



Arion Bank Mortgages Institutional Investor Fund

Interim Financial Statements 30 June 2017

ABMIF
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Endorsement and Signatures of the Board of Directors and the Managing Director

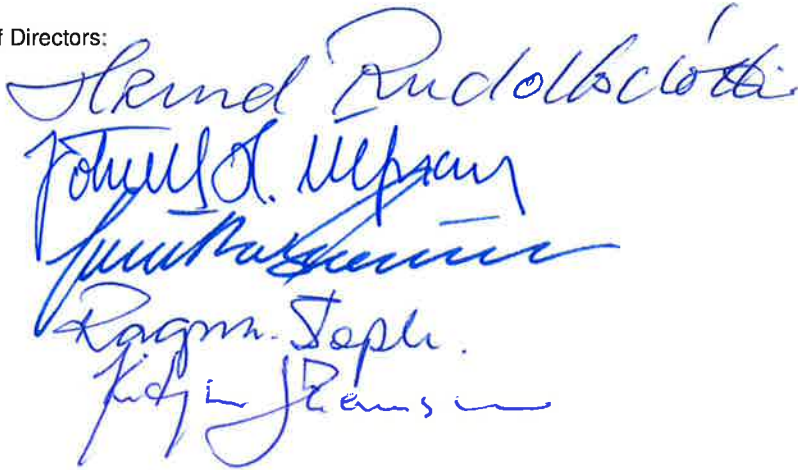
The Interim Financial Statements of ABMIIF are included in part B of the Interim Financial Statements of Stefir hf. which contains the Interim Financial Statements of UCITS, investment funds and institutional investors' funds under management. They have been prepared in accordance with law on Financial Statements and rules on the Financial Statements of management companies of UCITS set by the Icelandic Financial Supervisory Authority.

The fund reported profit of ISK 594.7 million according to the income statement and the profit is recognized as an increase in units in the fund's accounts. The net asset of the fund at the end of the period totalled ISK 16,701.5 million according to the balance sheet.

The Board of Directors and CEO of Stefir hf. hereby confirm the fund's Interim Financial Statements for the period 1 January - 30 June 2017 with their signatures.

Reykjavik, 21 August 2017

Board of Directors:



Handwritten signatures of the Board of Directors and CEO. The signatures are in blue ink and include: Skemil Rudolfsson, Jóni D. Magnússon, Jón Þ. Gunnarsson, Ragnr. Jónsson, and Jóni Jónsson.

CEO:



Handwritten signature of the CEO, Felli Handmann.

Review Report on Interim Financial Statements

To the Board of Directors the unit holder of ABMIF.

We have reviewed the accompanying interim financial statement of ABMIF for the period of 1 January to 30 June 2017, which comprise the endorsement and signatures of the board of directors and managing director, income statement, balance sheet, changes in net assets, statement of investment and a summary of significant accounting policies and other explanatory notes.

Management's and the Board of Directors Responsibility for the Financial Statements

Management and the board is responsible for the preparation and fair presentation of this interim financial information in accordance with Icelandic Financial Statements Act, Act on Financial Undertakings and Rules on the Financial Statements of management companies of UCITS.

Auditor's Responsibility

Our responsibility is to express an conclusion on this interim financial information based on our review.

Scope of Review

We conducted our review in accordance with International Standards on Review Engagements, ISRE 2410. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not give a true and fair view of the financial position of the entity as at 30 June 2017 and of its financial performance and its change in net assets in the period, in accordance with Icelandic Financial Statements Act, Act on Financial Undertakings and Rules on the Financial Statements of management companies of UCITS.

Reykjavik, 21 August 2017

Deloitte ehf.


