AS LHV Group
Group Annual Report 2022

(Translation of the Estonian original)

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

Legal name	**AS LHV Group**
Commercial Registry no.	**11098261**
Legal address	**Tartu mnt 2, 10145 Tallinn**
Phone	**(372) 6800400**
Fax	**(372) 6800410**
E-mail	**group@lhv.ee**

Main activities	**Banking** **Leasing and other lending** **Financial advisory** **Security brokerage** **Non-life insurance** **Activities of holding companies**
Financial year	**1 January – 31 December**
Management Board	**Madis Toomsalu** **Meelis Paakspuu** **Jüri Heero** **Martti Singi**
Supervisory Board	**Rain Lõhmus** **Andres Viisemann** **Tiina Mõis** **Heldur Meerits** **Raivo Hein** **Tauno Tats** **Sten Tamkivi**
Shares	**Listed on the Nasdaq Tallinn Stock Exchange**
Auditor	**KPMG Baltics OÜ**

Company's consolidated financial statements in pdf-format without European Single Electronic Format (ESEF) markups. The original document is submitted in machine-readable .xhtml format to the Nasdaq Tallinn Stock Exchange and digitally signed:

link: https://nasdaqbaltic.com/statistics/en/instrument/EE3100102203/reports

Mandatory elements of the European Single Electronic Format (ESEF) core taxonomy

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

Table of contents

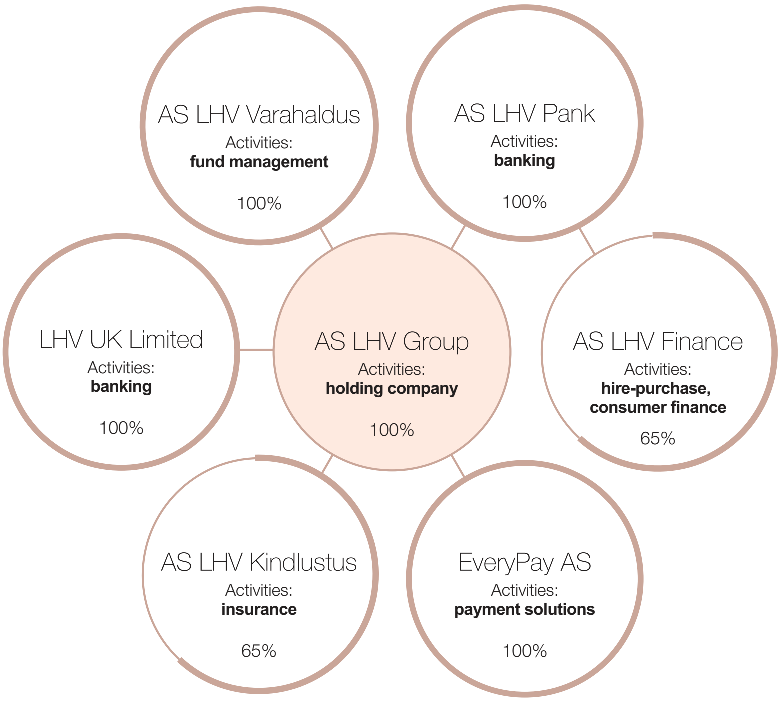
Management report

LHV at a glance

Group overview

AS LHV Group (also the Group, LHV Group or LHV) is the biggest domestic finance group and capital provider in Estonia. The main subsidiaries of AS LHV Group are AS LHV Pank (also the Bank or LHV Pank), LHV UK Ltd (LHV UK), AS LHV Varahaldus (LHV Varahaldus), AS LHV Kindlustus (LHV Kindlustus) and EveryPay AS (EveryPay). LHV was established in 1999 by people with extensive experience in investing and entrepreneurship. LHV's customer service offices in Estonia are in Tallinn, Tartu and Pärnu. Since 2018, LHV has widened its geographical coverage and entered the UK market. LHV has three offices there: in London, Leeds and Manchester.

LHV employs more than 850 people. Over 377,000 customers use LHV's banking services and LHV's pension funds have over 170,000 customers.



Operating principles

LHV concentrates on active and independent customers with an entrepreneurial mindset. Our service range is diverse. For private customers, we have high-quality universal banking services. For corporate customers, we have flexible and customised financing solutions as well as assistance in daily financial operations.

The products and services provided by LHV are simple, transparent and practical. We interact with our customers mainly through modern electronic communication channels. This helps us save on costs and keep the prices of our everyday services affordable.

LHV was created as a partnership and the concept of partnership is central to growing LHV's business. New initiatives will be implemented faster and more successfully if partners share the same interests and support each other in the long term.

LHV is a public company listed on the Tallinn Stock Exchange since May 2016. Thus, all our customers and partners have an opportunity to become LHV's owners.

Vision and mission

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

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

Our long-term goal is to build strong relationships with all stakeholders by being:

- the best financial services provider for customers;
- the most supportive financial services provider for international financial intermediaries;
- an attractive employer that offers high job satisfaction, development opportunities and self-fulfilment for current and prospective employees;
- a transparent company that delivers at least 20% return on equity per year for investors; and
- a company with the best management practices, positive social impacts and clear climate goals for society.

Main risks

- The biggest risk for LHV as a traditional banking group is credit risk, which accounts for 90.4% of our total risk weighted assets (RWA). Credit risk arises mainly from loan operations.
- The second-biggest risk for LHV is operational risk, which accounts for 8.7% of total RWA. Operational risk is the risk of loss arising from inadequate or failed internal processes, people and information systems, or from external events.
- Market risk accounts for 0.9% of the Group's total RWA. Market risk arises from LHV's positions which are exposed to changes in interest rates, foreign exchange rates and securities prices.
- While LHV's capitalisation is solid, especially taking profitability into account, the Group still sees the need for increasing its capitalisation levels over the coming years by 1%.

LHV keeps a very high liquidity profile, because part of its customer base activities is more volatile.

Letter from the CEO

Dear reader

Western society had barely managed to declare the pandemic over when it was replaced by war, the resultant energy crisis, steep price increases and tightening monetary policy.

The rapid increase in prices has caused the Estonian economy to decline. The eurozone countries and the United Kingdom also have to consider the risk of an economic downturn. All over Europe people are facing the same problems. All the basic everyday expenses have risen and many cost increases are still to hit people's accounts. The price increases in Estonia have been some of the most acute in Europe and have caused an overall decline in purchasing power. Confidence has decreased among companies across different sectors of the economy.

Due to the persistently large gap between inflation and interest rates, the latter are expected to continue increasing. Price stability is the European Central Bank's only mandate. In conditions of high inflation, financing becomes more expensive. Still, the change should be considered as normalisation, as the era of zero interest rates has been an anomaly and created fundamentally false expectations.

For banks, a stricter monetary policy entails an increase in interest income. However, the situation is not one-directional, as the decline in confidence among consumers and companies compounded with increasing costs will affect the decisions of home buyers and the investment plans of companies. The end of the formerly loose monetary policy is also forcing banks to again to strive for deposits. This will lead to smaller growth rates, increasing risks and growing deposit costs. In well-managed banks, however, the increase in income can be expected to exceed the increase in expenses.

The capital requirements for banks are also on the increase. It has to be admitted that understanding capital requirements is becoming ever more difficult for investors and forecasting the development of the requirements is becoming harder. There are many invisible factors involved and so the capital requirements for banks often consist largely of various buffers, the methodology of which the banks do not understand in detail. The complexity of the system has increased and the movement towards apparent order but systemic disorder is one of long-term risks for banks.

For instance, several new types of regulatory buffers have been introduced, some of them have been added into and some on top of the capital requirements. LHV's regulatory capital requirements have increased approximately 40% over the past ten years.

2023 will be the hardest year to forecast for LHV. Growth in loan volumes must be forecast against a backdrop of the last decade's most rapidly changing economy, employment and prices, while the increase in expenses is related to loan losses, an increase in salaries, deposit costs and regulatory expenses. LHV UK is working towards a banking licence, but has already started its lending activities through internal financing and a successful purchase of assets in 2022. The results and performance fee of pension funds depends on the development of the markets and the insurance business wishes to make a development leap. The cost of capital is growing and raising capital is more time-sensitive and expensive than before.

In saying this, we are heading into the year with a strong foundation and, as usual, strong internal confidence. We have always focused on the most important thing – creating conditions for the future. Strong results are the outcome of well-planned expectations. Our people, our customers and our shareholders as well as the long-term sustainability of our business activities are the most important. In this light, 2022 was a good year.

LHV was named both the best and most desirable employer in 2022. Our internal satisfaction surveys continue to show very good results. LHV Pank earned the title of both the best bank and the bank with the best services. This brought us an additional 81,000 new customers. We were able to fulfil the promise given to our shareholders regarding the financial plan, regardless of the impairment of a financial investment that took place during the year. LHV's loan portfolio grew by 20% in 2022 and despite the contradictory economic environment we managed to successfully raise capital on several occasions.

During the year, LHV made a significant development leap in the area of sustainability, paying more attention to the assessment of the impact of our business activities. Financial institutions have an important role to play here and LHV has made a firm commitment to comply with the principles of sustainability. We wish to reduce our negative impact on the natural environment and contribute to creating a positive social impact. As we can only control what we can measure, we have prioritised measuring the climate impact of our business activities more accurately and moving towards clear goals. In order to do this, we are increasing the awareness of both our customers and employees.

We are entering 2023 under the direct supervision of the European Central Bank. We believe that this is a step forward. The European banking sector has been one of the economic sectors with the lowest yield in the past decade, and a large number of banks are still trading under the book value. Europe needs an example of an innovative bank whose profitability derives from good cost-effectiveness and a high-quality loan portfolio. This is possible in Estonia and we are keen to prove the same in the United Kingdom.

Several of LHV's underlying principles are timeless. We have not tried to go along with the adventurist business environment, although there have been temptations at times. Our fundamental belief that with the best people we can offer the best experiences to our customers and in turn the best yield for our shareholders will also see us overcoming any bumps in the road ahead.

Madis Toomsalu

Chairman of the Management Board of AS LHV Group

Summary of the year 2022

For LHV the year 2022 was characterised by a changing environment and slowing economy. However, we and our customers' activities grew to higher levels than ever before.

LHV Pank

2022 was a complicated year due to a rapidly changing environment. In many areas the tailwind changed to a headwind several times during the year. All in all, the number of customers, loan portfolio, regular customer deposits, customer activity and net income increased. Only financial intermediaries' deposits decreased. The Bank has a strong position and is profitable.

LHV UK

The subsidiary is still in the process of obtaining a licence, which is expected to be received in Q1 2023. The largest business transaction was acquiring the loan portfolio from Bank North and starting from 2023, the company is providing loans to SMEs. After receiving licence, the company will take over the financial intermediaries' business from LHV Pank.

LHV Varahaldus

In 2022 securities markets dropped more than predicted, reducing the possibility of earning a success fee, especially taking into account the 20% inflation rate increasing the reference index. LHV Varahaldus has managed to offer the best return for pension investors in 2022 and in the long term. Moreover, LHV's actively managed pension funds were the only ones in the Estonian market with positive returns in 2022.

LHV Kindlustus

The central topic was finalising the product range and increasing sales. In 2022 LHV Kindlustus started cooperation with the largest insurance brokers in Estonia. Being a small company, the results have also been affected by one-off larger insurance cases.

EveryPay AS

In April 2022, LHV Group acquired 100% of EveryPay AS (EveryPay) shares. After the acquisition, EveryPay's focus has been on developing new payment methods and supporting the Group's strategic goals.

2022 in numbers

- **LHV share price** decreased from EUR 43.2 (after the split EUR 4.32) to 3.34, still outperforming the market indexes.
- **The number of bank customers** increased by 56,500 (+18% YoY) and the number of customers with an investment contract by 20,000 (+17% YoY). LHV managed to increase its role as the leader of the Estonian investment services market already in the second half of 2021, which is supported by a focus on providing a full range of services.
- **Total consolidated assets** of the Group were EUR 6.1 billion at the end of 2022, which is a 10% annual decline due to a decrease in the deposits of financial intermediaries.
- **The loan portfolio** increased by EUR 531 million to EUR 3.2 billion (+20% YoY). Retail loans grew by 22% and loans to corporates by 17%. In Q3, LHV acquired Bank North's loan portfolio in the amount of GBP 17 million. The quality of the loan portfolio stayed at its historically highest levels.
- **The volume of deposits** decreased to EUR 4.9 billion (-16% YoY), of which EUR 1.0 billion is attributable to financial intermediaries' deposits which were abnormally high at the end of 2021 due to high prices of crypto assets. Regular customers' deposits grew by EUR 60 million (+2%).
- **Assets under management** decreased by EUR 17 million to EUR 1.3 billion (-1% YoY) mainly due to market downturns.
- **The volume of custody accounts** decreased due to lower market prices by EUR 537 million and reached EUR 3.3 billion.
- **Net profit** was at a record-high level of EUR 61.4 million, an increase of EUR 1.2 million compared to last year. It was mainly positively affected by the growing loan portfolio together with increasing market interest rates.

Business environment

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

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

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

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

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

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

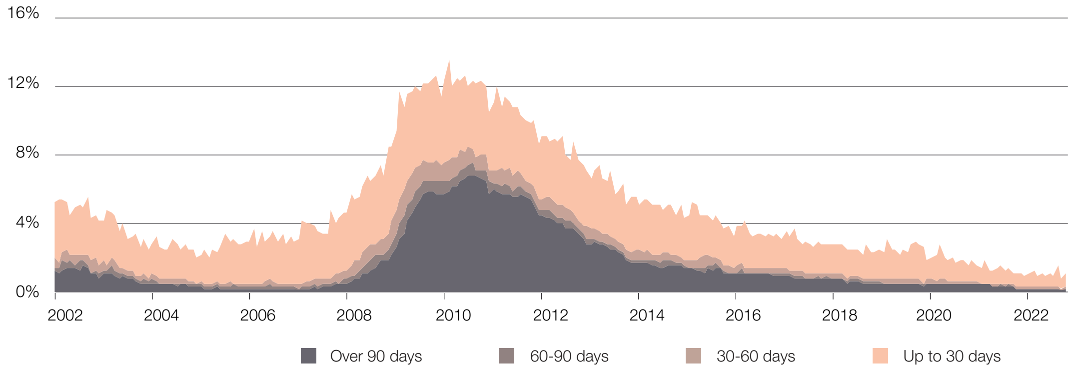
Estonia's growth already came to a standstill at the beginning of 2022, and from then on, the quarter-on-quarter comparison only showed a decline. While Estonia's economy was one of the best performers in Europe in 2021, last year was the opposite. As a result of the loss of confidence brought about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

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

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

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

Market average share of overdue loans in loan portfolio, %



Source: Bank of Estonia

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

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

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

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

Sources: Bank of Estonia, Statistics Estonia

Strategy and financial plan

1. Strategy and the future

LHV's home markets are Estonia and the UK. What both these markets strategically have in common is our ability to build technological solutions regardless of customers or locations. Our aim is to maximise growth based on pre-defined risks, our level of capitalisation and a 20% return on equity. This means that despite our strong ambitions we do not wish to grow at the expense of profitability and risk limits.

We see LHV as an international financial group that offers the best level of service, regardless of the customer group, from mobile banking to customer service offices. In fulfilling our plans, five main companies are included in the group: besides the bank and the asset management, insurance and payment services company, there is also a separate bank in the UK.

LHV Pank aims to become the largest and most profitable bank in Estonia by 2032, and second largest by 2027. We have made efforts for LHV Pank to have as strong a service and product offering as possible to ensure growth. In Estonia, we are now able to essentially finance all companies and our decisions are made promptly and locally. We are able to issue home loans all across Estonia, making decisions quickly and with additional terms and conditions suitable for the customer. We also offer free of charge payments, the most comprehensive investment service, the possibility to invest in crypto assets, payment collection services to companies, insurance solutions and pension funds with a good long-term yield. We are able to provide a large part of our services – including trading in securities, private loan applications and finalising loan contracts – via our mobile app.

For private customers, we are placing an emphasis on growing our customer base and increasing the activity of our customers. We are focusing on Estonian cities where we wish to engage active customers who prefer electronic channels. We wish to attract customers who settle their transactions and whose salary is paid into LHV and who use an LHV bank card for their everyday financial affairs. We are focussed on growing our home loan market share.

In the case of companies, we are focusing on growing the loan portfolio. We are seeking to attract customers who value a substantive understanding of their business activities and a financing structure based on that. We will continue with one-tier decision-making, which means that all the decisions are made locally, promptly and flexibly. We will also continue with our multi-year project of capital accounting based on internal ratings, the aim of which is to improve the return on equity through the efficient distribution of capital.

In the UK, we are focusing on obtaining a banking licence and then building our lending activities. The plans of LHV UK are based on three areas: banking services for financial intermediaries, loans to companies and services to e-businesses. LHV has already started to offer financing to SMEs, with loan amounts starting from GBP 500 thousand. To financial intermediary customers, we offer real-time euro and sterling payments via our application interface LHV Connect. We also continue to offer various accounts, making and receiving payments, and currency services. Our offices are in London, Manchester and Leeds.

LHV Kindlustus aims to repeat the Bank's success. The goal of LHV Kindlustus is to be a domestic capital-based insurer whose products are simple, innovative and customer friendly and who is able to offer these via different channels.

The pension funds managed by LHV Varahaldus prioritise the achievement of a strong long-term yield. We continue to implement our changed investment strategy, focusing more than before on finding listed companies and bond investments.

The business objectives related to the main business lines are disclosed in our long-term financial plan.

Our long-term goal is to offer strong relationships to our partners by being:

- a financial service provider with the best service for our customers;
- the most insightful financial service provider for international financial intermediaries;
- an attractive employer who offers people a high satisfaction level, development and self-realisation;
- a transparent company for investors, with an annual return on equity at least 20%;
- a company with the best management practices for society, positive social impacts, and climate goals.

LHV wishes to conduct its business activities in a sustainable manner. We understand that the financial sector has a central role in directing capital flows into sustainable activities in order to support the transition to a climate-neutral economy. We therefore plan to include even more ESG criteria in our credit decision-making process and to create a uniform system for ESG risk management. We thereby help guide companies towards more sustainable business activities and reduce business-related risks with regard to the changing world and natural environment. We have taken the first steps towards measuring the climate impact of our credit portfolio and investments, on the basis of which we will establish the goals of reducing our environmental and climate impact in the future.

2. Financial plan

As one of a very few listed companies LHV publishes a five-year financial plan every year. As the forecast horizon is long, only the first year should be taken as commitment, while the plan for the remaining four years serves as a guideline of where LHV sees its business developing over the next few years.

2.1 Assumptions behind the financial plan

There are several assumptions made, especially regarding the macro environment and interest rates.

The biggest assumption is about the macroeconomic situation, where we use Bank of Estonia and Ministry of Finance macro forecasts as a base for forecasting one year horizon. Currently these forecasts state around 0% or slightly negative GDP growth for the year 2023. In long term financial plan, we use modest growth scenario.

The second important assumption is regarding the interest rates, where we prepare our own forecast. We use market consensus as a base and add a conservative factor on these curves. We expect interest rates to increase to a 3% level in 2023 but to start lowering already by the end of the year and to stabilise slightly to above 2% through the rest of the forecasting horizon.

The third assumption is about competition, where in the long-term scenario we do not expect significant changes, no aggressive competitors entering nor leaving the market.

The year 2022 was affected by the war in Ukraine, which will have its effects also in the following years. The economic growth will be around zero in 2023 and some sectors will be negatively affected. Yet we expect that the credit portfolio will be well diversified and the economy will be flexible, and credit risk will appear through some individual counterparties.

The two main types of changes considered are the impending changes in legislation and market views on interest rates. There are no major changes in legislation, but the focus on ESG and higher capitalisation levels for banks is likely to increase even further.

2.2 Business areas

The plan is based on LHV's concept of four business areas

- Estonian banking
- UK banking
- Asset management
- Insurance

Estonian banking and asset management areas are solid already now. At the same time insurance is a relatively new business with high potential. UK banking consists of two different business lines, services to financial intermediaries and SME lending. UK banking is clearly in a start-up phase. LHV UK plans to receive a banking licence in late Q1 2023, after which we can start migrating products and customers from Estonian banking to UK banking. This process is planned to be completed by end of 2023, after which the business units' financial results should be more easily readable and entities should have a very clear focus.

2.3 Comments regarding financial results

Our income sources are broad-based. For some areas income is a function of different assets, for other areas a function of customer activity or the capital markets situation.

In 2023 LHV plans slow growth due to macroeconomic situation both in Estonia and Europe. The region is facing geopolitical instability and inflation is still high, which together increase the risk. Similarly, we expect very modest growth in capital markets - too low to earn success fees from asset management. Still, we expect that all business lines are profitable.

Starting from 2024 we see the macroeconomic situation more positively in all markets and then we plan to grow by 15-18% with the loan portfolio. Similarly, asset management, insurance and financial intermediaries business will grow.

The Estonian banking business line is affected mostly by macroeconomic trends and interest rates. Above 90% of capital is utilised by the credit portfolio, which indicates the largest risk in the business area. The portfolio is well diversified and capitalised, but if interest rates and inflation increase in correlation with a decreasing GDP, customer credit risk will increase, generating credit losses for the entity. Conversely, increasing GDP together with lowering inflation and still relatively high interest rates will significantly increase the business area profitability.

The profitability of UK banking is also mainly related to interest rates, but much less affected by changes in GDP. The effect is coming from deposit collection from financial intermediates, which are kept liquid and not used for funding.

The profitability of the asset management business line is mostly driven by the social tax paid to state budget in Estonia and returns of assets under management, which mostly correlates with capital markets.

Insurance as relatively new and small business line has not yet reached its potential. The business line is planned to become profitable in 2023. The profitability is not so much driven by the macroeconomic situation but more by one-off items, especially the occurrence of larger insurance cases.

2.4 Financial plan

Short version of financial plan figures is presented in table below.

Statement of profit or loss

EUR million	2023	2024	2025	2026	2027
Net interest income	216	234	238	276	321
Net fee and commission income	54	67	92	105	115
Other income	1	1	2	2	2
Total revenue	**270**	**302**	**332**	**383**	**438**
Total operating expenses	**-110**	**-123**	**-138**	**-155**	**-176**
Amortisation	-8	-9	-9	-8	-8
Impairment losses on loans and advances	-25	-31	-22	-25	-26
Earnings before income tax	**127**	**138**	**163**	**195**	**229**
Income tax	-2	-6	-8	-12	-21
Advance income tax	-17	-15	-17	-19	-22
Net profit	**108**	**117**	**138**	**165**	**187**
Profit attributable to non-controlling interest	1	2	5	6	8
Profit attributable to owners of the parent	107	115	133	159	178

Statement of financial position

EUR million	31 Dec 2023	31 Dec 2024	31 Dec 2025	31 Dec 2026	31 Dec 2027
Cash and cash equivalents	3,166	4,570	5,369	6,117	6,825
Financial assets at fair value	280	318	343	415	489
Loans granted (net)	3,428	3,933	4,627	5,433	6,305
Long-term financial investments	9	10	10	11	12
Other assets	75	78	91	101	110
Total assets	**6,958**	**8,909**	**10,440**	**12,077**	**13,740**
Deposits from customers	5,653	7,401	8,707	10,111	11,573
Loans received	520	584	653	700	772
Subordinated debt	137	152	172	222	217
Other liabilities	125	146	173	186	202
Total liabilities	**6,435**	**8,282**	**9,704**	**11,220**	**12,765**
Equity	**524**	**627**	**736**	**856**	**976**
Total liabilities and equity	**6,958**	**8,909**	**10,440**	**12,077**	**13,740**

Financial and operational ratios	2023	2024	2025	2026	2027
ROE from profit attributable to the owners of parent	23.3%	20.4%	20.2%	20.8%	20.4%
ROE from pre-tax profit attributable to the owners of the parent	27.4%	24.1%	23.9%	24.7%	25.3%
C/I	43.9%	43.9%	44.2%	42.5%	41.9%
L/D	60.6%	53.1%	53.1%	53.7%	54.5%
CoR	0.8%	0.8%	0.5%	0.5%	0.4%
EPS (EUR)	0.33	0.35	0.41	0.48	0.53
Dividend (EUR thousand)	12,617	22,397	40,945	54,520	76,510
DPS (EUR)	0.04	0.07	0.13	0.17	0.23
CET1	16.3%	17.0%	17.1%	16.9%	16.8%
T1	18.4%	18.8%	18.6%	18.5%	18.3%
CAD	21.5%	21.9%	21.9%	22.1%	21.3%

Ratios calculation principles

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

ROE (return on equity) from pre-tax profit attributable to the owners of parent = net profit before taxes (attributable to owners of the parent) / average equity (attributable to owners of the parent) * 100

C/I (cost to income ratio) = total operating expenses / total net income * 100

L/D (loan to deposit ratio) = net loans / deposits * 100

CoR (cost of risk) = impairment losses on loans / average loan portfolio

EPS (earning per share) = net profit (attributable to owners of the parent) / number of shares

Dividend = dividend payment during calendar year

DPS (dividend per share) = dividend payment during calendar year / number of shares at moment of payment

Capital adequacy levels are calculated in accordance with applicable requirements in Estonia

CET1 (common equity tier 1 capital adequacy ratio) = tier 1 common equity / risk weighted assets

T1 (tier 1 capital adequacy ratio) = tier 1 capital / risk weighted assets

CAD (total capital adequacy ratio) = (tier 1 capital + tier 2 capital) / risk weighted assets

2.5 Updates of the financial plan

LHV reviews the financial plan annually and publishes it in February. In general, there are no updates published during the year.

In case the actual results and a rolling forecast differ by more than 10% from the existing plan, LHV publishes an update to the current year financial plan but an update to long-term forecast is not published.

Sustainability report

1. Sustainability at LHV

1.1 Sustainability mission statement

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

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

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

1.2 CEO letter on sustainability

We are firm believers, that those who can adapt, will not only survive, but thrive under extraordinary, or unexpected circumstances. Recent years have tested economies, states, businesses, societies, and humanity in general. Peace and stability have claimed a newfound significance, as have success, sustainability, and resilience.

Changes in the natural as well as societal environment will become even more acute topics among people as well as businesses, becoming more evident in interpersonal relationships as well as in strategic boardroom discussions. Discussions will lead to decisions and decisions will have to, more than ever, be translated into clear action. For us, sustainability is not a matter of discussion, nor is it even a matter of philosophy. As years go by, it will even more prominently become an issue of practicality. Our aptitude for anticipating the future, understanding the implications it might bring as well as leveraging the opportunities change will bring about, will be emphasised by our confidence that trying times can and will catalyse remarkable strength when approached with positive opportunism and audacity. The sustainability mindset and integration of ESG principles into our business is just an example of understanding change and momentum.

Without flexibility, even the strongest of systems can break under the weight of their own scale and impact - be it people, organisations, states, or even the natural world around us. Resilience is the art of bending without breaking, and that’s why we’re keeping sustainability at the heart of everything we do.

2. Global sustainability frameworks

2.1 United Nations Environment Programme Finance Initiative Principles for Responsible Banking

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

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

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

Principle 1
Alignment

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

Principle 2
Impact & target setting

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

Principle 3
Clients & customers

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

Principle 4
Stakeholders

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

Principle 5
Governance & culture

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

Principle 6
Transparency & accountability

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

2.2 Partnership for Carbon Accounting Financials

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

The PCAF standard, which is in line with the GHG protocol, provides a consistent methodology for measuring and disclosing emissions from business activities, including those associated with corporate/business loans, commercial real estate loans, residential mortgages, motor vehicle loans, project finance and even the equity and bond positions that banks hold on their statements of financial position. This year we have estimated our climate impact in four asset classes: business loans, motor vehicle loans, commercial real estate loans and mortgages. The results are displayed in subsection 5.1.2 of Sustainability report.

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

2.3 Global Reporting Initiative

This sustainability report has been prepared in accordance with the widely used Global Reporting Initiative (GRI) Standards: Core Option. It includes a GRI Content Index located at the end of the Sustainability report. Using a standardised approach allows us to report to our stakeholders and the public on our impacts and activities in an even more structured and transparent way.

In this report, we have followed all the reporting principles of the GRI standards (GRI 101):

- stakeholder inclusiveness, sustainability context, materiality, and completeness for defining the scope of the report;
- accuracy, balance, clarity, comparability, reliability, and timeliness in ensuring the quality of the content.

We consider it essential to be more transparent and comprehensive in disclosing our sustainability information and therefore are open to feedback regarding our reporting methods and style. We are also preparing to comply with the emerging sustainability reporting requirements stemming from the Corporate Sustainability Reporting Directive (CSRD) which will apply to us from the beginning of 2025.

3. ESG strategy

3.1 Material ESG and sustainability topics

Our goal is to make an actual impact through the sustainability efforts we make. We devote our resources to addressing the environmental, social and governance (ESG) sustainability matters most affected by our business decisions.

With the help of UNEP FI Portfolio Impact Analysis Tool, we have identified our potential positive and negative environmental and social impacts arising from our business activities. Through engaging both internal and external stakeholder groups, as well as applying proper ESG management approach, we have determined the areas on which LHV has significant impact through its products and services.

Materiality and impact analysis findings

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

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

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

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

Working with our most material sustainability aspects contributes to these UN SDGs and their specific sub-targets

Sustainable Development Goal (SDG)	Specific SDG target to which LHV contributes	How LHV contributes?
SDG 1. End poverty in all its forms everywhere 1 NO POVERTY	1.2. By 2030, reduce at least by half the proportion of men, women and children of all ages living in poverty in all its dimensions according to national definitions 1.4. By 2030, ensure that all men and women, in particular the poor and the vulnerable, have equal rights to economic resources, as well as access to basic services, ownership and control over land and other forms of property, inheritance, natural resources, appropriate new technology and financial services, including microfinance	• Integrating social and environmental considerations into the core of our business. • Investing in spreading financial literacy.
SDG 7. Ensure access to affordable, reliable, sustainable, and modern energy for all 7 AFFORDABLE AND CLEAN ENERGY	7.1. By 2030, ensure universal access to affordable, reliable, and modern energy services 7.2. By 2030, increase substantially the share of renewable energy in the global energy mix	• Offering customers a choice of green financial products. • Improving processes of ESG-related due-diligence for corporate customers and partners.
SDG 8. Promote sustained, inclusive, and sustainable economic growth, full and productive employment and decent work for all 8 DECENT WORK AND ECONOMIC GROWTH	8.3. Promote development-oriented policies that support productive activities, decent job creation, entrepreneurship, creativity, and innovation, and encourage the formalisation and growth of micro-, small- and medium-sized enterprises, including through access to financial services 8.10. Strengthen the capacity of domestic financial institutions to encourage and expand access to banking, insurance, and financial services for all	• Driving sustainable growth, creating jobs, encouraging entrepreneurship, and fuelling innovation.
SDG 12. Ensure sustainable consumption and production patterns 12 RESPONSIBLE CONSUMPTION AND PRODUCTION	12.2. By 2030, achieve the sustainable management and efficient use of natural resources 12.6. Encourage companies, especially large and transnational companies, to adopt sustainable practices and to integrate sustainability information into their reporting cycle	• Considering environmental factors in business decisions. • Advocating for responsible lending and consumption.
SDG 13. Take urgent action to combat climate change and its impacts 13 CLIMATE ACTION	13.2. Integrate climate change measures into national policies, strategies, and planning 13.3. Improve education, awareness-raising and human and institutional capacity on climate change mitigation, adaptation, impact reduction and early warning	• Encouraging environmentally sustainable business practices within the sector and the State level through supporting sustainable financial sector development.

3.2 Stakeholder engagement

In LHV, we make sure to engage our stakeholders and external experts to ensure that we maximise the impact of our efforts within sustainability. Our stakeholders are the groups and individuals that LHV affects through its activities, and who, in turn, may affect LHV`s operations in the short or long run.

We hold a regular dialogue with the stakeholders with whom we have the most direct relations and with whom LHV could collaborate for better impact on the society. At the same time, we also keep in touch with the stakeholder groups that are part of shaping the trends and setting requirements for the financial market.

Table below outlines our major stakeholder groups, ways of their engagement and their major expectations to LHV.

Stakeholder groups	How we engage	Main expectations and key topics raised
Customers	Active communication and discussions, ESG questionnaire in credit application, green products, and services	Engagement, knowledge building, ESG integration into business and decision making
Employees	Annual survey, individual development and performance reviews, informative sustainability seminars	Feedback, engagement, internal capacity building
Shareholders	Annual shareholder meeting, active communication, ESG reporting	Profitability, engagement, feedback
Policy makers, regulators	Memberships in State level sustainability focused working groups, direct communication with government officials	Policy making input and information about EU legislation on the issues of sustainability and reporting
Business networks, financial sector	Active membership in Estonian Banking Association, Finance Estonia and Rohetiiger	Leadership in ESG promotion
Suppliers, cooperation partners	Direct communication	Sustainability integration into value chain
Sustainability organisations	Active membership in local sustainability focused initiatives and organizations, leading the ESG working group in Estonian Banking Association, member of UNEP FI PRB	Financing sustainable development, enabling green transition
Wider public and society	Active communication, public events and conferences, universities, press and media	Transparency, fair and ethical business conduct

Leadership for sustainable business development in Estonia

- LHV is a signatory to UNEP FI's Principles for Responsible Banking and an active member of several of its working groups.
- We lead the Estonian Banking Association's Sustainable Banking Committee.
- We are a founding member of Rohetiiger, a local initiative that contributes to improving local organisations' knowledge regarding environmental issues, maintains close contact with the state, and advises businesses on how to make the best environmental changes within the organisation and their supply chains
- We cooperate with other organisations on sustainability initiatives and regularly share our ESG journey with other businesses. Our management and ESG team members share our ESG experience at conferences and seminars and speak about the importance of moving towards a greener economy and more inclusive society.
- We cooperate with universities in spreading the word about sustainability in the financial sector.
- We continuously collaborate with external experts to better implement our ESG projects.
- We regularly engage with non-profit organisations and with the public sector.
- We hold seminars and workshops for or with other companies and organisations and talk about our progress, the importance of corporate sustainability and the future of green finance.

4. Management of ESG

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

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

4.1 ESG Steering Committee

Since 2021, we have an ESG Steering Committee, which serves as a high-level governing body for ESG issues in LHV Group. The committee follows the ESG policy adopted by the Supervisory Board of LHV Group. Its members include the Group CEO, the chairman of the Management Board of LHV Pank, the Chief Risk Officer of LHV Pank, the Chief Financial Officer of LHV Pank, the chairman of the Management Board of LHV Kindlustus, the chairman of the Management Board of LHV Varahaldus and the Head of ESG. It was launched to ensure the group-wide development and implementation of various ESG projects and processes so that all our objectives can be met. The committee also coordinates the flow of information on ESG projects, legislation and developments and advises members of the management of LHV's subsidiaries on ESG-related activities to keep them in line with LHV's business strategy, values, strategic ESG goals and best practices in ESG management. The meetings of the group-wide committee have taken place once a month but will be replaced with quarterly meetings from the beginning of January 2023.

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

4.2 Alignment with policies and procedures

Apart from adopting an ESG policy and a KPI roadmap, we have also made considerable improvements and additions to our credit policy and HR & remuneration policies as well as the ethics policy to support the implementation of sustainability principles and our ESG goals. LHV Varahaldus has adopted and follows a separate responsible investment policy for the management of pension funds. We are currently also reviewing and updating our risk policy and making ESG-related updates to other policies as well to integrate ESG even more on policy level.

We continue to use the ESG questionnaire as an integrated part of our credit application for our corporate customers onboarding process. Group-wide, we have approximately 10 ESG project streams currently running to integrate ESG into our business and operations. The project streams include policy implementation, KPIs and target setting, ESG data analysis, ESG governance structure, communications, ESG reporting standards, internal capacity building, credit granting processes, ESG compliance and regulatory gap analysis, portfolio and customer ESG assessment activities, financed emissions calculations, and ESG risk management framework development.

4.3 ESG risk management

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

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

4.4 Responsible investments

The principles of responsible investment are part of the investment analysis process at LHV. Apart from traditional factors such as fundamentals and valuation, the comprehensive analysis considers ESG factors, based on the sector and needs of each existing or new potential investment (considering the most relevant ESG risks of the company). We aim to generate sector-specific lists of material ESG issues. The sources for ESG information include periodic financial reports, ESG and sustainability reports, press releases, company management meetings, and other relevant publicly available information. To demonstrate leadership, LHV Varahaldus created Estonia's first green pension fund in 2020, and we regularly educate our customers and the public about the potential benefits of and the future of green investing. We believe that promoting and following the principles of sustainable investing is in the best long-term interests of our customers.

