Condensed Consolidated

Interim Financial Statements

Six months ended 30 June 2011

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

Contents

Endorsement and Statement by the Board of Directors and the CEO

The Condensed Consolidated Interim Financial Statements of Íslandsbanki hf. for the period 1 January to 30 June 2011 comprise the Condensed Interim Financial Statements of Íslandsbanki hf. and its subsidiaries, together referred to as "the Bank".

Accounting convention

The Condensed Consolidated Interim Financial Statements for the period 1 January to 30 June 2011 have been prepared on a going concern basis in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). The Financial Statements are presented in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting as adopted by the EU.

The profit from the Bank's operations for the period 1 January to 30 June 2011 amounted to ISK 8,062 million, which corresponds to a 12.9% return on equity. Bank equity, according to the Consolidated Financial Position, amounted to ISK 128,780 million at 30 June 2011. The Bank's total capital ratio, calculated according to the Act on Financial Undertakings, was 28.0% and the Tier 1 ratio was 23.7%. Under Icelandic law the minimum capital requirement is 8.0%. However, as part of granting the Bank an operating licence as a financial undertaking, the Icelandic Financial Supervisory Authority (FME) requires the Bank to maintain a minimum Core Tier 1 ratio of 12% of risk weighted assets and a solvency ratio, allowing for subordinated Tier 2 debt, of 16%.The Bank's total assets amounted to ISK 682,575 million at the end of the period.

The Board of Directors and the CEO would like to draw attention to uncertainties relating to foreign currency loans. Uncertainties in relation to loan assets are discussed in detail under notes 2 and 36.

To the best of our knowledge, the Condensed Consolidated Interim Financial Statements provide a true and fair view of the Bank's operating profits and its financial position as at 30 June 2011.

The Board of Directors and the CEO of Íslandsbanki hf. hereby confirm the Bank's Condensed Consolidated Interim Financial Statements for the period 1 January to 30 June 2011 by means of their signatures.

Reykjavík, 9 September 2011

Board of Directors:

Chief Executive Officer:

Condensed Consolidated Statement of Comprehensive Income for the six months ended 30 June 2011

	Notes	2011* 1.4-30.6	2010* 1.4-30.6	2011 1.1-30.6	2010 1.1-30.6
Interest income		15,158	16,207	27,555	34,122
Interest expense		(6,916)	(7,918)	(11,252)	(16,684)
Net interest income	6	8,242	8,289	16,303	17,438
Net valuation changes on loans and receivables	7	409	702	(255)	(474)
Provision for latent impairment losses	7,22	16	(49)	(155)	(610)
Net interest income after valuation changes on loans and receivables		8,667	8,942	15,893	16,354
Fee and commission income		1,805	3,108	4,402	5,147
Fee and commission expense		(507)	(1,400)	(1,389)	(1,815)
Net fee and commission income		1,298	1,708	3,013	3,332
Net financial expenses	8-9	(330)	(49)	(468)	(434)
Net foreign exchange gain	10	134	180	336	53
Other net operating income	11	297	392	656	479
Operating income		10,066	11,173	19,430	19,784
Administrative expenses	12-13	(4,636)	(4,941)	(9,806)	(9,295)
Share of profit of associates		0	50	0	50
Profit before tax		5,430	6,282	9,624	10,539
Income tax	14	(1,202)	(1,540)	(2,067)	(2,347)
Bank tax		(289)	0	(344)	0
Profit for the period from continuing operations		3,939	4,742	7,213	8,192
Profit (loss) from discontinued operations, net of income tax		537	(35)	849	98
Profit for the period		4,476	4,707	8,062	8,290
Other comprehensive income					
Foreign currency translation differences for foreign operations		39	(5)	40	(7)
Other comprehensive income for the period		39	(5)	40	(7)
Total comprehensive income for the period		4,515	4,702	8,102	8,283
Attributable to:					
Equity holders of Íslandsbanki hf.		4,485	4,697	8,077	8,286
Non-controlling interests		(9)	10	(15)	4
Profit for the period		4,476	4,707	8,062	8,290
Basic earnings per share	15	0.45	0.47	0.81	0.83
Diluted earnings per share	15	0.45	0.47	0.81	0.83

* unaudited information

The notes on pages 8 to 40 are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK million

Condensed Consolidated Statement of Financial Position as at 30 June 2011

	Notes	30.6.2011	31.12.2010
Assets			
Cash and balances with Central Bank	5,16	27,761	30,799
Derivatives	5,17	136	70
Bonds and debt instruments	5	50,456	68,024
Shares and equity instruments	5	3,240	3,022
Loans to credit institutions	5,18-19	41,627	30,870
Loans to customers	5,20-21	509,914	515,161
Investments in associates	23	744	354
Property and equipment		4,543	5,419
Intangible assets		261	187
Deferred tax assets		201	283
Non-current assets and disposal groups held for sale	26	23,990	23,489
Other assets	27	19,702	5,544
Total Assets		682,575	683,222
Liabilities			
Financial liabilities	5	10,582	9,090
Derivatives	5,17	1,738	429
Deposits from Central Bank	5,28	12	26
Deposits from credit institutions	5,28	93,837	96,212
Deposits from customers	5,29,30	320,961	327,158
Debt issued and other borrowed funds	5,31	55,529	55,425
Subordinated loans	5	22,887	21,241
Current tax liabilities		9,248	9,024
Deferred tax liabilities		510	18
Non-current liabilities and disposal groups held for sale	26	6,251	16,442
Other liabilities	32	32,240	26,694
Total Liabilities		553,795	561,759
Equity			
Share capital	33	10,000	10,000
Share premium	33	55,000	55,000
Other reserves		2,538	2,498
Retained earnings		61,251	53,174
Total equity attributable to the equity holders of Íslandsbanki hf.		128,789	120,672
Non-controlling interests		(9)	791
Total Equity		128,780	121,463
Total Liabilities and Equity		682,575	683,222

The notes on pages 8 to 40 are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK million

Condensed Consolidated Statement of Changes in Equity for the six months ended 30 June 2011

	Attributable to equity holders of Íslandsbanki hf.					Non-controlling interests	Total equity
	Share capital	Share premium	Other reserves	Retained earnings	Total		
Equity at 1.1.2010	10,000	55,000	2,059	24,204	91,263	840	92,103
Translation differences for foreign operations			(7)		(7)		(7)
Contribution to statutory reserve			179	(179)	0		0
Net income recognised directly in equity	0	0	172	(179)	(7)	0	(7)
Profit for the period				8,286	8,286	4	8,290
Total comprehensive income for the period	0	0	172	8,107	8,279	4	8,283
Equity at 30.6.2010	10,000	55,000	2,231	32,312	99,543	844	100,387
Equity at 1.1.2011	10,000	55,000	2,498	53,174	120,672	791	121,463
Translation differences for foreign operations			40		40		40
Net income recognised directly in equity	0	0	40	0	40	0	40
Profit for the period				8,077	8,077	(15)	8,062
Total comprehensive income for the period	0	0	40	8,077	8,117	(15)	8,102
Change in minority interest					0	(785)	(785)
Equity at 30.6.2011	10,000	55,000	2,538	61,251	128,789	(9)	128,780

The notes on pages 8 to 40 are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK million

Condensed Consolidated Statement of Cash Flows for the six months ended 30 June 2011

	Notes	2011 1.1-30.6	2010 1.1-30.6
Net cash provided by (used in) operating activities		9,955	(13,828)
Net cash (used in) provided by investing activities		(388)	82
Net cash (used in) provided by financing activities		(3,519)	0
Net increase (decrease) in cash and cash equivalents		6,048	(13,746)
Effects of exchange rate changes on cash and cash equivalents		34	(76)
Cash and cash equivalents at the beginning of the year		37,152	53,317
Cash and cash equivalents at the end of the period		43,234	39,495
Reconciliation of cash and cash equivalents:			
Cash on hand	16	2,256	2,072
Cash balances with Central Bank	16	20,074	17,663
Bank accounts	18	20,904	19,760
Total cash and cash equivalents		43,234	39,495

The notes on pages 8 to 40 are an integral part of these Condensed Consolidated Interim Financial Statements

For the six months ended 30 June 2011 7 Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

Notes to the Condensed Consolidated Financial Statements

Accounting policies

General information

1. The reporting entity

Íslandsbanki hf. is a limited company incorporated and domiciled in Iceland. The Condensed Consolidated Interim Financial Statements for the six months ended 30 June 2011 comprise Íslandsbanki hf. (the parent) and its subsidiaries (together referred to as "the Bank").

The Condensed Consolidated Interim Financial Statements were authorised for issue by the Board of Directors of Íslandsbanki hf. on 9 September 2011.

The Bank has changed its presentation of impairment and income from revised estimated future cash flow in the Condensed Consolidated Statement of Comprehensive Income and is now presenting individually and collectively assessed impairment and income from revised estimated future cash flow as a net figure under the line net valuation changes. Impairment, which is incurred but not yet indentified, is shown separately as latent impairment.

The Bank made a reclass transaction between interest income and income from revised estimated future cash flow at year end which affects the comparable information for 30 June 2010 whereas interest has been reduced by ISK 2.8bn and revised estimated future cash flow has been increased accordingly. This transaction had no effect on the net profit. Comparable information under notes 6 and 7 are affected by this change, as well as comparable information in the Condensed Consolidated Statement of Comprehensive Income.

