Condensed Consolidated Interim Financial Statements

Six months ended 30 June 2015

Íslandsbanki hf.
Kirkjusandur
155 Reykjavík
Iceland
Reg. no. 491008-0160

Contents

Endorsement and Statement by the Board of Directors and the CEO

The Condensed Consolidated Interim Financial Statements of Íslandsbanki hf. for the period 1 January to 30 June 2015 comprise the Condensed Interim Financial Statements of Íslandsbanki hf. and its subsidiaries, together referred to as "the Bank".

Ownership

The Bank has two shareholders, ISB Holding ehf., which holds 95% of the Bank's share capital and the Icelandic State Treasury which holds 5% through the Icelandic State Financial Investments (ISFI – Bankasýsla ríkisins). One board member is appointed by ISFI and the remaining six are appointed by ISB Holding ehf.

At the Annual General Meeting on 25 March 2015, John E. Mack who had served as Vice-Chairman of the Board since January 2010, resigned as a Board Member. The Bank has been fortunate to benefit from John E. Mack's vast banking experience worldwide during this period. John E. Mack was replaced by Eva Cederbalk, a Swedish national and a former managing director at SBAB Bank AB.

The reporting period

On 17 February 2015, the Bank's subsidiary Fastengi ehf. signed a sale agreement with Reginn hf. for the sale of 100% shareholding in Fjárvari ehf., Bréfabær ehf., and Sævarhöfdi ehf. The sale is in line with the Bank's commitment to divest assets received as a result of financial restructuring. The sale was completed on 31 May 2015.

The Bank has completed four transactions during the year 2015 under its USD 750 million Global Medium Term Note (GMTN) Programme. In February 2015, the Bank issued an SEK 300 million (ISK 4.7 billion) 4-year note, in April 2015 the Bank issued additional SEK 150 million (ISK 2.4 billion) under the same facility and in July the Bank issued further SEK 150 million (ISK 2.4 billion). All three issuances were sold mainly to Scandinavian investors. In July 2015, the Bank issued a EUR 100 million (ISK 14.7 billion) 2.875% fixed rate note due in 2018. The note was placed with investors in Scandinavia and continental Europe. Investors were offered switch terms out of the Bank's existing EUR 100 million note due in May 2016, and the Bank bought back EUR 47.7 million of those notes.

In April 2015, the rating agency Fitch assigned the Bank with an investment grade rating of BBB-/F3 with a stable outlook. The Bank is the first Icelandic bank to be assigned an investment grade rating since 2008. Standard & Poor's Ratings Services followed suit and raised the long-term and short-term rating on the Bank to BBB-/A-3 with a stable outlook.

In May 2015, the Bank consolidated two of its branches in the west and central Reykjavík into a modernised banking centre at Grandi, focusing on providing in-depth services to individuals and SMEs.

In July 2015, Euromoney named Íslandsbanki Best Bank in Iceland and awarded it with the Awards for Excellence. This is the third year in a row that the Bank has been selected for this award. The magazine considered several factors in its assessment of the Icelandic banks, including earnings from regular operations, cost efficiency and the ability to adapt to changing market conditions and client needs. Euromoney awards are placed in nearly 100 countries.

Outlook

On 8 June 2015, the Icelandic Ministry of Finance and Economic Affairs announced its plans to liberate the capital controls which have been in place in Iceland since 2008. This will be done in stages, the first stage being a stability tax of 39% of total assets being imposed on financial undertakings, previously operated as commercial banks and savings banks and currently in winding-up proceedings, that have not entered into a composition agreement by year-end 2015.

In July 2015, following the announcement and based on the Government's proposal, the Bank entered into a Heads of Agreement with Glitnir hf. and its subsidiaries ISB Holding ehf. and GLB Holding ehf., regarding re-capitalisation of the Bank and a payment of ISK 3 billion dividend to the minority shareholder ISFI. The proposed re-capitalisation is expected to be finalised before year-end 2015, subject to approval by all relevant parites including the Icelandic Financial Supervisory Authority and the Central Bank of Iceland. The re-capitalisation is expected to result in a reduction in Bank equity corresponding to a total capital ratio of approximately 23%. The agreement also stipulates restrictions on the sale of the Bank's shares to domestic investors. Details of the proposed re-capitalisation are disclosed in Note 39.

The economic environment in Iceland continues to improve and the job market has stabilised after unrest in recent months. The Board of Directors considers the potential lifting of capital controls to be a positive step towards restoring normal market conditions in Iceland. The Bank is currently well positioned with strong capital ratios, solid funding and a considerable liquidity buffer and will remain so after the re-capitalisation. The Bank is therefore in a good position to meet any perturbations that may follow in the wake of the liberation of the capital controls.

Accounting convention

The Condensed Consolidated Interim Financial Statements for the six months ended 30 June 2015 are presented in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting, as adopted by the European Union, the Act on Annual Accounts no. 3/2006 and the Act on Financial Undertakings no. 161/2002.

Endorsement and Statement by the Board of Directors and the CEO

Profit from the Bank's operations for the period 1 January to 30 June 2015 amounted to ISK 10,790 million, which corresponds to an 11.7% annualised return on equity. Bank equity, according to the Condensed Consolidated Financial Position, amounted to ISK 187,009 million at 30 June 2015. The Bank's total capital ratio, calculated according to the Act on Financial Undertakings, was 28.3%.The Board of Directors refers to Note 57 for further understanding of the capital requirements of the Bank. The Bank's total assets amounted to ISK 976,257 million at the end of the period.

On 21 April 2015, the Bank paid dividends amounting to ISK 9,000 million, equivalent to 40% of net profit, for the operating year 2014 to its shareholders in accordance with a resolution passed at the Bank's Annual General Meeting on 25 March 2015.

The Board of Directors draws special attention to the risks relating to the political and legal environment in Iceland where capital controls are still in place. The Bank has made appropriate provisions to reflect the risks associated with court rulings. The Board also notes that the Bank maintains a strong capital base and is therefore well positioned to meet future risks and challenges. The Board refers to Notes 2 and 38 for the principal risks and uncertainties currently faced by the Bank.

To the best of our knowledge the Condensed Consolidated Interim Financial Statements provide a true and fair view of the Bank's operating profits and cash flows of the Bank for the period 1 January to 30 June 2015 and its financial position as at 30 June 2015.

The Board of Directors and the CEO of Íslandsbanki hf. hereby confirm the Bank's Condensed Consolidated Interim Financial Statements for the period 1 January to 30 June 2015 by means of their signatures.

Reykjavík, 24 August 2015

Board of Directors:

Fridrik Sophusson, Chairman
Marianne Økland, Vice-Chairman
Árni Tómasson
Eva Cederbalk
Helga Valfells
Neil Graeme Brown
Þóranna Jónsdóttir

Chief Executive Officer:

Birna Einarsdóttir

Report on Review of Condensed Consolidated Interim Financial Statements

To the Board of Directors and Shareholders of Íslandsbanki hf.

We have reviewed the accompanying Condensed Consolidated Statement of Financial Position of Íslandsbanki hf. and its subsidiaries as at 30 June 2015 and the related Condensed Consolidated Income Statement, the Condensed Consolidated Statement of Comprehensive Income, the Condensed Consolidated Statement of Changes of Equity and Condensed Consolidated Statement of Cash Flows for the six months ended June 2015 and explanatory notes. Management is responsible for the preparation and fair presentation of these Condensed Consolidated Interim Financial Statements in accordance with the International Financial Reporting Standard, IAS 34 Interim Financial Reporting as adopted by the EU. Our responsibility is to express a conclusion on these Condensed Consolidated Interim Financial Statements based on our review.

Scope of Review

We conducted our review in accordance with the International Standard on Review Engagements 2410, Review of Interim Financial Information Performed by the Independent Auditor of the Entity. A review of interim financial statements 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 Statements are not prepared, in all material respects, in accordance with the International Financial Reporting Standard, IAS 34 Interim Financial Reporting, as adopted by the EU.

Reykjavík, 24 August 2015

Ernst & Young ehf.

Margrét Pétursdóttir

State Authorised Public Accountant

Condensed Consolidated Income Statement for the six months ended 30 June 2015

	Notes	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Interest income		14,536	13,399	26,173	26,261
Interest expense		(7,177)	(6,477)	(12,623)	(12,693)
Net interest income	10	7,359	6,922	13,550	13,568
Fee and commission income		5,374	4,369	10,051	8,702
Fee and commission expense		(1,856)	(1,551)	(3,628)	(3,030)
Net fee and commission income	11	3,518	2,818	6,423	5,672
Net financial income	12-13	275	19	2,039	882
Net foreign exchange loss	14	(141)	(12)	(281)	(303)
Share of profit of associates net of income tax		-	27	63	27
Other operating income	15	252	240	478	1,353
Other net operating income		386	274	2,299	1,959
Total operating income		11,263	10,014	22,272	21,199
Salaries and related expenses	16	(3,421)	(3,441)	(6,881)	(6,881)
Other operating expenses	17	(2,688)	(1,909)	(5,051)	(4,378)
Contribution to the Depositors' and Investors' Guarantee Fund		(265)	(260)	(534)	(518)
Bank tax		(710)	(623)	(1,328)	(1,215)
Total operating expenses		(7,084)	(6,233)	(13,794)	(12,992)
Profit before net loan impairment		4,179	3,781	8,478	8,207
Net loan impairment	18	1,977	4,219	4,308	5,739
Profit before tax		6,156	8,000	12,786	13,946
Income tax expense	19	(1,524)	(2,156)	(2,920)	(3,550)
Profit for the period from continuing operations		4,632	5,844	9,866	10,396
Profit from discontinued operations, net of income tax		762	515	924	4,259
Profit for the period		5,394	6,359	10,790	14,655
Profit attributable to:					
Equity holders of Íslandsbanki hf.		5,247	6,245	10,564	14,464
Non-controlling interests		147	114	226	191
Profit for the period		5,394	6,359	10,790	14,655
Earnings per share from continuing operations					
Basic and diluted earnings per share attributable to the shareholders of Íslandsbanki hf.	20	0.45	0.57	0.96	1.02

The half-year results were reviewed by the Bank's auditor. The quarterly statements and the split between quarters were not reviewed or audited by the Bank's auditor.

The notes on pages 10 to 52 are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK million

Condensed Consolidated Statement of Profit or Loss and other Comprehensive Income for the six months ended 30 June 2015

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Profit for the period	5,394	6,359	10,790	14,655
Other comprehensive income for the period (net of tax)	(43)	(10)	24	(154)
Total comprehensive income for the period	5,351	6,349	10,814	14,501

The half-year results were reviewed by the Bank's auditor. The quarterly statements and the split between quarters were not reviewed or audited by the Bank's auditor.

The notes on pages 10 to 52 are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK million

Condensed Consolidated Statement of Financial Position as at 30 June 2015

	Notes	30.6.2015	31.12.2014
Assets			
Cash and balances with Central Bank	6,21	126,900	103,389
Derivatives	6,22	1,581	1,810
Bonds and debt instruments	6	85,274	87,347
Shares and equity instruments	6	11,041	10,531
Loans to credit institutions	6,23	52,139	35,072
Loans to customers	6,24	653,728	634,799
Investments in associates	26	612	570
Property and equipment		7,600	7,402
Intangible assets		1,058	619
Deferred tax assets		45	521
Non-current assets and disposal groups held for sale	29	15,763	21,649
Other assets	30	20,516	7,619
Total Assets		976,257	911,328
Liabilities			
Derivative instruments and short positions	6,22	5,992	3,963
Deposits from Central Bank and credit institutions	6,31	24,017	25,796
Deposits from customers	6,32-33	566,678	529,447
Debt issued and other borrowed funds	6,34	107,421	96,889
Subordinated loans	6	20,336	21,306
Tax liabilities		8,627	8,388
Non-current liabilities and disposal groups held for sale	29	3,000	2,790
Other liabilities	35	53,177	37,262
Total Liabilities		789,248	725,841
Equity			
Share capital	36	10,000	10,000
Share premium	36	55,000	55,000
Other reserves		2,559	2,535
Retained earnings		117,852	116,288
Total equity attributable to the equity holders of Íslandsbanki hf.		185,411	183,823
Non-controlling interests		1,598	1,664
Total Equity		187,009	185,487
Total Liabilities and Equity		976,257	911,328

The notes on pages 10 to 52 are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK million

Condensed Consolidated Statement of Changes in Equity for the six months ended 30 June 2015

	Attributable to equity holders of Íslandsbanki hf.					Non-controlling interests	Total equity
	Share capital	Share premium	Other reserves	Retained earnings	Total		
Equity at 1.1.2014	10,000	55,000	2,471	98,548	166,019	1,299	167,318
Total comprehensive income for the period			(154)	14,464	14,310	191	14,501
Changes in non-controlling interests					-	(97)	(97)
Dividends				(4,000)	(4,000)		(4,000)
Equity at 30.6.2014	10,000	55,000	2,317	109,012	176,329	1,393	177,722
Equity at 1.1.2015	10,000	55,000	2,535	116,288	183,823	1,664	185,487
Total comprehensive income for the period			24	10,564	10,588	226	10,814
Dividends				(9,000)	(9,000)	(292)	(9,292)
Equity at 30.6.2015	10,000	55,000	2,559	117,852	185,411	1,598	187,009

The notes on pages 10 to 52 are an integral part of these Condensed Consolidated Interim Financial Statements

For the six months ended 30 June 2015 8 Amounts are in ISK million

Condensed Consolidated Statement of Cash Flows for the six months ended 30 June 2015

	Notes	2015 1.1-30.6	2014 1.1-30.6
Cash flows from operating activities:			
Profit for the period		10,790	14,655
Adjustments to reconcile profit for the period to cash flows provided by operating activities:			
Non-cash items included in profit for the period and other adjustments		(332)	(3,607)
Changes in operating assets and liabilities		26,903	(10,865)
Income tax paid		(3,576)	(1,915)
Net cash provided by (used in) operating activities		33,785	(1,732)
Net cash (used in) investing activities		(997)	(290)
Net cash provided by financing activities		525	6,161
Net (decrease) increase in cash and cash equivalents		33,313	4,139
Effects of exchange rate changes on cash and cash equivalents		10	(195)
Cash and cash equivalents at the beginning of the period		118,020	138,433
Cash and cash equivalents at the end of the period		151,343	142,377
Reconciliation of cash and cash equivalents:			
Cash on hand	21	2,926	2,737
Cash balances with Central Bank and term deposits	21	114,183	116,413
Bank accounts	23	34,234	23,227
Total cash and cash equivalents		151,343	142,377

Interest received from 1 January to 30 June 2015 amounted to ISK 25,627 million (H1 2014: ISK 25,436 million) and interest paid in the same period 2015 amounted to ISK 11,817 million (H1 2014: ISK 14,746 million). Interest is defined as having been paid when it has been deposited into the customer account and is available for the customer's disposal.

