AS LHV Pank
Consolidated annual report 2023

(Translation of the Estonian original)

Consolidated annual report **1 Jan 2023 – 31 Dec 2023**

Legal name	**AS LHV Pank**
Commercial Registry no.	**10539549**
Legal address	**Tartu mnt 2, 10145 Tallinn, Estonia**
Phone	**(+372) 6 800 400**
Fax	**(+372) 6 800 410**
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**

These are the Group'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	**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**

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Management report

Business overview

Group 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. LHV Pank defines itself as a local bank offering the full range of services to customers that keep their funds at LHV Pank and actively use LHV Pank's services.

LHV Pank has offices in Tallinn, Tartu and Pärnu. LHV Pank's consolidated financial statements comprise the accounts of LHV Pank and its 65% ownership subsidiary AS LHV Finance ('LHV Finance'), which specialises in consumer financing (together referred to 'the Group' or 'LHV'). Parent company of LHV Pank is AS LHV Group ('LHV Group').

1.1 Business activities

In 2023, AS LHV Pank was significantly impacted by the difficult macroeconomic environment, volatility, and changes in regulatory supervision, collectively affecting everyday business activities severely. For the first three quarters of the year, LHV Pank was influenced by the asset quality review process, diverting some focus from business growth. Economic conditions continued a negative trajectory that impacted customers' insecurities about the future, withholding them from making investments. The new environment affected plans towards increasing volumes and fees from investment and forex services, but the year was largely impacted by changes in the European Central Bank's decisions regarding interest rates, positively affecting net interest fees from the loan portfolio. Challenges persisted in building effective sanctions screening and monitoring systems and processes, resulting in an increased number of staff.

Still, LHV Pank continued to grow in 2023. The number of customers increased by 39,000 to 417,000, i.e., by 10%. The youth segment grew by 14% to 81,000 customers, fulfilling our target mission in excess. The growth in customer activity and business volumes was broad-based. LHV Pank's UK branch activities were transferred to LHV Bank Ltd, and we continued servicing financial intermediaries in euro payments and safeguarding services.

Deposits from customers increased by 12% to EUR 5,535 million. Deposits from regular customers grew by 11% to EUR 4,081 million, while deposits from financial intermediaries decreased by 23% to EUR 991 million. Competition in the deposit market was severe, but the focus was set on collecting more deposits than the market's organic growth, a goal that was fulfilled. The average cost, compared to the market, wasn't higher. With a high focus on deposits and liquidity, we also collected deposits from European platforms in the amount of EUR 462 million

The Group's loan portfolio grew by 11% to EUR 3,549 million during the year. Corporate loans grew by 9% to EUR 1,887 million and retail loans by 10% to EUR 1,595 million. The breakdown of the retail loan portfolio was as follows: home loans 73%, leases 10% and other loans 17%.

The Group's net profit for the year increased by 75% to EUR 141.4 million. Total net income increased by 61%, total operating expenses increased by 32%. Net interest income increased due to increased corporate and home loan portfolios, but great positive impact arose also from European Central Bank positive interest rate decisions made to tackle high inflation rates in Europe. The decrease in net fee and commission income was 16%. It was mainly impacted by the financial intermediaries' business and fee transfer to LHV Bank. Credit losses increased by EUR 8 million and were over EUR 4 million higher than initially planned. Still, the quality of the loan portfolio remained strong, with a very low share of non-performing loans. Results for the year also include EUR 22.1 million deferred tax expense for 2023 payable on the expected future dividend payment. The Group's performance indicators were solid: return on equity (on net profit attributable to shareholders) was 30.9%, the cost/income ratio was 32.8%, and risk cost ratio was 0.3%.

The Group's total assets increased by 12% to EUR 6,755 million in 2023.

Financial results

EUR million	2023	2022	Δ
Net interest income	228.5	129.5	76%
Net fee and commission income	27.2	32.4	-16%
Net financial income	2.7	-0.4	na
Other income	1.7	0.2	779%
Total net income	260.1	161.7	61%
Total operating expenses	85.2	64.5	32%
Impairment losses	11.4	3.0	280%
Income tax expense	22.1	13.3	67%
Net profit	**141.4**	**80.9**	**75%**

Business volumes

Loans (net)	3,549	3,187	11%
Deposits from customers	5,535	4,957	12%
No of bank customers, thous.	417	378	10%

Key figures, %

Return on equity (ROE)	30.9	24.0
Return on assets (ROA)	2.2	1.3
Net interest margin (NIM)	3.6	2.0
Spread	3.5	2.0
Cost / income ratio	32.8	39.9

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

Return on Assets (ROA) = net profit / average assets * 100

Net Interest Margin (NIM) = net interest income / average interest earning assets * 100

Spread = yield on interest-bearing assets - cost of interest bearing liabilities

Cost/Income ratio (C/I) = total operating expenses / total net income * 100

1.2 Development activities

In 2023, the focus was on customer experience, improving existing services, and enhancing efficiency. The migration of LHV Pank UK branch activities to LHV Bank Ltd was completed in August.

Several improvements were made to customers onboarding processes to improve convenience and speed as the main foundation of great customer experience. Digital channels were also opened to all users of various LHV Group services. Customers can use biometric authentication and payment confirmation, receiving notifications for outgoing transactions, which also serves as a mechanism for preventing and detecting fraudulent transactions. The mobile app gained new features for investment services, and the Financial Portal received a new platform and a modern look. Forward-looking developments for modernising the technological platform were in focus and will continue to be a focus in 2024.

1.3 Organisation

LHV Pank is divided into seven functional areas, each with its own departments. Business areas include retail banking, corporate banking, and financial intermediation. Support areas comprise IT, financial management and support services, risk management, and product management. Credit risk management, initially a separate area, was transferred under the risk management area by the end of the year. Human resource management, marketing and communication, and compliance are bank-wide activities. After transferring the UK branch activities to LHV Bank Ltd, the branch was closed.

In 2023, the number of the Group's employees converted to the full-time equivalent increased by 62 to 826, including inactive and part-time staff, and the 21 employees of LHV Finance.

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. LHV Pank ranked first in the Most Attractive Employers survey conducted by the job portal CVKeskus.ee and TOP Employer in survey conducted by the job portal CV-Online Estonia. LHV Pank also received highest ranking in the employer reputation survey conducted by employer branding agency Instar by being the most attractive employer. LHV Pank's staff satisfaction survey Q12 reflected continuously a very high level of satisfaction. City Plaza building, where LHV Pank's Tallinn office is located, has a BREEAM (Building Research Establish Environmental Assessment Method) certificate. We received marketing award Kuldmuna for the campaign "Rahasuhted" and LHV was selected for the Bravest Brand in Estonia.

1.4 Sustainability at LHV Pank

At LHV, we acknowledge the vital role of the financial sector in steering economic shifts and directing resources through lending and investments toward activities that promote a transition to a more sustainable economy. Since 2020, LHV Group has actively been a member of the United Nations Environment Programme Finance Initiative (UNEP FI), a comprehensive framework for sustainable banking developed through a partnership between banks worldwide and the United Nations. In 2023, LHV made substantial progress towards its sustainability goals, focusing on metrics, regulatory frameworks, ESG governance, credit portfolio analysis, and risk management processes.

Looking ahead, LHV is preparing for the sustainability reporting requirements arising from the Corporate Sustainability Reporting Directive (CSRD), demonstrating our ongoing dedication to transparent and responsible sustainability practices. Initiatives such as measuring and disclosing the climate impact of our loan portfolio will continue, with an ongoing commitment to enhancing data quality for more accurate reporting. This analytical approach enables us to identify the most emission-intensive sectors, allowing for targeted actions to reduce emissions within those areas.

In addition to our environmental commitment, LHV is dedicated to making a positive social impact. Recognised as the most attractive employer in Estonia, LHV prioritises organisational development and employee well-being, also targeting diversity and inclusion and a decrease in the gender pay gap. LHV Pank actively supports enterprises and initiatives that contribute to the development of Estonian society. Leading discussions on inclusive economies and backing culturally and socially significant initiatives, LHV remains committed to fostering innovative ideas and projects that enhance the quality of life in Estonia.

Business environment

The global economy witnessed a slowdown in economic activity and heightened divergences across regions in 2023. Although the year commenced with indications of economic resilience, the trajectory shifted in the third quarter. Restrictive monetary policy and increased uncertainty started to take effect, albeit unevenly across countries. The US demonstrated notable resilience, achieving a GDP growth of 1.2% in Q3 compared to the previous quarter, driven by robust consumption, exports, and substantial government spending. In contrast, the United Kingdom entered into standstill, and the euro area saw a decline of -0.1% in Q3, marking the first contraction since the COVID-19 pandemic. Despite facing a challenging environment, economic activity in Asia and the Pacific maintained its course and even surpassed growth expectations in the first half of 2023. However, the growth slowdown is evident due to China's reopening losing momentum and subdued investment, partly influenced by weakened external demand. Yet, central banks continued with restrictive monetary policy as target inflation levels had not been met.

Europe's economy is suffering from weak demand together with lowering export levels and continued exposure to Russia's war in Ukraine. The persistent impact of last year's energy price shock, coupled with sustained tightening of monetary policy, is further contributing to a deceleration in growth. The initial slowdown in growth during the first half of the year eventually receded to 0% YoY in Q3. This economic weakening is also evident among Estonia's primary trading partners, where weak domestic consumption, inflation, and elevated interest rates persist. Nordic countries are contending with reduced inventory levels and low investments in the construction sector. Latvia experienced weak growth, primarily influenced by the construction industry, while Lithuania saw a small decline, mainly attributed to contractions in the manufacturing sector, retail, and real estate activities.

The resilience of robust labour market in the euro area shows signs of slowing but has remained tight. The unemployment rate fell to 6.4% in November compared to 6.7% in the year before. The ongoing tightness may be indicative of a delayed adjustment in labour demand. Following the COVID-19 crisis, certain sectors experienced prolonged labour shortages, leading companies to refrain from reducing their workforce, while the manufacturing sector initiated layoffs. Nevertheless, significant disparities persist between countries, with unemployment increasing in some nations and decreasing in others. Specifically, unemployment rates range from nearly 12% in Spain to 2.5% in Malta. Estonia's rate stands just below the euro area average at 6.1%. Youth unemployment (under 25 years) has reached to nearly 28% in Spain but has remained at 5.6% in Germany.

In November, annual inflation in the euro area decreased to 2.4%, marking the lowest level since July 2021. The primary contributors to this decline were the decrease in energy prices and a deceleration in the growth of food prices. The moderation in headline inflation offered some relief to both households and businesses. Core inflation, i.e., consumer price inflation excluding energy and food, proved more difficult to tackle and was still persistent, despite slowing from 4.2% to 3.6% in November. The combination of low unemployment and rapid inflation has also driven wage growth, surpassing 5%. This could potentially lead to entrenched price increases, necessitating additional policy tightening and raising the risk of stagflation.

The uncertainty surrounding the persistence of inflation is substantial, and Europe is currently confronted with the formidable challenge of reinstating price stability. The European Central Bank (ECB) has consistently adhered to a restrictive monetary policy to bring inflation under control. In 2023, there were six consecutive hikes, resulting in a total increase of 2 percentage points in base rates. The Governing Council of the ECB decided to remain base rates unchanged in October and December meeting, with last hike occurring in September. Yet, the ECB's target level of 2% has not yet been attained. The Governing Council emphasises the necessity of maintaining a restrictive monetary policy stance to achieve the target, highlighting the significance of a data-dependent approach in determining future interest rate decisions. As of July 2023, the ECB discontinued reinvestments under the asset purchase program. Throughout the second half of 2024, the pandemic emergency purchase program portfolio is slated to be reduced by an average of €7.5 billion per month.

The adjustments in monetary policy were evident in market interest rates, experiencing a notable surge until November. The 6-month Euribor rate, linked to the majority of loan agreements, had reached 4.1%. Subsequently, rates exhibited a decline in the fourth quarter, aligning with expectations of forthcoming monetary policy easing. By the end of the year, the 6-month Euribor rate had declined to 3.9%. Longer-term interest rates in the interbank money market witnessed a decrease, with the 12-month Euribor dropping below both the 3-month and 6-month Euribor rates.

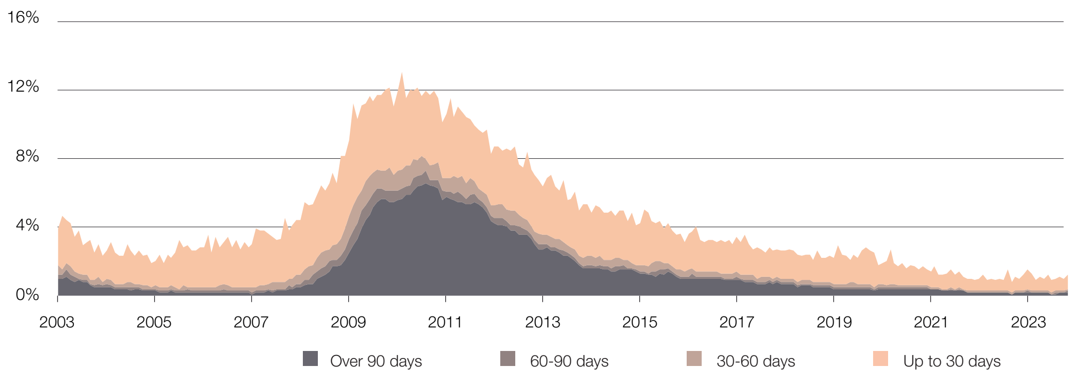
The economic downturn in Estonia has proven to be more severe than initially anticipated, primarily attributed to a decline in exports. During the Q3, Estonia experienced a 3.9% decrease in GDP compared to the same period the previous year and a 1.2% decline compared to the Q2. Heightened uncertainty among households, coupled with increased savings, has constrained demand within the domestic market. Simultaneously, foreign demand has been impeded by the lacklustre performance of Estonia's key export markets and the strengthening of the exchange rate relative to Nordic countries. Continued Russia's war in Ukraine has disrupted numerous supply chains, leading to the disappearance of certain business models. Additionally, elevated uncertainty and rising interest rates have not been conducive to fostering investments.

The added value in various economic sectors witnessed a decline, with a notable impact from activities heavily reliant on exports. Manufacturing experienced a 1.3% decrease, while transporting and storage saw a 1.5% decline. Sectors that have been driving economic growth in the past decade, such as information and communication, recorded a decrease of 0.9%. Conversely, there was a positive uptick in added value observed in the retail trade and public administration activities.

In 2023, the pace of price growth decelerated. Despite this, the cost of the consumer basket has shown little change for more than six months, and the current inflation rate of 4-5% is primarily a result of a lower reference base from the previous year. Although food prices began to decrease early in the year, simultaneously, the overall cost of the food consumer basket continued to rise at a relatively swift pace. A significant contributing factor to the moderation of inflation this year has been the decline in energy prices, particularly in electricity and gas.

Household consumption is constrained by the imperative to rebuild reserves and augment savings. Comparing Q3 to the previous year, consumption witnessed a decline of 2.4%. Under normal circumstances, households typically manage to save around 10% of their income consistently, but the savings rate barely surpassed 0% last year. The volume of term deposits has experienced substantial growth at the expense of demand deposits, expanding nearly three-fold over the year. By October, the average interest rate on households' term deposits exceeded 4%, reaching 4.5% or more for extended terms or promotional periods. In a comparison with the euro area, interest rates on private individuals' term deposits in Estonia are the highest, while those for companies fall within the average range. The loan market has exhibited some stabilisation in both demand and supply. The issuance of housing loans has decreased by approximately 20% in terms of both number and volume compared to the previous year. The annual growth of the corporate loan portfolio has stabilised at 6%.

Market average share of overdue loans in loan portfolio, %



Source: Bank of Estonia

The Estonian economic landscape faces challenges stemming from diminished external demand, ongoing competitiveness issues, and the looming external threat posed by the prolonged Ukraine-Russia war. The compounded uncertainties are further intensified by anticipated tax hikes. Projections indicate a contraction of Estonia's GDP by 0.4% in 2024. However, a rebound is anticipated in 2025 and 2026, with economic growth approaching 3%. The restoration of quarterly GDP to pre-recession levels is foreseen in 2026.

Key economic indicators of Estonia*

	2017	2018	2019	2020	2021	2022	Bank of Estonia forecast 2023E	2024E	2025E	2026E
Nominal GDP (EUR billion)	23.8	25.9	27.9	27.4	31.1	36.0	37.4	38.9	41.1	43.2
GDP volume**	5.5%	3.9%	3.9%	-0.7%	7.4%	-0.5%	-3.5%	-0.4%	3.2%	3.2%
Private consumption expenditures***	2.5%	4.8%	4.7%	-1.3%	9.1%	2.1%	-1.9%	0.1%	3.3%	2.5%
Government consumption expenditures	1.9%	1.1%	3.2%	3.0%	3.8%	0.1%	1.5%	3.5%	-1.1%	-0.7%
Fixed capital formation	13.8%	10.5%	6.2%	10.8%	7.3%	-4.9%	-6.9%	-5.0%	5.6%	4.9%
Exports	4.8%	2.9%	5.0%	-5.5%	22.1%	3.0%	-8.1%	-1.3%	3.5%	3.6%
Imports	4.0%	5.9%	3.7%	1.3%	23.2%	3.3%	-7.1%	-3.1%	3.2%	2.8%
CPI	3.4%	3.4%	2.3%	-0.4%	4.7%	19.4%	9.2%	3.4%	2.4%	2.2%
Unemployment rate (% of the labour force)	5.8%	5.4%	4.5%	6.8%	6.2%	5.6%	6.8%	9.0%	8.1%	7.8%
Current account (% of GDP)	2.3%	0.9%	2.5%	-1.9%	-2.6%	-3.2%	-3.2%	-4.8%	-4.5%	-3.7%
Budget balance (% of GDP) ****	-0.5%	-0.6%	0.1%	-5.4%	-2.5%	-0.8%	-2.9%	-3.4%	-4.5%	-3.6%

* 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.

