AS LHV Pank
Consolidated Annual Report 2020

(Translation of the Estonian original)

Consolidated Annual Report 01.01.2020 – 31.12.2020

Legal name	**AS LHV Pank**
Commercial Registry no.	**10539549**
Legal address	**Tartu mnt 2, 10145 Tallinn**
Phone	**(372) 6800400**
Fax	**(372) 6800410**
E-mail	**lhv@lhv.ee**
Main activities	**Banking**
	Security brokerage
	Financial advisory
	Finance lease and other lending
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
Auditor	
Auditors' legal name	**OÜ KPMG Baltics**
Auditors' Commercial Registry no.	**10096082**
Auditors' legal address	**Narva mnt. 5, 10117 Tallinn, Estonia**

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Management report

LHV's mission is to provide better access to financial services and capital. LHV's vision is helping people and businesses dare to think big and act big, set ambitious goals and invest in the future. LHV's values are: simple, supportive and effective.

LHV Pank ('the bank') 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. LHV's competitive edge is 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 setting affordable prices for our everyday banking services.

LHV Pank has a more than 10% market share in the Estonian daily banking, deposit and business loan segments and is currently the third-largest 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, which are innovative and the fastest in the market, we influence entrepreneurship and people's financial behaviour. The bank defines itself as a local bank offering the full range of services to customers that keep their funds at the bank and actively use the bank's services.

The bank has offices in Tallinn, Tartu and London. At the end of 2021, the bank will also open an office in Pärnu. The bank has around 500 employees and more than 250,000 customers. The bank's consolidated financial statements comprise the accounts of the bank and its 65% subsidiary AS LHV Finance ('LHV Finance'), which specialises in consumer finance (together referred to as 'the Group').

Business activities

The bank continued to grow rapidly in 2020. The number of customers increased by 50,000 to 258,000, i.e. by 28%. The outbreak of COVID-19 and the state of emergency declared by the government at the end of Q1 affected customer activity but only for a short term. By the end of Q2 customer activity had recovered and in annual terms both customer activity and business volumes hit new records. During the state of emergency, the majority of the bank's staff worked from home but offices providing customer service stayed open as usual. The bank's UK branch increased its number of customers to 130 financial intermediaries, who in turn have over 10 million end customers across the world.

Deposits from customers grew by 53% to EUR 4 141 million. Deposits from ordinary customers grew by 46% to EUR 2 871 million and deposits from financial intermediaries grew by 180% to EUR 1 054 million. The rise in deposits from financial intermediaries reflects the Q4 surge in the prices of virtual currencies and customers' increased interest in relevant investments. Deposits raised through deposit platforms decreased by 42% to EUR 216 million. In 2020, the bank did not actively raise funds through deposit platforms as related interest charges are higher and there was no real need for this.

The bank's loan portfolio grew by 31% to EUR 2,209 million during the year. Corporate loans grew by 40% to EUR 1 191 million and retail loans by 22% to EUR 1 017 million. The retail loan portfolio broke down as follows: home loans 68%, leases 13% and other loans 19%. At the beginning of October, LHV Pank and Danske Bank finalised a transaction by which LHV Pank acquired Danske Bank's Estonian corporate and public sector credit portfolio in the form of transfer of a business. The final value of the transaction was EUR 273 million. Taking into account the EUR 19 million write-down of the purchase price, the bank's loan portfolio grew by EUR 254 million. Altogether, 346 business customers, 252 apartment associations and 80 public sector customers transferred from Danske Bank to LHV Pank. 56% of the acquired portfolio was made up of loans to local governments. The additional profit generated by the portfolio since the acquisition amounts to around EUR 4 million per year.

The bank's net profit for the year grew by 57% to EUR 34.6 million. Income grew by 45%, compared with only 12% growth in expenses. Net interest income increased mainly through growth in corporate and home loans and earlier conversion of the impairment of loans in the Danske portfolio on the modification of agreements. The rise in net fee and commission income was largely driven by growth in investment services and services provided to financial intermediaries. Loan provisions increased by EUR 10.9 million over the year. Results for the year include advance income tax expense for 2021 of EUR 1.2 million payable on the expected future dividend, which has to be recognised in accordance with the amended accounting rules. The bank's performance indicators were solid: return on equity (on net profit attributable to shareholders) was 17.3%, the cost/income ratio was 41.0% and credit cost was 0.6%.

From April to the end of September, banks in Estonia applied a common policy on payment holidays. Customer requests for payment holidays surged in April, began to decrease in May and dropped to a minimum by the end of June. A major share of payment holidays expired in the second half of the year and by the year-end the total amount of loans on payment holiday had dropped to EUR 180 million. Although the credit ratings of some corporate clients directly affected by the crisis have been downgraded and we have had to recognise additional loss allowances, the quality of the bank's loan portfolio as a whole has remained high and the share of overdue loans is very small.

The bank's total assets grew by 64% to EUR 4,939 million in 2020. To invest its liquid assets more effectively, the bank participated in two bond issues by the government of Estonia, buying bonds for EUR 400 million in total. At the proposal of the Financial Supervision Authority, the European Central Bank granted the bank permission to issue covered bonds, enabling it to raise long-term funding, backed by mortgage loans, and thus reduce the cost of credit for customers. The bank's first issue of covered bonds in early June was a success: the bank issued five-year covered bonds for EUR 250 million. The annual yield of the bonds is 0.12%. The issue attracted 31 institutional investors from 13 countries across Europe. 41% of the order book was received from central banks and international institutions, 20% from institutional investors in Germany and 19% from institutional investors in the Nordic countries. The international rating agency Moody's assigned the covered bonds a (P)Aa1 rating. The issue helped diversify the bank's sources of funding, enabling the bank to raise future financing more flexibly and at a more favourable price. In September, the bank issued covered bonds for a further EUR 100 million and raised EUR 200 million under the third series of targeted longer-term refinancing operations (TLTRO III) of the European Central Bank.

In response to the COVID-19 pandemic, the Capital Requirements Regulation was revised. The changes included an increase in the capital discount for exposures to small and medium-sized enterprises (the SME supporting factor). This has reduced banks' risk-weighted assets for SMEs substantially. The aim of the instrument is to support lending to SMEs in the European Union. As SMEs account for over 90% of the bank's loan portfolio, this reduced the bank's risk-weighted assets by EUR 159.4 million and released capital of EUR 25.5 million last year.

At the end of 2020, Moody's Investors Service reconfirmed the previous credit rating assigned to the bank: investment-grade credit rating with a stable outlook. Moody's took into account the bank's strong capitalisation and profitability, which helps balance the bank's rapid growth.

In 2020, the auditor provided the bank with other assurance services which are required by the Credit Institutions Act and the Securities Markets Act.

Development activities

Numerous new products were introduced during the year. Since the beginning of the year, customers have been able to open children's bank accounts at the LHV internet bank. New payment solutions include Apple Pay, Google Pay, contactless payments with Fitbit and Garmin smartwatches, the Alexela credit card, a virtual ISIC for students and viewing the PIN of a bank card in the LHV mobile bank. Our new Proxy Payment service allows people to make payments, including interbank payments, simply based on the recipient's mobile phone number. For businesses, we introduced a new full-service payment collection solution, which allows merchants to offer their customers different payment options. Along with other banks, we raised the limit for contactless payments to EUR 50 and the limit for instant payments to EUR 100 000. In May, we reintroduced USD payments for customers who are Estonian residents.

At the beginning of the year, we launched real-time GBP payments for financial intermediaries. This provided us with a unique competitive edge: we could offer financial intermediaries an opportunity to use our application programming interface (API) LHV Connect to make real-time EUR and GBP payments 24/7. This is the first bank API to feature such an option. In addition, we launched the indirect membership of payment schemes. The service enables financial intermediaries to gain access to the payment system without having to build complex infrastructure. This unique service, which is based on LHV Connect, provides access to three payment systems: SEPA, SEPA Instant and Faster Payments.

From the beginning of 2020, users of our investment services are not charged service fees for trades in Baltic stocks. By abolishing the fees, we made investing accessible to everyone. The Mobile Bank app offers a convenient opportunity to open an account, sign an investment services agreement and start trading with Baltic stocks free of charge. Abolishment of the fees along with the volatility of stock markets boosted the volume of customers' securities transactions, which generated more fee income than expected. In addition, the bank lowered the fees for holding foreign securities and trading in foreign stocks from the beginning of 2021. In connection with the amendment of the

Funded Pensions Act, in January 2021 the bank launched a pension investment account and a related marketing campaign. We have become the market leader in investment services: customer assets managed by us extend to EUR 1.9 billion.

The range of financing products was extended to include loans for apartment associations. The bank also implemented remote identification at the notary's. As a result it is possible, for instance, to apply for a home loan, process the documents and finalise the transaction at the notary's remotely.

Organisation

The bank is divided into six functional areas, each with its own departments. Business areas include Retail Banking, Corporate Banking and Financial Intermediation, support areas include IT, Financial Management and Support Services, and Risk Management. Human Resource Management, Marketing and Communication, Compliance and Environmental, Social and Corporate Governance (ESG) are bank-wide activities. The bank's UK branch is part of the Financial Intermediation area.

Environmental, Social and Corporate Governance is a bank-wide area established in 2020. Another new structure is the Financial Intermediation Customer Acceptance Committee at the Management Board level, which is responsible for preventing the use of the bank for money laundering or terrorist financing or for facilitating such activities, and for applying the know-your-customer policy in the Financial Intermediation area.

In connection with the UK's exit from the EU, the bank filed an application for authorisation for its UK branch as a third-country branch with the UK's Financial Conduct Authority.

On 26 June 2020, the shareholders of LHV Finance passed a resolution to remove Rain Lõhmus as Member of the Supervisory Board as from 26 June 2020 and to appoint Madis Toomsalu as a new Member of the Supervisory Board.

On 30 November 2020, the bank's Supervisory Board passed a resolution to remove Erki Kilu as Chairman of the Management Board as from 20 January 2021 and to appoint Kadri Kiisel as the new Chairman of the Management Board. Erki Kilu was assigned to head LHV Group's new UK-based subsidiary with a view to obtaining authorisation for it to operate as a credit institution.

On 20 January 2021, the Supervisory Board of LHV Finance passed a resolution to remove Kadri Kiisel as Chairman of the Management Board as from 29 January 2021 and to appoint Mari-Liis Stalde as a new Member and Chairman of the Board. On the same day the shareholders passed a resolution to remove Erki Kilu as Chairman of the Supervisory Board as from 29 January 2021 and to appoint Kadri Kiisel as a new member of the Supervisory Board.

On 29 January 2021, the Supervisory Board passed a resolution to appoint Kadri Kiisel as the new Chairman of the Supervisory Board.

In 2020, the number of the bank's staff increased by 72 to 507, including inactive and part-time staff and the 21 employees of LHV Finance. The number of active staff converted to the full-time equivalent was 472.

The year brought several awards and accolades. Once again, LHV Pank was named the bank with the best customer service in Estonia in a survey conducted by the market research company Dive. The bank ranked third in the Most Attractive Employers survey conducted by the job portal CVKeskus.ee. The bank's staff satisfaction survey Q12 reflected a very high level of satisfaction. The Estonian Association for Environmental Management awarded the bank's Tallinn office in the City Plaza building the title of Best Green Office of the Year. Both Euromoney and The Banker magazine of The Financial Times named LHV Pank the best bank in Estonia, for the third and second year in a row, respectively.

LHV published a book that summarises its first 20 years of operation. The book is available in paper, e-book and audiobook formats.

ESG

In March, LHV Group officially joined the United Nations (UN) Principles for Responsible Banking and prepared an action plan for delivering on the promises made. Among other things, LHV plans to become climate neutral by 2022, to specify its lending and investment principles based on the targets set, and to encourage its customers and the Estonian financial sector to move towards greener options. Consistent with the UN Principles for Responsible Banking, LHV has four years to implement the activities.

The government of Estonia has decided to support the EU climate strategy and has made commitments that can be achieved only with the united effort of the whole society and all sectors. The financial sector plays a central role in the adjustment of the economy – through lending and investing banks can channel cash flows into sustainable activities that support transition to a climate-neutral economy.

The UN Principles for Responsible Banking provide a single framework for sustainable banking, developed through a partnership between banks worldwide and the UN Environment Programme Finance Initiative. The Principles for Responsible Banking set out the banking industry's role and responsibility in shaping a sustainable future, and in aligning the banking sector with the objectives of the UN Sustainable Development Goals and the Paris Climate Agreement. They also enable a bank to embed sustainability across all its business areas, and to identity where it has the potential to make the most impact in its contributions to sustainable development. They also position a bank to leverage new business opportunities with the emergence of a sustainable economy.

In 2020, the bank measured its carbon footprint and set the goal to reduce emissions and become climate neutral in 2022. The bank applied for the European Green Office Certificate, issued by the Estonian Association for Environmental Management, and for a BREEAM green label for its Tallinn office in the City Plaza building. The bank has evaluated the environmental impacts of its products and services, updated its credit policy and started to offer sustainable financial products, such as the green home loan, lease, hire purchase, investment loan and development loan.

The bank takes its social responsibility seriously. Where possible, the bank supports enterprises and initiatives that contribute to the development of the Estonian society. In sponsoring, the bank prefers long-term and substantive partnerships. The bank is ready to contribute to the pursuit of innovative ideas which improve life in Estonia. The bank's long-term partners include the Estonian Football Association, the Estonian Optimist Class Association, the Estonian Entrepreneur of the Year competition, Estonian Music Days and the Enn Soosaar Foundation.

Financial results

In 2020, the net profit of the Group increased by 57% compared to the previous year, amounting to EUR 34.6 million (2019: EUR 22.1 million). Net interest income increased by 44% and net fee and commission income increased by 44%. Financial income increased by 326% compared to the previous year.

The increase of the net interest income is attributable to the increase in of the lending and regular customer deposit volumes.

Among fee and commission income, the greatest contribution continues to come from security brokerage income. Income on cards and settlements are also showing a growth trend.

Operating expenses grew by 12% year-on-year, which was expected given the current phase of high growth and new business development.

Loan losses were 238% higher compared to the previous year.

The total volume of the Bank's loan portfolios at the end of December amounted to EUR 2 209 million (31.12.2019: EUR 1 687 million). The portfolio volume grew by 31% year-on-year. The majority of the loan portfolio consists of loans for companies, which grew by 42% year-on-year to EUR 1 353 million (31.12.2019: EUR 951 million). The portfolio of loans issued to private individuals increased by 16% to EUR 856 million (2019: EUR 737 million).

The volume of deposits of the Bank increased by 53% year-on-year and reached EUR 4 141 million by year-end (31.12.2019: EUR 2 713 million).

The proportion of demand deposits increased a bit, accounting for 88% of all deposits as at the end of December (31.12.2019: 81%).

Liquidity and capitalization

The liquidity coverage ratio (LCR) of the Bank, calculated according to the definitions of the Basel Committee, was 147% at the end of December (31.12.2019: 143%). The Bank includes cash and bond portfolios, accounting for 55% of the balance sheet total, among its liquidity buffer (31.12.2019: 43%). The Bank’s loan-to-deposit ratio at the end of 2020 was 48% (31.12.2019: 62%).

The debt security portfolio increased by 881% during 2020.

As a result of the issue of shares by the Bank's parent company, AS LHV Group, the Bank's share capital was increased by EUR 11 million.

The Bank's level of own funds as at 31.12.2020 was EUR 187.6 million (31.12.2019: EUR 158.5 million). The Bank is well capitalized as at the end of the reporting period with a capital adequacy level of 18.75% (31.12.2019: 17.61%).

AS LHV Pank and its subsidiary AS LHV Finance are included in the calculation of capital adequacy. 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.

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

Leverage ratio, calculated according to Basel Committee on Banking Supervision requirements, as at 31.12.2020 was 4.36% (31.12.2019: 5.70%). Leverage ratio is calculated as bank’s total Tier 1 own funds divided by its total risk exposure measure (including risk position on assets and off the balance sheet liabilities). As at the end of the reporting period, the leverage ratio is arithmetic mean of the monthly leverage ratios over the last quarter.

Statement of profit or loss,

(EUR million)	2020	2019	change
Net interest income	69.05	47.91	44%
Net fee and commission income	18.38	12.81	44%
Other financial income	0.88	0.21	319%
Total net operating revenues	88.31	60.93	45%
Other income	0.20	0.18	11%
Operating expenses	-36.26	-32.52	12%
Income tax expense	-6.76	-3.28	106%
Loan losses	-10.89	-3.22	238%

Key figures,

(EUR million)	2020	2019	change
Net profit	34.6	22.1	57%
Net profit attributable to owners of the parent	32.5	19.8	64%
Average equity	187.7	148.7	26%
Return on equity (ROE) %*	17.3	13.8	-3.5
Average assets	3 972	2 327	71%
Return on assets (ROA) %	0.9	0.9	0.0
Net interest income	69.0	47.9	44%
Average assets exposed to interest risk	3 964	2 320	71%
Net interest margin (NIM) %	1.9	2.1	-0.2
Spread %	1.84	2.02	-0.18
Cost / Income ratio %	41%	53%	-12

Volumes,

(EUR million)	31.12.2020	31.12.2019	change
Loan portfolio	2 208.8	1 687.0	31%
Bond portfolio	322.9	32.9	881%
Deposits	4 141.0	2 713.0	53%
Equity	214.7	171.7	25%
Number of customers holding assets in bank	258 962	202 186	28%

* Return on equity is calculated based on LHV Pank net profit and equity attributable to owners of the parent and does not include non-controlling interest

Explanations

Average equity (attributable to owners of the parent) = (Equity of current year end + Equity of previous year-end) / 2

Return on equity (ROE) = Net profit (attributable to owners of the parent) / Average equity (attributable to owners of the parent) * 100

Average assets = (Assets of current year end + Assets of previous year-end) / 2

Average assets exposed to interest risk = (Assets exposed to interest risk of current year end + Assets exposed to interes risk of previous year-end) / 2

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 earning assets – Cost of interest bearing liabilities

Cost / Income ratio = Total Operating expenses / Total Income * 100

Risk Management

The purpose of risk management is to identify, assess, manage and control all risks related to the activities of the Group. The principles of identification, measuring, reporting and control of risks at the Group are set out in the policies and procedures approved by the Supervisory Board and daily risk management is organized by Risk management unit. The purpose of the risk management is to identify, assess, monitor and manage all risks related with the Group in order to ensure the Group's reliability, stability and profitability. In the Group, risk management is based on three lines of defense. Business units as the first line of defense are responsible for taking and managing risks. The second line of defense – which includes the risk management unit – is responsible for developing and maintenance of the risk management framework. The third line of defense, internal audit function, carries out independent control over processes, operations and control functions in the entire Group. The rules and procedures of risk management are regularly reviewed at least once a year and updated in case of a need.

Detailed overview of the risks taken by the Group is presented in Note 3 of the annual report.

Capital base *(EUR thousand)*	31.12.2020	31.12.2019
Paid-in share capital	106 500	95 500
Statutory reserves paid in from net profit	4 022	3 237
Accumulated profit/deficit	62 972	45 619
Intangible assets (subtracted)	-807	-685
Net profit for accounting period (COREP)	17 441	14 863
Deductions	-2 511	-33
Tier 1 capital	**187 617**	**158 501**
Additional Tier 1 capital	38 000	23 000
Total Tier 1 capital	**225 617**	**181 501**
Subordinated debt	50 500	47 500
Total Tier 2 capital	**50 500**	**47 500**
Net own funds for capital adequacy calculation	**276 117**	**229 001**
Capital requirements		
Central governments and central banks under standard method	363	920
Credit institutions and investment companies under standard method	8 004	4 043
Companies under standard method	865 772	819 052
Retail claims under standard method	197 592	167 115
Public sector under standard method	3 250	2
Housing real estate under standard method	243 971	208 693
Overdue claims under standard method	13 668	5 387
Other assets under standard method	42 915	16 879
Total capital requirements for covering the credit risk and counterparty credit risk	**1 375 535**	**1 222 091**
Capital requirement against foreign currency risk	618	476
Capital requirement against interest position risk	0	0
Capital requirement against equity portfolio risks	972	960
Capital requirement against credit valuation adjustment risks under standard method	82	22
Capital requirement for operational risk under base method	95 104	76 766
Total capital requirements for adequacy calculation	**1 472 311**	**1 300 315**
Capital adequacy (%)	**18.75**	**17.61**
Tier 1 Capital Ratio (%)	**15.32**	**13.96**

Management and compensation policy

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

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 held for approval of the annual report is held at least once per annum.

The sole shareholder of LHV Pank is AS LHV Group. Shareholders with significant ownership interest in AS LHV Group are Rain Lõhmus and persons related to him with 23.4% and Andres Viisemann and persons related to him with 9.7%.

Supervisory Board

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

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

Management Board

The Management Board is a governing body of AS LHV Pank that represents and manages AS LHV Pank. The Management Board has three to seven members. The term of the Management Board member's powers is five years, unless otherwise decided by the Supervisory Board. The Chairman of the Management Board organizes the work of the Management Board. The company may be represented by two Management Board members jointly in each transaction.

The Management Board of AS LHV Pank had seven members. Starting from Jan 2021 the Management Board hs six members. Till January 2021 The Management Board was comprised of Erki Kilu, Andres Kitter, Indrek Nuume, Jüri Heero, Meelis Paakspuu, Kadri Kiisel and Martti Singi. Starting from January 2021 Erki Kilu is no longer the member of the board anymore.

Committees

The Supervisory Board of AS LHV Group, the sole shareholder of LHV Pank, has formed four committees on the AS LHV Group level, the aim of which is to advise the Supervisory Board of AS LHV Group in matters pertaining to audit and compensation as described below concerning all of the group companies that are part of AS LHV Group.

Audit Committee

The Audit Committee is above all an advisory body to the Supervisory Board of AS LHV Group in the fields of accounting, audit, risk management, internal control and internal audit, supervision and budgeting and the legality of the activities. The Audit Committee must comprise at least two members.

The duties of the Audit Committee are to monitor and analyze the processing of financial information to the extent necessary for preparing quarterly and annual financial statements, effectiveness of risk management and internal control, the audit process of financial statements or consolidated financial statements and the independence of the auditor and independent auditor who represents it on the basis of law and compliance of its activities with provisions of the Auditors Activities Act.

The Audit Committee is responsible for making proposals to the Supervisory Board of AS 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 organization and compliance with legislation and good professional practice.

Risk and Capital Committee

The purpose of the Risk and Capital Committee is to advise and support the Supervisory Board with regard to supervision of the general, actual and future risk appetite and strategy, considering all types of risk and ensuring their compliance with the business strategy, objectives, business practice and values.

Nomination Committee

The purpose of the Nomination Committee is to support the Supervisory Board in issues concerning the selection process and fit-and-proper requirements.

Compensation Committee

The duties of the Compensation Committee are to evaluate the implementation of compensation policy in the companies within AS LHV Group and the effect of compensation-related decisions on compliance with requirements related to risk management, own funds and liquidity. The Compensation Committee consists of at least three Supervisory Board members of AS LHV Pank.

The Compensation Committee supervises the compensation of Management Board members and employees of companies within AS LHV Group, evaluates the implementation of compensation policy at least annually and, if necessary, proposes to update the compensation policy and prepares draft resolutions related to compensation for the Supervisory Board of AS LHV Group.

Compensation policy

The policy of compensating members of the Management Board and employees of AS LHV Pank is set and its implementation is evaluated by the Compensation Committee established on the level of AS LHV Group.

A monthly base salary is paid to members of the Management Board and employees of AS LHV Pank. A supplementary monthly incentive salary is paid to a small number of employees directly engaged in sales and new customer acquisition. The Supervisory Board determines the base salaries of members of the Management Board and the Management Board determines the base salaries of employees. The Chairman of the Management Board is employed based on a service contract; everyone else is employed under employment contracts.

The Bank has made no major severance payments nor significant non-cash compensations.

Share options

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

As part of the program, there is an annual performance pay added to basic salary, the amount or issue of which corresponds to the fulfilment or non-fulfilment of individual and LHV objectives. The objectives of the program 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 program are 100% equity options. The term of share options is 3 years from the moment the options were granted. Additional criteria has apllied to options issued from 2018 onwards for Management Board members – they are not allowed to sell these shares after for another year after executing the rights under option. The three-year vesting period before issuance of shares gives the opportunity to evaluate the results in the long run. It is not possible to take the specified amount in cash in lieu of share options. Share options are issued annually in the amount of up to maximum 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 the 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 in 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 prescribed by law to the head or an employee 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 proved to be substantially misstated or incorrect.

Similarly to 2014, the share options were issued in 2015 to 2020. In 2020, the options issued in 2017 were fully exercised. Next share options issue could be in 2021 based on Supervisory Board decision.

The granting and size of share options was dependent upon the successful achievement of operational targets of the overall company and the targets of individual Management Board members and employees.

In the beginning of 2020, share options were granted to seven members of the Management Board of AS LHV Pank and ninety employees in the total amount of EUR 2 119 thousand. In the beginning of 2019, share options were granted to seven members of the Management Board of AS LHV Pank and seventy-one employees in the total amount of EUR 1 786 thousand. In the beginning of 2018, share options were granted to seven members of the Management Board of AS LHV Pank and fifty-six employees in the total amount of EUR 1 166 thousand. In the beginning of 2017, share options were granted to six members of the Management Board of AS LHV Pank and fifty-four employees in the total amount of EUR 1 204 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 issued in 2017 were fully exercised in 2020 and the shares with nominal value of EUR 1 were acquired for EUR 4.65 per share. Share options issued in 2018 can be exercised between the period of 01.04.2021-30.04.2021 and shares with nominal value of EUR 1 can be acquired for EUR 5.33 per share. Share options issued in 2019 can be exercised between the period of 01.04.2022-30.04.2022 and shares with nominal value of EUR 1 can be acquired for EUR 4.90 per share. Share options issued in 2020 can be exercised between the period of 01.04.2023-30.04.2023 and shares with nominal value of 1 euro can be acquired for 5.96 euros per share.

Members of the Management Board and employees were unable to opt for the determined amount in cash instead of share options. Share options cannot be exchanged, sold, pledged or encumbered. Share options can be inherited. The share option agreement will become void upon premature termination of the employment contract at the employee's initiative, exemptions to which can be made by the Supervisory Board of AS LHV Group and due to termination of employment contract on an extraordinary basis by the employer for a cause related to the employee. Pursuant to the Credit Institutions Act, the Supervisory Board of AS LHV Group may reduce the number of share options issued or cancel share options if the overall financial results of the company have materially deteriorated compared to the previous period, a member of the Management Board or employee of the company no longer meets award criteria, the company no longer meets the prudential ratios or the risks of the company are not adequately covered with own funds or determination of the performance pay was based on information which was inaccurate or incorrect to a material extent.

Wages and salaries

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

Calculated gross salaries and wages
(EUR thousand)

	Base salary	Incentive salary	Total	Number of employees
Retail banking	4 106	0	4 106	225
Private and corporate banking	1 980	0	1 980	49
Support services	4 817	0	4 817	176
Information technology	3 624	0	3 624	109
Total	**14 527**	**0**	**14 527**	**559**

Business environment

The COVID-19 pandemic, which broke out at the beginning of 2020, continues to drive the global political and economic agenda in many respects. An unprecedentedly steep economic downturn in Q2 was followed by a surprisingly quick rebound in the summer. The gross domestic product (GDP) of the G20 area grew by 8.1% in Q3 but still remained 2% lower than a year earlier. The strongest contributor to recovery was India (+21.9%) while growth in China, which had bounced back earlier, remained modest in Q3 (+2.7%).

Developments were similar in Europe where recovery was the strongest in countries whose Q2 GDP contraction had been the sharpest (France, Spain, the UK, Italy). The Baltic Sea region, which is relevant to Estonia, has clearly been less drastically affected by the present crisis: due to lower infection rates containment measures in the area have been predominantly more lenient than in other parts of Europe. Economic activity has remained high and, consequently, the losses resulting from the crisis are smaller. The fact that in the Baltic Sea region the GDP contribution of tourism is not as large as it is in the southern European countries also plays a role. It is true, however, that towards the end of the year the situation changed when both Latvia and Lithuania began to tighten restrictions at the time when many countries started lifting them.

On the whole, Europe's unemployment figures went up in the second half of 2020. In November the number of people out of work in the euro area was around a million higher than in Q2. Some months earlier unemployment was even higher. Across Europe, including the euro area, the UK and other European countries, the number of the unemployed grew by more than 2.5 million. The actual situation may be even more serious because the hardest-hit sectors include services (tourism, accommodation and catering, and transport) where the share of illegal and undocumented work is larger. Official statistics simply do not capture all terminations of employment relations.

Price inflation in the euro area, which had been sluggish, slowed further after the coronavirus outbreak in spring. During the summer, headline inflation was positive, remaining a few basis points above the zero mark, but in the second half of the year prices in the euro area decreased steadily. Downward pressure came mainly from tumbling energy prices. However, in the second half of the year, core inflation, which excludes goods and services whose prices are more volatile, also began to decelerate. The pass-through of low energy costs from producer prices to the prices of other industrial products has created additional deflationary pressure in the economy. Another contributing factor has been the temporary reduction of VAT rates in Germany, which has kept price inflation in Europe's largest economy at a standstill since July.

By the end of Q3 it was clear that the second wave of the pandemic was going to hit Europe at least as hard as the first one. Accordingly, the European Central Bank (ECB) decided to increase money supply to provide the economy with the liquidity required to survive the crisis. The envelope for the pandemic emergency purchase programme (PEPP) was expanded by EUR 500 billion to EUR 1.85 trillion and the net asset purchase phase of the programme was extended to at least the end of March 2022. Since the third series of targeted longer-term refinancing operations (TLTRO III) had been relatively well received by commercial banks, ECB decided to further improve its conditions. In general, the duration of all emergency incentives and programmes was extended and the ECB decided to offer four additional pandemic emergency longer-term refinancing operations (PELTROs) to provide an effective liquidity backstop. The ECB believes that the monetary policy measures that have been taken will contribute to preserving favourable financing conditions over the pandemic period, thereby supporting the flow of credit to all sectors of the economy, underpinning economic activity and safeguarding medium-term price stability.

The highly accommodative monetary policy stance together with an unseen amount of asset purchases have dropped the overnight interbank rate Euribor to below the deposit facility rate of ECB (-0.5%). Euribor has traditionally been higher than the deposit rate as banks have no incentive to loan money to each other with a lower interest rate than the risk-free deposit facility offers. But many market participants who have benefitted from massive asset purchases do not have access to ECB's deposit facility. And as the excess liquidity in ruling the market banks with already abundant reserves have started to charge a spread to accept additional deposits. As a result, the Euribor yield curve has fallen below the deposit facility rate in all its terms.

Estonia's economy contracted in Q3 by 1.9% year on year (growing by +7.6% quarter on quarter). The downturn was among the smallest in Europe and similar in scale to those of the neighbouring countries. The downturn for the first nine months was slightly above 3%. The strong rebound compared with Q2 reflected that the initial support measures taken to mitigate the impacts of the crisis had been effective: when conditions improved, companies were able to quickly resume their operations and restore their profitability.

In terms of sectors, the contraction was rather broad-based but fortunately relatively modest in most segments. Excluding the public sector, only the finance and insurance, energy, agriculture, and IT and communications sectors were able to increase their value added year on year. The construction sector posted growth in value added until Q2 but in Q3 the situation changed there as well and value added decreased by 8%. Considering the sector's long response lag, it is likely that the decrease in its value added will extend to 2021.

The manufacturing sector performed surprisingly well throughout the year despite the decline in demand and disruptions in the supply chains. Export growth also recovered in the last months of the year but the upsurge reflects mainly the lacklustre figures of the comparative period and strong results in certain segments rather than an overall export boom. For example, exports of electrical equipment accounted for roughly two thirds of total export growth in the autumn. Core exports, which are exports of products with at least 50% domestic value added, grew through the second half of the year at the rate of 4-5% on average.

Consumer prices in Estonia decreased by 0.4% in 2020. The decline was driven by a fall in global oil prices, which put pressure on the prices of motor fuels. Thus, on average, diesel fuel was 17% and petrol 6% cheaper than a year earlier. A supporting factor was the decline in housing costs, which primarily resulted from lower electricity prices. The government contributed by lowering the excise duty rates for diesel, gas and electricity from spring, which took Estonia's price decrease among the largest in Europe. Upward pressure resulted mainly from higher food prices.

Last year's price information needs to be reviewed keeping in mind that the consumption of many goods and services was seriously disrupted during the year. Hence, it is likely that the actual consumer basket did not meet the proportions set in statistics at the beginning of the year. People's gain from the price decrease was probably larger than usual because there were fewer spending opportunities. This is confirmed by growth in cash held in bank accounts.

