Landsbanki

Condensed Consolidated Interim Financial Statements

1 January - 31 March 2008

ISK

Landsbanki

Content

Consolidated Key Figures

Operations	2008 Q1	2007 Q1	%	2008 Q1	2007 Q4	%
Interest income	70,487	41,046	72%	70,487	57,935	22%
Interest expenses	55,232	30,167	83%	55,232	42,708	29%
Net interest income	**15,255**	**10,879**	**40%**	**15,255**	**15,227**	**0%**
Fee and commission income	13,444	10,886	23%	13,444	11,534	17%
Fee and commission expenses	2,541	1,124	126%	2,541	1,874	36%
Net fee and commission income	**10,904**	**9,762**	**12%**	**10,904**	**9,660**	**13%**
Net financial income	14,757	4,518	227%	14,757	(748)	2073%
Profit (losses) from associates	(80)	(58)	38%	(80)	671	-112%
Net gains of disposal groups held for sale, net of tax	2	4,339	-100%	2	9	-77%
Other operating income	**14,679**	**8,799**	**67%**	**14,679**	**(68)**	**21793%**
Net operating income	**40,837**	**29,441**	**39%**	**40,838**	**24,819**	**65%**
Salaries and related expenses	10,633	7,972	33%	10,633	10,769	-1%
Administrative expenses	6,601	4,444	49%	6,601	5,846	13%
Operating expenses	**17,233**	**12,415**	**39%**	**17,233**	**16,615**	**4%**
Impairment provisions on loans and advances and assets held for sale	3,915	1,549	153%	3,915	2,286	71%
Pre-tax profit	**19,690**	**15,476**	**27%**	**19,690**	**5,919**	**233%**
Income tax	2,265	1,716	32%	2,265	997	127%
Net profit	**17,425**	**13,760**	**27%**	**17,425**	**4,922**	**254%**
Attributable to:						
Shareholders of Landsbanki Íslands hf.	17,307	13,450	29%	17,307	4,584	278%
Minority interests	118	311	-62%	118	337	-65%

Five-year summary

	Q1 2008	2007	2006	2005	2004
Net interest income	15,255	54,052	41,491	22,996	14,734
Net fee and commission income	10,904	39,369	28,366	16,726	8,891
Other operating income	14,679	16,605	19,568	21,257	9,842
Net operating income	**40,838**	**110,025**	**89,426**	**60,978**	**33,467**
Operating expenses	17,233	57,515	38,588	20,967	14,460
Impairment on goodwill	0	0	0	3,033	0
Impairment on loans and advances and assets held for sale	3,915	6,956	6,144	6,197	4,485
Pre-tax profit	**19,690**	**45,555**	**44,694**	**30,781**	**14,521**
Income tax	2,265	5,605	4,479	5,764	1,798
Net profit	**17,425**	**39,949**	**40,215**	**25,017**	**12,723**
Attributable to:					
Shareholders of Landsbanki Íslands hf.	17,307	38,800	38,906	24,740	12,574
Minority interests	118	1,150	1,309	277	149

Balance Sheet	**31.3.2008**	**31.12.2007**	**Change**	**%**	**31.12.2006**	**31.12.2005**	**31.12.2004**
Cash and cash balances with Central Bank	103,522	81,559	21,963	27%	31,669	16,611	18,237
Loans and advances to financial institutions	268,285	162,929	105,357	65%	215,618	86,919	72,060
Loans and advances to customers	2,488,165	2,022,738	465,427	23%	1,438,395	984,593	542,215
Financial assets at fair value and associates	788,949	667,941	121,009	18%	376,809	218,894	64,730
Other assets	187,217	122,379	64,838	53%	110,432	98,443	39,900
Total assets	**3,836,139**	**3,057,546**	**778,593**	**25%**	**2,172,924**	**1,405,460**	**737,141**
Deposits from financial institutions	445,247	337,915	107,332	32%	141,105	144,596	63,476
Deposits from customers	1,636,910	1,421,410	215,500	15%	682,846	334,163	215,730
Borrowings	1,141,777	835,985	305,792	37%	1,014,976	689,989	375,084
Subordinated loans	145,503	111,890	33,613	30%	89,754	49,074	22,570
Other liabilities	268,255	166,342	101,913	61%	94,785	74,022	21,572
Equity	194,990	180,008	14,983	8%	144,282	110,059	37,705
Minority interests	3,457	3,996	(540)	-14%	5,175	3,557	1,004
Total liabilities and equity	**3,836,139**	**3,057,546**	**778,593**	**25%**	**2,172,924**	**1,405,460**	**737,141**

2 ISK million

Consolidated Key Figures

Operations	**2008 Q1**	**2007 Q4**	**2007 Q3**	**2007 Q2**	**2007 Q1**	**2006 Q4**
Interest income	70,487	57,935	54,036	49,078	41,046	34,887
Interest expenses	55,232	42,708	39,591	35,578	30,167	25,306
Net interest income	**15,255**	**15,227**	**14,445**	**13,500**	**10,879**	**9,581**
Fee and commission income	13,444	11,534	11,813	11,013	10,886	9,323
Fee and commission expenses	2,541	1,874	1,595	1,285	1,124	1,325
Net fee and commission income	**10,904**	**9,660**	**10,218**	**9,729**	**9,762**	**7,998**
Net financial income	14,757	(748)	3,029	4,754	4,518	6,587
Profit (losses) from associates	(80)	671	(1,171)	1,191	(58)	1,133
Net gains (losses) of disposal groups held for sale, net of tax	2	9	60	9	4,339	(479)
Other operating income	**14,679**	**(68)**	**1,918**	**5,955**	**8,799**	**7,240**
Net operating income	**40,837**	**24,819**	**26,582**	**29,184**	**29,441**	**24,819**
Salaries and related expenses	10,633	10,769	10,029	8,919	7,972	6,989
Administrative expenses	6,601	5,846	4,806	4,731	4,444	4,042
Operating expenses	**17,233**	**16,615**	**14,835**	**13,650**	**12,415**	**11,031**
Impairment provisions on loans and advances and assets held for sale	3,915	2,286	1,620	1,501	1,549	1,332
Pre-tax profit	**19,690**	**5,919**	**10,127**	**14,033**	**15,476**	**12,457**
Income tax	2,265	997	1,402	1,490	1,716	(1,596)
Net profit	**17,425**	**4,922**	**8,725**	**12,542**	**13,760**	**14,053**
Attributable to:						
Shareholders of Landsbanki Íslands hf.	17,307	4,584	8,518	12,248	13,450	13,664
Minority interests	118	337	207	294	311	389

Balance Sheet	**31.3.2008**	**31.12.2007**	**30.9.2007**	**30.6.2007**	**31.3.2007**	**31.12.2006**
Cash and cash balances with Central Bank	103,522	81,559	48,440	33,976	18,431	31,669
Loans and advances to financial institutions	268,285	162,929	134,379	278,072	251,881	215,618
Loans and advances to customers	2,488,165	2,022,738	1,840,584	1,567,895	1,483,887	1,438,395
Financial assets at fair value and associates	788,949	667,941	680,728	584,875	437,894	376,809
Other assets	187,217	122,379	142,552	132,329	125,097	110,432
Total assets	**3,836,139**	**3,057,546**	**2,846,682**	**2,597,147**	**2,317,190**	**2,172,924**
Deposits from financial institutions	445,247	337,915	210,332	161,826	117,378	141,105
Deposits from customers	1,636,910	1,421,410	1,390,022	1,187,254	913,183	682,846
Borrowings	1,141,777	835,985	749,629	781,541	903,780	1,014,976
Subordinated loans	145,503	111,890	82,517	77,766	83,524	89,754
Other liabilities	268,255	166,342	234,211	224,231	145,697	94,785
Equity	194,990	180,008	176,486	161,312	149,869	144,282
Minority interests	3,457	3,996	3,485	3,217	3,758	5,175
Total liabilities and equity	**3,836,139**	**3,057,546**	**2,846,682**	**2,597,147**	**2,317,190**	**2,172,924**

Key ratios	**2008 Q1**	**2007**	**2006**	**2005**	**2004**
Return on equity before taxes	50.3%	30.9%	40.3%	56.3%	57.2%
Return on equity after taxes	43.8%	27.1%	36.3%	45.8%	49.5%
Tier 1 ratio	8.8%	10.1%	13.0%	11.9%	7.8%
Equity ratio (CAD)	11.0%	11.7%	14.8%	13.1%	10.4%
Cost-income ratio	42.2%	52.3%	43.2%	34.4%	43.2%
Operating expenses as a ratio of average capital position	2.0%	2.2%	2.1%	2.0%	2.5%
Interest spread as a ratio of average capital position	1.8%	2.1%	2.3%	2.2%	2.6%
Deposits / loans to customers	65.8%	70.3%	47.5%	33.9%	39.6%
Deposits / total assets	42.7%	46.5%	31.4%	23.8%	29.3%
Ratio of provision to lending position at period-end	0.57%	0.32%	0.37%	0.58%	0.73%
Loan loss ratio	0.10%	0.07%	0.13%	0.19%	0.33%
Share price at period-end	29.60	35.50	26.50	25.30	12.10
Change in share price adjusted for dividend payments	-16.6%	35.5%	5.9%	110.7%	110.3%
Number of positions at period-end	2,702	2,640	2,117	1,725	1,121
Exchange rates					
Exchange rate ISK / EUR for P/L period average	101.98	87.64	87.57	76.59	86.97
Exchange rate ISK / EUR for balance sheet at period-end	119.57	91.65	93.72	74.7	83.51

ISK million

Report of the Board of Directors and Group Managing Directors & CEOs

The Condensed Consolidated Interim Financial Statements for the first three months of 2008 consist of the Condensed Consolidated Interim Financial Statements of Landsbanki Íslands hf. (the Bank) and its subsidiaries, (the Group). The Condensed Consolidated Interim Financial Statements are prepared in accordance with International Accounting Standard 34 "Interim Financial Reporting" (IAS 34).

The Bank's total share capital amounts to ISK 11,192,754,087 nominal value. All shares are in a single class, bear equal rights, and are divided into units of one Icelandic krona (1 ISK), or multiples thereof. As of 31 March 2008, shareholders in Landsbanki numbered 27,271 compared to 27,753 at the beginning of the year. Samson eignarhaldsfélag ehf., which holds 40.73% in the company, is the only shareholder with a stake over 10%.

According to the income statement, the Group's after tax-profit for the first three months amounted to ISK 17,425 million. The Group's equity at the end of this period totalled ISK 198,447 million. The capital adequacy ratio of the Group was 11.0%, well in excess of the statutory minimum of 8%. As of 31 March 2008, the Group's total assets were ISK 3,836,139 million.

According to the Directors' best knowledge, these Condensed Consolidated Interim Financial Statements comply with Act No. 3/2006, on Annual Accounts, and IAS 34 Interim Financial Reporting and give a true and fair picture of the Group's assets and liabilities, financial position and operating performance. They also describe the principal risk and uncertainty factors faced by the Group. The Report of the Board of Directors provides a clear overview of developments and achievements in the Group's operations and its situation.

The Board of Directors of the Bank and the Group Managing Directors and Chief Executive Officers hereby endorse the Condensed Consolidated Interim Financial Statements of Landsbanki Íslands hf. for the first three months of 2008.

