Condensed Interim
Consolidated Financial Statements

30 June 2019

Kvika banki hf. • Borgartún 25 • 105 Reykjavík • Iceland • Reg. no. 540502-2930

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Endorsement and Statement
by the Board of Directors and the CEO

The Condensed Interim Consolidated Financial Statements of Kvika banki hf. ("Kvika" or the "Bank") for the period 1 January to 30 June 2019 have been prepared in accordance with International Accounting Standard IAS 34 Interim Financial Reporting as adopted by the European Union, and additional requirements in the Icelandic Financial Statement Act. The Condensed Interim Consolidated Financial Statements comprise Kvika and its subsidiaries (together the "Group").

Kvika is a specialized bank focusing on asset management and investment services. The Bank operates four business segments, Asset Management, Corporate Finance, Corporate Banking and Capital Markets. Kvika provides businesses, investors and individuals with comprehensive investment banking and asset management services, as well as selected banking services. Kvika's Asset Management has an established reputation and offers solutions covering all major asset classes, including fixed-income securities, equities, and alternative investments in both domestic and international markets.

Kvika's shares were admitted to trading on Nasdaq OMX Iceland's main market in March 2019. The Bank's annual general meeting was held at 14 March 2019. At the meeting, the shareholders of the Bank approved a dividend payment of approximately ISK 443 million, which was subsequently paid at 26 March 2019. Further, the shareholders approved a resolution permitting the Bank to purchase up to 10% of own shares subject to regulatory approvals. This authorisation applies until the next annual general meeting in 2020.

1H 2019: Strong results on the back of favourable market conditions

The Bank's results in the first half of 2019 were strong as had been indicated by a positive profit announcement published 14 July. Market conditions remained favourable in the second quarter, resulting in the profit from banking and asset managment operations being above budget.

In November 2018 Kvika acquired all issued shares of GAMMA Capital Management hf. ("GAMMA"), a licenced fund management company focusing on asset- and fund management with ISK 135 billion of assets under management and 22 employees. The completion of the acquisition was subject to approval from competition authorities which granted their approval 6 March 2019. Consequently the acquisition was finalised and the operations of GAMMA are included in the Group's Financial Statements from 1 March 2019. At the end of June 2019 Kvika had ISK 445 billion of assets under management, compared to ISK 291 billion at year end 2018.

According to the Condensed Interim Consolidated Statement of Financial Position, equity at the end of the period amounted to ISK 13,998 million (31.12.2018: ISK 12,970 million) and total assets amounted to ISK 114,703 million (31.12.2018: ISK 88,274 million).

The Group's net operating income during the period was ISK 4,165 million (1H 2018: ISK 3,037 million). Net interest income amounted to ISK 846 million (1H 2018: ISK 794 million). Net fee income amounted to ISK 2,912 million (1H 2018: ISK 1,916 million). Other operating income amounted to ISK 407 million (1H 2018: ISK 327 million). Administrative expenses during first half amounted to ISK 2,658 million (1H 2018: ISK 1,987 million).

Profit for the period amounted to ISK 1,455 million (1H 2018: ISK 1,023 million), corresponding to an annualised 23.2% return on equity based on the equity position at the beginning of the year adjusted for changes in share capital and transactions with treasury shares during the period.

The Group's total capital ratio at 30.06.2019 is 24.6% (31.12.2018: 25.1%). The Bank's minimum regulatory capital requirement based on Financial Supervisory Authority's Supervisory Review and Evaluation Process (SREP) is 14.5%. The minimum regulatory capital requirement including the additional capital requirements imposed following the implementation of CRD IV is 20.75% as at 30 June 2019.

The Bank maintains a strong liquidity position. The Bank's assets are liquid and its access to funding is good, reflected in ample liquidity position. At the end of June 2019 the Group's 30 day liquidity coverage ratio (LCR) was 193%, well above the minimum level of 100%.

Risk management

The Bank is exposed to various types of risk in its operations. The Bank enforces a risk management framework which is further structured and outlined in the Bank's risk policy guide and rules on risk management. Refer to notes 38-48 on analysis of exposure to various types of risk.

Endorsement and Statement
by the Board of Directors and the CEO

Statement by the Board of Directors and the CEO

To the best of our knowledge the Condensed Interim Consolidated Financial Statements of Kvika banki hf. for the period 1 January to 30 June 2019 comply with IAS 34 Interim Financial Reporting as adopted by the EU and additional requirements in the Icelandic Financial Statement Act, and give a true and fair view of the Group's assets, liabilities and financial position as at 30 June 2019 and the financial performance of the Group and changes of cash flows for the period 1 January to 30 June 2019.

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

The Board of Directors and the CEO of the Bank have today discussed the Condensed Interim Consolidated Financial Statements for the period 1 January to 30 June 2019, and confirm them by the means of their signatures.

Reykjavík, 29 August 2019.

Board of Directors

CEO

Review Report on Interim Financial Information

To the Board of Directors and Shareholders of Kvika banki hf.

We have reviewed the accompanying Condensed Consolidated Interim Statement of financial position of Kvika banki hf. and its subsidiaries (the "Bank") as of 30 June 2019 and the related Condensed Consolidated Interim Income Statement, Condensed Consolidated Interim Statement of Comprehensive Income, Condensed Consolidated Interim Statement of changes in equity and Condensed Consolidated Interim Statement of cash flows for the six-month period then ended, and a summary of significant accounting policies and other explanatory notes.

Management's and the Board of directors Responsibility for the Financial Statements

The board of directors and management is responsible for the preparation and fair presentation of this interim financial information in accordance with International Financial Reporting Standards for Interim Financial Reporting, IAS 34, as adopted by the EU and additional requirements in the Icelandic Financial Statement Act.

Auditor's Responsibility

Our responsibility is to express a conclusion on this interim financial information based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements, ISRE 2410. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not give a true and fair view of the financial position of the Bank as at 30 June 2019, and of its financial performance and its cash flows for the six-month period then ended in accordance with International Financial Reporting Standards for Interim Financial Reporting, IAS 34, as adopted by the EU and additional requirements in the Icelandic Financial Statement Act.

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

Pursuant to the requirements of Paragraph 2 Article 104 of the Icelandic Act on Financial Statements No. 3/2006, we confirm to the best of our knowledge that the accompanying Endorsement and Statement by the Board of Directors and the CEO includes all information required by the Icelandic Act on Financial Statements that is not disclosed elsewhere in the Condensed Consolidated Interim Financial Statements.

Kópavogur, 29 August 2019.

Deloitte ehf.

Pálína Árnadóttir
State Authorized Public Accountant

Guðmundur Ingólfsson
State Authorized Public Accountant

Kvika Amounts are in ISK thousands

Condensed Interim Consolidated Income Statement
For the period 1 January 2019 to 30 June 2019

	Notes	6m 2019	6m 2018
Interest income		2,552,261	2,219,497
Interest expense		(1,706,552)	(1,425,662)
Net interest income	6	845,709	793,835
Fee and commission income		2,993,444	1,988,858
Fee and commission expense		(81,218)	(72,569)
Net fee and commission income	7	2,912,226	1,916,288
Net financial income	8	374,472	294,749
Share in loss of associates, net of income tax	24	(27,410)	(3,603)
Other operating income		60,435	35,742
Other operating income		407,498	326,888
Net operating income		4,165,433	3,037,011
Administrative expenses	10	(2,657,834)	(1,986,730)
Net impairment	12	22,143	5,462
Revaluation of contingent consideration		60,093	0
Profit before taxes		1,589,835	1,055,744
Income tax	13	(51,727)	(32,765)
Special tax on financial institutions	15	(83,400)	0
Profit for the period		1,454,708	1,022,978

	Notes	6m 2019	6m 2018
Attributable to the shareholders of Kvika banki hf.		1,456,665	1,012,738
Attributable to non-controlling interest	23	(1,957)	10,240
Profit for the period		1,454,708	1,022,978
Earnings per share	16		
Basic earnings per share (ISK per share)		0.79	0.55
Diluted earnings per share (ISK per share)		0.68	0.50

The notes on pages 11 to 41 are an integral part of these Condensed Interim Consolidated Financial Statements.

Kvika Amounts are in ISK thousands

Condensed Interim Consolidated Statement of Comprehensive Income

For the period 1 January 2019 to 30 June 2019

	Notes	6m 2019	6m 2018
Profit for the period		1,454,708	1,022,978
Translation of foreign operations			
Exchange difference on translation of foreign operations		13,733	295
Items that may be reclassified subsequently to profit and loss, net of tax		13,733	295
Total comprehensive income for the period		1,468,441	1,023,273

	Notes	6m 2019	6m 2018
Attributable to the shareholders of Kvika banki hf.		1,470,398	1,013,033
Attributable to non-controlling interest		(1,957)	10,240
Total comprehensive income for the period		1,468,441	1,023,273

The notes on pages 11 to 41 are an integral part of these Condensed Interim Consolidated Financial Statements.

Kvika Amounts are in ISK thousands

Condensed Interim Consolidated Statement of Financial Position

As at 30 June 2019

Assets	Notes	30.6.2019	31.12.2018
Cash and balances with Central Bank	17	30,784,218	21,339,185
Fixed income securities	18	4,804,198	5,127,335
Shares and other variable income securities	19	3,394,767	2,926,675
Securities used for hedging	20	29,565,108	21,526,794
Loans to customers	21	28,589,056	29,443,573
Derivatives	22	1,212,134	1,213,266
Investment in associates	24	771,646	774,832
Investment properties	25	979,685	950,000
Intangible assets	26	3,167,696	2,379,281
Property and equipment		591,638	42,894
Deferred tax assets		595,433	608,858
Other assets	27	10,247,277	1,941,070
Total assets		114,702,857	88,273,762

Liabilities			
Deposits from customers	28	58,003,384	47,893,959
Borrowings	29	21,962,389	15,634,648
Issued bills	30	3,932,665	3,577,718
Issued bonds	31	3,121,095	3,160,215
Subordinated liabilities	32	1,978,150	1,947,511
Short positions held for trading	33	1,136,951	805,334
Short positions used for hedging		435,176	0
Derivatives	22	1,483,041	593,934
Current tax liabilities		134,272	3,140
Deferred tax liabilities		389,061	76,980
Other liabilities	34	8,128,948	1,610,323
Total liabilities		100,705,131	75,303,763

Equity			
Share capital	35	1,844,996	1,844,996
Share premium		2,881,165	2,881,165
Option reserve		5,978	4,297
Warrants reserve	36	235,567	202,527
Deficit reduction reserve		3,103,697	3,103,697
Other reserves		1,710	(12,023)
Restricted retained earnings		592,424	506,896
Retained earnings		5,272,600	4,376,900
Total equity attributable to the shareholders of Kvika banki hf.		13,938,138	12,908,455
Non-controlling interest		59,587	61,544
Total equity		13,997,726	12,969,999
Total liabilities and equity		114,702,857	88,273,762

The notes on pages 11 to 41 are an integral part of these Condensed Interim Consolidated Financial Statements.