Source: Bank of Estonia, Statistics Estonia, Eurostat, IMF

Management and compensation policy

LHV Pank's 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 21.46% of share capital in aggregate and Andres Viisemann and persons related to him, who hold 11.18% of share capital in aggregate.

2. Supervisory Board

The Supervisory Board is the governing body of LHV Pank that plans the activities, organises the management 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 the Group. 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: Madis Toomsalu (Chairman, until 31 March 2026), Rain Lõhmus (until 31 December 2024), Andres Viisemann (until 31 March 2027), Tiina Mõis (until 31 December 2024), Heldur Meerits (until 31 March 2026), Raivo Hein (until 31 March 2027)

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: Kadri Kiisel (Chairman), Indrek Nuume, Jüri Heero, Andres Kitter, Meelis Paakspuu, Martti Singi (all until 31 March 2027)

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 four 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 the group companies.

4.1 Risk and Capital Committee

Both LHV Group and LHV Pank have established Risk and Capital Committees (jointly referred to as the Risk and Capital Committee) whose task is to monitor the implementation of the risk management policy and the capital management policy on the LHV Group consolidated level and LHV Pank consolidated level, respectively. The Risk and Capital Committee reviews regular risk reports, the processes ensuring capital adequacy, capital plans and the largest clients with high credit risk. The Risk and Capital Committee has at least three members who are elected from among the members of the Supervisory Board of LHV Group and LHV Pank, respectively.

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 based on 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 Board of LHV Group 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 on the level of Supervisory Board of LHV Group. The Remuneration Committee is charged with the task of assessing the principles of remuneration within the LHV consolidation group companies, as well as the impact of remuneration-related decisions on adherence to the requirements established for the management of risks, own funds and liquidity. The Remuneration Committee is set up of at least three members of the Supervisory Board of AS 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

In 2020 LHV shareholders approved the result-based share option programme for the Management Boards and equivalent staff as well as key employees of LHV and the group companies to be implemented from 2020 until 2024. In 2023 the recipients and amounts of share options to be granted for the results for 2022 were determined based on this 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 at least 3 years from the moment the options were granted. An additional criterion applies to options issued to Management Board members – they are not allowed to sell these shares for another year after executing the rights under option. The at least 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 2023. In 2023, the options issued in 2020 were fully exercised. The next share options issue could be in 2024 based on the Supervisory Board's decision.

The granting and amount of share options were dependent upon the successful achievement of operational targets of the overall company and the targets of individual Management Board members and employees. In 2023 in the Group, share options were granted to 7 Management Board members (6 from LHV Pank AS and 1 from LHV Finance AS) and 141 employees in the amount of EUR 4,426 thousand. In 2022, 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.

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 share options issued in 2023 can be exercised between the period from 1 April 2026 to 30 April 2026 and shares with the nominal value of EUR 0.1 can be acquired for EUR 1.70 per share.

Expenses related to share option program amounted to EUR 3,945 thousand (2022: EUR 3,390 thousand).

7. Wages and salaries

The table below provides wages, salaries paid, and the number of employees who received salaries and wages during the financial year 2023 (including trainees).

Calculated gross salaries and wages

EUR thousand

	Base salary	Incentive salary (excluding option program)	Total	Number of employees
Retail banking	8,375	0	8,375	396
Private and corporate banking	3,145	0	3,145	91
Financial intermediates	739	0	739	60
Support services	9,716	0	9,716	322
Information technology	7,790	0	7,790	219
Total	**29,765**	**0**	**29,765**	**1,088**

Sustainability report

1. Sustainability at LHV

1.1 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 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 to 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 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. In 2023, we submitted our 3rd PRB report.

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 to better understand our 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. The results are displayed in subsection 5.1.2 of 'Sustainability report'.

These results give us a valuable starting point and help us set emission reduction targets by the end of 2024. 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

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.

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.

4. Management of ESG

The core of our ESG strategy is specified in our ESG policy 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 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.

Over the past years, we have considerably increased and developed ESG competencies in-house, resulting in ESG-focused positions in the Financial Management, Retail Banking, Compliance, Credit, HR, Risk and Asset Management Departments. The group-wide management of ESG has now resulted smooth integration of sustainability principles into all relevant business lines, processes, strategy building, and risk management. From the beginning of 2024, all group-wide ESG matters will be discussed at the Group Management Board meetings to ensure group-wide development and implementation of various ESG projects and processes.

5. Management of impact areas

5.1 Environment

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 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. We extended Tallinn City Plaza office Green Office certificate and received the same certificate 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 2024.

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.

This year we also took part in various charitable projects, for example we made protective nets for the Ukrainian battlefront, we donated Christmas presents to families in a poor economic condition and took part in the charity project '500 dresses', which proceeds donated to the Estonian Cancer Patients Association.

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. 50% 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 2023 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 2022, LHV's office activity had a greenhouse gas emission footprint of 1,968 tonnes of CO_2-equivalent, which was 2.5 tonnes per employee at the time of calculation. For 2023 the results were 2,217 tonnes, or 2.4 tonnes per employee. The main reason for the increase in our operational level CO_2 footprint was due to increase of employees and office space.

Estimates of financed emissions

In 2022 we started assessing our emissions under scope 3 category 15 investments (as defined by the GHG Protocol Corporate Value Chain standard) using the PCAF methodology. Assessment of financed emissions is important, since a large share of our emissions is related to our financing activities.

As a new addition in 2023, we estimated emissions for sovereign debt, listed equity & corporate bonds, which make 0.01 % of our total financed emissions. We broadened the scope of business loans by estimating emissions of guarantees. We changed the PCAF database rights from AS LHV Pank to LHV Group, which gives us the opportunity to assess also other LHV Group's subsidiaries' emissions. Previously, only emissions of AS LHV Pank had been evaluated.

Since 2022 our financed emissions increased by 165,562 tCO_2e, with a total of 728,058 tCO_2e. As of 2023, we have estimated the emissions for six asset classes (business loans, motor vehicle loans, commercial real estate and mortgages, sovereign debt, listed equity & corporate bonds) with an emission intensity of 550.4 tCO_2/EURm. We have assessed 99% of our credit portfolio (business loans, motor vehicle loans, commercial real estate and mortgages) and 100% of sovereign debt, listed equity & corporate bonds. For business loans we report absolute emissions data at the sector level. Electricity, gas, steam and air conditioning supply sector, has the largest tCO_2 e amount with 30.0 % of total business loans' tCO_2 e.

The results of the emission estimations can vary to some extent depending on the quality of the input data used in the calculation models. In 2023 we made continuous work to improve the data quality, although for substantial improvement it is needed to obtain more specific information directly from our clients. PCAF data quality scores are on a scale of 1-5, where 1 is the highest possible score. Although PCAF's methodology has limitations, as of now it is the best available option and has helped us gain a better overview of our climate impact. Based on these findings we will be able to set emission reduction targets in the future.

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.

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.

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.

5.3.1 Social responsibility

We understand our increasing role in the Estonian economy and society in general. In line with our mission, we support activities that allow Estonian people and businesses to think more boldly about the future and realise their plans. We consider it important to increase the feeling of economic security and make the economic environment more coherent. In society at large, we primarily support ventures that make Estonia bigger and contribute to the capabilities of our communities. In addition to contributing to investor education and recognition of entrepreneurs, we have several longer-term and more recent cooperation projects, helping to achieve these goals.

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 organised 33 free seminars as part of the Investment School, with 16,000 participators in 2023.
- We carried out the annual stock market game Börsihai. This year, the number of participants reached 5,460. As part of Börsihai, we facilitated a virtual lesson introducing investing and the stock market game, which reached over 40 Estonian schools.
- At the beginning of the year, we participated in a TV project Rahareede, where on 8 shows we talked about important topics related to personal finances and investing.
- We supported the Investor Toomas conference organised by Äripäev, the Investment Festival carried out by the Investment Club and the Women's Investment Club.
- In collaboration with Äripäeva Kirjastus, we supported the publication of investment-related books in Estonian.

5.3.3 Sponsorships

We do all we can to support activities and initiatives which contribute to the development of Estonian society. In the case of our sponsorship projects, we prefer long-term and substantial cooperation. We are willing to contribute to the realisation of innovative ideas helping to make life in Estonia better. Our other sponsorship contributions are described below.

Estonian culture and society

- Estonian Music Days – for eight years now we have supported the Au-tasu prize for new Estonian music, which was awarded to Ülo Krigul in 2023.
- #TRESKIFEST music festival; concert of Smilers and Red Bull Soundclash – we continued supporting the Estonian music scene.
- EUR 25,000 prize money from the LHV 'Who does it?' support programme aimed at local communities was given to the Kose-Uuemõisa community this year, to restore the park terrace which has a long history.
- Through the charity function for LHV Pank ('Micro donation') we facilitated donations of more than EUR 105,000 to 13 charity organisations.
- 'Charge yourself' programme – we are one of the initiators of the programme giving priority to teaching physics.
- Rakett69 – support to the TV show that popularises science among pupils. In 2023 we also recognised the teacher of the student who won the show.
- Kood/Jõhvi – we are one of the supporting partners of the new IT college in Ida-Virumaa county.
- LHV employees volunteered at Toidupank and organised several charity workshops, where helmet covers and safety nets were knitted together for Ukrainian soldiers.
- OLE ROHKEM. – a network that brings together active Tartu student organisations and trains them. We were their main supporting partner.
- Negavatt – we were the main sponsor for the green business idea competition.

Sport & healthy lifestyle

- Estonian Football Association – LHV Pank has been the main sponsor of the Estonian Football Association and the Estonian national team since 2010. In addition, we supported football clubs with EUR 152,000 in 2023 through the LHV football card support system.
- Maijooks 2023 – LHV continued to be the name sponsor of the biggest women's health sports event in Estonia.
- Estonian Optimist Class Union – we support the development of Estonian sailing.
- Simple Session – we were one of the main sponsors of the top extreme sports event for the third year.
- Estonian Biathlon Federation – we supported Estonian biathletes during the season.
- Estonian Ski Association - LHV Kindlustus supported Estonian ski athletes and their team members in the 2023 season.
- Estonian Basketball Association – LHV became the main sponsor of Estonian women's basketball.
- Disc Golf European Championships 2023 in Tallinn – LHV supported one of the fastest growing sports' championships held in Estonia for the first time.

Estonian economy and business

- EY Estonian Entrepreneur of the Year competition – we have been one of the main sponsors since 2012.
- Young Entrepreneur Award – in cooperation with the Estonian Chamber of Commerce and Industry, we awarded the prize to Kristo Klement.
- Conferences Business Plan, Investment Festival, Investor Toomas – in cooperation with Äripäev, we supported Estonia's leading business and investment conferences.
- TalTech Business Forum – we supported a two-day business festival organised for students.
- Conference of Estonian Real Estate Association
- Latitude59 – we again were sponsors of the large startup meet up.

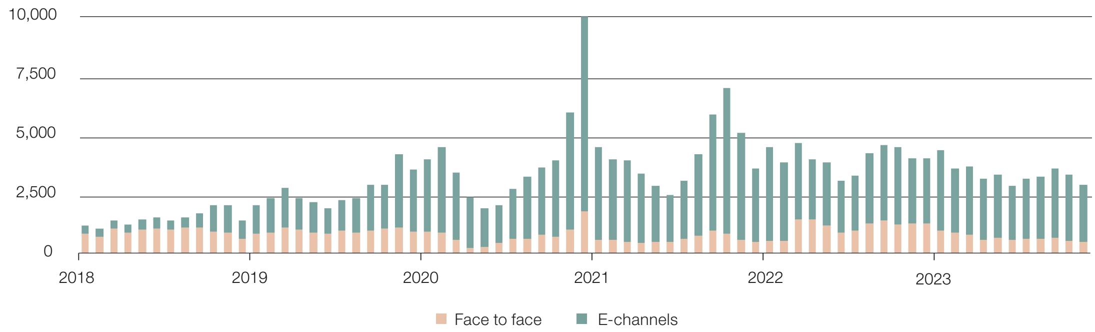
We also support smaller local initiatives with our knowledge, LHV's gifts, advice and the presence of our people. We work with universities. We are a member of the Estonian Information Technology and Telecommunications Association, the Estonian Chamber of Commerce and Industry and the Estonian Employers' Confederation. We consider it important to help Estonian producers and entrepreneurs by preferring their products and services.

5.3.4 Social impact through channels and customer experience

Customer satisfaction and high quality of e-channels has always been a top priority for us. While for the past few years, we have been more focusing on making banking services available online, especially to private customers and simple business structures, we are now working on wider segments and product portfolio, but also more effective 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 cross-sell targets, high customer activity, and make our e-channels available for wider audience including insurance customers, pension funds and consumer credit product users.

In 2023, we have onboarded an average of 4,400 new customers every month. Close to 83% 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. The percentage of customers using our services remotely and online has been growing steadily through previous years.

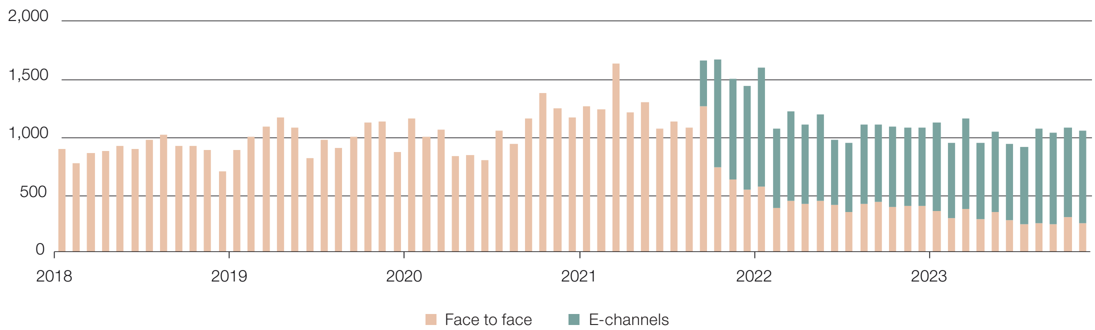
Identification upon onboarding of private persons



Since 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 75% in Q4 2023.

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.

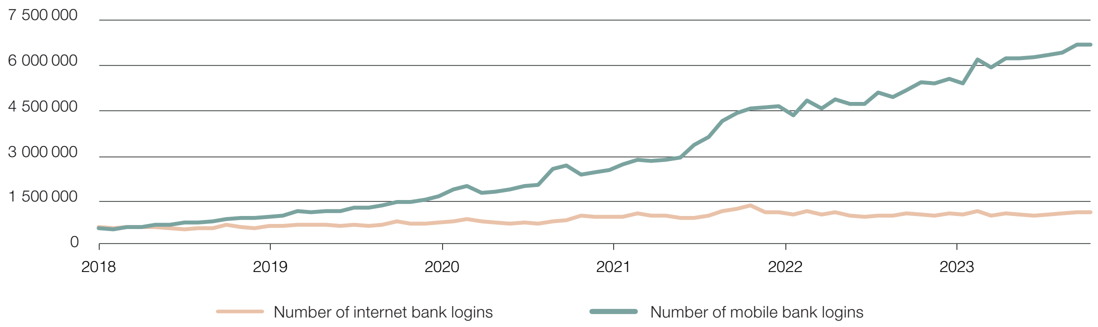
Identification upon onboarding of legal entities



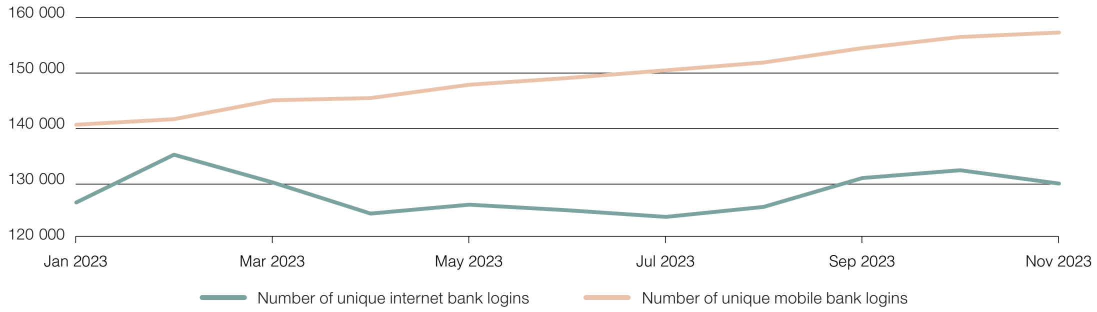
Since 2022 the monthly usage activity of our mobile bank has been exceeding internet bank usage. Our mobile bank app has been rapidly gaining popularity among both, private and legal customers. The monthly usage activity of our mobile bank app is showing approximately six times higher activity rates than internet bank. Also, when the statistics of unique monthly users for recent years have been in the same ballpark for both channels, 2023 has shown a decent growth for mobile bank app reaching approximately 155,000 monthly users.

Improving the usability and look&feel of our electronic channels and making user experience as seamless as possible has been our utmost priority. The percentage of new customers logging into the electronic channels has reached to 80% for mobile bank and up to 95% for internet bank by Dec of 2023. This means that customers are taking advantage of our electronic channels even more than a year before.