5. Management of impact areas

5.1 Environment

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

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

5.1.1 Green office operations

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

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

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

5.1.2 Our carbon footprint

For setting an action plan and targets for emission reductions, it is first necessary to identify and measure the GHG emissions of our business activities and to follow a standardised methodology in the process. We calculate our footprint based on the methodology provided by the Greenhouse Gas (GHG) Protocol Corporate Accounting and Reporting Standard, an internationally recognised and the most widely used greenhouse gas accounting standard. The results are expressed in CO2 equivalents, the universal greenhouse gas unit of measurement, indicating the potential for causing global warming.

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

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

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

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

In 2021, LHV's office activity had a greenhouse gas emission footprint of 1,444 tonnes of CO2-equivalent, which was 2.3 tonnes per employee at the time of calculation (see table below for more detailed overview). For 2022 the results were 1,968 tonnes, or 2.5 tonnes per employee. The main reason for the increase in our operational level CO2 footprint was due to increase in heating used for the Tallinn office as well as from the increase in plane trips taken for business purposes compared to the previous year where it was largely hindered due to the Covid-19 pandemic.

Emissions from own operations (GRI 305:2016)		2022	2021
	Scope 1	0	0
	Scope 2	567 tCO2e	445 tCO2e
	Scope 3 (excl. category 15)	1,400 tCO2e	999 tCO2e
	Total emissions from own operations	**1,968 tCO2e**	**1,444 tCO2e**
	GHG emissions intensity per FTE	2.48 tCO2e	2.28 tCO2e

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

Estimates of financed emissions

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

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

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

Financed emissions			2022
Scope 3 (Category 15 – investments)	**Type**	**tCO2 e**	**tCO2 e / EUR million**
	Business loans*	388,757	275.9
	Mortgages	88,490	82.8
	Commercial real estate	77,879	159.1
	Motor vehicles**	7,380	74.3
Total Scope 3 (Category 15 – investments)		**562,506**	

* Due to uncertainty scope 3 information is not available

**Emissions from passenger cars, busses, and trucks

Offsetting our carbon footprint locally through innovation

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

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

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

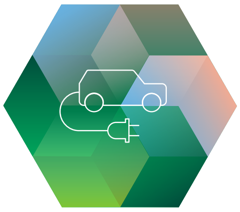
5.2 Sustainable products and services

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

Green Home Loan

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

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



Green 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. In line with a longer-term strategy and the desire to contribute to Estonia's climate objectives, LHV Pank has decided that LHV will no longer finance the purchasing of new diesel passenger cars from 2030 onwards.

Green hire-purchase

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

Green Investment Loan for Companies

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

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.

5.3 Social

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

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

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

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

5.3.1 Social responsibility

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

5.3.2 Financial literacy

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

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

5.3.3 Sponsorships

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

Estonian culture and society

- Estonian Music Days – for seven years now we have supported the Au-tasu prize for new Estonian music, which was awarded to Jüri Reinvere in 2022.
- Võnge Festival; concerts of Terminaator and Tommy Cash – we continued supporting the Estonian music scene.
- “Lotte ja vana õunapuu saladus” – we were the presenter sponsor for the biggest musical production for children in Estonia.
- “Arvo Pärt…and a Littlemore” festival in Oxford, UK – we helped the event promoting the Estonian composer in the UK.
- 32 community initiatives applied for support from the ‘Who does it?’ programme. The grants were given to Ristiküla community in Pärnu county and Viscosa Culture Factory in Hiiumaa.
- Through the charity function for LHV Pank (‘Micro donation’) we facilitated donations of more than EUR 120,000 to 13 charity organisations.
- “Charge yourself” programme – we were one of the initiators of the programme giving priority to teaching physics.
- Rakett69 – support to the TV show that popularises science among pupils.
- Cyber Battle of Estonia – a series of cyber hacking events aimed at young people.
- Kood/Jõhvi – we are one of the supporting partners of the new IT college in Ida-Virumaa county.
- LHV employees volunteered at Toidupank and Uuskasutuskeskus. In the upcoming year, we plan on carrying out at least one charity project quarterly.
- In 2022 we donated 66 computer sets to various schools and NGOs.

Sport & healthy lifestyle

- Estonian Football Association – LHV Pank has been the main sponsor of the Estonian Football Association and the Estonian national team since 2010. In addition, we supported football clubs with EUR 128,000 in 2022 through the LHV football card support system.
- Maijooks 2022 – LHV became the name sponsor of the biggest women’s health sports event in Estonia.
- Estonian Optimist Class Union – we support the development of Estonian sailing.
- Rally Estonia – we supported the World Rally Championship stage in Estonia for the third year.
- Simple Session – we were one of the main sponsors of the top extreme sports event for the third year.
- Estonian Biathlon Federation – we supported Estonian biathlon during the Olympic season, and the World Cup stage in Estonia.
- Estonian Ski Association - LHV Kindlustus became a supporter of Estonian skiing.

Estonian economy and business

- EY Estonian Entrepreneur of the Year competition – we have been one of the main sponsors since 2012.
- Young Entrepreneur Award – in cooperation with the Estonian Chamber of Commerce and Industry, we awarded the prize to Kristjan Lind.
- Conferences Business Plan, Investment Festival, Investor Toomas – in cooperation with Äripäev, we supported Estonia's leading business and investment conferences.
- Conference of Estonian Real Estate Association

- Nordic Testing Days 2022 – we supported the region's biggest conference for software testers.
- Latitude59 – we again were sponsors of the large startup meet up.

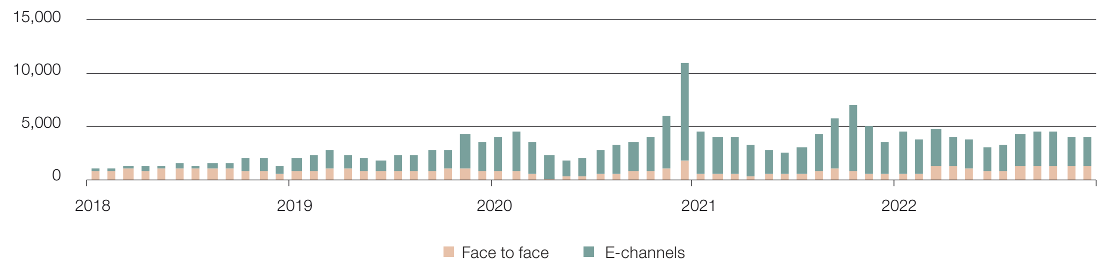
We also support smaller local initiatives with our knowledge, LHV's gifts, advice and the presence of our people. We work with universities. We are a member of the Estonian Information Technology and Telecommunications Association, the Estonian Chamber of Commerce and Industry and the Estonian Employers'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

5.3.4 Social impact through channels and customer experience

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

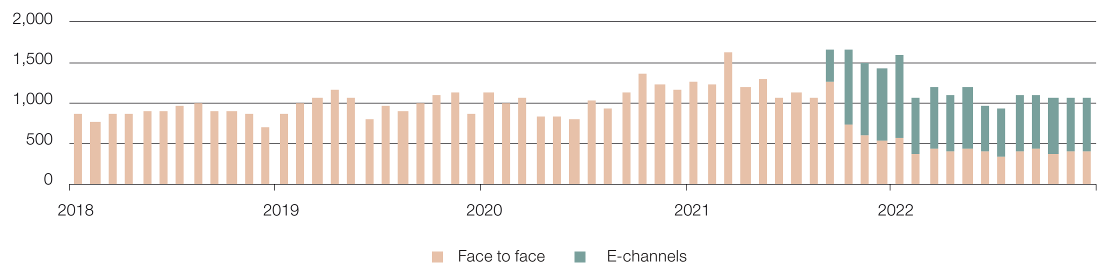
In 2022, we have onboarded an average of 5,100 new customers every month. Close to 70% of our new private customers open their bank accounts through our e-channels, either directly online or combining e-channels with face-to-face meeting with the bank representative. We have seen the percentage growing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

Identification upon onboarding of private persons



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

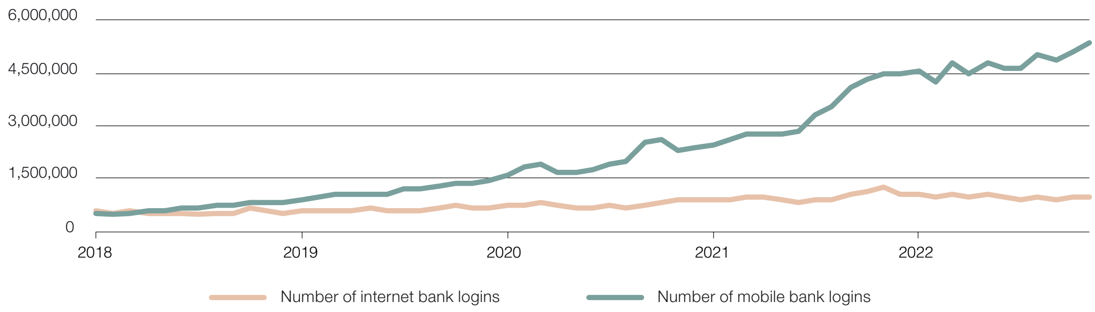
Identification upon onboarding of legal entities



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

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

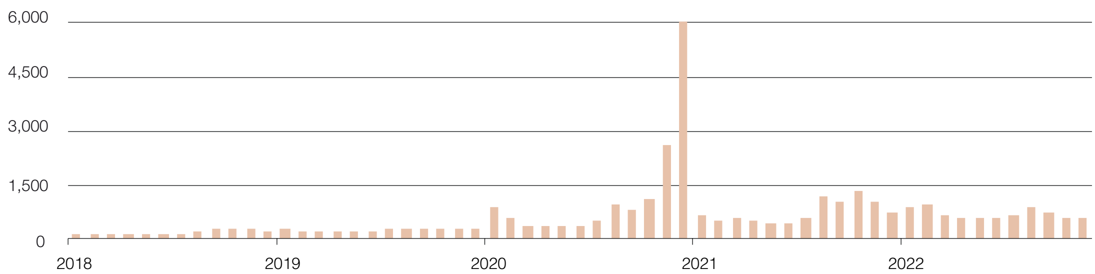
LHV internet bank and mobile bank usage activity



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

During 2022 LHV insurance services and product offering has expanded from insuring homes, cars and trips to equipment, machinery, warranty, and extended warranty insurance. All insurance applications and claims are submitted through our website or mobile app, keeping the ecological footprint minimal and customer satisfaction on a high level.

Number of new child accounts on monthly basis



Focus on customer experience

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

We keep promoting financial literacy. For that, we are developing an Assistant Budget Planner tool in our e-channel for customers to help them make smarter financial decisions. Also, LHV Financial Portal is being redesigned and restructured to provide even more details and insight into investing and saving. We aim to build a product that encourages customers to save money through gamification and goal setting techniques, while learning about the importance of investing

LHV has always been acting responsibly when planning our communication and marketing messages, both online and offline. We listen to our customers' opinions and preferences as much as possible and try to keep the low level of communication towards the customer. However, increasing phishing and financial crime rates have forced us to proactively warn and educate our customers about possible threats online.

All our marketing activities are based on customer segments and the unique needs of those segments. Our goal is to offer most of our products and services online and plan our sales activities increasingly by segments to support a positive customer experience.

5.3.5 Our societal impact as an employer

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

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

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

Equality and non-discrimination

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

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

LHV has not found it necessary to adopt separate diversity or equality policies but covers the guidelines in different internal documents. In 2021, a working relationships paragraph was added to the Rules of Organisation of Work, which sets out the whistleblowing procedure. In 2022 there were no notifications of any violations in LHV. There were no labour disputes, discrimination cases, or violations of human rights.

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

Breakdown of the company employees (head counts) by gender as of 31 December 2022 –58% Female (517), 42% Male (381)

Breakdown of employees by age and gender as at 31 Dec 2022

Age group	Women (%)	Men (%)	Total
19–25	91 (61.9%)	56 (38.1%)	147
26–40	298 (55.5%)	239 (44.5%)	537
41–55	121 (59.3%)	83 (40.7%)	204
56-…	7 (70%)	3 (30%)	10
Total	**517 (57.6%)**	**381 (42.4%)**	**898**

Staff turnover and job types as at 31 Dec 2022

	Total employees (change from 2021)	Tallinn office	Tartu office	Pärnu office	London office	Leeds office	Manchester office
Total employees	898 (+247)	713	106	11	32	18	18
Working part time women (%)	7%						
Working part time men (%)	2.9%						
Working contractual basis (of which % in IT Department)	27 (85)						
New hires (of which interns)	353 (51)						
Voluntary turnover rate (%)	10.69%						
Overall turnover rate (%)	14.21%						

Gender pay gap as of June 2022:

	Salary ratio (women to men)	Breakdown of female employees
Employees		
Administrative and office services – job value points 91-159	1,09	92%
Specialists 1 – job value points 160-210	0.93	72.7%
Specialists 2 – job value 211-260	0.96	80.5%
Top specialists 1 – job value points 261-310	0.86	48.6%
Top specialists 2 – job value points 311-370	0.91	51.1%
Top specialists 3 – job value points 371-566	0.87	35.4%
Managers		
First level managers 1 – job value points 184-250	0,80	85.7%
First level managers 2 – job value points 251-310	0.92	81.8%
First level managers 3 – job value points 311-380	0.75	66.7%
Middle level managers 1 – job value points 381-440	0.88	34.6%
Middle level managers 2 – job value points 441-500	1.16	27.3%
Function/area managers 1 – job value points 501-700	0.87	40.7%
Function/area managers 2 – job value points over 701	1.25	10.0%

Inclusive workplace

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

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

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

Employee development

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

In addition to personal and professional development, we hold monthly information sessions "What is really important?", the subjects have included – "New Year, New Me", "Conscious Woman", "Leading difficult conversations", "Nutrition as consumption", etc.

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

Work-life balance

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

We have not added any new perks as many of them have been implemented already – e.g., we offer part-time and flexible working schedule to students, new parents and to anyone who needs to work part-time. We pay an allowance to our employees on the birth of a child and when a child starts school. We grant time off for parents to attend their child's start of school or graduation ceremony and allow reduced hours on their child's birthday. We offer 3 free personal days per year, and 3 free days for weddings or for organising a funeral. We also offer an allowance to spend on mental health services, if needed. The use of this allowance has grown each year, as the employees feel more comfortable using professional help with also private worries.

Promotion of employees' health

To keep our employees healthy, LHV has an extensive occupational health package. We contribute to the physical and mental health of our employees. As well as keeping the balance between work and private life, it is important to ensure a supportive mental and physical working environment. LHV provides employees with healthy snacks at the office, promotes physical activity during the working day and offers an allowance for sports and recreation as well as a personal budget to use for your mental health. The sport and recreation compensation has been used increasingly by our employees this year: by 87% in LHV Pank; 83% in LHV Varahaldus; 80% in LHV Finance, and 84% in LHV Kindlustus. The usage has increased from last year. In addition to the mandatory medical examination, LHV offers an extensive medical examination for employees over the age of 40, which has been very popular: over 90% of the target group employees have used it.

A recognised employer

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

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

5.4 Governance

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

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

5.4.1 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 behaviour 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, which was updated in 2021. In 2020, we also created and published our very first ESG policy, clearly stating and explaining our responsibility and commitment to social and environmental issues. 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. LHV's underlying governance principles are described 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 analysing 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 defence for risk monitoring and risk control. The internal control framework covers both a well-functioning independent risk management, compliance checks, and staff performing audit functions. We have established 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.

5.4.2 Investor relations

LHV actively contributes to developing good relations with the investor community, and we have set high standards for ourselves in being open and 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 them of 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.

5.5 Sustainability reporting

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

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

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

5.5.1 ESG metrics

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

5.5.2 Taxonomy reporting

Article 8 of the EU Taxonomy Regulation No 2020/852 (the TR or Taxonomy Regulation) obligates any undertaking subject to an obligation to publish non-financial information pursuant to Article 19a or Article 29a of Directive 2013/34/EU (the NFRD companies) to include in its non-financial statements or consolidated non-financial statements information on how and to what extent the undertaking's activities are associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the TR.

The disclosure pursuant to Article 8 is further specified in Commission Delegated Regulation 2021/2178 (the Disclosures Delegated Act (DDA)). It is important to note here that the DDA will enter into force in several stages in 2022-2026.

LHV Pank's taxonomy eligibility

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

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

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

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

LHV Pank EU taxonomy reporting

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

Clarifications regarding LHV Pank EU taxonomy reporting

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

Exposures to central governments, central banks and supraxand therefore also excluded from the coverage ratios under 3a. Coverage ratios of items under 3b and 3c are provided as a proportion of total on balance-sheet assets.

Group level

AS LHV Group as the parent company of the Group has qualified itself as a non-financial undertaking according to the DDA. The parent company level activity can be categorised as "activities of holding companies" which is not considered a taxonomy-eligible economic activity and, as such, not eligible to be aligned with the taxonomy.

LHV Group subsidiaries listed below are not separately in scope of Article 19a or Article 29a of Directive 2013/34/EU. Therefore, AS LHV Group as parent company subject to the obligation to publish non-financial information pursuant to Article 29a of Directive 2013/34/EU will report the relevant information required by the DDA as follows.

LHV Varahaldus taxonomy eligibility

The share of the economic activities of LHV Varahaldus reported for 2022 as taxonomy-eligible is 0%. In determining the above result, the definition of taxonomy-eligible economic activities in the DDA was applied. The definition refers to economic activities that are currently specified in the Commission Delegated Regulation No. 2021/2139 (the CDA) for the environmental objectives of climate change mitigation and adaptation. Asset management services are not described under these economic activities.

As funds and other financial investments have not been taken into account for the year 2022, only LHV's asset management fee income should be considered in this disclosure. Nevertheless, the principles of ESG are taken into account when investing the assets of LHV Varahaldus funds, to the extent and in the manner provided in the document Principles of Responsible Investment.

LHV Kindlustus taxonomy eligibility

Taxonomy eligible investments of LHV Kindlustus include only exposures to NFRD companies. The proportion of eligible exposures is calculated on the basis of the most recent taxonomy eligibility data provided in annual reports. The proportion of eligible exposures is calculated as a proportion of total investments as determined by the DDA.

Taxonomy share of eligible underwriting activities includes the gross premiums written insurance revenue corresponding to taxonomy-eligible insurance activities specified in the Commission Delegated Regulation No. 2021/2139 (CDA) Annex II point 10.1.

Other subsidiaries

The share of the activities associated with taxonomy-eligible economic activities of LHV UK Limited and EveryPay AS is 0%.

LHV Kindlustus eligibility of investments

EUR thousand			Taxonomy eligible	Taxonomy non-eligible	Coverage %
Art 10	3a	Total investments	72	6,282	1%
	3b	Government & Central Bank	-	-	-
		Total exposure to derivatives	-	-	-
	3c	Total exposure to non-NFRD companies	-	6,060	95%

LHV Kindlustus eligibility of underwriting activities

EUR thousand	Taxonomy eligible	Taxonomy non-eligible	Coverage %
Underwriting activities	10,372	6,766	61%
incl land vehicle insurance (p. 10.1.e)	7,663	-	45%
incl fire and other property damage insurance (p. 10.1.g)	2,709	-	16%

5.5.3 GRI content index and ESG metrics

The report has been prepared in accordance with the Global Reporting Initiative (GRI) Standards: Core Option. As GRI does not provide enough financial-sector specific disclosures for reporting on portfolio impact, various non-GRI disclosures have been used. Such non-GRI disclosures have been categorised by material topics, and listed in the GRI content index below, to provide an overview of all main ESG and sustainability indicators covered in the report.

GRI standard	Disclosure number	Disclosure	Location in report and/or explanation See sections:
Foundation (GRI 101: 2016)			
General disclosures (GRI 102:2016)			
Organizational profile			
	102-1	Name of the organization	• Legal name • Note 1 General information
	102-2	Activities, brands, products, and services	• Management report • Note 1 General information • Activities of business areas
	102-3	Location of headquarters	• Legal address • Note 1 General information
	102-4	Location of operations	• Legal address • Note 1 General information
	102-5	Ownership and legal form	• General Meeting (for legal form) • Shares and bonds issued by LHV (for ownership) • Note 1 General information (for legal form) • Note 6 Subsidiaries and goodwill
	102-6	Markets served	• Strategy • Note 1 General information
	102-7	Scale of the organization	• Strategy • Note 1 General information
	102-8	Information on employees and other workers	• Strategy • Note 1 General information
	102-9	Supply chain	• Green office operations
	102-10	Significant changes to the organization and its supply chain	• Green office operations
	102-11	Precautionary principle or approach	• ESG Risks in credit risks
	102-12	External initiatives	• Global sustainability frameworks • Leadership for sustainable business development in Estonia
	102-13	Membership of associations	• Global sustainability frameworks • Leadership for sustainable business development in Estonia
Strategy			
	102-14	Statement from senior decision-maker	• Statement of the managing director • CEO letter on sustainability
Ethics and integrity			
	102-16	Values, principles, standards, and norms of behaviour	• Governance of the group
	102-17	Mechanisms for advice and concerns about ethics	• Equality and non-discrimination

Governance			
	102-18	Governance structure	• Note 1 General information
Stakeholders' engagement			
	102-40	List of stakeholder groups	• Stakeholder engagement
	102-41	Collective bargaining agreements	• Inclusive workplace
	102-42	Identifying and selecting stakeholders	• Stakeholder engagement
	102-43	Approach to stakeholder engagement	
	102-44	Key topics and concerns raised	
Reporting practice			
	102-45	Entities included in the consolidated financial statements	• Note 1 General information
	102-46	Defining report content and topic boundaries	• Sustainability mission statement • GRI
	102-47	List of material topics	• Material ESG and sustainability topics
	102-49	Changes in reporting	• Summary of significant accounting policies/ basis of preparation
	102-50	Reporting period	January 2022 – December 2022
	102-51	Date of most recent report	1 March 2022
	102-52	Reporting cycle	Annual
	102-53	Contact point for questions regarding the report	info@lhv.ee
	102-54	Claim of reporting in accordance with the GRI Standards	• Global sustainability frameworks – GRI • GRI content index
	102-55	GRI content index	• GRI content index and ESG metrics
	102-56	External assurance	• Independent auditors report

Material impact areas

1. Climate and biodiversity

Portfolio impact on climate and biodiversity (non-GRI disclosures)			See sections:
Management approach (GRI 103: 2016)	103-1 until 103-3		• ESG strategy • Stakeholder engagement • Management of ESG • Management of impact areas - Environment

Emissions (GRI 305: 2016)

Management approach (GRI 103: 2016)	103-1 until 103-3		• Our carbon footprint
	305-1	Direct (Scope 1) GHG emissions	
	305-2	Energy indirect (Scope 2) GHG emissions	
	305-3	Other indirect (Scope 3) GHG emissions	
	305-4	GHG emissions intensity	

Waste (GRI 306:2020)

Management approach (GRI 103:2016)	103-1 until 103-3		• Our carbon footprint
	306-3	Waste generated	

Waste and effluents (GRI 303: 2018)

Management approach (GRI 103: 2016)	103-1 until 103-3		• Our carbon footprint
	303-5	Water consumption	

2. Circular economy

Portfolio impact on circular economy (non-GRI disclosures)

Management approach (GRI 103: 2016)	103-1 until 103-3		• Material ESG and sustainability topics

3. Inclusive and cohesive economy

Indirect economic impacts (GRI 203: 2016)

Management approach (GRI 103: 2016)	103-1 until 103-3		• ESG strategy • Stakeholder engagement • Management of ESG Management of impact areas - Social
	203-2	Significant indirect economic impacts	• Social responsibility • Financial literacy • Sponsorships • Social impact through channels and customer experience

4. Financial literacy and economic sense of security

Indirect economic impacts (GRI 203: 2016)

Management approach (GRI 103: 2016)	103-1 until 103-3		• ESG strategy • Stakeholder engagement - • Management of ESG Management of impact areas - Social
	203-2	Significant indirect economic impacts	• Social responsibility • Financial literacy • Sponsorship • Social impact through channels and customer experience

5. Honest and transparent organisational culture

Anti-corruption (GRI 205:206)

Management approach (GRI 103: 2016)	103-1 until 103-3		GRI content index
	205-3	Confirmed incidents of corruption and actions taken	None

Socioeconomic compliance (GRI 419: 2016)

Management approach (GRI 103: 2016)	103-1 until 103-3		• Management of ESG • Management of impact areas – Governance • Management of impact areas – Social • Management of impact areas • Corporate Governance Report
	419-1	Non-compliance with laws and regulations in the social and economic area	None

Diversity and equal opportunities (GRI 405: 2016)

Management approach (GRI 103: 2016)	103-1 until 103-3		• Management of ESG • Management of impact areas – Social • Our societal impact as an employer - Equality and non-discrimination
	405-1	Diversity of governance bodies and employees	• Equality and non-discrimination • GRI content index and ESG metrics
	405-2	Ratio of basic salary and remuneration of women to men	• Equality and non-discrimination • GRI content index and ESG metrics

Stakeholder engagement (non-GRI disclosure)

Management approach (GRI 103-2016)	103-1 until 103-3		• Stakeholder engagement • Management of ESG

ESG key performance indicators (KPIs)

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

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

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

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

ESG key performance indicators in LHV Group

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

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

* logging in at least once a month

3. Financial literacy and economic sense of security (S)			
Share of young people (up to 26 years old) with an investment services contract	46.1%	45.7%	29.8%
Share of private clients with an investment services contract	40.8%	41.1%	30.8%
Share of female private clients with an investment services contract	36.3%	36.0%	24.6%
Number of microloans granted	1,068	1,001	948
Share of LHV Pank customers with 2nd pillar pension	35%	-	-
Total number of Investment School attendees	19,262	12,000	7,420

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

Governance of the Group

Supervisory board

Rain Lõhmus is one of the founders of LHV and the chairman of the Supervisory Board of LHV Group. He is a member of the Supervisory Board of LHV Pank and belongs to the Supervisory Board of Kodumaja AS. He is the owner and a member of the Management Boards of AS Lõhmus Holding, Lohmus Capital OÜ and LHV CAPITAL I PTE. LTD and the owner of OÜ Merona Systems and Kõrberebane OÜ. Additionally, he is the Management Board member and one of the owners of Zerospotnrg OÜ and Umblu Records OÜ. Rain Lõhmus graduated from Tallinn University of Technology (TalTech) and the management programme of Harvard Business School. Rain Lõhmus and persons related to him (Lõhmus Holdings OÜ, OÜ Merona Systems) own altogether 68,649,130 shares, representing 21.76% of all shares of LHV Group.

Raivo Hein is a member of the Supervisory Boards of LHV Group and LHV Pank. He also belongs to the Supervisory Board of AS Puumarket. He is the owner and a member of the Management Board of OÜ Kakssada Kakskümmend Volti and a Management Board member of OÜ Saarte Sillad and several other companies established for the management of personal investments. Raivo Hein graduated from Tallinn University of Technology (TalTech). Raivo Hein does not own shares of LHV Group. Persons related to him, OÜ Kakssada Kakskümmend Volti, Lame Maakera OÜ and Astrum OÜ own altogether 5,484,480 shares, representing 1.74% of all shares of LHV Group.

Heldur Meerits is a member of the Supervisory Boards of LHV Group and LHV Pank. He is also a member of the Supervisory Boards of Kodumaja AS and the foundations SA Põltsamaa Ühisgümnaasiumi Toetusfond and Audentese Koolide SA. Heldur Meerits is also the owner and a member of the Management Boards of the companies established for the management of personal economic interests, AS Amalfi, AS Altamira and SIA Valdemara Group, and the protector and beneficiary of Castra Hiberna Foundation. Heldur Meerits graduated from the Faculty of Economics and Business Administration of the University of Tartu. Heldur Meerits does not own shares of LHV Group. AS Amalfi owns 10,875,280 shares, representing 3.45% of all shares of LHV Group.

Tiina Mõis is a member of the Supervisory Boards of LHV Group and LHV Pank. She also belongs to the Supervisory Boards of Rocca al Mare Kooli AS and Rocca al Mare Kooli SA. She is the owner and a Management Board member of AS Genteel and one of the owners and a Management Board member of Nine Lives OÜ. Tiina Mõis graduated from Tallinn University of Technology (TalTech). Tiina Mõis and persons related to her (AS Genteel and Rocca al Mare Kooli SA) own altogether 11,359,990 shares, representing 3.6% of all shares of LHV Group.

Sten Tamkivi is a member of the Supervisory Board of LHV Group. He belongs to the Supervisory Boards of ASI Private Equity AS, Salv Technologies OÜ and Kistler-Ritso Eesti SA. In addition, he is the owner and a Management Board member of Seikatsu OÜ and Osaluste Hellalt Hoidmise OÜ and a Management Board member of OÜ Notorious, Kaigun OÜ, TBD Holdco OÜ and MTÜ Asutajad. He is also one of the owners of OÜ E-laen. Sten Tamkivi graduated from Stanford University Graduate School of Business. Sten Tamkivi and persons related to him (Seikatsu OÜ and OÜ Notorious) own altogether 335,630 shares, representing 0.11% of all shares of LHV Group.

Tauno Tats is a member of the Supervisory Board of LHV Group. He is also a member of the Supervisory Boards of EfTEN Kinnisvarafond AS, AS Ecomet Invest and OÜ Eesti Killustik and a member of the Management Boards of Ammende Hotell OÜ and MTÜ Plate torn. He is the Management Board member and one of the owners at Ambient Sound Investments OÜ as well as a Management Board member of companies established for the management of investments of the aforementioned companies. Tauno Tats graduated from Tallinn University of Technology (TalTech). Tauno Tats does not own shares of LHV Group. Ambient Sound Investments OÜ owns 10,828,210 shares, representing 3.43% of all shares of LHV Group.

Andres Viisemann is one of the founders of LHV and the manager of LHV pension funds. He is a member of the Supervisory Boards of LHV Group, LHV Pank and AS LHV Varahaldus. He also belongs to the Supervisory Boards of AS Fertilitas and AS Viimsi Haigla. He is the owner and a member of the Management Board of Viisemann Holdings OÜ and the owner of Viisemann Investments AG. Andres Viisemann graduated from the University of Tartu and obtained a master's degree from INSEAD in International Business Management. Andres Viisemann and the persons related to him (Viisemann Investments AG and Viisemann Holdings OÜ) own altogether 35,756,210 shares, representing 11.34% of all shares of LHV Group. Due to his position as the head of LHV pension funds, Andres Viisemann is entitled to subscribe a total of 96,850 shares of LHV Group for options issued in 2021 and 2022.

Management board

Madis Toomsalu is a member of the Management Board of LHV Group and the chairman of the Supervisory Boards of LHV Pank, AS LHV Kindlustus, AS LHV Varahaldus and EveryPay AS, a member of the Supervisory Board of AS LHV Finance, and the chairman of the board of directors of LHV UK Limited. He is also a member of the Management Board of MTÜ FinanceEstonia and a member of the council of the foundation SA Rohetiiger. Madis Toomsalu has obtained a bachelor's degree in business management from Tallinn University of Technology (TalTech) in 2009 and a master's degree in 2011 in public sector finance. Madis Toomsalu and persons related to him own altogether 1,031,090 shares, representing 0.33% of all shares of LHV Group. With the options issued in 2020, 2021 and 2022, Madis Toomsalu has the right to subscribe a total of 860,310 shares of LHV Group.

Meelis Paakspuu has been a member of the Management Board and CFO of LHV Pank since 2015 and a member of the Management Board of LHV Group since 2022. He is not a member of the governing bodies of any other company. Meelis Paakspuu graduated from the University of Tartu in 1996 with a degree in economics. Meelis Paakspuu and persons related to him own altogether 491,320 shares, representing 0.16% of all shares of LHV Group. With the options issued in 2020, 2021 and 2022, Meelis Paakspuu has the right to subscribe a total of 527,700 shares of LHV Group.

Martti Singi has been a member of the Management Board and Risk Manager of LHV Pank since 2012 and a member of the Management Board of LHV Group since 2022. He is not a member of the governing bodies of any other company. Martti Singi obtained a master's degree in international business administration from Estonian Business School in 2009. Martti Singi and persons related to him (incl OÜ Unitas) own altogether 853,530 shares, representing 0.27% of all shares of LHV Group. With the options issued in 2020, 2021 and 2022, Martti Singi has the right to subscribe a total of 506,410 shares of LHV Group.

Jüri Heero has been member of the Management Board and IT Manager of LHV Pank since 2007 and a member of the Management Board of LHV Group since 2022. He is not a member of the governing bodies of any other company. Jüri Heero graduated from the University of Tartu in 1999 with a degree in economics. Jüri Heero and persons related to him (incl Heero Invest OÜ) own altogether 1,012,180 shares, representing 0.32% of all shares of LHV Group. With the options issued in 2020, 2021 and 2022, Jüri Heero has the right to subscribe a total of 506,410 shares of LHV Group.

Committees formed on Supervisory Board level

Audit Committee

Kristel Aarna works as the CFO of AS TV Play Baltics since 2011 and before that was the chief controller of Swedbank Baltic Banking. Previously she has been the head of financial advisory services at KPMG Baltics AS and worked also at the Bank of Estonia and CVS Caremark Corporation. She is also the owner and a member of the Management Board of IKA Konsult OÜ. Kristel Aarna has a bachelor's degree from the Faculty of Economics of the University of Tartu and master's degree in Business Administration from the Bentley University Graduate School of Business. Kristel Aarna does not own any shares of LHV Group.

Urmas Peiker was the head of Compliance at LHV Pank from May 2013 until October 2014. Previously, Urmas Peiker worked as the head of Business Development in the Estonian start-up Funderbeam, as the head of Market Supervision Department of the EFSA (Estonian Financial Supervision and Crisis Resolution Authority), in the European Bank for Reconstruction and Development and Morgan Stanley's. Urmas Peiker is the owner and a Management Board member of OÜ Vesilind, OÜ PT Arendus, OÜ Bintous, OÜ Pioneer Engineering Group and OÜ Estcap and belongs to the Management Board of MTÜ Tööstuse Ekspordi ja Innovatsiooni Klaster. Urmas Peiker has a bachelor's degree from the University of Tartu and master's degree in Law from the Duke University in the USA. Urmas Peiker does not own any shares of LHV Group. Person related to him owns altogether 20 shares, representing 0% of all shares of LHV Group.

Tauno Tats (member of the Supervisory Board of AS LHV Group)

Remuneration Committee

Madis Toomsalu (member of the Management Board of LHV Group, chairman of the Supervisory Boards of LHV Pank, AS LHV Varahaldus, AS LHV Kindlustus and EveryPay AS, member of the Supervisory Board of AS LHV Finance and the chairman of the Board of Directors of LHV UK Limited)

Rain Lõhmus (chairman of the Supervisory Board of LHV Group and member of the Supervisory Board of LHV Pank)

Andres Viisemann (member of the Supervisory Boards of LHV Group, LHV Pank and AS LHV Varahaldus)

Nomination Committee

Madis Toomsalu (member of the Management Board LHV Group, chairman of the Supervisory Boards of LHV Pank, AS LHV Varahaldus, AS LHV Kindlustus and EveryPay AS, member of the Supervisory Board of AS LHV Finance and the chairman of the Board of Directors of LHV UK Limited)

Rain Lõhmus (chairman of the Supervisory Board of LHV Group and member of the Supervisory Board of LHV Pank)

Andres Viisemann (member of the Supervisory Boards of LHV Group, LHV Pank and AS LHV Varahaldus)

Risk and Capital Committee (formed on LHV Pank Supervisory Board level)

Rain Lõhmus (chairman of the Supervisory Board of LHV Group and member of the Supervisory Board of LHV Pank)

Andres Viisemann (member of the Supervisory Boards of LHV Group, LHV Pank and AS LHV Varahaldus)

Tiina Mõis (member of the Supervisory Boards of AS LHV Group and AS LHV Pank)

Madis Toomsalu (member of the Management Board LHV Group, chairman of the Supervisory Boards of LHV Pank, AS LHV Varahaldus, AS LHV Kindlustus and EveryPay AS, member of the Supervisory Board of AS LHV Finance and the chairman of the Board of Directors of LHV UK Limited)

Supervisory and Management Boards of the subsidiaries

AS LHV Pank

Supervisory Board: Madis Toomsalu (chairman, until 31 March 2026), Rain Lõhmus (until 31 December 2024), Andres Viisemann (until 31 March 2027), Tiina Mõis (until 31 December 2024), Heldur Meerits (until 31 March 2026), Raivo Hein (until 31 March 2027)

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

AS LHV Finance

Supervisory Board: Kadri Kiisel (chairman, until 28 January 2026), Madis Toomsalu (until 26 June 2025), Veiko Poolgas (until 24 August 2023), Jaan Koppel (until 24 August 2023)

Management Board: Mari-Liis Stalde (until 18 January 2023), Heidy Kütt (appointed on 18.01.2023)

AS LHV Varahaldus

Supervisory Board: Madis Toomsalu (chairman, until 31 March 2026), Kadri Kiisel (until 31 March 2027), Andres Viisemann (until 31 March 2026)

Management Board: Vahur Vallistu (chairman, until 5 June 2024), Joel Kukemelk (until 31 March 2027)

AS LHV Kindlustus

Supervisory Board: Madis Toomsalu (chairman), Erki Kilu, Veiko Poolgas, Jaan Koppel (all until 6 May 2025)

Management Board: Martti-Sten Merilai (chairman, until 24 November 2027), Tarmo Koll (until 6 May 2025)

LHV UK Ltd

Board of Directors: Erki Kilu (appointed on 4 February 2021), Andres Kitter (appointed on 4 February 2021), Madis Toomsalu (appointed on 4 February 2021), Gary Lewis Sher (appointed on 5 July 2021), Paul Horner (appointed on 4 January 2022), Keith Butcher (appointed on 1 May 2022), Sally Jane Veitch (appointed on 1 July 2022)

AS EveryPay

Supervisory Board: Madis Toomsalu (chairman) Andres Kitter, Erki Kilu, Kadri Kiisel (all until 4 April 2027)

Management Board: Lauri Teder (until 4 April 2027)

Corporate Governance report

This report, which is presented in accordance with the Accounting Act of the Republic of Estonia, provides an overview of the governance of AS LHV Group (LHV) and the compliance of governance with the advisory guidelines Corporate Governance Recommendations (CGR) of the EFSA and Nasdaq Tallinn Stock Exchange. LHV complies with the CGR, unless indicated otherwise in this report.