The Bank has changed its presentation of profit for discontinued operations in the Condensed Consolidated Statement of Comprehensive Income and is now presenting it net of income tax. The comparable figures have been adjusted accordingly.

At 31 December 2010, bonds designated at fair value through profit and loss totalling 31.823m were categorised as being unlisted. The bonds were in fact listed in May 2010, although no transactions occurred with these bonds until April 2011.

Comparable information for Members of the Board and Associated companies and other related parties under Related party disclosures in note 25 has been changed, whereas balances with an associate of ISK 351m were wrongly presented for Members of the Board instead of for Associated companies.

Comparative information under note 34 for credit card commitments has been changed from ISK 25.4bn to ISK 17.9bn as part of the commitments were duplicated in the Consolidated Financial Statement 2010.

2. Basis of preparation

Statement of compliance

The Condensed Consolidated Interim Financial Statements for the six months ended 30 June 2011 have been prepared on a going concern basis in accordance with the International Financial Reporting Standards (IFRS), as adopted by the European Union. The Financial Statements are presented in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting as adopted by the EU.

The Condensed Consolidated Interim Financial Statements do not include all the information required for annual financial statements and should be read in conjunction with the Consolidated Financial Statements of the Bank and the Risk Book for the year ended 31 December 2010. The Financial Statements and the Risk Book are available at the Bank's website www.islandsbanki.is.

Accounting policies

The same accounting policies, presentation and methods of computation have been followed in these Condensed Consolidated Interim Financial Statements as were applied in the preparation of the Bank's Consolidated Financial Statements for the year ended 31 December 2010.

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

Assumptions and uncertainties in relation to the Bank's loan assets

There were uncertainties in input parameters and assumptions used in valuation of the assets acquired from Glitnir at a deep discount. The Bank's management based their initial value estimates on expected five-year cumulative losses with conservative estimates for collateral values and a prudent risk premium, known facts, their knowledge of the customers and the market and on official macroeconomic forecasts from the Central Bank of Iceland, the IMF and the OECD.

2. Cont'd

Factors that can affect the recovery value of the loan portfolio include macroeconomic parameters such as the unemployment rate, inflation and wage growth, actions taken by the government to facilitate and ease debt service and legislation that lengthens the collection process or increases taxation and the extent of customer participation in flexible maturity and payment equalisation programmes.

At 30 June 2011 many of the uncertainties surrounding the valuation of the financial assets acquired at a deep discount and the economic environment were still present. The Bank's management is, however, confident that the Bank's capital base is robust enough to absorb reasonable variances in applied assumptions.

Critical assumptions used in the initial valuation are discussed in more detail in the Consolidated Financial Statements 2009. Contingencies relating to the acquired loan assets are further discussed under note 36.

Going concern

Supreme Court rulings on interest rates in the second half of 2010 and subsequent related legislative changes have reduced much of the inherent uncertainties surrounding foreign currency-linked loan contracts. The Bank conducted a thorough assessment of all of its corporate loan contract forms after a recent Supreme Court ruling on a corporate foreign exchange loan contract, to ascertain if any of them were affected by this ruling and subsequently recognised a provision for those loans deemed to be at the highest risk. The Bank ascertains that the financial effects of Supreme Court rulings and legislative changes are reflected in the consolidated financial statements. These issues are further discussed under note 36.

The Bank is subject to a currency risk due to a mismatch in contractual currencies of its assets and liabilities. This imbalance has been offset to some extent by the Bank's treatment of loans with non-ISK contractual currency to borrowers with ISK-based income as ISK assets, whereby the Bank impairs any increase in loan balances due to depreciation of the ISK. To address the remaining imbalance, the Bank entered into a foreign exchange swap on 30 December 2010. Currency risk is discussed under note 47.

Most of the Bank's funding is in the form of on-demand deposits. The Bank is confident that this will change over the coming years as investors' risk aversion reduces and they start seeking higher yielding investment opportunities. In the future, the Bank will focus on extending the maturities of its deposit base and, at the same time, issue short term unsecured notes and, to some extent, longer term secured bonds. Access to funding in foreign currencies will be limited in the short to medium term.

As well as working closely with customers experiencing payment difficulties in order to ensure maximum recovery of its assets, the Bank has been strengthening its infrastructure and internal controls. The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future. Therefore, the financial statements continue to be prepared on a going concern basis.

Changes within the Bank

3. Acquisition of subsidiary

Following financial restructuring of Icelandair Group hf., where the Bank had a leading position, Midengi ehf. acquired on 28 February 2011 71.1% shareholding in Bláfugl ehf., an aviation service company and 71.1% shareholding in IG Invest ehf., an aircraft brokerage and leasing company, through its 100% owned holding company, SPW ehf. Both entities qualify as being held for sale in accordance with IFRS 5 and have therefore been classified as non-current assets and disposal groups held for sale.

On 4 February 2011, the Bank acquired 62.9% shareholding in Bifreiðar og landbúnaðarvélar ehf., a car and farm vehicle dealership, and 62.9% shareholding in Ingvar Helgason ehf., a car dealership, through its 100% owned holding company, BLIH ehf. The acquisitions arose from foreclosures which were necessary to secure assets placed as collateral against loan assets. Both entities qualify as being held for sale in accordance with IFRS 5 and have therefore been classified as non-current assets and disposal groups held for sale.

On 12 January 2011, the Bank obtained control of Jarðboranir ehf., a geothermal drilling company, by exercising its option to acquire 100% of its shareholding. The option was part of restructuring of the previous owner, Atorka. The entity qualifies as being held for sale in accordance with IFRS 5 and has been classified as non-current asset and disposal group held for sale.

Acquisition of non-controlling interests

During the accounting period the Bank acquired an additional 45% shareholding in Kreditkort hf. The consideration was in the form of 15.71% shareholding in Borgun hf. The Bank recognised a decrease in non-controlling interest of 230m ISK.

Loss of control over subsidiary

During the accounting period the Bank disposed of 15.71% of its shareholding in Borgun hf. as consideration for 45% shareholding in Kreditkort. As a result of this transaction the Bank lost control over Borgun as the Bank's shareholding in Borgun reduced to 39.29% and the company has subsequently been classified as an associate of the Bank.

The Bank recognised a loss from disposal in the amount of ISK 58 million and included it in the statement of comprehensive income in the line item “Net financial expenses”. Comparative information in the comparative statement of comprehensive income and the comparative consolidated statement of financial position has not been restated.

The transaction did not result in any net cash inflow.

Discontinued operations

On 28 March 2011 the Bank sold its 100% shareholding in Steypustöðin hf. The entity was classified as non-current assets and disposal groups held for sale. The results from the disposal are included under profit from discontinued operations, net of income tax.

On 30 June 2011 the Bank sold 90% of its shareholding in Eik Fasteignafélag ehf. This entity was classified as non-current assets and disposal groups held for sale. The results from the disposal are included under profit from discontinued operations, net of income tax.

Quarterly statements

4. Operations by half year:

	Q2* 2011	Q1* 2011	Q4* 2010	Q3* 2010	Q2* 2010
Net interest income	8,242	8,061	9,128	8,308	8,289
Net valuation changes on loans and receivables	409	(664)	12,267	2,714	702
Provision for latent impairment	16	(171)	(41)	137	(49)
Net fee and commission income	1,298	1,715	2,146	1,902	1,708
Net financial (expenses) income	(330)	(138)	(548)	72	(49)
Net foreign exchange gain (loss)	134	202	1,391	(2,406)	180
Other net operating income	297	359	490	217	392
Administrative expenses	(4,636)	(5,170)	(4,525)	(4,653)	(4,941)
Other income	0	0	0	0	50
Profit before tax	5,430	4,194	20,308	6,291	6,282
Income tax	(1,202)	(865)	(3,323)	(1,544)	(1,540)
Bank tax	(289)	(55)	(221)	0	0
Profit for the period from continuing operations	3,939	3,274	16,764	4,747	4,742
Profit from discontinued operation, net of income tax	537	312	(545)	114	(35)
Profit for the period	4,476	3,586	16,219	4,861	4,707

* The split between quarters is not audited.

Financial assets and liabilities

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

At 30 June 2011	Notes	Held for trading	Designated at fair value through P&L	Loans & receivables	Other amortised cost	Total carrying amount
Cash and balances with Central Bank	16			27,761		27,761
Loans and receivables						
Loans to credit institutions	18-19			41,627		41,627
Loans to customers	20-21			509,914		509,914
Loans and receivables				579,302		579,302
Bonds and debt instruments						
Listed		17,466	30,321			47,787
Unlisted			2,669			2,669
Bonds and debt instruments		17,466	32,990			50,456
Shares and equity instruments						
Listed		673				673
Unlisted			2,567			2,567
Shares and equity instruments		673	2,567			3,240
Derivatives	17	136				136
Total financial assets		18,275	35,557	579,302		633,134
Financial liabilities		10,582				10,582
Derivatives	17	1,738				1,738
Deposits from Central Bank	28				12	12
Deposits from credit institutions	28				93,837	93,837
Deposits from customers	29-30				320,961	320,961
Debt issued and other borrowed funds	31				55,529	55,529
Subordinated loans					22,887	22,887
Total financial liabilities		12,320			493,226	505,546

