Íslandsbanki

Condensed Consolidated Interim Financial Statements

First half 2019

440 4000
@islandsbanki
islandsbanki.is

Contents

Highlights

Our profile

- A leader in financial services in Iceland, Íslandsbanki is a universal bank with total assets of ISK 1,230bn and a 25-50% market share across all domestic business segments.
- Building on over 140 years of servicing key industries, Íslandsbanki has developed specific expertise in tourism, seafood and energy related industries.
- Driven by the vision to be #1 for service, Íslandsbanki's relationship banking business model is propelled by three business divisions that manage and build relationships with the Bank's customers.
- Íslandsbanki has developed a wide range of online services such as the Íslandsbanki, Kort and Kass apps, enabling customers to do their banking whenever and wherever. At the same time, the Bank continues to operate the most efficient branch network in Iceland through its strategically located 14 branches.
- In 2018, Íslandsbanki led the Icelandic Customer Satisfactory Index for banks for the sixth consecutive year.
- Íslandsbanki has BBB+/A-2 ratings from S&P Global Ratings.

Our Bank

14 branches

806 Number of FTEs for parent company at period end

88,700 APP users

Market Share*

30% individuals

37% SMEs

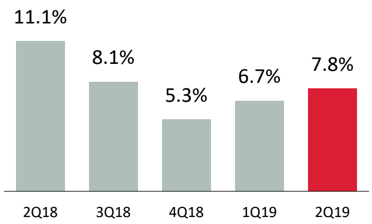
33% large companies

Credit Ratings

S&P Global Ratings

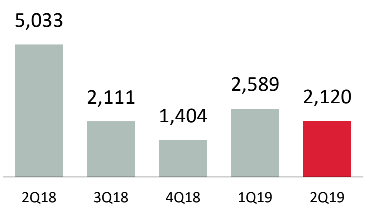
BBB+/A-2 Negative outlook

ROE reg. operations CET1 16%**

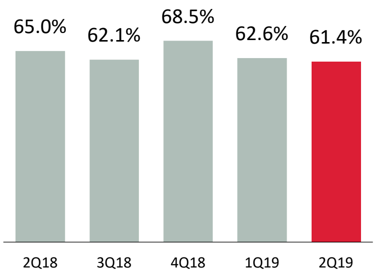


Profit after tax

(ISKbn)

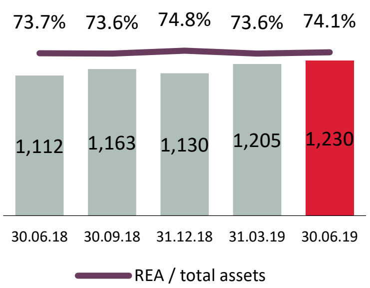


Cost / income ratio***



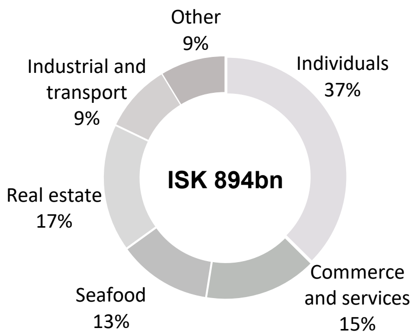
REA / total assets

(ISKbn)



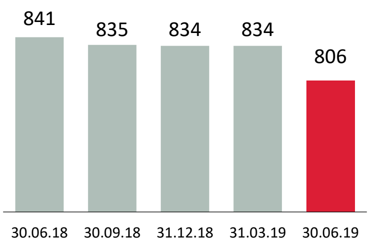
Loans to customers

(Sector split as of 30.06.19)



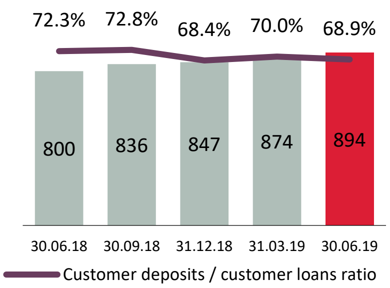
Number of FTEs for parent company

(Excluding seasonal employees)

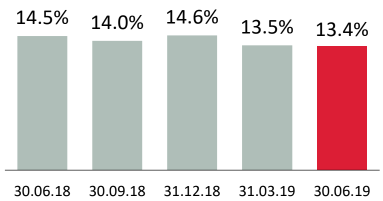


Loans to customers

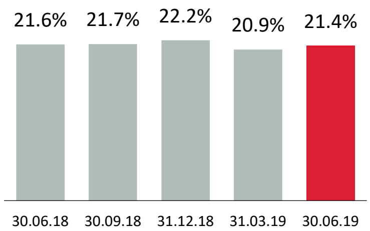
(ISKbn)



Leverage ratio



Total capital ratio



The highlights were not reviewed or audited by the Bank's auditor.

*Based on Gallup survey regarding primary bank.
**Earnings on regular income now includes profit from discontinued operations.
***The cost/income ratio for parent company 1H19 is 55.4%.

Directors' Report

These are the condensed consolidated interim financial statements for the first half of 2019 (“the interim financial statements”) of Íslandsbanki hf. (“the Bank” or “Íslandsbanki”) and its subsidiaries (together referred to as "the Group").

Operations in the reporting period

Íslandsbanki is a universal bank offering comprehensive financial services to households, corporations, and institutional investors in Iceland. The Group is one of Iceland's largest banking and financial services groups, with a strong domestic market share.

The profit from the Group's operations for the reporting period amounted to ISK 4,709 million, which corresponds to 5.4% annualised return on equity. At the end of the reporting period, the Group employed 1,053 full-time members of staff, including 806 within the Bank itself.

Net interest income rose by 9.4% between years and net fee and commission income was up by 14%, due to strong growth in both the Bank and one of its subsidiaries. Other net operating income was about 1.7 billion and mostly explained by a settlement of the Bank's claim deriving from the acquisition of Byr savings bank back in 2011. Salaries and related expenses were up by 5% between years and other operating expenses increased by 4%.

Net impairments were negative by ISK 1.8 billion and are explained by specific impairments for large customers, less favourable economic environment, change in relative weighting of economic forecasts and an unfavourable ruling in a court case. At the same time the Bank's ratio of non performing loans increased from 2.0% to 2.4%.

The Group's loan book grew by 5.7% in the first half of the year on the back of strong demand across all lending units. The Bank has gained market share in loans in recent months and will slow down growth in new loans in the months ahead.

Customer deposits increased by 6.4% in the period owing to an increase in deposits from retail customers and institutional investors. The Bank continued to have good access to capital markets and issued ISK 25 billion in covered bonds in the first half and about ISK 72 billion in foreign currency denominated senior unsecured debt, the largest issuance being a EUR 300 million benchmark transaction with maturity in 2022. At the same time the Bank tendered for about the same amount a part of the EUR 500 million bond maturing in 2020, thereby effectively managing the maturity profile of the Bank's outstanding debt. The Bank also issued SEK 500 million of Tier 2 bonds. The pricing of the subordinated bonds was 390 basis points above Stibor rates and thereby considerably more costly than the Bank's prior issuances of such paper.

The Bank continues its advancement in digital services, the most recent being the launch of Apple Pay. The Bank's customers can now use their mobile phones to puchase goods and services safely in a fast and convenient manner.

Outlook

A long period of continuous upswing in the Icelandic economy appears to be at an end, with the fall of Iceland's second largest airline at the end of the first quarter of 2019 marking a clear turning point in the domestic economy. According to Íslandsbanki Research's June forecast, GDP looks set to contract by 0.7% in 2019, making this year the first to see a contraction since 2010. A decline in exports is the main reason for the contraction. The outlook is for growth to pick up again and measure 1.5% in 2020, as growth in exports resumes and domestic demand gathers steam.

Domestic balance sheets are relatively well placed to weather a temporary setback as economy-wide leverage is moderate in comparison with peers and historical levels. The Icelandic króna has also remained broadly stable recently and the inflation outlook has improved, enabling the Central Bank to react to darkening short-term prospects by lowering its policy rate.

There is now less uncertainty than in the first quarter results about where the Icelandic economy is heading in the near term and the size of the contraction in the tourism industry. However, it remains to be seen how Icelandic companies and households, with relatively strong balance sheets, will weather this downturn and what the impact will be on the Bank's impairments and balance sheet. The momentum in the growth in revenue has continued at a strong pace and efficiency gains through IT investments will remain a core focus point in the months ahead.

Directors' Report

Statement by the Board of Directors and the CEO

The interim financial statements for the period 1 January to 30 June 2019 have been prepared on a going concern basis 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; the Act on Financial Undertakings, no. 161/2002; and rules on accounting for credit institutions, where applicable.

To the best of our knowledge, these interim financial statements provide a true and fair view of the Group's operating profits and cash flows in the reporting period and its financial position as of 30 June 2019.

The Board of Directors and the CEO have today discussed and approved the Condensed Consolidated Interim Financial Statements for the period 1 January to 30 June 2019.

Kópavogur, 31 July 2019

Board of Directors:

Friðrik Sophusson, Chairman
Tómas Már Sigurðsson, Vice-Chairman
Anna Þórðardóttir
Auður Finnbogadóttir
Árni Stefánsson
Hallgrímur Snorrason
Heiðrún 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 Interim Financial Statements of Íslandsbanki hf. and its subsidiaries as at June 30, 2019 which comprise of Consolidated interim statement of Financial Position as at June 30, 2019 and the related Consolidated Interim Income Statement, the Consolidated Interim Statement of Comprehensive Income, the Consolidated Interim Statement of Changes in Equity and Consolidated Interim Statement of Cash Flows for the six months ended 30 June 2019 and explanatory notes. The Board of Directors and CEO are 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, 31 July 2019

Margrét Pétursdóttir
State Authorised Public Accountant

Ernst & Young ehf.
Borgartún 30
105 Reykjavík

Consolidated Interim Income Statement

	Notes	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Interest income*		32,570	29,337	17,343	14,342
Interest expense		(15,792)	(13,995)	(8,717)	(6,740)
Net interest income	10	16,778	15,342	8,626	7,602
Fee and commission income		10,357	9,236	5,346	4,963
Fee and commission expense		(3,734)	(3,426)	(1,940)	(1,931)
Net fee and commission income	11	6,623	5,810	3,406	3,032
Net financial income	12	621	95	173	378
Net foreign exchange loss	13	(101)	(67)	(71)	(57)
Other operating income	14	1,173	1,600	29	1,587
Other net operating income		1,693	1,628	131	1,908
Total operating income		25,094	22,780	12,163	12,542
Salaries and related expenses	15	(8,363)	(7,952)	(4,312)	(4,026)
Other operating expenses	16	(6,000)	(5,770)	(2,961)	(2,846)
Contribution to the Depositors' and Investors' Guarantee Fund		(510)	(579)	(198)	(287)
Bank tax		(1,814)	(1,597)	(934)	(812)
Total operating expenses		(16,687)	(15,898)	(8,405)	(7,971)
Profit before net impairment on financial assets		8,407	6,882	3,758	4,571
Net impairment on financial assets	17	(1,848)	1,934	(929)	1,846
Profit before tax		6,559	8,816	2,829	6,417
Income tax expense	18	(1,779)	(2,480)	(626)	(1,465)
Profit for the period from continuing operations		4,780	6,336	2,203	4,952
Discontinued operations, net of income tax	19	(71)	794	(83)	81
Profit for the period		4,709	7,130	2,120	5,033

*Of which interest income amounting to ISK 31,249 million (2018: ISK 28,423 million) is calculated using the effective interest method.

	Notes	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Profit attributable to:					
Shareholders of Íslandsbanki hf.		4,919	7,321	2,268	5,135
Non-controlling interests		(210)	(191)	(148)	(102)
Profit for the period		4,709	7,130	2,120	5,033
Earnings per share from continuing operations					
Basic and diluted earnings per share attributable to the shareholders of Íslandsbanki hf.	20	0.50	0.65	0.24	0.51

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 12 to 55 are an integral part of these Condensed Consolidated Interim Financial Statements.

Financial Statements first half 2019 6 Amounts are in ISK million

Consolidated Interim Statement of Comprehensive Income

	2019	2018	2019	2018
	1.1-30.6	1.1-30.6	1.4-30.6	1.4-30.6
Profit for the period	4,709	7,130	2,120	5,033
Items that will not be reclassified to profit or loss				
Changes in fair value of financial assets and financial liabilities, net of tax	62	1,114	43	812
Other comprehensive income for the period, net of tax	62	1,114	43	812
Total comprehensive income for the period	4,771	8,244	2,163	5,845

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 12 to 55 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Financial Position

	Notes	30.6.2019	31.12.2018
Assets			
Cash and balances with Central Bank	21	122,794	135,056
Bonds and debt instruments	5	77,033	69,415
Shares and equity instruments	5	19,176	13,074
Derivatives	22	5,843	4,550
Loans to credit institutions	23	77,387	41,577
Loans to customers	24	894,446	846,599
Investments in associates	26	687	682
Property and equipment	28	9,504	5,271
Intangible assets		4,882	5,002
Other assets	29	18,224	9,177
Total Assets		1,229,976	1,130,403
Liabilities			
Deposits from Central Bank and credit institutions	30	19,830	15,619
Deposits from customers	31	615,869	578,959
Derivative instruments and short positions	22	6,903	5,521
Debt issued and other borrowed funds	33	337,473	300,976
Subordinated loans	34	23,431	16,216
Tax liabilities		8,674	7,150
Other liabilities	36	42,012	29,649
Total Liabilities		1,054,192	954,090
Equity			
Share capital		10,000	10,000
Share premium		55,000	55,000
Reserves		6,816	6,499
Retained earnings		101,534	102,496
Total equity attributable to the equity holders of Íslandsbanki hf.		173,350	173,995
Non-controlling interests		2,434	2,318
Total Equity		175,784	176,313
Total Liabilities and Equity		1,229,976	1,130,403

The notes on pages 12 to 55 are an integral part of these Condensed Consolidated Interim Financial Statements.