LHV internet bank and mobile bank usage activity



LHV internet bank and mobile bank unique users



Opening a bank account online for underage children through our electronic channels 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.

As one of the developments in 2023 we have redesigned and simplified the flow to allow the underage account setup without signing the customer agreement with the parent. As a result, we have secured a steady flow of an average of 600 underage accounts opened per month.

LHV insurance services and product portfolio has expanded from insuring homes, cars, trips, equipment, machinery, warranty, and extended warranty insurance to dwelling, corporate and liability insurance. Most of the insurance applications are submitted through our website or mobile app, keeping the ecological footprint minimal and customer satisfaction on a high level. In addition to applications, we are planning to integrate all the insurance claim reporting workflows with the insurance backend software to minimise manual work and improve response metrics.

Focus on customer experience

Excellent customer experience is critical to the sustainable growth of any business. Keeping the high level of customer experience promotes loyalty, helps us retain customers, and encourages brand advocacy. Therefore, when redesigning and improving our electronic channels, we have also considered the needs of visually impaired people and have been working closely together on testing and implementing visual and navigational changes.

We are in progress of developing a Budget Planner tool in our e-channels for customers to promote financial literacy and help them to make smarter financial everyday decisions and support them with an AI based solution. Also, LHV Financial Portal has been redesigned and restructured to provide even more details and insight into investing and saving. We are launching a savings product that encourages customers to save money through gamification and goal setting techniques, while learning about the importance of investing.

LHV has always been acting responsibly when planning our communication and marketing messages, both online and offline. We are working on solutions to ensure that our marketing activities are based on customer segments and the unique needs of those segments. Our goal is to offer most of our products and services online and plan our sales activities increasingly by segments and customer lifecycle.

Increasing phishing and financial crime rates have forced us to proactively warn and educate our customers about possible threats online and take proactive measures to detect unusual usage patterns.

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 our employees we look for the same values and follow this mindset in all our practices, processes, and daily actions internally. We carry out different surveys during the employee lifecycle – e.g., during exit interviews, end-of-probation talks, etc – to evaluate how we are doing in the eyes of our employees, and where we could do better. We have set up a monthly get-together for team leads, where they can share and discuss different topics, where many team leads share their own experiences and ideas of how to make the workplace better.

We use the international Gallup Q12 format to measure employee engagement survey. The survey consists of 16 questions that measure factors affecting 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 good, in both we got 4.4 points out of 5. 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 not related 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.

We have developed and established a Diversity Policy. LHV recognises that people have different values, abilities, and skills, which affects the way they think and see things. LHV wants to take advantage of these differences, especially in decision making, incl. in management bodies. Different backgrounds, experiences, values, opinions, and views are welcome. Individual differences are embraced, respected, and expected to promote thoughtful disagreement. LHV believes in meritocracy, where people are considered based on their skills, experience, and the value of their ideas. In 2023 there were no notifications about labour disputes, discrimination or violations of human rights.

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. 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 2023, 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 0,86 to 0,91. In the manager categories the range was slightly higher, from 0.70 to 0.90, but these roles are often more specific, incomparable with each other.

Inclusive workplace

It is important to us that our employees' ideas, thoughts, and statements are heard and taken into consideration. We believe that great success comes from working together and using our collective intelligence. It is important that employees feel free to express themselves, ensuring their voices reach top management. LHV includes all employees in the process of setting goals for each team, fostering a collaborative team effort.

While we encourage our employees to express their thoughts daily, this focus intensifies at least twice a year during our engagement survey, Q12. In the seventh question of the survey, respondents must indicate their agreement or disagreement with the statement 'At work, my opinions seem to count.' Employees can provide responses on a 5-point scale, in April the score was 4.6 and in November it was 4.5. Additionally, the survey format includes one-on-one conversations for every team member with their manager, allowing for in-depth discussions and proposing actions if improvements are needed. This topic has been identified as one of the key focus areas by HR and communicated to the team leaders.

LHV employees are not covered by a collective agreement, as this is not a very common practice in the financial sector in Estonia. However, we are a member of the Estonian Employers' Confederation.

We value diversity and inclusion through several initiatives aimed at both internal and external communities. One of our main initiatives is organising hackathons within LHV, which bring together individuals from diverse backgrounds and fields to collaborate on solving challenges and generating innovative ideas. In 2023, there was an investment-themed hackathon where the winning work was selected, based on which new value added to our existing services was developed.

Such events not only foster creativity, but also create a platform for showcasing diverse perspectives. An illustration of LHV's commitment to inclusive business and the embrace of diversity is the collaborative development of the benefits package by employees from various backgrounds and fields, utilising the service design method. The company considers different needs and preferences, offering a diverse range of benefits that align with the expectations and lifestyles of its employees.

As a new process, we introduced managers' covision meetings, which facilitate structured discussions to share thoughts and support each other in finding solutions to various management challenges. These meetings contribute to the development of leadership skills, fostering stronger team spirit and enhancing problem-solving abilities, thus creating value for the organisation

The SEMU program is another example of LHV's commitment to inclusive entrepreneurship. It is a mentoring program in which LHV employees take the role of mentors, sharing their experience and knowledge with new colleagues. This program provides an opportunity for new employees to learn from experienced colleagues, contribute to the company's development, and engage in real challenges that foster professional growth.

Conversation evenings around LHV values, where the discussion partners are the company's own employees, show the company's effort to create a platform where employees can encourage each other and share their thoughts and experiences according to the company's core values. In summary, LHV is committed to fostering diversity, inclusion, and open communication through various initiatives, creating an environment where everyone feels valued, and diverse perspectives are not only recognised but also supported.

LHV is a member of The Estonian Employer's Confederation, Estonian Chamber of Commerce and Industry, Responsible Business Forum in Estonia and Estonian Human Resource Management Association PARE.

Employee development

Professional and personal development is part of LHV's culture, reflecting our commitment to innovation and continuous improvement in delivering 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. Our training approach is tailored to individual needs, motivations, and goals, aligning with regulatory guidelines for professional development.

In addition to professional trainings, we have contributed to team trainings with the aim of enhancing collaboration within teams. Furthermore, we have intensified our focus on leadership development through a dedicated leadership training program. Our particular emphasis lies in mapping employees' strengths using Gallup's Clifton Strengths Finder test. Over 60% of our teams and employees have taken the test, providing them with a comprehensive overview of their greatest strengths.

Beyond personal and professional development, we regularly organise discussion evenings where guests are LHV's own employees. The topics have included 'We listen to the customer and offer a solution', 'Simple, supportive and effective', 'Setting high goals and investing in the future', 'Let's talk about things as they are', 'Cooperation is important to us'. All these topics are related closely aligned with LHV values.

Every month there is also a workshop aimed at managers, where we deal with issues related to management. The topics have been 'Insight into LHV through an external eye', 'Everyday misconceptions', 'Team cohesion', 'Q12 experience story', 'Many levels of leadership', 'Strength Finder Gallup', 'Leader as a culture designer'. 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 your progress, and have you had opportunities to learn and grow in the past year? In the latest survey, from November 2023, 76% of our employees replied with a 4 or a 5 to first two questions and 80% of the employees say that they have had opportunities to learn and grow in the past year in their role. All these have decreased slightly from last year.

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. On behalf of the company, we offer a flexible working arrangement that provides an opportunity for balance.

LHV encourages employees to work in the office, and while many prefer this setting, we recognise the importance of flexibility. Our benefits package for employees is diverse, offering days off both for personal and family events. For example, employees are entitled for free days for personal use (3), a wedding (3), in case of the loss of a loved one (3), an employee returning from parental leave (3), participating in a child's school function (1) or to participate in their own school function day (1). During the period of training of reservists, we retain 100% of the employee's salary.

A notable addition to our benefits is the creation of a six-week sabbatical, emphasising the value we place on employee development and work-life balance. This serves as a token of gratitude for those who have contributed significantly to LHV's development. Above all, we prioritise the ability of our employees to attend important family events.

Promotion of employees' health

To prioritise the health of our employees, LHV provides an extensive occupational health package aimed at both physical and mental well-being. We understand the importance of maintaining a healthy balance between work and private life, as well as fostering a supportive mental and physical working environment.

Supporting mental health, health audits, supporting sports activities, offering joint training sessions within the company, and summer hiking projects are integral to promoting the overall health of LHV employees. By offering opportunities to maintain a balance of both physical and mental health, we contribute to the well-being of our entire company.

Throughout the year, we conducted the Peaasi.ee survey ‘Peaasi.ee Mental health vitamins + Emotional Wellbeing Test’ and the HeBa occupational health service provider ‘HeBA questionnaire: Work related stress’. These assessments help us continually address and improve the well-being of our employees.

A recognised employer

While attractive employer awards have never been the primary goal for LHV, they are still a great acknowledgement. In recent years, LHV has gained a growing reputation for being a desirable employer. Our objective has been to provide our employees with opportunities for professional growth and an inspiring company culture. Throughout this year, we have had numerous opportunities to share our experiences and our leadership culture in various podcasts, conferences, schools and universities.

All of these efforts have not gone unnoticed. 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. Additionally, CV Keskus ranked LHV as the most desirable employer, and in Instar’s survey, we were recognised as the most attractive employer by both students and experienced professionals. This year, we participated in the Dream Employer competition and proudly emerged as the private sector winner.’

Such recognition plays a crucial role in attracting talented individuals to join our company, especially in today’s highly competitive labour market. Throughout this year, we had the opportunity to engage with almost 6,500 applicants, ultimately hiring 5.4% of them. Alongside our job offerings, we have sustained our internship program, actively promoted job-shadowing, and facilitated rotation opportunities. In the summer of 2023, we welcomed 48 interns to contribute to our vibrant and dynamic workplace.

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, financial crime, 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 2023, we submitted our third report to UNEP FI regarding our progress of implementing the UNEP FI Principles of Responsible Banking and continue to do so in the upcoming year while also considering 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.

We are preparing for the upcoming CSRD which will require us to report on various aspects on a more detailed level. Aligning our reporting practices with international standards also means disclosing more non-financial information. To do that, we put effort into gathering and analysing ESG data, improving ESG communication and internal processes, developing and publishing more sustainability-related materials and reports, and building in-house capacity for adhering to globally recognised ESG reporting standards.

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 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 2024 and onward would be to establish a more specific target setting plan for these metrics and include additional business specific ESG targets which are tangible and aligned with both our ambition as well as the global goals.

5.5.2 EU Taxonomy reporting

The EU taxonomy regulation for sustainable finance (EU regulation no. 2020/852) is a system for classifying economic activities as environmentally sustainable. It categorizes economic activities based on their substantial contribution to EU environmental objectives of Climate Change Mitigation (CCM), Climate Change Adaptation (CCA), Water and Marine Resources, Biodiversity, Pollution and Circular Economy.

Article 8 of the EU taxonomy regulation requires any undertaking subject to an obligation to publish non-financial information pursuant to Directive 2013/34/EU (the NFRD companies) to include in its non-financial statement or consolidated non-financial statement information on how and to what extent the undertaking's activities are associated with economic activities that qualify as environmentally sustainable under the EU taxonomy regulation.

LHV Pank's approach to taxonomy reporting

LHV Pank considers as its main taxonomy alignment KPI the Green Asset Ratio (GAR). The GAR is the main KPI used for disclosing information on the extent of taxonomy alignment of credit institutions' activities. It shows the proportion of assets financing and invested in taxonomy-aligned economic activities, and it is computed as a proportion of total covered on-balance sheet assets.

The main KPI GAR and other relevant KPIs are required to be disclosed on the basis of the prudential scope of consolidation specified in the EU regulation no. 575/2013 (the CRR). The KPIs based on the prudential consolidated situation together with qualitative information are disclosed in the consolidated LHV Group Annual report EU taxonomy reporting section 5.5.2 which includes the disclosure in the form of Taxonomy tables 1, 2 and 3.

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

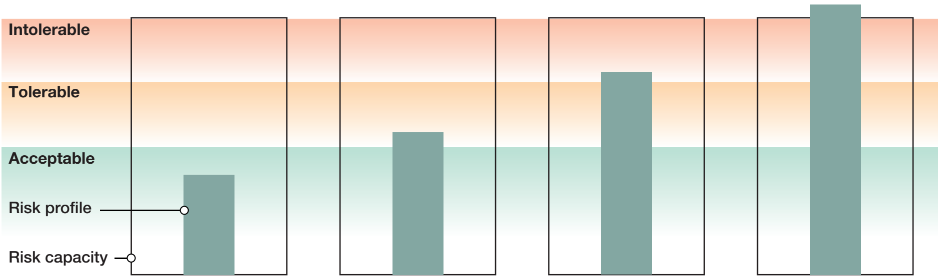
- Risk tolerance levels
- Measurement of risks
- Rights and limits

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.

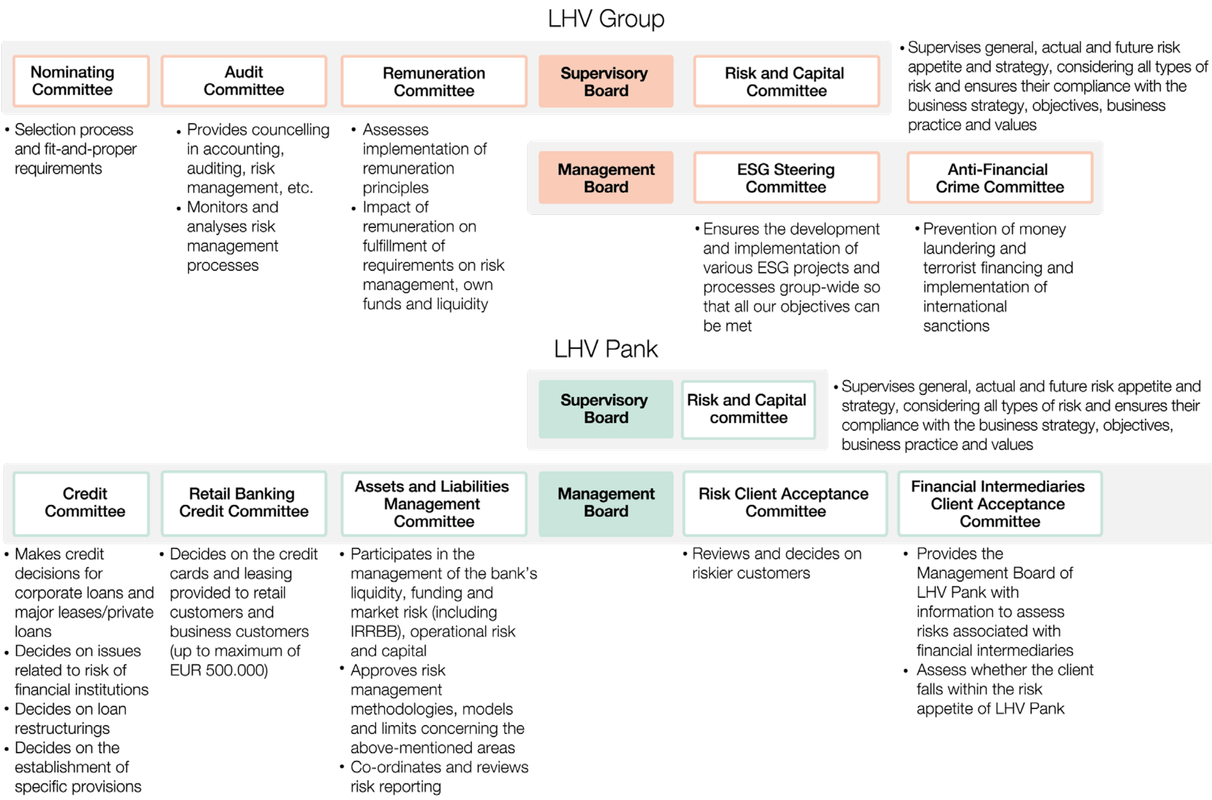
Risk capacity – the maximum amount of risk LHV is capable to take given its capital base, its risk management and control capabilities, and its regulatory constraints.

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 solvency risk, credit risk, market risk, operational risk, funding and liquidity risk, insurance risk and financial crime risk. The risk appetite limits are defined in each of the respective risk policies, which are approved by the Supervisory Board. The policies are accompanied of 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 LHV Group	Risk report	Quarterly	All main risk types
		Compliance overview	Monthly	Compliance risk
		ICAAP report, ICAAP macro scenario, SREP report	Once a year	All main risk types
Supervisory Board of LHV Pank	All the members of the Supervisory Board of LHV Pank	Risk report	Monthly	All main risk types
		ICAAP report, ICAAP macro scenario, SREP report	Once a year	All main risk types
Risk and Capital Committee of LHV Pank	Rain Lõhmus Andres Viisemann Tiina Mõis Madis Toomsalu	Risk report	Quarterly	All main risk types
Audit Committee	Kristel Aarna, Urmas Peiker Tauno Tats	Risk report	Quarterly	All main risk types
CEO of the LHV Group, the chairman of the Supervisory Board of LHV Pank	Madis Toomsalu	Risk report	Monthly	All main risk types
Assets and Liability Committee of LHV Pank	Management Board members of LHV Pank, Head of Treasury	Risk report	Monthly	Credit risk, market risk, interest rate risk, liquidity risk, operational risk
		Business continuity test and planning	After each test	Operational risks
		Risk self-assessment	After assessment	Operational risks
Management Board of LHV Pank	Management Board members of LHV Pank	Compliance overview	Once in a year	Compliance risks
		Anti-financial crime overview	Once in a year	Financial crime risks
		Monitoring of legislation	Monthly	Compliance risks
		Compliance audit	After each 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, LHV has 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 framework for addressing the main risk types the Group is more significantly exposed to, including solvency risk, credit risk, market risk, funding and liquidity risk, operational risk, and financial crime 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 an exclusion 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 CRD IV and CRD V, 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 & V also define 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.

