserve capital at central bank	48,689	57,298
Demand deposit from central banks*	2,342,275	3,816,986
Total	**2,479,240**	**3,986,933**
*cash and cash equivalents in the statement of cash flows	2,430,551	3,929,635

Mandatory banking reserve as at 31 Dec 2022 was 1% (2021: 1%) of all financial resources collected (deposits from customers and loans received). The reserve requirement is to be fulfilled as a monthly average in euros or in the foreign securities preapproved by the central bank.

NOTE 8 Investments in debt and equity securities

Mandatory measurement as fair value through profit or loss

EUR thousand	31 Dec 2022	31 Dec 2021
Shares and fund units	367	367
Debt securities	0	127,349
Foreign exchange forwards	40	4
Total financial assets	**407**	**127,720**
Interest rate swaps and foreign exchange forwards	3,850	157
Total financial liabilities	**3,850**	**157**

Financial assets at fair value through profit or loss 1 Jan 2021	**322,930**
Net changes of investment securities at fair value through profit or loss	-193,852
Negative interest income (Note 5)	-353
Revaluation	-1,005
Financial assets at fair value through profit or loss 31 Dec 2021	**127,720**
Net changes of investment securities at fair value through profit or loss	334,516
Negative interest income (Note 5)	-231
Revaluation	2,429
Reclassification	-464,027
Financial assets at fair value through profit or loss 31 Dec 2022	**407**

Investments in debt and equity securities measured at amortised cost

EUR thousand	
Financial assets at amortised cost 1 Jan 2022	**0**
Reclassification	464,027
Net change in investment securities measured at amortised cost	-99,706
Impairment	-91
Financial assets at amortised cost 31 Dec 2022	**364,230**

Bid price is the fair value of investments in the case of publicly listed securities. In 2022, a loss of EUR 1,475 thousand (2021: EUR 1,142 thousand) was recognised on the revaluation of bonds. Loss was obtained from the revaluation of interest rate swaps in 2022 and in 2021. Interest income from bonds is recognised in interest income.

NOTE 9 Loans and advances to customers

EUR thousand	31 Dec 2022	31 Dec 2021
Loans to legal entities	**1,959,052**	**1,683,891**
incl. corporate loans	1,725,720	1,469,216
incl. leasing	121,015	111,001
incl. overdraft	36,686	32,327
incl. trade finance	36,255	37,162
incl. leveraged loans	3,679	5,304
incl. credit cards and hire-purchase	747	570
incl. apartment association loans	18,273	10,929
incl. factoring	16,677	17,382
Loans to individuals	**1,248,514**	**1,012,318**
incl. hire-purchase	15,824	13,081
incl. mortgage loans	1,049,386	840,736
incl. consumer loans	77,119	56,936
incl. private loans	52,801	49,683
incl. leasing	31,678	30,127
incl. leveraged loans	6,857	9,008
incl. credit card loans	8,933	7,540
incl. overdraft	25	19
incl. study loan	2,559	1,213
incl. real estate leasing	3,332	3,975
Total	**3,207,566**	**2,696,209**
incl. related parties (Note 20)	5,815	6,047
Allowance for credit loss	-20,577	-19,049
Total	**3,186,989**	**2,677,160**

In 2022, the average effective interest rate of new consumer loans issued to individuals was 16.05%. The average effective interest rate for hire-purchase was around 24.8%, credit cards 17.85% and leasing 4.31%. The contractual interest rate of leveraged loans issued to individuals is generally equal to their effective interest rate because no other significant fees have been received upon their issue.

Changes in impairments *EUR thousand*	Balance as at 1 January	Impairment provisions / reversals set up during the year	Written off during the reporting period	Balance as at 31 December
Corporate Lending	-15,288	-5,361	5,214	-15,435
Consumer Financing	-1,319	-2,092	1,304	-2,107
Investment Financing	-130	-8	125	-13
Leasing	-1,250	-1,204	446	-2,008
Private Lending	-1,062	-593	641	-1,014
Total 2022	**-19,049**	**-9,258**	**7,730**	**-20,577**
Corporate Lending	-13,449	-9,706	7,867	-15,288
Consumer Financing	-1,178	-1,318	1,176	-1,320
Investment Financing	-25	-130	26	-129
Leasing	-1,385	-1,226	1,361	-1,250
Private Lending	-821	-707	466	-1,062
Total 2021	**-16,858**	**-13,087**	**10,896**	**-19,049**

Impairment losses accumulated during the year differ from the amount of impairment losses recognised in the statement of profit or loss by the amounts which were written off as uncollectible in earlier periods but collected during the reporting period. These receipts were recorded among impairment losses in the statement of profit or loss.

For credit risk exposures and loan collateral, see Risk management section 2.4.4. Distribution of loans granted by currencies is disclosed in Risk management section 3.1.
Distribution of loans granted by maturity is disclosed in Risk management section 4
The geographical distribution of loans granted is disclosed in Risk management section 2.3.1.
For interest income on loans granted, see Note 4.

NOTE 10 Receivables from customers

EUR thousand	31 Dec 2022	31 Dec 2021
Asset management fees from customers	607	738
Other fees for providing services to customers	8,612	981
Payments in transit	34	1,251
Total	**9,253**	**2,970**

All fees, other than receivables related to collection of receivables, are receivable within 12 months of the end of the reporting period and are considered as current asset.

NOTE 11 Other assets

EUR thousand	31 Dec 2022	31 Dec 2021
Financial assets		
Guarantee deposits of Baltic stock exchanges	24	17
Guarantee deposits of VISA and MasterCard	100	2,219
Subtotal	**124**	**2,236**
Non-financial assets		
Prepayments to Financial Supervision Authority	1,020	829
Other prepayments*	1,846	1,617
Subtotal	2,866	2,446
Total	**2,990**	**4,682**

* Prepayments include office rent, insurance, periodicals and training

Prepayments are expected to be received or used within 12 months of the end of the reporting period and are therefore considered current assets. Guarantee deposits on the Baltic stock exchanges are held to guarantee securities trading activity on the stock exchanges of Tallinn, Riga and Vilnius and the deposits of VISA (2021 also MasterCard) to guarantee credit card transactions and should therefore both be considered non-current assets.

