

Report on the activities of the Supervisory Board and assessment of the Annual Report 2016 of AS LHV Group for submission to the annual general meeting of the shareholders

22 February 2017

The Supervisory Board of AS LHV Group (LHV), consisting of Chairman of the Supervisory Board Rain Lõhmus and members of the Supervisory Board Andres Viisemann, Tiina Mõis, Heldur Meerits, Raivo Hein, Tauno Tats and Sten Tamkivi, discussed the following issues:

1. Activities in the financial year 2016

LHV has had another successful year. Most of our objectives were achieved, with room to spare. LHV's shares were listed on the Tallinn Stock Exchange in May, the overall staff satisfaction is the highest on record, and we received several important recognitions during the year.

Certainly, the year 2016 marked a milestone in corporate growth. On May 23, AS LHV Group launched public trading of its shares on the NASDAQ Tallinn Stock Exchange. A total of more than five thousand investors decided to invest in the success of LHV, contributing to our mission of boosting domestic capital. The listing of the shares marked the fulfilment of a long-term objective and a logical continuation of the listing of subordinated bonds in 2015. In order to support LHV's growth, we engaged a total of EUR 13.9 million from our investors, issuing two million new shares. The issue was oversubscribed three times, with the earnings per share amounting to nearly 40 % in 2016.

LHV posted a net profit of EUR 19.9 million in 2016. This constitutes a EUR 5.1 million increase from last year, with a 20.7% return on equity for the shareholders of LHV. Profit was supported by strong customer activity, strong credit quality and the extraordinary revenue generated by the acquisition of Danske Capital. Business volumes and profits were boosted in all core activities.

At the end of September, the Financial Supervision Authority issued the annual Supervisory Review and Evaluation Process (SREP) to LHV Group and LHV Bank. Based on the rates as at the end of 2015, the Financial Supervision Authority established the minimum total capital ratio at 14.39 % and the minimum Tier 1 capital ratio at 11.49% for LHV Group and LHV Bank. In view of the Financial Supervision Authority's evaluation, and by adding the negative scenario buffer, LHV Group established the group's minimum total capital ratio at 16.19 % and the minimum Tier 1 capital ratio at 13.29%.

The net profit posted by the largest business unit - LHV Bank - amounted to EUR 13.2 million, having grown by EUR 3.3 million, year-over-year. Loans to customers increased by EUR 126 million and totalled EUR 532 million. EUR 156 million worth of new deposits were engaged during the year, with the total volume of deposits amounting to EUR 784 million by the end of the year. The number of customers grew by 31 thousand, year-over-year, amounting to 144.1 thousand as at the end of the year.

The Bank received various recognitions at the beginning of the year. In January, Nasdaq declared LHV Bank the Baltic Member of the Year. In February, the survey company Dive declared LHV Bank the bank with the best service in Estonia. In the annual Most Valuable Employer poll conducted by CV-Keskus, LHV Bank rose from last year's 17th position to the 8th position, succumbing only to Estonia's largest companies and ranking second among banks.

In 2016, LHV Bank focused mainly on gaining new customers, enhancing user convenience and expanding the credit product offers. We launched the corporate micro-loan product and laid greater emphasis on small enterprise financing, together with the provision of the required banking services. Home loan - a product, whose existence eliminates the main obstacle for a private customer wishing to change his or her bank - was launched at the end of the year. We have brought our cost structure to a level which allows to provide the home loan product on favourable conditions. We opened a new, more spacious office in Tartu. Both LHV's investment seminars and the *Börsihai* (Stock Exchange Shark) game witnessed a record number of participants. We have responded to growing public

interest by enhancing the flexibility of our Growth Account product, allowing all interested customers to start regular investment with small amounts.

LHV Bank has positioned itself the third-largest local bank in Estonia. Our home market in Estonia, and we wish to excel here. This means ranking among the top three banks, with regard to both customer numbers and business volumes, as well as efficiency and profitability per employee.

LHV Asset Management posted a net profit of EUR 6.1 million in 2016 - EUR 1.5 million more than last year. Net fee and commission income increased by EUR 3.7 million to EUR 12.9 million. The expense side was affected by a depreciation of client agreements in the amount of EUR 0.4 million. The revenue of LHV Asset Management is bound to decrease by an average of 19 % in February 2017, when the new rates for the 2nd pillar funds take effect. The lowering of the fees is a benefit gained by 2nd pillar fund customers from the Danske Capital transaction.