Financial Statements first half 2019 8 Amounts are in ISK million

Consolidated Interim Statement of Changes in Equity

	Share capital	Share premium	Statutory reserve	Restricted reserves	Fair value reserve	Liability credit reserve	Retained earnings	Total shareholders' equity	Non-controlling interests	Total equity
Equity as at 1.1.2019	10,000	55,000	2,500	3,750	625	(376)	102,496	173,995	2,318	176,313
Profit for the period							4,919	4,919	(210)	4,709
Dividends paid							(5,300)	(5,300)		(5,300)
Net change in fair value of financial assets					567			567	326	893
Net change in fair value of financial liabilities						(384)	(447)	(831)		(831)
Restricted due to capitalised development costs				(138)			138	-		-
Restricted due to fair value changes				275			(275)	-		-
Restricted due to subsidiaries and associates				(3)			3	-		-
Equity as at 30.6.2019	10,000	55,000	2,500	3,884	1,192	(760)	101,534	173,350	2,434	175,784
Equity as at 1.1.2018	10,000	55,000	2,500	3,440	239	(1,486)	104,760	174,453	2,485	176,938
Profit for the period							7,321	7,321	(191)	7,130
Dividends paid							(13,000)	(13,000)		(13,000)
Net change in fair value of financial assets					227			227	131	358
Net change in fair value of financial liabilities						756		756		756
Restricted due to capitalised development costs				325			(325)	-		-
Restricted due to fair value changes				(71)			71	-		-
Restricted due to subsidiaries and associates				(332)			332	-		-
Equity as at 30.6.2018	10,000	55,000	2,500	3,362	466	(730)	99,159	169,757	2,425	172,182

The Annual General Meeting ("AGM") for the operating year 2018 was held on 21 March 2019. At the AGM shareholders approved the Board's proposal to pay dividends to shareholders amounting to ISK 5,300 million which is equivalent to ISK 0.53 per share (2018: ISK 1.30 per share). The dividends were paid on 27 March 2019.

The notes on pages 12 to 55 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Cash Flows

	Notes	2019 1.1-30.6	2018 1.1-30.6
Profit for the period		4,709	7,130
Non-cash items included in profit for the period		12,127	5,513
Changes in operating assets and liabilities		(37,932)	(71,398)
Dividends received		32	61
Income tax and bank tax paid		(2,020)	(2,063)
Net cash used in operating activities		(23,084)	(60,757)
Net investment in subsidiaries and associated companies		-	2,039
Proceeds from sales of property and equipment		7	6
Purchase of property and equipment		(192)	(86)
Purchase of intangible assets		(193)	(515)
Net cash (used in) provided by investing activities		(378)	1,444
Proceeds from borrowings		101,423	76,092
Repayment of borrowings		(75,371)	(9,940)
Repayment of lease liabilities		(186)	-
Dividends paid		(5,300)	(13,000)
Net cash provided by financing activities		20,566	53,152
Net decrease in cash and cash equivalents		(2,896)	(6,161)
Effects of foreign exchange rate changes		(3)	(107)
Cash and cash equivalents at the beginning of the period		143,203	187,438
Cash and cash equivalents at the end of the period		140,304	181,170

Reconciliation of cash and cash equivalents			
Cash on hand	21	4,369	2,102
Cash balances with Central Bank	21	118,425	164,092
Bank accounts	23	32,836	30,189
Mandatory reserve and special restricted balances with Central Bank	21	(15,326)	(15,213)
Cash and cash equivalents at the end of the period		140,304	181,170

The Group has prepared its consolidated interim statement of cash flows using the indirect method. The statement is based on the net profit after tax for the period and shows the cash flows from operating, investing and financing activities and the increase or decrease in cash and cash equivalents during the period.

Interest received from 1 January to 30 June 2019 amounted to ISK 29,697 million (2018: ISK 28,539 million) and interest paid in the same period 2019 amounted to ISK 13,080 million (2018: ISK 9,560 million). Interest paid is defined as having been paid when it has been deposited into the customer account and is available for the customer's disposal.

The notes on pages 12 to 55 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Cash Flows

	2019 1.1-30.6	2018 1.1-30.6
Depreciation and amortisation	811	441
Share of (profit) loss of associates	(5)	34
Accrued interest and fair value changes on debt issued and subordinated loans	5,944	5,047
Net impairment on financial assets	1,804	(1,999)
Foreign exchange loss	101	67
Net gain from sales of subsidiary, property and equipment	(2)	(1,555)
Unrealised fair value (gain) loss recognised in profit or loss	(190)	188
Discontinued operations, net of income tax	71	(794)
Bank tax	1,814	1,597
Income tax	1,779	2,480
Other changes	-	7
Non-cash items included in profit for the period	12,127	5,513

Mandatory reserve and special restricted balances with Central Bank	1,786	2,353
Loans to credit institutions	(24,508)	(18,436)
Loans to customers	(39,202)	(47,636)
Bonds and debt instruments	(4,661)	(21,239)
Shares and equity instruments	(4,939)	(3,200)
Other operating assets	(8,688)	3,045
Non-current assets and liabilities held for sale	3	2,165
Deposits with credit institutions and Central Bank	3,812	4,243
Deposits from customers	32,176	11,136
Short positions	219	(270)
Derivatives	(1,707)	(923)
Other operating liabilities	7,777	(2,636)
Changes in operating assets and liabilities	(37,932)	(71,398)

Non-cash transactions 2019

During the period the Bank repurchased own debt securities amounting to ISK 4,319 million by issuing new debt.

The recognition of right-of-use assets amounting to ISK 4,489 million and the same amount in lease liabilities following the adoption of IFRS 16 - Leases had no cash flow effect (see Note 3).

Non-cash transactions 2018

The Group sold a subsidiary during the period and the outstanding balance at the end of the period amounted to ISK 1,241 million.

The notes on pages 12 to 55 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

1. Corporate information

Íslandsbanki hf., the parent company, was incorporated on 8 October 2008 and is a limited liability company domiciled in Iceland. The condensed consolidated interim financial statements for the first half of 2019 ("the interim financial statements") comprise the financial statements of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") and its subsidiaries together referred to as "the Group".

At the end of the period the Bank was wholly owned by the Icelandic Government. The shares are administered by the Icelandic State Financial Investments in accordance with Act no. 88/2009 on Icelandic State Financial Investments.

The interim financial statements were authorised for issue by the Board of Directors of Íslandsbanki hf. on 31 July 2019.

2. Basis of preparation

The interim financial statements have been prepared in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting, as adopted by the European Union and additional requirements in the Act on Annual Accounts no. 3/2006, the Act on Financial Undertakings no. 161/2002 and rules on accounting for credit institutions.

The 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 Group for the year ended 31 December 2018, as well as the unaudited Pillar 3 Report for the year ended 31 December 2018. Both are available on the Bank's website: www.islandsbanki.is.

The accounting policies and the basis of measurement are unchanged in comparison with Notes 70 and 72 in the consolidated financial statements for the year 2018 except for the changes presented in Note 3.

The interim financial statements are presented in Icelandic króna (ISK), which is the functional currency of Íslandsbanki hf. All amounts presented in ISK have been rounded to the nearest million, except when otherwise indicated. At 30 June 2019 the exchange rate of the ISK against the USD was 124.46 and 141.70 for the EUR (year-end 2018: USD 116.33 and EUR 133.23).

The Group's management has made an assessment of the Group's ability to continue as a going concern and is satisfied that the Group has the resources to continue in business for the foreseeable future. Therefore, the interim financial statements have been prepared on a going concern basis.

Significant accounting estimates and judgements

The preparation of the 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. Actual results may differ from those estimates.

Estimates and underlying assumptions are under constant review. Changes in accounting estimates are recognised when they occur.

Key areas where management has made difficult, complex or subjective judgements, include those relating to impairment of financial assets, the fair value of financial instruments and intangible assets.

3. Changes to accounting policies and presentation

The accounting policies in the interim financial statements are consistent with those applied in the consolidated financial statements for the year 2018, except for changes to the accounting for leases resulting from the adoption of IFRS 16. Those changes are described below.

IFRS 16 – Leases

The Group adopted a new IFRS standard, IFRS 16 – Leases, which replaced IAS 17, IFRIC 4, SIC 15 and SIC 27 as of 1 January 2019. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for most leases under a single on-balance sheet model.

As a result of the adoption of IFRS 16, the Group has changed its accounting policy for lease contracts as follows.

The Group as a lessee

Recognition

At the inception of a contract, the Group assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Group has elected not to separate non-lease components and account for lease and non-lease components of a contract as a single lease component. This policy is applied to contracts entered into, or changed, on or after 1 January 2019.

The Group recognises a lease liability and a right-of-use asset at the lease commencement date.

The Group has elected not to recognise right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low-value assets. The Group recognises lease payments associated with these leases as an expense on a straight-line basis over the lease term.

Notes to the Condensed Consolidated Interim Financial Statements

3. Cont'd

Measurement

Lease liabilities

The lease liability is initially measured at the present value of the lease payments, both fixed and variable, discounted using the entity's incremental borrowing rate. The lease liability is measured at amortised cost using the effective interest method and remeasured when there is a change in future payments, e.g. arising from a change in an index or an assessment of whether extension or termination options will be exercised.

After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made.

Right-of-use assets

The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred less any lease incentives received. For any remeasurement of the lease liability a corresponding adjustment is made to the carrying amount of the right-of-use asset or recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

The right-of-use-asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. Right-of-use assets are subject to impairment.

Modification

If a lease modification increases the scope of the lease by adding a right to use of one or more underlying assets and the consideration for the lease increases by an amount commensurate with the stand-alone price for the increased scope and any adjustments to the price that reflects the circumstances of the particular contract, then the modification is accounted for as a separate lease.

For lease modifications that are not accounted for as separate leases the lease term of the modified lease is redetermined and the lease liability remeasured using the revised lease payments and discounted using the incremental borrowing rate at the effective date of modification. Any adjustment of the lease liability is then correspondingly made to the right-of-use asset.

Presentation

The Group presents right-of-use assets in the line item "Property and equipment" and lease liabilities in the line item "Other liabilities" in the statement of financial position. Maturity analysis of lease liabilities is disclosed in Note 50. Interest on lease liabilities is recognised in profit or loss in the line item "Interest expense". Depreciation of right-of-use assets is recognised in profit or loss in the line item "Other operating expenses".

Impact of adoption of IFRS 16

The Group applied IFRS 16 using the modified retrospective approach and therefore the comparative information has not been restated. On transition to IFRS 16 the Group elected to apply the practical expedient to apply the standard only to contracts previously identified as leases under IAS 17.

At transition, lease liabilities were measured at the present value of the remaining lease payments, discounted with each entity's incremental borrowing rate as at 1 January 2019. Right-of-use assets are measured at an amount equal to the lease liabilities at transition.

On transition to IFRS 16, the Group recognised ISK 4,489 million of right-of-use assets and the same amount in lease liabilities. All lease liabilities and right-of-use assets at transition and throughout the first half of 2019 stem from CPI-linked real estate lease commitments for offices, branches and storage. When measuring lease liabilities, each entity discounted lease payments using its incremental borrowing rate at 1 January 2019. The weighted average rate applied by the Group is 2.12% for CPI-linked leases.

Reconciliation between IAS 17 lease commitments and IFRS 16 lease liabilities as at 1 January 2019

Operating lease commitments at 31 December 2018 as disclosed in the Group's consolidated financial statements	5,143
Effects of discounting operating lease commitments using the incremental borrowing rate	(593)
Recognition exemption for short-term and low-value asset leases	(61)
Lease liabilities recognised as at 1 January 2019	4,489

When applying IFRS 16 to leases previously classified as operating leases under IAS 17 the Group used the following practical expedients; not to recognise right-of-use assets and liabilities for leases with less than 12 months of lease term and for leases of low-value assets; exclude initial direct costs from measuring right-of-use assets at the date of initial application, and using hindsight when determining the lease term if the contract contains options to extend or terminate the lease.

3. Cont'd

The Group as a lessor

Lessor accounting under IFRS 16 is substantially unchanged from IAS 17. Lessors will continue to classify leases as either operating or finance leases using similar principles as in IAS 17. Therefore, IFRS 16 did not have an impact on leases where the Group is the lessor.

Other changes in presentation

Other changes in presentation in the statement of financial position are that the line item "Non-current assets and disposal groups held for sale" has been included in the line item "Other assets" and the line item "Non-current liabilities and disposal groups held for sale" has been included in the line item "Other liabilities".

4. Operating segments

Segment information is presented in accordance with the Group's management and internal reporting structure. The Bank has three main business segments: Personal Banking, Business Banking and Corporate & Investment Banking. Operating segments pay and receive interest to and from Treasury to reflect the allocation of capital, funding costs and the relevant risk premium. The accounting policies for the reportable segments are in line with the Group's accounting policies. The Group operates mainly in the Icelandic market.

The Group comprises the following operating segments:

Personal Banking

Personal Banking provides comprehensive financial services to individuals, such as lending, savings and payments. Íslandsbanki's customers are increasingly taking care of their day-to-day banking via digital solutions such as apps, the online bank and the secure web chat. Customers can also visit the Bank's efficient branch network for comprehensive consultancy services.

Business Banking

Business Banking provides wide-ranging financial services to small- and medium-sized enterprises. Business Banking is organised around the branches where it can service its customers close to their own business. In addition, Business Banking operates Ergo, the asset based financing unit of the Bank.

Corporate & Investment Banking

Corporate & Investment Banking provides universal banking services to large companies, municipalities, institutional investors and affluent individuals. Services include customised products and services to customers including lending and advisory, risk management, brokerage and private banking services. The division is sector-focused, building and maintaining relationships with key customer segments within Iceland. Outside of Iceland, Íslandsbanki has a special focus on the North Atlantic seafood industry, leveraging its expertise in the domestic market and global contacts.

Treasury and Proprietary Trading

Treasury is responsible for funding the Bank's operations and for managing the internal pricing framework. It is also responsible for the Bank's balance sheet management and for the relations with investors, financial institutions, stock exchanges and rating agencies. Equity that is not allocated to business units sits within Treasury. Proprietary Trading includes equity and debt investments in the trading book and banking book.

Cost centres

Cost centres comprise the CEO's office (Human Resources, Marketing & Communications, Strategy, and Legal), Finance excluding Treasury and Proprietary Trading, Operations & IT, Risk Management and Compliance. Group Internal Audit is included in cost centres, however, it is independent from the Bank and the Chief Audit Executive reports directly to the Bank's Board of Directors.

Subsidiaries, eliminations and adjustments

Subsidiaries include Borgun hf., Íslandssjóðir hf., Allianz Ísland hf. and other less significant subsidiaries (see Note 27).

Following is an overview showing the Group's performance with a breakdown by operating segments. Comparative amounts due to organisational changes have not been restated.