NOTE 12 Tangible and intangible assets

EUR thousand	Tangible assets	Right-of-use assets	Total tangible assets	Intangible assets	Total
Balance as at 31 Dec 2020					
Cost	6,691	5,446	12,137	4,600	16,737
Accumulated depreciation and amortisation	-3,925	-1,641	-5,566	-3,793	-9,359
Carrying amount 31 Dec 2020	**2,766**	**3,805**	**6,571**	**807**	**7,378**
Changes in 2020:					
Purchase of non-current assets	2,251	992	3,243	1,496	4,739
Write-off of non-current assets	0	-67	-67	-807	-874
Depreciation/amortisation charge	-835	-773	-1,608	-1,060	-2,668
Balance as at 31 Dec 2021					
Cost	8,942	6,438	15,380	5,289	20,669
Accumulated depreciation and amortisation	-4,760	-2,481	-7,241	-4,046	-11,287
Carrying amount 31 Dec 2021	**4,182**	**3,957**	**8,139**	**1,243**	**9,382**
Purchase of non-current assets	4,851	131	4,982	2,568	7,550
Write-off of non-current assets	0	0	0	-352	-352
Depreciation/amortisation charge	-1,086	-1,075	-2,161	-930	-3,091
Balance as at 31 Dec 2022					
Cost	13,793	6,569	20,362	7,505	27,867
Accumulated depreciation and amortisation	-5,846	-3,556	-9,402	-4,624	-14,026
Carrying amount 31 Dec 2022	**7,947**	**3,013**	**10,960**	**2,881**	**13,841**

Tangible assets include computer technology and office equipment, furniture, capitalised costs of office renovation. Intangible assets include licenses, client contracts and development costs. In 2022 and 2021, there was no indication of impairment of tangible and intangible assets.

NOTE 13 Deposits from customers and loans received

31 Dec 2022

EUR thousand	Individuals	Financial entities	Non-financial entities	Public sector	Total
Demand deposits	1,065,135	1,533,598	2,042,117	58,406	4,699,256
Term deposits	63,208	23,046	146,137	24,587	256,978
Accrued interest liability	336	192	156	13	697
Total	**1,128,679**	**1,556,836**	**2,188,410**	**83,006**	**4,956,931**
incl. related parties (Note 20)	2,369	0	61,809	0	64,178

31 Dec 2021

EUR thousand	Individuals	Financial entities	Non-financial entities	Public sector	Total
Demand deposits	1,005,757	2,512,958	2,008,349	161,510	5,688,574
Term deposits	39,209	15,679	81,808	22,587	159,283
Accrued interest liability	285	-1,537	-5	2	-1,255
Total	**1,045,251**	**2,527,100**	**2,090,152**	**184,099**	**5,846,602**
incl. related parties (Note 20)	2,349	0	28,290	0	30,639

	31 Dec 2022		**31 Dec 2021**	
EUR thousand	Loan principal	Accrued interest	Loan principal	Accrued interest
Debt securities in issue	133,771	953	99,633	310
Covered bonds	249,284	141	248,980	140
Total	**383,055**	**1,094**	**348,613**	**450**

	31 Dec 2022		**31 Dec 2021**	
EUR thousand	Loan principal	Accrued interest	Loan principal	Accrued interest
Received loan from central banks (TLTRO)	150,000	-2,159	200,000	-2,539
Total	**150,000**	**-2,159**	**200,000**	**-2,539**

The nominal interest rates of most deposits from customers and loans received equal their effective interest rates as no other significant fees have been paid.

Distribution of deposits from customers and loans received by currency is presented in Risk management section point 3.1.

Distribution of deposits from customers and loans received by maturity is presented in Risk management section 4.

Distribution of deposits from customers and loans received by geography and risk concentration is presented in Risk management section 2.3.1.

NOTE 14 Accounts payable and other liabilities

EUR thousand	31 Dec 2022	31 Dec 2021
Financial liabilities		
Trade payables	991	2,682
Other short-term financial liabilities	10,676	6,904
Lease liabilities	1,842	3,266
Payments in transit	40,101	27,202
Financial guarantee contracts issued	1,228	1,101
Subtotal	**54,838**	**41,155**
Non-financial liabilities		
Prepaid expenses	736	816
Performance guarantee contracts issued	1,058	543
Tax liabilities	2,417	1,908
Payables to employees	2,852	2,194
Subtotal	**7,063**	**5,461**
Total	**61,901**	**46,616**

Payables to employees consist of unpaid salaries; bonus accruals and vacation pay accrual for the reporting period and the increase in liabilities is caused by the increase in the number of employees during the year. Payments in transit consist of foreign payments and payables to customers related to intermediation of securities transactions, for which the customer's current account have been debited. All liabilities, except for financial guarantees, are payable within 12 months and are therefore recognised as current liabilities. Income tax payable on dividends expected to be paid out in the next financial year in the amount of EUR 1,032 thousand (2021: 1,184 thousand) has been included in other short term financial liabilities.

NOTE 15 Right-of-use assets and lease liabilities

The Group leases office premises. From 1 January 2019, leases are recognised as a right-of-use asset and a corresponding liability from the date when the leased asset becomes available for use by the Group. All lease agreements are cancellable upon the consent of both parties.

The Group's total assets in the statement of financial position as at 31 Dec 2022 is EUR 3,013 thousand (31 Dec 2021: 3,957 thousand) and the liability is EUR 1,842 thousand (31 Dec 2021: 3,266 thousand). The right-of-use assets balance as of 31 December 2022 is disclosed in the Note 10. The lease liability is disclosed in the Note 14. Interest expense on lease liabilities in 2022 was EUR 89 thousand (2021: 101 thousand) and the depreciation of the right of use assets was EUR 1,075 thousand (2021: 840 thousand) (Note 12). The repayments of principal of lease liabilities in 2022 were EUR 1,423 thousand (2021: 963 thousand).