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 2023 was EUR 557,561 thousand (31 December 2022: EUR 494,956 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.
- Within the Group's legal structure, the capital should be located as high as possible. This increases the Group's ability to allocate the capital to subsidiaries based on their business needs.

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 CRD IV, 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 ECB 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 1.5%. Only systemic risk buffer is currently set at 0.0% (imposed by the 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 2023 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 requirements	**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	1.50%	1.50%	1.50%
Regulatory capital requirements	**12.41%**	**14.55%**	**17.40%**
Pillar 2 guidance	2.00%	2.00%	2.00%
Capital requirements total	**14.41%**	**16.55%**	**19.40%**

In addition to the regulatory capital requirements, the ECB 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 LHV Pank'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 indicated at 26.30% for MREL-TREA and 5.91% for MREL-LRE. The interim targets were at 19.08% for MREL-TREA and 5.91% for MREL-LRE. To distribute earnings, additional buffers must be applied on top of the abovementioned targets. Each year the regulator will recalibrate the MREL requirements.

Internal capital adequacy targets as at 31 Dec 2023 were as follows:

Internal capitalisation targets of LHV Group	%
Core Tier 1 capital adequacy	14.70%
Tier 1 capital adequacy	16.85%
Total capital adequacy	19.70%
MREL-TREA (until 2024)	19.50%
MREL-TREA (starting from 2024)	26.50%
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 2024 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 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 Group follows both regulatory requirements and capitalisation targets in daily capital management.

Capital management in 2023

As a credit institution, LHV Pank has a capital adequacy requirement on a solo basis. No regulatory capital requirements have been established for other LHV Pank consolidation group companies.

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

LHV Group issued EUR 35 million of Tier 2 bonds in October 2023. The issue was very successful and was oversubscribed by more than 16 times. Subsequently, EUR 40 million of Tier 2 bonds were called back in November 2023 because the bonds would have otherwise become inefficient as capital instruments. Also, the Group has strong internal capital generation through profits.

The Group's level of net own funds amounted to EUR 547,687 million as at 31 Dec 2023 (31 Dec 2022: EUR 484,553 million).

Total capital adequacy level was as at the end of the reporting period of 22.07% (31 Dec 2022: 21.86%). The Group's internal target for total capital adequacy was changed in December 2023 by Supervisory Board and stands now at 18.7% (was 18.9%). The Group 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 Group has complied with all capital requirements during the financial year and in previous year.

The Group's leverage ratio stood at 6.95% as at the end of 2023 (31 Dec 2022: 6.28%). The Group is not subject to MREL requirements on an individual basis.

Capital base

EUR thousand	31 Dec 2023	31 Dec 2022
Paid-in share capital	141,500	141,500
Legal reserves transferred from net profit	12,669	8,736
Accumulated profit	222,187	147,685
Intangible assets (subtracted)	-2,945	-2,881
Profit for accounting period (COREP)	70,142	78,656
Deductions	-9,300	-2,643
Tier 1 capital	**434,253**	**371,053**
Additional Tier 1 capital	53,000	53,000
Total Tier 1 capital	**487,253**	**424,053**
Subordinated debt	60,434	60,500
Total Tier 2 capital	**60,434**	**60,500**
Net own funds for capital adequacy calculation	**547,687**	**484,553**
Capital requirements		
Central governments and central bank under standard method	0	0
Credit institutions and investment companies under standard method	23,951	11,355
Companies under standard method	1,293,686	1,202,058
Retail claims under standard method	225,907	218,342
Public sector under standard method	0	0
Housing real estate under standard method	583,503	506,767
Overdue claims under standard method	19,759	8,004
Particularly high-risk assets	42,451	47,032
Other assets under standard method	50,473	39,247
Total capital requirements for covering the credit risk and counterparty credit risk	**2,239,730**	**2,032,805**
Capital requirement against foreign currency risk under standard method	2,514	7,167
Capital requirement against interest position risk under standard method	0	0
Capital requirement against equity portfolio risks under standard method	745	740
Capital requirement against credit valuation adjustment risks under standard method	1,966	2,228
Capital requirement for operational risk under base method	236,380	173,468
Total capital requirements for adequacy calculation	**2,481,335**	**2,216,408**
Capital adequacy (%)	**22.07**	**21.86**
Tier 1 Capital Ratio (%)	**19.64**	**19.13**

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. Therefore, management 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. The responsibilities of the 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 consumer 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 considers 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 cooling economy

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 year 2023, the Estonian economy was in a mild recession. So far, the cooling economy has had only slight negative impact on the credit portfolio quality. The forborne and the overdue portfolio have been increasing in consumer finance and somewhat also among corporates throughout the year 2023. As precaution measure, the lending principles have been revised to more restrictive in consumer finance, while impairment allowance levels increased across all credit portfolios, due to uncertain outlook. 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 LHV Pank'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
Endangered plant and animal species, well-being of animals	• Those engaged in trading in endangered or Red List plants and animals; • 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 Organisation; • 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 has been developed in cooperation with environmental and social field experts. The heat map highlights environmental and social risks assessment for each individual economic sector, considering 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	2023	2022
Environmental and climate change risk (E)	High	13.5%	10.5%
	Medium	58.0%	56.3%
	Low	28.5%	33.1%
Social risk (S)	High	13.5%	10.6%
	Medium	63.4%	57.5%
	Low	23.1%	32.0%

For exposures related to higher ESG risk (high or medium sectoral risk level according to the heatmap) and risk exposures above EUR 0.5 million, a more intensive analysis is conducted regarding the client's openness and management of ESG risks. This assessment is complemented by a tool for corporate client ESG analysis, which employs a quantifiable methodology to focus on the most critical ESG factors in each sector. With the help of this tool LHV can manage ESG risks at both client and portfolio levels by calculating sector risk levels and client-specific ESG ratings. The rating is based on 1) determining the openness to each sector's ESG factors (physical climate risks, transition risk, water usage, waste management, employee health and safety) based on the client's primary economic activities and 2) assessing the client's ESG governance capabilities through a management questionnaire.

2.1 Credit risk measurement and distribution

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

a) Cash and cash equivalents, 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) Cash and cash equivalents, due from central 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 using expert-based rating model. 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.

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. The scoring process is carried out at the time of loan application, and it is one of the criteria for issuing the credit. The PD estimate is calculated based on social-demographic, delinquency and other characteristics. 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 statistical scoring PD models are used. 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	SMEs, incl. micro enterprises	Loans to companies with total exposure to LHV <= EUR 500 thousand, loans to apartment associations 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		

- **Retail**

In retail portfolio, the risk assessment is firstly done at loan origination. After the initial recognition, the transactional and payment behaviour of the borrower is monitored and incorporated into monthly automated update of risk estimates. Any other known information about the borrower which impacts their creditworthiness – such as financial statements of legal entities – is also incorporated into the 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.

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.

- **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 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.

The LGD and CCF estimates are categorised across product types, collateralisation, and remaining balance.

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 Estonian Business and Innovation Agency, 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:

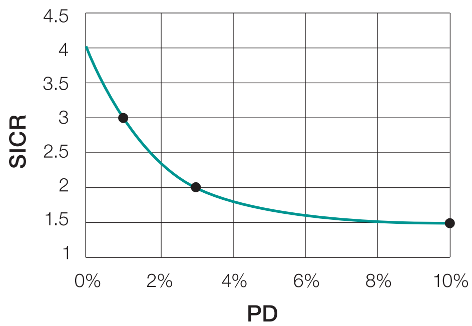
Quantitative criteria

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:

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 > 2.50+exp(0.45-50.00*Initial PD_life)

Retail portfolio

To illustrate the formula, see the SICR curve graphic below. In addition to the curve, the PD increase must 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.

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 2024	28 Feb 2024	31 Mar 2024	30 Apr 2024	31 May 2024	30 Jun 2024	31 Jul 2024	31 Aug 2024	30 Sep 2024
(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 31/12/2023 [Sum (6)]	18.85								

Note. Discounting is done, assuming the current reporting date 31 December 2023 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.

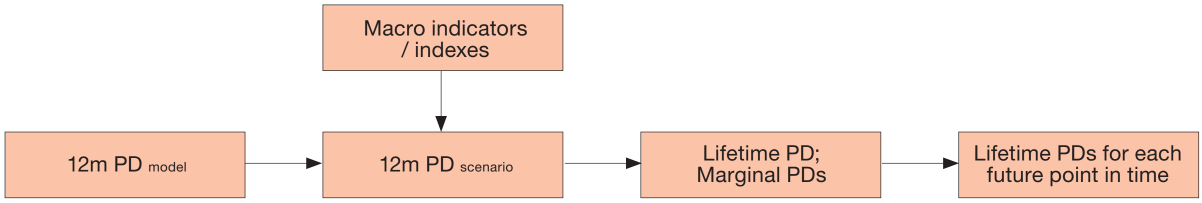
	IFRS 9 parameters
PD	• 12-month PD; lifetime PD broken down further into marginal probabilities for sub-periods • Forward-looking PiT estimate, reflecting assessment of current and future economic conditions, and a range of possible future outcomes • No regulatory floors or margins of conservatism applied
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 is discussed in detail 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 individuals credit portfolios

The relative importance of selected macro indicators for private individuals credit portfolios are shown in the table below.

	Weights
Euribor + Margin	29%
HPI growth	14%
Household consumption growth	19%
Real GDP growth	17%
Unemployment rate	21%
Total	**100%**

Note. The relative importance of each of the indicator is calculated based on the indicator's 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 Asset and Liabilities Committee.

The most significant period-end assumptions used for the ECL estimate as at 31 December 2023 are set out below. The base, downside and upside scenarios were used for all portfolios.

Assumptions in companies ECL estimate. valid at 31 Dec 2023

	Base scenario		Downside scenario		Upside scenario	
General macro-financial indicators	**2024E**	**2025E**	**2024E**	**2025E**	**2024E**	**2025E**
Real GDP growth. %	-0.4%	3.2%	-1.0%	2.0%	0.0%	4.0%
Household consumption. %	0.1%	3.3%	-0.5%	2.5%	0.5%	3.9%
Government consumption. %	3.5%	-1.1%	-1.0%	0.0%	4.5%	0.0%
Gross fixed capital formation. %	-5.0%	5.6%	-7.0%	3.6%	-3.0%	7.5%
Exports of goods and services. %	-1.3%	3.5%	-2.3%	1.5%	0.0%	4.0%
Imports of goods and services. %	-3.1%	3.2%	-4.5%	1.5%	0.0%	4.5%
Nominal GDP. EUR million	39,100	41,319	39,345	41,537	39,286	41.756
GDP deflator. % change	4.3%	2.4%	5.7%	3.5%	3.8%	2.2%
Consumer price growth. %	3.4%	1.9%	5.0%	4.0%	3.0%	1.7%
Unemployment rate. %	9.0%	8.1%	9.5%	8.5%	6.7%	6.5%
Change in employment. %	-3.3%	0.1%	-3.9%	0.0%	-1.9%	1.0%
Net monthly wage growth. %	4.2%	4.3%	3.6%	3.8%	4.6%	5.3%
House price index growth. %	-5.0%	5.0%	-6.0%	3.0%	-3.0%	5.5%
Euribor 6m	3.3%	2.5%	3.5%	3.3%	3.2%	2.4%
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	**2024E**	**2025E**	**2024E**	**2025E**	**2024E**	**2025E**
Total - all NACE activities	4.8%	6.6%	5.8%	8.3%	4.7%	7.7%
Agriculture. forestry. and fishing	-0.5%	5.7%	0.2%	5.6%	1.7%	6.3%
Industrial sector. except construction	3.9%	6.3%	7.8%	6.2%	5.1%	6.3%
Industrial sector. except construction and manufacturing (mostly energy related)	3.9%	3.7%	12.5%	3.7%	3.8%	6.3%
Manufacturing	3.9%	7.5%	5.6%	7.4%	5.7%	6.3%
Construction	7.7%	9.4%	2.7%	19.8%	7.4%	8.1%
Wholesale and retail trade. transport. accommodation. and food service activities	4.5%	6.3%	8.9%	9.1%	4.4%	6.9%
Information and communication	6.7%	7.8%	6.1%	8.4%	7.3%	7.7%
Financial and insurance activities	6.3%	0.9%	7.1%	0.8%	1.4%	7.3%
Real estate activities	5.1%	7.6%	7.2%	7.5%	5.6%	8.3%
Professional. scientific. and technical activities; administrative and support service activities	5.2%	8.9%	6.0%	8.8%	5.8%	9.5%
Public administration. defence. education. human health and social work activities	4.6%	5.7%	1.0%	8.6%	2.4%	9.4%
Arts. entertainment. and recreation; other service activities; activities of household and extra-territorial organisations and bodies	2.0%	6.6%	2.3%	8.0%	3.8%	6.3%

The weightings assigned to each economic scenario were as follows:

Weights of economic scenarios

	Base scenario	Downside scenario	Upside scenario
Valid on 31 Dec 2023	60%	25%	15%
Valid on 31 Dec 2022	60%	25%	15%

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%

2.2.5 Credit 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 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			35	100	100	100	100	100	100	100
Secured (immovable property collateral)				25	35	55	70	80	85	100
Secured (other collateral)				25	35	55	80	100	100	100
Export credit guarantee/insurance								100	100	100

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 must 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 2023

EUR thousand	Note	Estonia	Germany	Other EU	USA	UK	Other	Total
Cash and cash equivalents, due from central banks and investment companies	7	2,440,148	0	367,348	27,363	2,887	146	**2,837,892**
Financial assets at fair value	8	319	6	6,586	29	1	4	**6,945**
Financial assets measured at amortised cost	8	166,205	0	155,683	0	0	0	**321,888**
Loans and advances to customers	9	3,448,834	845	25,917	560	67,346	5,011	**3,548,513**
Receivables from customers	10	17,833	0	0	0	0	0	**17,833**
Other financial assets	11	0	0	0	100	0	0	**100**
Total financial assets		**6,073,339**	**851**	**555,534**	**28,052**	**70,234**	**5,161**	**6,733,171**
Amounts owed to central banks (TLTRO)	13	0	0	0	0	0	0	**0**
Deposits from customers	13	4,094,733	132,432	985,299	72,933	220,184	29,139	**5,534,720**
Loans received and debt securities in issue	13	0	0	486,568	0	0	0	**486,568**
Subordinated debt	16	114,054	0	0	0	0	0	**114,054**
Accounts payable and other financial liabilities	14	78,561	0	0	0	0	0	**78,561**
Financial liabilities at fair value	8	1,843	0	0	0	0	0	**1,843**
Total financial liabilities		**4,289,191**	**132,432**	**1,471,867**	**72,933**	**220,184**	**29,139**	**6,215,746**

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

EUR thousand	Note	Estonia	Germany	Other EU	USA	UK	Other	Total
Cash and cash equivalents, due from central 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	0	0	384,149	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		**3,977,432**	**5,292**	**1,178,250**	**14,891**	**452,415**	**33,385**	**5,661,665**

2.3.2 Distribution of loans granted by industry

Distribution of loans granted by industry (net)

EUR thousand	31 Dec 2023	%	31 Dec 2022	%
Individuals	1,356,775	38.24%	1,245,358	39.08%
Agriculture	100,564	2.83%	79,448	2.49%
Mining and quarrying	1,471	0.04%	1,630	0.05%
Manufacturing	173,535	4.89%	154,069	4.83%
Energy	175,504	4.95%	93,170	2.92%
Water and utilities	17,435	0.49%	29,129	0.91%
Construction	97,056	2.74%	108,401	3.40%
Wholesale and retail	196,774	5.55%	148,560	4.66%
Transport and logistics	75,426	2.13%	24,831	0.78%
Hotels and restaurants	15,686	0.44%	30,742	0.96%
Information and communication	16,260	0.46%	14,301	0.45%
Financial services	169,089	4.77%	127,950	4.01%
Real estate	809,392	22.81%	777,830	24.41%
Professional, scientific, and technical activities	84,613	2.38%	75,174	2.36%
Administrative activities	102,490	2.89%	116,551	3.66%
Public management	63,062	1.78%	79,145	2.48%
Education	4,414	0.12%	5,445	0.17%
Health	17,414	0.49%	11,542	0.36%
Art and entertainment	57,939	1.63%	55,271	1.73%
Other servicing activities	13,614	0.38%	8,442	0.26%
Total (Note 9)	**3,548,513**	**100.00%**	**3,186,989**	**100.00%**

2.3.3 Loan portfolio by ratings

Distribution of legal entity financing by internal ratings

EUR thousand	31 Dec 2023	31 Dec 2022	Grading
3 low credit risk	0	0	Investment grade
4 low credit risk	8,741	34,069	
5 low credit risk	100,869	48,410	
6 low credit risk	385,896	365,287	
7 medium credit risk	507,531	433,152	
8 medium credit risk	649,032	591,503	
9 heightened credit risk	255,224	196,840	
10 high credit risk	52,606	39,252	Non-investment grade (incl. special monitoring)
11 high credit risk	38,858	55,843	
12 non-satisfactory rating	12,011	18,912	
13 insolvent	9,924	717	Default
Total corporates	**2,020,692**	**1,783,985**	
Retail SMEs	171,046	157,646	
Total	**2,191,738**	**1,941,631**	