Notes to the Condensed Consolidated Interim Financial Statements

4. Cont'd

1 January to 30 June 2019	Personal Banking	Business Banking	Corporate & Investment Banking	Treasury & Proprietary Trading	Cost centres	The Bank total	Subsidiaries, eliminations & adjustments	The Group total
Net interest income	5,221	5,457	4,205	1,512	(104)	16,291	487	16,778
Net fee and commission income	2,292	815	1,831	(136)	5	4,807	1,816	6,623
Other operating income	-	9	210	805	1,241	2,265	(572)	1,693
Total operating income	7,513	6,281	6,246	2,181	1,142	23,363	1,731	25,094
Salaries and related expenses	(1,422)	(1,024)	(924)	(136)	(3,283)	(6,789)	(1,574)	(8,363)
Other operating expenses	(1,059)	(585)	(317)	(140)	(2,928)	(5,029)	(971)	(6,000)
Contribution to the Depositors' and Investors' Guarantee Fund	(286)	(174)	(50)	-	-	(510)	-	(510)
Bank tax	(230)	(173)	(254)	(1,149)	(8)	(1,814)	-	(1,814)
Net impairment on financial assets	(348)	(896)	(386)	(180)	-	(1,810)	(38)	(1,848)
Cost allocation	(2,697)	(1,470)	(1,477)	155	5,489	-	-	-
Profit (loss) before tax	1,471	1,959	2,838	731	412	7,411	(852)	6,559
Income tax expense	(443)	(554)	(804)	98	(109)	(1,812)	33	(1,779)
Profit (loss) for the period from continuing operations	1,028	1,405	2,034	829	303	5,599	(819)	4,780
Net segment revenue from external customers	9,020	7,246	9,530	(3,642)	1,209	23,363	1,731	25,094
Net segment revenue from other segments	(1,507)	(965)	(3,284)	5,823	(67)	-	-	-
Fee and commission income	3,003	821	1,861	36	5	5,726	4,631	10,357
Depreciation and amortisation	(93)	(83)	(12)	-	(531)	(719)	(92)	(811)
At 30 June 2019								
Loans to customers	315,051	235,166	339,629	541	-	890,387	4,059	894,446
Other assets	2,642	3,425	10,451	287,248	11,647	315,413	20,117	335,530
Total segment assets	317,693	238,591	350,080	287,789	11,647	1,205,800	24,176	1,229,976
Deposits from customers	278,061	173,808	111,941	55,350	-	619,160	(3,291)	615,869
Other liabilities	1,094	2,259	9,874	399,045	6,220	418,492	19,831	438,323
Total segment liabilities	279,155	176,067	121,815	454,395	6,220	1,037,652	16,540	1,054,192
Allocated equity	28,769	39,095	58,901	40,833	550	168,148	7,636	175,784
Risk exposure amount	182,433	247,961	378,770	71,100	6,283	886,547	25,237	911,784

The individual segment balance sheet positions are with external customers, and exclude internal transactions thus explaining the differences in total assets and total liabilities and equity.

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

4. Cont'd

Subsidiaries, eliminations & adjustments

1 January to 30 June 2019	Borgun hf.	Íslands-sjóðir hf.	Allianz Ísland hf.	Other subsidiaries	Eliminations & adjustments	Total
Net interest income	444	16	14	15	(2)	487
Net fee and commission income	768	534	536	(15)	(7)	1,816
Other operating income	39	149	1	2	(763)	(572)
Total operating income	1,251	699	551	2	(772)	1,731
Salaries and related expenses	(1,210)	(279)	(85)	-	-	(1,574)
Other operating expenses	(720)	(92)	(226)	(3)	70	(971)
Net impairment on financial assets	(39)	-	-	-	1	(38)
(Loss) profit before tax	(718)	328	240	(1)	(701)	(852)
Income tax expense	143	(66)	(48)	-	4	33
(Loss) profit for the period from cont. operations	(575)	262	192	(1)	(697)	(819)
Net segment revenue from external customers	1,695	784	549	(16)	(1,281)	1,731
Net segment revenue from other segments	(444)	(85)	2	18	509	-
Fee and commission income	4,893	750	536	-	(1,548)	4,631
Depreciation and amortisation	(89)	-	-	-	(3)	(92)
At 30 June 2019						
Total assets	26,996	2,543	1,065	7,542	(13,970)	24,176
Total liabilities	20,488	285	382	49	(4,664)	16,540
Total equity	6,508	2,258	683	7,493	(9,306)	7,636

1 January to 30 June 2018	Retail Banking	Corporate & Investment Banking	Treasury	Proprietary Trading & Subsidiaries	Cost centres & eliminations	Total
Net interest income	9,950	3,040	1,983	500	(131)	15,342
Net fee and commission income	2,921	1,559	(102)	1,424	8	5,810
Other operating income	8	196	137	2,722	(1,435)	1,628
Total operating income	12,879	4,795	2,018	4,646	(1,558)	22,780
Salaries and related expenses	(2,404)	(816)	(84)	(1,444)	(3,204)	(7,952)
Other operating expenses	(1,742)	(315)	(216)	(1,121)	(2,376)	(5,770)
Deposit Guarantee Fund	(564)	(7)	(8)	-	-	(579)
Bank tax	-	-	(1,597)	-	-	(1,597)
Net impairment on financial assets	1,793	313	(93)	(78)	(1)	1,934
Cost allocation	(3,872)	(1,331)	301	(28)	4,930	-
Profit (loss) before tax	6,090	2,639	321	1,975	(2,209)	8,816
Income tax expense	(1,583)	(686)	(364)	(421)	574	(2,480)
Profit (loss) for the period from cont. operations	4,507	1,953	(43)	1,554	(1,635)	6,336
Net segment revenue from external customers	13,223	8,785	(2,665)	4,865	(1,428)	22,780
Net segment revenue from other segments	(344)	(3,990)	4,683	(219)	(130)	-
Fee and commission income	3,702	1,670	(74)	5,379	(1,441)	9,236
Depreciation and amortisation	(136)	(9)	(2)	(85)	(209)	(441)
At 30 June 2018						
Loans to customers	504,404	289,693	52	5,789	-	799,938
Other assets	3,483	906	257,301	55,418	(5,304)	311,804
Total segment assets	507,887	290,599	257,353	61,207	(5,304)	1,111,742
Deposits from customers	501,110	15,172	65,353	83	(3,304)	578,414
Other liabilities	3,021	4,459	325,583	26,426	1,657	361,146
Total segment liabilities	504,131	19,631	390,936	26,509	(1,647)	939,560
Allocated equity	59,595	48,050	51,203	22,250	(8,916)	172,182
Risk exposure amount	417,172	327,684	26,517	49,893	(1,917)	819,349

Amounts are in ISK million

5. Classification of financial assets and financial liabilities

At 30 June 2019

	Mandatorily at FVTPL	Held for hedging	Designated as at FVTPL	Fair value through OCI	Amortised cost	Carrying amount
Cash and balances with Central Bank	-	-	-	-	122,794	122,794
Listed bonds and debt instruments	75,454	-	-	-	-	75,454
Unlisted bonds and debt instruments	1,579	-	-	-	-	1,579
Listed shares and equity instruments	13,252	-	-	-	-	13,252
Unlisted shares and equity instruments	3,188	-	-	2,736	-	5,924
Derivatives	4,677	1,166	-	-	-	5,843
Loans to credit institutions	-	-	-	-	77,387	77,387
Loans to customers	-	-	-	-	894,446	894,446
Other financial assets	-	-	-	-	16,389	16,389
Total financial assets	98,150	1,166	-	2,736	1,111,016	1,213,068
Deposits from Central Bank and credit institutions	-	-	-	-	19,830	19,830
Deposits from customers	-	-	-	-	615,869	615,869
Derivative instruments and short positions	6,903	-	-	-	-	6,903
Debt issued and other borrowed funds	-	43,640	72,424	-	221,409	337,473
Subordinated loans	-	-	-	-	23,431	23,431
Other financial liabilities	-	-	-	-	40,499	40,499
Total financial liabilities	6,903	43,640	72,424	-	921,038	1,044,005

At 31 December 2018

	Mandatorily at FVTPL	Held for hedging	Designated as at FVTPL	Fair value through OCI	Amortised cost	Carrying amount
Cash and balances with Central Bank	-	-	-	-	135,056	135,056
Listed bonds and debt instruments	67,901	-	-	-	-	67,901
Unlisted bonds and debt instruments	1,514	-	-	-	-	1,514
Listed shares and equity instruments	8,386	-	-	-	-	8,386
Unlisted shares and equity instruments	2,846	-	-	1,842	-	4,688
Derivatives	3,923	627	-	-	-	4,550
Loans to credit institutions	-	-	-	-	41,577	41,577
Loans to customers	-	-	-	-	846,599	846,599
Other financial assets	-	-	-	-	7,511	7,511
Total financial assets	84,570	627	-	1,842	1,030,743	1,117,782
Deposits from Central Bank and credit institutions	-	-	-	-	15,619	15,619
Deposits from customers	-	-	-	-	578,959	578,959
Derivative instruments and short positions	5,521	-	-	-	-	5,521
Debt issued and other borrowed funds	-	40,714	68,154	-	192,108	300,976
Subordinated loans	-	-	-	-	16,216	16,216
Other financial liabilities	-	-	-	-	27,186	27,186
Total financial liabilities	5,521	40,714	68,154	-	830,088	944,477

Amounts are in ISK million

6. Fair value information for financial instruments

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 Group 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.

The table below shows financial instruments carried at fair value at 30 June 2019 categorised into three levels of fair value hierarchy that reflect the type of inputs used in making the fair value measurements. 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 Group can access at the measurement date.

Level 2: Valuation techniques based on observable inputs other than the quoted prices included in Level 1, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Valuation techniques based on significant unobservable inputs, e.g. internal assumptions.

At 30 June 2019

	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	75,454	-	1,579	77,033
Shares and equity instruments	13,163	38	5,975	19,176
Derivative instruments	-	5,843	-	5,843
Total financial assets	88,617	5,881	7,554	102,052
Short positions	219	-	-	219
Derivative instruments	-	6,684	-	6,684
Debt issued and other borrowed funds designated as at FVTPL	72,424	-	-	72,424
Total financial liabilities	72,643	6,684	-	79,327

At 31 December 2018

	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	67,901	-	1,514	69,415
Shares and equity instruments	8,344	42	4,688	13,074
Derivative instruments	-	4,550	-	4,550
Total financial assets	76,245	4,592	6,202	87,039
Derivative instruments	-	5,521	-	5,521
Debt issued and other borrowed funds designated as at FVTPL	68,154	-	-	68,154
Total financial liabilities	68,154	5,521	-	73,675

Changes in Level 3 assets measured at fair value:	Bonds and debt instruments	Shares and equity instruments
Fair value at 1 January 2019	1,514	4,688
Purchases	-	194
Sales	(536)	(52)
Net gain on financial instruments recognised in profit or loss	538	226
Net gain on financial instruments recognised in other comprehensive income	-	893
Other	63	26
Fair value at 30 June 2019	1,579	5,975

Amounts are in ISK million

6. Cont'd

	Bonds and debt instruments	Shares and equity instruments
Fair value at 1 January 2018	1,828	3,373
Purchases	8	790
Net loss on financial instruments recognised in profit or loss	(249)	(135)
Net gain on financial instruments recognised in other comprehensive income	-	610
Transfers from Level 1 or 2	-	50
Other	(73)	-
Fair value at 31 December 2018	1,514	4,688

The responsibility for the valuation of the fair value of financial instruments lies with the relevant business units. Each quarter, the business units present a valuation report to the Investment Committee for approval. The report and its assumptions are reviewed by Risk Management.

Where applicable, fair values are determined using quoted prices in active markets for identical assets and liabilities. 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.

At the end of each reporting period the Group determines whether transfers have occured between levels in the hierarchy, by reassessing categorisation based on the lowest level input that is significant to the fair value measurement as a whole.

Level 1: Fair value established from quoted market prices.

Level 1 financial assets and financial liabilities contain actively traded bonds and equities that are listed either domestically or abroad.

Level 2: Fair value established using valuation techniques with observable market information.

Level 2 assets and liabilities contain domestic bonds, equities as well as derivatives. For interest rate derivatives contracts such as interest rate swaps (IRS) and cross-currency interest rate swaps (CIRS) the Group 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.

Level 3: Fair value established using valuation techniques using significant unobservable market information.

Level 3 assets contain primarily unlisted and illiquid equities and bonds. Unlisted equities and bonds are initially recorded at their transaction price but are revalued each quarter based on the models as described above. At 30 June 2019 the Group's Level 3 equities amounted to ISK 5,975 million. These include shares in five professional investment funds and investment companies investing in unlisted equities and specialised investments in Iceland totalling ISK 1,604 million. The Group receives information from fund managers which use valuation models for the valuation of these equities. Full access to information of all components in these valuation models is unavailable to the Group and is therefore no basis for assumptions for sensitivity analysis.

The Group holds Series C preferred shares in Visa Inc., amounting to ISK 2,736 million, which are subject to selling restrictions for a period of up to 9 years and under certain conditions may have to be recalled. The fair value of the preferred shares is closely linked to the market value of Visa Inc. at NYSE stock exchange, written down by 30% due to uncertainty of the final number of shares and marketability.

For other Level 3 equities, changes in components for valuation will have minimal impact on the Group's income statement.

The Group's Level 3 bonds amounted to ISK 1,579 million. The majority of the amount in Level 3 bonds is estimated by discounting cash flow where the yield is the contractual currency's base rate with a premium that is decided by expert judgement on projected risk and financing cost.

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7. Financial instruments not carried at fair value

Assets

The fair value of "Loans to customers" may differ from their net carrying amount because the interest rates they carry may not reflect the interest rates that similar new loans would carry. The fair value is estimated by subtracting from or adding to the net carrying amount of the loans the discounted interest rate difference calculated from the reporting date until the next interest reset or maturity, whichever comes first. Since the interest rate difference is estimated using 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 adequately approximated by the carrying amount as 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. 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. The fair value for longer term fixed rate deposits is calculated with a duration approach, using the difference in each liability's current interest rate from the rate that a similar deposit would carry today. All deposits are classified as Level 2 based on the use of observable market interest rates to estimate the fair value.

Observed market value is used for the fair value of "Debt issued and other borrowed funds" 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 Group's current funding premium on similar debt. These liabilities are classified as Level 2. The funding premium is based on the interest margin in the Group's issued papers including covered bonds, commercial papers as well as foreign currency denominated bonds.

Other financial liabilities mainly include unsettled securities transactions and liabilities to retailers for credit card provisions and they 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 tables show the fair value measurement and classification of the Group's assets and liabilities not carried at fair value. The different levels are defined in Note 6.