Economic sentiment improved in the last months of the year, underpinned by optimism in the manufacturing sector. However, the onslaught of the second wave of coronavirus infections has lowered consumer confidence and, according to recent polls, many have started to build up their reserves by postponing major purchases. The new containment measures, which are somewhat more stringent than expected, will mostly affect this year. On a positive note, vaccines have already reached the market. Deploying the vaccines as effectively and quickly as possible is key to economic recovery. Against the backdrop of the global quantitative easing craze, Estonia needs to make smart forward-looking decisions in order to use available support in exiting the crisis as effectively and efficiently as possible. Holding on to outdated business models will make it hard to regain pre-crisis growth rates.

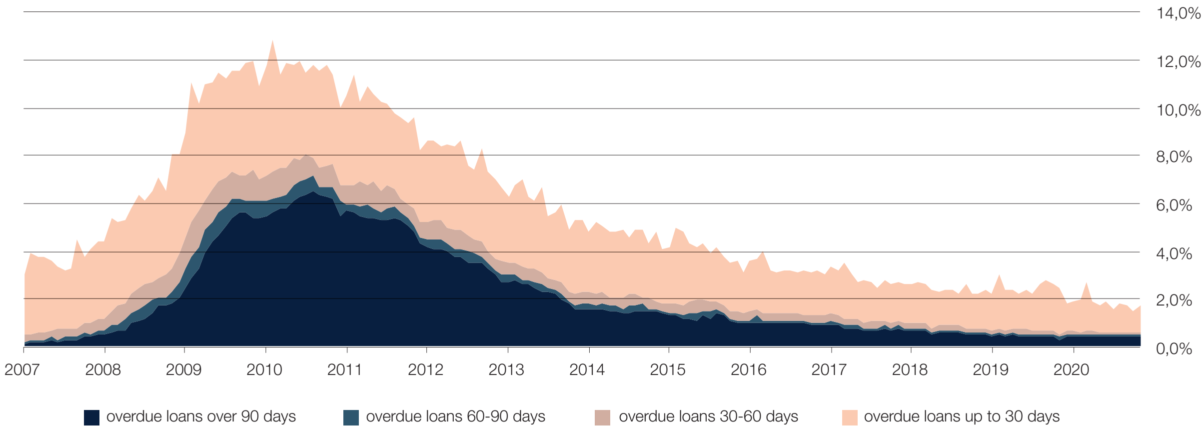
Key economic indicators of Estonia* — **Bank of Estonia forecast**

	2014	2015	2016	2017	2018	2019	2020E	2021E	2022E	2023E
Nominal GDP (EUR billion)	19.76	20.25	21.10	23.62	26.04	28.11	27.12	28.37	30.28	31.88
GDP volume**	2.8%	1.4%	2.1%	4.9%	4.8%	5.0%	-2.5%	2.9%	4.2%	2.6%
Private consumption expenditures***	3.3%	4.7%	4.4%	2.6%	4.3%	1.7%	-2.2%	3.8%	7.1%	4.0%
Government consumption expenditures	2.7%	3.4%	1.9%	0.6%	0.9%	0.5%	4.2%	-1.3%	-1.2%	-1.7%
Fixed capital formation	-8.1%	-3.3%	-1.2%	12.5%	1.7%	2.8%	-6.6%	7.5%	4.9%	5.4%
Exports	3.1%	-0.6%	4.1%	3.5%	4.3%	6.2%	-8.3%	5.7%	5.0%	3.4%
Imports	2.2%	-1.4%	5.3%	3.6%	5.7%	3.7%	-8.9%	8.1%	6.0%	4.4%
CPI	-0.1%	-0.5%	0.1%	3.4%	3.4%	2.3%	-0.4%	1.4%	1.9%	1.8%
Unemployment rate (% of the labour force)	7.4%	6.2%	6.8%	5.8%	5.4%	4.4%	7.3%	9.9%	8.0%	6.8%
Current account (% of GDP)	0.9%	2.2%	1.9%	3.3%	1.8%	2.0%	4.0%	2.0%	1.9%	1.7%
Budget balance (% of GDP)****	0.7%	0.1%	-0.3%	-0.4%	-0.5%	0.1%	-5.4%	-5.2%	-3.4%	-2.7%

* Numbers reported are annual rates of change in per cent, if not noted otherwise; ** GDP and its components are chain-linked; *** including NPISH; **** the budget balance forecast considers only those measures on which sufficient information was availanble at the date of the forecast.

Sources: Bank of Estonia, Statistics Estonia

Overdue loans share in loan portfolio



Source: Bank of Estonia

CEO letter on sustainabilty

LHV Group is the largest and fastest growing financial group based on Estonian capital. Through our international business line, we help make financial services more efficient and accessible. We feel increasingly responsible for safeguarding the environment and the well-being of society and we realise that it depends on us whether LHV's financing and investment decisions make a positive or negative impact.

LHV's main stakeholder groups are customers, employees, investors and the public. We believe that we can achieve the best outcomes for both the company and society when we take into account as broad a range of interests as possible. In practice, we expect LHV to remain a well-performing growth company but believe that this can be achieved while pursuing the best governance practices, positive social impacts and internationally agreed climate goals.

LHV has always paid a lot of attention to the impacts of governance and social risks. In recent years, we have expanded our focus to environmental risk management. Climate change and other ecological problems received considerable attention in 2020, both across the world and in the business sector. Environmental hazards also dominate the Global Risks Report published by the World Economic Forum, which ranks the biggest global threats on the basis of likelihood and the severity of impact. For the first time in history, the top five global risks in terms of likelihood are all environmental: extreme weather, major biodiversity loss, climate action failure, natural disasters and human-made environmental disasters. It is not surprising that the financial sector is also increasingly concerned with sustainable development and understanding the urgency of these issues.

We have committed to five United Nations (UN) sustainable development goals and have become signatories to the UN Principles for Responsible Banking. We aim to make our operations climate neutral by 2022. Still, we can make the strongest impact with our financing and investment policies. We have updated our exclusion list, which is the list of activities and projects that we do not finance or invest in, and are working hard to start driving environmental change together with our customers through a common set of measurable environmental targets. In 2020, we launched several new green products, including the green pension fund, home loan, lease, hire-purchase and business loan, which help LHV as well as the Estonian economy as a whole work towards the Paris climate goals.

In the area of corporate governance, the greatest recognition was the award granted to LHV as the company with the best investor relations on the Nasdaq Baltic stock exchanges. Transparency of governance provides assurance to investors and the public as well as better visibility to exercise control over topics such as potential conflicts of interest, corruption risks, etc. LHV's management model and management structure along with its supporting committees and risk controls, remuneration policies and compensation rates are described in detail in our annual report.

We interpret social responsibility in a broader sense as contributing to the development of the Estonian economy and capital markets and improving the financial literacy of people, and in a narrower sense as offering the best services to our customers and creating a motivating work environment for our employees. As regards the latter two goals, we are proud to report that we have been named the best bank in Estonia by the business magazine Euromoney and the third most attractive employer by the largest job portal in Estonia. Developing the Estonian economy and capital market is a part of LHV's mission. We are aware of LHV's role in driving change: we want to help both Estonian people and businesses move towards wiser financial behaviour and economic decisions. We are developing a modern economy that respects social contracts through our credit policies and the investment policies of our pension funds. The stronger the economy, the greater the wellbeing of Estonian people.

We are not quite there yet. In order to achieve the above goals, we need complete harmony with society as a whole. The financial sector may lead the way but to get the best outcome we need a concerted effort from the public sector, regulators, businesses and consumers. However, we have worked hard to set a good example in the achievement of environmental, social and governance-related goals. LHV has adopted a sustainability strategy along with related goals and internal regulations that help achieve these goals. We have created metrics and processes for getting the best results and provided sustainability training. We have launched several green products and aim to become climate neutral. We are prepared to do our part.

Our Approach to Sustainability

Purpose

LHV has a strong focus on sustainability and consideration for new societal needs. We are conscious and aware of the unprecedented challenge of climate change and exceptional environmental circumstances caused by human activity. We acknowledge that although in LHV, there are initiatives that deal with environmental and social issues, there is much more that could be done to align our everyday business and activities with our ESG goals.

Environmental and Social objectives and considerations are integrated into our everyday operations and value creation strategy. We are actively improving and developing the processes of managing and mitigating environmental and social risks associated with our business engagements and strive for continuous improvement and positive change in environmental and social practices across all business lines.

Commitment to UN SDGs

We are committed to collective as well as individual accountability in sustainable business. We regard it as our mission to promote and practice responsible banking that does not harm the environment and the people.

As of 2020, we have narrowed down our sustainability focus on five UN Sustainable Development Goals to set a goal-oriented framework for our activities and commitment towards a more sustainable future.

SDG 1: No Poverty

We believe that integrating social and environmental considerations into the core of our business, and investing in spreading financial literacy, can support the reduction of inequality, poverty, and hardship in society.

SDG 7: Affordable and clean energy

Sustainability is an integral part of our value creation and product development process. This includes offering our clients a comprehensive choice of green financial products and improving our processes of ESG-related due-diligence for our corporate clients and partners.

SDG 8: Decent work and economic growth

We recognize the importance of banks and financial institutions in driving sustainable growth, creating jobs, encouraging entrepreneurship, and fueling innovation.

SDG 12: Responsible consumption and production

LHV is committed to considering environmental factors in our business decisions and advocating for responsible lending and consumption.

SDG 13: Climate action

As a part of supporting sustainable financial sector development in Estonia, we are encouraging environmentally sustainable business practices within our sector and the State level.

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 competencies, develop sustainable financial products and services, improve business processes, and develop sector-wide partnerships to work toward more responsible business operations.

- **We realize the extent to which our business decisions affect society and the environment, and as a result, focus on managing these impacts in particular.**
- **We aim to be a leader in sustainable development in the financial world by striving toward initiating systemic change and creating possibilities for innovative and sustainable solutions that guide society toward sustainable development.**
- **We will bring our activities into conformity with the UN Sustainable Development Goals and the Paris Agreement.**
- **We operate transparently and publicly account for our progress and obstacles in various sustainability reports and through our corporate communication channels. We are continually improving our know-how on sustainability reporting standards and which to move towards a more comprehensive GRI reporting in our annual reports.**
- **We are committed to creating the necessary conditions for adhering to our sustainability strategy. This can be achieved by internal capacity building and integrating ESG aspects into the group-wide business processes.**

Our Focus and Impact

LHV's ESG focus topics were decided based on the following:

- **Potential positive and negative environmental and social impacts of the business activities of LHV Bank, drawing on the UNEP FI Portfolio Impact Analysis Tool;**
- **expectations of external interest groups (experts on social and environmental impact, clients and partners);**
- **opinions of internal interest groups (LHV management, key persons, and employees).**

Based on the above inputs, LHV's sustainability focus topics going forward are:

UN goals (SDGs) | Our goals

All these focus areas are managed through three levels:

- Positive and negative impact areas of LHV's operating activity (e.g., the impact of financial decisions on the environment and society)
- LHV as an organization (i.e., management and organizational impacts, e.g., "house in order" activities.
- LHV's broader impact in society (activities supporting and guiding a more comprehensive, systemic change in Estonian society)

ESG indicators and metrics

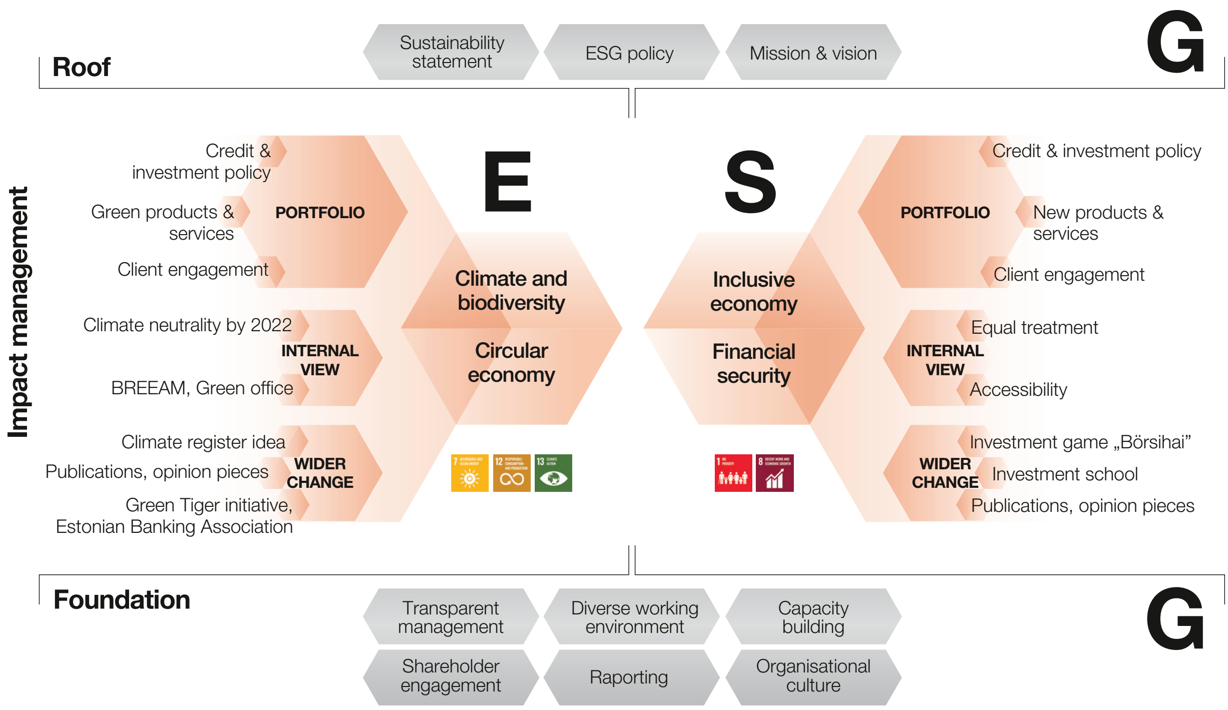
To meet our goals for more sustainable business development, we comprehend the challenges of measuring or impact and setting KPIs to sustainability goals. For that, we must invest more time and effort in the future and build internal capacity to measure our success better. For that, we have today set key indicators to all of our impact areas and developed a plan on what data we need to start gathering and measuring in the coming years to understand and meet our targets. We have also developed an ESG roadmap for 2021-2023 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 goals for LHV in regard to ESG moving forwards.

Below are some of our key ESG indicators we are working on with respective data:

Focus area		Key indicator	2019	2020
Environment (E)		LHV's CO_2 footprint (t CO_2-eqv)	1210t	865t
		Share of corporate banking loan portfolio to the biomethane industry	0.55%	1.25%
		Share of green assets in LHV Asset Management portfolio	N/A	4.2%
		Share of loan portfolio to solar energy industry	0.05%	2%
		Proportion of active clients in II pillar Pension Fund Green	N/A	2.2%
Social (S)	Inclusive and cohesive economic space	Share of corporate banking loan portfolio to Local Governments	0	14.4%
		Proportion of consumer banking customers registered outside Harjumaa	34.3%	34.9%
		Proportion of home loans outside Harjumaa	19.8%	19.7%
	Financial literacy and economic sense of security	Total number of Investment School attendees	6000	7420
		Average number of clicks per article in Finantsportaal	2372	2393
		Share of use of investment products among customers up to 25 years of age	19.3%	26.1%
		Share of use of investment products among clients with native language other than Estonian	5.6%	5.5%
Governance (G)		Percentage of female employees in leadership positions	26.5%	44.8%
		Client satisfaction index	93.5 %	94.9 %
		Number of legal proceedings pending against the company as of end of year	0	0
		Incidents of ethics and corruption	0	0
		CEO pay ratio	0.18	0.19

ESG framework and core activities

The graph below illustrates LHV's main impact areas, goals, and respective core activities, as well as the main elements governing and supporting our sustainability efforts.



The principles of responsible banking

The UN Principles for Responsible Banking give banks a framework for sustainable operation and sets out guidelines for promoting life in society. We joined with the initiative to show our commitment to the UN Sustainable Development Goals and align our activities with the Paris Climate Agreement's goals. We take part in international cooperation in the financial sector and sharing best practices.

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.

Environmental

Contributing most to our focus SDGs:

We realize that business enterprises and economic progress can often draw on natural resources. However, we also recognize that there is an alternative, more sustainable way to achieve growth and create value. Through their business and offerings, financial institutions have a transformational capacity to create positive change and scale sustainable business practices through innovation, creativity, and the entrepreneurial spirit.

LHV desires to operate sustainably, and as an Estonian company, we want to help the Estonian economy to adapt to meet the climate targets. To do so, LHV is

- **Contributing to achieving the goals of the Paris Climate Agreement**
- **Supporting Estonia's goal of attaining a climate-neutral economy by 2050**
- **Open to the opportunities afforded by the new economy**
- **Working together with external stakeholders to bring about more positive change (i.e., Estonian Banking Association, external consultants, and organizations to help build capacity)**
- **Following green office principles and monitoring its annual carbon footprint to become carbon-neutral by 2022**

A financial institution's sustainable business operation means consistently incorporating ESG-friendly practices into its offering and product development. To date, we have developed special loan offers that motivate our clients to make environmentally responsible consumer decisions. We have also created and disclosed an exclusion list of activities that are not in accordance with our credit policy and the principles of sustainable and responsible operations.

Green operations

Our goal is to make our office activity climate-neutral by the year 2022. Even though our greatest environmental impact comes from financing and investing activities, it is no less important how we administer our business every day.

That’s why we wanted to make sure that our own consumption is sustainable, that we keep our house in order and serve as an example on all fronts of the effort to meet climate goals.

Green Office Principles

LHV has decided to take steps towards more environmentally friendly operations. This has been done by improving the office environment and involving employees in the Green Office process by awareness-raising. In 2020, LHV's Tallinn office was awarded the Green Office Certificate, which confirms our office operations environmentally sustainable activities. In December 2020, LHV’s Tallinn Office was awarded „Best Green Office of the Year“ award bu the Estonian Association for Environmental Management.

Our Carbon Footprint

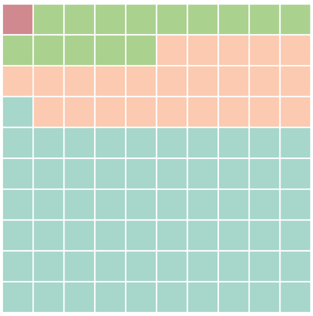
Greenhouse gas emissions must be reduced significantly to avoid the worst consequences of climate change. Our office activity also generates emissions - both directly and indirectly. Mostly, due to the use of heating, power, employee commute, and business travel.

What have we already accomplished?

At the beginning of 2020, we started collecting emissions data for the first time and ran the calculations for our carbon emissions for 2019. We did the same for 2020 at the beginning of 2021

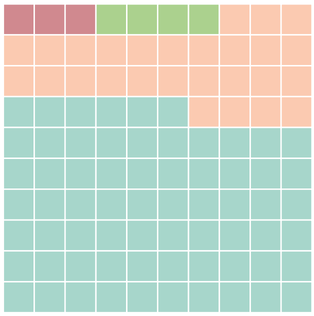
In 2019, LHV's office activity had a greenhouse gas emission footprint of 1210 tonnes of CO2-equivalent, which is 2.6 tonnes per employee at the time of calculation. For 2020 the results were 865 tonnes, or 1.7 tonnes per employee.

Carbon emissions sources (Scope 1 and Scope) comparison 2019 and 2020



2019

- 61% from the use of heat and power
- 24% from employees commuting to work
- 14% from business trips
- 1% from office expenses, such as paper, water and waste.



2020

- 66% from the use of heat and power
- 27% from employees commuting to work
- 4% from business trips
- 3% from office expenses, such as paper, water and waste.

We have put together a climate neutrality achievement plan in order to operate more sustainably and reduce our negative environmental impact. In 2020 we made the transition to electricity furnished with a green energy certificate, which has cut emissions by 30%. In addition to that, working towards the Green Office Principles, we have also organically reduced our emissions. We are also working on developing a local and ethical project for carbon offset which we can contribute to offset CO2 which we cannot offset through our everyday office operations.

We calculated our footprint based on the internationally recognized Greenhouse Gas Protocol. We will repeat and refine the calculation each year. Based on which additional categories we are able to gather reliable data in, we will strive toward a fuller picture.

Green 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 clients 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, which at the same time reduces greenhouse gas emissions, pollution, and waste generation.

Green Home Loan

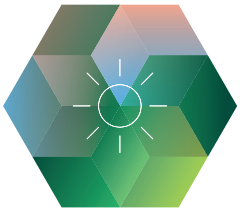
One of the most important consumer decisions a person will ever make – in terms of the financial cost and the environmental impact – is regarding purchasing their home. One-third of the average Estonian's annual CO2 footprint is related to their home – mostly deriving from energy used for heating and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

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

Green Car Leasing

We aim to promote the purchase of energy-efficient vehicles. The most energy-efficient vehicle you can choose to drive is a fully electric car. But to be sure of its sustainability level, the energy needs to derive from renewable sources entirely.

From 2026 onwards, only cars with zero CO2 emissions per kilometer are considered clean vehicles. Only electric and hydrogen vehicles will meet this standard. We, therefore, offer car leasing for new fully electric vehicles purchased for general use.



Green hire-purchase

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

Green Investment Loan for Companies

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

Green Loan for Housing Development

For people to have energy-efficient apartments, someone has to build them. Therefore, we offer investment loans for energy class A housing developers with a lower-than-usual interest rate.

Pension Fund Green (II pillar)

In March 2020, we launched Estonia's first green pension fund. We had been working on it for exactly a year. LHV Pension Fund Green is meant for anyone who cares even a little about green philosophies and believes that capital investment should be profitable in the long-term and environmentally sound and sustainable. The fund always invests 75% to 100% into equity. At least half of the portfolio is invested in investment funds that abide by sustainability principles or have environmental themes.

Pension Fund Green Plus (III pillar)

In December 2020, LHV established the Pension Fund Green Plus, which is the sister fund of the first Estonian second pillar fund that makes green investments. The first green third pillar fund's investment portfolio will consist of socially responsible, sustainable, and environmental assets. The equity risk to be taken with the fund will always remain between 75% and 100%. The green second and third pillar funds are aimed at everyone who cares about the green mindset and believes that investments must be productive in the long term and environmentally friendly and sustainable.

Social

Contributing most to our focus SDGs:

While banks and financial institutions play an integral part in driving economic growth in a society, 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, clients, and employees.

By acknowledging our role and societal influence on the local level, we

- **Preserve a budget to support the advancement of music or arts, education, sports, and community events.**
- **May provide support to external movements and partners to promote the cultural and economic development of local communities.**
- **Stand for the equal opportunities of people and companies active in the economy**
- **Build the confidence of our customers toward LHV as a non-discriminatory financial services provider**
- **Encourage financial literacy and economic knowledge-sharing**
- **Continuously improve our competencies in the field of ESG to further advance the cohesion of society.**

The prosperity and welfare of our people is the core of our business operation. We realize that good business results and growth do not happen in isolation of people who create value, are well taken care of, and are engaged in their personal and collective mission, and feel highly valued.

Social responsibility

Along with the growth of LHV, we are also becoming increasingly aware of our growing role in the Estonian economy and society in general. Based on our mission, we support activities that allow Estonian people and businesses to think more boldly about the future and realize 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 said goals.

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 simultaneously, we actively contribute to educating the investor community. In our relations with more than 10,000 shareholders, we are open, transparent, and inclusive.

- We organize free seminars as part of the Investment School, where over 7400 people participated in 2020 (the number of participants in 2019 was 6,000). This year, most seminars were held in the form of webinars.
- We also carry out the annual stock market game Börsihai. This year, the number of participants reached 6,576 (the number in 2019 was 4,600).
- For the second year in a row, we organized an advertising campaign on financial literacy, targeted at young clients with insightful content on the website.
- In cooperation with the University of Tartu, we prepared an elective subject 'Functioning of a modern banking company on the example of LHV Pank' for which 54 students registered.
- We participated in projects for improving financial literacy organised by the Estonian Banking Association.
- We supported the Investor Toomas - a conference organised by Äripäev and the Investment Festival carried out by the Investment Club, the Women's Investment Club, and the stock training

Sponsorships

Within its means, LHV supports activities that contribute to the development of Estonian society. In our sponsorship projects, we prefer long-term and substantial cooperation.

Estonian Culture and Society

- Estonian Music Days – for five years already, we have supported the Estonian New Music Award, which was awarded to Märt-Matis Lill in 2020.
- Enn Soosaar Foundation – we support issuing the Ethical Essayists Award. In 2020, the award went to Eero Epner.
- Estonian Film and Television Awards 2020 – we supported the recognition of outstanding achievements.
- Intsikurmu Music Festival in Põlva – we supported the music festival for the fifth time.
- 'Who does it?' support program. We launched a support project for communities to fund a joint initiative. In 2020, we directed a grant amount to the Leesi Tarbitajate Ühisus project to renovate the village store.
- Charity function for bank cards. In 2020, we developed a function for LHV bank cards, which the customer can use to make micro-donations to the selected charity organization. We will launch this option at the beginning of 2021.

Sports and Healthy Lifestyle

- The Estonian Football Association – LHV Pank has been the main sponsor of the Association and the Estonian National Team since 2010. Also, we have created the support system of LHV's Football Card through which we gave 79,766 euros to Estonian football clubs in 2019.
- Estonian Optimist Class Association – we have supported Estonian sailing for more than ten years. We support the promotion of sailing among children and young people. In addition to that, we also supported Olympic athlete Ingrid Puusta.
- Rally Estonia – we supported the World Rally Championship round in Estonia for the first time.
- Simple Session – LHV was one of the main sponsors of this top extreme sports event.
- We supported the BMW Golf Cup amateur golf competition.
- We organize a corporate football event, the LHV Cup. In 2020, it was held for the fourth time.

Estonian Economy and Entrepreneurship

- Estonian Entrepreneur of the Year competition – we have been one of the Estonian Entrepreneur of the Year competition's main sponsors since 2012. In 2020, the title of Entrepreneur of the Year was awarded to Kaarel Kotkas.
- Gazelle Movement – LHV supported the gazelle movement to recognize fast-growing companies.
- We supported the conference Economic Security 2020

We also support smaller local initiatives with our knowledge, LHV themed gifts, advice, and performances by our people. We participate in fairs, as well as cooperate with universities. We belong to the Estonian Association of Information Technology and Telecommunications, the Estonian Chamber of Commerce and Industry, and the Estonian Employers' Confederation. We consider it essential to help Estonian manufacturers and entrepreneurs with their procurements and cooperation relations, consciously using their products and services.

Social impact through sales and channels

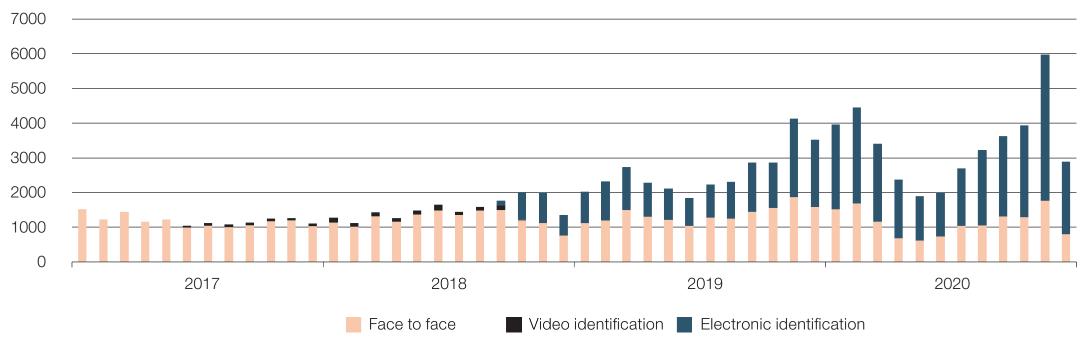
We aim to offer the best and most straightforward use of all our products and services to our customers. The year 2020 was remarkable due to COVID-19 and because social distancing made electronic channels play an even more critical role in business and society. This clearly demonstrates that our focus on digital channels is the right way forward in making our services available to everyone.

The Best E-channels in Estonia

For LHV, it is continually essential to develop our e-channels so that our internet bank and mobile app will support the availability of all of our services. For the past few years, our main target has been the services targeted at private customers, but clearly, we want to offer the same experience to our business customers.

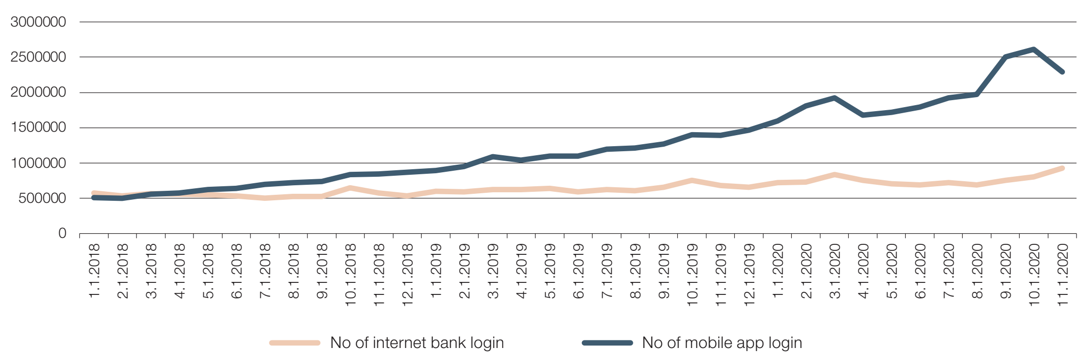
In 2020, we have onboarded about 3500-4000 new customers every month. More than half of our new customers open their bank accounts through our e-channel. We have seen this growing trend in previous years, but 2020 has shown that most of our customers can use our services remotely and online.

Identification upon onboarding of customers (private customers)



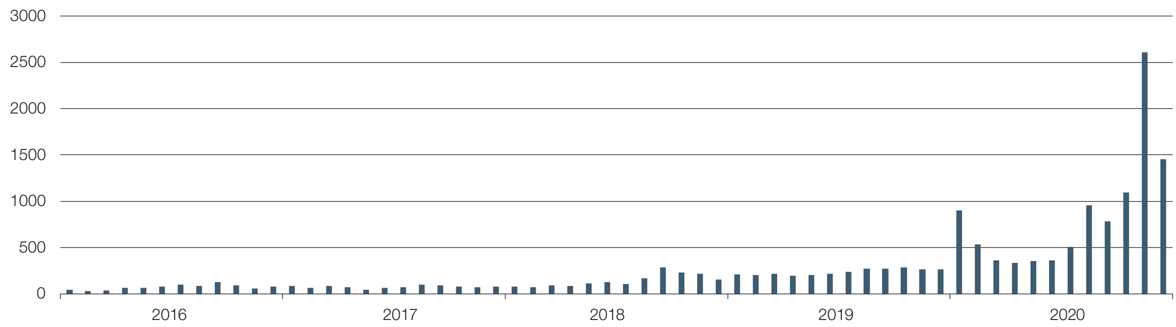
The increase of new customers login into the internet bank and mobile app was 20% and 40% in the past year. This means that customers use electronic channels even more than before.

LHV online banking and mobile bank usage activity by login



At the beginning of 2020, we launched an effortless and smooth way to open a bank account for underage children through our internet bank or mobile app. Only the child's ID card, passport, or residence permit card issued in Estonia is required for opening the account.

No of Child Accounts



In the year 2020, we made functionality that we can send e-notifications to our customers in e-channels.

LHV is also the first bank in the world to offer virtual ISIC Student card orders via its own mobile app. Virtual card means the students no longer need to have an extra plastic card to prove their student status or get international discounts.

All our customers who have bank cards can see their card PIN code in our mobile app. That means we have reduced the number of notifications significantly that we usually send my mail.

Our customers can also use ApplePay and Google Pay in their mobile app – so there is no need to carry plastic bank cards with them.

Focus on Customer Experience

A positive customer experience is critical to the sustainable growth of any business. And customer experience is essential for us. A positive customer experience promotes loyalty, helps us retain customers, and encourages brand advocacy. Therefore we have also considered the needs of visually impaired people when developing our channels.

As in previous years, we also focus on promoting financial literacy. For that, we will develop an Assistant Budget Planner tool in our e-channel for our customers to act even smarter in their financial decisions.

We are always responsible in planning our sales and marketing campaigns and trying to offer the best possible solution for the customer. We try to take into account our customer opinion and preferences. All our activities are based on customer segments and the unique needs of those segments. Our goal is to offer all of our products and services online and plan our sales activities by segments even more to support a positive customer experience.

Our societal impact as an employer

People are the most important asset of LHV. Our team is a community of 515 people, who carry the same corporate values and work towards a common goal. We strive for an honest, open and supportive internal climate. LHV aims at being the best employer, so that every person in the company can be involved in the development of the company, feel the importance of their contribution and prosper professionally.

We want to promote the feeling of ownership in our employees. Which is why we have established a stock option programme. The programme is a performance pay system for key employees, thereby combining the interests of owners and those receiving the performance pay and encouraging focussing on long-term performance while considering the risks.