1. General Meeting

LHV is a public limited company whose governing bodies are the General Meeting, the Supervisory Board, and the Management Board.

The General Meeting where shareholders exercise their rights is the highest governing body of LHV. The primary duties of the General Meeting include amending the Articles of Association, increasing and decreasing share capital, taking decisions on the issuance of convertible bonds, electing and extending the mandate of Supervisory Board members, removing Supervisory Board members before the expiry of their term of office, approving the annual report and allocation of profit, approving share option programmes, determining the number of auditors, appointing and removing the auditor(s) and taking other decisions within the power of the General Meeting under the law and the Articles of Association.

A resolution on the amendment of the Articles of Association is adopted when at least two-thirds of the votes represented at the General Meeting are in favour. A resolution on the amendment of the Articles of Association enters into force at the time when the corresponding entry is made in the commercial register. The resolution of the General Meeting on the amendment of the Articles of Association, the minutes of the General Meeting and the new text of the Articles of Association are attached to the application filed with the commercial register.

A shareholder has the right to participate in the General Meeting, address the General Meeting regarding items on the agenda, ask relevant questions and make proposals.

The General Meeting is called by the Management Board. The Annual General Meeting whose agenda includes the approval of the annual report is called at least once a year. The Management Board calls the Annual General Meeting within six months after the end of the financial year at the latest. The Management Board gives at least three weeks' notice of Annual or Extraordinary General Meetings.

The agenda of the General Meeting, proposals of the Management Board and Supervisory Board, draft resolutions and other relevant materials are made available to the shareholders prior to the General Meeting. The materials are made available on LHV's website. Shareholders are given an opportunity to ask questions about items on the agenda before the General Meeting and to vote electronically on the draft resolutions on the agendas of the General Meeting. The shareholders not wishing to participate in the meeting in person are granted the opportunity to watch the meeting via video broadcast. The option to participate in the General Meeting and exercise the rights using electronic means without physically attending the General Meeting via secure electronic means is provided in the Articles of Association.

The list of shareholders entitled to participate in the General Meeting is determined based on the share register seven days before the General Meeting.

In 2022, the Annual General Meeting was held on 30 March 2022. The agenda included the approval of the annual report for 2021, the profit allocation for the 2021 financial year, and the payment of dividends; the approval of the remuneration principles and the remuneration report of the Management Board for 2021; the approval of the transaction to acquire a 100% share in AS EveryPay and related increase of share capital of LHV; the amendments to the Articles of Association (in two different successive versions, including a reduction of the nominal value of the shares); and the appointment of the auditor for the 2023 financial year and 2024–2028 financial years. In addition, an overview was given of the financial results, the business environment for the first two months of 2022 and the financial forecast for the next five years. No extraordinary General Meetings were held in 2022.

The Annual General Meeting in 2022 was held in Estonian and chaired by Daniel Haab, Head of Legal Department of LHV Pank, who introduced the procedure for conducting the General Meetings and the procedure for asking the Management Board questions regarding the company's activities.

The Annual General Meeting was attended by Madis Toomsalu, the chairman of the Management Board, and Rain Lõhmus, the chairman of the Supervisory Board. The other members of the Supervisory Board, i.e., Andres Viisemann, Tiina Mõis, Heldur Meerits, Raivo Hein, Sten Tamkivi and Tauno Tats cast their votes electronically. The auditor, Eero Kaup (KPMG), was also present.

No shareholders of LHV hold shares which would grant them special control or voting rights. LHV is not aware of any agreements between shareholders regarding coordinated exercise of shareholder rights.

The shareholders with significant influence are Rain Lõhmus and persons related to him, who hold 22.68% of share capital in aggregate and Andres Viisemann and persons related to him, who hold 11.34% of share capital in aggregate.

2. Management Board

2.1 Composition and duties of Management Board

The Management Board is the governing body representing and managing LHV. The members of the Management Board are elected and removed by the Supervisory Board. To elect a member of the Management Board, the candidate's written consent is required. Only a person who has sufficient knowledge and experience to participate in the work of the Management Board and to fulfil the duties of a member of the Management Board and who meets the requirements arising from LHV's Articles of Association, rules of procedure of the Management Board and other internal regulations, and legislation, may be appointed as a member of the Management Board. Before appointment, the suitability of the person for the position is assessed in accordance with LHV's rules for the assessment of the suitability of members of the governing bodies and key function holders, taking into account the specific nature of LHV's operations.

According to the Articles of Association of LHV, the Management Board has one to five members. A member of the Management Board is appointed for a term of five years unless otherwise decided by the Supervisory Board. The extension of the term of office of a member of the Management Board may not be decided earlier than one year before the scheduled expiry of the term of office or for a period exceeding the maximum period permitted by law or the Articles of Association. If the Management Board of LHV has more than two members, the Supervisory Board appoints the chairman of the Management Board. The chairman of the Management Board organises the work of the Management Board. The Supervisory Board may remove a member of the Management Board regardless of the reason. A member of the Management Board may resign from the board, regardless of the reason, by informing the Supervisory Board. The rights and obligations arising from a contract entered with a member of the Management Board expire in accordance with the contract.

Until 31 October 2022 LHV's Management Board had one member: Madis Toomsalu. From 1 November 2022 the Management Board has four members: Madis Toomsalu (the chairman of the Management Board, CEO), Meelis Paakspuu (responsible for financial management function), Martti Singi (responsible for risk management function) and Jüri Heero (responsible for IT operations, IT development and information security functions).

The Supervisory Board has signed Management Board member contracts with the Management Board members. The Supervisory Board determines the remuneration principles of the members of the Management Board and compensation for early termination of the contract. The term of office of Madis Toomsalu expires on 30 March 2026 and the terms of office of the newly elected members of the Management Board, i.e., Meelis Paakspuu, Martti Singi and Jüri Heero, expire on 30 March 2027. The aim of the changes in the Management Board of LHV as of 1 November 2022, was to reorganise the organisational structure and governance of LHV as a financial holding company taking into account the fact that LHV does not have an independent business and operates as a separate holding company, also the fact that the additional members of the Management Board of LHV are responsible for the relevant function at the level of the Management Board of LHV's subsidiary LHV Pank.

The Management Board makes everyday management decisions at its own discretion and in the best interests of LHV and its shareholders, putting aside personal interests. The duties of a member of the Management Board include day-to-day management of LHV, representing the company, managing LHV's operations in foreign markets and communicating with investors, coordinating the development of LHV's strategy and implementing the strategy by serving as a chairman of the Supervisory Boards of LHV's major subsidiaries. The right of representation specification of the members of the Management Board resulting from the Articles of Association of LHV has also been entered in the Commercial Register: the chairman of the Management Board alone or two members of the Management Board jointly may represent LHV in transactions.

The Management Board ensures that LHV has risk management and internal control systems appropriate for its operations and business area. LHV's internal control system covers all activities carried out by LHV's Supervisory Board, management, and employees to ensure efficiency of operations, adequate risk management, reliability and accuracy of internal and external reporting and unconditional compliance with all laws and regulations. The internal control system covers all business, support, and control units.

The objectives of risk management within LHV are to identify, correctly quantify and manage risks. The wider objective of risk management is to increase the value of the company by minimising losses and reducing volatility of results.

LHV's risk management is based on a strong risk culture and follows the principle of three lines of defence. The first line of defence, i.e., represented mainly by the business lines, alongside other support functions, is responsible for risk-taking and daily risk management. The second line of defence, i.e., the risk management function and the compliance function, including the AML compliance function, is responsible for ownership, continuous review, and implementation of a risk management framework. The third line of defence, i.e., the independent internal audit function, exercises supervision over the entire organisation, i.e., reviews, through conducting internal audits, the internal governance arrangements, processes, and mechanisms to ascertain that they are sound, effective, implemented and consistently applied.

2.2 Principles of remuneration of the Management Board

The purpose of LHV's remuneration principles is to provide fair, motivating, transparent and lawful remuneration.

The authority to determine the remuneration principles and remuneration of the Management Board is vested in the Supervisory Board. The Remuneration Committee reviews the bases of the remuneration of the Management Board on an annual basis. In assessing the activities of the Management Board, the Remuneration Committee considers, above all, the duties and activities of the members of the Management Board as well as LHV's financial position, the current status and outlook of business operations in comparison with other companies operating in the same sector.

The remuneration payable to a member of the Management Board, including the options programme, must motivate the person to act in the best interests of LHV and to avoid a situation of conflict of interest by refraining from acting in the personal or other interests. The basic salary and remuneration principles of the members of the Management Board are set forth in the Management Board member contracts concluded with them. The principles of remuneration of the members of the Management Board engaged in internal control and risk management must ensure their independence and objectivity in the performance of their risk management / internal control duties. The remuneration of those persons must not depend on the results of the areas under their supervision. The goals set must be described at an individual level.

In setting the key quantitative and qualitative performance indicators and risk assessment metrics, LHV is governed by the following principles:

- The performance criteria developed by LHV must not stimulate excessive risk-taking or sale of inappropriate products.
- The performance criteria must not consist only of performance efficiency indicators (e.g., profit, revenue, return, costs, and volume indicators) or market-based indicators (e.g., share price or bond yield) but must be adjusted for risk-based indicators (e.g., capital adequacy, liquidity).
- The criteria used for measuring risks and results must be as closely as possible related to the decisions of the member of the Management Board whose results are being appraised, and they should ensure that remuneration is determined in a way that has the desired impact on the Management Board member's behaviour.
- The performance criteria must be developed by ensuring a good balance between quantitative and qualitative as well as absolute and relative criteria.
- The quantitative criteria must cover a period that is sufficiently long to take into account the risks taken by the member of the Management Board or units they are responsible for, and they should be risk-adjusted and contain economic efficiency indicators.
- The examples of qualitative criteria include achievement of strategic objectives, customer satisfaction, adherence to the risk management policy, compliance with internal and external regulations, management skills, teamwork, creativity, motivation and cooperation with other business units and the internal control function.

LHV applies a long-term incentive plan (LTI plan), i.e., an option programme. The basic salaries of Management Board members, top management and key personnel included in the option programme (including staff members considered equal to Management Board members) are added an annual performance pay the amount and disbursement of which depend on the achievement of individual targets and LHV's targets. The lower limit of the performance pay, approved by the shareholders, is EUR 0 and the upper limit is 200% of the annual remuneration. As a rule, if the financial plan is met, options will be granted to the extent of 2% of the total number of LHV shares. The bases for assigning performance pay through the options programme must be objective and justified and pre-determine the period for which performance pay is paid. The performance pay instruments consist fully of share options.

Severance compensation payable to members of the Management Board is related to their previous performance. No severance compensation is paid if this would damage the interests of LHV. The size of the severance compensation must correspond to the results achieved over time and to the remuneration received.

Until 31 October 2022 LHV's Management Board had one member: Madis Toomsalu. From 1 November 2022 the Management Board has four members: Madis Toomsalu (the chairman), Meelis Paakspuu, Martti Singi and Jüri Heero. Madis Toomsalu was paid in January 2022 a remuneration of EUR 13 thousand and for rest of 2022 a monthly remuneration of EUR 16 thousand, i.e. an annual remuneration of EUR 189 thousand under his Management Board member contract concluded with LHV. The chairman of the Management Board of LHV, Madis Toomsalu, is entitled to receive, as performance pay, a total of 860,310 shares of LHV for the options granted in 2020, 2021 and 2022. Meelis Paakspuu, Martti Singi and Jüri Heero were paid in January 2022 a remuneration of EUR 10 thousand and for the rest of 2022 a monthly remuneration of EUR 13 thousand, i.e. an annual remuneration of EUR 153 thousand under their Management Board member contracts concluded with LHV Pank. Under their Management Board member contracts concluded with LHV, Meelis Paakspuu, Martti Singi and Jüri Heero do not receive any additional remuneration for the performance of duties of the Management Board members of LHV. The member of the Management Board of LHV, Meelis Paakspuu, is entitled to receive, as performance pay, a total of 527,700 shares of LHV for the options granted in 2020, 2021 and 2022. The members of the Management

Board of LHV, Martti Singi and Jüri Heero, are each entitled to, as performance pay, a total of 506,410 shares of LHV for the options granted in 2020, 2021 and 2022. The Management Board members are not entitled to any additional bonuses or benefits for performing the duties of the Management Board members of LHV.

2.3 Conflicts of interests

The Management Board submits a declaration of economic interests and conflicts of economic interests once a year. There have been no conflicts of interest; accordingly, no corrective measures have been applied.

Transactions between LHV and the Management Board, their close family members or persons related to them, and the terms of these transactions must be approved by the Supervisory Board prior to the transaction taking place. In 2022, there were no such transactions between the members of the Management Board, their close family members, or related persons and LHV, nor are there any valid contracts of that nature from earlier periods. The Management Board members have no shareholdings above 5% in other companies who are LHV's business partners, suppliers, clients or other related companies.

None of the Management Board members of LHV are Management Board members or Supervisory Board members at any other issuer. The Management Board members have not been granted the authority to issue or buy back shares.

3. Supervisory Board

3.1 Composition and duties of Supervisory Board

The Supervisory Board is a governing body of LHV which plans the activities of LHV, organises the management of LHV and conducts supervision over the activities of the Management Board. The Supervisory Board determines and regularly reviews LHV's strategy, the general action plan, risk management principles and the annual budget. The Supervisory Board has five to seven members. The members of the Supervisory Board are appointed for a term of three years. The members of the Supervisory Board elect from among themselves the chairman of the Supervisory Board, who organises the activities of the Supervisory Board. The authority to elect and to extend the mandate of the Supervisory Board members is vested in the General Meeting.

Only a person who has sufficient knowledge and experience to participate in the work of the Supervisory Board and to fulfil the duties of a member of the Supervisory Board and who meets the requirements arising from the Articles of Association, rules of procedure of the Supervisory Board and other internal regulations, and applicable legislation, may be elected as a member of the Supervisory Board. Before appointment, the suitability of the person for the position is assessed in accordance with LHV's rules for the assessment of the suitability of members of the governing bodies and key function holders, taking into account the specific nature of LHV's operations.

The members of the Supervisory Board of LHV are Rain Lõhmus (the chairman of the Supervisory Board), Andres Viisemann, Tiina Mõis, Heldur Meerits, Raivo Hein, Tauno Tats and Sten Tamkivi. The term of office of Supervisory Board members lasts until 29 March 2023.

In 2022 the Supervisory Board had eleven ordinary meetings, three extraordinary meetings and on eight occasions decisions were adopted electronically. During the year, three members of the Supervisory Board (Tiina Mõis, Heldur Meerits and Raivo Hein) participated in all Supervisory Board meetings, three members of the Supervisory Board (Rain Lõhmus, Andres Viisemann and Tauno Tats) were absent from one Supervisory Board meeting and one member of the Supervisory Board (Sten Tamkivi) was absent from two Supervisory Board meetings. All the members of the Supervisory Board cast their vote electronically on all of the eight occasions the Supervisory Board adopted their decisions electronically in 2022.

Three committees have been formed at the Supervisory Board level of LHV, which are responsible for advising the Supervisory Board in matters related to audit, remuneration, and the appointment of members of the Management Board as described in subsections 3.3–3.5 of 'Corporate governance report'.

In the framework of its meetings in 2022, the Supervisory Board received regular overviews of the operating and financial results of LHV and its subsidiaries, and the activities, development, and results of the related areas. Risk reports and the internal auditor's and Audit Committee reports, compliance reports were reviewed on a quarterly basis. In Q1 2022, the Supervisory Board approved the annual report for 2021 and the report on the activities of the Supervisory Board. The Supervisory Board submitted the documents to the General Meeting for approval and made other various proposals for approval to the General Meeting (described in section 1 of 'Corporate governance report'). The proposals of the Nominating Committee for the regular assessment of the individual suitability of the Management Board member, the Supervisory Board members and the collective suitability of the Supervisory Board were approved in January 2022. The pricing of share options and the grant of share options for the results of 2021 (the LTI plan), and the exercise of share options for the 2018 results were approved, in addition the decision to provide a one-off grant to the NGO Estonian Refugee Aid to assist refugees in the context of the humanitarian crisis in Ukraine was adopted in February 2022. In March 2022 the Supervisory Board's decision to make an investment in the Estonian financial technology company Modular Technologies OÜ (trademark 'Tuum') was carried out. The decision to increase the share capital of LHV in connection with exercise of the share options programme (LTI plan) was adopted in April 2022 and the decision to increase the share capital of LHV by issuing new ordinary shares in the form of a public offering was adopted in May 2022. In both, July and December 2022, the Supervisory Board's consent was given to increase the share capital of LHV UK. At the regular meeting of the Supervisory Board in August 2022, the primary focus was on the discussion of the strategy of LHV and its subsidiaries. In the same month the write-down of a financial investment in the UK financial undertaking Bank North Ltd was decided (an additional write-down was decided also in September 2022) and the consent to acquire the small and medium-sized enterprises lending business of the same company was given to LHV UK, the latter transaction was finalised in October 2022. In September the 2023 financial calendar was approved, and consent was given to increase the share capital of LHV Pank. In October 2022, to reorganise the organisational structure and governance of LHV as a financial holding company the proposals of the Nominating Committee for the assessment of the individual suitability of the new Management Board members and the collective suitability of the Management Board with a new composition, were approved, following which the new Management Board members were elected, and the chairman of the Management Board was appointed. The issue of EUR 100 million of senior unsecured, unsubordinated bonds to meet regulatory requirements (the so-called MREL ratio) was also decided at the October 2022 meeting. In November 2022 the Supervisory Board decided to organise a private offering of additional Tier 1 temporary write-down notes to financial institutions and proficient investors with a larger investment portfolio. In December the term of office of the Nominating Committee members was extended and the new capital targets were confirmed. At the last two meetings of the year, the Supervisory Board discussed the assumptions for next year's operational and financial plans and the 5-year financial forecast of LHV and its subsidiaries. During the year, overviews of the AML trends, results of the employee survey questionnaire Q12 of LHV and its subsidiaries were presented and training days for the Supervisory Board members were organised as part of the training programme put in place at the beginning of 2022 as part of the suitability assessment procedure to keep the Supervisory Board members' knowledge up to date. In addition, several procedures, policies, and internal regulations of LHV and its subsidiaries were reviewed, updated, and approved, the main aim of which on the LHV level was to reorganise the organisational structure and governance of LHV as a financial holding company.

3.2 Principles of remuneration of the Supervisory Board and conflicts of interest

The size of the remuneration of the members of the Supervisory Board and remuneration procedure are decided by the General Meeting, which takes into account, among other things, the duties of the Supervisory Board and their scope as well as the members' participation in the meetings and the activities of the Supervisory Board as a governing body.

A member of the Supervisory Board may be assigned additional remuneration for participation in the activities of the Audit Committee or another body of the Supervisory Board.

The General Meeting has resolved to provide members of the Supervisory Board with a gross remuneration of EUR 1,500 per each ordinary meeting of the Supervisory Board in which the member participates. The remuneration is paid out on the next working day following the Supervisory Board meeting at the latest. No separate additional or performance payments, bonuses or benefits have been established.

In 2022, the total amount of remuneration paid to LHV's Supervisory Board was EUR 108 thousand, including all taxes, out of which three members (Tiina Mõis, Heldur Meerits and Raivo Hein) received EUR 16.5 thousand each (participated in all 11 ordinary meetings), three members (Rain Lõhmus, Andres Viisemann and Tauno Tats) received EUR 15 thousand each (participated in 10 ordinary meetings) and one member (Sten Tamkivi) received EUR 13.5 thousand (participated in 9 ordinary meetings).

For reasons of clarity, LHV considers it important to note that for Supervisory Board member Andres Viisemann LHV applies the LTI plan, i.e., an option programme, based on his activity as the head of pension funds at LHV's subsidiary LHV Varahaldus. The LTI instrument comprises fully of share options. Andres Viisemann is entitled to subscribe a total of 96,850 shares of LHV for the options issued in 2021 and 2022.

Once a year, the members of the Supervisory Board submit a declaration of economic interests and conflicts of economic interests. LHV did not conduct any significant transactions with its Supervisory Board members, their close family members or related parties in 2022, nor are there any valid contracts of that nature from earlier periods. There have been no conflicts of interest and accordingly, no corrective measures have been applied. The Supervisory Board members have no shareholdings above 5% in other companies who are LHV's business partners, suppliers, clients or other related companies.

3.3 Audit Committee

The Audit Committee is an advisory body formed by the Supervisory Board for exercising oversight over the effectiveness of accounting and reporting (including the budgeting process), audit, risk and capital management, the internal control system and internal audit as well as legal and regulatory compliance. The Audit Committee is governed in its activities primarily by the Auditors Activities Act and the rules of procedure established by the Supervisory Board of LHV.

One of the responsibilities of the Audit Committee is to monitor and analyse the processes which must ensure the accurate and efficient preparation of monthly reports and annual accounts, the efficiency of the audit of the group companies' annual accounts, the independence of the audit firm and the auditor representing the audit firm on the basis of the law, and the compliance of their activities with the requirements of the Auditors Activities Act.

The Audit Committee is responsible for making proposals to the Supervisory Board and providing recommendations for the appointment or removal of the audit firm, the appointment or removal of the internal auditor, prevention or elimination of problems and inefficiencies within the organisation and ensuring compliance with laws and regulations and with best practice.

The Audit Committee has at least three members. Members of the Audit Committee are appointed by the Supervisory Board for a term of three years in a manner that should ensure diversity of competences and independence of committee members. The persons selected for the Audit Committee must be sufficiently independent of LHV in order to fulfil their role effectively, and at least two of them must be experts in accounting, finance or law. LHV's employee, member of the Management Board, internal auditor, authorised signatory or audit service provider may not be a member of the Audit Committee. For the appointment of a member of the Audit Committee, the candidate's written consent is required. The size of remuneration paid to the members of the Audit Committee is decided by the Supervisory Board of LHV.

The members of the Audit Committee are Kristel Aarna, Tauno Tats and Urmas Peiker (the Chairman). The term of office of the Audit Committee lasts until 31 March 2023. Further information on the members of the Audit Committee is presented in the Governance of the Group section of this annual report. LHV's Audit Committee members are paid a monthly gross remuneration of EUR 500.

According to its rules of procedure, the Audit Committee meets at least quarterly, however, in 2022 the Audit Committee had ten meetings. At seven meetings, representatives of the Risk Management Department provided the members of the Audit Committee with an overview of various risk management topics, bank and group risk exposures, and the indicators and measures used to monitor and manage them, including matters related to credit risk management, anti-money laundering, management of IT risks, and compliance control. At one meeting (in May), the Head of Credit Risk gave an overview of the updated status of impacts of the war in Ukraine related crisis and the measures taken and the impact to LHV were discussed.

In most meetings, the topics discussed included issues raised by the internal audit, particularly those related to audit reports. The internal auditor gave an overview of the concluded audits. The Audit Committee has reviewed all internal audit reports, discussed the observations raised and formed an opinion on them. At the first meeting of the year, the internal audit work plan for 2022 was approved and at the last meeting held in December instructions for the internal audit work plan for 2023 were discussed. The plan was approved in January 2023.

Four meetings were attended by the external auditor (KPMG). In January and February, the external auditor gave an overview of the 2021 annual report audit process and findings. In October, KPMG provided an overview of the risk assessment, plan, team, and schedule of the financial audit of 2022. At the December meeting, the external auditor presented the findings raised during the interim audit.

As the assignment of KPMG as the external auditor was to expire in 2022, a new tender was organised by the Audit Committee in 2021, the results of which were presented to the General Meeting in March 2022. As a result, the term of appointment of KPMG as the external auditor was prolonged for 2023 by the General Meeting. Thereafter, starting from service provision for the Annual Financial Statements for 2024, the General Meeting appointed PwC as the external auditor.

During the year, the Audit Committee confirmed and approved specific additional services to be provided by the external auditor. No conflicts of interest were identified.

3.4 Remuneration Committee

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

The Remuneration Committee exercises oversight over the remuneration of the Management Board members and employees of LHV, LHV Pank, LHV Finance and LHV Kindlustus, evaluates the implementation of the remuneration policy at least annually and, where necessary, makes proposals for updating the remuneration principles and prepares the related draft resolutions for the Supervisory Board.

The Remuneration Committee has at least three members who are elected from among the members of the Supervisory Board of LHV Pank. The members of the Remuneration Committee are appointed and removed by the Supervisory Board of LHV. A member of the Remuneration Committee is appointed for a term of three years. Members of the Remuneration Committee can be re-elected, and their mandate extended unlimited times. A person elected to the Remuneration Committee must have sufficient relevant knowledge, expertise, and experience in the area of remuneration policy and practices, risk management and control. The size of remuneration payable to the members of the Remuneration Committee is decided by the Supervisory Board of LHV.

Members of LHV's Remuneration Committee are Madis Toomsalu (the chairman), Rain Lõhmus and Andres Viisemann, whose term of office lasts until 11 April 2024. Further information on the members of the Remuneration

Committee is presented in the Governance of the Group section of this annual report. The members of the Remuneration Committee are not remunerated.

In 2022, the Remuneration Committee met once, in January, when the remuneration policy and strategic remuneration principles, the remuneration principles of the Management Board of LHV and the remuneration report for the Management Board of LHV, also benchmarking, and critical and planned positions for 2022 were reviewed. The committee also discussed and made a proposal to the Supervisory Board with regard to the recipients and amounts of share options to be granted for the results for 2021 (LTI plan, i.e., the option programme), as well as the pricing of the share options. In addition, the committee approved the exercise of the options granted in 2019 for the results of 2018 and not to cancel of the options of the employees who left in 2021. The remuneration system, including the goals and remuneration of the members of the Management Board of LHV and its Estonian subsidiaries, and the principles of remunerating the members of the Management Board and persons considered equal to the members of the Management Board were reviewed and submitted for approval to the Supervisory Board.

3.4.1 Remuneration policy

The remuneration principles for LHV and its affiliated companies (Group companies) are described in the internal remuneration policy.

There are no regional differences in the remuneration principles of the Group companies. The most significant differences between the Group companies are that LHV Varahaldus has no remuneration committee and applies specific disclosure requirements and LHV UK applies rules arising from its country of operations.

The purpose of establishing remuneration principles within the Group companies is to ensure the organisation of fair, motivating and transparent remuneration in accordance with the law. A broader goal of the remuneration policy is the recruitment of employees with the capabilities, skills, and experience necessary to implement the strategy, to reconcile the interests of employees and shareholders, to motivate employees and to ensure effective risk management for growing business activities. The remuneration system consists of basic remuneration, compensations, and employee benefits. The Group companies do not provide employees with services at a lower than the market price, do not make payments to a III pillar pension fund at the expense of the employer and do not provide benefits such as a company car, a mobile phone or a laptop for personal use.

The general remuneration strategy is to ensure a motivating pay to achieve long-term goals, creating a strong link between remuneration and the financial results of the Group companies. When measuring the key quantitative and qualitative results and assessing the risk, the Group companies are governed by the following principles:

- The performance criteria are in line with sound and effective risk management principles. The performance criteria established must keep in mind the long-term interests of the Group companies and not stimulate excessive risk-taking or the sale of unsuitable products.
- The performance criteria must not merely contain performance efficiency indicators (e.g., profit, revenue, profitability, expenditure, and volume indicators) or market-based indicators (e.g., stock price or bond yield) but must also be adjusted with risk-based indicators (e.g., capital adequacy, liquidity).
- The criteria used for measuring risks and results must be as closely as possible related to the decisions of the staff member whose results are being appraised and should ensure that the process of determining the remuneration would have an appropriate impact on the staff member’s professional behaviour. In the interest of long-term goals, the assessment and control of risk behaviour will take place at an individual employee level.
- A good balance of both quantitative and qualitative as well as absolute and relative criteria must be used for specifying the performance criteria.
- Quantitative criteria must cover a sufficient period to allow consideration of the risks taken by the staff members or business units. The criteria must be risk-adjusted and contain economic efficiency indicators.
- Examples of qualitative criteria include achievement of strategic objectives, customer satisfaction, adherence to the risk management policy, adherence to internal or external rules of procedure, management skills, creativity, motivation and cooperation with other business units and the internal control function.

The recruitment strategy is to find, engage and keep the best people in the labour market. In determining remuneration, the Group companies are willing to make exceptions rather than restrict its choices with strict remuneration intervals for a specific position. To keep its employees, the Group companies will develop their benefits and compensations in cooperation with their employees. In determining remuneration, the following is taken into account:

- Commitment and results of the employee
- Workload
- Responsibility
- The required level of education
- Management level
- Intensity of work
- The necessary knowledge and experience for the position
- The existence of additional benefits
- The situation in the labour market
- The pay level of the geographical location
- The level of criticality of the position.

The determination of the amount of remuneration must be objective. The remuneration is paid according to the work done and its value, not according to the personality, gender, age, origin, etc. of the employee.

The Group companies apply a general principle that employees should not use personal hedging strategies or remuneration and liability insurance, which would undermine the effectiveness of the hedging of risks integrated into the remuneration policy. In the decisions concerning the remuneration policy, the financial situation and sustainability of the capital base of the Group companies are taken into account.

The Group companies carry out regular self-assessment, the purpose of which is to identify all employees whose professional activities affect or may significantly affect the risk profile of the Group companies. These specified groups of employees are listed in the table below together with ratios between basic and variable remuneration paid in 2022:

Basic and variable remuneration ratio of group of employees who affect Group's risk profile, as at 31 Dec 2022

Senior management	1.14
Staff performing control functions	0.37
Employees with significant impact on the credit risk position (the nominal value of transactions made by the employee is at least 0.5% of LHV Tier 1 own funds and amounts to at least EUR 5 million)	0.77

Self-assessment is carried out once a year at the beginning of the financial year. The assessment covers the past period (including financial results, risk analysis) and takes into account the forthcoming financial year. The specified group of employees that are determined in the course of the self-assessment are required, within one calendar year after exercising the options, to keep the underlying LHV shares in their own possession and to not sell them or to encumber them in any form (including pledge). The specified group of employees are forbidden to transfer the risk of the decline of the share price to other parties, for example, through insurance or certain types of financial instrument. The self-assessment takes account of the degree of job complexity, performance indicators and structure of the Group companies. The analysis is conducted by the Management Board of the Group company in the form of a discussion at a board meeting. The self-assessment is initiated by the Human Resources Department, the compliance of the process and results are assessed by the Compliance Control Department, whose representative is also present at the self-assessment. The Remuneration Committee reviews annually the qualitative and quantitative criteria related to the employee and the self-assessment process, which are used for decision-making. The results of the self-assessment are independently reviewed by the internal audit. The results are summarised and presented to the Supervisory Boards of the Group companies.

Share options

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

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

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

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

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

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

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

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

The granting and size of share options were dependent upon the successful achievement of operational targets of the overall company and the targets of individual Management Board members and employees. In 2022, share options were granted to 167 people in the amount of EUR 7,727 thousand. In 2021, share options were granted to 138 people in the amount of EUR 3,684 thousand. In 2020, share options were granted to 106 people in the amount of EUR 2,443 thousand. The company entered into share option agreements with the members of the Management Boards and employees for a three-year term for the granting of share options.

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

3.5 Nominating Committee

The purpose of the Nominating Committee is to support the Supervisory Boards of LHV, LHV Pank and LHV Finance in matters related to the selection process and eligibility requirements for the members of the Management Boards, Supervisory Boards and the key function holders (if applicable) of the mentioned companies. The responsibilities of the Nominating Committee include individual assessment of the suitability of candidates for members of governing bodies and key function holders, collective suitability assessment of governing bodies, assessment of the composition, structure and activities of the governing bodies, continuous monitoring of the decision-making process by the governing bodies, periodical review and decision-making on the content, format and frequency of the risk information received, ensuring the involvement of Risk Management, Compliance Testing, Internal Audit and other department managers where appropriate in relevant matters. Inter alia, the Nominating Committee is guided by the diversity policy in its activities, which relies on overarching principles stated with ECB guide to fit and proper assessments and EU directive on gender balance on corporate boards. As a result it has been concluded that Tiina Mõis is a member of the Supervisory Board of LHV, Kristel Aarna is a member of the Audit Committee and Relika Mell is a key function holder as the Head of Internal Audit in LHV, in addition LHV's Estonian subsidiaries employ a total of 153 middle-level managers of whom 74 are women; and there are 12 Management Board members including two women.

The Nominating Committee is comprised of at least three members, who are selected from among the members of LHV's Supervisory Board who are also members of LHV Pank's Supervisory Board. The persons elected to the Nominating Committee must have, individually and collectively, sufficient and relevant knowledge, expertise, and experience in the area of the selection process and eligibility requirements, including knowledge of the requirements provided in the EBA and ESMA guidelines for assessing the suitability of members of management bodies and key function holders. The responsibilities, rights and operating principles of the committee and the remuneration of committee members are decided by the Supervisory Board of LHV.

Madis Toomsalu (the chairman), Rain Lõhmus and Andres Viisemann are the members of the Nominating Committee, and their term of office lasts until 18 December 2023. Further information on the members of the Nominating Committee is presented in the Governance of the Group section of this annual report. Members of the Nominating Committee are not remunerated.

Three meetings of the Nominating Committee were held in 2022 during which the regular assessment of the individual and collective suitability of the members of the Management Board and the Supervisory Board and the management bodies, and if necessary, of key function holders, of LHV, LHV Pank and LHV Finance was carried out; the assessment of the individual suitability of the members of the Management Board and two of the Supervisory Board members and the collective suitability the management bodies of LHV Pank in connection with the proposed extension of the term of office of the mentioned members was carried out; the assessment of the individual suitability of the proposed additional members of the Management Board of LHV and the collective suitability of the Management Board of LHV was carried out.

4. Cooperation of Management Board and Supervisory Board

The Management Board and Supervisory Board work in close cooperation to best protect the interests of LHV. The cooperation is, above all, based on an open exchange of views between and within the Management Board and the Supervisory Board.

The Management Board and the Supervisory Board collaborate in developing the goals and strategy of LHV. In managing LHV, the Management Board observes the strategic instructions of the Supervisory Board. The Management Board discusses strategic management issues with the Supervisory Board regularly, honestly, and openly. The Management Board is invited to participate in the monthly meetings of the Supervisory Board.

The Management Board regularly informs the Supervisory Board of all significant circumstances related to LHV's business planning, operations and performance, risk exposures and risk management.

There were no conflicts of interest in the financial year 2022 and accordingly, no corrective measures have been applied.

5. Disclosure of information

LHV treats all shareholders equally and notifies all shareholders of significant circumstances equitably, ensuring quick and equal access to relevant information. Information is disclosed in accordance with the rules established for publicly traded companies.

LHV contributes actively to the development of good relations with the investor community and to raising the awareness of investors. LHV has set up an investor relations website, where it makes all documents and information available to shareholders in accordance with the CGR and legal requirements. LHV publishes monthly financial results as well as next-year and five-year financial forecasts. This information has also been disclosed for 2022 and in 2023. The website of LHV includes the financial calendar for the current and the next year, which outlines the publication dates of the annual report and interim reports and the date of the Annual General Meeting. The disclosed information is available on the website in Estonian, English and Russian. LHV also discloses its annual plans and monthly results in its stock exchange announcements.