Reykjavík, 6 May 2008

Board of Directors

Björgólfur Guðmundsson
Chairman

Kjartan Gunnarsson
Vice Chairman

Þorgeir Baldursson
Board Member

Andri Sveinsson
Board Member

Svafa Grönfeldt
Board Member

Group Managing Directors and Chief Executive Officers

Sigurjón Þ. Árnason

Halldór J. Kristjánsson

Report on Review of Interim Financial Information

Introduction
We have reviewed the accompanying Condensed Consolidated Interim Balance Sheet of Landsbanki Íslands hf. and its subsidiaries as of 31 March 2008 and the related condensed consolidated statements of income, changes in equity and cash flows for the three-month period then ended. Management is responsible for the preparation and presentation of this condensed consolidated interim financial information in accordance with International Accounting Standard 34, "Interim Financial Reporting". Our responsibility is to express a 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 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". 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 Condensed Consolidated Interim Financial Information is not prepared, in all material respects, in accordance with International Accounting Standard 34 "Interim Financial Reporting".

Reykjavík, 6 May 2008

PricewaterhouseCoopers hf.

Vignir Rafn Gíslason

Jón H. Sigurðsson

Condensed Consolidated Interim Income Statement 1 January – 31 March 2008

Notes		Q1 2008	Q1 2007
	Interest income	70,487	41,046
	Interest expenses	55,232	30,167
8	**Net interest income**	**15,255**	**10,879**
	Fee and commission income	13,444	10,886
	Fee and commission expenses	2,541	1,124
	Net fee and commission income	**10,904**	**9,762**
9, 10	Net financial income	14,757	4,518
19	Losses from associates	(80)	(58)
	Net gains of disposal groups held for sale, net of tax	2	4,339
	Other operating income	**14,679**	**8,799**
	Net operating income	**40,837**	**29,441**
11	Salaries and related expenses	10,633	7,972
	Administrative expenses	6,601	4,444
	Operating expenses	**17,233**	**12,415**
12	Impairment provisions on loans and advances and assets held for sale	3,915	1,549
	Pre-tax profit	**19,690**	**15,476**
13	Income tax	2,265	1,716
	Net profit	**17,425**	**13,760**
	Attributable to:		
	Shareholders of Landsbanki Íslands hf.	17,307	13,450
	Minority interest	118	311
14	**Earnings per share:**		
	Earnings per share	1.61	1.27
	Diluted earnings per share	1.45	1.19

The notes on pages 9 to 35 are an integral part of these Condensed Consolidated Interim Financial Statements

Landsbanki Condensed Consolidated Interim Financial Statements 6 ISK million

Condensed Consolidated Interim Balance Sheet as of 31 March 2008

Notes		31.3.2008	31.12.2007
	Assets		
	Cash and cash balances with Central Bank	103,522	81,559
	Loans and advances to financial institutions	268,285	162,929
15	Loans and advances to customers	2,488,165	2,022,738
16	Bonds	351,436	362,617
16	Equities	91,062	64,407
16	Hedged securities	160,047	176,181
16, 17	Derivatives held for trading	165,575	50,198
18	Derivatives held for hedging	15,943	8,719
19	Investments in associates	4,886	5,820
	Property and equipment	12,180	11,862
20	Intangible assets	38,363	27,679
	Deferred tax asset	810	960
21	Non-current assets and disposal groups classified as held for sale	4,968	3,641
	Unsettled securities trading	101,830	58,845
	Other assets	29,066	19,392
	Total assets	**3,836,139**	**3,057,546**
	Liabilities		
22	Deposits from financial institutions	445,247	337,915
23	Deposits from customers	1,636,910	1,421,410
24	Borrowings	1,059,755	774,754
25	Financial liabilities designated at fair value	82,022	61,231
26	Subordinated loans	145,503	111,890
17	Trading liabilities	131,710	62,161
18	Derivatives held for hedging	6,489	6,953
27	Tax liabilities	9,943	8,149
	Unsettled securities trading	84,593	48,399
	Other liabilities	35,520	40,679
	Total liabilities	**3,637,692**	**2,873,542**
	Equity		
	Share capital	10,836	10,865
	Share premium	50,845	53,417
	Reserves	468	191
	Retained earnings	132,842	115,535
		194,990	**180,008**
	Minority interest	3,457	3,996
	Total equity	**198,447**	**184,004**
	Total liabilities and equity	**3,836,139**	**3,057,546**

The notes on pages 9 to 35 are an integral part of these Condensed Consolidated Interim Financial Statements

Landsbanki Condensed Consolidated Interim Financial Statements 7 ISK million

Condensed Consolidated Interim Statement of Changes in Equity 1 January - 31 March 2008

	Attributable to Equity Holders of the Company							
		Share Premium		Reserves				
	Share capital	Additionally paid in capital	Statutory account	Translation	Fair value	Retained earnings	Minority interest	Total
Equity 1 January 2008	**10,865**	**53,148**	**268**	**191**	**0**	**115,535**	**3,996**	**184,004**
Exchange difference on translating foreign operations				276				276
Net income/(expense) recognised directly in equity	0	0	0	276	0	0	0	276
Net profit January - March 2008						17,307	118	17,425
Total recognised income and expense 31 March 2008	**0**	**0**	**0**	**276**	**0**	**17,307**	**118**	**17,701**
Purchases, sales, and fair value changes of treasury shares	(29)	(3,335)						(3,364)
Accrued stock options		763						763
Changes in minority interest							(657)	(657)
	(29)	**(2,572)**	**0**	**0**	**0**	**0**	**(657)**	**(3,258)**
Equity 31 March 2008	**10,836**	**50,577**	**268**	**468**	**0**	**132,842**	**3,457**	**198,447**
Equity 1 January 2007	**10,581**	**50,326**	**268**	**196**	**1,864**	**81,046**	**5,175**	**149,457**
Exchange difference on translating foreign operations				(29)				(29)
Fair value adjustment of investment properties, included in disposal groups					(1,864)			(1,864)
Net income/(expense) recognised directly in equity	0	0	0	(29)	(1,864)	0	0	(1,893)
Net profit January - March 2007						13,450	311	13,760
Total recognised income and expense 2007	**0**	**0**	**0**	**(29)**	**(1,864)**	**13,450**	**311**	**11,867**
Purchases, sales, and fair value changes of treasury shares	(50)	(1,960)						(2,011)
Accrued stock options		352						352
Dividends paid						(4,311)		(4,311)
Changes in minority interest							(1,727)	(1,727)
	(50)	**(1,609)**	**0**	**0**	**0**	**(4,311)**	**(1,727)**	**(7,697)**
Equity 31 March 2007	**10,531**	**48,718**	**268**	**167**	**0**	**90,185**	**3,758**	**153,628**

Condensed Consolidated Interim Statement of Cash Flow 1 January - 31 March 2008

	2008 1.1 - 31.3	2007 1.1 - 31.3
Cash flows from operating activities	(71,757)	178,797
Cash flows from investing activities	(6,032)	(5,207)
Cash flows from financing activities	94,344	(72,286)
Net Increase in cash and cash equivalents	**16,556**	**101,304**
Cash and cash equivalents at beginning of year	149,271	41,147
Foreign exchange difference	23,742	(2,179)
Cash and cash equivalents at period-end	**189,569**	**140,272**

The notes on pages 9 to 35 are an integral part of these Condensed Consolidated Interim Financial Statements

Landsbanki Condensed Consolidated Interim Financial Statements 8 ISK million

1. General information

Landsbanki (the Group) is a universal bank that provides retail, corporate, and investment banking services. The Group operates in 14 countries and had 2,702 employees at period-end.

The Group's parent company is Landsbanki Íslands hf. (the Bank), which is a limited-liability company incorporated and domiciled in Iceland. Its registered office is Austurstræti 11, 155 Reykjavík. The Bank was established in 1886 and remained State-owned until 1998 when the Government of Iceland decided to privatise the Bank through a public offering. Today, the Bank's shares are listed on the OMX Nordic Exchange.

These condensed consolidated interim financial statements were approved for issue by the Board of Directors on 6 May 2008.

2. Summary of significant accounting policies

The principal accounting policies applied in preparing these condensed consolidated interim financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

2.1 Basis of preparation

These condensed consolidated interim financial statements of Landsbanki Íslands hf. cover the three months from 1 January to 31 March 2008. They have been prepared in accordance with IAS 34, Interim Financial Reporting. Condensed interim financial statements such as these do not include information as extensive as annual financial statements, and should be read in conjunction with Landsbanki's annual Consolidated Financial Statements for the year 2007.

These consolidated interim financial statement reflect the IFRS and interpretations issued and effective in March 2008.

These consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of financial statements in accordance with IFRS requires the use of certain accounting estimates. It also requires management to exercise judgement in the process of applying various accounting policies. Critical accounting estimates and judgements in applying accounting policies are disclosed in Note 3.

2.2 Consolidation

(a) Subsidiaries

Subsidiaries are all entities (including certain special-purpose entities (SPEs) where appropriate) over which the Group has the power to govern financial and operating policies generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases. SPEs are consolidated when the substance of the relationship between the Group and that entity indicates control. Potential indicators of control, as set out in SIC 12 'Consideration – Special Purpose Entities', include, amongst others, an assessment of the Group's exposure to the risks and benefits of the SPE.

On the date of reporting, the Group's significant subsidiaries were:

Company	Share owned	Activity
Heritable Bank Ltd (UK)	100%	Corporate banking
Landsbanki Securities (UK) Holdings plc	100%	Stockbrokers and financial services
Landsbanki Holdings Europe SA (Luxembourg)	100%	Holding company
- Landsbanki Luxembourg SA (Luxembourg)	100%	Private and corporate banking
- Landsbanki Kepler SA (France)	100%	Stockbrokers and financial services
Landsbanki Guernsey Ltd (UK)	100%	Retail banking
Merrion Capital Group Ltd (Ireland)	84%	Stockbrokers and financial services
LI Investments AB (Sweden)	100%	Holding company
Landsbanki Holdings (UK) plc	100%	Holding company
LI Investments Ltd (British Virgin Islands)	100%	Holding company
Landsvaki hf. (Iceland)	100%	Operation company for mutual funds
Landsbankinn eignarhaldsfélag ehf. (Iceland)	100%	Holding company
Landsbankinn - Fjárfesting hf. (Iceland)	100%	Holding company
Landsbankinn fasteignafélag ehf. (Iceland)	100%	Real estate company
Landsbanki Vatnsafl ehf. (Iceland)	100%	Holding company
SP – Fjármögnun hf. (Iceland)	51%	Leasing company
Verðbréfun hf. (Iceland)	100%	Securitization company
Hömlur hf. (Iceland)	100%	Holding company for appropriated assets
Span ehf. (Iceland)	100%	IT services

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of acquisition is measured as the fair value of the assets given, equity instruments issued, and liabilities incurred or assumed at the transaction date, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair value on the acquisition date, irrespective of the extent of any minority interest.

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The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances, and unrealised gains on transactions between Group companies are eliminated in the consolidated accounts. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Transactions and minority interests

The Group applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Disposals to minority interests result in gains and losses for the Group that are recorded in the income statement. Purchases from minority interests result in goodwill, which is the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

(c) Associates

Associates are all entities in which the Group has significant influence, but not control, generally accompanying a shareholding of between 20% and 50% of the share capital conferring voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of its associates' post-acquisition profits or losses is recognised in the income statement, and its share of movements in reserves is recognised in reserves within equity. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

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 an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

2.3 Segment reporting

A business segment is a part of the Group's assets and operations that is subject to risks and returns differing from those of other business segments. A geographical segment is a part of the assets and operations within a particular economic environment that is subject to risks and returns that is different from those of segments operating in other economic environments.