NOTE 16 Subordinated debt

The Group has received subordinated debts in order to increase long-term capital. In the case of default of the Group, the subordinated debts are repayable after all other debts have been paid, but before debts to shareholders are paid.

Subordinated bonds issued in 2016 in the amount of EUR 5,000 thousand were redeemed in 2022.

In 2017, no subordinated bonds were issued or redeemed.

In December 2018, subordinated bonds were issued totalling EUR 10 000 thousand carrying a rate of interest at 6.50%. The due date of the bonds is 20.12.2028.

In June 2019, subordinated bonds were issued totalling EUR 20,500 thousand (due date 29.06.2029) and in October 2019 totalling EUR 5,000 thousand (due date 29.10.2029), both carrying a rate of interest at 6.50%.

In September 2020, subordinated bonds were issued totalling EUR 10,000 thousand (due date 30.09.2030) carrying a rate of interest at 7.0%.

In February 2022, subordinated bonds were issued totalling EUR 15,000 thousand (due date 27.02.2032) carrying a rate of interest at 6.0%.

In 2019 Tier 1 subordinated loans were issued totalling EUR 23,000 thousand carrying a rate of interest at 9.50%.

In 2020 Tier 1 subordinated loans were issued totalling EUR 15,000 thousand carrying a rate of interest at 9.50%.

In 2022 Tier 1 subordinated loans were issued totalling EUR 15,000 thousand carrying a rate of interest at 11.50%.

The balances of subordinated debt as at the end of each reporting period is disclosed in the table below. Interest liabilities are accounted in the statement of financial position using the effective interest rate.

Subordinated debt
EUR thousand

Subordinated debt as at 1 Jan 2021	**88,500**
Subordinated debt as at 31 Dec 2021	**88,500**
Subordinated bonds issued	30,000
Subordinated bonds redeemed	-5,000
Subordinated debt as at 31 Dec 2022	**113,500**

Interest expenses on subordinated bonds for each reporting period and accrued interest liabilities as at the end of each reporting period is disclosed in the table below.

Interest liability from subordinated debt
EUR thousand

Accrued interest on subordinated debt as at 1 Jan 2021	**489**
Interest calculated for 2021 (Note 5)	6,942
Paid out during 2021	-6,942
Accrued interest on subordinated debt as at 31 Dec 2021	**489**
Interest calculated for 2022 (Note 5)	9,322
Paid out during 2022	-9,255
Accrued interest on subordinated debt as at 31 Dec 2022	**556**

NOTE 17 Shareholders' equity in the public limited company

The sole shareholder of the Group is a company registered in Estonia, AS LHV Group. Rain Lõhmus who owns 21.8% of the voting rights and Andres Viisemann who owns 11.3% of the voting rights in AS LHV Group have significant influence over the company (31 December 2021: 22.7% and 9.6%, respectively). According to the Company's articles of association, the minimum share capital is EUR 25 million and the maximum share capital is EUR 100 million (at 31 December 2021: EUR 25 million and EUR 100 million, respectively). The share capital is paid in full through cash contributions. In 2022, the share capital of AS LHV Pank was increased by EUR 30 million and in 2021 by EUR 5 million through a cash contribution by the sole shareholder AS LHV Group. The Bank's share capital increased to EUR 141.5 million by the year-end 2022.

As at 31 Dec 2022, the adjusted unconsolidated retained earnings of the Group amounted to EUR 231,805 thousand (31 December 2021: EUR 156,690 thousand). Thus, as at 31 December 2022 it is possible to pay out dividends in amount EUR 185,653 thousand (2021: EUR 125,556 thousand) and the related income tax charge would be EUR 46,152 thousand (2021: EUR 31,134 thousand). If the dividends were to be paid, the Group's capital adequacy would remain compliant.

Transactions with share capital

	31 Dec 2022	31 Dec 2021
Share capital	**141,500**	**111,500**
Number of shares	141,500,000	111,500,000
Par value of a share	1 EUR	1 EUR

In 2014, the General Meeting of shareholders of AS LHV Group approved the criteria for the granting of share options to the Management Board members and equivalent employees and department managers and equivalent employees of group companies that are part of AS LHV Group. The aim of issuing share options is to align the interests of Management Board members and employees more effectively with the interests of shareholders and customers. Another objective is to offer a system of compensation on the labour market that is equal to competitors and comprehensive. The share options were issued in 2021 and in 2022.

In 2022, share options were granted to six members of the Management Board of AS LHV Pank and to one member of Management Board of subsidiary AS LHV Finance; and 132 employees of the group in the total amount of EUR 5,172 thousand.

In 2021, share options were granted to six members of the Management Board of AS LHV Pank and 119 employees in the total amount of EUR 2,764 thousand.

The company entered into share option agreements with the members of the Management Board and employees for a three-year term for the granting of share options. Share options can be exercised after the expiry of a three-year period.

Share options issued in 2016 were exercised in 2019, when shares with nominal value of EUR 1 could be acquired for EUR 3.0 per share. In total, the former and current employees of the Group subscribed for 195,703 shares.

Share options issued in 2017 were exercised in 2020, when shares with nominal value of EUR 1 could be acquired for EUR 4.65 per share. In total, the former and current employees of the Group subscribed for 279,362 shares.

Share options issued in 2018 were exercised in 2021, when shares with nominal value of EUR 1 could be acquired for EUR 5.33 per share.

Share options issued in 2019 were exercised in 2022, when shares with nominal value of EUR 1 could be acquired for EUR 4.90 per share. All the options were exercised before the share split.

Share options issued in 2020 can be exercised between the period of 01.04.2023-30.04.2023 and shares with nominal value of EUR 1 can be acquired for EUR 0.596 per share.

Share options issued in 2021 can be exercised between the period of 01.04.2024-30.04.2024 and shares with nominal value of EUR 1 can be acquired for EUR 0.923 per share.

Share options issued in 2022 can be exercised between the period of 01.04.2025-30.04.2025 and shares with nominal value of EUR 1 can be acquired for EUR 2.182 per share.