Kvika Amounts are in ISK thousands

Condensed Interim Consolidated Statement of Changes in Equity

For the period 1 January 2019 to 30 June 2019

1 January 2019 to 30 June 2019	Notes	Share capital	Share premium	Option reserve	Warrants reserve	Deficit reduction reserve	Trans-lation reserve	Restricted retained earnings	Retained earnings	Total share-holders' equity	Non-controlling interest	Total equity
Equity as at 1 January 2019		1,844,996	2,881,165	4,297	202,527	3,103,697	(12,023)	506,896	4,376,900	12,908,455	61,544	12,969,999
Impact of adopting IFRS 16									(32,637)	(32,637)		(32,637)
Restated opening balance under IFRS 16		1,844,996	2,881,165	4,297	202,527	3,103,697	(12,023)	506,896	4,344,263	12,875,818	61,544	12,937,362
Profit for the period									1,456,665	1,456,665	(1,957)	1,454,708
Translation of foreign operations												
Exchange difference on translation of foreign operations							13,733			13,733		13,733
Total comprehensive income for the period		0	0	0	0	0	13,733	0	1,456,665	1,470,398	(1,957)	1,468,441
Restricted retained earnings								85,529	(85,529)	0		0
Transactions with owners of the Bank												
Dividend paid to shareholders									(442,799)	(442,799)		(442,799)
Stock options				1,681						1,681		1,681
Warrants sold					33,040					33,040		33,040
Equity as at 30 June 2019		1,844,996	2,881,165	5,978	235,567	3,103,697	1,710	592,424	5,272,600	13,938,138	59,587	13,997,726

The notes on pages 11 to 41 are an integral part of these Condensed Interim Consolidated Financial Statements

Amounts are in ISK thousands

Condensed Interim Consolidated Statement of Changes in Equity
For the period 1 January 2018 to 30 June 2018

1 January 2018 to 30 June 2018	Notes	Share capital	Share premium	Option reserve	Warrants reserve	Deficit reduction reserve	Trans-lation reserve	Restricted retained earnings	Retained earnings	Total share-holders' equity	Non-controlling interest	Total equity
Equity as at 1 January 2018		1,805,060	2,722,583	903	207,048	3,103,697	(21,722)	254,844	2,858,439	10,930,854	51,423	10,982,276
Impact of adopting IFRS 9									28,709	28,709		28,709
Restated opening balance under IFRS 9		1,805,060	2,722,583	903	207,048	3,103,697	(21,722)	254,844	2,887,148	10,959,563	51,423	11,010,985
Profit for the period									1,012,738	1,012,738	10,240	1,022,978
Translation of foreign operations												
Exchange difference on translation of foreign operations							295			295		295
Reclassified to profit and loss on sale of subsidiaries							0			0		0
Total comprehensive income for the period		0	0	0	0	0	295	0	1,012,738	1,013,033	10,240	1,023,273
Restricted retained earnings								109,208	(109,208)	0		0
Transactions with owners of the Bank												
Capital increase		29,936	96,327		(2,509)					123,754		123,754
Transactions with own shares		10,000	60,242							70,242		70,242
Stock options				1,685						1,685		1,685
Equity as at 30 June 2018		1,844,996	2,879,153	2,588	204,539	3,103,697	(21,426)	364,053	3,790,678	12,168,277	61,663	12,229,940

The notes on pages 11 to 41 are an integral part of these Condensed Interim Consolidated Financial Statements

Kvika Amounts are in ISK thousands

Condensed Interim Consolidated Statement of Cash Flows
For the period 1 January 2019 to 30 June 2019

Cash flows from operating activities	**Notes**	**6m 2019**	**6m 2018**
Profit for the period		1,454,708	1,022,978
Adjustments for:			
Indexation and exchange rate difference		648,415	437,804
Share in loss (profit) of associates, net of income tax	24	27,410	3,603
Depreciation and amortisation		63,603	11,441
Net interest income	6	(845,709)	(793,835)
Net impairment		(22,143)	(5,462)
Income tax		135,127	32,765
Other adjustments		(58,028)	(5,491)
		1,403,383	703,802
Changes in:			
Fixed income securities		56,058	640,058
Shares and other variable income securities		(51,030)	175,455
Securities used for hedging		(8,038,314)	(4,016,178)
Loans to customers		1,011,082	(1,451,159)
Derivatives - assets		1,132	(89,590)
Deferred tax assets and tax liabilities		(113,544)	(12,872)
Other assets		(5,819,431)	(5,165,128)
Deposits from customers		9,620,158	11,813,438
Short positions		766,793	(279,498)
Derivatives - liabilities		889,107	191,687
Other liabilities		5,134,214	4,440,307
		3,456,224	6,246,521
Interest received		2,436,732	2,145,581
Interest paid		(1,183,479)	(891,651)
Net cash from operating activities		6,112,860	8,204,253
Cash flows from investing activities			
Net proceeds from the sale of investment properties		0	160,000
Acquisition of intangible assets	26	(101,227)	(39,567)
Acquisition of property and equipment		(54,951)	(3,893)
Proceeds from the sale of property and equipment		0	6,201
Dividend from assoiciates		3,750	3,750
Acquisition of subsidiary, net of cash		(892,174)	0
Net investment in associates		19,227	0
Proceeds from the sale of assets classified as held for sale		0	11,700
Net cash (to) from investing activities		(1,025,375)	138,191
Cash flows from financing activities			
Borrowings		5,128,787	7,958,341
Issued bills		354,947	(388,696)
Issued bonds		0	1,655,637
Subordinated liabilities		0	600,000
Increase (decrease) in warrants		33,040	(2,509)
Dividend paid to shareholders		(442,799)	0
Treasury share transactions		0	196,506
Net cash from financing activities		5,073,975	10,019,280
Net increase in cash and balances with Central Bank		10,161,460	18,361,723
Cash and balances with Central Bank at the beginning of the year	17	21,339,185	20,493,739
Change in cash and cash equivalents due to acquisition of subsidiary		8,016	0
Effects of exchange rate fluctuations on cash and balances with Central Bank		(724,442)	(403,553)
Cash and balances with Central Bank at the end of the period	17	30,784,218	38,451,909

Investing and financing activities not affecting cash flows due to a acquisitions, refer to note 5

Assets and liabilities acquired from GAMMA Capital Management hf.		1,090,717	0

The notes on pages 11 to 41 are an integral part of these Condensed Interim Consolidated Financial Statements.

Notes to the Condensed Interim Consolidated Financial Statements

Notes to the Condensed Interim Consolidated Financial Statements

General information

1. Reporting entity

Kvika banki hf. ("Kvika" or the "Bank") is a limited liability company incorporated and domiciled in Iceland, with its registered office at Borgartún 25, Reykjavík. The Bank operates as a bank based on Act No. 161/2002, on Financial Undertakings, and is supervised by the Financial Supervisory Authority of Iceland.

The Condensed Interim Consolidated Financial Statements for the period ended 30 June 2019 comprise Kvika banki hf. and its subsidiaries (together referred to as the Group). Kvika is a specialized bank focusing on asset management and investment services. The Bank operates four business segments, Asset Management, Corporate Finance, Corporate Banking and Capital Markets. Kvika provides businesses, investors and individuals with comprehensive investment banking and asset management services as well as selected banking services.

The Condensed Interim Consolidated Financial Statements were approved and authorised for issue by the Board of Directors and the CEO on 29 August 2019.

2. Basis of preparation

a. Statement of compliance

The Condensed Interim Consolidated Financial Statements have been prepared in accordance with International Accounting Standard IAS 34 Interim Financial Reporting, as adopted by the European Union and additional requirements in the Icelandic Financial Statement Act. The Condensed Interim Consolidated Financial Statements are also prepared in accordance with Icelandic laws on financial statements.

The Condensed Interim Consolidated Financial Statements do not include all of the information required for full Consolidated Financial Statements, and should be read in conjunction with the Bank's Consolidated Financial Statements for the financial year ending 31 December 2018, which are available at www.kvika.is.

b. Basis of measurement

The Condensed Interim Consolidated Financial Statements have been prepared using the historical cost basis except for the following:
- fixed income securities are measured at fair value;
- shares and other variable income securities are measured at fair value;
- securities used for hedging are measured at fair value;
- loans to customers which are measured at fair value;
- derivatives are measured at fair value;
- investment properties are measured at fair value;
- contingent consideration is measured at fair value;
- short positions are measured at fair value; and
- assets classified as held for sale are measured at the lower of cost or fair value less cost to sell.

c. Functional and presentation currency

The Condensed Interim Consolidated Financial Statements are prepared in Icelandic Krona (ISK), which is the Bank's functional currency. All financial information has been rounded to the nearest thousand, unless otherwise stated.
The Group's assets and liabilities which are denominated in other currency than ISK are translated to ISK using the exchange rate as at the end of day 30 June 2019.

d. Going concern

The Bank's management has assessed the Group's ability to continue as a going concern and are satisfied that the Group has the resources to continue its operations.

e. Estimates and judgements

The preparation of interim financial statements in accordance with IFRSs 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.

The estimates and underlying assumptions are based on historical result and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period and future periods if the revision affects both current and future periods.

Information about areas of estimation uncertainty and critical judgements made by management in applying accounting policies that can have a significant effect on the amounts recognised in the Condensed Interim Consolidated Financial Statements, is provided in the Consolidated Financial Statements as at and for the year ended 31 December 2018

f. Relevance and importance of notes to the reader

In order to enhance the informational value of the Financial Statements, the notes are evaluated based on relevance and importance for the reader. This can result in information, that has been evaluated as neither important or relevant for the reader, not being presented in the notes.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

3. Significant accounting policies

The accounting policies applied in the Condensed Interim Consolidated Financial Statements are consistent with those applied in the Consolidated Financial Statements as at and for the year ended 31 December 2018, except for IFRS 16 Leases, which became effective on 1 January 2019. Refer to note 4 for more information on the impact of IFRS 16 Leases on the Group's accounting policies.