Our goal is to increase the job satisfaction of LHV's employees, motivate them, raise their competence (knowledge, skills, experience and capacity), expand personal fulfilment opportunities, and guide the development of staff satisfaction. We're also working hard to ensure the availability of young talent, and foster the feelings of solidarity and pride. The main focus of LHV as an employer is set on an inspiring organizational culture and a good feeling of employees when coming to work every day.

LHV is a fast-growing company, which is also reflected in recruitment. In a year, LHV recruited 79 new people. Of all people in LHV, 97% work full time. In 2020, the voluntary staff turnover in LHV Group companies was 5,7%, which is significantly lower than the 10.9% in 2019. This is presumably due to a general situation in the labor market, where the number of job offers has decreased, and therefore, employees are less likely to change employers.

Employee Development

We contribute to the personal and professional development of our people. Our training approach is guided by a person-centered approach focusing on an individual's specific needs, motivation, and qualifications. If necessary, we offer rotation within LHV. We have developed an internal training program, including thorough training for new employees and language courses. Leadership training has provided our managers with practical tools to improve the management, instructions for smoother internal communication, advice on recruitment, and the current talent market's demands. Based on the feedback from managers, we can today say that there has been improved communication skills and co-operation deriving from more networking experiences. We are continually updating the format of performance and development discussions to ensure that people can most benefit from them.

Promotion of Employees' Health

LHV contributes to the physical and mental health of its employees. We offer our employees the possibility to use free psychological counseling services for personal or professional issues they might face. From Autumn 2020, we provide health audits for all employees over 40 years of age who have worked in LHV for at least two years. Health audits can be repeated every three years. We also provide flu vaccinations to employees who want them and reimburse the costs of vision and dental care.

We compensate our employees' health-related expenses quarterly (gym memberships, public sports events, room rent for sporting activities, rehabilitation) in a set amount.

The Quarterly health compensation was used actively in 2020: AS LHV Pank 75%; AS LHV Varahaldus 78%; AS LHV Finance 74%.

LHV has an outstanding occupational health package. LHV is part of a health-promoting network of employers in Estonia. We also consider health care recommendations: we use eye-sensitive computer screens, 100% adjustable chairs and desks, and, if necessary, provide people with ergonomic devices and the opportunity to participate in office gymnastics following the instructions pre-recorded by the trainer. We use as many health-friendly and natural materials as possible in the office space. In the office, we have healthy and natural carpeting with high wool content. The share of sick days in LHV companies in 2020 was 0.4%.

Work-life balance

We value the balance between work and private life. Among other goals, as a family-friendly employer, we wanted to harmonize our activities with the Ministry of Social Affairs' family-friendly employer program. As a result of two years of work, we earned the gold level of the family-friendly employer program in 2019, which means that LHV supports its employees at every stage of their life. We try to consider the personal needs of people working at LHV as much as possible. For example, we can offer students part-time working hours or, if possible, flexible working hours. To ensure the right work-life balance, we value family life: employees receive monetary bonuses when their child starts school, can work reduced hours on their child's birthday, and get three days off for having a wedding. We organize a Christmas event for families with children every year. We offer a childbirth allowance and a death grant.

Inclusive workplace

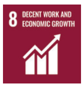
We have developed various measures to get feedback from our employees and encourage in-house communication. In Autumn 2020, we have launched a new engagement survey (Gallup Q12 questionnaire), which we will conduct once every six months going forwards. 92% of employees participated in the first Q12 engagement survey. The overall result of the survey was an average of 4.3 points out of 5. Our goal is to keep employee satisfaction high and understand what our people need to remain happy and engaged. Gallup Q12 process also includes individual and team discussions and gives an excellent opportunity for everyone to have their say. We take employees' suggestions seriously and integrate them in our management decisions. Employees can provide their input and contribute to the development of the company at meetings and strategy days. We collect feedback from new employees at the end of the probationary period and take it into account in their future work.

A Recognized Employer

LHV is a sought-after and recognized employer. In the employer survey of CV-Online, published at the beginning of 2020, LHV was considered the second most attractive employer in Estonia. The CV Keskus annual survey of Desirable Employers also revealed that LHV reached the third place as a newcomer. We were also recognized as an attractive employer among students of economics and experienced specialists (based on Instar survey). Attractiveness as an employer enables LHV to have a flexible recruitment process, as the interest in LHV has improved year by year. We communicated with more than 4,500 candidates during the past year and selected 2,9% of them to work with us. We have also emphasized requesting the candidates' feedback, and this process has been significantly improved by implementing the Greenhouse recruitment software. We also give feedback to the candidates. We take care of our young talents by offering internships and job-shadowing. Every 10th employee started at LHV as an intern.

Governance

Contributing most to our focus SDGs:



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 standard. We are carefully managing all potential conflicts of interest, avoid bribery, money-laundering, unlawful behavior, and corruption

To encourage the sustainability mindset across all management levels and the organization, we:

- Maintain a flat, non-hierarchical organizational structure to promote 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
- Recognize 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 analyzing 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 Financial Supervision Authority and the Nasdaq Tallinn Stock Exchange.
- Have integrated ESG targets into executive compensation program.

Responsible management culture

Responsibility and openness in management are the core pillars of our operating principles and are firmly rooted in our mission and values. We strongly believe that our high ethical standards and consideration of all stakeholders, high-level risk management, and lawful behavior are critical to our success in the long term. All managers and employees of LHV must behave ethically and responsibly and following the Code of Ethics is mandatory. LHV's Code of Ethics is the foundation of LHV's various policies, including the Company Governance Policy, internal regulations, and procedures governing the specifics of adherence to the Code of Ethics. In 2020, we also created and published our very first ESG Policy, where our responsibility and commitment to social and environmental issues are clearly stated and explained.

Primarily we rely on the lawfulness, best practices, and common-sense principle, doing our job responsibly, transparently, and with a fundamental goal to "do no harm." The work of the Supervisory Board of the Group is supported by different committees: the Remuneration Committee, the Nominating Committee, the Audit Committee, the Risk and Capital Committees. LHV's underlying governance principles are described in more detail in the "Best Practice of Corporate Governance."

The LHV management structure is easy-to-understand and includes clear lines of responsibility. An essential part of responsible governance is meticulous risk management and critically analyzing our own activities. The mapping and mitigation of credit risks, liquidity risks, market risks, crime risks, and operational risks are taken very seriously at LHV.

We have three lines of defense for risk monitoring and risk control. The internal control framework covers both well-functioning independent risk management, compliance checks, and staff performing audit functions. We have established the necessary committees to advise on risk management. The company gives a comprehensive overview of the risks in the annual "Risk and Capital Report of AS LHV Group."

In January 2020, the credit rating agency Moody's again assigned LHV Pank an investment-grade credit rating, confirming a sustainable, strong financial profile and its ability to serve the commitments taken. The critical role of responsible management is coordinated with legislation and sector-specific rules. LHV is precise and cooperative in dealing with regulators and monitoring agencies. We comply with all obligations and accountability arising from the law. In 2020, no nonconformities to regulations or requirements were identified regarding LHV.

Equality and non-discrimination

LHV is an equality-driven, fair, and inclusive employer that always fosters and maintains non-discriminatory business and HR practices. In the management and recruitment process, we are guided by LHV's best interests and our people's welfare and hold ourselves to the highest of ethical standards. In promotion and recruitment activities, we make the decisions in a gender-neutral and non-discriminatory manner based on the candidate's education, skills, and prior experience and, if necessary, requirements arising from the respective legislation. LHV has not found it necessary to implement any diversity of equality policies. In our remuneration policy, we are objective and unaffected by the employee's person. If required for the positions, we always check compliance with the entry criteria.

Equal treatment and non-discrimination of employees is essential for LHV. In 2020, there were no such violations in LHV. There were no labor disputes, discrimination cases, or violations of human rights. We always act neutrally and do not discriminate against our customers nor our employees due to their political opinions or personal preferences.

Investor relations

LHV actively contributes to developing good relations with the investor community, and we have set high standards for ourselves in being open, transparent, and raising the awareness of our investors. We have set up an investor relations website, making all documents and information available to the shareholders following the Corporate Governance Recommendations and statutory requirements. LHV treats all shareholders equally and notifies all relevant essential circumstances, ensuring equal and quick access to the respective information and being open to questions. Information is disclosed in accordance with the rules set forth for publicly traded companies. In 2019, LHV Group triumphed in the Nasdaq Baltic Awards' main category, winning the "Investor Relations of the Year" award. We were recognized for the best investor relations practices and the highest shareholder returns among Baltic listed companies over the past two years.

Cooperation

Organizations we work with

The relationship between sustainability and cooperation is intuitive for LHV and we realize there is much more power in working together with like-minded people and organizations. Our commitment to achieving a prosperous, inclusive, and resilient economy supported by a sustainable development and a world where natural resources are used reasonably, can only be achieved in usion and by engaging many stakeholders.

Green Tiger

Green Tiger is a new initiative from Let's Do It, the organization that launched the global World Cleanup Day project. Green Tiger aims to shape the movement into the next significant countrywide initiative. Green Tiger can also be compared to the Estonian Tiger Leap computerization project from a few decades ago. Green Tiger creates a circular economy model for individuals, the community, and the private and the public sector. Green Tiger will be a future trendsetter for other countries. So far, LHV is the initiative's only representative and partner from the banking sector.

Estonian Banking Association

The Estonian Banking Association's sustainable banking committee was created in January 2020 at the initiative of LHV. One of the committee's main goals is to use financing activities to help identify and leverage new sustainable business opportunities that will increase the competitiveness of local companies, communities, and the country as a whole. The committee will also contribute to building sustainability-related awareness and be a partner for governmental institutions, the Bank of Estonia, and influential organizations in developing sustainable financing.

Finance Estonia

LHV is a member of FinanceEstonia. Our activity in this non-profit allows us to contribute to the spread of sustainable banking principles throughout the financial sector. We also support the Green Finance conference organized by FinanceEstonia, dedicated to discussions on the green ethos as a future trend throughout the financial services world. FinanceEstonia supports the development of the financial sector, innovation, and the export of services. The event has, however, been postponed until further notice due to COVID-19.

NGOs

In 2020, we engaged with several local non-governmental organizations to introduce our sustainability commitment, validate our portfolio impact analysis results, and get feedback on our action plan and potential activities for the next few years. We understand the importance of involving various stakeholders and maintaining a discussion with organizations dealing with specific social and environmental issues daily.

Discussions on State Level

We are making efforts to support Estonia's bid to become the first in the world to develop a sustainability performance measurement system for corporate lending where private and public interests can be linked for climate-related goals.

Estonia has set the goal of a climate-neutral economy by the year 2050. Achieving this objective will require cooperation between the state and the private sector. It would also need a detailed plan. The plan should, however, be based on a transparent system to measure sustainability performance. To support this process, we've thought about motivating the private sector to effectively measure climate impact and help the entire financial industry direct capital into sustainable investments.

We have put together our first concept note for a database of climate impacts. Banks could rely on the central database in making financial decisions, and it would also be the underpinning for state support and guarantee programs. The final system should be automated, without undue burden on companies, and should be in line with data collection minimization and the once-only principle. We have already promoted our idea, brainstormed with partners (policy planners, other market participants, etc.). We are working to keep up the discussion to reach a point where the private and government sector can collectively shape the final system and test the idea.

Commitment to sustainability metrics

To increase our positive impacts and reduce the adverse effects of our business and manage the risks to the environment and the people, we have, in 2020, set a specific plan for 2021-2023 on what we need to start tracking to influence our most significant impact areas. We are committed to creating data gathering methodologies across all business lines, setting starting positions, and regularly monitoring and assessing our progress in moving closer to our ESG goals. In 2020, we have also investigated ways of visualizing ESG data by developing specialized digital ESG dashboard solutions. In addition to that, in 2020, we became a member of the Forum of Responsible Entrepreneurship (Vastutustundliku Ettevõtluse Foorum). Being part of the community will give us access to a unique sustainability index methodology, which will even better help us track, understand, and report our current ESG status and progress.

Transparency through sustainability reporting

We have taken it a goal to improve our sustainability reporting and non-financial disclosure practices and know-how in the coming years. In 2020, we started improving our know-how on reporting ESG metrics and also contributed to several voluntary non-financial disclosure initiatives like the Nasdaq Environmental and Social Disclosure Form and an Estonian banking-sector specific ESG disclosure project led by a local Estonian NGO Estwatch. The year 2021 will be our first year of reporting to UNEP FI about our progress with the Principles of Responsible Banking. In 2021 we will also make an action plan to better align our reporting practices with GRI requirements and the Nasdaq ESG Reporting Guide for Nordic & Baltic Market. We understand that aligning our reporting practices with international standards also means disclosing more non-financial information than we do right now. To do that, we will put much more effort into gathering and analyzing ESG data, improving ESG communication and internal processes, developing and publishing more sustainability-related materials and reports, and building in-house capacity on globally recognized ESG reporting standards.

CONSOLIDATED FINANCIAL STATEMENTS

Consolidated statement of profit or loss and other comprehensive income

(EUR thousand)	Note	2020	2019
Interest income		88 374	61 413
incl interest income based on EIR		84 480	57 804
Interest expense		-19 327	-13 498
Net interest income	**5**	**69 047**	**47 915**
Fee and commission income		31 152	24 157
Fee and commission expense		-12 769	-11 349
Net fee and commission income	**6**	**18 383**	**12 808**
Net gains from financial assets measured at fair value	10	834	126
Foreign exchange rate gains/losses		43	79
Net gains from financial assets		**877**	**205**
Other income		208	176
Staff costs	7	-21 115	-17 042
Administrative and other operating expenses	7	-15 150	-15 475
Profit before credit losses		**52 250**	**28 587**
Impairment losses on loans and advances	11	-10 898	-3 210
Profit before income tax		**41 352**	**25 377**
Income tax expense		-6 749	-3 277
Profit for the year		**34 603**	**22 100**
Other comprehensive income/loss:			
Items that may be reclassified subsequently to profit or loss:			
Available-for-sale investments:			
Net gains on investments in equity instruments designated at FVOCI	9	0	134
Total profit and other comprehensive income for the year		**34 603**	**22 234**
Total profit attributable to:			
Owners of the parent		32 514	19 804
Non-controlling interest		2 089	2 296
Total profit for the year		**34 603**	**22 100**
Total profit and other comprehensive income attributable to:			
Owners of the parent		32 514	19 938
Non-controlling interest		2 089	2 296
Total profit and other comprehensive income for the year		**34 603**	**22 234**

Notes on pages 19 to 103 are an integral part of the consolidated financial statements.

Initialled for identification purposes only
Allkirjastatud identifitseerimiseks
03. 03. 2021
Signature / allkiri
KPMG, Tallinn

Consolidated statement of financial position

Assets

(in thousands of euros)	Note	31.12.2020	31.12.2019
Assets			
Due from central bank	8	2 213 211	1 232 733
Due from credit institutions	8	170 062	32 247
Due from investment companies	8	9 985	5 473
Equity instruments at fair value through other comprehensive income	9	0	432
Financial assets at fair value through profit or loss	10	322 930	32 499
Loans and advances to customers	11	2 208 823	1 687 034
Receivables from customers	12	2 454	2 745
Other financial assets	13	2 073	2 246
Other assets	13	1 943	1 857
Tangible assets	14	2 766	1 903
Right-of-use assets	14	3 805	4 777
Intangible assets	14	807	685
Total assets		**4 938 859**	**3 004 631**
Liabilities			
Deposits from customers and loans received	15	4 610 015	2 738 601
Financial liabilities at fair value through profit or loss	10	221	8
Accounts payable and other liabilities	16	25 441	23 774
Subordinated debt	18	88 500	70 500
Total liabilities		**4 724 177**	**2 832 883**
Equity			
Share capital	19	106 500	95 500
Statutory reserve capital	19	4 022	3 025
Other reserves	9	0	212
Retained earnings		98 285	67 793
Total equity attributable to owners of the parent		**208 807**	**166 530**
Non-controlling interest		5 875	5 218
Total equity		**214 682**	**171 748**
Total liabilities and equity		**4 938 859**	**3 004 631**

Notes on pages 19 to 103 are an integral part of the consolidated financial statements.

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03. 03. 2021
Signature / allkiri
KPMG, Tallinn

Consolidated statement of cash flows

(EUR thousand)	Note	2020	2019
Cash flows from operating activities			
Interest received		87 145	60 045
Interest paid		-20 733	-10 609
Fees and commissions received		31 152	24 157
Fees and commissions paid		-12 769	-11 349
Other income received		-4	171
Staff costs paid		-19 079	-16 072
Administrative and other operating expenses paid		-11 455	-11 122
Income tax paid		-4 158	-3 236
Cash flows from operating activities before change in operating assets and liabilities		**50 099**	**31 985**
Net increase/(decrease) in operating assets:			
Net increase/(decrease) in financial assets held for trading at fair value through profit or loss		-64	49
Loans and advances to customers		-531 929	-770 388
Mandatory reserve at central bank	8	-14 827	-12 146
Security deposits	13	173	690
Other assets		730	-481
Net increase/(decrease) in operating liabilities:			
Demand deposits of customers	15	1 455 310	871 616
Term deposits of customers	15	-25 248	390 754
Loans received	15	448 685	10 000
Repayments of loans received	15	-5 886	-5 886
Financial liabilities held for trading at fair value through profit or loss		212	-3
Other liabilities		-1 420	-6 300
Net cash from/(used in) operating activities		**1 375 835**	**509 890**
Cash flows from investing activities			
Purchase of tangible and intangible assets	14	-2 430	-2 071
Disposal of tangible assets		0	5
Proceeds from disposal and redemption of investment securities at fair value through other comprehensive income	9	432	0
Net changes of investment securities at fair value through profit or loss	10	-289 533	6 492
Net cash from/(used in) investing activities		**-291 531**	**4 426**
Cash flows from financing activities			
Paid in share capital	19	11 000	26 000
Proceeds from subordinated debt	18	25 000	48 500
Subordinated loans redeemed		-7 000	-8 000
Dividends paid		-4 091	-3 431
Repayment of principal of lease liabilities		-1 278	-1 003
Net cash from financing activities		**23 631**	**62 066**
Effect of exchange rate changes on cash and cash equivalents		**43**	**79**
Net increase/(decrease) in cash and cash equivalents		**1 107 978**	**576 461**
Cash and cash equivalents at the beginning of the year	8	1 244 027	667 566
Cash and cash equivalents at the end of the year	8	**2 352 005**	**1 244 027**

Notes on pages 19 to 103 are an integral part of the consolidated financial statements.

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Consolidated statement of changes in equity

(EUR thousand)	Share capital	Statutory reserve capital	Other reserves	Accumulated deficit/ retained earnings	Total	Non-controlling interest	Total equity
Balance as at 01.01.2019	**69 500**	**2 191**	**78**	**49 687**	**121 456**	**4 123**	**125 579**
Transfer to statutory reserve capital (Note 19)0		834	0	-834	0	0	**0**
Paid in share capital (Note 19)	26 000	0	0	0	26 000	0	**26 000**
Dividends paid	0	0	0	-2 230	-2 230	-1 201	**-3 431**
Share options (Note 19)	0	0	0	1 366	1 366	0	**1 366**
Profit of the year	0	0	0	19 804	19 804	2 296	**22 100**
Other comprehensive income	0	0	134	0	134	0	**134**
Total profit and other comprehensive income for 2019	0	0	134	19 804	19 938	2 296	**22 234**
Balance as at 31.12.2019	**95 500**	**3 025**	**212**	**67 793**	**166 530**	**5 218**	**171 748**
Balance as at 01.01.2020	**95 500**	**3 025**	**212**	**67 793**	**166 530**	**5 218**	**171 748**
Transfer to statutory reserve capital (Note 19)0		997	0	-997	0	0	**0**
Paid in share capital (Note 19)	11 000	0	0	0	11 000	0	**11 000**
Dividends paid	0	0	0	-2 658	-2 658	-1 432	**-4 090**
Share options (Note 19)	0	0	0	1 633	1 633	0	**1 633**
Profit of the year	0	0	0	32 514	32 514	2 089	**34 603**
Other comprehensive income	0	0	-212	0	-212	0	**-212**
Total profit and other comprehensive income for 2020	0	0	-212	32 514	32 302	2 089	**34 391**
Balance as at 31.12.2020	**106 500**	**4 022**	**0**	**98 285**	**208 807**	**5 875**	**214 682**

Additional information on equity is provided in Note 19.

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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 by European Union for the year ended 31 December 2020 for AS LHV Pank (hereinafter the Bank) 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 (Bank) provides banking, financial advisory and securities brokerage services to customers in Estonia and in UK. There are offices for client servicing in Tallinn, Tartu and also London branch was opened in 2018. LHV is a limited liability company incorporated and domiciled in Estonia. The address of its registered office is Tartu mnt. 2, Tallinn. As at 31.12.2020, the Group employed 497 people, including 26 non-active employees (31.12.2019: 420 people, 25 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 17 February 2021. The consolidated annual report will be presented for approval to the sole shareholder AS LHV Group. Rain Lõhmus, who owns 23.4% of the voting rights and Andres Viisemann, who owns 9.7% of the voting rights (see also Note 19), 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 Summary of significant accounting policies

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

Changes in accounting policies

In the third quarter, we received confirmation that the IFRS Interpretations Committee (IFRIC) decided not to accept the 20- year income tax deferral logic in Estonia, which is why all IFRScompliant companies must be recognized in the balance sheet for future dividend payments.

In accordance with paragraph 39 of IAS 12, an enterprise recognizes a deferred tax liability for all investments in subsidiaries, associates, joint ventures and branches that give rise to temporary taxable differences, unless: (a) the entity is able to control the timing of the reversal of the temporary difference; and (b) it is probable that the temporary difference will not reverse in the foreseeable future. Deferred income tax is not recognized if the investment meets both criteria (a) and (b) above. To meet criterion (a), an enterprise must have control over its investment. Control generally exists over subsidiaries and branches. In the case of associates and joint ventures, there is generally no control, so the temporary taxable differences in these investments are usually subject to income tax liability. To meet criterion (b), the company must be able to demonstrate that the temporary difference will not reverse in the foreseeable future. Cancellation refers to transactions such as the distribution of profits, the sale of a business, liquidation or the like. The near future is not explained in the standard, but the common view is that 12 months from the balance sheet date and planned transactions after that date should be taken into account. In the case of LHV Bank, this change will result in the immediate assumption of the income tax liability associated with the planned dividend from subsidiaries in the following years.

2.1 Basis of preparation

The consolidated financial statements of the Group for the financial year 2020 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. The financial statements have been prepared under the historical cost convention, except as disclosed in some of the accounting policies below, such as “financial assets and liabilities at fair value through profit or loss”, including derivatives and assets held at fair value through OCI.

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 4.

The financial year started at 1 January 2020 and ended at 31 December 2020. The financial figures have been presented in thousands of euros unless referred differently in specific disclosures.

Certain new IFRS amendments to existing standards and the interpretations of the standards have been published by the time of compiling these financial statements, which became mandatory for the Group's reporting periods beginning on or after 1 January 2020. The overview of these standards and the potential impact of applying the new standards and interpretations are stated below.

(a) Adoption of new or revised standards and interpretations

A number of new standards are effective for annual periods beginning on or after 1 January 2020, but do not have a material impact on the Group's financial statements.

(b) New accounting pronouncements

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 company'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.

Annual improvements to IFRS standards 2018-2020

(Effective for annual periods beginning on or after 1 January 2022. Early application is permitted)

These amendments are not yet endorsed by the EU.

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

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

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

IFRS 17, Insurance Contracts (effective for annual periods beginning on or after 1 January 2023; not yet adopted by the EU).

IFRS 17 replaces IFRS 4, which has given companies dispensation to carry on accounting for insurance contracts using existing practices. As a consequence, it was difficult for investors to compare the financial performance of similar insurance companies. IFRS 17 is a single principle-based standard to account for all types of insurance contracts, including reinsurance contracts that an insurer holds. The standard requires recognition and measurement of groups of insurance contracts at: (i) a risk-adjusted present value of the future cash flows (the fulfilment cash flows) that incorporates all of the available information about the fulfilment cash flows in a way that is consistent with observable market information; plus (if this value is a liability) or minus (if this value is an asset) (ii) an amount representing the unearned profit in the group of contracts (the contractual service margin). Insurers will be recognising the profit from a group of insurance contracts over the period they provide insurance coverage, and as they are released from

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risk. If a group of contracts is or becomes loss-making, an entity will be recognising the loss immediately. The Group is currently assessing the impact of the standard to it's financial statements.

There are no other new or revised standards or interpretations that are not yet effective that would be expected to have a material impact on the Group.

2.2 Consolidation

The 2020 consolidated financial statements include the financial statements of AS LHV Pank (parent company) and its subsidiary AS LHV Finance.

Subsidiaries are all entities over which the Group has control. 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. The acquisition method of accounting is used to account for the acquisition of subsidiaries (except for acquisitions among enterprises under common control) and business operations. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Transaction costs incurred for issuing equity instruments are deducted from equity; transaction costs incurred for issuing debt are deducted from its carrying amount 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 non-controlling interest that represents 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 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 non-controlling interest in the acquiree and fair value of an interest in the acquiree held immediately before the acquisition date. Any negative amount ("bargain purchase gain") is recognised in profit or loss, after management reassesses whether it identified all the assets acquired and all liabilities and contingent liabilities assumed, and reviews appropriateness of their measurement.

Intercompany transactions balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless transaction provides evidence of an impairment of the asset transferred.

Revenues and expenses of the subsidiaries acquired within the financial year are consolidated into the Group's statement of profit or loss and other comprehensive income starting from the date of acquisition to the end of the financial year. Result of operations of subsidiaries disposed of during the year are consolidated into Group's statement of profit or loss and other comprehensive income from the beginning of the financial year until the date of disposal.

Pursuant to the Accounting Act of the Republic of Estonia, information of the unconsolidated financial statements (primary statements) of the consolidating entity (parent company) shall be disclosed in the notes to the consolidated financial statements. In preparing the primary financial statements of the parent company, the same accounting policies have been used as in preparing the consolidated financial statements. The accounting policy for accounting subsidiaries has been amended in the separate primary financial statements disclosed as supplementary information in the Annual Report in conjunction with IAS 27 "Separate Financial Statements". In the parent separate primary financial statements, disclosed in these consolidated financial statements (see Note 24), the investments into the shares of subsidiaries are accounted for at cost less any impairment recognised

Non-controlling interest

Non-controlling interest is that part of the net results and of the net assets of a subsidiary, which is attributable to interests, which are not owned, directly or indirectly, by the Group. Non-controlling interest forms a separate component of the Group's equity. Non-controlling interest in the consolidated statement of financial position is disclosed separately from the equity attributable to the shareholders of the parent company. In consolidated statement of profit or loss and other comprehensive income, non-controlling interest share of profit is disclosed separately from owners of the parent.

2.3 Foreign currency translation

(a) Functional and presentation currency

The functional and presentation currency of entities in the Group is euro except the branch in UK which has pound as functional currency. As the branch had limited activities and transactions in 2020, the effect to Group financial statements is immaterial.

(b) Foreign currency transactions and balances

Foreign currency transactions are recorded based on the foreign currency exchange rates of the European Central Bank prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into euros based on the foreign currency exchange rates of the European Central Bank prevailing at the end of the reporting period. Non-monetary financial assets and liabilities measured at fair value denominated in foreign currencies are translated into euros based on the foreign currency exchange rates of the European Central Bank prevailing at the fair value measurement date. Gains and losses on translation from monetary assets and liabilities are recorded in the statement of profit or loss under the line "Foreign exchange rate gains/losses". Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss in the statement of profit or loss under the line "Net gains from financial assets measured at fair value".

2.4 Cash and cash equivalents

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

2.5 Financial assets

Initial recognition and derecognition

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

Financial assets are derecognised when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired 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 risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all 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.

Subsequent measurement

The Group classifies and subsequently measures its financial assets in the following categories: financial instruments at fair value through profit or loss; fair value through other comprehensive income and amortised cost. The classification will depend on if the financial asset is a debt instrument, an equity instrument or a derivative.

Debt instruments (Loans and debt securities)

The classification is based on a combination of assessing the business model for managing the financial assets and whether the contractual cash flows consist of solely payments of principal and interest ('SPPI'). The business model assessment is performed for homogenous portfolios/products identified based on how the business is managed in the divisions of the Group. The assessment is based on reasonable scenarios taking into consideration how the portfolio is evaluated and reported to management; the risks affecting the performance of the portfolio and how these risks are managed; how managers are compensated; and the frequency, value and timing of sales including the reasons for the sales. In determining if the cash flows consist solely of principal and interest, the principal is defined as the fair value of the debt instrument at initial recognition, which can change over the life if there are repayments or capitalisation of interest. Interest cash flows are consistent with components per a basic lending arrangement including consideration for time value of money, credit risk, liquidity risk as well as administrative costs and profit margin. If there are contractual features introducing an exposure to other risks or volatility, it is not considered to consist of solely payments of principal and interest. SPPI tests are performed as a part of new product approval tests. In implementation of IFRS 9 in 2018 SPPI was applied to 22 larger products carried at amortised cost.

Debt instruments are presented in the statement of financial position line items: Due from central banks, credit institutions and investment companies; Loans and advances

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to customers; Financial assets at fair value through other comprehensive income; Financial assets at fair value through profit or loss; Receivables from customers and Other financial assets, and include instruments in the following measurement categories.

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

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

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

Equity instruments

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

Derivatives

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

Modification

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

Reclassification

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

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 dercognition event.

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

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

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

IFRS 9 category		Class (applied by the Group)		31.12.2020	31.12.2019
Financial assets	Amortised cost	Due from banks and investment companies		2 393 258	1 270 453
		Loans and advances to customers	Loans to legal entities	1 352 700	950 541
			Loans to individuals	856 123	736 493
		Receivables from customers		2 454	2 745
		Other financial assets		2 073	2 246
	Financial assets at fair value through profit and loss	Mandatory measurement at fair value through profit or loss	Shares and fund units	142	164
			Listed bonds	322 699	32 331
			Derivatives	89	4
	Equity instruments at fair value through other comprehen-sive income	Investment securities	Unlisted shares	0	432

2.6 Impairment of financial assets carried at amortised cost

Measurement

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

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

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

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

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

Significant increase in credit risk

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

Definition of default

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

Quantitative criteria

The borrower is more than 90 days and over 10 euros past

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due on its contractual payments. The threshold of 10 euros is put in place with debt management procedures that is a trigger for debt collection activities and also indicated as materiality threshold in Definition of Default.

Qualitative criteria

The borrower meets unlikeliness to pay criteria, which indicates the borrower is in significant financial difficulty. The following circumstances are considered as indicators for the customer not to pay the debt in full:

- Non-accrued status is applied to the contract
- Specific credit adjustments has been formed due to the decline in the credit quality
- Sale of credit obligation with economic loss higher than 5 %
- Distressed restructuring measures have been applied to the contract resulting with diminished financial obligation higher than 1 %
- It is becoming probable that the borrower will enter bankruptcy or has filed for bankruptcy
- a customer's resources of cash flow are no longer available to meet the payments of instalments
- The Group has called any collateral including a guarantee.

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. Financial instruments in default are in Stage 3. All financial assets in Stage 3 are considered credit-impaired.

Modelling

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

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

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

Forward-looking information

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

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

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

Individual assesments and Management´s judgement

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

2.7 Tangible fixed assets

Tangible fixed assets are non-current assets used in the operating activities of the Group with a useful life of over one year. An item of tangible fixed assets is initially recognised at its cost which consists of the purchase price (incl. customs duties and other non-refundable taxes) and other expenditures directly related to the acquisition that are necessary for bringing the asset to its operating condition and location. Subsequent costs are included in the asset's carrying amount or are 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 repairs and maintenance are charged to operating expenses during the reporting period in which they are incurred.

An item of tangible fixed assets 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%, for improvements of rental space either 20% p.a. or amortization throughout the rental period, depending on which is shorter. Depreciation is calculated starting from the month of acquisition until the carrying amount reaches the residual value of the asset. In case the residual value is greater than the carrying amount of the asset, no further depreciation expense is calculated.

The appropriateness of the assets´ residual values, depreciation methods used and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. The Group performs an impairment test when there are circumstances indicating impairment. Where an asset's carrying amount is greater than its estimated recoverable amount (higher of an asset's fair value less costs to sell or its value in use), it is written down immediately to its recoverable amount recognising an impairment loss in the statement of profit or loss for the reporting period.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in operating expenses or other income in the statement of profit or loss for the reporting period.

2.8 Intangible assets

Intangible assets are identifiable, non-monetary assets without physical substance and currently comprise of acquired software licences. 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, except client agreements (see below). The annual amortisation rate for purchased licenses is 33%.

Sales costs for the acquisition of new clients are capitalised. The amortisation method for client agreements is the diminishing balance method. The annual amortisation rate for purchased client agreements is 12% of the residual value of those assets. At the end of each reporting period, the appropriateness of amortization rates, methods and residual values is assessed. The Group reviews intangible assets for impairment losses 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.