Legal reserve in equity is composed of:

EUR thousand	
Legal reserve as at 1 Jan 2021	**4,022**
Transferred from 2020 net profit	1,626
Legal reserve as at 31 Dec 2021	**5,648**
Transferred from 2021 net profit	3,088
Legal reserve as at 31 Dec 2022	**8,736**

NOTE 18 Assets under management

AS LHV Pank, operating as an account manager for its customers, has custody of or intermediates the following customer assets

EUR thousand	31 Dec 2022	31 Dec 2021
Cash balance of customers	13,609	3,806
Securities of customers	3,194,837	3,599,285
incl. parent company (Note 20)	149,279	206,700
incl. shareholders of the parent company and related entities (Note 20)	483,452	660,351
Total	**3,208,446**	**3,603,091**

Asset management fees for the management of these assets have been in the range of 0.01 – 0.02 % p.a. (for respective income, see Note 5).

The monetary funds of the customers who use the platform of an active securities trader or the trading system LHV Trader offered by the Bank, have been recognised as off-balance sheet assets. Due to the nature of the system, the Bank has deposited these funds in personalised accounts with its partner and as the monetary funds of these customers are not used for business purposes by the Bank (they cannot be lent to other customers or used as collateral); therefore the monetary funds are recognised as off-balance sheet assets. The Bank earns commission and interest income on intermediation of transactions in these accounts similarly to customers' accounts reflected in the Group's financial statement. The Bank has provided contractual guarantees to its partner in respect of LHV Trader accounts, guaranteeing potential losses to be incurred from financing of the transactions executed by customers intermediated by itself (leveraging), with the primary collateral being the securities used as collateral for leveraged loans. The customer has similar guarantee to the Bank and therefore, the Bank has in substance transferred the guarantee to end customer. To avoid potential losses, the Bank has a daily practice to monitor the potential decrease of collateral and deficiency of customer accounts. In its current practice, no such losses in respect of which the guarantee provided by the Bank would apply have incurred and the Bank has not paid any compensation relating to the guarantee.

NOTE 19 Contingent assets and liabilities

Non-cancellable transactions *EUR thousand*	Performance guarantees	Financial guarantees	Letters of credit	Unused loan commitments	Total
Liability in contractual amount as at 31 December 2022	30,174	52,577	6,605	601,093	**690,449**
Liability in contractual amount as at 31 December 2021	19,919	49,409	1,438	679,579	**750,345**

Income tax from potential future dividends is disclosed in Note 17.

Financial guarantees and unused loan commitments are subject to ECL requirements of IFRS 9, see also note Risk management section point 2 for more information.

Tax authorities have the right to review the company's tax records for up to 5 years after submitting the tax declaration and upon finding errors, impose additional taxes, interest and fines. The tax authorities have not performed any tax audits at the Group during 2021-2022. The Group's management estimates that in 2023 there are no such circumstances which may lead the tax authorities to impose significant additional taxes on the Group.

Performance guarantees are contracts that provide compensation if another party fails to perform a contractual obligation. Such contracts do not transfer credit risk. The risk under performance guarantee contracts is the possibility that the insured event (i.e., the failure to perform the contractual obligation by another party) occurs. The key risks the Group faces are significant fluctuations in the frequency and severity of payments incurred on such contracts relative to expectations. The Group uses historical data and statistical techniques to predict levels of such payments. Claims must be made before the contract matures and most claims are settled within short term. This allows the Group to achieve a high degree of certainty about the estimated payments and therefore future cash flows. The Group manages such risks by constantly monitoring the level of payments for such products and has the ability to adjust its fees in the future to reflect any change in claim payments experience. The Group has a claim payment requests handling process, which includes the right to review the claim and reject fraudulent or non-compliant requests. The exposure and concentration of performance guarantees is as follows:

Breakdown by economic sectors

EUR thousand	31 Dec 2022	31 Dec 2021
Construction	19,123	11,404
Water and utilities	4,180	3,186
Manufacturing	3,021	2,758
Administrative activities	715	691
Professional, scientific and technical activities	553	651
Other areas at activities	2,582	1,229
Total	**30,174**	**19,919**

Breakdown by internal ratings

EUR thousand		
5 low credit risk	1,361	1,141
6 low credit risk	1,973	898
7 medium credit risk	6,161	5,127
8 medium credit risk	5,574	7,648
9 heightened credit risk	9,852	1,309
10 high credit risk	151	671
11 high credit risk	730	0
12 non-satisfactory rating	1,616	0
13 insolvent	0	214
Non-rated	2,756	2,911
Total	**30,174**	**19,919**

Performance guarantees are over-collateralised as at each reporting date. Therefore, the Group has not borne any losses from performance guarantee contracts neither in 2022 nor in previous period.

NOTE 20 Transactions with related parties

In preparing the consolidated financial statements of AS LHV Pank, the following entities have been considered related parties:

- owners that have significant impact on the Group and the entities related to them;
- members of the Management Board and legal entities controlled by them (together referred to as management);
- members of the Supervisory Board;
- close relatives of the persons mentioned above and the entities related to them.

Transactions	Note	2022	2021
Interest income	5	**178**	**144**
incl. management		42	63
Interest expenses	5	**9,270**	**6,969**
incl. management		5	7
incl. parent company		9,234	6,942
incl. shareholders, their related entities and close relatives that have significant influence		31	20
Fee and commission income	6	**88**	**12**
incl. management		5	7
incl. shareholders, their related entities and close relatives that have significant influence		83	5

Balances	Note	31 Dec 2022	31 Dec 2021
Loans and receivables	11	**7,570**	**6,047**
incl. management		3,928	2,887
incl. shareholders, their related entities and close relatives that have significant influence		3,642	3,160
Deposits		**64,178**	**30,639**
incl. management	15	765	788
incl. parent company	18	29,684	16,941
incl. shareholders, their related entities and close relatives that have significant influence	15	33,729	12,910

The table provides an overview of the material balances and transactions involving related parties. All transactions involving the close relatives and the entities related to members of the Management Board and Supervisory Board and the minority shareholders of the parent company AS LHV Group have occurred in the course and on the terms of ordinary business.