At 30 June 2019	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Cash and balances with Central Bank	-	122,794	-	122,794	122,794
Loans to credit institutions	-	77,387	-	77,387	77,387
Loans to customers	-	-	897,893	897,893	894,446
Other financial assets	-	16,389	-	16,389	16,389
Total financial assets	-	216,570	897,893	1,114,463	1,111,016
Deposits from Central Bank and credit institutions	-	19,868	-	19,868	19,830
Deposits from customers	-	616,204	-	616,204	615,869
Debt issued and other borrowed funds	165,437	107,845	-	273,282	265,049
Subordinated loans	23,381	-	-	23,381	23,431
Other financial liabilities	-	40,499	-	40,499	40,499
Total financial liabilities	188,818	784,416	-	973,234	964,678

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At 31 December 2018	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Cash and balances with Central Bank	-	135,056	-	135,056	135,056
Loans to credit institutions	-	41,577	-	41,577	41,577
Loans to customers	-	-	848,751	848,751	846,599
Other financial assets	-	7,511	-	7,511	7,511
Total financial assets	-	184,144	848,751	1,032,895	1,030,743
Deposits from Central Bank and credit institutions	-	15,633	-	15,633	15,619
Deposits from customers	-	579,232	-	579,232	578,959
Debt issued and other borrowed funds	151,767	84,476	-	236,243	232,822
Subordinated loans	16,167	-	-	16,167	16,216
Other financial liabilities	-	27,186	-	27,186	27,186
Total financial liabilities	167,934	706,527	-	874,461	870,802

8. Offsetting financial assets and financial liabilities

The tables below show reconciliation to the net amounts of financial assets and financial liabilities, which are subject to offsetting, enforceable master netting agreements and similar agreements.

Financial assets	Financial assets subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 30 June 2019	Financial assets before netting	Netting with financial liabilities	Net financial assets	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 financial assets recognised in the balance sheet
Reverse repurchase agreements	464	-	464	-	-	-	464	-	464
Derivatives	5,843	-	5,843	(1,305)	(2,406)	(100)	2,032	-	5,843
Total assets	6,307	-	6,307	(1,305)	(2,406)	(100)	2,496	-	6,307
At 31 December 2018									
Reverse repurchase agreements	153	-	153	-	-	-	153	-	153
Derivatives	4,550	-	4,550	(1,655)	(1,383)	(698)	814	-	4,550
Total assets	4,703	-	4,703	(1,655)	(1,383)	(698)	967	-	4,703

Financial liabilities	Financial liabilities subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 30 June 2019	Financial liabilities before netting	Netting with financial assets	Net financial liabilities	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 financial liabilities recognised in the balance sheet
Derivative instruments and short positions	6,903	-	6,903	(1,305)	(534)	-	5,064	-	6,903
At 31 December 2018									
Derivative instruments and short positions	5,521	-	5,521	(1,655)	(85)	-	3,781	-	5,521

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Notes to the Condensed Consolidated Interim Financial Statements

9. Quarterly statements

	2019 Q2	2019 Q1	2018 Q4	2018 Q3	2018 Q2
Net interest income	8,626	8,152	8,294	8,301	7,602
Net fee and commission income	3,406	3,217	3,478	2,939	3,032
Net financial income (expense)	173	448	(637)	(420)	378
Net foreign exchange (loss) gain	(71)	(30)	76	(8)	(57)
Other operating income	29	1,144	120	64	1,587
Salaries and related expenses	(4,312)	(4,051)	(4,047)	(3,501)	(4,026)
Other operating expenses	(2,961)	(3,039)	(3,418)	(2,962)	(2,846)
Contribution to the Depositors' and Investors' Guarantee Fund	(198)	(312)	(299)	(295)	(287)
Bank tax	(934)	(880)	(740)	(944)	(812)
Net impairment on financial assets	(929)	(919)	(297)	(53)	1,846
Profit before tax	2,829	3,730	2,530	3,121	6,417
Income tax expense	(626)	(1,153)	(1,118)	(1,136)	(1,465)
Profit for the period from continuing operations	2,203	2,577	1,412	1,985	4,952
Discontinued operations, net of income tax	(83)	12	(8)	126	81
Profit for the period	2,120	2,589	1,404	2,111	5,033

10. Net interest income

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Cash and balances with Central Bank	2,637	4,047	1,271	1,886
Loans at amortised cost	28,612	24,376	15,339	12,023
Financial assets mandatorily at fair value through profit or loss	1,281	827	713	396
Other assets	40	87	20	37
Total interest income	32,570	29,337	17,343	14,342
Deposits from credit institutions and Central Bank	(229)	(206)	(122)	(109)
Deposits from customers	(8,703)	(7,958)	(4,660)	(3,863)
Debt issued and other borrowed funds at fair value through profit or loss	(374)	(580)	(194)	(292)
Debt issued and other borrowed funds at amortised cost	(5,138)	(3,958)	(2,915)	(1,908)
Subordinated loans	(173)	(71)	(93)	(37)
Other interest expense*	(1,175)	(1,222)	(733)	(531)
Total interest expense	(15,792)	(13,995)	(8,717)	(6,740)
Net interest income	16,778	15,342	8,626	7,602

*Thereof is lease liabilities' interest expense amounting to ISK 47 million.

Amounts are in ISK million

11. Net fee and commission income

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Asset management	1,123	1,031	575	556
Investment banking and brokerage	1,144	1,048	614	552
Payment processing	6,367	5,636	3,397	3,082
Loans and guarantees	754	769	376	429
Other fee and commission income	969	752	384	344
Total fee and commission income	10,357	9,236	5,346	4,963
Brokerage	(144)	(130)	(75)	(62)
Clearing and settlement	(3,579)	(3,289)	(1,876)	(1,865)
Other fee and commission expense	(11)	(7)	11	(4)
Total fee and commission expense	(3,734)	(3,426)	(1,940)	(1,931)
Net fee and commission income	6,623	5,810	3,406	3,032

Fee and commission income by segment is disclosed in Note 4.

12. Net financial income

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Net gain on financial assets and liabilities mandatorily at FVTPL	876	276	372	459
Net loss on financial liabilities designated as at FVTPL	(259)	(162)	(215)	(94)
Net gain (loss) on fair value hedges	4	(19)	16	13
Net financial income	621	95	173	378

13. Net foreign exchange loss

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Cash and balances with Central Bank	(3)	(107)	(12)	(47)
Financial assets mandatorily at fair value through profit or loss	900	(2,111)	1,099	(569)
Loans at amortised cost	14,114	40	5,798	6,760
Other assets	223	23	42	101
Net foreign exchange gain (loss) for assets	15,234	(2,155)	6,927	6,245
Deposits	(5,134)	(208)	(1,520)	(3,294)
Debt issued and other borrowed funds designated as at FVTPL	(4,706)	849	(2,518)	(1,555)
Debt issued and other borrowed funds at amortised cost	(4,800)	885	(2,600)	(1,232)
Subordinated loans	(532)	637	(286)	(32)
Other liabilities	(163)	(75)	(74)	(189)
Net foreign exchange (loss) gain for liabilities	(15,335)	2,088	(6,998)	(6,302)
Net foreign exchange loss	(101)	(67)	(71)	(57)

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

14. Other operating income

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Share of gain (loss) of associates, net of income tax	5	(34)	5	(2)
Net (loss) gain from sale of subsidiaries	(16)	1,529	(16)	1,529
Legal dispute settlement*	1,103	-	-	-
Legal fees	43	44	23	25
Rental income	19	19	9	10
Other net operating income	19	42	8	25
Other operating income	1,173	1,600	29	1,587

*In February 2019 Íslandsbanki and Old Byr reached an agreement on the settlement of the dispute deriving from the acquisition of Byr savings bank in 2011.

15. Salaries and related expenses

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Salaries	6,477	6,121	3,333	3,101
Contributions to pension funds	942	905	484	465
Social security charges and financial activities tax*	868	871	446	438
Other salary-related expenses	76	59	49	26
Capitalisation of internal staff costs in software development	-	(4)	-	(4)
Salaries and related expenses	8,363	7,952	4,312	4,026

*Financial activities tax calculated on salaries is 5.5% (2018: 5.5%).

16. Other operating expenses

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Professional services	1,058	1,193	530	554
Software and IT expenses	2,399	2,090	1,218	1,030
Real estate and office equipment	626	1,000	309	503
Depreciation and amortisation	811	441	414	227
Other administrative expenses	1,106	1,046	490	532
Other operating expenses	6,000	5,770	2,961	2,846

17. Net impairment on financial assets

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Allowance for expected credit losses, on-balance sheet items*	(1,801)	883	(881)	830
Allowance for expected credit losses, off-balance sheet items	(41)	40	(48)	5
Changes of provision due to court rulings	(6)	1,011	-	1,011
Net impairment on financial assets	(1,848)	1,934	(929)	1,846

*The main reasons for the additional allowance are: increased loan impairments for a few customers (ISK 860 million), due to a less favourable economic environment (ISK 640 million), a change in the relative weighting of economic forecasts (ISK 125 million), and an unfavourable ruling in a court case (ISK 210 million).

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

18. Income tax expense

Income tax is recognised based on applicable tax rates and tax laws. The income tax rate for legal entities in 2019 is 20% (2018: 20%). Special financial activities tax is calculated as 6% of taxable profits exceeding ISK 1 billion in accordance with the Act on Financial Activities Tax no. 165/2011. The effective income tax rate in the Group's income statement for the first half of 2019 is 27.1% (2018: 28.1%).

	2019 1.1-30.6	2018 1.1-30.6
Current tax expense excluding discontinued operations	1,267	2,318
Special financial activities tax	283	625
Difference in prior year's calculated income tax	(2)	(6)
Changes in temporary differences due to deferred tax assets and deferred tax liabilities	231	(457)
Income tax recognised in the income statement	1,779	2,480
Income tax due to equity activities	(157)	(874)

	2019 1.1-30.6		2018 1.1-30.6	
Profit before tax	6,559		8,816	
20% income tax calculated on the profit of the period	1,312	20.0%	1,763	20.0%
Special financial activities tax	283	4.3%	625	7.1%
Income not subject to tax	(212)	(3.2%)	(233)	(2.7%)
Non-deductible expenses	365	5.6%	320	3.6%
Other differences	31	0.4%	5	0.1%
Effective income tax expense	1,779	27.1%	2,480	28.1%

The Bank is taxed jointly with its subsidiary Íslandssjóðir hf.

19. Discontinued operations, net of income tax

	2019 1.1-30.6	2018 1.1-30.6	2019 1.4-30.6	2018 1.4-30.6
Net (loss) profit from sales of foreclosed mortgages	(34)	39	(33)	(1)
Net share of (loss) profit from disposal groups held for sale	(37)	755	(50)	82
Discontinued operations, net of income tax	(71)	794	(83)	81

20. Earnings per share

	Discontinued operations			
	Excluded		Included	
	2019 1.1-30.6	2018 1.1-30.6	2019 1.1-30.6	2018 1.1-30.6
Profit attributable to shareholders of the Bank	4,990	6,527	4,919	7,321
Weighted average number of outstanding shares	10,000	10,000	10,000	10,000
Basic earnings per share	0.50	0.65	0.49	0.73

The Group's basic and diluted earnings per share are equal as the Group has not issued any options, warrants, convertables, or other potential sources of dilution (2018: none).

Amounts are in ISK million

21. Cash and balances with Central Bank

	30.6.2019	31.12.2018
Cash on hand	4,369	3,095
Balances with Central Bank	103,099	114,849
Balances with Central Bank subject to special restrictions*	2,205	3,049
Included in cash and cash equivalents	109,673	120,993
Mandatory reserve deposits with Central Bank	13,121	14,063
Cash and balances with Central Bank	122,794	135,056

*Balances as defined in Act no. 37/2016 on the treatment of króna-denominated assets subject to special restrictions and rules no. 490/2016 on special reserve requirements for new foreign currency inflows.

22. Derivative instruments and short positions

At 30 June 2019	Assets	Notional values related to assets	Liabilities	Notional values related to liabilities
Interest rate swaps	1,898	130,095	3,627	117,164
Cross-currency interest rate swaps	3,092	64,640	1,205	50,747
Equity forwards	77	2,516	526	6,657
Foreign exchange forwards	501	16,498	57	5,550
Foreign exchange swaps	266	15,904	1,112	38,655
Bond forwards	9	3,940	157	18,143
Derivatives	5,843	233,593	6,684	236,916
Short positions in listed bonds	-	-	219	199
Total	5,843	233,593	6,903	237,115
At 31 December 2018				
Interest rate swaps	1,037	102,429	3,422	134,010
Cross-currency interest rate swaps	1,821	69,691	1,184	28,309
Equity forwards	419	4,596	78	1,195
Foreign exchange forwards	359	9,242	196	3,869
Foreign exchange swaps	875	35,726	440	13,373
Bond forwards	39	3,511	201	19,993
Derivatives	4,550	225,195	5,521	200,749

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

Short positions are in Icelandic Government bonds and bonds issued by institutions with government guarantees. As a primary dealer the Group has access to securities lending facilities provided by the Central Bank and the Housing Financing Fund. Majority of the securities lending facilities have a maturity of less than a year.

The Group applies hedge accounting only with respect to certain EUR denominated interest rate swaps, whereby the Group pays floating rate interest and receives fixed rate interest. The interest rate swaps are hedging the exposure of changes in the fair value of certain fixed-rate EUR denominated bonds (see Note 33) arising from changes in interest rates. The Group applies fair value hedge accounting to the hedging relationships. At the end of the second quarter 2019 the total fair value of the interest rate swaps was positive and amounted to ISK 1,166 million and their total notional amount was ISK 42,510 million.