Páll Grétar Steingrímsson

State Authorized Public Accountant


Petur Hansson

State Authorized Public Accountant

Interim Statement of Income 1 January - 30 June 2017

		1.1. - 30.6 2017	1.1. - 30.6 2016
	Note		
Income	2-5		
Interests		1,900,104	1,800,336
Indexation		1,708,645	2,251,148
Other income		111	276
Total income		<u>3,608,860</u>	<u>4,051,760</u>
Expenses			
Administration fee	6	61,163	61,905
Interest expenses and indexation		2,935,263	3,310,460
Other operating expenses		17,719	(48,067)
Total expenses		<u>3,014,145</u>	<u>3,324,298</u>
Net income (expenses)		594,715	727,462
Profit transferred to units		<u>594,715</u>	<u>727,462</u>
Financing activities			
Units sold		(8,500,000)	0
Total financing activities		<u>(8,500,000)</u>	<u>0</u>
Changes in net assets		(7,905,285)	727,462
Net assets at the beginning of the year		<u>24,606,797</u>	<u>23,069,558</u>
Net assets at the end of the period		<u>16,701,512</u>	<u>23,797,020</u>

Interim Statement of Financial Positions at 30 June 2017

	Note	30.6.2017	31.12.2016
Assets			
Transferable securities		91,348,672	95,869,223
	Total assets	7	91,348,672
Other assets:			
Cash	8	26,180,551	29,628,707
Other assets	9	504,648	461,363
	Total other assets	26,685,199	30,090,070
	Total assets	118,033,871	125,959,293
Liabilities			
Loan from financial institutions		101,322,388	101,342,179
Liabilities with the management company		9,971	10,316
Other liabilities	10	0	1
	Total liabilities	101,332,359	101,352,496
Net assets		16,701,512	24,606,797
Number of units (in thousands)		23,200	23,200
Exchange rate of units at the end of the period		0.72	1.06

Breakdown of Assets

1. Breakdown of Assets.

	Assets 30.6.2017	Rate %	Assets 31.12.2016	Rate %	Issuer
Other transferable securities:					
Mortgages, unindexed	6,527,097	5.5	7,049,446	5.6	Individuals
Mortgages, indexed	84,821,575	71.9	88,819,777	70.5	Individuals
Other transferable securities, total	91,348,672	77.4	95,869,223	76.1	
Investments, total	91,348,672	77.4	95,869,223	76.1	
Cash	26,180,551	22.2	29,628,707	23.5	
Other assets	504,648	0.4	461	0.4	
Total assets	118,033,871	100.0	125,959,293	100.0	

2. Comparison with Investment Policy.

	Book value 30.6.2017	Rate of invest- ment %	Book value 31.12.2016	Rate of investment %	Investment policy %	
					Minimum	Maximum
Mortgages	91,348,672	100.0	95,869,223	100.0	0	100
Total investments	91,348,672	100.0	95,869,223	100.0		

3. Cumulative Purchases and Sales.

	Cumulative purchases 1.1.-30.6.2017	Cumulative sales 1.1.-30.6.2017	Cumulative purchases 2016	Cumulative sales 2016
Units sold	0	0	0	0
	0	0	0	0

4. Segmentation of investments by Countries and Currency.

		Book value 30.6.2017	Rate of investment %	Book value 31.12.2016	Rate of investment %
Iceland	ISK	91,348,672	100.0	95,869,223	100.0
		91,348,672	100.0	95,869,223	100.0

Breakdown of Assets, cont.

5. Statement of Main Assets

	Assets	Assets	Changes of	
	30.6.2017	31.12.2016	book value	%
Mortgages, unindexed	6,527,097	7,049,446	(522,349)	(0.4%)
Mortgages, indexed	84,821,575	88,819,777	(3,998,201)	(3.4%)
Mortgages	91,348,672	95,869,223	(4,520,551)	(3.8%)
Other assets	26,685,199	30,090,070	(3,404,871)	(2.9%)
Total assets	118,033,871	125,959,293	(7,925,422)	(6.7%)

6. Net Assets and return of the Fund

	30.6.2017	31.12.2015	31.12.2014	31.12.2013
Net assets	16,701,512	24,606,797	23,069,558	46,981,837
Exchange rate	0.7199	1.0606	0.9944	2.0251

7. Return of the Fund

	30.6.2017	2016	2015	2014
Return of the fund	(32.13%)	6.66%	(50.90%)	8.13%
Real return of the fund	(32.83%)	4.47%	(51.86%)	7.02%

8. Loan from Financial Institutions

The fund and Arion Banki hf. made Subordinated Intercompany Loan Agreements to finance the acquisition of the mortgages. The loan agreements are calculated taking into account accrued interest and the consumer price index. Interest on the loan agreements ranges from 3.75% - 4.00% p.a.

