# Condensed Consolidated Interim Financial Statements

for the nine months ended 30 September 2015

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# Endorsement and Statement by the Board of Directors and the CEO

The Condensed Consolidated Interim Financial Statements of Landsbankinn hf. (the "Bank" or "Landsbankinn") for the first nine months ended 2015 include the Bank and its subsidiaries (collectively referred to as the "Group").

Landsbankinn was founded on 7 October 2008. The Bank is a leading bank in the domestic market and offers a complete range of financial products and services to personal, corporate and institutional customers.

## Operations

Consolidated profit amounted to ISK 24,413 million for the first nine months of the financial year 2015. Consolidated total equity amounted to ISK 252,484 million and total assets amounted to ISK 1,175,804 million at the end of this period. The capital adequacy ratio of the Group, calculated according to the Act on Financial Undertakings, was 29.2% at the end of the third quarter of 2015.

On 15 October 2015, the Supreme Court ruled in favour of the Bank in two cases where a company disputed the right of the Bank to receive additional payment as a result of recalculations of foreign currency indexed loans in accordance with Central Bank interest rates instead of contractual interest rates in accordance with final receipts. The Supreme Court concluded that conditions for the exception from the legal right to receive additional payment had not been met since the difference in the comparative position between the parties was insignificant and the additional claim would not cause a serious disruption to the company's financial position comparable to the impact that such claims would have on an individual or small enterprise. The effect of the ruling on these Financial Statements results in a reversal of previously recognised expenses in the amount of ISK 9,145 million in the consolidated income statement at the end of the third quarter of 2015 (see Note 3).

On 21 September 2015, the Bank and the Winding-up Board of LBI hf. reached an agreement whereby, *inter alia* , the Bank commits itself to prepay during 2015 the earlier maturities of the senior secured foreign currency bonds issued by the Bank to LBI hf. The amount for prepayment is equivalent to ISK 47,000 million. The prepayment was subject to the Bank concluding a refinancing arrangement under acceptable conditions. This agreement in hand, the Bank concluded a successful series of fixed income investor meetings in Europe, arranged by three major international banks. Following the investor meetings, the Bank issued EUR 300 million in senior unsecured bonds, equivalent to ISK 42,600 million, on 12 October 2015. Following this issuance an additional prepayment of ISK 22,000 million is scheduled, provided the Winding-up Board of LBI hf. finalizes a composition agreement with the payment of a stability contribution (see Notes 19 and 26).

On 4 September 2015, the Bank took over all assets, liabilities and operations of Sparisjóður Norðurlands ses., a local savings bank in North Iceland, in accordance with a merger agreement between Landsbankinn hf. and Sparisjóður Norðurlands ses. As remuneration for the assets and liabilities taken over by the Bank, the guarantee capital owners of the savings bank received shares in Landsbankinn. The acquisition price of the savings bank was ISK 594 million, which was equivalent to 0.25% of issued share capital of the Bank (see Note 5).

## Risk management

The Bank's core operations are sound and have been improving in recent years. Processes are being revised on a continuous basis to improve risk management, efficiency and customer relationship management. The ratio of non-performing loans has decreased and borrower credit quality of performing loans has increased in the third quarter of 2015. The Bank's liquidity position remains strong and total market risk has remained stable.

On 8 June 2015, the Government of Iceland announced a comprehensive strategy for capital account liberalisation. A major milestone of that strategy was reached on 28 October 2015, when the Central Bank of Iceland made public its opinion that the draft composition agreements, submitted by the estates of the three failed Icelandic banks, satisfy the requirements set forth in the Foreign Exchange Act, to the extent that the implementation of the composition agreements together with the proposed mitigating measures will not jeopardise monetary, exchange rate, or financial stability. Landsbankinn expects that implementation of the composition agreements will lead to an outflow of deposits, reducing the Bank's balance sheet by up to 10%. The Bank believes it is well prepared to withstand the expected outflow and aims to maintain liquidity ratios comfortably above regulatory requirements.

The Financial Supervisory Authority (FME) has concluded its latest Supervisory Review and Evaluation Process (SREP), based on data from 31 December 2014, whereby the FME determined the minimum capital requirement for the Group to be 14.3%, consisting of the 8% regulatory capital requirement under Pillar I and a 6.3% capital requirement under Pillar II. In addition to these capital requirements, new legislation entered into force during the third quarter of 2015, implementing capital buffer requirements under the European Union Capital Requirements Directive (EU CRD) IV. The aggregate of different capital buffers is determined to be 7.5% and, as a result, the total capital requirement plus capital buffers is set at 21.8% (see Note 27).

## Outlook

The forecast of Landsbankinn Economic Research and Statistics Iceland for GDP growth in 2015 remains unchanged since the second quarter of 2015, while the Central Bank has revised its forecast upwards. There is still a strong consensus amongst forecasters for robust growth: Landsbankinn Economic Research expects 4.3% GDP growth in 2015, the Central Bank of Iceland forecasts 4.6% and Statistics Iceland 3.8%.

## Statement by the Board of Directors and the CEO

The Condensed Consolidated Interim Financial Statements of Landsbankinn hf. for the first nine months ended 30 September 2015 have been prepared on a going concern basis in accordance with International Financial Reporting Standards as adopted by the EU.

In our opinion, the Condensed Consolidated Interim Financial Statements of Landsbankinn hf. give a true and fair view of the consolidated financial performance of the Group for the first nine months of 2015, its consolidated financial position as at 30 September 2015 and its consolidated cash flows for the first nine months of 2015.

Furthermore, in our opinion, the Condensed Consolidated Interim Financial Statements of Landsbankinn hf. and Endorsement of its Board of Directors and CEO give a fair view of the development and performance of the Group's operations and its position and describe the principal risks and uncertainties faced by the Group.

The Board of Directors of the Bank and Chief Executive Officer hereby endorse the Condensed Consolidated Interim Financial Statements of Landsbankinn hf. for the first nine months ended 30 September 2015.

Reykjavík, 5 November 2015.

Board of Directors

Tryggvi Pálsson

Chairman

Danielle Pamela Neben

Eva Sóley Guðbjörnsdóttir

Jóhann Hjartarson

Jón Sigurðsson

Kristján Þ. Davíðsson

Tinna Laufey Ásgeirsdóttir

CEO

Steinþór Pálsson

# Independent Auditor's Review Report

**To the Board of Directors and Shareholders of Landsbankinn hf.**

### Introduction

We have reviewed the accompanying Condensed Consolidated Statement of Financial Position of Landsbankinn hf. (the Bank) as at 30 September 2015 and the related Condensed Consolidated Income Statement, Condensed Consolidated Changes in Equity and Condensed Consolidated Cash Flows for the nine-month period then ended, and a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and presentation of these Condensed Consolidated Interim Financial Statements in accordance with International Financial Reporting Standard IAS 34 "Interim Financial Reporting" as adopted by the European Union. 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 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 do not give a true and fair view of the financial position of the Bank as at 30 September 2015, and of its financial performance and its cash flows for the nine-month period then ended in accordance with IAS 34 "Interim Financial Reporting" as adopted by the European Union.

Reykjavík, 5 November 2015.

***Grant Thornton endurskoðun ehf.***

Davíð A. Einarsson

Davíð Arnar Einarsson
State Authorised Public Accountant

J. Sturla Jónsson

Sturla Jónsson
State Authorised Public Accountant

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# Condensed Consolidated Income Statement for the nine months ended 30 September 2015

| Notes | | 2015 1.7-30.9 | 2014 1.7-30.9 | 2015 1.1-30.9 | 2014 1.1-30.9 |
|---|---|---|---|---|---|
| | Interest income | 16,000 | 13,745 | 44,676 | 42,410 |
| | Interest expense | (7,166) | (6,688) | (19,644) | (20,113) |
| 7 | **Net interest income** | **8,834** | **7,057** | **25,032** | **22,297** |
| 8 | Net valuation adjustments and credit impairment charges | 10,489 | 2,581 | 12,334 | 14,027 |
| | **Net interest income after net valuation adjustments and credit impairment charges** | **19,323** | **9,638** | **37,366** | **36,324** |
| | Fee and commission income | 2,322 | 1,714 | 6,645 | 5,609 |
| | Fee and commission expense | (577) | (439) | (1,506) | (1,413) |
| | **Net fee and commission income** | **1,745** | **1,275** | **5,139** | **4,196** |
| 9 | Net gain on financial assets designated as at fair value through profit or loss | 852 | 1,267 | 6,502 | 2,409 |
| 10 | Net gain on financial assets and liabilities held for trading | 1,173 | 571 | 2,897 | 740 |
| 11 | Net foreign exchange (loss) gain | (748) | 154 | (1,219) | (40) |
| | Other income and (expenses) | (188) | (1,104) | 239 | 1,089 |
| | **Other net operating income** | **1,089** | **888** | **8,419** | **4,198** |
| | **Total operating income** | **22,157** | **11,801** | **50,924** | **44,718** |
| 12 | Salaries and related expenses | 3,466 | 3,019 | 10,347 | 9,762 |
| | Other operating expenses | 1,757 | 1,740 | 5,838 | 5,910 |
| | Depreciation and amortisation | 167 | 171 | 496 | 523 |
| | Contribution to the Depositors' and Investors' Guarantee Fund | 203 | 253 | 970 | 775 |
| | **Total operating expenses** | **5,593** | **5,183** | **17,651** | **16,970** |
| | Share of profit of equity-accounted associates | 145 | 0 | 257 | 340 |
| | **Profit before tax** | **16,709** | **6,618** | **33,530** | **28,088** |
| 13 | Income tax | (3,953) | (566) | (6,677) | (5,523) |
| 13 | Tax on liabilities of financial institutions | (748) | (945) | (2,440) | (2,580) |
| | **Profit for the period** | **12,008** | **5,107** | **24,413** | **19,985** |
| | **Profit for the period attributable to:** | | | | |
| | **Owners of the Bank** | | | | |
| | Profit for the period from continuing operations | 12,008 | 5,092 | 24,413 | 19,921 |
| | **Profit for the period attributable to owners of the Bank** | **12,008** | **5,092** | **24,413** | **19,921** |
| | **Non-controlling interests** | | | | |
| | Profit for the period from continuing operations | 0 | 15 | 0 | 64 |
| | **Profit for the period attributable to non-controlling interests** | **0** | **15** | **0** | **64** |
| | **Profit for the period** | **12,008** | **5,107** | **24,413** | **19,985** |
| | **Earnings per share:** | | | | |
| 22 | Basic and diluted earnings per share from continuing operations | 0.51 | 0.20 | 1.03 | 0.80 |
| | **Total basic and diluted earnings per share** | **0.51** | **0.20** | **1.03** | **0.80** |

The accompanying notes are an integral part of these Condensed Consolidated Interim Financial Statements.

All amounts are in ISK million

# Condensed Consolidated Statement of Financial Position as at 30 September 2015

| Notes | | 30.9.2015 | 31.12.2014 |
|---|---|---|---|
| | **Assets** | | |
| | Cash and balances with Central Bank | 27,120 | 10,160 |
| 14, 40 | Bonds and debt instruments | 235,788 | 243,589 |
| 14 | Equities and equity instruments | 26,467 | 29,433 |
| 14, 15 | Derivative instruments | 247 | 78 |
| 16, 40 | Loans and advances to financial institutions | 46,511 | 49,789 |
| 36, 40 | Loans and advances to customers | 807,033 | 718,355 |
| | Investments in equity-accounted associates | 886 | 777 |
| | Property and equipment | 5,688 | 5,691 |
| | Intangible assets | 2,089 | 1,225 |
| | Deferred tax assets | 199 | 83 |
| 17 | Other assets | 10,961 | 20,978 |
| 18 | Assets classified as held for sale | 12,815 | 18,212 |
| | **Total assets** | **1,175,804** | **1,098,370** |
| | **Liabilities** | | |
| | Due to financial institutions and Central Bank | 49,550 | 53,827 |
| | Deposits from customers | 624,924 | 551,435 |
| 15 | Derivative instruments and short positions | 4,136 | 5,409 |
| 19, 40 | Borrowings | 207,699 | 207,028 |
| 20 | Subordinated liabilities | 775 | 0 |
| | Other liabilities | 34,718 | 27,034 |
| | Liabilities associated with assets classified as held for sale | 1,518 | 2,834 |
| | **Total liabilities** | **923,320** | **847,567** |
| 21 | **Equity** | | |
| | Share capital | 23,782 | 23,687 |
| | Share premium | 122,105 | 121,275 |
| | Reserves | 6,000 | 6,000 |
| | Retained earnings | 100,567 | 99,841 |
| | **Total equity attributable to owners of the Bank** | **252,454** | **250,803** |
| | Non-controlling interests | 30 | 0 |
| | **Total equity** | **252,484** | **250,803** |
| | **Total liabilities and equity** | **1,175,804** | **1,098,370** |

The accompanying notes are an integral part of these Condensed Consolidated Interim Financial Statements.

All amounts are in ISK million

# Condensed Consolidated Statement of Changes in Equity for the nine months ended 30 September 2015

| Notes | | Attributable to owners of the Bank | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | **Change in equity for the nine months ended 30 September 2015** | **Share capital** | **Share premium** | **Statutory reserve** | **Share-based payment reserve** | **Retained earnings** | **Total** | **Non-controlling interests** | **Total** |
| | Balance as at 1 January 2015 | 23,687 | 121,275 | 6,000 | | 99,841 | 250,803 | | 250,803 |
| | Profit for the period | | | | | 24,413 | 24,413 | | 24,413 |
| | Dividends paid | | | | | (23,687) | (23,687) | | (23,687) |
| 5 | Merger consideration allocated to former guarantee capital owners of Sparisjóður Vestmannaeyja ses. and Sparisjóður Norðurlands ses. | 95 | 830 | | | | 925 | | 925 |
| | Increase in non-controlling interests due to merger of Landsbankinn and Sparisjóður Norðurlands ses. | | | | | | 0 | 30 | 30 |
| 21 | **Balance as at 30 September 2015** | **23,782** | **122,105** | **6,000** | **0** | **100,567** | **252,454** | **30** | **252,484** |
| | **Change in equity for the nine months ended 30 September 2014** | | | | | | | | |
| | Balance as at 1 January 2014 | 23,618 | 120,700 | 6,000 | 1,046 | 90,002 | 241,366 | (7) | 241,359 |
| | Profit for the period | | | | | 19,921 | 19,921 | 64 | 19,985 |
| | Own shares allocated to employees | 112 | 934 | | (1,046) | | 0 | | 0 |
| | Purchase of own shares for settlement of tax obligations and pension liabilities | (43) | (359) | | | | (402) | | (402) |
| | Dividends paid | | | | | (19,897) | (19,897) | | (19,897) |
| | Decrease in non-controlling interests due to sale of subsidiaries | | | | | | 0 | (58) | (58) |
| 21 | **Balance as at 30 September 2014** | **23,687** | **121,275** | **6,000** | **0** | **90,026** | **240,988** | **(1)** | **240,987** |

The accompanying notes are an integral part of these Condensed Consolidated Interim Financial Statements.

All amounts are in ISK million

## Condensed Consolidated Statement of Cash Flows for the nine months ended 30 September 2015

| Notes | | 2015<br>1.1-30.9 | 2014<br>1.1-30.9 |
|---|---|---|---|
| | **Operating activities** | | |
| | Profit for the period | 24,413 | 19,985 |
| | Adjustments for non-cash items included in profit for the period | (37,571) | (29,485) |
| | Changes in operating assets and liabilities | 23,156 | 34,986 |
| | Interest received | 35,871 | 35,478 |
| | Interest paid | (12,045) | (6,275) |
| | Dividends received* | 3,281 | 3,089 |
| | Income tax and special tax on financial institutions paid | (5,318) | 0 |
| | **Net cash from operating activities** | **31,787** | **57,778** |
| | **Investing activities** | | |
| | Proceeds from equity-accounted associates | 0 | 5,783 |
| | Purchase of property and equipment | (189) | (1,222) |
| | Proceeds from sale of property and equipment | 58 | 75 |
| | Purchase of intangible assets | (430) | (377) |
| | **Net cash (to) from investing activities** | **(561)** | **4,259** |
| | **Financing activities** | | |
| | Proceeds from new long-term debt issue | 5,800 | 2,400 |
| | Aquisition of non-controlling interest | 0 | 1,026 |
| | Repayment of long-term debt | (180) | (10,393) |
| | Dividends paid | (23,687) | (19,897) |
| | **Net cash used in financing activities** | **(18,067)** | **(26,864)** |
| | Net change in cash and cash equivalents | 13,159 | 35,174 |
| | Cash and cash equivalents as at the beginning of the period | 16,585 | 19,927 |
| 5 | Cash and cash equivalents acquired in business combination | 1,491 | 0 |
| | Effect of exchange rate changes on cash and cash equivalents held | 1,255 | 23 |
| | **Cash and cash equivalents as at 30 September** | **32,490** | **55,124** |
| | **Investing and financing activities not affecting cash flows** | | |
| 5 | Assets acquired and liabilities assumed from Sparisjóður Vestmannaeyja and Sparisjóður Norðurlands | (343) | 0 |
| 5 | Goodwill | (583) | 0 |
| 5 | Own shares allocated to former guarantee capital owners of Sparisjóður Vestmannaeyja and Sparisjóður Norðurlands | 926 | 0 |
| 19 | Unsettled issued new bills | 1,300 | 0 |
| 17 | Unsettled securities trading | (1,300) | 0 |

The accompanying notes are an integral part of these Condensed Consolidated Interim Financial Statements.

* While dividends received from equity accounted associates were classified as investing activities in prior periods, they are now classified as operating activities. The comparative amounts have been adjusted accordingly and an amount of ISK 1,846 million has been reclassified to conform to this new presentation.