For the six months ended 30 June 2011 12 Amounts are in ISK million

5. Cont'd

At 31 December 2010	Notes	Held for trading	Designated at fair value through P&L	Loans & receivables	Other amortised cost	Total carrying amount
Cash and balances with Central Bank	16			30,799		30,799
Loans and receivables						
Loans to credit institutions	18-19			30,870		30,870
Loans to customers	20-21			515,161		515,161
Loans and receivables				576,830		576,830
Bonds and debt instruments						
Listed		36,201	30,338			66,539
Unlisted			1,485			1,485
Bonds and debt instruments		36,201	31,823			68,024
Shares and equity instruments						
Listed		411	51			462
Unlisted			2,560			2,560
Shares and equity instruments		411	2,611			3,022
Derivatives	17	70				70
Total financial assets		36,682	34,434	576,830		647,946
Financial liabilities		9,090				9,090
Derivatives	17	429				429
Deposits from Central Bank	28				26	26
Deposits from credit institutions	28				96,212	96,212
Deposits from customers	29-30				327,158	327,158
Debt issued and other borrowed funds	31				55,425	55,425
Subordinated loans					21,241	21,241
Total financial liabilities		9,519			500,062	509,581

Amounts are in ISK million

Net interest income

6. Net interest income is specified as follows:

	2011* 1.4.-30.6	2010* 1.4.-30.6	2011 1.1-30.6	2010 1.1-30.6
Interest income:				
Cash and balances with Central Bank	212	353	494	707
Loans and receivables	14,464	15,007	26,045	31,669
Financial assets held for trading	164	260	322	532
Financial assets designated at fair value through profit or loss	311	578	641	1,197
Other assets	7	10	53	17
Total interest income	15,158	16,207	27,555	34,122
Interest expense:				
Deposits from credit institutions and Central Bank	(648)	(1,243)	(1,097)	(2,618)
Deposits from customers	(3,421)	(4,846)	(5,957)	(9,886)
Borrowings	(2,243)	(1,329)	(3,216)	(3,163)
Subordinated loans	(303)	(254)	(583)	(534)
Financial liabilities held for trading	(110)	(124)	(178)	(251)
Other interest expense	(191)	(121)	(221)	(231)
Total interest expense	(6,916)	(7,918)	(11,252)	(16,684)
Net interest income	8,242	8,289	16,303	17,438

* unaudited information

Net valuation changes on loans and receivables

7. Net valuation changes on loans and receivables:

	2011* 1.4.-30.6	2010* 1.4.-30.6	2011 1.1-30.6	2010 1.1-30.6
Impairment charged to comprehensive income:				
Specific impairment losses on financial assets	(7,951)	(24,258)	(10,494)	(26,765)
(Impairment) reversal of impairment of foreign exchange gain	(3,291)	3,972	(4,963)	5,493
Net specific impairment losses on financial assets	(11,242)	(20,286)	(15,457)	(21,272)
Provision for latent impairment losses	16	(49)	(155)	(610)
Total impairment charged to comprehensive income (see note 22)	(11,226)	(20,335)	(15,612)	(21,882)
Net valuation changes:				
Income due to revised estimated future cash flow from loans	8,360	25,408	10,239	26,739
Net specific impairment losses on financial assets	(11,242)	(20,286)	(15,457)	(21,272)
Foreign exchange gain (loss) (see note 10)	3,291	(4,420)	4,963	(5,941)
Net valuation changes on loans and receivables	409	702	(255)	(474)

* unaudited information

(Impairment) reversal of impairment of foreign exchange gain from customers with foreign exchange loans and cash flow in ISK is offset against total foreign exchange gain (loss) as per note 10.

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Net financial expenses

8. Net financial expenses are specified as follows:

	2011* 1.4.-30.6	2010* 1.4.-30.6	2011 1.1-30.6	2010 1.1-30.6
Net (loss) gain on financial instruments held for trading	(272)	134	(413)	164
Net (loss) gain on financial instruments designated at fair value through P&L	0	(183)	3	(598)
Net loss on loss of control over subsidiary	(58)	0	(58)	0
Net financial expenses	(330)	(49)	(468)	(434)

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

Shares	0	(183)	3	(598)
Net loss on financial instruments designated at fair value through P&L	0	(183)	3	(598)

* unaudited information

Net foreign exchange gain

10. Net foreign exchange gain (loss) is specified as follows:

	2011* 1.4-30.6	2010* 1.4.-30.6	2011 1.1-30.6	2010 1.1-30.6
Assets:				
Cash and balances with Central Bank	8	(59)	34	(76)
Financial assets held for trading	(1,414)	(1,158)	(854)	(884)
Loans to credit institutions	808	(2,547)	1,548	(3,243)
Loans to customers	5,903	(7,078)	9,542	(9,975)
Other assets	3	(30)	12	(53)
Total	5,308	(10,872)	10,282	(14,231)
Liabilities:				
Deposits from credit institutions	(70)	4,572	(136)	215
Deposits from customers	(1,207)	4,239	(3,072)	4,929
Subordinated loan	(504)	(2,177)	(1,646)	3,194
Other liabilities	(102)	(2)	(129)	5
Total	(1,883)	6,632	(4,983)	8,343
Unadjusted net foreign exchange gain (loss)	3,425	(4,240)	5,299	(5,888)
Foreign exchange reversal on loans to customers with ISK cash flow	(3,291)	4,420	(4,963)	5,941
Net foreign exchange gain	134	180	336	53

* unaudited information

Other net operating income

11. Other net operating income is specified as follows:

	2011* 1.4.-30.6	2010* 1.4.-30.6	2011 1.1-30.6	2010 1.1-30.6
Agency fees and service level agreement fees	70	85	151	192
Legal cost and fees	22	35	45	72
Rental income	76	26	135	57
Rental income on foreclosed mortgages	72	46	145	75
Other net operating income	57	200	180	83
Other net operating income	297	392	656	479

* unaudited information

For the six months ended 30 June 2011 15 Amounts are in ISK million

Administrative expenses

12. Administrative expenses are specified as follows:

	2011* 1.4.-30.6	2010* 1.4.-30.6	2011 1.1-30.6	2010 1.1-30.6
Salaries and related expenses	2,477	2,432	4,969	4,597
Other administrative expenses**	2,000	2,379	4,510	4,439
Depreciation and amortisation	159	130	327	259
Administrative expenses	4,636	4,941	9,806	9,295

* unaudited information

**Included in other administrative expenses for H1 2011 is an insurance fund premium of ISK 432m for the Depositors and Investors Guarantee Fund (H1 2010: ISK 562m).

Salaries and related expenses

13. Salaries and related expenses are specified as follows:

	2011* 1.4.-30.6	2010* 1.4.-30.6	2011 1.1-30.6	2010 1.1-30.6
Salaries	2,004	1,961	4,014	3,684
Pension and similar expenses	273	260	542	492
Social security charges	193	175	371	337
Other	7	36	42	84
Salaries and related expenses	2,477	2,432	4,969	4,597

* unaudited information

Effective income tax rate

14. The corporate income tax rate in Iceland changed from 18% in 2010 to 20% from 1 January 2011. Taxes for the six month period to 30 June 2011 are calculated at 20%. The effective income tax rate in the Bank's income statement is 21,5% for the six months ended 30 June 2011. The difference is specified as follows:

	2011 1.1-30.6		2010 1.1-30.6	
Profit before tax	9,624		10,538	
Income tax calculated on the profit of the period	1,925	20.0%	1,897	18.0%
Effect of different tax rate in other countries	(22)	(0.2%)	0	0.0%
Non-deductable expenses	114	1.2%	0	0.0%
Income not subject to tax	(14)	(0.1%)	0	0.0%
Acquisition price of subsidiaries reduced by gain on sale of shares	0	0.0%	14	0.1%
Correction in accordance with ruling on prior years' taxable income	(43)	(0.4%)	345	3.3%
Other differences	107	1.1%	91	0.8%
Income tax according to the statement of comprehensive income	2,067	21.5%	2,347	22.3%

Earnings per share

15. Earnings per share are specified as follows:

	2011 1.1-30.6	2010 1.1-30.6
Net profit of the equity holders of the parent, according to the statement of comprehensive income	8,077	8,286
Average outstanding shares:		
Weighted average number of outstanding shares for the period, million	10,000	10,000
Average outstanding shares, million	10,000	10,000
Basic earnings per share	0.81	0.83
Diluted earnings per share	0.81	0.83

For the six months ended 30 June 2011 16 Amounts are in ISK million

Cash and balances with Central Bank

16. Specification of cash and balances with Central Bank:

	30.6.2011	31.12.2010
Cash on hand	2,256	1,833
Balances with Central Bank other than mandatory reserve deposits	6,258	16,352
Certificates of deposit	13,816	6,865
Included in cash and cash equivalents	22,330	25,050
Mandatory reserve deposits with Central Bank	5,431	5,749
Cash and balances with Central Bank	27,761	30,799

Mandatory reserve deposits are not available for use in the Bank's day-to-day operations.

Certificates of deposit (CDs) are short term instruments issued by the Central Bank at predetermined interest rates. CDs are issued solely to banks and other financial institutions and are not transferable except to other comparable institutions.