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

Credit quality of commitments accounted for off the statement of financial position

(unused loan commitments for corporate loans and financial guarantees)

EUR thousand	31 Dec 2023	31 Dec 2022
3 low credit risk	0	100,000
4 low credit risk	0	35,000
5 low credit risk	69,556	10,078
6 low credit risk	58,147	106,057
7 medium credit risk	45,577	81,891
8 medium credit risk	282,101	143,622
9 heightened credit risk	81,093	109,119
10 high credit risk	2,804	7,742
11 high credit risk	1	3,346
12 non-satisfactory rating	636	1,718
13 insolvent	4,466	0
Non-rated (retail clients)	68,290	85,142
Total	**612,671**	**683,715**

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 2023 (net)

EUR thousand	Stage 1	Stage 2	Stage 3	Allowance for credit losses	Total
Individuals	1,266,071	89,683	7,593	-6,572	1,356,775
Agriculture	96,489	4,410	6	-341	100,564
Mining and quarrying	915	583	54	-81	1,471
Manufacturing	137,540	28,214	12,816	-5,035	173,535
Energy	176,400	170	12	-1,078	175,504
Water and utilities	17,619	25	0	-209	17,435
Construction	83,200	15,426	33	-1,603	97,056
Wholesale and retail	182,818	14,518	1,336	-1,898	196,774
Transport and logistics	66,531	9,586	0	-691	75,426
Hotels and restaurants	12,571	2,862	406	-153	15,686
Information and communication	15,725	551	45	-61	16,260
Financial services	170,081	174	0	-1,166	169,089
Real estate	727,905	87,849	824	-7,186	809,392
Professional, scientific, and technical activities	81,198	3,307	376	-268	84,613
Administrative activities	100,311	2,746	17	-584	102,490
Public management	58,391	4,946	0	-275	63,062
Education	2,487	3,300	3	-1,376	4,414
Health	17,002	504	0	-92	17,414
Art and entertainment	37,591	21,657	0	-1,309	57,939
Other servicing activities	12,858	827	7	-78	13,614
Total	**3,263,703**	**291,338**	**23,528**	**-30,056**	
Allowance for credit losses	-12,237	-9,766	-8,053		
Total loan portfolio	**3,251,466**	**281,572**	**15,475**		**3,548,513**

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**

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

EUR thousand	Stage 1	Stage 2	Stage 3	Purchased or Initiated credit impaired	Allowance for credit losses	Total
Corporate lending	1,881,294	178,453	13,841	0	-21,399	2,052,189
Consumer financing	90,697	16,128	2,473	0	-4,310	104,988
Investment financing	9,951	23	7	0	-11	9,970
Leasing	141,419	24,277	2,103	0	-2,107	165,692
Private lending	1,140,342	72,457	5,104	0	-2,229	1,215,674
Total as at 31 Dec 2023	**3,263,703**	**291,338**	**23,528**	**0**	**-30,056**	**3,548,513**
Corporate lending	1,687,958	145,015	636	0	-15,435	1,818,174
Consumer financing	94,818	6,661	1,145	0	-2,107	100,517
Investment financing	10,532	4	0	0	-13	10,523
Leasing	122,833	28,419	1,442	0	-2,008	150,686
Private lending	997,972	105,887	4,244	0	-1,014	1,107,089
Total as at 31 Dec 2022	**2,914,113**	**285,986**	**7,467**	**0**	**-20,577**	**3,186,989**

Stage 1

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	1,678,196	720,712	-410,598	-107,016	-10,884	1,870,410
Consumer financing	94,376	40,803	-35,940	-8,542	-536	90,161
Investment financing	10,519	2,233	-2,771	-30	-9	9,942
Leasing	122,459	67,362	-47,220	-1,182	-476	140,943
Private lending	997,689	196,413	-81,800	28,040	-332	1,140,010
Total	**2,903,239**	**1,027,523**	**-578,329**	**-88,730**	**-12,237**	**3,251,466**

Stage 2

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	139,644	9,816	-64,204	93,197	-6,261	172,192
Consumer financing	6,035	6,519	-3,280	6,854	-1,905	14,223
Investment financing	4	1	-7	25	0	23
Leasing	27,361	4,142	-7,381	155	-884	23,393
Private lending	105,310	6,004	-8,911	-29,946	-716	71,741
Total	**278,354**	**26,482**	**-83,783**	**70,285**	**-9,766**	**281,572**

Stage 3

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	334	601	-912	13,818	-4,254	9,587
Consumer financing	106	265	-190	2,292	-1,869	604
Investment financing	0	0	1	6	-2	5
Leasing	866	274	-541	1,504	-747	1,356
Private lending	4,090	56	-948	1,906	-1,181	3,923
Total	**5,396**	**1,196**	**-2,590**	**19,526**	**-8,053**	**15,475**

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 2023 (gross)

EUR thousand	1 > 2	1 > 3	2 > 1	2 > 3	3 > 1	3 > 2
Corporate lending	141,777	977	46,990	11,896	0	16
Consumer financing	7,343	890	970	739	0	111
Investment financing	18	7	0	0	0	0
Leasing	7,393	413	6,780	425	0	16
Private lending	35,153	1,013	96,862	1,513	0	646
Total	**191,684**	**3,300**	**151,602**	**14,573**	**0**	**789**

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 of secured loans is presented as unsecured loans.

Loans against collateral as at 31 Dec 2023 (net)

EUR thousand	Corporate lending	Consumer financing	Investment financing	Leasing	Private lending	Total
Listed securities	0	0	8,925	0	0	**8,925**
Unlisted equity securities	23,419	0	0	0	3,573	**26,992**
Mortgages, real estate	1,185,368	0	0	0	1,180,791	**2,366,159**
Guarantee of Estonian Business and Innovation Agency, and Rural Development Foundation	45,859	0	0	0	4,690	**50,549**
Pledges of rights of claim	147,919	0	0	0	0	**147,919**
Deposits	6,942	0	658	0	1,300	**8,900**
Leased assets	0	0	0	130,340	0	**130,340**
Others	37,695	0	0	0	7,930	**45,625**
Unsecured loans or unsecured part of secured loans	604,987	104,988	387	35,352	17,390	**763,104**
Total	**2,052,189**	**104,988**	**9,970**	**165,692**	**1,215,674**	**3,548,513**

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 Estonian Business and Innovation Agency, 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 or unsecured part of secured 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**

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 2023	**1,774,369**	**2,840,469**	**1,774,144**	**1,011,080**	**3,548,513**	**3,851,549**
Corporate lending	738,049	1,066,778	1,314,140	709,152	2,052,189	1,775,930
Consumer financing	0	0	104,988	0	104,988	0
Investment financing	7,690	28,055	2,280	1,893	9,970	29,948
Leasing	24,840	36,880	140,852	105,500	165,692	142,380
Private lending	1,003,790	1,708,756	211,884	194,535	1,215,674	1,903,291
31 Dec 2022	**1,740,956**	**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	100,516	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

Over and under-collateralised loans by stages as at 31 Dec 2023 (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	**1,601,382**	**2,568,667**	**1,650,081**	**939,492**	**3,251,463**	**3,508,159**
Corporate Lending	642,083	940,685	1,228,326	654,198	1,870,409	1,594,883
Consumer Financing	0	0	90,161	0	90,161	0
Investment Financing	7,676	28,032	2,265	1888	9,941	29,920
Leasing	18,937	27,210	122,005	92,015	140,942	119,225
Private Lending	932,686	1,572,740	207,324	191,391	1,140,010	1,764,131
Stage 2	**162,772**	**251,716**	**118,802**	**68,017**	**281,574**	**319,733**
Corporate Lending	90,801	118,633	81,392	51,598	172,193	170,231
Consumer Financing	0	0	14,223	0	14,223	0
Investment Financing	9	15	14	4	23	19
Leasing	4,781	7,823	18,613	13,271	23,394	21,094
Private Lending	67,181	125,245	4,560	3,144	71,741	128,389
Stage 3	**10,215**	**20,086**	**5,261**	**3,571**	**15,476**	**23,657**
Corporate Lending	5,166	7,459	4,421	3,357	9,587	10,816
Consumer Financing	0	0	604	0	604	0
Investment Financing	5	9	1	0	6	9
Leasing	1,121	1,847	235	214	1,356	2,061
Private Lending	3,923	10,771	0	0	3,923	10,771

2.4.5 ECL sensitivity analysis

The following tables show the impact of changing the PD thresholds for SICR on the ECL allowance as at 31 December 2023 and 31 December 2022. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognised.

Loan portfolio as at 31 Dec 2023

EUR thousand	Effect on impairment
+10% change in SICR	-195
-10% change in SICR	141
SICR with 0.5% threshold	4
SICR with 1.5% threshold	-5

Loan portfolio as at 31 Dec 2022

EUR thousand	Effect on impairment
+10% change in SICR	-379
-10% change in SICR	340
SICR with 0.5% threshold	5
SICR with 1.5% threshold	-9

As evidenced by the tables, changing SICR by +/- 10% or changing the 1% threshold to 0.5% or 1.5% have limited impact on the overall ECL of the Group.

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

Retail portfolio

- Unemployment rate
- Interest rate
- Household consumption growth
- Real GDP growth
- House price index
- GVA

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 +/- 5pp, 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 2023 and 31 December 2022.

31 Dec 2023

EUR thousand	60-10-30 (base/up/down)	60-20-20 (base/up/down)
Change in scenario weights	1,033	-1,052

31 Dec 2022

EUR thousand	65-10-30 (base/up/down)	60-20-20 (base/up/down)
Change in scenario weights	896	-896

Set out below are the changes to the ECL as at 31 December 2023 and 31 December 2022 that would result from reasonably possible changes in these parameters compared with the actual values used in the Group's economic variable assumptions:

Impact on ECL, 31 Dec 2023

EUR thousand	Impact of increase	Impact of decrease
Unemployment rate +/-1pp	102	-104
Interest rate +/- 1pp	129	-218
Household consumption growth +/-1pp	-49	45
Real GDP growth +/-1pp	-42	40
House price index +/- 5pp	-64	54
Gross value added by sectors, YoY growth rates +/- 5pp	-192	266

Impact on ECL, 31 Dec 2022

EUR thousand	Impact of increase	Impact of decrease
Unemployment rate +/-1pp	135	-156
Interest rate +/- 1pp	177	-276
Household consumption growth +/-1pp	-89	88
Real GDP growth +/-1pp	-83	85
House price index +/- 5pp	-12	8
Gross value added by sectors, YoY growth rates +/- 5pp	-177	228

The Group has also performed scenarios where both PD and LGD estimates where modified. The impact of these 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.

2023

EUR thousand	Impact on credit loss allowances
LGD negative 0.80	871
LGD negative 0.90	-831
Average PiT PD -0.5pp	-3,351
Average PiT PD +0.5pp	3,056

2022

EUR thousand	Impact on credit loss allowances
LGD negative 0.85	803
LGD negative 0.95	-608
Average PiT PD -0.5pp	-3,527
Average PiT PD +0.5pp	3,369

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 Group is to correctly identify and quantify market risk and ensure that risk-conscious decisions are taken on market risk.

The Group is exposed to the following types of market risk:

- Foreign exchange risk from the Group's net open positions in foreign currencies;
- Price risk from the Group'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.

The Group's market risk management is documented in the market risk management policy and other internal rules, which set out the Group'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 LHV Pank 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 Group's foreign currency assets and liabilities. Most items in the Group's statement of financial position are denominated in euros but a mismatch could result from the foreign currency transactions of LHV Pank's customers. Additionally, there is some foreign currency risk inherent in the fund units of own-managed pension funds that must be held by LHV Varahaldus as prescribed by legislation.

Foreign currency risk is measured by estimating the potential loss to the Group 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 Group's net own funds.

In addition to the risk appetite levels approved at the LHV Group level, LHV Pank's ALCO has implemented additional risk limits for various types of market risks in LHV Pank. Foreign currency risk limits in LHV Pank 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 +/- 6% which is in line with the stress scenario used by the Group for measuring foreign currency risk of its net open positions (2022: +/- 7%). The Group's foreign currency risk exposure is very low.

Impact on statement of profit or loss

EUR thousand	2023	2022
USD exchange rate	+/-47	+/- 375
SEK exchange rate	+/-10	+/-2
GBP exchange rate	+/-24	+/-68
CHF exchange rate	+/-9	+/-4

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 Group 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 (property, plant and equipment 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 Group's business is conducted in euro currency.

Currency risk exposures as at 31 Dec 2023

EUR thousand	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Financial assets bearing currency risk								
Cash and cash equivalents, due from central banks and investment companies	7	2,803,213	1,047	9,734	1,480	13,570	8,849	**2,837,892**
Investments in debt and equity securities	8	322,524	1	0	6,275	31	2	**328,833**
Loans and advances to customers	9	3,472,835	23	66,674	189	8,676	116	**3,548,513**
Receivables from customers	10	17,211	0	317	168	1,822	-1,685	**17,833**
Other financial assets	11	100	0	0	0	0	0	**100**
Total financial assets bearing currency risk		**6,615,883**	**1,071**	**76,725**	**8,112**	**24,099**	**7,281**	**6,733,171**
Financial liabilities bearing currency risk								
Amounts owed to central banks (TLTRO)	13	0	0	0	0	0	0	**0**
Deposits from customers	13	5,334,564	9,494	20,924	8,867	151,070	9,801	**5,534,720**
Loans received and debt securities in issue	13	486,568	0	0	0	0	0	**486,568**
Financial liabilities at fair value	8	1,843	0	0	0	0	0	**1,843**
Accounts payable and other financial liabilities	14	68,067	30	1,380	479	6,574	2,031	**78,561**
Subordinated debt	16	114,054	0	0	0	0	0	**114,054**
Total financial liabilities bearing currency risk		**6,005,096**	**9,524**	**22,304**	**9,346**	**157,644**	**11,832**	**6,215,746**
Open gross position derivative assets at contractual value		0	8,359	0	1,334	133,071	5,633	**148,397**
Open gross position derivative liabilities at contractual value		94,218	0	54,179	0	**0**	0	**148,397**
Open foreign currency position		**516,569**	**-94**	**242**	**100**	**-474**	**1,081**	**517,425**

Currency risk exposures as at 31 Dec 2022

EUR thousand	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Financial assets bearing currency risk								
Cash and cash equivalents, due from central 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	9,403	0	**171,694**
Open foreign currency position		**381,747**	**-40**	**684**	**25**	**-3,748**	**-89**	**378,578**

3.2 Price risk

Price risk arises from securities held by the Group 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 Group in a stress scenario. The loss from price risk in the stress scenario should not exceed a prescribed percentage of the Group'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 Group.

A sensitivity analysis has been performed to show the effect of movements in securities prices on the net result of the Group. The potential securities price movements used in the sensitivity analysis are in line with the stress scenarios used by the Group for measuring price risk and have been derived from actual historical volatility of the instruments included in the relevant portfolios. Only LHV Pank's debt securities portfolio that is measured in fair value through profit and loss is subject to price risk.

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

EUR thousand	2023	2022
Equity securities and fund units +/-26% (2022: +/-25%)	+/-96	+/-92
Debt securities +/-2.0%	+/-126	+/-0

It can be seen that the majority of the Group's price risk results from the debt securities held in the Group'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 profit and loss statement. The Group 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), imperfect correlation 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 LHV Pank's net own funds.

LHV Pank'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.

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. 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. 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 10 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.
- Term deposit redemption rate is used in the assessment of the early redemption of the term deposits.
- 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 2023

EUR thousand	Change in the economic value of equity	Change in the next 12 months' net interest income
Parallel shock up	-7,614	25,816
Parallel shock down	-10,692	-50,172
Steepener shock	9,279	-29,155
Flattener shock	-10,623	20,552
Short rates shock up	-9,787	27,645
Short rates shock down	-90	-53,643

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

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

Interest rate sensitivity gap as at 31 Dec 2023

EUR thousand	Note	Up to 3 months	3-12 months	1-5 years	Over 5 years	Subtotal	Accrued interest	Impair-ments	Total
Financial assets									
Cash and cash equivalents, due from central banks and investment companies	7	2,837,892	0	0	0	2,837,892	0	0	2,837,892
Financial assets at fair value (debt securities)	8	6,945	0	0	0	6,945	0	0	6,945
Financial assets measured at amortised cost (debt securities)	8	89,282	153,577	77,944	0	320,803	1,165	-80	321,888
Loans and advances to customers	9	1,638,005	1,730,394	142,508	51,795	3,562,702	15,867	-30,056	3,548,513
Total		**4,572,124**	**1,883,971**	**220,452**	**51,795**	**6,728,342**	**17,032**	**-30,136**	**6,715,238**
Financial liabilities									
Deposits from customers	13	3,343,240	1,598,719	415,656	153,002	5,510,617	24,103	0	5,534,720
Loans received and debt securities in issue	13	0	69,000	415,000	0	484,000	2,568	0	486,568
Subordinated debt	16	31,000	27,500	55,000	0	113,500	554	0	114,054
Total		**3,374,240**	**1,695,219**	**885,656**	**153,002**	**6,108,117**	**27,225**	**0**	**6,135,342**
Net interest sensitivity gap		**1,197,884**	**188,752**	**-665,204**	**-101,207**	**620,225**			

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									
Cash and cash equivalents, due from central 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 debt	16	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**			

3.4 Credit valuation adjustment risk

Credit valuation adjustment (CVA) risk is 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 Group applies the standardised approach to calculate the capital charge for CVA risk. The Group's capital requirement for CVA risk as of 31 December 2023 amounted to EUR 157 thousand (2022: EUR 178 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 Group assesses liquidity risk from the following separate perspectives:

- Funding risk is the risk that the Group 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 Group'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 Group 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 Group'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 Group'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 monthly.