2.9 Impairment of assets

Assets that have indefinite useful lives (including goodwill) are not subject to amortization but 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 is compared with the carrying amount.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount of the asset is the higher of an asset's fair value less costs to sell and value in use. For the purpose of 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 statement of profit or loss.

At the end of each following end of the 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 the statement of profit or loss as a reduction of the impairment loss.

2.10 Loan commitments, Financial guarantees and performance guarantees

The Group issues commitments to provide loans. These commitments are irrevocable or revocable only in response to 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 in the event that a customer cannot meet its obligations 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 loss 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.

2.11 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

Recognition of a financial liability (derivative) at fair value through profit or loss is disclosed under accounting policy 2.6. 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 the statement of profit or loss during the term of the instrument, using the effective interest rate. Interest costs are included in the statement of profit or loss line "Interest expenses".

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 in the statement of financial position line "Deposits from customers and loans received", accrued interest liabilities are included in the same line. Interest expense is recognised in the statement of profit or loss line "Interest expense" on the accrual basis.

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

LHV entered into two new type of funding transaction in 2020:

- covered bonds;
- TLTRO III

Both of these instruments are accounting as other loans received using effective interest rates. Covered bonds are secured by mortgage book and issues are rated by Moodys and listed in Dublin stock exchange. TLTRO III is secured by mortgage bonds and loans given to local municipalities.

TLTRO III has conditional interest rate, where interest rate depends based on the fulfilment of conditions. LHV has taken conservative approach and calculates the effective interest without taking positive potential uplift of interest into account. In case the conditions will be fulfilled, then LHV will recalculate interest income and book difference into running period without restating the previous accounting periods.

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

2.12 Payables to employees

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

Social security tax includes payments to the state pension fund. The Group has neither existing legal nor constructive obligations to make pension or similar payments supplementary to social security tax.

2.13 Share-based payments

LHV Pank owner AS LHV Group operates a share-based compensation plan, under which the company receives services from group employees as consideration for 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 group's staff expense and as an increase in the 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:

- including any market performance conditions influencing the share price (e.g. LHV Group share price);
- excluding the impact of any service and non-market performance vesting conditions (for example, profitability, sales growth targets and remaining an employee of the entity over a specified time period).

At the end of each reporting period, the bank 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 the statement of profit or loss, with a corresponding adjustment to equity.

The grant by LHV Group of options over its equity instruments to the employees of subsidiary undertakings in the group 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 to investment in subsidiary undertakings, with a corresponding credit to equity in the parent entity accounts. According to the contractual conditions of the share options, there are no social security tax charges when exercising the options after the 3-year period.

2.14 Provisions and contingent liabilities

Liabilities arising from an obligating event before the end of the reporting period that have either a legal basis or that have arisen from the Group's current operating practice (legal or constructive obligation) that require probable outflow of resources, the realisation of which is probable (it is more likely than not that an outflow of resources will be required to settle the obligation) and the amount of which can reliably be estimated but for which the timing or amount are not definitely known are recognised as provisions in the statement of financial position. The provisions are recognised based on the management's estimates regarding the amount and timing of the expected outflows. A provision is recognised in the statement of financial position in the amount which according to the management is necessary as at the end of the reporting period for the meeting of the obligation arising from the provision or transfer to the third party. The provision expense and an expense from the change in the carrying amount of provisions are included within expenses in the reporting period. Provisions are not set up to cover future operating losses.

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

Other contingent liabilities (guarantees, except financial guarantees, and other commitments) the realisation of which is less probable than non-realisation or related costs cannot be determined reliably, that in certain circumstances may become obligations, 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 portfolio of items previously dealt with 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).

2.15 Distinction between short- and long-term assets and liabilities

Assets from which resources are expected to flow to the Group within 12 months are recognised as current assets. The portion of assets with expected inflows later than 12 months after the end of the reporting period is recognised as non-current assets (see Note 3.4).

Liabilities are classified as current when they are due within twelve months after the end of the reporting period or if the Group does not have an unconditional right to defer the payment for later than 12 months after the end of the reporting period. Loans received with due date within 12 months after the end of the reporting period which are refinanced as non-current after the end of the reporting period but before the financial statements are authorised for issue, are recognised as current. Loans received that the lender has the right to recall at the end of the reporting period due to breaches of contractual terms are also classified as current.

For all long-term assets and liabilities, the long-term portion is separately disclosed in respective disclosure to these financial statements (see Note 3.4).

2.16 Revenues and expenses

The effective interest method is applied to recognise interest income and interest expenses in profit or loss for financial assets and financial liabilities measured at amortised cost or debt investments at fair value through other comprehensive income.

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

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

Fee and commission income

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

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

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

Fee and commission income is recognised over time on a straight line basis as the services are 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 major types of fees are described below.

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

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

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

Net financial income

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

Dividend income

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

2.17 Asset management services

The Group is engaged in providing asset management services (Note 20). Such assets have been given to the Group to be managed by third parties and these assets are recorded off-balance sheet. Service fees are derived from management of such assets and no associated credit and market risks arise for the Group.

2.18 Leases - Group as the lessee

Since 1 January 2019 the IFRS 16 Leases are recognised in the Group's financial reporting.

Lessees are required to recognise:

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

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

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

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

Lease liabilities were recognised as present value of lease payments. The right-of use assets were measured at the amount equal to the lease liability, as no adjustments to right of use assets were necessary. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease period to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use asset is depreciated over the shorter of the asset's useful life or the lease term on a straight-line basis.

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

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

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

Short-term leases are leases with a lease term of 12 months or less. Low value assets comprise IT-equipment and small items of office furniture. In determining the lease term, management considers all facts and circumstances that create an economic incentive to exercise an extension option or not to exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended (or not terminated). The management reviews the assessment if a significant event or a significant change in circumstances occurs which affects the probability of using options and that is within the control of the management. Alternatively, the extension period of the contract has changed (for example, Group has exercised an option, which initially was considered reasonably uncertain or has not exercised an option, which was initially considered reasonably certain).

According to the contracts, Group has not granted any residual value guarantees in the end of the contract.

The Group has used the following practical expedients permitted by the standard:

- the accounting for operating leases with a remaining lease term of less than 12 months as at reporting date as short-term leases.

- lease agreements for low value assets are excluded.
- the exclusion of initial direct costs for the measurement of the right-of-use asset at the date of initial application.

2.19 Taxation and deferred income tax

Corporate income tax in Estonia

Estonian companies generally do not pay corporate income tax on profits on a current basis. Tax is paid on distributions of profit, either formal (dividends, other payments from equity) or deemed (non-business expenses, transfer pricing adjustments, certain payments to tax havens, etc.). Dividends and other profit distributions are subject to corporate income tax at the rate of 20/80 on the net amount. Starting from 2019, regular dividend payments will be subject to corporate income tax at the reduced rate of 14/86 to the extent of the average dividend distribution of three preceding years. The first year to be taken into account is 2018. Corporate income tax arising from dividend distributions is recorded as a liability and income tax expense when the dividends are declared. The tax becomes due to the tax authorities on the 10th day of the month following the dividend payment.

Starting from second quarter of 2018 credit institutions are obliged to pay advance income tax of 14% on quarterly profits under IFRS (Note 24). The tax becomes due to the tax authorities on the 10th day of the third month following the quarter. Advance income tax paid is non-refundable and thus recorded as expense, but can be used to reduce income tax payable on future dividend distributions.

Corporate income tax in other countries

In accordance with the local income tax laws, the net profit of companies located in United Kingdom that has been adjusted for the permanent and temporary differences as stipulated by law is subject to corporate income tax.

Corporate income tax rates	2020	2019
United Kingdom	19%	19%

Deferred income tax is calculated on all significant temporary differences between the tax bases of assets and liabilities and their carrying values in the consolidated statement of financial position. The main temporary differences arise from depreciation and tax loss carry-forwards. Deferred tax balances are measured at tax rates enacted or substantively enacted at the end of the reporting period which are expected to apply to the period when the temporary differences will reverse or the tax loss carry-forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry-forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

A deferred income tax liability in respect of the Group's available equity which would accompany the payment of available equity as dividends, is not reported in the statement of financial position. The maximum amount of income tax payable, which would arise from paying out the retained earnings as dividends, is disclosed in the Note 19 to the financial statements.

2.20 Offsetting

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously. More detailed information in Note 3.8.

2.21 Statutory reserve capital

Statutory reserve capital is formed from annual net profit allocations to comply with the requirements of the Commercial Code. During each financial year, at least one-twentieth of the net profit shall be transferred to the statutory reserve, until the reserve reaches one-tenth of share capital. Statutory reserve may be used to cover a loss, or to increase share capital. Payments to shareholders from statutory reserve are not allowed.

NOTE 3 Risk management

Risk is defined as a potential negative deviation from expected financial results. The Group encounters several risks in its day-to-day operations. The objective of risk management at the Group 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 the Group by minimising losses and reducing the volatility of results. Risk management at the Group is based on a strong risk culture and is built on the principle of three lines of defence where the first line of defence, the business units, are responsible for taking risk and for day-to-day management. The second line of defence, the risk management division, is responsible for the development of risk management methodologies and for the reporting of risks. The third line of defence, the internal audit, conducts independent supervision over the entire group. Risk management principles, requirements and areas of responsibility are described in risk management policy. The principles and objectives of capital management processes are described in the policies of the respective field.

3.1. Capital management

The goal of the Group's capital management is to:

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

The Group considers net own funds valid according to capital adequacy regulation as capital. The amount of capital that the Group managed as at 31.12.2020 was EUR 276 117 thousand (31.12.2019: EUR 229 001 thousand). The goals of the Group's capital management are set based on both the regulative requirements and additional internal buffer.

The Group follows the general principles in its capital management:

- The Group must be adequately capitalized at all times, having necessary capital to ensure economic preservation and enabling financing of new profitable growth opportunities;
- The main focus of the capital management is on tier 1 own funds, because only tier 1 own funds can absorb losses. All other capital layers in use are dependent of tier 1 own funds volume;
- Capital of the Group can be divided into: 1) regulated minimum capital and 2) capital buffer held by the Group. In order to reach its long-term economic goals the Group must on one hand strive towards proportional lowering of the regulated minimum capital (through minimizing risks and high transparency). On the other hand, the Group must strive towards sufficient and conservative capital reserve, which will ensure economic preservation even in the event of severe negative risk scenario;
- The risk appetite set by the Group is an important input to capital management planning and capital goal setting. Higher risk appetite requires maintaining higher capital buffer.

Own funds

(in thousands of euros)	31.12.2020	31.12.2019
Paid-in share capital	106 500	95 500
Statutory reserves transferred from net profit	4 022	3 237
Accumulated profit/(deficit)	62 972	45 619
Intangible assets (subtracted)	-807	-685
Net profit for accounting period (COREP)	17 441	14 863
Deductions	-2 511	-33
Tier 1 own funds	**187 617**	**158 501**
Additional Tier 1 capital	38 000	23 000
Total Tier 1 capital	**225 617**	**181 501**
Subordinated debt	50 500	47 500
Total Tier 2 own funds	**50 500**	**47 500**
Total net own funds	**276 117**	**229 001**

The net capital of a credit institution at any time shall be equal to or exceed the minimum amount of share capital prescribed in the Credit Institutions Act (EUR 5 million). Started from 2014, the capital of banks and investment firms in the European Union became subject to a legal framework (CRD IV/CRR), largely based on the Basel III framework that was 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 an 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 capital requirements directive also define measures for macro-financial supervision that member states can use to control the behaviour of credit institutions in amplifying the cycles and to alleviate risks arising from market structure. Every year additional smaller changes have been implemented in the regulations and completely updated regulation will be valid started from 2022.

The regulation, which is directly applicable in the member states, obligates all credit institutions operating in the European Union (including their consolidating holding companies) and investment firms to maintain 4.5% of Common Equity Tier 1 (CET 1) and 6.0% of Tier 1 Capital against risk assets. The overall Capital Adequacy Requirement (CAD), including both Tier 1 and Tier 2 capital, remains at the existing 8.0% level.

In addition to the main requirements based on uniform rules, the directive defines the principles for forming capital buffers. In Estonia, in addition to the baseline capital requirements, credit institutions have been subjected to capital maintenance and systemic risk buffers, which are 2.5% (imposed by the Financial Supervisory Authority), 1.0% (imposed by Bank of Estonia) and systematically importance buffer (imposed by Financial Supervisory Authority), respectively. In 2018 the grouping of capital requirements changed and SREP buffers were moved to higher capital buffers, meaning that first bank will breach other buffers before SREP buffers. Breaching each buffer triggers different actions from regulators side and first one in list is set by Estonian Central Bank triggering limitation of ECB transactions.

The latter is also subject to the specific supplementary Pillar 2 requirement applicable to credit institutions. An overview of capital requirements as of 31.12.2020 is provided in the table below:

Capital requirements	CET1	Tier 1	CAD
Base capital requirement	4.50%	6.00%	8.00%
Capital conservation buffer	2.50%	2.50%	2.50%
Systemic risk buffer	1.00%	1.00%	1.00%
Capital requirements total	**8.00%**	**9.50%**	**11.50%**

Capital requirements valid until October 2018 are provided in the table below:

Capital requirements	CET1	Tier 1	CAD
Base capital requirement	4.50%	6.00%	8.00%
Capital conservation buffer	2.50%	2.50%	2.50%
Systemic risk buffer	0.92%	0.92%	0.92%
Capital requirements total	**7.92%**	**9.42%**	**11.42%**

Capitalization levels have been increased not due to riskiness of the bank, but because of the increasing market share of the bank. In 2018 LHV was considered as one of four systematically important bank in Estonia. LHV has been keeping conservative approach in capital management and keeps additional internal buffers compared to regulatory ones.

LHV has received the new SREP report only in December 2020, which was due to COVID-19 not changing any of the quantitative requirement.

Each year, the Bank's supervisory board confirms the goals of capitalization and the target level of capital adequacy to cover potential risks arising from fast growth. Each year, an internal capital adequacy assessment process (ICAAP) is performed, the goal of which is to identify potential internal capital needs in addition to regulatory capital requirements.

MREL requirement will change from end of Q2 2021 to the level of 10.15%, as LHV is treated as systematic bank and bank has to keep sizable amount of suitable liabilities which could be converted to own funds in case of resolution process. Same time MREL calculation formula changes and is going to be aligned with EBA definitions and the MREL requirements will be recalibrated.

Capital adequacy and the use of regulatory capital are monitored by the Finance Department. Reports about the compliance with prudential and capital requirements for covering the risks are submitted regularly to supervision authorities. Those reports about the Bank as the Group's parent company are presented separately. LHV uses standard method for calculating capital requirements for credit and market risk and basic indicator approach calculating operational risk capital requirement. The Bank has complied with all capital requirements during the financial year and in previous year.

3.2 Credit risk

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

Credit risk is one of the largest risk for the Group's business; management therefore carefully manages its exposure to credit risk. In order to evaluate credit risk, Group analyses the operations and financial position of its customers and business partners. After approving the credit, the solvency of the customer and the value of the collateral are regularly monitored. The credit risk management and control are centralised in a credit risk management unit which reports regularly to the Management Board and Supervisory Board.

The coronavirus outbreak, which started 2020, has significant impact both on LHV and its clients. A swift and coordinated response from monetary, fiscal and regulatory authorities has substantially smoothed the potential impact for the whole economy. The measures include, in many instances, some forms of moratorium on payments of credit obligations, with the aim of supporting the short-term operational and liquidity challenges faced by borrowers.

On the onslaught of the Covid 19 crises, LHV quickly offered to its clients moratoria on payments which took away the immediate pressure from the clients and offered them to pile up the necessary reserves. Furthermore, the conditions to use state guarantees (Kredex) to secure client loans were eased which helped smooth offering of loans.

From credit risk measurement side, LHV continued using conservative approach in credit risk measurement. LHV decided not to use any of the temporary measures allowing not changing client risk treatment due to Covid-19. This decision was based on the fact that LHV Group shares are listed and it would have made more difficult for investors to understand the actual financial results.

3.2.1 Distribution of credit risks

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

a) due from central bank and credit institutions (referred to as “banks” in the tables) and investment companies
b) debt securities and derivatives
c) loans to legal entitites, including
   - 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)

d) loans to individuals, including
   - mortgage loans (private lending)
   - private loans (private lending)
   - consumer loans (consumer financing)
   - hire-purchase (consumer financing)
   - leveraged loans (investment financing)
   - leasing
   - credit card loans (consumer financing)
   - overdraft (private lending)
   - study loan (private lending)
   - real estate leasing (private lending)

Maximum exposure to credit risk

(in thousands of euros)	31.12.2020	31.12.2019
Due from banks and investment companies (Note 8)	2 393 258	1 270 453
Financial assets at fair value (debt securities) (Note 10)	322 930	32 499
Loans and advances to customers (Note 11)	2 208 823	1 687 034
Receivables from customers (Note 12)	2 454	2 745
Other financial assets (Note 13)	2 073	2 246
Total financial assets	**4 929 538**	**2 995 409**
Exposures related to off-balance sheet items (Note 21), excluding performance guarantees	450 318	373 379
Total maximum exposure to credit risk	**5 379 856**	**3 368 788**

3.2.2 Credit risk measurement

For all loan products, except leverage loans, LHV uses either rating or scoring systems to assess customer credit risk, as outlined in the table below. In retail, for credit decisions, application PD models are used, while portfolio scoring PD models are developed for existing contracts. There are also separate models to cover the dimensions of Loss Given Default (LGD) and Credit Conversion Factor (CCF).

Portfolio	Segment	Definition	PD	LGD	CCF/EAD
Corporate	Corporate exposures	Loans to companies with total exposure to LHV > EUR 500 000	Rating models	Model	Model
Retail	SME, incl. micro enterprises	Loans to companies with total exposure to LHV < = EUR 500 000	Scoring models		
	Private mortgage	All mortgage loans to private individuals	Scoring models		
	Private consumer	All consumer financing products and car leasing to private individuals	Scoring models		

(a) Due from banks and investment companies

Management estimates that the credit risk exposure from cash and cash equivalents, held at the central bank, other correspondent banks and investment institutions has inherently low credit risk. Loans and advances to central bank, credit institutions and investments companies are not overdue, and are also unsecured. The funds of the Group according to ratings given by Standard & Poor's or equivalent (central bank without a rating). In case there are ratings available from more than one rating agency, the average, or the most conservative rating is used. The positions are held as follows:

Rating

(in thousands of euros)	Credit institutions	Investment companies	Total 31.12.2020	Credit institutions	Investment companies	Total 31.12.2019
Central bank (The Bank of Estonia, The Bank of England)	2 213 211	0	2 213 211	1 232 733	0	1 232 733
AA- to AA+	118	0	118	312	0	312
A- to A+	24 004	0	24 004	7 293	0	7 293
BBB to BBB+	355	9 899	10 254	4 091	4 917	9 008
B to B+	0	86	86	0	556	556
Non-rated	145 585	0	145 585	20 551	0	20 551
Total (Note 8)	**2 383 273**	**9 985**	**2 393 258**	**1 264 980**	**5 473**	**1 270 453**

Non-rated credit institutions are banks or financial institutions without external credit rating, however management considers their credit quality to be good based on available market information. If credit institutions do not have the external rating and they are subsidiaries of large EU banks, then the rating of the parent company is used. Management has assessed that the ECL from credit institutions and investment companies exposures is immaterial due to the strong ratings of corresponding parties, their financial position and also due to the positive economic outlook in short-term perspective, as the Group holds only very liquid positions with the counterparties. See also note 3.2.4.1 for additional information.

(b) Debt securities and derivatives

The Credit Committee sets limits for taking credit risk associated with debt securities considering the issuer's rating. The Risk Capital Committee or authorised employees make decisions regarding investments within the limits set.

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

The Group´s derivatives, debt securities at fair value through profit or loss (FVTPL) or fair value through other comprehensive income (FVOCI) according to ratings given by Standard & Poor's or equivalent:

Ratings distribution
(in thousands of euros)

	Mandatory FVTPL				
	Investment portfolio	Liquidity portfolio	Trading portfolio	Foreign exchange forwards	Total 31.12.2020
AAA	0	310 675	0	0	310 675
A- to A+	8 281	1 815	0	0	10 096
Non-rated	0	1 928	0	89	2 017
Total (Note 9, 10)	**8 281**	**314 418**	**0**	**89**	**322 788**

Ratings distribution
(in thousands of euros)

	Mandatory FVTPL				
	Investment portfolio	Liquidity portfolio	Trading portfolio	Foreign exchange forwards	Total 31.12.2019
AAA	11 627	0	0	0	11 627
A- to A+	2 890	17 814	0	0	20 704
Non-rated	0	0	0	4	4
Total (Note 9, 10)	**14 517**	**17 814**	**0**	**4**	**32 335**

Debt securities classified as FVTPL is based on the management assessment of the instrument's business model and how management monitor these investments.

(c) Other receivables

Credit quality of other receivables
(in thousands of euros)

	31.12.2020	31.12.2019
Receivables (not overdue)	2 246	2 634
Receivables (overdue)	208	111
incl. receivables from individuals	196	101
incl. receivables from legal entities	12	10
Total (Note 12)	**2 454**	**2 745**

As at 11 February 2021, other receivables of EUR 205 thousand euros are uncollected and in previous years, the Group has not written off any receivables. Other financial assets (see Note 13) in amount EUR 2 073 thousand (31.12.2019: EUR 2 246 thousand) are guarantee deposits on the Baltic stock exchanges held to guarantee securities trading activity on the stock exchanges of Tallinn, Riga and Vilnius and the deposits of VISA and MasterCard to guarantee credit card transactions. The Group considers the counterparties credit risk as very low.

(d) Loans to legal entities

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

Credits below EUR 500 thousand to legal entities and loans to apartment association irrespective of loan amount are analysed with a more cost-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 loan. Financial data and information on payment behaviour of the company is used when calculating the probability of default (PD). The structure of assets and liabilities are taken into account, also the profitability and cash flow ratios.

(e) Loans to private individuals

Credits to private individuals are also analysed with a cost-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. Credit decisions are made by the Retail Banking Credit Committee or by lower decision level. The maximum loan amount of mortgage loans is in line with the regulations set by Central Bank of Estonia. Consumer financing products to private individuals are offered through its subsidiary LHV Finance in Estonia. The Group has entered into agreements where most overdue consumer loans and hire purchase agreements are sold – usually when loans reaching overdue at least of 79 days.

Risk concentration

Several tolerance limits that are regularly monitored and reported have been introduced in LHV Pank's Credit Policy to control and hedge concentration risk. These limits are set for overall credit portfolio and separately for the largest – corporate credit portfolio. The most significant metrics and limits measured at the last day of each quarter are as follows:

a) The share of small financing in the LHV Pank's total credit portfolio

b) The share of financing non-domicile customers in the LHV Pank's total credit portfolio

c) The share of shadow banking financing compared to net owned funds

d) The share of ten largest credit customers compared to net owned funds

e) The share of financing the higher risk rating classes compared to the total corporate credit portfolio

f) The share of financing the catering and construction sector compared to the total corporate credit portfolio

g) Th share of financing outside of Estonia (incl. financing in EU countries and UK).

Distribution of assets and liabilities by geographic region is presented below.

As at 31.12.2020, the loans issued to 5 customers (2019: total 12) had a large risk exposure, i.e. more than 10% of the net own funds (NOF) of Group either individually or via group risk, totalling 83% of NOF (2019: 190%).

As of 31.12.2020 the LHV Pank had invested in short term bonds issued by the Government of Estonia in the amount of EUR 310.7 million which were equal to 113% of NOF (as of 31.12.2019: no position exceeded 10% of NOF).

Of customer deposits, the deposits of 8 (2019: 4) customers have a high risk concentration, which amounts to 423% (2019: 213%) of NOF. There are 5 clients holding more than 1% of all deposits (2019: 4). Their total deposits amount was EUR 1 069 million (2019: 487). Share of Top 20 depositors was 34.3% as of 31.12.2020 compared to more than 25.3% as end of 2019.

31.12.2020
(in thousands of euros)

	Estonia	Germany	Other EU	USA	UK	Other	Total
Due from banks and investment companies	2 175 007	0	84 264	17 566	116 222	199	**2 393 258**
Financial assets at fair value	312 703	2	10 219	5	0	1	**322 930**
Loans and advances to customers	2 180 999	823	14 577	360	7 954	4 110	**2 208 823**
Receivables from customers	2 454	0	0	0	0	0	**2 454**
Other financial assets	122	0	0	1 951	0	0	**2 073**
Total financial assets	**4 671 285**	**825**	**109 060**	**19 882**	**124 176**	**4 310**	4 929 538
Deposits of customers and loans received	3 268 551	216 261	705 206	1 633	375 657	42 707	**4 610 015**
Subordinated debt	88 500	0	0	0	0	0	**88 500**
Financial liabilities at fair value	221	0	0	0	0	0	**221**
Accounts payable and other financial liabilities	21 398	0	0	0	0	0	**21 398**
Total financial liabilities	**3 378 670**	**216 261**	**705 206**	**1 633**	**375 657**	**42 707**	4 720 134

31.12.2019
(in thousands of euros)

	Estonia	Germany	Other EU	USA	UK	Other	Total
Due from banks and investment companies	1 228 469	0	10 972	4 929	23 041	3 042	**1 270 453**
Financial assets at fair value	453	9 840	22 618	4	0	16	**32 931**
Loans and advances to customers	1 656 373	840	26 257	379	0	3 185	**1 687 034**
Receivables from customers	2 745	0	0	0	0	0	**2 745**
Other financial assets	110	0	0	2 136	0	0	**2 246**
Total financial assets	**2 888 150**	**10 680**	**59 847**	**7 448**	**23 041**	**6 243**	2 995 409
Deposits of customers and loans received	1 882 514	372 390	428 102	1 241	0	54 354	**2 738 601**
Subordinated debt	70 500	0	0	0	0	0	**70 500**
Financial liabilities at fair value	8	0	0	0	0	0	**8**
Accounts payable and other financial liabilities	20 563	0	44	3	3	0	**20 613**
Total financial liabilities	**1 973 585**	**372 390**	**428 146**	**1 244**	**3**	**54 354**	2 829 722

Distribution of loans granted by industry (gross):

(in thousands of euros)	31.12.2020	%	31.12.2019	%
Individuals	858 141	38.6%	738 152	43.6%
Real estate	498 927	22.4%	353 405	20.9%
Manufacturing	152 968	6.9%	114 104	6.7%
Art and entertainment	59 184	2.7%	42 638	2.5%
Financial services	69 694	3.1%	71 690	4.2%
Wholesale and retail	88 642	4.0%	80 767	4.8%
Administrative activities	74 466	3.3%	67 064	4.0%
Transport and logistics	27 534	1.2%	15 337	0.9%
Agriculture	72 398	3.3%	59 657	3.5%
Other servicing activities	8 012	0.4%	7 290	0.4%
Construction	45 314	2.0%	38 951	2.3%
Information and communication	12 705	0.6%	7 017	0.4%
Professional, scientific and technical activities	41 678	1.9%	47 368	2.8%
Education	16 403	0.7%	1 976	0.1%
Local municipales	120 805	5.4%	112	0.0%
Other areas at activities	78 808	3.5%	47 610	2.8%
Total (Note 11)	**2 225 681**	**100.0%**	**1 693 138**	**100%**

Loans and advances (incl. loan commitments and guarantees)

The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Group measures credit risk using Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD). This is similar to the approach used for the purposes of measuring Expected Credit Loss (ECL) under IFRS 9. Refer to note 3.3.2 for more details.

Credit risk grading

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

1) obligor risk characteristics -

a. for corporate exposures: financial statements, industry type, support from parent company and etc.;

b. for retail exposures: financial statements or personal income information, socio-demographic information, behavioural information and etc.

2) transactional risk characteristics - type of product, type of collateral and etc.

3) delinquency characteristics from internal and external sources.

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

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

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

Retail

After the date of initial recognition, for retail business, the payment behaviour of the borrower is monitored on a periodic basis to develop a behavioural score. Any other known information about the borrower which impacts their creditworthiness – such as unemployment and previous delinquency history – is also incorporated into the behavioural score. This score is mapped to a PD.

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 also update information about the creditworthiness of the borrower at least every year from sources such as public financial statements. This will determine the updated internal credit rating and PD.

Treasury

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

Credit Risk

The Group's rating method used for evaluating the PD of corporate loans consists of a total of 13 credit ratings where 1 stands for the lowest and 13 for the highest credit risk (default). Ratings 1 and 2 are attributed only based on average ratings of rating agencies Fitch, Moody's and Standard & Poor's, and are subject to the Group's financial analysis as necessary.

Thus, 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. Also rating classes 3 -13 are partly based on the evaluation of rating agencies, although this category includes mainly Estonian enterprises that do not have an international rating.

The group's 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 an annual validation and recalibration so that they reflect the latest projections in the light of all actually observed defaults.

All retail loans have a behavioural score. This score is mapped to a PD. Retail loans are divided into three groups: investment grade, special monitoring and default. Investment grade is allocated when the loan is not overdue as at balance sheet date. Special monitoring status is allocated when the loan has overdue status more than 31 days or default status is based on the definition of default principle.

3.2.3 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 in 'Stage 1' and has its credit risk 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 Risk management section point 3.2.3.1 for a description of how the Group determines when a significant increase in credit risk has occurred.

If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. Please refer to Risk management section point 3.2.3.2 for a description of how the Group defines credit-impaired and default.

Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis. Please refer to Risk management section point 3.2.3.3 for a description of inputs, assumptions and estimation techniques used in measuring the ECL.

A pervasive concept in measuring ECL in accordance with IFRS 9 is that it should consider forward-looking information. Risk management section point 3.2.3.4 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.

3.2.3.1 Significant increase in credit risk

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

Quantitative criteria

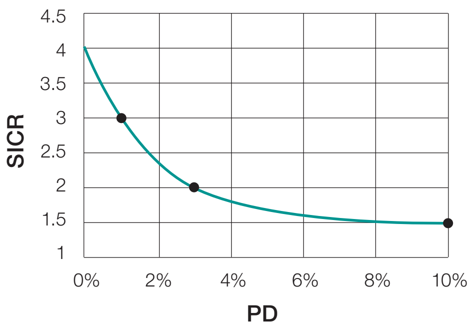
Quantitative criteria is applied to all credit contracts initiated since 2018 in the current portfolio and Wholesale legacy portfolio, for which a rating based Lifetime PD is used.

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

Current portfolio – contracts initiated from 1st January 2018

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

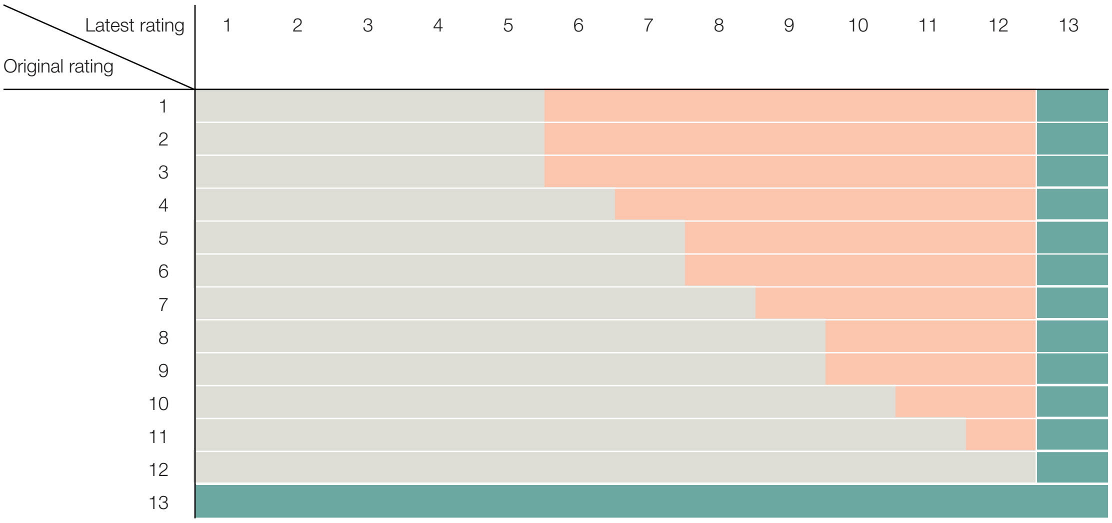
To illustrate the formula, see SICR curve graphic below. In addition to the curve, the PD increase has to be at least 100 bps.



SICR curve: 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 significant increase in credit risk has occurred.

Legacy portfolio – corporate contracts initiated before 1st January 2018.



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 Lifetime PD, which is not considered indicative of a significant increase in credit risk. The average maturity of the corporate portfolio is short, namely 2.5 years.

Qualitative criteria

Qualitative criteria is applied in SICR calculation to legacy retail portfolio that was initiated before 2018. For the current portfolio, the qualitative criteria is included in the PD calculation and therefore included in the SICR calculation through Lifetime PD.