Derivatives financial instruments

17. Derivatives held for trading:	Assets 30.6.2011	Notional values related to assets 30.6.2011	Liabilities 30.6.2011	Notional values related to liabilities 30.6.2011
Interest rate swap	5	800	0	0
Cross currency interest rate swaps	0	0	1,573	61,020
Foreign exchange forwards	71	3,926	0	77
Foreign exchange swaps	42	6,136	88	6,281
Bond forwards	17	1,280	3	620
Bond options	0	0	73	25,700
Derivatives held for trading	136	12,142	1,738	93,698

Derivatives held for trading:	Assets 31.12.2010	Notional values related to assets 31.12.2010	Liabilities 31.12.2010	Notional values related to liabilities 31.12.2010
Cross currency interest rate swaps	0	0	312	48,217
Equity options	58	500	0	0
Foreign exchange forwards	12	3,453	44	8,859
Foreign exchange swaps	0	231	0	1,537
Bond options	0	0	73	25,000
Derivatives held for trading	70	4,184	429	83,613

For the six months ended 30 June 2011 17 Amounts are in ISK million

Loans

18. Loans to credit institutions:

	30.6.2011	31.12.2010
Money market loans	20,070	17,788
Bank accounts	20,904	12,102
Repo loans	358	980
Other loans	295	0
Loans to credit institutions	41,627	30,870

19. Loans to credit institutions :

			30.6.2011			31.12.2010
	Gross amount	impairment allowance	Carrying amount	Gross amount	impairment allowance	Carrying amount
Loans	42,190	(563)	41,627	31,456	(586)	30,870
Loans to credit institutions	42,190	(563)	41,627	31,456	(586)	30,870

20. Loans to customers:

	30.6.2011	31.12.2010
Loans and advances to customers at amortised cost	509,914	515,161
Loans to customers	509,914	515,161

Amounts are in ISK million

21. Loans to customers at amortised cost:

	Gross amount	Impairment allowance	30.6.2011 Carrying amount	Gross amount	impairment allowance	31.12.2010 Carrying amount
Loans to customers						
Individuals	181,626	(11,382)	170,244	181,566	(8,853)	172,713
Commerce and Services	70,107	(7,660)	62,447	63,068	(11,922)	51,146
Construction	17,203	(4,986)	12,217	21,091	(4,003)	17,088
Energy	3,846	(104)	3,742	2,233	(111)	2,122
Financial institutions	4,264	(46)	4,218	4,257	(9)	4,248
Government secured customer loan	45,554	0	45,554	52,182	0	52,182
Industrials	35,847	(3,083)	32,764	23,670	(3,020)	20,650
Investment companies	31,859	(11,791)	20,068	55,495	(13,507)	41,988
Public sector and non-profit organisations	10,368	(355)	10,013	11,061	(496)	10,565
Real estate	102,977	(23,819)	79,158	92,456	(17,932)	74,524
Seafood	71,486	(1,997)	69,489	69,797	(1,862)	67,935
Loans to customers	575,135	(65,223)	509,914	576,876	(61,715)	515,161

The internal industry classification was changed in the first half of the year making the comparison to the credit risk notes in the 2010 annual accounts inappropriate. This change included a reclassification of some of the Bank's customers resulting in a shift between industries, for example a part of the exposure to Investment companies has moved to Commerce and service and to Industrials.

22. Financial assets - impairments

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

	Individually assessed	Collectively assessed	Latent	30.6.2011 Total	31.12.2010 Total
At 1 January	45,704	15,606	991	62,301	72,391
Disposal of subsidiaries	(171)	0	0	(171)	0
Amounts written-off	(6,579)	(992)	0	(7,571)	(25,840)
Recoveries of amounts previously written-off	166	0	0	166	402
Principal credit adjustment	(1,714)	(2,836)	0	(4,550)	(4,667)
Charged to the comprehensive income	14,365	1,091	155	15,612	20,015
At the end of the period*	51,771	12,869	1,146	65,786	62,301

*The provision for impairment losses at 30 June 2011 includes ISK 563 million relating to loans to credit institutions (2010: ISK 586 million).

	2011 1.1-30.6	2010 1.1-30.6
Impairment losses charged to the comprehensive income:		
Loans to customers	15,635	20,326
Loans to credit institutions	(23)	1,556
Impairment losses charged to the comprehensive income	15,612	21,882

For the six months ended 30 June 2011 19 Amounts are in ISK million

Investments in associates

23. Changes in investments in associates:

	30.6.2011	31.12.2010
Investments in associates at the beginning of the period	354	827
Purchases of shares in associates	0	54
Sale of shares in associates	0	(8)
Transfers	390	0
Revaluation	0	(519)
Investments in associates at the end of the period	744	354

Investment in subsidiaries

24. The parent’s interest in its subsidiaries are as follows:

	Location	Ownership
Kreditkort hf.	Iceland	100%
Íslandssjóðir hf.	Iceland	100%
Miðengi ehf.	Iceland	100%
Eik Properties ehf.	Iceland	100%
Jarðboranir hf.	Iceland	100%
Island Fund S.A. (formerly Glitnir Asset Management)	Luxembourg	100%
Glacier Geothermal and Seafood Corporation	USA	100%
Glacier Securities LLC	USA	100%
Air Atlanta Properties Ltd.	UK	100%
18 other subsidiaries (SME)	Iceland	

Related party disclosures

25. Parent and ultimate controlling party

The Bank has determined that ISB Holding is the ultimate controlling party of the Bank with GLB Holding having significant influence. This is reflected in the related party transactions.

Entities which are controlled, jointly controlled or significantly influenced by the government (state-controlled entities) are not considered as being a related party if neither entity actually influenced the other and if the state did not actually influence either entity with regards to transactions between them. Transactions with state-controlled entities during the period were based on general business terms of the Bank.

Related party transactions

The Bank has a related party relationship with its subsidiaries, the Board of Directors of the parent company, the executive vice presidents of the Bank, close family members of individuals referred to herein and entities with significant influence as the largest shareholders of the Bank.

All loans to employees are provided on general business terms of the Bank. Included in assets are loans to key management.

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

	30.6.2011	31.12.2010
CEO and Managing Directors (including companies owned by them)	(69)	(59)
Members of the Board (including companies owned by them)	(76)	(817)
Associated companies and other related parties	14,074	21,147
Total	13,929	20,271
Guarantees	129	55
Loan commitments, overdraft and credit card commitments	658	187

Impairment allowances of ISK 3.2bn were recognised in the period against balances outstanding with associated companies.

No share option programmes were operated during 2011.

For the six months ended 30 June 2011 20 Amounts are in ISK million

Non-current assets and disposal groups held for sale

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

	30.6.2011	31.12.2010
Repossessed collateral	9,213	7,435
Assets of disposal groups classified as held for sale	14,777	16,054
Total	23,990	23,489

Repossessed collateral:

Residential property	5,385	4,880
Vehicles	396	253
Equipment	92	160
Shares	3,267	2,067
Other assets	73	75
Total	9,213	7,435

Assets of disposal groups classified as held for sale:	30.6.2011	31.12.2010
Cash	1,555	5
Investment properties	246	15,086
Equipment	2,440	609
Receivables	3,205	98
Inventory	1,104	157
Intangible assets	1,090	0
Tax assets	309	0
Other assets	4,828	99
Total	14,777	16,054

Liabilities associated with assets classified as held for sale:	30.6.2011	31.12.2010
Payables	1,142	59
Deferred tax liabilities	210	0
Borrowings and other liabilities	3,846	16,383
Other liabilities	1,053	0
Total	6,251	16,442

For the six months ended 30 June 2011 21 Amounts are in ISK million

Other assets

27. Other assets are specified as follows:

	30.6.2011	31.12.2010
Receivables	608	1,532
Unsettled securities transactions	16,423	687
Prepaid expenses	268	303
Accruals	403	620
Inventory (real estate)	1,635	1,889
Other assets	365	513
Other assets	19,702	5,544

Inventory comprises real estate valued at the lower of cost and net realisable value.

Deposits from Central Bank and credit institutions

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

	30.6.2011	31.12.2010
Repurchase agreements with Central Bank	12	26
Deposits from credit institutions	93,837	96,212
Deposits from Central Bank and credit institutions	93,849	96,238

Deposits from customers

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

	30.6.2011	31.12.2010
Demand deposits	200,392	214,597
Time deposits	120,569	112,561
Deposits from customers	320,961	327,158

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

	30.6.2011		31.12.2010	
	Amount	% of total	Amount	% of total
Central government and state-owned enterprises	8,312	3%	4,065	1%
Municipalities	4,256	1%	4,927	2%
Other companies	179,508	56%	185,886	57%
Individuals	128,885	40%	132,280	40%
Deposits from customers	320,961	100%	327,158	100%

Amounts are in ISK million

Debt issued and other borrowed funds

31. Specification of debt issued and other borrowed funds:

	30.6.2011	31.12.2010
Issued bonds	51,351	52,717
Loans from credit institutions	0	353
Other debt securities	4,178	2,355
Debt issued and other borrowed funds	55,529	55,425

Other liabilities

32. Specification of other liabilities:

	30.6.2011	31.12.2010
Accruals	2,457	1,951
Liabilities to retailers for credit card provision	0	12,921
Guarantees	416	1,664
Chargeable gain tax	535	1,357
Unsettled securities transactions	23,314	1,386
Deferred income	232	345
Sundry liabilities	5,286	7,070
Other liabilities	32,240	26,694

Equity

33. Authorised share capital of the Bank is 10,000m ordinary shares of ISK 1 each. At 30.6.2011 paid up share capital totalled ISK 65,000m which is the total stated share capital of the Bank.

Total share capital

	30.6.2011	31.12.2010
Ordinary share capital	10,000	10,000
Share premium account	55,000	55,000
Total share capital	65,000	65,000

Off balance sheet items

Obligations

34. The Bank provides off balance sheet commitments. These items are specified as follows:

	30.6.2011	31.12.2010
Guarantees granted to customers	8,054	8,404
Committed undrawn lines of credit	15,847	13,453
Unused overdrafts	15,899	17,186
Credit card commitments	18,720	17,916
The Depositors and Investors Guarantee Fund – declaration of guarantee	3,689	3,689

New legislation for the Depositors and Investors Guarantee Fund was introduced in June 2011. The Bank has not been presented with a new declaration of guarantee to match this legislative change.