All amounts are in ISK million

## Condensed Consolidated Statement of Cash Flows for the nine months ended 30 September 2015

| Notes | | 2015<br>1.1-30.9 | 2014<br>1.1-30.9 |
|---|---|---|---|
| | **Adjustments for non-cash items included in profit for the period** | | |
| 7 | Net interest income | (25,032) | (22,297) |
| 8 | Net adjustments to loans and advances acquired at deep discount | 0 | (13,543) |
| 8, 37 | Net impairment and loss of guarantees | (5,070) | (484) |
| 8 | Reversal on foreign currency linkage of loans and advances to customers | (7,264) | 0 |
| 9 | Net (gain) on financial assets designated as at fair value through profit or loss | (6,502) | (2,409) |
| 10 | Net (gain) on financial assets and liabilities held for trading | (2,897) | (740) |
| 11 | Net foreign exchange (gain) loss | (36) | 17 |
| | Loss on sale of property and equipment | 23 | 34 |
| | Net (gain) loss on assets classified as held for sale | (149) | 1,651 |
| | Depreciation and amortisation | 496 | 523 |
| | Share of profit of equity-accounted associates | (257) | (340) |
| 13 | Income tax | 6,677 | 5,523 |
| 13 | Tax on liabilities of financial institutions | 2,440 | 2,580 |
| | | **(37,571)** | **(29,485)** |
| | **Changes in operating assets and liabilities** | | |
| | Change in reserve requirement with Central Bank | (4,284) | 3,268 |
| | Change in bonds and equities | 15,890 | 2,308 |
| | Change in loans and advances to financial institutions | 7,418 | 13,729 |
| | Change in loans and advances to customers | (65,711) | (12,763) |
| | Change in other assets | 8,566 | (493) |
| | Change in assets of disposal groups | 5,226 | (1,766) |
| | Change in due to financial institutions and Central Bank | (4,251) | 11,509 |
| | Change in deposits from customers | 53,963 | 28,295 |
| | Change in deferred tax assets/liabilities | (116) | 27 |
| | Change in repossessed collateral | 2,635 | (1,637) |
| | Change in other liabilities | 4,175 | (7,818) |
| | Change in liabilities associated with assets classified as held for sale | (355) | 327 |
| | | **23,156** | **34,986** |
| | **Cash and cash equivalents is specified as follows:** | | |
| | Cash and unrestricted balances with Central Bank | 16,139 | 35,632 |
| 16 | Bank accounts with financial institutions | 16,351 | 19,492 |
| | **Cash and cash equivalents as at the end of the period** | **32,490** | **55,124** |

The accompanying notes are an integral part of these Condensed Consolidated Interim Financial Statements.

All amounts are in ISK million

# Notes to the Condensed Consolidated Interim Financial Statements

# Notes to the Condensed Consolidated Interim Financial Statements

## 1. Reporting entity

Landsbankinn hf. (hereinafter referred to as the "Bank" or "Landsbankinn") was founded on 7 October 2008. The Bank is a limited liability company incorporated and domiciled in Iceland. The Bank operates in accordance with Act No. 161/2002. The Bank is subject to supervision of the Financial Supervisory Authority (FME) in accordance with Act No. 87/1998, on Official Supervision of Financial Activities. The registered address of the Bank's office is Austurstræti 11, 155 Reykjavík.

The Condensed Consolidated Interim Financial Statements of the Bank for the nine months ended 30 September 2015 include the Bank and its subsidiaries (collectively referred to as the "Group" and individually as "Group entities"). The Group's primary lines of business are corporate and personal banking, markets, asset management and other related services. The Group operates solely in Iceland.

The issue of these Condensed Consolidated Interim Financial Statements was authorised by the Board of Directors and the CEO of the Bank on 5 November 2015.

## 2. Basis of preparation

### Statement of compliance

These Condensed Consolidated Interim Financial Statements for the nine months ended 30 September 2015 have been prepared in accordance with International Accounting Standard (IAS) 34 Interim Financial Reporting, as adopted by the European Union.

The Condensed Consolidated Interim Financial Statements do not include all the information required for full annual financial statements and should be read in conjunction with the Consolidated Financial Statements of the Group as at and for the year ended 31 December 2014, which are available on the Bank's website, www.landsbankinn.is.

### Going concern

The Bank's management has assessed the Group's ability to continue as a going concern and it has a reasonable expectation that the Group has adequate resources to continue its operations. Accordingly, these Condensed Consolidated Interim Financial Statements have been prepared on a going concern basis.

### Basis of measurement

The Condensed Consolidated Interim Financial Statements have been prepared on a historical cost basis except for the following:
• Financial assets and liabilities classified as held for trading are measured at fair value;
• Financial assets and liabilities designated as at fair value through profit or loss are measured at fair value;
• Non-current assets and disposal groups classified as held for sale are measured at the lower of cost or fair value less costs to sell.

### Functional and presentation currency

Items included in the financial statements of each individual Group entity are measured using the currency of the economic environment in which the respective entity operates (its functional currency). All amounts are presented in Icelandic *króna* (ISK), which is also the Bank's functional currency, rounded to the nearest million unless otherwise stated.

### Use of estimates and judgements

The preparation of 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. Actual results may differ from these estimates.

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

### 3. Critical accounting estimates and judgements in applying accounting policies

In accordance with prudent accounting policies the Group recognised expenses for the potential impact of rulings of the Supreme Court on recalculation of foreign currency indexed loans in its consolidated income statement at year-end 2011 and at the end of the third quarter of 2012. On 15 October 2015, the Supreme Court ruled in favour of the Bank in two cases where a company brought lawsuits against the Bank demanding recalculation of previous recalculations of foreign currency indexed loans in accordance with Supreme Court judgments No. 600/2011 and No. 464/2012. The Supreme Court concluded that the difference in the comparative position between the parties was insignificant and that the additional claim would not cause a serious disruption to the company's financial position comparable to the impact that unexpected claims for additional payment would have on an individual or a small enterprise. Consequently, the company's claim for recalculation of previous recalculations was unfounded. These rulings serve as a precedent for other homogeneous foreign currency indexed loans to companies where circumstances are similar. The effect of these rulings on these Financial Statements result in a reversal of previously recognised expenses in the amount of ISK 9,145 million in the Consolidated Income Statement at the end of the third quarter of 2015 under sub-line item "Reversal on foreign currency linkage of loans and advances to customers" (see Note 8).

### 4. Significant accounting policies

The Condensed Consolidated Interim Financial Statements have been prepared using uniform accounting policies for like transactions and other events in similar circumstances. The accounting policies applied by the Group in the Condensed Consolidated Interim Financial Statements are the same as those applied by the Group in its Consolidated Financial Statements as at and for the year ended 31 December 2014. The accounting policies applied have been applied consistently to all periods presented.

In addition to the accounting policies set out in the Group's Consolidated Financial Statements as at and for the year ended 31 December 2014, the Group has applied the following accounting policies from 1 January 2015:

#### Goodwill

Goodwill is recognised as an asset only if acquired in a business combination. It is recognised as of the acquisition date and measured as the aggregate of (a) the fair value of the consideration transferred, (b) the recognised amount of any non-controlling interest in the acquiree, and (c) the fair value of any previously held equity interest in the acquiree, less the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed, all measured as at the acquisition date. The consideration transferred includes the fair value of assets transferred, liabilities incurred and equity interests issued by the Group. In addition, consideration transferred includes the fair value of any contingent consideration. Following initial recognition, goodwill is measured at cost, less any accumulated impairment losses. Goodwill is generally reviewed for impairment annually, but more frequently if events or changes in circumstances indicate a potential impairment of the carrying amount. For the purpose of impairment testing, goodwill is allocated as of the acquisition date to each of the Group's cash-generating units (CGUs) or group of CGUs which are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. Each unit to which this goodwill is allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes. Where goodwill is attached to a particular unit of a CGU (or of a group of CGUs) and part of the operations within that unit is disposed of, the goodwill that is associated with the operations disposed of is included in the carrying amount of these operations when determining the gain or loss incurred upon disposing of the operations.

#### Subordinated liabilities

Subordinated liabilities are initially recognised at fair value less transaction costs and are subsequently measured at amortized cost using the effective interest method. Accrued interest is recognised as part of the carrying amount of subordinated liabilities.

## 5. Business combinations

### Merger of Landsbankinn and Sparisjóður Vestmannaeyja

On 29 March 2015, the Bank took over all assets, liabilities and operations of Sparisjóður Vestmannaeyja ses., a local savings bank in Vestmannaeyjar, in accordance with the decision of the Financial Supervisory Authority (FME) and an agreement between Landsbankinn hf. and the Board of Directors of Sparisjóður Vestmannaeyja ses. The activities and operations of the savings bank have been integrated into that of Landsbankinn.

As remuneration for the assets and liabilities taken over by the Bank, the guarantee capital owners of the savings bank received shares in Landsbankinn. The acquisition price of the savings bank was ISK 332 million, which is equivalent to 0.14% of the issued share capital of the Bank. The fair value of the shares issued by the Bank is based on the book value per outstanding shares as of 31 December 2014, adjusted for the dividend payment to the Bank's shareholders in March 2015.

Since the acquisition in March 2015, Sparisjóður Vestmannaeyja ses. has contributed total operating income of ISK 298 million and a profit of ISK 11 million to the Group's 2015 third quarter results. The assets acquired and liabilities assumed from Sparisjóður Vestmannaeyja ses. have been recognised in these financial statements at the preliminary fair value of ISK 10.5 billion and ISK 10.7 billion, respectively.

| Identifiable assets acquired and liabilities assumed | Fair value |
|---|---|
| **Assets** | |
| Cash and balances with Central Bank | 1,408 |
| Bonds and debt instruments | 705 |
| Equities and equity instruments | 255 |
| Loans and advances to financial institutions | 157 |
| Loans and advances to customers | 6,888 |
| Property and equipment | 135 |
| Deferred tax assets | 383 |
| Other assets | 128 |
| Assets classified as held for sale | 435 |
| **Total** | **10,494** |
| | |
| **Liabilities** | |
| Deposits from customers | 9,935 |
| Other borrowings | 188 |
| Subordinated liabilities | 427 |
| Other liabilities | 177 |
| **Total** | **10,727** |
| | |
| **Total identifiable net assets** | **(233)** |
| **Goodwill** | **565** |
| | |
| **Acquisition price** | **332** |

| | As at 29 March 2015 | | | |
|---|---|---|---|---|
| Loans and advances to customers | Acquiree's carrying amounts | Contractual cash flows* | Cash flows expected to be collected* | Fair value |
| Corporations and public entities | 1,467 | 2,958 | 1,719 | 1,467 |
| Individuals | 5,421 | 9,733 | 7,718 | 5,421 |
| **Total** | **6,888** | **12,691** | **9,437** | **6,888** |

*The cash flows presented in the table above consist of undiscounted principal and interest receivable.

If this business combination had been effective as of 1 January 2015, the total operating income contribution of the merged company at the end of Q3 2015 would have amounted to ISK 491 million and the net loss contribution to ISK 41 million.

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## 5. Business combinations (continued)

### Merger of Landsbankinn and Sparisjóður Norðurlands

On 4 September 2015, the Bank took over all assets, liabilities and operations of Sparisjóður Norðurlands ses., a local savings bank in North Iceland, in accordance with a merger agreement between Landsbankinn hf. and Sparisjóður Norðurlands ses. The activities and operations of the savings bank are currently being integrated into that of Landsbankinn.

As remuneration for the assets and liabilities taken over by the Bank, the guarantee capital owners of the savings bank received shares in Landsbankinn. The acquisition price of the savings bank was ISK 594 million, which is equivalent to 0.25% of issued share capital of the Bank. The fair value of shares issued by the Bank is based on the book value per outstanding shares as of 31 March 2015, adjusted for the the merger of Landsbankinn and savings bank Sparisjóður Vestmannaeyja ses.

Since the acquisition in September 2015, Sparisjóður Norðurlands ses. has contributed total operating income of ISK 34 million and a profit of ISK 7 million to the Group's 2015 third quarter results. The assets acquired and liabilities assumed from Sparisjóður Norðurlands ses. have been recognised in these financial statements at the preliminary fair value of ISK 10.1 billion and ISK 9.6 billion, respectively.

| Identifiable assets acquired and liabilities assumed | Fair value |
|---|---|
| **Assets** | |
| Cash and balances with Central Bank | 83 |
| Bonds and debt instruments | 227 |
| Equities and equity instruments | 82 |
| Loans and advances to financial institutions | 2,424 |
| Loans and advances to customers | 6,501 |
| Investments in associates | 14 |
| Interest in subsidiaries | 14 |
| Property and equipment | 102 |
| Deferred tax assets | 567 |
| Other assets | 23 |
| Assets classified as held for sale | 101 |
| **Total** | **10,138** |
| | |
| **Liabilities** | |
| Deposits from customers | 8,966 |
| Subordinated liabilities | 387 |
| Other liabilities | 201 |
| **Total** | **9,554** |
| | |
| **Total identifiable net assets** | **576** |
| **Goodwill** | **18** |
| | |
| **Acquisition price** | **594** |

| | As at 4 September 2015 | | | |
|---|---|---|---|---|
| **Loans and advances to customers** | **Acquiree's carrying amounts** | **Contractual cash flows*** | **Cash flows expected to be collected*** | **Fair value** |
| Corporations and public entities | 2,157 | 3,138 | 2,615 | 2,157 |
| Individuals | 4,344 | 7,507 | 6,725 | 4,344 |
| **Total** | **6,501** | **10,645** | **9,340** | **6,501** |

*The cash flows presented in the table above consist of undiscounted principal and interest receivable.

If this business combination had been effective as of 1 January 2015, the total operating income contribution of the merged company at the end of Q3 2015 would have amounted to ISK 351 million and the net loss contribution to ISK 76 million.

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### 5. Business combinations (continued)

**Total acquisitions during the period**

The table below summarises the recognised fair value amounts of the identifiable assets acquired and liabilities assumed from the mergers of the savings banks with the Bank during the nine months ended 30 September 2015:

| Identifiable assets acquired and liabilities assumed | Sparisjóður Vestmannaeyja | Sparisjóður Norðurlands | Total |
|---|---|---|---|
| **Assets** | | | |
| Cash and balances with Central Bank | 1,408 | 83 | 1,491 |
| Bonds and debt instruments | 705 | 227 | 932 |
| Equities and equity instruments | 255 | 82 | 337 |
| Loans and advances to financial institutions | 157 | 2,424 | 2,581 |
| Loans and advances to customers | 6,888 | 6,501 | 13,389 |
| Investments in associates | - | 14 | 14 |
| Interest in subsidiaries | - | 14 | 14 |
| Property and equipment | 135 | 102 | 237 |
| Deferred tax assets | 383 | 567 | 950 |
| Other assets | 128 | 23 | 151 |
| Assets classified as held for sale | 435 | 101 | 536 |
| **Total** | **10,494** | **10,138** | **20,632** |
| | | | |
| **Liabilities** | | | |
| Deposits from customers | 9,935 | 8,966 | 18,901 |
| Other borrowings | 188 | - | 188 |
| Subordinated liabilities | 427 | 387 | 814 |
| Other liabilities | 177 | 201 | 378 |
| **Total** | **10,727** | **9,554** | **20,281** |
| | | | |
| **Total identifiable net assets** | **(233)** | **576** | **343** |
| **Goodwill** | **565** | **18** | **583** |
| | | | |
| **Acquisition price** | **332** | **594** | **926** |

An assessment is made at each reporting date to determine whether there is any indication of potential impairment of the carrying amount of goodwill acquired in business combinations. As at 30 September 2015, the Bank performed an impairment test of the goodwill acquired and identified no impairment losses.

### 6. Operating segments

Business segments are presented in accordance with internal reporting to the CEO and the Board of Directors, who are responsible for allocating resources to the reportable segments and assessing their financial performance.

The Group has four main business segments as at the end of the reporting period:

• **Personal Banking** provides financial services through the Bank's branch network to individuals and to small and medium-size businesses outside the capital city region.
• **Corporate Banking** provides financial services to corporate clients and to small and medium-size businesses in the capital city region. It also provides restructuring solutions for underperforming businesses.
• **Markets** provides brokerage services in securities, foreign currencies and derivatives, securities offerings and advisory services. Markets also handles market making for listed securities and foreign currencies. Markets provides a range of wealth and asset management products and services for individuals, corporations and institutional investors. Landsbréf hf., a subsidiary of the Bank, is included in Markets as an operating segment.
• **Treasury** incorporates the Bank's funding and liquidity management and market making in money markets and determines the Bank's internal pricing. Treasury also manages the Bank's exchange rate, interest rate and inflation risks, within limits that are set by the Board of Directors. The Bank allocates capital to the operating segments based on the Bank's target for a total capital ratio.

Support functions are comprised of Finance (excluding Treasury), Risk Management and Operations & IT.

Reconciliation consists of eliminations and transactions that cannot be allocated to any one segment.

Administrative expenses of the Group's support functions are allocated to appropriate business segments based on the underlying cost drivers. Expenses are allocated to the business units at market price level. Support functions supply services to business units and transactions are settled at unit prices or on an arm's-length basis, if possible, on the basis of consumption and activity.

All amounts are in ISK million

### 6. Operating segments (continued)

The following table summarises each segment's financial performance as disclosed in the internal management reports on segment profits before tax. In these reports, all income statement items are reported on a net basis, including the total interest income and expense. Inter-segment pricing is determined on an arm's length basis.