LHV organises quarterly investor meetings and webinars, the summaries of which are available on LHV's website. Additional meetings with analysts and presentations and press conferences for analysts, investors or institutional investors are arranged when needed and if requested by stakeholder groups. On its website, LHV explains its goals, directions and opinions about possible trends and changes in the regulatory and business environment. LHV strives to be approachable, transparent, and accountable to investors. In 2019, 2020 and 2023 LHV was named the winner of the Nasdaq Baltic Award – an award which recognises Nasdaq Baltic-listed companies in the area of transparency, sound corporate governance and investor relations – in the main category Investor Relations of the Year. In 2021 and 2023, AS LHV Pank was named the Stock Exchange Member of the Year, for the eight time, for most actively contributing to capital market development initiatives.

LHV's dividend policy, available on LHV's website, sets out the dividend distribution principles, according to which the key precondition for dividend distribution is sustainable compliance with both external and internal regulatory capital requirements. Depending on its growth and/or investment plans, LHV may decide not to pay a dividend. Provided the preconditions are met, LHV will distribute at least 25% of profit before tax attributable to LHV shareholders as dividends together with the related income tax.

6. Financial reporting and auditing

LHV publishes an annual report, which is audited, approved by the Supervisory Board and ultimately approved by the General Meeting.

The number of auditors is determined and the auditors are appointed by the General Meeting, which also determines the auditors' remuneration procedure. The key criteria that the Audit Committee considers in making a proposal to the General Meeting for the appointment of an auditor include the 'auditor's prior experience in the financial services sector and auditing public interest entities, teamwork skills, expertise and ability to involve experts and, in the case of significant differences, the audit fee. Auditors are appointed for a single audit or for a specified term.

In 2022, the auditor provided the group companies with contractual services, including audits of the annual accounts of group companies and reviews of the profits reported in quarterly financial statements, translation services, tax advisory services, advisory services related to the planned amendments to the Investment Funds Act and other assurance services, which are required by the Credit Institutions Act, the Securities Market Act and the Investment Funds Act.

Transactions with related parties are disclosed in Note 24 to the financial statements.

In 2019, the Management Board and the Audit Committee organised a competition for selecting an auditor for the audit of the annual reports for the years 2020–2022. The four biggest internationally recognised audit firms were asked to submit their offers and meetings with their representatives were held. In selecting the auditor, the candidates' previous professional experience, competence, expertise, reliability, transparency of communication and terms offered compared to market terms as well as LHV's business-specific criteria were assessed. An invitation to participate was sent to the three largest audit firms and from the two firms that submitted an offer KPMG Baltics OÜ was selected and appointed as the auditor of group companies for the financial years 2020–2022 at the Annual General Meeting of 2019. In 2022 Annual General Meeting agreed to prolong the agreement by 1 year.

In 2022, the fees paid or payable for the services provided by the auditor amounted to EUR 295 thousand of which EUR 119 thousand was for audits and EUR 176 thousand was for other services.

7. Declaration of conformity

LHV complies with the CGR, with the exception of the following instructions and recommendations for the reasons stated below:

'3.2.2. At least half of the members of the Supervisory Board of the Issuer shall be independent. If the Supervisory Board has an odd number of members, then there may be one independent member less than the number dependent members.'

The Supervisory Board of LHV has no independent members subject to the features set out in the "Requirements of independence" annex to the CGR. LHV is still in the stage of active development and growth, where it has preferred people with long-term management and banking experience as members of the Supervisory Board. These people are also the largest shareholders of LHV. LHV believes that in their capacity as members of the Supervisory Board, the largest shareholders are best motivated to contribute to the management and long-term development of LHV. Based on objective and verifiable data, two of the seven members of the Supervisory Board have significant ownership interests (Rain Lõhmus and related persons hold 21.76% of share capital and Andres Viisemann and related persons hold 11.34% of share capital). No member of the Supervisory Board has the power to appoint, by any means, the majority of the members of the Management Board or Supervisory Board of LHV or to control LHV in some other manner; they are not connected with LHV through a material business interest; they are not related to a shareholder of LHV that exercises control over LHV; they are not employees or business partners of LHV or members of the key personnel of a business partner. Accordingly, LHV does not consider it necessary to apply any corrective measures and considers the Supervisory Board of LHV in its present composition to be suitable, including in terms of independence. Furthermore, when assessing the independence of the members of the Supervisory Board, it has been concluded that their behavioural skills include courage, conviction, and strength to effectively assess and challenge the proposed decisions of other members of the Supervisory Board and being able to resist group-thinking.

Remuneration report

This remuneration report has been prepared in accordance with the Estonian Securities Market Act and provides an overview of the remuneration paid to the Management Board of AS LHV Group (LHV Group) according to the remuneration principles approved by the General Meeting for the 2022 financial year. In the context of the Estonian Securities Market Act, from 1 November 2022 the managers of LHV Group are Madis Toomsalu, the chairman of the Management Board, and Meelis Paakspuu, Martti Singi and Jüri Heero, the members of the Management Board (until 31 October 2022 only Madis Toomsalu, as the sole member of the Management Board, was considered manager of LHV Group in the same context). The remuneration principles of LHV Group are described in the internal remuneration policy of LHV Group, in the section of the annual report titled 'Corporate governance report' and in the remuneration principles approved by the General Meeting.

1. Remuneration of members of Management Board

1.1 Overview

Under the terms of the contract of Management Board member concluded with LHV Group, Madis Toomsalu, the chairman of the Management Board, was paid a monthly basic remuneration of EUR 13 thousand in January 2022, and a monthly basic remuneration of EUR 16 thousand from February 2022, i.e., an annual remuneration of EUR 189 thousand in total in 2022. The Management Board members Meelis Paakspuu, Martti Singi and Jüri Heero were each paid a monthly basic renumeration of EUR 10 thousand in January 2022, and a monthly basic renumeration of EUR 13 thousand from February 2022, i.e., each an annual remuneration of EUR 153 thousand under their contracts of Management Board member concluded with LHV Pank, a subsidiary of LHV Group.

The amounts and payment procedure of the basic remuneration to the members of the Management Board were determined by resolutions of the Supervisory Board of LHV Group. According to the Management Board member contracts concluded with LHV Group and Meelis Paakspuu, Martti Singi and Jüri Heero, the latter do not receive any basic remuneration for the performance of duties of the Management Board members of LHV Group, as their performance is remunerated at the level of LHV Pank and when evaluating the performance of the members of the Management Board, the Remuneration Committee, which makes the associated suggestions to the Supervisory Board, considers among other factors the tasks and activities of each member of the Management Board as a whole on the entire LHV Group level on a consolidated basis.

LHV Group implements a long-term incentive plan (LTI plan) for the payment of performance fees, i.e., the option programme, which has been approved by the Annual General Meeting of the shareholders. Madis Toomsalu, Meelis Paakspuu, Martti Singi and Jüri Heero are subject to the option programmes approved by the resolutions of the General Meeting of LHV Group of 29 April 2015 and of 13 March 2020. These option programmes also set out the conditions for reducing or cancelling options.

In accordance with the resolutions of the Supervisory Board adopted on the basis of the above-mentioned option programmes and the option contracts concluded with the Management Board members, Madis Toomsalu is entitled to receive a total of 860,310 shares of LHV Group as a performance fee for options granted in 2020, 2021, and 2022, of which the options granted in 2022 amount to a total of 149,170 shares in the amount of EUR 312 thousand. Meelis Paakspuu is entitled to receive a total of 527,700 shares of LHV Group as a performance fee for options issued in 2020, 2021, and 2022, of which the options granted in 2022 amount to a total of 114,740 shares in the amount of EUR 240 thousand. Martti Singi and Jüri Heero, are each entitled to receive a total of 506,410 shares of LHV Group as a performance fee for options granted in 2020, 2021, and 2022, of which the options granted in 2022 amount to a total of 114,740 shares in the amount of EUR 240 thousand.

As a result of the option programme, Madis Toomsalu, Meelis Paakspuu, Martti Singi and Jüri Heero are subject to a retention period of at least one year from the date of exercise of the options, during which all of them undertake to hold the shares of LHV Group underlying the options in their ownership and not to transfer or encumber them in any form.

As options are granted for the results of the previous financial year, in 2022 options were granted for the results of 2021. Due to the fact that the vesting period of options is at least three years from the grant date, the options granted in 2019 for the 2018 results were exercised in 2022. In 2022, the right to reduce or cancel options under the option programme established by the shareholders was not exercised.

An overview of the key performance indicators, the remuneration paid to Madis Toomsalu, Meelis Paakspuu, Martti Singi and Jüri Heero on a consolidated basis and the performance indicators of LHV Group over the last five financial years is presented in the table below, while other performance indicators are disclosed in the consolidated accounts of LHV Group:

Remuneration of the Management Board

		2018	2019	2020	2021	2022
Annual basic remuneration *(EUR thousand)*	Madis Toomsalu	136	144	144	156	189
	Meelis Paakspuu	90	105	108	120	153
	Martti Singi	90	105	108	120	153
	Jüri Heero	90	105	108	120	153
Annual performance pay granted *(EUR thousand)*	Madis Toomsalu	205,550 shares 100	333,050 shares 144	370,600 shares 200	340,540 shares 288	149,170 shares 312
	Meelis Paakspuu	123,330 shares 60	173,470 shares 75	200,120 shares 108	212,840 shares 180	114,740 shares 240
	Martti Singi	123,330 shares 60	173,470 shares 75	200,120 shares 108	191,550 shares 162	191,550 shares 162
	Jüri Heero	123,330 shares 60	208,160 shares 90	200,120 shares 108	191,550 shares 162	114,740 shares 240
Consolidated profit of LHV Group *EUR thousand)*		27,190	27,092	39,846	60,263	61,431
Return on equity (ROE)		18.4%	14.0%	17.3%	22.1%	16.5%

LHV Group has not signed any employment contracts and the only persons performing official duties under their Management Board Member contracts in LHV Group are Madis Toomsalu, Meelis Paakspuu, Martti Singi and Jüri Heero. The remuneration of the Management Board members on a consolidated basis are used in calculating the average remuneration of a full-time employee of LHV Group, i.e., the monthly basic salary is considered to be EUR 13.5 thousand and the annual basic salary is considered is considered to be EUR 162 thousand of a full-time employee of LHV Group in 2022.

Madis Toomsalu, Meelis Paakspuu, Martti Singi and Jüri Heero were not granted any exceptions to, or exemptions from, the remuneration principles in 2022. They are not eligible to any financial benefits other than those described in this section for performing their duties in LHV Group and its subsidiaries.

1.2 Compatibility of remuneration with remuneration principles

According to the Management Board member contract concluded between LHV Group and the chairman of the Management Board of LHV Group, Madis Toomsalu, the latter was paid an average monthly remuneration of EUR 15.75 thousand in 2022 as the basic remuneration, which amounts to an annual basic remuneration of EUR 189 thousand. As a performance fee, Madis Toomsalu was granted the right to subscribe to a total of 149,170 shares of LHV Group in the amount of EUR 312 thousand in 2022. In 2022, Madis Toomsalu exercised his right for a performance fee for the results of the 2018 financial year according to the LTI plan and share option agreement concluded with him in 2019. He subscribed to all 333,050 options granted to him in 2019 for the results of the previous financial year in the amount of EUR 144 thousand.

According to the Management Board member contracts concluded between LHV Pank and the other three members of the Management Board of LHV Group, Meelis Paakspuu, Martti Singi and Jüri Heero, they were paid an average monthly remuneration of EUR 12.75 thousand in 2022 as the basic remuneration, which amounts to an annual basic remuneration of EUR 153 thousand on a consolidated basis. As a performance fee, they were each granted the right to subscribe to a total of 114,740 shares of LHV Group in the amount of EUR 240 thousand in 2022. In 2022, they all exercised their rights for performance fees for the results of the 2018 financial year according to the LTI plan and share option agreements concluded with them in 2019. Jüri Heero subscribed to all 208,160 options granted to him in 2019 for the results of the previous financial year in the amount of EUR 90 thousand and Meelis Paakspuu and Martti Singi each subscribed to all 173,470 options granted to them in 2019 for the results of the previous financial year in the amount of EUR 75 thousand.

According to the proposal of the Remuneration Committee, the Supervisory Board of LHV Group amended the monthly basic remuneration of Madis Toomsalu from February 2022 and set it at EUR 16 thousand (was EUR 13 thousand), and the Supervisory Board of LHV Pank amended the monthly basic remuneration of Meelis Paakspuu, Martti Singi and Jüri Heero from February 2022 and set it at EUR 13 thousand (was EUR 10 thousand), while taking into account, among other things, the dedication and performance, the entrepreneurial spirit, the scope, responsibility, and intensity of each duties, the situation on the labour market, the remuneration level and importance of the position in the geographical location, the economic situation of LHV Group and LHV Pank, the current and future business performance and trends in comparison with the companies in the same economic sector, as well as the changed and continuously changing environment. The establishment of the basic remuneration also reflects the principle that basic remuneration should represent a sufficiently large part of the total remuneration to allow, where appropriate, not assigning or paying the performance fee in accordance with the option programme established by the shareholders. Further, considering the fact that LHV Group is the largest domestic financial group and capital provider in Estonia, and in view of the strategic trends and long-term objectives of LHV Group, the Supervisory Boards deemed the monthly remunerations set for 2022 to be such as to motivate the members of the Management Board to act in the best interests of LHV Group and to refrain from acting in personal or other persons' interests, and to act in a way that is fair, transparent, and in compliance with the law.

At the beginning of 2022, the Remuneration Committee, established at the level of the Supervisory Board of LHV Group, also discussed the objectives set for the chairman of the Management Board of LHV Group for 2022, to assess their performance in 2023 and determine their performance fee accordingly. The Remuneration Committee also established the objectives for the other members of the Management Board of LHV Group for 2022 on the LHV Pank level, which were supplemented as part of the renewal of the management structure in the second half of the year, to assess their performance in 2023 and determine their performance fee accordingly. As a result of the achievement of the previously agreed objectives set for the Management Board members on an individual basis and their performance in the difficult year affected by an extremely volatile economic environment, the Supervisory Board of LHV Group, on the proposal of the Remuneration Committee, decided to use the approval of the shareholders of LHV Group to set the performance fee at the maximum amount and to approve the amount of the performance fees for members of Management Board in 2022 at 200% of their annual remuneration in 2021.

The Remuneration Committee also discussed and found, in connection with the exercise of the options granted in 2022, that there had been no subsequent changes to the 2018 financial results and no subsequent material weaknesses had been identified that would indicate that the members of the Management Board had been compromised in the proper performance of their duties in meeting their objectives. As there were no such additional details on their contribution to the 2018 accrual period which would make it necessary to revise the estimate of the number of options to be exercised in 2022 and reduce the number of instruments granted, the Supervisory Board of LHV Group approved the performance bonuses of the members of the Management Board in 2022 for the results of the 2018 financial year and the rights of the Management Board members to subscribe to all options granted to them in 2019 for the results of the previous financial year. Each of the Management Board members exercised their rights.

In 2022, the implementation of the remuneration principles was also reviewed by the Remuneration Committee of LHV Group, whose members have sufficient knowledge and experience in risk management and remuneration. In addition, LHV Group Internal Audit and Compliance Control monitored the compliance of the internal remuneration policy with the legislation on remuneration and other internal rules of LHV Group. There were no observations about non-compliance in 2022.

In the light of the above, in 2022 the remuneration of Madis Toomsalu, Meelis Paakspuu, Martti Singi and Jüri Heero complies with the remuneration principles of LHV Group, which are described in the internal remuneration policy of LHV Group, in the section of the annual report titled 'Corporate governance report' and in the remuneration principles approved by the General Meeting.

Financial results

1. Activities of business areas

Looking backwards, 2022 was a complicated year for LHV. However, we achieved all our financial targets, and our customer satisfaction level was the highest in the banking sector. As geopolitical situation and market sentiment changed in early 2022 it was a year of many challenges: war in Ukraine affected several customers' supply chain; markets were afraid of Estonian country risk making it difficult to issue MREL instruments, financial intermediaries activities decreased; stock markets dropped reducing the investors activity and affecting asset management results. And from regulatory side additional capital requirements were set by both Bank of Estonia and Estonian Financial authority. Year started with negative interest rates and banks trying to minimise the costs of deposits by passing the negative rates further to large customers and ended with highly positive rates and stagnating deposit volumes.

Overall, we managed to fulfil our financial profitability targets, lend more than initially planned and issue capital related instruments. It was complicated year for forecasting and delivering results because everything changed during the year. On average forecasts held in place only 2 months, till they became outdated. Similarly, the business focus changed. The most complicated and new cost factor has been fulfilling all the sanctions requirements. Coping with that LHV had to hire more than 30 additional employees across the entity.

Corporate banking showed a strong growth in 2022 as the portfolio increased 17% YoY despite several Scandinavian-owned banks becoming very active in lending. Our market share is around 18% of the corporate loan market volumes. and the corporate loan portfolio amounted to EUR 1,731 million. The quality of loan portfolio remains strong, with a very low share of non-performing loans.

In retail banking, we focused on home loans, raising awareness of investment services and developing customer-tailored services. Regarding home loans, we focused on process automation and use fully automated decision-making. At the end of the year, the retail loan portfolio totalled EUR 1,456 million, representing approximately 10% market share.

In addition to lending, investment activities have been growing in Estonia. The growth started 2021 with two banks lowering the fees for investments in local stock exchanges and reduced the ticket costs for small investors. In two years, number of LHV shareholders almost tripled.

In financial intermediation, we focused on searching new customers and expanding the product portfolio. As part of regular risk management, we carried through de-risking activities and terminated customer relationship with higher risk customers. In total number of customers remained almost same, but the customer concentration decreased several times. In the beginning of year, the financial intermediaries' activities dropped significantly as sentiment changed, they were not able to receive funding so easily. Our business in the UK is profitable and the revenue base is growing, with revenue generated mainly from interest income, payments, currency exchange, card payment mediation, credit services and maintenance fees.

The total volume of investment funds under the management of LHV Varahaldus reached EUR 1.33 billion in 2022, decreasing by 1% YoY due to the lowering capital markets. Still LHV funds outperformed all other pension funds in Estonia. LHV Varahaldus keeps around 30% market share. As markets dropped, but salaries still increased due to inflation LHV Varahaldus didn't manage to earn success fee.

LHV Kindlustus had difficult year, as being still small business, the results are affected by handful of single items. 2022 had many of them starting from COVID-19 impacts to strikes affecting travel insurance. Starting from 2023, the business line is expected to become profitable.

Financial results for last 7 years

EUR million	2016*	2017*	2018*	2019	2020	2021	2022
Net interest income	30.0	35.5	39.8	47.3	68.5	97.3	129.1
Net fee income	19.2	22.2	26.0	25.7	33.3	42.6	44.7
Net financial income	1.3	1.0	3.4	0.7	1.6	-0.9	-0.6
Net income	50.5	58.7	70.0	73.8	103.4	140.4	173.5
Expenses	28.9	31.9	33.8	39.3	44.0	65.2	89.6
Profit before credit losses	21.7	26.6	36.2	34.6	59.6	75.2	83.9
Impairments	1.5	3.2	5.3	3.2	10.9	3.9	8.1
Tax expense	0.3	1.2	3.8	4.2	8.8	11.0	14.4
Net profit	**19.9**	**22.2**	**27.2**	**27.1**	**39.8**	**60.3**	**61.4**
net profit attributable to owners of the parent	13.7	17.8	19.6	25.2	24.8	38.0	58.3

Volumes for last 7 years

EUR million	31 Dec 2016*	31 Dec 2017*	31 Dec 2018*	31 Dec 2019	31 Dec 2020	31 Dec 2021	31 Dec 2022
Volume of deposits and loans received	778	1,543	1,444	2,727	4,588	6,354	5,487
incl. financial intermediates deposits	32	607	194	376	1,054	2,246	1,281
Volume of net loans	538	732	919	1,687	2,209	2,677	3,209
Volume of assets	935	1,773	1,677	3,032	4,971	6,845	6,135
Volume of funds	974	1,103	1,214	1,374	1,537	1,349	1,332
Volume of custody accounts	1,072	1,287	1,486	1,565	2,066	3,866	3,329

**includes discontinued operations*

The Group's pre-tax profit for 2022 amounted to EUR 75.9 million and net profit totalled EUR 61.4 million. Pre-tax profit is 6% more than a year before. Net interest income grew 33% and net fee income increased 3%. The Group's net income was EUR 173.5 million, an increase of 24% compared to the previous year. Operating expenses amounted to EUR 89.6 million, increasing by 38% over the year. Most of the cost increase has been related investments to LHV UK and increased numbers of employees due to fulfilling the sanctions requirements. The Group achieved the financial forecast published at the beginning of 2022.

Group's cost/income ratio was modest 51.7% due to higher investments. Lowering administrative costs by 10%, what would be in normalised year, the cost income ratio would also be on very decent 46.5% level and net profit higher by 13%.

By the end of December, the total volume of the Group's loan portfolio less impairments amounted to EUR 3,209 million (December 2021: EUR 2,677 million). The volume of portfolio increased 20% in a year. The majority of the loans in the portfolio are corporate loans that increased 17% in a year to EUR 1,731 million (2021: EUR 1,493 million). Retail loans increased 22% in a year, amounting to EUR 1,456 million (2021: EUR 1,203 million).

The volume of the Group's deposits decreased 16% in a year and totalled EUR 4,899 million by the year-end (2021: EUR 5,807 million). The share of demand deposits of all deposits decreased to 95% (31 December 2021: 97%), as interest rates increased and made term deposits more attractive to customers. In 2022 LHV has repaid almost all deposits collected from deposit platforms and only small amount of roll-overs with minimal rates have remained.

LHV Pank's as the largest business unit's net profit for 2022 was EUR 80.9 million, growing 16.8 million compared with previous year. Loans to customers increased by EUR 510 million reaching EUR 3,187 million. During the year, payment intermediaries' deposits decreased by EUR 967 million, whereby core banking customers' deposits increased by EUR 75 million. Total deposits reached EUR 4,957 million by the end of year.

In 2022 LHV Varahaldus earned net loss in the amount of EUR 0.1 million, compared to EUR 0.7 million profit previous year. When comparing the numbers, we need to consider also change in market sentiment, which changed quicker than the reference rate. LHV Varahaldus paid dividends in the amount of EUR 5.1 million (2021: 6.5 million).

LHV Kindlustus had a difficult year, still setting up some products and being affected by several unlucky larger insurance incidences. The company earned EUR 1.5 million of gross income in 2022, compared to EUR 1.1 million in 2021. The company had a net loss of EUR 1.7 million (2021: 0.8 million).

LHV UK did not have any income in 2022 as the company deals with receiving the banking licence in Q1 of 2023. Main activities were related to hiring and discussions with UK's FSA. Overall, the net loss was EUR 11.7 million compared to EUR 3.0 million last year.

LHV Group as a stand-alone entity earned a net profit of EUR 3.5 million (2021: 8.9 million), because the subsidiary LHV Pank paid dividends and guarantee payments to LHV Group.

2. Financial ratios

Financial ratios	2016	2017	2018	2019	2020	2021	2022
Common equity Tier 1 %	15.10	14.02	13.65	12.39	13.26	13.32	15.09
Tier 1 %	15.10	14.02	13.65	13.88	15.56	15.13	17.51
CAD %	20.70	18.30	20.91	17.97	20.50	19.02	20.80
MREL %	12.25	7.78	11.43	8.70	6.38	-	-
MREL-TREA %	-	-	-	-	-	24.00	29.07
MREL-LRE %	-	-	-	-	-	6.90	10.78
Leverage ratio %	6.96	5.01	6.56	6.18	4.40	4.32	6.49
LCR %	221.5	121.3	148.5	144.8	147.9	142.7	139.7
NSFR %	-	140.8	147.6	152.9	152.6	163.4	144
Return on equity (ROE) %*	20.7	17.6	18.4	14.0	17.3	21.1	16.4
Return on assets (ROA) %	2.4	1.6	1.6	1.2	1.0	1.0	0.9
CFROI %	23.9	22.6	25.4	19.0	26.4	26.4	22.5
Cost to income ratio %	57.2	54.4	48.3	53.2	42.5	46.4	51.7
Net interest margin (NIM) %	3.60	2.66	2.34	2.04	1.73	1.66	2.01
Spread %	3.52	2.62	2.32	1.99	1.70	1.63	1.98
Loan to asset %	57.86	41.61	55.24	55.64	44.43	39.11	52.30
Loan to deposit %	69.68	48.00	65.14	62.52	53.63	46.10	65.47
Price to earnings ratio	13.29	13.56	9.75	13.77	14.81	22.14	17.62
Dividend to net profit ratio %	26.70	21.00	21.60	20.17	13.57	13.87	19.45
Dividend per share, EUR	-	0.15	0.16	0.21	0.19	0.29	0.04

Calculation principles

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

capital adequacy levels are calculated as reported in COREP report as at end of each year

MREL = (own funds + qualifying liabilities) / total liabilities * 100

MREL-TREA = (own funds and eligible liabilities) / total risk exposure amount * 100

MREL-LRE = (own funds and eligible liabilities) / leverage ratio exposure measure * 100

LCR, NSFR are calculated as reported in COREP report as of end of each year

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

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

CFROI = operating profit / total equity (average)

cost to income ratio = total operating expenses / total net income * 100

net interest margin (NIM) = net interest income / average interest earning assets * 100

spread = yield on interest earning assets – cost of interest-bearing liabilities

loan to asset = net loans / total assets * 100

loan to deposit = net loans / deposits * 100

price to earnings ratio = share price/net profit / number of shares (average)

dividend to net profit ratio = dividend / net profit

dividend per share = dividend payment during calendar year / number of shares at moment of payment

3. Sensitivity analyses

LHV has four major business lines: Estonian banking, UK banking, asset management and insurance. These business lines are very different in their sensitivities to different risk factors.

Estonian banking is clearly procyclical, meaning that its results are directly affected by macroeconomic developments. In general, there are three major components affecting the Bank's results:

- Interest rate
- Credit losses
- Personnel cost

Every 100 bps increase in interest rates will increase LHV interest income by EUR 11.4 million within the first 12 months. An equivalent interest rate decrease will reduce LHV interest income by EUR 11.4 million.

Credit losses are dependent on the economic situation. LHV has knowledgeable credit risk management, which does not allow excess risk in any economic sector. The rapid growth hides credit losses as a significant part of the portfolio has not yet matured. For understanding the actual levels of credit losses, LHV calculates the credit risk in addition to its current portfolio also for the 12-month-old portfolio. LHV has had very few defaults in history and the only real credit losses the Bank has incurred have been related to fraud rather than wrong credit decisions.

Personnel cost is the biggest cost base for the Bank and equals around 50% of the total costs. LHV has the internal policy to follow the market levels in compensation packages. LHV offers its services mainly through electronic channels. To offer these services effectively LHV has made a decision to develop systems in-house. As a result, the IT team accounts for almost 25% of the total personnel. As the salary levels for IT personnel have been increasing and seem to increase in the nearest future more than for other personnel segments despite the latest changes in market, LHV has forecasted a higher salary growth than its competitors.

UK banking contains two business lines: lending and servicing financial intermediaries. First one is the partially similar to Estonian banking, where credit losses and collateralisation are important. The second is volume business and it is sensitive to macroeconomic developments, but in a way quite different from banking. In general, there are three major components affecting payment intermediaries' business results:

- Trading activities between countries
- FX rates volatility
- AML risks

The first two are very similar, as most payment intermediaries offer transferring/converting certain currency to another region/currency within a short time frame. The need for such business grows when there are either solid business relationships between countries or when one currency becomes very volatile and businesses need to hedge their positions quickly. The third area is related to regulations and controlling the AML risk: the financial intermediaries' business models are moving towards more regulations, but from LHV side, bank doesn't see the full chain of transfers meaning that partially it has to rely on financial intermediaries own activities. LHV does its own controls over transactions and also does on- and off-site inspections to mitigate the risk.

Asset management is almost insensitive to macroeconomic developments. The performance depends on two major items:

- Pension fund management
- Political risk

Pension fund management is key to results. Starting from Q4 2019 the calculation of fund management fees changed to performance bonus principle. LHV has targeted to beat the agreed benchmark over longer period, but not in the coming years. LHV has outperformed all its competitors over the past 10 years.

Another large risk side of the asset management is political risk. In every year during the last 5 years there has been some larger changes in the pension funds management fee calculation. LHV has been successful of managing these changes and being able to deliver good result despite of the constant changes in legislation.

Insurance is relatively insensitive to macroeconomic developments as well. It's more open to fraud, pandemic, weather and strikes risks. The insurance uses reinsurance for reducing the risk to acceptable level. Still the profitability will be hit in case of under or over hedging the risk.

4. Shares and bonds issued by LHV

Over the last years LHV has been rapidly growing local universal bank with a clear niche towards financial intermediaries.

Over the last years the business model has widened and includes several other financial activities. All these activities have required capital, partially funded from profits and partially issuing capital related instruments. In 2022 LHV issued new shares in amount of EUR 35 million. Including all share capital related transactions, the number of shares increased by 5.32%

The profits and investments of LHV are not only reflected in the share price, but also in the dividends and interest paid on subordinated bonds.

LHV Group has several securities outstanding:

Shares and bonds outstanding as at 31 Dec 2022	ISIN	Issuer	Outstanding amount	Maturity	Listing
Common share	EE3100073644	AS LHV Group	315,424,530	-	Nasdaq Tallinn main list
Additional Tier 1 subordinated bond	EE3300111780	AS LHV Group	20,000,000	perpetual	not listed
Additional Tier 1 subordinated bond	EE3300001668	AS LHV Group	15,000,000	perpetual	not listed
Additional Tier 1 subordinated bond	EE3300002856	AS LHV Group	20,000,000	perpetual	not listed
Tier 2 subordinated bond	EE3300001791	AS LHV Group	35,000,000	30.09.2030	Nasdaq Baltic bond list
Tier 2 subordinated bond	EE3300111558	AS LHV Group	40,000,000	28.11.2028	Nasdaq Baltic bond list
Senior unsecured bond	XS2379637767	AS LHV Group	200,000,000	09.09.2025	Euronext Dublin
Covered bond	XS2185891111	AS LHV Pank	250,000,000	09.06.2025	Euronext Dublin
Retained covered bond	XS2225426936	AS LHV Pank	100,000,000	28.02.2024	Euronext Dublin

In mid-2022 the share split with 1/10 ratio was carried out, where each shareholder received additional 9 shares for 1 existing share.

LHV Group has very simple share capital structure – there is only one class of shares with nominal value of 0.1 EUR, each share gives 1 voting right.

The shares of LHV Group are traded on NASDAQ Tallinn main list since May 2016

Shareholder statistics as at 31 Dec 2022	
Number of shareholders	32 001
Number of countries represented	46
Share of Estonian residents	76.4%
Share of Estonian residents including two founders	95.1%
Share of legal entities	69.7%
Share of private individuals	27.3%
Share of institutional investors	1.5%
Share of nominee accounts	1.4%
Share of LHV clients	86.3%

46.5% of shares belonged to the members of the Supervisory Board and Management Board and to their related parties.

Geographical distribution of shareholders as at 31 Dec 2022	Percentage
Estonia	76.1%
Switzerland	19.7%
Latvia	2.4%
United States	0.8%
United Kingdom	0.4%
Portugal	0.2%
Lithuania	0.1%
Germany	0.0%
Finland	0.0%
Russian Federation	0.0%
Other	0.2%

Ten largest shareholders as at 31 Dec 2022	Number of shares	Percentage
AS Lõhmus Holdings	37,162,070	11.8%
Viisemann Investments AG	33,910,370	10.8%
Rain Lõhmus	25,449,470	8.1%
Krenno OÜ	12,265,090	3.9%
AS Genteel	11,310,000	3.6%
AS AMALFI	10,875,280	3.5%
Ambient Sound Investments OÜ	10,828,210	3.4%
SIA KRUGMANS	7,188,990	2.3%
Bonaares OÜ	6,691,020	2.1%
OÜ Merona Systems	6,037,590	1.9%

Starting from 2021, when LHV and one another bank significantly lowered prices for trading Baltic equities, the number of new investors has been growing rapidly. LHV's investor base has grown by 12 thousand investors within a year.

5. Share price

The year 2022 started with the share price of EUR 43.2 (after split EUR 4.33). During the year the share price lowered by 22.7%, reaching EUR 3.34 by the end of 2022, outperforming the OMX general indexes.

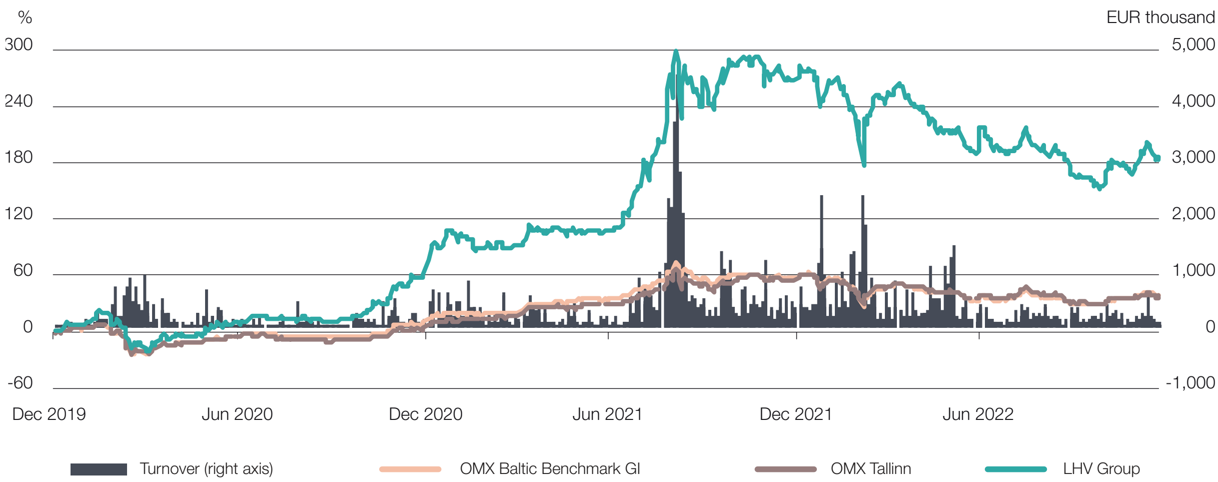
In 2022, the lowest traded price was EUR 2.9 and the highest EUR 4.5. The weighted average price was EUR 3.72.

In total 21.9 million shares were traded with monetary turnover of EUR 81.5 million. Based on the year-end stock price, LHV's market value was EUR 1,054 million, which is EUR 191.5 million lower compared to last year.

Graph below presents LHV Group share performance compared to OMX Tallinn index and OMX Baltics benchmark index. In last three years, LHV Group's share has outperformed both indexes and has risen 196%, when comparison indexes have increased by 76% and 79%, respectively.

Regarding dividend policy, LHV strives to achieve long-term dividend growth without negatively impacting the Group's targeted capital ratios. The annual dividend together with the related taxes should account for 25% of pre-tax profit. Each year's dividend is assessed in the light of prevailing economic conditions and the Group's earnings, growth possibilities, regulatory requirements, and capital position. In addition, LHV has made a conservative decision not to have trading positions in LHV shares nor use them as collateral. In case of exercising share option programmes, the shareholders have delegated the right of issuing new shares to the Supervisory Board.

LHV share price change and daily turnover



Overview of the Group’s subsidiaries in 2022

1. AS LHV Pank group

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. Our competitive edge is the best customer experience and offering customers the best options for growing their money. Our services for business customers include flexible and tailored financing solutions and management of daily financial affairs, and our services for financial intermediaries include a single banking platform for both EUR and GBP payments. LHV Pank’s products and services are simple, transparent, and relevant. We communicate with customers mainly through modern digital channels and use the resulting cost savings for the benefit of our customers by keeping the prices of everyday banking services affordable.

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

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

1.1 Business activities

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

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

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

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

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

return on equity (on net profit attributable to shareholders) was 24.9%, the cost/income ratio was 39.9% and risk cost ratio was 0.1%.

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

1.2 Development activities

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

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

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

1.3 Organisation

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

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

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

1.4 Sustainability at LHV Pank

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

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

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

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

Financial results

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

Volumes

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

2. AS LHV Varahaldus group

AS LHV Varahaldus is a fund management company focusing mostly on active investment strategies. As of the end of 2022, the funds under management include one UCITS fund, seven II pillar and three III pillar pension funds. The investment management department is supported by the risk management, operations, and sales units.

AS LHV Varahahaldus has a 100% owned subsidiary VH Incorporation Entity OÜ, which was established in 2021. The sole purpose of VH Incorporation Entity OÜ is to establish companies for real estate transactions of pension funds.

2022 was a very difficult year for financial markets. When in 2021 major stock market indices in the developed world showed very strong returns, opposite was unfortunately true in 2022. Persistently high inflation and subsequently rising interest rates, anxiety about potential recession, turbulence in energy prices and war in Ukraine all contributed to negative trends in markets. MSCI World, S&P500 and Euro Stoxx 50 all experienced strong declines, falling in euro-denominated value by 12.8%, 14.4% and 9.5%, respectively. It was especially difficult for technology companies with Nasdaq, after strong returns in previous years, declined in euro-denominated value by 28.9%.