Dividends received from 1 January to 30 June 2015 amounted to ISK 557 million (H1 2014: ISK 259 million) and dividends paid amounted to ISK 9,000 million (H1 2014: ISK 4,000 million).

The notes on pages 10 to 52 are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

Notes to the Condensed Consolidated Interim Financial Statements

Accounting policies

General information

1. **The reporting entity**

Íslandsbanki hf. is a limited company incorporated and domiciled in Iceland. The Condensed Consolidated Interim Financial Statements for the six months ended 30 June 2015 comprise Íslandsbanki hf. (the parent) and its subsidiaries (together referred to as "the Bank").

The Condensed Consolidated Interim Financial Statements were authorised for issue by the Board of Directors of Íslandsbanki hf. on 24 August 2015.

2. **Basis of preparation**

2.1 *Statement of compliance*

The Condensed Consolidated Interim Financial Statements for the six months ended 30 June 2015 are presented in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting, as adopted by the European Union, the Act on Annual Accounts no. 3/2006 and the Act on Financial Undertakings no. 161/2002.

The Condensed Consolidated Interim Financial Statements do not include all the information required for annual financial statements and should be read in conjunction with the audited Consolidated Financial Statements of the Bank for the year ended 31 December 2014, as well as the unaudited Pillar 3 Report for the year ended 31 December 2014. Both are available at the Bank's website www.islandsbanki.is.

2.2 *Basis of measurement*

The Condensed Consolidated Interim Financial Statements have been prepared on an historical cost basis except for the following items in the statement of financial position: bonds and debt instruments which are measured at fair value, shares and equity instruments which are measured at fair value, derivative financial instruments which are measured at fair value and non-current assets and disposal groups classified as held for sale which are measured at the lower of cost and fair value less cost to sell.

The Condensed Consolidated Interim Financial Statements are presented in Icelandic krona (ISK), which is the functional currency of the Bank, rounded to the nearest million.

2.3 *Significant accounting judgements and estimates*

The preparation of the Condensed Consolidated Interim Financial Statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses recognised. The accounting estimates and underlying assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

The accounting estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

2.4 *Going concern*

The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has adequate resources to continue its operations for the foreseeable future. Therefore, the Condensed Consolidated Interim Financial Statements are prepared on a going concern basis.

2.5 *Changes in presentation*

The following changes have been made in presentation between the years:
a) The Bank has changed its presentation in the Consolidated Statement of Financial Position as follows:
- The line items Deposits from Central Bank and Deposits from credit institutions have been combined into one line: Deposits from Central Bank and credit institutions. These line items have also been combined in Notes 6, 8, 49 and 53.
- The line items Current tax liabilities and Deferred tax liabilities have been combined into one line: Tax liabilities.
b) Comparable information in Note 28 Related party has been changed as the balances were deemed to include information which is outside the scope of the definition of a related party according to IAS24 Related party. In addition, a new line item Shareholders with control over the group was added to the disclosure and two line items were united into one in Board of Directors and key management personnel.

3 **Significant accounting policies**

The accounting policies in these Condensed Consolidated Interim Financial Statements are the same as those applied in the Bank's consolidated financial statements for the year ended 31 December 2014.

Operating segments

4. An operating segment is a distinguishable component of the Bank that is engaged in providing products or services that are subject to risks and rewards that may be different from those of other operating segments. Transactions between the operating segments are on normal commercial terms and conditions. The Bank operates mainly in the Icelandic market. No single customer generates 10% or more of the combined revenue of the Bank.

The accounting policies for the reportable segments are in line with the Bank's accounting policies. The segment profit presented is the profit reported to the chief operating decision maker (CEO) and the Board of Directors for the purpose of resource allocation and assessment of segment performance.

The Bank is organised into six main operating segments based on products and services:

a) Retail banking provides comprehensive banking services to individuals and small and medium-sized enterprises through 17 branches, call centre, self service and digital banking platforms. Retail Banking also operates two separately branded units: Ergo for asset-based financing and the credit card branch Kreditkort.

b) Corporate Banking provides lending and tailor-made financial services to larger companies and professional investors. Building on experience and industry expertise Corporate Banking offers universal banking services to customers through cross-selling and by connecting customers to other business units of the Bank. Furthermore, Corporate Banking overseas the Bank's international business in the North Atlantic region where the focus is on the seafood, the offshore supply vessel and the energy industries.

c) Markets incorporates brokerage services in securities, foreign currencies and derivatives as well as providing money market lending and interbank services. The division further offers an extensive range of corporate finance services.

d) Wealth Management offers a range of wealth and asset management products and services for individuals, corporations and institutional investors. The Wealth Management unit consists of VÍB which offers a broad range of asset management products and services and the fund management companies Íslandssjódir and Summa.

e) Treasury is responsible for the management of capital, liquidity risk, foreign exchange risk and interest rate risk within regulatory requirements and internal limits established by the Board of Directors. Treasury is responsible for funding the Bank's operations and managing an internal pricing framework. Treasury also manages relations with investors and rating agencies.

f) Subsidiaries and equity investments include equity investments in the banking book and subsidiaries, the most significant being:

• Borgun, a credit card settlement company.
• Allianz Ísland hf., an agent for the German insurance company Allianz, and its holding company Hringur eignarhaldsfélag ehf.
• D1 ehf., a commercial real estate company which holds and manages a portfolio of properties for leasing, thereof 17 properties leased by the Bank.
• Midengi, an asset management company managing commercial real estate and businesses which the Bank has acquired through repossessions following loan defaults, debt restructuring and bankruptcies.

Cost centres comprise Head Office, Human Resources, Legal, Risk Management, Finance, Operations & IT, Group Internal Audit, Compliance and Business Development

On the following page is an overview showing the Bank's performance with a breakdown by operating segments as well as a reconciliation to the Bank's total profit and loss.

4. Cont'd

1 January to 30 June 2015

Operations	Retail Banking	Corporate Banking	Markets	Wealth Manage-ment	Treasury	Subsidiaries & Equity Investments	Cost Centres & Eliminations	Total
Net interest income	8,676	2,472	630	331	1,632	14	(205)	13,550
Net fee and commission income	2,209	89	914	1,022	(52)	2,223	18	6,423
Other net operating income (exps.)	37	4	16	136	(119)	2,861	(636)	2,299
Total operating income	10,922	2,565	1,560	1,489	1,461	5,098	(823)	22,272
Salaries and related expenses	(2,104)	(238)	(446)	(511)	(41)	(839)	(2,702)	(6,881)
Other operating expenses	(1,522)	(43)	(62)	(95)	(72)	(942)	(2,315)	(5,051)
Deposit guarantee fund and bank tax	(471)	(11)	(0)	(31)	(1,349)	(0)	-	(1,862)
Net loan impairment	471	3,873	(0)	(0)	-	104	(140)	4,308
Profit (loss) before cost allocation & tax	7,296	6,146	1,052	852	(1)	3,421	(5,980)	12,786
Net segment revenue from external customers	11,985	6,491	1,836	389	(3,359)	5,532	(602)	22,272
Net segment revenue from other segments	(1,063)	(3,926)	(276)	1,100	4,820	(434)	(221)	0
Depreciation and amortisation	(81)	(1)	(1)	(1)	(0)	(99)	(192)	(375)

At 30 June 2015	Retail Banking	Corporate Banking	Markets	Wealth Manage-ment	Treasury	Subsidiaries & Equity Investments	Cost Centres & Eliminations	Total
Total segment assets	425,365	231,399	26,414	7,368	229,591	74,350	(18,230)	976,257
Total segment liabilities	419,859	8,194	11,132	44,940	277,359	46,834	(19,070)	789,248
Allocated equity	48,066	33,737	2,555	3,171	94,148	11,966	(6,634)	187,009

1 January to 30 June 2014

Operations	Retail Banking	Corporate Banking	Markets	Wealth Manage-ment	Treasury	Subsidiaries & Equity Investments	Cost Centres & Eliminations	Total
Net interest income	8,499	2,103	341	381	2,757	(271)	(242)	13,568
Net fee and commission income	2,145	56	1,026	962	(49)	1,509	23	5,672
Other net operating income (exps.)	39	385	(110)	(97)	(307)	2,128	(79)	1,959
Total operating income	10,683	2,544	1,257	1,246	2,401	3,366	(298)	21,199
Salaries and related expenses	(2,134)	(220)	(455)	(470)	(53)	(747)	(2,802)	(6,881)
Other operating expenses	(952)	(33)	(59)	(93)	(112)	(845)	(2,284)	(4,378)
Deposit guarantee fund and bank tax	(453)	(9)	(0)	(38)	(1,233)	(0)	-	(1,733)
Net loan impairment	2,941	2,362	-	0	34	563	(161)	5,739
Profit (loss) before cost allocation & tax	10,085	4,644	743	645	1,037	2,337	(5,545)	13,946
Net segment revenue from external customers	11,056	5,944	1,569	(116)	(994)	3,789	(49)	21,199
Net segment revenue from other segments	(373)	(3,401)	(312)	1,362	3,395	(423)	(248)	0
Depreciation and amortisation	(78)	-	(1)	(1)	(2)	(94)	(218)	(394)

At 30 June 2014	Retail Banking	Corporate Banking	Markets	Wealth Manage-ment	Treasury	Subsidiaries & Equity Investments	Cost Centres & Eliminations	Total
Total segment assets	407,679	200,320	18,281	2,820	219,432	94,926	(35,927)	907,531
Total segment liabilities	396,479	7,992	3,615	56,055	241,620	46,290	(22,242)	729,809
Allocated equity	41,381	25,532	2,121	2,338	100,045	27,835	(21,530)	177,722

Amounts are in ISK million

Quarterly statements

5. Operations by quarters:

	Q2* 2015	Q1* 2015	Q4* 2014	Q3* 2014	Q2* 2014
Net interest income	7,359	6,191	6,469	7,068	6,922
Net fee and commission income	3,518	2,905	2,962	2,849	2,818
Net financial income	275	1,764	603	83	19
Net foreign exchange (loss) gain	(141)	(140)	116	352	(12)
Share of profit of associates	-	63	-	-	27
Other operating income	252	226	509	233	240
Salaries and related expenses	(3,421)	(3,460)	(3,497)	(2,930)	(3,441)
Other operating expenses	(2,688)	(2,363)	(2,914)	(2,301)	(1,909)
Contribution to the Depositors' and Investors' Guarantee Fund	(265)	(269)	(265)	(272)	(260)
Bank tax	(710)	(618)	(565)	(664)	(623)
Net loan impairment	1,977	2,331	3,006	65	4,219
Profit before tax	6,156	6,630	6,424	4,483	8,000
Income tax	(1,524)	(1,396)	(1,434)	(1,255)	(2,156)
Profit for the period from continuing operations	4,632	5,234	4,990	3,228	5,844
Profit (loss) for the period from discontinued operations	762	162	(430)	307	515
Profit for the period	5,394	5,396	4,560	3,535	6,359

*The half-year results were reviewed by the Bank's auditor. The quarterly statements and the split between quarters are not reviewed by the Bank's auditor.

Amounts are in ISK million

Financial assets and liabilities

6. The following tables show the carrying value of financial assets and financial liabilities according to their IAS39 classification.

At 30 June 2015	Notes	Held for trading	Designated at fair value through P&L	Loans & receivables	Liabilities at amortised cost	Total carrying amount
Cash and balances with Central Bank	21	-	-	126,900	-	126,900
Loans and receivables						
Loans to credit institutions	23	-	-	52,139	-	52,139
Loans to customers	24	-	-	653,728	-	653,728
Loans and receivables		-	-	832,767	-	832,767
Bonds and debt instruments						
Listed		50,707	31,406	-	-	82,113
Unlisted		-	3,161	-	-	3,161
Bonds and debt instruments		50,707	34,567	-	-	85,274
Shares and equity instruments						
Listed		5,404	3,920	-	-	9,324
Unlisted		-	1,717	-	-	1,717
Shares and equity instruments		5,404	5,637	-	-	11,041
Derivatives	22	1,581	-	-	-	1,581
Other financial assets		-	-	16,675	-	16,675
Total financial assets		57,692	40,204	849,442	-	947,338
Derivative instruments and short positions	22	5,992	-	-	-	5,992
Deposits from Central Bank and credit institutions	31	-	-	-	24,017	24,017
Deposits from customers	32-33	-	-	-	566,678	566,678
Debt issued and other borrowed funds	34	-	-	-	107,421	107,421
Subordinated loans		-	-	-	20,336	20,336
Other financial liabilities		-	-	-	43,156	43,156
Total financial liabilities		5,992	-	-	761,608	767,600

Amounts are in ISK million

6. Cont'd

At 31 December 2014	Notes	Held for trading	Designated at fair value through P&L	Loans & receivables	Liabilities at amortised cost	Total carrying amount
Cash and balances with Central Bank	21	-	-	103,389	-	103,389
Loans and receivables						
Loans to credit institutions	23	-	-	35,072	-	35,072
Loans to customers	24	-	-	634,799	-	634,799
Loans and receivables		-	-	773,260	-	773,260
Bonds and debt instruments						
Listed		54,273	31,347	-	-	85,620
Unlisted		-	1,727	-	-	1,727
Bonds and debt instruments		54,273	33,074	-	-	87,347
Shares and equity instruments						
Listed		4,810	2,917	-	-	7,727
Unlisted		-	2,804	-	-	2,804
Shares and equity instruments		4,810	5,721	-	-	10,531
Derivatives	22	1,810	-	-	-	1,810
Other financial assets		-	-	3,931	-	3,931
Total financial assets		60,893	38,795	777,191	-	876,879
Derivative instruments and short positions	22	3,963	-	-	-	3,963
Deposits from Central Bank and credit institutions	31	-	-	-	25,796	25,796
Deposits from customers	32-33	-	-	-	529,447	529,447
Debt issued and other borrowed funds	34	-	-	-	96,889	96,889
Subordinated loans		-	-	-	21,306	21,306
Other financial liabilities		-	-	-	25,363	25,363
Total financial liabilities		3,963	-	-	698,801	702,764

For the six months ended 30 June 2015 16 Amounts are in ISK million

Fair value information for financial instruments

7. Financial instruments carried at fair value

The fair value of a financial instrument is the transaction price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Where a market price is not readily available, the Bank applies valuation techniques based on estimates and assumptions that are consistent with that which market participants would use in setting a price for the financial instrument. In some instances the Bank uses approximation methods. These approximation methods are explained in more detail below.