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23. Loans to credit institutions

	30.6.2019	31.12.2018
Money market loans	42,477	16,314
Bank accounts	32,836	25,259
Other loans	2,074	4
Loans to credit institutions	77,387	41,577

24. Loans to customers

At 30 June 2019	Gross carrying amount			Expected credit loss allowance			Net carrying amount
	Stage 1	Stage 2	Stage 3	Stage 1	Stage 2	Stage 3	
Individuals	323,418	5,146	8,681	(1,177)	(213)	(1,106)	334,749
Commerce and services	127,335	4,115	5,717	(742)	(194)	(1,190)	135,041
Construction	31,732	1,691	361	(256)	(35)	(48)	33,445
Energy	6,215	744	-	(21)	(4)	-	6,934
Financial services	23	-	-	-	-	-	23
Industrial and transportation	73,043	6,457	4,020	(410)	(39)	(1,287)	81,784
Investment companies	20,605	5,628	457	(284)	(117)	(237)	26,052
Public sector and non-profit organisations	11,387	10	83	(10)	-	(17)	11,453
Real estate	151,341	686	2,286	(726)	(22)	(488)	153,077
Seafood	108,300	3,568	482	(178)	(44)	(240)	111,888
Loans to customers	853,399	28,045	22,087	(3,804)	(668)	(4,613)	894,446

At 31 December 2018							
Individuals	308,870	5,901	6,860	(1,130)	(256)	(855)	319,390
Commerce and services	118,563	4,981	3,358	(643)	(179)	(1,838)	124,242
Construction	25,958	3,301	298	(196)	(247)	(19)	29,095
Energy	6,145	740	-	(20)	(7)	-	6,858
Financial services	1,708	-	-	(4)	-	-	1,704
Industrial and transportation	74,338	2,625	3,800	(398)	(53)	(488)	79,824
Investment companies	18,709	5,128	398	(217)	(103)	(116)	23,799
Public sector and non-profit organisations	12,054	22	30	(18)	-	(1)	12,087
Real estate	139,073	2,588	2,087	(528)	(154)	(181)	142,885
Seafood	103,014	3,616	479	(123)	(80)	(191)	106,715
Loans to customers	808,432	28,902	17,310	(3,277)	(1,079)	(3,689)	846,599

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

25. Expected credit loss

Loans to customers

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2019	3,277	1,079	3,689	8,045
Transfer to Stage 1	1,014	(835)	(179)	-
Transfer to Stage 2	(868)	1,085	(217)	-
Transfer to Stage 3	(84)	(409)	493	-
Net remeasurement of loss allowance (including changes in models)	(284)	(319)	1,479	876
New financial assets originated or purchased	894	208	135	1,237
Derecognitions and maturities	(145)	(136)	(165)	(446)
Write-offs	-	(5)	(971)	(976)
Recoveries of amounts previously written off	-	-	129	129
Foreign exchange	-	-	64	64
Unwinding of interests	-	-	156	156
At 30 June 2019	3,804	668	4,613	9,085
At 1 January 2018	2,701	1,244	9,151	13,096
Transfer to Stage 1	2,652	(1,733)	(919)	-
Transfer to Stage 2	(1,053)	2,317	(1,264)	-
Transfer to Stage 3	(99)	(1,167)	1,266	-
Net remeasurement of loss allowance	(2,073)	126	(429)	(2,376)
New financial assets originated or purchased	1,474	478	711	2,663
Derecognitions and maturities	(323)	(185)	(618)	(1,126)
Write-offs	(2)	(1)	(5,254)	(5,257)
Recoveries of amounts previously written off	-	-	416	416
Foreign exchange	-	-	87	87
Unwinding of interests	-	-	542	542
At 31 December 2018	3,277	1,079	3,689	8,045

Total expected credit loss

	Stage 1	Stage 2	Stage 3	Total
Cash and balances with Central Bank	3	-	-	3
Loans to credit institutions	101	-	-	101
Loans to customers	3,804	668	4,613	9,085
Other financial assets	5	2	96	103
Off-balance sheet loan commitments and financial guarantees	462	31	185	678
At 30 June 2019	4,375	701	4,894	9,970
Cash and balances with Central Bank	48	-	-	48
Loans to credit institutions	62	-	-	62
Loans to customers	3,277	1,079	3,689	8,045
Other financial assets	5	3	83	91
Off-balance sheet loan commitments and financial guarantees	410	142	84	636
At 31 December 2018	3,802	1,224	3,856	8,882

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

26. Investments in associates

	2019 1.1-30.6	2018 1.1-31.12
Investments in associates at the beginning of the year	682	704
Additions during the period	-	86
Sales of shares in associates	-	(39)
Transfer from associates to subsidiaries	-	(80)
Share of gain of associates	5	29
Dividends paid	-	(18)
Investments in associates	687	682

27. Investments in subsidiaries

		30.6.2019	31.12.2018
Borgun hf., a payment acquirer and issuing processor, Ármúli 30, 108 Reykjavík	Iceland	63.5%	63.5%
B-Payment Group Szolgáltató Zrt., a payment processing company, H-1132 Budapest	Hungary	100%	100%
Íslandssjóðir hf., an investment fund management company, Hagasmári 3, 201 Kópavogur	Iceland	100%	100%
Hringur-eignarhaldsfélag ehf., a holding company, Dalshraun 3, 220 Hafnarfjörður	Iceland	100%	100%
Allianz Ísland hf., an insurance agent, Dalshraun 3, 220 Hafnarfjörður	Iceland	100%	100%

In addition Íslandsbanki has control over 13 other non-significant subsidiaries.

28. Property and equipment

At 30 June 2019 **Historical cost**	Land and buildings	Right-of-use assets: Properties	Fixtures, equipment & vehicles	Total
Balance at the beginning of the year	4,054	-	3,984	8,038
Impact of adopting IFRS 16, see Note 3	-	4,489	-	4,489
Additions during the period	52	-	140	192
Disposals and write-offs during the period	-	-	(198)	(198)
Remeasurement	-	82	-	82
Total	4,106	4,571	3,926	12,603
Accumulated depreciation				
Balance at the beginning of the year	(1,402)	-	(1,365)	(2,767)
Depreciation during the period	(19)	(209)	(270)	(498)
Disposals and write-offs during the period	-	-	166	166
Total	(1,421)	(209)	(1,469)	(3,099)
Carrying amount	2,685	4,362	2,457	9,504
Depreciation rates	0-2%	8-33%	8-33%	

Official real estate value of land and buildings	3,747
Insurance value of buildings	4,890
Insurance value of fixtures, equipment and vehicles	3,515

Amounts are in ISK million

28. Cont'd

At 31 December 2018

Historical cost	Land and buildings	Fixtures, equipment & vehicles	Total
Balance at the beginning of the year	5,722	4,683	10,405
Additions during the year	15	829	844
Disposals and write-offs during the year	(1,683)	(1,528)	(3,211)
Total	4,054	3,984	8,038
Accumulated depreciation			
Balance at the beginning of the year	(1,330)	(1,947)	(3,277)
Depreciation during the year	(72)	(496)	(568)
Disposals and write-offs during the year	-	1,078	1,078
Total	(1,402)	(1,365)	(2,767)
Carrying amount	2,652	2,619	5,271
Depreciation rates	0-2%	8-33%	
Official real estate value of buildings and land			3,747
Insurance value of buildings			4,889
Insurance value of fixtures, equipment and vehicles			3,500

29. Other assets

	30.6.2019	31.12.2018
Receivables	5,954	5,793
Unsettled securities transactions	9,479	1,033
Accruals	311	289
Prepaid expenses	669	395
Deferred tax assets	394	215
Other assets	244	222
Non-current assets and disposal groups held for sale	1,173	1,230
Other assets	18,224	9,177

Non-current assets and disposal groups held for sale	30.6.2019	31.12.2018
Repossessed collateral:		
Land and property	906	995
Industrial equipment and vehicles	26	17
Assets of disposal groups classified as held for sale	241	218
Total	1,173	1,230

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30. Deposits from Central Bank and credit institutions

	30.6.2019	31.12.2018
Deposits from credit institutions	19,823	15,527
Repurchase agreements with Central Bank	7	92
Deposits from Central Bank and credit institutions	19,830	15,619

31. Deposits from customers

	30.6.2019	31.12.2018
Demand deposits*	535,483	499,170
Time deposits	80,386	79,789
Deposits from customers	615,869	578,959

*Demand deposits include deposits with maturity of up to 3 months.

Deposits from customers specified by owners:

	30.6.2019		31.12.2018	
	Amount	% of total	Amount	% of total
Central government and state-owned enterprises	9,373	2%	9,331	2%
Municipalities	8,395	1%	5,574	1%
Companies	310,095	50%	278,209	48%
Individuals	288,006	47%	285,845	49%
Deposits from customers	615,869	100%	578,959	100%

32. Pledged assets

	30.6.2019	31.12.2018
Financial assets pledged as collateral against liabilities	200,325	190,471
Financial assets pledged as collateral in foreign banks	583	1,105
Financial assets pledged as collateral in repurchase agreements	463	153
Pledged assets against liabilities	201,371	191,729

The Group has pledged assets against the issuance of covered bonds under Icelandic law, which are pledged on a pool of consumer mortgage loans. The underlying cover pool must withstand a weekly stress test.

The Group has also pledged cash in foreign banks and financial institutions, mainly as collateral for trades under ISDA agreements to hedge market risk.

Financial Statements first half 2019 32 Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

33. Debt issued and other borrowed funds

	Issued	Maturity	Maturity type	Terms of interest	30.6.2019	31.12.2018
Covered bond in ISK*	2014-2017	2019	At maturity	Fixed rates	-	9,866
Covered bond in ISK	2019	2021	At maturity	Fixed rates	3,303	-
Covered bond in ISK	2015-2019	2023	At maturity	Fixed rates	19,117	10,890
Covered bond in ISK - CPI-linked*	2012-2014	2019	At maturity	Fixed rates	-	8,937
Covered bond in ISK - CPI-linked	2014-2015	2020	At maturity	Fixed rates	4,316	4,248
Covered bond in ISK - CPI-linked	2015-2017	2022	At maturity	Fixed rates	18,313	18,009
Covered bond in ISK - CPI-linked	2012-2018	2024	At maturity	Fixed rates	35,484	35,009
Covered bond in ISK - CPI-linked	2015-2018	2026	At maturity	Fixed rates	27,406	26,992
Covered bond in ISK - CPI-linked	2019	2028	At maturity	Fixed rates	12,098	-
Covered bond in ISK - CPI-linked	2017-2018	2030	At maturity	Fixed rates	25,236	24,862
Covered bonds					145,273	138,813
Senior unsecured bond in SEK	2015	2019	At maturity	Fixed rates	-	7,844
Senior unsecured bond in EUR	2017	2019	At maturity	Fixed rates	-	4,398
Senior unsecured bond in SEK	2018	2019	At maturity	Fixed rates	1,345	1,302
Senior unsecured bond in EUR**	2016	2020	At maturity	Fixed rates	29,358	68,154
Senior unsecured bond in SEK	2018	2020	At maturity	Fixed rates	3,362	3,259
Senior unsecured bond in SEK	2019	2020	At maturity	Floating rates	4,710	-
Senior unsecured bond in SEK	2018	2021	At maturity	Fixed rates	1,347	1,311
Senior unsecured bond in SEK	2018-2019	2021	At maturity	Floating rates	19,568	15,053
Senior unsecured bond in SEK	2018	2022	At maturity	Floating rates	13,423	12,995
Senior unsecured bond in NOK	2019	2022	At maturity	Floating rates	14,692	-
Senior unsecured bond in EUR***	2018	2024	At maturity	Fixed rates	43,640	40,714
Senior unsecured bond in NOK	2019	2024	At maturity	Fixed rates	5,942	-
Senior unsecured bond in EUR	2019	2021	At maturity	Floating rates	1,626	-
Senior unsecured bond in EUR**	2019	2022	At maturity	Fixed rates	43,066	-
Bonds issued					182,079	155,030
Bills issued					10,121	6,729
Other debt securities					-	404
Other borrowed funds					10,121	7,133
Debt issued and other borrowed funds					337,473	300,976

*Íslandsbanki repurchased own covered bonds during the period amounting to ISK 4,319 million.

**These bond issuances are classified as being designated as at fair value through profit or loss. At 30 June 2019 the total carrying amount of the bonds amounted to ISK 72,424 million and included in the amount are fair value changes amounting to ISK 1,344 million. The carrying amount of the bond at 30 June 2019 was ISK 599 million higher than the contractual amount due at maturity. Íslandsbanki repurchased part of the bond issuance maturing in 2020 during the period, amounting to ISK 42,361 million.

***The Group applies hedge accounting to this bond issuance and uses certain EUR denominated interest rate swaps as hedging instruments (see Note 22). The interest rate swaps are hedging the exposure of the Group's changes in the fair value of this fixed-rate EUR denominated bond arising from changes in interest rates. The Group applies fair value hedge accounting to the hedging relationships. At 30 June 2019 the total carrying amount of the bond issuance amounted to ISK 43,640 million and included in the amount are fair value changes amounting to ISK 593 million.

The covered bond amounts do not contain the bonds reserved for securities lending.

Amounts are in ISK million

34. Subordinated loans

	Issued	Maturity	Maturity type	Terms of interest	30.6.2019	31.12.2018
Loans which qualify as Tier 2 capital:						
Subordinated loans in SEK	2017	2027	At maturity	Floating, STIBOR + 2.0%	10,040	9,724
Subordinated loans in SEK	2018	2028	At maturity	Floating, STIBOR + 2.5%	6,701	6,492
Subordinated loans in SEK	2019	2029	At maturity	Floating, STIBOR + 3.9%	6,690	-
Subordinated loans					23,431	16,216

35. Changes in liabilities arising from financing activities

			Non-cash changes			
	1.1.2019	Cash flows	Interest expense	Foreign exchange	Fair value changes	30.6.2019
Covered bonds NIL	20,756	1,050	614	-	-	22,420
Covered bonds CPI-linked	118,057	1,176	3,620	-	-	122,853
Senior unsecured bonds FX	46,162	17,148	477	2,228	-	66,015
Senior unsecured bonds FX at fair value	68,154	(2,154)	374	4,706	1,344	72,424
Senior unsecured bonds used for hedging	40,714	(465)	249	2,549	593	43,640
Short-term borrowings	7,133	2,787	178	23	-	10,121
Subordinated loans	16,216	6,510	173	532	-	23,431
Total	317,192	26,052	5,685	10,038	1,937	360,904

					Non-cash changes			
	31.12.2017	Reclas & remeasure	1.1.2018	Cash flows	Interest expense	Foreign exchange	Fair value changes	31.12.2018
Covered bonds NIL	17,589	-	17,589	2,055	1,112	-	-	20,756
Covered bonds CPI-linked	91,351	-	91,351	20,134	6,572	-	-	118,057
Senior unsecured bonds FX	37,182	(19,003)	18,179	23,275	531	4,177	-	46,162
Senior unsecured bonds FX at fair value	-	84,563	84,563	(20,083)	963	3,868	(1,157)	68,154
Senior unsecured bonds used for hedging ..	63,652	(63,652)	-	37,406	430	2,390	488	40,714
Short-term borrowings	7,974	-	7,974	(1,231)	390	-	-	7,133
Subordinated loans	9,505	-	9,505	5,629	198	884	-	16,216
Total	227,253	1,908	229,161	67,185	10,196	11,319	(669)	317,192

Amounts are in ISK million

36. Other liabilities

	30.6.2019	31.12.2018
Accruals	4,010	3,906
Liabilities to retailers for credit cards	18,937	20,722
Lease liabilities	4,385	-
Off-balance sheet loan commitments and financial guarantees	678	636
Withholding tax	755	1,733
Unsettled securities transactions	10,801	612
Deferred income	442	193
Sundry liabilities	1,973	1,841
Non-current liabilities and disposal groups held for sale	31	6
Other liabilities	42,012	29,649

Off-balance sheet loan commitments and financial guarantees

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2019	410	142	84	636
Transfer to Stage 1	99	(70)	(29)	-
Transfer to Stage 2	(11)	16	(5)	-
Transfer to Stage 3	(7)	(3)	10	-
Net remeasurement of loss allowance (including changes in models)	(123)	(44)	86	(81)
New loan commitments and financial guarantees	130	10	30	170
Derecognitions and maturities	(36)	(20)	9	(47)
At 30 June 2019	462	31	185	678

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2018	467	101	106	674
Transfer to Stage 1	595	(545)	(50)	-
Transfer to Stage 2	(58)	67	(9)	-
Transfer to Stage 3	(6)	(69)	75	-
Net remeasurement of loss allowance	(828)	481	(132)	(479)
New loan commitments and financial guarantees	521	130	132	783
Derecognitions and maturities	(281)	(23)	(38)	(342)
At 31 December 2018	410	142	84	636

37. Custody assets

	30.6.2019	31.12.2018
Custody assets - not managed by the Group	2,675,914	2,167,946

Amounts are in ISK million

38. Related party

Íslandsbanki is wholly owned by the Icelandic Government. The shares are administered by the Icelandic State Financial Investments (ISFI). As a result, the Icelandic Government and the Icelandic State Financial Investments are defined as related parties. The Group has applied the partial exemption for government-related entities, as described in IAS 24, and does not disclose those transactions in the related party note.