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 Group keeps a counterbalancing buffer of high-quality liquid assets that can be used in either a market-wide or idiosyncratic stress scenario. The liquidity buffer of the Group 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 Group 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 Group is not exposed to excessive asset encumbrance that could limit its access to funding markets.

As set out in the LHV Group's funding policy, diversification of the funding profile is an important element of the Group's liquidity risk management framework. The Group'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. LHV Group has issued covered bonds to raise targeted funding for its residential mortgage loans portfolio.

It has also issued unsecured bonds which are used for both funding and for complying with the regulatory MREL requirement.

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.

Liquidity management in 2023

The Group's volume of deposits increased during 2023, mainly due to the increase of term deposits from retail and corporate customers. Deposits from financial intermediaries remained relatively stable in 2023, though they are not used for funding the Group's lending activities. The Group has also fully repaid the remaining funding obtained from the ECB by means of TLTRO loans. In 2023, the Group issued EUR 250 million of retained covered bonds (replacing prematurely cancelled EUR 100 million retained covered bonds with initial maturity 28 February 2024. Retained covered bonds can be readily used as collateral in liquidity providing operations.

The following table presents the values of the LCR and NSFR ratios in comparison to regulatory thresholds. 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 2023	Actual 31 Dec 2022
LCR	Minimum 100%	191.4%	135.6%
NSFR	Minimum 100%	157.7%	144.5%

The level of the LCR ratio improved significantly over the reporting year. The ratio was positively impacted by the rising volume of term deposits and stable retail deposits, contributing to a sound and granular deposit base and more efficient liquidity management.

The NSFR ratio improved over the year due to the Group's collection of stable retail deposits that are considered as available stable funding. The level of the ratio exceeds the regulatory and internal requirements with a wide headroom.

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 2023

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								
Deposits from customers	13	3,697,523	578,906	1,223,758	70,035	339	5,570,561	5,534,720
Loans received and debt securities in issue	13	0	0	85,318	425,250	0	510,568	486,568
Subordinated debt	16	0	33,311	31,782	63,913	0	129,006	114,054
Accounts payable and other financial liabilities	14	0	78,561	0	0	0	78,561	78,561
Unused loan commitments	19	0	495,653	0	0	0	495,653	0
Financial guarantees by contractual amounts	19	0	55,061	0	0	0	55,061	0
Foreign exchange derivatives (gross settled)		0	148,397	0	0	0	148,397	0
Financial liabilities at fair value	8	0	1,843	0	0	0	1,843	1,843
Total liabilities		3,697,523	1,391,732	1,340,858	559,198	339	6,989,650	6,215,746
Assets held for managing liquidity risk by contractual maturity dates								
Cash and cash equivalents, due from central banks and investment companies	7	2,837,892	0	0	0	0	2,837,892	2,837,892
Investments in debt and equity securities	8	0	96,722	153,577	77,944	0	328,243	328,833
Loans and advances to customers	9	0	233,162	538,946	2,606,400	1,692,834	5,071,342	3,548,513
Receivables from customers	10	0	17,833	0	0	0	17,833	17,833
Other financial assets	11	100	0	0	0		100	100
Foreign exchange derivatives (gross settled)		0	148,397	0	0		148,397	0
Total assets held for managing liquidity risk		2,837,992	496,114	692,523	2,684,344	1,692,834	8,403,807	6,733,171
Maturity gap from assets and liabilities		-859,531	-895,618	-648,335	2,125,146	1,692,495	1,414,157	

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								
Cash and cash equivalents, due from central banks and investment companies	7	2,479,240	0	0	0	0	2,479,240	2,479,240
Investments in debt and equity 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	

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 2023	31 Dec 2022
Current assets			
Cash and cash equivalents	7	35,631	84,885
Due from central bank	7	2,789,752	2,390,964
Due from investment companies	7	12,509	3,391
Financial assets at fair value through profit or loss	8	6,945	407
Financial assets measured at amortised cost	8	243,944	241,005
Loans and advances to customers	9	505,700	508,795
Receivables from customers	10	17,833	9,253
Other assets	11	2,795	2,866
Total current assets		**3,615,109**	**3,241,566**
Non-current assets			
Financial assets measured at amortised cost	8	77,944	123,225
Loans and advances to customers	9	3,042,813	2,678,194
Other financial assets	11	100	124
Property, plant and equipment	12	15,732	10,960
Intangible assets	12	2,946	2,881
Total non-current assets		**3,139,535**	**2,815,384**
Total assets		**6,754,644**	**6,056,950**
Liabilities			
Current liabilities			
Deposits from customers	13	5,469,644	4,939,370
Amounts owed to central banks (TLTRO)	13	0	147,841
Financial liabilities at fair value through profit or loss	8	1,843	3,850
Accounts payable and other liabilities	14	87,984	62,457
Subordinated debt	16	58,500	10,000
Total current liabilities		**5,617,971**	**5,163,518**
Non-current liabilities			
Deposits from customers	13	65,076	17,561
Loans received and debt securities in issue	13	486,568	384,149
Subordinated debt	16	55,000	103,500
Total non-current liabilities		**606,644**	**505,210**
Total liabilities		**6,224,615**	**5,668,728**

5. Operational risk

Operational risk is the risk of losses 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 and in other relevant operational risk management procedures. 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 18,910 thousand as at 31 December 2023 (31 December 2022: EUR 13,877 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 for this objective.

In addition to the general operational risk management 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 AFC 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.

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. Going forward continuous adaptation to supervisory expectations of the ECB and the SRB will influence compliance risk management and thus the compliance function.

7. Anti-financial crime (AFC)

7.1. AFC governance

A high level of awareness and commitment towards risk management and AFC issues is the foundation of a strong AFC culture which is further supported by continuous activities of awareness raising, information and dissemination, networking and exchange of best practices, training, and reporting. 2023 is marked as the first year where the enterprise-wide risk assessment of financial crime risks was conducted as a group-wide exercise. All obliged entities of the LHV Group assessed their risk based on the same methodology. This enables more in-depth analyses of group-wide risks and implement aligned practices that affect LHV's operations.

The Management Board and the Supervisory Board of LHV Group and LHV Pank have a strong commitment towards implementing, maintaining and developing AFC regime across all the group entities. Related policies and procedures for AFC are revised at least yearly to properly reflect changes in the environment. In 2023 the Management Board's dedicated committee was reorganised and brought to the LHV Group level, as the new AFC Committee, providing consolidated overview for financial crime issues and further possibilities for co-operation and coordination between group units in this important area.

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

7.2 AFC governance structure of LHV Group

Supervisory Board

- Gives guidelines for general AFC risk appetite
- Supervisory role
- Regular reporting

Management Board

- Adopts AFC procedures and guidelines
- Adopts risk assessment and risk appetite framework
- Receives regular input on AFC topics and provides guidance
- Accepts high risk customers

High Risk Customer Acceptance Committee

- Accepts high-risk customers (retail

Banking Services Customers Assessment Committee

- Assesses financial intermediaries prior to approval by Management Board

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

7.3 Anti-financial crime framework

AFC framework at LHV is based on 10 core principles that showcase high ethical principles, high standards of compliance and risk management. These are:

1) Risk-based approach;
2) Assessment of risks and establishment of risk appetite;
3) KYC – know-your-customer;
4) Due diligence measures – applying control measures when doing business;
5) Monitoring and screening – applying technical solutions to detect malicious activities;
6) Reporting of suspicious activities – any detected suspicions are duly reported;
7) Prohibited business relationships – certain customers or activities are not accepted;
8) Information sharing and escalation – information is shared within LHV and with our counterparts in accordance with regulations;
9) Training – key to effective financial crime prevention is knowledgeable people;
10) Data retention - records of data concerning financial fraud are retained in accordance with laws to ensure auditability and investigation.

7.4 Banking Services

Via banking services business line, LHV continued to provide services to other financial institutions (including fintech companies) that in turn can provide financial services to their own customers. Provision of correspondent services to other financial institutions present 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 clients of banking services business line. LHV employs dedicated Client Relationship Managers to this sector, alongside specific first-line and second-line units that monitor and mitigate potential 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, AFC 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 periodic on-site visits to assess AFC framework of clients. LHV employs a transaction monitoring programme designed to identify characteristics in client behaviour that indicate financial crime. If 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 AFC system and the outlook

The sanctions' packages introduced by the EU and the western allies, including UK, as a direct response to the Russian war of aggression against Ukraine brought out the need to allocate substantial resources to the implementation of sanctions also by LHV. Throughout the year the decoupling the Estonian and, at large, European economy from the Russian oligarchs and Russian and Belorussian impact continued. The growing number and reach of sanctions' packages grew increasingly difficult to navigate. To ensure the effective implementation of international sanctions, LHV implemented multiples measures throughout the year, such as introducing increased pricing for payment transactions related to high-risk jurisdictions in May, effectively limiting payments related to countries linked to potential sanctions evasion attempts and restricting card payments connected to Belarus in September 2023. Therefore, this showcases the focus to strengthen the scope of the control measures to be implemented to avoid the risks of circumvention of sanctions.

The regulatory landscape remained stable as the outcome of Estonian assessment by MONEYVAL, report published in January 2023, was perceived as positive. The ranking of Estonia in the Basel AML Index of 2023 put the country in third place globally as being least affected by ML/TF risk.

There is growing anticipation of the new EU AML Package, including the establishment of the new AML supervisory authority, AMLA, which will be laid out in detail during 2024. The regulation and harmonisation in EU will be brough to a new era, affecting LHV in the foreseeable future.

8. Other risks

8.1 Strategic risk

Strategic risk is the risk of losses, including in the form of foregone revenues or additional costs, due to poor strategical planning and/or decisions or due to poor reputation not supporting strategic goals. Strategic risk includes both business, as well as sustainability strategy risk.

Main triggers for strategic risk are changes in different external factors to which LHV does not timely and appropriately adapt to, for example competitive landscape, technological shifts, customer preferences, ESG, especially climate changes, changes in regulation, and industry and product profitability.

Strategic risk is mitigated through the well understanding of the business environment and home markets, as well as risks threatening strategic goals, and considering them in the strategy planning process.

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 ESG risks

Moving towards a greener way of doing things brings challenges and opportunities for both the economy and banks. The palpable impact of climate change and environmental degradation on the real economy and financial system stands as a force that cannot be underestimated.

ESG risk is a risk of loss resulting from current or prospective impacts of ESG factors, i.e. from environmental, social and/or governance factors, as applied directly to the Group or towards its counterparties or invested assets.

ESG risk materialises through other risk categories, such as credit risk, market risk, operational risk, liquidity and funding risk, strategic risk, i.e. acts as a cross-taxonomy risk driver. If ESG risk impact towards main risk is material, it shall be reflected, as a sub-risk under this main risk.

For the identification of material ESG risks a dedicated materiality assessment is conducted, which is the main input for setting risk appetite and relevant risk limits, as well as relevant qualitative risk management tools, for example client engagement.

To gain a thorough understanding of the risks and opportunities embedded in LHV's portfolio and services, we've embarked on an extensive materiality assessment update in 2023, a process scheduled for completion in 2024. This comprehensive undertaking involves meticulous risk and business mapping, adopting a holistic approach that spans the long, medium, and short term.

This forward-thinking approach not only underscores our commitment to responsible business practices but ensures that our risk management frameworks and strategic initiatives are dynamic and responsive, aligned with the evolving challenges and opportunities that define our path forward.

8.3 Reputational risk

Reputational risk, i.e. loss of reputation is one of negative consequences resulting from several LHV main risks. Loss of reputation occurs due to failure to meet stakeholders' (investors, employees, regulators, clients etc) expectations as a result of any event, behaviour, action or inaction, either by LHV itself, its employees or those with whom LHV is associated, that may cause stakeholders to form a negative view of LHV, either justified or not.

Good reputation and trust from existing and possible new clients, investors and employees is one of the enablers to achieve strategic business goals. Reputational risk is treated as a gross-taxonomy risk consequence and its management is integrated into existing risk management processes covering LHV's main risk types.

Consolidated statement of profit or loss and other comprehensive income

EUR thousand	Note	2023	2022
Interest income		305,507	152,168
incl interest income based on EIR		286,346	145,992
Interest expense		-77,036	-22,679
Net interest income	**4**	**228,471**	**129,489**
Fee and commission income		47,917	52,889
Fee and commission expense		-20,700	-20,481
Net fee and commission income	**5**	**27,217**	**32,408**
Net gain/loss from financial assets measured at fair value	8	1,108	-1,829
Foreign exchange gain/loss		1,544	1,407
Net gain/loss from financial assets		**2,652**	**-422**
Other income		1,737	199
Staff costs	6	-44,291	-36,129
Administrative and other operating expenses	6	-40,944	-28,416
Profit before credit losses		**174,842**	**97,129**
Impairment losses on financial instruments measured at amortised cost	9	-11,372	-2,996
Profit before income tax		**163,470**	**94,133**
Income tax expense	22	-22,107	-13,260
Net profit for the year		**141,363**	**80,873**
Total comprehensive income for the reporting period		**141,363**	**80,873**
Total profit and comprehensive income attributable to:			
Owners of the parent		140,133	78,658
Non-controlling interest		1,230	2,215
Total profit and comprehensive income for the reporting period		**141,363**	**80,873**

Pages 26 to 107 are an integral part of the consolidated financial statements.

Consolidated statement of financial position

EUR thousand	Note	31 Dec 2023	31 Dec 2022
Assets			
Cash and cash equivalents	7	35,631	84,885
Due from central bank	7	2,789,752	2,390,964
Due from investment companies	7	12,509	3,391
Financial assets at fair value through profit or loss	8	6,945	407
Financial assets measured at amortised cost	8	321,888	364,230
Loans and advances to customers	9	3,548,513	3,186,989
Receivables from customers	10	17,833	9,253
Other financial assets	11	100	124
Other assets	11	2,795	2,866
Property, plant and equipment	12	8,806	7,947
Right-of-use assets	12	6,926	3,013
Intangible assets	12	2,946	2,881
Total assets		**6,754,644**	**6,056,950**
Liabilities			
Loans received from central banks (TLTRO)	13	0	147,841
Deposits from customers	13	5,534,720	4,956,931
Loans received and debt securities in issue	13	486,568	384,149
Financial liabilities at fair value through profit or loss	8	1,843	3,850
Accounts payable and other liabilities	14	87,430	61,901
Subordinated debt	16	114,054	114,056
Total liabilities		**6,224,615**	**5,668,728**
Equity			
Share capital	17	141,500	141,500
Legal reserve	17	12,669	8,736
Retained earnings		369,674	231,805
Total equity attributable to owners of the parent		**523,843**	**382,041**
Non-controlling interest		6,186	6,181
Total equity		**530,029**	**388,222**
Total liabilities and equity		**6,754,644**	**6,056,950**

Pages 26 to 107 are an integral part of the consolidated financial statements.

Consolidated statement of cash flows

EUR thousand	Note	2023	2022
Cash flows from operating activities			
Interest received		297,525	148,992
Interest paid		-51,337	-20,545
Fees and commissions received	5	47,917	52,889
Fees and commissions paid	5	-20,700	-20,481
Other income received		1,737	199
Staff costs paid		-39,747	-32,080
Administrative and other operating expenses paid		-39,988	-23,902
Income tax paid		-22,103	-11,639
Cash flows from operating activities before change in operating assets and liabilities		**173,304**	**93,433**
Net increase/decrease in operating assets:			
Net decrease in financial assets at fair value through profit or loss		-264	-35
Loans and advances to customers	9	-368,467	-518,254
Mandatory deposit at central bank	7	-7,211	8,609
Security deposits	11	24	2112
Other assets		34	4,874
Net increase/decrease in operating liabilities:			
Demand deposits of customers	13	-1,004,362	-989,318
Term deposits of customers	13	1,558,745	97,695
Repayments of loans received	13	-147,547	-49,216
Debt securities issued	13	100,135	65,000
Debt securities redeemed		0	-31,000
Financial liabilities at fair value through profit or loss		-2,007	3,693
Other liabilities		27,540	6,697
Net cash from/used in operating activities		**329,924**	**-1,305,710**
Cash flows from investing activities			
Purchase of PPE and intangible assets	12	-12,494	-7,548
Proceeds from disposal of PPE		486	0
Net changes of investment securities at fair value through profit or loss and amortised cost	8	37,175	-234,810
Net cash from/used in investing activities		**25,167**	**-242,358**
Cash flows from financing activities			
Paid in share capital	17	0	30,000
Proceeds from subordinated debt	16	0	30,000
Subordinated loans redeemed		0	-5,000
Dividends paid		-3,500	-6,000
Repayment of principal of lease liabilities		-1,693	-1,423
Net cash from/used in financing activities		**-5,193**	**47,577**
Effect of exchange rate changes on cash and cash equivalents		**1,544**	**1,407**
Net increase/decrease in cash and cash equivalents		**351,442**	**-1,499,084**
Cash and cash equivalents at the beginning of the year	**7**	**2,430,551**	**3,929,635**
Cash and cash equivalents at the end of the year	**7**	**2,781,993**	**2,430,551**

Pages 26 to 107 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 2022	**111,500**	**5,648**	**156,745**	**273,893**	**6,066**	**279,959**
Transfer to legal reserve	0	3,088	-3,088	**0**	0	**0**
Paid in share capital	30,000	0	0	**30,000**	0	**30,000**
Dividends paid	0	0	-3,900	**-3,900**	-2,100	**-6,000**
Share options	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	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**
Balance as at 1 Jan 2023	**141,500**	**8,736**	**231,805**	**382,041**	**6,181**	**388,222**
Transfer to legal reserve	0	3,933	-3,933	**0**	0	**0**
Dividends paid	0	0	-2,275	**-2,275**	-1,225	**-3,500**
Share options	0	0	3,944	**3,944**	0	**3,944**
Profit for the year	0	0	140,133	**140,133**	1,230	**141,363**
Total comprehensive income	0	0	140,133	**140,133**	1,230	**141,363**
Balance as at 31 Dec 2023	**141,500**	**12,669**	**369,674**	**523,843**	**6,186**	**530,029**

Additional information on equity is provided in Note 17.