Balance of custody assets

35. Balance of custody assets:

	30.6.2011	31.12.2010
Custody assets	636,185	642,502

Amounts are in ISK million

Contingencies

36. **Litigation threats**

Several former customers of Glitnir private banking services have threatened litigation against the Bank in order to claim compensation for alleged mistakes made by former employees of Glitnir. A few of those customers have already filed lawsuits against the Bank with the Reykjavík District Court. The Bank has not accepted liability and will challenge these lawsuits on the grounds that these claims relate to events that happened prior to the incorporation of the Bank and the assignment of related liabilities and assets and are therefore not the responsibility of the Bank in any way. The District Court has now ruled in favour of the Bank in one of these cases stating that the Bank cannot be held responsible for a mistake made by a former employee of Glitnir. This ruling was not appealed. The Bank estimates the total amount of compensation liabilities currently claimed by customers of Glitnir to be ISK 5.5bn.

Netting agreement

When certain assets and obligations were transferred from Glitnir to the Bank, the FME (Financial Supervisory Authority) ruled that customers would, upon liquidation of Glitnir, maintain their right to claim netting of assets and liabilities held by Glitnir prior to the Bank's acquisition. The Bank made an agreement with Glitnir that the latter will compensate the Bank for any losses incurred as a result of netting of assets and liabilities. The claims in question are priority claims on the liquidated assets of Glitnir and the netting exercise is therefore unlikely to affect either the net asset value or the earnings of the Bank.

Allocation of liens, guarantees and comparable rights

When certain assets and obligations were transferred from Glitnir to the Bank, the FME ruled that the Bank would take over all rights used to secure the performance of obligations of the debtors of Glitnir, including all liens, guarantees and other comparable rights connected to the claims of the Bank.

The Bank should, however, be accountable to Glitnir for specific collateral of its customers, as applicable, due to claims and derivatives which were not transferred to the Bank. The Bank has, in accordance with this decision, transferred to Glitnir certain collateralised obligations of customers. One customer filed a lawsuit against the Bank with the Reykjavík District Court challenging the Bank's decision to transfer the customer's money market deposit to Glitnir which the Bank, in good faith, identified as collateral for a foreign exchange future contract. The claim was for approximately ISK 450 million. The District Court ruled in favour of the Bank and the case has now been appealed to the Iceland Supreme Court. Any future allocation of collaterals will be made under an agreement with Glitnir, whereby Glitnir indemnifies the Bank against any future claims arising from the transfer of such rights.

Indexed loans and foreign currency loans

In order to address the uncertainty surrounding which foreign currency loans should be deemed to be illegally linked to foreign currency, the Parliament introduced in 2010 a new legislation proposing a change to the Interest Law 38/2001. The legislation was passed as Amendment to Interest Law 151/2010, taking effect on 28 December 2010. Based on the context of this new law, the Bank treated all foreign currency dominated mortgages and car loans according to the method previously set forth in a September 2010 ruling of the Supreme Court concerning car loans/leasing contracts. All customers with foreign currency mortgages will be presented with an offer of having their mortgage recalculated according to a similar formula, regardless of the validity of the contract in question. The definition of a mortgage in the new legislation refers to tax law. The recalculation has to be offered if the debtor was eligible for a refund in part of paid interest (interest subsidy) of the loan. The Bank decided to expand this definition to cover all residential loans to individuals, although the debtors are not obliged to accept the offer. The interest rate on car loans going forward will, according to the law, be replaced by non-indexed CPI-rate. The same goes for mortgages for the first five years, in addition to a choice of indexed CPI rate. At the end of the five year term, mortgages will revert back to market rates.

At the end of April 2011 the District Court of Reykjavík ruled that all financial lease agreements within the Bank should be treated as loan agreements. The ruling quotes the precedent set by the Supreme Court in June 2010 to the effect that leasing contracts can be regarded as loan contracts as far as the Interest Law 38/2001 is concerned. The Bank has made an appeal against the ruling to the Supreme Court and a ruling is expected in the second half of 2011. If the Supreme Court confirms the District Court ruling, approximately 4,100 agreements with a book value of ISK 10.2bn will need to be recalculated.

The effect on other types of foreign currency loan contracts remains uncertain. It is however clear that, although the amount owed may be changed by the Courts, loan obligations containing illegal foreign currency provisions will not be declared null and void. Several court rulings are expected in relation to whether or not certain types of loans are truly foreign currency denominated loans or deemed to be illegally linked to foreign currency.

For instance, the District Court of South Iceland ruled on 29 October 2010 that a loan in foreign currency granted by the Bank should indeed be treated as a foreign currency denominated contract. The contract in question was not considered to be in breach of articles 13 and 14 of the Interest Law 38/2001 and was therefore deemed lawful. Furthermore, the loan obligations and their implementation is not unfair according to article 36 of the Contract Law 07/1936 which gives the Courts the authority to change or declare void unreasonable or unfair provisions in private contracts. The case has been appealed to the Supreme Court along with 2-3 cases, one involving a financial leasing contract.

36. Cont'd

In June 2011, the Supreme Court ruled on a relatively common type of a corporate foreign exchange loan contract originating in Landsbankinn in 2007 (Landsbankinn vs. Mótormax). Following this judgement, the Bank has assessed all of its corporate contract forms as to their validity as true foreign currency loan contracts. Based in part on this assessment, the Bank will be making assumptions as to the possible financial effect of the remaining lawsuits, adjusting for the fact that the Bank has already offered its customers principal adjustment of their foreign currency loans and taking into account that a ruling on a certain type of replacement interest has been passed. The assessment categorises the contracts into four levels of risk, highest being identical to the form ruled on in June. The Bank has already recognised a provision for the highest risk category. The work on processing each category is in its initial stages. In the meanwhile, those eligible for recalculation will have the option of fixed payments.

Formal investigation by the EFTA Surveillance Authority regarding alleged government aid granted by the Icelandic government to investment funds and associated fund management companies connected to the three failed Icelandic banks Glitnir, Kaupthing and Landsbanki

At the height of the financial crisis in Iceland, in early October 2008, investment funds suspended redemption of unit certificates in order to protect the equality of unit certificate holders. The funds were subsequently wound-up and the unit certificate holders paid out the value of their unit shares. This was partly achieved by the banks buying the assets (mainly domestic bonds) held by the funds and adding the proceeds from that sale to assets already held in the form of deposits. The price paid for the assets was decided by the boards of the newly restored banks, based on internal valuations and valuations of external consultants (audit firms).

In this case, it is alleged that management companies of the investment funds and depositories of the three major Icelandic banks received unlawful government aid from the Icelandic authorities in October 2008. It is alleged that the government influenced the decisions of the new banks to purchase assets from the funds (managed by their subsidiaries) on favourable terms and, thus, enabling them to wind-up the funds and repay investors when there was no effective market for the assets.

The Icelandic government and the banks claim that the transactions were neither influenced by the government nor funded by its resources. Even if the banks were public undertakings, the acquisition was decided on independently by each bank and based on commercial motives. The assets acquired were valued in a professional manner, albeit in a period of uncertainty.

Formal investigation by the EFTA Surveillance Authority into state aid granted in the restoration of certain operations of Glitnir and the establishment and capitalisation of Íslandsbanki

The EFTA Surveillance Authority (Authority) decided to open formal investigations into the government aid granted in October 2008 and September 2009 to rescue domestic operations of the three main Icelandic banks: Glitnir, Kaupthing and Landsbanki, and to establish and capitalise new successor banks, now called Íslandsbanki, Arion and NBI (Landsbanki) respectively.

The measures to restore certain operations of the old Icelandic banks and to establish and capitalise new banks should have been notified prior to their implementation. The Icelandic authorities should also have submitted detailed restructuring plans outlining viable futures for the banks without a need for a government support.

The Authority has to assess whether the state aid granted to the banks adequately addresses each bank's situation without unduly distorting competition. In order to do so, it is imperative that detailed restructuring plans are submitted. As part of the investigation, the Authority will assess e.g. potential aid to the new banks in the form of a special liquidity facility. Also under scrutiny is the transfer of assets and deposits liabilities from Straumur to Íslandsbanki.

The Icelandic authorities and the Bank claim that the measures are compatible with the functioning of the EEA Agreement Article 61(3)(b), on the basis that they were necessary in order to remedy a serious disturbance in the Icelandic economy. The Icelandic authorities have stressed that the situation in Iceland in October 2008 was extreme and required immediate action in order to restore financial stability and confidence in the Icelandic economy.

The Bank has submitted a detailed restructuring plan to the Authority outlining viable futures for the Bank without a need for state support.

Events after the end of the reporting period

37. **Acquisition of Byr hf.**

On 13 July 2011 the Bank announced its offer to acquire all of the shares of Byr hf. (Byr). The shares will be acquired from the Byr Savings Bank's winding-up committee of and the Icelandic government. The acquisition is subject to approval by the competition and regulatory authorities.

Byr is a newly incorporated financial institution built on the foundation of a savings bank which became insolvent in April 2010. Byr focuses mainly on retail banking. The Bank's intention is to merge Byr's operations fully with those of the parent. The Bank's CAD ratio after the merger is expected to remain well above the minimum requirements stipulated in the Act on Financial Undertakings. The acquisition price will remain confidential until the transaction has been completed, which is expected to occur in the second half of 2011.