The Board of Directors and key management personnel of the Bank, ISFI and subsidiaries of the Bank, close family members of individuals referred to herein and legal entities controlled by them, are defined as related parties.

The Group's associates are also defined as related parties.

The Group's products and services are offered to the Icelandic Government and government-related entities in competition with other vendors and under generally accepted commercial terms. In a similar manner, the Bank and other Group entities purchase products and services from government-related entities under generally accepted commercial terms. Transactions with related parties were made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third party counterparties.

Cash and balances with the Central Bank are disclosed under Note 21 and Deposits from the Central Bank are disclosed under Note 30.

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

At 30 June 2019	Assets	Liabilities	Net balance	Commitments & overdrafts
Shareholders with control over the Group	-	-	-	1
Board of Directors, key management personnel and other related parties	258	381	(123)	62
Associated companies	143	671	(528)	226
Balances with related parties	401	1,052	(651)	289

1 January - 30 June 2019	Interest income	Interest expense	Other income	Other expense
Board of Directors and key management personnel	16	6	-	-
Associated companies	6	8	2	815
Transactions with related parties	22	14	2	815

At 31 December 2018	Assets	Liabilities	Net balance	Commitments & overdrafts
Shareholders with control over the Group	-	105	(105)	-
Board of Directors, key management personnel and other related parties	220	493	(273)	82
Associated companies	198	469	(271)	210
Balances with related parties	418	1,067	(649)	292

1 January - 30 June 2018	Interest income	Interest expense	Other income	Other expense
Shareholders with control over the Group	-	1	-	-
Board of Directors and key management personnel	7	8	-	-
Associated companies	9	4	1	911
Transactions with related parties	16	13	1	911

At 30 June 2019 ISK 2 million were recognised as Stage 1 expected credit loss against balances outstanding with related parties (2018: ISK 2 million). No share option programmes were operated during the reporting period.

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39. Contingencies

Contingent liabilities

Borgun hf.

Borgun hf., a subsidiary of Íslandsbanki, is a payment acquirer and issuing processor. Landsbankinn hf. sold its 31.2% stake in Borgun in late 2014. Landsbankinn claims that Borgun's management did not disclose all available information that might have affected the value of Borgun during the sales process, namely the worth of its stake in Visa Europe which was sold to Visa International shortly after the Borgun sale. In order to reclaim the alleged loss, Landsbankinn filed a lawsuit on 12 January 2017 against four defendants, including Borgun hf., claiming the right to damages for having been deprived of the true value of the stake involved in the sale. Landsbankinn does not quantify the claim, but its estimate of the lost profit from having sold its shares in Borgun is approximately ISK 1,930 million. Seeing that the conclusion of the case is uncertain and the financial effect cannot be estimated the Group has not recognised a provision in relation to this matter. The court has appointed professionals to assess certain matters regarding the claim but it is uncertain when the assessment will be completed. Therefore, it is uncertain when a ruling is to be expected.

40. Events after the reporting period

No events have arisen after the reporting period that require amendments or additional disclosures in the interim financial statements for the first half of 2019.

41. Risk management

Risk governance

The Group is exposed to various risk factors and managing these risks is an integral part of its operations. More information about the Group's risk management and risk assessment processes is available in the unaudited Pillar 3 Report. The Pillar 3 2018 Report is available on the Bank's website: www.islandsbanki.is.

42. Credit risk

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 financial contract with the Group.

Credit concentration risk is the significantly increased risk that is driven by common underlying factors, e.g. industrial sector, economy, geographical location, type of financial instrument or due to connections or relations among counterparties. This includes 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 loans and advances to customers and other banks but also from balances with the Central Bank and off-balance sheet items such as financial guarantees, loan commitments and derivatives.

The Group has policies and procedures dedicated to accepting, measuring, and managing credit risk. The objective of the Group's credit risk management is to achieve an appropriate balance between risk and return and to minimise potential adverse effects of credit risk on the Group's financial performance.

A thorough analysis of the counterparty's financial standing, analysis of past and estimated future cash flows as well as the borrower's general ability to repay its obligations forms the basis for all credit decisions. The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, groups of borrowers, countries and industry segments. The Group measures and consolidates its credit risk for each counterparty or group of connected clients in accordance with internal and external criteria of connection between parties.

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security in borrower's assets. The principal collateral types for loans are properties, vehicles, equipment, vessels and securities. When applicable, other credit risk mitigants are employed.

43. Maximum credit exposure

The Group'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. The maximum exposure for off-balance sheet items is the amount that the Group might have to pay out against financial guarantees and loan commitments, less provisions that have been made because of these items. The maximum credit exposure for a derivative contract is calculated by adding potential future credit exposure to the positive market value of the contract.

The industry breakdown shows the 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 Group's credit exposure, before taking account of any collateral held or other credit enhancements, is as follows:

At 30 June 2019	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	-	122,794	-	-	-	-	-	-	-	-	-	122,794
Bonds and debt instruments	-	53,406	-	-	171	20,664	1,512	67	951	262	-	77,033
Derivatives	2	-	243	-	2,604	6,032	642	325	-	116	329	10,293
Loans to credit institutions	-	-	-	-	-	77,387	-	-	-	-	-	77,387
Loans to customers:	334,749	-	135,041	33,445	6,934	23	81,784	26,052	11,453	153,077	111,888	894,446
Overdrafts	11,965	-	16,280	3,781	107	1	6,473	477	335	3,266	9,151	51,836
Credit cards	15,055	-	1,496	232	5	21	437	35	112	61	38	17,492
Mortgages	267,762	-	-	-	-	-	-	-	-	-	-	267,762
Capital leases	6,130	-	33,034	2,239	6	-	7,750	109	43	1,051	226	50,588
Other loans	33,837	-	84,231	27,193	6,816	1	67,124	25,431	10,963	148,699	102,473	506,768
Other financial assets	416	6	575	2	1	14,949	115	222	73	19	11	16,389
Off-balance sheet items:	34,546	-	23,739	16,733	10,725	7,307	15,420	2,052	5,386	24,414	15,108	155,430
Financial guarantees	1,469	-	5,923	5,295	62	1,173	2,277	82	37	1,956	262	18,536
Undrawn loan commitments	-	-	2,942	8,618	10,163	-	7,472	1,436	-	16,298	6,527	53,456
Undrawn overdrafts	9,269	-	10,636	2,066	474	6,006	4,612	407	4,654	5,914	8,167	52,205
Credit card commitments	23,808	-	4,238	754	26	128	1,059	127	695	246	152	31,233
Total maximum credit exposure	369,713	176,206	159,598	50,180	20,435	126,362	99,473	28,718	17,863	177,888	127,336	1,353,772

Amounts are in ISK million

43. Cont'd

At 31 December 2018	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	-	135,056	-	-	-	-	-	-	-	-	-	135,056
Bonds and debt instruments	-	53,341	-	-	447	12,925	1,724	68	724	186	-	69,415
Derivatives	-	-	121	2	2,322	4,687	451	1,090	-	61	205	8,939
Loans to credit institutions	-	-	-	-	-	41,577	-	-	-	-	-	41,577
Loans to customers:	319,390	-	124,242	29,095	6,858	1,704	79,824	23,799	12,087	142,885	106,715	846,599
Overdrafts	11,769	-	11,699	3,304	31	1,509	4,483	780	754	4,501	9,751	48,581
Credit cards	15,779	-	1,516	251	4	21	433	33	112	59	34	18,242
Mortgages	249,296	-	-	-	-	-	-	-	-	-	-	249,296
Capital leases	6,504	-	27,552	2,270	5	-	7,166	116	48	1,197	258	45,116
Other loans	36,042	-	83,475	23,270	6,818	174	67,742	22,870	11,173	137,128	96,672	485,364
Other financial assets	409	-	451	5	1	6,532	23	34	3	18	35	7,511
Off-balance sheet items:	33,928	-	24,673	18,703	6,091	8,160	12,413	3,817	4,517	20,850	12,805	145,957
Financial guarantees	1,494	-	5,863	4,563	12	1,172	2,416	160	5	1,828	508	18,021
Undrawn loan commitments	-	-	4,986	11,662	5,996	-	4,899	1,100	-	14,629	5,782	49,054
Undrawn overdrafts	10,187	-	9,908	1,830	63	6,863	4,124	2,433	3,884	4,167	6,374	49,833
Credit card commitments	22,247	-	3,916	648	20	125	974	124	628	226	141	29,049
Total maximum credit exposure	353,727	188,397	149,487	47,805	15,719	75,585	94,435	28,808	17,331	164,000	119,760	1,255,054

Amounts are in ISK million

44. 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 Group takes a charge over assets such as real estate, 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 Group 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 Group'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 the gross carrying amount of loans and nominal off-balance sheet items, and is measured without including the effect of overcollateralisation. This means that if some loans have collateral values in excess of their gross carrying amount, then the excess is removed in order to reflect the Group's actual maximum exposure to credit risk. The total value of pledged assets can thus be higher than the cover indicates. The maximum credit risk exposure is measured on net carrying value basis, and therefore collateral allocation can in some instances be higher.

For capital leases the Group remains the owner of the leased object. In total ISK 40,432 million of the collateral are leased objects.

The following tables show the maximum exposure to credit risk by class of financial asset and collateral held against those exposures. An overview of collateral held by the Group against credit exposure is shown below for exposures in Stages 1 and 2 (non credit-impaired) and exposures in Stage 3 (credit-impaired):

At 30 June 2019

Collateral held against non credit-impaired exposures	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral
Derivatives	10,293	-	-	1,943	-	-	1,943
Loans and commitments to customers:	1,031,756	602,698	92,319	10,180	54,373	72,919	832,489
Individuals	361,483	280,939	6	350	13,453	131	294,879
Commerce and services	153,980	60,686	865	330	31,937	23,856	117,674
Construction	49,846	32,654	-	589	1,981	3,573	38,797
Energy	17,659	4,129	-	448	-	6	4,583
Financial services*	7,330	-	-	118	-	-	118
Industrial and transportation	94,427	42,780	11	108	6,525	15,989	65,413
Investment companies	27,873	9,906	-	3,299	92	11,567	24,864
Public sector and non-profit organisations	16,769	964	-	6	28	-	998
Real estate	175,652	156,322	-	1,804	229	1,249	159,604
Seafood	126,737	14,318	91,437	3,128	128	16,548	125,559
Total	1,042,049	602,698	92,319	12,123	54,373	72,919	834,432

*Included is off-balance sheet exposure towards credit institutions amounting to ISK 3.7 billion.

Collateral held against credit-impaired exposures	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral
Loans and commitments to customers:	18,120	12,221	1,415	123	1,201	747	15,707
Individuals	7,812	6,813	17	8	164	3	7,005
Commerce and services	4,800	2,620	-	1	900	516	4,037
Construction	332	253	-	2	22	6	283
Industrial and transportation	2,777	270	1,369	112	79	165	1,995
Investment companies	231	208	-	-	-	-	208
Public sector and non-profit organisations	70	39	-	-	-	-	39
Real estate	1,839	1,887	-	-	5	-	1,892
Seafood	259	131	29	-	31	57	248
Total	18,120	12,221	1,415	123	1,201	747	15,707

Amounts are in ISK million

44. Cont'd

At 31 December 2018 **Collateral held against non credit-impaired exposures**	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral
Derivatives	8,939	-	-	2,232	-	-	2,232
Loans and commitments to customers:	978,396	563,362	89,350	6,149	49,883	69,902	778,646
Individuals	347,490	266,508	6	359	13,485	155	280,513
Commerce and services	146,286	56,407	733	189	27,574	23,915	108,818
Construction	47,495	28,694	-	379	1,880	3,761	34,714
Energy	12,949	3,737	-	366	-	5	4,108
Financial services	9,864	-	-	309	-	-	309
Industrial and transportation	89,289	39,523	9	82	6,437	15,980	62,031
Investment companies	27,392	9,588	26	2,891	83	11,361	23,949
Public sector and non-profit organisations	16,551	974	-	7	37	2	1,020
Real estate	161,864	144,530	-	1,549	231	1,113	147,423
Seafood	119,216	13,401	88,576	18	156	13,610	115,761
Total	987,335	563,362	89,350	8,381	49,883	69,902	780,878

Collateral held against credit-impaired exposures	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral
Loans and commitments to customers:	14,160	9,003	2,282	106	328	487	12,206
Individuals	5,828	5,256	17	7	83	3	5,366
Commerce and services	2,629	1,023	139	-	78	247	1,487
Construction	303	232	-	-	21	14	267
Industrial and transportation	2,948	317	2,077	99	109	170	2,772
Investment companies	224	180	-	-	-	-	180
Public sector and non-profit organisations	53	37	-	-	-	-	37
Real estate	1,871	1,829	-	-	1	-	1,830
Seafood	304	129	49	-	36	53	267
Total	14,160	9,003	2,282	106	328	487	12,206

45. Credit quality of financial assets

The following table provides the gross carrying amount of loans and credit risk exposure on loan commitments and financial guarantees. Amounts are broken down by risk class and the method by which their respective credit loss allowances (ECL) are calculated, i.e. Stage 1, 2 and 3.