2.4 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's individual entities are measured using the currency of the economic environment in which the entity operates (the functional currency). These consolidated financial statements are presented in millions of Icelandic kronas (ISK), which is also the Bank's functional currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions, and the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement, except when deferred in equity as qualifying net investment hedges. Translation differences on non-monetary items, such as equities held at fair value through profit and loss, are reported as part of the fair value gain or loss.

(c) Group companies

The results and financial position of the Group's entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

(i) the assets and liabilities of each balance sheet are translated at the closing rate at the period-end;
(ii) items of each income statement are translated at the average exchange rate for the year (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions);
(iii) all resulting exchange differences are recognised as a separate component of equity.

Exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges on such investments, are taken to shareholders' equity. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on the sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

2.5 Derivative financial instruments and hedge accounting

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are based on quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is based on comparison with comparable transactions in similar instruments. Fair value can also be based or founded on the basis of pricing models.

Derivatives embedded in other financial instruments are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit and loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

(a) Fair value hedge

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as hedges of the fair value of assets or liabilities (fair value hedges). Hedge accounting is used for derivatives designated in this way provided certain criteria are met.

At the inception of the transaction, the Group documents the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The relationship is documented and an assessment made, both at hedge inception and at each reporting period, of whether the derivatives used in hedging transactions are highly effective in offsetting changes in fair values of hedged items.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. Any ineffectiveness is recorded in 'Fair value adjustments in hedge accounting'.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to profit or loss over the period to maturity.

(b) Net investment hedge

Any gain or loss on a hedging instrument relating to the effective portion of a hedge of net investments in foreign operations is recognised in equity as translation reserve; the gain or loss relating to the ineffective portion is recognised immediately in the income statement. Gains and losses accumulated in equity are included in the income statement when the foreign operation is disposed of.

(c) Derivatives that do not qualify for hedge accounting

Derivative financial instruments that do not qualify for hedge accounting are recognised as trading assets or trading liabilities. Changes in their fair value are recognised immediately in the income statement.

2.6 Interest income and expense

Interest income and expense for all instruments measured at amortised cost are recognised in the income statement using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset, or a financial liability, and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts exactly estimated future cash flows or receipts through the expected life of the financial instrument or, when appropriate, a shorter period, making it equivalent to the net carrying amount of the financial asset or financial liability in the balance sheet. When calculating the effective interest rate, the Group estimates cash flows, considering all contractual terms of the financial instrument, but does not consider future credit losses. The calculation includes all fees and amounts paid or received between parties to the contract that are an integral part of the effective interest rate, as well as transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

2.7 Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Loan commitment fees for loans are generally deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan. Commissions and fees arising from participating in the negotiation of a transaction for a third party – such as arrangement of transactions with equities or other securities or the purchase or sale of businesses – are recognised on completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportionate basis. Asset management fees related to investment funds are recognised rateably over the period the service is provided. The same principle for income reporting is applied for other custody services that are continuously provided over an extended period of time.

2.8 Dividend income

Dividends are recognised in the income statement when the entity's right to receive payment is established.

2.9 Financial assets

The Group classifies its financial assets in the following categories: financial assets designated at fair value through profit or loss including financial assets held for trading and loans and advances. Management determines the classification of its investments at initial recognition.

(a) Assets held for trading

A financial asset at fair value through profit or loss is classified in this category if it is primarily held for the purpose of trading in the near term. Derivatives are classified as assets held for trading unless designated as a hedging instrument.

(b) Financial assets designated at fair value through profit or loss

Financial assets are designated at fair value through profit or loss when:

- Certain investments, such as equity investments, are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy; and
- Financial instruments, such as debt securities held, contain one or more embedded derivatives significantly modify the cash flows; and
- Financial assets backing investment contracts have related liabilities that have cash flows that are contractually based on the performance of the assets.

Such financial assets are carried at fair value with changes in fair value recognised in the income statement. The classification of financial assets designated in this category cannot be subsequently changed.

(c) Loans and advances

Loans and advances are financial assets with defined payments that are not quoted in an active market. They arise when the Group provides funds directly to a debtor with no intention of trading them.

Regular way purchases and sales of financial assets designated at fair value through profit or loss are recorded on the date on which the Group commits to purchase or sell the asset. Loans are recognised when the funds related to the loan are disbursed to the borrowers.

Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit and loss are initially recognised at fair value, and transaction costs are expensed in the income statement.

The Group derecognises financial assets when:

(i) the assets are redeemed or the rights to cash flows from the assets otherwise expire or;
(ii) the Group has transferred substantially all the risks and rewards of ownership of the assets or;
(ii) the Group has neither transferred nor retained substantially all risks and reward of ownership, but has not retained 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 additional restrictions on the sale.

Financial assets designated at fair value through profit or loss and trading assets are subsequently carried at fair value. Loans and advances are carried at amortised cost using the effective interest method. Gains and losses arising from changes in the fair value of the financial assets at fair value through profit and loss and trading assets are recorded in the income statement in the period in which they arise.

The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using recognised valuation techniques. These include the use of information about recent arm's length transactions, references to other materially equivalent instruments, discounted cash flow analysis and option pricing models and other valuation techniques commonly used by market participants.

2.10 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legal enforceable right to offset the recognised amounts and there is an intention to settle on a net basis.

2.11 Sale and repurchase agreements

Sale and repurchase agreements (repos) provide for the sale of securities under agreement to repurchase the same securities at a predetermined price on a predetermined future date. Securities sold under sale and repurchase agreements are not derecognised as the Group does not transfer substantially all risks and rewards associated with them.

2.12 Securities lending and borrowings

Lending agreements are financial instruments where the securities are not sold, but are returned to the Group at the end of contract. Control of the securities remains in the hands of the Group during their entire transaction period and the securities remain on its balance sheet as trading assets or as financial assets designated at fair value through profit or loss, as appropriate.

Securities borrowed are not recognised in the financial statements, unless these are sold to third parties, at which point the obligation to repurchase the securities is recorded as a trading liability at fair value and any subsequent gain or loss included in net trading income.

2.13 Impairment of loans and advances

At each balance sheet date, the Group assesses whether there is objective evidence that a loan or loan portfolio is impaired. A loan or loan portfolio is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset ('loss event') and that loss event (or events) has an impact on the estimated future cash flows of the loan or group of loans that can be reliably estimated. Objective evidence of impairment includes observable data about the following loss events:

(i) significant financial difficulty of the borrower;
(ii) a breach of contract, such as a default on instalments or on interest or principal payments;
(iii) the Group grants to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a refinancing concession, that the lender would not otherwise consider;
(iv) it becomes probable that the borrower will enter bankruptcy or undergo other financial reorganisation; or
(v) observable data indicates that there is a measurable decrease in the estimated future cash flows from a group of loans since the initial recognition of those assets, even if the decrease cannot yet be identified with the individual financial assets in the group, including:
– adverse changes in the payment status of borrowers in the group; or
– general deterioration of economic conditions connected with a group of loans.

The Group defines loans that are individually significant and assesses first whether objective evidence of their impairment exists, and individually or collectively for loans and advances that have not been defined as individually significant. If the Group determines that no objective evidence of impairment exists for significant loans, it includes the loan in a group of loans with similar credit risk characteristics and collectively assesses them for impairment. Individual significant assets for which an impairment loss is recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and advances has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the asset's recoverable value. The recoverable value is the present value of estimated future cash flows (excluding future credit losses that have not been incurred), discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced by the amount of impairment through the use of an allowance account and the amount of the loss is recognised in the income statement. In the case of loans with variable interest rates, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, loans are grouped on the basis of similar credit risk characteristics (i.e., on the basis of the Group's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such loans by being indicative of the debtors' ability to pay all amounts due according to their contractual terms.

Future cash flows in a group of loans that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with similar credit risk characteristics. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience was originally based and to remove the effects of previously existing loss factors that do not exist currently.

Estimates of changes in future cash flows for groups of assets should be consistent with changes in observable data from period to period (for example, changes in property prices, payment status, or other factors indicative of changes in the probability of losses on the Group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to minimise any differences between loss estimates and actual loss experience.

When a loan is uncollectible, it is written off against the provision for loan impairment on the balance sheet. Loans are written off after all the necessary procedures have been completed, as set out in the Group's lending directives, and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recognised in the income statement.

If, in the subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the original impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement in impairment charge for credit losses.

2.14 Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary/associate at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in intangible assets. Goodwill on acquisitions of associates is included in investments in associates. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Gains and losses on the disposal of a subsidiary/associate include the carrying amount of goodwill relating to the entity sold. Goodwill is allocated to cash-generating units for the purpose of impairment testing.

(b) Computer software and other intangible assets

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring into service the specific software. Computer software recognised as intangible assets is amortised over its useful life (determined to be 5 years).

Costs associated with maintaining computer software are recorded as expenses, when incurred.

Other intangible assets are customer agreements identified at business acquisition, amortised over their useful life (determined to be 15 years).

2.15 Property and equipment

All property and equipment is stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and these costs can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Land is not depreciated. Depreciation on property and equipment, other than land, is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

Buildings	25-100 years,
Computer hardware	3-5 years,
Other equipment and motor vehicles	3-10 years.

The assets' residual values and useful lives are reviewed annually and adjusted, if appropriate.

Gains and losses on disposals are determined by comparing the sale price of an asset with its carrying amount on the date of sale. Gains and losses are included in the income statement.

2.16 Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed 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 asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.17 Non-current assets held for sale

Non-current assets held for sale comprise of repossessed collateral, which is in the process of being sold, as well as disposal groups. Liabilities connected with the disposal group are recognised as a separate liability on the balance sheet. Items included under non-current assets held for sale are recognised at the lower of carrying amount and fair value less cost to sell.

2.18 Leases

(a) A group company is the lessee

The leases entered into by the Group are primarily operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

(b) A group company is the lessor

When assets are held subject to a finance lease, the present value of the lease payments is recognised as a receivable as a part of loans and advances to customers. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using a method that reflects a constant periodic rate of return.

2.19 Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents are defined as cash and non-restricted balances with the Central Bank and amounts due from other financial institutions.

2.20 Provisions

Provisions for restructuring costs and legal claims are recognised when (i) the Group has a present legal or constructive obligation as a result of past events; (ii) it is more likely than not that an outflow of resources will be required to settle the obligation; (iii) and the amount has been reliably estimated.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as interest expense.

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2.21 Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions, and other bodies on behalf of customers to secure loans, overdrafts, and other banking facilities.

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Group's liabilities under such guarantees are measured at the higher of the initial measurement, less amortisation calculated to recognise in the income statement the fee income earned on a straight-line basis over the life of the guarantee and the best estimate of the expenditure required to settle any financial obligation arising at the balance sheet date. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgment of management.

2.22 Employee benefits

(a) Pension obligation

Group companies operate various pension schemes. Most of the Group companies have defined contribution plans, where the companies pay fixed contributions to publicly or privately administered pension insurance plans on a mandatory, contractual, or voluntary basis. The Group has no further payment obligations once these contributions have been paid. The contributions are recognised as an expense when they become due.

A few of the Group's companies have defined benefit plans. A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors, such as age, years of service, and compensation.