Due to the average short maturity of the legacy portfolio (1.75 years) it was not practical to go back to history to predict initial PDs for the contracts initiated before the of 1st December, 2017 and therefore the application PD or rating PD were used as initial PDs for legacy portfolio.

Retail legacy portfolio – private person contracts initiated before 1st January 2018

If the borrower meets one or more of the following conditions, then there is significant increase in credit risk:

- At the report date the contract is over 30 days past due with more than 10 euros
- The contract has been overdue over 30 days and in the amount of more than 10 euros more than once over the last 12 months or
- The customer has had more than one payment alert or tax debt over the last 12 months
- In case of home or private loan the contract LTV >100% is also considered.

Retail legacy portfolio – business contracts initiated before 1st January 2018.

If the borrower meets one or more of the following conditions, then there is significant increase in credit risk:

- At the report date the contract is over 30 days past due with more than 10 euros
- The contract has been overdue over 30 days and in the amount of more than 10 euros more than once over the last 12 months or
- The customer has had more than one payment alert or has had at least four incidents of tax debt in the amount of over 640 euros over the last 12 months.

The assessment of SICR incorporates forward-looking information (see Risk management section point 3.2.3.4. for further information) and is performed on a quarterly basis. The criteria used to identify SICR are monitored and reviewed periodically for appropriateness by the independent member of Credit Risk team.

Backstop

A backstop is applied and the financial instrument considered to have experienced a significant increase in credit risk if the borrower is more than 30 days past due on its contractual payments.

The Group has used the low credit risk exemption for cash and nostro accounts fulfilling the liquidity portfolio criteria in the year ended 31 December 2020 and 31 December 2019.

The following tables show the impact on the 31 December 2020 and 31 December 2019 ECL allowance of changing the PD thresholds for SICR. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognised.

Loan portfolio 2020

(in thousands of euros)	Effect on impairment
+10% Change in SICR	155
-10% Change in SICR	127
SICR with 0.5% treshold	0
SICR with 1.5% treshold	-1

Loan portfolio 2019

(in thousands of euros)	Effect on impairment
+10% Change in SICR	-20
-10% Change in SICR	15
SICR with 0.5% treshold	1
SICR with 1.5% treshold	0

As evidenced by above tables, changing SICR by +/- 10% or changing the 100bps threshold to 50bps or 150bps have limited impact to the overall ECL of the Group.

3.2.3.2 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 is more than 90 days and over 10 euros past due on its contractual payments. The threshold of 10 euros is put in place with debt management procedures that is a trigger for debt collection activities and also indicated as materiality threshold in Definition of Default.

Qualitative criteria

The borrower meets unlikeliness to pay criteria, which indicates the borrower is in significant financial difficulty. The following circumstances are considered as indicators for the customer not to pay the debt in full:

- Non-accrued status is applied to the contract
- Specific credit adjustments has been formed due to the decline in the credit quality
- Sale of credit obligation with economic loss higher than 5 %
- Distressed restructuring measures have been applied to the contract resulting with diminished financial obligation higher than 1 %
- It is becoming probable that the borrower will enter bankruptcy or has filed for bankruptcy
- a customer's resources of cash flow are no longer available to meet the payments of instalments
- The Group has called any collateral including a guarantee.

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 default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD) and Loss given Default (LGD) throughout the Group's expected loss calculations.

For applying the default status a customer based approach is used for wholesale and contract based approach is used for the retail portfolio.

An instrument is considered to no longer be in default when it no longer meets any of the default criteria for the probation period of corresponding to the reason of default. The shortest probation period of three months is applied to the contracts that defaulted due to filling the quantitative criteria from the date the criteria is no longer met.

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 by the time it is fully repaid. Therefore the probation period for these loans is defined as at least 1 year from the latter of:

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

3.2.3 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 widely accepted sum of marginal losses approach, whereby ECLs are calculated as the sum of the marginal losses occurring in each time 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 probability of default for each period (the probability of a default between time periods t and t+1).

ECL calculations are based on four components:

Probability of Default (PD) is an estimate of the likelihood of default over a given time horizon.

Exposure at Default (EAD) is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, and expected drawdowns on committed facilities.

Loss Given Default (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 the EAD.

Discount factor is used to discount an expected loss to a present value at the reporting date.

Mathematically, the ECL amount for prediction horizon T (12 months or lifetime, depending on whether 12-month or lifetime ECL estimates are concerned) 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 illustrated in 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, ECL model takes into account the possible decrease of collateral fair value over time through different scenarios.

	31.01.2021	28.02.2021	31.03.2021	30.04.2021	31.05.2021	30.06.2021	31.07.2021	31.08.2021	30.09.2021
(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	0	0	0	0
(6) Expected marginal loss, discounted	7.97	5.65	3.56	1.67	0	0	0	0	0
Lifetime ECL at 31.12.2020 [Sum (6)]	18.85								

Note. Discounting is done, assuming current reporting date 31.12.2020 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 the internally developed rating- and scoring models. These models have been developed for the business- and credit management.

As can be concluded, the key issue in ECL modelling is to transform the available risk parameter values into forward looking PiT estimates and 'feed' them into the expected credit loss calculation formula.

IFRS 9 parameters

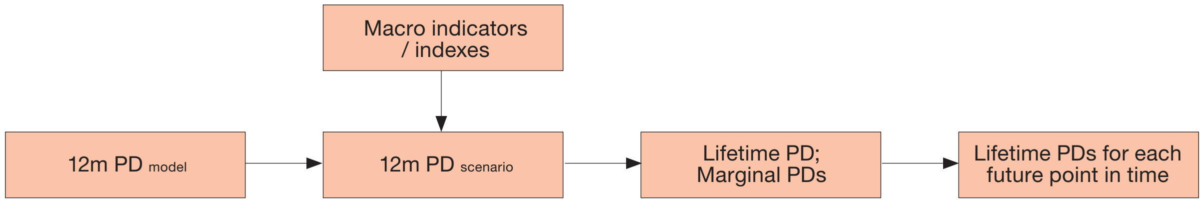
Definition of Default	• 90 days past due • Unlikely to pay without the bank turning to recourses such as selling collateral
PD	• 12-month PD; lifetime PD broken down further into marginal probabilities for sub-periods • Forward looking PiT estimate, reflecting assessment of current and future economic conditions, and a range of possible future outcomes • No regulatory floors or margins of conservatism applied
LGD	• Neutral PiT projections • Consider current and future economic conditions, and a range of possible future outcomes • Recoveries discounted, using EIR as discount rate • No regulatory floors or margins of conservatism applied
CCF/EAD	• Reflects expected changes in the balance outstanding over the lifetime of the lending exposure, incl. scheduled loan payments and prepayments
ECL	• PV of cash shortfalls. For Stage 1 exposures, 12-month PD is used. For stage 2 exposures, lifetime PD is used. For Stage 3 exposures, PD = 100%

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

3.2.3.3.1 '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 IFRS 9 expected credit loss calculation.

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



Firstly, model PD is re-calibrated to the forward looking 12-month PiT estimate, given the defined macro scenario (12m PDscenario). Selected macro indicators, transformed into macro indexes, serve as inputs for this purpose.

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.

3.2.3.3.2 'Feeding' LGDs from underlying models into ECL model

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

As IFRS 9 parameter should take into account the expected drop in the exposure amount over time, LGD for the secured part of the secured loans is directly calculated from the estimated fire-sale price of the collateral; no input from the underlying LGD models is used.

LGDs from the underlying LGD models 'feed' into the ECL calculation for the unsecured exposures and unsecured parts of the secured exposures.

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

3.2.3.3.3 'Feeding' CCF estimates from underlying models into ECL model

Internal CCF estimates feed directly to the ECL model and are used in the EAD. No further adjustments are needed for the CCF as the internal estimates do not include margins of conservatism, or through the cycle (TtC) or downturn adjustments.

3.2.3.4 Forward-looking information incorporated in the ECL model

In order to incorporate forward looking information into the ECL measurements 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. Among others, 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:

pbase, pup, pdown	– probabilities of the base, upside and downside scenarios respectively;
ECLbase, ECLup, ECLdown	– 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:

PDbase, PDup, PDdown	– lifetime PD estimates corresponding to each of the defined scenarios.

3.2.3.4.1 Selected indicators for private person credit portfolios

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

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

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

3.2.3.4.2 Selected indicators for companies

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

1) broad industry sector level based on letter codes / alphabetical branch 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 of 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 tends to be too volatile for drawing conclusions on substantial change in default risk.

A few macro indicators are significant to 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 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 are oriented to internal consumption such as retail trade.
- In conclusion, gross value added by industry sectors was selected as the indicator for companies, this given several considerations:
- Observed correlation with the considered proxies for default rates;
- GDP, which is close indicator to the gross value added, is the preferred approach for the industry;

It is easier to project for a macro economist than alternative indicators.

Economic variable assumptions

Macoreconomic scenarios (forecasts) and its indicators (incl. corporate portfolio PD and LGD estimates) are developed at least once a year and which are developed internally in the Credit Management Department that consults with the macro analysts and experts from Risk Control, business and finance units.

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

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

The most significant period-end assumptions used for the ECL estimate as at 31 December 2020 are set out below. The scenarios "base", "upside" and "downside" were used for all portfolios.

Valid at 31.12.2020

	Base scenario		Downside scenario		Upside scenario	
General macro-financial indicators	**2021E**	**2022E**	**2021E**	**2022E**	**2021E**	**2022E**
Real GDP growth, %	**2.4%**	**4.5%**	**-1.1%**	**6.6%**	**4.5%**	**3.5%**
Household consumption, %	2.3%	4.1%	-1.1%	5.0%	4.5%	4.6%
Government consumption, %	-1.9%	0.6%	2.3%	0.8%	2.0%	1.5%
Gross fixed capital formation, %	3.2%	7.5%	-5.0%	9.0%	8.0%	4.5%
Exports of goods and services, %	3.5%	6.6%	-3.8%	9.3%	6.0%	3.5%
Imports of goods and services, %	4.2%	6.5%	-5.0%	9.0%	7.0%	4.5%
Nominal GDP, EURm	27,658	29,481	26,764	28,945	28,364	30,120
GDP deflator, % change	1.3%	2.1%	1.1%	1.7%	1.7%	2.6%
Consumer price growth, %	1.0%	1.9%	0.5%	1.5%	1.5%	2.3%
Unemployment rate, %	9.1%	8.2%	12.0%	10.0%	8.5%	7.5%
Change in employment, %	-1.1%	1.0%	-3.7%	2.2%	1.7%	1.0%
Net monthly wage growth, %	-0.6%	2.6%	-1.0%	1.6%	3.0%	4.2%
House price index growth, %	-5.0%	3.5%	-10.0%	2.1%	-3.0%	4.5%
Euribor 6m	-0.5%	-0.5%	-0.5%	-0.5%	-0.5%	-0.5%
Bank lending margins on new loans (NFC)	3.1%	3.3%	3.3%	3.5%	3.0%	3.1%

Nominal growth

	Base scenario		Downside scenario		Upside scenario	
Gross value added by sectors, y-o-y growth rates	**2021E**	**2022E**	**2021E**	**2022E**	**2021E**	**2022E**
Total - all NACE activities	**2.6%**	**5.8%**	**-0.2%**	**6.8%**	**5.2%**	**5.4%**
Agriculture, forestry and fishing	4.1%	6.6%	0.3%	8.7%	6.8%	6.2%
Industry (except construction)	4.3%	7.3%	-0.3%	9.6%	7.6%	7.5%
Industry, except construction and manufacturing (mostly energy related)	0.8%	6.6%	-2.5%	8.1%	3.3%	6.2%
Manufacturing	5.3%	7.5%	0.3%	10.0%	8.8%	7.9%
Construction	-0.1%	8.0%	-3.3%	10.2%	2.5%	7.6%
Wholesale and retail trade, transport, accomodation and food service activities	5.5%	8.3%	0.3%	10.7%	9.9%	7.3%
Information and communication	1.0%	3.8%	0.3%	6.8%	4.9%	3.5%
Financial and insurance activities	1.3%	1.6%	0.3%	5.7%	3.9%	1.3%
Real estate activities	2.8%	9.2%	-1.8%	9.5%	6.3%	8.8%
Professional, scientific and technical activities; administrative and support service activities	-2.3%	2.7%	-5.5%	8.1%	0.2%	2.3%
Public administration, defence, education, human health and social work activities	0.0%	2.2%	1.6%	-2.6%	-3.0%	6.2%
Arts, entertainment and recreation; other service activities; activities of household and extra-territorial organizations and bodies	8.0%	6.6%	-4.5%	18.4%	10.8%	6.2%

The weightings assigned to each economic scenario at 31 December 2020 were as follows:

Valid at 31.12.2020

	Base scenario	Downside scenario	Upside scenario
Weights of economic scenarios	60%	30%	10%

The weightings assigned to each economic scenario at 31 December 2019 were as follows:

Valid at 31.12.2019

	Base scenario	Downside scenario	Upside scenario
Weights of economic scenarios	65%	25%	10%

The most significant period-end assumptions used for the ECL estimate as at 31 December 2019 are set out below. The scenarios "base", "upside" and "downside" were used for all portfolios.

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Valid at 31.12.2019

	Base scenario		Downside scenario		Upside scenario	
General macro-financial indicators	2020E	2021E	2020E	2021E	2020E	2021E
Real GDP growth, %	**2,2%**	**2,6%**	**0,2%**	**0,6%**	**2,7%**	**3,1%**
Household consumption, %	3,6%	2,8%	1,6%	0,8%	4,1%	3,3%
Government consumption, %	0,1%	-0,2%	-2,0%	-2,2%	0,6%	0,3%
Gross fixed capital formation, %	0,6%	2,7%	-1,5%	0,7%	1,1%	3,2%
Exports of goods and services, %	1,6%	3,1%	-0,4%	1,1%	2,1%	3,6%
Imports of goods and services, %	2,1%	3,1%	0,1%	1,1%	2,6%	3,6%
Nominal GDP, EURm	**29 472**	**31 010**	**27 791**	**28 111**	**30 048**	**31 924**
GDP deflator, % change	**3,0%**	**2,6%**	**1,0%**	**0,6%**	**3,5%**	**3,1%**
Consumer price growth, %	2,1%	2,0%	2,0%	2,0%	2,6%	2,5%
Unemployment rate, %	5,6%	5,9%	7,6%	7,9%	5,1%	5,4%
Change in employment, %	0,2%	-0,1%	-0,3%	-0,8%	0,7%	0,5%
Net monthly wage growth, %	5,5%	5,1%	3,4%	3,1%	5,9%	5,6%
House price index growth, %	4,0%	4,1%	-4,8%	-4,4%	5,5%	5,1%
Euribor 6m	-0,6%	-0,5%	-0,6%	-0,6%	-0,5%	-0,3%
Bank lending margins on new loans	2,3%	2,5%	2,5%	2,7%	2,0%	2,0%

Nominal growth

	Base scenario		Downside scenario		Upside scenario	
Gross value added by sectors, y-o-y growth rates	2020E	2021E	2020E	2021E	2020E	2021E
Total - all NACE activities	**5,3%**	**5,2%**	**1,2%**	**1,2%**	**6,2%**	**6,2%**
Agriculture, forestry and fishing	5,0%	5,0%	0,6%	0,5%	9,3%	6,0%
Industry (except construction)	4,9%	5,0%	-0,2%	0,3%	6,2%	5,7%
Industry, except construction and manufacturing (mostly energy related)	5,0%	5,0%	-0,5%	-0,6%	6,0%	6,0%
Manufacturing	5,0%	5,0%	-0,1%	0,5%	6,3%	5,7%
Construction	3,6%	5,0%	-8,5%	0,5%	6,0%	7,4%
Wholesale and retail trade, transport, accomodation and food service activities	4,5%	4,5%	0,1%	0,1%	5,5%	6,9%
Information and communication	8,5%	8,4%	8,5%	8,4%	9,5%	9,4%
Financial and insurance activities	7,2%	5,0%	2,7%	-2,6%	7,1%	6,0%
Real estate activities	4,0%	4,1%	-4,8%	-4,4%	5,5%	5,1%
Professional, scientific and technical activities; administrative and support service activities	5,0%	5,0%	0,6%	0,5%	6,0%	6,0%
Public administration, defence, education, human health and social work activities	5,0%	5,0%	6,1%	5,5%	6,0%	6,0%
Arts, entertainment and recreation; other service activities; activities of household and extra-territorial organizations and bodies	0,8%	0,6%	-1,5%	-3,7%	1,7%	1,6%

Sensitivity analysis
The most significant assumptions affecting the ECL allowance are as follows:

Retail portfolio

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

Corporate portfolio

- Estimated portfolio PiT PD values for each scenario
- Estimated LGD impact on downside scenario

The purpose of the sensitivity tests is to show that what is the effect of changing the weights of positive and negative scenarios. Thus, in the sensitivity tests, the weight of the baseline scenario is retained and two tests have been carried out, where the weights of the positive and negative scenarios have been changed by +/- 5% respectively. Compared to 2019, covid-19 has led to an increase in risks, which is reflected in an increase in the share of risk scenarios and at the expense of the baseline scenario. The table below illustrates the impact of changing scenario weights of positive and negative scenarios to the portfolio as it was at 31 December 2019 and 31 December 2020

31.12.2020	60-5-35	60-15-25
(in thousands of euros)	(base/up/down)	(base/up/down)
Change in scenario weights	1 048	-1 127

31.12.2019	65-5-30	65-15-20
(in thousands of euros)	(base/up/down)	(base/up/down)
Change in scenario weights	293	-284

Set out below are the changes to the ECL as at 31 December 2020 and 31 December 2019 that would result from reasonably possible changes in these parameters from the actual assumptions used in the Group's economic variable assumptions (for example, the impact on ECL of increasing the estimated unemployment rate by X% in each of the base, upside, downside scenarios):

31.12.2020

(in thousands of euros)	Impact of increase	Impact of decrease
Unemployment rate +/-1%	51	-66
Wage growth +/- 5%	-99	38
Euribor +/-0.5%	9	-15
Bank lending margins +/-0.5%	39	-129
Consumer price growth +/-1%	-41	24
House price index +/- 2%	-3	2
Gross value added by sectors, yoy growth rates +/- 5%	-52	48

31.12.2019

(in thousands of euros)	Impact of increase	Impact of decrease
Unemployment rate +/-1%	114	-93
Wage growth +/- 5%	-113	92
Euribor +/-0.5%	17	-11
Bank lending margins +/-0.5%	159	-167
Consumer price growth +/-1%	-37	30
House price index +/- 2%	-4	4
Gross value added by sectors, yoy growth rates +/- 5%	-37	34

The Group has performed stress test scenarios when PD and LGD estimations will both increase by 0.5. The impact of the described stress test to impairments is aggregated in the table below. The table includes loans, which have collective impairment and which have material balances and potential impact.

2020

(in thousands of euros)	Impact on loss allowances
LGD negative 0.9	812
LGD negative 1.0	-756
Average PiT PD -0.5%	-2 267
Average PiT PD +0.5%	2 719

2019

(in thousands of euros)	Impact on loss allowances
LGD negative 0.9	136
LGD negative 1.0	29
Average PiT PD -0.5%	-898
Average PiT PD +0.5%	875

2.4 Credit risk exposure

2.4.1 Maximum exposure to credit risk – Financial instruments subject to impairment

The following tables contain an analysis of the credit risk exposure of financial instruments for which an ECL allowance is recognised. 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 Expected Credit Loss (ECL) is measured and how the three stages above are determined is included in Risk management section point 3.2.3. „Expected credit loss measurement".

Distribution of corporate loans, overdraft and trade financing by internal ratings

(in thousands of euros)	31.12.2020	31.12.2019	Grading
3 low credit risk	5 696	0	Investment Grade
4 low credit risk	54 330	40	
5 low credit risk	93 398	14 984	
6 low credit risk	118 262	133 531	
7 medium credit risk	230 066	217 399	
8 medium credit risk	426 019	264 910	
9 heightened credit risk	159 787	153 067	
10 high credit risk	60 329	49 691	Non-investment grade
11 high credit risk	16 770	4 559	(incl. special monitoring)
12 non-satisfactory rating	21 014	4 505	
13 insolvent	7 414	1 036	Default
Total Corporates	**1 193 085**	**843 722**	
Retail SMEs	58 953	41 361	
Leasing	102 297	66 060	
Apartment Associations	7 135	0	
Other	6 070	3 827	
Total	**1 367 540**	**954 970**	

Corporate Lending portfolio

Corporate Lending ECL staging

(in thousands of euros)	2020 Stage 1 12-month ECL	2020 Stage 2 Lifetime ECL	2020 Stage 3 Lifetime ECL	2020 Purchased or Initiated Credit Impaired	2020 Total	2019 Stage 1 12-month ECL	2019 Stage 2 Lifetime ECL	2019 Stage 3 Lifetime ECL	2019 Purchased or Initiated Credit Impaired	2019 Total
Credit grade										
Investment grade	926 530	161 028	0	0	**1 087 558**	772 136	11 796	0	0	**783 932**
Non-investment grade										
(incl. special monitoring)	27 749	70 364	0	0	**98 113**	**31 891**	**26 863**	**0**	**0**	**58 754**
Default	51 352	14 083	8 067	0	**73 502**	**36 565**	**4 629**	**1 203**	**0**	**42 397**
Gross carrying amount	1 005 631	245 475	8 067	0	**1 259 173**	840 592	43 288	1 203	0	**885 083**
Loss allowances	3 940	8 029	1 480	0	**13 449**	2 546	1 174	98	0	**3 818**
Carrying amount	**1 001 691**	**237 446**	**6 587**	**0**	**1 245 724**	**838 046**	**42 114**	**1 105**	**0**	**881 265**

As at 31.12.2020 stage 3 includes 9 loans which are well collateralised taking into consideration all three scenarios and, therefore, the related ECL is considered to be EUR 1 222 thousand.

As at 31.12.2019 stage 3 includes 3 loans which are well collateralised taking into consideration all three scenarios and, therefore, the related ECL is considered to be 0 EUR.

For off-balance sheet exposures related with corporate credit portfolio, a provision of EUR 446 thousand was recorded as of 31.12.2020 (31.12.2019: EUR 178 thousand).

As at 31.12.2020, the impairment reserve makes up 1.09% of corporate loans and overdraft and the related interest receivables (31.12.2019: 0.44%)

As at 31.12.2020, the group-based impairment reserve makes up 0.436% of trade financing portfolio and the related interest receivables (31.12.2019: 0.38%).

As at 31.12.2020, the group-based impairment reserve makes up 0.1% of corporate factoring portfolio and the related interest receivables (31.12.2019: 0.1%).

As at 31.12.2020, the group-based impairment reserve makes up 0.03% of apartment association loan portfolio and the related interest receivables (31.12.2019 there were no such loans).

Leasing

ECL staging

(in thousands of euros)	2020 Stage 1 12-month ECL	2020 Stage 2 Lifetime ECL	2020 Stage 3 Lifetime ECL	2020 Purchased or Initiated Credit Impaired	2020 Total	2019 Stage 1 12-month ECL	2019 Stage 2 Lifetime ECL	2019 Stage 3 Lifetime ECL	2019 Purchased or Initiated Credit Impaired	2019 Total
Credit grade										
Investment grade	101 187	0	0	0	**101 187**	77 686	0	0	0	**77 686**
Non-investment grade (incl. special monitoring)	0	27 269	0	0	**27 269**	0	11 711	0	0	**11 711**
Default	0	0	395	0	**395**	0	0	91	0	**91**
Gross carrying amount	101 187	27 269	395	0	**128 851**	77 686	11 711	91	0	**89 488**
Loss allowances	295	1 010	80	0	**1 385**	143	478	18	0	**639**
Carrying amount	100 892	26 259	315	0	**127 466**	77 543	11 233	73	0	**88 849**

As of 31 December 2020, the group-based impairment reserve amounted to 1.07% of leasing portfolio (31.12.2019: 0.71%).

Private lending

ECL staging

(in thousands of euros)	2020 Stage 1 12-month ECL	2020 Stage 2 Lifetime ECL	2020 Stage 3 Lifetime ECL	2020 Purchased or Initiated Credit Impaired	2020 Total	2019 Stage 1 12-month ECL	2019 Stage 2 Lifetime ECL	2019 Stage 3 Lifetime ECL	2019 Purchased or Initiated Credit Impaired	2019 Total
Credit grade										
Investment grade	667 113	0	0	0	**667 113**	593 926	0	0	0	**593 926**
Non-investment grade (incl. special monitoring)	0	80 705	0	0	**80 705**	0	43 101	0	0	**43 101**
Default	0	0	2 517	1 157	**3 674**	0	0	175	1 891	**2 066**
Gross carrying amount	667 113	80 705	2 517	1 157	**751 492**	593 926	43 101	175	1 891	**639 093**
Loss allowances	174	481	133	33	**821**	222	552	9	68	**851**
Carrying amount	666 939	80 224	2 384	1 124	**750 671**	593 704	42 549	166	1 823	**638 242**

The provisions for mortgage portfolio are made based on the same framework as for consumer loans. As of 31 December 2020, the group-based impairment amounted to 0.09% of mortgage portfolio (31.12.2019: 0.13%).

Consumer Financing

ECL staging

(in thousands of euros)	2020 Stage 1 12-month ECL	2020 Stage 2 Lifetime ECL	2020 Stage 3 Lifetime ECL	2020 Purchased or Initiated Credit Impaired	2020 Total	2019 Stage 1 12-month ECL	2019 Stage 2 Lifetime ECL	2019 Stage 3 Lifetime ECL	2019 Purchased or Initiated Credit Impaired	2019 Total
Credit grade										
Investment grade	64 052	0	0	0	**64 052**	66 713	0	0	0	**66 713**
Non-investment grade (incl. special monitoring)	0	9 661	0	0	**9 661**	0	6 631	0	0	**6 631**
Default	0	0	534	1	**535**	0	0	138	3	**141**
Gross carrying amount	64 052	9 661	534	1	**74 248**	66 713	6 631	138	3	**73 485**
Loss allowances	398	481	298	1	**1 178**	390	329	68	3	**790**
Carrying amount	63 654	9 180	236	0	**73 070**	66 323	6 302	70	0	**72 695**

PD and LGD values are updated at least once a year with new historical data in order to maintain adequate provision levels on portfolio. If necessary, additional impairments will be made in the statement of financial position. If non-performing or doubtful loan recovery is neither economical nor practical to continue, the loan is written off as irrecoverable.

The gross amount of consumer loans written off and recorded as off-balance sheet EUR 298 thousand as at 31 December 2020 (2019: 68 thousand).

As at 31.12.2020, the group-based impairment reserve makes up 1.79% of consumer loans and the related interest receivables (31.12.2019: 1.26%).

For off-balance sheet exposures related with consumer credit portfolio, a provision of EUR 0 thousand was recorded as of 31.12.2020 and 31.12.2019.

As of 31 December 2020, the group-based impairment reserve amounted to 1.21% of hire-purchase portfolio (31.12.2019: 0.68%).

As of 31 December 2020, the group-based impairment reserve amounted to 0.94% of credit card loans and related receivables (31.12.2019: 0.7%).

For off-balance sheet exposures related with credit cards portfolio, a provision of EUR 3.5 thousand was recorded as of 31.12.2020 (31.12 2019: EUR 2.5 thousand).

Investment Financing

ECL staging

(in thousands of euros)	2020 Stage 1 12-month ECL	2020 Stage 2 Lifetime ECL	2020 Stage 3 Lifetime ECL	2020 Purchased or Initiated Credit Impaired	2020 Total	2019 Stage 1 12-month ECL	2019 Stage 2 Lifetime ECL	2019 Stage 3 Lifetime ECL	2019 Purchased or Initiated Credit Impaired	2019 Total
Credit grade										
Investment grade	11 917	0	0	0	**11 917**	5 988	0	0	0	**5 988**
Non-investment grade (incl. special monitoring)	0	0	0	0	**0**	0	0	0	0	**0**
Default	0	0	0	0	**0**	0	0	0	0	**0**
Gross carrying amount	11 917	0	0	0	**11 917**	5 988	0	0	0	**5 988**
Loss allowances	25	0	0	0	**25**	6	0	0	0	**6**
Carrying amount	11 892	0	0	0	**11 892**	5 982	0	0	0	**5 982**

The impairment reserve amounted to 0.21% of the leveraged loans portfolio (2019: 0.11%).

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3.2.4.2 Maximum exposure to credit risk – Financial instruments not subject to impairment

Financial assets kept in fair value are by definition not subject to impairment, their changes in credit risk is automatically accounted through market value changes.

In addition some accounts carrying smaller credit risk are not part of impairment calculation:

- **Cash and balances with central bank**
- **Nostro accounts**

Both of these account types carry very limited amount of credit risk and maturity tenor in general is just 1 day. Cash and central bank balances are limited per currencies – only currencies bank is active are allowed. Nostro accounts are subject to credit risk limits, all counterparts have to minimally have investment grade rating. In case counterparts rating is lowered below investment grade, the nostro account will not qualify for having balances by the end of banking day.

3.2.4.3 Collateral

The Group employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. 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, the location, the likelihood of realization and liquidity.

Expert evaluations are used to evaluate immovables. In order to ensure that market values are up to date, the individual assessments 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 principal collateral types for loans and advances are:

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

The preferred collateral is where there is no strong correlation between the client's default risk and value of the collateral. In general, the pledged assets need to be secured, 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 loan can be issued to private customers up to a specified amount. For corporate customers this is only allowed when cash flow forecast shows stable and significantly strong cash flows and/or customer's credit risk is valued to be low.

The Group's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Group since the prior period.

Mortgage business has sufficiently low 'loan to value' (LTV) ratios, which results in low loss allowance being recognised in accordance with the Group's expected credit loss model. The carrying amount of such financial assets is EUR 695 204 thousand as at 31 December 2020.

The Group closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Group will take possession of collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

31.12.2020

(in thousands of euros)	Gross exposure	Impairment allowance	Carrying amount	Fair value of collateral held
Credit-impaired assets				
Loans to corporate entities:				
- Large corporate customers	7 576	1 298	6 278	8 301
Loans to private individuals:				
- Mortgage loans	2 797	80	2 717	9 339
Total credit-impaired assets	**10 373**	**1 378**	**8 995**	**17 640**

31.12.2019

(in thousands of euros)	Gross exposure	Impairment allowance	Carrying amount	Fair value of collateral held
Credit-impaired assets				
Loans to corporate entities:				
- Large corporate customers	1 036	0	1 036	2 800
Loans to private individuals:				
- Mortgage loans	1 808	54	1 754	2 243
Total credit-impaired assets	**2 844**	**54**	**2 790**	**5 043**

In the table below, collateral information of loans and advances are disclosed based on the collateral type and carrying value or fair value of collateral held if it is lower. The under-collateralised amount is presented as “Unsecured loans”.

Loans against collateral as at 31.12.2020 (in thousands of euros)	Corporate loans incl. overdraft, factoring, apartment association loans, trade financing	Consumer loans, incl credit cards, hire-purchase	Investment financing	Leasing	Private loans incl. mortgage, overdraft, study loan, real estate leasing	Total
Listed Securities	0	0	11 917	0	0	**11 917**
Unlisted equity securities	14 888	0	0	0	1 024	**15 912**
Mortgages, real estate	670 484	0	0	0	735 067	**1 405 551**
Guarantee of KredEx and Rural Development Foundation	38 232	0	0	0	9 537	**47 769**
Pledges of rights of claim	63 810	0	0	0	0	**63 810**
Deposits	3 469	0	0	0	2 000	**5 469**
Leased assets	0	0	0	88 309	0	**88 309**
Others	78 018	0	0	0	0	**78 018**
Unsecured loans	390 272	74 247	0	40 543	3 864	**508 926**
Total	**1 259 173**	**74 247**	**11 917**	**128 852**	**751 492**	**2 225 681**

Loans against collateral as at 31.12.2019 (in thousands of euros)	Corporate loans incl. overdraft, factoring, apartment association loans, trade financing	Consumer loans, incl credit cards, hire-purchase	Investment financing	Leasing	Private loans incl. mortgage, overdraft, study loan, real estate leasing	Total
Listed Securities	0	0	5 988	0	0	**5 988**
Unlisted equity securities	35 396	0	0	0	1 066	**36 462**
Mortgages, real estate	581 750	0	0	0	626 880	**1 208 630**
Guarantee of KredEx and Rural Development Foundation	30 377	0	0	0	3 293	**33 670**
Pledges of rights of claim	84 365	0	0	0	0	**84 365**
Deposits	3 141	0	0	0	2 000	**5 141**
Leased assets	0	0	0	76 407	0	**76 407**
Others	51 174	0	0	0	-237	**50 937**
Unsecured loans	98 881	73 487	0	13 080	6 091	**191 539**
Total	**885 083**	**73 487**	**5 988**	**89 487**	**639 093**	**1 693 138**

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Collaterals for leveraged loans are monitored on a daily basis and, if collateral value is falling, immediate measures are taken to avoid credit losses. As of 31 December 2020 and as of 31 December 2019, all leveraged loans are over-collateralized. Consumer loans and credit card loans are issued without collateral and risk mitigation is done by regular monitoring of clients payment behaviour. Leasing and mortgage loans are all over-collateralized. The Group monitors customers in arrears of leasing, hire-purchase, mortgage loans and overdraft to private individuals on regular basis.