LHV offers a wide range of investment strategies to its customers within the II pillar pension system, including a passively managed index fund, one Article 8 of DDA ESG/green fund and five actively managed funds with varying risk classes. In recent years actively managed funds have concentrated more on alternative asset classes and non-listed securities, guided by the belief that over a long investment horizon the average annual expected return will exceed that of publicly traded securities. The size of the funds as well as changes in regulation have allowed LHV to invest more into local non-listed assets, such as real estate, as well as provide financing to Estonian companies through debt securities. LHV's pension funds have been among the biggest and most active institutional investors in Estonia in recent years. Allocation between different asset classes should also provide better diversification and risk return relationship and make the results of the funds less dependent on the returns of the biggest stock markets.

This was very much the case in 2022. Three of the biggest actively managed II pillar pension funds M, L and XL had net returns of 2.4%, 3.6% and 2.8%, respectively. These were also the only pension funds in the Estonian market with positive returns in 2022 with the biggest contribution coming from real estate and debt securities issued to local companies. It was more complicated year for actively managed conservative funds S and XS, which lost 2.2% and 3.6%, respectively, but were still ahead of other competing funds in the Estonian pension funds market with similar strategies due to shorter duration and thus less exposure to rising interest rates. LHV II pillar fund Indeks lost 14.3% and ESG oriented fund Roheline with high stock market exposure and narrower investment universe declined by 19.8%.

2022 was also the first year after the pension reform, which gave the clients in II pillar the chance to opt out of the system and withdraw collected funds with at least five months' notice at any time. While at the beginning of the year outflows and number of applications were still significant, the last nine months showed declining interest in leaving the II pillar. By the end of the year number of new clients joining the II pillar system already outnumber those planning to leave with monthly inflows also exceeding the outflows related to opting out. Stability, better visibility regarding assets under management and organic growth has again been restored.

Despite positive returns in three of the biggest funds, negative results of other funds as well as withdrawals related to opting out of the pension system meant that total assets under management in 2022 fell slightly, being around EUR 1.3 billion by year end.

LHV with its seven funds in the II pillar pension system is the chosen fund manager for more than 130 thousand people. The company manages the savings for 25.1% of II pillar pension system participants and holds a market share of 31.2% in terms of assets under management. By the end of the year, LHV's three III pillar pension funds had close to 33 thousand customers.

Net loss of LHV Varahaldus was EUR 0.1 million in 2022, a result strongly affected by the higher amortisation cost related to withdrawals from the II pillar as well as weaker than expected returns for own assets in pension funds. No fund was also eligible for performance fee based on 2022 results.

Financial results of LHV Varahaldus

EUR million	2022	2021	change
Net fee income	8.0	11.4	-30%
Other finance income	-0.1	0.6	-125%
Total net operating income	7.8	12.0	-35%
Operating expenses	-7.1	-10.0	-29%
Income tax expenses	-0.8	-1.2	-33%
Net profit	**-0.1**	**0.7**	**-115%**

Volumes

EUR million	31 Dec 2022	31 Dec 2021	change
Assets under management	1,332	1,349	-1%
Number of customers in pension funds (thousands)	164	170	-4%

3. AS LHV Kindlustus

AS LHV Kindlustus is a non-life insurance company, which was founded in May 2020. The shareholders of LHV Kindlustus are LHV Group (65%) and Toveko Invest OÜ (35%). The company received the licence for insurance activities from the EFSA on 29 December 2020 and started selling insurance policies as of 1 January 2021. Thus, the year 2022 was the second year for active business for LHV Kindlustus.

LHV Kindlustus has launched 12 product solutions since 2021. The main products are motor own damage insurance, motor third-party liability insurance, travel insurance, property and liability insurance, payment protection insurance and extended warranty insurance. The products are sold for both private and commercial clients. As a new product LHV Kindlustus introduced health insurance for commercial clients in cooperation with Confido in October 2022. LHV Kindlustus works on amending the product range for both private and commercial customers.

LHV Kindlustus implements a multi-channel sales strategy by using online, insurance intermediaries, brokers, and direct sales. The focus is on supporting LHV Pank and Euronics with best insurance solutions. In 2022 LHV Kindlustus started cooperation with the largest insurance brokers in Estonia, which increased the share of broker channel to 41% by the year-end.

The year 2022 was challenging year for the whole insurance market. Rapidly growing inflation influenced the loss amounts and the average loss per claim increased in all product lines. At the same time insurers observed also increase in claim frequency figures. This results in significant growth of the average premium per policy for the customers, which may make insurance less affordable in the future.

As of 31 December 2022, LHV Kindlustus had 218 thousand active insurance contracts and 150 thousand customers. The biggest share of active contracts and customers is related to the extended warranty insurance portfolio, followed by the LHV Pank credit card travel and purchase insurance. However, the year 2022 showed rapid growth in the number of motor and private property insurance contracts.

The annual gross written premium amount for LHV Kindlustus was EUR 17.1 million (254% growth from previous year). On an annual basis, the gross written premium for motor own damage and motor third party liability insurance combined was EUR 11.3 million. The share of property and travel insurance formed both 8% of the total portfolio amount.

LHV Kindlustus earned EUR 8.4 million as net premiums and paid out EUR 4.8 million in claim payments to the customers. Customer satisfaction index was a high 97% in 2022.

Net losses incurred amounted to EUR 6.2 million. The company registered 6980 new claims in 2022, out of which 1583 are still open as of 31 December 2022. The gross claim provisions including for IBNR (incurred but not reported) claims and UALE (unallocated loss adjustment expenses) formed EUR 2.4 million as of 31 December 2022.

Net financial loss for 2022 amounted to EUR 1.7 million. The year-end result was worse than expected due the changing market environment, however company's statement of financial position stays strong with solvency ratio being above 125% at the year-end.

4. LHV UK Limited

LHV UK, a wholly owned subsidiary, was founded in February 2021 with the aim of becoming a separate and independent bank in the UK within the LHV Group. After the bank has been established and has received the necessary regulatory permissions, all existing business of LHV Pank's UK branch will be transferred to LHV UK.

LHV Group has decided to establish a bank in the UK to separate LHV Pank's current business activities in Estonia and the UK. LHV UK will focus on servicing international payment institutions, for whom it is often important to communicate with the local bank and people. Unbundling also allows for better compliance with regulatory and supervisory requirements. A clear separation will also make it possible to better highlight the results and value to be created for investors.

In 2022, LHV UK was focusing on banking licence application process and submitted its application in March 2022. It was also focusing on building up the organisation and hiring the key executives; opening offices in London and Leeds; building up the information systems and separating IT infrastructure from LHV Pank. The company was capitalised with an additional GBP 34.1 million in 2022.

In October 2022, LHV UK acquired the SME lending business from Bank North. The acquisition of Manchester-based bank's loan business provides a strong platform for commencing the SME loan activity. As a result of the transaction, LHV UK acquired an SME loan portfolio of GBP 17.9 million, 20 sales and customer service, credit analysis and IT employees, modern loan management software and cooperation agreements with major loan brokers.

LHV UK was registered in the Financial Conduct Authority's financial services register on in November 2022 and thereby gained the right to start issuing SME loans in the UK.

In 2023, LHV UK will focus on obtaining the banking licence, staffing the company, building up the information systems and IT infrastructure and transferring business and people from LHV Pank's UK Branch and LHV Pank. The banking licence is subject to regulatory approval by the Prudential Regulatory Authority and Financial Conduct Authority.

LHV UK's growth plans in the UK are underpinned by three business lines: providing banking services for financial intermediaries, SME lending and banking services for e-merchants.

For financial intermediaries, LHV UK will offer a single platform enabling banking services in GBP and EUR. Under its long-term vision, LHV UK sees itself as one of the leaders in modern banking in Europe, contributing to the development of financial services without borders. The company positions itself as a new generation bank that can integrate and be the link between traditional banking and the new generation of financial services through the use of open banking. The company focuses on greater integration with Europe's banking infrastructure. The company's existing services and technological standards allow it to provide services to international customers and financial technology companies, including major payment institutions.

For SME's, LHV UK offers commercial term loans starting from the amount of GBP 0.5 million secured by commercial real estate and other guarantees. The main sales channel is credit brokers. The lending operations were started in and around Manchester, but in the future, there are plans to create an additional sales and customer service team in London.

The operating principle and objectives of LHV UK will be as follows:

- **Leader in Open Banking**. LHV UK will be a full-service banking services provider for businesses. LHV UK sees itself as an innovative link between businesses and the banking infrastructure and believes it is a prime example of how open banking can work for businesses.
- **Digital.** LHV UK will be a digital bank for the modern digital society and businesses that adopt e-commerce solutions. LHV UK will use cutting-edge modern technology that allows its customers to incorporate innovative and unique products that fit their goals.
- **User experience driven.** LHV UK will be customer centric, focused on putting the customer at the heart of every product and creating a better user experience. The company believes in incremental improvements at every step of the customer service process. It will be easy to communicate with LHV UK – open an account, access the account through e-channels or API connection, and make transactions.

5. Everypay AS

EveryPay AS (Everypay) was established in 2012. EveryPay is developing and operating a cloud-based payment gateway platform for digital payments acceptance in digital environments and is Payment Card Industry Data Security Standard level 1 certified. EveryPay's customers are financial institutions that need the platform as a part of their online payments' acceptance offering or for their internal needs. EveryPay is not providing services to the merchants directly.

EveryPay is operating primarily in the Baltics, servicing commercial banks and a few smaller financial institutions.

In April 2022, LHV Group acquired 100% of EveryPay shares. In 2022 EveryPay focused less on marketing and did not actively sell the platform to new financial institutions outside the Baltics. EveryPay worked on adding new functionalities including new payment methods like Apple Pay, Google Pay, easier and more dynamic card payments integration option Secure Elements and optimisation of open banking payment methods. The focus is on adding new payment methods to cover relevant regions and support LHV Group's strategic goals.

2022 was relatively stable year for e-commerce after a very quick growth during the COVID-19 pandemic in 2021. Companies continued working on their e-commerce and self-service environments and improving payment flows. Optimising self-service environments and digitalising purchasing processes, invoicing and cashflow management became more relevant in achieving efficiency in business processes. Open banking payments are gaining more traction and the major players on the market are replacing old bank link payments with open banking payments.

E-purchases in Estonia showed growth of 38% in eleven months 2022 compared to same period in previous year. In payment methods, the growths were 70% in card payments, 108% in open banking payments, and 9% in bank link payments. EveryPay's annual processing volumes grew 81% in 2022.

Consolidated financial statements

Risk management

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

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

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

Risk framework

Risk management principles, roles and responsibilities

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

Goals, measures and controls

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

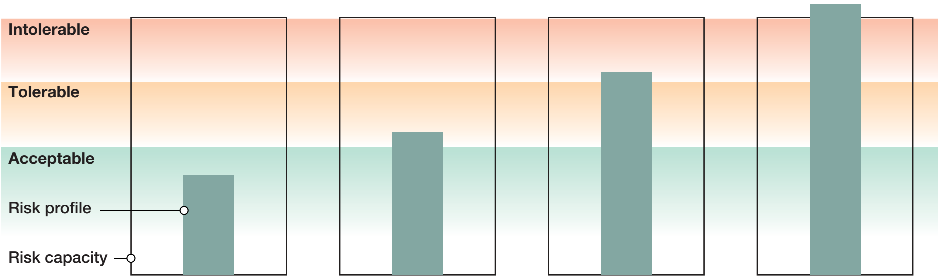
Internal and external reporting

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

- Qualitative guidance is worded simply and adopts the terminology commonly used in the organisation and in the business plan.
- Quantitative limits are set at a level that is sufficiently detailed to capture all key risk categories and sub-categories, but at the same time sufficiently aggregated to maintain each metric of relevance to the group-wide risk profile of LHV. Where quantification is possible, the acceptable, tolerable and intolerable amounts of risk are defined as follows:

- acceptable – the amount of risk allowed to be taken under normal business conditions;
- tolerable – the amount of risk that gives a warning signal: the increase of risk must be properly assessed, and an action plan defined to return to the acceptable area; the assessment results and the action plan must be reported at least to the Management Board of LHV;
- intolerable – a hard limit violation, the level of risk LHV does not wish to exceed under any circumstances: immediate action must be taken to return at least to the tolerable area; the violation, assessment results and an action plan must be reported to the Supervisory Board of LHV.

Risk appetite framework



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

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

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

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

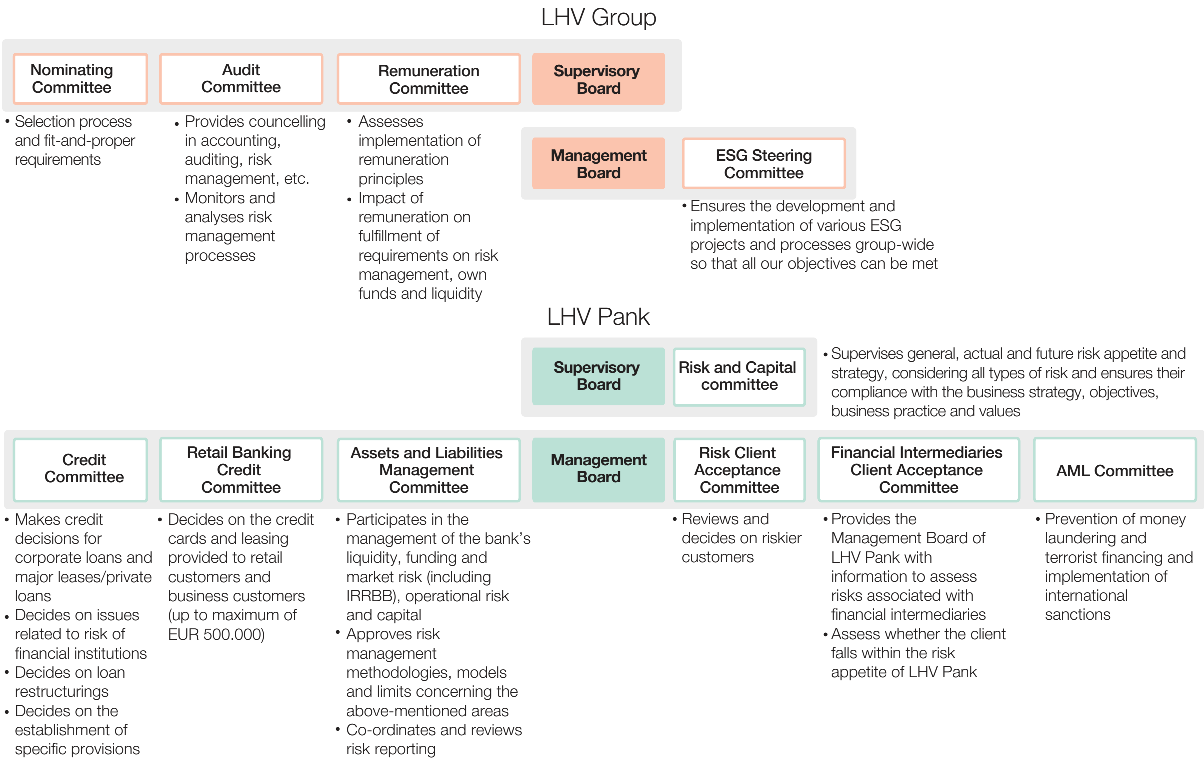
Risk capacity – the maximum amount of risk LHV is capable to take given its capital base, its risk management and control capabilities, and its regulatory constraints.

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

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

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

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



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

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

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

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

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

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

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

Risk management framework

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

1. Capital management

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

The goals of the Group's capital management are:

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

The Group considers net own funds, as defined in the capital adequacy regulation, as capital. Its own funds consist of Common Equity Tier 1 (CET1) capital, Additional Tier 1 capital and Tier 2 capital. The amount of net own funds that the Group managed as at 31 December 2022 was EUR 473,931 thousand (31 December 2021: EUR 385,357 thousand). The goals of the Group's capital management are set based on both regulative requirements and additional internal buffer requirements.

The Group follows these general principles in its capital management:

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

In addition to LHV Group, separate regulative capital requirements have been set for several subsidiaries: LHV Pank on stand-alone level, LHV Varahaldus and LHV Kindlustus. After receiving the credit institutions licence there will be separate regulative requirements valid also for LHV UK Ltd. All these companies follow both regulatory requirements and the Group's capitalisation targets in daily capital management.

Capital management in 2022

The Group is strongly capitalised. The Group's CET1 capital base was strengthened by the issue of new shares to investors in the first half of the year. Additionally, the Group also issued EUR 20 million of AT1 subordinated bonds in the Q4 of 2022.

The Group's total capital adequacy ratio equalled 20.80% as at 31 December 2022 (31 December 2021: 19.97%). The Tier 1 and CET 1 capital ratios equalled 17.51% and 15.09% as at 31 December 2022, respectively (31 December 2021: 16.08% and 14.27%, respectively). All of the capital ratios increased during the year despite rapid growth in risk weighted assets because of the Group's raising of additional capital externally and also strong internal capital generation through profits. Thus, as of 31 December 2022, the Group was in compliance with all of the regulatory and internal capital requirements.

LHV Group issued additional EUR 100 million of MREL eligible bonds in November 2022 in order to fulfil the MREL target ratios.

As of 31 December 2022, the Group's MREL-TREA ratio equalled 29.07% (31 December 2021: 24.00%) and the Group's MREL-LRE ratio equalled 10.78% (31 December 2021: 6.9%), thus complying with the regulatory requirements.

The Group's leverage ratio amounted to 6.49% as of 31 December 2022 (31 December 2021 4.32%).

Capital base

EUR thousand	31 Dec 2022	31 Dec 2021
Paid-in share capital	31,542	29,864
Share premium	141,186	97,361
Legal reserves transferred from net profit	4,713	4,713
Other reserves	-1,441	47
Accumulated profit/(deficit)	170,010	179,746
Intangible assets (subtracted)	-23,333	-14,473
Profit for accounting period (COREP)	25,611	0
Deductions	-369	-128
CET1 capital elements or deductions	-456	-12,209
CET1 instruments of financial sector entities where the institution does not have significant investment	-181	-5,236
CET1 instruments of financial sector entities where the institution has a significant investment	-3,351	-4,328
Tier 1 capital	**343,931**	**275,357**
Additional Tier 1 capital	55,000	35,000
Total Tier 1 capital	**398,931**	**310,357**
Subordinated debt	75,000	75,000
Total Tier 2 capital	**75,000**	**75,000**
Exceeding limitations of subordinated debt and preference shares	0	0
Net own funds for capital adequacy calculation	**473,931**	**385,357**

Capital requirements

Central governments and central bank under standard method	0	0
Credit institutions and investment companies under standard method	11,553	10,465
Companies under standard method	1,204,523	1,141,853
Retail claims under standard method	219,031	212,860
Public sector under standard method	0	6
Housing real estate under standard method	513,483	291,338
Overdue claims under standard method	8,004	19,332
Investment funds' shares under standard method	186	190
Other assets under standard method	102,697	93,939
Total capital requirements for covering the credit risk and counterparty credit risk	**2,059,477**	**1,769,983**
Capital requirement against foreign currency risk under standard method	18,324	3,489
Capital requirement against interest position risk under standard method	0	0
Capital requirement against equity portfolio risks under standard method	740	2,079
Capital requirement against credit valuation adjustment risks under standard method	2,228	1,211
Capital requirement for operational risk under base method	197,920	152,778
Total capital requirements for adequacy calculation	**2,278,689**	**1,929,540**
Capital adequacy (%)	**20.80**	**19.97**
Tier 1 Capital Ratio (%)	**17.51**	**16.08**
Core Tier 1 Capital Ratio (%)	**15.09**	**14.27**

2. Credit risk

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

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

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

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

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

Impact from COVID-19 and cooling economy

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

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

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

ESG risks in credit risk

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

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

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

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

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

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

General ESG principles

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

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

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

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

Credit portfolio distribution by risk classification

	Risk level	2022	2021
Environmental and climate change risk (E)	High	10.9%	14.4%
	Medium	54.7%	52.7%
	Low	34.3%	32.8%
Social risk (S)	High	10.9%	15.2%
	Medium	55.9%	54.8%
	Low	33.1%	30.0%

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

2.1 Credit risk measurement and distribution

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

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

b) debt securities and derivatives

c) loans to legal entities

d) loans to individuals

a) Due from banks and investment companies

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

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

b) Debt securities and derivatives

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

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

c) Loans to legal entities

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

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

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

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

d) Loans to private individuals

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

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

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

Credit risk measurement

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

Models used for credit worthiness assessment

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

Credit risk grading

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

1) obligor risk characteristics
- for corporate exposures: financial statements, management experience, support from parent company, etc.
- for retail exposures: financial statements or personal income information, socio-demographic information, behavioural information, etc.

2) transactional risk characteristics – type of product, remaining balance, etc.

3) delinquency characteristics from internal and external sources.

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

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

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

- **Retail**

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

- **Corporate**

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

- **Treasury**

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

- **Credit risk ratings**

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

Internal rating scale for corporate loans and mapping of external ratings

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

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

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

Collateral

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

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

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

The main collateral types for loans and advances are:

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

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

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

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

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

2.2 Expected credit loss measurement

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

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

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

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

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

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

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

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

Change in credit quality since initial recognition

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

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

2.2.1 Significant increase in credit risk

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

Quantitative criteria

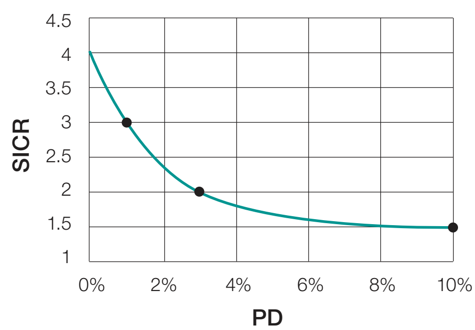
The remaining lifetime PD at the reporting date has increased, compared to the lifetime PD expected at the reporting date when the exposure was first recognised, if it exceeds the relevant threshold per the table below:

Retail portfolio

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

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

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



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

Backstop

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

Low credit risk exemption

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

2.2.2 Definition of default and credit-impaired assets

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

Quantitative criteria

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

Qualitative criteria

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

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

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

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

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

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

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

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

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

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

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

ECL calculations are based on four components:

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

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

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

Where:

t = 0

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

for a 12-month ECL estimate

T = 12 months; for a lifetime ECL estimate

T = expected life of the lending exposure

PDt – marginal PD for month t

LGDt – LGD as estimated for month t

EADt – exposure amount, incl. expected

drawdowns of undrawn commitments, at month t

dt – discount factor for month t

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

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

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

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

For the defaulted exposures, ECL is computed as:

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

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

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

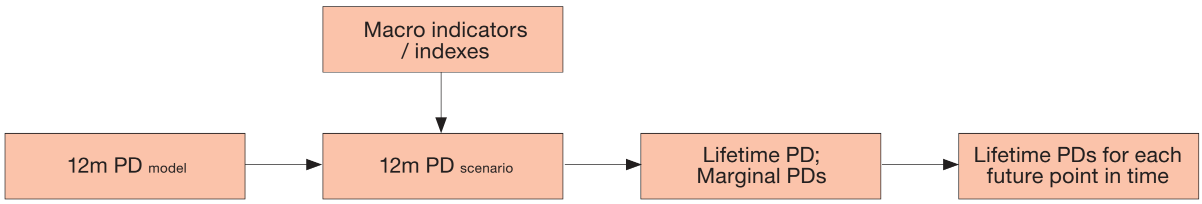
	IFRS 9 parameters
PD	• 12-month PD; lifetime PD broken down further into marginal probabilities for sub-periods • Forward-looking PiT estimate, reflecting assessment of current and future economic conditions, and a range of possible future outcomes • No regulatory floors or margins of conservatism applied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

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

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

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

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



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

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

Feeding LGDs from underlying models into ECL model

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

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

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

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

Feeding CCF estimates from underlying models into ECL model

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

2.2.4 Forward-looking information incorporated in the ECL model

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

Mathematically:

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

Where:

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

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

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

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

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

Where:

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

Selected indicators for private person credit portfolios

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

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

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

Selected indicators for companies

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

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

The following conclusions were drawn from the analysis:

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

Economic variable assumptions

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

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

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

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

Assumptions in companies ECL estimate, valid at 31 Dec 2022

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

Nominal growth

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

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

Valid at 31 Dec 2022

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

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

Valid at 31 Dec 2021

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

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

Assumptions in companies ECL estimate, valid at 31 Dec 2021

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

Nominal growth

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

2.2.5 Loss allowance

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

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

Allowances based on individual assessments

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

Minimum provisioning level for loans that become non-performing

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

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

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

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

2.2.6 Write-off policy

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

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

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

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

Credit cards, consumer loan and hire purchase

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

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

Leasing, private and business loans

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

2.2.7 Modifications of financial assets

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

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

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

2.3 Credit risk exposure

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

2.3.1 Risk concentration

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

EUR thousand	Note	Estonia	Germany	Other EU	USA	UK	Other	Total
Due from banks and investment companies	10	1,938,118	0	329,496	24,727	189,847	101	2,482,288
Financial assets at fair value	11	8,715	7	601	21	3	6	9,354
Financial assets measured at amortised cost	11	236,130	4,966	123,134	0	0	0	364,230
Loans and advances to customers	12	3,161,803	612	17,867	622	22,974	4,694	3,208,572
Receivables from customers	14	21,019	0	0	0	0	0	21,019
Other financial assets	15	24	0	0	100	0	0	124
Total financial assets		**5,365,809**	**5,585**	**471,098**	**25,470**	**212,823**	**4,801**	**6,085,587**
Amounts owed to central banks (TLTRO)	17	147,841	0	0	0	0	0	147,841
Deposits from customers	17	3,617,636	5,292	794,100	14,890	439,714	28,883	4,900,515
Loans received and debt securities in issue	17	438,642	0	0	0	0	0	438,642
Subordinated debt	20	130,843	0	0	0	0	0	130,843
Accounts payable and other financial liabilities	18	84,125	0	0	0	0	0	84,125
Financial liabilities at fair value	11	3,850	0	0	0	0	0	3,850
Total financial liabilities		**4,422,937**	**5,292**	**794,100**	**14,890**	**439,714**	**28,883**	**5,705,816**

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

EUR thousand	Note	Estonia	Germany	Other EU	USA	UK	Other	Total
Due from banks and investment companies	10	3,611,765	0	76,010	29,900	269,593	42	**3,987,310**
Financial assets at fair value	11	55,949	6	79,709	30	2	159	**135,855**
Loans and advances to customers	12	2,652,960	781	17,292	903	849	4,375	**2,677,160**
Receivables from customers	14	9,752	0	0	0	0	0	**9,752**
Other financial assets	15	117	0	0	2,119	0	0	**2,236**
Total financial assets		**6,330,543**	**787**	**173,011**	**32,952**	**270,444**	**4,576**	**6,812,313**
Amounts owed to central banks (TLTRO)	17	197,461	0	0	0	0	0	**197,461**
Deposits from customers	17	3,449,803	113,798	1,484,106	62,541	631,356	66,013	**5,807,617**
Loans received and senior bonds	17	349,146	0	0	0	0	0	**349,146**
Subordinated debt	20	110,378	0	0	0	0	0	**110,378**
Accounts payable and other financial liabilities	18	49,262	0	0	0	0	0	**49,262**
Financial liabilities at fair value	11	157	0	0	0	0	0	**157**
Total financial liabilities		**4,156,207**	**113,798**	**1,484,106**	**62,541**	**631,356**	**66,013**	**6,514,021**

2.3.2 Distribution of loans granted by industry

Distribution of net loans granted by industry is presented in the table below.

Distribution of loans granted by industry (net)

EUR thousand	31 Dec 2022	%	31 Dec 2021	%
Individuals	1,245,358	38.8%	1,009,927	37.7%
Agriculture	79,448	2.5%	68,459	2.6%
Mining and quarrying	1,630	0.1%	2,019	0.1%
Manufacturing	154,069	4.8%	151,638	5.7%
Energy	93,170	2.9%	58,504	2.2%
Water and utilities	29,129	0.9%	23,505	0.9%
Construction	109,941	3.4%	83,011	3.1%
Wholesale and retail	150,330	4.7%	131,630	4.9%
Transport and logistics	24,831	0.8%	28,752	1.1%
Hotels and restaurants	33,803	1.1%	28,680	1.1%
Information and communication	13,810	0.4%	10,878	0.4%
Financial services	127,950	4.0%	85,505	3.2%
Real estate	790,309	24.6%	654,325	24.4%
Professional, scientific, and technical activities	75,173	2.3%	44,669	1.7%
Administrative activities	116,551	3.6%	114,446	4.3%
Public management	79,145	2.5%	97,622	3.6%
Education	5,445	0.2%	4,328	0.2%
Health	14,767	0.5%	13,139	0.5%
Art and entertainment	55,271	1.7%	48,832	1.8%
Other servicing activities	8,442	0.3%	17,291	0.6%
Total (Note 13)	**3,208,572**	**100.0%**	**2,677,160**	**100.0%**

2.3.3 Loan portfolio by ratings

Distribution of legal entity financing by internal ratings

EUR thousand	31 Dec 2022	31 Dec 2021	Grading
3 low credit risk	0	0	Investment grade
4 low credit risk	34,069	49,031	
5 low credit risk	48,410	64,896	
6 low credit risk	365,287	277,748	
7 medium credit risk	432,662	369,284	
8 medium credit risk	591,503	479,112	
9 heightened credit risk	196,840	184,268	
10 high credit risk	39,252	32,516	Non-investment grade
11 high credit risk	55,843	48,780	(incl. special monitoring)
12 non-satisfactory rating	18,912	19,111	
13 insolvent	717	1,619	Default
Total corporates	1,783,495	1,526,365	
Retail SMEs	179,720	135,361	
Total	1,963,215	1,661,726	

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

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

EUR thousand	31 Dec 2022	31 Dec 2021
3 low credit risk	100,000	100,000
4 low credit risk	35,000	32,091
5 low credit risk	10,078	8,425
6 low credit risk	106,057	80,577
7 medium credit risk	81,181	143,825
8 medium credit risk	143,622	192,424
9 heightened credit risk	109,119	80,244
10 high credit risk	7,742	4,491
11 high credit risk	3,346	6,833
12 non-satisfactory rating	1,718	103
13 insolvent	0	214
Non-rated (retail clients)	85,142	96,387
Total	**683,005**	**745,614**

2.4 Quality of credit portfolio

2.4.1 Distribution of loans by economic sectors and stages

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

EUR thousand	Stage 1	Stage 2	Stage 3	Allowance for credit losses	Total
Individuals	1,127,636	115,433	5,446	-3,157	1,245,358
Agriculture	76,817	2,743	0	-112	79,448
Mining and quarrying	1,038	519	122	-49	1,630
Manufacturing	126,670	28,626	81	-1,308	154,069
Energy	92,186	1,305	0	-321	93,170
Water and utilities	29,314	90	0	-275	29,129
Construction	106,356	5,243	58	-1,716	109,941
Wholesale and retail	144,586	6,599	69	-924	150,330
Transport and logistics	15,198	10,323	1	-691	24,831
Hotels and restaurants	11,844	23,446	44	-1,531	33,803
Information and communication	10,839	3,004	1	-34	13,810
Financial services	119,436	9,337	0	-823	127,950
Real estate	757,443	34,577	1,558	-3,269	790,309
Professional, scientific, and technical activities	68,001	7,313	30	-171	75,173
Administrative activities	115,072	4,563	32	-3,116	116,551
Public management	79,272	0	0	-127	79,145
Education	5,151	596	0	-302	5,445
Health	14,312	541	0	-86	14,767
Art and entertainment	27,619	30,225	15	-2,588	55,271
Other servicing activities	6,970	1,503	11	-42	8,442
Total	**2,935,760**	**285,986**	**7,468**	**-20,642**	
Allowance for credit losses	-10,938	-7,632	-2,072		
Total loan portfolio	**2,924,822**	**278,354**	**5,396**		**3,208,572**

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

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

2.4.2 Distribution of loans by loan types and stages

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

Loans by loan types and stages

EUR thousand	Stage 1	Stage 2	Stage 3	Purchased or Initiated credit impaired	Allowance for credit losses	Total
Corporate lending	1,709,606	145,015	637	0	-15,498	1,839,760
Private lending	997,972	105,887	4,244	0	-1,014	1,107,089
Leasing	122,832	28,419	1,442	0	-2,009	150,684
Consumer financing	94,818	6,661	1,145	0	-2,108	100,516
Investment financing	10,532	4	0	0	-13	10,523
Total as at 31 Dec 2022	**2,935,760**	**285,986**	**7,468**	**0**	**-20,642**	**3,208,572**
Corporate lending	1,382,163	182,474	2,378	0	-15,288	1,551,727
Private lending	777,868	107,810	9,949	0	-1,062	894,565
Leasing	120,117	18,848	2,162	0	-1,250	139,877
Consumer financing	71,408	5,367	1,353	0	-1,320	76,808
Investment financing	14,189	0	123	0	-129	14,183
Total as at 31 Dec 2021	**2,365,745**	**314,499**	**15,965**	**0**	**-19,049**	**2,677,160**

Stage 1

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	1,382,153	532,050	-335,414	130,817	-9,826	1,699,780
Private lending	777,861	248,818	40,533	-69,240	-283	997,689
Leasing	120,141	55,078	-23,881	-28,506	-374	122,458
Consumer financing	71,419	54,373	-37,439	6,465	-442	94,376
Investment financing	14,189	1,865	10,173	-15,695	-13	10,519
Total	**2,365,763**	**892,184**	**-346,028**	**23,841**	**-10,938**	**2,924,822**

Stage 2

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

Stage 3

EUR thousand	Initial	New	Unwind	Migration	Allowance for credit losses	Total
Corporate lending	2,377	0	-1,430	-310	-301	336
Private lending	9,949	159	-2,124	-3,740	-154	4,090
Leasing	2,160	44	-158	-604	-577	865
Consumer financing	1,353	276	-804	320	-1,040	105
Investment financing	123	0	-472	349	0	0
Total	**15,962**	**479**	**-4,988**	**-3,985**	**-2,072**	**5,396**

2.4.3 Transfers between stages

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

Inter-stage transfers in 2022 (gross)

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

2.4.4 Loans against collateral

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

Loans against collateral as at 31 Dec 2022 (net)

EUR thousand	Corporate lending	Consumer financing	Investment financing	Leasing	Private lending	Total
Listed securities	0	0	9,184	0	0	**9,184**
Unlisted equity securities	23,137	0	0	0	2,031	**25,168**
Mortgages, real estate	1,078,341	0	0	0	1,085,002	**2,163,343**
Guarantee of KredEx and Rural Development Foundation	37,543	0	0	0	2,521	**40,064**
Pledges of rights of claim	117,570	0	0	0	0	**117,570**
Deposits	3,361	0	818	0	2,000	**6,179**
Leased assets	0	0	0	84,054	0	**84,054**
Others	51,821	0	0	0	6159	**57,980**
Unsecured loans	527,987	100,516	521	66,630	9,376	**705,030**
Total	**1,839,760**	**100,516**	**10,523**	**150,684**	**1,107,089**	**3,208,572**

Loans against collateral as at 31 Dec 2021 (net)

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

Over and under-collateralised loans (net)

	Over-collateralised loans		Under-collateralised loans		Total	
EUR thousand	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral
31 Dec 2022	**1,740,958**	**2,825,209**	**1,467,614**	**762,610**	**3,208,572**	**3,587,819**
Corporate lending	732,788	1,075,592	1,106,972	579,012	1,839,760	1,654,604
Consumer financing	0	0	100,517	0	100,516	0
Investment financing	8,093	29,836	2,430	1,909	10,523	31,745
Leasing	17,684	30,171	133,000	66,370	150,684	96,541
Private lending	982,393	1,689,610	124,696	115,319	1,107,089	1,804,929
31 Dec 2021	**1,272,430**	**2,445,616**	**1,404,730**	**782,907**	**2,677,160**	**3,228,523**
Corporate lending	472,746	880,020	1,078,981	603,640	1,551,727	1,483,660
Consumer financing	0	0	76,808	0	76,808	0
Investment financing	14,183	150,842	0	0	14,183	150,842
Leasing	17,501	31,903	122,376	60,251	139,877	92,154
Private lending	768,000	1,382,851	126,565	119,016	894,565	1,501,867

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

	Over-collateralised loans		Under-collateralised loans		Total	
EUR thousand	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral	Carrying value	Fair value of collateral
Stage 1	**1,573,312**	**2,572,693**	**1,351,510**	**691,963**	**2,924,822**	**3,264,656**
Corporate lending	665,681	984,695	1,034,100	532,506	1,699,781	1,517,201
Consumer financing	0	0	94,376	0	94,376	0
Investment financing	8,089	29,830	2430	1909	10519	31739
Leasing	13,591	22,756	108,867	53,171	122,458	75,927
Private lending	885,952	1,535,412	111,737	104,377	997,689	1,639,789
Stage 2	**162,483**	**240,281**	**115,871**	**70,607**	**278,354**	**310,888**
Corporate lending	66,772	89,656	72,872	46,506	139,644	136,162
Consumer financing	0	0	6,035	0	6,035	0
Investment financing	3	6	1	0	4	6
Leasing	3,339	6,139	24,022	13,159	27,361	19,298
Private lending	92,369	144,480	12,941	10,942	105,310	155,422
Stage 3	**5,161**	**12,235**	**235**	**41**	**5,396**	**12,276**
Corporate lending	335	1,241	0	0	335	1,241
Consumer financing	0	0	105	0	105	0
Investment financing	0	0	0	0	0	0
Leasing	753	1,276	112	41	865	1,317
Private lending	4,073	9,718	18	0	4,091	9,718

2.4.5 ECL sensitivity analysis

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

Loan portfolio as at 31 Dec 2022

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

Loan portfolio as at 31 Dec 2021

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

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

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

Retail portfolio

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

Corporate portfolio

- Estimated portfolio PiT PD values for each scenario

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

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

31 Dec 2022

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

31 Dec 2021

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

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

Impact on ECL, 31 Dec 2022

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

Impact on ECL, 31 Dec 2021

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

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

2022

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

2021

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

3. Market risk

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

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

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

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

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

3.1 Foreign currency risk

Foreign currency risk arises from the mismatch of the Group's foreign currency assets and liabilities. Most items in the Group's statement of financial position are denominated in euros but a mismatch could result from the foreign currency transactions of the Bank's customers. Additionally, there is some foreign currency risk inherent in the fund units of own-managed pension funds that must be held by LHV Varahaldus as prescribed by legislation.