The liability recognised in the balance sheet in respect of defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating the terms of the related pension liability.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions in excess of the greater of 10% of the value of plan assets or 10% of the defined benefit obligation are charged or credited to income over the employees' expected average remaining working lives. Past service costs are recognised immediately in administrative expenses, unless the changes to the pension plan are conditional on the employees' remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

(b) Share-based compensation

The Group has entered into stock options contracts with its employees' enabling them to acquire shares in the Bank. In all instances, the exercise price corresponds to the market value of the shares at grant date. Cost related to the stock option agreements is expensed during the vesting period based on the related terms.

All stock options are equity settled share-based compensation, and the Group recognises the fair value of the services received as an expense in the period that these services are received.

The Group uses the Black-Scholes valuation model to determine the fair value of options granted. The significant inputs into the model were share prices at the grant date, exercise price, the volatility of standard deviation of expected share price, dividend yield and a risk-free interest rate.

2.23 Deferred income tax

Deferred income tax is recognised in full as a liability, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However deferred income tax is not recognised, if it arises from the initial recognition of an asset or liability in a transaction other than a business combination, which, at the time of the transaction, affects neither its accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from revaluation of certain financial assets and liabilities, including derivative contracts. Temporary differences also include tax losses carried forward and the difference between the fair values of assets acquired and their tax base. Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax arising from temporary differences in connection with investments in subsidiaries and associates is recognised in the consolidated financial statements. However this is not done, where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the difference will not reverse in the foreseeable future.

The tax effects of tax losses available for carry-forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

2.24 Borrowings

Borrowings are recognised initially at fair value net of transaction costs incurred. Borrowings are subsequently stated at amortised cost using the effective interest method.

2.25 Subordinated loans

The Group has borrowed funds by issuing bonds on subordinated terms. These bonds are subordinated to the other liabilities of the Group. For the purpose of the calculation of the capital ratio, the bonds are included within Tier I and Tier II capital. Subordinated loans are carried at amortised cost.

2.26 Financial liabilities designated at fair value through profit or loss at inception

Financial liabilities are designated at fair value through profit or loss when:

- Doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortised cost such as loans and advances to customers or banks and debt securities in issue; and
- Financial instruments, such as debt securities held, contain one or more embedded derivatives that significantly modify the cash flows; and
- The Group is engaged in a unit-linked investment contracts where the liability reflects the value of assets held within unit-linked investment pools.

Such financial liabilities are reported at current fair value and changes recognised in the income statement. The classification of financial liabilities placed in this category cannot be changed after their original classification.

2.27 Share capital

(a) Share issue costs

Costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds.

(b) Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the period in which they are approved by the Group's shareholders' meeting.

(c) Treasury shares

Where the Bank, or other members of the Group, purchases the Group's equity share capital, the consideration paid is deducted from total shareholders' equity as treasury shares until they are cancelled. Where such shares are subsequently sold or reissued, any consideration received is included in shareholders' equity.

2.28 Fiduciary activities

The Group acts as a custodian, holding or placing assets on behalf of individuals, institutions, and pension funds. These include various mutual funds managed by the Group. These assets and income arising therefrom are excluded from these financial statements, as they are not assets of the Group.

2.29 Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year.

3. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. By definition, the accounting estimate based on these assumptions will seldom be equivalent to the relevant real outcome. The discussion below examines estimates and assumptions that involve a substantial risk of causing material correction to the carrying amounts of assets and liabilities within the next financial year.

(a) Impairment losses on loans and advances

The Group reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgements as to whether there are any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(b) Fair value of derivatives

The fair value of financial instruments not quoted in active markets is determined by various recognised valuation techniques. When valuation techniques (e.g. models) are used to determine fair value, they are validated and periodically reviewed by qualified personnel independent of the area that created them. All models are certified before they are used, and are calibrated to ensure that outputs reflect actual data and comparative market prices. To the extent practicable, models use only observable data, however, areas such as credit risk require management to make estimates. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

4. Management of financial risk

The Group's risk policy and procedures ensure that the risks involved in its operations are known, measured, and monitored. Risk is managed to ensure that it remains within the limits adopted by the Group for its operations and complies with regulatory requirements. The Group structures its portfolio to ensure that fluctuations resulting from unexpected events, affecting both the Group's equity and its performance, are both limited and manageable.

The Board of Directors is responsible for the Group's general policy on risk, ensuring that it conforms to the Group's strategy, the experience of its management, its capital adequacy and readiness to accept risk. The Group's CEOs are responsible to the Board for its daily operations and manage its risk through committees. Furthermore, managing directors report to the CEOs for the activities of their respective divisions and for ensuring that risk accords with the Group's policy.

The Group has five standing committees: the Asset and Liability Committee (ALCO), the Asset Management Committee, the Credit Committee, the Operations Committee and the Landsbanki Group Risk Committee. The Landsbanki Group Risk Committee (LGRC) is responsible for effective risk management and control in the Landsbanki Group.

The Board of Directors has two sub-committees, an Audit Committee and Remuneration Committee, which prepare examination by the Board of specific areas of operation and detailed investigation of issues falling within their sphere of responsibility.

In addition to these committees, meetings of managing directors serve as a forum for consultation between the CEOs and managing directors.

The Compliance Officer ensures that the Group's rules on securities trading and insider trading are followed, and that Group operations comply with the Act on Securities Transactions, the Act on Actions to Combat Money Laundering and other relevant statutes and regulations. Each of the Bank's subsidiaries has a compliance officer, and the Group's Compliance Officer supervises their work and reports to the Board of Directors.

Landsbanki's internal auditing is carried out on a Group basis and the Director of Internal Audit for the Bank audits all Group companies. Internal auditing is an essential aspect of the Group's risk management control; each operating unit is audited at least once a year.

4.1 Financial instruments and risk management strategy

Clients' assets and liabilities bear fixed or variable rates of interest over longer or shorter terms, as it is essential for the Group to control its investments closely to maintain a balance in the interest rates and maturities of assets and liabilities. The Group also endeavours to increase its interest rate margin by offering both short-term and long-term credit, while at the same time it must maintain sufficient liquidity to meet its commitments. By extending credit to both corporations and individuals, on varying terms reflecting the risk of loss in each instance, the Group aims to achieve an acceptable interest rate margin. Interest rate risk is not limited to interest-bearing assets on the Group's balance sheet, but also includes guarantees and derivatives.

By taking positions and trading in listed and unlisted financial instruments, the Group can take advantage of short-term movements on the equity and bond markets, as well as currency and interest rate fluctuations. Currency risk is generally kept in balance. Part of the Group's currency risk is hedged with currency swaps. Interest rate swaps and currency interest rate swaps are used to partly hedge interest rate risk against any drop in the fair value of fixed interest rate assets and any increase in the fair value of customers' deposits on fixed terms.

4.1.1 Hedge accounting

In order to decrease volatility in profit and loss due to changes in market rates, the Group aims to hedge future cash flow of fixed income payment by entering into interest rate and cross-currency swaps, effectively exchanging the fixed rate for floating rate. The Group designates specific derivatives as hedges of the fair value of assets or liabilities. Hedge accounting is used for derivatives designated in this way provided certain criteria are met.

(a) Fair value hedge

The Group uses interest rate and currency swaps to hedge part of its interest rate risk against any possible impairment of the fair value of fixed and floating interest rate assets and liabilities in both ISK and foreign currencies. The net fair value of these swaps as of 31 March 2008 was positive in the amount of ISK 9,453 million.

(b) Net investment hedge

The Group balances currency risk arising from net investment in foreign operation against foreign currency borrowing. At 31 March 2008, loans amounting to ISK 115,217 million (31.12.2007: ISK 86,489 million) were recognised as hedges, resulting in exchange rate loss for the first three months of the year of ISK 24,362 million (2007: ISK 2,504 million profit) recognised in equity against exchange rate profit from investments in subsidiaries.

The Group has decided to reduce its net investment hedge in foreign operations from the beginning of Q2 2008, reducing related foreign exchange difference from borrowing recognised in equity.

4.1.2 Credit risk

Credit risk is the Group's greatest single risk factor. Credit risk is the risk that a borrower or counterparty in a transaction will be unable to meet its financial obligations. The Group manages this risk by setting limits for acceptable risk for individual borrowers or groups of borrowers, specific regions or industrial sectors. Such risk factors are under constant surveillance and are reviewed regularly. Credit risk is also managed through regular assessments of clients' credit ratings, modifications of lending authorisations, or acquiring better collateral to secure clients' commitments.

The Board of Directors sets detailed lending rules, including maximum obligations for individual clients and related parties. The purpose of these rules is to limit the maximum risk of the Group. They cover clients' total exposures, so that the indirect risk to the Group through its clients is added to the direct claims of the Bank and its subsidiaries. Financial instruments issued by a client, which are used to guarantee other obligations of third parties not financially connected, are also added to the direct claims. According to the Bank's internal rules, the maximum total exposures through an individual customer or financially connected parties may not exceed 20% of the Group's equity.

Clients classified in the best risk classes according to the Group's rating system, may comprise an aggregate exposure of as much as 25% of the Group's equity, but only in the form of short-term obligations. Parties classified in poorer risk categories may not comprise overall exposures for the Group exceeding 10% of its equity. In similar fashion, however, this exposure may be increased to as much as 15%, provided the portion exceeding 10% is in the form of short-term commitments.

The Credit Committee sets detailed lending rules based on the basic policy laid down by the Board of Directors. Employees' lending authorisations are well defined and incremental. The Credit Committee delegates and reviews employees' authorisations and is responsible for reviewing lending rules. Comprised of the CEOs and managing directors, it meets regularly to discuss all credit decisions exceeding the authorisations of branches, subsidiaries, or the Corporate Banking Division. The Committee checks the composition of the loan portfolio with regard to industrial sectors, geographical regions, collateral, and other aspects, as well as monitoring defaults and default trends. Detailed reports on the position of the Group's largest debtors are reviewed by the Credit Committee, together with special reports, e.g. on the situation of the economy in general and specific industrial sectors, etc.

(a) Collateral

Securing loans by collateral is the traditional method of mitigating credit risk. The Group obtains collateral to secure customer liabilities where considered appropriate, normally in the form of a lien on customer assets, giving the bank a claim on these assets for both existing and future liabilities. Credit extended by the bank may be secured by residential or corporate real estate, land, securities, transport vessels, fishing vessels together with their non-transferable fishing quotas, aircraft, etc. The Group also secures its loans with receivables and operating assets, such as machinery and equipment, raw materials, and inventories. Residential housing mortgages are generally fully secured by a charge against residential property. Less stringent requirements are set for securing short-term personal loans, such as overdrafts and credit card borrowing.

(b) Derivatives

Counterparty risk from derivative contracts is managed by the Bank's Securities and Treasury division. Risk from derivative contracts is assessed as a credit equivalent, comprised of the fair value of the contract and its assessed future risk.

(c) Credit-related commitments

Guarantees and letters of credit, which irrevocably commit the Group to make payment to a third party in the event a customer cannot fulfil his obligations, involve the same credit risk as loans. Import guarantees and documentary credits are secured by the goods shipments they cover, thus representing a lower risk than direct loans. Unused credit lines represent a commitment to increase loans or guarantees. The Group could conceivably suffer losses equivalent to the total amount of open credit lines. The Group monitors the duration of credit lines, since longer-term obligations generally imply a greater credit risk.