The table below shows financial instruments carried at fair value categorised into levels of fair value hierarchy that reflect the significance of inputs used in making the fair value measurements as at 30 June 2015. The different levels have been defined as follows:

Level 1: Inputs that are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Bank can access at the measurement date.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Inputs that are unobservable, e.g. internal assumptions.

At 30 June 2015

Financial assets:	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	50,951	33,118	1,205	85,274
Shares and equity instruments	9,213	1,034	794	11,041
Derivative instruments	-	1,581	-	1,581
Total financial assets	60,164	35,733	1,999	97,896

Financial liabilities:	Level 1	Level 2	Level 3	Total
Short positions	2,097	-	-	2,097
Derivative instruments	-	3,804	91	3,895
Total financial liabilities	2,097	3,804	91	5,992

The following table shows financial instruments carried at fair value categorised into levels of fair value hierarchy as at 31 December 2014.

At 31 December 2014

Financial assets:	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	54,618	31,539	1,190	87,347
Shares and equity instruments	7,617	98	2,816	10,531
Derivative instruments	-	1,810	-	1,810
Total financial assets	62,235	33,447	4,006	99,688

Financial liabilities:	Level 1	Level 2	Level 3	Total
Short positions	686	0	-	686
Derivative instruments	-	3,184	93	3,277
Total financial liabilities	686	3,184	93	3,963

For the six months ended 30 June 2015 17 Amounts are in ISK million

7. Cont'd

Reconciliation of financial assets and liabilities categorised into Level 3

1 January to 30 June 2015	Bonds and debt instruments	Shares and equity instruments	Derivatives
Fair value at 31 December 2014	1,190	2,816	(93)
Purchases	-	10	-
Sales	-	(762)	-
Net gains on financial instruments	15	158	2
Transfers from level 1 or 2	-	-	-
Transfers to level 1 or 2	-	(1,428)	-
Fair value at 30 June 2015	1,205	794	(91)

1 January to 31 December 2014	Bonds and debt instruments	Shares and equity instruments	Derivatives
Fair value at 31 December 2013	1,279	2,791	(85)
Purchases	-	709	-
Sales	(32)	(383)	-
Net gains on financial instruments	(57)	459	(8)
Transfers from level 1 or 2	-	-	-
Transfers to level 1 or 2	-	(760)	-
Fair value at 31 December 2014	1,190	2,816	(93)

One equity instrument, a total of ISK 1,194 million, was transferred from Level 3 to Level 1 due to its listing on the domestic market. One equity instrument, a total of ISK 234 million, was transferred to Level 2 as its value is now derived from its listed assets. Equity instruments worth ISK 505 million and bond options with a negative market value of ISK 91 million were then transferred to Level 2 following a revision of the significancy of the unobservable inputs used in their valuation models. No other instruments were transferred between levels in the first half of 2015.

The responsibility for the measurement of fair value of financial instruments lies within the business units that are responsible for the positions. The business units are required to assess the valuation of their assets quarterly and present them for the Investment Committee for approval. Risk Management is responsible for reviewing the valuations, assessing the extent of market data used and categorising the valuation methods.

The objective of this valuation process is to arrive at a fair value measurement which reflects the price of the asset or liability that would be paid or received in an orderly transaction between market participants at the measurement date.

Where applicable, fair values are determined using quoted prices in active markets for identical assets and liabilities. The Bank defines an active market as one where transactions take place with sufficient frequency and volume. In other cases, where there is no active market, the fair value is estimated using valuation techniques such as net present value and discounted cash flow models; comparison with similar instruments for which observable market data exists; net asset value (NAV) for investment fund units or expected recovery for distressed bonds. These valuation techniques are based on various assumptions and inputs such as risk-free rate, expected revenue growth and credit and liquidity spreads. In some cases, where significant inputs into these models are not observable, expert judgement and estimation for these inputs are required.

Actively traded bonds and shares are classified as Level 1. The Bank classifies mutual fund units as shares and equity instruments in Level 3 and estimates the fair value for these units based on NAV where the unit prices are not readily available. Unlisted equities are initially booked at their transaction price but are revalued each quarter based on the models as described above. They are classified as Level 3. For interest rate derivatives contracts such as interest rate swaps (IRS) and cross-currency interest rate swaps (CIRS) the Bank calculates the net present value of estimated future cash flows based on yield curves with key inputs such as interest swap rates and forward-rate agreements (FRAs) rates. Foreign-currency forwards and foreign-currency swaps are valued using the FX spot rate adjusted for forward pricing points that can be obtained from market sources. These products are classified as Level 2. Bond forwards and equity forwards are also classified as Level 2 as they are valued using standard models with key inputs observed from stock prices, estimated dividend rates and funding rates. In general, standard bond options are classified as Level 2. The Bank classifies non-standard bond options as Level 3 due to the level of internal estimation used in their valuation.

For the six months ended 30 June 2015 18 Amounts are in ISK million

7. Cont'd

The Bank's Level 1 financial assets and financial liabilities contain bonds and equities that are listed either domestically or abroad. Level 2 assets and liabilities contain illiquid bonds in the domestic markets, unlisted equities as well as derivatives. Level 3 assets contain primarily unlisted and illiquid equities and bonds and bond options.

At the end of 30 June 2015 the Bank's Level 3 shares amounted to ISK 289 million and were valued with a discounted cash flow model. This model uses various unobservable inputs, most notably the weighted average cost of capital (WACC) and both forecasted yearly revenue growth and future EBITDA-to-sales ratio. The model is sensitive to changes in all of these estimated variables. An increase in the WACC would result in a lower fair value and a decrease would result in a higher fair value. On the other hand an increase in both the forecasted yearly revenue growth and EBITDA-to-sales ratio would result in a higher fair value and a decrease would result in a lower fair value.

The Bank's Level 3 bonds amounted to ISK 1,205 million and were valued based on expected recovery of the bond issuers' assets. The expected recovery of these bonds ranges from 0-75% and is subject to uncertainty regarding various assumptions, such as the outcome of legal disputes. An increase or decrease in the expected recovery would result in a similar change in the fair value.

8. Financial instruments not carried at fair value

The table below shows the fair value measurement and classification of financial assets and liabilities not carried at fair value at 30 June 2015. The different levels are defined as before (see note 7).

Assets

Loans to customers on the Bank's balance sheet that are carried at amortised cost consist of two types:

1) Loans whose carrying amount is less than their claim value, due to either impairments or deep discount.
2) Loans whose carrying amount equals the claim value.

Loans in category 1) are specifically measured at least every six months and every three months for significant amounts and therefore it is considered that their carrying amount is a good approximation of their fair value. Since measurement is partially based on internal models they are classified as Level 3. The fair value of the loans in category 2) may differ from their carrying amount because the interest rate they carry may not reflect the interest rate that similar new loans would carry. This difference stems from two sources:

a) Credit migration: The debtors may not have the same credit-worthiness they had when the loans’ interest rates were last reset and the collateralisation of the loan may have changed.
b) Fixed rate loans: The interest rate level used as a base for pricing fixed rate loans may have shifted.

The Bank calculates the fair value of loans in category 2) by discounting from the carrying amount the resulting interest rate difference from 30 June 2015 to the loan's next interest reset or maturity, whichever comes first. Since the credit-worthiness is estimated using the Bank's internal models these assets are classified as Level 3.
For “Cash and balances with Central Bank”, “Loans to credit institutions” and “Other financial assets” the fair value is very well approximated by the carrying amount since they are short term in nature. They are thus classified as Level 2.

Liabilities

The fair value of a financial liability with a demand feature, such as a demand deposit, is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid.

On the liabilities side most deposits are on demand or carry floating interest rates and as such their carrying amount is considered a good approximation of their fair value. For longer term, fixed rate deposits the Bank calculates the fair value with a duration approach, using the difference in each liability´s current interest rate from the rate that a similar deposit would carry today. The fair value estimate of deposits does not take into account the effect of the Payment Service Directive on interest reset dates. All deposits are classified as Level 2 based on the use of observable market interest rates to estimate the fair value.

For the fair value of "Debt issued and other borrowed funds" the Bank uses an observed market value where it is available. Issued bonds and bills with quoted market prices are classified as Level 1. If there is no quoted market price the fair value of the debt is valued in the same manner as deposits if it carries a fixed rate. If the debt carries a floating rate its fair value is estimated by comparing the margin with the Bank’s current funding premium on debt with similar terms. These liabilities are classified as Level 2. The Bank estimates its funding premium based on the interest margin on its issued papers including covered bonds, commercial papers as well as foreign currency denominated bonds.

The fair value of liabilities in "Subordinated loans" is estimated using a duration approach by comparing the contractual interest margin with the interest margin in the market on the Bank's issuance in foreign currency plus a margin to account for the fact that the subordinated liabilities are junior to the market traded debt. These liabilities are classified as Level 2.

Other financial liabilities mainly include unsettled securities transactions and liabilities to retailers for credit card provision and are classified as level 2 since their value is not observable from active market prices. Due to the short term nature of these liabilities their carrying amount is considered a good approximation of their fair value.

The following table shows the fair value for the Bank's assets and liabilities recognised at amortised cost.

8. Cont'd

At 30 June 2015	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Financial assets:					
Cash and balances with Central banks	-	126,900	-	126,900	126,900
Loans to credit institutions	-	52,139	-	52,139	52,139
Loans to customers	-	-	656,574	656,574	653,728
Other financial assets	-	16,675	-	16,675	16,675
Total financial assets	-	195,714	656,574	852,288	849,442

At 30 June 2015	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Financial liabilities:					
Deposits from Central Bank and credit institutions	-	24,017	-	24,017	24,017
Deposits from customers	-	566,699	-	566,699	566,678
Debt issued and other borrowed funds	44,262	63,591	-	107,853	107,421
Subordinated loans	-	20,336	-	20,336	20,336
Other financial liabilities	-	43,156	-	43,156	43,156
Total financial liabilities	44,262	717,799	-	762,061	761,608

At 31 December 2014	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Financial assets:					
Cash and balances with Central banks	-	103,389	-	103,389	103,389
Loans to credit institutions	-	35,072	-	35,072	35,072
Loans to customers	-	-	636,141	636,141	634,799
Other financial assets	-	3,931	-	3,931	3,931
Total financial assets	-	142,392	636,141	778,533	777,191

At 31 December 2014	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Financial liabilities:					
Deposits from Central Bank and credit institutions	-	25,796	-	25,796	25,796
Deposits from customers	-	529,519	-	529,519	529,447
Debt issued and other borrowed funds	37,293	59,601	-	96,894	96,889
Subordinated loans	-	21,306	-	21,306	21,306
Other financial liabilities	-	25,363	-	25,363	25,363
Total financial liabilities	37,293	661,585	-	698,878	698,801

Amounts are in ISK million

Offsetting financial assets and financial liabilities

9. Offsetting financial assets and financial liabilities

The table below provides a summary of the financial assets and financial liabilities which are subject to enforceable master netting agreements of similar arrangements, even if they have not been offset in the statement of financial position.

a) Financial assets subject to offsetting, enforceable netting arrangements and similar agreements

	Financial assets subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 30 June 2015	Gross recognised financial assets before balance sheet netting	Balance sheet netting with gross recog- nised financial liabilities	Financial assets recognis- ed on the balance sheet, net	Recognised financial liabilities	Cash collateral received	Financial instruments collateral received	Net amount after consideration of potential effect of netting arrangements	Assets outside the scope of offsetting disclosure requirements	Total assets recognised on the balance sheet
Derivatives	1,581	-	1,581	(416)	(56)	(13)	1,096	-	1,581
Total assets	1,581	-	1,581	(416)	(56)	(13)	1,096	-	1,581
At 31 December 2014									
Derivatives	1,810	-	1,810	(306)	(48)	(18)	1,438	-	1,810
Total assets	1,810	-	1,810	(306)	(48)	(18)	1,438	-	1,810

b) Financial liabilities subject to offsetting, enforceable netting arrangements and similar agreements

	Financial liabilities subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 30 June 2015	Gross recognised financial liabilities before balance sheet netting	Balance sheet netting with gross recog- nised financial assets	Financial liabilities recognis- ed on the balance sheet, net	Recognised financial assets	Cash collateral pledged	Financial instruments collateral pledged	Net amount after consideration of potential effect of netting arrangements	Liabilities outside the scope of offsetting disclosure requirements	Total liabilities recognised on the balance sheet
Derivative instruments and short positions	3,895	-	3,895	(416)	-	(1,341)	2,138	2,097	5,992
Total liabilities	3,895	-	3,895	(416)	-	(1,341)	2,138	2,097	5,992
At 31 December 2014									
Derivative instruments and short positions	3,277	-	3,277	(306)	-	(1,899)	1,072	686	3,963
Total liabilities	3,277	-	3,277	(306)	-	(1,899)	1,072	686	3,963

Amounts are in ISK million

Net interest income

10. Net interest income is specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Interest income:				
Cash and balances with Central Bank	1,319	1,695	2,479	3,378
Loans and receivables	12,697	10,841	22,591	21,159
Financial assets held for trading	115	376	314	768
Financial assets designated at fair value through profit or loss	375	442	725	857
Other assets	30	45	64	99
Total interest income	14,536	13,399	26,173	26,261
Interest expense:				
Deposits from credit institutions and Central Bank	(108)	(124)	(199)	(263)
Deposits from customers	(5,023)	(4,544)	(8,870)	(8,820)
Borrowings	(1,810)	(1,449)	(2,946)	(2,838)
Subordinated loans	(257)	(232)	(516)	(462)
Other financial liabilities	(34)	(87)	(67)	(180)
Other interest expense	55	(41)	(25)	(130)
Total interest expense	(7,177)	(6,477)	(12,623)	(12,693)
Net interest income	7,359	6,922	13,550	13,568

Net fee and commission income

11. Net fee and commission income is specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Fee and commission income:				
Asset management	457	435	861	828
Investment Banking and brokerage	737	576	1,159	1,086
Payment processing	3,468	2,740	6,617	5,444
Loans and guarantees	327	307	662	636
Other fee and commission income	385	311	752	708
Total fee and commission income	5,374	4,369	10,051	8,702
Commission expenses:				
Brokerage	(20)	(36)	(41)	(70)
Clearing and settlement	(1,826)	(1,452)	(3,572)	(2,784)
Other commission expenses	(10)	(63)	(15)	(176)
Total commission expenses	(1,856)	(1,551)	(3,628)	(3,030)
Net fee and commission income	3,518	2,818	6,423	5,672