4. Changes in accounting policies

The Group has initially adopted IFRS 16 Leases from 1 January 2019. The Group has not early adopted any standards, interpretations or amendments that have been issued but are not effective. The Group has applied IFRS 16 using the modified retrospective approach, with no restatement of comparative information.

At the commencement date of a lease, the Group recognizes a liability to make lease payments and an asset representing the right to use the underlying asset during the lease term. The Group will elect to use the exemptions authorized by the standard on lease contracts for which the lease terms ends within 12 months as of the date of initial application, and lease contracts for which the underlying asset is of low value. Interest expense on the lease liability and the depreciation expense on the right-of-use asset are recognized separately in the Condensed Interim Consolidated Financial Statements.

5. Acquisition of GAMMA Capital Management hf.

On 19 November 2018, the Bank and the shareholders of GAMMA Capital Management hf. ("GAMMA") signed a sales and purchase agreement regarding the Bank's acquisition of all the share capital in GAMMA. The transaction was subject to approval from regulatory authorities and approval from Kvika's shareholders. In early March 2019 the final conditions were fulfilled and is GAMMA and its subsidiaries a part of the Group and the Consolidated Financial Statements from 1 March 2019. The purchase price is composed of several items, some of which are conditional based on certain conditions, such as the amount of performance related fees which GAMMA will receive over a certain period. Most of the purchase price will be paid by cash although a part of it, about ISK 499 million, will be paid by buying unit shares from GAMMA and delivering them to the sellers. At the acquisition date, the purchase price was estimated to amount to ISK 2,542 million. As at 30 June 2019 ISK 1,392 million have been paid and ISK 1,097 million are recognised as a contingent consideration on the Group's Condensed Interim Consolidated Statement of Financial Position. The amount of the contingent consideration is subject to change and fair value changes will be recognised through the Consolidated Income Statement.

A part of the purchase price, ISK 200 million, will be deposited into an escrow account to be used to offset possible claims that the Bank might set forth during the three years following the acquisition date. After that time, these funds will be paid to the former owners of GAMMA. In 2018, the Bank incurred transaction costs and costs related to the acquisition amounting to ISK 44 million.

In accordance with IFRS 3, Business Combinations, the purchase price of GAMMA was allocated to identifiable assets and liabilities acquired. The following table summarises the recognised amounts of assets and liabilities acquired by the Group at the date of the acquisition. Assets acquired from GAMMA and its subsidiaries were recognised at the fair value amount of ISK 3,689 million. The liabilities assumed from GAMMA and its subsidiaries were recognised at the fair value amount of ISK 1,846 million. The purchase price allocation of GAMMA, as outlined below, is a preliminary assessment and will be finalised before end of February 2020.

Identifiable assets acquired and liabilities assumed

Assets	Fair value
Cash and balances with Central Bank	8,016
Shares and other variable income securities	916,396
Property and equipment	545,223
Other assets	2,219,698
Total	3,689,334
Liabilities	
Borrowings	1,156,667
Deferred tax liabilities	387,323
Other liabilities	302,387
Total	1,846,377
Non-controlling interest	0
Total identifiable net assets	1,842,958
Goodwill on acquisition	699,360
Acquisition price	2,542,318

Other assets are mostly comprised of receivables, such as fund management fees. Out of the ISK 2,220 million which are recognised as other assets, ISK 1,612 relate to long-term performance related fees from the management of certain closed-end funds and ISK 468 million relate to accrued fees from funds which are managed by GAMMA. At the acquisition date, it was management's opinion that there is no indication that these receivables will not be collected in full. Certain assets that are owned by GAMMA form a part of the estimated book value of the contingent consideration as the purchase price will change if the book value of those assets changes. As a result, a large part of the economical risk of those assets lies with the former shareholders and not the Group.

As the acquisition took place in March, the operating figures for the period are mostly composed of figures related to the Group before the acquisition of GAMMA. If the acquisition had occurred on 1 January 2019, it is estimated that the consolidated revenue would have been ISK 4,269 million and the consolidated profit for the year would have been ISK 1,364 million.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

Income statement

6. Net interest income

Interest income is specified as follows:

	6m 2019	6m 2018
Cash and balances with Central Bank	403,691	513,249
Derivatives	776,872	506,840
Loans to customers	1,308,982	1,170,961
Other interest income	62,716	28,448
Total	2,552,261	2,219,497

Interest expense is specified as follows:

	6m 2019	6m 2018
Deposits from customers	806,562	669,202
Borrowings	549,024	507,529
Issued bills	93,906	93,991
Issued bonds	90,521	53,341
Subordinated liabilities	94,934	51,082
Derivatives	6,490	3,549
Other interest expense*	65,115	46,970
Total	1,706,552	1,425,662

* Thereof are lease liabilities' interest expense amounting to ISK 9 million

Total interest income recognised in respect of financial assets not carried at fair value through profit or loss amounts to ISK 1,692 million (6m 2018: ISK 1,649 million). Total interest expense recognised in respect of financial liabilities not carried at fair value through profit or loss amounts to ISK 1,700 million (6m 2018: ISK 1,422 million).

7. Net fee and commission income

Fee income and expenses are presented on a net fee basis, as presented in internal reporting to management for decision making purposes, and broken down by business segments. The business segments are representative of the nature and types of activity from which the Group generates fee income from. A description of each business segment is provided in note 52.

Net fee and commission income by business segment	6m 2019	6m 2018
Corporate Banking	366,332	323,610
Corporate Finance	183,374	280,635
Capital Markets	452,311	314,365
Proprietary trading and Treasury	59,578	24,900
Asset Management	1,926,005	1,043,404
Support functions and eliminations	(75,374)	(70,625)
Total	2,912,226	1,916,288

8. Net financial income

Net financial income is specified as follows:

	6m 2019	6m 2018
Net gain on financial assets and financial liabilities mandatorily measured at fair value through profit or loss		
Fixed income securities	362	125,781
Shares and other variable income securities	402,430	85,737
Derivatives	(48,914)	20,707
Loans to customers	65,129	46,883
Foreign currency exchange difference	(44,535)	15,641
Total	374,472	294,749

9. Foreign currency exchange difference

Foreign currency exchange difference is specified as follows:

	6m 2019	6m 2018
Gain on financial instruments at fair value through profit and loss	325,719	106,378
Loss on other financial instruments	(370,254)	(90,737)
Total	(44,535)	15,641

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

10. Administrative expenses

Administrative expenses are specified as follows:	6m 2019	6m 2018
Salaries and related expenses	1,749,729	1,350,926
Other operating expenses	797,645	574,815
Depositors' and Investors' Guarantee Fund contributions	46,857	49,548
Depreciation and amortisation	45,932	11,441
Depreciation of right of use asset	17,671	0
Total	2,657,834	1,986,730

11. Salaries and related expenses

Salaries and related expenses are specified as follows:	6m 2019	6m 2018
Salaries	1,219,502	1,064,278
Performance based payments excluding share-based payments	145,103	1,573
Share-based payment expenses	1,681	1,685
Pension fund contributions	155,911	135,434
Tax on financial activity	93,289	62,351
Other salary related expenses	134,243	85,605
Total	1,749,729	1,350,926
Average number of full time employees during the period	125	110
Total number of full time employees at the end of the period	124	112

According to Act No. 165/2011, passed in 2011, banks and other financial institutions providing VAT exempt services, must pay a tax based on salary payments, called tax on financial activity. The current tax rate is 5.50% (2018: 5.50%).

The amount of performance based payments that has been expensed is based on the results for 1H 2019, the Group‘s 2019 budget and the guidelines on performance based payments set forth in the Bank’s remuneration policy. The performance based payments have not been allocated to any employees or business segments and are subject to approval by the Board of Directors.

12. Net impairment

	6m 2019	6m 2018
Net change in impairment of loans	(33,211)	(22,056)
Net change in impairment of other assets	7,371	(1,977)
Net change in impairment of loan commitments, guarantees and unused credit facilities	3,696	18,571
Total	(22,143)	(5,462)

13. Income tax

The Bank and most of its subsidiaries will not pay income tax on its profit for 2019 due to the fact that it has a tax loss carry forward that offsets the calculated income tax. At year end 2018, the tax loss carry forward of the Group amounted to ISK 104 billion. A substantial part of the tax loss carry forward is utilisable until end of year 2019. Management is of the opinion that the Group's operations in the years to come will result in taxable results which will be offset with the tax loss carry forward. The Group has therefore recognised a part of the tax loss carry forward as a deferred tax asset in the consolidated statement of financial position. The deferred tax asset is recognised only to the extent that it is probable to be utilisable against future taxable profits.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

14. Special tax on financial activity

The special tax on financial activity is an additional income tax which becomes effective when the income tax base exceeds ISK 1,000 million. It is levied on the same entities as the tax on financial activity according to Act No. 90/2003. The tax rate is set at 6.0% (2018: 6.0%) and the tax is not a deductible expense for income tax purposes. The tax is presented separately in the consolidated income statement.

15. Special tax on financial institutions

According to Act No. 155/2010 on Special Tax on Financial Institutions, certain types of financial institutions, including banks, must pay annually a tax based on the carrying amount of their liabilities as determined for tax purposes in excess of ISK 50 billion at year-end. The tax rate is set at 0.376% (2018: 0.376%) and the tax is not a deductible expense for income tax purposes. The tax is presented separately in the consolidated income statement. In 2019 the Bank began expensing this tax proportionally during the year instead of expensing the whole amount at the end of the year.

16. Earnings per share

The calculation of basic earnings per share is based on earnings attributable to shareholders and a weighted average number of shares outstanding during the period. The diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Bank has issued warrants and stock options that have a dilutive effect.