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

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

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

Impact on statement of profit or loss

EUR thousand	2022	2021
USD exchange rate +/- 7%	+/-262	+/-204
SEK exchange rate +/- 7%	+/-2	+/-6
GBP exchange rate +/- 7%	+/-1,221	+/-17
CHF exchange rate +/- 7%	+/-3	+/-0

Open currency exposures

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

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

Currency risk exposures as at 31 Dec 2022

EUR thousand	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Financial assets bearing currency risk								
Due from banks and investment companies	10	2,255,128	1,466	197,580	2,538	17,806	7,769	**2,482,288**
Investments in debt and equity securities	11	373,514	0	2	1	26	42	**373,584**
Loans and advances to customers	12	3,180,499	74	22,306	385	5,068	241	**3,208,572**
Receivables from customers	14	25,865	5	751	241	-4,512	-1,330	**21,019**
Other financial assets	15	124	0	0	0	0	0	**124**
Total financial assets bearing currency risk		**5,835,130**	**1,545**	**220,639**	**3,164**	**18,388**	**6,721**	**6,085,587**
Financial liabilities bearing currency risk								
Amounts owed to central banks (TLTRO)	17	147,841	0	0	0	0	0	**147,841**
Deposits from customers	17	4,533,633	5,323	193,442	10,968	148,058	9,089	**4,900,515**
Loans received and debt securities in issue	17	438,642	0	0	0	0	0	**438,642**
Financial liabilities at fair value	11	0	0	0	0	3,849	1	**3,850**
Accounts payable and other financial liabilities	18	65,099	19	9,757	172	8,987	91	84,125
Subordinated debt	20	130,843	0	0	0	0	0	130,843
Total financial liabilities bearing currency risk		**5,316,058**	**5,343**	**203,199**	**11,140**	**160,895**	**9,182**	**5,705,817**
Open gross position derivative assets at contractual value		0	3,757	0	8,001	157,565	2,371	**171,694**
Open gross position derivative liabilities at contractual value		171,694	0	0	0	0	0	**171,694**
Open foreign currency position		**347,377**	**-40**	**17,440**	**25**	**15,058**	**-89**	**379,770**

Currency risk exposures as at 31 Dec 2021

EUR thousand	Note	EUR	CHF	GBP	SEK	USD	Other	Total
Financial assets bearing currency risk								
Due from banks and investment companies	10	3,687,255	1,367	277,043	1,075	18,433	2,137	**3,987,310**
Investments in debt and equity securities	11	135,812	0	1	0	37	4	**135,855**
Loans and advances to customers	12	2,669,321	18	463	396	6,616	346	**2,677,160**
Receivables from customers	14	7,818	0	491	226	167	1,050	**9,752**
Other financial assets	15	117	0	0	0	2,119	0	**2,236**
Total financial assets bearing currency risk		**6,500,323**	**1,385**	**277,998**	**1,697**	**27,372**	**3,538**	**6,812,313**
Financial liabilities bearing currency risk								
Amounts owed to central banks (TLTRO)	17	197,461	0	0	0	0	0	**197,461**
Deposits from customers	17	5,409,103	5,037	271,784	7,837	101,149	12,708	**5,807,617**
Loans received and debt securities in issue	17	349,146	0	0	0	0	0	**349,146**
Financial liabilities at fair value	11	0	0	0	16	123	18	**157**
Accounts payable and other financial liabilities	18	36,376	218	6,456	217	5,676	319	**49,262**
Subordinated debt	20	110,378	0	0	0	0	0	**110,378**
Total financial liabilities bearing currency risk		**6,102,464**	**5,254**	**278,240**	**8,070**	**106,948**	**13,045**	**6,514,021**
Open gross position derivative assets at contractual value		0	3,872	0	6,454	82,496	9,026	**101,848**
Open gross position derivative liabilities at contractual value		101,848	0	0	0	0	0	**101,848**
Open foreign currency position		**296,011**	**3**	**-242**	**81**	**2,920**	**-481**	**298,292**

3.2 Price risk

Price risk arises from securities held by the Group in the liquidity portfolio, trading portfolio and investment portfolios (Notes 11, 12). The portfolios mainly comprise securities held by LHV Pank. Additionally, the pension fund units held by LHV Varahaldus are subject to price risk. The investment portfolio of LHV Kindlustus carries minimal price risk.

Price risk is measured by estimating the potential loss that can be incurred by the Group in a stress scenario. The loss from price risk in the stress scenario should not exceed a prescribed percentage of the Group's net own funds. In LHV Pank, the ALCO has set additional limits on the size of the trading and investment portfolios. There are criteria in place for acceptable credit ratings as well as other parameters of the debt securities that can be held by the Bank. In LHV Kindlustus, there are also criteria in place for the securities that can be included in the investment portfolio. Pursuant to the Investment Funds Act, LHV Varahaldus as a pension fund management company is obliged to hold a minimum of 0.5% of the number of units in each of the II pillar pension funds managed by it.

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

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

EUR thousand	2022	2021
Equity securities and fund units +/-25%	+/-269	+/-182
II pillar pension fund units +/-5%	+/-374	+/-381
Debt securities +/-0.5% and +/-2.0%	+/-15	+/-2,550

It can be seen that the majority of the Group's price risk results from the debt securities held in the Bank's liquidity portfolio. However, most of these debt securities are valued at amortised cost, so the materialisation of the price risk would not result in an immediate impact on the statement of profit or loss.

The Bank does not hold significant amounts of equity securities (see Note 12); accordingly, the sensitivity to change in the market price of these positions is marginal. Some price risk is also contributed from holdings of II pillar pension fund units by LHV Varahaldus. The price risk of the investment portfolio of LHV Kindlustus is low.

3.3 Interest rate risk

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

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

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

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

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

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

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

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

- The repricing terms of demand deposits of households and non-financial corporations vary between 1 day and 5 years, depending on their interest rate sensitivity.
- For deposits of financial institutions, immediate repricing is assumed.
- A 0% interest rate floor is applied to deposits of retail customers.
- For term deposits, contractual maturities are used.
- For loans, contract-specific interest rate floors are used.
- Conditional prepayment rate is used in the assessment of the early repayment of loans.
- In the case of items accounted for off the statement of financial position (e.g., loan commitments and credit limits), the credit conversion factor is included in the model and it is assumed that the use of the limit will increase on a straight-line basis until the expiry date.

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

Stress tests scenarios impacts, valid at 31 Dec 2022

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

Stress tests scenarios impacts, valid at 31 Dec 2021

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

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

Interest rate sensitivity gap as at 31 Dec 2022

EUR thousand	Note	Up to 3 months	3-12 months	1-5 years	Over 5 years	Subtotal	Accrued interest	Impair-ments	Total
Financial assets									
Due from banks and investment companies	10	2,482,288	0	0	0	2,482,288	0	0	2,482,288
Financial assets at fair value (debt securities)	11	0	0	294	471	765	0	0	765
Financial assets measured at amortised cost (debt securities)	11	236,130	4,965	122,671	0	363,766	555	-91	364,230
Loans and advances to customers	14	1,475,880	1,622,099	90,799	31,931	3,220,709	8,505	-20,642	3,208,572
Total		**4,194,298**	**1,627,064**	**213,764**	**32,402**	**6,067,528**	**9,060**	**-20,733**	**6,055,855**
Financial liabilities									
Amounts owed to central banks (TLTRO)	17	0	150,000	0	0	150,000	-2,159	0	147,841
Deposits from customers	17	3,775,569	304,833	819,416	0	4,899,818	697	0	4,900,515
Loans received and debt securities in issue	17	0	0	437,956	0	437,956	686	0	438,642
Subordinated debt	20	0	40,000	90,000	0	130,000	843	0	130,843
Total		**3,775,569**	**494,833**	**1,347,372**	**0**	**5,617,774**	**67**	**0**	**5,617,841**
Net interest sensitivity gap		**418,729**	**1,132,231**	**-1,133,608**	**32,402**	**449,754**			

Interest rate sensitivity gap as at 31 Dec 2021

EUR thousand	Note	Up to 3 months	3-12 months	1-5 years	Over 5 years	Subtotal	Accrued interest	Impair-ments	Total
Financial assets									
Due from banks and investment companies	10	3,987,310	0	0	0	3,987,310	0	0	3,987,310
Financial assets at fair value (debt securities)	11	46,000	3,350	77,218	152	126,720	784	0	127,504
Loans and advances to customers	12	1,214,410	1,375,207	85,595	15,869	2,691,081	5,128	-19,049	2,677,160
Total		**5,247,720**	**1,378,557**	**162,813**	**16,021**	**6,805,111**	**5,912**	**-19,049**	**6,791,974**
Financial liabilities									
Amounts owed to central banks (TLTRO)	17	0	0	200,000	0	200,000	-2,539	0	197,461
Deposits from customers	17	2,249,662	101,744	3,457,466	0	5,808,872	-1,255	0	5,807,617
Loans received and debt securities in issue	17	0	0	350,000	0	350,000	-854	0	349,146
Subordinated debt	20	0	0	0	110,000	110,000	378	0	110,378
Total		**2,249,662**	**101,744**	**4,007,466**	**110,000**	**6,468,872**	**-4,270**	**0**	**6,464,602**
Net interest sensitivity gap		**2,998,058**	**1,276,813**	**-3,844,653**	**-93,979**	**336,239**			

3.4 Credit valuation adjustment risk

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

4. Liquidity risk

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

The Group assesses liquidity risk from the following separate perspectives:

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

In the context of liquidity risk management, LHV Pank is the most relevant out of all Group companies, as the largest share of the Group's funding is raised by the Bank (mostly through deposits) that are used for funding long term assets (mostly loans).

The Group's liquidity risk management is documented in the liquidity and funding risk management policy and other internal rules, which set out the Group's funding strategy and liquidity risk appetite, early warning indicators and various internal procedures such as reporting routines and contingency plans. LHV Pank's Treasury Department and Assets and Liabilities Management Committee (ALCO) have key roles in managing liquidity risk as the first line of defence. The Financial Risks Department and the Internal Audit Department are responsible for the second and third line of defence functions, respectively.

The Group's liquidity risk appetite is defined through the following metrics:

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

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

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

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

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

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

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

Liquidity management in 2022

The Group's volume of deposits declined during 2022, mainly driven due to lower volumes of deposits received from financial intermediaries. However, these deposits are considered unstable from the perspective of the Group's liquidity management, so they are not used for funding the Group's lending activities. The Group also repaid ahead of the original maturity date part of the TLTRO funding that it had received from the ECB. The repaid amount was EUR 50 million and the outstanding balance of TLTRO that remains as of 31 December 2022 is EUR 150 million.

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

Ratio	Regulatory requirement	Actual 31 Dec 2022	Actual 31 Dec 2021
LCR	Minimum 100%	139.7%	142.7%
NSFR	Minimum 100%	144.0%	163.4%

The level of the LCR ratio slightly decreased over the reporting year. On one hand, the ratio was positively impacted by the declining volumes of financial intermediaries' deposits (high levels of financial intermediaries deposits pull the LCR ratio downwards) but on the other hand, the relatively large growth of the Group's loan book and the reduction of its liquid assets had a negative impact on the LCR.

The NSFR ratio declined over the year due to the Group's asset growth exceeding the growth in long term funding sources. However, the level of the ratio still exceeds the regulatory and internal requirements with a wide headroom.

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

Financial assets and liabilities by maturities 31 Dec 2022

EUR thousand	Note	On demand	Up to 3 months	3-12 Months	1-5 Years	Over 5 years	Total	Carrying amount
Liabilities by contractual maturity dates								
Amounts owed to central banks (TLTRO)		0	0	0	150,082		**150,082**	**147,348**
Deposits from customers	17	4,643,310	95,807	143,740	18,082	0	**4,900,939**	**4,900,515**
Loans received and debt securities in issue		0	0	2,000	452,250	0	**454,250**	**439,135**
Subordinated debt	20	0	2,406	46,694	105,538	0	**154,638**	**130,843**
Accounts payable and other financial liabilities	18		84,125	0	0	0	**84,125**	**84,125**
Unused loan commitments	23		601,093	0	0	0	**601,093**	**0**
Financial guarantees by contractual amounts	23		52,577	0	0	0	**52,577**	**0**
Foreign exchange derivatives (gross settled)			171,694	0	0	0	**171,694**	**0**
Financial liabilities at fair value	11		3,850	0	0	0	**3,850**	**3,850**
Total liabilities		**4,643,310**	**1,011,552**	**192,434**	**725,952**	**0**	**6,573,248**	**5,705,816**
Assets held for managing liquidity risk by contractual maturity dates								
Due from banks and investment companies	10	2,428,288	0	0	0	0	**2,428,288**	**2,428,288**
Financial assets at amortised cost (debt securities)	11	0	236,130	4,966	123,519	471	**365,086**	**365,313**
Loans and advances to customers	12	0	186,547	487,298	2,115,010	1,258,430	**4,047,285**	**3,208,572**
Receivables from customers	14	0	21,019	0	0	0	**21,019**	**21,019**
Other financial assets	15	124	0	0	0	0	**124**	**124**
Foreign exchange derivatives (gross settled)		0	171,694	0	0	0	**171,694**	**0**
Total assets held for managing liquidity risk		**2,428,412**	**615,390**	**492,264**	**2,238,529**	**1,258,901**	**7,033,496**	**6,023,316**
Maturity gap from assets and liabilities		**-2,214,898**	**-396,162**	**299,830**	**1,512,577**	**1,258,901**	**460,248**	

Financial assets and liabilities by maturities 31 Dec 2021

EUR thousand	Note	On demand	Up to 3 months	3-12 Months	1-5 Years	Over 5 years	Total	Carrying amount
Liabilities by contractual maturity dates								
Amounts owed to central banks (TLTRO)		0	0	0	197,000	0	**197,000**	**197,461**
Deposits from customers	17	5,648,302	55,271	101,784	2,288	0	**5,807,645**	**5,807,617**
Loans received and debt securities in issue		0	0	1,140	352,538	0	**353,678**	**349,146**
Subordinated debt	20	0	1,903	5,727	124,341	0	**131,971**	**110,378**
Accounts payable and other financial liabilities	18	0	49,262	0	0	0	**49,262**	**49,262**
Unused loan commitments	23	0	679,579	0	0	0	**679,579**	**0**
Financial guarantees by contractual amounts	23	0	49,409	0	0	0	**49,409**	**0**
Foreign exchange derivatives (gross settled)		0	101,848	0	0	0	**101,848**	**0**
Financial liabilities at fair value	11	0	157	0	0	0	**157**	**157**
Total liabilities		**5,648,302**	**937,429**	**108,651**	**676,167**	**0**	**7,370,549**	**6,514,021**
Assets held for managing liquidity risk by contractual maturity dates								
Due from banks and investment companies	10	3,987,310	0	0	0	0	**3,987,310**	**3,987,310**
Financial assets at amortised cost (debt securities)	11	0	46,047	3,387	77,915	155	**127,504**	**127,876**
Loans and advances to customers	12	0	173,534	431,582	1,661,341	924,419	**3,190,876**	**2,677,160**
Receivables from customers	14	0	9,752	0	0	0	**9,752**	**9,752**
Other financial assets	15	2,236	0	0	0	0	**2,236**	**2,236**
Foreign exchange derivatives (gross settled)		0	101,848	0	0	0	**101,848**	**0**
Total assets held for managing liquidity risk		**3,989,546**	**331,181**	**434,969**	**1,739,256**	**924,574**	**7,419,526**	**6,804,334**
Maturity gap from assets and liabilities		**-1,658,756**	**-606,248**	**326,318**	**1,063,089**	**924,574**	**48,977**	

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

Assets and liabilities by classification of current and non-current

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Current assets			
Due from central bank	10	2,390,964	3,874,284
Due from credit institutions	10	87,933	106,838
Due from investment companies	10	3,391	6,188
Financial assets at fair value through profit or loss	11	1,880	128,235
Financial assets at amortised cost	11	241,005	0
Loans and advances to customers	12	508,297	455,929
Receivables from customers	14	21,019	9,752
Other assets	15	6,775	3,471
Total current assets		**3,261,264**	**4,584,697**
Non-current assets			
Financial assets at fair value through profit or loss	11	7,474	7,620
Financial assets at amortised cost	11	123,225	0
Loans and advances to customers	14	2,700,275	2,221,231
Other financial assets	15	124	2,236
Tangible assets	16	16,858	8,474
Intangible assets	16	13,854	11,825
Strategic financial investments at fair value through profit or loss	6	1,180	5,236
Goodwill	6	10,748	3,614
Total non-current assets		**2,873,738**	**2,260,236**
Total assets	**5**	**6,135,002**	**6,844,933**
Liabilities			
Current liabilities			
Deposits from customers	17	4,882,954	5,805,336
Loans received	17	2,000	0
Financial liabilities at fair value through profit or loss	11	3,850	157
Accounts payable and other liabilities	18	93,305	55,751
Total current liabilities		**4,982,109**	**5,861,244**
Non-current liabilities			
Amounts owed to central banks (TLTRO)	17	147,841	197,461
Deposits from customers	17	17,561	2,281
Loans received and debt securities in issue	17	436,642	349,146
Subordinated debt	20	130,000	110,000
Total non-current liabilities		**732,044**	**658,888**
Total liabilities	**5**	**5,714,153**	**6,520,132**

5. Operational risk

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

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

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

Risk and control self-assessment

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

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

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

Operational risk event and business continuity management

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

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

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

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

Key risk indicators

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

Capital calculation

The operational risk capital charge is calculated based on the basic indicator approach and amounts to EUR 15,834 thousand as at 31 December 2022 (31 December 2021: EUR 12,222 thousand).

ICT and information security risk management

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

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

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

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

6. Compliance risk

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

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

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

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

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

7. Anti-money laundering (AML)

7.1. AML/CTF governance

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

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

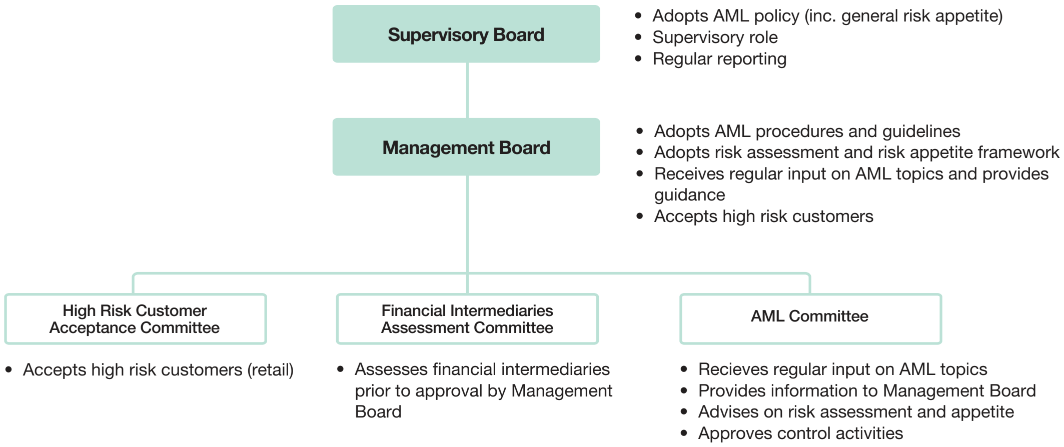
All lines of defence follow a risk-based approach in assessing products, services, customers, and countries. Proper risk mitigating measures, including customer due diligence (CDD) and EDD), are applied on the basis of risk-based screening and monitoring activities and defined risk levels. A high level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

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

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

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

7.2 AML governance structure



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

7.3 AML/KYC measures

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

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

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

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

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

7.4 Banking Services

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

7.5 Estonian AML system and the outlook

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

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

8. Other risks

8.1 Underwriting risk

Underwriting risk is one of the most important risks for the insurance subsidiary reflecting the core business of insurance, i.e., taking and managing insurance risk. The most important aspect of underwriting risk is the insurance premium and reserve risk deriving from the possible inadequacy of the pricing of insurance contracts and the assumptions used in the assessment of contractual liabilities.

Underwriting risk includes catastrophe accumulation risk deriving from extreme or extraordinary events (e.g. windstorms, floods, hailstorms, damage attributable to human causes) during which the materialisation of risks insured under individual insurance contracts accumulate extraordinarily.

Above all, underwriting risk involves risks associated with pricing, technical provisions, and adequacy of the reinsurance cover.

Underwriting risk is managed and controlled via the following processes:

- establishment of the insurance subsidiary's risk strategy in accordance with the business strategy;
- using actuarial analysis and sound assumptions in pricing of insurance contracts;
- calculation of technical provisions and solvency capital requirement (SCR) by using Solvency II standard formula and holding the necessary liquid assets accordingly;
- assessment of loss reserving assumptions, performing liability adequacy tests and monitoring the profitability of the insurance portfolio;
- conduct regular/irregular own risk and solvency assessment (ORSA);
- use of the reinsurance programme for reinsuring major risks.

8.2 Strategic and business risk

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

8.3 Country risk

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

Consolidated statement of profit or loss and other comprehensive income

EUR thousand	Note	2022	2021
Interest income		152,413	124,641
incl. interest income based on the effective interest rate		146,216	118,990
Interest expense		-23,302	-27,322
Net interest income	5, 7	**129,111**	**97,319**
Fee and commission income		61,495	60,824
Fee and commission expense		-16,595	-17,345
Net fee and commission income	5, 8	**44,900**	**43,479**
Net loss from financial assets measured at fair value	5, 11	-2,008	-924
Foreign exchange gains/losses		1,414	-22
Net loss from financial assets	5	**-594**	**-946**
Other income		228	534
Other expense		-102	-4
Net other income		**126**	**530**
Net income		**173,543**	**140,382**
Staff costs	9	-46,795	-31,322
Administrative and other operating expenses	9	-42,843	-33,863
Profit before expected credit losses and other credit impairment		**83,905**	**75,197**
Impairment losses on financial instruments at fair value	11	-5,056	0
Impairment losses on financial instruments measured at amortised cost	13	-2,996	-3,948
Profit before income tax		**75,853**	**71,249**
Income tax expense	5, 6, 26	-14,421	-10,986
Net profit for the year	5	**61,432**	**60,263**
Other comprehensive income:			
Items that may be reclassified subsequently to profit or loss:			
Unrealised exchange differences on translating the financial statements of foreign operations		-1,489	48
Total comprehensive income for the year		**59,943**	**60,311**
Total profit attributable to:			
Owners of the parent		59,808	58,261
Non-controlling interests		1,624	2,002
Total profit for the year	5	**61,432**	**60,263**
Total comprehensive income attributable to:			
Owners of the parent		58,319	58,309
Non-controlling interests		1,624	2,002
Total comprehensive income for the year		**59,943**	**60,311**
Basic earnings per share (in euros)	25	0.19	0.20
Diluted earnings per share (in euros)	25	0.19	0.19

The notes on pages 136 to 162 are an integral part of the consolidated financial statements.

Consolidated statement of financial position

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Assets			
Due from central banks	10	2,390,964	3,874,284
Due from credit institutions	10	87,933	106,838
Due from investment companies	10	3,391	6,188
Financial assets at fair value through profit or loss	11	9,354	135,855
Financial assets measured at amortised cost	11	364,230	0
Loans and advances to customers	12	3,208,572	2,677,160
Receivables from customers	14	21,019	9,752
Other financial assets	15	124	2,236
Other assets	15	6,775	3,471
Strategic financial investments at fair value through profit or loss	11	1,180	5,236
Tangible assets	16	9,552	4,517
Right-of-use assets	16	7,307	3,957
Intangible assets	16	13,853	11,825
Goodwill	6	10,748	3,614
Total assets	5	**6,135,002**	**6,844,933**
Liabilities			
Amounts owed to central banks (TLTRO)	17	147,841	197,461
Deposits from customers	17	4,900,515	5,807,617
Loans received and debt securities in issue	17	438,642	349,146
Financial liabilities at fair value through profit or loss	11	3,850	157
Accounts payable and other liabilities	18	92,462	55,373
Subordinated debt	20	130,843	110,378
Total liabilities	**5**	**5,714,153**	**6,520,132**
Equity			
Share capital	21	31,542	29,864
Share premium	21	141,186	97,361
Legal reserve	21	4,713	4,713
Other reserves	21	5,683	4,733
Retained earnings		229,817	179,746
Total equity attributable to owners of the parent		**412,941**	**316,417**
Non-controlling interests	6	7,908	8,384
Total equity		**420,849**	**324,801**
Total liabilities and equity		**6,135,002**	**6,844,933**

The notes on pages 136 to 162 are an integral part of the consolidated financial statements.

Consolidated statement of cash flows

EUR thousand	Note	2022	2021
Cash flows from operating activities			
Interest received		149,230	124,692
Interest paid		-21,159	-29,888
Fees and commissions received		61,493	59,904
Fees and commissions paid		-16,595	-17,345
Other income received		-2,095	-845
Staff costs paid		-40,894	-27,104
Administrative and other operating expenses paid		-31,365	-23,816
Income tax paid		-12,732	-10,798
Cash flows from operating activities before changes in operating assets and liabilities		**85,883**	**74,800**
Increases/decreases in operating assets:			
Net increase/decrease in financial assets at fair value through profit or loss		-35	-140
Loans and advances to customers		-540,335	-475,118
Mandatory reserves at central banks		8,609	-16,045
Security deposits		2,112	-164
Other assets		-4,053	1,426
Increases/decreases in operating liabilities:			
Demand deposits of customers		-1,006,749	2,014,423
Term deposits of customers		97,695	-324,019
Loans received		88,267	0
Repayments of loans received		-49,216	-21,764
Financial liabilities at fair value through profit or loss		3,693	-64
Other liabilities		23,942	28,244
Net cash from/used in operating activities		**-1 290 187**	**1,281,579**
Cash flows from investing activities			
Purchase of tangible and intangible assets	16	-11,299	-6,688
Acquisition of strategic financial investment		-1,000	-5,237
Acquisition of subsidiary		-8,000	0
Money received via acquisition of the subsidiary		34	0
Net change in investment securities at fair value through profit or loss and amortised cost	11	-235,818	193,394
Net cash from/used in investing activities		**-256,083**	**181,469**
Cash flows from financing activities			
Paid in share capital (incl. share premium)	21	45,503	26,938
Dividends paid	21	-14,046	-10,458
Subordinated debt raised	20	20,264	139,388
Subordinated debt settled	20	0	-40,000
Repayments of lease principal	19	-1,423	-1,254
Net cash from financing activities		**50,298**	**114,614**
Effect of changes in foreign exchange rates on cash and cash equivalents		**-441**	**66**
Increase/decrease in cash and cash equivalents		**-1,496,413**	**1,577,728**
Cash and cash equivalents at the beginning of the year	10	**3,930,012**	**2,352,284**
Cash and cash equivalents at the end of the year	10	**2,433,599**	**3,930,012**

The notes on pages 136 to 162 are an integral part of the consolidated financial statements.

Consolidated statement of changes in equity

EUR thousand	Share capital	Share premium	Legal reserve	Other reserves	Retained earnings	Total	Non-controlling interest	Total equity
Balance as at 1 Jan 2021	**28,819**	**71,468**	**4,713**	**3,409**	**128,385**	**236,794**	**8,482**	**245,276**
Paid in share capital	1,045	25,893	0	0	0	**26,938**	0	**26,938**
Dividends paid	0	0	0	0	-8,358	**-8,358**	-2,100	**-10,458**
Share options	0	0	0	1,276	1,458	**2,734**	0	**2,734**
Profit for the year	0	0	0	0	58,261	**58,261**	2,002	**60,263**
Other comprehensive income	0	0	0	48	0	**48**	0	**48**
Total comprehensive income for 2021	0	0	0	48	58,261	**58,309**	2,002	**60,311**
Balance as at 31 Dec 2021	**29,864**	**97,361**	**4,713**	**4,733**	**179,746**	**316,417**	**8,384**	**324,801**
Balance as at 1 Jan 2022	**29,864**	**97,361**	**4,713**	**4,733**	**179,746**	**316,417**	**8,384**	**324,801**
Paid in share capital	1,678	43,825	0	0	0	**45,503**	0	**45,503**
Dividends paid	0	0	0	0	-11,946	**-11,946**	-2,100	**-14,046**
Share options	0	0	0	2,439	2,209	**4,648**	0	**4,648**
Profit for the year	0	0	0	0	59,808	**59,808**	1,624	**61,432**
Other comprehensive income	0	0	0	-1,489	0	**-1,489**	0	**-1,489**
Total comprehensive income for 2022	0	0	0	-1,489	59,808	**58,319**	1,624	**59,943**
Balance as at 31 Dec 2022	**31,542**	**141,186**	**4,713**	**5,683**	**229,817**	**412,941**	**7,908**	**420,849**

Additional information on equity is provided in Note 21.

The notes on pages 136 to 162 are an integral part of the consolidated financial statements.

Summary of significant accounting policies

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

1. Basis of preparation

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

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

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

1.1 Changes in used accounting policies

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

1.2 Summary of significant accounting policies

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

New currently effective requirements

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

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

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

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

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

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

Forthcoming requirements

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

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

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

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

IFRS 17, Insurance Contracts (Effective for annual periods beginning on or after 1 January 2023; to be applied prospectively. Early application is permitted.)

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 risk. If a group of contracts is or becomes loss-making, an entity recognises the loss immediately. The Group will have an impact of EUR 237 thousand, which will be recognised in 2023 as liability and a decrease in retained earnings.

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

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

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

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

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

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

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

Amendments to IFRS 16 Leases impact how a seller-lessee accounts for variable lease payments that arise in a sale-and-leaseback transaction. The Group is currently assessing the impact of the amendments on its financial statements.

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

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

2. Consolidation

The consolidated financial statements for 2022 comprise the financial statements of AS LHV Group (the parent company) and its subsidiaries AS LHV Pank, AS LHV Finance (a subsidiary of AS LHV Pank), AS LHV Varahaldus, AS LHV Kindlustus, LHV UK Ltd (established in 2021) and EveryPay AS (acquired in 2022). AS LHV Group holds a 65% interest in LHV Finance through AS LHV Pank. AS LHV Group holds a 65% interest in LHV Kindlustus.

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

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

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

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

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

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

Consistent with the Accounting Act of the Republic of Estonia, the primary financial statements of the consolidating entity (the parent company) have to be disclosed in the notes to the consolidated financial statements. In preparing the primary financial statements of the parent, the same accounting policies have been used as in preparing the consolidated financial statements, except for investments in subsidiaries, which in the parent's separate primary financial statements (see Note 27) are accounted for at cost less any impairment losses. A non-controlling interest is that part of the net results and net assets of a subsidiary, which is not attributable, directly or indirectly, to the parent company. A non-controlling interest forms a separate component of the Group's equity. A non-controlling interest in the consolidated statement of financial position is disclosed separately from the equity attributable to the owners of the parent company. In the consolidated statement of profit or loss and other comprehensive income, a non-controlling interest's share of profit or loss and total comprehensive income is disclosed separately from that of the owners of the parent.

3. Associates

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

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

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

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

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

4. Foreign currency translation

4.1 Functional and presentation currency

The functional and presentation currency of Group entities is the euro (EUR), except for LHV UK Ltd in the UK whose functional currency is the pound sterling (GBP).

4.2 Foreign currency transactions and balances

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

5. Cash and cash equivalents

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

6. Financial assets

6.1 Initial recognition and derecognition

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

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

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

6.2 Subsequent measurement

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

6.3 Debt instruments (loans and debt securities)

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

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

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

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

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

6.4 Equity instruments

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

6.5 Derivatives

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

6.6 Modification

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

6.7 Reclassification

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

6.8 Write-off

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

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

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

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

IFRS 9 measurement category		Asset class		31 Dec 2022	31 Dec 2021
Financial assets	Amortised cost	Due from banks and investment companies		2,482,288	3,987,310
		Loans and advances to customers	Loans to legal entities	1,963,215	1,667,234
			Loans to individuals	1,245,357	1,009,926
		Debt securities		364,230	0
		Receivables from customers		21,019	9,752
		Other financial assets		124	2,236
	Fair value through profit or loss	Shares and fund units		1,075	727
		Listed bonds		765	127,504
		Derivatives		40	4
		Pension fund units		7,474	7,620
Financial liabilities	Amortised cost	Amounts owed to central banks (TLTRO)		147,841	197,461
		Deposits from customers		4,900,515	5,807,617
		Loans received and debt securities in issue		438,642	349,146
		Accounts payable and other liabilities		92,462	55,373
		Subordinated debt		130,843	110,378
	Fair value through profit or loss	Derivatives		3,850	157

7. Impairment of financial assets

7.1 Measurement

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

All financial assets measured at amortised cost and fair value through other comprehensive income, as well as lease receivables, financial guarantee contracts, contract assets and certain loan commitments are in the scope for the recognition of ECLs.

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

The assessment of credit risk and the estimation of the ECL must be unbiased and probability-weighted and incorporate all available information which is relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. LHV calculates ECLs using both models and individual assessments which are based on input from experts.

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

7.2 Significant increase in credit risk

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

7.3 Definition of default

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

1) Quantitative criteria

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

2) Qualitative criteria

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

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

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

7.4 Modelling

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

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

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

7.5 Forward-looking information

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

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

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

7.6 Individual assessments and management's judgement

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

8. Tangible fixed assets

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

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

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

9. Intangible assets

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

Sales costs related to the acquisition of new contracts with customers are capitalised. The capitalised acquisition costs of contracts with customers are amortised using the diminishing balance method. The annual amortisation rate for the capitalised acquisition costs is 12% of the residual value of those assets. The appropriateness of amortisation rates, methods and residual values is assessed at the end of each reporting period. The Group reviews intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of an asset's fair value less costs of disposal and value in use.

10. Impairment of non-financial assets

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

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

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

Impairment losses are recognised in profit or loss.

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

11. Loan commitments, financial guarantees, and performance guarantees

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

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

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

12. Financial liabilities

The Group classifies financial liabilities as either:

a) financial liabilities measured at fair value through profit or loss;

b) financial liabilities measured at amortised cost; or

c) financial guarantee contracts and loan commitments.

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

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

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

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

- preferred bonds.

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

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

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

13. Payables to employees

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

The social security tax includes payments to the state pension system. The Group has no existing legal or constructive obligations to make pension or similar payments supplementary to the social security tax.

14. Share-based payments

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

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

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

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

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

15. Provisions and contingent liabilities

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

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

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

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

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

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

17. Revenues and expenses

17.1 Interest income and expenses

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

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

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

17.2 Fee and commission income and expenses

Fee and commission income comprises revenue from contracts with customers. It does not include revenue from lease contracts or financial instruments and other contractual obligations within the scope of IFRS 9 Financial Instruments.

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

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

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 the execution of the underlying transaction. The amount of a fee or commission received or receivable represents the transaction price for the services identified as distinct performance obligations.

The main types of fees are described below.

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

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

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

17.3 Finance income and costs

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

17.4 Dividend income

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

18. Asset management services

The Group provides asset management services (Note 22). Assets managed by the Group that belong to third parties are accounted for off the statement of financial position. The Group derives service fees from the holding and management of such assets. The services do not involve any credit or market risks for the Group.