For the six months ended 30 June 2015 22 Amounts are in ISK million

Net financial income

12. Net financial income is specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Net gain on financial instruments held for trading	381	151	706	58
Net (loss) gain on financial instruments designated at fair value through P&L	(106)	(132)	1,333	824
Net financial income	275	19	2,039	882

13. Net (loss) gain on financial instruments designated at fair value through profit or loss is specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Shares	(131)	(95)	1,301	883
Bonds	25	(37)	32	(59)
Net (loss) gain on financial instruments designated at fair value through P&L	(106)	(132)	1,333	824

Net foreign exchange loss

14. Net foreign exchange loss is specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Assets:				
Cash and balances with Central Bank	4	17	(14)	(41)
Financial assets held for trading	616	(619)	(3,092)	(898)
Loans and receivables	(2,176)	(174)	352	(2,639)
Other assets	(235)	88	148	74
Total assets	(1,791)	(688)	(2,606)	(3,504)
Liabilities:				
Deposits	1,640	78	548	1,785
Subordinated loan	(1)	159	969	612
Debt issued and other borrowed funds	(152)	496	1,021	843
Other liabilities	163	(57)	(213)	(39)
Total liabilities	1,650	676	2,325	3,201
Net foreign exchange loss	(141)	(12)	(281)	(303)

Other operating income

15. Other operating income is specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Service level agreement fees	46	62	105	133
Legal cost and fees	54	30	95	66
Rental income	32	47	56	78
Rental income on foreclosed mortgages	66	82	125	174
Other net operating income	54	19	97	902
Other operating income	252	240	478	1,353

Amounts are in ISK million

Salaries and related expenses

16. Salaries and related expenses are specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Salaries	2,680	2,609	5,375	5,270
Pension and similar expenses	389	397	783	779
Social security charges and financial activities tax	376	390	739	753
Other	41	45	101	79
Capitalisation of internal staff costs in software development	(65)	-	(117)	-
Salaries and related expenses	3,421	3,441	6,881	6,881

Other operating expenses

17. Other operating expenses are specified as follows:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Other administrative expenses	2,501	1,712	4,676	3,984
Depreciation and amortisation	187	197	375	394
Other operating expenses	2,688	1,909	5,051	4,378

Net loan impairment

18. Net loan impairment:

	2015 1.4-30.6	2014 1.4-30.6	2015 1.1-30.6	2014 1.1-30.6
Loan impairment charged to the income statement:				
Specific impairment losses on loans and receivables	(735)	(767)	(1,900)	(772)
Collective impairment	(17)	(103)	288	353
Total impairment charged to the income statement (see Note 25)	(752)	(870)	(1,612)	(419)
Net loan impairment				
Impairment reversal due to revised estimated future cash flows	2,729	5,089	5,920	6,158
Net specific impairment losses on loans and receivables	(735)	(767)	(1,900)	(772)
Net loan impairment before collective impairment	1,994	4,322	4,020	5,386
Collective impairment	(17)	(103)	288	353
Total net loan impairment	1,977	4,219	4,308	5,739

For the six months ended 30 June 2015 24 Amounts are in ISK million

Income taxes

19. Income tax for the six month period ended 30 June 2015 is calculated at 20%. Special financial activities tax (FAT) is calculated as 6% of taxable profits above ISK 1 billion. The effective income tax rate in the Bank's income statement is 22,8% for the six months ended 30 June 2015.

Income tax expense recognised in the income statement is specified as follows:	2015 1.1-30.6	2014 1.1-30.6
Current tax expense	1,953	2,543
Special financial activities tax	465	719
Difference in prior year's imposed and calculated income tax	26	-
Origination and reversal of temporary differences due to deferred tax assets	476	288
Total	2,920	3,550

The effective income tax rate is computed as follows:	2015 1.1-30.6		2014 1.1-30.6	
Profit before tax	12,786		13,946	
20% income tax calculated on profit before tax	2,557	20.0%	2,789	20.0%
Special financial activities tax	465	3.6%	719	5.2%
Non-deductable expenses	284	2.2%	196	1.4%
Tax on income not subject to tax	(447)	(3.4%)	(735)	(5.3%)
Correction in accordance with ruling on prior year's taxable income	77	0.5%	(14)	(0.1%)
Other differences	(16)	(0.1%)	595	4.3%
Income tax expense	2,920	22.8%	3,550	25.5%

Earnings per share

20. Earnings per share are specified as follows:

	Discontinued operations			
	Excluded		Included	
	2015 1.1-30.6	2014 1.1-30.6	2015 1.1-30.6	2014 1.1-30.6
Net profit of the equity holders of the parent, according to the Condensed Consolidated Income Statement	9,640	10,205	10,564	14,464
Weighted average number of outstanding shares for the period, million	10,000	10,000	10,000	10,000
Basic earnings per share	0.96	1.02	1.06	1.45

There were no instruments at the end of the period that could potentially dilute basic earnings per share (2014: none).

For the six months ended 30 June 2015 25 Amounts are in ISK million

Cash and balances with Central Bank

21. Specification of cash and balances with Central Bank:

	30.6.2015	31.12.2014
Cash on hand	2,926	2,256
Balances with Central Bank other than mandatory reserve deposits	20,902	10,738
Term deposits	93,281	80,843
Included in cash and cash equivalents	117,109	93,837
Mandatory reserve deposits with Central Bank	9,791	9,552
Cash and balances with Central Bank	126,900	103,389

The average balance of the Central bank current account for each month must be equivalent to at least mandatory reserve deposits, amounted to ISK 9,791 million (December 2014: ISK 9,629 million).

Derivative instruments and short positions

22. Derivative instruments and short positions:

At 30 June 2015	Assets	Notional values related to assets	Liabilities	Notional values related to liabilities
Interest rate swaps	171	10,605	1,417	33,455
Cross currency interest rate swaps	1,049	21,783	1,650	28,743
Equity forwards	132	1,269	254	1,971
Foreign exchange forwards	16	2,646	426	7,462
Foreign exchange swaps	171	8,644	5	922
Bond forwards	42	2,040	52	5,820
Bond options	-	-	91	25,000
Derivatives held for trading	1,581	46,987	3,895	103,373
Short positions in listed bonds	-	-	2,097	-
Total	1,581	46,987	5,992	103,373

At 31 December 2014	Assets	Notional values related to assets	Liabilities	Notional values related to liabilities
Interest rate swaps	360	10,800	1,027	18,950
Cross currency interest rate swaps	886	34,369	1,926	24,252
Equity forwards	144	1,605	117	1,482
Foreign exchange forwards	16	1,468	97	3,695
Foreign exchange swaps	306	4,744	2	963
Bond forwards	98	4,371	15	1,100
Bond options	-	-	93	25,000
Derivatives held for trading	1,810	57,357	3,277	75,442
Short positions in listed bonds	-	-	686	-
Total	1,810	57,357	3,963	75,442

For the six months ended 30 June 2015 26 Amounts are in ISK million

Loans and receivables

23. Loans to credit institutions:

	30.6.2015	31.12.2014
Money market loans	17,905	10,889
Bank accounts	34,234	24,183
Loans to credit institutions	52,139	35,072

24. Loans to customers - impairment allowance per sector:

At 30 June 2015

	Gross amount	Specific impairment allowance	Loans less impairment allowance
Loans to customers:			
Individuals	264,169	(4,377)	259,792
Commerce and services	93,715	(2,850)	90,865
Construction	23,299	(3,535)	19,764
Energy	3,791	-	3,791
Financial services	114	(8)	106
Industrial and transportation	67,240	(646)	66,594
Investment companies	21,499	(3,153)	18,346
Public sector and non-profit organisations	11,524	-	11,524
Real estate	103,865	(545)	103,320
Seafood	83,171	(983)	82,188
Loans to customers before collective impairment allowance			656,290
Collective impairment allowance			(2,562)
Loans to customers	672,387	(16,097)	653,728

At 31 December 2014

	Gross amount	Specific impairment allowance	Loans less impairment allowance
Loans to customers:			
Individuals	268,053	(5,205)	262,848
Commerce and services	83,590	(3,932)	79,658
Construction	21,472	(2,721)	18,751
Energy	7,315	-	7,315
Financial services	121	-	121
Industrial and transportation	63,019	(1,141)	61,878
Investment companies	15,531	(1,620)	13,911
Public sector and non-profit organisations	12,234	(18)	12,216
Real estate	100,774	(1,234)	99,540
Seafood	82,449	(1,037)	81,412
Loans to customers before collective impairment allowance			637,650
Collective impairment allowance			(2,851)
Loans to customers	654,558	(16,908)	634,799

Amounts are in ISK million

25. Impairment

The following table shows the movement in the provision for impairment losses for loans and receivables.

	Specific impairment allowance	Collective impairment allowance	Total
At 1 January 2015	16,908	2,851	19,759
Amounts written-off	(2,785)	-	(2,785)
Recoveries of amounts previously written-off	340	-	340
Principal credit adjustment	(266)	-	(266)
Charged to the income statement	1,900	(288)	1,612
At 30 June 2015	16,097	2,562	18,659

	Specific impairment allowance	Collective impairment allowance	Total
At 1 January 2014	24,234	3,682	27,915
Reclass 1 January	(137)	137	-
Amounts written-off	(9,745)	-	(9,745)
Recoveries of amounts previously written-off	934	-	934
Principal credit adjustment	(1,200)	-	(1,200)
Charged to the income statement	2,822	(967)	1,855
At 31 December 2014	16,908	2,851	19,759

Investment in associates

26. Changes in investments in associates:

	30.6.2015	31.12.2014
Investment in associates at the beginning of the year	570	1,563
Additions during the period	-	62
Revaluation	(21)	(20)
Share of results	63	27
Distribution of capital	-	(1,062)
Investments in associates at the end of the period	612	570

Investment in subsidiaries

27. Significant subsidiaries:

	Location	Ownership 30.6.2015	Ownership 31.12.2014
Borgun hf., Ármúla 30, 108 Reykjavík	Iceland	63.5%	63.5%
Íslandssjódir hf., Kirkjusandi 2, 105 Reykjavík	Iceland	100%	100%
Midengi ehf., Lækjargötu 12, 155 Reykjavík	Iceland	100%	100%
Hringur eignarhaldsfélag ehf., Digranesvegi 1, 200 Kópavogur	Iceland	100%	100%
Allianz Ísland hf., Digranesvegi 1, 200 Kópavogur	Iceland	100%	100%
D-1 ehf., Kirkjusandi 2, 105 Reykjavík	Iceland	100%	100%
Geysir Green Investment Fund slhf., Kirkjusandi 2, 105 Reykjavík	Iceland	100%	100%
Fergin ehf., Hesthálsi 6-8, 110 Reykjavík	Iceland	80%	80%
Frumherji hf., Hesthálsi 6-8, 110 Reykjavík	Iceland	80%	80%
20 other subsidiaries (SME)			

Amounts are in ISK million

Related party disclosures

28. Ultimate controlling party

The Bank has determined that ISB Holding ehf. is the ultimate controlling party of the Bank with GLB Holding ehf. and Glitnir hf. having significant influence. This is in accordance with the definition of a related party in IAS 24 Related party disclosures and is reflected in the related party transactions.

The Icelandic State Treasury owns 5% of the Bank's shareholding through the Icelandic State Financial Investments (ISFI). Entities which are controlled, jointly controlled or significantly influenced by the government (state-controlled entities) are not considered as being a related party if neither entity actually influenced the other and if the state did not actually influence either entity with regards to transactions between them. The Bank's transactions with state-controlled entities during the period were based on general business terms and are therefore not considered to be related party transactions.

Cash and balances with the Central Bank are disclosed under Note 21 and Deposits from Central Bank are disclosed under Note 31. The Bank also holds a Tier II subordinated loan in EUR with the Central Bank of Iceland with a total balance of ISK 20,336 million (2014: ISK 21,306 million). The Tier II is expected to be replaced by a subordinated loan issued by Glitnir by the end of the year 2015, as part of a proposed re-capitalisation of the Bank (see Note 39).

Related party transactions

The Bank has a related party relationship with its associates, the Board of Directors of the parent company and the ultimate controlling party, the Management Board, close family members of individuals referred to herein, and entities with significant influence as the largest shareholders of the Bank.

All loans to employees are provided on general business terms of the Bank. The balances do not reflect collaterals held by the Bank.

Related parties have transacted with the Bank during the period as follows:

At 30 June 2015

	Assets	Liabilities	Net balance	Guarantees	Commitments and overdraft
Shareholders with control over the Bank	-	(111)	(111)	-	-
Board of Directors and key Management personnel	446	(775)	(329)	27	125
Associated companies and other related parties	460	(1,164)	(704)	415	27
Total	906	(2,050)	(1,144)	442	152

At 31 December 2014

	Assets	Liabilities	Net balance	Guarantees	Commitments and overdraft
Shareholders with control over the Group	-	(147)	(147)	-	-
Board of Directors and key Management personnel	430	(611)	(181)	27	77
Associated companies and other related parties	553	(1,316)	(763)	435	26
Total	983	(2,074)	(1,091)	462	103

Impairment allowances of ISK 302 million (2014: ISK 714 million) were recognised in the period against balances outstanding with associated companies.

No share option programmes were operated during the reporting period 1 January - 30 June 2015.

Amounts are in ISK million

Non-current assets and disposal groups held for sale

29. Specification of non-current assets and disposal groups held for sale:

	30.6.2015	31.12.2014
Repossessed collateral	6,915	8,592
Assets of disposal groups classified as held for sale	8,848	13,057
Total	15,763	21,649

Repossessed collateral:

Land and property	6,443	8,176
Industrial equipment and vehicles	107	51
Shares and equity instruments	365	365
Total	6,915	8,592

Assets of disposal groups classified as held for sale:	30.6.2015	31.12.2014
Cash	648	150
Equity instruments	775	775
Receivables	661	1,050
Tax assets	16	78
Properties and land	2,892	6,820
Equipment	462	411
Other assets	3,394	3,773
Total	8,848	13,057

Liabilities associated with assets classified as held for sale:	30.6.2015	31.12.2014
Payables	123	80
Deferred tax liabilities	79	76
Income tax payable	52	45
Borrowings	2,369	2,284
Other liabilities	377	305
Total	3,000	2,790

On 31 May 2015 the Bank sold 100% of its shareholding in Bréfabær ehf., Fjárvari ehf. and Sævarhöfdi ehf. The entities were classified as disposal group held for sale. The Bank has derecognised the assets and liabilities and other components related to the subsidiaries. Any surplus or deficit arising on the loss of control is recognised in profit or loss in the line item "Profit from discontinued operations, net of income tax".