No revenue from transactions with a single external customer or counterparty amounted to 10% or more of the Group's total revenue during the period from 1 January to 30 September 2015 and 2014.

| 1 January - 30 September 2015 | Personal Banking | Corporate Banking | Markets | Treasury | Support functions | Recon-ciliation | Total |
|---|---|---|---|---|---|---|---|
| Net interest income (expense) | 9,992 | 10,349 | 236 | 5,134 | 5 | (684) | **25,032** |
| Net credit impairment charges and valuation adjustments | 2,526 | 9,856 | (1) | (47) | - | - | **12,334** |
| Net fee and commission income | 2,640 | 531 | 2,423 | (241) | 54 | (268) | **5,139** |
| Other net operating income | (259) | (711) | 1,612 | 6,836 | 366 | 575 | **8,419** |
| **Total operating income (expense)** | **14,899** | **20,025** | **4,270** | **11,682** | **425** | **(377)** | **50,924** |
| Operating expenses | (4,752) | (1,104) | (1,425) | (1,260) | (9,394) | 284 | **(17,651)** |
| Share of profit (loss) of equity-accounted associates | 182 | - | - | 33 | 42 | - | **257** |
| **Profit (loss) before cost allocation and tax** | **10,329** | **18,921** | **2,845** | **10,455** | **(8,927)** | **(93)** | **33,530** |
| Cost allocated from support functions to business segments | (3,969) | (3,104) | (869) | (655) | 8,597 | - | **0** |
| **Profit (loss) before tax** | **6,360** | **15,817** | **1,976** | **9,800** | **(330)** | **(93)** | **33,530** |
| | | | | | | | |
| Net revenue from external customers | 16,175 | 28,245 | 4,048 | 2,425 | 408 | - | **51,301** |
| Net revenue (expenses) from other segments | (1,276) | (8,220) | 222 | 9,257 | 17 | - | **0** |
| **Total operating income** | **14,899** | **20,025** | **4,270** | **11,682** | **425** | **0** | **51,301** |
| | | | | | | | |
| **As at 30 September 2015** | | | | | | | |
| **Total assets** | 372,371 | 485,922 | 38,511 | 519,179 | 18,441 | (258,620) | **1,175,804** |
| **Total liabilities** | 320,236 | 379,452 | 31,352 | 432,459 | 18,441 | (258,620) | **923,320** |
| **Allocated capital** | 52,135 | 106,470 | 7,159 | 86,720 | - | | **252,484** |

| 1 January - 30 September 2014 | Personal Banking | Corporate Banking | Markets | Treasury | Support functions | Recon-ciliation | Total |
|---|---|---|---|---|---|---|---|
| Net interest income (expense) | 10,928 | 12,102 | 565 | (357) | 5 | (946) | **22,297** |
| Net credit impairment charges and valuation adjustments | 4,030 | 8,025 | - | (12) | 1,984 | - | **14,027** |
| Net fee and commission income | 2,248 | 469 | 1,945 | (260) | 73 | (279) | **4,196** |
| Other net operating income | (657) | (231) | (166) | 6,078 | (1,757) | 931 | **4,198** |
| **Total operating income (expense)** | **16,549** | **20,365** | **2,344** | **5,449** | **305** | **(294)** | **44,718** |
| Operating expenses | (4,778) | (1,093) | (1,458) | (1,103) | (8,832) | 294 | **(16,970)** |
| Share of profit of equity-accounted associates | 315 | (11) | - | 36 | - | - | **340** |
| **Profit (loss) before cost allocation and tax** | **12,086** | **19,261** | **886** | **4,382** | **(8,527)** | **0** | **28,088** |
| Cost allocated from support functions to business segments | (3,953) | (2,514) | (892) | (735) | 8,094 | - | **0** |
| **Profit (loss) before tax** | **8,133** | **16,747** | **(6)** | **3,647** | **(433)** | **0** | **28,088** |
| | | | | | | | |
| Net revenue from external customers | 11,064 | 30,424 | 2,066 | 1,169 | 289 | - | **45,012** |
| Net revenue (expenses) from other segments | 5,485 | (10,059) | 278 | 4,280 | 16 | - | **0** |
| **Total operating income** | **16,549** | **20,365** | **2,344** | **5,449** | **305** | **0** | **45,012** |
| | | | | | | | |
| **As at 30 September 2014** | | | | | | | |
| **Total assets** | 493,460 | 440,299 | 25,024 | 566,478 | 35,324 | (359,338) | **1,201,247** |
| **Total liabilities** | 443,057 | 329,873 | 16,180 | 495,164 | 35,324 | (359,338) | **960,260** |
| **Allocated capital** | 50,403 | 110,426 | 8,844 | 71,314 | - | | **240,987** |

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## Notes to the Condensed Consolidated Interim Income Statement

### 7. Net interest income

| | 2015 | 2014 | 2015 | 2014 |
|---|---|---|---|---|
| **Interest income** | **1.7-30.9** | **1.7-30.9** | **1.1-30.9** | **1.1-30.9** |
| Cash and balances with Central Bank | 213 | 239 | 501 | 969 |
| Bonds and debt instruments classified as loans and receivables | 1,391 | 1,391 | 3,857 | 4,119 |
| Loans and advances to financial institutions | 80 | 105 | 282 | 361 |
| Loans and advances to customers | 14,311 | 12,006 | 40,020 | 36,941 |
| Other interest income | 5 | 4 | 16 | 20 |
| **Total** | **16,000** | **13,745** | **44,676** | **42,410** |
| | | | | |
| **Interest expense** | | | | |
| Due to financial institutions and Central Bank | (293) | (703) | (847) | (2,271) |
| Deposits from customers | (4,988) | (4,058) | (13,400) | (12,129) |
| Borrowings | (1,775) | (1,924) | (5,219) | (5,704) |
| Subordinated liabilities | 1 | - | (9) | - |
| Other interest expense | (111) | (3) | (169) | (9) |
| **Total** | **(7,166)** | **(6,688)** | **(19,644)** | **(20,113)** |
| | | | | |
| **Net interest income** | **8,834** | **7,057** | **25,032** | **22,297** |

Interest income and interest expense disclosed above arose on financial assets and financial liabilities that are not carried at fair value through profit or loss.

### 8. Net valuation adjustments and credit impairment charges

| | 2015<br>1.7-30.9 | 2014<br>1.7-30.9 | 2015<br>1.1-30.9 | 2014<br>1.1-30.9 |
|---|---|---|---|---|
| Net valuation adjustments to loans and advances acquired at deep discount | - | 2,531 | - | 13,543 |
| Net impairment | 1,948 | 50 | 5,674 | 484 |
| Net impairment loss of guarantees | (604) | - | (604) | - |
| Reversal on foreign currency linkage of loans and advances to customers | 9,145 | - | 7,264 | - |
| **Net valuation adjustments and credit impairment charges** | **10,489** | **2,581** | **12,334** | **14,027** |
| | | | | |
| **Valuation adjustments and impairment charges by customer type** | | | | |
| Individuals | 568 | (67) | 440 | 1,332 |
| Corporates | 9,921 | 2,648 | 11,894 | 12,695 |
| **Net valuation adjustments and credit impairment charges** | **10,489** | **2,581** | **12,334** | **14,027** |

### 9. Net gain on financial assets designated as at fair value through profit or loss

| | 2015<br>1.7-30.9 | 2014<br>1.7-30.9 | 2015<br>1.1-30.9 | 2014<br>1.1-30.9 |
|---|---|---|---|---|
| Bonds and debt instruments | 170 | (54) | 1,057 | (276) |
| Equities and equity instruments | 682 | 1,321 | 5,445 | 2,685 |
| **Total** | **852** | **1,267** | **6,502** | **2,409** |

### 10. Net gain on financial assets and liabilities held for trading

| | 2015<br>1.7-30.9 | 2014<br>1.7-30.9 | 2015<br>1.1-30.9 | 2014<br>1.1-30.9 |
|---|---|---|---|---|
| Bonds and debt instruments | 301 | 513 | 1,129 | 890 |
| Equities and equity instruments | 1,176 | 52 | 2,501 | (194) |
| Derivative instruments | (304) | 6 | (733) | 44 |
| **Total** | **1,173** | **571** | **2,897** | **740** |

All amounts are in ISK million

## 11. Net foreign exchange (loss) gain

| Assets | 2015 1.7-30.9 | 2014 1.7-30.9 | 2015 1.1-30.9 | 2014 1.1-30.9 |
|---|---|---|---|---|
| Cash and balances with Central Bank | (125) | 6 | (140) | (45) |
| Bonds and debt instruments | (4,639) | 4,555 | (1,853) | 3,417 |
| Equities and equity instruments | (565) | (77) | (1,383) | (368) |
| Derivative instruments | 473 | (84) | (1,065) | (524) |
| Loans and advances to financial institutions | (1,566) | 1,131 | (1,533) | (583) |
| Loans and advances to customers | (7,704) | 3,299 | (8,958) | (587) |
| Other assets | (18) | 13 | (11) | 9 |
| **Total** | **(14,144)** | **8,843** | **(14,943)** | **1,319** |
| | | | | |
| **Liabilities** | | | | |
| Due to financial institutions and Central Bank | 29 | (1,818) | 45 | (384) |
| Deposits from customers | 5,748 | (1,835) | 6,235 | (268) |
| Borrowings | 7,515 | (4,913) | 7,443 | (645) |
| Subordinated liabilities | 14 | - | 25 | - |
| Other liabilities | 90 | (123) | (24) | (62) |
| **Total** | **13,396** | **(8,689)** | **13,724** | **(1,359)** |
| | | | | |
| **Net foreign exchange (loss) gain** | **(748)** | **154** | **(1,219)** | **(40)** |

The foreign exchange difference recognised during the period 1 January to 30 September 2015 in the Condensed Consolidated Income Statement that arose on financial instruments not measured at fair value through profit or loss, amounted to a loss of ISK 10,642 million for financial assets (1.1-30.9.2014: loss of ISK 1,206 million) and a gain of ISK 13.724 million for financial liabilities (1.1-30.9.2014: loss ISK 1,359 million).

## 12. Salaries and related expenses

| | 2015 1.7-30.9 | 2014 1.7-30.9 | 2015 1.1-30.9 | 2014 1.1-30.9 |
|---|---|---|---|---|
| Salaries | 2,608 | 2,243 | 7,935 | 7,473 |
| Contributions to defined pension plans | 415 | 370 | 1,157 | 1,082 |
| Social security contributions, special financial activities tax on salaries and other expenses | 443 | 406 | 1,255 | 1,207 |
| **Total salaries and related expenses** | **3,466** | **3,019** | **10,347** | **9,762** |

## 13. Income tax and other taxes

Income tax is recognised based on the tax rates and tax laws enacted by the end of the year, according to which the domestic corporate income tax rate was 20.0% (2014: 20.0%). An additional special income tax on financial institutions is recognised at a rate of 6% on an income tax base exceeding ISK 1,000 million in accordance with Act No. 165/2011, on Financial Activity Tax.

Income tax recognised in the income statement is specified as follows:

| | 2015 1.1-30.9 | 2014 1.1-30.9 |
|---|---|---|
| Current tax expense | (4,346) | (4,807) |
| Special income tax on financial institutions | (1,497) | (1,361) |
| Difference of prior year's imposed and calculated income tax | - | 110 |
| Deferred tax expense | (834) | 535 |
| **Total** | **(6,677)** | **(5,523)** |

The tax on Group profit differs to the following extent from the amount that would theoretically arise by the domestic corporate income tax rate:

| | | 1.1-30.9 2015 | | 1.1-30.9 2014 |
|---|---|---|---|---|
| Profit before tax | | 33,530 | | 28,088 |
| Tax on liabilities of financial institutions | | (2,440) | | (2,580) |
| Profit before income tax | | 31,090 | | 25,508 |
| Income tax calculated using the domestic corporate income tax rate | 20.0% | (6,218) | 20.0% | (5,102) |
| Special income tax on financial institutions | 4.8% | (1,497) | 5.3% | (1,361) |
| Income not subject to tax | (5.3%) | 1,633 | (3.5%) | 882 |
| Non-deductable expenses | 2.0% | (617) | 2.6% | (657) |
| Other | (0.1%) | 22 | (2.8%) | 715 |
| **Effective income tax** | **21.5%** | **(6,677)** | **21.6%** | **(5,523)** |

All amounts are in ISK million

## Notes to the Condensed Consolidated Statement of Financial Position

### 14. Classification and fair value of financial assets and liabilities

According to IAS 39, financial assets and liabilities must be classified into specific categories which affect how they are measured after initial recognition. Each category's basis of subsequent measurement is specified below:

- Loans and receivables, measured at amortised cost;
- Financial assets and liabilities held for trading, measured at fair value;
- Financial assets designated as at fair value through profit or loss, measured at fair value;
- Other financial liabilities, measured at amortised cost.

The following table shows the classification of the Group's financial assets and liabilities according to IAS 39 and their fair values as at 30 September 2015:

| Financial assets | Loans and receivables | Held for trading | Designated as at fair value | Liabilities at amortised cost | Other liabilities at fair value | Total carrying amount | Fair value |
|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank | 27,120 | - | - | - | - | 27,120 | 27,120 |
| Bonds and debt instruments | 116,895 | 109,676 | 9,217 | - | - | 235,788 | 236,645 |
| Equities and equity instruments | - | 9,847 | 16,620 | - | - | 26,467 | 26,467 |
| Derivative instruments | - | 247 | - | - | - | 247 | 247 |
| Loans and advances to financial institutions | 46,511 | - | - | - | - | 46,511 | 46,511 |
| Loans and advances to customers | 807,033 | - | - | - | - | 807,033 | 811,461 |
| Other financial assets | 10,133 | - | - | - | - | 10,133 | 10,133 |
| **Total** | **1,007,692** | **119,770** | **25,837** | **0** | **0** | **1,153,299** | **1,158,584** |
| **Financial liabilities** | | | | | | | |
| Due to financial institutions and Central Bank | - | - | - | 49,550 | - | 49,550 | 49,550 |
| Deposits from customers | - | - | - | 624,924 | - | 624,924 | 624,816 |
| Derivative instruments and short positions | - | 4,136 | - | - | - | 4,136 | 4,136 |
| Borrowings | - | - | - | 207,699 | - | 207,699 | 208,143 |
| Other financial liabilities | - | - | - | 15,683 | - | 15,683 | 15,683 |
| **Total** | **0** | **4,136** | **0** | **897,856** | **0** | **901,992** | **902,328** |

The following table shows the classification of the Group's financial assets and liabilities according to IAS 39 and their fair values as at 31 December 2014:

| Financial assets | Loans and receivables | Held for trading | Designated as at fair value | Liabilities at amortised cost | Other liabilities at fair value | Total carrying amount | Fair value |
|---|---|---|---|---|---|---|---|
| Cash and balances with Central Bank | 10,160 | - | - | - | - | 10,160 | 10,160 |
| Bonds and debt instruments | 113,074 | 106,788 | 23,727 | - | - | 243,589 | 243,663 |
| Equities and equity instruments | - | 5,871 | 23,562 | - | - | 29,433 | 29,433 |
| Derivative instruments | - | 78 | - | - | - | 78 | 78 |
| Loans and advances to financial institutions | 49,789 | - | - | - | - | 49,789 | 49,789 |
| Loans and advances to customers | 718,355 | - | - | - | - | 718,355 | 726,505 |
| Other financial assets | 19,733 | - | - | - | - | 19,733 | 19,733 |
| **Total** | **911,111** | **112,737** | **47,289** | **0** | **0** | **1,071,137** | **1,079,361** |
| **Financial liabilities** | | | | | | | |
| Due to financial institutions and Central Bank | - | - | - | 53,827 | - | 53,827 | 53,826 |
| Deposits from customers | - | - | - | 551,435 | - | 551,435 | 551,468 |
| Derivative instruments and short positions | - | 5,409 | - | - | - | 5,409 | 5,409 |
| Borrowings | - | - | - | 207,028 | - | 207,028 | 207,557 |
| Other financial liabilities | - | - | - | 7,509 | - | 7,509 | 7,509 |
| **Total** | **0** | **5,409** | **0** | **819,799** | **0** | **825,208** | **825,769** |

All amounts are in ISK million

## 14. Classification and fair value of financial assets and liabilities (continued)

The fair value of financial assets and liabilities is determined based on the same valuation methods as those described in the Group's Consolidated Financial Statements as at and for the year ended 31 December 2014.

### Fair value hierarchy

The Group has used a valuation hierarchy for disclosure of inputs to valuation used to measure fair value. Fair value measurements of financial instruments are made on the basis of the following hierarchy:

• Level 1: Quoted prices are used for assets and liabilities traded in active markets. Unadjusted quoted prices are used as the measurement of fair value.

• Level 2: Valuation technique based on observable inputs. The most recent transaction prices in combination with generally accepted valuation methods are used to measure the fair value of shares. However, the yield of actively traded bonds with the same duration is used as a benchmark for the valuation of bonds.

• Level 3: Valuation technique based on significant non-observable inputs. It covers all instruments for which the valuation technique includes inputs based on unobservable data and the unobservable inputs have significant effect on the instrument's valuation. For unlisted shares and bonds where there is no market data available, various generally accepted valuation techniques are used to measure fair value. Valuation using discounted cash flow or a comparison of peer companies' multiples are the most commonly used methods to calculate the fair value of unlisted shares, in addition to recent transactions and current market conditions.

Assumptions and inputs used in the valuation technique include risk-free and benchmark interest rates for estimating discount rates, credit spreads, bonds and equity prices, foreign currency exchange rates, market multipliers, market conditions for estimating future growth and other market indicators.

### Valuation framework

The Bank's Risk & Finance Committee oversees the Group's overall risk and is responsible for fair value measurements of financial assets and liabilities classified as Level 2 and 3 instruments. The Bank's Valuation group reports its valuation results to the Risk & Finance Committee for verification. The Valuation group is comprised of personnel from Risk Management, Treasury and Accounting. The Valuation group holds meetings monthly to determine the value of Level 2 and Level 3 financial assets and liabilities.

The following table shows the Level in the hierarchy into which the fair value of financial assets and liabilities, carried at fair value in the Consolidated Statement of Financial Position, is categorised as at 30 September 2015:

| Financial assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Bonds and debt instruments | 109,821 | 8,625 | 447 | 118,893 |
| Equities and equity instruments | 10,833 | - | 15,634 | 26,467 |
| Derivative instruments | - | 247 | - | 247 |
| **Total** | **120,654** | **8,872** | **16,081** | **145,607** |

| Financial liabilities | | | | |
|---|---|---|---|---|
| Derivative instruments | - | 497 | - | 497 |
| Short positions | 3,639 | - | - | 3,639 |
| **Total** | **3,639** | **497** | **0** | **4,136** |

During the period from 1 January to 30 September 2015 there were no transfers into Level 2 from other levels. Financial assets were transferred to Level 1 from Level 3 because quoted prices for the assets became available in an active market during the period.