The Group 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 Group uses two different statistical rating models. One model is for individuals and another is for small companies with a total exposure to the Group 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.

Amounts are in ISK million

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Risk classes 1-4 represent low risk, risk classes 5-6 moderate risk, risk classes 7-8 increased risk, risk class 9 high risk, and risk class 10 represents customers that are 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.

Further information on the risk classes, including the mapping from risk classes to the probability of default, can be found in Section 4.2.2 of the unaudited Pillar 3 2018 Report.

The same customer can have loans and off-balance sheet commitments in Stages 1 and 2 simultaneously. However, if a customer has an exposure in Stage 3 then all other loans and commitments are classified as Stage 3 as well.

As explained in Note 72.3 in the consolidated financial statements for the year 2018, the Group has a new harmonised definition of default. The new definition is broader than each individual definition, in particular the previous definition of Risk class 10.

In the following tables ISK 3.7 billion of off-balance sheet exposure are towards credit institutions, all of which is classified as Stage 1.

At 30 June 2019

Loans to customers:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	220,063	106	-	220,169
Risk class 5-6	390,079	5,405	-	395,484
Risk class 7-8	200,809	14,911	-	215,720
Risk class 9	38,058	7,593	-	45,651
Risk class 10	-	-	21,954	21,954
Unrated	4,390	30	133	4,553
	853,399	28,045	22,087	903,531
Expected credit loss	(3,804)	(668)	(4,613)	(9,085)
Net carrying amount	849,595	27,377	17,474	894,446

Off-balance sheet loan commitments and financial guarantees:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	71,762	55	-	71,817
Risk class 5-6	57,326	4,068	-	61,394
Risk class 7-8	19,091	1,114	-	20,205
Risk class 9	1,270	485	-	1,755
Risk class 10	-	-	831	831
Unrated	102	4	-	106
	149,551	5,726	831	156,108
Expected credit loss	(462)	(31)	(185)	(678)
Total	149,089	5,695	646	155,430

At 30 June 2019	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	ECL	Total
Loans and commitments to customers:								
Individuals	76,938	138,973	111,630	31,486	8,879	4,056	(2,667)	369,295
Commerce and services	31,208	93,904	24,389	5,131	6,035	402	(2,289)	158,780
Construction	3,665	25,266	19,937	1,332	389	48	(459)	50,178
Energy	15,877	582	1,229	-	1	-	(30)	17,659
Financial services	6,940	396	4	-	-	4	(14)	7,330
Industrial and transportation	28,781	53,081	8,421	4,573	4,066	67	(1,785)	97,204
Investment companies	2,395	9,534	15,999	369	476	1	(670)	28,104
Public sector and non-profit organisations	13,730	2,715	268	-	90	70	(34)	16,839
Real estate	41,450	85,862	46,484	2,681	2,336	10	(1,332)	177,491
Seafood	71,002	46,565	7,564	1,834	513	1	(483)	126,996
Total	291,986	456,878	235,925	47,406	22,785	4,659	(9,763)	1,049,876

Amounts are in ISK million

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At 31 December 2018

Loans to customers:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	213,012	104	-	213,116
Risk class 5-6	367,843	1,055	-	368,898
Risk class 7-8	184,807	15,339	-	200,146
Risk class 9	38,633	12,363	-	50,996
Risk class 10	-	-	17,215	17,215
Unrated	4,137	41	95	4,273
	808,432	28,902	17,310	854,644
Expected credit loss	(3,277)	(1,079)	(3,689)	(8,045)
Net carrying amount	805,155	27,823	13,621	846,599

Off-balance sheet loan commitments and financial guarantees:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	68,712	30	-	68,742
Risk class 5-6	55,112	194	-	55,306
Risk class 7-8	16,913	1,899	-	18,812
Risk class 9	1,517	1,460	-	2,977
Risk class 10	-	-	623	623
Unrated	130	3	-	133
	142,384	3,586	623	146,593
Expected credit loss	(410)	(142)	(84)	(636)
Total	141,974	3,444	539	145,957

At 31 December 2018	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	ECL	Total
Loans and commitments to customers:								
Individuals	74,325	135,721	101,859	33,354	6,955	3,499	(2,395)	353,318
Commerce and services	33,700	84,690	23,538	5,455	3,718	585	(2,771)	148,915
Construction	3,387	21,930	21,711	1,024	336	53	(643)	47,798
Energy	11,472	544	965	-	-	-	(32)	12,949
Financial services	9,450	419	8	-	-	4	(17)	9,864
Industrial and transportation	34,253	41,922	8,331	4,930	3,705	69	(973)	92,237
Investment companies	5,709	6,976	10,751	4,241	414	-	(475)	27,616
Public sector and non-profit organisations	13,150	3,119	240	-	52	66	(23)	16,604
Real estate	41,768	73,484	44,312	2,909	2,172	36	(946)	163,735
Seafood	54,644	55,399	7,243	2,060	486	94	(406)	119,520
Total	281,858	424,204	218,958	53,973	17,838	4,406	(8,681)	992,556

Amounts are in ISK million

46. Forbearance and write-offs

When restructuring or modification measures are believed to be more appropriate than collection procedures, the Group offers several debt relief measures and restructuring frameworks for customers in financial difficulties. These forbearance measures include temporary payment holidays, extension of loan terms, capitalisation of arrears and waiving of covenants.

When a loan has been renegotiated or modified but not derecognised the Group also reassesses, after a certain trial period, whether the loan is still considered to have a significant increase in credit risk. The Group also considers whether forborne assets classified as Stage 3 should be recognised and transferred to Stage 2.

Once an asset has been classified as forborne, it will remain forborne for a minimum 24-month probation period. In order for a loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:
- All of the customer's facilities have to be considered performing; and
- The customer does not have any contract that is more than 30 days past due; and
- The probation period of two years has passed from the date the forborne contract was considered performing; and
- Regular payments of more than an insignificant amount of principal or interest have been made during at least half of the probation period.

The following table provides a summary of the Group's forborne assets.

At 30 June 2019

	Stage 1	Stage 2	Stage 3	Total
Individuals	1,291	2,074	1,476	4,841
Companies	14,001	7,583	6,021	27,605
Gross carrying amount	15,292	9,657	7,497	32,446

	Stage 1	Stage 2	Stage 3	Total
Individuals	(9)	(61)	(178)	(248)
Companies	(81)	(209)	(1,714)	(2,004)
Expected credit loss	(90)	(270)	(1,892)	(2,252)

Gross carrying amount written off during the first half of 2019 and still subject to enforcement activity:	Gross carrying amount
Individuals	285
Companies	754
Total	1,039

At 31 December 2018

	Stage 1	Stage 2	Stage 3	Total
Individuals	1,741	2,020	1,238	4,999
Companies	14,377	2,016	4,588	20,981
Gross carrying amount	16,118	4,036	5,826	25,980

	Stage 1	Stage 2	Stage 3	Total
Individuals	(13)	(92)	(198)	(303)
Companies	(139)	(49)	(1,160)	(1,348)
Expected credit loss	(152)	(141)	(1,358)	(1,651)

Gross carrying amount written off during the first half of 2018 and still subject to enforcement activity:	Gross carrying amount
Individuals	477
Companies	250
Total	727

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47. Large exposures disclosure

When the Group's total exposure to a group of connected clients is 10% or higher of the Group'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 regulation no. 233/2017. The Group has internal criteria that define connections between clients. These criteria reflect the Group's interpretation of Article (1)(a) of the Act on Financial Undertakings no. 161/2002, where groups of connected clients are defined.

The exposure is evaluated both before and after credit risk mitigating effects. After mitigating effects, the Group currently has four large exposures. No large exposure is above the maximum 25% single large exposure limit set by the law.

The following tables show the Group's large exposures as a percentage of the Group's capital base, before and after eligible credit risk mitigating effects.

At 30 June 2019

Groups of connected clients:	Before	After
Group 1	67%	-
Group 2	13%	11%
Group 3	12%	11%
Group 4	12%	11%
Group 5	11%	11%

At 31 December 2018

Groups of connected clients:	Before	After
Group 1	73%	-
Group 2	12%	12%
Group 3	12%	11%
Group 4	11%	11%
Group 5	13%	11%

48. Liquidity risk

The Group 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.

The Group's main source of funding is customer deposits. Treasury is responsible for the Bank's funding and liquidity management in line with internal and regulatory limits and policies. Treasury manages the Bank's intraday liquidity. Risk Management, as the second line of defence, is responsible for independent reporting on the liquidity position to internal and external stakeholders and providing a holistic view on liquidity risk on a consolidated basis.

49. Liquidity Coverage and Net Stable Funding Ratio

Key measures for the assessment of liquidity risk are the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). The Central Bank of Iceland, which is the main supervisory authority regarding liquidity risk, has incorporated the LCR and the NSFR based on the CRD IV standards into the rules on liquidity ratio and the rules on funding ratio in foreign currencies. In addition, the Group complies with the Financial Supervisory Authority's guidelines no. 2/2010 on best practices in liquidity management and liquidity coverage ratio rules no. 266/2017.

The following tables show the NSFR and the LCR for the Group at the end of June 2019 and at year-end 2018.

Net Stable Funding Ratio	30.6.2019	31.12.2018
For all currencies	117%	114%
Foreign currencies	179%	149%

Amounts are in ISK million

49. Cont'd

Liquidity Coverage Ratio	30.6.2019	31.12.2018
For all currencies	185%	172%
Foreign currencies	456%	544%

At 30 June 2019	For all currencies		Foreign currencies	
	Unweighted	Weighted	Unweighted	Weighted
Liquid assets level 1*	162,096	162,096	46,142	46,142
Liquid assets level 2	3,725	841	3,725	841
Total liquid assets	165,821	162,937	49,867	46,983
Deposits	453,068	130,214	78,700	32,633
Debt issued	1,411	1,411	174	174
Other outflows	123,552	44,370	24,203	8,371
Total outflows	578,031	175,995	103,077	41,178
Short-term deposits with other banks**	75,750	72,788	75,625	72,788
Other inflows	30,313	15,303	4,578	3,884
Restrictions on inflows	-	-	-	(45,789)
Total inflows	106,063	88,091	80,203	30,883
Liquidity coverage ratio		185%		456%

At 31 December 2018	For all currencies		Foreign currencies	
	Unweighted	Weighted	Unweighted	Weighted
Liquid assets level 1*	169,217	169,217	42,608	42,608
Liquid assets level 2	2,754	775	2,754	775
Total liquid assets	171,971	169,992	45,362	43,383
Deposits	455,883	127,018	67,513	25,191
Debt issued	875	875	875	875
Other outflows	72,598	32,095	15,277	5,849
Total outflows	529,356	159,988	83,665	31,915
Short-term deposits with other banks**	39,718	39,718	39,716	39,716
Other inflows	42,739	21,443	9,702	7,950
Restrictions on inflows	-	-	-	(23,730)
Total inflows	82,457	61,161	49,418	23,936
Liquidity coverage ratio		172%		544%

*Level 1 liquid assets include cash and balances with the Central Bank, domestic bonds eligible as collateral against borrowing at the Central Bank and foreign government bonds in accordance with rules no. 266/2017 on liquidity ratio.

**Short-tem deposits with other banks with maturity less than 30 days.

Amounts are in ISK million

49. Cont'd

Deposits by Liquidity Coverage Ratio category

The Group's deposits are categorised by counterparty according to the Liquidity Coverage Ratio (LCR) standard. The groups are listed in order of estimated stability and the respective LCR outflow weight. Deposits are also classified as stable if the customer has an established business relationship with the Bank and is covered by an effective insurance scheme.

	Deposits maturing within 30 days					
At 30 June 2019	Less stable	Weight (%)	Stable	Weight (%)	Term deposits	Total deposits
Retail	219,088	12%	85,374	5%	76,265	380,726
Operational relationships	3,227	25%	-	5%	-	3,227
Corporations	70,747	40%	334	20%	23,303	94,384
Sovereigns, Central Bank and public sector entities	8,641	40%	278	20%	530	9,449
Pension funds	35,180	100%	-	-	31,462	66,642
Domestic financial entities	28,513	100%	-	-	37,447	65,960
Foreign financial entities	4,912	100%	-	-	10,399	15,311
Total	370,308		85,986		179,406	635,699

	Deposits maturing within 30 days					
At 31 December 2018	Less stable	Weight (%)	Stable	Weight (%)	Term deposits	Total deposits
Retail	216,428	12%	80,804	5%	78,476	375,708
Operational relationships	2,572	25%	-	5%	-	2,572
Corporations	63,887	40%	341	20%	22,809	87,037
Sovereigns, Central Bank and public sector entities	7,613	40%	246	20%	591	8,450
Pension funds	30,686	100%	-	-	26,987	57,673
Domestic financial entities	27,467	100%	-	-	24,622	52,089
Foreign financial entities	3,242	100%	-	-	7,807	11,049
Total	351,895		81,391		161,292	594,578

50. Maturity analysis of assets and liabilities

The following tables show the contractual payments of principal and interest for the Group'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 accordance with the IFRS 16 standard lease liabilities have been added to the maturity analysis of financial liabilities.

Maturity analysis 30 June 2019

Financial liabilities	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Deposits from CB and credit institutions	19,830	6,745	5,242	6,494	2,994	-	-	21,475
Deposits from customers	615,869	435,587	89,813	39,858	24,631	46,774	-	636,663
Debt issued and other borrowed funds	337,473	-	2,582	12,925	330,908	90,711	-	437,126
Subordinated loans	23,431	-	94	442	3,037	38,561	-	42,134
Other financial liabilities:	40,499	33,739	2,493	353	1,818	2,644	-	41,047
Lease liabilities	4,385	-	118	353	1,818	2,644	-	4,933
Other liabilities	36,114	33,739	2,375	-	-	-	-	36,114
Total	1,037,102	476,071	100,224	60,072	363,388	178,690	-	1,178,445

Amounts are in ISK million

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Off-balance sheet liabilities show the amount of contractual obligations that the Group 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 Group'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 Group 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	18,536	-	-	-	-	-	18,536
Undrawn loan commitments	53,456	-	-	-	-	-	53,456
Undrawn overdrafts	52,205	-	-	-	-	-	52,205
Credit card commitments	31,233	-	-	-	-	-	31,233
Total	155,430	-	-	-	-	-	155,430
Total non-derivative financial liabilities and off-balance sheet liabilities	631,501	100,224	60,072	363,388	178,690	-	1,333,875

The table below shows the contractual cash flow of the Group's derivative liabilities, i.e. derivatives that have a negative and a positive carrying amount at the reporting date. 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.