As at 31 Dec 2022 and 31 Dec 2021, the management did not have term deposits and the interest rate on demand deposits corresponds to the terms applicable to customers.

The subordinated debt received in 2018-2019 have the interest rate of 6.5%. The subordinated debt received in 2020 has the interest rate of 7.0%. The subordinated debt received in 2022 has the interest rate of 6.0%. Tier 1 subordinated debt received 2019 and 2020 have the interest rate of 9.5%. %. Tier 1 subordinated debt received 2022 has the interest rate of 11.5%.

The interest rate of all subordinated debts is the same as the parent company is paying on its own subordinated loans received from third parties and deposited the funds at the Bank.

In 2022, salaries and other compensations paid to the management of LHV totalled EUR 1,368 thousand (2021: EUR 984 thousand), including all taxes. The Management Board of the Bank has six members and The Management Board of the subsidiary has one member.

As at 31 Dec 2022, the remuneration for December and accrued holiday pay in the amount of EUR 85 thousand (as at 31 Dec 2021: EUR 51 thousand) is reported as a payable to management (Note 14). The Group did not have any long-term payables or commitments to the members of the Management Board and the Supervisory Board as at 31 Dec 2022 and 31 Dec 2021 (pension liabilities, termination benefits, etc.). In 2022 and 2021, no remuneration was paid to the members of the Supervisory Board.

The Group has signed contracts with the members of the Management Board, which do not provide for severance benefits upon termination of the contract. In any matters not regulated by the contract, the parties adhere to the procedure specified in the legislation of the Republic of Estonia. Information on assets of related parties held as an account manager is presented in Note 18.

NOTE 21 Subsidiaries

As at 31 Dec 2022 and 31 Dec 2021, the Bank has one subsidiary that has been consolidated in these financial statements:

- AS LHV Finance (ownership interest 65%)

AS LHV Pank paid in 2013 EUR 325 thousand of monetary contribution for 65% ownership in LHV Finance and a non-controlling interest paid EUR 175 thousand of monetary contribution for 35% ownership.

The contribution of the non-controlling interest has been reflected in the consolidated statement of financial position on the line „Non-controlling interest".

Set out below is the summarised financial information for the subsidiary. The information disclosed is the amount before inter-company eliminations.

Summarised statement of financial position

	AS LHV Finance	
EUR thousand	31 Dec 2022	31 Dec 2021
Loans and advances to customers and other current assets	91,591	69,079
Non-current assets	120	10
Current liabilities	2,297	1,968
Non-current liabilities	70,495	48,449
Total net assets	**18,919**	**18,672**

Summarised statement of profit or loss and other comprehensive income

Net interest and fee and commission income	10,439	9,887
Profit before income tax	7,288	7,726
Income tax expense	-1,107	-1,184
Net profit	**6,181**	**6,542**
Total comprehensive income	6,181	6,542
Profit and other comprehensive income allocated to non-controlling interests	2,217	2,291

Summarised statement of cash flows

Cash flows from operating activities	-12,284	6,494
Interest paid	-2,407	-1,797
Income tax paid	-1,107	-1,184
Net cash from/ (used in) operating activities	-15,798	3,513
Net cash from/ (used in) investing activities	-134	0
Net cash from/ (used in) financing activities	15,932	-3,515
Net increase/(decrease) in cash and cash equivalents	**0**	**-2**
Cash and cash equivalents at the beginning of the year	0	2
Cash and cash equivalents at the end of the year	**0**	**0**

NOTE 22 Income tax expense

The Bank is calculating 14% advance income tax. Advance corporate income tax for the year 2022 was EUR 12,305 thousand (2021: EUR 9,338 thousand).

EUR thousand	2022	2021
Advance corporate income tax	12,305	9,338
Corporate income tax	955	1,219
Total income tax expense	**13,260**	**10,557**

The Bank has paid advance corporate income tax in the amount of EUR 17,471 thousand (2021: 6,941 thousand) in total, which has been recoded as an expense in the income statement.

NOTE 23 Operating segments

Bank divides its business activities by 4 main business segments: retail banking, corporate banking, hire purchase and consumer finance, and financial intermediates. The business segments form LHV Pank, with a separate access to financial data and which are subject to regular monitoring of operating result by the Group's chief decision-maker. The full planning and KPI setting is done on the segment level. For each segment, a full statement of financial position and statement of profit or loss is prepared. In addition to the segment level, the Group carries out planning/measurement on the department level.

Grouping is done based on the client/product base, where similar departments are grouped under one segment. The retail banking segment covers services to private individuals and small legal entities with a credit exposure under EUR 500 thousand. This is a regular universal banking segment offering payments, cards, credit, etc.

The corporate banking segment covers all corporate customers and other legal entities with credit exposure over EUR 500 thousand. The main products are credits and payments.

The hire-purchase and consumer finance segment covers the activities of LHV Finance that offers hire purchase and consumer finance services to private individuals in Estonia.

The financial intermediaries segment covers services to fintech companies with a large volume of payments both in Estonia and in the United Kingdom. LHV's regular payment services are also reported in that segment.

Other activities include treasury activities through providing internal bank function to segments. Assets and liabilities are disclosed in a way how it is reported to the management of the Bank, i.e. the treasury function investments and funding are allocated to other segments, but some of the interest income and expense are allocated to treasury. That part is eliminated through intra-group eliminations.

The management board of AS LHV Pank has been designated as the chief decision-maker responsible for allocation of funds and assessment of the profitability of the business activities. The result reported by a segment includes revenue and expenditure directly related to the segment.

The revenue reported by a segment is based on the revenue recorded in the financial statements and includes gains from transactions between the segments such as loans granted by AS LHV Pank to other group companies. The breakdown of interest income and fee and commission income by customer location is presented in Notes 4 and 5. The Group does not have any customers, whose income would account for more than 10% of the corresponding type of revenue.