Other assets

30. Other assets are specified as follows:

	30.6.2015	31.12.2014
Receivables	5,846	4,845
Unsettled securities transactions	13,229	1,660
Accruals	736	606
Prepaid expenses	407	213
Other assets	298	295
Other assets	20,516	7,619

Amounts are in ISK million

Deposits from Central Bank and credit institutions

31. Deposits from Central Bank and credit institutions are specified as follows:

	30.6.2015	31.12.2014
Repurchase agreements with Central Bank	26	69
Deposits from credit institutions	23,991	25,727
Deposits from Central Bank and credit institutions	24,017	25,796

Deposits from customers

32. Deposits from customers are specified by type as follows:

	30.6.2015	31.12.2014
Demand deposits	436,060	421,332
Time deposits	130,618	108,115
Deposits from customers	566,678	529,447

33. Deposits from customers are specified by owners as follows:

	30.6.2015		31.12.2014	
	Amount	% of total	Amount	% of total
Central government and state-owned enterprises	10,693	2%	11,437	2%
Municipalities	11,272	2%	6,810	1%
Companies	341,787	61%	310,317	59%
Individuals	202,926	35%	200,883	38%
Deposits from customers	566,678	100%	529,447	100%

Debt issued and other borrowed funds

34. Specification of debt issued and other borrowed funds:

	30.6.2015	31.12.2014
Non-listed issued bonds	25,605	27,810
Listed issued bonds	79,092	66,460
Loans from credit institutions	3	2
Other debt securities	2,721	2,617
Debt issued and other borrowed funds	107,421	96,889

Amounts are in ISK million

Other liabilities

35. Specification of other liabilities:

	30.6.2015	31.12.2014
Accruals	3,590	3,250
Liabilities to retailers for credit card	28,257	22,639
Provision for effects of court rulings*	2,476	2,808
Provision for estimated losses from guarantees and others**	495	1,629
Capital gains tax	886	1,623
Unsettled securities transactions	13,897	1,798
Deferred income	186	192
Sundry liabilities	3,390	3,323
Other liabilities	53,177	37,262

	Provision for effects of court rulings*	Provision for estimated losses from guarantees and others**	Total
At 1 January 2015	2,808	1,629	4,437
Provision used during the period	(332)	-	(332)
New provisions and reversed provisions during the period	-	(1,134)	(1,134)
At 30 June 2015	2,476	495	2,971

Equity

36. Authorised share capital of the Bank is 10,000m ordinary shares of ISK 1 each. At 30.6.2015 paid up share capital totalled ISK 65,000m which is the total stated share capital of the Bank.

Total share capital:

	30.6.2015	31.12.2014
Ordinary share capital	10,000	10,000
Share premium account	55,000	55,000
Total share capital	65,000	65,000

Balance of custody assets

37. Balance of custody assets:

	30.6.2015	31.12.2014
Custody assets	699,054	666,715

Contingencies

38. **Contingencies**

Provisions

Foreign currency loans

Several rulings of the Supreme Court of Iceland during the period from 2010 to the first months of 2015 in relation to foreign currency-linked (“FX-linked”) loans have affected the Bank. Most important of these rulings was a ruling in June 2010 on the illegality of the principal of loans in ISK being linked to foreign currencies. Consequently, such loans could not carry Libor/Euribor interest rates.

The effects of these rulings and the subsequent corrections to the recalculations of illegal FX-linked loans have been reflected in the value of the loans in the Bank's Consolidated Financial Statements.

Amounts are in ISK million

38. Cont'd

The combined court rulings have reduced the uncertainty regarding which foreign currency loans are illegal and how they should be recalculated. The corrective process is in its final stages and the last remaining recalculation involves corporate financial leasing contracts.

The majority of the 10 remaining court cases involve loan contracts with minor deviations in terms from those cases that have already been ruled upon. The remaining cases involve FX-linked mortgage contracts which have repeatedly been found to be legal foreign currency denominated loan contracts. The cases involving loan contracts do not involve large sums and are unlikely to set any significant precedent as far as other loan contracts are concerned. As to the mortgage contracts, the Banks presumes that the courts have already ruled on the issues presented by the plaintiffs. The likelihood of the Bank having to perform another round of mortgage mass-recalculation is very slim. The Bank has recognised a provision of ISK 2,476 million in relation to foreign currency loans (see Note 35).

Contingent liabilities

Variable rate loans

The Consumer Agency (“Agency”) published in September 2014 its decision on a matter regarding the terms of, and information relating to the granting of, a consumer mortgage with interest reset terms granted by the Bank in 2005. The Agency found that the terms offered by the Bank and its predecessor, regarding the method and conditions of resetting interest to be in breach of Articles 6 and 9 of Act no. 121/1994 on Consumer Credit (superseded in November 2013). The Agency believes that the terms offer insufficient explanation on how or what can affect the decision on the revised interest rate. To support its decision, the Agency cites among other things a decision from 2009 by the Consumer Appellate Committee. The Bank has stated officially that it disagrees with the Agency's decision on the point that the law requires such detailed explanations on the outcome of a change in interest rate. The terms explicitly state the time period when the Bank can change the interest rate (every five years) and, moreover, that the borrower can settle the loan without a pre-settlement charge if the borrower is not content with the terms. The precedent quoted by the Agency did not involve such terms.

As previously mentioned, Article 12 of the former Consumer Credit Act no. 121/1994 allows the calculation of the Annual Percentage Rate of Charge ("ARPC") on the assumption that the price level, interest rate and other charges will remain unchanged to the end of the credit agreement. Thus, the Bank notified each borrower on the effects of variable interest rates, for example the payment schedule document did state: “Please note that this schedule is based on the present CPI, interest rate and service charges list in effect at Íslandsbanki at the time of issuance."

The Bank decided to postpone some scheduled interest rate changes following the Agency´s decision. Customers have the option of receiving better terms by restructuring their loans with the appropriate documentation, fully adapted to the new legislation on consumer loans. There is no doubt that similar terms were applied by all major financial institutions serving the housing loan market, including the Housing Financing Fund (“HFF”).

The decision of the Agency was appealed to the Consumer Appellate Committee which published its decision on 19 June. The Committee confirmed the decision of the Agency. The Bank has the option to put the matter before the courts which is currently under consideration. The consequences of a similar court verdict are not easily quantifiable seeing that the loan contract forms in question have been reducing greatly in numbers through refinancing and the general increases in the property market. The Bank made an offer to its customers in 2010 to postpone the interest rate increase until September 2013. Therefore, potential claims would only apply to a period of 24 months. The Bank considers it doubtful that the outcome will be unfavourable to the Bank and has not recognised a provision in relation to this matter.

Formal investigation by the Icelandic Competition Authority regarding an alleged violation of competition law by Íslandsbanki

The Icelandic Competition Authority (“ICA”) has initiated an investigation concerning alleged violations of the Competition Law by the Bank. Details of the investigation remain confidential.

The ICA has requested and received information from the Bank and has, following its review, sent the Bank an opposition document. The ICA considers the violations to be extensive, to have been in existence for a considerable period of time and to concern important markets. The opposition document is one stage in the processing of the case and does not comprise a final administrative decision.

The Bank strongly disagrees with the ICA's findings and has presented its objections. However, should the ICA's findings be final, sanctions may come into consideration, in accordance with Article 37 of the Competition Act. The Bank has not recognised a provision in relation to this matter.

Formal request for information by the EFTA Surveillance Authority into alleged unlawful state aid to Íslandsbanki

On 22 October 2013 the EFTA Surveillance Authority (“ESA”), following a complaint, formally requested information on alleged unlawful state aid granted to the Bank through long-term funding at favourable interest rates by the Central Bank of Iceland. The funding was in the form of an approximately 55 billion ISK bond with a ten year tenure, issued by the Bank, to the Central Bank. It is alleged that the funding was provided on terms more favourable than the then current market terms.

The Icelandic authorities and the Bank have sent all relevant information and their observations as per the ESA request, in order to determine whether or not the measures involve state aid based on the interpretation of Article 61 of the EEA Agreement, or if they qualify for an exemption under Article 61(2) or (3) of the EEA Agreement. Both parties state that the measures cannot be considered state aid within the meaning of Article 61(1) of the EEA Agreement, as the funding in question was provided at what has to be considered market rates at the time and were indeed favourable to the Central Bank. However, should ESA disagree, then the measures must be considered state aid compatible with the functioning of the EEA Agreement under Article 61(3) (b) of the EEA Agreement. If the funding is found to be an unlawful state aid, then it is expected that the Bank may have to reimburse the Central Bank with an amount equal to the difference between market terms, and the terms of the Bond. The Bank has not recognised a provision in relation to this matter.

38. Cont'd

The Depositors' and Investors' Guarantee Fund

In 2010, under a previous legislation, the Bank was required to grant the Depositors' and Investors' Guarantee Fund a declaration of guarantee in case the fund's assets did not meet the required minimum amount. Accordingly, the Bank issued a declaration of guarantee for future obligations amounting to ISK 3,724 million. The Bank did not recognise a liability in its financial statements in respect of this declaration which is now considered void. The amended legislation does not stipulate a requirement for such a declaration of guarantee. However, there remains some uncertainty as to its validity in relation to losses originated in the period from October 2008 to June 2012.

Contingent assets

Settlement of the 2011 Byr acquisition

The Bank acquired Byr hf. ("Byr"), a former savings bank, in 2011 from the Byr Winding-up Committee ("Committee") and the Icelandic Ministry of Finance and Economic Affairs ("Ministry"). According to standard practice, the Bank retained the right to re-evaluate the fair value of the net assets acquired and subsequently to demand a refund if the fair value of the net assets was not in line with what was presented in the entity's financial statements. A claim amounting to ISK 6,943 million plus interest was filed with the Committee in June 2013. The claim is filed as a priority claim, according to Article 110 of Act on Bankruptcy no. 21/1991, to be set off against a bond amounting to ISK 5,834 million with settlement dates in November 2014 and 2015. Payments on the bond have been, and will be, made with reservation. The Committee rejected the claim with a letter dated 30 September 2013. At a creditor's meeting in December 2013 it was decided that the Committee would refer the dispute to the District Court of Reykjavík. A formal claim amounting to ISK 911 million plus interest was filed with the Ministry on 24 September 2014. Both claims have now been filed with the District Court of Reykjavík. Furthermore, the District Court has appointed two independent professionals, at the request of Íslandsbanki, to perform a formal evaluation of the Bank's claim on the Ministry and the Committee. The evaluation is expected to be completed before the end of 2015. Court proceedings will therefore presumably commence in the fourth quarter of 2015. The Bank has not recognised any revenues relating to this claim.

A new Act, Stability Tax no. 60/2015, passed by Parliament in July 2015 may affect the Bank's claim on Byr, whereas the Byr estate may be liable to pay a one-off stability tax of 39% of total assets, providing the estate has not reached a composition agreement with its creditors before the end of 2015. This taxation, if payable, will rank before the Bank's claim. At present, it is uncertain if the Byr estate will seek composition.

Other

Indexed loans

Three court cases have been filed, one against the Bank and the others against the Housing Financing Fund ("HFF") and Landsbanki, challenging the legality of fixing the principal of a mortgage to the consumer price index ("CPI"). Such indexation has been the industry standard in Iceland for over 30 years, although the method of calculating the index has changed over the years with the most recent change being introduced in 1995. The court proceedings have lasted for almost three years, partly because the courts did support a motion by the plaintiffs in all the cases to seek an opinion of the EFTA court on some key issues.

The case against the Bank was based on the indexation being in violation of the EU Directive 93/13/EU ("Directive") on unfair terms in consumer loan contracts. As a secondary ground, the plaintiff sought to nullify the CPI increase by stating that the index was wrongfully applied as far as a proper forecast of the effect of the CPI was concerned, namely by using a zero-inflation forecast in calculating the APRC and the payment schedule. This, the plaintiff stated, was in violation of the procedure mandated by the Law on Consumer Credit then in force. The Directive does not prohibit the use of price indexation, provided that the consumer is adequately informed about the method of calculating the index and the factors that affect changes in the index. Thus, the case did not challenge the indexation as such, but only the context in which it was deployed. The scope of the Directive is limited to consumer loans. As the Directive does not require full harmonisation, it was not adopted by Iceland in its entirety. Instead, the existing contract law was amended by adding four new articles.

The EFTA Court published its opinion on 28 August 2014. In short, the Court stated that:

1. The EU Directive 93/13/EU does not generally prohibit contractual terms on the indexation of mortgage loans in contracts between a supplier and a consumer. It is for the referring court to assess whether the term at issue is deemed to be unfair.
2. The Directive does not limit the discretion of a European Economic Area State to determine, whether through legislation or by means of administrative regulation, the factors that may cause changes in a pre-determined index, such as the Icelandic consumer price index, as well as the methods for measuring those changes, provided they are explicitly described in the contract.
3. It is for the competent court to establish whether a particular contract term has been negotiated individually within the meaning of the Directive.
4. It is for the competent court to establish whether a contract term relating to the indexation of repayment instalments of a loan to finance real estate purchases must be regarded as having been explicitly and comprehensibly described to the consumer.
5. Article 6(1) of the Directive must be interpreted as meaning that, where a national court considers that a given term is unfair within the meaning of the Directive, that court must ensure that such a clause is not binding to the consumer provided that the contract is capable of continuing in existence without the unfair term in so far as, in accordance with the rules of domestic law, such a continuity of the contract is legally possible.

Thus, the general conclusion of the EFTA Court was that indexation is permissible in consumer contracts, but Icelandic courts must decide if it is properly applied and described to the consumer and on the consequences if it was not.

38. Cont'd

The District Court of Reykjavik ruled on the case against the Bank, as well as the HFF case, on 6 February 2015. It found that indexation was neither in violation of EU Directive 93/13/EEC, nor the Icelandic Act on Contracts no. 7/1936. Although not presented as an argument by the plaintiff in the beginning of the court proceedings, the Court also ruled on the compatibility of using zero-inflation forecast in calculating the APRC and the payment schedule. Like the EFTA Court and the Consumer Agency (see below), it found that although such a forecast was not satisfactory in light of the Act on Consumer Credit no. 121/1994, the increase of principal was nevertheless enforceable. The Court found that the plaintiff did not demonstrate in any way that the increase was beyond what the plaintiff should have expected, given the widespread and common use of indexation in the past decades. The ruling in the HFF case was founded on the same arguments.