(d) Netting arrangements

In order to further limit counterparty risk arising from financial instruments, the Group enters into netting agreements. In the case of foreclosure, these arrangements ensure that the Group can set off all contracts covered by the netting agreement against the debt. The arrangements generally include all market transactions between the Group and the client.

4.2 Geographical location of loans and advances to customers

	31.3.2008		31.12.2007	
		%		%
Iceland	1,327,316	53	1,191,700	58
UK & Ireland	500,326	20	413,493	20
Continental Europe	420,284	17	293,423	14
US and CAN/other countries	267,749	11	146,103	7
Provisions for credit losses on loans and advances	(27,510)		(21,981)	
Total	**2,488,165**	**100**	**2,022,738**	**100**

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4.3 Market risk

Market risk is the risk arising from the impact of changes in market prices on the value of the Group's assets and liabilities, both on and off its balance sheet. This includes both interest rate and equity risk on its trading portfolio, as well as currency risk on its portfolios. However market risk is, mainly limited to the Group's trading book transactions.

The Board of Directors has set a ceiling on the Group's market risk, which may not exceed 15% of its total risk-weighted asset base. Within this limit, equity risk may not exceed 12%, currency risk may not be more than 7.6% for long positions or 3.3% for short positions, and the maximum interest rate risk on market bonds and other financial instruments may not exceed 6%. ALCO sets detailed rules on the Group's maximum market risk. Risk control is effected on a Group basis, under the direction of Risk Management. Authorisations to take positions subject to market risk are mainly limited to the Investment Banking Division of the Group, where total market risk for the Group is also managed. In addition to the Investment Banking Division of the Group, trading desks of its subsidiaries, Landsbanki Kepler, Landsbanki Securities UK, and Merrion Capital, have limited authorisations for exposures on own account.

Total market risk for the Group is calculated at the end of each banking day and controlled by means of an authorisation system adopted by ALCO. Since no single instrument can cover all the aspects of market risk, the Group applies several methods in its daily risk measurement, including VaR (Value-at-Risk) and stress testing, and uses indicators such as net position and value per bp (Vpb).

Value at Risk (VaR) is a statistical measurement indicating the likelihood of loss due to unfavourable changes in market conditions within a specific time period and wit a specified probability.

The first of the following tables shows the VaR estimate for market risk for the Group's total exposure. The second table shows market risk excluding unlisted securities and the third table shows market risk excluding unlisted securities and financial assets designated at fair value through profit and loss:

Market risk	**1 January to 31 March 2008**				**12 months to 31 December 2007**		
	Average	**High**	**Low**	**31.3.2008**	**Average**	**High**	**Low**
Interest rate risk	881	1,076	779	1,034	401	886	169
Foreign exchange risk	2,521	5,292	1,672	5,194	791	2,067	2
Equities risk	2,660	4,056	1,743	3,962	1,482	3,288	501
Diversification	(3,309)			(5,996)	(1,217)		
Total VaR (99% 1-day holding period)	**2,754**	**4,195**	**2,221**	**4,195**	**1,457**	**2,849**	**733**
Total VaR (99% 10-day holding period)	**8,707**	**13,265**	**7,023**	**13,265**	**4,606**	**9,008**	**2,317**

Market risk without unlisted securities

	Average	**High**	**Low**	**31.3.2008**	**Average**	**High**	**Low**
Interest rate risk	881	1,076	779	1,034	401	886	169
Foreign exchange risk	2,521	5,292	1,672	5,194	791	2,067	2
Equities risk	1,351	2,217	891	2,143	820	1,673	358
Diversification	(2,048)			(3,644)	(759)		
Total VaR (99% 1-day holding period)	**2,706**	**4,807**	**2,178**	**4,728**	**1,252**	**2,508**	**668**
Total VaR (99% 10-day holding period)	**8,556**	**15,200**	**6,889**	**14,951**	**3,960**	**7,930**	**2,113**

Market risk without unlisted securities and financial assets designated at fair value through profit and loss

	Average	**High**	**Low**	**31.3.2008**	**Average**	**High**	**Low**
Interest rate risk	881	1,076	779	1,034	401	886	169
Foreign exchange risk	2,521	5,292	1,672	5,194	791	2,067	2
Equities risk	813	1,348	448	1,292	675	1,531	278
Diversification	(1,348)			(2,404)	(689)		
Total VaR (99% 1-day holding period)	**2,867**	**5,255**	**2,188**	**5,117**	**1,177**	**2,585**	**493**
Total VaR (99% 10-day holding period)	**9,066**	**16,616**	**6,919**	**16,180**	**3,723**	**8,173**	**1,559**

The Group recognises the importance of assessing the effectiveness of its VaR models. The models are back-tested, i.e. the number of days when trading losses actually exceeded the estimated VaR figure are counted. According to the regulatory standard for back-testing, its purpose is to measure VaR assuming a one-day holding period with a 99% level of confidence. For Landsbanki's regulatory trading book, there were 0 instances in the last 12 months exceeding the corresponding VaR in the back-testing.

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4.3.1 Currency risk

The Group's currency risk is managed with the objective of limiting this total risk factor within defined net position limits set by ALCO. Changes in prices of currency pairs against ISK will affect the Group's equity ratio as its foreign denominated assets are 75% of the Group's asset base while the Group's equity is ISK denominated. The Group maintains a considerable open currency position and issues subordinated debt in foreign currency to

The following table shows the carrying amount of the Group's assets and liabilities by currency. Off-balance sheet amounts show the notional amounts of financial instruments in foreign currencies.

Concentrations of assets, liabilities, and off-balance sheet items.

At 31 March 2008	ISK	EUR	GBP	Other	Total
Assets					
Cash and cash balances with Central Bank	78,805	20,341	4,069	307	103,522
Loans and advances to financial institutions	64,401	108,260	37,726	57,898	268,285
Loans and advances to customers	587,385	581,618	409,718	909,444	2,488,165
Bonds	75,137	189,031	11,427	75,841	351,436
Equities	26,330	27,076	12,675	24,981	91,062
Hedged securities	74,989	44,894	22,974	17,190	160,047
Derivatives held for trading	17,450	69,450	17,302	61,373	165,575
Derivatives held for hedging	1,035	1,254	0	13,654	15,943
Investments in associates	4,318	568	0	0	4,886
Property and equipment	10,709	826	645	0	12,180
Intangible assets	3,818	17,385	17,160	0	38,363
Deferred tax asset	58	585	167	0	810
Non-current assets and disposal groups classified as held for sale	1,278	0	3,689	0	4,968
Unsettled securities trading	9,498	68,755	16,241	7,337	101,830
Other assets	5,714	15,688	6,247	1,417	29,066
Total assets	**960,927**	**1,145,730**	**560,040**	**1,169,442**	**3,836,139**
Liabilities and equity					
Deposits from financial institutions	140,158	257,933	3,044	44,112	445,247
Deposits from customers	333,800	294,422	972,808	35,880	1,636,910
Borrowing	161,997	604,491	14,291	278,976	1,059,755
Financial liabilities designated at fair value	1,025	48,273	0	32,724	82,022
Subordinated loans	6,609	98,231	0	40,664	145,503
Trading liabilities	11,242	47,498	17,455	55,515	131,710
Derivatives held for hedging	0	6,130	0	359	6,489
Tax liabilities	9,188	218	537	0	9,943
Unsettled securities trading	1,466	66,271	9,347	7,509	84,593
Other liabilities	12,101	9,987	12,661	771	35,520
Total equity	198,447	0	0	0	198,447
Total liabilities and equity	**876,033**	**1,433,454**	**1,030,143**	**496,510**	**3,836,139**
Net on-balance sheet position	84,894	(287,723)	(470,103)	672,932	
Net off-balance sheet position	(213,711)	360,692	486,493	(633,475)	
Net position 31 March 2008	**(128,817)**	**72,969**	**16,390**	**39,457**	
Net positon 31 December 2007	**(114,199)**	**62,690**	**15,168**	**36,341**	

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4.4 Mismatch of assets and liabilities

(a) Interest rate risk on portfolios

Portfolio interest rate risk arises from the impact on the interest margin and/or the market value of equity caused by interest rate changes on assets and liabilities outside of the Group's trading book. This risk results primarily from duration mismatch of assets and liabilities. Portfolio interest rate risk is among the Group's more important risk factors.

The following table gives a summary of the Group's interest rate risk. It shows the carrying amounts of its assets and liabilities. The carrying amount classification is based on either the repricing date of the contract or its maturity, whichever comes first.

At 31 March 2008	Up to 3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
Assets						
Cash and cash balances with Central Bank	103,522	0	0	0	0	103,522
Loans and advances to financial institutions	266,453	1,765	67	0	0	268,285
Loans and advances to customers	1,670,156	437,622	181,974	198,414	0	2,488,165
Bonds	238,821	23,573	39,528	49,513	0	351,436
Equities	0	0	0	0	91,062	91,062
Hedged securities	15,521	1,278	10,500	25,105	107,643	160,047
Derivatives held for trading	165,575	0	0	0	0	165,575
Derivatives held for hedging	15,943	0	0	0	0	15,943
Investments in associates	0	0	0	0	4,886	4,886
Property and equipment	0	0	0	0	12,180	12,180
Intangible assets	0	0	0	0	38,363	38,363
Deferred tax asset	0	0	0	0	810	810
Non-current assets and disposal groups classified as held for sale	0	0	0	0	4,968	4,968
Unsettled securities trading	0	0	0	0	101,830	101,830
Other assets	0	0	0	0	29,066	29,066
Total assets	**2,475,991**	**464,238**	**232,069**	**273,032**	**390,808**	**3,836,139**
Liabilities and equity						
Deposits from financial institutions	415,557	27,306	2,056	328	0	445,247
Deposits from customers	1,272,463	253,481	90,366	20,599	0	1,636,910
Borrowing	591,146	133,815	234,639	100,155	0	1,059,755
Financial liabilities designated at fair value	6,912	15,850	14,821	1,734	42,704	82,022
Subordinated loans	38,087	2,861	1,217	103,338	0	145,503
Trading liabilities	131,710	0	0	0	0	131,710
Derivatives held for hedging	6,489	0	0	0	0	6,489
Tax liabilities	0	0	0	0	9,943	9,943
Unsettled securities trading	0	0	0	0	84,593	84,593
Other liabilities	0	0	0	0	35,520	35,520
Total equity	0	0	0	0	198,447	198,447
Total liabilities and equity	**2,462,364**	**433,314**	**343,099**	**226,154**	**371,207**	**3,836,139**
Net on-balance sheet position	13,626	30,924	(111,030)	46,878	19,601	
Net off-balance sheet position	(389,043)	100,650	211,490	131,366	(54,463)	
Total interest sensitivity gap 31 March 2008	**(375,417)**	**131,575**	**100,460**	**178,244**	**(34,862)**	
Total interest sensitivity gap 31 December 2007	**(253,265)**	**249,489**	**(8,767)**	**101,077**	**(88,534)**	

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(b) Liquidity Risk

Liquidity risk is the risk of being unable to obtain the funds to meet its financial obligations as they come due, either by increasing liabilities or by converting assets without incurring significant losses. This in turn requires reliable access to enough cash resources, at unpredictable times and due to unforeseeable events, to meet uncertain cash flow obligations. Such access – and indeed the cash flow obligations themselves – depends on market conditions and other external events and on other agents' behaviour.