	6m 2019	**6m 2018**
Net earnings attributable to equity holders of the Bank	1,456,665	1,012,738
Weighted average number of outstanding shares	1,844,996	1,825,808
Adjustments for warrants and stock options	287,495	199,989
Total	2,132,491	2,025,797
Basic earnings per share (ISK)	0.79	0.55
Diluted earnings per share (ISK)	0.68	0.50

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

Statement of Financial Position

17. Cash and balances with Central Bank

Cash and balances with Central Bank are specified as follows:

	30.6.2019	31.12.2018
Deposits with Central Bank	18,247,791	8,934,131
Cash on hand	12,516	9,114
Balances with banks	5,046,532	6,903,004
Foreign treasury bills	4,334,435	3,472,741
Included in cash and cash equivalents	27,641,273	19,318,990
Restricted balances with Central Bank - average maintenance level	853,543	708,656
Restricted balances with Central Bank - fixed reserve requirement	853,543	708,656
Receivables from Central Bank	1,435,858	602,882
Total	30,784,218	21,339,185

The Bank holds mandatory reserve deposit accounts with the Central Bank of Iceland in compliance with the Central Bank's Rules on Minimum Reserve Requirements No. 585/2018. Under these rules the reserve requirement is divided into two parts: a fixed reserve requirement bearing no interest and an average maintenance level requirement bearing the same interest as that on deposit-taking institutions' current accounts with the Central Bank. The mandatory reserve deposit with the Central Bank and the receivables from the Central Bank are not available for the Group to use in its daily operations.

18. Fixed income securities

Fixed income securities are specified as follows:

Mandatorily measured at fair value through profit or loss	30.6.2019	31.12.2018
Listed government bonds and bonds with government guarantees	473,874	1,841,982
Listed bonds	3,934,111	3,150,409
Unlisted bonds	396,213	134,944
Total	4,804,198	5,127,335

19. Shares and other variable income securities

Shares and other variable income securities are specified as follows:

Mandatorily measured at fair value through profit or loss	30.6.2019	31.12.2018
Listed shares	837,917	751,470
Unlisted shares	1,902,998	1,391,018
Unlisted unit shares	653,853	784,187
Total	3,394,767	2,926,675

20. Securities used for hedging

Securities used for hedging are specified as follows:

	30.6.2019	31.12.2018
Listed government bonds and bonds with government guarantees	7,023,883	7,625,469
Listed bonds	8,084,519	4,487,698
Listed shares	14,321,132	9,395,761
Unlisted unit shares	135,573	17,866
Total	29,565,108	21,526,794

21. Loans to customers

The breakdown of the loan portfolio by individuals and corporates is specified as follows:

	Individuals		**Corporates**		**Total**	
30.6.2019	Gross carrying amount	Book value	Gross carrying amount	Book value	Gross carrying amount	Book value
Loans to customers at amortised cost	4,141,660	4,115,679	22,430,089	22,268,361	26,571,749	26,384,040
Loans to customers at fair value through profit or loss	0	0	2,205,016	2,205,016	2,205,016	2,205,016
Total	4,141,660	4,115,679	24,635,105	24,473,377	28,776,765	28,589,056

	Individuals		**Corporates**		**Total**	
31.12.2018	Gross carrying amount	Book value	Gross carrying amount	Book value	Gross carrying amount	Book value
Loans to customers at amortised cost	5,407,411	5,364,291	22,096,616	21,918,759	27,504,028	27,283,050
Loans to customers at fair value through profit or loss	0	0	2,160,522	2,160,522	2,160,522	2,160,522
Total	5,407,411	5,364,291	24,257,139	24,079,282	29,664,550	29,443,573

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

22. Derivatives

Derivatives are specified as follows:

30.6.2019	Notional Assets	Notional Liabilities	Carrying value Assets	Carrying value Liabilities
Interest rate derivatives	4,347,864	4,105,832	242,031	0
Currency forwards	1,630,921	1,612,816	19,626	1,520
Bond and equity total return swaps	31,070,895	31,584,166	806,304	1,337,348
Equity options	11,760	11,760	144,173	144,173
Total	37,061,439	37,314,574	1,212,134	1,483,041

31.12.2018	Notional Assets	Notional Liabilities	Carrying value Assets	Carrying value Liabilities
Interest rate derivatives	4,803,789	4,607,104	196,684	0
Currency forwards	400,192	413,565		13,372
Bond and equity total return swaps	22,983,930	22,547,910	966,627	530,607
Equity options	7,900	7,900	49,955	49,955
Total	28,195,811	27,576,479	1,213,266	593,934

23. Group entities

The main subsidiaries held directly or indirectly by the Group are listed in the table below.

Entity	Nature of operations	Domicile	Share 30.6.2019	Share 31.12.2018
FÍ Fasteignafélag GP ehf.	Real estate fund management	Iceland	100%	100%
GAMMA Capital Management hf.	Fund management	Iceland	100%	-
Júpíter rekstrarfélag hf.	Fund management	Iceland	100%	100%
M-Investments ehf.	Holding company	Iceland	100%	100%
Netgíró reikningar ehf.	Holding company	Iceland	100%	100%
Netgíró lán ehf.	Holding company	Iceland	100%	100%
Netgíró lán II ehf.	Holding company	Iceland	100%	100%
Rafklettur ehf.	Holding company	Iceland	100%	100%
Rekstrarfélag Virðingar hf.	Fund management	Iceland	100%	100%
AC GP 3 ehf.	Fund management	Iceland	80%	80%
Kvika Securities ltd.	Business consultancy services	UK	100%	100%

24. Investment in associates

a. Investment in associates is accounted for using the equity method and is specified as follows:

Entity	Nature of operations	Domicile	Share 30.6.2019	Share 31.12.2018
Akta sjóðir hf.	Fund management	Iceland	34%	49%
Kjölfesta GP ehf.	Holding company	Iceland	50%	50%
KORTA hf.	Payment Institution	Iceland	45%	47%
Gláma fjárfestingar slhf.	Holding company	Iceland	24%	-

The Group does not consider its associates material, neither individually nor as a group.

b. Changes in investments in associates are specified as follows:

	30.6.2019	31.12.2018
Balance at the beginning of the year	774,832	676,610
Acquisition of shares in associates	47,201	408,671
Dividend received	(3,750)	(7,500)
Disposal of shares in associates	(19,227)	0
Share in loss of associates, net of income tax	(27,410)	(302,949)
Total	771,646	774,832

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

25. Investment properties

Investment properties are specified as follows:

	30.6.2019	31.12.2018
Balance at year beginning	950,000	953,874
Acquisitions	29,685	31,544
Disposal	0	(150,000)
Revaluation on investment properties	0	114,582
Total	979,685	950,000

26. Intangible assets

Intangible assets are specified as follows:

30.6.2019	Goodwill	Software	Other	Total
Balance as at 1 January 2019	2,244,521	118,428	16,332	2,379,281
Acquisitions	0	49,894	51,333	101,227
Additions through a business combination	699,360	0	0	699,360
Amortisation	0	(6,488)	(5,684)	(12,172)
Balance as at 30 June 2019	2,943,881	161,834	61,981	3,167,696
Gross carrying amount	2,943,881	95,336	48,800	3,088,017
Accumulated amortisation and impairment losses	0	66,498	13,181	79,679
Balance as at 30 June 2019	2,943,881	161,834	61,981	3,167,696

31.12.2018	Goodwill	Software	Other	Total
Balance as at 1 January 2018	2,244,521	23,959	15,860	2,284,340
Acquisitions	0	98,952	5,352	104,304
Amortisation	0	(4,482)	(4,880)	(9,362)
Balance as at 31 December 2018	2,244,521	118,428	16,332	2,379,281
Gross carrying amount	2,244,521	45,442	48,800	94,242
Accumulated amortisation and impairment losses	0	(21,484)	(32,940)	(54,424)
Balance as at 1 January 2018	2,244,521	23,959	15,860	2,284,340
Gross carrying amount	2,244,521	38,924	48,800	87,724
Accumulated amortisation and impairment losses	0	79,505	(32,468)	47,036
Balance as at 31 December 2018	2,244,521	118,428	16,332	2,379,281

27. Other assets

Other assets are specified as follows:

	30.6.2019	31.12.2018
Unsettled transactions	5,477,419	120,563
Accounts receivable	3,815,687	1,283,215
Right of use asset	329,412	0
Sundry assets	624,759	537,292
Total	10,247,277	1,941,070

28. Deposits from customers

Deposits from customers are specified as follows:

	30.6.2019	31.12.2018
Demand deposits	44,011,451	32,463,907
Time deposits	13,991,933	15,430,052
Total	58,003,384	47,893,959

29. Borrowings

Borrowings are specified as follows:

	30.6.2019	31.12.2018
Loans from credit institutions	1,413,446	1,215,343
Money market deposits	20,548,943	14,407,558
Other borrowings	0	11,747
Total	21,962,389	15,634,648

Money market deposits typically have a principal of ISK 5-500 million and maturity between 1 day and 6 months and pay fixed interest rates.

The Bank has not had any defaults of principal, interest or other breaches with respect to its debt issued and other borrowed funds.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

30. Issued bills

Issued bills are specified as follows:

	30.6.2019	31.12.2018
Issued bills	3,932,665	3,577,718
Total	3,932,665	3,577,718

31. Issued bonds

Issued bonds are specified as follows:

Currency, nominal value	First issued	Maturity	Maturity type	Terms of interest	30.6.2019	31.12.2018
KVB 17 02, ISK 2,160 million	2017	2020	At maturity	Floating, 1 month REIBOR + 1.25%	1,876,780	1,963,336
Total					1,876,780	1,963,336
Unlisted senior unsecured bonds, total					1,244,315	1,196,879
Total					3,121,095	3,160,215

Unlisted senior unsecured bonds are composed of KVB 17 01, KVB 18 01, KVB 18 03 and KVB 18 04 which were issued in 2017 and 2018 and mature in 2019, 2020 and 2021 respectively. For further information on the bonds, refer to the issue descriptions which are available on Nasdaq CSD Iceland's website.

32. Subordinated liabilities

Subordinated liabilities:

Currency, nominal value	First issued	Maturity	Maturity type	Terms of interest	30.6.2019	31.12.2018
KVB 15 01, ISK 1,000 million	2015	2025	At maturity	CPI-Indexed, fixed 5.50%	1,103,988	1,093,162
KVB 18 02, ISK 800 million	2018	2028	At maturity	CPI-Indexed, fixed 7.50%	874,163	854,350
Total					1,978,150	1,947,511

At the interest payment date in the year 2020 for KVB 15 01, the annual interest rate increases from 5.50% p.a. to 7.50% p.a. At the same date, the Group has the right to repay the subordinated bond and on any subsequent interest payment dates until maturity.