The following table shows the Level in the hierarchy into which the fair value of financial assets and liabilities, carried at fair value in the Consolidated Statement of Financial Position, is categorised as at 31 December 2014:

| Financial assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Bonds and debt instruments | 107,418 | 15,066 | 8,031 | 130,515 |
| Equities and equity instruments | 7,525 | - | 21,908 | 29,433 |
| Derivative instruments | - | 78 | - | 78 |
| **Total** | **114,943** | **15,144** | **29,939** | **160,026** |

| Financial liabilities | | | | |
|---|---|---|---|---|
| Derivative instruments | - | 332 | - | 332 |
| Short positions | 5,077 | - | - | 5,077 |
| **Total** | **5,077** | **332** | **0** | **5,409** |

In 2014, there were no transfers between Level 1, Level 2 and Level 3.

All amounts are in ISK million

### 14. Classification and fair value of financial assets and liabilities (continued)

The following tables show the reconciliation of fair value measurement in Level 3 for the nine months ended 30 September 2015 and for the year 2014:

| 1 January - 30 September 2015 | Bonds and debt instruments | Equities and equity instruments | Total financial assets |
|---|---|---|---|
| Carrying amount as at 1 January 2015 | 8,031 | 21,908 | 29,939 |
| Total gains recognised in income statement | 285 | 5,287 | 5,572 |
| Purchases | 4 | 153 | 157 |
| Sales | (7,922) | (471) | (8,393) |
| Settlements | (2) | - | (2) |
| Dividend received | - | (2,964) | (2,964) |
| Acquisitions through business combination | 51 | 265 | 316 |
| Transfers from Level 3 to Level 1 | - | (8,544) | (8,544) |
| **Carrying amount as at 30 September 2015** | **447** | **15,634** | **16,081** |

| 1 January - 31 December 2014 | Bonds and debt instruments | Equities and equity instruments | Total financial assets |
|---|---|---|---|
| Carrying amount as at 1 January 2014 | 10,674 | 28,064 | 38,738 |
| Total (losses) gains recognised in income statement | (1,692) | 5,894 | 4,202 |
| Purchases | - | 360 | 360 |
| Sales | (209) | (15,889) | (16,098) |
| Settlements | (742) | - | (742) |
| Dividend received | - | (1,054) | (1,054) |
| Reclassification from investments in equity-accounted associates | - | 4,533 | 4,533 |
| **Carrying amount as at 31 December 2014** | **8,031** | **21,908** | **29,939** |

The following tables show the line items in the Consolidated Income Statement where the total gains (losses) were recognised during the nine months ended 30 September 2015 and 30 September 2014, for fair value measurements in Level 3:

| 1 January - 30 September 2015 | Bonds and debt instruments | Equities and equity instruments | Total |
|---|---|---|---|
| Net gain on financial assets designated as at fair value through profit or loss | 333 | 5,298 | 5,631 |
| Net foreign exchange (loss) | (48) | (11) | (59) |
| **Total** | **285** | **5,287** | **5,572** |

| 1 January - 30 September 2014 | Bonds and debt instruments | Equities and equity instruments | Total |
|---|---|---|---|
| Net (loss) gain on financial assets designated as at fair value through profit or loss | (951) | 3,085 | 2,134 |
| Net foreign exchange (loss) | (340) | (365) | (705) |
| **Total** | **(1,291)** | **2,720** | **1,429** |

All amounts are in ISK million

## 14. Classification and fair value of financial assets and liabilities (continued)

### Unobservable inputs in fair value measurement

The following table shows the unobservable inputs used in measuring fair value as at 30 September 2015 and 31 December 2014.

| | | | | | Range of inputs | |
|---|---|---|---|---|---|---|
| **As at 30 September 2015** | **Assets** | **Liabilities** | **Valuation technique** | **Key unobservable inputs** | **Lower** | **Higher** |
| Bonds and debt instruments | 447 | - | See note 1) | See note 1) | n/a | n/a |
| Equities and equity instruments | 15,634 | - | See note 2) | See note 2) | n/a | n/a |
| | **16,081** | **0** | | | | |
| **As at 31 December 2014** | | | | | | |
| Bonds and debt instruments | 8,031 | - | See note 1) | See note 1) | n/a | n/a |
| Equities and equity instruments | 21,908 | - | See note 2) | See note 2) | n/a | n/a |
| | **29,939** | **0** | | | | |

The table above provides information on Level 3 financial assets and liabilities. A further description of the categories is given below:

1) Fair value of corporate bonds and claims on financial institutions in winding-up proceedings and other insolvent assets is estimated on the basis of an analysis of the estates' financial position and expected recovery. Reference is also made to prices in recent transactions. Given the nature of the valuation method, a range of key unobservable inputs is not available.

2) Equities and equity instruments classified as Level 3 assets, are unlisted and not traded in an active market and therefore subject to unobservable inputs for fair value measurements. Valuation using discounted cash flows, comparison of peer companies' multiples, analysis of financial position and results, outlook and recent transactions are the methods or inputs used to estimate the fair value of investments in equities and equity instruments. Given the nature of the valuation method, a range of key unobservable inputs is not available.

### The effect of unobservable inputs in fair value measurement

Although the Group believes that its estimates of fair value are appropriate, the use of different valuation methodologies and assumptions could lead to different estimates of fair value. The following table shows how profit before tax would have been affected if one or more of the inputs for fair value measurements in Level 3 were changed to likely alternatives:

| | Effect on profit before tax | |
|---|---|---|
| **As at 30 September 2015** | **Favourable** | **Unfavourable** |
| Bonds and debt instruments | 21 | (21) |
| Equities and equity instruments: | | |
| Equities | 296 | (296) |
| Mutual funds | 327 | (327) |
| Total equities and equity instruments | 623 | (623) |
| **Total** | **644** | **(644)** |

| | Effect on profit before tax | |
|---|---|---|
| **As at 31 December 2014** | **Favourable** | **Unfavourable** |
| Bonds and debt instruments | 402 | (402) |
| Equities and equity instruments: | | |
| Equities | 992 | (855) |
| Mutual funds | 315 | (315) |
| Total equities and equity instruments | 1,307 | (1,170) |
| **Total** | **1,709** | **(1,572)** |

All amounts are in ISK million

### 15. Derivative instruments and short positions

| | 30.9.2015 | | | 31.12.2014 | | |
|---|---|---|---|---|---|---|
| | Notional | Fair value | | Notional | Fair value | |
| **Foreign exchange derivatives** | amount | Assets | Liabilities | amount | Assets | Liabilities |
| Currency forwards | 29,815 | 145 | 116 | 24,024 | 39 | 52 |
| Cross-currency interest rate swaps | 6,108 | 54 | 232 | 871 | - | 251 |
| | **35,923** | **199** | **348** | **24,895** | **39** | **303** |
| **Interest rate derivatives** | | | | | | |
| Interest rate swaps | 500 | 2 | - | 500 | - | 8 |
| Total return swaps | 3,254 | 34 | 1 | 1,453 | 3 | - |
| Bond options | 750 | - | 8 | 750 | - | 12 |
| | **4,504** | **36** | **9** | **2,703** | **3** | **20** |
| **Equity derivatives** | | | | | | |
| Total return swaps | 5,507 | 12 | 73 | 1,726 | 36 | 9 |
| Equity options | 1,686 | - | 67 | - | - | - |
| | **7,193** | **12** | **140** | **1,726** | **36** | **9** |
| **Short positions** | | | | | | |
| Listed bonds* | 3,056 | - | 3,639 | 4,715 | - | 5,077 |
| | **3,056** | **0** | **3,639** | **4,715** | **0** | **5,077** |
| **Total** | **50,676** | **247** | **4,136** | **34,039** | **78** | **5,409** |

* The comparative amounts have been restated due to an error in the year-end 2014 amounts previously disclosed. The amounts in this table are of an informative nature only and do not have any effect on the amounts reported by the Group in the income Statement or Statement of Financial Position.

The Group uses derivatives both for hedging and trading purposes.

### 16. Loans and advances to financial institutions

| | 30.9.2015 | 31.12.2014 |
|---|---|---|
| Bank accounts with financial institutions | 16,351 | 13,125 |
| Money market loans | 23,317 | 22,209 |
| Overdrafts | 955 | 6,892 |
| Other loans | 5,888 | 7,563 |
| **Total** | **46,511** | **49,789** |

### 17. Other assets

| | 30.9.2015 | 31.12.2014 |
|---|---|---|
| Unsettled securities trading | 7,059 | 16,468 |
| Other accounts receivable | 3,074 | 3,265 |
| Sundry assets | 828 | 1,245 |
| **Total** | **10,961** | **20,978** |

### 18. Assets classified as held for sale

| | 30.9.2015 | 31.12.2014 |
|---|---|---|
| Repossessed collateral | 11,084 | 12,270 |
| Assets of disposal groups | 1,731 | 5,942 |
| **Total** | **12,815** | **18,212** |

#### Repossessed collateral

Repossessed collateral consists mainly of property and equipment resulting from collateral foreclosed by the Group as security for loans and advances. The Group's policy is to pursue timely realisation of the repossessed collateral in an orderly manner. The Group generally does not use the non-cash repossessed collateral for its own operations. Repossessed collateral is recognised as assets of either the Bank or its subsidiary Hömlur ehf.

| **Repossessed collateral** | 30.9.2015 | 31.12.2014 |
|---|---|---|
| Carrying amount as at the beginning of the period | 12,270 | 17,213 |
| Repossessed during the period | 4,165 | 8,151 |
| Disposed of during the period | (5,821) | (11,678) |
| Impairment and gain (loss) of sale | 470 | (1,416) |
| **Carrying amount as at the end of the period** | **11,084** | **12,270** |

#### Assets of disposal groups classified as held for sale

Assets of disposal groups classified as held for sale consist of all the assets and liabilities of subsidiaries acquired by the Bank exclusively with a view to resale.

All amounts are in ISK million

## 19. Borrowings

### Secured bonds

| As at 30.9.2015 | Currency | Final maturity | Remaining principal | Contractual interest rate (Base rate + Initial margin/ Step-up margin) | Carrying amount |
|---|---|---|---|---|---|
| BOND B1 | EUR | 9.10.2016 | € 99 million | EURIBOR + 2.90% | 14,200 |
| BOND B2 | USD | 9.10.2016 | $ 18 million | LIBOR + 2.90% | 2,312 |
| BOND B3 | GBP | 9.10.2016 | £ 66 million | LIBOR + 2.90% | 12,835 |
| BOND C1 | EUR | 9.10.2018 | € 132 million | EURIBOR + 2.90% | 18,924 |
| BOND C2 | USD | 9.10.2018 | $ 24 million | LIBOR + 2.90% | 3,082 |
| BOND C3 | GBP | 9.10.2018 | £ 88 million | LIBOR + 2.90% | 17,106 |
| BOND D | USD | 9.10.2020 | $ 271 million | LIBOR + 2.90% / 3.50% | 34,797 |
| BOND E | EUR | 9.10.2022 | € 192 million | EURIBOR + 2.90% / 3.65% | 27,525 |
| BOND F | USD | 9.10.2024 | $ 271 million | LIBOR + 2.90% / 3.95% | 34,797 |
| BOND G | EUR | 9.10.2026 | € 192 million | EURIBOR + 2.90% / 4.05% | 27,525 |
| **Total issued bonds to LBI hf.** | | | | | **193,103** |

| As at 30.9.2015 | Currency | Final maturity | Remaining principal | Indexed/ Non-indexed | Contractual interest rate | Carrying amount |
|---|---|---|---|---|---|---|
| LBANK CB 16 | ISK | 10.6.2016 | 3,360 | Non-indexed | Fixed 6.3% | 3,423 |
| LBANK CB 17 | ISK | 23.10.2017 | 1,340 | Non-indexed | Fixed 6.0% | 1,408 |
| LBANK CB 19 | ISK | 17.9.2019 | 2,580 | Non-indexed | Fixed 6.8% | 2,602 |
| LBANK CBI 22 | ISK | 28.4.2022 | 5,800 | CPI-indexd | Fixed 3.0% | 5,889 |
| **Total covered bonds** | | | | | | **13,322** |
| | | | | | | |
| **Total secured bonds** | | | | | | **206,425** |

### Unsecured debt securities issued

| As at 30.9.2015 | Carrying amount |
|---|---|
| Unlisted bonds | 8 |
| **Total unsecured bonds** | **8** |

### Bills issued

| As at 30.9.2015 | Currency | Final maturity | Remaining principal | Indexed/ Non-indexed | Contractual interest rate | Carrying amount |
|---|---|---|---|---|---|---|
| LBANK 16 0310 | ISK | 10.3.2016 | 1,300 | Non-indexed | - | 1,266 |
| **Total bills issued** | | | | | | **1,266** |
| | | | | | | |
| **Unsecured debt securities issued** | | | | | | **1,274** |
| | | | | | | |
| **Total borrowings as at 30.9.2015** | | | | | | **207,699** |

| As at 31.12.2014 | Currency | Final maturity | Remaining principal | Contractual interest rate (Base rate + Initial margin/ Step-up margin) | Carrying amount |
|---|---|---|---|---|---|
| BOND B1 | EUR | 9.10.2016 | € 99 million | EURIBOR + 2.90% | 15,276 |
| BOND B2 | USD | 9.10.2016 | $ 18 million | LIBOR + 2.90% | 2,285 |
| BOND B3 | GBP | 9.10.2016 | £ 66 million | LIBOR + 2.90% | 13,083 |
| BOND C1 | EUR | 9.10.2018 | € 132 million | EURIBOR + 2.90% | 20,368 |
| BOND C2 | USD | 9.10.2018 | $ 24 million | LIBOR + 2.90% | 3,047 |
| BOND C3 | GBP | 9.10.2018 | £ 88 million | LIBOR + 2.90% | 17,443 |
| BOND D | USD | 9.10.2020 | $ 271 million | LIBOR + 2.90% / 3.50% | 34,402 |
| BOND E | EUR | 9.10.2022 | € 192 million | EURIBOR + 2.90% / 3.65% | 29,626 |
| BOND F | USD | 9.10.2024 | $ 271 million | LIBOR + 2.90% / 3.95% | 34,402 |
| BOND G | EUR | 9.10.2026 | € 192 million | EURIBOR + 2.90% / 4.05% | 29,626 |
| **Total issued bonds to LBI hf.** | | | | | **199,558** |

| As at 31.12.2014 | Currency | Final maturity | Remaining principal | Indexed/ Non-indexed | Contractual interest rate | Carrying amount |
|---|---|---|---|---|---|---|
| LBANK CB 16 | ISK | 10.6.2016 | 3,360 | Non-indexed | Fixed 6.3% | 3,476 |
| LBANK CB 17 | ISK | 23.10.2017 | 1,340 | Non-indexed | Fixed 6.0% | 1,345 |
| LBANK CB 19 | ISK | 17.9.2019 | 2,580 | Non-indexed | Fixed 6.8% | 2,649 |
| **Total covered bonds** | | | | | | **7,470** |
| | | | | | | |
| **Total secured bonds as at 31.12.2014** | | | | | | **207,028** |

All amounts are in ISK million

## 19. Borrowings (continued)

The secured foreign currency bonds consist of ten bonds which the Bank issued to LBI hf. as consideration and additional consideration for the assets and liabilities transferred from LBI hf. to the Bank in October 2008. These bonds were issued in December 2014 following the conclusion of an agreement to extend the previous repayment schedule to the years 2016-2026 and replace the bonds originally issued for the same purpose in October 2010 and April 2013. Under this agreement, bond tranches mature biennially throughout the period, as summarised in the table above. The agreement further provides that should the Bank's long-term credit rating in foreign currency, as rated by Standard & Poor's, be lower than BBB- as of 30 June 2018, the Bank will have the option to amend and extend partly or wholly the maturity date of the tranches maturing in 2018 and 2020.

Interest rate terms are 3-month EURIBOR for the EUR-denominated bonds and 3-month LIBOR for the GBP and USD-denominated bonds plus a 2.90% margin until October 2018, stepping up to a 3.50% margin for the 2020 tranche, a 3.65% margin for the 2022 tranche, a 3.95% margin for the 2024 tranche and a 4.05% margin for the 2026 tranche.

The Bank has committed itself to pledge certain pools of loans to customers as collateral for the secured bonds issued to LBI hf. and the issue of the covered bonds. The Bank must maintain a minimum coverage ratio of 115.0% for the secured bonds issued to LBI hf. and a minimum coverage ratio of 120% for the covered bonds. For further details on encumbered assets, see Note 40.

In September 2015, the Bank and the Winding-up Board of LBI hf. reached an agreement whereby, *inter alia* , the Bank commits itself to prepay during 2015 the foreign currency bonds maturing in October 2016, and to partially prepay the foreign currency bonds maturing in October 2018. The amount for prepayment is equivalent to ISK 47,000 million. The prepayment was subject to the Bank concluding a refinancing arrangement under conditions deemed acceptable by the Bank. This agreement in hand, the Bank concluded a successful series of fixed income investor meetings in Europe, arranged by three major international banks. Following the investor meetings, the Bank issued EUR 300 million in senior unsecured bonds, equivalent to ISK 42,600 million, on 12 October 2015. For further details, see Note 26.

In September 2015, the Bank concluded the sale of an additional tranche of its indexed covered bonds series, LBANK CBI 22, in the amount of ISK 1,100 million. These bonds are consumer price indexed with a maturity of seven years and the option to extend maturity for another three years. The bonds carry a fixed interest rate of 3.0%. The total size of this bond series is limited to ISK 20,000 million. The Bank had previously issued ISK 4,760 million in the same series. The bonds have been admitted for trading on NASDAQ OMX Iceland.

The non-indexed covered bond issues have different fixed interest rates and mature within the next four years. The size of each series is limited to ISK 10,000 million. The three series, LBANK CB 16, LBANK CB 17 and LBANK CB 19, have all been admitted for trading on NASDAQ OMX Iceland.

The unsecured bonds consist of bonds issued by Sparisjóður Vestmannaeyja ("the savings bank") which were assumed by Landsbankinn through the merger of the savings bank with Landsbankinn on 29 March 2015.