Material accounting policy information

Material 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 2023 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 2023 and ended at 31 December 2023. The financial figures have been presented in thousands of euros (EUR) unless otherwise indicated.

Summary of new reporting requirements

A number of new standards, interpretations and amendments are effective for annual periods beginning on or after 1 January 2023 but did not have a material impact on the Group's financial statements.

New currently effective requirements

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 did not have a material impact on the Group's financial statements

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 amendments did not have a material impact on the Group's financial statements.

New requirements not yet effective

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.

Amendments to IAS 7 Statement of Cash Flows and IFRS 7 Financial Instruments: Disclosures (effective for annual periods beginning on or after 1 January 2024)

These amendments require the disclosures of the entity's supplier finance arrangements that would enable the users of financial statements to assess the effects of those arrangements on the entity's liabilities and cash flows and on the entity's exposure to liquidity risk.

2. Consolidation

The consolidated financial statements for 2023 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 25) 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. Functional and presentation currency

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

4. 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 but excludes mandatory cash balances with central banks, which represent non-interest-bearing mandatory reserve deposits which are not available to finance LHV's day to day operations.

5. Financial assets

5.1 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.

5.2 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.

5.3 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 cash and cash equivalents, 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.

5.4 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.

5.5 Derivatives

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

5.6 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.

5.7 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.

5.8 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 2023	31 Dec 2022
Financial assets	Amortised cost	Cash and cash equivalents, due from central banks and investment companies		2,837,892	2,479,240
		Loans and advances to customers	Loans to legal entities	2,191,738	1,667,234
			Loans to individuals	1,356,775	1,009,926
		Debt securities		321,888	364,230
		Receivables from customers		17,833	9,253
		Other financial assets		100	124
	Fair value through profit or loss	Shares and fund units		369	367
		Listed bonds		6,275	0
		Derivatives		301	40
Financial liabilities	Amortised cost	Amounts owed to central banks (TLTRO)		0	147,841
		Deposits from customers		5,534,720	4,956,931
		Loans received and debt securities in issue		486,568	384,149
		Accounts payable and other liabilities		78,561	54,838
		Subordinated debt		114,054	114,056
	Fair value through profit or loss	Derivatives		1,843	3,850

6. Impairment of financial assets

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.

The detailed description of credit risk measurement, definition of default, ECL modelling and incorporation of forward-looking information into credit risk measurement are described in subsection ‘2. Credit risk’ under the ‘Risk management’ section.

7. Property, plant and equipment

Property, plant and equipment (PPE) are non-current assets used in the Group’s operating activities that have a useful life of over one year. PPE 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.

PPE 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.

8. 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.

9. 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.

10. 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.

11. 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. 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.

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

12. 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.

13. Contingent liabilities

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).

14. 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.

15. Taxation and deferred income tax

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 22). 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.

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 2023 for AS LHV Pank (hereinafter the Bank or LHV Pank, the branch in UK was closed in 2023) 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 Pärnu. 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 2023, the Group employed 827 people, including 41 non-active employees (31 Dec 2022: 765 people, 45 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 23 February 2024. The consolidated annual report will be presented for approval to the sole shareholder AS LHV Group. Rain Lõhmus, who owns 21.5% of the voting rights and Andres Viisemann, who owns 11.2% 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 accounting 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 Group has offset the following assets and liabilities.

Offset assets and liabilities

EUR thousand

As at 31 Dec 2023	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	301	0	301	0	0	0
Liabilities						
Derivatives	1,843	0	1,843	0	0	0
As at 31 Dec 2022						
Assets						
Derivatives	40	0	40	0	0	0
Liabilities						
Derivatives	3,850	0	3,850	0	0	0

NOTE 4 Net interest income

Interest income

EUR thousand	Note	2023	2022
Interest income using effective interest calculation			
Corporate loans		138,673	78,909
incl. loans to related parties	20	163	78
incl. stage 3 interest*		309	63
Hire purchase		3,453	3,338
Consumer loans		12,126	9,607
Leveraged loans and lending of securities		1,383	1,629
Credit card loans		1,027	836
From balances with credit institutions and investment companies		4,397	3,664
Mortgage loans		62,885	28,144
incl. loans to related parties	20	94	42
Private loans		3,735	2,450
incl. loans to related parties	20	49	7
From balances with central bank		56,664	8,594
Other loans		2,003	8,821
Subtotal		**286,346**	**145,992**
Other similar interest income			
Leasing		11,362	6,407
incl. leases to related parties	20	41	11
From debt securities		7,799	-231
incl. debt securities at amortised cost		6,802	0
incl. debt securities at fair value through profit or loss	8	997	-231
Subtotal		**19,161**	**6,176**
Total		**305,507**	**152,168**
Interest expense			
Deposits from customers and loans received		-67,098	-5,696
From balances with central bank		0	-7,661
Other interest		-698	0
Subordinated debt	16, 20	-9,240	-9,322
Total		**-77,036**	**-22,679**
Net interest income		**228,471**	**129,489**

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

	2023	2022
Estonia	233,482	140,141
United Kingdom	3,165	0
Total	**236,647**	**140,141**

*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

Net fee and commission income

EUR thousand	Note	2023	2022
Security brokerage and commission fees		4,400	4,329
Asset management and related fees		6,696	5,807
Currency exchange fees		5,868	8,462
Fees from cards and settlements		23,286	27,498
Other fee and commission income		7,667	6,793
Total	23	**47,917**	**52,889**
Fee and commission expense			
Security brokerage and commission fees paid		-2,502	-2,386
Expenses related to cards		-7,397	-6,312
Expenses related to card payments		-8,600	-7,344
Fees related to consumer loans and hire-purchase paid		-741	-830
Other fee expense		-1,460	-3,609
Total	23	**-20,700**	**-20,481**
Net fee and commission income	23	**27,217**	**32,408**

Fee and commission income by customer location:	2023	2022
Estonia	39,912	45,537
United Kingdom	8,005	7,352
Total	**47,917**	**52,889**

NOTE 6 Operating expenses

EUR thousand	2023	2022
Wages, salaries and bonuses	34,045	27,654
Social security and other taxes*	10,246	8,475
Total staff costs	**44,291**	**36,129**
IT expenses	6,458	4,943
Information services and banking services	1,418	1,297
Marketing expenses	2,823	2,583
Office expenses	1,534	1,358
Transportation and communication costs	509	492
Training and travelling expenses of employees	1,047	1,073
Other outsourced services	7,302	5,343
Other administrative expenses	11,556	6,964
Depreciation and amortisation	7,170	3,091
Rental payments	186	293
Other operating expenses	941	979
Total other operating expenses	**40,944**	**28,416**
Total operating expenses	**85,235**	**64,545**

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

The average number of employees working for the Group in 2023 was 784 (2022: 710).

NOTE 7 Cash and cash equivalents, due from central banks and investment companies

EUR thousand	31 Dec 2023	31 Dec 2022
Demand and term deposits with maturity of less than 3 months*	48,140	88,276
Reserve requirement at central banks	55,899	48,689
Demand deposit from central banks*	2,733,853	2,342,275
Total	**2,837,892**	**2,479,240**

*cash and cash equivalents in the statement of cash flows

Mandatory banking reserve as at 31 Dec 2023 was 1% (2022: 1%) of all financial resources collected (deposits from customers). 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 2023	31 Dec 2022
Shares and fund units	369	367
Debt securities	6,275	0
Foreign exchange forwards	301	40
Total financial assets	**6,945**	**407**
Interest rate swaps and foreign exchange forwards	1,843	3,850
Total financial liabilities	**1,843**	**3,850**

Financial assets at fair value through profit or loss 01 Jan 2022	**127,720**
Net changes of investment securities at fair value through profit or loss	334,516
Negative interest income (Note 4)	-231
Revaluation	2,429
Reclassification	-464,027
Financial assets at fair value through profit or loss 31 Dec 2022	**407**
Net changes of investment securities at fair value through profit or loss	5,804
Interest income (Note 4)	997
Revaluation	-263
Financial assets at fair value through profit or loss 31 Dec 2023	**6,945**

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**
Interest income	6,802
Net change in investment securities measured at amortised cost	-49,155
Impairment	11
Financial assets at amortised cost as at 31 Dec 2023	**321,888**

NOTE 9 Loans and advances to customers

EUR thousand	31 Dec 2023	31 Dec 2022
Loans to legal entities	**2,215,222**	**1,959,052**
incl. corporate loans	1,865,776	1,725,720
incl. leasing	136,723	121,015
incl. overdraft	123,953	36,686
incl. trade finance	30,484	36,255
incl. leveraged loans	3,968	3,679
incl. credit cards and hire-purchase	942	747
incl. apartment association loans	23,418	18,273
incl. factoring	29,958	16,677
Loans to individuals	**1,363,347**	**1,248,514**
incl. hire-purchase	13,820	15,824
incl. mortgage loans	1,162,113	1,049,386
incl. consumer loans	83,681	77,119
incl. private loans	48,512	52,801
incl. leasing	31,076	31,678
incl. leveraged loans	6,012	6,857
incl. credit card loans	10,855	8,933
incl. overdraft	17	25
incl. study loan	4,721	2,559
incl. real estate leasing	2,540	3,332
Total	**3,578,569**	**3,207,566**
incl. related parties (Note 20)	8,565	7,570
Allowance for credit loss	-30,056	-20,577
Total	**3,548,513**	**3,186,989**

In 2023, the average effective interest rate of new consumer loans issued to individuals was 14.67% (2022: 16.05%). The average effective interest rate for hire-purchase was around 21.44% (2022: 24.8%), credit cards 17.54% (2022: 17.85%) and leasing 6.42% (2022: 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	-15,435	-14,931	8,967	-21,399
Consumer Financing	-2,107	-3,232	1,029	-4,310
Investment Financing	-13	-5	7	-11
Leasing	-2,008	-759	660	-2,107
Private Lending	-1,014	-1,688	473	-2,229
Total 2023	**-20,577**	**-20,615**	**11,136**	**-30,056**
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**

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 2023	31 Dec 2022
Asset management fees from customers	671	607
Other fees for providing services to customers	17,153	8,612
Payments in transit	9	34
Total	**17,833**	**9,253**

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 2023	31 Dec 2022
Financial assets		
Guarantee deposits of Baltic stock exchanges	0	24
Guarantee deposits of VISA and MasterCard	100	100
Subtotal	**100**	**124**
Non-financial assets		
Prepayments to Financial Supervision Authority	0	1,020
Other prepayments*	2,795	1,846
Subtotal	**2,795**	**2,866**
Total	**2,895**	**2,990**

* 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. The deposits of VISA are held to guarantee credit card transactions and should therefore be considered non-current assets. In 2022 also guarantee deposits on the Baltic stock exchanges were held to guarantee securities trading activity on the stock exchanges of Tallinn, Riga and Vilnius.

NOTE 12 Property, plant and equipment, and intangible assets

EUR thousand	PPE	Right-of-use assets	Total tangible assets	Intangible assets	Total
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**
Changes in 2021:					
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**
Purchase of non-current assets	2,543	7,908	10,451	2,043	12,494
Write-off of non-current assets	-89	0	-89	-736	-825
Proceeds from disposal of PPE (at carrying amount)	-487	0	-487	0	-487
Depreciation/amortisation charge	-1,197	-3,995	-5,192	-1,978	-7,170
Balance as at 31 Dec 2023					
Cost	15,734	14,477	30,211	8,813	39,024
Accumulated depreciation and amortisation	-6,928	-7,551	-14,479	-5,867	-20,346
Carrying amount 31 Dec 2023	**8,806**	**6,926**	**15,732**	**2,946**	**18,678**

PPE include computer technology and office equipment, furniture, capitalised costs of office renovation. Intangible assets include licenses, client contracts and development costs. In 2023 and 2022, there was no indication of impairment of PPE and intangible assets.

NOTE 13 Deposits from customers and loans received

31 Dec 2023

EUR thousand	Individuals	Financial entities	Non-financial entities	Public sector	Total
Demand deposits	745,277	1,129,382	1,745,664	74,571	3,694,894
Term deposits	920,080	98,730	753,648	43,265	1,815,723
Accrued interest liability	13,047	1,419	9,063	574	24,103
Total	**1,678,404**	**1,229,531**	**2,508,375**	**118,410**	**5,534,720**
incl. related parties (Note 20)	3,748	0	43,704	0	47,452

31 Dec 2022

EUR thousand					
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 2023		31 Dec 2022	
EUR thousand	Loan principal	Accrued interest	Loan principal	Accrued interest
Debt securities in issue	233,907	2,943	133,771	953
Covered bonds	249,577	141	249,284	141
Total	**483,484**	**3,084**	**383,055**	**1,094**

	31 Dec 2023		31 Dec 2022	
EUR thousand	Loan principal	Accrued interest	Loan principal	Accrued interest
Received loan from central banks (TLTRO)	0	0	150,000	-2,159
Total	**0**	**0**	**150,000**	**-2,159**

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 2023**	**31 Dec 2022**
Financial liabilities		
Trade payables	1,879	991
Other short-term financial liabilities	18,226	9,653
Lease liabilities	8,057	1,842
Payments in transit	48,632	40,101
Provision of loan commitments and financial quarantees	1,152	1,023
Prepayments received for financial guarantees	615	1,228
Subtotal	**78,561**	**54,838**
Non-financial liabilities		
Prepaid expenses	751	736
Prepayments received for performance guarantees	1,750	1,058
Tax liabilities	2,917	2,417
Payables to employees	3,451	2,852
Subtotal	**8,869**	**7,063**
Total	**87,430**	**61,901**

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 376 thousand (2022: 1,032 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 right-of-use assets in the statement of financial position as at 31 Dec 2023 is EUR 6,926 thousand (31 Dec 2022: 3,013 thousand) and the liability is EUR 8,057 thousand (31 Dec 2022: 1,842 thousand). The right-of-use assets balance is disclosed in the Note 12. The lease liability is disclosed in the Note 14. Interest expense on lease liabilities in 2023 was EUR 275 thousand (2022: 89 thousand) and the depreciation of the right of use assets was EUR 3,995 thousand (2022: 1,075 thousand) (Note 12). The repayments of principal of lease liabilities in 2023 were EUR 1,694 thousand (2022: 1,423 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%.

In 2023, no subordinated bonds were issued or redeemed.

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 01 Jan 2022	**88,500**
Subordinated bonds issued	30,000
Subordinated bonds redeemed	-5,000
Subordinated debt as at 31 Dec 2022	**113,500**
Subordinated debt as at 31 Dec 2023	**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 2022	**489**
Interest calculated for 2022 (Note 4)	9,322
Paid out during 2022	-9,255
Accrued interest on subordinated debt as at 31 Dec 2022	**556**
Interest calculated for 2023 (Note 4)	9,240
Paid out during 2023	-9,242
Accrued interest on subordinated debt as at 31 Dec 2023	**554**

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 21.5% of the voting rights and Andres Viisemann who owns 11.2% of the voting rights in AS LHV Group have significant influence over the company (31 December 2022: 21.8% and 11.3%, 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 2022: 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 through a cash contribution by the sole shareholder AS LHV Group. The Group's share capital increased to EUR 141.5 million by the year-end 2022. There were no changes in share capital in 2023.

As at 31 Dec 2023, the adjusted unconsolidated retained earnings of the Bank amounted to EUR 369,674 thousand (31 December 2022: EUR 231,805 thousand). Thus, as at 31 December 2023 it is possible to pay out dividends in amount EUR 295,941 thousand (2022: EUR 185,653 thousand) and the related income tax charge would be EUR 73,733 thousand (2022: EUR 46,152 thousand). If the dividends were to be paid, the Group's capital adequacy would remain compliant.

Transactions with share capital	**31 Dec 2023**	**31 Dec 2022**
Share capital	141,500	141,500
Number of shares	141,500,000	141,500,000
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 underlying assets of the share options issued are the shares of 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 2022 and in 2023.

In 2023, 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 140 employees of the group in the total amount of EUR 4,426 thousand.

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.

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

Share options issued in 2020 were exercised in 2023, when shares with nominal value of EUR 0.1 could 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 0.1 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 0.1 can be acquired for EUR 2.182 per share.

Share options issued in 2023 can be exercised between the period of 01.04.2026-30.04.2026 and shares with nominal value of EUR 0.1 can be acquired for EUR 1.7 per share.