19. Leases – the Group as a lessee

Lessees are required to recognise:

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

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

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

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

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

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

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

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

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

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

20. Taxation and deferred tax

20.1 Corporate income tax in Estonia

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

Starting from Q2 2018 credit institutions have to make advance payments of income tax at the rate of 14% of their quarterly profits (Note 26). The tax has to be paid by the 10th day of the third month following the quarter. Advance income tax payments are non-refundable and thus recognised as an expense but they can be used to reduce the income tax payable on future dividend distributions. LHV is a growing company and cannot utilise the paid advance income tax in the foreseeable future. Therefore, the tax is recognised as an expense.

20.2 Corporate income tax in other countries

The profit of the entity located in the United Kingdom that has been adjusted for permanent and temporary differences as permitted by local tax laws is subject to corporate income tax.

Corporate income tax rates	2022	2021
United Kingdom	20%	19%

20.3 Deferred tax

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

The contingent income tax liability reflecting the tax obligation that would arise if all the Group's unrestricted equity were distributed as dividends is not recognised in the statement of financial position. The maximum amount of income tax payable on the distribution of the entire retained earnings as dividends is disclosed in Note 21 to the financial statements.

21. Classification of insurance contracts

An insurance contract is a written agreement between the insurer and the policyholder under which the policyholder undertakes to pay the insurance premiums specified the contract, and the insurer undertakes to pay the insured amount or the insurance benefits or to fulfil other contractual obligations when the insured event occurs. All contracts concluded between the Group's insurance company and its customers qualify as insurance contracts

The contracts issued by the company are non-life insurance contracts and in most cases the contract term is one year. Exceptions include short-term travel insurance contracts, which provide cover for one trip and are entered into for the duration of the trip, and equipment insurance and extended warranty contracts, which may have a term exceeding one year.

Premiums are recognised at the commencement date of the contract in their gross amount without deducting brokerage fees. Premiums are fully earned when the insurance cover expires.

Reinsurance

Reinsurance is partial transfer of the insurance risks taken by the insurer to a reinsurer under a reinsurance contract. Reinsurance contracts are usually signed for a term of one year. As an exception, proportional reinsurance contracts in motor third party liability insurance are signed for a term of three years.

Reinsurers' share of the provision for unearned premiums and the provisions for claims outstanding is recognised in accordance with the reinsurance contracts.

Provision for unearned premiums

The unearned premiums provision is calculated in all lines of business using the 365-day pro rata temporis method. The calculations are made separately for each contract. The unearned premiums provision for a contract makes up the same percentage of gross written premiums under the contract as the post-reporting date term of the contract makes up of the entire term of the contract.

Reinsurers' share of the unearned premiums provision is calculated only for those contracts that are covered by a proportional reinsurance contract.

Provision for claims outstanding

The claims outstanding provision is recognised to cover claims incurred but not settled by the reporting date and corresponding claims handling costs. The provision for claims outstanding comprises provisions for:

- claims handled but not settled;
- claims reported but not settled;
- claims incurred but not reported (IBNR).

Claims handling professionals estimate the amount of claims incurred but not settled on a case-by-case basis, taking into account all available information.

Reinsurers' share of the provision for claims outstanding is calculated in accordance with contracts covered by a reinsurance contract.

22. Offsetting

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

23. Legal reserve

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

Notes to the consolidated financial statements

NOTE 1 General information

The consolidated financial statements of AS LHV Group and its subsidiaries (collectively referred to as the Group or LHV) for the year ended 31 December 2022 have been prepared in accordance with International Financial Reporting Standards as adopted by European Union. The subsidiaries are AS LHV Pank (the Bank), AS LHV Finance (a subsidiary of AS LHV Pank), AS LHV Varahaldus, AS LHV Kindlustus, AS EveryPay and LHV UK Ltd. AS LHV Group holds a 65% interest in LHV Finance through AS LHV Pank and a 65% interest in AS LHV Kindlustus.

AS LHV Group is a limited liability company incorporated and domiciled in Estonia. The address of its registered office is Tartu mnt 2, Tallinn. AS LHV Group is a holding company. AS LHV Pank provides banking, financial advisory and securities brokerage services to customers in Estonia and in the UK. It has customer service offices in Tallinn, Tartu and Pärnu (opened in 2022) and a branch in London, which was opened in 2018. LHV UK Ltd, which was established in 2021, is based in the UK. AS LHV Finance offers hire-purchase and consumer finance services. AS LHV Varahaldus offers pension and other fund management services. AS LHV Kindlustus offers various non-life insurance products. EveryPay AS provides payment solutions. At 31 December 2022 the Group had 922 full-time employees, incl. 47 non-active staff (31 December 2021: 652 employees, incl. 43 non-active staff).

The Group's annual report (incl. consolidated financial statements) was approved by the Management Board on 23 February 2023. Rain Lõhmus, who owns 21.8% of the voting rights, and Andres Viisemann, who owns 11.3% of the voting rights (see also Note 21), have significant influence over AS LHV Group.

The Group's annual report which has been approved by the Management Board must also be approved by the Supervisory Board and the shareholders. The shareholders have the right not to approve the annual report and to demand that a new annual report is prepared.

NOTE 2 Significant management estimates and assumptions

Consistent with IFRS, management makes estimates and assumptions which affect the amounts reported in the financial statements. Although the estimates are based on management's best knowledge and judgement, actual outcomes may differ from these estimates. Management's estimates have been applied in the valuation of loans, receivables and investments (Notes 10, 11, 12 and 14) and the determination of the useful lives of tangible and intangible assets (Note 16).

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

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

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

Change in the management of LHV's liquidity portfolios

In 2022 LHV changed the structure of its financial investment portfolios, in particular the banking portfolios containing liquid bonds. The change in the structure of the financial investment portfolios was related to developments in how LHV views the management of its liquidity buffer.

The management of the liquidity portfolios is driven by the underlying need for liquidity buffers, which depend on the structure of LHV's statement of financial position. Based on the estimated need for liquidity buffers, bond portfolios can be built up.

Different items in the statement of financial position generate different liquidity needs and must be backed up with corresponding liquidity buffers of the right size and liquidity category. Some items require instant liquidity while for others it could be sufficient if there is some lead time to monetising the liquid assets. The composition of the liquidity portfolios and their treatment in LHV's processes such as accounting as well as risk management must be aligned with the supposed use of the assets that they contain.

In summary, LHV views the requirement for liquidity buffers in the following three categories:

- Very liquid
- Liquid
- Less liquid

The very liquid portfolio is effectively cash at the central bank, which can be used in intra-day liquidity management for settling all payments and other outflows.

The liquid portfolio contains assets, which can be sold or otherwise monetised within a few hours in the instances when cash balances in the central bank are not sufficient or otherwise optimal for covering liquidity outflows. In general, this portfolio would contain sovereign bonds of the highest credit quality, minimal price risk and very high liquidity. The portfolio does not currently contain any positions. Once any bonds are bought for the portfolio, they will be accounted for at fair value through profit or loss as it is possible that they could be sold before their maturity date.

The less liquid portfolio holds high quality bonds which are eligible as collateral with ECB and are considered liquid in the market. It is LHV's intention to hold the securities in this portfolio until maturity in order to collect the cash flows which are solely principal and interest payments. Accordingly, the less liquid portfolio is accounted for at amortised cost. All existing positions were reclassified to this portfolio starting from 1 April 2022. The portfolio is also subject to the calculation of expected credit losses.

The treatment of the portfolios was implemented as a result of the changes in business model for managing LHV's financial investment portfolios. LHV decided to move all the positions from the FVTPL portfolio to the new 'less liquid' portfolio through reclassification. Based on management's assessment, the criteria for the reclassification were fulfilled. The reclassification affected almost 8% (Note 11) of the Bank's statement of financial position. However, the largest position in the portfolio (covering more than 75% of the portfolio) was in the FVTPL portfolio just for one day before the reclassification was implemented. As a result the change in fair value was zero and impairment of the portfolio after reclassification was EUR 120 thousand. This was the first time that LHV has implemented such reclassification of the bond portfolios from FVTPL to amortised cost. Preceding the reclassification, the concept relating to the financial investment portfolios was redefined and the relevant internal rules were amended. Additionally, the solution for calculating credit impairments was implemented. The reclassification triggered also changes in the reporting to ECB and the public stakeholders.

NOTE 3 Offsetting assets and liabilities

The group has offset the following assets and liabilities.

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

NOTE 4 Fair value of financial assets and financial liabilities

Fair value of financial assets and financial liabilities as at 31 Dec 2022

EUR thousand	Note	Level 1	Level 2	Level 3	Total fair value	Carrying value	Difference
Financial assets at fair value through profit or loss							
Shares and fund units*	11	1,075	7,474	0	8,549	8,549	0
Debt securities at fair value through profit or loss	11	765	0	0	765	765	0
Strategic financial investments at fair value through profit or loss	6	0	0	1,180	1,180	1,180	0
Interest rate swaps and foreign exchange forwards	11	0	40	0	40	40	0
Total financial assets at fair value through profit or loss		**1,840**	**7,514**	**1,180**	**10,534**	**10,534**	**0**
Financial liabilities at fair value through profit or loss							
Interest rate swaps and foreign exchange forwards	11	0	3,850	0	3,850	3,850	0
Total financial liabilities at fair value through profit or loss		**0**	**3,850**	**0**	**3,850**	**3,850**	**0**
Financial assets at amortised cost							
Due from central banks	10	0	2,390,964	0	2,390,964	2,390,964	0
Due from credit institutions	10	0	87,933	0	87,933	87,933	0
Due from investment companies	10	0	3,391	0	3,391	3,391	0
Debt securities	11	0	359,080	0	359,080	364,230	-5,150
Loans and advances to customers	12	0	0	3,276,305	3,276,305	3,208,572	67,733
Receivables from customers	13	0	21,019	0	21,019	21,019	0
Other financial assets	14	0	124	0	124	124	0
Total financial assets at amortised cost		**0**	**2,862,511**	**3,276,305**	**6,138,816**	**6,076,233**	**62,583**
Financial liabilities at amortised cost							
Amounts owed to central banks (TLTRO)	16	0	147,788	0	147,788	147,841	-53
Deposits from customers	16	0	4,898,396	0	4,898,396	4,900,515	-2,119
Loans received and debt securities in issue	16	407,290	0	0	407,290	438,642	-31,352
Subordinated debt	19	0	125,790	0	125,790	130,843	-5,053
Accounts payable and other liabilities	17	0	84,125	0	84,125	84,125	0
Total financial liabilities at amortised cost		**407,290**	**5,256,099**	**0**	**5,663,389**	**5,701,966**	**-38,577**

Fair value of financial assets and financial liabilities as at 31 Dec 2021

EUR thousand	Note	Level 1	Level 2	Level 3	Total fair value	Carrying value	Difference
Financial assets at fair value through profit or loss							
Shares and fund units*	11	727	7,620	0	8,347	8,347	0
Debt securities at fair value through profit or loss	11	127,504	0	0	127,504	127,504	0
Strategic financial investments	11	0	0	5,236	5,236	5,236	0
Interest rate swaps and foreign exchange forwards	11	0	4	0	4	4	0
Total financial assets at fair value through profit or loss		**128,231**	**7,624**	**5,236**	**141,091**	**141,091**	**0**
Financial liabilities at fair value through profit or loss							
Interest rate swaps and foreign exchange forwards	11	0	157	0	157	157	0
Total financial liabilities at fair value through profit or loss		**0**	**157**	**0**	**157**	**157**	**0**
Financial assets at amortised cost							
Due from central banks	10	0	3,874,284	0	3,874,284	3,874,284	0
Due from credit institutions	10	0	106,838	0	106,838	106,838	0
Due from investment companies	10	0	6,188	0	6,188	6,188	0
Loans and advances to customers	12	0	0	2,717,991	2,717,991	2,677,160	40,831
Receivables from customers	13	0	9,752	0	9,752	9,752	0
Other financial assets	14	0	2,236	0	2,236	2,236	0
Total financial assets at amortised cost		**0**	**3,999,298**	**2,717,991**	**6,717,289**	**6,676,458**	**40,831**
Financial liabilities at amortised cost							
Amounts owed to central banks (TLTRO)	16	0	197,461	0	197,461	197,461	0
Deposits from customers	16	0	5,646,953	159,277	5,806,230	5,807,617	-1,387
Loans received and debt securities in issue	16	350,220	0	0	350,220	349,146	1,074
Subordinated debt	19	0	111,813	0	111,813	110,378	1,435
Accounts payable and other liabilities	17	0	49,262	0	49,262	49,262	0
Total financial liabilities at amortised cost		**350,220**	**6,005,489**	**159,277**	**6,514,986**	**6,513,864**	**1,122**

*Shares and fund units include the investments of the Group's subsidiary AS LHV Varahaldus in pension fund units in the amount of EUR 7,474 thousand (31 December 2021: EUR 7,620 thousand). Pursuant to the Investment Funds Act, the mandatory share of AS LHV Varahaldus as the management company is 0.5% of the number of units in each of the II pillar pension funds managed by it.

The Group's Management Board has assessed the fair values of assets and liabilities carried at amortised cost. Fair value is estimated by discounting the future cash flows based on the market interest yield curve.

Levels of the fair value hierarchy (based on inputs used):

1. Level 1 – quoted prices in active markets
2. Level 2 – valuation techniques based on observable inputs (market data such as 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 fair value measurement to changes in unobservable inputs (if the change might result in a significant change in fair value measurement); c) the effect of reasonable possible changes in unobservable inputs

For the term structure of financial assets and financial liabilities, please refer to the 'Risk management' section, subsection 4.

NOTE 5 Operating segments

The Group divides its business activities into 7 main operating segments: retail banking, corporate banking, asset management, hire purchase and consumer finance, financial intermediaries, insurance, and LHV UK Ltd. An operating segment is a part of the Group for which separate financial data is available and which is subject to regular monitoring of operating results by the Group's chief decision maker. The full planning and KPI setting is done on the segment level. For each segment, a full statement of financial position and statement of profit or loss is prepared. In addition to the segment level, the Group carries out planning/measurement on the department level. Similar departments are grouped into segments based on their customer/product base.

The retail banking segment covers services to private individuals and small legal entities with a credit exposure under EUR 500 thousand. This is a regular universal banking segment offering payments, cards, credit, etc.

The corporate banking segment covers services to corporate customers and other legal entities with a credit exposure over EUR 500 thousand. The main products are different kinds of credit and payments.

The asset management segment provides II and III pillar pension fund and other funds management services.

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

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

The insurance segment covers the activities of LHV Kindlustus that offers non-life insurance.

LHV UK Ltd is a UK-based company, which is applying for a banking licence in the UK, planned to be received in Q1 2023. After receiving the licence, the company will take over most of the financial intermediaries' business segment.

Other activities include treasury activities such as the provision of internal financing services to segments and parent company's activities, which are mostly capital and funding related.

The Management Board of AS LHV Group has been designated as the chief decision maker responsible for the allocation of funds and the assessment of the profitability of business activities. The result reported by a segment includes revenue and expenditure directly related to the segment. The revenue reported by a segment is based on the revenue recorded in the financial statements and includes gains from transactions between the segments such as loans granted by AS LHV Pank to other group companies. The breakdown of interest income and fee and commission income by customer location is presented in Notes 7 and 8. The Group does not have any customers that account for more than 10% of any revenue type.

Financial information of operating segments 2022

EUR thousand	Retail banking	Corporate banking	Asset manage-ment	Hire-purc-hase and consumer finance	Financial intermedi-ates	Insurance	LHV UK Ltd	Other activities	Total
Interest income	53,531	74,998	0	12,945	8,276	26	226	2,411	152,413
incl. external interest income	44,805	74,998	0	12,945	7,968	26	226	11,445	152,413
incl. internal interest income	8,726	0	0	0	308	0	0	-9,034	0
Interest expense	0	-16,918	0	-2,521	0	-16	-164	-3,683	-23,302
Net interest income/expense	**53,531**	**58,080**	**0**	**10,424**	**8,276**	**10**	**62**	**-1,272**	**129,111**
Fee and commission income	9,356	2,573	7,951	845	39,326	1,487	0	-43	61,495
Fee and commission expense	-2,361	-59	0	-830	-14,935	0	0	1,590	-16,595
Net fee and commission income	**6,995**	**2,514**	**7,951**	**15**	**24,391**	**1,487**	**0**	**1,547**	**44,900**
Net gain/loss from financial assets	**-357**	**0**	**-147**	**0**	**-24**	**-32**	**7**	**-41**	**-594**
Net other income/expense	**8**	**105**	**0**	**0**	**-27**	**-5**	**0**	**45**	**126**
Net income	**60,177**	**60,699**	**7,804**	**10,439**	**32,616**	**1,460**	**69**	**279**	**173,543**
Administrative and other operating expenses, staff costs	-21,169	-12,574	-7,076	-2,241	-20,834	-3,153	-11,739	-10,852	-89,638
Profit/loss before credit losses	**39,008**	**48,125**	**728**	**8,198**	**11,782**	**-1,693**	**-11,670**	**-10,573**	**83,905**
Impairment losses on loans and advances, investment portfolio and financial investments	-1,467	-472	0	-910	-53	0	0	-5,150	-8,052
Profit/loss before tax	**37,541**	**47,653**	**728**	**7,288**	**11,729**	**-1,693**	**-11,670**	**-15,723**	**75,853**
Income tax	**-4,365**	**-4,871**	**-830**	**-1,107**	**-1,634**	**0**	**0**	**-1,614**	**-14,421**
Net profit/loss for the reporting period	**33,176**	**42,782**	**-102**	**6,181**	**10,095**	**-1,693**	**-11,670**	**-17,337**	**61,432**
Total assets	**2,840,041**	**3 201 314**	**23,681**	**91,711**	**0**	**29,892**	**41,437**	**-93,074**	**6,135,002**
Total liabilities	**3,702,964**	**482 009**	**590**	**72,792**	**1,485,722**	**24,814**	**5,750**	**-60,488**	**5,714,153**

Financial information of operating segments 2021

EUR thousand	Retail banking	Corporate banking	Asset manage-ment	Hire-purc-hase and consumer finance	Financial intermedi-ates	Insurance	LHV UK Ltd	Other activities	Total
Interest income incl.	36,226	59,564	0	11,577	5,107	4	0	12,163	124,641
incl. external interest income	36,226	59,564	0	11,577	43	4	0	17,227	124,641
ncl. internal interest income	0	0	0	0	5,064	0	0	-5,064	0
Interest expense	-1,066	-10,172	-14	-1,791	0	0	0	-14,279	-27,322
Net interest income/expense	**35,160**	**49,392**	**-14**	**9,786**	**5,107**	**4**	**0**	**-2,116**	**97,319**
Fee and commission income	10,003	2,515	11,374	768	34,647	919	0	598	60,824
Fee and commission expense	-1,831	-354	0	-667	-14,946	0	0	453	-17,345
Net fee and commission income	**8,172**	**2,161**	**11,374**	**101**	**19,701**	**919**	**0**	**1,051**	**43,479**
Net gain/loss from financial assets	**-97**	**0**	**591**	**0**	**-436**	**0**	**4**	**-1,008**	**-946**
Net other income/expense	**15**	**397**	**0**	**0**	**96**	**0**	**0**	**22**	**530**
Net income	**43,250**	**51,950**	**11,951**	**9,887**	**24,468**	**923**	**4**	**-2,051**	**140,382**
Administrative and other operating expenses, staff costs	-15,788	-9,853	-10,015	-1,868	-14,732	-1,895	-2,995	-8,039	-65,185
Profit before credit losses	**27,462**	**42,097**	**1,936**	**8,019**	**9,736**	**-972**	**-2,991**	**-10,090**	**75,197**
Impairment losses on loans and advances	-475	-3,110	0	-293	-43	0	0	-27	-3,948
Profit/loss before tax	**26,987**	**38,987**	**1,936**	**7,726**	**9,693**	**-972**	**-2,991**	**-10,117**	**71,249**
Income tax	**-3,120**	**-4,544**	**-1,241**	**-1,184**	**-1,670**	**-1**	**0**	**774**	**-10,986**
Net profit/loss for the reporting period	**23,867**	**34,443**	**695**	**6,542**	**8,023**	**-973**	**-2,991**	**-9,343**	**60,263**
Total assets	**2,885,760**	**3,905,861**	**28,185**	**69,089**	**0**	**14,859**	**9,009**	**-67,830**	**6,844,933**
Total liabilities	**3,297,057**	**711,642**	**544**	**50,417**	**2,520,127**	**8,212**	**143**	**-68,010**	**6,520,132**

The geographical distribution of the Group's interest income and the breakdown of interest income by product are presented in Note 7.

NOTE 6 Subsidiaries and goodwill

As at 31 December 2022, the Group's subsidiaries, which have been consolidated in these financial statements, included:

- AS LHV Pank (Estonia, ownership interest 100%);
- AS LHV Varahaldus (Estonia, ownership interest 100%);
- AS LHV Finance (Estonia, ownership interest 65% through AS LHV Pank);
- AS LHV Kindlustus (Estonia, ownership interest 65%);
- LHV UK Ltd (the UK, ownership interest 100%);
- EveryPay AS (Estonia, ownership interest 100%).

35% ownership interest in AS LHV Kindlustus and AS LHV Finance belongs to Toveko Invest OÜ.

EveryPay AS was bought in April 2022 for EUR 8,000 thousand. For the amount received, EveryPay shareholders subscribed for new shares issued by LHV Group AS.

Cuber Technology OÜ was liquidated at the end of 2021 (2020: ownership interest 100%).

LHV UK Ltd was established in United Kingdom in 2021.

AS LHV Pank established LHV Finance in 2013 and owns 65% of it. The 35% non-controlling interest has been recognised in the consolidated statement of financial position within non-controlling interests.

In 2020, AS LHV Group made a monetary contribution of EUR 5,200 thousand for a 65% and a non-controlling interest made a monetary contribution of EUR 2,800 thousand for a 35% of ownership interest in LHV Kindlustus. The non-controlling interest has been recognised in the consolidated statement of financial position within non-controlling interests.

As at 31 December 2022, goodwill recognised in the consolidated financial statements of AS LHV Group in the amount of EUR 10,748 thousand consisted of:

- goodwill from the acquisition of an ownership in AS LHV Varahaldus of EUR 1,044 thousand;
- goodwill from the acquisition of ownership interest in Danske Capital AS by AS LHV Varahaldus of EUR 2,570 thousand;
- goodwill from the acquisition of an ownership in EveryPay AS of EUR 7,134 thousand.

Impairment tests were performed as at 31 December 2022 and 31 December 2021. The cash-generating unit to which goodwill has been allocated are AS LHV Varahaldus and AS EveryPay. Both value in use calculations were based on a 5-year forecast and terminal value.

AS LHV Varahaldus impairment test had following assumptions:

- The volume of assets under management is expected to increase by 18% in 2023 due to government compensation of pension funds payments suspension and overall growth in stock markets. After that growth stays on stable 11% (2021: average of 7%).
- Success fee has been partially included in future forecasts starting from year 2024 (2021: included partially starting from the second forecast period)
- Due to the economic environment, indirect costs are expected to grow by 6% per year (2021: 5%).
- The discount rate applied was 16% (2021: 16%).

AS EveryPay's impairment test had following assumptions:

- Revenues are expected to increase on average over 20% a year. Growth is fast in 2023-2024 and after that stabilises. Over half of company's revenue comes from AS LHV Pank.
- Due to the economic environment and company's growth plans, indirect costs are expected to grow by 10% per year.
- The discount rate applied was 14%.

In both tests, deriving the main assumptions, management relied on previous years' experience, on its best estimate of probable scenarios and on market data. Expectations were revised to a more conservative level due to changes in the market situation and legislation concerning LHV Varahaldus. Based on the results of both impairment tests, the recoverable amounts of the cash generating units as at 31 December 2021 and 31 December 2022 exceeded its carrying amount and, therefore, no impairment loss was recognised.

As at 31 December 2022, the Group had 2 (31 December 2021: 2) subsidiaries with non-controlling interests: AS LHV Kindlustus and AS LHV Finance.

Set out below is the summarised financial information for AS LHV Finance and AS LHV Kindlustus. The information disclosed is presented before intra-group eliminations.

Summarised statement of Financial Position	AS LHV Finance		AS LHV Kindlustus	
EUR thousand	31 Dec 2022	31 Dec 2021	31 Dec 2022	31 Dec 2021
Current assets	91,591	69,079	28,624	13,893
Non-current assets	120	10	1,268	966
Current liabilities	2,297	1,968	24,047	8,212
Non-current liabilities	70,495	48,449	767	0
Total net assets	**18,919**	**18,672**	**5,078**	**6,647**

Summarised statement of profit or loss and other comprehensive income				
EUR thousand				
Total net interest and fee income (including revenues from insurance)	10,439	9,887	1,497	1,073
Profit/loss before income tax	7,288	7,726	-1,693	-823
Income tax expense	-1,107	-1,184	0	0
Net profit/loss	**6,181**	**6,542**	**-1,693**	**-823**
Total comprehensive income/loss	6,181	6,542	-1,693	-823
Total comprehensive income/loss attributable to non-controlling interests	2,217	2,291	-593	-288

Summarised statement of cash flows				
EUR thousand				
Cash generated from operations	-12,284	6,494	4,837	3,168
Interest paid	-2,407	-1,797	-16	0
Income tax paid	-1,107	-1,184	0	-1
Net cash generated from/used in operating activities	-15,798	3,513	4,821	3,167
Net cash generated from/used in investing activities	-134	0	-1,844	-1,157
Net cash generated from/used in financing activities	15,932	-3,515	750	0
Net increase/decrease in cash and cash equivalents	**0**	**-2**	**3,727**	**2,010**
Cash and cash equivalents at beginning of year	0	2	9,359	7,349
Cash and cash equivalents at end of year	0	0	13,086	9,359

On October 17th 2022 LHV UK Ltd purchased lending business from Bank North Limited. The purchase price for the lending business was EUR 22,080 thousand and was calculated as follows:

EUR thousand	
Loan principal	20,078
Impairment provision held at 30 Sep	-65
Total basis for the purchase price	20,013
Margin (10%)	2,001
Accrued interest	66
Total purchase price	**22,080**

In accordance with the sale purchase agreement, 20 employees have been transferred from Bank North to LHV UK and the contracts of employment had effect from the effective date of the sale purchase agreement.

When a loan is acquired, it is initially measured at fair value in accordance with the requirements of IFRS 9.

The fair value of the loan portfolio purchased as a result of transaction was independently valued by Grant Thornton (GT). GT concluded EUR 22,080 thousand paid for acquisition of loan portfolio is within the fair value range. Therefore, EUR 2,001 thousand margin on purchase of the loan book has been accounted for as part of the fair value of loans (split proportionately based on the nominal value of loans purchased as part of transaction) and amortised using the effective interest rate over the remaining term of loans.

Purchase price was clearly linked to the portfolio acquired and the preliminary assessment by management has been that the fair value of the portfolio equals the payment for the business in amount of EUR 22,080 thousand. This implies a 10% premium to the nominal amounts of loans driven by high quality and above the market interest rates.

NOTE 7 Net interest income

Net interest income

EUR thousand	Note	2022	2021
Interest income using the effective interest method			
Corporate loans		79,130	62,213
incl. loans to related parties	24	78	54
incl. Stage 3 interest*		63	303
Hire purchase		3,338	3,409
Consumer loans		9,607	8,156
Private loans		2,450	2,299
Mortgage loans		28,144	21,441
Leveraged loans and lending of securities		1,629	1,742
Credit card loans		836	834
Due from credit institutions and investment companies		3,668	281
Due from central banks		8,594	2,283
Other loans		8,820	16,332
Subtotal		**146,216**	**118,990**
Other similar interest income			
Leases		6,407	6,000
incl. leases to related parties	24	11	9
Debt securities		-210	-349
incl. debt securities at fair value through profit or loss	11	-342	-349
Subtotal		**6,197**	**5,651**
Total interest income	5	**152,413**	**124,641**
Interest expense			
Deposits from customers and loans received		-5,965	-5,323
incl. deposits from related parties	24	-36	-27
Due to central banks		-7,661	-14,170
Subordinated debt	20	-9,676	-7,829
incl. loans from related parties	24	-331	-323
Total interest expense	5	**-23,302**	**-27,322**
Net interest income	5	**129,111**	**97,319**

Interest income on loans by customer location (excl. interest on bank balances and debt securities)

EUR thousand	2022	2021
Estonia	140,140	121,461
Other	221	965
Total	**140,361**	**122,426**

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

The distribution of the Group's interest income by operating segment is presented in Note 5. The loan portfolio is presented in Note 12.

NOTE 8 Net fee and commission income

Net fee and commission income

EUR thousand	Note	2022	2021
Fee and commission income			
Security brokerage and commission fees		4,329	6,159
incl. related parties	24	88	12
Asset management and related fees		13,581	16,540
incl. funds managed by the Group*	24	7,766	11,215
Currency exchange fees		8,462	8,618
Fees from cards and settlements		27,580	23,635
Fees from consumer loans and hire purchase		845	768
Fees from insurance services		237	919
Other fee and commission income		6,461	4,185
Total fee and commission income	**5**	**61,495**	**60,824**
Fee and commission expense			
Security brokerage and commission fees paid		-2,340	-1,778
Expenses related to cards		-6,216	-5,734
Expenses related to card payments		-7,344	-7,104
Transaction costs		-1,103	-1,135
Costs related to ATMs		-148	-748
Other fee expense		556	-846
Total fee and commission expenses	**5**	**-16,595**	**-17,345**
Net fee and commission income	**5**	**44,900**	**43,479**

* Commission fees from pension and investment funds are calculated as a fixed percentage of the total assets of the fund and vary between 0.2-2.0% per year.and varies between 0.39% -1.2% p.a.

Fee and commission income by customer location

EUR thousand	2022	2021
Estonia	54,143	53,527
Other	7,352	7,297
Total	**61,495**	**60,824**

NOTE 9 Operating expenses

Operating expenses

EUR thousand	Note	2022	2021
Salaries and bonuses		35,077	23,888
Social security and other taxes*		11,718	7,433
Total staff costs		**46,795**	**31,322**
IT expenses		8,232	4,467
Information and banking services		1,356	1,343
Marketing expenses		3,273	2,511
Office expenses		1,934	1,030
Transportation and communication costs		568	318
Training and travel expenses of employees		1,309	450
Other outsourced services		9,059	6,432
Other administrative expenses		8,513	7,654
Depreciation and amortisation	16	7,378	8,204
Rental payments		161	807
Other operating expenses		1,060	648
Total other operating expenses		**42,843**	**33,863**
Total operating expenses		**89,638**	**65,185**

* Social security tax and health insurance and other contributions

The average number of employees working for LHV Group in 2022 was 779 (2021: 597).

From 2018, the acquisition costs of contracts signed with the customers of pension funds have been capitalised as intangible assets based on the expected lifetime of a customer relationship, i.e., 20 years

If the costs had been recognised as an expense and not capitalised, marketing expenses would have been EUR 881 thousand (2021: EUR 750 thousand) larger.

NOTE 10 Due from central banks, credit institutions and investment companies

Due from central banks, credit institutions and investment companies

EUR thousand	31 Dec 2022	31 Dec 2021
Demand and term deposits with a maturity of less than 3 months*	91,324	113,026
Statutory reserve capital at central banks	48,689	57,298
Demand deposits with central banks*	2,342,275	3,816,986
Total	**2,482,288**	**3,987,310**
* Cash and cash equivalents in the statement of cash flows	2,433,599	3,930,012

The distribution of receivables by country is presented in the 'Risk management' section, subsection 2. The mandatory banking reserve as at 31 December 2022 was 1% (2021: 1%) of all financial resources raised (deposits from customers and loans received). The reserve requirement is to be fulfilled as a monthly average in euros or in foreign securities preapproved by the Estonian Central Bank.

NOTE 11 Investments in debt and equity securities

Mandatory measurement as fair value through profit or loss

EUR thousand	31 Dec 2022	31 Dec 2021
Shares and fund units	1,075	727
Debt securities	765	127,504
Investments (fund units) in managed pension funds	7,474	7,620
Foreign exchange forwards	40	4
Total financial assets	**9,354**	**135,855**
Interest rate swaps and foreign exchange forwards	3,850	157
Total financial liabilities	**3,850**	**157**

Investments in debt and equity securities measured at fair value through profit or loss

EUR thousand	
Financial assets at fair value through profit or loss as at 31 December 2020	**330,055**
Net change in investment securities at fair value through profit or loss	-193,626
Negative interest income (Note 7)	-349
Revaluation	-225
Financial assets at fair value through profit or loss as at 31 December 2021	**135,855**
Reclassification to investment securities measured at amortised cost	-464,027
Net change in investment securities at fair value through profit or loss	335,524
Negative interest income (Note 7)	-210
Revaluation	2,212
Financial assets at fair value through profit or loss as at 31 December 2022	**9,354**

Investments in debt and equity securities measured at amortised cost

EUR thousand	
Financial assets measured at amortised cost as at 31 December 2021	**0**
Reclassification	464,027
Net change in investment securities measured at amortised cost	-99,706
Impairment (Note 13)	-91
Financial assets measured at amortised cost as at 31 December 2022	**364,230**

Strategic financial investments at fair value through profit or loss

In 2021 AS LHV Group has made an investment of EUR 5,236 thousand (GBP 4.455 million) in Bank North, for 9.9% interest in the company. Unluckily Bank North didn't manage to raise the capital required by regulators and entered into winddown process. In this process, firstly, LHV wrote down the full investment and in the end of year wrote it up to EUR 180 thousand, as this is the estimated amount LHV will receive after winddown process is completed. The fair value loss in the amount of EUR 5,056 thousand is recorded in the income statement. LHV UK Ltd acquired the corporate loan portfolio of Bank North for a price of EUR 22 080 thousand. Together with the assets, LHV received fully functional business line including several people, IT system for managing loan portfolio and agreements with brokers. Setting up of such a business line would have cost much more.

LHV made a small investment of EUR 1 million to Tuum, the provider of core platform to LHV UK. AS LHV Group has 1.4% interest in the company. LHV main interest was to protect its subsidiaries interests, as Tuum is the most important vendor for LHV UK. Tuum offers modular bank software, with agility and flexibility in mind. Modularity is a key concept in product design; provides option to choose the capabilities needed and, like a multi-tool, Tuum provides the most appropriate choice of technology to supercharge business from within. The platform is API-first and built around a microservices architecture, ensuring quick and simple integration.

The fair value of investments in listed securities is their bid price. In 2022, a loss of EUR 1,475 thousand was recognised on the revaluation of debt securities (2021: a loss of EUR 1,142 thousand). The revaluation of interest rate swaps did not give rise to any gain or loss in 2022 and 2021.

NOTE 12 Loans and advances to customers

Loans and advances to customers
EUR thousand

	31 Dec 2022	31 Dec 2021
Loans to legal entities	**1,980,700**	**1,683,891**
incl. corporate loans	1,747,860	1,469,216
incl. leases	121,015	111,001
incl. overdrafts	36,194	32,327
incl. trade finance	36,255	37,162
incl. leveraged loans	3,679	5,304
incl. credit cards and hire-purchase	747	570
incl. apartment association loans	18,273	10,929
incl. factoring	16,677	17,382
Loans to individuals	**1,248,514**	**1,012,318**
incl. hire-purchase	15,824	13,081
incl. mortgage loans	1,049,386	840,736
incl. consumer loans	77,119	56,936
incl. private loans	52,801	49,683
incl. leases	31,678	30,127
incl. leveraged loans	6,857	9,008
incl. credit card loans	8,933	7,540
incl. overdrafts	25	19
incl. study loans	2,559	1,213
incl. leases of real estate	3,332	3,975
Total	**3,229,214**	**2,696,209**
incl. related parties (Note 24)	5,815	6,047
Allowance for credit losses	-20,642	-19,049
Total	**3,208,572**	**2,677,160**

Changes in allowances for credit losses
EUR thousand

	Balance as at 1 January	Recognition/ reversal of allowances for credit losses during the period	Written off during the period	Balance as at 31 December
Corporate lending	-15,288	-5,426	5,216	-15,498
Consumer financing	-1,319	-2,092	1,303	-2,108
Investment financing	-130	-8	125	-13
Leasing	-1,250	-1,204	445	-2,009
Private lending	-1,062	-593	641	-1,014
Total 2022	**-19,049**	**-9,323**	**7,730**	**-20,642**
Corporate lending	-13,449	-9,706	7,867	-15,288
Consumer financing	-1,178	-1,318	1,176	-1,320
Investment financing	-25	-130	26	-129
Leasing	-1,385	-1,226	1,361	-1,250
Private lending	-821	-707	466	-1,062
Total 2021	**-16,858**	**-13,087**	**10,896**	**-19,049**

Impairment losses accumulated during the year differ from the amount of impairment losses recognised in profit or loss by the amount of items which were written off as uncollectable in previous periods but collected during the reporting period. Related receipts were recognised within impairment losses in profit or loss statement.