In relation to under-collateralized 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-collateralized loans are mainly considered to bear higher risk, for which the Group carries out monthly monitoring in credit committee, in order to mitigate potential credit losses. Under-collateralized loans include contracts with more than 90 days overdue totalling EUR 1 465 thousand (2019: EUR 322 thousand) euros with a collateral value of 1 208 thousand (2019: EUR 131 thousand) euros.

	Over-collateralised loans		**Under-collateralised loans**	
(in thousands of euros)	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral
As at 31.12.2020	**964 450**	**351 235**	**1 261 231**	**448 867**
Corporate loans incl. overdraft, factoring, apartment association loans, trade financing	371 650	794 170	887 523	328 285
Consumer loans, incl credit cards, hire-purchase	0	0	74 247	0
Investment financing	11 917	233 811	0	0
Leasing	16 625	26 134	112 226	59 575
Private loans incl. mortgage, overdraft, study loan, real estate leasing	564 257	1 254 497	187 235	61 007
As at 31.12.2019	**886 339**	**1 713 189**	**806 799**	**501 127**
Corporate loans incl. overdraft, factoring, apartment association loans, trade financing	272 450	477 402	612 633	364 976
Consumer loans, incl credit cards, hire-purchase	0	0	73 487	0
Investment financing	5 988	137 767	0	0
Leasing	76 407	76 407	13 081	0
Private loans incl. mortgage, overdraft, study loan, real estate leasing	531 494	1 021 613	107 598	136 151

3.2.5 Loss allowance

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

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of 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 de-recognised 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 inputs to models;
- 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 Risk management section point 3.2.6.).

The following tables explain the changes in the loss allowances between the beginning and the end of the annual period due to these factors.

Corporate lending
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2020	2 547	1 174	98	0	**3 819**
Movements with P&L impact					
Transfers:					
From Stage 1 to Stage 2	-1 013	2 888	NA	NA	**1 875**
From Stage 1 to Stage 3	-25	NA	1 004	NA	**979**
From Stage 2 to Stage 1	1	-5	NA	NA	**-4**
From Stage 3 to Stage 1	0	NA	0	NA	**0**
New financial assets originated or purchased	2 137	699	0	0	**2 836**
Changes in PDs/LGDs/EADs	-842	-766	974	0	**-634**
Changes to model assumptions and methodologies	1 423	4 150	-589	0	**4 984**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Unwind of discount[a]	0	0	0	0	**0**
FX and other movements	0	0	0	0	**0**
Total net P&L charge during the period	**1 680**	**6 967**	**1 389**	**0**	**10 036**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	-28	28	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
Financial assets derecognised during the period	-287	-83	-36	0	**-406**
Write-offs	0	0	0	0	0
Loss allowance as at 31 December 2020	**3 940**	**8 030**	**1 479**	**0**	**13 449**

Corporate lending
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2019	2 308	1 296	5 245	186	**9 035**
Movements with P&L impact	-133	133	0	0	**0**
Transfers:					
From Stage 1 to Stage 2	-156	156	NA	NA	**0**
From Stage 1 to Stage 3	0	NA	0	NA	0
From Stage 2 to Stage 1	23	-23	NA	NA	**0**
New financial assets originated or purchased	811	731	0	0	**1 542**
Changes in PDs/LGDs/EADs	-81	-37	0	NA	**-118**
Changes to model assumptions and methodologies	-1	0	0	NA	**0**
Modifications of contractual cash flows of financial assets	0	0	0	NA	**0**
Unwind of discount[a]	-357	-949	-5 147	-186	**-6 640**
FX and other movements	0	0	0	NA	**0**
Total net P&L charge during the period	**239**	**-123**	**-5 147**	**-186**	**-5 216**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	0	0	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
Financial assets derecognised during the period	0	0	0	NA	**0**
Write-offs	0	0	6 665	NA	6 665
Loss allowance as at 31 December 2019	**2 547**	**1 174**	**98**	**0**	**3 819**

Consumer Financing
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2020	371	329	86	3	**789**
Movements with P&L impact					
Transfers:					
From Stage 1 to Stage 2	-58	151	NA	NA	**93**
From Stage 1 to Stage 3	-8	NA	153	NA	**145**
From Stage 2 to Stage 1	9	-91	NA	NA	**-82**
From Stage 3 to Stage 1	0	NA	-1	NA	**-1**
New financial assets originated or purchased	290	172	41	0	**503**
Changes in PDs/LGDs/EADs	-132	-3	37	-1	**-99**
Changes to model assumptions and methodologies	7	25	23	0	**55**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Unwind of discount[(a)]	0	0	0	0	**0**
FX and other movements	0	0	0	0	**0**
Total net P&L charge during the period	**108**	**254**	**253**	**-1**	**614**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	-18	18	NA	**0**
From Stage 3 to Stage 2	NA	1	-1	NA	**0**
Financial assets derecognised during the period	-50	-8	-5	0	**-63**
Write-offs	-39	-77	-45	-1	-162
Loss allowance as at 31 December 2020	**390**	**481**	**306**	**1**	**1 178**

Consumer Financing
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2019	276	329	131	0	**735**
Movements with P&L impact	-15	11	4	0	**0**
Transfers:					
From Stage 1 to Stage 2	-12	12	NA	NA	**0**
From Stage 1 to Stage 3	-4	NA	4	NA	**0**
From Stage 2 to Stage 1	1	-1	NA	NA	**0**
New financial assets originated or purchased	330	303	69	3	**706**
Changes in PDs/LGDs/EADs	-32	-21	0	NA	**-53**
Changes to model assumptions and methodologies	8	8	0	NA	**16**
Modifications of contractual cash flows of financial assets	0	0	0	NA	**0**
Unwind of discount[(a)]	-195	-301	-118	0	**-614**
FX and other movements	0	0	0	NA	**0**
Total net P&L charge during the period	**96**	**0**	**-45**	**3**	**54**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	2	-2	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
Financial assets derecognised during the period	0	0	0	NA	**0**
Write-offs	0	0	1 024	NA	**1 024**
Loss allowance as at 31 December 2019	**372**	**329**	**86**	**3**	**789**

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Private lending
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2020	221	552	10	68	**851**
Movements with P&L impact					
Transfers:					
From Stage 1 to Stage 2	-41	193	NA	NA	**152**
From Stage 1 to Stage 3	-1	NA	18	NA	**17**
From Stage 2 to Stage 1	16	-159	NA	NA	**-143**
From Stage 3 to Stage 1	0	NA	0	NA	**0**
New financial assets originated or purchased	81	104	60	0	**245**
Changes in PDs/LGDs/EADs	-96	-154	14	-22	**-258**
Changes to model assumptions and methodologies	6	19	2	8	**35**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Unwind of discount[(a)]	0	0	0	0	**0**
FX and other movements	0	0	0	0	**0**
Total net P&L charge during the period	**-35**	**3**	**94**	**-14**	**48**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	-31	31	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
Financial assets derecognised during the period	-13	-38	-1	-1	**-53**
Write-offs	0	-5	-1	-19	**-25**
Loss allowance as at 31 December 2020	**174**	**481**	**133**	**33**	**821**

Private lending
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2019	25	9	1	0	**36**
Movements with P&L impact	-44	42	1	0	**0**
Transfers:					
From Stage 1 to Stage 2	-44	44	NA	NA	**0**
From Stage 1 to Stage 3	-1	NA	1	NA	**0**
From Stage 2 to Stage 1	2	-2	NA	NA	**0**
New financial assets originated or purchased	190	499	5	68	**762**
Changes in PDs/LGDs/EADs	-3	-9	-1	NA	**-13**
Changes to model assumptions and methodologies	155	391	51	NA	**597**
Modifications of contractual cash flows of financial assets	0	0	0	NA	**0**
Unwind of discount[(a)]	-102	-380	-49	NA	**-531**
FX and other movements	0	0	0	NA	**0**
Total net P&L charge during the period	**196**	**543**	**8**	**68**	**815**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	0	0	NA	**0**
From Stage 3 to Stage 2	NA	3	-3	NA	**0**
Financial assets derecognised during the period	0	0	0	NA	**0**
Write-offs	0	0	0	NA	**0**
Loss allowance as at 31 December 2019	**221**	**553**	**9**	**68**	**851**

Leasing
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2020	143	478	18	0	**639**
Movements with P&L impact					
Transfers:					
From Stage 1 to Stage 2	-61	146	NA	NA	**85**
From Stage 1 to Stage 3	0	NA	8	NA	**8**
From Stage 2 to Stage 1	11	-55	NA	NA	**-44**
From Stage 3 to Stage 1	0	NA	0	NA	**0**
New financial assets originated or purchased	190	235	13	0	**438**
Changes in PDs/LGDs/EADs	-35	-48	9	0	**-74**
Changes to model assumptions and methodologies	63	387	-1	0	**449**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Unwind of discount[(a)]	0	0	0	0	**0**
FX and other movements	0	0	0	0	**0**
Total net P&L charge during the period	**168**	**665**	**29**	**0**	**862**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	-45	45	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
Financial assets derecognised during the period	-16	-89	-11	0	**-116**
Write-offs	0	0	0	0	**0**
Loss allowance as at 31 December 2020	**295**	**1 010**	**81**	**0**	**1 385**

Leasing
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2019	92	312	63	0	**467**
Movements with P&L impact	-140	140	0	0	**0**
Transfers:					
From Stage 1 to Stage 2	-148	148	NA	0	**0**
From Stage 1 to Stage 3	0	NA	0	0	**0**
From Stage 2 to Stage 1	8	-8	NA	0	**0**
New financial assets originated or purchased	64	156	0	0	**220**
Changes in PDs/LGDs/EADs	-5	-17	-1	0	**-23**
Changes to model assumptions and methodologies	-2	-8	0	0	**-10**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Unwind of discount	138	-106	-47	0	**-15**
FX and other movements	0	0	0	0	**0**
Total net P&L charge during the period	**55**	**165**	**-48**	**0**	**172**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	0	0	0	**0**
From Stage 3 to Stage 2	NA	3	-3	0	**0**
Financial assets derecognised during the period	0	0	0	0	**0**
Write-offs	0	0	8	0	**8**
Loss allowance as at 31 December 2019	**147**	**477**	**15**	**0**	**639**

Investment Financing
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2020	6	0	0	0	**6**
Movements with P&L impact					
Transfers:					
From Stage 1 to Stage 2	0	0	NA	NA	**0**
From Stage 1 to Stage 3	0	NA	0	NA	**0**
From Stage 2 to Stage 1	0	0	NA	NA	**0**
From Stage 3 to Stage 1	0	NA	0	NA	**0**
New financial assets originated or purchased	8	0	0	0	**8**
Changes in PDs/LGDs/EADs	6	0	0	0	**6**
Changes to model assumptions and methodologies	6	0	0	0	**6**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Unwind of discount[a]	65	0	0	0	**65**
FX and other movements	0	0	0	0	**0**
Total net P&L charge during the period	**85**	**0**	**0**	**0**	**85**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	0	0	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
Financial assets derecognised during the period	-1	0	0	0	**-1**
Write-offs	-65	0	0	0	**-65**
Loss allowance as at 31 December 2020	**25**	**0**	**0**	**0**	**25**

Investment Financing
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Loss allowance as at 1 January 2019	3	0	0	0	**3**
Movements with P&L impact	0	0	0	0	**0**
Transfers:					
From Stage 1 to Stage 2	0	0	NA	NA	**0**
From Stage 1 to Stage 3	0	NA	0	NA	**0**
From Stage 2 to Stage 1	0	0	NA	NA	**0**
New financial assets originated or purchased	3	0	0	0	**3**
Changes in PDs/LGDs/EADs	0	0	0	NA	**0**
Changes to model assumptions and methodologies	0	0	0	NA	**0**
Modifications of contractual cash flows of financial assets	0	0	0	NA	**0**
Unwind of discount(a)	0	0	0	NA	**0**
FX and other movements	0	0	0	NA	**0**
Total net P&L charge during the period	**3**	**0**	**0**	**0**	**3**
Other movements with no P&L impact					
Transfers:					
From Stage 2 to Stage 3	NA	0	0	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
Financial assets derecognised during the period	0	0	0	NA	**0**
Write-offs	0	0	0	NA	**0**
Loss allowance as at 31 December 2019	**6**	**0**	**0**	**0**	**6**

Other loan portfolios and changes in the impairments between the beginning and the end of the annual period are disclosed in the Note 11. ECL allowance related information is disclosed in the Risk management section point 3.2.4.1.

Significant changes in the gross carrying amount of financial assets that contributed to changes in the loss allowance were as follows:

- Changes in loss allowances of corporate loan portfolio explained in detail in table below

The following table further explains changes in the gross carrying amount of the portfolio to help explain their significance to the changes in the loss allowance for the same portfolio as discussed above:

Corporate loans
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Gross carrying amount as at 1 January 2020	804 027	38 659	1 036		**843 722**
Movements with P&L impact					
Transfers:					
From Stage 1 to Stage 2	-175 207	175 207	NA	NA	**0**
From Stage 1 to Stage 3	-5 279	NA	5 279	NA	**0**
From Stage 2 to Stage 3	NA	-1 145	1 145	NA	**0**
From Stage 3 to Stage 2	NA	0	0	NA	**0**
From Stage 2 to Stage 1	2 166	-2 166	NA	NA	**0**
Financial assets derecognised during the period	-132 312	-8 624	-129		**-141 065**
New financial assets originated or purchased	460 360	29 239	0		**489 599**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Changes in interest accrual	524	222	83	0	**829**
Write-offs	0	0	0	0	**0**
FX and other movements	0	0	0	0	**0**
Gross carrying amount as at 31 December 2020	**954 279**	**231 392**	**7 414**	**0**	**1 193 085**

Corporate loans
(in thousands of euros)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Purchased Credit Impaired	Total
Gross carrying amount as at 1 January 2019	607 468	28 378	12 045	380	**648 271**
Movements with P&L impact					
Transfers:					
From Stage 1 to Stage 2	-16 784	16 784	NA	NA	**0**
From Stage 1 to Stage 3	0	NA	0	NA	**0**
From Stage 2 to Stage 3	NA	-46	46	NA	**0**
From Stage 3 to Stage 2	NA	0	0	0	**0**
From Stage 2 to Stage 1	3 318	-3 318	NA	NA	**0**
Financial assets derecognised during the period	-110 503	-14 242	-24 048	-379	**-149 172**
New financial assets originated or purchased	320 821	11 025	0	0	**331 846**
Modifications of contractual cash flows of financial assets	0	0	0	0	**0**
Changes in interest accrual	-293	78	-35	-1	**-251**
Write-offs	0	0	13 028	0	**13 028**
FX and other movements	0	0	0	0	**0**
Gross carrying amount as at 31 December 2019	**804 027**	**38 659**	**1 036**	**0**	**843 722**

The Group considers the loan as non-performing and assesses impairment when the loan payments have not been collected by the due date and/or the expected cash flows from the realization of collateral are not sufficient for covering the carrying amount of the loan principal and interest payments.

The Group evaluates these loans individually. In case of individual evaluation, the amount of the impairment loss is the difference between the carrying value of the receivable and expected cash flows discounted at the effective interest rate. In 2020, the Group provisioned corporate loans in the total amount of EUR 13 002 thousand (2019: EUR 3 431 thousand).

Loan customers with ratings of 10-13 are subject to more frequent monitoring during which the solvency of the borrower is evaluated. In case of a deterioration of payment behaviour, the requirement for individual provisioning is evaluated, considering, among other factors, the collateral of the loan, therefore some loans are not individually impaired, because they are sufficiently secured. The ratings-based rate of the collective provisioning is applied to those loans.

In addition to loans issued, loan agreements have been concluded and signed for the unused loan commitment amount of 399 362 thousand euros at 31.12.2020 (31.12.2019: 359 230 thousand euros).

In the following table there are presented unused portions of corporate loans and financial guarantee limits. In addition to that as at 31.12.2020 the Group has also committed to grant mortgage loans, hire-purchase loans, consumer loans, overdraft loans and credit card loans to individuals in total amount of EUR 81 250 thousand (31.12.2019: EUR 69 898 thousand). All uncommissioned loans available to individuals have at least investment grade scoring as at the end of each reporting period.

Credit quality of off-balance sheet liabilities

(unused loan commitments for corporate loans and financial guarantees)

(in thousands of euros)	31.12.2020	31.12.2019
3 very low risk	100 000	100 000
5 low credit risk	2 735	615
6 low credit risk	35 402	42 265
7 medium credit risk	37 332	29 462
8 medium credit risk	176 195	86 923
9 heightened credit risk	16 628	41 016
10 high credit risk	4 039	15 743
11 high credit risk	1 003	16
12 payments are delayed	747	77
Non-rated (retail clients)	10 204	2 730
Total	**384 285**	**318 847**

The total amount of undiscounted expected credit losses at initial recognition for purchased or originated credit-impaired financial assets recognised during the period was EUR 71 thousand.

3.2.6. 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 recognized as income.

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

Credit cards and hire-purchase

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

A bankruptcy has been announced to the client or the client has been declared insolvent.

The court confirms the debt restructuring plan (the claim recognized 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 after the inventory of the estate bankruptcy is declared.

The client forwarded to the bailiff has a foreign address or none at all.

Leasing, private and business loans

The client does not voluntarily reimburse the Group's claim risen from the difference of original claim and the realization of the collateral.

3.2.7. 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 (refer to note 2.6). The Group monitors the subsequent performance of modified assets. The Group may determine that the 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. The gross carrying amount of such assets held as at 31 December 2020 was EUR 0 (2019: 0).

The Group continues to monitor if there is a subsequent significant increase in credit risk in relation to such assets through the use of specific models for modified assets.

There were no such financial assets with lifetime ECL whose cash flows were modified during the period.

3.3 Market risk

Market risk arises from the Group's positions which are exposed to changes in interest rates, foreign exchange rates and securities prices. Such positions arise from the Group's trading, market making and investment activities as well as from the Bank's lending and funding activities (banking book). The Bank has set very conservative limits for the trading, liquidity and investment portfolios and open foreign currency exposures.

LHV Varahaldus invests most of its available resources into its own managed pension funds. The management of LHV Varahaldus is responsible for monitoring the market risk.

3.3.1 Foreign currency risk

Foreign currency risk arises from the potential mis-match of the Bank's foreign currency assets and liabilities. Treasury is responsible for the daily monitoring of net open foreign currency positions. The Group's management of foreign currency risk is governed by risk policies, risk metrics, limits and internal procedures. The internal limits for net open foreign currency positions are proposed by the Risk Control unit and Treasury and the limits are set internally by the Asset and Liability Committee . The limits set by the Committee are maximum nominal limits in euro equivalent for each currency. The nominal limits are calibrated to ensure that the total potential loss from foreign currency risk would remain within a specified percentage with respect to the Group's net own funds. If the open currency position exceeds the limits set by the Committee, measures are immediately implemented to close or reduce such positions (hedging the risk with relevant instruments, such as foreign currency spot, forwards or futures).

A sensitivity analysis has been performed for the effect of possible changes attributable to net open currency positions on statement of profit or loss, with the assumption of other conditions remaining constant.

Impact on statement of profit or loss
(in thousands of euros)

	2020	2019
USD exchange rate +/- 10%	+/-11	+/-3
SEK exchange rate +/- 10%	+/-7	+/-3
GBP exchange rate +/- 10%	+/-14	+/-1
CHF exchange rate +/- 10%	+/-0	+/-2

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 off-balance sheet assets and liabilities. 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. The balances of total assets and total liabilities bearing currency risk do not include currency futures at their fair value, but they are shown here at their full contractual cash flow amounts as off-balance sheet assets and liabilities; also, the table does not include the assets (tangible and intangible assets) and liabilities (provisions) not bearing currency risk and equity.

31.12.2020
(in thousands of euros)

	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Assets bearing currency risk								
Due from banks and investment companies	8	2 251 277	1 163	119 368	1 943	12 295	7 212	**2 393 258**
Investments in debt and equity securities	9,10	322 834	7	0	9	52	28	**322 930**
Loans and advances to customers	11	2 195 133	24	7 016	484	5 997	169	**2 208 823**
Receivables from customers	12	841	0	350	11	464	788	**2 454**
Other financial assets	13	117	0	0	0	1 956	0	**2 073**
Total assets bearing currency risk		**4 770 202**	**1 194**	**126 734**	**2 447**	**20 764**	**8 197**	**4 929 538**
Liabilities bearing currency risk								
Deposits from customers and loans received	15	4 376 293	3 950	125 267	7 292	85 616	11 597	**4 610 015**
Financial liabilities at fair value	10	221	0	0	0	0	0	**221**
Accounts payable and other financial liabilities	16	13 126	21	1 610	661	4 343	1 637	**21 398**
Subordinated debt	18	88 500	0	0	0	0	0	**88 500**
Total liabilities bearing currency risk		**4 478 140**	**3 971**	**126 877**	**7 953**	**89 959**	**13 234**	**4 720 134**
Open gross position derivative assets at contractual value		0	2 778	0	5 581	69 080	4 350	**81 789**
Open gross position derivative liabilities at contractual value		81 789	0	0	0	0	0	**81 789**
Open foreign currency position		**210 273**	**1**	**-143**	**74**	**-115**	**-687**	**209 404**

31.12.2019
(in thousands of euros)

	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Assets bearing currency risk								
Due from banks and investment companies	8	1 231 088	514	27 690	1 053	1 362	8 745	**1 270 453**
Investments in debt and equity securities	9,10	16 683	0	0	1	16 241	5	**32 931**
Loans and advances to customers	11	1 685 519	4	62	584	788	77	**1 687 034**
Receivables from customers	12	1 742	10	601	56	0	335	**2 745**
Other financial assets	13	110	0	0	0	2 136	0	**2 246**
Total assets bearing currency risk		**2 935 142**	**528**	**28 353**	**1 695**	**20 528**	**9 163**	**2 995 409**
Liabilities bearing currency risk								
Deposits from customers and loans received	15	2 667 370	4 538	27 138	8 139	20 356	11 061	**2 738 601**
Financial liabilities at fair value	10	5	0	0	1	1	1	**8**
Accounts payable and other financial liabilities	16	16 934	62	1 201	345	245	1 826	**20 613**
Subordinated debt	18	70 500	0	0	0	0	0	**70 500**
Total liabilities bearing currency risk		**2 754 809**	**4 601**	**28 339**	**8 485**	**20 602**	**12 888**	**2 829 722**
Open gross position derivative assets at contractual value		615	4 054	0	6 816	713	3 359	**15 557**
Open gross position derivative liabilities at contractual value		14 942	0	0	0	615	0	**15 557**
Open foreign currency position		**166 006**	**-19**	**14**	**26**	**25**	**-366**	**165 687**

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3.3.2 Price risk

Financial instruments bearing price risk at Group are securities held in the liquidity portfolio, trading portfolio and investment portfolio (Note 9, 10). Limits have been set for 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. The Risk Control unit monitors the compliance with limits.

Pursuant to the Investment Funds Act, the minimum shares of LHV Varahaldus as the management company is 0.5% (according to the Investment Funds Act in force until 9 January 2017, it was 1%) of the number of units in each of the mandatory pension fund managed by it. Based on historical performance and volatility of the pension fund unit NAV changes, the price changes should remain +/- 10% in the next 12-month period with the most likely change +/-5% and the impact to statement of profit or loss is presented in the next table.

LHV Varahaldus invests the remaining available assets in euros, to ensure liquidity and to not bear investment risk.

The Bank does not hold significant amounts of equity securities in its position (see Note 12), accordingly the sensitivity to change in the market price of these positions is marginal.

Bank's debt securities portfolio recognised at the market price is short-term and of high quality, therefore, the effect of the changes in market risk premiums on the market value of the debt security portfolio should remain at around 1.0% (2019: 1.0%).

The following table presents the results of a sensitivity analysis (the impact from the risk exposures to the net result of the Group's largest entity AS LHV Pank from a reasonably possible change in thousands euros):

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

(in thousands of euros)	2020	2019
Equity securities and fund units +/-10%	+/-14	+/-50
Debt securities (FVTPL) +/-1.0% (+/-1.0%)	+/-3 227	+/-323

Impact on other comprehensive income

(in thousands of euros)	2020	2019
Equity securities (FVOCI/AFS) +/-10%	+/- 0	+/- 43

3.3.3 Interest rate risk

Interest rate risk arises from the mismatch of interest rate types, refixing periods or base rates of assets and liabilities (both balance sheet and off-balance sheet items). The Group's interest rate risk management is based on risk policies, limits and internal procedures which identify all significant sources of interest rate risk and provide for balanced risk taking.

Interest rate risk is measured by conducting gap and duration analysis under different scenarios. The goal of the analysis is to determine the maximum potential loss in case of an adverse change in interest rates.

Duration analysis (change in the economic value of equity) aims to assess the change in the economic value of the assets, liabilities and equity in different interest rate scenarios. Gap analysis assesses the impact of interest rate changes on net interest income in the next 12-month period.

Both duration analysis and gap analysis are regularly conducted for two scenarios including an increase as well as decrease of interest rates. The key scenario is parallel upward or downward shift in interest rates of 200 bps. The statement of financial position and margins on assets and deposits are assumed to be constant over time.

Internal limits for interest rate risk management are set by AS LHV Pank's Asset and Liability Committee. Limits on interest rate risk are set in relation to net own funds. Treasury is responsible for managing interest rate risk on an ongoing basis.

Interest rates on term deposits decreased gradually in 2020 while interest rates on demand deposits remained at a low level (0.01% for regular EUR deposits).

The interest rates for leveraged loans granted are changed at most once a month according to fluctuations in market interest rates. As at the end of 2020, the interest rate on loans received for specific purposes (excluding loans received from central banks), equalled 0.43% (2019: 0.62%). The effective interest rate of subordinated debts entered into in 2016- 2019 was 6.5%, the effective interest rate of subordinated debts entered into in 2020 was 7.5% and the effective interest rate of perpetual subordinated debts entered into in 2019-2020 was 9.5%. The information about subordinated debt contractual interest rates is provided in Note 18.

As at 31.12.2020, an increase of 1 percentage point in interest rates would affect the Bank's annual net interest income and profit by EUR +13 559 thousand (2019: EUR +9 362 thousand). In the same time, a decrease of 1 percentage point in interest rates would affect the Bank's annual net interest income (profit) by EUR -2 065 thousand (2019: EUR +127 thousand). A 1 percentage point increase in market interest rates would raise the Bank's economic value, i.e. equity, by EUR +39 122 thousand (2019: EUR +16 946 thousand). A 1 percentage point decrease in market interest rates would affect the Bank's economic value (equity) by

EUR 84 167 thousand (2019: 74 229 thousand). The effect on the Group's economic value in both scenarios is positive due to the fact that the Group has majorly invested in current assets, the loans granted to customers are largely based on the 6-month Euribor, the level of which does not fall below 0% according to loan agreements, and due to the longer-term nature of the demand obligations, the average duration of interest-bearing assets is shorter than the average duration of interest-bearing liabilities.

When calculating the effects of the change in the net interest income on profit and the simulation of the change in the economic capital, the terms of loan contracts are taken into account (including interest rate floors which are relevant in the case of downward scenario). Lower limits are also used for certain other assets. On the liabilities side, it is assumed that deposit interest rates will not become negative. Demand deposits are assumed to have a behavioural duration of 2 years for interest rate changes. Part of the deposits are assumed to be converted into term deposits in the case of interest rate increase.

The table below shows the structure of the interest-bearing assets and interest-bearing liabilities of LHV Group grouped by the recalculation dates of interest rates at the principal amounts of receivables and liabilities. Leveraged loans are treated as a one-month product maturing at the next interest fixing date.

31.12.2020 *(in thousands of euros)*	Note	Up to 3 months	3-12 months	1-5 years	Over 5 years	Subtotal	Accrued interest	Impair-ments	Total
Financial assets									
Due from banks and investment companies	8	2 393 258	0	0	0	2 393 258	0	0	**2 393 258**
Financial assets at fair value (debt securities)	9, 10	200 045	117 300	4 280	0	321 625	1 074	0	**322 699**
Loans and advances to customers	11	993 697	1 113 053	103 141	10 616	2 220 507	5 174	-16 858	**2 208 823**
Total		**3 587 000**	**1 230 353**	**107 421**	**10 616**	**4 935 390**	**6 248**	**-16 858**	**4 924 780**
Financial liabilities									
Deposits from customers and loans received	15	974 235	398 683	3 235 625	28	4 608 571	1 444	0	**4 610 015**
Subordinated debt*	18	0	0	0	88 500	88 500	489	0	**88 989**
Total		**974 235**	**398 683**	**3 235 625**	**88 528**	**4 697 071**	**1 933**	**0**	**4 699 004**
Net interest sensitivity gap		**2 612 765**	**831 670**	**-3 128 204**	**-77 912**	**238 319**			

31.12.2019 *(in thousands of euros)*	Note	Up to 3 months	3-12 months	1-5 years	Over 5 years	Subtotal	Accrued interest	Impair-ments	Total
Financial assets									
Due from banks and investment companies	8	1 270 453	0	0	0	1 270 453	0	0	**1 270 453**
Financial assets at fair value (debt securities)	9, 10	10 682	0	12 950	7 925	31 557	774	0	**32 331**
Loans and advances to customers	11	729 768	851 657	84 798	22 988	1 689 211	3 927	-6 104	**1 687 034**
Total		**2 010 903**	**864 607**	**92 723**	**22 988**	**2 991 221**	**4 701**	**-6 104**	**2 989 818**
Financial liabilities									
Deposits from customers and loans received	15	375 862	491 080	1 868 767	1	2 735 710	2 891	0	**2 738 601**
Subordinated debt*	18	0	0	0	70 500	70 500	429	0	**70 929**
Total		**375 862**	**491 080**	**1 868 767**	**70 501**	**2 806 219**	**3 320**	**0**	**2 809 530**
Net interest sensitivity gap		**1 635 041**	**373 527**	**-1 776 044**	**-47 513**	**185 011**			

* The contractual term of subordinated debts received in 2018 is 10 years and the interest rate is fixed at 6.0%. The contractual term of subordinated debts received in 2019 is 10 years and the interest rate is fixed at 8.0%. The contractual term of subordinated debts received in 2020 is 10 years and the interest rate is fixed at 7.0%, perpetual subordinated loans received in 2020 have interest rate fixed at 9.5%.

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3.4 Liquidity risk

Liquidity risk relates to the ability of LHV Pank to meet its contractual obligations on time. Liquidity risk is most relevant in the context of the Bank as there is a difference between the maturity of the Bank's assets (loans provided to customers) and liabilities (mostly deposits). The LHV Pank's liquidity risk management is documented in the Liquidity Risk Management Policy and other internal rules, providing for liquidity risk metrics, limits and internal procedures. As per policy statements, the Group's liquidity management reflects a conservative approach towards liquidity risk. The liquidity risk management framework includes stress testing, early warning indicators and business continuity plan for liquidity management. The key internal metric for liquidity risk management is survival period which is calculated both in stress as well as base scenario. Minimum required limit for the survival period is set out to ensure that the bank would have a sufficient liquidity buffer which would allow response time for the Bank in case of market-wide or idiosyncratic stress scenarios. Additionally, concentration risk of deposits is monitored and limited to avoid dependence on a small number of large depositors.

Internal metrics are complemented by the Basel III metrics - the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR), which LHV Pank is fully compliant with as at 31.12.2020 and 31.12.2019. The aim of the liquidity coverage ratio (LCR) standard is to ensure that the bank has an adequate amount of unencumbered assets of high quality and liquidity that could be monetized without incurring material losses to meet a liquidity requirement in a 30-day stress scenario. The output of the standard is the ratio of liquid assets to stress scenario liquidity requirement, which has a limit of 100%. The bank's liquidity coverage ratio level as at 31.12.2020 was 147% (2019: 143%).

The objective of the net stable funding ratio (NSFR) is to ensure that the bank has adequate stable funding sources to finance longer-term assets. The Groups's NSFR level stood at 154% as of 31.12.2020 (31.12.2019: 157%).

The Treasury of LHV Pank is responsible for the management of liquidity risk. One of the key instruments for managing liquidity risk is maintaining an adequate buffer of high quality and liquid instruments. The liquidity buffer consists of cash and deposits with the central bank and liquid securities held by the Treasury, which can be readily sold or used as a collateral in funding operations with the central bank. For longer term liquidity planning, Treasury is involved in preparing the financial plan which includes a longer term view of the required funding to support the Group's business. As at 31.12.2019 and 31.12.2018, the Group does not have any debts past due.