ALCO formulates liquidity management policy, monitors the Group's liquidity position and provides advice on the composition of its assets and liabilities. The overriding objective is to minimise fluctuations in liquidity and ensure that the Group always has sufficient access to funding to cover outflows arising from its obligations in the coming month. Treasury is responsible for implementing this policy and estimates future cash flow in co-operation with Risk Management.

The Group policy is to maintain a liquid position (net of haircuts) such that it can sustain at least 12 months non-access to capital markets with a modest reduction in business activity. The Group's approach to liquidity management closely aligns with the framework of Moody's Bank Financial Strength Rating (BFSR).

The Bank follows rules on liquidity set by the Central Bank of Iceland, governing the ratio of weighted liquid assets and liabilities. The rules require a ratio higher than 1 for the next three months. The Central Bank rules involve a type of stress test, according to which assets and liabilities are weighted using specific co-efficient reflecting how accessible the asset in question would be in a liquidity crisis and how great the need is to repay the liability in question when due.

The Group comfortably fulfils its requirements set in its liquidity policy and as well at the end of the reporting period, the Group liquidity ratio, calculated by balancing assets and liabilities in accordance with the Central Bank's Rules No. 317/2006 was 1.7

The following table shows the cash flow payable by the Group under non-derivative financial assets and liabilities classified by remaining contractual maturities at the balance sheet date. Except for Bonds, Hedged securities, and Equities. They are classified by expected maturities. The amounts disclosed in the table are the contractual undiscounted cash flows.

At 31 March 2008	Up to 3 months	3-12 months	1-5 years	Over 5 years	Total
Assets					
Cash and cash balances with Central Bank	103,522	0	0	0	103,522
Loans and advances to financial institutions	262,824	4,543	2,479	0	269,845
Loans and advances to customers	553,731	423,677	1,213,977	734,858	2,926,243
Bonds	353,030	0	0	0	353,030
Equities	91,062	0	0	0	91,062
Hedged securities	160,047	0	0	0	160,047
Unsettled securities trading	101,830	0	0	0	101,830
Total assets 31 March 2008	**1,626,047**	**428,219**	**1,216,456**	**734,858**	**4,005,580**
Total assets 31 December 2007	**1,321,104**	**337,526**	**945,953**	**706,549**	**3,311,132**
Liabilities					
Deposits from financial institutions	413,904	33,374	2,695	470	450,443
Deposits from customers	1,319,563	243,750	65,707	33,027	1,662,047
Borrowings	185,146	135,721	726,450	175,748	1,223,065
Financial liabilities designated at fair value	145	8,959	25,623	48,220	82,947
Subordinated loans	2,450	8,513	35,909	272,363	319,236
Trading liabilities	14,109	0	0	0	14,109
Unsettled securities trading	84,593	0	0	0	84,593
Total liabilities 31 March 2008	**2,019,910**	**430,317**	**856,384**	**529,828**	**3,836,439**
Total liabilities 31 December 2007	**1,644,157**	**261,887**	**730,413**	**425,452**	**3,061,909**

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4.5 Derivative cash flow

4.5.1 Derivatives settled on a net basis

The Group's derivatives that will be settled on a net basis include:
Commodity derivatives: Commodity option
Credit derivatives: Total return swap
Equity derivatives: Equity forwards
Foreign exchange derivatives: OTC currency options bought and sold
Interest rate derivatives: Interest rate swaps

The table below analyses the Group's derivative financial instruments that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

At 31 March 2008	Up to 3 months	3-12 months	1-5 years	Over 5 years	Total
Assets					
Derivatives held for trading					
Equity derivatives	18,671	53	0	0	18,724
Foreign exchange derivatives	16	0	0	0	16
Interest rate derivatives	1,622	4,333	6,772	1,189	13,915
Derivatives held for hedging					
Interest rate derivatives	442	4,741	10,885	1,586	17,654
Total assets 31 March 2008	**20,751**	**9,127**	**17,657**	**2,775**	**50,310**
Total assets 31 December 2007	**44,332**	**24,374**	**49,001**	**14,219**	**131,926**
Liabilities					
Derivatives held for trading					
Commodity derivatives	12	0	0	0	12
Credit derivatives	398	1,149	4,071	0	5,618
Equity derivatives	2,216	198	0	0	2,414
Foreign exchange derivatives	229	0	0	0	229
Interest rate derivatives	5,301	5,924	8,552	15,542	35,318
Derivatives held for hedging					
Interest rate derivatives	753	295	(4)	7,864	8,908
Total liabilities 31 March 2008	**8,909**	**7,566**	**12,619**	**23,406**	**52,500**
Total liabilities 31 December 2007	**29,053**	**19,182**	**45,905**	**42,201**	**136,341**

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4.5.2 Derivatives settled on a gross basis

The Group's derivatives that will be settled on a gross basis include:
Equity derivatives: Listed and OTC stock options bought and sold
Foreign exchange derivatives: Currency forwards, cross-currency interest rate swaps

The table below analyses the Group's derivative financial instruments that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

At 31 March 2008	Up to 3 months	3-12 months	1-5 years	Over 5 years	Total
Assets					
Derivatives held for trading					
Equity derivatives	23,181	3,163	0	0	26,344
Foreign exchange derivatives	1,785,874	292,335	284,489	5,801	2,368,500
Total assets 31 March 2008	**1,809,054**	**295,498**	**284,489**	**5,801**	**2,394,843**
Total assets 31 December 2007	**1,061,630**	**140,851**	**252,444**	**5,837**	**1,460,762**
Liabilities					
Derivatives held for trading					
Equity derivatives	23,181	3,163	0	0	26,344
Foreign exchange derivatives	1,774,087	267,399	278,470	4,993	2,324,949
Total liabilities 31 March 2008	**1,797,268**	**270,562**	**278,470**	**4,993**	**2,351,293**
Total liabilities 31 December 2007	**1,077,795**	**146,550**	**264,733**	**6,774**	**1,495,853**

4.6 Capital risk management

The Group manages its capital resources to meet the regulatory capital requirements prescribed by the Icelandic Financial Supervisory Authority (FME). FME requires the Group to hold sufficient capital resources to meet minimum the regulatory capital requirements laid down in the Rules on the Capital Requirement and Risk-Weighted Assets of Financial Undertakings, No. 215/2007. These rules are based on the standards of the Basel Committee on Banking Supervision in the Basel II accord. Minimum requirements are expressed as the ratio of capital resources to risk-weighted assets. Risk-weighted assets are determined by applying specific risk weight to the Group's assets following calculations developed by the Basel Committee. The Group's strategy is to maintain its CAD ratio above 10.5%, which is considerably higher that the minimum statutory requirement of 8%.

In 2008, the Group continued to manage its capital resources. At 31 March 2008, the capital ratio was 11.0%.

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4.7 Fair value of financial assets and financial liabilities

The following table provides a summary of the carrying amount and fair value of financial assets and financial liabilities not carried at fair value. The fair value has been estimated by discounting the cash flow of financial assets and financial liabilities based on market interest rates for assets and liabilities of the same or similar duration.

At 31 March 2008	Carrying value	Fair value	Difference
Financial assets			
Loans and advances to customers	2,488,165	2,469,901	(18,264)
Financial liabilities			
Borrowings	1,059,755	1,047,371	12,384
Subordinated loans	145,503	144,787	716
Net difference			**(5,164)**

4.8 Inflation-indexed assets and liabilities

The Group's balance sheet has a positive balance between indexed and non-indexed assets. At period-end, indexed assets exceeded indexed liabilities by ISK 140 billion. These amounts only apply to assets and liabilities in ISK.

	31.3.2008	31.12.2007
Assets	371,200	375,174
Liabilities	(231,574)	(226,310)
	139,625	**148,864**

4.9 Core earnings

Calculation of core earnings is intended to illustrate the underlying profit of the Group. To obtain this figure, net gain/loss from equity holdings of any kind, as well as gain from securities and FX trading, are deducted from net interest income and fee and commission income. Net interest income is consequently increased to reflect the Group's cost of funding bond and equity positions and from 1st of January 2008 net interest income is as well increased for the disadvantage resulting from the Group's positive FX position which is funded in ISK. The LIBOR three-month flat rate is used for each underlying currency to calculate the adjustment increase in net interest income. In spite of the Group's definition of its core earnings, its performance also depends on equity and bond positions taken on own account.

The following table gives a comparison between the Group's income and Core income for the years 2005-2007 and the first quarter in 2008:

Actual income	Q1 2008	2007	2006	2005
Net interest income	15,255	54,052	41,491	22,996
Net commissions and fees	10,904	39,369	28,366	16,726
Other operating income	14,679	16,605	19,568	21,257
Net operating income	**40,837**	**110,025**	**89,426**	**60,978**
Operating expenses	17,233	57,515	38,588	20,967
Impairment on loans and advances and assets held for sale	3,915	6,956	6,144	6,197
Impairment on goodwill	0	0	0	3,033
Pre-tax profit	**19,690**	**45,555**	**44,694**	**30,781**
Cost-income Ratio	42%	52%	43%	34%
Pre-tax ROE	50%	31%	40%	56%
Adjustments				
Net interest income	4,401	5,753	3,640	3,652
Other operating income	(14,679)	(16,605)	(19,568)	(21,257)
Impairment on goodwill	0	0	0	3,033
	(10,278)	**(10,852)**	**(15,929)**	**(14,572)**
Core earnings				
Net interest income	19,656	59,804	45,131	26,647
Net commissions and fees	10,904	39,369	28,366	16,726
Net operating income	**30,560**	**99,173**	**73,497**	**43,373**
Operating expenses	17,233	57,515	38,588	20,967
Impairment on loans and advances and assets held for sale	3,915	6,956	6,144	6,197
Pre-tax profit	**9,412**	**34,703**	**28,765**	**16,210**
Cost-income ratio for core operations	56%	58%	53%	48%
Pre-tax ROE for core operations	22%	24%	26%	30%

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5. Income statement by quarters

Operations	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Interest income	70,487	57,935	54,036	49,078	41,046
Interest expenses	55,232	42,708	39,591	35,578	30,167
Net interest income	**15,255**	**15,227**	**14,445**	**13,500**	**10,879**
Fee and commission income	13,444	11,534	11,813	11,013	10,886
Fee and commission expenses	2,541	1,874	1,595	1,285	1,124
Net fee and commission income	**10,904**	**9,660**	**10,218**	**9,729**	**9,762**
Net financial income	14,757	(748)	3,029	4,754	4,518
Profit (losses) from associates	(80)	671	(1,171)	1,191	(58)
Net gains of disposal groups held for sale, net of tax	2	9	60	9	4,339
Other operating income	**14,679**	**(68)**	**1,918**	**5,955**	**8,799**
Net operating income	**40,837**	**24,819**	**26,582**	**29,184**	**29,441**
Salaries and related expenses	10,633	10,769	10,029	8,919	7,972
Administrative expenses	6,601	5,846	4,806	4,731	4,444
Operating expenses	**17,233**	**16,615**	**14,835**	**13,650**	**12,415**
Impairment on loans and advances during the period	3,915	2,286	1,620	1,501	1,549
Pre-tax profit	**19,690**	**5,919**	**10,127**	**14,033**	**15,476**
Income tax	2,265	997	1,402	1,490	1,716
Net profit	**17,425**	**4,922**	**8,725**	**12,542**	**13,760**
Attributable to:					
Shareholders of Landsbanki Islands hf.	17,307	4,584	8,518	12,248	13,450
Minority interest	118	337	207	294	311

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6. Business segments

The Group operates in four business segments:

- Retail banking
- Corporate banking
- Investment banking
- Asset management and private banking

Retail banking includes the services provided through the branch network in Iceland to individuals and small and medium-size businesses, leasing services provided by the subsidiary SP fjármögnun hf. (Iceland), and mortgage lending services provided by Heritable Bank Ltd (UK).