For credit risk exposures and loan collateral, see the 'Risk management' section, subsection 2.

The distribution of loans granted by currency is disclosed in the 'Risk management' section, subsection 3.

The distribution of loans granted by maturity is disclosed in the 'Risk management' section, subsection 4.

The geographical distribution of loans granted is disclosed in the 'Risk management section', subsection 2.

For interest income on loans granted, see Note 7.

NOTE 13 Impairment losses on financial assets measured at amortised cost

Impairment losses on financial assets measured at amortised cost

EUR thousand	2022	2021
Impairment losses on loans and advances	2,905	3,948
Impairment losses on financial assets (liquidity portfolio)	91	0
Total	**2,996**	**3,948**

NOTE 14 Receivables from customers

Receivables from customers

EUR thousand	31 Dec 2022	31 Dec 2021
Asset management fees from customers	1,281	3,990
incl. related parties (Note 24)	674	3,252
Other fees for providing services to customers	8,719	794
Receivables from insurance activities	10,985	3,717
Payments in transit	34	1,251
Total	**21,019**	**9,752**

All fees are expected to be settled within 12 months of the end of the reporting period and are thus considered to be current assets.

NOTE 15 Other assets

Other assets

EUR thousand	31 Dec 2022	31 Dec 2021
Financial assets		
Baltic stock exchange guarantee deposits	24	16
VISA and MasterCard guarantee deposits	100	2,220
Subtotal	**124**	**2,236**
Non-financial assets		
Prepayments to Financial Supervision and Crisis Resolution Authority	1,323	1,112
Prepayments related to insurance activities	2,742	564
Other prepayments*	2,710	1,795
Subtotal	**6,775**	**3,471**
Total	**6,899**	**5,707**

* Prepayments for office rental, insurance, communication services, periodicals and training

Prepayments are expected to be refunded or used within 12 months of the end of the reporting period and are therefore classified as current assets. Baltic stock exchange guarantee deposits, which secure securities transactions on the stock exchanges of Tallinn, Riga and Vilnius, and VISA (2021 also MasterCard) guarantee deposits, which secure credit card transactions, are classified as non-current assets.

NOTE 16 Tangible, intangible and right-of-use assets

Tangible, intangible and right-of-use assets *EUR thousand*	Tangible assets	Right-of-use assets	Total tangible assets	Intangible assets	Acquisition costs of contracts with customers	Total intangible assets	Total
Balance as at 31 Dec 2020							
Cost	6,763	5,446	12,209	9,457	15,964	25,421	37,630
Accumulated depreciation and amortisation	-3,983	-1,641	-5,624	-5,579	-4,695	-10,274	-15,898
Carrying amount as at 31 Dec 2020	**2,780**	**3,805**	**6,585**	**3,878**	**11,269**	**15,147**	**21,732**
Purchases	2,515	1,077	3,592	2,496	0	2,496	6,088
Capitalised acquisition costs	0	0	0	0	750	750	750
Write-off	0	-67	-67	-807	0	-807	-874
Depreciation/amortisation (Note 9)	-863	-773	-1,636	-2,610	-3,958	-6,568	-8,204
Balance as at 31 Dec 2021							
Cost	9,278	6,523	15,801	11,146	16,714	27,860	43,661
Accumulated depreciation and amortisation	-4,846	-2,481	-7,327	-7,382	-8,653	-16,035	-23,362
Carrying amount as at 31 Dec 2021	**4,432**	**4,042**	**8,474**	**3,764**	**8,061**	**11,825**	**20,299**
Purchases	6,527	5,642	12,169	3,745	0	3,745	15,914
Capitalised acquisition costs	0	0	0	0	881	881	881
Tangible and intangible assets added by the acquisition of a subsidiary	23	0	23	896	0	896	919
Write-off	-13	0	-13	-366	0	-366	-379
Depreciation/amortisation (Note 9)	-1,431	-2,377	-3,808	-1,990	-1,503	-3,493	-7,301
Balance as at 31 Dec 2022							
Cost	15,815	12,165	27,980	15,421	17,595	33,016	60,996
Accumulated depreciation and amortisation	-6,264	-4,858	-11,122	-9,006	-10,156	-19,162	-30,284
Carrying amount as at 31 Dec 2022	**9,551**	**7,307**	**16,858**	**6,415**	**7,439**	**13,854**	**30,712**

Tangible assets include computers, office equipment, furniture, and capitalised office renovation costs. Intangible assets include licences, acquisition costs of contracts with customers and development costs.

In 2022 and 2021, there was no indication of impairment of tangible and intangible assets. The carrying amount of right-of-use assets and changes in in their balance during the year are disclosed in Note 19.

NOTE 17 Deposits from customers and loans received

Deposits from customers 31 Dec 2022

EUR thousand	Individuals	Financial entities	Non-financial entities	Public sector	Total
Demand deposits	1,065,135	1,477,182	2,042,117	58,406	4,642,840
Term deposits	63,208	23,046	146,137	24,587	256,978
Accrued interest liabilities	336	192	156	13	697
Total	**1,128,679**	**1,500,420**	**2,188,410**	**83,006**	**4,900,515**
incl. related parties (Note 24)	765	0	6,998	0	7,763

Deposits from customers 31 Dec 2021

EUR thousand					
Demand deposits	1,005,757	2,473,973	2,008,349	161,510	5,649,589
Term deposits	39,209	15,679	81,808	22,587	159,283
Accrued interest liabilities	285	-1,537	-5	2	-1,255
Total	**1,045,251**	**2,488,115**	**2,090,152**	**184,099**	**5,807,617**
incl. related parties (Note 24)	2,349	0	28,290	0	30,639

Loans from financial institutions and debt securities in issue		**31 Dec 2022**		**31 Dec 2021**
EUR thousand	Loan principal	Accrued interest	Loan principal	Accrued interest
Debt securities in issue	188,672	545	100,000	26
Covered bonds	249,284	141	248,980	140
Total	**437,956**	**686**	**348,980**	**166**

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

In June 2020, LHV Pank carried out a successful debut issue of covered bonds of EUR 250 million to international investors. 31 institutional investors participated in the 5-year issue and the interest rate was 0.12%. The issue by LHV Pank was the first debut issue since the beginning of the COVID-19 crisis. The issue received an Aa1 rating from Moody's and was listed on the Euronext Dublin.

In Q3 2021, the Bank raised EUR 200 million in negative interest funds through the TLTRO III programme offered by the European Central Bank of which EUR 50 million was returned during 2022.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.

The distribution of deposits from customers and loans received by currency is presented in the 'Risk management' section, subsection 3.

The distribution of deposits from customers and loans received by maturity is presented in the 'Risk management' section, subsection 4.

The geographical distribution of deposits from customers and loans received and the concentration of risk are presented in the 'Risk management' section, subsection 2.

NOTE 18 Accounts payable and other liabilities

Accounts payable and other liabilities

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Financial liabilities			
Trade payables		1,943	2,779
Other short-term financial liabilities		10,676	6,904
Lease liabilities	19	6,766	3,350
Payments in transit		40,101	27,202
Insurance payables		23,411	7,926
Financial guarantee contracts issued		1,228	1,101
Subtotal		**84,125**	**49,262**
Non-financial liabilities			
Performance guarantee contracts issued		1,058	543
Tax liabilities		3,086	2,207
Payables to employees		3,457	2,545
incl. related parties	24	214	107
Other short-term liabilities		736	816
Subtotal		**8,337**	**6,111**
Total		**92,462**	**55,373**

Payables to employees consist of salaries payable and bonus and vacation pay accruals for the reporting period. The increase in payables to employees is attributable to growth in the number of employees during the year. Payments in transit consist of foreign payments and payables to customers related to the intermediation of securities transactions, for which the customer's current account has been debited. All liabilities, except for financial guarantees, are payable within 12 months and are therefore classified as current liabilities.

Insurance payables include insurance reserves in the amount of EUR 14,062 thousand (2021: EUR 4,778 thousand) and advance premiums of insurance contracts in the amount of EUR 6,348 thousand (2021: EUR 2,627 thousand).

Income tax payable on dividends expected to be paid out in the next financial year in the amount of EUR 1,521 thousand (2021: 1,603 thousand) has been included in other short term financial liabilities.

NOTE 19 Right-of-use assets and lease liabilities

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

As at 31 December 2022, the Group's statement of financial position included right-of-use assets of EUR 7,307 thousand (31 December 2021: EUR 4,042 thousand) and lease liabilities of EUR 6,767 thousand (31 December 2021: EUR 3,350 thousand). The increase in 2022 was related to new leases and the extension of existing leases. The right-of-use assets balance is disclosed in Note 17. The balance of lease liabilities is disclosed in Note 18. Interest expense on lease liabilities was EUR 253 thousand (2021: EUR 101 thousand) and depreciation of right-of-use assets was EUR 2 377 thousand (2021: EUR 773 thousand) (Note 16). Repayments of lease principal were EUR 1 423 thousand (2021: EUR 963 thousand).

NOTE 20 Subordinated debt

Consistent with the nature of the Group's operations, only subordinated debt raised is reported within cash flows from financing activities in the statement of cash flows. Other loans raised are reported within cash flows from operating activities. This note contains changes in subordinated debt, including monetary and non-monetary movements and the effects of movements in foreign exchange rates, if any, during the reporting period and the comparative period.

The Group has raised subordinated debt to increase long-term capital. In the case of default of the Group, the subordinated debt is repayable after all other debts have been settled, but before debts to shareholders are paid. The balances of subordinated debt as at the end of the reporting and the comparative period are disclosed in the table below

Subordinated debts

EUR thousand	Amount	Interest rate	Maturity date
Subordinated debt as at 31 Dec 2021	**110,000**		
Subordinated debt as at 31 Dec 2022	**130,000**		
Subordinated bond	40,000	6.0%	28 November 2028
Subordinated bond	35,000	6.0%	30 September 2030
Tier 1 subordinated bond	20,000	10.5%	perpetual
Tier 1 subordinated bond	20,000	8.0%	perpetual
Tier 1 subordinated bond	15,000	9.5%	perpetual

Interest expense on subordinated bonds for the period and accrued interest liabilities as at the end of the period are disclosed in the table below. Interest liabilities are recognised in the statement of financial position using the effective interest method.

Interest accrued on subordinated debt

EUR thousand	
Accrued interest on subordinated debt as at 1 Jan 2021	**603**
Interest calculated for 2021 (Note 7)	7,266
Paid out during 2021	-7,491
Accrued interest on subordinated debt as at 31 Dec 2021	**378**
Interest calculated for 2022 (Note 7)	7,724
Paid out during 2022	-7,259
Accrued interest on subordinated debt as at 31 Dec 2022	**843**

NOTE 21 Shareholders' equity

Transactions with share capital and share premium	Time	Share price (EUR)	Number of shares (thousand)	Share premium (EUR thousand)	Total (EUR thousand)
Share capital as at 1 Jan 2021*			**288,191**	**71,468**	
Paid in share capital	Apr 2021	0.53	2,998	1,298	1,598
Paid in share capital	Oct 2021	3.40	7,453	24,595	25,340
Share capital as at 31 Dec 2021			**298,642**	**97,361**	
Paid in share capital	Apr 2022	4.10	1,951	7,805	9,756
Paid in share capital	Apr 2022	0.39	5,109	1,992	7,101
Paid in share capital	Jun 2022	3.60	9,722	34,028	43,750
Share capital and share premium as at 31 Dec 2022			**315,424**	**141,186**	

*all figures effective after the share split

Share capital has been fully paid in using cash contributions. The nominal value of the shares is 0,1 euro each and as at 31 December 2022 the number of shares was 315,424,530 (31 December 2021: 298,641,670). Each share carries one vote at the General Meeting.

According to AS LHV Group's articles of association, the company's minimum share capital is EUR 15 million and maximum share capital is EUR 60 million (31 December 2021: EUR 15 and EUR 60 million, respectively).

Rain Lõhmus, who owns 21.8% of the voting rights, and Andres Viisemann, who owns 11.3% of the voting rights in AS LHV Group, have significant influence over the company (31 December 2021: 22.7% and 9.6%, respectively).

In the reporting period, the Group paid dividends to shareholders of EUR 0.40 (2021: EUR 0.29) per share and EUR 11,946 thousand (2021: EUR 8,358 thousand) in total.

As at 31 December 2022, the retained earnings of the Group totalled EUR 229,817 thousand (31 December 2021: EUR 179,746 thousand). Using the retained earnings as at the reporting date, the Group could distribute a maximum dividend of EUR 184,368 thousand (2021: EUR 144,244 thousand). Part of the potential dividend (the portion equal to 1/3 of the dividends paid out in 2020-2022) would be taxed at 14% (the amount of tax payable would be calculated as 14/86 of the net distribution) and the remaining part at 20% (the amount of tax payable would be calculated as 20/80 of the net distribution). The related income tax charge would be EUR 45,449 thousand (2021: EUR 35,502 thousand).

Legal reserve in equity *EUR thousand*	
Legal reserve as at 1 Jan 2021	**4,713**
Legal reserve as at 31 Dec 2021	**4,713**
Legal reserve as at 31 Dec 2022	**4,713**

Other reserves in the consolidated statement of changes in equity consist of:

Other reserves *EUR thousand*	31 Dec 2022	31 Dec 2021
Reserve of share options granted to staff	7,124	4,685
Total	**7,124**	**4,685**

The Group grants share options to the members of the Management Boards and equivalent staff as well as the department managers and equivalent staff of Group entities.

Outstanding amount of share options	Number of shares	Strike price per share (EUR)	Year of expiry	Number of people to whom the share options were granted
Outstanding amount of share options at 1 Jan 2021	**1,263,513**			
Granted during the period	435,606	9.23	2024	138
Exercised during the period	-299,781			
Outstanding amount of share options at 31 Dec 2021	**1,399,338**			
Granted during the period	369,437	21.82	2025	167
Exercised during the period	-510,943			
Outstanding amount of share options at 31 Dec 2022	**1,257,832**			

The Group may grant share options for the results of 2022. The vesting period for all share options in the option programme is 3 years. The right to subscribe for shares arises on the first day of the exercise period. The option strike price was calculated using the Black-Scholes model. The model inputs were the LHV Group share price in Q4 2022, expected volatility, the interest rates of Latvian and Lithuanian government bonds used as proxies for risk-free instruments and the dividend yield. Inputs for 2023 share options are as follows: strike price EUR 1.70, share price EUR 3.39, volatility 0.18, risk-free interest rate 3.45% and dividend yield 1.20%. In 2022, the share options granted in 2019 were fully exercised.

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

Total expenses arising from share-based payment transactions amounted to EUR 4,661 thousand in 2022 (2021: EUR 2,734 thousand).

NOTE 22 Assets under management

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

EUR thousand	31 Dec 2022	31 Dec 2021
Cash balances of customers	13,609	3,806
Securities of customers	3,045,558	3,392,585
incl. shareholders of the parent company and entities related to them (Note 24)	483,452	660,351
Total	**3,059,167**	**3,396,391**

Asset management fees for the management of the above assets were in the range of 0.01-0.02% per year in 2022 (2021: 0.01-0.02% per year) (for respective income, see Note 8).

The monetary funds of customers who use the platform for an active securities trader, i.e., the trading system LHV Trader offered by the Bank are not recognised in the statement of financial position. Due to the nature of the system, the Bank deposits the funds in personalised accounts with its partner and as the funds cannot be used for business purposes by the Bank (they cannot be lent to other customers or used as collateral), they are accounted for off the statement of financial position. The Bank earns commission and interest income on the intermediation of transactions involving these accounts similarly to transactions involving customer accounts recognised in the financial statements. The Bank has provided contractual guarantees to its partner in respect of LHV Trader accounts, according to which the Bank will cover the losses which may arise from the financing of customer transactions intermediated by the Bank (leveraging); thereby the primary collateral is the securities used as collateral for the leveraged loans. Customers have provided similar guarantees to the Bank and, therefore, the Bank has in substance transferred the guarantees received. To avoid potential losses, the Bank monitors customer accounts on a daily basis to identify potential decreases in collateral or deficiency of funds. To date, no claims have been filed against the guarantees and the Bank has not made any payments under the guarantees.

NOTE 23 Contingent assets and liabilities

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

Income tax on potential future dividends is disclosed in Note 21.

Financial guarantees and unused loan commitments are subject to the ECL requirements of IFRS 9. See also the 'Risk management' section, subsection 2 for more information.

Tax authorities have the right to review the Group's tax records for up to 5 years after the submission of a tax return and upon finding errors may charge additional taxes, interest and fines. Tax authorities did not perform any tax audits at the Group during 2021-2022. According to the assessment of the Group's management, there are no circumstances which would cause tax authorities to charge a significant amount of additional tax from the Group in 2023.

Performance guarantees are contracts that provide compensation in the event 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., another party's failure to perform a contractual obligation) 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 the levels of such payments. Claims must be made before the contract expires and most claims are settled within a short term. This allows the Group to achieve a high degree of certainty about the estimated payments and, therefore, future cash flows. The Group manages such risks by constantly monitoring the level of payments for such products and has the ability to adjust its fees in the future to reflect any change in claim settlement experience. The Group has a claims handling process and the right to review the claims received and to reject any fraudulent or non-compliant claims. The exposure to and concentration of performance guarantees expressed in the amounts guaranteed is as follows:

Performance guarantees breakdown by industry

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

Performance guarantees breakdown by internal ratings

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

Performance guarantees are over-collateralised as at each reporting date. Therefore, the Group has not incurred any losses from performance guarantee contracts in 2022 or in earlier periods.

NOTE 24 Transactions with related parties

For the purposes of the Group's financial statements, related parties include:

- owners that have significant influence over the Group and companies related to them;
- members of the Management Board and companies controlled by them (collectively referred to as management);
- members of the Supervisory Board;
- close family members of the above persons and companies related to them.

Transactions

EUR thousand	Note	2022	2021
Interest income	7	**178**	**144**
incl. management		79	63
incl. shareholders with significant influence, companies related to them and their close family members		99	81
Fee and commission income	8	**88**	**12**
incl. management		15	7
incl. shareholders with significant influence, companies related to them and their close family members		73	5
Interest expense on deposits	7	**36**	**27**
incl. management		6	7
incl. shareholders with significant influence, companies related to them and their close family members		30	20
Interest expense on subordinated debt	7	**331**	**323**
incl. management		9	9
incl. shareholders with significant influence, companies related to them and their close family members		322	314

Balances

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Loans and receivables		**7,570**	**6,047**
incl. management	15	3,901	2,887
incl. shareholders with significant influence, companies related to them and their close family members	15	3,669	3,160
Deposits		**7,763**	**30,639**
incl. management	18	765	788
incl. shareholders with significant influence, companies related to them and their close family members	18	6,998	29,851
Subordinated debt		**4,434**	**4,134**
incl. management	21	148	148
incl. shareholders with significant influence, companies related to them and their close family members	21	4,286	3,986

The table provides an overview of material balances and transactions with related parties. All transactions involving close family members and companies related to the members of the Management Board and the Supervisory Board and the minority shareholders of the parent company, AS LHV Group, were conducted in the course and on the terms of ordinary business. There are no doubtful receivables from related parties and no loans to related parties have been written down. Transactions with related parties include balances and transactions with following companies related to Management Board and Supervisory Board members: Heero Invest OÜ, AS Lõhmus Holdings, Viisemann Holdings OÜ, MP Advisory OÜ, Unitas OÜ, Kingu OÜ, Merona Systems OÜ, Umblu Records OÜ, Arco Vara AS, Kõrberebane OÜ, KM Investeeringud OÜ and Viisemann Investments AG.

Loans granted to related parties have been issued on market terms.

As at 31 December 2022 and 31 December 2021, management did not have term deposits with the Group and the interest rates of their demand deposits corresponded to the Group's official price list.

The interest rate of the subordinated debt raised in November 2018 is 6.0%. The interest rate of the subordinated debt raised in June 2019 is 8.0%. The interest rate of the subordinated debt raised in May 2020 is 9.5% and the interest rate of the subordinated debt raised in September 2020 is 6%. The interest rate of the subordinated debt raised in 2022 is 10,5%.

Salaries and other compensation paid to the management of the parent AS LHV Group and its subsidiaries in 2022 totalled EUR 3,289 thousand (2021: EUR 2,101 thousand), including all taxes. As at 31 December 2022, remuneration for December and accrued holiday pay of EUR 214 thousand (31 December 2021: EUR 107 thousand) were reported as payables to management (Note 18). 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 December 2022 and 31 December 2021 (pension liabilities, termination benefits, etc.). The remuneration paid to the members of the Group's Supervisory Board in 2022 totalled EUR 109 thousand (2021: EUR 114 thousand).

The Group has signed contracts with the members of the Management Board, which do not provide for severance benefits upon termination of the contract. Any matters not regulated by the contracts are resolved in accordance with the laws of the Republic of Estonia.

Management is eligible to participate in the share option programme. In 2022, the members of the Management Board were granted share options of EUR 1,718 thousand (2021: EUR 1,102 thousand).

Information on assets belonging to related parties which are held by the Group in the capacity of an account manager is presented in Note 22.

NOTE 25 Basic and diluted earnings per share

Basic earnings per share are calculated by dividing net profit attributable to owners of the parent by the weighted average number of shares outstanding.

Basic and diluted earnings per share	2022	2021
Profit (incl. discontinued operations) attributable to owners of the parent (EUR thousand)	59,808	58,261
Weighted average number of shares (thousand)	311,229	292,300
Basic earnings per share (EUR)	0.19	0.20
Weighted average number of shares used in calculating diluted earnings per share (thousands)	317,518	299,670
Diluted earnings per share (EUR)	0.19	0.19

Weighted average number of shares used as the denominator (thousand)	2022	2021
Weighted average number of ordinary shares used as the denominator in calculating basic earnings per share	311,229	292,300
Adjustments made for the calculation of diluted earnings per share:		
Share options	6,289	7,370
Weighted average number of ordinary shares and potential ordinary shares used as the denominator in calculating diluted earnings per share	317,518	299,670

NOTE 26 Income tax expense

The Bank calculates advance corporate income tax at the rate of 14%. Advance corporate income tax for the year 2022 was EUR 12,304 thousand (2021: EUR 9,338 thousand).

Income tax expense

EUR thousand	2022	2021
Advance corporate income tax	12,304	9,338
Corporate income tax	2,117	1,648
Total income tax expense	**14,421**	**10,986**

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

NOTE 27 Separate primary financial statements of parent company

In accordance with the Estonian Accounting Act, the notes to the consolidated financial statements have to include the separate primary financial statements of the parent of the Group.

Parent company statement of profit or loss and other comprehensive income

EUR thousand	2022	2021
Interest income	9,236	7,494
Interest expense	-9,676	-7,829
Net interest expense	**-440**	**-335**
Fee and commission income	2,002	0
Fee and commission income	**2,002**	**0**
Dividend income	9,000	10,400
Net gain/loss from investments in subsidiaries	0	-26
Net gain/loss from financial assets	**9,000**	**10,374**
Operating expenses	-1,737	-1,146
Profit before impairment losses	**8,825**	**8,893**
Impairment losses on the financial instruments	-5,056	0
Profit before income tax	**3,769**	**8,893**
Income tax expense	-263	0
Profit for the year	**3,506**	**8,893**
Total comprehensive income for the year	**3,506**	**8,893**

Parent company statement of financial position

EUR thousand	Note	31 Dec 2022	31 Dec 2021
Assets			
Due from banks and investment companies		29,684	16,941
Loans granted		249,507	189,260
Other receivables and assets		155	85
Investments in subsidiaries		219,407	142,496
Other financial investments		1,180	0
Total assets		**499,933**	**348,782**
Liabilities			
Accrued expenses and other liabilities		108	55
Debt securities in issue		189,217	100,026
Subordinated debt		130,574	110,378
Total liabilities		**319,899**	**210,459**
Equity			
Share capital	21	31,542	29,864
Share premium	21	141,186	97,361
Legal reserve		4,713	4,713
Other reserves		7,124	4,685
Retained earnings/accumulated losses		-4,531	1,700
Total equity		**180,034**	**138,323**
Total liabilities and equity		**499,933**	**348,782**

Parent company statement of cash flows

EUR thousand	2022	2021
Cash flows from operating activities		
Interest received	9,236	7,494
Interest paid	-9,676	-7,829
Fees and commissions received	2,002	0
Income tax paid	-263	0
Administrative and other operating expenses paid	-1,391	-863
Cash flows from operating activities before changes in operating assets and liabilities	**-92**	**-1,198**
Adjustments for		
Investments in subsidiaries resulting from share options	-4,302	-2,451
Increases/decreases in operating assets and liabilities:		
Change in other receivables	-831	-347
Change in other liabilities	5,475	2,406
Net cash from/used in operating activities	**250**	**-1,590**
Cash flows from investing activities		
Loans granted	-95,487	-140,000
Repayments of loans granted	36,000	40,600
Capital repayments from subsidiaries	0	2
Capital contributions to financial investments	-1,000	-5,236
Capital contributions to subsidiaries	-77,845	-16,810
Net cash used in investing activities	**-138,332**	**-121,444**
Cash flows from financing activities		
Subordinated debt raised	108,268	139,755
Subordinated debt settled	0	-40,000
Contribution to share capital (incl. share premium)	45,503	26,938
Dividends received	9,000	10,400
Dividends paid	-11,946	-8,358
Net cash from financing activities	**150,825**	**128,735**
Increase in cash and cash equivalents	**16,941**	**5,701**
Cash and cash equivalents at the beginning of the year	12,743	11,240
Cash and cash equivalents at the end of the year	**29,684**	**16,941**

Parent company statement of changes in equity

EUR thousand	Share capital	Share premium	Legal reserve	Other reserves	Accumulated loss/retained earnings	Total
Balance as at 1 January 2021	**28,819**	**71,468**	**4,713**	**3,409**	**-404**	**108,005**
Paid in share capital	1,045	25,893	0	0	0	**26,938**
Dividends paid	0	0	0	0	-8,358	**-8,358**
Transfer to legal reserve	0	0	0	0	0	**0**
Share options	0	0	0	1,276	1,457	**2,733**
Total comprehensive income for 2021	0	0	0	0	8,893	**8,893**
Balance as at 31 December 2021	**29,864**	**97,361**	**4,713**	**4,685**	**1,588**	**138,211**
Carrying amount of interests under control and significant influence	0	0	0	0	-135,842	**-135,842**
Value of interests under control and significant influence under equity method	0	0	0	0	314,048	**314,048**
Adjusted unconsolidated equity as at 31 December 2021	**29,864**	**97,361**	**4,713**	**4,685**	**179,794**	**316,417**
Balance as at 1 January 2022	**29,864**	**97,361**	**4,713**	**4,685**	**1,588**	**138,211**
Paid in share capital	1,678	43,825	0	0	0	**45,503**
Dividends paid	0	0	0	0	11,946	**-11,946**
Transfer to legal reserve	0	0	0	0	0	**0**
Share options	0	0	0	2,439	2,321	**4,760**
Total comprehensive income for 2022	0	0	0	0	3,506	**3,506**
Balance as at 31 December 2022	**31,542**	**141,186**	**4,713**	**7,124**	**-4,531**	**180,034**
Carrying amount of interests under control and significant influence	0	0	0	0	-210,954	**-210,954**
Value of interests under control and significant influence under equity method	0	0	0	0	443,861	**443,861**
Adjusted unconsolidated equity as at 31 December 2022	**31,542**	**141,186**	**4,713**	**7,124**	**228,376**	**412,941**

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

Signatures of the Management Board to the annual report

The Management Board has prepared the management report and the consolidated financial statements of AS LHV Group for the financial year ended 31 December 2022.

The Management Board confirms that the management report on pages 5 to 73 gives a true and fair view of the business operations, financial performance and financial position of the Group consisting of the parent company and other consolidated entities as a whole.

The Management Board confirms that according to their best knowledge the consolidated financial statements on pages 74 to 162 give a true and fair view of the assets, liabilities, financial position and financial performance of the Group consisting of the parent company and other consolidated entities as a whole in accordance with International Financial Reporting Standards as adopted by the European Union and contains a description of the main risks and uncertainties.

23 February 2023

Madis Toomsalu
Chairman of the Management Board
/signed digitally/

Meelis Paakspuu
Member of the Management Board
/signed digitally/

Jüri Heero
Member of the Management Board
/signed digitally/

Martti Singi
Member of the Management Board
/signed digitally/

Independent auditor's report

This page has been retained in LHV Group annual report 2022 to maintain the structural logic of the report and to refer the reader to the location of the independent auditor's report. The independent auditor's report is available in the DigiDoc container named AS LHV Group consolidated and audited annual report 2022.asice as a separate document. The auditor's report is applicable and applies only to the signed original annual report, which is available as the file AS LHV Group consolidated annual report 2022.asice in the same DigiDoc container as the independent auditor's report and contains the report in the ESEF (529900JG015JC10LED24-2022-12-31-EN.zip).

Proposal for profit distribution

The Management Board of LHV Group proposes to the General Meeting of shareholders that the profit for 2022 be distributed as follows:

- to pay a dividend of EUR 0.04 per share and EUR 12,617 thousand in total, the related income tax would amount to EUR 3,154 thousand;
- to transfer the profit for the reporting period attributable to the shareholders of the parent of EUR 45,702 thousand to retained earnings.

Allocation of income according to EMTAK

Consolidated:

EMTAK	Activity	2022	2021
66121	Security and commodity contracts brokerage	7,003	9,757
64191	Credit institutions (banks) (granting loans)	192,547	157,415
64911	Leasing	6,407	6,000
66301	Fund management	7,951	11,374
	Total income	**213,908**	**184,546**

Unconsolidated:

EMTAK	Activity	2022	2021
64201	Activities of holding companies	11,238	7,494
	Total income	**11,238**	**7,494**

EMTAK – Estonian classification of economic activities

Independent auditors' report

To the Shareholders of AS LHV Group

(Translation of the Estonian original)

Report on the Audit of the Consolidated Financial Statements

Opinion

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

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

Basis for Opinion

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

Key Audit Matters

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

Impairment of loans and advances to customers	
Refer to Risk Management section, Summary of significant accounting policies, Note 2 “Significant management estimates and assumptions”, Note 12 “Loans and advances to customers” and Note 13 “Impairment losses on financial assets measured at amortised cost”.	
The key audit matter	**How the matter was addressed in our audit**
As at 31 December 2022, loans and advances to customers amounted to EUR 3 229 million and related impairment loss allowance amounted to EUR 20.6 million. We have focused on this area because of overall financial significance and the matter that measurement of expected credit losses (ECL) on financial instruments involves significant judgement. ECL calculations are forward looking and probability weighted accounting estimates. The key areas where we identified greater level of management judgement and therefore increased level of audit focus in the Group’s ECL related accounting estimates: — Judgmental modelling is used to estimate ECL which involves determining the Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD). The PD models are the key drivers of complexity in the ECL and also impact the staging of relevant financial assets, and hence, are considered the most significant judgmental aspect of the Group’s ECL modelling approach. — Economic scenarios – IFRS 9 requires the Group to measure ECL on an unbiased forward-looking basis reflecting a range of future economic conditions. Significant management judgement is applied in determining the economic scenarios used and the probability weights applied to them when considering the current uncertain economic environment. — For defaulted corporate loans, an individual impairment loss is calculated based on the exposure and realizable value of relevant collateral at the reporting date, and also requires significant accounting estimates.	In this area, we conducted, among others, the following audit procedures: We have assessed the Group’s accounting policies and methodology applied for the calculation of impairment of loans and advances to customers in relation to the requirements of IFRS 9. We have performed end to end process walkthrough to identify key systems, applications and controls used in the ECL calculation process. We tested relevant manual, general IT and application controls over key systems used in ECL process. We have tested the design, implementation and operating effectiveness of the credit file periodic review, rating assessment and monitoring of collaterals for corporate loans. We have performed test of details over the following: • completeness and accuracy of data used in ECL calculation • compliance of key inputs used in ECL calculation with the IFRS 9 methodology • accuracy and compliance of 12-month and lifetime ECL calculations with IFRS 9 methodology • adequacy of discounting in the ECL model • accuracy and completeness of data used for staging loans • internal assignment of credit ratings to corporate exposures • adequacy of information about collaterals and their values • completeness of exposures of assets with impaired credit quality and related ECL calculations. We have assessed the reasonableness of key assumptions made by the management, which serve as critical inputs in the ECL model, such as weights of different scenarios, loan portfolio point in time PD estimates, criteria to determine significant increase in credit risk, key forecasts of macroeconomic information and multipliers used for different scenarios. We also assessed adequacy and sufficiency of information disclosed in the Note “Risk Management “ and Notes 2, 12 and 13 in the consolidated financial statements.

Other Information

Management is responsible for the other information. The other information includes management report and the remuneration report but does not include the consolidated financial statements and our auditors' report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. In addition, our responsibility is to state whether the information presented in the management report has been prepared in accordance with the applicable legal and regulatory requirements. With respect to the remuneration report, our responsibility also includes considering whether the remuneration report has been prepared in accordance with the requirements of Article 135^3 of the Securities Market Act.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard and we state that the information presented in the management report is materially consistent with the consolidated financial statements and in accordance with the applicable legal and regulatory requirements. In our opinion, the remuneration report has been prepared in accordance with the requirements of Article 135^3 of the Securities Market Act.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards as adopted in the European Union, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (Estonia) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with International Standards on Auditing (Estonia), we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of

the Group’s internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group’s ability to continue as a going concern. If we conclude that a material uncertainty exists, then we are required to draw attention in our auditors’ report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors’ report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors’ report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

Report on Compliance with the Requirements for iXBRL tagging of Consolidated Financial Statements included within the European Single Electronic Format Regulatory Technical Standard (ESEF RTS)

We have undertaken a reasonable assurance engagement on the iXBRL tagging of the consolidated financial statements included in the digital files 529900JG015JC10LED24-2022-12-31-EN.zip prepared by **AS LHV Group**.

Responsibilities of Management for the Digital Files Prepared in Compliance with the ESEF RTS

Management is responsible for preparing digital files that comply with the ESEF RTS. This responsibility includes:

- the selection and application of appropriate iXBRL tags using judgement where necessary;
- ensuring consistency between digitized information and the consolidated financial statements presented in human-readable format; and
- the design, implementation and maintenance of internal control relevant to the application of the ESEF RTS.

Auditors' Responsibilities

Our responsibility is to express an opinion on whether the electronic tagging of the consolidated financial statements complies in all material respects with the ESEF RTS based on the evidence we have obtained. We conducted our reasonable assurance engagement in accordance with International Standard on Assurance Engagements 3000 (Revised), *Assurance Engagements Other than Audits or Reviews of Historical Financial Information* (ISAE 3000) issued by the International Auditing and Assurance Standards Board.

A reasonable assurance engagement in accordance with ISAE 3000 involves performing procedures to obtain evidence about compliance with the ESEF RTS. The nature, timing and extent of procedures selected depend on the practitioner's judgment, including the assessment of the risks of material departures from the requirements set out in the ESEF RTS, whether due to fraud or error. A reasonable assurance engagement includes:

- obtaining an understanding of the tagging and the ESEF RTS, including of internal control over the tagging process relevant to the engagement;
- reconciling the tagged data with the audited consolidated financial statements of the Group dated 31 December 2022;
- evaluating the completeness of the tagging of the consolidated financial statements;
- evaluating the appropriateness of the Group's use of iXBRL elements selected from the ESEF taxonomy and the creation of extension elements where no suitable element in the ESEF taxonomy has been identified;
- evaluating the use of anchoring in relation to the extension elements.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

In our opinion, the consolidated financial statements included in the annual report of AS LHV Group identified as 529900JG015JC10LED24-2022-12-31-EN.zip for the year ended 31 December 2022 are tagged, in all material respects, in compliance with the ESEF RTS.

Other Requirements of the Auditors' Report in Accordance with Regulation (EU) No 537/2014 of the European Parliament and of the Council

We were appointed by those charged with governance on 13 March 2019 to audit the consolidated financial statements of AS LHV Group for the year ended 31 December 2022. Our total uninterrupted period of engagement is three years, covering the periods ended 31 December 2020, 31 December 2021, 31 December 2022.

We confirm that:

– our audit opinion is consistent with the additional report presented to the Audit Committee of the Group;

– we have not provided to the Group the prohibited non-audit services (NASs) referred to in Article 5(1) of EU Regulation (EU) No 537/2014. We remained independent of the audited entity in conducting the audit.

Tallinn, 27 February 2023

/digitally signed/

Eero Kaup

Certified Public Accountant,
License No 459

KPMG Baltics OÜ
License no 17

KPMG Baltics OÜ

Narva Road 5

Tallinn 10117

Estonia

Tel +372 626 8700
www.kpmg.ee