The Supreme Court ruled on the Bank´s case on 13 May 2015. The Bank´s case was granted a simple and a speedy procedure because it only involved an enforcement dispute. The Court upheld the decision of the District Court, based mostly on the same arguments. In addition, as to the question on the use of zero-inflation, the Court acknowledged that some discrepancy was evident when the Directive on consumer loans was adopted to local law in 1994. Despite the fact that Icelandic law should be interpreted as close to the EU/EEA law as possible, such a rule could not change the meaning derived from the wording of the Icelandic law which states that it is permissible to assume when calculating the APRC and the payment schedule that the inflation will remain unchanged.

The Consumer Agency (“Agency”) published in February 2014 its decision on a matter regarding the terms of, and information relating to the granting of, a consumer price indexed (“CPI-linked”) mortgage by the Bank in 2005. The decision was based on the arguments later presented by the EFTA Court. The Consumer Appellate Committee decided on the case on 23 February 2015 along the same lines now as presented by EFTA Court. However, the committee did not agree with the Consumer Agency on the method of forecasting, stating that the two-month change in the CPI prior to the granting of the loan did not constitute a satisfactory foundation for forecasting. In light of the court decision described above, the decision of the Appellate Committee is of no consequence. The procedure in question has been upgraded following the implementation of the new Act on Consumer Credit no. 33/2013.

The Bank considers this matter concluded based on the ruling of the Supreme Court and therefore provisions are not applicable.

Events after the end of the reporting period

39. **Heads of Agreement**

On 3 July 2015, the Icelandic Parliament passed an Act imposing a one-off stability levy of 39% of total assets on financial undertakings previously operated as commercial banks or savings banks, that are currently in winding-up proceedings and have not concluded composition agreements by the end of 2015 that satisfy stability conditions set by the authorities. The objective of the Act is to facilitate liberation of the capital controls in Iceland and at the same time ensure stability in the interest of the general public. One of these financial undertakings is Glitnir hf. (Glitnir).

Based on the above and a proposal put forth by the Icelandic Ministry of Finance and Economic Affairs, the Bank entered into a Heads of Agreement with Glitnir and its subsidiaries ISB Holding ehf. and GLB Holding ehf., concerning the re-capitalisation of the Bank in order to facilitate the composition of Glitnir. The proposed re-capitalisation is expected to result in a reduction in Bank's equity corresponding to a total capital ratio of approximately 23%. The main components of the re-capitalisation will be as follows:

• In order to reduce the total capital ratio to 23%, the Bank will issue an unsecured ISK denominated bond amounting to ISK 36 billion with a 10 year maturity and subordinated notes amounting to ISK 16 billion with a minimum tenure of 10 years. The subordinated notes will be either in the form of Tier 2 notes or Alternative Tier 1.
The Bank will issue a new Tier 2 note to Glitnir replacing the existing Tier 2 note denominated in EUR with a minimum tenure of 10 years.
• The Bank will issue an ISK denominated bond to Glitnir with a tenure of 10 years to replace Glitnir's deposits in ISK currently held by the Bank.
• The Bank will issue Euro Medium Term Note ("EMTN") notes equivalent to an aggregate amount of approximately 40 billion, thereof 37 billion will come from deposits in foreign currency held by the Bank and 3 billion from the sale of Glitnir's domestic assets for foreign currency. The notes will be issued in tranches with a minimum tenure of 7 years.
• The Bank will pay a dividend of ISK 3 billion to the minority shareholder Icelandic State Financial Investments in the form of an ISK bond.
• Certain restrictions will be implemented on the transfer of the Bank's shares to domestic investors.
• All issues will be on market terms.

The Heads of Agreement is subject to approval by all relevant parties including the Icelandic Financial Supervisory Authority (FME) and the Central Bank of Iceland. The re-capitalisation is expected to come into effect in the fourth quarter of 2015 or early 2016.

Risk Management

40. Risk governance

The Bank is exposed to various risks and managing these risks is an integral part of the Bank's operations. More information about the Bank's risk management and risk assessment processes is available in the Pillar 3 Report 2014. The Pillar 3 Report is available at the Bank's website under investor relations: www.islandsbanki.is/pillar3report

Credit risk

41. Credit risk is defined as current or prospective risk to earnings and capital arising from an obligor's potential failure to meet the terms of any contract with the Bank or to otherwise fail to perform as agreed.

This risk comprises default risk, recovery risk, country risk, settlement risk and credit concentration risk.

Credit concentration risk is the significantly increased risk that is driven by common underlying factors, e.g. sector, economy, geographical location, type of financial instrument or due to connections or relations among counterparties. This includes large individual exposures to parties under common control and significant exposures to groups of counterparties whose likelihood of default is driven by common underlying factors.

Credit risk arises principally from the Bank's loans and advances to customers and other banks but also from balances with the Central Bank and off-balance sheet items such as guarantees, loan commitments and derivatives.

42. Maximum credit exposure

The Bank's credit risk exposure comprises both on-balance sheet and off-balance sheet items. Maximum exposure to credit risk for on-balance sheet assets is the net carrying amount as reported in the statement of financial position before the collective impairment allowance is subtracted, see note 24. The maximum exposure for off-balance sheet items is the amount that the Bank might have to pay out against financial guarantees and loan commitments, less provisions the Bank has made because of these items. The maximum credit exposure for a derivative contract is calculated by adding future credit exposure to the market value of the contract as described in Annex III of the European Parliament directive 2006/48/EC (Basel II).

The industry breakdown shows the Bank's credit exposure by industry classification. The breakdown follows an internal industry classification which is based on the Icelandic ISAT2008 that derives from the European NACE Rev. 2 classification standard.

The Bank's credit exposure, before taking account of any collateral held or other credit enhancements, is as follows:

Credit risk exposure

42. Cont'd

Maximum credit exposure 30.6.2015

	Individuals	Central governments	Commerce and services	Construction	Energy	Financial services	Industrial and transportation	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	126,900	-	-	-	-	-	-	-	-	-	126,900
Derivatives	22	-	32	22	1,125	1,594	30	26	279	41	16	3,187
Bonds and debt instruments	-	77,738	1,499	-	1,016	3,575	279	877	6	284	-	85,274
Loans to credit institutions	-	-	-	-	-	52,139	-	-	-	-	-	52,139
Loans to customers:	259,792	-	90,865	19,764	3,791	106	66,594	18,346	11,524	103,320	82,188	656,290
Overdrafts	12,886	-	10,415	3,898	75	51	6,457	581	597	2,773	1,724	39,457
Credit cards	14,981	-	1,359	164	5	23	409	32	129	45	41	17,188
Mortgages	184,994	-	-	-	-	-	-	-	-	-	-	184,994
Leases	10,342	-	22,431	2,324	-	1	6,416	217	156	1,250	245	43,382
Other loans	36,589	-	56,660	13,378	3,711	31	53,312	17,516	10,642	99,252	80,178	371,269
Off-balance sheet items:												
Financial guarantees	1,448	-	3,454	2,556	-	1,669	1,717	41	29	142	517	11,573
Undrawn loan commitments	-	-	3,112	6,615	9,457	-	10,480	3,162	6,223	2,547	2,150	43,746
Undrawn overdraft	8,574	-	9,480	1,626	31	4,180	2,453	231	2,868	1,328	1,481	32,252
Credit card commitments	24,292	3	3,639	513	30	162	913	167	795	204	149	30,867
Total maximum credit exposure	294,128	204,641	112,081	31,096	15,450	63,425	82,466	22,850	21,724	107,866	86,501	1,042,228

Amounts are in ISK million

42. Cont'd

Maximum exposure 31.12.2014

	Individuals	Central governments	Commerce and services	Construction	Energy	Financial services	Industrial and transportation	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	103,389	-	-	-	-	-	-	-	-	-	103,389
Derivatives	28	-	423	17	805	2,644	28	16	121	49	-	4,131
Bonds and debt instruments	-	79,834	-	-	291	5,785	-	890	251	296	-	87,347
Loans to credit institutions	-	-	-	-	-	35,072	-	-	-	-	-	35,072
Loans to customers:	262,848	-	79,658	18,751	7,315	121	61,878	13,911	12,216	99,540	81,412	637,650
Overdrafts	12,751	-	10,075	3,432	34	60	4,762	549	1,343	2,164	2,058	37,228
Credit cards	15,583	-	1,334	156	4	23	355	29	132	43	31	17,690
Mortgages	186,583	-	-	-	-	-	-	-	-	-	-	186,583
Leases	10,241	-	15,559	2,581	-	1	5,960	213	196	1,249	231	36,231
Other loans	37,690	-	52,690	12,582	7,277	37	50,801	13,120	10,545	96,084	79,092	359,918
Off-balance sheet items:												
Financial guarantees	1,444	-	2,318	2,281	-	1,170	1,134	39	39	166	533	9,124
Undrawn loan commitments	-	-	996	8,248	5,816	-	2,639	1,400	7,247	4,234	443	31,023
Undrawn overdraft	9,216	-	7,459	1,618	23	3,673	2,561	187	1,874	975	1,361	28,947
Credit card commitments	23,183	-	3,455	477	31	167	906	166	818	197	144	29,544
Total maximum credit exposure	296,719	183,223	94,309	31,392	14,281	48,632	69,146	16,609	22,566	105,457	83,893	966,227

Amounts are in ISK million

43. Credit exposure covered by collateral

Collateral and other credit mitigants vary between types of obligors and credit facilities. Loans to credit institutions are usually unsecured. For loans to individuals the principal collateral taken is residential property against mortgages. In the case of corporate entities the Bank takes a charge over assets such as real estate, fishing vessels, cash and securities and as well as other collateral including accounts receivables, inventory, vehicles and equipment. Loans to government entities and to municipalities are more often than not unsecured. Derivative exposures are generally made under ISDA master agreements with Credit Support Annex or corresponding terms with pledged collateral in the form of cash and government bonds.

In some cases the Bank uses guarantees as a credit enhancement but since guarantees effectively transfer credit risk from one counterparty to another they do not represent a reduction in maximum exposure to credit risk. Covenants in loan agreements are also an important credit enhancement but do not reduce maximum credit exposure.

Valuation of collateral is based on market price, official valuation for tax purposes or expert opinion of the Bank's employees, depending on availability. In the case of fishing vessels the associated fishing quota is included in the valuation. Collateral is allocated according to claim value of loans, not carrying amount, and is measured without including the effect of overcollateralisation. This means that if some loans have collateral values in excess of their claim value, then the excess is removed in order to reflect the Bank's actual maximum exposure to credit risk. The total value of pledged assets can thus be higher than the cover indicates.

An estimate of the collateral held by the Bank against credit exposure is shown below:

At 30 June 2015

	Real estate	Fishing vessels	Cash & securities	Vehicles & equipment	Other collateral	Credit exposure covered by collateral
Derivatives	-	-	2,847	-	-	2,847
Loans and commitments to customers:	403,777	72,104	6,802	38,743	24,332	545,758
Individuals	212,129	32	510	9,808	1	222,480
Commerce and services	43,760	439	329	21,153	9,449	75,130
Construction	15,672	249	71	1,683	83	17,758
Energy	2,930	-	414	-	99	3,443
Financial services	40	-	23	1	-	64
Industrial and transportation	22,124	1	306	5,291	11,816	39,538
Investment companies	5,811	-	3,799	264	153	10,027
Public sector and non-profit organisations	1,037	-	9	141	-	1,187
Real estate	96,797	-	1,060	155	600	98,612
Seafood	3,477	71,383	281	247	2,131	77,519
Total	403,777	72,104	9,649	38,743	24,332	548,605

At 31 December 2014

	Real estate	Fishing vessels	Cash & securities	Vehicles & equipment	Other collateral	Credit exposure covered by collateral
Derivatives	-	-	2,500	-	-	2,500
Loans and commitments to customers:	391,139	74,032	5,991	33,473	24,174	528,809
Individuals	213,550	41	469	9,901	12	223,973
Commerce and services	40,484	290	472	14,525	8,838	64,609
Construction	13,217	269	59	2,473	1,592	17,610
Energy	1,260	-	411	1	152	1,824
Financial services	39	-	32	1	-	72
Industrial and transportation	16,487	-	148	5,760	7,914	30,309
Investment companies	4,973	-	3,434	248	2,642	11,297
Public sector and non-profit organisations	1,510	-	11	179	-	1,700
Real estate	94,859	-	650	143	564	96,216
Seafood	4,760	73,432	305	242	2,460	81,199
Total	391,139	74,032	8,491	33,473	24,174	531,309

For the six months ended 30 June 2015 39 Amounts are in ISK million

44. Credit quality of financial assets

Loans are classified as impaired loans if there is objective evidence that an impairment loss has been incurred on loans, their carrying amount is reduced through the use of an allowance account to the present value of expected future cash flows, discounted at their effective interest rate.

The full carrying amount of all loans which give rise to individual impairment is included in impaired loans, even if parts are covered by collateral. The collective impairment has not been subtracted from the carrying amount here.

At 30 June 2015

	Neither past due nor impaired	Past due but not impaired	Classified as impaired	Total carrying amount
Cash and balances with Central Bank	126,900	-	-	126,900
Derivatives	3,187	-	-	3,187
Bonds and debt instruments	85,274	-	-	85,274
Loans to credit institutions	52,139	-	-	52,139
Loans to customers:	614,469	31,009	10,812	656,290
Individuals	235,961	19,219	4,612	259,792
Commerce and services	86,209	3,284	1,372	90,865
Construction	17,584	1,274	906	19,764
Energy	3,791	-	-	3,791
Financial services	74	-	32	106
Industrial and transportation	64,698	1,228	668	66,594
Investment companies	17,718	498	130	18,346
Public sector and non-profit organisations	11,492	32	-	11,524
Real estate	99,228	3,657	435	103,320
Seafood	77,714	1,817	2,657	82,188
Total	881,969	31,009	10,812	923,790

At 31 December 2014

	Neither past due nor impaired	Past due but not impaired	Classified as impaired	Total carrying amount
Cash and balances with Central Bank	103,389	-	-	103,389
Derivatives	4,131	-	-	4,131
Bonds and debt instruments	87,347	-	-	87,347
Loans to credit institutions	35,072	-	-	35,072
Loans to customers:	595,903	27,619	14,128	637,650
Individuals	237,253	18,752	6,843	262,848
Commerce and services	75,572	2,253	1,833	79,658
Construction	17,319	914	518	18,751
Energy	7,315	-	-	7,315
Financial services	84	37	-	121
Industrial and transportation	60,295	881	702	61,878
Investment companies	12,500	766	645	13,911
Public sector and non-profit organisations	12,165	51	-	12,216
Real estate	96,905	1,969	666	99,540
Seafood	76,495	1,996	2,921	81,412
Total	825,842	27,619	14,128	867,589

Amounts are in ISK million

45. Neither past due nor impaired loans

The Bank uses internal rating models to assess the default probability of corporate and retail customers. The models assign each customer to one of ten risk classes. One risk class is for customers in default (risk class 10), and nine risk classes are for performing customers (risk classes 1-9). Risk classes are assigned on customer level and not facility level.