The following tables present the distribution of financial assets and liabilities, excl. derivatives, by due dates and by future contractual undiscounted cash flows and in a separate column the statement of financial position balance is disclosed. In the maturity analysis, the cash flows are split into the maturity buckets in which the cash flows occur (including interest cash flows). Explanation of the fair value of these financial assets and liabilities is presented in Note 3.5.

31.12.2020

(in thousands of euros)	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 and loans received	15	3 657 063	99 647	386 654	465 776	1 473	**4 610 613**	**4 610 015**
Subordinated debt	18	0	1 736	5 207	27 770	98 564	**133 277**	**88 500**
Accounts payable and other financial liabilities	16	0	21 398	0	0	0	**21 398**	**21 398**
Unused loan commitments	21	0	413 818	0	0	0	**413 818**	**0**
Financial guarantees by contractual amounts	21	0	36 492	0	0	0	**36 492**	**0**
Foreign exchange derivatives (gross settled)		0	81 180	0	609	0	**81 789**	**0**
Financial liabilities at fair value	10	0	221	0	0	0	**221**	**221**
Total liabilities		**3 657 063**	**655 101**	**391 861**	**494 155**	**100 037**	**5 297 608**	**4 720 134**
Assets held for managing liquidity risk by contractual maturity dates								
Due from banks and investment companies	8	2 393 258	0	0	0	0	**2 393 258**	**2 393 258**
Financial assets at fair value (debt securities)	9, 10	0	200 448	117 716	4 534	0	**322 698**	**322 698**
Loans and advances to customers	11	0	146 192	329 310	1 375 417	741 393	**2 592 312**	**2 208 823**
Receivables from customers	12	0	2 454	0	0	0	**2 454**	**2 454**
Foreign exchange derivatives (gross settled)		0	81 789	0	0	0	**81 789**	**0**
Other financial assets	13	2 073	0	0	0	0	**2 073**	**2 073**
Total assets held for managing liquidity risk		**2 395 331**	**430 883**	**447 026**	**1 379 951**	**741 393**	**5 394 584**	**4 929 306**
Maturity gap from assets and liabilities		**-1 261 732**	**-224 218**	**55 165**	**886 405**	**641 356**	**96 976**	**209 172**

31.12.2019

(in thousands of euros)	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 and loans received	15	2 201 704	41 522	476 248	18 721	2 906	**2 741 101**	**2 738 601**
Subordinated debt	18	0	1 318	3 954	21 090	81 745	**108 107**	**70 500**
Accounts payable and other financial liabilities	16	0	20 613	0	0	0	**20 613**	**20 613**
Unused loan commitments	21	0	359 230	0	0	0	**359 230**	**0**
Financial guarantees by contractual amounts	21	0	14 139	0	0	0	**14 139**	**0**
Foreign exchange derivatives (gross settled)		0	14 942	0	615	0	**15 557**	**0**
Financial liabilities at fair value	10	0	8	0	0	0	**8**	**8**
Total liabilities		**2 201 704**	**451 772**	**480 202**	**40 426**	**84 651**	**3 258 755**	**2 829 722**
Due from banks and investment companies	8	1 270 453	0	0	0	0	**1 270 453**	**1 270 453**
Financial assets at fair value (debt securities)	9, 10	0	10 883	13 018	8 429	0	**32 330**	**32 331**
Loans and advances to customers	11	0	113 590	251 806	1 029 520	582 889	**1 977 805**	**1 687 034**
Receivables from customers	12	0	2 745	0	0	0	**2 745**	**2 745**
Foreign exchange derivatives (gross settled)		0	14 942	0	615	0	**15 557**	**0**
Other financial assets	13	2 246	0	0	0	0	**2 246**	**2 246**
Total assets held for managing liquidity risk		**1 272 699**	**142 160**	**264 824**	**1 038 564**	**582 889**	**3 301 136**	**2 994 809**
Maturity gap from assets and liabilities		**-929 005**	**-309 612**	**-215 378**	**998 138**	**498 238**	**42 381**	**165 087**

The following table shows the distribution of short- and long-term assets and liabilities.

(in thousands of euros)

	Note	31.12.2020	31.12.2019
Current assets			
Due from central banks	8	2 213 211	1 232 733
Due from credit institutions	8	170 062	32 247
Due from investment companies	8	9 985	5 473
Financial assets at fair value through profit or loss	10	322 930	32 499
Loans and advances to customers	11	395 341	301 327
Receivables from customers	12	2 454	2 745
Other assets	13	1 943	1 857
Total current assets		**3 115 926**	**1 608 881**
Non-current assets			
Equity instruments at FVOCI	9	0	432
Other financial assets	13	2 073	2 246
Loans and advances to customers	11	1 813 482	1 385 707
Tangible assets	14	6 571	6 680
Intangible assets	14	807	685
Total non-current assets		**1 822 933**	**1 395 750**
Total assets		**4 938 859**	**3 004 631**
Liabilities			
Current liabilities			
Deposits from customers and loans received	15	4 142 766	2 716 974
Financial liabilities at fair value through profit or loss	10	221	8
Accounts payable and other liabilities	16	25 441	23 774
Total current liabilities		**4 168 428**	**2 740 756**
Non-current liabilities			
Deposits from customers and loans received	15	467 249	21 627
Subordinated debt	18	88 500	70 500
Total non-current liabilities		**555 749**	**92 127**
Total liabilities		**4 724 177**	**2 832 883**

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3.5 Fair value of financial assets and financial liabilities

(in thousands of euros)	Note	Level 1	Level 2	Level 3	Total fair value 31.12.2020	Carrying value 31.12.2020	Difference
Financial assets at fair value through profit or loss							
Shares	10	142	0	0	142	142	0
Debt securities at fair value through profit or loss	10	322 699	0	0	322 699	322 699	0
Interest rate swaps and foreign exchange forwards	10	0	89	0	89	89	0
Total financial assets at fair value through profit or loss		**322 841**	**89**	**0**	**322 930**	**322 930**	**0**
Financial liabilities at fair value through profit or loss							
Interest rate swaps and foreign exchange forwards	10	0	221	0	221	221	0
Total financial liabilities at fair value through profit or loss		**0**	**221**	**0**	**221**	**221**	**0**
Financial assets at amortised cost							
Due from other banks	8	0	2 213 211	0	2 213 211	2 213 211	0
Due from credit institutions	8	0	170 062	0	170 062	170 062	0
Due from investment companies	8	0	9 985	0	9 985	9 985	0
Loans and advances to customers	11	0	0	2 239 759	2 239 759	2 208 823	30 936
Receivables from customers	12	0	2 454	0	2 454	2 454	0
Other financial assets	13	0	2 073	0	2 073	2 073	0
Total financial assets at amortised cost		**0**	**2 397 785**	**2 239 759**	**4 637 544**	**4 606 608**	**30 936**
Financial liabilities at amortised cost							
Deposits from customers and loans received	15	0	3 636 156	953 447	4 589 603	4 588 355	1 248
Subordinated debt	18	0	0	91 491	91 491	88 500	2 991
Accounts payable and other liabilities	16	0	21 398	0	21 398	21 398	0
Total financial liabilities at amortised cost		**0**	**3 657 554**	**1 044 938**	**4 702 492**	**4 698 253**	**4 239**

Total net gain recognised in OCI for level 3 financial assets amounted to EUR 0 thousand.

(in thousands of euros)	Note	Level 1	Level 2	Level 3	Total fair value 31.12.2019	Carrying value 31.12.2019	Difference
Financial assets at fair value through profit or loss							
Shares	10	164	0	0	164	164	0
Equity instruments at fair value through other comprehensive income	9	0	0	432	432	432	0
Debt securities at fair value through profit or loss	10	32 331	0	0	32 331	32 331	0
Interest rate swaps and foreign exchange forwards	10	0	4	0	4	4	0
Total financial assets at fair value through profit or loss		**33 495**	**4**	**432**	**32 931**	**32 931**	**0**
Financial liabilities at fair value through profit or loss							
Interest rate swaps and foreign exchange forwards	10	0	8	0	8	8	0
Total financial liabilities at fair value through profit or loss		**0**	**8**	**0**	**8**	**8**	**0**
Financial assets at amortised cost							
Due from other banks	8	0	1 232 733	0	1 232 733	1 232 733	0
Due from credit institutions	8	0	32 247	0	32 247	32 247	0
Due from investment companies	8	0	5 473	0	5 473	5 473	0
Loans and advances to customers	13	0	0	1 707 842	1 707 842	1 687 034	20 808
Receivables from customers	14	0	2 745	0	2 745	2 745	0
Other financial assets	15	0	2 246	0	2 246	2 246	0
Total financial assets at amortised cost		**0**	**1 275 444**	**1 707 842**	**2 983 286**	**2 962 478**	**6 064**
Financial liabilities at amortised cost							
Deposits from customers and loans received	15	0	2 204 495	537 577	2 742 072	2 738 601	3 471
Subordinated debt	18	0	0	73 010	73 010	70 500	2 510
Accounts payable and other liabilities	16	0	20 613	0	20 613	20 613	0
Total financial liabilities at amortised cost		**0**	**2 225 108**	**610 587**	**2 835 695**	**2 829 714**	**5 981**

Total net gain recognised in OCI for level 3 financial assets amounted to EUR 134 thousand.

The management board of the Group has assessed the fair value of assets and liabilities carried at amortised cost in the statement of financial position. For estimating fair value, the future cash flows are discounted based on the market interest yield curve.

Levels used in hierarchy:

1. Level 1 – quoted prices in active market
2. Level 2 – valuation technique based on observable market data as inputs (rates and interest curves from similar transactions)
3. Level 3 – other valuation techniques (a)Quantitative information about the significant unobservable inputs used in fair value measurement (if developed and available for the entity); b)a narrative description of the sensitivity of FV measurement to changes in unobservable inputs (if the change might result in a significant change in FV measurement); c)effect of reasonable possible changes to unobservable inputs

For the term structure of financial assets and financial liabilities, refer to Note 3.4.

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3.6 Operational risk

Operational risk is a potential loss caused by human, process or information system flaws. When completing transactions, transaction limits and competence systems are used to minimise potential losses and the segregation of duties principle is used in the Group's working procedures, according to which there should be an approval by at least two employees or units in order to carry out a transaction or procedure.

The information received from monitoring operating risk helps to gather initial information to secure capital adequacy of the Group and to evaluate capital requirements. The analysis of cases collected into the database enables the Group to identify the flaws in business processes, avoid making mistakes in the future and mitigate possible risks or define the terms of their acceptance. The risk control manager of Group is responsible for collecting information.

Compliance control and internal audit department have an important role in evaluating, monitoring and mitigating the operating risk. The main task of the Compliance Officer is to evaluate the activities of the Group in accordance with legislation, the supervision guidelines of the Financial Supervision Authority and procedure rules of the Group. Internal audit is an independent and objective function, assuring and consulting activity that is targeted at improving the Group's performance, processes and adding value. Internal audit helps achieving the goals of the Group, using a systematic and disciplined approach to assess and increase the efficiency of the risk management, control and organisational management process.

3.7. Compliance risk

Compliance risk is the existing or potential risk to income and capital as a consequence of a failure to comply with laws, regulations, guidelines, standards or ethical principles. The realization of a risk may result in fines, claims, loss in reputation, termination of contractual relationships and, in revocation of the licence.

The aim of managing compliance risk is to prevent the negative consequences from materializing.

Considering the volume and pace of changes to regulatory requirements and complexity of business activities LHV assesses compliance risk to remain high for the foreseeable future.

In order to manage the risk, the compliance function assesses changes to regulatory environment, evaluates their potential impact, informs management of changes and participates in the implementation thereof.

Monthly overviews to management include information collected from various sources, including supervisory guidelines, EU, UK and Estonian regulatory acts. Board members take responsibility in implementing identified changes. In addition, the compliance function keeps track of all regulatory requirements applicable to LHV group entities.

The function also performs compliance audits, assesses new and changes to existing products and processes, provides advice and training and performs certain monitoring activities.

The biggest challenges that LHV continues to face are similar to other market participants and include MiFID, GDPR, AMLD and CRR/CRD.

Due to the nature of business model LHV performs those duties also for the UK branch through the function in Estonia and UK. Additional burden follows the decision of UK to leave EU. This brings on changes to regulatory and supervisory environment.

3.8. Anti-money laundering

AML/CTF Governance

The internal governance of LHV is based on the Three Lines of Defence model. AML together with Compliance form a part of the second line of defence which is established to ensure the first line of defence (i.e. operational management) is properly designed, in place, and operating as intended. As management functions, they provide framework and guidance for developing and modifying risk management and internal controls.

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

The Management Board and the Supervisory Board of LHV Group and LHV Pank have a strong commitment towards implementing, maintaining and developing AML/KYC regime all over the group entities. Most of the AML/CTF policies and procedures are updated at least yearly. In 2020, the Management Board of LHV Pank approved a new version of the Risk Assessment and Risk Appetite Framework.

Analytical and technical capabilities of the group entities are the key elements of building a solid AML/KYC system. Although in 2019 new tools for monitoring (FICO Tonbeller software Siron) and screening (Accuity software Compliance Link) activities were implemented, co-operation with OÜ Salv Technology was initiated in 2020 to improve the monitoring and screening capabilities even further.

In addition to the investments in IT systems, the number of employees directly and indirectly involved in AML has significantly raised. New positions were created both in the AML department and in the KYC-EDD team as part of the first line of defence. The data analysis capabilities in AML/CTF area are enhanced by the new position of a data-analyst and new recruitments are planned for 2021.

AML/CTF Governance structure

Supervisory Board
- Adopts AML Policy
- Supervisory role

Management Board
- Adopts AML procedures and Risk Assessment
- Sets Risk Appetite
- Accepts high risk customers

High Risk Customer Acceptance Committee
- Acceptance of high risk customers

Financial Intermediaries Assessment Committee
- Assessment of Financial Intermediaries prior Management Board

AML Committee
- Provides information to Management Board
- Advises on risk assessment and appetite

First Line of Defence		Second Line of Defence		Third Line of Defence
Customer relations	**High Risk Customer Department**	**AML Department**	**Compliance**	**Internal Audit**
• Implementation of KYC	• On-boarding higher risk clients • Liaison to AML department • EDD measures and data quality	• Coordinates AML procedures and processes • Risk assessment of higher risk factors • AML monitoring and screening • Coordinating EDD measures • Reports to the board and FIU	• Advises management bodies on AML compliance • Performas AML inspections and compliance audits • Reports to governing bodies	• Carries out independent assessment of AML measures • Reports to Supervisory Board and Audit Committee

AML/KYC measures

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

- strong on-boarding CDD supported by the Customers Acceptance Principles;
- conservative approach towards the risk segmentation;
- regular CDD and EDD;
- robust risk-based monitoring;
- screening customers and transactions against international financial sanctions lists and other similar lists (incl. UN and EU lists, but also US OFAC list and UK HM Treasury list);
- strong commitment of the senior and middle managers;
- regular training of employees;
- ongoing communication and cooperation with FIU and other relevant stakeholders;
- active participation in setting up industry best practices.

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

- The Customer Relationship Manager.
- The Customer Relationship Manager together with a senior manager (so called 4-eyes principle).
- Risk Customer Acceptance Committee.
- The Management Board.

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

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Banking Services

LHV is providing services to FinTech companies that provide financial services to their customers. Compared to servicing regular customers, different risks are involved in servicing the FinTech companies. Therefore, LHV has paid special attention to and applied additional measures to mitigating the risks related to the FinTech companies. LHV has dedicated Customer Relationship Managers with vast FinTech sector competence. The AML team constantly monitors trends, developments and threats related to the FinTech sector and updates KYC measures accordingly. LHV applies the same AML/KYC measures to all customers from the FinTech sector as to the correspondent service provider. LHV expects FinTech customers have same level of AML/KYC measures in place as banks do. During the on-boarding process and continuous KYC of the FinTech companies, LHV assesses their business model, ownership structure, team and managers, AML/KYC measures, technical capabilities for screening and monitoring, customer focus, customer risk segmentation, limit policy, source of funds, etc. LHV carries out regular on-site visits to ensure that the appropriate policies, processes and procedures are in place and are working as intended. LHV pays special and continuous attention to the financial activities of the FinTech companies through robust monitoring.

Estonian AML system and perspectives

Several money-laundering allegations have shaken Estonia in recent years causing a severe damage to the reputation of Estonia abroad. Nevertheless, the Estonian financial system and the country itself is deemed to be one of the least risky countries in world. In 2020 the Basel Institute on Governance ranked Estonia as the least risky country from the money laundering risks perspective. Even if some financial institutions have historically failed to set proper KYC and risk mitigating measures which correspond to their risk appetite, the Estonian AML system in general is assessed to be strong. The next significant evaluation of the Estonian AML system against the FATF standards is planned to be carried out by Moneyval in 2021-2022. New version of National Risk Assessment will be introduced

The Estonian regulator, FIU and financial sector have taken the AML situation very seriously and a lot of different steps have been taken to improve the Estonian AML system in all aspects. The banking sector has heavily invested in human capital both in quantitative terms and from the competence perspective. All market participants are continuously improving the usage of modern information technology (incl. machine learning) in relation to AML in order to improve their technical and analytical capabilities. From a regulatory point of view, many legislative initiatives are ongoing and aimed at improving the Estonian AML system and cooperation between all stakeholders.

Control activities

In 2020 FSA carried out two on-site inspections in LHV. The first inspection focused on the risk assessment and risk appetite framework implemented by LHV. The second inspection was targeted to due diligence measures applied to the FinTech companies as financial intermediaries. As a result of both inspections, LHV initiated an action plan to enhance the areas where shortcomings were detected.

In 2020 LHV used a UK compliance company FsCom to assess its AML/KYC compliance framework and practice. No serious deficiencies were identified and minor proposals were implemented to enhance the processes.

3.9. Other risks

3.9.1 Strategic and business risk

Strategic risk is expressed mainly in wrong strategic decisions. Strategic risk is mitigated through well-considered business plans and analyses. In addition, members of both LHV Pank's and LHV Group's management (both Management Board and 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.

3.9.2 Risk on reputation

Risk on reputation is defined as a risk, which arises from a loss of reputation for clients, business partners, owners, investors or supervisors. Risk on reputation is usually a result from realization of other risks (for example operational risk or strategic risk). In order to mitigate the risk on reputation, LHV regularly carries out risk management trainings and also the framework of risk management is constantly improved which will provide a strong risk culture.

3.9.3 Country risk

Similarly to the risk on reputation, the country risk is usually expressed through another risk (operational risk, credit risk, strategic risk). In addition to Estonia, LHV is conducting business activities in the United Kingdom.

3.10. Offsetting assets and liabilities

The group has offset the following assets and liabilities.

				Related arrangements not set off in the statement of financial position		
31.12.2020	Gross amounts before offsetting in the statement of financial position	Offsetting	Net amount of exposure presented in the statement of financial position	Financial instruments	Cash collateral received	Net amounts
ASSETS						
Derivatives	89	0	89	0	0	0
LIABILITIES						
Derivatives	221	0	221	0	0	0

31.12.2019						
ASSETS						
Derivatives	4	0	4	0	0	0
LIABILITIES						
Derivatives	8	0	8	0	0	0

NOTE 4 Significant management estimates and assumptions

In accordance with IFRS, several financial figures presented in the financial statements are strictly based on critical accounting estimates and assumptions made by management, which affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities presented in the financial statements at the end of the reporting period, and the reported amounts of income and expenses of subsequent reporting periods. Although these estimates have been made to the best of management's knowledge and their judgement of current events, the actual outcome may ultimately not coincide with them and may significantly differ from these estimates. Management's estimates have been applied to valuation of loans, receivables and investments (Notes 3.2, 8, 9, 10 and 11).

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 reported prospectively.

The most significant management estimates and assumptions are related with the financial instrument standard IFRS 9, namely the criteria for SICR, calculation of PD and LGD, business model and SPPI assessment for classification of financial assets. Please see more information in Note 3.2 and below. There were no significant other changes in management estimates and assumptions in 2020.

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 expert based judgement in order to determine ECLs. The objective of applying expert based judgement is to incorporate the estimated impact of factors not captured in the modelled ECL. The degree of judgement that is required to estimate expected credit losses depends on the outcome from calculations, materiality and the availability of detailed information. The models, assessment and assumptions are regularly reviewed by the risk organisation of the Group and approved by the Group Risk Committee.

NOTE 5 Net interest income

Interest income *(in thousands of euros)*	Note	2020	2019
Interest income using effective interest calculation			
Corporate loans		46 834	37 130
incl. loans to related parties	22	31	28
incl. stage 3 interests*		129	164
Hire-purchase		3 708	3 968
Consumer loans		8 314	7 240
Leveraged loans and lending of securities		753	500
Credit card loans		849	813
From balances with credit institutions and investment companies		33	270
Mortgage loans		18 170	5 248
incl. loans to related parties	22	34	34
Private loans		2 109	´1 744
incl. loans to related parties	22	7	7
Other loans		3 710	891
Subtotal		**84 480**	**57 804**
Other similar interest income			
Leasing		4 329	3 253
incl. loans to related parties	22	4	3
From debt securities		-435	356
incl. debt securities at FVOCI		-	-
incl. debt securities at fair value through profit or loss	10	-435	356
Subtotal		**3 894**	**3 609**
Total		**88 374**	**61 413**
Interest expense			
Deposits from customers and loans received		-7 569	-5 579
From balances with central bank		-5 966	-4 265
Subordinated debt	18, 22	-5 792	-3 654
Total		**-19 327**	**-13 498**
Net interest income		**69 047**	**47 915**

Interest income of loans by customer location (interests from bank balances and debt securities not included):	2020	2019
Estonia	88 776	60 787
Total	**88 776**	**60 787**

*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 6 Net fee and commission income

Fee and commission income *(in thousands of euros)*	2020	2019
Security brokerage and commission fees	4 825	3 658
Asset management and related fees	3 662	2 962
Currency exchange fees	3 418	1 867
Fees from cards and settlements	15 226	12 485
Other fee and commission income	4 021	3 185
Total	**31 152**	**24 157**
Fee and commission expense		
Security brokerage and commission fees paid	-1 062	-546
Expenses related to cards	-4 722	-3 979
Expenses related to acquiring	-4 498	-3 967
Fees related to consumer loans and hire-purchase paid	-635	-674
Other fee expense	-1 852	-2 183
Total	**-12 769**	**-11 349**
Net fee and commission income	**18 383**	**12 808**

Fee and commission income by customer location:	2020	2019
Estonia	31 152	24 157
Total	**31 152**	**24 157**

NOTE 7 Operating expenses

(in thousands of euros)	2020	2019
Wages, salaries and bonuses	**16 159**	**13 078**
Social security and other taxes*	**4 956**	**3 964**
Total staff costs	**21 115**	**17 042**
IT expenses	2 986	2 509
Information services and banking services	961	823
Marketing expenses	1 434	1 799
Office expenses	638	598
Transportation and communication costs	266	263
Training and travelling expenses of employees	299	647
Other outsourced services	2 528	2 104
Other administrative expenses	3 263	3 220
Depreciation	2 417	2 802
Operating lease payments	41	246
Other operating expenses	317	464
Total other operating expenses	**15 150**	**15 475**
Total operating expenses	**36 265**	**32 517**

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

The average number of employees working for the Group in 2020 was 465 (2019: 405).

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NOTE 8 Due from central bank, credit institutions and investment companies

(in thousands of euros)	31.12.2020	31.12.2019
Demand and term deposits with maturity of less than 3 months*	180 047	37 720
Statutory reserve capital at central bank	41 253	26 426
Demand deposit from central bank*	2 171 958	1 206 307
Total	**2 393 258**	**1 270 453**
* cash and cash equivalents in the statement of cash flows	2 352 005	1 244 027

Distribution of receivables by countries is presented in Note 3.2.

Mandatory banking reserve as at 31.12.2020 was 1% (2019: 1%) of all financial resources collected (deposits from customers and loans received). The reserve requirement is to be fulfilled as a monthly average in euros or in the foreign securities preapproved by the central bank. See also note 3.3.1, 3.3.3 and 3.4 for additional information.

NOTE 9 Equity instruments at fair value through other comprehensive income

(in thousands of euros)	
Equity instruments 31.12.2018	**298**
Revaluation of equity instruments	134
Equity instruments 31.12.2019	**432**
Equity instruments sold	-432
Equity instruments 31.12.2020	**0**

As of 31.12.2019 the Group has VISA shares in the amount of EUR 432 thousand. The balance of other reserves in equity as at 31.12.2019 was EUR 212 thousand, see also Note 19. During the accounting period VISA shares were sold. See also note 3.2 and 3.3.3 for additional information.

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NOTE 10 Investments in debt and equity securities

Mandatory measurement as fair value through profit or loss:	**31.12.2020**
Shares and fund units	142
Debt securities	322 699
Foreign exchange forwards	89
Total financial assets	**322 930**
Interest rate swaps and foreign exchange forwards	221
Total financial liabilities	**221**

Mandatory measurement as fair value through profit or loss:	**31.12.2019**
Shares and fund units	164
Debt securities	32 331
Foreign exchange forwards	4
Total financial assets	**32 499**
Interest rate swaps and foreign exchange forwards	8
Total financial liabilities	**8**

Financial assets at fair value through profit or loss 31.12.2018	**38 913**
Net changes of investment securities at fair value through profit or loss	-6 311
Interest income (Note 5)	356
Revaluation	-459
Financial assets at fair value through profit or loss 31.12.2019	**32 499**
Net changes of investment securities at fair value through profit or loss	289 533
Negative interest income (Note 5)	-435
Revaluation	1 333
Financial assets at fair value through profit or loss 31.12.2020	**322 930**

Bid price is the fair value of investments in the case of publicly listed securities (Note 3.6). In 2020, a gain of EUR 865 thousand (2019: EUR 86 thousand) was recognised on the revaluation of bonds. Loss was obtained from the revaluation of interest rate swaps in 2020 and in 2019. Interest income from bonds is recognised in interest income. See also note 3.2, 3.3.1, 3.3.3 and 3.4 for additional information.

NOTE 11 Loans and advances to customers

(in thousands of euros)	31.12.2020	31.12.2019
Loans to legal entities	**1 367 540**	**954 970**
incl. corporate loans	1 192 803	815 740
incl. leasing	102 297	66 060
incl. overdraft	30 338	31 193
Incl. trade finance	20 497	32 761
incl. leveraged loans	5 551	3 148
incl. credit cards and hire-purchase	519	679
incl. apartment association loans	7 135	-
incl. credit letters	8 400	5 389
Loans to individuals	**858 141**	**738 168**
incl. hire-purchase	14 294	16 121
incl. mortgage loans	695 204	587 855
incl. consumer loans	52 202	49 424
incl. private loans	50 264	44 776
incl. leasing	26 554	23 427
incl. leveraged loans	6 366	2 840
incl. credit card loans	7 232	7 263
incl. overdraft	23	34
incl. study loan	974	749
incl. real estate leasing	5 027	5 679
Total	**2 225 681**	**1 693 138**
incl. related parties (note 22)	4 096	3 290
Impairment provisions	-16 858	-6 104
Total	**2 208 823**	**1 687 034**

In 2019 LHV purchased from Danske Bank Estonian Branche retail portfolio, increasing the retail loan portfolio by EUR 393 million, from which 97% were mortgage loans. In 2020 LHV purchased from Danske Bank Estonia Branche corporate portfolio, increasing the portfolio by EUR 254 million.

In 2020, the average effective interest rate of new consumer loans issued to individuals was 16-20%.The average effective interest rate for hire-purchase was around 17.3%, credit cards 20% and leasing 3.38%. 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. See also note 3.2.2, 3.3.3 and 3.4 for additional information.

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Changes in impairments in 12M 2020 *(in thousands of euros)*	Corporate loans incl. overdraft, factoring, apartment association loans, trade financing	Consumer loans, incl credit cards, hire-purchase	Leveraged loans	Leasing	Private loans incl. mortgage, overdraft, study loan, real estate leasing	Total
Balance as at 1 January	**-3 819**	**-789**	**-6**	**-639**	**-851**	**-6 104**
Impairment provisions/reversals set up during the year	1 714	534	2	235	528	3 013
Written off during the reporting period	-11 344	-923	-21	-981	-498	-13 767
Balance as at December 31 2020	**-13 449**	**-1 178**	**-25**	**-1 385**	**-821**	**-16 858**

Changes in impairments in 12M 2019 *(in thousands of euros)*						
Balance as at 1 January	**-9 035**	**-735**	**-3**	**-467**	**-36**	**-10 276**
Impairment provisions/reversals set up during the year	7 544	583	1	253	28	8 409
Written off during the reporting period	-2 328	-637	-5	-424	-843	-4 237
Balance as at December 31 2019	**-3 819**	**-789**	**-6**	**-639**	**-851**	**-6 104**

Impairment losses accumulated during the year differ from the amount of impairment losses recognised in the statement of profit or loss, that have been written off earlier as uncollectible claims. These receipts were recorded among impairment losses in the statement of profit or loss.

Net and gross investments on finance leases according to remaining maturity	Gross investment	Unearned future interest income	Impairment loss provision	Present value of lease payments receivable
up to 1 year	43 519	-4 009	-413	39 097
1-5 years	89 314	-6 325	-899	82 100
over 5 years	9 865	-2 128	-83	7 654
Total as at 31.12.2020	**142 698**	**-12 462**	**-1 385**	**128 851**
up to 1 year	26 375	-2 710	-164	23 501
1-5 years	68 211	-4 395	-457	63 359
over 5 years	2 753	-107	-18	2 628
Total as at 31.12.2019	**97 339**	**-7 212**	**-639**	**89 488**

For credit risk exposures and loan collateral, see Note 3.2. Distribution of loans granted by currencies is disclosed in Note 3.3.

Distribution of loans granted by maturity is disclosed in Note 3.4.

The geographical distribution of loans granted is disclosed in Note 3.2.

For interest income on loans granted, see Note 5.

NOTE 12 Receivables from customers

(in thousands of euros)	31.12.2020	31.12.2019
Asset management fees from customers	1 203	222
Other fees for providing services to customers	1 242	2 523
Payments in transit	9	0
Total	**2 454**	**2 745**

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. See also note 3.2, 3.3.1 and 3.4 for additional information.

NOTE 13 Other assets

(in thousands of euros)	31.12.2020	31.12.2019
Financial assets		
Guarantee deposits of Baltic stock exchanges	15	10
Guarantee deposits of MasterCard and VISA	2 058	2 236
Subtotal	**2 073**	**2 246**
Non-financial assets		
Prepayments to Financial Supervision Authority	592	399
Other prepayments *	1 351	1 458
Subtotal	**1 943**	**1 857**
Total	**4 016**	**4 103**

* Prepayments include office rent, insurance, communication services, periodicals and training.

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

See also note 3.2, 3.3.1 and 3.4 for additional information.

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NOTE 14 Tangible and intangible assets

(in thousands of euros)	Tangible assets	Right-of-use assets	Total tangible assets	Intangible assets	Total
Balance as at 31.12.2018					
Cost	4 072	0	4 072	4 495	8 567
Accumulated depreciation and amortisation	-2 950	0	-2 950	-3 209	-6 159
Carrying amount 31.12.2018	**1 122**	**0**	**1 112**	**1 286**	**2 408**
Changes in 2019:					
Purchase of non-current assets	1 336	0	1 336	747	2 083
Non-current assets sold	-15	0	-15	0	-15
Changes in accounting policies	0	5 676	5 676	0	5 676
Write-off of non-current assets	-338	0	-338	-1 436	-1 774
Depreciation/amortisation charge	-555	-899	-1 454	-1 348	-2 802
Balance as at 31.12.2019					
Cost	5 055	5 676	10 731	3 806	14 537
Accumulated depreciation and amortization	-3 152	-899	-4 051	-3 121	-7 172
Carrying amount 31.12.2019	**1 903**	**4 777**	**6 680**	**685**	**7 365**
Changes in 2020:					
Purchase of non-current assets	1 636	0	1 636	794	2 430
Write-off of non-current assets	0	-230	-230	0	-230
Depreciation/amortisation charge	-773	-972	-1 745	-672	-2 417
Balance as at 31.12.2020					
Cost	6 691	5 446	12 137	4 600	16 737
Accumulated depreciation and amortization	-3 925	-1 641	-5 566	-3 793	-9 359
Carrying amount 31.12.2020	**2 766**	**3 805**	**6 571**	**807**	**7 378**

Tangible assets include computer technology and office equipment, furniture, capitalized costs of office renovation. Intangible assets include licenses, client contracts and development costs.

In 2020 and 2019, there was no indication of impairment of tangible and intangible assets. See also note 3.4 for additional information.