Repayments on loan agreements at the end of June 2017 are as follows:

	Virði
Repayments 2017	1,935,233
Repayments 2018	2,251,407
Repayments 2019	2,337,345
Repayments 2020	2,426,564
Repayments 2021	2,519,189
Repayments later	89,852,651
	<u>101,322,388</u>

Notes to the Interim Financial Statements

Accounting methods

1. General information

The purpose of the ABMIIF Fund is to invest in residential real estate loans from Arion Bank and its subsidiaries, in accordance with the terms of the issuance of Covered Bonds. Its purpose is also to guarantee the payment of all amounts due under any Covered Bonds issued by the Issuer under the Programme, subject to the term of the Covered Bond Guarantee.

2. Basis of preparation

The Interim Financial Statements of Arion Bank Mortgages Institutional Investor Fund have been prepared in accordance with the Financial Statements Act and rules regarding Financial Statements of UCITS and investment funds set by the Icelandic Financial Supervisory Authority. They are prepared on the historical cost basis. The Interim Financial Statements have been prepared in Icelandic krónur (ISK) rounded to the nearest thousand. The fund is a part of Stefnir hf. which is a subsidiary of Arion Bank hf. The Interim Financial Statements form part of the consolidated Interim Financial Statements of Arion Bank hf.

3. Assessment and decisions

When preparing the financial statements, the management is required by the Annual Accounts Act to assess and make decisions on important components of the financial statements which are subjective by their nature. The assessment is based on experience and other relevant factors which are otherwise unavailable. Any changes according to this assessment are recognized during the period in which they occur.

4. Indexed assets and liabilities

Indexed assets and liabilities are calculated on basis of indexes valid 1 July 2017. Accrued indexation on principal of assets and liabilities is recognised in the income statement.

5. Interest income and expenses

Interest income and expense are recognised in the income statement as they are incurred.

6. Administration fee

The fund pays Stefnir hf. administration fee which includes the following operating costs for the fund: salaries of employees of the management company, marketing costs and administration; included in the administration fee is a custody fee to Arion banki hf. Administration fees are 0.1% of the fund's total assets.

The fund also pays fee for official supervisory.

7. Securities with fixed income

- a. Mortgages are recognised with accrued interest and indexation at the end of June 2017. At the end of June 12,58% of the fund's mortgages were calculated according to the index for mortgage payment adjustment.
- b. Provisions are done by a general provision and a special provision. Total provision for losses amounts to ISK 157 millions, which of specific provision amounts to ISK 102 millions and collective provision amounts to ISK 55 millions. The provision account has been deducted from Securities with fixed income in the Balance sheet.

Notes, cont.:

7. Securities with fixed income, cont.

c. Mortgages are specified as:	30.6.2017	31.12.2016
Mortgages before impairment	91,506,059	96,010,305
Provision at the beginning of the year	(141,082)	(248,576)
Write-offs during the period	0	4,801
Reversal during the period	(16,305)	102,693
Mortgages at the end of the period	<u>91,348,672</u>	<u>95,869,223</u>
Provision for losses as a ratio of total loans	0.17%	0.15%

8. Cash

Cash consists of cash and deposits with credit institutions including accrued interests.

9. Other assets.

Other assets include unsettled trades and deviations in exchange translations of assets.

10. Other liabilities.

Other liabilities include withhold capital gain tax on profits, unsettled trades and deviations in exchange translations of liabilities.

11. Taxation

The fund does not pay income tax; instead profit or loss from operations are taxed with the unit holders. Individuals pay capital gains tax on profits on their securities when redeemed. Profit and loss on unit shares owned by companies are treated as taxable income and expenses, regardless of redemption.

The fund is exempt from capital gains tax in Iceland but not in those countries where capital gains tax is imposed on income of foreign residents and when no double taxation agreement stating that such income should be taxed in Iceland exists between Iceland and the relevant country.