Corporate banking includes the services provided to large and medium-sized corporate clients through the corporate division of Landsbanki in Reykjavik and the division's network of international branches. Services provided by Heritable Bank Ltd (UK) and Landsbanki Luxembourg SA (Lux) to medium-sized businesses is also included under corporate banking.

Investment banking includes capital markets services, treasury, proprietary trading, and corporate advisory services that are provided through the investment banking division and international branches and Landsbanki Securities (UK) Ltd, Landsbanki Kepler SA (France) and Merrion Capital Group Ltd (Ireland).

Assets management and private banking includes fund and wealth management services provided by divisions of Landsbanki in Reykjavik and Landsbanki Luxembourg SA (Lux), and by the subsidiary Landsvaki hf. (Iceland).

Q1 2008	Retail banking	Corporate banking	Investment banking	Asset management private banking	Unallocated	Group
Net interest revenues	5,040	12,604	(3,831)	1,441	0	15,255
Net fee and commission income	759	1,874	6,876	1,396	0	10,904
Other operating income	(35)	(2,529)	17,119	123	0	14,679
Net operating income	**5,764**	**11,949**	**20,164**	**2,960**	**0**	**40,837**
Operating expenses	2,585	3,008	8,860	1,598	1,182	17,233
Impairment on loans and advances	765	1,879	1,271	0	0	3,915
Pre-tax profit	**2,414**	**7,062**	**10,034**	**1,362**	**(1,182)**	**19,690**
Total assets 31 March 2008	**621,242**	**1,637,211**	**880,720**	**665,620**	**31,345**	**3,836,139**
Total liabilities 31 March 2008	**603,606**	**1,557,734**	**816,273**	**649,851**	**10,228**	**3,637,692**
Total equity 31 March 2008	**17,636**	**79,477**	**64,448**	**15,769**	**21,117**	**198,447**

Q1 2007	Retail banking	Corporate banking	Investment banking	Asset management private banking	Unallocated	Group
Net interest revenues	3,928	7,618	(1,401)	734	0	10,879
Net fee and commission income	595	551	7,800	816	0	9,762
Other operating income	(23)	18	8,777	28	0	8,799
Net operating income	**4,500**	**8,187**	**15,176**	**1,578**	**0**	**29,441**
Operating expenses	2,307	2,397	5,834	1,009	868	12,415
Impairment on loans and advances	502	987	63	(2)	0	1,549
Pre-tax profit	**1,692**	**4,803**	**9,278**	**571**	**(868)**	**15,476**
Total assets 31 December 2007	**523,287**	**1,333,768**	**741,701**	**429,474**	**29,317**	**3,057,546**
Total liabilities 31 December 2007	**502,735**	**1,258,081**	**688,814**	**414,988**	**8,924**	**2,873,542**
Total equity 31 December 2007	**20,552**	**75,687**	**52,887**	**14,485**	**20,392**	**184,004**

Equity is allocated to each business segment at the beginning of each year according to its share of the Group's risk-weighted average (RWA).

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7. Geographical segments - breakdown of income

Q1 2008	Iceland	UK & Ireland	Luxembourg	Other*	Total
Net interest income	6,825	5,916	1,450	1,064	15,255
Net fee and commission income	4,242	3,208	621	2,833	10,904
	11,068	**9,124**	**2,071**	**3,896**	**26,159**
	42%	**35%**	**8%**	**15%**	**100%**
Other operating income	22,396	(7,862)	166	(21)	14,679
Net operating income	**33,463**	**1,262**	**2,237**	**3,875**	**40,837**
	82%	**3%**	**5%**	**9%**	**100%**
Total assets 31 March 2008	**1,877,017**	**735,288**	**422,697**	**801,136**	**3,836,139**

Q1 2007	Iceland	UK & Ireland	Luxembourg	Other*	Total
Net interest income	6,320	2,559	996	1,004	10,879
Net fee and commission income	3,629	3,085	381	2,667	9,762
	9,950	**5,644**	**1,377**	**3,671**	**20,641**
	48%	**27%**	**7%**	**18%**	**100%**
Other operating income	7,219	619	39	923	8,799
Net operating income	**17,169**	**6,262**	**1,416**	**4,594**	**29,441**
	58%	**21%**	**5%**	**16%**	**100%**
Total assets 31 December 2007	**1,604,684**	**558,262**	**314,826**	**579,774**	**3,057,546**

*** Other=Continental Europe, Scandinavia, Canada, USA, and other.**

8. Net interest income

Interest income	Q1 2008	Q1 2007
Interest on deposits and loans to financial institutions	2,581	2,044
Interest on loans and advances to customers	53,886	31,496
Interest on other financial assets	7,643	2,053
Other interest income	6,377	5,452
	70,487	**41,046**

Interest expenses	Q1 2008	Q1 2007
Interest on deposits from financial institutions	4,430	1,682
Interest on deposits from customers	27,983	13,297
Interest on borrowings	13,726	9,931
Interest on subordinated loans	2,439	1,109
Other interest expenses	6,654	4,148
	55,232	**30,167**
Net interest income	**15,255**	**10,879**
Interest spread is calculated as the ratio of net interest income to average balance sheet position	**1.8%**	**1.9%**

9. Dividend income

	Q1 2008	Q1 2007
Trading	119	311
Financial assets designated at fair value through profit and loss	0	74
	119	**385**

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10. Net financial income

	Equity	Bonds	FX	Derivatives and other	Total Q1 2008	Total Q1 2007
Dividend income	119	0	0	0	119	385
Net gains (losses) on financial assets and financial liabilities held for trading	(1,007)	(4,196)	0	(3,935)	(9,137)	3,098
Net gains (losses) on financial assets designated at fair value through profit and loss	(1,034)	0	0	0	(1,034)	436
Fair value adjustments in hedge accounting	0	0	0	34	34	(7)
Foreign exchange difference	0	0	24,776	0	24,776	607
	(1,922)	**(4,196)**	**24,776**	**(3,901)**	**14,757**	**4,518**

11. Salaries and related expenses

	Q1 2008	Q1 2007
Salaries	8,703	6,377
Pension fund contributions	1,000	759
Other personnel expenses	930	836
	10,633	**7,972**

12. Impairment provisions on loans and advances and assets held for sale

	Q1 2008	Q1 2007
Loans and advances	3,868	1,602
Non-current assets held for sale	54	(21)
	3,922	**1,581**
Collected previously written-off loans	(7)	(32)
	3,915	**1,549**

13. Income tax

	Q1 2008	Q1 2007
Current income tax	1,471	1,268
Deferred income tax	794	448
	2,265	**1,716**

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the basic tax rate of the Bank as follows:

Profit before tax	19,690	15,476
Tax calculated at a local tax rate of 18%	3,544	2,786
Effect of different tax rates in other countries	214	43
Income not subject to tax	(2,305)	(161)
Other	812	(952)
Income tax	**2,265**	**1,716**

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14. Earnings per share

Basic

Basic earnings per share is calculated by dividing the net profit attributable to equity holders of the Bank by the weighted average number of ordinary shares in issue during the year, excluding the average number of ordinary shares purchased by the Bank and held as treasury shares.

	Q1 2008	Q1 2007
Profit attributable to equity holders of the Bank	17,307	13,450
Weighted average number of ordinary shares in issue	10,770	10,631
Basic earnings per share (ISK per share)	**1.61**	**1.27**

Diluted

Diluted earnings per share are calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. For the share options, a calculation is carried out to determine the number of shares that could have been acquired at fair value (determined as the average annual market share price of the Group's shares) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the share options.

	Q1 2008	Q1 2007
Profit attributable to equity holders in the Bank	17,307	13,450
Weighted average number of ordinary shares in issue	10,770	10,631
Adjustments for:		
– share options	1,142	662
Weighted average number of ordinary shares in issue and diluted potential ordinary shares	**11,912**	**11,293**
Diluted earnings per share (ISK per share)	**1.45**	**1.19**

15. Loans and advances to customers

	31.3.2008	31.12.2007
Public entities	27,829	23,759
Corporates		
Fisheries	220,263	173,489
Retail trade	288,731	245,200
Agriculture	11,836	12,467
Manufacturing and construction	404,310	327,423
Services	1,110,090	879,252
Other	7,575	3,721
Individuals	445,041	379,409
Provisions for credit losses on loans and advances	(27,510)	(21,981)
Total loans and advances to customers	**2,488,165**	**2,022,738**

Provisions for credit losses on loans and advances

Changes during the period	31.3.2008	31.12.2007
Balance at beginning of year	21,981	16,611
Impairment on loans and advances	3,868	7,645
Loans written off	(698)	(1,525)
Translation difference	2,360	(750)
Balance at period-end	**27,510**	**21,981**
Provision ratio (Provisions for credit losses/total loans and advances to customers and guarantees issued)	1.04%	1.02%

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16. Bonds, equities and hedged securities

Bonds	31.3.2008 Trading assets	Fin. assets designated at fair value	Total	31.12.2007 Trading assets	Fin. assets designated at fair value	Total
Domestic						
Listed	55,640	0	55,640	43,163	0	43,163
Unlisted	0	0	0	0	0	0
	55,640	**0**	**55,640**	**43,163**	**0**	**43,163**
Foreign						
Listed	291,345	1,286	292,631	316,400	973	317,373
Unlisted	426	2,739	3,165	1,694	387	2,081
	291,771	**4,025**	**295,796**	**318,093**	**1,361**	**319,454**
Total bonds	**347,411**	**4,025**	**351,436**	**361,256**	**1,361**	**362,617**
Equities						
Domestic			**Total**			**Total**
Listed	11,360	7,146	18,506	5,651	7,880	13,532
Unlisted	5,512	2,369	7,882	4,309	1,816	6,125
	16,872	**9,516**	**26,388**	**9,960**	**9,696**	**19,656**
Foreign						
Listed	22,066	12,303	34,369	18,702	10,198	28,900
Unlisted	4,398	25,907	30,305	2,400	13,450	15,850
	26,465	**38,210**	**64,675**	**21,101**	**23,649**	**44,750**
Total equities	**43,337**	**47,726**	**91,062**	**31,061**	**33,345**	**64,407**
Hedged securities			**Total**			**Total**
Bonds	49,511	2,893	52,404	50,690	2,546	53,236
Equities	65,305	42,337	107,643	89,147	33,797	122,944
Total hedged securities	**114,817**	**45,230**	**160,047**	**139,837**	**36,344**	**176,181**
Derivatives held for trading	**165,575**	**0**	**165,575**	**50,198**	**0**	**50,198**
Total	**671,139**	**96,981**	**768,120**	**582,353**	**71,049**	**653,402**