Risk Management

The Bank is exposed to various risks through its use of financial instruments. Managing these risks is an integral part of the Bank's operations. More information about Risk Management at Íslandsbanki is available in the Risk Book 2010 at www.islandsbanki.is/riskbook.

Credit risk

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

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

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

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

The loan portfolio acquired from Glitnir is the largest part of the credit exposure of the Bank. Due to the extraordinary circumstances in the Icelandic economy and the fact that the loan portfolio was acquired at a deep discount, care must be taken when interpreting conventional measures of credit risk.

38. Maximum credit exposure

The Bank's credit risk exposure comprises both on-balance sheet and off-balance sheet items. Maximum exposure to credit risk for on-balance sheet assets is the net carrying amount as reported in the statement of financial position. The maximum exposure for off-balance sheet items is the amount that the Bank might have to pay out against financial guarantees and loan commitments, less provisions the Bank has made because of these items.

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

The internal industry classification was changed in the first half of the year making the comparison to the credit risk notes in the 2010 annual accounts inappropriate. This change included a reclassification of some of the Bank's customers resulting in a shift between industries, for example a part of the exposure to Investment companies has moved to Commerce and service and to Industrials.

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

Credit risk exposure

38. **Maximum credit exposure**

Maximum credit exposure 30.6.2011

	Individuals	Central Governments	Commerce and Services	Construction	Energy	Financial institutions	Government secured customer loan	Industrials	Invest-ment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	27,761	-	-	-	-	-	-	-	-	-	-	27,761
Loans to credit institutions	-	-	-	-	-	41,627	-	-	-	-	-	-	41,627
Loans to customers:													
Overdrafts	8,601	-	4,595	2,274	2	1,056	-	4,020	927	1,150	796	1,071	24,492
Credit cards	12,231	-	986	110	0	21	5	321	14	176	48	29	13,941
Mortgages	108,472	-	-	-	-	-	-	-	-	-	-	-	108,472
Leases	10,965	-	8,816	2,429	17	20	-	4,013	232	786	2,020	385	29,683
Other loans	29,975	-	48,050	7,404	3,723	3,120	45,549	24,411	18,895	7,901	76,293	68,005	333,326
Bonds and debt instruments:	-	45,231	-	-	343	3,119	-	-	881	37	845	-	50,456
Derivatives	2	-	5	-	-	54	-	71	4	-	-	-	136
Balance sheet total	170,246	72,992	62,452	12,217	4,085	49,017	45,554	32,836	20,953	10,050	80,002	69,490	629,894
Financial guarantees	928	-	1,017	2,355	4	1,048	-	1,534	65	74	714	315	8,054
Loan commitments	-	-	1,762	-	8,695	5,000	-	267	-	-	123	-	15,847
Undrawn overdraft	6,837	-	3,828	601	203	1,512	-	1,161	51	770	310	626	15,899
Credit card commitments	16,441	-	1,219	196	6	56	13	290	51	332	51	65	18,720
Off-balance sheet total	24,206	-	7,826	3,152	8,908	7,616	13	3,252	167	1,176	1,198	1,006	58,520
Total	194,452	72,992	70,278	15,369	12,993	56,633	45,567	36,088	21,120	11,226	81,200	70,496	688,414

Amounts are in ISK million

38. Cont'd

Maximum exposure 31.12.2010

	Individuals	Central Governments	Commerce and Services	Construction	Energy	Financial institutions	Government secured customer loan	Industrials	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	30,799	-	-	-	-	-	-	-	-	-	-	30,799
Loans to credit institutions	-	-	-	-	-	30,870	-	-	-	-	-	-	30,870
Loans to customers:													
Overdrafts	7,943	-	3,963	2,794	254	1,046	-	3,037	676	1,347	605	973	22,638
Credit cards	14,307	-	710	94	0	15	6	229	16	76	33	26	15,512
Mortgages	105,637	-	-	-	-	-	-	-	-	-	-	-	105,637
Leases	11,678	-	6,835	2,337	19	55	-	3,955	208	843	2,068	248	28,246
Other loans	33,148	-	39,380	11,864	1,849	3,132	52,176	13,734	41,223	8,118	71,817	66,687	343,128
Bonds and debt instruments:	-	64,087	-	-	324	2,129	-	-	659	-	825	-	68,024
Derivatives	-	-	-	58	-	12	-	-	-	-	-	-	70
Balance sheet total	172,713	94,886	50,888	17,147	2,446	37,259	52,182	20,955	42,782	10,384	75,348	67,934	644,924
Financial guarantees	920	-	1,308	2,499	-	-	-	2,266	82	22	700	607	8,404
Loan commitments	-	-	1,072	-	5,044	5,000	-	1,827	-	-	510	-	13,453
Undrawn overdraft	7,945	-	3,339	644	202	1,239	-	1,458	529	944	434	452	17,186
Credit card commitments	15,829	-	1,052	197	1	50	10	316	48	304	49	60	17,916
Off-balance sheet total	24,694	-	6,771	3,340	5,247	6,289	10	5,867	659	1,270	1,693	1,119	56,959
Total	197,407	94,886	57,659	20,487	7,693	43,548	52,192	26,822	43,441	11,654	77,041	69,053	701,883

Amounts are in ISK million

39. Impaired loans to credit institutions and customers

Loans are classified as impaired loans if contractual cash payments are not expected to be fulfilled and if financial restructuring of the obligor is expected to lead to a loss on that particular loan. In most cases, loss is avoided because of the difference between the claim value and the carrying amount resulting from the deep discount of the acquired loan portfolio.

Loans are also classified as impaired if the Bank has made impairments to offset currency movements. For individuals and smaller companies this is the main reason for loans being classified as impaired. This impairment does not signal a loss from the deep discount.

The full carrying amount of all loans which give rise to individual impairment or collective impairment is included in impaired loans, even if parts are covered by collateral.

At 30 June 2011	Loans neither past due nor impaired	Past due loans but not impaired	Loans classified as impaired loans	Total carrying amount of loans
Loans to credit institutions	41,627	0	0	41,627
Loans to customers				
Individuals	122,092	25,483	22,669	170,244
Commerce and Services	45,314	2,956	14,177	62,447
Construction	3,549	2,682	5,986	12,217
Energy	2,562	1	1,179	3,742
Financial institutions	3,945	17	256	4,218
Government secured customer loan	45,554	0	0	45,554
Industrial	21,759	2,324	8,681	32,764
Investment companies	5,907	753	13,407	20,067
Public sector and non-profit organisations	6,290	223	3,500	10,013
Real estate	28,001	3,778	47,379	79,158
Seafood	62,457	2,585	4,448	69,490
Total	389,057	40,802	121,682	551,541

At 31 December 2010	Loans neither past due nor impaired	Past due loans but not impaired	Loans classified as impaired loans	Total carrying amount of loans
Loans to credit institutions	30,842	8	20	30,870
Loans to customers				
Individuals	123,086	21,194	28,433	172,713
Commerce and Services	25,075	3,442	22,369	50,886
Construction	8,326	2,680	6,082	17,088
Energy	1,003	15	1,104	2,122
Financial institutions	4,229	8	11	4,248
Government secured customer loan	52,182	0	0	52,182
Industrial	7,858	1,727	11,370	20,955
Investment companies	12,423	1,409	28,292	42,124
Public sector and non-profit organisations	6,255	1,549	2,579	10,383
Real estate	25,653	6,582	42,290	74,525
Seafood	56,003	951	10,981	67,935
Total	352,935	39,565	153,531	546,031

For the six months ended 30 June 2011 29 Amounts are in ISK million

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

Amounts reported as past due refer to the total loan exposure and not only the payment or sum of payments that are past due. Past due but not impaired loans are as follows:

At 30 June 2011	Past due up to 30 days	Past due 31-60 days	Past due 61-90 days	Over 90 days	Total
Loans to credit institutions	0	0	0	0	0
Loans to customers					
Individuals	7,262	3,131	2,073	13,017	25,483
Commerce and Services	932	265	307	1,452	2,956
Construction	581	79	123	1,899	2,682
Energy	0	0	0	1	1
Financial institutions	17	0	0	0	17
Government secured customerloan	0	0	0	0	0
Industrial	662	159	102	1,401	2,324
Investment companies	505	58	19	171	753
Public sector ad non-profit organisations	162	24	12	25	223
Real estate	510	148	325	2,795	3,778
Seafood	1,065	52	673	795	2,585
Total	11,696	3,916	3,634	21,556	40,802

At 31 December 2010	Past due up to 30 days	Past due 31-60 days	Past due 61-90 days	Over 90 days	Total
Loans to credit institutions	8	0	0	0	8
Loans to customers					
Individuals	5,189	2,577	685	12,743	21,194
Commerce and Services	713	243	85	2,401	3,442
Construction	335	94	136	2,115	2,680
Energy	14	1	0	0	15
Financial institutions	1	0	1	6	8
Government secured customerloan	0	0	0	0	0
Industrial	383	153	192	999	1,727
Investment companies	56	553	8	792	1,409
Public sector ad non-profit organisations	1,355	103	72	19	1,549
Real estate	2,754	386	259	3,183	6,582
Seafood	44	227	20	660	951
Total	10,852	4,337	1,458	22,918	39,565

Amounts are in ISK million

41. Large exposure disclosure

When the Bank's total exposure to a group of connected clients exceeds 10% of the Bank's capital base, it is considered a large exposure. The exposure is evaluated net of credit risk mitigating effects eligible according to FME rules 216/2007.