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	-	41,280	44,329	56,913	-	-	142,522
Outflow	-	(30,584)	(39,993)	(59,101)	-	-	(129,678)
Total	-	10,696	4,336	(2,188)	-	-	12,844
Net settled derivatives	-	(805)	-	-	-	-	(805)
Total	-	9,891	4,336	(2,188)	-	-	12,039

Maturity classification of assets is based on contractual maturity. 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 Central Bank	122,794	9,358	113,436	-	-	-	-	122,794
Bonds and debt instruments	77,033	-	22,778	26,292	13,018	14,945	-	77,033
Shares and equity instruments	19,176	-	-	-	-	-	19,176	19,176
Loans to credit institutions	77,387	32,253	43,060	-	2,074	-	-	77,387
Loans to customers	894,446	2,551	87,468	88,982	308,952	406,493	-	894,446
Other financial assets	16,389	15,798	533	49	9	-	-	16,389
Total	1,207,225	59,960	267,275	115,323	324,053	421,438	19,176	1,207,225

Amounts are in ISK million

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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	-	27,824	41,712	27,479	6,724	-	103,739
Outflow	-	(22,609)	(41,748)	(27,519)	(6,557)	-	(98,433)
Total	-	5,215	(36)	(40)	167	-	5,306
Net settled derivatives	-	85	-	-	-	-	85
Total	-	5,300	(36)	(40)	167	-	5,391

The tables below show the comparative amounts for maturity analysis at year-end 2018.

Maturity analysis 31 December 2018

Financial liabilities	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Deposits from CB and credit institutions	15,619	4,594	3,229	4,992	3,249	-	-	16,064
Deposits from customers	578,959	420,242	81,178	37,952	26,976	38,070	-	604,418
Debt issued and other borrowed funds	300,976	404	24,214	21,178	154,315	141,098	-	341,209
Subordinated loans	16,216	-	90	307	2,242	20,417	-	23,056
Other financial liabilities	27,186	24,431	1,729	1,026	-	-	-	27,186
Total	938,956	449,671	110,440	65,455	186,782	199,585	-	1,011,933

Off-balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial guarantees	18,021	-	-	-	-	-	18,021
Undrawn loan commitments	49,054	-	-	-	-	-	49,054
Undrawn overdrafts	49,833	-	-	-	-	-	49,833
Credit card commitments	29,049	-	-	-	-	-	29,049
Total	145,957	-	-	-	-	-	145,957
Total non-derivative financial liabilities and off-balance sheet liabilities	595,628	110,440	65,455	186,782	199,585	-	1,157,890

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	-	20,124	23,147	49,380	1,771	-	94,422
Outflow	-	(20,638)	(24,189)	(51,654)	(1,943)	-	(98,424)
Total	-	(514)	(1,042)	(2,274)	(172)	-	(4,002)
Net settled derivatives	-	(280)	-	-	-	-	(280)
Total	-	(794)	(1,042)	(2,274)	(172)	-	(4,282)

Amounts are in ISK million

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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 Central Bank	135,056	47,746	87,310	-	-	-	-	135,056
Bonds and debt instruments	69,415	-	18,946	24,189	14,409	11,604	267	69,415
Shares and equity instruments	13,074	-	-	-	-	-	13,074	13,074
Loans to credit institutions	41,577	24,152	17,425	-	-	-	-	41,577
Loans to customers	846,599	2,054	90,269	74,716	282,624	396,936	-	846,599
Other financial assets	7,511	1,888	475	71	9	-	5,068	7,511
Total	1,113,232	75,840	214,425	98,976	297,042	408,540	18,409	1,113,232

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	-	57,050	22,267	77,126	327	-	156,770
Outflow	-	(56,077)	(21,929)	(74,072)	(343)	-	(152,421)
Total	-	973	338	3,054	(16)	-	4,349
Net settled derivatives	-	869	-	-	-	-	869
Total	-	1,842	338	3,054	(16)	-	5,218

51. Market risk

The Group 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 within the Group can broadly be split into two categories, trading book and banking book. The trading book includes market risk exposures related, directly or indirectly, to the Group's short- and medium-term trading in securities, currencies and other capital market instruments and derivatives. 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. The banking book includes market risk exposures related to securities held for long-term investment purposes, unlisted securities or holdings in subsidiaries or affiliates. A large part of the banking book market risk is due to mismatches in the composition of assets and liabilities, for example with respect to currencies, interest rates, CPI-indexation or other factors that can affect the Group's earnings or earnings volatility. These mismatches are reported to management and are subject to internal and regulatory limits.

52. Derivatives

The Group uses derivatives to hedge currency exposure, interest rate risk in the banking book as well as inflation risk. However, the Group is subject to indirect exposure through customers' margin trading. Margin trading is subject to continuous monitoring and collateral requirements. Other derivatives held for trading or for other purposes are insignificant.

53. Interest rate risk

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

Sensitivity measures like Basis Point Value (BPV) are used 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.

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53. Cont'd

Interest rate risk in the trading book

The fixed income trading unit invests mainly in government bonds, bonds issued by the Housing Financing Fund (HFF) which are guaranteed by the Icelandic Government, domestic municipality bonds and covered bonds issued by other Icelandic banks. Bonds and bills in the Group's liquidity portfolio are also categorised in the trading book. In the table below the total market value (MV) of long and short positions may not be the same as reported in Note 5 since netting between short and long positions is not applied here. Derivatives and securities used for hedging are excluded from the table.

	30.6.2019			31.12.2018		
Trading bonds and debt instruments, long positions	MV	Duration	BPV	MV	Duration	BPV
Indexed	2,418	6.07	(1.47)	1,872	6.13	(1.15)
Non-indexed	46,391	0.44	(2.03)	43,550	0.32	(1.40)
Total	48,809	0.72	(3.50)	45,422	0.56	(2.55)

	30.6.2019			31.12.2018		
Trading bonds and debt instruments, short positions	MV	Duration	BPV	MV	Duration	BPV
Non-indexed	-	-	-	198	5.00	0.09
Total	-	-	-	198	5.00	0.09
Net position of trading bonds and debt instruments	48,809	0.72	(3.50)	45,224	0.54	(2.46)

Interest rate risk in the banking book

Interest rate risk in the banking book arises from the Group'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 Group's assets and liabilities are of different maturities and are priced relative to different interest rates.

The following table shows the interest sensitivity of the Group's banking book from a parallel 100 basis points change in all yield curves, with all other variables held constant, categorised by the date of next interest rate reset.

Sensitivity analysis for interest rate risk in the banking book

At 30 June 2019

Currency	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
ISK, indexed	3	141	(221)	(1,815)	2,006	21	135
ISK, non-indexed	11	17	(48)	55	(9)	-	26
EUR	10	(23)	(17)	119	-	-	89
SEK	10	(3)	-	-	-	-	7
USD	(38)	(5)	-	-	-	-	(43)
Other	13	(6)	-	4	-	-	11
Total	9	121	(286)	(1,637)	1,997	21	225

At 31 December 2018

Currency	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
ISK, indexed	20	8	110	(3,318)	3,185	72	77
ISK, non-indexed	9	57	(7)	(193)	(77)	(1)	(212)
EUR	87	(25)	13	(1,605)	1,709	-	179
SEK	92	-	(16)	-	-	-	76
USD	(63)	-	-	-	-	-	(63)
Other	(1)	(11)	-	-	-	-	(12)
Total	144	29	100	(5,116)	4,817	71	45

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54. Currency risk

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 Group'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.

Currency analysis at 30 June 2019

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	CAD	Other foreign currencies	Total foreign currencies
Cash and balances with Central Bank	824	380	227	59	15	65	93	116	4	207	1,990
Bonds and debt instruments	21,285	11,414	24	-	-	-	13,083	-	-	-	45,806
Shares and equity instruments	52	380	424	-	-	-	43	-	-	-	899
Loans to credit institutions	22,944	38,230	4,830	283	553	80	5,498	1,537	5	1,131	75,091
Loans to customers	116,545	28,892	2,093	698	3,419	2	4,198	1,197	-	6,187	163,231
Other assets	1,399	2,511	1,181	3	-	8	3	14	1	946	6,066
Total assets	163,049	81,807	8,779	1,043	3,987	155	22,918	2,864	10	8,471	293,083
Liabilities											
Deposits from credit institutions	8,808	950	92	-	-	-	18	-	-	-	9,868
Deposits from customers	32,699	34,647	4,426	336	539	989	2,962	2,121	-	546	79,265
Debt issued and other borrowed funds	117,689	-	-	-	-	43,755	20,634	-	-	-	182,078
Subordinated loans	-	-	-	-	-	23,431	-	-	-	-	23,431
Other liabilities	2,891	1,428	1,529	6	23	47	4	54	34	887	6,903
Total liabilities	162,087	37,025	6,047	342	562	68,222	23,618	2,175	34	1,433	301,545
Net on-balance sheet position	962	44,782	2,732	701	3,425	(68,067)	(700)	689	(24)	7,038	(8,462)
Net off-balance sheet position	(2,188)	(47,113)	(2,496)	(712)	(3,467)	68,052	465	(659)	-	(6,283)	5,599
Net position	(1,226)	(2,331)	236	(11)	(42)	(15)	(235)	30	(24)	755	(2,863)

Amounts are in ISK million

54. Cont'd

Currency analysis at 31 December 2018

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	CAD	Other foreign currencies	Total foreign currencies
Cash and balances with Central Bank	377	250	135	23	10	54	51	88	29	73	1,090
Bonds and debt instruments	32,313	10,968	24	-	-	-	-	-	-	-	43,305
Shares and equity instruments	45	2,202	398	-	-	-	40	-	-	-	2,685
Loans to credit institutions	15,662	12,614	4,488	258	613	4,683	1,901	530	123	538	41,410
Loans to customers	105,852	31,603	2,037	734	3,213	2	4,318	572	5,710	39	154,080
Other assets	1,270	2,056	834	4	91	83	2	45	-	1,737	6,122
Total assets	155,519	59,693	7,916	1,019	3,927	4,822	6,312	1,235	5,862	2,387	248,692
Liabilities											
Deposits from credit institutions	5,622	538	83	-	96	-	16	-	-	-	6,355
Deposits from customers	26,605	26,819	4,293	329	430	927	3,211	1,728	434	144	64,920
Debt issued and other borrowed funds	113,670	-	-	-	-	41,764	-	-	-	-	155,434
Subordinated loans	-	-	-	-	-	16,216	-	-	-	-	16,216
Other liabilities	2,502	1,269	578	30	266	82	154	138	-	2,098	7,117
Total liabilities	148,399	28,626	4,954	359	792	58,989	3,381	1,866	434	2,242	250,042
Net on-balance sheet position	7,120	31,067	2,962	660	3,135	(54,167)	2,931	(631)	5,428	145	(1,350)
Net off-balance sheet position	(7,589)	(31,140)	(2,964)	(667)	(3,170)	54,350	(2,844)	642	(5,418)	(147)	1,053
Net position	(469)	(73)	(2)	(7)	(35)	183	87	11	10	(2)	(297)

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

55. Inflation risk

The Group is exposed to inflation risk since the value of CPI-linked assets exceeds CPI-linked 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 affect profit and loss. A 1% increase in the index would lead to an ISK 133 million increase in the balance sheet and a 1% decrease would lead to a corresponding decrease, other risk factors held constant.

Assets, CPI-linked	30.6.2019	31.12.2018
Bonds and debt instruments	3,045	2,721
Loans to customers	295,982	293,917
Total assets	299,027	296,638
Liabilities, CPI-linked		
Deposits from customers	94,628	95,917
Debt issued and other borrowed funds	122,900	118,103
Off-balance sheet position	68,200	70,617
Total liabilities	285,728	284,637
CPI imbalance	13,299	12,001

56. Capital management

The following table shows the capital base, risk exposure amount, the resulting capital ratios, and leverage for the Group at 30 June 2019 and 31 December 2018.

The Group's regulatory capital requirement is calculated according to CRD IV as implemented through Act no. 161/2002 on Financial Undertakings and regulation no. 233/2017 on prudential requirements for financial undertakings. Capital requirement calculations for credit risk and market risk are based on the standardised approach whereas the capital requirement calculations for operational risk are based on the basic indicator approach.

The Group aims at managing its capital position and the corresponding capital ratios above the overall regulatory capital requirement. According to the latest SREP report from the Financial Supervisory Authority, published in October 2018, the overall capital requirement is 19.3%. The Group's capital target includes a 0.5-2.0% management buffer on top of the overall capital requirement.

The minimum leverage ratio for Icelandic financial institutions is 3%.

	30.6.2019	31.12.2018
CET1 capital		
Ordinary share capital	10,000	10,000
Share premium	55,000	55,000
Reserves	6,816	6,499
Retained earnings	101,534	102,496
Non-controlling interests	2,434	2,318
Fair value changes due to own credit standing	760	376
Tax assets	(394)	(215)
Intangible assets	(4,882)	(5,002)
Total CET1 capital	171,268	171,472
Tier 2 capital		
Qualifying subordinated liabilities	23,431	16,216
Total capital base	194,699	187,688

Amounts are in ISK million

56. Cont'd

	30.6.2019	31.12.2018
Risk exposure amount		
- due to credit risk	809,840	750,801
- due to market risk	13,988	7,622
Market risk, trading book	10,072	6,649
Currency risk	3,916	973
- due to credit valuation adjustment	2,815	2,385
- due to operational risk	85,141	85,141
Total risk exposure amount	911,784	845,949
Capital ratios		
CET1 ratio	18.8%	20.3%
Total capital ratio	21.4%	22.2%
Official Tier 1 ratio	18.8%	20.3%
Official capital ratio	21.4%	22.2%
Leverage ratio		
Exposure amount		
On-balance sheet exposures	1,218,856	1,120,637
Off-balance sheet exposures	47,736	47,119
Derivative exposures	10,285	8,935
Leverage ratio total exposure measure	1,276,877	1,176,691
Tier 1 capital	171,268	171,472
Leverage ratio	13.4%	14.6%

Financial Statements first half 2019 55 Amounts are in ISK million

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