On 28 September 2015, the Bank concluded a closed auction of a new series of bills maturing in March 2016, LBANK 16 0310. The Bank received offers in the amount of ISK 5,020 million, of which ISK 1,300 million were accepted. On 5 October 2015, the bills were admitted for trading on NASDAQ OMX Iceland.

## 20. Subordinated liabilities

| As at 30.9.2015 | Currency | Final maturity | Remaining principal in currencies | Indexed/ Non-indexed | Contractual interest rate (Base rate + Margin) | Carrying amount |
|---|---|---|---|---|---|---|
| Subordinated bonds unlisted | ISK | 1.12.2017 | 55.3 | | REIBOR + 4% | 56 |
| Subordinated loan | EUR | 2.12.2020 | EUR 0.2 million | | LIBOR + 5% | 28 |
| Subordinated loan | JPY | 2.12.2020 | JPY 106.1 million | | LIBOR + 5% | 114 |
| Subordinated loan | CHF | 2.12.2020 | CHF 0.7 million | | LIBOR + 5% | 94 |
| Subordinated loan | JPY | 1.12.2023 | JPY 49.1 million | | LIBOR + 5% | 53 |
| Subordinated loan | CHF | 1.12.2023 | CHF 0.3 million | | LIBOR + 5% | 43 |
| Subordinated loan | ISK | 31.12.2020 | 27.0 | CPI-indexd | Fixed 12.0% | 33 |
| Subordinated loan | ISK | 1.10.2021 | 70.0 | CPI-indexd | Fixed 7.0% | 81 |
| Subordinated loan | ISK | 22.9.2017 | 121.3 | CPI-indexd | Fixed 7.0% | 150 |
| Subordinated bonds unlisted | ISK | 22.11.2019 | 115.7 | CPI-indexd | Fixed 5.0% | 123 |
| **Total subordinated liabilities** | | | | | | **775** |

The subordinated liabilities are comprised of liabilities assumed by Landsbankinn through two separate mergers, with savings banks Sparisjóður Vestmannaeyja ses. and Sparisjóður Norðurlands ses. on 29 March 2015 and 4 September 2015, respectively. The subordinated liabilities thus assumed share characteristics of equity in that they are subordinated to other Group liabilities and are included in equity in equity ratio calculation, see Note 27, Capital base and capital adequacy ratio. The outstanding amounts of the subordinated liabilities are subject to regulatory amortisation whereby the amount eligible for Tier 2 capital treatment is amortised on a straight-line basis over the final 5 years to maturity. The subordinated liabilities mature over the next 8 years and are recognised as financial liabilities inclusive of accrued interest at the end of the reporting period.

## 21. Equity

At the Annual General Meeting of the Bank for the operating year 2014 held on 18 March 2015, shareholders approved the Board's proposal to pay dividends to shareholders in the amount of ISK 1.00 per share for the year 2014. Dividend was paid on 25 March 2015 to parties registered in the shareholders' registry on 18 March 2015. The dividend payment amounted to ISK 23,687 million on the outstanding shares.

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## Other notes

### 22. Earnings per share

| Profit for the period | 2015 1.7-30.9 | 2014 1.7-30.9 | 2015 1.1-30.9 | 2014 1.1-30.9 |
|---|---|---|---|---|
| Profit for the period attributable to owners of the Bank | 12,008 | 5,092 | 24,413 | 19,921 |

Diluted earnings per share are calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares.

| Number of shares | 2015 1.7-30.9 | 2014 1.7-30.9 | 2015 1.1-30.9 | 2014 1.1-30.9 |
|---|---|---|---|---|
| Number of ordinary shares issued at beginning of period | 24,000 | 24,000 | 24,000 | 24,000 |
| Average number of own shares | (259) | (313) | (292) | (328) |
| **Weighted average number of shares outstanding** | **23,741** | **23,687** | **23,708** | **23,672** |
| | | | | |
| **Basic and diluted earnings per share from continuing operations** | **0.51** | **0.21** | **1.03** | **0.84** |

The Bank's basic and diluted earnings per share are equal as the Bank has not issued any options, warrants, convertibles or other potential sources of dilution.

### 23. Litigation

The Bank and its subsidiaries are from time to time party to litigation cases which arise in the ordinary course of business. Some of these cases are material in the sense that management considers that they may have a significant impact on the amounts disclosed in the Group's financial statements and are not comparable to other, previously closed, cases.

All the material cases that were reported open and not concluded at year-end 2014 in the litigation section of the Group's Consolidated Financial Statement for the year 2014, and in the litigation section of the Group's Condensed Consolidated Interim Financial Statements for the six months ended 30 June 2015, were open on 30 September 2015. However, after the end of the reporting period, on 15 October 2015, the Supreme Court ruled in favour of the Bank in two of these cases, cf. point 1) below. The pending material litigation cases at the end of the third quarter of 2015 are the following:

Recalculation of foreign currency indexed loans

1) In December 2013, a company brought two lawsuits against the Bank demanding recalculation of previous recalculations of a foreign currency indexed loan in accordance with Supreme Court judgements No. 600/2011 and No. 464/2012. The plaintiff argues that conditions are met for derogating from the legal principle that a claimant has the right to receive additional payment. As such, contractual interest should be paid in accordance with final receipts rather than Central Bank interest rates. Landsbankinn rejected the company's claim, referring, *inter alia*, to Supreme Court judgement No. 463/2013 concluding that conditions for the exception had not been met since the difference in the comparative position between the parties was insignificant and the additional claim would not cause a serious disruption to the company's financial position comparable to the impact unexpected demands for additional payment would have on an individual or small enterprise. On 7 November 2014, Landsbankinn was acquitted in both cases by the District Court. The District Court concluded that the company had not shown that the Bank's insistence on Central Bank interest rates had had such a material and unexpected impact on its financial position that the Bank should absorb the risk arising from the imbalance between contractual rates and Central Bank rates. The cases were appealed to the Supreme Court and were heard by the Court on 8 September 2015. On 10 September 2015, the Court decided that the cases should be heard again by the Court consisting of five judges on 1 October 2015, and on 15 October 2015, the Court ruled in its judgements Nos. 34/2015 and 35/2015 in favour of the Bank in both cases. The effect of these rulings result in a reversal of previously recognised expenses in the amount of ISK 9,145 million at the end of the third quarter of 2015 (see Note 3).

Inflation-indexation of financial obligations

2) In January 2013, a customer commenced litigation against the Bank, seeking acknowledgement of the unlawfulness of a consumer price indexation provision in a bond issued by him to the Bank and that it is not permissible for the Bank to revalue the principle amount of the bond on a monthly basis in accordance with the consumer price index. The EFTA Court handed down its advisory opinion on the case on 24 November 2014. The District Court will now review the EFTA Court's opinion and establish, based on Icelandic law, whether and to what extent it impacts judgement in the case. The case was to be heard by the District Court on 8 May 2015. The hearing was postponed to await a forthcoming ruling by the Supreme Court in a similar case involving another Icelandic financial undertaking. The Supreme Court delivered its judgment in that case (Case No. 160/2015) on 13 May 2015, ruling in favour of the financial undertaking. Due to the similarities between the two cases, it is considered likely that the District Court will rule in favour of the Bank at the end of 2015.

Transfer of assets and liabilities from Landsbanki Íslands (LBI hf.) to Landsbankinn

3) In November 2012, Landsbankinn Guernsey Ltd. commenced litigation against the Bank et al., concerning money market deposits placed with Landsbanki Íslands (now LBI hf.). The District Court acquitted the Bank of the plaintiff's claims on 19 December 2014 and concluded that the deposits should not have been classified as obligations to be transferred to Landsbankinn in accordance with the decisions of the Financial Supervisory Authority dated 9 October and 11 November 2008. The case has been referred to the Supreme Court and will be heard on 2 November 2015.

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## 23. Litigation (continued)

Investigation of the Icelandic Competition Authority into lending terms

4) In March 2013, the Icelandic Competition Authority submitted to the Bank its preliminary assessment concerning certain preferential terms and conditions offered during 2004-2010 by Landsbanki Íslands hf. (now LBI hf.) and, subsequently, by the Bank, in 2004 to 2010, to clients for retail banking services, in particular for household mortgage loans. In June 2013, the Bank gave its response and refuted allegations of a breach of competition rules. The Bank does not have information as to whether the Competition Authority will take further action in the case but has expressed willingness to discuss the matter. On 1 July 2014, the Authority notified the Bank that a decision in the case would not be forthcoming until the first six months of 2015. The Authority has not notified the Bank of any such decision. On 11 September 2015, the Authority and the Bank agreed to enter into discussions concerning resolution of the case.

Claim for damages by a payment card company

5) In June 2013, a payment card company commenced litigation against the Bank and other financial undertakings claiming tort liability in the amount of around ISK 1.2 billion, plus interest. The plaintiff argues that the defendants are liable in tort for alleged violation of competition rules. The Bank refutes the allegations and the claims. The plaintiff has requested an appraisal by court-appointed assessors on issues regarding its allegations. Work on the appraisal is currently on-going and it is anticipated that the Bank's defence will be submitted once the appraisal has been completed.

## 24. Interest in subsidiaries

The main subsidiaries held directly or indirectly by the Group as at 30 September 2015 were as detailed in the table below. This includes those subsidiaries that are most significant in the context of the Group's business.

**Main subsidiaries as at 30 September 2015**

| Company | Ownership interest | Activity |
|---|---|---|
| Eignarhaldsfélag Landsbankans ehf. (Iceland) | 100% | Holding company |
| Landsbréf hf. (Iceland) | 100% | Management company for mutual funds |
| Hömlur ehf. (Iceland)* | 100% | Holding company |

*Hömlur ehf. is a parent of a number of subsidiaries, which are neither individually nor combined significant in the context of the Group's business.

The Group does not have significant restrictions on its ability to access or use its assets and settle its liabilities other than those resulting from the supervisory framework. The Group did not have any material non-controlling interests as at 30 September 2015.

## 25. Related party transactions

### Transactions with related parties

### Transactions with the Icelandic government and government-related entities

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 at market price and otherwise under generally accepted commercial terms. The nature and outstanding amounts receivable from public entities are disclosed in Note 29.

In March 2015, Landsbankinn and the savings bank Sparisjóður Vestmannaeyja ses. merged, as addressed in Note 5. Prior to the merger, the Icelandic State Treasury, on behalf of the Icelandic State, held the majority of guarantee capital shares in the savings bank. Upon the merger, owners of the guarantee capital of the savings bank received shares in Landsbankinn in exchange for their guarantee capital shares.

Similarly, in September 2015, there was another merger between Landsbankinn and the savings bank Sparisjóður Norðurlands ses., as addressed in Note 5. Upon the merger, owners of the guarantee capital of the savings bank, the largest being the Icelandic State, also received shares in Landsbankinn in exchange for their guarantee capital shares.

for the nine months ended 30 September 2015 27 All amounts are in ISK million

## 25. Related party transactions (continued)

### Transactions with other related parties

The following table presents the total amounts of loans to key management personnel and parties related to them and loans to associates of the Group:

| | 2015 | | 2014 | |
|---|---|---|---|---|
| **Loans in ISK million** | **Balance as at 30 September** | **Highest amount outstanding during the period** | **Balance as at 31 December** | **Highest amount outstanding during the period** |
| Key management personnel | 132 | 168 | 95 | 155 |
| Parties related to key management personnel | 35 | 65 | 62 | 165 |
| Associates | 17,651 | 20,149 | 17,583 | 56,357 |
| Other | 127 | 130 | 11 | 17 |
| **Total** | **17,945** | **20,512** | **17,751** | **56,694** |

No specific allowance for impairment was recognised in respect of these loans.

No pledges or commitments have been given or received in respect of these transactions during the period. There are no leasing transactions between related parties during the period.

The following table presents the total amounts of deposits received from key management personnel and parties related to them and associates of the Group:

| | 2015 | | 2014 | |
|---|---|---|---|---|
| **Deposits in ISK million** | **Balance as at 30 September** | **Highest amount outstanding during the period** | **Balance as at 31 December** | **Highest amount outstanding during the period** |
| Key management personnel | 55 | 163 | 55 | 123 |
| Parties related to key management personnel | 21 | 119 | 23 | 74 |
| Associates | 166 | 460 | 304 | 18,107 |
| Other | 1 | 1 | 1 | 2 |
| **Total** | **243** | **743** | **383** | **18,306** |

The following table presents the total amount of guarantees to key management personnel and parties related to them and associates of the Group:

| **Guarantees in ISK million** | **Balance as at 30 September 2015** | **Balance as at 31 December 2014** |
|---|---|---|
| Key management personnel | - | - |
| Parties related to key management personnel | 4 | - |
| Associates | - | - |
| **Total** | **4** | **0** |

All of the above transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third party counterparties.

## 26. Events after the reporting period

On 12 October 2015, the Bank issued EUR 300 million in senior unsecured bonds, equivalent to ISK 43,000 million. The bonds have a 3-year maturity with a fixed 3.00% coupon and were priced at terms equivalent to a 295 basis point spread above mid-swaps in euros. They are issued under the Bank's 1 billion Euro Medium Term Note (EMTN) Programme and will be listed on the Irish Stock Exchange.

On 19 October 2015, the Bank used the proceeds of this new issuance to make simultaneous early repayments on the foreign currency senior secured bonds maturing in October 2016 and partial payment on bonds maturing in October 2018. Following this issuance, provided the Winding-up Board of LBI hf. finalizes a composition agreement with the payment of a stability contribution, the Bank will also prepay the remaining outstanding amounts of the 2018 senior secured foreign currency bonds, in total equivalent to around ISK 22,000 million. From the time of such latter prepayment, LBI hf. will invest the proceeds as foreign currency term deposits with the Bank, maturing in October 2018, and at terms equal to 150 basis points above interbank rates. Also, provided that the Winding-up Board of LBI hf. finalizes a composition agreement with the payment of a stability contribution, the Bank will for 15 months have the option to convert the 2020 to 2026 maturities of the senior secured foreign currency bonds into senior unsecured foreign currency bonds under the Bank's EMTN Programme, at market terms.

On 15 October 2015, the Supreme Court ruled in favour of the Bank in two cases where recalculations of foreign currency indexed loan were disputed. For further details see Note 3 and Note 23.

## Capital management

### 27. Capital management

The Bank's capital management policies and practices ensure that the Bank has sufficient capital to cover the risks associated with its activities on a consolidated basis. The capital management framework of the Bank comprises four interdependent areas: capital assessment, risk appetite/capital target, capital planning, and reporting/monitoring. The Bank regularly monitors and assesses its risk profile in its most important business areas on a consolidated basis and for the most important risk types. Risk appetite sets out the level of risk the Bank is willing to take in pursuit of its business objectives.

The Bank's capital requirements are defined in Icelandic law and regulations, on the one hand, and by the Icelandic Financial Supervisory Authority (FME), on the other. The requirements are based on the European legal framework for capital requirements (CRD IV and CRR) implementing the Basel III capital framework. The regulatory minimum capital requirement under Pillar I of the Basel framework is 8% of Risk-Weighted Assets (RWA) for credit risk, market risk and operational risk. In conformity with Pillar II of the Basel framework, the Bank annually assesses its own capital needs through the Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP results are subsequently reviewed by the FME in the Supervisory Review and Evaluation Process (SREP). The Bank's Total Capital Requirement, as determined by the FME, is the sum of Pillar I and Pillar II requirements.

On 9 July 2015, legislation amending the Icelandic Act on Financial Undertakings No. 161/2002 entered into force, implementing capital buffer requirements under CRD IV. Under the new legal framework, the FME can impose proportionate restrictions on a credit institution's dividend payments, variable remuneration to employees and/or other payments of similar nature, if its capital adequacy ratio falls below the total capital requirement plus capital buffers.

On 14 April 2015, the Icelandic Financial Stability Council defined the Bank as a systematically important institution in Iceland.

The Group's most recent capital requirements, as determined by the FME, are as follows (as a percentage of RWA):

| | SREP based on data from | |
|---|---|---|
| | 31.12.2014 | 31.12.2013* |
| Pillar I | 8.0% | 8.0% |
| Pillar II | 6.3% | 7.8% |
| **Total capital requirement** | **14.3%** | **15.8%** |
| | | |
| Systemic risk buffer | 3.0% | 3.0% |
| Capital buffer for systematically important institutions | 2.0% | 2.0% |
| Countercyclical capital buffer | 0.0% | 0.0% |
| Capital conservation buffer | 2.5% | 2.5% |
| **Total capital buffers** | **7.5%** | **7.5%** |
| | | |
| **Total capital requirement plus capital buffers** | **21.8%** | **23.3%** |

*Legislation regarding capital buffers was not in place with regards to SREP based on data from 31.12.2013.

The Bank's target for the Group's minimum total capital ratio is at each time the higher of 20.0% of RWA and total FME capital requirement plus capital buffers. As a result and as at the reporting date, the Bank's target for the Group's minimum total capital ratio is 21.8% of RWA.

All amounts are in ISK million

## 28. Capital base and capital adequacy ratio

The Group's equity as at 30 September 2015 amounted to ISK 252,484 million (31.12.2014: ISK 250,803 million), equivalent to 21.5% (31.12.2014: 22.8%) of total assets, according to the Consolidated Statement of Financial Position. The total capital ratio (capital adequacy ratio), calculated in accordance with Article 84 of Act No. 161/2002, on Financial Undertakings, was29.1% at 30 September 2015 (31.12.2014: 29.5%).

| **Capital base** | **30.9.2015** | **31.12.2014** |
|---|---|---|
| Share capital | 23,782 | 23,687 |
| Share premium | 122,105 | 121,275 |
| Reserves | 6,000 | 6,000 |
| Retained earnings | 100,567 | 99,841 |
| Non-controlling interests | 30 | - |
| **Total equity** | **252,484** | **250,803** |
| Intangible assets | (2,089) | (1,225) |
| Deferred tax assets | (199) | (83) |
| **Tier 1 capital** | **250,196** | **249,495** |
| Subordinated liabilities | 775 | - |
| Regulatory amortisation | (143) | - |
| **Tier 2 capital** | **632** | **0** |
| | | |
| **Capital base** | **250,828** | **249,495** |
| | | |
| **Risk-weighted assets** | | |
| Credit risk* | 728,963 | 665,167 |
| Market risk* | 34,312 | 83,601 |
| Operational risk** | 96,836 | 96,836 |
| **Total risk-weighted assets** | **860,111** | **845,604** |
| | | |
| Tier 1 capital ratio | 29.1% | 29.5% |
| Total capital ratio (capital adequacy ratio) | 29.2% | 29.5% |

*The Group has revised its classification of equities and bond and debt instrument exposures in the trading book as of 1 January 2015. Accordingly, risk-weighted assets in equities in the banking book and bond and debt instruments in the banking book are classified as credit risk rather than market risk.