When assessing the exposure, both on-balance sheet and off-balance sheet items from all types of financial instruments are included as defined by the FME rules. The Bank has an internal criteria that defines connections between clients. This criteria reflect the Bank's interpretation of Article (1)(a) of Law no. 161/2002 on Financial Undertakings, where groups of connected clients are defined.

The following table shows the Bank's large exposures as a percentage of the Bank's capital base, gross and net of eligible credit risk mitigating effects.

	30.6.2011		31.12.2010	
Client groups	Gross	Net	Gross	Net
Group 1	43%	0%	44%	0%
Group 2	30%	1%	37%	1%
Group 3	14%	14%	15%	15%

The Bank has one large exposure to a group of connected clients that amounts to 14% of the Bank’s capital base which is below the aggregated 800% limit set by the law. No large exposure exceeds the maximum 25% set by the law.

Amounts are in ISK million

Liquidity Risk

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

Liquidity risk management

The Bank's main source of funding is customer deposits. The Bank's Treasury is responsible for the Bank's funding and long-term liquidity management. The Interbank desk is responsible for day-to-day liquidity management.

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

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

The tables below show the contractual payments of principal and interest for the Bank's financial liabilities. Therefore, the total figure for each liability class is higher than its respective balance sheet amount.
For dated financial liabilities the amounts are grouped into maturity buckets according to contractual maturities of principal and estimated contractual payments of interest. For demand deposits or other non-dated liabilities, the figures are grouped according to the first possible required payment date.

Maturity analysis 30 June 2011

Financial Liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Short positions	10,582	0	0	0	0	0	10,582
Deposits from Central Bank	12	0	0	0	0	0	12
Deposits from credit institutions	69,606	4,247	20,606	0	0	0	94,459
Deposits from customers	229,501	43,429	8,267	36,888	10,393	0	328,478
Debt issued and other borrowed funds	0	2,137	6,590	34,381	29,448	0	72,556
Subordinated loans	0	0	1,011	6,787	30,775	0	38,573
Other financial liabilities	4,570	25,622	10,052	1,068	225	151	41,688
Total financial liabilities	314,271	75,435	46,526	79,124	70,841	151	586,348

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

Off balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial gurantees	8,054	0	0	0	0	0	8,054
Undraw loan commitments	15,847	0	0	0	0	0	15,847
Undrawn overdraft	15,899	0	0	0	0	0	15,899
Credit card commitments	18,720	0	0	0	0	0	18,720
Total	58,520	0	0	0	0	0	58,520
Total non-derivative financial liabilities and off-balance sheet liabilities	372,791	75,435	46,526	79,124	70,841	151	644,868

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

Amounts are in ISK million

42. Cont'd

Derivative financial liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	0	8,106	3,880	77,109	28,066	0	117,161
Outflow	0	(8,310)	(4,106)	(80,887)	(28,145)	0	(121,448)
Total	0	(204)	(226)	(3,778)	(79)	0	(4,287)
Net settled derivatives	0	(3)	0	0	0	0	(3)
Total	0	(207)	(226)	(3,778)	(79)	0	(4,290)

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

Financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with Central bank	13,945	13,816	0	0	0	0	27,761
Bonds and debt instruments	4,889	11,300	0	310	31,288	2,669	50,456
Shares and equity instruments	0	0	0	0	0	3,240	3,240
Loans to credit institutions	14,845	26,487	2	4	288	0	41,626
Loans to customers	0	51,093	34,903	169,602	254,316	0	509,914
Other financial assets	1	16,798	407	141	0	608	17,955
Total financial assets	33,680	119,494	35,312	170,057	285,892	6,517	650,952
Derivative financial assets							
Gross settled derivatives							
Inflow	0	7,340	528	80	0	0	7,948
Outflow	0	(7,237)	(514)	(79)	0	0	(7,830)
Total	0	103	14	1	0	0	118
Net settled derivatives	0	15	0	0	0	0	15
Total	0	118	14	1	0	0	133

The tables below show the comparative amounts for financial assets and liabilities at year end 2010. In the Consolidated Financial Statements 2010, the signs were reversed for the inflow and outflow of derivative financial liabilities and credit card commitments were overestimated. This has been corrected in the tables below.

Maturity analysis 31 December 2010

Financial Liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Short positions	9,090	0	0	0	0	0	9,090
Deposits from Central Bank	26	0	0	0	0	0	26
Deposits from credit institutions	58,439	18,419	11,051	8,705	0	0	96,614
Deposits from customers	243,797	39,600	3,965	36,165	8,716	0	332,243
Debt issued and other borrowed funds	1,899	2,084	6,458	33,754	29,887	0	74,082
Subordinated loans	0	266	822	6,019	29,671	0	36,778
Other financial liabilities	15,712	6,687	9,237	527	507	1,011	33,681
Total financial liabilities	328,963	67,056	31,533	85,170	68,781	1,011	582,514

Amounts are in ISK million

42. Cont'd

Off balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial gurantees	8,404	0	0	0	0	0	8,404
Undraw loan commitments	13,453	0	0	0	0	0	13,453
Undrawn overdraft	17,186	0	0	0	0	0	17,186
Credit card commitments	17,916	0	0	0	0	0	17,916
Total	56,959	0	0	0	0	0	56,959
Total non-derivative financial liabilities and off-balance sheet liabilities	385,922	67,056	31,533	85,170	68,781	1,011	639,473

Derivative financial liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	0	10,811	1,267	57,837	25,000	0	94,915
Outflow	0	(10,797)	(1,403)	(60,757)	(25,113)	0	(98,070)
Total	0	14	(136)	(2,920)	(113)	0	(3,155)
Net settled derivatives	0	0	0	0	0	0	0
Total	0	14	(136)	(2,920)	(113)	0	(3,155)

Financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with Central bank	23,934	6,865	0	0	0	0	30,799
Bonds and debt instruments	4,492	30,378	1	4	31,111	2,038	68,024
Shares and equity instruments	0	0	0	0	0	3,022	3,022
Loans to credit institutions	7,027	23,501	0	0	342	0	30,870
Loans to customers	4,542	57,662	36,782	156,700	259,475	0	515,161
Other financial assets	0	1,235	766	30	513	548	3,092
Total financial assets	39,995	119,641	37,549	156,734	291,441	5,608	650,968

Derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	0	3,685	0	0	0	0	3,685
Outflow	0	(3,672)	0	0	0	0	(3,672)
Total	0	13	0	0	0	0	13
Net settled derivatives	0	0	0	0	0	0	0
Total	0	13	0	0	0	0	13

As a part of managing liquidity risk, the Bank holds a portfolio of liquid assets to meet unexpected outflow of funds or a temporary shortage in access to new funding. These assets are subject to strict criteria with respect to maximum liquidation time and price volatility. The table below shows the composition and amount of the Bank's liquidity back-up at 30 June 2011 and at the year end 2010.

Composition and amount of liquidity back-up	30.6.2011	31.12.2010
Cash and balances with Central Bank	27,761	30,799
Domestic bonds eligible as collateral against borrowing at the Central Bank	56,898	54,881
Foreign government bonds	11,040	30,378
Short-term placements with credit institutions	39,325	28,332
Government liquidity facility	25,000	25,000
Composition and amount of liquidity back-up	160,024	169,390

Amounts are in ISK million

Market risk

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

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

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

Interest rate risk

44. Interest rate risk in trading portfolios

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

Trading bonds and debt instruments, long positions	30.6.2011			31.12.2010		
	MV	Duration	BPV	MV	Duration	BPV
Indexed	2,582	10.72	(2.77)	2,124	9.01	(1.91)
Non-indexed	14,560	1.06	(1.54)	34,078	0.86	(2.92)
Total	17,142	2.51	(4.31)	36,202	1.33	(4.83)

Trading bonds and debt instruments, short positions	30.6.2011			31.12.2010		
	MV	Duration	BPV	MV	Duration	BPV
Indexed	1,426	1.82	0.26	1,129	4.74	0.54
Non-indexed	8,371	1.86	1.56	7,961	1.32	1.05
Total	9,797	1.86	1.82	9,090	1.75	1.59
Net position of trading bonds and debt instruments	7,345	3.38	(2.48)	27,112	1.20	(3.24)

Amounts are in ISK million

45. Interest rate risk in the non-trading portfolio

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

The Bank holds a government bond designated at fair value amounting to ISK 30.3 billion (31 December 2010: ISK 30.3 billion). The bond pays floating rates and carries relatively low interest rate risk.

The Bank uses traditional measures for assessing the sensitivity of the Bank's financial assets, financial liabilities and earnings to changes in the underlying interest rates. Standard scenarios include an adverse 100 basis point parallel shift in all yield curves.