Legal reserve in equity is composed of:

EUR thousand	
Legal reserve as at 1 Jan 2022	**5,648**
Transferred from 2021 net profit	3,088
Legal reserve as at 31 Dec 2022	**8,736**
Transferred from 2022 net profit	3,933
Legal reserve as at 31 Dec 2023	**12,669**

NOTE 18 Assets under custody

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

EUR thousand	31 Dec 2023	31 Dec 2022
Cash balance of customers	13,780	13,609
Securities of customers	3,490,269	3,194,837
incl. parent company (Note 20)	151,129	149,279
incl. shareholders of the parent company and related entities (Note 20)	562,486	483,452
Total	**3,504,049**	**3,208,446**

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 agreements	Performance guarantees	Financial guarantees	Letters of credit	Unused loan commitments	Total
Liability in contractual amount 31 Dec 2023	56,217	55,061	3,732	495,653	610,663
Liability in contractual amount 31 Dec 2022	30,174	52,577	6,605	601,093	690,449

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 2022-2023. The Group's management estimates that in 2024 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 2023	31 Dec 2022
Construction	39,418	19,123
Water and utilities	5,316	4,180
Manufacturing	4,008	3,021
Administrative activities	639	715
Professional, scientific and technical activities	550	553
Other areas at activities	6,286	2,582
Total	**56,217**	**30,174**

Breakdown by internal ratings

EUR thousand		
5 low credit risk	4,960	1,361
6 low credit risk	4,375	1,973
7 medium credit risk	5,948	6,161
8 medium credit risk	16,440	5,574
9 heightened credit risk	19,252	9,852
10 high credit risk	6	151
11 high credit risk	0	730
12 non-satisfactory rating	322	1,616
13 insolvent	1,568	0
Non-rated	3,346	2,756
Total	**56,217**	**30,174**

Performance guarantees are over-collateralised as at each reporting date. Therefore, the Group has not borne any losses from performance guarantee contracts neither in 2023 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	2023	2022
Interest income	4	**1,338**	**178**
incl. management		62	42
Interest expenses	4	**18,013**	**9,270**
incl. management		27	5
incl. parent company		17,904	9,234
incl. shareholders, their related entities and close relatives that have significant influence		82	31
Fee and commission income	5	**82**	**88**
incl. management		9	5
incl. shareholders, their related entities and close relatives that have significant influence		73	83

Balances	Note	31 Dec 2023	31 Dec 2022
Loans and receivables	9	**28,579**	**7,570**
incl. management		2,104	3,928
incl. shareholders, their related entities and close relatives that have significant influence		26,475	3,642
Deposits	13	**47,452**	**64,178**
incl. management		1,519	765
incl. parent company		25,946	29,684
incl. shareholders, their related entities and close relatives that have significant influence		19,987	33,729

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 2023 the interest rate on demand deposits and term deposits corresponds to the terms applicable to customers. As at 31 Dec 2022 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 2023, salaries and other compensations paid to the management of LHV totalled EUR 1,363 thousand (2022: EUR 1,368 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 2023, the remuneration for December and accrued holiday pay in the amount of EUR 83 thousand (as at 31 Dec 2022: EUR 85 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 2023 and 31 Dec 2022 (pension liabilities, termination benefits, etc.). In 2023 and 2022, 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 2023 and 31 Dec 2022, 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 2023	31 Dec 2022
Loans and advances to customers and other current assets	93,408	91,591
Non-current assets	141	120
Current liabilities	1,491	2,297
Non-current liabilities	73,712	70,495
Total net assets	**18,346**	**18,919**

Summarised statement of profit or loss and other comprehensive income

EUR thousand	31 Dec 2023	31 Dec 2022
Total net interest and fee income	10,085	10,439
Profit before income tax	3,425	7,288
Income tax expense	-569	-1,107
Net profit	**2,856**	**6,181**
Total comprehensive income	2,856	6,181
Profit and other comprehensive income allocated to non-controlling interests	1,230	2,217

Summarised statement of cash flows

EUR thousand	31 Dec 2023	31 Dec 2022
Cash generated from operations	6,626	-12,284
Interest paid	-5,383	-2,407
Income tax paid	-569	-1,107
Net cash generated from/used in operating activities	674	-15,798
Net cash generated from/used in investing activities	-86	-134
Net cash generated from/used in financing activities	-588	15,932
Net increase/decrease in cash and cash equivalents	**0**	**0**
Cash and cash equivalents at beginning of year	0	0
Cash and cash equivalents at end of year	0	0

NOTE 22 Income tax expense

The Bank is calculating 14% advance income tax. Advance corporate income tax for the year 2023 was EUR 22,195 thousand (2022: EUR 12,305 thousand).

EUR thousand	2023	2022
Advance corporate income tax	22,195	12,305
Corporate income tax	-88	955
Total income tax expense	**22,107**	**13,260**

The Group has cumulatively paid advance corporate income tax in the amount of EUR 39,006 thousand in total by the end of the reporting period (2022: 17,471 thousand) This has been recorded as an expense in the income statement in the respective periods.

NOTE 23 Operating segments

The Group divides its business activities by 4 main business segments: retail banking, corporate banking, hire purchase and consumer finance, and financial intermediates. An operating segment is a part of the Group for which separate financial data is available and which is subject to regular monitoring of operating results by the Group's chief decision maker.

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 in LHV Pank. Although the activities of the UK branch of LHV Pank were transferred to LHV Bank in the middle of the year, LHV Pank continues servicing financial intermediaries in euro payments and safeguarding services.

Other activities include treasury activities through providing internal bank function to segments and activities related to other LHV Group companies. Assets and liabilities are disclosed in a way how it is reported to the Management Board of LHV Pank, 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 2023

EUR thousand	Retail banking	Corporate banking	Hire-purchase and consumer finance	Financial intermediaries	Other activities	Total
Interest income	85,829	132,615	15,580	-22,996	94,478	305,507
Interest expense	40,786	-55,310	-6,215	28,929	-85,226	-77,036
Net interest income	**126,615**	**77,305**	**9,365**	**5,933**	**9,252**	**228,471**
Fee and commission income	34,318	6,499	951	5,816	332	47,917
Fee and commission expense	-16,849	-3,378	-740	387	-119	-20,700
Net fee and commission income	**17,469**	**3,122**	**211**	**6,203**	**213**	**27,217**
Net gains from financial assets	**14**	**-1**	**0**	**-3**	**2,643**	**2,652**
Net other income	**19**	**1,513**	**2**	**0**	**202**	**1,737**
Net income	**144,117**	**81,940**	**9,578**	**12,132**	**12,310**	**260,077**
Administrative and other operating expenses, staff costs	-43,728	-20,521	-3,767	-13,553	-3,667	-85,235
Operating profit	**100,389**	**61,419**	**5,811**	**-1,421**	**8,643**	**174,842**
Impairment losses on loans and advances	-812	-6,187	-3,746	0	-627	-11,372
Income tax	-10,176	-7,323	-689	-1,890	-2,029	-22,107
Net profit for the reporting period	**89,401**	**47,909**	**1,376**	**-3,311**	**5,988**	**141,363**
Total assets as at 31 Dec 2023	**2,742,899**	**3,726,731**	**93,549**	**0**	**191,465**	**6,754,644**
Total liabilities as at 31 Dec 2023	**4,180,348**	**885,028**	**75,203**	**1,114,526**	**-30,490**	**6,224,615**

31 Dec 2022

EUR thousand	Retail banking	Corporate banking	Hire-purchase and consumer finance	Financial intermediaries	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**

NOTE 24 Discontinued operations

On 22 August the business of the UK branch was transferred to LHV Bank. This involved moving the servicing of pound sterling payments for UK business clients from existing branch to LHV Bank. Branch was officially closed by the year end. LHV Bank paid for the net assets EUR 3,195 thousand and additionally EUR 1,986 thousand as a transfer value of the business which is recorded as net gain from financial assets measured at fair value.

The financial statements of the branch are presented below:

Statement of profit or loss and other comprehensive income

EUR thousand	1 Jan - 22 Aug 2023	2022
Interest income	3,769	3,016
Interest expense	-401	-16
Net interest income	**3,368**	**3,000**
Fee and commission income	1,910	1,583
Fee and commission expense	-14	-29
Net fee and commission income	**1,896**	**1,554**
Net loss from financial assets measured at fair value	0	3
Foreign exchange gains	242	-2,126
Net gain/loss from financial assets	**242**	**-2,123**
Net income	**5,506**	**2,431**
Staff costs	-613	-1,479
Administrative and other operating expenses	-433	-1,992
Profit before income tax	**4,460**	**-1,040**
Income tax expense	34	0
Net profit for the reporting period	**4,494**	**-1,040**

Statement of financial position

EUR thousand	22 Aug 2023	31 Dec 2022
Assets		
Cash and cash equivalents	6,724	4,181
Due from central bank	210,869	186,221
Receivables from customers	554	336
Total assets	**218,147**	**190,738**
Liabilities		
Deposits from customers	155,236	119,423
Loans received and debt securities in issue	59,671	63,079
Accounts payable and other liabilities	45	9,535
Total liabilities	**214,952**	**192,037**
Equity		
Retained earnings	3,195	-1,299
Total equity	**3,195**	**-1,299**
Total liabilities and equity	**218,147**	**190,738**

Statement of cash flows

EUR thousand	1 Jan - 22 Aug 2023	2022
Cash flows from operating activities		
Interest received	3,769	3,016
Interest paid	-411	-16
Fees and commissions received	1,910	1,583
Fees and commissions paid	-14	-29
Other income received	0	3
Staff costs paid	-613	-1,479
Administrative and other operating expenses paid	-433	-1,992
Income tax paid		
Cash flows from operating activities before change in operating assets and liabilities	**4,208**	**1,086**
Net increase/decrease in operating assets:		
Other assets	-218	-312
Net increase/decrease in operating liabilities:		
Demand deposits of customers	35,823	-9,368
Net loans received (including loan repayments)	-3,408	-73,032
Other liabilities	-9,456	6,413
Net cash from/used in operating activities	**26,949**	**-75,213**
Effect of exchange rate changes on cash and cash equivalents	**242**	**-2,126**
Net increase/decrease in cash and cash equivalents	**27,191**	**-77,339**
Cash and cash equivalents at the beginning of the financial year	**190,402**	**267,741**
Cash and cash equivalents at the end of the period	**217,593**	**190,402**

NOTE 25 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	2023	2022
Interest income	295,617	141,744
Interest expense	-77,036	-22,679
Net interest income	**218,581**	**119,065**
Fee and commission income	46,981	52,044
Fee and commission expense	-19,959	-19,651
Net fee and commission income	**27,022**	**32,393**
Net gains from financial assets measured at fair value	3,383	2,071
Foreign exchange gain	1,544	1,407
Net gains from financial assets	**4,927**	**3,478**
Other income	2,581	2,456
Administrative and other operating expenses	-83,165	-64,561
Operating profit	**169,946**	**92,831**
Impairment losses on loans and advances and liquidity portfolio	-7,626	-2,086
Profit before income tax	**162,320**	**90,745**
Income tax expense	-22,195	-12,305
Net profit for the year	**140,125**	**78,440**
Total comprehensive income for the year	**140,125**	**78,440**

Statement of financial position of the parent

EUR thousand	Note	31 Dec 2023	31 Dec 2022
Assets			
Cash and cash equivalents		35,631	84,885
Due from central bank		2,789,752	2,390,964
Due from investment companies		12,509	3,391
Financial assets at fair value through profit or loss		6,945	407
Financial assets measured at amortised cost		321,888	364,230
Loans and advances to customers		3,528,839	3,166,562
Receivables from customers and other financial assets		17,809	14,028
Other assets		2,946	2,842
Subsidiaries	21	325	325
Property, plant and equipment		8,806	7,947
Right-of-use assets		6,926	3,013
Intangible assets		2,805	2,761
Total assets		**6,735,181**	**6,041,355**
Liabilities			
Amounts owed to central banks (TLTRO)		0	147,841
Deposits from customers		5,534,720	4,956,931
Loans received		486,568	384,149
Financial liabilities at fair value through profit or loss		1,843	3,850
Accounts payable and other liabilities		77,556	62,026
Lease liability		8,057	1,842
Subordinated debt		114,054	114,056
Total liabilities		**6,222,798**	**5,670,695**
Equity			
Share capital	17	141,500	141,500
Legal reserve capital		12,669	8,736
Retained earnings		358,214	220,424
Total equity		**512,383**	**370,660**
Total liabilities and equity		**6,735,181**	**6,041,355**

Statement of cash flows of the parent

EUR thousand	Note	2023	2022
Cash flows from operating activities			
Interest received		287,849	138,723
Interest paid		-51,642	-20,659
Fees and commissions received		46,981	52,044
Fees and commissions paid		-19,959	-19,651
Other income received		2,581	2,456
Staff costs paid		-38,779	-31,629
Administrative and other operating expenses paid		-39,032	-24,474
Income tax paid		-21,534	-10,532
Cash flows from operating activities before change in operating assets and liabilities		**166,465**	**86,278**
Net increase/(decrease) in operating assets:			
Net acquisition/disposal of trading portfolio		-264	-35
Loans and advances to customers		-366,040	-516,919
Mandatory reserve at central bank		-7,211	8,609
Security deposits		24	2,112
Other assets		-4	-421
Net increase/(decrease) in operating liabilities:			
Demand deposits of customers		-1,004,362	-989,318
Term deposits of customers		1,558,745	97,695
Net loans received (including loan repayments)		-47,412	-49,535
Subordinated loans received (senior bonds)		0	65,000
Subordinated loans repaid (senior bonds)		0	-31,000
Financial liabilities at fair value through profit or loss		-2,007	3,693
Other liabilities		28,404	11,997
Net cash from/ (used in) operating activities		**326,338**	**-1,311,844**
Cash flows from investing activities			
Purchase of PPE and intangible assets		-12,408	-7,414
Proceeds from disposal of PPE		486	0
Net changes of investment securities at fair value through profit or loss		37,175	-234,810
Net cash from/ (used in) investing activities		**25,253**	**-242,224**
Cash flows from financing activities			
Paid in share capital	17	0	30,000
Proceeds from subordinated debt	16	0	30,000
Subordinated debt redeemed	16	0	-5,000
Dividends paid		-2,275	-3,900
Dividends received		2,275	3,900
Repayment of principal of lease liabilities	15	-1,693	-1,423
Net cash from financing activities		**-1,693**	**53,577**
Effect of exchange rate changes on cash and cash equivalents		**1,544**	**1,407**
Net increase/ (decrease in cash and cash equivalents		**351,442**	**-1,499,084**
Cash and cash equivalents at the beginning of the financial year		**2,430,551**	**3,929,635**
Cash and cash equivalents at the end of the financial year		**2,781,993**	**2,430,551**

Statement of changes in shareholders' equity

EUR thousand	Share capital	Legal reserve capital	Retained earnings	Total
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	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**
Balance as at 1 Jan 2023	**141,500**	**8,736**	**220,424**	**370,660**
Transferred into legal reserve	0	3,933	-3,933	**0**
Dividends paid	0	0	-2,275	**-2,275**
Share options	0	0	3,873	**3,873**
Net profit for the year	0	0	140,125	**140,125**
Total comprehensive income	0	0	140,125	**140,125**
Balance as at 31 Dec 2023	**141,500**	**12,669**	**358,214**	**512,383**
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	11,785	**11,785**
Adjusted unconsolidated equity as at 31 Dec 2023	**141,500**	**12,669**	**369,674**	**523,843**

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

Signatures of the Management Board to the 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 2023. The consolidated financial statements present a true and fair view of LHV Pank's consolidated financial position, the consolidated results of operations and its consolidated cash flows.

23 February 2024

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 LHV Pank's annual report 2023 to maintain the structural logic of the report and to refer the reader to the location of the independent auditor's report. Due to the final generation of the machine-readable reporting files before the signing of the independent auditor's report, and the logic of submitting digital signatures in chronological order, the independent auditor's report is available in the DigiDoc container named 'AS LHV Pank consolidated and audited annual report 2023.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 2023.asice' in the same DigiDoc container as the independent auditor's report and contains the report in the ESEF format '529900GJOSVHI055QR67-2023-12-31-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 2023 as follows:

- transfer EUR 1,481 thousand to legal reserve capital
- pay dividends EUR 76,300 thousand
- transfer the profit for reporting period attributable to shareholders of the parent in the amount of EUR 62,352 thousand to retained earnings.

Allocation of income according to EMTAK

EMTAK	Activity	2023	2022
66121	Security and commodity contracts brokerage	11,096	10,136
64191	Credit institutions (banks) (granting loans)	330,966	188,514
64911	Finance lease	11,362	6,407
	Total income	**353,424**	**205,057**

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 subsidiary ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2023, the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising material 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 2023, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by 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.

Impairment of loans and advances to customers	
Refer to Risk Management section, Material accounting policy information, 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 2023, loans and advances to customers amounted to EUR 3 579 million and related impairment loss allowance amounted to EUR 30.1 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.	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

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, that also requires significant accounting estimates.	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 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 and key forecasts of macroeconomic information. 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 comprises the information included in the 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 by 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 scepticism 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 529900GJOSVHI055QR67-2023-12-31-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 digitised 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 apply the provisions of the International Standard on Quality Control (Estonia) 1 and accordingly maintain a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

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 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 (Revised) 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 2023;

– 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 Pank identified as 529900GJOSVHI055QR67-2023-12-31-EN.zip for the year ended 31 December 2023 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 30 March 2022 to audit the consolidated financial statements of AS LHV Pank for the year ended 31 December 2023. Our total uninterrupted period of engagement is four years, covering the periods ending 31 December 2020, 31 December 2021, 31 December 2022 ,31 December 2023.

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, 23 February 2024

/digitally signed/

Eero Kaup

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