**The amounts are updated on a yearly basis.

for the nine months ended 30 September 2015 30 All amounts are in ISK million

### 29. Maximum exposure to credit risk and concentration by industry sectors

The following tables show the Group's maximum credit risk exposure at 30 September 2015 and 31 December 2014. For on-balance sheet assets, the exposures set out below are based on net carrying amounts as reported in the Statement of Financial Position. Off-balance sheet amounts in the tables below are the maximum amounts the Group might have to pay for guarantees, loan commitments in their full amount, and undrawn overdraft and credit card facilities.

The Group uses the ISAT 08 industry classification for corporate customers.

| | | | | Corporates | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| As at 30 September 2015 | Financial institutions | Public entities* | Individuals | Fisheries | Construction and real estate companies | Holding companies | Retail | Services | ITC** | Manu-facturing | Agriculture | Other | Carrying amount |
| Cash and balances with Central Bank | - | 27,120 | - | - | - | - | - | - | - | - | - | - | **27,120** |
| Bonds and debt instruments | 935 | 224,737 | - | - | 8,582 | 127 | - | - | - | - | - | 1,407 | **235,788** |
| Derivative instruments | 25 | 7 | - | 115 | 53 | 5 | - | - | - | - | - | 42 | **247** |
| Loans and advances to financial institutions | 46,511 | - | - | - | - | - | - | - | - | - | - | - | **46,511** |
| Loans and advances to customers | - | 13,186 | 280,541 | 167,767 | 135,375 | 55,165 | 37,067 | 61,318 | 20,427 | 27,171 | 9,012 | 4 | **807,033** |
| Other financial assets | 7,761 | 327 | 614 | 13 | 668 | 43 | 6 | 438 | 2 | 227 | 1 | 33 | **10,133** |
| **Total on-balance sheet exposure** | **55,232** | **265,377** | **281,155** | **167,895** | **144,678** | **55,340** | **37,073** | **61,756** | **20,429** | **27,398** | **9,013** | **1,486** | **1,126,832** |
| **Off-balance sheet exposure** | **9,399** | **18,289** | **24,711** | **22,085** | **37,880** | **1,296** | **15,199** | **16,459** | **3,585** | **9,083** | **2,847** | **444** | **161,277** |
| Financial guarantees and underwriting commitments | 26 | 616 | 882 | 7,542 | 1,851 | 10 | 2,313 | 2,240 | 1,095 | 452 | 27 | 440 | 17,494 |
| Undrawn loan commitments | 600 | 10,561 | 100 | 10,481 | 32,129 | 942 | 7,291 | 1,638 | 1,348 | 6,396 | 2,335 | - | 73,821 |
| Undrawn overdraft/credit card facilities | 8,773 | 7,112 | 23,729 | 4,062 | 3,900 | 344 | 5,595 | 12,581 | 1,142 | 2,235 | 485 | 4 | 69,962 |
| **Maximum exposure to credit risk** | **64,631** | **283,666** | **305,866** | **189,980** | **182,558** | **56,636** | **52,272** | **78,215** | **24,014** | **36,481** | **11,860** | **1,930** | **1,288,109** |
| Percentage of carrying amount | 5.0% | 22.0% | 23.7% | 14.7% | 14.2% | 4.4% | 4.1% | 6.1% | 1.9% | 2.8% | 0.9% | 0.1% | 100% |

* Public entities consist of central government, state-owned enterprises, Central Bank and municipalities.

** ITC consists of corporations in the information, technology and communication industry sectors.

All amounts are in ISK million

### 29. Maximum exposure to credit risk and concentration by industry sectors (continued)

| | | | | Corporates | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **As at 31 December 2014** | **Financial institutions** | **Public entities*** | **Individuals** | **Fisheries** | **Construction and real estate companies** | **Holding companies** | **Retail** | **Services** | **ITC**** | **Manu-facturing** | **Agriculture** | **Other** | **Carrying amount** |
| Cash and balances with Central Bank | - | 10,160 | - | - | - | - | - | - | - | - | - | - | **10,160** |
| Bonds and debt instruments | 41 | 221,293 | - | - | 13,345 | 7,880 | - | - | - | - | - | 1,030 | **243,589** |
| Derivative instruments | 38 | - | 7 | - | - | 1 | - | - | - | - | - | 32 | **78** |
| Loans and advances to financial institutions | 49,789 | - | - | - | - | - | - | - | - | - | - | - | **49,789** |
| Loans and advances to customers | - | 13,708 | 238,932 | 156,023 | 112,880 | 42,861 | 39,118 | 56,387 | 19,798 | 28,760 | 8,751 | 1,137 | **718,355** |
| Other financial assets | 913 | 343 | 331 | - | 614 | 71 | 130 | 711 | 3 | 16,554 | 1 | 62 | **19,733** |
| **Total on-balance sheet exposure** | **50,781** | **245,504** | **239,270** | **156,023** | **126,839** | **50,813** | **39,248** | **57,098** | **19,801** | **45,314** | **8,752** | **2,261** | **1,041,704** |
| | | | | | | | | | | | | | |
| **Off-balance sheet exposure** | **2,648** | **13,688** | **22,507** | **28,197** | **33,802** | **5,150** | **11,143** | **12,652** | **3,423** | **8,974** | **525** | **706** | **143,415** |
| Financial guarantees and underwriting commitments | 45 | 611 | 572 | 7,740 | 1,917 | 3,525 | 2,240 | 2,250 | 673 | 559 | 37 | 331 | 20,500 |
| Undrawn loan commitments | - | 7,238 | - | 17,956 | 29,877 | 913 | 4,926 | 578 | 1,763 | 6,510 | 182 | 174 | 70,117 |
| Undrawn overdraft/credit card facilities | 2,603 | 5,839 | 21,935 | 2,501 | 2,008 | 712 | 3,977 | 9,824 | 987 | 1,905 | 306 | 201 | 52,798 |
| | | | | | | | | | | | | | |
| **Maximum exposure to credit risk** | **53,429** | **259,192** | **261,777** | **184,220** | **160,641** | **55,963** | **50,391** | **69,750** | **23,224** | **54,288** | **9,277** | **2,967** | **1,185,119** |
| | | | | | | | | | | | | | |
| Percentage of carrying amount | 4.5% | 21.9% | 22.1% | 15.5% | 13.6% | 4.7% | 4.3% | 5.9% | 2.0% | 4.6% | 0.8% | 0.3% | 100% |

* Public entities consist of central government, state-owned enterprises, Central Bank and municipalities.

** ITC consists of corporations in the information, technology and communication industry sectors.

All amounts are in ISK million

## 30. Collateral and loan-to-value by industry sectors

The loan-to-value (LTV) ratio expresses the maximum exposure of credit risk (gross carrying amount of loans and off-balance sheet items) as a percentage of the total value of collateral less a haircut. Loan-to-value is one of the key risk factors assessed when qualifying borrowers for a loan. The risk of default is always at the forefront of lending decisions, and the likelihood of a lender absorbing a loss in the foreclosure process increases as the collateral value decreases. A high LTV indicates that there are smaller buffers to protect against price falls or increases in the loan if repayments are not made and interest is added to the outstanding balance.

| | LTV ratio - Fully collateralised | | | | | LTV ratio - Partially collateralised | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **As at 30 September 2015** | 0% - 25% | 25% - 50% | 50% - 75% | 75% - 100% | Total | >100% | Collateral value | Without collateral | Allowance for impairment | Maximum exposure to credit risk |
| Financial institutions | - | - | - | - | - | - | - | 55,911 | - | 55,911 |
| Public entities | 19 | 73 | 200 | 892 | 1,184 | 3,968 | 412 | 26,561 | (238) | 31,475 |
| Individuals | 12,690 | 28,312 | 44,975 | 72,160 | 158,137 | 80,479 | 59,680 | 82,108 | (15,473) | 305,251 |
| **Corporates** | **5,863** | **18,620** | **56,993** | **132,589** | **214,065** | **343,346** | **197,813** | **84,672** | **(19,899)** | **622,184** |
| Fisheries | 2,117 | 10,020 | 34,140 | 66,829 | 113,106 | 62,589 | 46,953 | 17,117 | (2,960) | 189,852 |
| Construction and real estate companies | 1,202 | 3,232 | 9,799 | 26,301 | 40,534 | 126,885 | 66,686 | 12,626 | (6,790) | 173,255 |
| Holding companies | 138 | 143 | 3,591 | 11,514 | 15,386 | 38,799 | 21,220 | 3,507 | (1,232) | 56,460 |
| Retail | 226 | 1,085 | 2,472 | 5,688 | 9,471 | 36,619 | 21,601 | 8,414 | (2,238) | 52,266 |
| Services | 1,029 | 2,627 | 4,527 | 8,833 | 17,016 | 40,310 | 21,214 | 23,604 | (3,153) | 77,777 |
| Information, technology and communication | 66 | 107 | 65 | 48 | 286 | 15,733 | 7,185 | 8,525 | (531) | 24,013 |
| Manufacturing | 510 | 834 | 1,122 | 12,359 | 14,825 | 14,656 | 8,590 | 9,499 | (2,726) | 36,254 |
| Agriculture | 575 | 572 | 1,277 | 1,017 | 3,441 | 7,755 | 4,364 | 932 | (269) | 11,859 |
| Other | - | - | - | - | - | - | - | 448 | - | 448 |
| **Total** | **18,572** | **47,005** | **102,168** | **205,641** | **373,386** | **427,793** | **257,905** | **249,252** | **(35,610)** | **1,014,821** |
| **As at 31 December 2014** | | | | | | | | | | |
| Financial institutions | - | - | - | - | - | - | - | 52,438 | - | 52,438 |
| Public entities | 36 | 86 | 198 | 807 | 1,127 | 2,767 | 437 | 23,626 | (124) | 27,396 |
| Individuals* | 10,491 | 22,826 | 34,122 | 58,785 | 126,224 | 82,048 | 55,350 | 69,190 | (16,022) | 261,440 |
| **Corporates** | **6,398** | **21,417** | **43,297** | **114,054** | **185,166** | **336,838** | **200,498** | **73,582** | **(25,301)** | **570,285** |
| Fisheries | 3,715 | 13,169 | 22,288 | 55,862 | 95,034 | 84,487 | 59,605 | 11,184 | (6,484) | 184,221 |
| Construction and real estate companies | 903 | 2,586 | 6,605 | 25,102 | 35,196 | 107,462 | 60,068 | 11,069 | (7,046) | 146,681 |
| Holding companies | 268 | 184 | 2,021 | 11,463 | 13,936 | 30,421 | 16,525 | 6,241 | (2,590) | 48,008 |
| Retail | 168 | 2,384 | 2,250 | 8,704 | 13,506 | 32,111 | 18,744 | 7,725 | (3,080) | 50,262 |
| Services | 742 | 1,929 | 3,869 | 7,640 | 14,180 | 39,745 | 21,702 | 17,955 | (2,841) | 69,039 |
| Information, technology and communication | 47 | 65 | 61 | 50 | 223 | 15,891 | 7,032 | 7,762 | (656) | 23,220 |
| Manufacturing | 141 | 521 | 4,659 | 4,424 | 9,745 | 20,396 | 12,465 | 9,670 | (2,077) | 37,734 |
| Agriculture | 413 | 579 | 1,544 | 809 | 3,345 | 5,228 | 3,415 | 1,222 | (519) | 9,276 |
| Other | 1 | - | - | - | 1 | 1,097 | 942 | 754 | (8) | 1,844 |
| **Total** | **16,925** | **44,329** | **77,617** | **173,646** | **312,517** | **421,653** | **256,285** | **218,836** | **(41,447)** | **911,559** |

* The comparative amounts have been restated due to an error in the year-end 2014 amounts previously disclosed. The amounts in this table are of an informative nature only and do not have any effect on the amounts reported by the Group in Income Statement or Statement of Financial Position.

All amounts are in ISK million

## 31. Collateral types

The following tables show the collateral value less a haircut held to mitigate credit risk.

| As at 30 September 2015 | Real estate | Vessels | Deposits | Securities | Other* | Total |
|---|---|---|---|---|---|---|
| Public entities | 2,018 | - | 48 | - | 115 | 2,181 |
| Individuals | 327,697 | 558 | 307 | 2,661 | 15,367 | 346,590 |
| **Corporates** | **203,159** | **163,514** | **3,061** | **64,146** | **80,054** | **513,934** |
| Fisheries | 12,424 | 162,695 | 224 | 17,103 | 25,267 | 217,713 |
| Construction and real estate companies | 113,450 | 28 | 330 | 386 | 3,360 | 117,554 |
| Holding companies | 9,079 | 15 | 727 | 36,879 | 664 | 47,364 |
| Retail | 13,619 | 22 | 274 | 1,193 | 18,957 | 34,065 |
| Services | 35,419 | 717 | 781 | 922 | 14,120 | 51,959 |
| Information, technology and communication | 718 | 2 | 485 | 987 | 5,703 | 7,895 |
| Manufacturing | 9,224 | 18 | 235 | 6,676 | 9,943 | 26,096 |
| Agriculture | 9,207 | 17 | 5 | - | 2,040 | 11,269 |
| Other | 19 | - | - | - | - | 19 |
| **Total** | **532,874** | **164,072** | **3,416** | **66,807** | **95,536** | **862,705** |

| As at 31 December 2014 | Real estate | Vessels | Deposits | Securities | Other* | Total |
|---|---|---|---|---|---|---|
| Public entities | 1,935 | - | 35 | - | 43 | 2,013 |
| Individuals** | 260,452 | 472 | 408 | 2,449 | 15,730 | 279,511 |
| **Corporates** | **178,130** | **156,904** | **2,215** | **54,720** | **74,776** | **466,745** |
| Fisheries | 11,123 | 155,421 | 36 | 14,623 | 23,911 | 205,114 |
| Construction and real estate companies | 97,317 | 18 | 647 | 393 | 2,655 | 101,030 |
| Holding companies | 8,168 | - | 52 | 29,975 | 482 | 38,677 |
| Retail | 13,557 | 456 | 192 | 662 | 18,968 | 33,835 |
| Services | 30,174 | 608 | 726 | 1,940 | 11,360 | 44,808 |
| Information, technology and communication | 578 | 2 | 140 | 1,002 | 5,784 | 7,506 |
| Manufacturing | 9,080 | 382 | 415 | 6,075 | 8,874 | 24,826 |
| Agriculture | 8,116 | 17 | 7 | - | 1,850 | 9,990 |
| Other | 17 | - | - | 50 | 892 | 959 |
| **Total** | **440,517** | **157,376** | **2,658** | **57,169** | **90,549** | **748,269** |

* Other includes collateral like financial claims, invoices, liquid assets, vehicles, machines, aircrafts and inventories.

** The comparative amounts have been restated due to an error in the year-end 2014 amounts previously disclosed. The amounts in this table are of an informative nature only and do not have any effect on the amounts reported by the Group in Income Statement or Statement of Financial Position.

## 32. Loans and advances credit monitoring

The following tables show the credit risk monitoring split on colour classification.

| Industry sectors as at 30 September 2015 | Green | Yellow | Orange | Red | Carrying amount |
|---|---|---|---|---|---|
| Financial institutions | 46,511 | - | - | - | 46,511 |
| Public entities | 11,623 | 344 | 315 | 904 | 13,186 |
| Individuals | 237,025 | 12,911 | 20,620 | 9,985 | 280,541 |
| **Corporates** | **442,889** | **36,189** | **19,914** | **14,314** | **513,306** |
| Fisheries | 161,080 | 1,970 | 2,508 | 2,211 | 167,769 |
| Construction and real estate companies | 109,542 | 14,093 | 6,508 | 5,231 | 135,374 |
| Holding companies | 48,445 | 5,140 | 1,300 | 280 | 55,165 |
| Retail | 31,517 | 2,303 | 2,335 | 911 | 37,066 |
| Services | 45,786 | 9,021 | 5,317 | 1,194 | 61,318 |
| Information, technology and communication | 19,801 | 269 | 274 | 83 | 20,427 |
| Manufacturing | 19,426 | 1,948 | 1,418 | 4,379 | 27,171 |
| Agriculture | 7,288 | 1,445 | 254 | 25 | 9,012 |
| Other | 4 | - | - | - | 4 |
| **Total** | **738,048** | **49,444** | **40,849** | **25,203** | **853,544** |

All amounts are in ISK million

### 32. Loans and advances credit monitoring (continued)

| Industry sectors as at 31 December 2014 | Green | Yellow | Orange | Red | Carrying amount |
|---|---|---|---|---|---|
| Financial institutions | 49,789 | - | - | - | 49,789 |
| Public entities | 12,878 | 718 | 96 | 16 | 13,708 |
| Individuals | 196,551 | 12,277 | 18,647 | 11,456 | 238,931 |
| **Corporates** | **354,590** | **64,583** | **31,162** | **15,381** | **465,716** |
| Fisheries | 114,306 | 23,127 | 16,226 | 2,364 | 156,023 |
| Construction and real estate companies | 85,072 | 17,904 | 5,205 | 4,699 | 112,880 |
| Holding companies | 37,835 | 4,044 | 649 | 333 | 42,861 |
| Retail | 32,681 | 2,978 | 2,266 | 1,192 | 39,117 |
| Services | 41,556 | 8,325 | 4,788 | 1,718 | 56,387 |
| Information, technology and communication | 15,831 | 3,650 | 232 | 85 | 19,798 |
| Manufacturing | 19,209 | 3,565 | 1,131 | 4,856 | 28,761 |
| Agriculture | 7,095 | 857 | 665 | 134 | 8,751 |
| Other | 1,005 | 133 | - | - | 1,138 |
| **Total** | **613,808** | **77,578** | **49,905** | **26,853** | **768,144** |

### 33. Credit quality of financial assets

| | Gross carrying amount | | | | | |
|---|---|---|---|---|---|---|
| **As at 30 September 2015** | Neither past due nor individually impaired | Past due but not individually impaired | Individually impaired | Total | Allowance for impairment | Carrying amount |
| Cash and balances with Central Bank | 27,120 | - | - | 27,120 | - | 27,120 |
| Bonds and debt instruments | 235,398 | 390 | - | 235,788 | - | 235,788 |
| Derivative instruments | 247 | - | - | 247 | - | 247 |
| Loans and advances to financial institutions | 46,511 | - | - | 46,511 | - | 46,511 |
| Loans and advances to customers | 759,623 | 26,395 | 56,625 | 842,643 | (35,610) | 807,033 |
| Other financial assets | 10,133 | - | - | 10,133 | - | 10,133 |
| **Total** | **1,079,032** | **26,785** | **56,625** | **1,162,442** | **(35,610)** | **1,126,832** |
| **As at 31 December 2014** | | | | | | |
| Cash and balances with Central Bank | 10,160 | - | - | 10,160 | - | 10,160 |
| Bonds and debt instruments | 235,568 | 8,021 | - | 243,589 | - | 243,589 |
| Derivative instruments | 78 | - | - | 78 | - | 78 |
| Loans and advances to financial institutions | 49,789 | - | - | 49,789 | - | 49,789 |
| Loans and advances to customers | 657,564 | 25,015 | 77,223 | 759,802 | (41,447) | 718,355 |
| Other financial assets | 19,733 | - | - | 19,733 | - | 19,733 |
| **Total** | **972,892** | **33,036** | **77,223** | **1,083,151** | **(41,447)** | **1,041,704** |

The allowance for impairment includes both the allowance for individual impairment and the allowance for collective impairment.