The rating of corporate customers is based on a company's most recent financial statement, together with a qualitative assessment of its management, market position and industry sector.

For retail customers the Bank uses two different statistical rating models. One model is for individuals and another is for small companies with a total exposure to the Bank of less than ISK 150 million. These models are behavioural scoring models and use information about a customer's payment history, amount of debt and deposits, and demographic variables to assess the probability that a customer will default on any of his obligations within 12 months of the rating assessment.

The table below shows loans that are neither past due nor impaired aggregated in five customer groups based on the default probability. Group 1-4 represents low risk, group 5-6 moderate risk, group 7-8 increased risk, risk class 9 high risk, and risk class 10 represents customers in default. Unrated are loans originating from subsidiaries of Íslandsbanki that do not have rating models, in addition to loans that are yet to be rated or with an expired rating.

Note that the same customer can have loans that are more than 90 days past due or impaired, and at the same time other loans that are neither past due nor impaired. Those customers will be in risk class 10 and their loans that are neither past due nor impaired are included in the table below.

At 30 June 2015

	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	Total
Loans to customers							
Individuals	10,853	87,275	89,189	42,571	2,639	3,434	235,961
Commerce and services	13,591	50,134	17,022	3,264	199	1,999	86,209
Construction	344	8,354	7,822	955	108	1	17,584
Energy	359	3,387	45	-	-	-	3,791
Financial services	42	12	5	15	-	-	74
Industrial and transportation	23,835	33,241	6,455	1,110	57	-	64,698
Investment companies	2,094	6,666	5,940	1,857	143	1,018	17,718
Public sector and non-profit organisations	6,022	5,254	208	6	-	2	11,492
Real estate	31,167	45,014	19,309	2,216	1,198	324	99,228
Seafood	36,858	28,208	9,321	471	2,454	402	77,714
Total	125,165	267,545	155,316	52,465	6,798	7,180	614,469

At 31 December 2014

	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	Total
Loans to customers							
Individuals	10,432	91,744	84,838	43,101	3,659	3,479	237,253
Commerce and services	15,240	35,903	18,182	3,891	1,873	483	75,572
Construction	381	6,698	7,032	846	2,321	41	17,319
Energy	3,877	3,396	42	-	-	-	7,315
Financial services	50	13	19	1	-	1	84
Industrial and transportation	21,850	30,334	6,822	1,128	161	-	60,295
Investment companies	1,143	7,013	2,604	1,450	25	265	12,500
Public sector and non-profit organisations	7,094	4,815	248	6	-	2	12,165
Real estate	31,145	46,626	14,369	2,686	2,012	67	96,905
Seafood	39,777	28,171	6,176	746	1,625	-	76,495
Total	130,989	254,713	140,332	53,855	11,676	4,338	595,903

Amounts are in ISK million

46. Forbearance

Forbearance measures which the Bank can make available include temporary payment holidays, extension of loan terms, capitalisation of arrears and waiving of covenants. In many cases these measures are precursors to the more formal restructuring process.

47. Past due but not impaired loans

Past due but not impaired loans are loans where contractual interest or principal payments have passed due date without the obligor making full payment, but where specific impairment is not appropriate. The reason is usually that contractual payments are eventually expected to be fulfilled or these loans are expected to be restructured without any loss to the Bank. In some cases, loss is avoided because of the difference between the claim value and the carrying amount resulting from the deep discount of the acquired loan portfolio. In other cases, there is sufficient collateral.

Amounts reported as loans past due refer to the total loan exposure and not only the payment or sum of payments that are past due. Payments three days in arrears or less are not considered to be past due and the corresponding loans are therefore omitted here. Past due but not impaired loans are as follows:

At 30 June 2015

	Past due 4-30 days	Past due 31-60 days	Past due 61-90 days	Past due more than 90 days	Total past due loans
Loans to customers:					
Individuals	8,578	4,177	1,664	4,800	19,219
Commerce and services	2,130	688	205	261	3,284
Construction	384	238	39	613	1,274
Energy	-	-	-	-	-
Financial services	-	-	-	-	-
Industrial and transportation	633	385	67	143	1,228
Investment companies	265	31	25	177	498
Public sector and non-profit organisations	9	5	18	-	32
Real estate	2,732	479	92	354	3,657
Seafood	668	428	59	662	1,817
Total	15,399	6,431	2,169	7,010	31,009

At 31 December 2014

	Past due 4-30 days	Past due 31-60 days	Past due 61-90 days	Past due more than 90 days	Total past due loans
Loans to customers:					
Individuals	8,331	3,458	680	6,283	18,752
Commerce and services	1,144	516	256	337	2,253
Construction	429	116	76	293	914
Energy	-	-	-	-	-
Financial services	37	-	-	-	37
Industrial and transportation	390	156	104	231	881
Investment companies	145	363	47	211	766
Public sector and non-profit organisations	38	6	7	-	51
Real estate	914	602	179	274	1,969
Seafood	1,203	162	37	594	1,996
Total	12,631	5,379	1,386	8,223	27,619

Amounts are in ISK million

48. Large exposure disclosure

When the Bank's total exposure to a group of connected clients is 10% or higher of the Bank's capital base it is considered a large exposure. Both on-balance sheet and off-balance sheet items from all types of financial instruments are included in the exposure as defined by FME rules 625/2013. The Bank has internal criteria that define connections between clients. These criteria reflect the Bank's interpretation of Article (1)(a) of law 161/2002 on Financial Undertakings, where groups of connected clients are defined. In line with the law, the capital base from 30 June 2015 is used.

The exposure is evaluated both before and after credit risk mitigating effects eligible according to the FME rules. After mitigating effects, the Bank has currently one large exposure which is 14% of its capital base. No large exposure is above the maximum 25% single large exposure limit set by the law.

The following tables show the Bank's large exposures as a percentage of the Bank's capital base, before and after eligible credit risk mitigating effects. Note that group references might change between reporting periods, i.e. Group 1 might not be the same group in the two tables.

	30.6.2015	
Client groups	Before	After
Group 1	81%	0%
Group 2	14%	14%

	31.12.2014	
Client groups	Before	After
Group 1	69%	0%
Group 2	12%	12%

Amounts are in ISK million

Liquidity Risk

49. The Bank defines liquidity risk as the risk of not being able to fund its financial obligations or planned growth, or only being able to do so substantially above the prevailing market cost of funds.

Liquidity risk management

The Bank's main source of funding is customer deposits. The Bank's Treasury is responsible for the Bank's funding and liquidity management within the limits approved by the Board and the Asset and Liability Committee. The Interbank desk manages the Bank's intraday liquidity.

Risk management is responsible for measuring, monitoring and reporting on the Bank's liquidity position.

The Bank's liquidity risk policy assumes that the Bank has at all times sufficient liquidity to meet liabilities and other obligations over the next twelve months.

The tables below show the contractual payments of principal and interest for the Bank's financial liabilities. Thus, the total figures for each liability class are higher than the respective balance sheet amount. Cash flows for payments of unknown nature, such as for floating rate, CPI-linked or foreign currency denominated instruments, are based on internal yield curves and forecasts.

For dated financial liabilities the amounts are grouped into maturity buckets according to contractual maturities of principal and estimated contractual payments of interest. For demand deposits or other non-dated liabilities, the figures are grouped according to the first possible required payment date.

In the table below the total amount for loans to customers is shown before collective impairment allowance and is therefore higher than the total amount shown in the financial statement.

Maturity analysis 30 June 2015

Financial liabilities	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Short positions	2,097	1,819	-	-	278	-	-	2,097
Deposits from CB and credit institutions	24,017	20,113	3,985	-	-	-	-	24,098
Deposits from customers	566,678	358,837	78,497	95,098	20,595	29,445	-	582,472
Debt issued and other borrowed funds	107,421	3	3,977	32,768	66,082	18,698	-	121,528
Subordinated loans	20,336	-	258	798	25,376	-	-	26,432
Other financial liabilities	61,560	47,344	7,147	4,493	2,575	-	-	61,559
Total financial liabilities	782,109	428,116	93,864	133,157	114,906	48,143	-	818,186

Off-balance sheet liabilities show the amount of contractual obligations that the Bank has taken towards customers, either by committing to lend out money in the future or as third party guarantees. The amounts shown reflect the maximum amount, not taking into account the Bank's ability to reduce overdraft or credit card limits before the current undrawn amount is fully utilised by the customer. These obligations all fall into the first time bucket since contractually, on a case-by-case basis, the Bank could be required to fulfil these obligations instantaneously.

Off-balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial guarantees	11,573	-	-	-	-	-	11,573
Undrawn loan commitments	43,746	-	-	-	-	-	43,746
Undrawn overdrafts	32,252	-	-	-	-	-	32,252
Credit card commitments	30,867	-	-	-	-	-	30,867
Total	118,438	-	-	-	-	-	118,438
Total non-derivative financial liabilities and off-balance sheet liabilities	546,554	93,864	133,157	114,906	48,143	-	936,624

The following page shows the contractual cash flow of the Bank's derivative liabilities, i.e. derivatives that have a negative carrying amount at the date of reporting. Derivatives with a positive carrying amount are detailed separately. For derivatives settled on a gross basis, the cash flow for both legs of the derivative is shown, since netting cannot be applied upon settlement.

Amounts are in ISK million

49. Cont'd

Derivative financial liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	6,174	23,312	58,580	3,357	-	91,423
Outflow	-	(6,226)	(25,380)	(59,352)	(3,938)	-	(94,896)
Total	-	(52)	(2,068)	(772)	(581)	-	(3,473)
Net settled derivatives	-	(614)	-	-	-	-	(614)
Total	-	(666)	(2,068)	(772)	(581)	-	(4,087)

Maturity classification of assets is based on contractual maturity. For loans that were acquired at a deep discount and have not yet been restructured, the contractual amount is scaled to reflect the carrying amount of the claim. For bonds and debt instruments in the banking book the maturity classification is based on contractual maturity dates while for bonds and debt instruments held for trading the maturity classification is based on the estimated liquidation time of the asset.

Financial assets	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with CB	126,900	33,620	93,280	-	-	-	-	126,900
Bonds and debt instruments	85,274	1,048	19,812	17,204	42,739	4,471	-	85,274
Shares and equity instruments	11,041	-	-	-	-	-	11,041	11,041
Loans to credit institutions	52,139	33,411	18,728	-	-	-	-	52,139
Loans to customers	653,728	5,612	71,198	58,463	192,717	325,738	-	653,728
Other financial assets	20,516	13,895	806	1,587	55	9	4,164	20,516
Total financial assets	949,598	87,586	203,824	77,254	235,511	330,218	15,205	949,598

Derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	11,130	16,642	16,049	20	-	43,841
Outflow	-	(10,803)	(15,948)	(15,720)	(11)	-	(42,482)
Total	-	327	694	329	9	-	1,359
Net settled derivatives	-	349	-	-	-	-	349
Total	-	676	694	329	9	-	1,708

The tables below show the comparative amounts for financial assets and liabilities at year-end 2014.

Maturity analysis 31 December 2014

Financial liabilities	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Short positions	686	686	-	-	-	-	-	686
Deposits from CB and credit institutions	25,796	22,331	3,054	434	-	-	-	25,819
Deposits from customers	529,447	341,454	80,037	72,685	20,602	28,342	-	543,120
Debt issued and other borrowed funds	96,889	2	4,255	18,940	71,141	14,365	-	108,703
Subordinated loans	21,306	-	-	837	27,292	-	-	28,129
Other financial liabilities	45,395	32,715	5,108	7,868	(296)	-	-	45,395
Total financial liabilities	719,519	397,188	92,454	100,764	118,739	42,707	-	751,852

For the six months ended 30 June 2015 45 Amounts are in ISK million

49. Cont'd

Off-balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial guarantees	9,124	-	-	-	-	-	9,124
Undrawn loan commitments	31,023	-	-	-	-	-	31,023
Undrawn overdrafts	28,947	-	-	-	-	-	28,947
Credit card commitments	29,544	-	-	-	-	-	29,544
Total	98,638	-	-	-	-	-	98,638
Total non-derivative financial liabilities and off-balance sheet liabilities	495,826	92,454	100,764	118,739	42,707	-	850,490

Derivative financial liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	2,371	7,758	56,798	-	-	66,927
Outflow	-	(2,292)	(8,165)	(60,437)	-	-	(70,894)
Total	-	79	(407)	(3,639)	-	-	(3,967)
Net settled derivatives	-	(133)	-	-	-	-	(133)
Total	-	(54)	(407)	(3,639)	-	-	(4,100)

Financial assets	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with CB	103,389	22,546	80,843	-	-	-	-	103,389
Bonds and debt instruments	87,347	1,076	20,645	25,298	35,209	5,119	-	87,347
Shares and equity instruments	10,531	-	-	-	-	-	10,531	10,531
Loans to credit institutions	35,072	23,185	11,837	50	-	-	-	35,072
Loans to customers	634,799	5,481	73,629	55,235	176,402	326,903	-	637,650
Other financial assets	7,619	1,703	825	1,865	54	27	3,144	7,619
Total financial assets	878,757	53,991	187,779	82,448	211,665	332,049	13,675	881,607

Derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	6,387	11,738	35,515	1,710	-	55,350
Outflow	-	(5,885)	(11,063)	(34,724)	(1,975)	-	(53,647)
Total	-	502	675	791	(265)	-	1,703
Net settled derivatives	-	242	-	-	-	-	242
Total	-	744	675	791	(265)	-	1,945

As a part of managing liquidity risk, the Bank holds a portfolio of liquid assets to meet unexpected outflow of funds or a temporary shortage in access to new funding. These assets are subject to strict criteria with respect to credit quality, liquidation time and price volatility. The table below shows the composition and amount of the Bank's liquidity back-up at the end of June 2015 and end of 2014.