31 Dec 2022 *EUR thousand*	Retail banking	Corporate banking	Hire-purchase and consumer finance	Financial intermediates	Other activities	Total
Interest income	53,531	74,998	12,945	8,276	2,418	152,168
Interest expense	0	-16,918	-2,521	0	-3,240	-22,679
Net interest income	**53,531**	**58,080**	**10,424**	**8,276**	**-822**	**129,489**
Fee and commission income	9,356	2,573	845	39,326	789	52,889
Fee and commission expense	-2,361	-59	-830	-14,935	-2,296	-20,481
Net fee and commission income	**6,995**	**2,514**	**15**	**24,391**	**-1,507**	**32,408**
Net gains from financial assets	**-357**	**0**	**0**	**-24**	**-41**	**-422**
Net other income	**8**	**105**	**0**	**-27**	**113**	**199**
Net income	**60,177**	**60,699**	**10,439**	**32,616**	**-2,257**	**161,674**
Administrative and other operating expenses, staff costs	-21,169	-12,574	-2,241	-20,834	-7,727	-64,545
Operating profit	**39,008**	**48,125**	**8,198**	**11,782**	**-9,984**	**97,129**
Impairment losses on loans and advances	-1,467	-472	-910	-53	-94	-2,996
Income tax	-4,365	-4,871	-1,107	-1,634	-1,283	-13,260
Net profit for the reporting period	**33,176**	**42,782**	**6,181**	**10,095**	**-11,361**	**80,873**
Total assets as at 31 Dec 2022	**2,840,041**	**3,201,314**	**91,711**	**0**	**-76,116**	**6,056,950**
Total liabilities as at 31 Dec 2022	**3,702,964**	**482,009**	**72,792**	**1,485,722**	**-74,759**	**5,668,728**

31 Dec 2021 *EUR thousand*	Retail banking	Corporate banking	Hire-purchase and consumer finance	Financial intermediates	Other activities	Total
Interest income	36,226	59,564	11,577	5,107	12,163	124,637
Interest expense	-1,066	-10,172	-1,791	0	-13,944	-26,973
Net interest income	**35,160**	**49,392**	**9,786**	**5,107**	**-1,781**	**97,664**
Fee and commission income	10,003	2,515	768	34,647	778	48,711
Fee and commission expense	-1,831	-354	-667	-14,946	260	-17,538
Net fee and commission income	**8,172**	**2,161**	**101**	**19,701**	**1,038**	**31,173**
Net gains from financial assets	**-97**	**0**	**0**	**-436**	**-1,008**	**-1,541**
Net other income	**15**	**397**	**0**	**96**	**91**	**599**
Net income	**43,250**	**51,950**	**9,887**	**24,468**	**-1,660**	**127,895**
Administrative and other operating expenses, staff costs	-15,788	-9,853	-1,868	-14,732	-7,099	-49,340
Operating profit	**27,462**	**42,097**	**8,019**	**9,736**	**-8,759**	**78,555**
Impairment losses on loans and advances	-475	-3,110	-293	-43	-27	-3,948
Income tax	-3,120	-4,544	-1,184	-1,670	-39	-10,557
Net profit for the reporting period	**23,867**	**34,443**	**6,542**	**8,023**	**-8,825**	**64,050**
Total assets as at 31 Dec 2021	**2,885,760**	**3,905,861**	**69,089**	**0**	**-51,863**	**6,808,847**
Total liabilities as at 31 Dec 2021	**3,297,057**	**711,642**	**50,417**	**2,520,127**	**-50,355**	**6,528,888**

NOTE 24 Separate primary financial statements of parent company

In accordance with the Estonian Accounting Act, information on the separate primary financial statements of the parent of the consolidation group shall be disclosed in the notes to the consolidated financial statements.

Statement of profit or loss and other comprehensive income of the parent

EUR thousand	2022	2021
Interest income	141,744	114,851
Interest expense	-22,679	-26,973
Net interest income	**119,065**	**87,878**
Fee and commission income	52,044	47,943
Fee and commission expense	-19,651	-16,871
Net fee and commission income	**32,393**	**31,072**
Net gains from financial assets measured at fair value	2,071	2,385
Foreign exchange rate gains/losses	1,407	-26
Net gains from financial assets	**3,478**	**2,359**
Other income	2,456	2,893
Administrative and other operating expenses	-64,561	-49,766
Operating profit	**92,831**	**74,436**
Impairment losses on loans and advances and liquidity portfolio	-2,086	-3,655
Profit before income tax	**90,745**	**70,781**
Income tax expense	-12,305	-9,372
Net profit for the year	**78,440**	**61,409**
Total comprehensive income for the year	**78,440**	**61,409**

Statement of financial position of the parent

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Assets			
Due from central bank		2,390,964	3,874,284
Due from credit institutions		84,885	106,461
Due from investment companies		3,391	6,188
Financial assets at fair value through profit or loss		407	127,720
Financial assets measured at amortised cost		364,230	0
Loans and advances to customers		3,166,562	2,656,811
Receivables from customers and other financial assets		14,028	8,036
Other assets		2,842	2,423
Subsidiaries	21	325	325
Tangible fixed assets		7,947	4,182
Right-of-use assets		3,013	3,957
Intangible assets		2,761	1,233
Total assets		**6,041,355**	**6,791,620**
Liabilities			
Amounts owed to central banks (TLTRO)		147,841	197,461
Deposits from customers		4,956,931	5,846,602
Loans received		384,149	349,063
Financial liabilities at fair value through profit or loss		3,850	157
Accounts payable and other liabilities		62,026	43,287
Lease liability		1,842	3,266
Subordinated debt		114,056	88,989
Total liabilities		**5,670,695**	**6,528,825**
Equity			
Share capital	17	141,500	111,500
Legal reserve		8,736	5,648
Retained earnings		220,424	145,647
Total equity		**370,660**	**262,795**
Total liabilities and equity		**6,041,355**	**6,791,620**