At the interest payment date in the year 2023 for KVB 18 02, the Group has the right to repay the subordinated bond and on any subsequent interest payment dates until maturity.

Subordinated liabilities are financial liabilities in the form of subordinated capital which, in case of the Group's voluntary or compulsory winding-up, will not be repaid until after the claims of ordinary creditors have been met. In the calculation of the capital ratio, they are included within Tier 2 and are a part of the equity base. The amount eligible for Tier 2 capital treatment is amortised on a straight-line basis over the final 5 years to maturity or up to 20% a year. The Group may only retire subordinated liabilities with the permission of the Icelandic Financial Supervisory Authority.

33. Short positions held for trading

Short positions held for trading are specified as follows:

	30.6.2019	31.12.2018
Listed government bonds and bonds with government guarantees	673,886	569,471
Listed bonds	463,065	235,863
Total	1,136,951	805,334

34. Other liabilities

Other liabilities are specified as follows:

	30.6.2019	31.12.2018
Unsettled transactions	4,911,717	186,794
Expected credit loss allowance for loan commitments, guarantees and unused credit facilities	21,135	17,439
Accounts payable and accrued expenses	344,703	250,522
Special taxes on financial institutions and financial activities	233,735	150,336
Withholding taxes	334,179	461,153
Salaries and salary related expenses	706,456	313,274
Lease liability	362,987	0
Contingent consideration	1,090,717	0
Other liabilities	123,318	230,806
Total	8,128,948	1,610,323

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

35. Equity

a. Share capital

The nominal value of shares issued by the Bank is ISK 1 per share. All currently issued shares have a nominal value of ISK 1 per share, and are fully paid. The holders of shares are entitled to receive dividends as approved by the general meeting and are entitled to one vote per nominal value of ISK 1 at shareholders' meetings. Reference is made to the Bank's Articles of Association for more information about the share capital.

	30.6.2019	31.12.2018
Share capital according to the Bank's Articles of Association	1,844,996	1,844,996
Nominal amount of treasury shares	0	0
Authorised but not issued shares	938,635	838,635

b. Changes made to the nominal amount of share capital

No changes were made to the Bank's share capital during the period from 1 January to 30 June 2019.

c. Share capital increase authorisations

According to the Bank's Articles of Association dated 17 April 2019, the Board of Directors is authorised to increase the share capital of the Bank by up to ISK 100 million through subscription for new shares. This authorisation is based on temporary provision I to the Articles of Association and is valid until 15 March 2022.

The Board of Directors is furthermore authorised to increase the share capital of the Bank in stages by up to ISK 50,000,000 in nominal value, for the purposes of fulfilling share option agreements in accordance with the Bank's share incentive scheme. This authorisation is based on temporary provision I, cf. paragraph B of the provision, to the Articles of Association and is valid until 30 November 2021.

The Board of Directors is, according to temporary provision II to the Bank‘s Articles of Association, authorised to issue warrants for 100 million new shares until the Bank‘s annual general meeting in 2020. The Board is furthermore, until 14 March 2024, authorised to increase share capital to serve warrants issued under the aforementioned authorisation.

Temporary provision III to the Articles of Association moreover authorises the Board of Directors to issue new share capital in the maximum amount of ISK 58,635,392 nominal value, to serve warrants which have been issued. This authorisation is valid until 31 December 2019.

Temporary provision IV to the Articles of Association authorises the Board of Directors to issue warrants and increase the share capital accordingly. According to section A of temporary provision IV the Board of Directors is authorised to increase share capital by up to ISK 480 million to serve issued warrants. According to section B of temporary provision IV the Board of Directors is furthermore granted a conditioned authorisation to increase the share capital by an additional amount of ISK 200 million to serve issued warrants. The authorisation under section B of temporary provision IV is directly linked to the Board of Directors' authorisation under section A of temporary provision I.

The aforementioned authorisation under section B of temporary provision IV currently stands at ISK 150 million. However, should the Board of Directors utilise its authorisation according to section A of temporary provision I and increase the Bank's share capital by ISK 100 million, the authorisation under section B of temporary provision IV will increase from ISK 150 million to ISK 200 million, as stipulated in the provision. The Board of Directors' authorisation under temporary provision IV to increase share capital thus currently totals ISK 630 million but can increase to ISK 680 million by the usage by the Board of Directors of its authorisation pursuant to section A of temporary provision I. This authorisation is valid until 31 December 2022.

A copy of the Bank's Articles of Association, including the temporary provisions, is available on the Bank's website, www.kvika.is, reference is made to them for more information.

36. Warrants

The Bank has issued warrants for shares in the total nominal amount of ISK 722,986,137 as at 30 June 2019. The number of owners of these warrants is 122 and they purchased the warrants for a total consideration of ISK 235,567,528. The purchase price of the warrants was determined using market standard methodology and a valuation from an independent appraiser as applicable. Should the owners of the warrants exercise their warrants, the Bank is obliged to issue new shares and sell to the warrant owners at a predefined price, usually referred to as strike price. If all the warrants would be exercised, the Bank's share capital would increase to 2,567,982,445, and the newly issued shares would represent 28.2% of the Bank's total issued capital, post dilution.

Issue Date	Nominal amount	Purchase price of warrants	Annual increase of strike price	Strike price at expiry date	Exercise period
October 2016	58,486,138	11,793,759	5.0%	4.20	Until October 2019
September 2017	201,333,333	60,601,333	7.5%	6.64	Sept. 2019 - Sept. 2020
September 2017	201,333,333	60,601,333	7.5%	7.67	Sept. 2020 - Sept. 2022
September 2017	201,333,333	60,601,333	7.5%	7.67	Sept. 2021 - Sept. 2022
December 2017	7,333,333	2,471,333	7.5%	7.55	Dec. 2019 - Dec. 2020
December 2017	7,333,333	2,471,333	7.5%	8.73	Dec. 2020 - Dec. 2022
December 2017	7,333,333	2,471,333	7.5%	8.73	Dec. 2021 - Dec. 2022
May 2018	1,166,667	505,167	7.5%	9.25	Dec. 2019 - Dec. 2020
May 2018	1,166,667	505,167	7.5%	10.69	Dec. 2020 - Dec. 2022
May 2018	1,166,667	505,167	7.5%	10.69	Dec. 2021 - Dec. 2022
April 2019	17,500,000	16,520,000	7.5%	15.05	Dec. 2020 - Dec. 2022
April 2019	17,500,000	16,520,000	7.5%	15.05	Dec. 2021 - Dec. 2022
Total	722,986,137	235,567,258			

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

37. Capital adequacy ratio (CAD)

Equity at the end of the period was ISK 13,998 million (31.12.2018: 12,970 million), equivalent to 12.2% of total assets according to the statement of financial position (31.12.2018: 14.7%). The capital adequacy ratio of the Group, calculated in accordance with Article 84 of Act No. 161/2002 on Financial Undertakings, was 24.6% (31.12.2018: 25.1%). The minimum according to the Act is 8.0%. The ratio is calculated as follows:

Own funds	**30.6.2019**	**31.12.2018**
Total equity	13,997,726	12,969,999
Goodwill and intangibles	(3,167,696)	(2,379,281)
Shares in financial institutions	(88,440)	(172,206)
Subordinated fixed income securities	(93,154)	(54,595)
Deferred tax asset	(595,433)	(608,858)
Foreseeable dividends according to Dividend Policy	(362,469)	0
Common equity Tier 1 capital (CET 1)	9,690,533	9,755,059
Tier 2 capital	1,919,645	1,886,506
Total own funds	11,610,178	11,641,565
Risk weighted assets		
Credit risk	34,258,639	31,948,930
Market risk	2,823,752	4,474,728
Operational risk	10,019,764	10,019,764
Total Capital requirements	47,102,154	46,443,422
Capital adequacy ratio (CAD)	24.6%	25.1%
CET1 ratio	20.6%	21.0%
Capital adequacy ratio, without adjustment for foreseeable dividends	25.4%	25.1%
CET1 ratio, without adjustment for foreseeable dividends	21.3%	21.0%
Minimum Capital adequacy ratio requirement	14.5%	14.5%
Minimum CET 1 ratio requirement	14.4%	13.9%
Surplus own funds	4,773,738	4,907,430
Surplus CET 1	2,898,251	3,296,682

The Icelandic Financial Supervisory Authority (FME) supervises the Bank on a consolidated basis and, as such, receives information on the capital adequacy of, and sets capital requirements for, the Bank as a whole. 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.

Minimum capital requirement is based on the Bank's Internal Capital Adequacy Assessment Process (ICAAP) and is reviewed by the FME through the Supervisory Review and Evaluation Process (SREP). The Bank's minimum regulatory capital requirement, based on the SREP from 2017, is 14.5%. The minimum regulatory capital requirement including the additional capital buffer imposed following the implementation of CRD IV is 20.75% as at 30 June 2019.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

Risk management

38. Maximum exposure to credit risk

The maximum exposure to credit risk for on-balance sheet and off-balance sheet items, before taking into account any collateral held or other credit enhancements, is specified as follows:

30.6.2019	**Public entities**	**Financial institutions**	**Corporate customers**	**Individuals**	**30.6.2019**
Cash and balances with Central Bank	25,737,686	5,046,532			30,784,218
Fixed income securities	1,801,526	3,002,672			4,804,198
Loans to customers		10,616,123	13,831,300	4,141,633	28,589,056
Derivatives		648,954	523,077	40,103	1,212,134
Other assets	43,362	74,836	10,129,080		10,247,277
	27,582,574	19,389,118	24,483,457	4,181,735	75,636,884
Loan commitments		1,739,367	2,377,210	683,744	4,800,322
Financial guarantee contracts		157,500	716,011		873,511
Total	27,582,574	21,285,985	27,576,678	4,865,480	81,310,717

31.12.2018	**Public entities**	**Financial institutions**	**Corporate customers**	**Individuals**	**31.12.2018**
Cash and balances with Central Bank	14,436,181	6,903,004			21,339,185
Fixed income securities	2,829,688	1,968,174	329,473		5,127,335
Loans to customers		54,260	24,044,069	5,345,243	29,443,573
Derivatives		624,399	541,364	47,503	1,213,266
Other assets	23,517	56,377	1,766,389	94,786	1,941,070
	17,289,386	9,606,214	26,681,296	5,487,532	59,064,428
Loan commitments		255,329	2,818,631	388,975	3,462,935
Financial guarantee contracts		100,000	823,074		923,074
Total	17,289,386	9,961,542	30,323,000	5,876,508	63,450,436