17. Derivatives held for trading and trading liabilities

	31.3.2008			31.12.2007		
	Contract/notional	Fair value		Contract/notional	Fair value	
Foreign exchange derivatives	**amount**	**Assets**	**Liabilities**	**amount**	**Assets**	**Liabilities**
Currency forwards	1,725,724	60,564	53,124	1,351,036	8,650	19,852
OTC currency options bought and sold	142,769	16,283	10,632	95,087	3,508	2,956
Cross-currency interest rate swaps	355,727	46,302	21,277	343,192	10,204	11,656
	2,224,220	**123,149**	**85,033**	**1,789,315**	**22,362**	**34,463**
Interest rate derivatives						
Interest rate swaps	2,054,015	19,572	24,525	1,490,765	11,622	13,437
	2,054,015	**19,572**	**24,525**	**1,490,765**	**11,622**	**13,437**
Equity derivatives						
Equity forwards	56,499	18,678	1,085	83,134	12,107	3,384
Listed and OTC stock options bought and sold	38,465	4,104	1,961	9,757	3,996	2,845
Equity futures	376	0	1	0	0	0
	95,340	**22,782**	**3,047**	**92,891**	**16,103**	**6,229**
Credit derivatives						
Total return swaps	88,953	0	4,997	89,099	0	2,435
	88,953	**0**	**4,997**	**89,099**	**0**	**2,435**
Commodity derivatives						
Listed and OTC commodity options bought and sold	106	12	0	695	110	0
	106	**12**	**0**	**695**	**110**	**0**
Other trading liabilities	**15,818**	**61**	**14,109**	**5,598**	**0**	**5,598**
Total derivatives held for trading and trading liabilities	**4,478,451**	**165,575**	**131,710**	**3,468,364**	**50,198**	**62,161**

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18. Derivatives held for hedging

	31.3.2008			31.12.2007		
	Contract/notional	Fair value		Contract/notional	Fair value	
	amount	Assets	Liabilities	amount	Assets	Liabilities
Derivatives designated as fair value hedges						
Interest rate swaps	424,819	15,943	6,489	393,705	8,719	6,953
	424,819	**15,943**	**6,489**	**393,705**	**8,719**	**6,953**

19. Investment in associates

Company	Total assets	Total liabilities	Ownership %	Profit (loss) from associates	Book value 31.3.2008	Book value 31.12.2007
Eignarhaldsfélagið Portus hf.	8,030	6,099	50.0	0	1,045	1,045
Eignarhaldsfélagið ehf.	1,421	1	49.0	(135)	1,037	1,171
Valitor hf.	29,853	27,844	38.0	30	757	728
Rockview Merrion Investments Ltd.	1,126	11	50.0	13	557	416
Reiknistofa bankanna	1,518	222	33.9	0	515	515
Kredikort hf.	3,600	2,655	20.0	4	189	184
Borgun hf.	11,385	10,783	20.0	7	120	114
Intrum hf.	566	392	33.0	0	174	173
Líftryggingamiðstöðin hf.	547	233	34.0	0	142	142
HydroKraft Invest hf.	202	13	50.0	0	100	100
Other partially owned companies					249	1,231
				(80)	**4,886**	**5,820**

All these investments are in unlisted companies.

20. Intangible assets

Goodwill	31.3.2008	31.12.2007
Opening net book amount	23,062	12,077
Translation differences	6,265	1,014
Acquisition of Bridgewell Group plc	0	6,804
Acquisition of additional 17% share in Merrion Capital Group Ltd.	2,992	0
Other addition during period	511	4,482
Disposals	0	(1,315)
Net book amount at period-end	**32,831**	**23,062**

Software and other intangible assets		
Opening net book amount	4,617	2,273
Translation differences	450	0
Additions indentified in the acquisition of Bridgewell Group plc	0	1,170
Other additions during period	758	2,208
Disposals	(46)	0
Amortisation	(246)	(1,034)
Net book amount at period-end	**5,532**	**4,617**
Total intangible assets	**38,363**	**27,679**

All goodwill is tested annually for impairment. The goodwill has been divided among the smallest cash generating units based on the required rate of return from each unit. An assessment of a recoverable value of a goodwill is based on its use value.

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21. Non-current assets and disposal groups classified as held for sale

	31.3.2008	31.12.2007
Repossessed collaterals	1,270	827
Allowance for repossessed collaterals	(305)	(252)
	965	**576**
Disposal group held for sale		
– Investment properties included in disposal groups	3,578	2,942
– Other assets included in disposal groups	426	123
	4,003	**3,066**
Total non-current assets and disposal groups classified as held for sale	**4,968**	**3,641**

22. Deposits from financial institutions

	31.3.2008	31.12.2007
Loans from Central Bank and repurchase agreements	232,312	202,178
Loans from other credit institutions	212,935	135,737
	445,247	**337,915**

23. Deposits from customers

	31.3.2008	31.12.2007
Demand deposits	882,501	777,179
Time deposits	754,409	644,231
	1,636,910	**1,421,410**

24. Borrowings

	31.3.2008	31.12.2007
Securities issued	764,379	620,610
Syndicated loans and other borrowings	295,377	154,144
	1,059,755	**774,754**

Securities issued:		
Europe - MTN	457,860	361,652
USA - MTN	177,243	143,371
European Commercial Paper (ECP)	14,930	11,542
Other	114,346	104,045
	764,379	**620,610**

The Group has not had any defaults of principal, interest, or other breaches with respect to their liabilities during the period (2007: nil).

25. Financial liabilities designated at fair value

	31.3.2008	31.12.2007
Liabilities to customers under unit-linked investment contracts	42,704	33,706
Financial liabilities with matched interest rate swaps	30,148	22,219
Financial liabilities with embedded derivatives	9,169	5,306
	82,022	**61,231**

The Group is engaged in a unit-linked investment contracts. The value of those contracts reflects the fair value of the assets that are held within unitised investment pools.
These contracts are payable on demand and therefore have no maturity. The contractual amount that must be paid on demand is the fair value of the liability.

Certain long-term debt securities issued have been matched with interest rate swaps as part of a documented interest rate risk management strategy. An accounting mismatch would arise if the debt securities in issue were accounted for at amortised cost, because the related derivatives are measured at fair value with movements in the fair value taken through the income statement. By designating the long-term debt at fair value, the movement in the fair value of the long-term debt will be accounted for in the income statement.

Certain long-term debt securities issued by the Group are linked to equity price indices. In such cases, the Group has opted to designate the entire contract at fair value through profit and loss rather than recognise them separately as derivatives held at fair value and loans at amortised cost.

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26. Subordinated loans

	31.3.2008	31.12.2007
Tier I – Non-innovative hybrid capital	52,501	38,741
Tier I – Innovative hybrid capital	55,920	44,225
Tier II	37,082	28,925
	145,503	**111,890**

Subordinated loans	**Classification**	**Currency**	**Rate**	**Maturity**		
London Stock Exchange	Tier I	EUR	6.25%	callable	41,106	30,560
Unlisted	Tier I	USD	7.43%	callable	34,633	26,437
Luxembourg Stock Exchange	Tier I	EUR	4.65%	callable	17,539	14,077
London Stock Exchange	Tier I	EUR	Euribor+1,23%	callable	11,395	8,181
OMX Nordic Exchange	Tier I	ISK	6,5%+CPI	callable	1,279	1,280
OMX Nordic Exchange	Tier I	ISK	5,8%+CPI	callable	1,252	1,251
OMX Nordic Exchange	Tier I	ISK	8,65%+CPI	callable	1,217	1,180
					108,421	**82,965**
Luxembourg Stock Exchange	Tier II	EUR	Euribor+0,35%	2015	23,934	18,348
Luxembourg Stock Exchange	Tier II	JPY	3.45%	2033	3,757	2,685
Luxembourg Stock Exchange	Tier II	EUR	7.20%	2026	1,339	1,009
Luxembourg Stock Exchange	Tier II	EUR	5.44%	2018	1,268	914
Luxembourg Stock Exchange	Tier II	EUR	4.40%	2035	1,165	850
Luxembourg Stock Exchange	Tier II	EUR	Euribor+0,8%	2013	485	372
Unlisted	Tier II	USD	Libor+1,85%	2011	2,273	1,889
Unlisted	Tier II	ISK	5,6%+CPI	callable	1,905	1,902
Unlisted	Tier II	ISK	6,09%+CPI	callable	956	956
					37,082	**28,925**
Total subordinated loans					**145,503**	**111,890**

Subordinated loans are considered as part of capital according to regulation on the calculation of Capital adequacy ratio (see Note 28). Subordinated loans are fully applied in calculating the overall capital adequacy ratio. However, according to CAD rules, subordinated loans can comprise a maximum of 33% of Tier I capital. Consequently, ISK 26,849 million of Tier I classified subordinated loans are applied to Tier II capital.

27. Tax liabilities

	31.3.2008	31.12.2007
Tax to be paid	5,101	5,255
Deferred tax liabilities	4,842	2,894
	9,943	**8,149**

28. Capital ratio

	31.3.2008	31.12.2007
Risk-weighted assets	2,823,500	2,317,362
Capital:		
Tier I capital:		
Equity	194,990	180,008
Subordinated loans	81,572	73,780
Goodwill	(32,831)	(24,190)
Minority interests	3,457	3,996
	247,188	**233,594**
Tier II capital:		
Subordinated loans	63,932	38,111
– deduction in accordance with Articles 28 and 85 of Act No 161/2002	(1,066)	(1,025)
Total capital	**310,053**	**270,679**
Tier I ratio	**8.8%**	**10.1%**
Capital ratio	**11.0%**	**11.7%**

The Group's capital adequacy ratio as of 31 March 2008 is calculated in accordance with EU Directive 2006/48/EC, cf. Article 78 (Basel II), which has been incorporated into Icelandic legislation.

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29. Contingent liabilities and commitments

Off-balance sheet contingent liabilities are specified as follows:	**31.3.2008**	**31.12.2007**
Guarantees issued	136,330	112,602
Available overdrafts	30,637	61,721
Unused credit commitments	78,821	70,036

30. Fiduciary activities

The Group provides asset custody, asset management, investment management, and advisory services. All of these require the Group to make decisions on the treatment, acquisition, or disposal of financial instruments. Assets in Landsbanki's custody are not reported in its accounts. Part of these services involves the Group approving objectives and criteria for the investment of assets in its custody. As of 31 March 2008, financial assets managed by the Group amounted to ISK 544.5 billion (2007: 513.2 bn). Amounts in custody accounts amounted to ISK 2,394 billion (2007: 2,109 bn).

31. Related-party transactions

Loans to CEOs and managing directors, and to companies owned by these persons, amounted to ISK 158 million as at 31 March 2008. Loans to members of the Board of Directors, and companies owned by them, amounted to ISK 42,405 million, including credit granted to companies with which members of the Board are connected through membership on the companies' Boards or ownership ties. The holding company, Samson eignarhaldsfélag ehf., has a 40.73% holding in the Group. The Group has not assisted the company with any provision of credit. One of the company's owners sits on Landsbanki's Board of Directors', and loans granted to this person are included in the above amounts. Total credit extended to associated companies by the Group amounted to ISK 11,266 million as at 31 March 2008. Total loans to related party amounted to ISK 53,829 million (ISK 62,789 million 31.12.2007).

All of the loans referred to here have been granted in accordance with the Group's credit rules and on normal commercial terms. No impairment has been recognised by the Group against these loans. Fees and interest received for services provided to related-parties amounted to ISK 1,377 million in Q1 2008.

32. Acquisitions

On February 2008 the Group acquired an additional 17% share in Merrion Capital Group Ltd. The consideration paid in cash was ISK 4,028 million. The amount in excess of the fair value of net assets, ISK 2,992 million, is recognised as goodwill, see note 20.

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