Statement of cash flows of the parent

EUR thousand	Note	2022	2021
Cash flows from operating activities			
Interest received		138,723	114,871
Interest paid		-20,659	-29,533
Fees and commissions received		52,044	47,943
Fees and commissions paid		-19,651	-16,871
Other income received		2,456	2,893
Staff costs paid		-31,629	-24,599
Administrative and other operating expenses paid		-24,474	-19,300
Income tax paid		-10,532	-8,372
Cash flows from operating activities before change in operating assets and liabilities		**86,278**	**67,032**
Net increase/(decrease) in operating assets:			
Net acquisition/disposal of trading portfolio		-35	-140
Loans and advances to customers		-516,919	-473,990
Mandatory reserve at central bank		8,609	-16,045
Security deposits		2,112	-164
Other assets		-421	-515
Net increase/(decrease) in operating liabilities:			
Demand deposits of customers		-989,318	2,031,748
Term deposits of customers		97,695	-324,019
Net loans received (including loan repayments)		-49,535	-21,691
Subordinated loans received (senior bonds)		65,000	99,633
Subordinated loans repaid (senior bonds)		-31,000	0
Financial liabilities at fair value through profit or loss		3,693	-64
Other liabilities		11,997	22,965
Net cash from/ (used in) operating activities		**-1,311,844**	**1,384,750**
Cash flows from investing activities			
Purchase of tangible and intangible assets		-7,414	-4,673
Net changes of investment securities at fair value through profit or loss		-234,810	193,835
Net cash from/ (used in) investing activities		**-242,224**	**189,162**
Cash flows from financing activities			
Paid in share capital	17	30,000	5,000
Proceeds from subordinated debt	16	30,000	0
Subordinated debt redeemed	16	-5,000	0
Dividends paid		-3,900	-3,900
Dividends received		3,900	3,900
Repayment of principal of lease liabilities	15	-1,423	-1,254
Net cash from financing activities		**53,577**	**3,746**
Effect of exchange rate changes on cash and cash equivalents		**1 407**	**-26**
Net increase/ (decrease in cash and cash equivalents		**-1,499,084**	**1,577,632**
Cash and cash equivalents at the beginning of the financial year		**3,929,635**	**2,352,003**
Cash and cash equivalents at the end of the financial year		**2,430,551**	**3,929,635**

Statement of changes in shareholders' equity

EUR thousand	Share capital	Legal reserve	Retained earnings	Total
Balance as at 1 Jan 2021	**106,500**	**4,022**	**87,596**	**198,118**
Transferred into legal reserve	0	1,626	-1,626	0
Paid in share capital	5,000	0	0	5,000
Dividends paid	0	0	-3,900	-3,900
Share options	0	0	2,168	2,168
Net profit for the year	0	0	61,409	61,409
Total comprehensive income for 2021	0	0	61,409	61,409
Balance as at 31 Dec 2021	**111,500**	**5,648**	**145,647**	**262,795**
Carrying amount of holdings under control and significant influence	0	0	-325	-325
Value of holdings under control and significant influence under equity method	0	0	11,368	11,368
Adjusted unconsolidated equity as at 31 Dec 2021	**111,500**	**5,648**	**156,690**	**273,838**
Balance as at 1 Jan 2022	**111,500**	**5,648**	**145,647**	**262,795**
Transferred into legal reserve	0	3,088	-3,088	0
Paid in share capital	30,000	0	0	30,000
Dividends paid	0	0	-3,900	-3,900
Share options	0	0	3,325	3,325
Net profit for the year	0	0	78,440	78,440
Total comprehensive income for 2022	0	0	78,440	78,440
Balance as at 31 Dec 2022	**141,500**	**8,736**	**220,424**	**370,660**
Carrying amount of holdings under control and significant influence	0	0	-325	-325
Value of holdings under control and significant influence under equity method	0	0	11,706	11,706
Adjusted unconsolidated equity as at 31 Dec 2022	**141,500**	**8,736**	**231,805**	**382,041**

Adjusted unconsolidated equity is the maximum amount that can be distributed to shareholders' according to Estonian legislation.

Signatures of the Management Board to the consolidated annual report

The Management Board has prepared the management report and the consolidated financial statements of AS LHV Pank for the financial year ended 31 December 2022. The consolidated financial statements present a true and fair view of the Bank's consolidated financial position, the consolidated results of operations and its consolidated cash flows.

23 February 2023

Kadri Kiisel
Chairman of the Management Board
/signed digitally/

Andres Kitter
Member of the Management Board
/signed digitally/

Indrek Nuume
Member of the Management Board
/signed digitally/

Jüri Heero
Member of the Management Board
/signed digitally/

Meelis Paakspuu
Member of the Management Board
/signed digitally/

Martti Singi
Member of the Management Board
/signed digitally/

Independent auditor’s report

This page has been retained in Group annual report 2022 to maintain the structural logic of the report and to refer the reader to the location of the independent auditor’s report. The independent auditor’s report is available in the DigiDoc container named AS LHV Pank consolidated and audited annual report 2022.asice as a separate document. The auditor’s report is applicable and applies only to the signed original annual report, which is available as the file AS LHV Pank consolidated annual report 2022.asice in the same DigiDoc container as the independent auditor’s report and contains the report in the ESEF format (529900GJOSVHI055QR67-2022-12-31-EN.zip).

Proposal for profit distribution

The Management Board of AS LHV Pank proposes to the General Meeting of shareholders to distribute the profit of the financial year 2022 as follows:

- transfer EUR 3,933 thousand to legal reserve capital
- pay dividends EUR 2,275 thousand
- transfer the profit for reporting period attributable to shareholders of the parent in the amount of EUR 72,450 thousand to retained earnings.

Allocation of income according to EMTAK

Consolidated:

EMTAK	Activity	2022	2021
66121	Security and commodity contracts brokerage	10,136	11,513
64191	Credit institutions (banks) (granting loans)	188,514	155,835
64911	Finance lease	6,407	6,000
	Total income	**205,057**	**173,348**

EMTAK – Estonian classification of economic activities

Independent auditors' report

To the Shareholders of AS LHV Pank

(Translation of the Estonian original)

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of **AS LHV Pank** and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2022, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2022, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted in the European Union.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (Estonia). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Code of Ethics for Professional Accountants (Estonia) (including International Independence Standards), and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. We have determined the matter described below to be the key audit matter to be communicated in our report.