Non-trading portfolio interest rate adjustment periods 30 June 2011

Assets	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
Cash and balances with Central Bank......................	25,504	0	0	0	0	0	25,504
Bonds and debt instruments....................................	32,973	1,487	0	0	353	0	34,813
Loans to credit institutions..	41,402	225	0	0	0	0	41,627
Loans to customers..	395,524	29,658	12,745	62,194	921	8,872	509,914
Total assets	495,403	31,370	12,745	62,194	1,274	8,872	611,858
Off balance sheet items...	47,954	0	0	0	0	0	47,954
Liabilities							
Deposits from Central Bank.....................................	12						12
Deposits from credit institutions	84,000	9,837	0	0	0	0	93,837
Deposits from customers...	310,747	7,114	83	1,417	1,600	0	320,961
Debt issued and other borrowed funds.....................	476	0	0	3,117	50,875	1,061	55,529
Subordinated loans..	22,887	0	0	0	0	0	22,887
Other liabilities...	6,987	0	0	0	0	0	6,987
Total liabilities	425,109	16,951	83	4,534	52,475	1,061	500,213
Off balance sheet items...	48,552	0	0	0	0	0	48,552
Net interest gap on 30 June 2011	69,696	14,419	12,662	57,660	(51,201)	7,811	111,047

Amounts are in ISK million

45. Cont'd

Non-trading portfolio interest rate adjustment periods 31 December 2010

Assets	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
Cash and balances with Central Bank......................	28,966	0	0	0	0	0	28,966
Bonds and debt instruments....................................	31,142	659	0	0	0	22	31,823
Loans to credit institutions..	30,520	350	0	0	0	0	30,870
Loans to customers..	389,089	37,855	9,481	60,557	2,572	15,607	515,161
Total assets	479,717	38,864	9,481	60,557	2,572	15,629	606,820
Off balance sheet items...	47,903	0	0	0	0	0	47,903
Liabilities							
Deposits from Central Bank.....................................	26	0	0	0	0	0	26
Deposits from credit institutions	86,856	1,037	8,319	0	0	0	96,212
Deposits from customers...	322,274	2,521	0	1,420	943	0	327,158
Debt issued and other borrowed funds.....................	432	0	0	808	52,639	1,546	55,425
Subordinated loans..	21,241	0	0	0	0	0	21,241
Total liabilities	430,829	3,558	8,319	2,228	53,582	1,546	500,062
Off balance sheet items...	48,216	0	0	0	0	120	48,336
Net interest gap on 31 December 2010	48,576	35,306	1,162	58,329	(51,010)	13,963	106,327

Amounts are in ISK million

Currency risk

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

The analysis of the Bank's foreign currency exposure presented below is based on the contractual currency of the underlying balance sheet items. Additionally, there are off-balance sheet items that carry currency risk and are included in the total currency imbalance. The off-balance sheet amounts below represent the notional amounts of derivatives and unsettled spot agreements. Most of the net non-adjusted currency imbalance is due to loans with a non-ISK contractual currency to customers with ISK income. As a part of the transfer of assets from Glitnir, the Bank determined that these loans have a recovery value that is limited in ISK terms. To reflect the ISK based recovery value of these loans the Bank has impaired fully the foreign exchange gains on these assets from the date of transfer. Should there be an appreciation of the ISK there will be a corresponding reversal of the impairment charge. This is in accordance with IFRS accounting standards. The Bank's regulators allow for an adjustment of the contractual currency imbalance to reflect the recovery of foreign currency denominated loans to customers with ISK income. The tables below summarise the Bank's exposure to currency risk at 30 June 2011 and 31 December 2010, based on contractual currencies, off-balance sheet items along with the currency adjustment.

Currency analysis 30 June 2011

Assets	EUR	USD	GBP	CHF	JPY	Other	Total
Cash and balances with Central Bank......................	401	273	102	39	11	263	1,089
Bonds and debt instruments....................................	10,292	343	0	0	0	1,111	11,746
Shares and equity instruments.................................	2	146	0	1	0	0	149
Loans to credit institutions..	20,313	13,232	1,240	434	198	3,260	38,677
Loans to customers..	70,811	18,076	4,072	35,393	30,667	2,796	161,815
Investments in associates..	20	347	0	0	0	0	367
Total assets	101,839	32,417	5,414	35,867	30,876	7,430	213,843
Liabilities							
Deposits from credit institutions	4,199	9,524	442	365	24	960	15,514
Deposits from customers...	16,916	13,703	4,164	409	773	5,131	41,096
Debt issued and other borrowed funds.....................	0	0	0	0	0	0	0
Subordinated loans..	22,887	0	0	0	0	0	22,887
Other liabilities...	6,968	0	0	0	0	19	6,987
Total liabilities	50,970	23,227	4,606	774	797	6,110	86,484
Non-adjusted foreign exchange on balance sheet imbalance....................................	50,869	9,190	808	35,093	30,079	1,320	127,359
Adjustment of currency imbalance for FX/ISK loans......................................	(27,801)	(4,388)	(964)	(21,231)	(19,177)	(1,251)	(74,812)
Adjusted imbalance	23,068	4,802	(156)	13,862	10,902	69	52,547
Off balance sheet items							
Off balance sheet assets...	10,418	18,409	1,570	2,857	2,689	36	35,979
Off balance sheet liabilities......................................	31,121	23,864	916	15,989	13,946	842	86,678
Net off balance sheet items	(20,703)	(5,455)	654	(13,132)	(11,257)	(806)	(50,699)
Net currency imbalance on 30 June 2011	2,365	(653)	498	730	(355)	(737)	1,848

Amounts are in ISK million

46. Cont'd

Currency analysis 31 December 2010

Assets	EUR	USD	GBP	CHF	JPY	Other	Total
Cash and balances with Central Bank	405	191	114	38	15	349	1,112
Bonds and debt instruments	15,018	10,695	3,473	0	0	1,953	31,139
Shares and equity instruments	12	51	0	0	0	0	63
Loans to credit institutions	16,620	6,403	1,173	30	200	2,589	27,015
Loans to customers	67,094	26,092	5,333	41,579	36,613	3,501	180,212
Investments in associates	218	0	0	0	0	0	218
Other assets	195	373	42	0	0	3	613
Total assets	99,562	43,805	10,135	41,647	36,828	8,395	240,371
Liabilities							
Deposits from credit institutions	7,701	6,920	5,412	0	11	590	20,634
Deposits from customers	15,791	13,165	2,732	465	1,202	4,935	38,290
Debt issued and other borrowed funds	134	0	0	0	0	32	166
Subordinated loans	21,241	0	0	0	0	0	21,241
Other liabilities	647	696	302	0	0	45	1,690
Total liabilities	45,514	20,781	8,446	465	1,213	5,602	82,021
Non-adjusted foreign exchange on balance sheet imbalance	54,048	23,024	1,689	41,182	35,615	2,793	158,350
Adjustment of currency imbalance for FX/ISK loans	(37,057)	(12,362)	(1,551)	(26,412)	(24,194)	(1,620)	(103,196)
Adjusted imbalance	16,991	10,662	138	14,770	11,421	1,173	55,155
Off balance sheet items							
Off balance sheet assets	3,877	5,995	1,151	1,258	2,578	156	15,015
Off balance sheet liabilities	24,945	22,015	1,280	6,967	13,514	688	69,409
Net off balance sheet items	(21,069)	(16,020)	(129)	(5,709)	(10,936)	(532)	(54,394)
Net currency imbalance on 31 December 2010	(4,078)	(5,358)	9	9,061	485	641	759

Inflation risk

47. The Bank is exposed to inflation risk since the value of CPI-indexed assets exceeds the value of CPI-indexed liabilities. The value of these assets and liabilities changes according to changes in the CPI at any given time and all changes in the CPI index affect profit and loss. On 30 June 2011 the CPI gap amounted to ISK 30.1bn (31 December 2010: ISK 25.1bn). Thus, a 1% increase in the index would have a positive impact on the profit and loss account to the amount of ISK 301m in profit and a 1% decrease would result in a corresponding loss, other risk factors held constant.

Amounts are in ISK million

Capital management

48. Icelandic capital adequacy rules are based on the EU capital requirements directives (CRD). The capital adequacy rules require an absolute minimum capital level of 8% of risk weighted assets.

As part of the conditions for granting the Bank an operating license as a financial undertaking, the Icelandic Financial Supervisory Authority (FME) requires the Bank to maintain a minimum Core Tier 1 ratio of 12% of risk weighted assets and a total capital ratio, allowing for subordinated Tier 2 debt, of 16%.

The Bank's regulatory capital calculations for credit risk and market risk are based on the standardised approach and the capital calculations for operational risk are based on the basic indicator approach. Market risk exposure for currency risk is based on the adjusted currency imbalance described in note 46.

The table below shows the capital base, risk weighted assets and capital ratios of the Bank at 30 June 2011 and 31 December 2010.

	30.6.2011	31.12.2010
Tier 1 capital		
Ordinary share capital	10,000	10,000
Share premium	55,000	55,000
Other reserves	2,538	2,498
Retained earnings	61,251	53,174
Minority interest	(9)	791
Tax assets	(201)	(283)
Intangible assets	(261)	(187)
Total Tier 1 capital	128,318	120,993
Tier 2 capital		
Qualifying subordinated liabilities	22,887	21,241
Total regulatory capital	151,205	142,234
Risk weighted assets		
- due to credit risk	453,457	440,586
- due to market risk:	8,311	14,766
Market risk, trading book	4,499	4,583
Currency risk foreign exchange	3,812	10,183
- due to operational risk	79,079	79,079
Total risk weighted assets	540,847	534,431
Capital ratios		
Tier 1 ratio	23.7%	22.6%
Total capital ratio	28.0%	26.6%

In 2010, the Bank did an assessment of its internal capital adequacy (ICAAP) and submitted its findings to the FME. Such an assessment is an integral part of the Bank's capital and risk management. Current capitalisation levels are well above the requirements of the ICAAP.

Amounts are in ISK million