All amounts are in ISK million

### 34. Loans and advances neither past due nor individually impaired

The following tables show the credit quality, measured by rating grade, of loans and advances neither past due nor individually impaired.

| As at 30 September 2015 | Rating grades 10-7 | 6-4 | 3-1 | 0 | Unrated | Gross carrying amount |
|---|---|---|---|---|---|---|
| Financial institutions | 46,510 | 1 | - | - | - | 46,511 |
| Public entities | 12,148 | 514 | 169 | - | 123 | 12,954 |
| Individuals | 82,113 | 132,884 | 38,980 | 289 | 3,065 | 257,331 |
| **Corporates** | **63,113** | **306,535** | **117,237** | **2,156** | **297** | **489,338** |
| Fisheries | 26,360 | 100,042 | 36,649 | 1,910 | 66 | 165,027 |
| Construction and real estate companies | 5,097 | 83,593 | 36,886 | 18 | 1 | 125,595 |
| Holding companies | - | 41,319 | 13,120 | 9 | 34 | 54,482 |
| Retail | 12,916 | 15,224 | 7,100 | 18 | 14 | 35,272 |
| Services | 9,070 | 34,691 | 14,151 | 168 | 147 | 58,227 |
| Information, technology and communication | 4,669 | 11,059 | 4,865 | - | - | 20,593 |
| Manufacturing | 4,058 | 14,921 | 2,730 | 27 | - | 21,736 |
| Agriculture | 943 | 5,683 | 1,736 | 6 | 35 | 8,403 |
| Other | - | 3 | - | - | - | 3 |
| **Total** | **203,884** | **439,934** | **156,386** | **2,445** | **3,485** | **806,134** |

| As at 31 December 2014 | Rating grades 10-7 | 6-4 | 3-1 | 0* | Unrated | Gross carrying amount |
|---|---|---|---|---|---|---|
| Financial institutions | 49,789 | - | - | - | - | 49,789 |
| Public entities | 12,229 | 1,330 | 47 | - | 12 | 13,618 |
| Individuals | 76,490 | 97,345 | 35,635 | 266 | 3,718 | 213,454 |
| **Corporates** | **47,154** | **250,992** | **129,553** | **2,253** | **540** | **430,492** |
| Fisheries | 31,388 | 79,640 | 36,900 | 1,947 | 2 | 149,877 |
| Construction and real estate companies | 605 | 55,037 | 51,002 | 63 | 11 | 106,718 |
| Holding companies | - | 22,178 | 8,603 | 61 | 35 | 30,877 |
| Retail | 1,096 | 29,066 | 6,749 | 16 | 3 | 36,930 |
| Services | 12,404 | 27,523 | 13,342 | 5 | 54 | 53,328 |
| Information, technology and communication | 206 | 11,084 | 8,822 | 5 | 1 | 20,118 |
| Manufacturing | 1,024 | 19,072 | 2,901 | 156 | 422 | 23,575 |
| Agriculture | 431 | 6,373 | 1,109 | - | 12 | 7,925 |
| Other | - | 1,019 | 125 | - | - | 1,144 |
| **Total** | **185,662** | **349,667** | **165,235** | **2,519** | **4,270** | **707,353** |

* Due to the accounting policies, loans and advances acquired at deep discount are not impaired even though the Group considers the obligor likely not to meet its obligations. Hence such loans can be defaulted but neither past due nor individually impaired.

### 35. Loans and advances past due but not individually impaired

The following table shows the gross carrying amount of loans and advances to financial institutions and customers that have failed to make payments which had become contractually due by one or more days.

| As at 30 September 2015 | Past due 1-5 days | Past due 6-30 days | Past due 31 - 60 days | Past due 61 - 90 days | Past due over 90 days | Gross carrying amount |
|---|---|---|---|---|---|---|
| Public entities | - | 17 | - | - | - | 17 |
| Individuals | 133 | 10,463 | 1,695 | 1,076 | 950 | 14,317 |
| Corporates | 3,253 | 6,150 | 519 | 649 | 1,490 | 12,061 |
| **Total** | **3,386** | **16,630** | **2,214** | **1,725** | **2,440** | **26,395** |
| **As at 31 December 2014** | | | | | | |
| Public entities | - | 1 | 84 | 7 | 6 | 98 |
| Individuals | 2,419 | 7,321 | 3,430 | 1,352 | 976 | 15,498 |
| Corporates | 521 | 3,787 | 3,336 | 696 | 1,079 | 9,419 |
| **Total** | **2,940** | **11,109** | **6,850** | **2,055** | **2,061** | **25,015** |

All amounts are in ISK million

## 36. Loans and advances by industry sectors

The tables below show credit exposure, allowances and impairment by industry and customer segment.

| | | | | Individually impaired | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | Of which performing | | Of which non-performing* | | |
| As at 30 September 2015 | Gross carrying amount | Gross not individually impaired | Collective allowance | Gross carrying amount | Individual allowance | Gross carrying amount | Individual allowance | Carrying amount |
| Financial institutions | 46,511 | 46,511 | - | - | - | - | - | 46,511 |
| Public entities | 13,425 | 12,970 | (18) | 423 | (203) | 31 | (17) | 13,186 |
| Individuals | 296,012 | 271,649 | (2,377) | 6,147 | (3,137) | 18,216 | (9,957) | 280,541 |
| **Corporates** | **533,205** | **501,399** | **(4,398)** | **17,544** | **(7,051)** | **14,264** | **(8,452)** | **513,306** |
| Fisheries | 170,727 | 165,776 | (232) | 2,086 | (1,214) | 2,866 | (1,513) | 167,769 |
| Construction and real estate companies | 142,164 | 130,313 | (1,298) | 7,226 | (2,739) | 4,626 | (2,754) | 135,374 |
| Holding companies | 56,397 | 55,390 | (523) | 117 | (52) | 890 | (657) | 55,165 |
| Retail | 39,305 | 36,545 | (489) | 1,117 | (748) | 1,643 | (1,002) | 37,066 |
| Services | 64,471 | 61,386 | (1,187) | 738 | (487) | 2,347 | (1,479) | 61,318 |
| Information, technology and communication | 20,958 | 20,685 | (376) | 13 | (3) | 260 | (152) | 20,427 |
| Manufacturing | 29,898 | 22,388 | (235) | 5,965 | (1,667) | 1,544 | (824) | 27,171 |
| Agriculture | 9,281 | 8,912 | (58) | 282 | (141) | 88 | (71) | 9,012 |
| Other | 4 | 4 | - | - | - | - | - | 4 |
| **Total** | **889,153** | **832,529** | **(6,793)** | **24,114** | **(10,391)** | **32,511** | **(18,426)** | **853,544** |

| | | | | Individually impaired | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | Of which performing | | Of which non-performing* | | |
| As at 31 December 2014 | Gross carrying amount | Gross not individually impaired | Collective allowance | Gross carrying amount | Individual allowance | Gross carrying amount | Individual allowance | Carrying amount |
| Financial institutions | 49,789 | 49,789 | - | - | - | - | - | 49,789 |
| Public entities | 13,831 | 13,717 | (25) | 59 | (57) | 56 | (42) | 13,708 |
| Individuals | 254,955 | 228,952 | (2,240) | 7,118 | (3,776) | 18,884 | (10,007) | 238,931 |
| **Corporates** | **491,015** | **439,910** | **(5,451)** | **37,612** | **(12,196)** | **13,494** | **(7,653)** | **465,716** |
| Fisheries | 162,507 | 150,959 | (637) | 8,881 | (4,497) | 2,667 | (1,350) | 156,023 |
| Construction and real estate companies | 119,926 | 109,273 | (1,552) | 6,119 | (2,850) | 4,534 | (2,644) | 112,880 |
| Holding companies | 45,451 | 31,249 | (603) | 13,443 | (1,451) | 758 | (535) | 42,861 |
| Retail | 42,198 | 37,788 | (491) | 2,752 | (1,621) | 1,657 | (968) | 39,117 |
| Services | 59,228 | 56,166 | (1,137) | 929 | (579) | 2,133 | (1,125) | 56,387 |
| Information, technology and communication | 20,454 | 20,219 | (486) | 86 | (61) | 149 | (109) | 19,798 |
| Manufacturing | 30,837 | 24,324 | (433) | 5,276 | (1,015) | 1,238 | (629) | 28,761 |
| Agriculture | 9,269 | 8,786 | (104) | 126 | (122) | 358 | (293) | 8,751 |
| Other | 1,145 | 1,146 | (8) | - | - | - | - | 1,138 |
| **Total** | **809,590** | **732,368** | **(7,716)** | **44,789** | **(16,029)** | **32,434** | **(17,702)** | **768,144** |

*Non-performing past due more than 90 days

All amounts are in ISK million

### 37. Allowance for impairment on loans and advances to financial institutions and customers and other financial assets

| | 1.1.-30.9.2015 | | | 1.1.-30.9.2014 | | |
|---|---|---|---|---|---|---|
| | Individual allowance | Collective allowance | Total | Individual allowance | Collective allowance | Total |
| Balance at the beginning of the period | (33,731) | (7,716) | (41,447) | (41,278) | (9,666) | (50,944) |
| New provisions | (5,727) | - | (5,727) | (18,013) | - | (18,013) |
| New provisions due to merger | (2,862) | (490) | (3,352) | - | - | 0 |
| Reversals | 8,198 | 1,413 | 9,611 | 17,810 | 1,208 | 19,018 |
| Provisions used to cover write-offs | 5,305 | - | 5,305 | 4,948 | - | 4,948 |
| Translation difference | - | - | 0 | 33 | 77 | 110 |
| **Balance at the end of the period** | **(28,817)** | **(6,793)** | **(35,610)** | **(36,500)** | **(8,381)** | **(44,881)** |

| | 1.1.-30.9.2015 | | | 1.1.-30.9.2014 | | |
|---|---|---|---|---|---|---|
| | Customers | Financials | Total | Customers | Financials | Total |
| New provisions | (5,727) | - | (5,727) | (18,013) | - | (18,013) |
| Write-offs | (5,515) | - | (5,515) | (8,305) | - | (8,305) |
| Provisions used to cover write-offs | 5,305 | - | 5,305 | 4,948 | - | 4,948 |
| Reversals | 9,611 | - | 9,611 | 19,019 | - | 19,019 |
| Recoveries | 2,000 | - | 2,000 | 2,725 | - | 2,725 |
| Translation difference | - | - | 0 | 110 | - | 110 |
| **Net impairment loss for the period** | **5,674** | **0** | **5,674** | **484** | **0** | **484** |

### 38. Large exposures

As at 30 September 2015, three Group customers were rated as large exposures in accordance with FME's Rules on Large Exposures Incurred by Financial Undertakings, No. 625/2013. Customers are rated as large exposures if their total obligations, or those of financially or administratively connected parties, exceed 10% of the Group's capital base. No large exposure may attain the equivalent of 25% of the capital base. The following table shows the Bank's large expsoures after credit mitigation.

| **As at 30 September 2015** | Number of large exposures | Large exposures after credit mitigation |
|---|---|---|
| Large exposures between 10% and 20% of the Group's capital base | 1 | 31,831 |
| Large exposures between 0% and 10% of the Group's capital base | 2 | 214 |
| **Total** | **3** | **32,045** |
| | | |
| Total large exposure to capital base (400% is the maximum limit) | | 13% |
| | | |
| **As at 31 December 2014** | | |
| Large exposures between 10% and 20% of the Group's capital base | 3 | 102,217 |
| Large exposures between 0% and 10% of the Group's capital base | 3 | - |
| **Total** | **6** | **102,217** |
| | | |
| Total large exposure to capital base (400% is the maximum limit) | | 41% |

## Liquidity risk

### 39. Liquidity risk management

The Group complies with the liquidity and funding rules set by the Central Bank of Iceland, No. 1031/2014 and 1032/2014, as well as the guidelines of the Icelandic Financial Supervisory Authority (FME) No. 2/2010 on best practices for managing liquidity in banking organisations. Rules No. 1031/2014 require the Group to maintain a LCR minimum of 80% total and 100% for foreign currencies in the year 2015 and rules No. 1032/2014 set requirements for a minimum of an 80% NSFR in foreign currencies for the year 2015. The Group submits monthly reports on its liquidity position to the Central Bank of Iceland and the FME.

| | Liquidity coverage ratio total | Liquidity coverage ratio FX | Net stable funding ratio FX |
|---|---|---|---|
| As at 30 September 2015 | 109% | 190% | 120% |
| As at 31 December 2014 | 131% | 614% | 134% |

for the nine months ended 30 September 2015 38 All amounts are in ISK million

### 40. Encumbered assets

| As at 30 September 2015 | Collateral pledged against: Covered bonds | Issued bonds to LBI hf. | Other* | Un-encumbered | Total |
|---|---|---|---|---|---|
| Cash and balances with Central Bank | 196 | - | - | 26,924 | 27,120 |
| Bonds and debt instruments | - | - | 14,801 | 220,987 | 235,788 |
| Equities and equity instruments | - | - | - | 26,467 | 26,467 |
| Derivative instruments | - | - | - | 247 | 247 |
| Loans and advances to financial institutions | - | - | 1,167 | 45,344 | 46,511 |
| Loans and advances to customers | 16,946 | 232,919 | - | 557,168 | 807,033 |
| Investments in equity-accounted associates | - | - | - | 886 | 886 |
| Property and equipment | - | - | - | 5,688 | 5,688 |
| Intangible assets | - | - | - | 2,089 | 2,089 |
| Deferred tax assets | | - | - | 199 | 199 |
| Other assets | - | - | - | 10,961 | 10,961 |
| Assets classified as held for sale | - | - | - | 12,815 | 12,815 |
| **Total** | **17,142** | **232,919** | **15,968** | **909,775** | **1,175,804** |

| As at 31 December 2014 | Collateral pledged against: Covered bonds | Issued bonds to LBI hf. | Other* | Un-encumbered | Total |
|---|---|---|---|---|---|
| Cash and balances with Central Bank | 1 | - | - | 10,159 | 10,160 |
| Bonds and debt instruments | - | - | 12,771 | 230,818 | 243,589 |
| Equities and equity instruments | - | - | - | 29,433 | 29,433 |
| Derivative instruments | - | - | - | 78 | 78 |
| Loans and advances to financial institutions | - | - | 4,953 | 44,836 | 49,789 |
| Loans and advances to customers | 9,537 | 234,283 | - | 474,535 | 718,355 |
| Investments in equity-accounted associates | - | - | - | 777 | 777 |
| Property and equipment | - | - | - | 5,691 | 5,691 |
| Intangible assets | - | - | - | 1,225 | 1,225 |
| Deferred tax assets | | - | - | 83 | 83 |
| Other assets | - | - | - | 20,978 | 20,978 |
| Assets classified as held for sale | - | - | - | 18,211 | 18,211 |
| **Total** | **9,538** | **234,283** | **17,724** | **836,824** | **1,098,369** |

*Other represents assets pledged as collateral to the Central Bank of Iceland to secure settlement in the Icelandic clearing systems, assets pledged as collateral to secure trading lines and credit support for ISDA master agreements and other pledges of similar nature.

## Market risk

### 41. Market risk management

The following table summarises the Group's exposure to market risk as at 30 September 2015 and 31 December 2014:

| Market risk factor | 30.9.2015 % of RWA | 31.12.2014 % of RWA |
|---|---|---|
| Equity price risk* | 1.1% | 4.7% |
| Interest rate risk* | 0.2% | 2.6% |
| Foreign exchange risk | 2.7% | 2.5% |
| **Total** | **4.0%** | **9.9%** |

*The Group has revised its classification of equities and bond and debt instrument exposures in the trading book as of 1 January 2015. Accordingly, risk-weighted assets in equities in the banking book and bond and debt instruments in the banking book are classified as credit risk rather than market risk. Furthermore, risk weights for equity price risk have been updated according to regulations.

The currency risk in the Group's trading portfolios is disclosed together with that in its non-trading portfolios in Notes 45-46, together with the related sensitivity analysis.