Impairment of loans and advances to customers	
Refer to Risk Management section, Summary of significant accounting policies, Note 2 "Significant management estimates and assumptions" and Note 9 "Loans and advances to customers".	
The key audit matter	**How the matter was addressed in our audit**
As at 31 December 2022, loans and advances to customers amounted to EUR 3 208 million and related impairment loss allowance amounted to EUR 20.6 million. We have focused on this area because of overall financial significance and the matter that measurement of expected credit losses (ECL) on financial instruments involves significant judgement. ECL calculations are forward looking and probability weighted accounting estimates. The key areas where we identified greater level of management judgement and therefore increased level of audit focus in the Group's ECL related accounting estimates: — Judgmental modelling is used to estimate ECL which involves determining the Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD). The PD models are the key drivers of complexity in the ECL and also impact the staging of relevant financial assets, and hence, are considered the most significant judgmental aspect of the Group's ECL modelling approach. — Economic scenarios – IFRS 9 requires the Group to measure ECL on an unbiased forward-looking basis reflecting a range of future economic conditions. Significant management judgement is applied in determining the economic scenarios used and the probability weights applied to them when considering the current uncertain economic environment. — For defaulted corporate loans, an individual impairment loss is calculated based on the exposure and realizable value of relevant collateral at the reporting date, and also requires significant accounting estimates.	In this area, we conducted, among others, the following audit procedures: We have assessed the Group's accounting policies and methodology applied for the calculation of impairment of loans and advances to customers in relation to the requirements of IFRS 9. We have performed end to end process walkthrough to identify key systems, applications and controls used in the ECL calculation process. We tested relevant manual, general IT and application controls over key systems used in ECL process. We have tested the design, implementation and operating effectiveness of the credit file periodic review, rating assessment and monitoring of collaterals for corporate loans. We have performed test of details over the following: • completeness and accuracy of data used in ECL calculation • compliance of key inputs used in ECL calculation with the IFRS 9 methodology • accuracy and compliance of 12-month and lifetime ECL calculations with IFRS 9 methodology • adequacy of discounting in the ECL model • accuracy and completeness of data used for staging loans • internal assignment of credit ratings to corporate exposures • adequacy of information about collaterals and their values • completeness of exposures of assets with impaired credit quality exposures and related ECL calculations. We have assessed the reasonableness of key assumptions made by the management, which serve as critical inputs in the ECL model, such as weights of different scenarios, loan portfolio point in time PD estimates, criteria to determine significant increase in credit risk, key forecasts of macroeconomic information and multipliers used for different scenarios. We also assessed adequacy and sufficiency of information disclosed in the Note "Risk Management " and Notes 2 and 9 in the consolidated financial statements.

Other Information

Management is responsible for the other information. The other information includes management report but does not include the consolidated financial statements and our auditors' report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. In addition, our responsibility is to state whether the information presented in the management report has been prepared in accordance with the applicable legal and regulatory requirements.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard and we state that the information presented in the management report is materially consistent with the consolidated financial statements and in accordance with the applicable legal and regulatory requirements.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards as adopted in the European Union, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (Estonia) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with International Standards on Auditing (Estonia), we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, then we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

Report on Compliance with the Requirements for iXBRL tagging of Consolidated Financial Statements included within the European Single Electronic Format Regulatory Technical Standard (ESEF RTS)

We have undertaken a reasonable assurance engagement on the iXBRL tagging of the consolidated financial statements included in the digital files 529900GJOSVHI055QR67-2022-12-31-EN.zip prepared by **AS LHV Pank**.

Responsibilities of Management for the Digital Files Prepared in Compliance with the ESEF RTS

Management is responsible for preparing digital files that comply with the ESEF RTS. This responsibility includes:

- the selection and application of appropriate iXBRL tags using judgement where necessary;
- ensuring consistency between digitized information and the consolidated financial statements presented in human-readable format; and
- the design, implementation and maintenance of internal control relevant to the application of the ESEF RTS.

Auditors' Responsibilities

Our responsibility is to express an opinion on whether the electronic tagging of the consolidated financial statements complies in all material respects with the ESEF RTS based on the evidence we have obtained. We conducted our reasonable assurance engagement in accordance with International Standard on Assurance Engagements 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* (ISAE 3000) issued by the International Auditing and Assurance Standards Board.

A reasonable assurance engagement in accordance with ISAE 3000 involves performing procedures to obtain evidence about compliance with the ESEF RTS. The nature, timing and extent of procedures selected depend on the practitioner's judgment, including the assessment of the risks of material departures from the requirements set out in the ESEF RTS, whether due to fraud or error. A reasonable assurance engagement includes:

- obtaining an understanding of the tagging and the ESEF RTS, including of internal control over the tagging process relevant to the engagement;
- reconciling the tagged data with the audited consolidated financial statements of the Group dated 31 December 2022;
- evaluating the completeness of the tagging of the consolidated financial statements;
- evaluating the appropriateness of the Group's use of iXBRL elements selected from the ESEF taxonomy and the creation of extension elements where no suitable element in the ESEF taxonomy has been identified;
- evaluating the use of anchoring in relation to the extension elements.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

In our opinion, the consolidated financial statements included in the annual report of AS LHV Group identified as 529900GJOSVHI055QR67-2022-12-31-EN.zip for the year ended 31 December 2022 are tagged, in all material respects, in compliance with the ESEF RTS.

Other Requirements of the Auditors' Report in Accordance with Regulation (EU) No 537/2014 of the European Parliament and of the Council

We were appointed by those charged with governance on 13 March 2019 to audit the consolidated financial statements of AS LHV Group for the year ended 31 December 2022. Our total uninterrupted period of engagement is three years, covering the periods ended 31 December 2020, 31 December 2021, 31 December 2022.

We confirm that:

– our audit opinion is consistent with the additional report presented to the Audit Committee of the Group;

– we have not provided to the Group the prohibited non-audit services (NASs) referred to in Article 5(1) of EU Regulation (EU) No 537/2014. We also remained independent of the audited entity in conducting the audit.

Tallinn, 27 February 2023

/digitally signed/

Eero Kaup

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