39. Credit quality of financial assets

The tables below show financial assets subject to the impairment requirements of IFRS 9 broken down by credit quality bands where band i denotes the lowest and iv the highest credit risk. Assets serviced by debtors already recognised as being in default by the rating agency are shown outside credit quality bands. Assets measured at fair value through profit or loss are not subject to the impairment requirements of IFRS 9 but are nevertheless included in the tables in order to give a more complete picture of the credit quality of loans to customers and reconcile the tables to the carrying amount on the balance sheet. Exposures which are non-rated relate to Legal Entities not rated by rating agency or Individuals where individual rating has not been obtained. Probability of default for these exposures is based on average probability for similar exposures and is furthermore individually assessed by credit specialists.

a. Credit quality of financial assets by credit quality band is specified as follows:

30.6.2019

Loans to customers:	**Stage 1**	**Stage 2**	**Stage 3**	**FVTPL**	**Total**
Credit quality band I	15,526,713	486,035	56,816	725,046	16,794,610
Credit quality band II	3,285,099	24,409		724,863	4,034,370
Credit quality band III	990,171	708,642		108,712	1,807,525
Credit quality band IV	80,789	967,753		481,678	1,530,220
In default		0	121,650		121,650
Non-rated	4,323,631	41		164,717	4,488,390
Gross carrying amount	24,206,404	2,186,879	178,466	2,205,016	28,776,765
Expected credit loss	(112,762)	(33,616)	(41,331)		(187,709)
Book value	24,093,641	2,153,263	137,136	2,205,016	28,589,056

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

39. Credit quality of financial assets (cont.)

Loan commitments, guarantees and unused credit facilities:	Stage 1	Stage 2	Stage 3	FVTPL	Total
Credit quality band I	2,993,558	3,109			2,996,667
Credit quality band II	1,006,029	0		128,125	1,134,154
Credit quality band III	227,985	38,452			266,438
Credit quality band IV	360	54,770		40,322	95,452
In default	100,000		17,633		117,633
Non-rated	1,062,041	1,448			1,063,489
Gross carrying amount	5,389,973	97,779	17,633	168,448	5,673,833
Expected credit loss	(11,538)	(2,555)	(7,042)		(21,135)
Book value	5,378,435	95,224	10,592	168,448	5,652,698

31.12.2018

Loans to customers:	Stage 1	Stage 2	Stage 3	FVTPL	Total
Credit quality band I	16,152,412	10,693	11,158	648,966	16,823,228
Credit quality band II	5,493,100	31,662		858,937	6,383,699
Credit quality band III	596,103	287,862	31,814	373,741	1,289,520
Credit quality band IV	51,116	281,862			332,978
In default		156,446	309,702		466,147
Non-rated	2,999,188	1,090,911		278,879	4,368,979
Gross carrying amount	25,291,919	1,859,436	352,673	2,160,522	29,664,550
Expected credit loss	(160,684)	(27,930)	(32,363)		(220,977)
Book value	25,131,235	1,831,506	320,310	2,160,522	29,443,573

Loan commitments, guarantees and unused credit facilities:	Stage 1	Stage 2	Stage 3	FVTPL	Total
Credit quality band I	2,802,424	971			2,803,394
Credit quality band II	753,562	326		183,141	937,030
Credit quality band III	280,896	3,101			283,997
Credit quality band IV	76	5,716			5,792
In default			5,108		5,108
Non-rated	350,688				350,688
Gross carrying amount	4,187,646	10,113	5,108	183,141	4,386,008
Expected credit loss	(15,462)	(683)	(1,293)		(17,439)
Book value	4,172,184	9,430	3,814	183,141	4,368,569

b. Breakdown of loans to customers into not past due and past due

30.6.2019	Claim value	Expected credit loss	Carrying amount
Not past due	27,005,552	(160,951)	26,844,601
Past due 1-30 days	1,375,201	(16,138)	1,359,063
Past due 31-60 days	297,795	(3,995)	293,800
Past due 61-90 days	14,748		14,748
Past due 91-180 days	81,932	(5,683)	76,248
Past due 181-360 days			0
Past due more than 360 days	1,537	(942)	594
Total	28,776,765	(187,709)	28,589,056

31.12.2018	Claim value	Expected credit loss	Carrying amount
Not past due	28,900,493	(197,946)	28,702,547
Past due 1-30 days	570,167	(4,857)	565,309
Past due 31-60 days	158,379	(3,921)	154,458
Past due 61-90 days			0
Past due 91-180 days	11,158	(2)	11,156
Past due 181-360 days			0
Past due more than 360 days	24,353	(14,251)	10,102
Total	29,664,550	(220,977)	29,443,573

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

39. Credit quality of financial assets (cont.)

c. Breakdown of loans to customers by industry

The breakdown of the loan portfolio by industries is specified as follows:

30.6.2019	**Claim value**	**Expected credit loss**	**Carrying amount**	**%**
Financial institutions	56	0	56	0.0%
Corporate				
Services	10,343,330	(74,589)	10,268,741	35.9%
Holding companies	6,401,934	(15,924)	6,386,009	22.3%
Real estate, construction and industry	4,287,090	(35,114)	4,251,975	14.9%
Retail	1,186,077	(10,364)	1,175,713	4.1%
Other	2,416,618	(25,736)	2,390,882	8.4%
Individual	4,141,660	(25,981)	4,115,679	14.4%
Total	28,776,765	(187,709)	28,589,056	100.0%

31.12.2018	**Claim value**	**Expected credit loss**	**Carrying amount**	**%**
Financial institutions	3,988	(8)	3,979	0.0%
Corporate				
Services	11,393,477	(112,157)	11,281,320	38.3%
Holding companies	6,707,672	(18,015)	6,689,657	22.7%
Real estate, construction and industry	2,834,688	(33,759)	2,800,929	9.5%
Retail	1,034,244	(12,819)	1,021,424	3.5%
Other	2,283,070	(22,098)	2,260,972	7.7%
Individual	5,407,411	(22,120)	5,385,291	18.3%
Total	29,664,550	(220,977)	29,443,573	100.0%

d. Breakdown of loans to customers by seniority

The following definitions are used when ranking the loan portfolio by seniority:

- Senior I
  Loans in this category have first priority claims on the borrower's assets, are secured with collateral which can be marked to market and have asset coverage exceeding 100%.
- Senior II
  Loans in this category have sufficient coverage and liquid collateral, but the collateral can in some cases not be marked to market, e.g. unlisted shares.
- Junior
  Junior loans have second lien claims on the borrower’s assets or lower levels of collateral coverage.
- Mezzanine
  Mezzanine loans are loans which are unsecured and subordinated to all of the borrower’s other liabilities.

The breakdown of loans to customers by categories is as follows:

	Senior I	**Senior II**	**Junior**	**Mezzanine**	**30.6.2019**
Amortised cost - Stage 1	6,858,862	8,683,096	3,016,207	5,385,940	23,944,105
Amortised cost - Stage 2	777,845	401,131	942,439	150,573	2,271,988
Amortised cost - Stage 3	51,215	34,073		82,659	167,948
Fair value through profit and loss	184,499	759,282	1,096,518	164,717	2,205,016
Total	7,872,421	9,877,583	5,055,163	5,783,889	28,589,056

	Senior I	**Senior II**	**Junior**	**Mezzanine**	**31.12.2018**
Amortised cost - Stage 1	6,030,827	8,442,103	4,316,905	6,143,591	24,933,426
Amortised cost - Stage 2	1,283,008	345,169	173,640	170,558	1,972,375
Amortised cost - Stage 3	163,415	65,451		148,383	377,250
Fair value through profit and loss	181,415	837,798	907,762	233,548	2,160,522
Total	7,658,665	9,690,522	5,398,306	6,696,080	29,443,573

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

39. Credit quality of financial assets (cont.)

e. Allowance for expected credit loss on loans to customers and loan commitments, guarantees and unused credit facilities

The following tables show changes in the expected credit loss allowance of loans to customers and for loan commitments, guarantees and unused credit facilities during the period.

30.6.2019

Expected credit loss allowance total

	Stage 1	Stage 2	Stage 3	Total
Transfers of financial assets:				
Balance as at 31 December 2018	176,146	28,614	33,657	238,416
Transfer to Stage 1 - (Initial recognition)	8,905	(8,845)	(60)	0
Transfer to Stage 2 - (significantly increased credit risk)	(6,407)	6,407		0
Transfer to Stage 3 - (credit impaired)	(2,379)		2,379	0
Net remeasurement of loss allowance	(32,987)	9,529	6,012	(17,446)
New financial assets, originated or purchased	39,689	14,491	26,101	80,281
Derecognitions and maturities	(58,665)	(14,024)	(18,123)	(90,813)
Write-offs			(1,594)	(1,594)
Balance as at 30 June 2019	124,301	36,171	48,373	208,844

Expected credit loss allowance for loans to customers

	Stage 1	Stage 2	Stage 3	Total
Transfers of financial assets:				
Balance as at 31 December 2018	160,684	27,930	32,363	220,977
Transfer to Stage 1 - (Initial recognition)	8,902	(8,841)	(60)	0
Transfer to Stage 2 - (significantly increased credit risk)	(5,900)	5,900		0
Transfer to Stage 3 - (credit impaired)	(2,379)		2,379	0
Net remeasurement of loss allowance	(31,379)	8,737	5,782	(16,860)
New financial assets, originated or purchased	34,990	13,667	20,475	69,132
Derecognitions and maturities	(52,154)	(13,778)	(19,609)	(85,541)
Balance as at 30 June 2019	112,762	33,616	41,331	187,709

Expected credit loss allowance for loan commitments, guarantees and unused credit facilities

	Stage 1	Stage 2	Stage 3	Total
Transfers of financial assets:				
Balance as at 31 December 2018	15,462	683	1,293	17,439
Transfer to Stage 1 - (Initial recognition)	4	(4)		0
Transfer to Stage 2 - (significantly increased credit risk)	(507)	507		0
Transfer to Stage 3 - (credit impaired)	(0)		0	0
Net remeasurement of loss allowance	(1,608)	792	230	(587)
New financial assets, originated or purchased	4,699	823	5,626	11,148
Derecognitions and maturities	(6,512)	(246)	(108)	(6,865)
Balance as at 30 June 2019	11,538	2,555	7,042	21,135