NOTE 15 Deposits from customers and loans received

31.12.2020
(in thousands of euros)

	Individuals	Financial intermediates	Legal entities	Public sector	Total
Demand deposits	745 304	1 043 509	1 447 554	420 460	3 656 827
Term deposits	256 764	10 118	194 403	22 017	483 302
Loans received	0	0	268 442	200 000	468 442
Accrued interest liability	1 208	0	230	6	1 444
Total	**1 003 276**	**1 053 627**	**1 910 629**	**642 483**	**4 610 015**
incl. related parties (Note 22)	1 791	0	19 527	0	21 318

31.12.2019

	Individuals	Financial intermediates	Legal entities	Public sector	Total
Demand deposits	525 938	376 068	1 279 219	20 293	2 201 518
Term deposits	415 349	0	90 100	3 100	508 549
Loans received	0	0	25 643	0	25 643
Accrued interest liability	2 692	0	196	3	2 891
Total	**943 979**	**376 068**	**1 395 158**	**23 396**	**2 738 601**
incl. related parties (Note 22)	1 308	0	14 755	0	16 063

AS LHV Pank concluded an unsecured 10-year loan agreement with the European Investment Fund (EIF) in the amount of EUR 12.5 million to increase the credit facilities of small and medium-sized enterprises. As at 31.12.2020, the loan amount taken into use by the Bank amounted to EUR 12 250 thousand and the Bank repaid the principal in the amount of EUR 3 604 thousand. The outstanding balance as at 31.12.2020 is EUR 8 646 thousand. As at 31. 12.2020, the Bank has received EUR 20 000 thousand loan from Nordic Investment Bank (NIB) and repaid the principal in the amount of EUR 8 889 thousand. As at 31.12.2020 the balance of the loan received from (NIB) is EUR 11 111 thousand. NIB loan will be fully repaid in 2023.

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 Note 3.3.

Distribution of deposits from customers and loans received by maturity is presented in Note 3.4.

Distribution of deposits from customers and loans received by geography and risk concentration is presented in Note 3.2.

NOTE 16 Accounts payable and other liabilities

Financial liabilities *(in thousands of euros)*	31.12.2020	31.12.2019
Trade payables	575	4 872
Other short-term financial liabilities	5 591	3 067
Accrued interest on subordinated loans (Note 18)	489	4 672
Lease liabilities (Note 17)	3 394	429
Payments in transit	10 952	7 395
Financial guarantee contracts issued	397	178
Subtotal	**21 398**	**20 613**
Non-financial liabilities		
Prepaid expenses	239	324
Performance guarantee contracts issued	299	266
Tax liabilities	1 624	1 094
Payables to employees	1 881	1 477
Subtotal	**4 043**	**3 161**
Total	**25 441**	**23 774**

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. See also note 3.4 for additional information. Accrued Income tax calculated on future dividends in the amount of EUR 2 416 thousand is included in other short term

NOTE 17 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. In 2020, the operating lease payments, i.e leases subject to low value items and short-term, for office premises were in the amount of EUR 125 thousand (2019: EUR 327 thousand).

As of 01.01.2019 the future non-cancellable lease payments in the amount of EUR 4 512 thousand were discounted at the Group's incremental borrowing rate of 3.75%. As a result the Group's total assets in the statement of financial position as at 01.01.2019 increased 4 042 thousand euros and liabilities increased 4 042 thousand euros. During the year 2020 EUR 315 thousand was deducted from right-of-use assets and lease liability which was related to the new lease properties. The right of use assets balance as of 31 December 2020 is disclosed in the Note 14. The lease liability is disclosed in the Note 16. Interest expense on lease liabilities was EUR 144 (2019: 81) thousand and the depreciation of the right of use assets was EUR 972 (2019: 899) thousand (Note 14). The repayments of principal of lease liabilities in 2020 were EUR 963 (2019: 1003) thousand.

NOTE 18 Subordinated debts

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. The balances of subordinated debt as at the end of each reporting period is disclosed in the table below.

Subordinated bonds issued in 2015 in the amount of EUR 7 000 thousand were redeemed in 2020.

In May 2016, subordinated bonds were issued totaling EUR 5 000 thousand carrying rate of interest at 6.50%. The due date of the bonds is 29 July 2026.

In 2017, no subordinated bonds were issued or redeemed.

In December 2018, subordinated bonds were issued totaling 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 totaling 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 totaling EUR 10 000 thousand (due date 30.09.2030) carrying a rate of interest at 7.0%.

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

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

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

Subordinated debt
(in thousands of euros)

Subordinated debt as at 31.12.2018	**30 000**
Subordinated bonds issued	48 500
Subordinated bonds redeemed	-8 000
Subordinated debt as at 31.12.2019	**70 500**
Subordinated bonds issued	25 000
Subordinated bonds redeemed	-7 000
Subordinated debt as at 31.12.2020	**88 500**

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 liabilities are accounted in the statement of financial position using the effective interest rate.

Accrued interest on subordinated debts
(in thousands of euros)

Accrued interest on subordinated debts as at 31.12.2018	**150**
Interest calculated for 2019 (Note 5)	3 654
Paid out during 2019	-3 375
Accrued interest on subordinated debts as at 31.12.2019	**429**
Interest calculated for 2020 (Note 5)	5 792
Paid out during 2020	-5 732
Accrued interest on subordinated debts as at 31.12.2020	**489**

See also note 3.3.3 and 3.4 for additional information.

NOTE 19 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 23.4% of the voting rights and Andres Viisemann who owns 9.7% of the voting rights in AS LHV Group have significant influence over the company (31.12.2019: 23.7% and 9.8%, 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 31.12.2019: EUR 25 million and EUR 100 million, respectively). The share capital is paid in full through cash contributions. In 2020, the share capital of AS LHV Pank was increased by EUR 11 million and in 2019 by EUR 26 million through a cash contribution by the sole shareholder AS LHV Group. The bank's share capital increased to EUR 106.5 million by the year-end 2020.

As at 31.12.2020, the adjusted unconsolidated retained earnings of the Group amounted to EUR 98 249 thousand (31.12.2019: EUR 65 775 thousand). Thus, as at 31.12.2020 it is possible to pay out dividends in amount EUR 78 764 thousand (2019: EUR 52 723 thousand) and the related income tax charge would be EUR 19 485 thousand (2019: EUR 13 052 thousand). If the dividends were to be paid, the Group's capital adequacy would remain compliant.

	31.12.2020	31.12.2019
Share capital *(EUR thousand)*	**106 500**	**95 500**
Number of shares (pcs)	106 500 000	95 500 000
Par value of a share	1 EUR	1 EUR

In 2014, the General meeting of shareholders of AS LHV Group approved the criteria for the granting of share options to the Management Board members and equivalent employees and department managers and equivalent employees of group companies that are part of AS LHV Group. The aim of issuing share options is to align the interests of Management Board members and employees more effectively with the interests of shareholders and customers. Another objective is to offer a system of compensation on the labor market that is equal to competitors and comprehensive. The share options were issued in 2019 and in 2020.

In 2020, share options were granted to seven members of the Management Board of AS LHV Pank and ninety employees in the total amount of EUR 2 119 thousand. In 2019, share options were granted to seven members of the Management Board of AS LHV Pank and seventy-one employees in the total amount of EUR 1 786 thousand. The company entered into share option agreements with the members of the Management Board and employees for a three-year term for the granting of share options. Share options can be exercised after the expiry of a three-year period.

Share options issued in 2016 were exercised in 2019, when shares with nominal value of EUR 1 could be acquired for EUR 3.0 per share. In total, the former and current employees of the Group noted 195 703 shares. Share options issued in 2017 were exercised in 2020, when shares with nominal value of EUR 1 could be acquired for EUR 4.65 per share. In total, the former and current employees of the Group noted 279 362 shares.

Share options issued in 2018 can be exercised between the period of 01.04.2021-30.04.2021 and shares with nominal value of EUR 1 can be acquired for EUR 5.33 per share. Share options issued in 2019 can be exercised between the period of 01.04.2022-30.04.2022 and shares with nominal value of EUR 1 can be acquired for EUR 4.90 per share. Share options issued in 2020 can be exercised between the period of 01.04.2023-30.04.2023 and shares with nominal value of EUR 1 can be acquired for EUR 5.96 per share.

Statutory reserve capital in equity is composed of:

(EUR thousand)

Statutory reserve capital as at 31.12.2018	**2 191**
Transferred from 2018 net profit	834
Statutory reserve capital as at 31.12.2019	**3 025**
Transferred from 2019 net profit	997
Statutory reserve capital as at 31.12.2020	**4 022**

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NOTE 20 Assets under management

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

(in thousands of euros)	31.12.2020	31.12.2019
Cash balance of customers	7 938	9 967
Securities of customers	**2 058 404**	**1 554 796**
incl. parent company (Note 22)	202 300	169 050
incl. shareholders of the parent company and related entities (Note 22)	306 625	195 914
Total	**2 066 342**	**1 564 763**

Asset management fees for the management of these assets have been in the range of 0.015 – 0.025 % p.a. (for respective income, see Note 6).

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 21 Contingent assets and liabilities

Non-cancellable agreements	Performance guarantees	Financial guarantees	Letters of credit	Unused loan commitments	Total
Liability in contractual amount 31.12.2020	15 217	36 492	8	413 818	**465 535**
Liability in contractual amount 31.12.2019	11 078	14 139	10	359 230	**384 457**

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 2019-2020. The Group's management estimates that in 2021 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

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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 expressed at the amounts guaranteed is as follows:

According to sectors

(in thousands of euros)	31.12.2020	31.12.2019
Construction	9 302	6 429
Water supplies	950	1 001
Manufacturing	1 879	1 045
Professional, scientific and technical activities	523	1 307
Other areas at activities	2 563	1 297
Total	**15 217**	**11 078**

According to internal ratings

(in thousands of euros)	31.12.2020	31.12.2019
5 low credit risk	1 878	300
6 low credit risk	4 228	4 206
7 medium credit risk	2 267	4 054
8 medium credit risk	1 630	779
9 heightened credit risk	1 220	603
10 high credit risk	414	268
11 high credit risk	218	0
13 non-satisfactory rating	0	9
Non-rated	3 362	859
Total	**15 217**	**11 078**

Performance guarantees are over-collateralised as at each reporting date. Therefore, the Group has not borne any losses from performance guarantee contracts neither in 2020 nor in previous period. See also note 3.2 and 3.4 for additional information.

NOTE 22 Transactions with related parties

In preparing the 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

(in thousands of euros)	Note	2020	2019
Interest income	**5**	**76**	**37**
incl. management		76	37
Interest expenses	**5**	**5 803**	**3 662**
incl. management		4	1
incl. parent company		5 786	3 654
incl. shareholders, related entities and close relatives that have significant influence		13	7
Fee and commission income	**6**	**13**	**22**
incl. management		7	5
incl. shareholders, related entities and close relatives that have significant influence		6	17

Balances

(in thousands of euros)	Note	31.12.2020	31.12.2019
Loans and receivables as at the year-end	**11**	**4 096**	**3 290**
incl. management		2 153	2 085
incl. shareholders, related entities and close relatives that have significant influence		1 943	1 205
Deposits and loans received as at the year-end		**21 318**	**16 063**
incl. management	15	626	283
incl. parent company	18	11 240	7 075
incl. shareholders, related entities and close relatives that have significant influence	15	9 452	8 705

The table provides an overview of the material balances and transactions involving related parties. All other 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 31.12.2020 and 31.12.2019, the management did not have term deposits and the interest rate on demand deposits corresponds to the terms applicable to customers.

The subordinated loans received in 2015 were redeemed during 2020. The subordinated debt received in 2016-2019 have the interest rate of 6.5%. The subordinated debt received in 2020 has the interest rate of 7.0%. Tier 1 subordinated debt received 2019 and 2020 have the interest rate of 9.5%.

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

In 2020, salaries and other compensations paid to the management of LHV totaled EUR 1 057 thousand (2019: EUR 1 009 thousand), including all taxes. The Management Board of the Bank had seven members in 2019 and 2020. Starting from the beginning of 2021 the Management Board of the Bank has 6 members. As at 31.12.2020, the remuneration for December and accrued holiday pay in the amount of EUR 60 thousand (as at 31.12.2019: EUR 57 thousand) is reported as a payable to management (Note 16). The Group did not have any long-term payables or commitments to the members of the Management Board and the Supervisory Board as at 31.12.2020 and 31.12.2019 (pension liabilities, termination benefits, etc.). In 2020 and 2019, 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 20. See also Note 5, 6, 11, 15 and 18 for additional information.

NOTE 23 Subsidiary

As at 31.12.2020, 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% of ownership in LHV Finance and a non-controlling interest paid EUR 175 thousand of monetary contribution for 35% of 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 are the summarized financial information for each subsidiary that has non-controlling interests that are material to the Bank. The information disclosed is the amount before inter-company eliminations.

Summarized statement of financial position *(in thousands of euros)*	**AS LHV Finance** 31.12.2020	31.12.2019
Loans and advances to customers and other current assets	65 804	65 415
Non-current assets	45	91
Current liabilities	1 808	1 966
Non-current liabilities	45 970	48 582
Total net assets	**18 071**	**14 958**

Summarized statement of profit or loss and other comprehensive income *(in thousands of euros)*	**AS LHV Finance** 2020	2019
Net interest and fee & commission income	10 215	9 446
Profit before income tax	7 979	7 318
Income tax expense	-826	-760
Net profit	**7 153**	**6 558**
Total comprehensive income	7 153	6 558
Profit and other comprehensive income allocated to non-controlling interests	2 089	2 296

Summarized statement of cash flows *(in thousands of euros)*	**AS LHV Finance** 2020	2019
Cash flows from operating activities	9 411	-4 925
Interest paid	-1 899	-1 636
Income tax paid	-826	-760
Net cash from/(used in) operating activities	**6 686**	**-7 321**
Net cash from/(used in) investing activities	0	-87
Net cash from/(used in) financing activities	-6 684	7 403
Net increase/(decrease) in cash and cash equivalents	**2**	**-5**
Cash and cash equivalents at the beginning of the year	0	5
Cash and cash equivalents at the end of the year	**2**	**0**

NOTE 24 Income tax expense

The Bank is calculating 14% advance income tax. Advance corporate income tax for the year 2020 was EUR 4 740 thousand (2019: 2 517 thousand).

(in thousand of euros)	2020	2019
Advance corporate income tax	4 740	2 517
Income tax paid on dividends	826	760
Income tax calculated on future dividends	1 183	0
Total income tax expense	**6 749**	**3 277**

NOTE 25 Operating segments

Bank divides its business activities by 3 main business segments: retail banking, financial intermediates and corporate banking. The business segments form LHV Pank Group, with a separate access to financial data and which are subject to regular monitoring of operating result by the Group's decision-maker. The full planning and KPI setting is done on segments level. For each of the segment full statement of financial position and profit and loss statement is prepared. In addition to these high-level segments, Group has planning/measurement on department level.

Grouping is done based on the client/product base, where similar departments are grouped under one segment.

Retail banking segment covers all private individuals and small legal entities with credit exposure under EUR 500 thousand. This is the regular universal banking segment offering payments, cards, credits etc.

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.

Hire-purchase and consumer finance unit in Estonia is separate legal entity covering small loan business to private individuals. These portfolios are relatively small, but due to clients different payment history these segments have to be looked separately.

Financial intermediates cover fintech companies with large volume of payments both in Estonia and in United Kingdom. Under that segment LHV reports also regular payment services.

Other activites include treasury activities through providing internal bank function to segments. Assets and liabilities are disclosed in a way how it is reported to the management of the Bank, ie the treasury function investments and fundings are allocated to other segments, but some of the interest income and expense are allocated to treasury. This is, eliminated with intra-segment eliminations.

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

The revenue of a reported segment is based on the revenue per financial statements and includes gains from transactions between the segments, i.e. loans granted by AS LHV Pank to other group companies. The division of interest income and fee and commission income by customer location has been presented in Notes 5 and 6. The Group does not have any customers, whose income would account for more than 10% of the corresponding type of revenue.

31.12.2020 *(in thousands of euros)*	Retail banking	Corporate banking	Hire-purchase and consumer finance in Estonia	Financial intermediates	Other activities	Intra-segment eliminations	Total
Interest income	28 867	44 659	12 022	941	4 706	-2 821	88 374
Interest expense	-2 072	-6 246	-1 880	0	-11 950	2 821	-19 327
Net interest income	**26 795**	**38 413**	**10 142**	**941**	**-7 244**	**0**	**69 047**
Fee and commission income	8 284	1 000	708	21 160	0	0	31 152
Fee and commission expense	-1 042	-44	-635	-11 032	-16	0	-12 769
Net fee and commission income	**7 242**	**956**	**73**	**10 128**	**-16**	**0**	**18 383**
Net income	**34 037**	**39 369**	**10 215**	**11 069**	**-7 260**	**0**	**87 430**
Net gains from financial assets	**-50**	**-1**	**0**	**17**	**911**	**0**	**877**
Administrative and other operating expenses, staff costs	-13 213	-7 691	-1 703	-9 588	-3 862	0	-36 057
Operating profit	**20 774**	**31 677**	**8 512**	**1 498**	**-10 211**	**0**	**52 250**
Impairment losses on loans and advances	-976	-9 363	-533	-26	0	0	-10 898
Income tax	-1 825	-2 394	-826	-521	-1 183	0	-6 749
Net profit	**17 973**	**19 920**	**7 153**	**951**	**-11 394**	**0**	**34 603**
Total assets 31.12.2020	**1 722 042**	**3 050 474**	**65 851**	**147 604**	**0**	**-47 112**	**4 938 859**
Total liabilities 31.12.2020	**2 172 121**	**1 274 941**	**47 778**	**1 274 941**	**0**	**-45 604**	**4 724 177**

31.12.2019 *(in thousands of euros)*	Retail banking	Corporate banking	Hire-purchase and consumer finance in Estonia	Financial intermediates	Other activities	Intra-segment eliminations	Total
Interest income	18 907	35 107	11 209	752	6 825	-11 387	61 413
Interest expense	-3 723	-6 071	-1 691	-10	-13 390	11 387	-13 498
Net interest income	**15 184**	**29 036**	**9 518**	**742**	**-6 565**	**0**	**47 915**
Fee and commission income	6 754	2 147	602	14 654	0	0	24 157
Fee and commission expense	-502	-363	-674	-9 797	-13	0	-11 349
Net fee and commission income	**6 252**	**1 784**	**-72**	**4 857**	**-13**	**0**	**12 808**
Net income	**21 436**	**30 820**	**9 446**	**5 599**	**-6 578**	**0**	**60 723**
Net gains from financial assets	**-10**	**-4**	**0**	**46**	**173**	**0**	**205**
Administrative and other operating expenses, staff costs	-10 895	-7 661	-1 881	-9 114	-2 790	0	-32 341
Operating profit	**10 531**	**23 155**	**7 565**	**-3 469**	**-9 195**	**0**	**28 587**
Impairment losses on loans and advances	-1 194	-1 736	-247	-33	0	0	-3 210
Income tax	-803	-1 640	-760	-74	0	0	-3 277
Net profit	**8 534**	**19 779**	**6 558**	**-3 576**	**-9 195**	**0**	**22 100**
Total assets 31.12.2019	**1 075 705**	**1 613 557**	**65 506**	**298 806**	**0**	**-48 943**	**3 004 631**
Total liabilities 31.12.2019	**1 992 547**	**450 089**	**50 548**	**388 317**	**0**	**-48 618**	**2 832 883**

NOTE 26 Separate 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 financial statements.

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

(in thousands of euros)	2020	2019
Interest income	78 232	51 895
Interest expense	-19 327	-13 498
Net interest income	**58 905**	**38 397**
Fee and commission income	30 444	23 555
Fee and commission expense	-12 134	-10 675
Net fee and commission income	**18 310**	**12 880**
Net gains from financial assets measured at fair value	3 493	2 356
Foreign exchange rate gains/losses	43	79
Net gains/losses from financial assets	**3 536**	**2 435**
Other income	1 048	171
Administrative and other operating expenses	-35 402	-30 631
Operating profit	**46 397**	**23 252**
Impairment losses on loans and advances	-10 365	-2 963
Profit before income tax	**36 032**	**20 289**
Income tax expense	-4 740	-2 517
Profit for the year	**31 292**	**17 772**
Other comprehensive income/loss:		
Items that may be reclassified subsequently to profit or loss:		
Changes in the fair value of debt instruments measured at FVOCI	0	0
Items that will not be reclassified to profit or loss:		
Net gains on investments in equity instruments designated at FVOCI	0	134
Total profit and other comprehensive income for the year	**31 292**	**17 906**

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Statement of financial position of the parent

(in thousands of euros)	31.12.2020	31.12.2019
Assets		
Due from central bank	2 213 211	1 232 733
Due from credit institutions	170 060	32 247
Due from investment companies	9 985	5 473
Equity instruments at fair value through other comprehensive income	0	432
Financial assets at fair value through profit or loss	322 930	32 499
Loans and advances to customers	2 189 287	1 670 533
Receivables from customers and other financial assets	5 082	4 723
Other assets	1 907	1 828
Subsidiaries	325	325
Tangible assets	2 766	1 903
Right-of-use assets	3 805	4 777
Intangible assets	762	594
Total assets	**4 920 120**	**2 988 067**
Liabilities		
Deposits from customers and loans received	4 610 015	2 738 601
Financial liabilities at fair value through profit or loss	221	8
Accounts payable and other liabilities	23 267	21 844
Subordinated debt	88 500	70 500
Total liabilities	**4 722 003**	**2 830 953**
Equity		
Share capital	106 500	95 500
Statutory reserve capital	4 022	3 025
Other reserves	0	212
Retained earnings	87 595	58 377
Total equity	**198 117**	**157 114**
Total liabilities and equity	**4 920 120**	**2 988 067**

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Statement of cash flows of the parent

(in thousands of euros)	2020	2019
Cash flows from operating activities		
Interest received	76 980	50 635
Interest paid	-20 714	-10 664
Fees and commissions received	30 444	23 555
Fees and commissions paid	-12 134	-10 675
Other income received	836	171
Staff costs paid	-18 349	-15 260
Administrative and other operating expenses paid	-11 428	-10 073
Income tax paid	-3 332	-2 476
Cash flows from operating activities before change in operating assets and liabilities	**42 303**	**25 213**
Net increase/(decrease) in operating assets:		
Net acquisition/disposal of trading portfolio	-64	49
Loans and advances to customers	-528 397	-767 006
Mandatory reserve at central bank	-14 827	-12 146
Security deposits	173	690
Other assets	-80	-511
Net increase/(decrease) in operating liabilities:		
Demand deposits of customers	1 455 310	871 616
Term deposits of customers	-25 248	390 754
Net loans received (including loan repayments)	442 799	4 114
Financial liabilities held for trading at fair value through profit or loss	212	-3
Other liabilities	-439	-6 393
Net cash from/(used in) operating activities	**1 371 742**	**506 377**
Cash flows from investing activities		
Purchase of tangible and intangible assets	-2 430	-1 979
Proceeds from disposal and redemption of investment securities	432	0
Net changes of investment securities at fair value through profit or loss	-286 875	8 722
Net cash from/(used in) investing activities	**-288 873**	**6 743**
Cash flows from financing activities		
Paid in share capital	11 000	26 000
Proceeds from subordinated debt	25 000	48 500
Subordinated debt redeemed	-7 000	-8 000
Dividends paid	-2 658	-2 230
Repayment of principal of lease liabilities	-1 278	-1 003
Net cash from financing activities	**25 064**	**63 267**
Effect of exchange rate changes on cash and cash equivalents	**43**	**79**
Net increase/(decrease) in cash and cash equivalents	**1 107 976**	**576 466**
Cash and cash equivalents at the beginning of the year	1 244 027	667 561
Cash and cash equivalents at the end of the year	**2 352 003**	**1 244 027**

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Statement of changes in shareholders' equity *(in thousands of euros)*	Share capital	Statutory reserve capital	Other reserves	Retained earnings	Total
Balance as at 01.01.2019	**69 500**	**2 191**	**78**	**42 330**	**114 099**
Paid in statutory reserve capital	0	834	0	-834	**0**
Paid in share capital	26 000	0	0	0	**26 000**
Dividends paid	0	0	0	-2 230	**-2 230**
Share options	0	0	0	1 339	**1 339**
Net profit for the year	0	0	0	17 772	**17 772**
Other comprehensive income	0	0	134	0	**134**
Net profit and other comprehensive income for 2019	0	0	134	17 772	**17 906**
Balance as at 31.12.2019	**95 500**	**3 025**	**212**	**58 377**	**157 114**
Carrying amount of holdings under control and significant influence	0	0	0	-325	**-325**
Value of holdings under control and significant influence under equity method	0	0	0	9 723	**9 723**
Adjusted unconsolidated equity as at 31.12.2019	**99 500**	**3 025**	**212**	**65 775**	**166 512**
Balance as at 01.01.2020	**95 500**	**3 025**	**212**	**58 377**	**157 114**
Paid in statutory reserve capital	0	997	0	-997	**0**
Paid in share capital	11 000	0	0	0	**11 000**
Dividends paid	0	0	0	-2 658	**-2 658**
Share options	0	0	0	1 581	**1 581**
Net profit for the year	0	0	0	31 293	**31 293**
Other comprehensive income	0	0	-212	0	**-212**
Net profit and other comprehensive income for 2020	0	0	-212	31 293	**31 081**
Balance as at 31.12.2020	**106 500**	**4 022**	**0**	**87 596**	**198 118**
Carrying amount of holdings under control and significant influence	0	0	0	-325	**-325**
Value of holdings under control and significant influence under equity method	0	0	0	10 978	**10 978**
Adjusted unconsolidated equity as at 31.12.2020	**106 500**	**4 022**	**0**	**98 249**	**208 771**

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

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Signatures of the Management Board to the consolidated annual report

The Management Board has prepared the management report and the consolidated financial statements of AS LHV Pank for the financial year ended on 31 December 2020. The consolidated financial statements present a true and fair view of the Bank's financial position, the results of operations and its cash flows.

17.02.2021

Kadri Kiisel
Chairman of the Management Board

Andres Kitter
Member of the Management Board

Indrek Nuume
Member of the Management Board

Jüri Heero
Member of the Management Board

Meelis Paakspuu
Member of the Management Board

Martti Singi
Member of the Management Board

Independent Auditors' Report

(Translation of the Estonian original)

To the Shareholder of AS LHV Pank

Report on the Audit of the Consolidated Financial Statements

Opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of AS LHV Pank and its subsidiary (collectively, the Group) as at 31 December 2020, 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.

What we have audited

We have audited the consolidated financial statements of the Group, which are set out on pages 35 to 120 of the consolidated financial statements, which comprise:

- the consolidated statement of financial position as at 31 December 2020,
- the consolidated statement of profit or loss and other comprehensive income,
- the consolidated statement of cash flows for the year then ended,
- the consolidated statement of changes in equity for the year then ended, and
- the notes to the consolidated financial statements, comprising significant accounting policies and other explanatory information.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (Estonia) (ISAs (EE)). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Group in accordance with the ethical requirements of the Auditor's Activities Act of the Republic of Estonia and with the ethical requirements of the ethics standards for professional accountants as set out in the same act, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Audit Scope

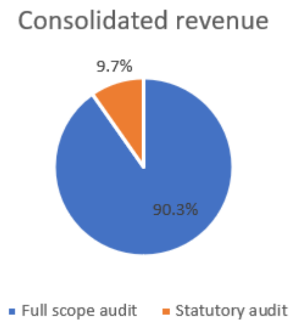
Because we are solely responsible for our audit opinion, we are also responsible for the direction, supervision and performance of the group audit. In this respect, we have determined the type of work to be performed for Group entities based on their financial significance and/or the other risk characteristics.

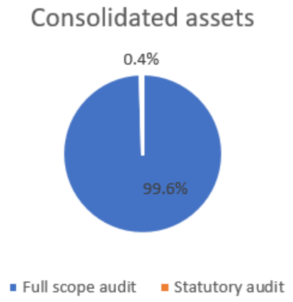
We, as Group auditors, determined only AS LHV Pank to be significant Group component and we subjected this component to a full scope audit.

We have used the results of statutory audit of financial statements of AS LHV Finance.

We also performed procedures over the consolidation process at Group level.

Coverage of the Group's consolidated revenue and consolidated total assets with procedures performed:





The audit work on the financial information of all Group components was performed by the Group audit team in Estonia.

By performing the procedures mentioned above over the Group entities, together with additional procedures at the Group level, we have been able to obtain sufficient and appropriate audit evidence to form an opinion on the consolidated financial statements as a whole.

KPMG

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 Note 3 „Risk management", Note 4 "Significant management estimates and assumptions", and Note 11 "Loans and advances to customers"	
The key audit matter	**How the matter was addressed in our audit**

As at 31 December 2020 loans and advances to customers amounted to EUR 2,208 million and related impairment loss for 2020 amounted to EUR 10.9 million. We focused on this area because of financial significance and also because the estimation of expected credit losses ("ECL") on financial instruments, involves significant judgement and estimates.
 	
ECL calculations are forward looking and probability-weighted. The key areas where we identified greater levels of management judgement and therefore increased levels of audit focus in the Group's estimation of ECLs are
 	
• Judgemental modelling is used to estimate ECL which involves determining Probabilities of Default ("PD"), Loss Given Default ("LGD"), and Exposures at Default ("EAD"). The PD models are the key drivers of complexity in the ECL and also impact the staging of assets and as a result are considered the most significant judgemental aspect of the Group's ECL modelling approach.
 	
• Economic scenarios – IFRS 9 requires the Group to measure ECLs 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
	In this area, we conducted, among others, the following audit procedures:
	
	• We 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 set under IFRS 9 by involving our valuation specialists.
	• We performed end to end process walkthroughs to identify the key systems, applications and controls used in the ECL calculation processes. We tested the relevant manual, general IT and application controls over key systems used in the ECL process.
	• In addition, we tested the design and operating effectiveness of the credit file periodic review and rating assessment, and monitoring of collateral controls for corporate loans.
	• We performed detailed testing over:
	  • the completeness and accuracy of data used in the ECL calculation system;
	  • the compliance of key inputs used in the ECL calculation system with IFRS 9 methodology;
	  • the accuracy and compliance of 12-month and lifetime ECL calculations with IFRS 9 methodology;
	  • the correctness of discounting in ECL model;

probability weightings applied to them especially when considering the current uncertain economic environment as a result of COVID-19. For defaulted corporate loans, an individual impairment is calculated based on the exposure and realisable value of the collateral at the balance sheet date and also requires significant management estimates.	• the accuracy and completeness of data used for staging of loans; • the correctness of applying the criteria to determine significant increase in credit risk; • the internal assignment of credit ratings for corporate loan customers, which serve as inputs into the corporate loan ECL model; • the correctness of information on collaterals and their values in the loan systems, which serve as an input into the ECL model; and • the completeness of loans subject to stage 3 assessment and related ECL calculations. • We have assessed the reasonableness of key assumptions made by management, which serve as critical inputs in the ECL model, such as weights of different scenarios, loan portfolio point in time PD estimate, key forecasts of macroeconomic information and weights used for different scenarios. We challenged the reasonableness of management estimates regarding ECL model inputs taking into account the uncertain economic environment caused by COVID-19 pandemic. • Furthermore, we assessed the adequacy of disclosures related to ECL.

Other Information

Management is responsible for the other information contained in the Group's consolidated annual report in addition to 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. 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.

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 the 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 judgment 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 Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, 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 Company 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, related safeguards.

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 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

We were first appointed by those charged with governance on 13 March 2019 to audit the consolidated financial statements of AS LHV Pank for the periods ended 31 December 2020 to 31 December 2022. Our total uninterrupted period of engagement has lasted for one year, covering the period ended 31 December 2020.

We confirm that our audit opinion is consistent with the additional report presented to the Audit Committee of the Group and 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.

Eero Kaup

Certified Public Accountant, Licence No 459

Tallinn, 3 March 2021

KPMG Baltics OÜ
Licence No 17

KPMG Baltics OÜ

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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 2020 as follows:

- transfer EUR 1 626 thousand to statutory reserve capital
- pay dividends in total amount of EUR 3 900 thousand
- transfer the profit for reporting period attributable to shareholders of the parent in the amount of EUR 26 988 thousand to the accumulated deficit.

Signatures of the supervisory board to the annual report

The Supervisory Board has reviewed the annual report, which consists of the management report and the financial statements, the independent auditor's report and the profit allocation proposal, and approved it for presentation at the General meeting of shareholders.

17.02.2021

Madis Toomsalu
Chariman of the Supervisory Board

Rain Lõhmus
Member of the Supervisory Board

Andres Viisemann
Member of the Supervisory Board

Tiina Mõis
Member of the Supervisory Board

Raivo Hein
Member of the Supervisory Board

Heldur Meerits
Member of the Supervisory Board

Allocation of income according to EMTAK classificators

EMTAK	Activity	2020	2019
66121	Security and commodity contracts brokerage	8 487	6 620
64191	Credit institutions (banks) (granting loans)	106 710	75 697
64911	Finance lease	4 329	3 253
	Total income	**119 526**	**85 570**