All amounts are in ISK million

## 42. Equity price risk

Equity price risk is the risk of equity value fluctuations due to open positions in equity-based instruments.

The Group's main equity portfolios consist of a trading portfolio and a proprietary portfolio. The former is strictly focused on listed equites in ISK for market-making purposes and the latter contains both listed and unlisted equities as part of asset and liability management. Furthermore, the Bank has a hedge portfolio for derivative sales, containing listed equities in ISK. Further details are disclosed in Note 46, Concentration of currency risk.

## 43. Interest rate risk

The following tables summarise the Group's exposure to interest rate risk. The tables include interest-bearing financial assets and liabilities at their carrying amounts, while off-balance sheet amounts are the notional amounts of the derivative instruments (see Note 15). The amounts presented are categorised by the earlier of either the contractual repricing or the maturity date.

| As at 30 September 2015 | Up to 3 months | 3-12 months | 1-5 years | Over 5 years | Carrying amount |
|---|---|---|---|---|---|
| **Financial assets** | | | | | |
| Cash and balances with Central Bank | 27,120 | - | - | - | 27,120 |
| Bonds and debt instruments | 219,485 | 4,125 | 3,538 | 8,640 | 235,788 |
| Derivative instruments | 247 | - | - | - | 247 |
| Loans and advances to financial institutions | 45,557 | 954 | - | - | 46,511 |
| Loans and advances to customers | 562,263 | 111,843 | 81,023 | 51,904 | 807,033 |
| Other financial assets | 9,575 | - | 558 | - | 10,133 |
| **Total** | **864,247** | **116,922** | **85,119** | **60,544** | **1,126,832** |
| | | | | | |
| **Financial liabilities** | | | | | |
| Due to financial institutions and Central Bank | (49,550) | - | - | - | (49,550) |
| Deposits from customers | (615,112) | (7,413) | (2,067) | (332) | (624,924) |
| Derivative instruments and short positions | (500) | (13) | (584) | (3,039) | (4,136) |
| Borrowings | (194,377) | (3,423) | (4,010) | (5,889) | (207,699) |
| Subordinated liabilities | (775) | - | - | - | (775) |
| Other financial liabilities | (15,683) | - | - | - | (15,683) |
| **Total** | **(875,997)** | **(10,849)** | **(6,661)** | **(9,260)** | **(902,767)** |
| | | | | | |
| Net on-balance sheet position | (11,750) | 106,073 | 78,458 | 51,284 | 224,065 |
| Net off-balance sheet position | 120 | 65 | (184) | - | |
| | | | | | |
| **Total interest repricing gap** | **(11,630)** | **106,138** | **78,274** | **51,284** | |

| As at 31 December 2014 | Up to 3 months | 3-12 months | 1-5 years | Over 5 years | Carrying amount |
|---|---|---|---|---|---|
| **Financial assets** | | | | | |
| Cash and balances with Central Bank | 10,160 | - | - | - | 10,160 |
| Bonds and debt instruments | 223,686 | 4,103 | 2,000 | 13,800 | 243,589 |
| Derivative instruments | 78 | - | - | - | 78 |
| Loans and advances to financial institutions | 43,154 | 6,635 | - | - | 49,789 |
| Loans and advances to customers | 512,873 | 96,206 | 68,537 | 40,739 | 718,355 |
| Other financial assets | 19,178 | - | 555 | - | 19,733 |
| **Total** | **809,129** | **106,944** | **71,092** | **54,539** | **1,041,704** |
| | | | | | |
| **Financial liabilities** | | | | | |
| Due to financial institutions and Central Bank | (53,827) | - | - | - | (53,827) |
| Deposits from customers | (529,221) | (20,703) | (1,511) | - | (551,435) |
| Derivative instruments and short positions | (332) | (3,221) | (178) | (1,678) | (5,409) |
| Borrowings | (199,558) | - | (7,470) | - | (207,028) |
| Other financial liabilities | (7,509) | - | - | - | (7,509) |
| **Total** | **(790,447)** | **(23,924)** | **(9,159)** | **(1,678)** | **(825,208)** |
| | | | | | |
| Net on-balance sheet position | 18,682 | 83,020 | 61,933 | 52,861 | 216,495 |
| Net off-balance sheet position | 430 | (140) | (290) | - | |
| | | | | | |
| **Total interest repricing gap** | **19,112** | **82,880** | **61,643** | **52,861** | |

All amounts are in ISK million

## 44. CPI indexation risk (all portfolios)

The consumer price index (CPI) indexation risk is the risk that the fair value or future cash flows of CPI-linked financial instruments may fluctuate due to changes in the Icelandic CPI. The Group has a considerable imbalance in its CPI-linked assets and liabilities. To mitigate this imbalance the Bank offers non-CPI-linked loans and CPI-linked deposits as well as CPI-linked interest rate swaps.

CPI indexation risk is managed centrally within the Group by Treasury, and is monitored by Market Risk. The following table summarises the Group's CPI imbalance, calculated as the difference between CPI-linked financial assets and liabilities, as at 30 September 2015 and 31 December 2014.

| Carrying amount | 30.9.2015 | 31.12.2014 |
|---|---|---|
| **Assets** | | |
| Bonds and debt instruments | 9,431 | 16,680 |
| Loans and advances to customers | 267,512 | 239,605 |
| **Total** | **276,943** | **256,285** |
| | | |
| **Liabilities** | | |
| Short positions | (773) | (756) |
| Deposits from customers | (103,801) | (97,378) |
| Borrowings | (5,889) | - |
| Subordinated liabilities | (387) | - |
| **Total** | **(110,850)** | **(98,134)** |
| | | |
| Total on-balance sheet position | 166,093 | 158,152 |
| Total off-balance sheet position | (196) | (572) |
| | | |
| **Total CPI indexation balance** | **165,897** | **157,580** |

## 45. Currency risk (all portfolios)

The Group follows Rules No. 950/2010, on Foreign Exchange Balances, as set by the Central Bank of Iceland. The Rules stipulate that an institution's foreign exchange balance (whether long or short) must always be within 15% of its capital base, in each currency and for all currencies combined. The Bank submits daily and monthly reports to the Central Bank with information on its foreign exchange balance.

The Group's combined net foreign exchange balance as at 30 September 2015 was +9.1% of the Group's capital base (31.12.2014: +8.14%).

## 46. Concentration of currency risk

The following tables summarise the Group's exposure to currency risk as at 30 September 2015 and 31 December 2014. The off-balance sheet amounts shown are the notional amounts of the Group's derivative instruments.

Amounts presented under assets and liabilities include all spot deals as at 30 September 2015 and 31 December 2014. When managing liquidity risk the Group regards spot deals as non-derivative assets or liabilities.

| As at 30 September 2015 | EUR | GBP | USD | JPY | CHF | Other | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and balances with Central Bank | 767 | 190 | 342 | 37 | 60 | 300 | 1,696 |
| Bonds and debt instruments | 10,044 | 42,347 | 32,769 | - | - | - | 85,160 |
| Equities and equity instruments | 135 | - | 2 | - | - | 33 | 170 |
| Derivative instruments | 94 | 1 | 104 | - | - | - | 199 |
| Loans and advances to financial institutions | 22,861 | 3,080 | 5,931 | 329 | 16 | 8,562 | 40,779 |
| Loans and advances to customers | 106,494 | 13,282 | 77,200 | 5,610 | 6,859 | 9,650 | 219,095 |
| Other assets | 660 | - | 64 | 1 | - | 38 | 763 |
| **Total** | **141,055** | **58,900** | **116,412** | **5,977** | **6,935** | **18,583** | **347,862** |
| | | | | | | | |
| **Liabilities** | | | | | | | |
| Due to financial institutions and Central Bank | (189) | (94) | (187) | - | - | (492) | (962) |
| Deposits from customers | (59,521) | (27,170) | (34,658) | (1,055) | (1,634) | (5,984) | (130,022) |
| Derivative instruments and short positions | (85) | (49) | (192) | - | - | (23) | (349) |
| Borrowings | (88,174) | (29,941) | (74,988) | - | - | - | (193,103) |
| Subordinated liabilities | (29) | - | - | (166) | (137) | - | (332) |
| Other liabilities | (1,025) | (210) | (4,127) | - | (4) | (230) | (5,596) |
| **Total** | **(149,023)** | **(57,464)** | **(114,152)** | **(1,221)** | **(1,775)** | **(6,729)** | **(330,364)** |
| | | | | | | | |
| Net on-balance sheet position | (7,968) | 1,436 | 2,260 | 4,756 | 5,160 | 11,854 | **17,498** |
| Net off-balance sheet position | 16,795 | 477 | 4,206 | (4,728) | (4,306) | (7,100) | **5,344** |
| | | | | | | | |
| **Net currency position** | **8,827** | **1,913** | **6,466** | **28** | **854** | **4,754** | **22,842** |

All amounts are in ISK million

### 46. Concentration of currency risk (continued)

| As at 31 December 2014 | EUR | GBP | USD | JPY | CHF | Other | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and balances with Central Bank | 513 | 240 | 261 | 10 | 43 | 277 | 1,344 |
| Bonds and debt instruments | 12,970 | 30,485 | 44,519 | - | - | - | 87,974 |
| Equities and equity instruments | 146 | - | 2 | - | - | 73 | 221 |
| Derivative instruments | 39 | - | - | - | - | - | 39 |
| Loans and advances to financial institutions | 17,270 | 13,448 | 3,255 | 440 | 175 | 5,695 | 40,283 |
| Loans and advances to customers | 97,232 | 14,308 | 64,190 | 4,265 | 7,350 | 12,037 | 199,382 |
| Other assets | 16,645 | - | 14 | 1 | - | 31 | 16,691 |
| **Total** | **144,815** | **58,481** | **112,241** | **4,716** | **7,568** | **18,113** | **345,934** |
| | | | | | | | |
| **Liabilities** | | | | | | | |
| Due to financial institutions and Central Bank | (137) | (155) | (79) | - | (1) | (25) | (397) |
| Deposits from customers | (52,938) | (26,779) | (35,299) | (799) | (1,311) | (6,372) | (123,498) |
| Derivative instruments and short positions | (65) | (1) | (237) | - | - | - | (303) |
| Borrowings | (94,895) | (30,526) | (74,136) | - | - | - | (199,557) |
| Other liabilities | (762) | (245) | (407) | (7) | (7) | (431) | (1,859) |
| **Total** | **(148,797)** | **(57,706)** | **(110,158)** | **(806)** | **(1,319)** | **(6,828)** | **(325,614)** |
| | | | | | | | |
| Net on-balance sheet position | (3,982) | 775 | 2,083 | 3,910 | 6,249 | 11,285 | **20,320** |
| Net off-balance sheet position | 21,259 | (198) | (1,297) | (3,676) | (6,668) | (9,420) | **0** |
| | | | | | | | |
| **Net currency position** | **17,277** | **577** | **786** | **234** | **(419)** | **1,865** | **20,320** |

### 47. Foreign exchange rates used

The following foreign exchange rates were used by the Group:

| | As at 30 September 2015 | As at 31 December 2014 | % Change | Average for 1.1-30.9 2015 | Average for 1.1-30.9 2014 |
|---|---|---|---|---|---|
| EUR/ISK | 142.65 | 154.25 | (7.5%) | 147.83 | 154.94 |
| GBP/ISK | 193.16 | 198.09 | (2.5%) | 202.33 | 191.26 |
| USD/ISK | 127.66 | 126.89 | 0.6% | 131.91 | 114.66 |
| JPY/ISK | 1.07 | 1.06 | 0.9% | 1.09 | 1.11 |
| CHF/ISK | 130.87 | 128.29 | 2.0% | 138.22 | 127.35 |
| CAD/ISK | 95.34 | 109.58 | (13.0%) | 104.72 | 104.86 |
| DKK/ISK | 19.12 | 20.72 | (7.7%) | 19.82 | 20.77 |
| NOK/ISK | 14.96 | 17.10 | (12.5%) | 16.72 | 18.70 |
| SEK/ISK | 15.22 | 16.41 | (7.3%) | 15.78 | 17.18 |

All amounts are in ISK million

## 48. Operations by quarters (unaudited)

| Operations | 2015 Q3* | 2015 Q2 | 2015 Q1 | 2014 Q4* | 2014 Q3 | 2014 Q2 | 2014 Q1 |
|---|---|---|---|---|---|---|---|
| Interest income | 16,000 | 15,938 | 12,738 | 11,325 | 13,745 | 14,215 | 14,450 |
| Interest expense | (7,166) | (7,009) | (5,469) | (5,549) | (6,688) | (6,830) | (6,595) |
| **Net interest income** | **8,834** | **8,929** | **7,269** | **5,776** | **7,057** | **7,385** | **7,855** |
| Net adjustments to loans and advances acquired at deep discount | - | - | - | 6,467 | 2,531 | 4,301 | 6,711 |
| Gain (loss) from foreign currency linkage of loans and advances to customers | 9,145 | 134 | (2,015) | 2,156 | - | - | - |
| Net impairment | 1,344 | 115 | 3,611 | (2,522) | 50 | 2,975 | (2,541) |
| **Net adjustments in valuation** | **10,489** | **249** | **1,596** | **6,101** | **2,581** | **7,276** | **4,170** |
| **Net interest income after net adjustments in valuation** | **19,323** | **9,178** | **8,865** | **11,877** | **9,638** | **14,661** | **12,025** |
| Fee and commission income | 2,322 | 2,274 | 2,049 | 2,128 | 1,714 | 1,772 | 2,123 |
| Fee and commission expense | (577) | (521) | (408) | (488) | (439) | (369) | (605) |
| **Net fee and commission income** | **1,745** | **1,753** | **1,641** | **1,640** | **1,275** | **1,403** | **1,518** |
| Net gain on financial assets designated as at fair value through profit or loss | 852 | 1,838 | 3,812 | 2,891 | 1,267 | 1,929 | (787) |
| Net gain on financial assets and liabilities held for trading | 1,173 | 1,273 | 451 | 723 | 571 | 51 | 118 |
| Net foreign exchange gain (loss) | (748) | (147) | (324) | 107 | 154 | (171) | (23) |
| Other income and (expenses) | (188) | 189 | 238 | 1,193 | (1,104) | 2,401 | (208) |
| **Other net operating income** | **1,089** | **3,153** | **4,177** | **4,914** | **888** | **4,210** | **(900)** |
| **Total operating income** | **22,157** | **14,084** | **14,683** | **18,431** | **11,801** | **20,274** | **12,643** |
| Salaries and related expenses | 3,466 | 3,179 | 3,702 | 3,805 | 3,019 | 3,288 | 3,455 |
| Other operating expenses | 1,757 | 2,011 | 2,070 | 2,635 | 1,740 | 1,965 | 2,205 |
| Depreciation and amortisation | 167 | 165 | 164 | 419 | 171 | 175 | 177 |
| Contribution to the Depositors' and Investors' Guarantee Fund | 203 | 421 | 346 | 259 | 253 | 255 | 267 |
| **Total operating expenses** | **5,593** | **5,776** | **6,282** | **7,118** | **5,183** | **5,683** | **6,104** |
| Share of profit of equity-accounted associates | 145 | 103 | 9 | 125 | - | 329 | 11 |
| **Profit before tax** | **16,709** | **8,411** | **8,410** | **11,438** | **6,618** | **14,920** | **6,550** |
| Income tax | (3,953) | (1,546) | (1,178) | (1,298) | (566) | (3,530) | (1,427) |
| Tax on liabilities of financial institutions | (748) | (872) | (820) | (388) | (945) | (800) | (835) |
| **Profit for the period** | **12,008** | **5,993** | **6,412** | **9,752** | **5,107** | **10,590** | **4,288** |

| Balance sheet | 30.9.2015 | 30.6.2015 | 31.3.2015 | 31.12.2014 | 30.9.2014 | 30.6.2014 | 31.3.2014 |
|---|---|---|---|---|---|---|---|
| Cash and cash balances with Central Bank | 27,120 | 38,719 | 14,347 | 10,160 | 38,820 | 7,964 | 34,024 |
| Bonds and debt instruments | 235,788 | 248,604 | 250,005 | 243,589 | 293,796 | 297,141 | 284,418 |
| Equities and equity instruments | 26,467 | 25,498 | 33,354 | 29,433 | 40,991 | 42,221 | 36,414 |
| Loans and advances to financial institutions | 46,511 | 68,707 | 86,951 | 49,789 | 68,192 | 67,163 | 63,896 |
| Loans and advances to customers | 807,033 | 761,290 | 735,479 | 718,355 | 719,627 | 699,648 | 681,883 |
| Other assets | 20,070 | 17,104 | 34,638 | 28,832 | 20,222 | 18,342 | 28,615 |
| Assets classified as held for sale | 12,815 | 12,747 | 17,606 | 18,212 | 19,599 | 22,119 | 24,554 |
| **Total assets** | **1,175,804** | **1,172,669** | **1,172,380** | **1,098,370** | **1,201,247** | **1,154,598** | **1,153,804** |
| Due to financial institutions and Central Bank | 49,550 | 62,428 | 57,019 | 53,827 | 179,085 | 166,172 | 174,031 |
| Deposits from customers | 624,924 | 621,023 | 624,063 | 551,435 | 497,583 | 473,356 | 468,661 |
| Borrowings | 207,699 | 212,792 | 210,902 | 207,028 | 233,785 | 231,378 | 234,844 |
| Subordinated liabilities | 775 | 414 | 427 | - | - | - | - |
| Other liabilities | 38,854 | 34,710 | 43,140 | 32,443 | 46,593 | 43,972 | 46,681 |
| Liabilities associated with assets classified as held for sale | 1,518 | 1,450 | 2,969 | 2,834 | 3,214 | 3,826 | 4,195 |
| Equity | 252,484 | 239,852 | 233,860 | 250,803 | 240,987 | 235,894 | 225,392 |
| **Total liabilities and equity** | **1,175,804** | **1,172,669** | **1,172,380** | **1,098,370** | **1,201,247** | **1,154,598** | **1,153,804** |

*The results for the first three quarters of the years 2015 and 2014 were reviewed by the Bank's independent auditors.

All amounts are in ISK million