31.12.2018

Expected credit loss allowance total

	Stage 1	Stage 2	Stage 3	Total
General and specific loss provision at 31.12.2017	243,944	10,856	33,911	288,710
Net remeasurement	(91,791)	39,687	23,395	(28,709)
Opening expected credit loss balance at 1.1.2018	152,153	50,543	57,305	260,001
Transfers of financial assets:				
Transfer to Stage 1 - (Initial recognition)	2,673	(223)	(2,450)	0
Transfer to Stage 2 - (significantly increased credit risk)	(15,005)	15,032	(26)	0
Transfer to Stage 3 - (credit impaired)	(614)	(30,814)	31,429	0
Net remeasurement of loss allowance	(2,893)	(512)	(24,586)	(27,990)
New financial assets, originated or purchased	101,385	12,792	6,913	121,091
Derecognitions and maturities	(61,553)	(18,204)	(25,258)	(105,015)
Write-offs			(9,671)	(9,671)
Balance as at 31 December 2018	176,146	28,614	33,657	238,416

Expected credit loss allowance for loans to customers

	Stage 1	Stage 2	Stage 3	Total
General and specific loss provision at 31.12.2017	243,944	10,856	33,911	288,710
Net remeasurement	(106,713)	38,782	22,487	(45,444)
Opening expected credit loss balance at 1.1.2018	137,231	49,638	56,398	243,266

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

39. Credit quality of financial assets (cont.)

Transfers of financial assets:				
Transfer to Stage 1 - (Initial recognition)	2,396	(215)	(2,181)	0
Transfer to Stage 2 - (significantly increased credit risk)	(14,871)	14,898	(26)	0
Transfer to Stage 3 - (credit impaired)	(568)	(30,814)	31,383	0
Net remeasurement of loss allowance	(1,998)	(911)	(25,243)	(28,152)
New financial assets, originated or purchased	92,969	12,747	6,888	112,603
Derecognitions and maturities	(54,475)	(17,411)	(25,184)	(97,069)
Write-offs			(9,671)	(9,671)
Balance as at 31 December 2018	160,684	27,930	32,363	220,977

Expected credit loss allowance for loan commitments, guarantees and unused credit facilities

	Stage 1	Stage 2	Stage 3	Total
General and specific loss provision at 31.12.2017				0
Net remeasurement	14,922	905	908	16,735
Opening expected credit loss balance at 1.1.2018	14,922	905	908	16,735
Transfers of financial assets:				
Transfer to Stage 1 - (Initial recognition)	277	(8)	(269)	0
Transfer to Stage 2 - (significantly increased credit risk)	(134)	134		0
Transfer to Stage 3 - (credit impaired)	(46)		46	0
Net remeasurement of loss allowance	(895)	399	657	162
New financial assets, originated or purchased	8,416	46	26	8,488
Derecognitions and maturities	(7,078)	(793)	(75)	(7,945)
Write-offs				0
Balance as at 31 December 2018	15,462	683	1,293	17,439

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

40. Collateral and other credit enhancements

a. Valuation

The Group applies the same valuation methods to collateral held as other comparable assets held by the Group. The methods used for financial assets are outlined in note 51. For other types of assets the Group uses third party valuation where possible. Haircuts are then applied to account for liquidity and other factors which may affect the collateral value of the asset or other credit enhancement.

b. Loans to customers

	Deposits	Fixed income securities	Variable income securities	Real estate	Other fixed assets	Other	30.6.2019
Financial institutions	111,431	92,058	502,619	428,427			1,134,536
Corporate customers	788,669	459,104	7,273,611	9,850,452	151,685	373,197	18,896,718
Individuals	9,529	42,419	519,471	406,192			977,611
Total	909,629	593,581	8,295,701	10,685,071	151,685	373,197	21,008,865

	Deposits	Fixed income securities	Variable income securities	Real estate	Other fixed assets	Other	31.12.2018
Financial institutions	604	49,588	46,164	310,655			407,011
Corporate customers	1,441,389	194,594	8,209,045	9,974,043	173,193	976,223	20,968,489
Individuals	10,568	40,665	1,220,231	434,033			1,705,498
Total	1,452,561	284,848	9,475,440	10,718,732	173,193	976,223	23,080,997

Amounts have been adjusted to exclude collateral in excess of claim value, i.e. overcollateralisation. Other collateral includes financial claims, inventories, receivables and letters of credit and guarantees.

c. Derivatives

	Deposits	Fixed income securities	Variable income securities	Real estate	Other fixed assets	Other	30.6.2019
Financial institutions	238,139	342,227	1,768,553				2,348,918
Corporate customers	611,222	65,890	1,177,327				1,854,439
Individuals	31,945		79,316				111,261
Total	881,305	408,117	3,025,196	0	0	0	4,314,617

	Deposits	Fixed income securities	Variable income securities	Real estate	Other fixed assets	Other	31.12.2018
Financial institutions	596,407	233,346	1,329,991				2,159,744
Corporate customers	571,234	154,567	768,923				1,494,725
Individuals	34,028		103,944				137,972
Total	1,201,669	387,913	2,202,858	0	0	0	3,792,441

Amounts have been adjusted to exclude collateral in excess of claim value, i.e. overcollateralisation.

41. Loan-to-value

a. General

The loan-to-value ratio (LTV) is the ratio of the gross amount of the loan to the value of the collateral, if any. The general creditworthiness of a customer is viewed as the most reliable indicator of credit quality of a loan. Valuation of collateral held against loans is therefore not updated unless the creditworthiness of a borrower deteriorates.

b. Breakdown

The breakdown of loans to customers by LTV is specified as follows:

	30.6.2019	%	31.12.2018	%
Less than 50%	11,652,736	40.8%	10,041,505	34.1%
51-70%	4,144,663	14.5%	6,286,414	21.4%
71-90%	2,815,147	9.8%	4,542,377	15.4%
91-100%	467,372	1.6%	525,403	1.8%
More than 100%	4,226,536	14.8%	3,216,506	10.9%
No collateral:				
Purchased short-term retail claims	2,991,569	10.5%	3,511,938	11.9%
Other loans with no collateral	2,291,032	8.0%	1,319,429	4.5%
Total	28,589,056	100.0%	29,443,573	100.0%

The Group has entered into an agreement to purchase short term consumer credit (the claims) from an originator. The purchase of claims are subject to conditions such as credit rating of the borrower and maximum maturity of 24 months. Further, the originator receives final payment of the purchased claim when the claim is fully repaid, until then a part of the purchase price is held as collateral against defaults.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

42. Large exposures

In accordance with the Financial Supervisory Authority's regulation no. 625/2013 on financial institutions' large exposures, total exposure towards a customer is classified as a large exposure if it exceeds 10% of the Bank's capital base (see note 37).

According to the regulation a single exposure, net of risk adjusted mitigation, cannot exceed 25% of the capital base. Single large exposures net of risk adjusted mitigation take into account the effects of collateral held by the Bank, and other credit enhancements, in accordance with the Financial Supervisory Authority's regulation no. 625/2013.

		30.6.2019		31.12.2018
Large exposures before risk adjusted mitigation	**Number**	**Amount**	**Number**	**Amount**
10-20% of capital base	6	8,985,329	5	6,740,154
20-25% of capital base	0	0	1	2,359,382
Exceeding 25% of capital base	1	4,334,435	1	3,472,741
Total	7	13,319,764	7	12,572,277
Thereof nostro accounts with foreign banks with S&P rating of A- or higher	2	3,528,973	1	2,359,382
Thereof foreign governments and central banks exposures	1	4,334,435	0	
Large exposures net of risk adjusted mitigation	3	4,787,531	1	2,359,382

No single large exposure net of risk adjusted mitigation exceeds 25% of capital base in accordance with the Financial Supervisory Authority's regulation no. 625/2013.

43. Liquidity risk

a. Definition

Liquidity risk is the risk that the Group will encounter difficulty in meeting contractual payment obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. This risk mainly arises from mismatches in the timing of cash flows. The Group has internal rules that require certain matching of the maturities of assets and liabilities. Furthermore, to ensure the ability to meet liquidity needs, the Group maintains a stock of highly liquid unencumbered assets, e.g. cash, treasury bills and treasury bonds.

b. Management

Liquidity is managed by treasury and monitored by risk management. Liquidity position is reported to the ALCO committee. The Central Bank of Iceland sets minimum requirements for the coverage ratio between cash flows of assets and liabilities (LCR) and stable funding in foreign currencies (NSFR). The minimum 30 day LCR regulatory requirement is 100%. The minimum regulatory requirment for foreign currencies NSFR is 100%.

The Group was in compliance with internal and external liquidity requirements throughout the years 2019 and 2018. At end of June 2019 the LCR was 193% and at year-end 2018 it was 277%.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

43. Liquidity risk (cont.)

c. Maturity analysis of financial assets and financial liabilities

30.6.2019 **Financial assets by type**	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative assets							
Cash and balances with Central Bank	28,323,981	2,489,200				30,813,181	30,784,218
Fixed income securities	4,621,093	93,154	89,952			4,804,198	4,804,198
Shares and other variable income securities	1,054,306	2	2,340,459			3,394,767	3,394,767
Securities used for hedging	29,565,108					29,565,108	29,565,108
Loans to customers	2,323,608	3,880,727	15,368,838	7,205,453	451,636	29,230,261	28,589,056
Other assets	7,764,686	540,820	608,414	1,333,357		10,247,277	10,247,277
	73,652,782	7,003,903	18,407,663	8,538,810	451,636	108,054,793	107,384,625
Derivative assets							
Inflow	9,676,148	40,255	484,208	148,500		10,349,111	
Outflow	(8,854,028)	(1,031)	(421,353)	(2,968)		(9,279,380)	
	822,120	39,224	62,855	145,533	0	1,069,731	1,212,134