For LHV Asset Management, the highlight of the year was the acquisition of AS Danske Capital on January 29. Immediately after conclusion of the contract and acquisition of the required permits, LHV launched the merger of the two management companies. The merger took effect on July 28, with the balance sheet date of May 1. As a result of the merger, Danske Capital was dissolved, with LHV Asset Management becoming its legal successor. LHV's business plan also includes merger of pension funds with a similar strategy. Similar mandatory pension funds will be merged on 3 May 2017.

In order to finance the purchase of Danske Capital, the share capital of LHV Asset Management was increased by EUR 8.2 million to EUR 12.0 million in February. In view of the current profit and lowering of the capital requirements as a result of merger of the management companies, LHV Asset Management decreased its share capital by EUR 2.7 million before the end of the year. The acquisition of and merger with Danske Capital generated EUR 6.6 million in intangible assets, with the client agreements to be depreciated over a period of several years.

Alongside actively managed pension funds, LHV Asset Management also launched passively managed pension funds in the second half of the year. The principal feature of passive funds is that these funds are not actively managed. This, in turn, allows to offer passive funds at lower management fees. Passive funds are invested in markets at all times, with the yield mimicking the fluctuations of global markets.

We witnessed several stock market declines during the year, but the markets rebounded quickly. Actively managed pension funds avoided major investment risks, with the funds easily navigating all market fluctuations. Our flagship - LHV Pension Fund L - ranked second in its category in terms of yield as at the end of the year. Among conservative funds, LHV Pension Fund S generated the highest yield for the year.

The number of active customers of LHV's mandatory pension funds grew by 49 thousand, year-over-year, amounting to 179.6 thousand. The pension funds acquired through the purchase of Danske Capital had a total of 35.4 thousand customers as at the end of the year. The volume of funds managed by LHV grew by EUR 404 million to EUR 974 million, of which EUR 253 million can be attributed to the transaction-related pension funds.

Mokilizingas posted a net profit of EUR 1.9 million in 2016 - a EUR 0.8 million increase, year-over-year. Profit was positively affected by the disposal of uncollectable receivables in the amount of EUR 0.9 million in Q4. The loan portfolio shrank by EUR 1 million during the year, totalling EUR 36 million. Mokilizingas' return on equity was 31.6%. Mokilizingas is the second largest hire-purchase provider on the Lithuanian market, and is recognised for the good service and transparent pricing. In cooperation with a partner in the telecommunication sector, Mokilizingas also started offering hire-purchase services in Latvia. Furthermore, the credit card product is currently in pilot stage.

A total of eleven ordinary meetings and one extraordinary meeting of the Supervisory Board was held in 2016. At these meetings, the Supervisory Board was provided with regular overviews of the results of operations and financial results of LHV and its subsidiaries, as well as the various new initiatives. The Supervisory Board approved the conditional increase of share capital of LHV, public offering of shares, issue of new shares and the listing of all shares on the Nasdaq Tallinn Stock Exchange Baltic Main List. The Supervisory Board authorised and approved the results of the subscription of shares and the allocation of shares. The core strategy of LHV was the principal topic of discussion at the meeting held in August.

The Supervisory Board approved the dividend payment principles and dividend policy, the acquisition of the shares of Danske Capital AS by AS LHV Varahaldus, and the change in the share capital of AS

LHV Varahaldus. The Supervisory Board approved the Annual Report 2015, the report of the Supervisory Board and the issue of share options for the results posted in 2015. The share capital of AS LHV Pank was increased, Erkki Raasuke was removed from the position of the Management Board member and Madis Toomsalu was appointed the new member of the Management Board of LHV.

The Supervisory Board is quite pleased with the management and economic activities in 2016.

2. Annual Report 2016

The Supervisory Board has examined the Annual Report 2016 prepared by the Management Board, and the auditor's report. In the opinion of the Supervisory Board, the Annual Report has been prepared in accordance with the generally accepted accounting principles, international standards and other acts regulating accounting.

The Supervisory Board is pleased with the work of the auditor in 2016.

3. Calling of the annual general meeting and submission of proposals regarding items on the agenda of the general meeting

The Supervisory Board proposes to call the annual general meeting on 29 March 2017, with the following agenda:

1. Approval of the Annual Report 2016
2. Approval of the specification of the dividend policy
3. Profit allocation for 2016
4. Overview of the economic results for the first two months of 2017
5. Approval of the amendment of the Articles of Association
6. Approval of the conditions of performance pay
7. Extension of the authorisation of the members of the Supervisory Board