Composition and amount of liquidity back-up	30.6.2015	31.12.2014
Cash and balances with the Central Bank	126,900	103,455
Domestic bonds eligible as collateral against borrowing at Central Bank	31,455	29,478
Foreign government bonds	37,955	46,593
Short-term placements with credit institutions	51,209	34,006
Composition and amount of liquidity back-up	247,519	213,532

Amounts are in ISK million

Market risk

50. The Bank defines market risk as the current or prospective risk to earnings and capital arising from adverse movements in the level or volatility of prices of market instruments, such as those that arise from changes in interest rates, equity prices, commodity prices and foreign exchange rates.

Market risk management
The Bank's market risk appetite is determined by the Board of Directors. The Asset and Liability Committee (ALCO) decides on limits for portfolios and products in accordance with the market risk policy approved by the Board. Risk management is responsible for monitoring and reporting on the Bank's overall market risk positions and compliance to limits. The objective of market risk management is to manage and control market risk exposures within acceptable parameters.

The Bank separates exposures to market risk into trading book and banking book (non-trading portfolios). The Bank's primary sources of market risk in the trading portfolio are shares, debt instruments and foreign currency positions. All financial assets and liabilities in the trading portfolio are recognised at fair value and all resulting changes are immediately reflected in the income statement. Market risk in the banking book is mainly due to mismatches in interest rate terms and denomination currency of assets and liabilities. These mismatches are reported to management and are subject to regulatory and internal limits.

Interest rate risk

51. Interest rate risk is defined as the current or prospective risk to earnings or capital arising from adverse movements in interest rates.

The Bank uses sensitivity measures like Basis Point Value (BPV) to measure and manage risk arising from its fixed income exposures. The BPV measures the effect of a 0.01 percentage point upward parallel shift in the yield curve on the fair value of these exposures.

52. Interest rate risk in trading portfolios

The fixed income trading unit invests mainly in government bonds and bonds issued by the Housing Financing Fund (HFF), which are guaranteed by the Icelandic government. These positions can include short positions. Government bonds are either indexed to the Icelandic Consumer Price Index (CPI) or non-indexed, with duration up to 10 years. HFF bonds are CPI linked and have duration up to 13 years. All bond trading positions are subject to BPV limits, both intraday and end-of-day. In addition to BPV limits short and long positions in each instrument are subject to separate limits. Risk Management monitors these limits and reports all breaches to ALCO.

Note that in the table below the total market value of long and short positions may not be exactly the same as reported in note 6. The reason for this difference is that in note 6 the net positions in each security are summed up while the table below ignores both netting of long and short positions in specific securities between different portfolios and hedge positions against derivative contracts.

Trading bonds and debt instruments, long positions		30.6.2015			31.12.2014	
	MV	Duration	BPV	MV	Duration	BPV
Indexed	1,189	9.03	(1.07)	1,772	8.03	(1.42)
Non-indexed	42,992	0.55	(2.35)	48,260	0.41	(1.96)
Total	44,181	0.78	(3.42)	50,032	0.68	(3.38)

Trading bonds and debt instruments, short positions		30.6.2015			31.12.2014	
	MV	Duration	BPV	MV	Duration	BPV
Indexed	1,672	7.53	1.26	-	-	-
Non-indexed	1,487	4.06	0.60	73	7.39	0.05
Total	3,159	5.90	1.86	73	7.39	0.05
Net position of trading bonds and debt instruments	41,022	0.38	(1.56)	49,959	0.67	(3.33)

Amounts are in ISK million

53. Interest rate risk in the banking book

Interest rate risk in the banking book arises from the Bank’s core banking activities. The main source of this type of interest rate risk is the risk of loss from fluctuations in future cash flows or fair value of financial instruments as interest rates change over time, reflecting the fact that the Bank's assets and liabilities are of different maturities and are priced relative to different interest rates.

The Bank holds a government bond designated at fair value amounting to ISK 30.6 billion (31 December 2014: ISK 30.6 billion). The bond pays floating rates and carries relatively low interest rate risk.

The Bank uses traditional measures for assessing the sensitivity of the Bank's financial assets, financial liabilities and earnings to changes in the underlying interest rates.

In the table below the total amount for loans to customers is shown before collective impairment allowance is subtracted and is therefore not the same as the total amount shown in the financial statement. Loans with specific impairment have been placed in the category 0-3 months since such loans bear no interest rate risk until possibly after debt restructuring.

Banking book interest rate adjustment periods on 30 June 2015

Assets	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
Balances with Central Bank	126,900	-	-	-	-	-	126,900
Bonds and debt instruments	32,088	458	1,301	108	426	185	34,566
Loans to credit institutions	52,136	3	-	-	-	-	52,139
Loans to customers	464,067	35,764	35,251	110,471	1,519	9,218	656,290
Total assets	675,191	36,225	36,552	110,579	1,945	9,403	869,895
Off-balance sheet items..	79,684	16,416	2,497	3,133	-	-	101,730
Liabilities							
Deposits from CB and credit institutions	24,017	-	-	-	-	-	24,017
Deposits from customers	554,175	1,214	1,062	9,379	848	-	566,678
Debt issued and other borrowed funds	5,189	40,756	29,499	16,540	11,266	4,171	107,421
Subordinated loans	-	20,336	-	-	-	-	20,336
Total liabilities	583,381	62,306	30,561	25,919	12,114	4,171	718,452
Off-balance sheet items	74,833	1,473	9,823	24,334	3,024	-	113,487
Net interest gap on 30 June 2015	96,661	(11,138)	(1,335)	63,459	(13,193)	5,232	139,686

Amounts are in ISK million

53. Cont'd

Banking book interest rate adjustment periods on 31 December 2014

Assets	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
Balances with Central Bank	103,389	-	-	-	-	-	103,389
Bonds and debt instruments	31,119	-	67	1,230	291	367	33,074
Loans to credit institutions	35,072	-	-	-	-	-	35,072
Loans to customers	451,191	47,768	29,963	97,052	1,868	9,809	637,650
Total assets	620,771	47,768	30,030	98,282	2,159	10,176	809,185
Off-balance sheet items	68,186	7,508	21,649	112	-	-	97,455
Liabilities							
Deposits from CB and credit institutions	25,375	421	-	-	-	-	25,796
Deposits from customers	514,898	3,643	1,030	2,383	7,493	-	529,447
Debt issued and other borrowed funds	17,723	9,403	22,760	34,421	12,582	-	96,889
Subordinated loans	21,306	-	-	-	-	-	21,306
Total liabilities	579,302	13,467	23,790	36,804	20,075	-	673,438
Off-balance sheet items	77,732	3,272	7,701	17,850	-	-	106,555
Net interest gap on 31 December 2014	31,923	38,537	20,188	43,740	(17,916)	10,176	126,647

Amounts are in ISK million

Currency risk

54. Currency risk is the risk that earnings or capital may be negatively affected from the fluctuations of foreign exchange rates, due to transactions in foreign currencies or due to a mismatch in the currency composition of assets or liabilities.

The analysis of the Bank's foreign currency exposure presented below is based on the contractual currency of the underlying balance sheet items. Additionally, there are off-balance sheet items that carry currency risk and are included in the total currency imbalance. The off-balance sheet amounts below represent the notional amounts of derivatives and unsettled spot agreements. The tables below summarise the Bank's exposure to currency risk at 30 June 2015 and 31 December 2014, based on contractual currencies and off-balance sheet items, but excluding assets categorised as held-for-sale.

There is uncertainty regarding the impact on the financial market following the liberation of capital controls in Iceland. This is taken into account in the Bank's risk management. The Bank holds a strategic long position in foreign currencies and can easily convert foreign currencies into ISK.

The Bank's net currency imbalance is likely to diminish following the completion of the proposed re-capitalisation (see Note 39). The anticipated composition of the financial undertakings that are currently in winding-up proceedings will further reduce the uncertainty surrounding the liberation of the capital controls.

Currency analysis 30 June 2015

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	Other	Total
Cash and balances with CB........	404	282	150	51	10	56	79	99	47	1,178
Bonds and debt instruments.......	24,308	12,763	-	-	-	1,599	-	-	1,062	39,732
Shares and equity instrum..........	209	279	-	-	-	-	1	-	-	489
Loans to credit institutions..........	19,596	15,163	954	400	2,285	334	627	1,478	372	41,209
Loans to customers...................	65,254	24,561	6,782	7,901	7,296	289	11,421	1,232	132	124,868
Other assets...............................	873	2,161	230	2	4	61	26	21	68	3,446
Total assets	110,644	55,209	8,116	8,354	9,595	2,339	12,154	2,830	1,681	210,922
Liabilities										
Deposits from credit institut........	562	306	29	476	582	-	1	-	-	1,956
Deposits from customers	49,524	30,510	6,190	3,241	2,269	1,045	4,447	1,079	1,440	99,745
Borrowings.................................	14,690	-	-	-	-	20,013	-	-	-	34,703
Subordinated loans	20,336	-	-	-	-	-	-	-	-	20,336
Other liabilities...........................	4,806	6,513	1,152	4	102	187	90	69	268	13,191
Total liabilities	89,918	37,329	7,371	3,721	2,953	21,245	4,538	1,148	1,708	169,931
On-balance sheet imbalance	20,726	17,880	745	4,633	6,642	(18,906)	7,616	1,682	(27)	40,991
Off-balance sheet items										
Off-balance sheet assets	23,341	22,012	1,407	903	-	19,349	700	1,418	1,493	70,623
Off-balance sheet liabilities	34,575	36,365	114	4,942	6,517	23	5,806	-	1,134	89,476
Net off-balance sheet items	(11,234)	(14,353)	1,293	(4,039)	(6,517)	19,326	(5,106)	1,418	359	(18,853)
Net currency imbalance on 30 June 2015................	9,492	3,527	2,038	594	125	420	2,510	3,100	332	22,138

For the six months ended 30 June 2015 50 Amounts are in ISK million

54. Cont'd

Currency analysis 31 December 2014

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	Other	Total
Cash and balances with CB	263	168	95	30	9	43	50	83	26	767
Bonds and debt instruments	29,322	9,323	-	-	-	4,109	1,708	1,036	1,095	46,593
Shares and equity instrum..........	203	257	-	1	-	-	-	-	-	461
Loans to credit institutions	9,092	12,091	2,137	3,911	1,238	1,313	1,442	2,027	349	33,600
Loans to customers	62,131	25,654	6,124	7,869	7,206	308	8,943	1,387	352	119,974
Other assets	318	1,672	132	1	37	44	10	23	34	2,271
Total assets	101,329	49,165	8,488	11,812	8,490	5,817	12,153	4,556	1,856	203,666
Liabilities										
Deposits from credit institut........	140	16	13	-	13	-	1	-	-	183
Deposits from customers	39,200	26,309	5,385	2,364	1,586	1,164	6,777	1,129	1,892	85,806
Borrowings..................................	15,572	-	-	-	-	13,212	-	-	-	28,784
Subordinated loans	21,306	-	-	-	-	-	-	-	-	21,306
Other liabilities	3,704	5,792	763	-	117	66	35	46	363	10,886
Total liabilities	79,922	32,117	6,161	2,364	1,716	14,442	6,813	1,175	2,255	146,965
On-balance sheet imbalance	21,407	17,048	2,327	9,448	6,774	(8,625)	5,340	3,381	(399)	56,701
Off-balance sheet items										
Off-balance sheet assets	19,202	21,345	662	-	-	9,990	888	185	1,614	53,886
Off-balance sheet liabilities	29,552	34,234	79	8,979	6,468	-	3,634	140	920	84,006
Net off-balance sheet items	(10,350)	(12,889)	583	(8,979)	(6,468)	9,990	(2,746)	45	694	(30,120)
Net currency imbalance on 31 December 2014.........	11,057	4,159	2,910	469	306	1,365	2,594	3,426	295	26,581

Derivatives

55. The Bank uses derivatives to hedge currency exposure, interest rate risk in the banking book as well as inflation risk. The Bank carries indirect exposure due to margin trading with clients and the Bank holds collaterals for possible losses. Other derivatives in the Bank held for trading or for other purposes are insignificant.

Inflation risk

56. The Bank is exposed to inflation risk since the value of CPI-indexed assets exceeds CPI-indexed liabilities. The value of these assets and liabilities changes according to changes in the CPI at any given time and all changes in the CPI index affect profit and loss. On 30 June 2015 the CPI gap amounted to ISK 40.3 billion (31 December 2014: ISK 57.5 billion). Thus, a 1% increase in the index would lead to an ISK 403 million increase in the balance sheet and a 1% decrease would lead to a corresponding decrease, other risk factors held constant.

For the six months ended 30 June 2015 51 Amounts are in ISK million

Capital management

57. Risk exposure and capital base

The table below shows the capital base, risk weighted assets and the resulting capital ratios of the Bank at 30 June 2015 and 31 December 2014. The Bank's total capital ratio, calculated according to the Act on Financial Undertakings, was 28.3% and the Tier 1 ratio was 25.8%.

The eligibility of the Tier 2 subordinated loan issued by the Bank as Tier 2 capital will decrease linearly by 20% until maturity in 2019 because the remaining term is now less than 5 years. As a result the Tier 2 subordinated loan only attributes 90% into the total capital base.

The Board of Directors has approved a minimum capital target for the Bank at 18% of RWA.. The target is based on the Bank's internal capital adequacy assessment (ICAAP) and the views expressed by the regulator through the latest SREP results. The capital target is intended to support the Bank's business strategy and takes into account changes or uncertainties in the operating environment. Unlike the 8% regulatory minimum, the Bank's capital target can change over time reflecting changes in the Bank's risk profile, business strategy and external environment. Thus, falling below the capital target does not impose any direct regulatory actions but the Bank's dividend payments and remuneration can be impacted.

The Bank's regulatory capital calculations for credit risk and market risk are based on the standardised approach and the capital calculations for operational risk are based on the basic indicator approach.

	30.6.2015	31.12.2014
Tier 1 capital		
Ordinary share capital	10,000	10,000
Share premium	55,000	55,000
Other reserves	2,559	2,535
Retained earnings	117,852	116,288
Non-controlling interests	1,598	1,664
Tax assets	(45)	(521)
Intangible assets	(1,058)	(619)
Total Tier 1 capital	185,906	184,347
Tier 2 capital		
Adjustment to eligible capital instruments	(2,034)	-
Qualifying subordinated liabilities	20,336	21,306
Total regulatory capital	204,208	205,653
Risk-weighted assets		
- due to credit risk	614,472	583,375
- due to market risk:	27,679	33,326
Market risk, trading book	5,392	6,594
Currency risk foreign exchange	22,287	26,732
- due to operational risk	78,401	78,401
Total risk-weighted assets	720,552	695,102
Capital ratios		
Tier 1 ratio	25.8%	26.5%
Total capital ratio	28.3%	29.6%

Amounts are in ISK million