Financial liabilities by type	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative liabilities							
Deposits from customers	(44,102,996)	(9,334,014)	(2,567,890)	(2,058,531)	(187,619)	(58,251,050)	58,003,384
Borrowings	(4,739,514)	(9,151,789)	(8,249,028)	(73,391)		(22,213,722)	21,962,389
Issued bills		(2,000,000)	(2,000,000)			(4,000,000)	3,932,665
Issued bonds	(9,630)	(419,251)	(645,077)	(2,531,008)		(3,604,966)	3,121,095
Subordinated liabilities		(59,958)	(62,285)	(366,728)	(2,411,907)	(2,900,879)	1,978,150
Short positions held for trading	(1,136,951)					(1,136,951)	1,136,951
Short positions used for hedging	(435,176)					(435,176)	435,176
Other liabilities	(5,273,803)	(885,362)	(824,258)	(1,145,525)		(8,128,948)	8,128,948
	(55,698,070)	(21,850,374)	(14,348,537)	(6,175,184)	(2,599,527)	(100,671,691)	98,698,757
Derivative liabilities							
Inflow	21,109,029	553,812				21,662,841	
Outflow	(22,437,800)	(553,873)				(22,991,673)	
	(1,328,771)	(61)	0	0	0	(1,328,832)	1,483,041
Unrecognised financial items							
Loan commitments							
Inflow	419,493	795,929	3,261,665	553,524		5,030,611	
Outflow	(4,800,322)					(4,800,322)	
Financial guarantee contracts							
Inflow	88,570	15,190	322,901	413,010	33,840	873,511	
Outflow	(873,511)					(873,511)	
	(5,165,770)	811,120	3,584,565	966,534	33,840	230,289	
Summary							
Non-derivative assets	73,652,782	7,003,903	18,407,663	8,538,810	451,636	108,054,793	
Derivative assets	822,120	39,224	62,855	145,533		1,069,731	
Non-derivative liabilities	(55,698,070)	(21,850,374)	(14,348,537)	(6,175,184)	(2,599,527)	(100,671,691)	
Derivative liabilities	(1,328,771)	(61)				(1,328,832)	
Net assets (liabilities) excluding unrecognised items	17,448,061	(14,807,308)	4,121,981	2,509,158	(2,147,891)	7,124,001	
Net unrecognised items	(5,165,770)	811,120	3,584,565	966,534	33,840	230,289	
Net assets (liabilities)	12,282,290	(13,996,188)	7,706,546	3,475,693	(2,114,051)	7,354,290	

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

43. Liquidity risk (cont.)

31.12.2018 **Financial assets by type**	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative assets							
Cash and balances with Central Bank	21,339,185					21,339,185	21,339,185
Fixed income securities	4,936,503	54,595	133,230			5,124,328	5,127,335
Shares and other variable income securities	989,332		1,937,344			2,926,675	2,926,675
Securities used for hedging	21,526,794					21,526,794	21,526,794
Loans to customers	3,665,736	6,002,954	14,048,774	7,601,019	508,769	31,827,251	29,443,573
Other assets	592,443	592,986	353,118	402,522		1,941,070	1,941,070
	53,049,993	6,650,536	16,472,465	8,003,541	508,769	84,685,303	82,304,631
Derivative assets							
Inflow	9,646,806	86,784	47,909	155,880		9,937,378	
Outflow	(8,681,151)	(85,812)	(1,533)	(5,571)		(8,774,068)	
	965,654	972	46,376	150,309	0	1,163,311	1,213,266

Financial liabilities by type	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative liabilities							
Deposits from customers	(32,904,108)	(11,450,562)	(2,066,844)	(1,912,032)	(83,029)	(48,416,575)	47,893,959
Borrowings	(1,427,044)	(8,447,186)	(5,668,787)			(15,543,017)	15,634,648
Issued bills		(1,800,000)	(1,840,000)			(3,640,000)	3,577,718
Issued bonds	(16,226)	(24,923)	(499,311)	(3,137,596)		(3,678,055)	3,160,215
Subordinated liabilities			(120,119)	(360,527)	(2,431,190)	(2,911,837)	1,947,511
Short positions held for trading	(805,334)					(805,334)	805,334
Other liabilities	(322,295)	(762,318)	(470,901)	(54,809)		(1,610,323)	1,610,323
	(35,475,008)	(22,484,990)	(10,665,961)	(5,464,964)	(2,514,219)	(76,605,142)	74,629,708
Derivative liabilities							
Inflow	12,213,045	510,776	399,690			13,123,511	
Outflow	(12,728,897)	(525,531)	(420,750)			(13,675,178)	
	(515,852)	(14,755)	(21,060)	0	0	(551,667)	593,934
Unrecognised financial items by type							
Loan commitments							
Inflow	505,137	1,014,347	1,417,147	601,431		3,538,062	
Outflow	(3,462,935)					(3,462,935)	
Financial guarantee contracts							
Inflow	923,074					923,074	
Outflow	(923,074)					(923,074)	
	(2,957,798)	1,014,347	1,417,147	601,431	0	75,127	
Summary							
Non-derivative assets	53,049,993	6,650,536	16,472,465	8,003,541	508,769	84,685,303	
Derivative assets	965,654	972	46,376	150,309		1,163,311	
Non-derivative liabilities	(35,475,008)	(22,484,990)	(10,665,961)	(5,464,964)	(2,514,219)	(76,605,142)	
Derivative liabilities	(515,852)	(14,755)	(21,060)			(551,667)	
Net assets (liabilities) excluding unrecognised items	18,024,787	(15,848,237)	5,831,820	2,688,886	(2,005,450)	8,691,805	
Net unrecognised items	(2,957,798)	1,014,347	1,417,147	601,431		75,127	
Net assets (liabilities)	15,066,989	(14,833,890)	7,248,967	3,290,317	(2,005,450)	8,766,933	

Maturity analysis of financial assets and financial liabilities is based on contractual cash flows or, in the case of held for trading securities, expected cash flows. If an amount receivable or payable is not fixed, e.g. for inflation indexed assets and liabilities, the maturity analysis uses estimates based on current conditions.

Cash flows relating to unrecognised balance sheet items (unused loan commitments and financial guarantee contracts) are presented separately from financial assets and financial liabilities. Both contractual outflows and inflows are shown, to fully reflect the nature of these items.

It should be noted that the Group's expected cash flows sometimes vary considerably from the contractual cash flows, most significantly in that demand deposits from customers are expected to remain stable or increase in the long term. In this case the presentation used reflects the worst case scenario from the Group's perspective. Furthermore, the analysis does not consider any measures that could be taken to convert long-term assets to cash through sale.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

44. Interest rate risk associated with trading portfolios

a. Breakdown

The breakdown of financial assets and liabilities in trading portfolios by the earlier of interest repricing time or maturity is specified as follows:

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	30.6.2019
Fixed income securities	528,781		787,895	1,228,778	2,258,745	4,804,198
Short positions - fixed income securities			(80,758)	(206,517)	(849,676)	(1,136,951)
Net imbalance	528,781	0	707,137	1,022,261	1,409,069	3,667,248

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	31.12.2018
Fixed income securities		17,913	999,491	1,561,987	2,547,944	5,127,335
Short positions - fixed income securities				(755,454)	(49,880)	(805,334)
Net imbalance	0	17,913	999,491	806,534	2,498,063	4,322,001

b. Sensitivity analysis

The Group performs monthly sensitivity analysis on financial assets and liabilities in trading portfolios that are subject to interest rate risk. The sensitivity analysis assumes a shift in the yield curves for all currencies. A parallel shift in yield curves would have the following impact on the Group's pre-tax profit and equity, assuming all other risk factors remain constant:

	Shift in basis points	Downward	30.6.2019 Upward	Downward	31.12.2018 Upward
Indexed	50	114,634	(114,634)	70,216	(70,216)
Non-indexed	100	18,253	(18,253)	69,481	(69,481)
Total		132,887	(132,887)	139,697	(139,697)

45. Interest rate risk associated with non-trading portfolios

a. Breakdown

The breakdown of financial assets and liabilities in non-trading portfolios by the earlier of interest repricing time or maturity is specified as follows:

30.6.2019

Financial assets	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Cash and balances with Central Bank	26,449,783	4,334,435				30,784,218
Loans to customers	24,387,910	1,082,288	1,930,592	1,164,149	24,117	28,589,056
Financial assets excluding derivatives	50,837,693	5,416,723	1,930,592	1,164,149	24,117	59,373,274
Effect of derivatives	30,764,946	1,553,812	1,000,000	2,100,000		35,418,758
Total	81,602,639	6,970,535	2,930,592	3,264,149	24,117	94,792,032

Financial liabilities	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Deposits from customers	58,003,384					58,003,384
Borrowings	4,736,816	9,092,021	8,063,515	70,037		21,962,389
Issued bills	1,977,249		1,955,416			3,932,665
Issued bonds	303,877	397,820	542,618	1,876,780		3,121,095
Subordinated liabilities					1,978,150	1,978,150
Financial liabilities excluding derivatives	65,021,326	9,489,841	10,561,548	1,946,817	1,978,150	88,997,682
Effect of derivatives	2,507,104	2,100,000				4,607,104
Total	67,528,430	11,589,841	10,561,548	1,946,817	1,978,150	93,604,787
Total interest repricing gap	14,074,209	(4,619,306)	(7,630,956)	1,317,332	(1,954,034)	1,187,245

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

45. Interest rate risk associated with non-trading portfolios (cont.)

31.12.2018

Financial assets	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
Cash and balances with Central Bank	17,867,444	3,471,741				21,339,185
Loans to customers	23,872,709	1,432,779	2,821,790	1,158,425	157,870	29,443,573
Financial assets excluding derivatives	41,740,153	4,904,520	2,821,790	1,158,425	157,870	50,782,758
Effect of derivatives	22,590,158	597,560	1,500,000	3,100,000		27,787,718
Total	64,330,311	5,502,080	4,321,790	4,258,425	157,870	78,570,476

Financial liabilities	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
Deposits from customers	47,893,959					47,893,959
Borrowings	1,437,087	8,610,188	5,587,373			15,634,648
Issued bills		1,779,152	1,798,565			3,577,718
Issued bonds	266,454		399,725	2,494,035		3,160,215
Subordinated liabilities					1,947,511	1,947,511
Financial liabilities excluding derivatives	49,597,500	10,389,341	7,785,664	2,494,035	1,947,511	72,214,051
Effect of derivatives	4,607,104					4,607,104
Total	54,204,604	10,389,341	7,785,664	2,494,035	1,947,511	76,821,155
Total interest repricing gap	10,125,707	(4,887,261)	(3,463,874)	1,764,389	(1,789,641)	1,749,321

b. Sensitivity analysis

The Group performs monthly sensitivity analysis on financial assets and liabilities in non-trading portfolios subject to interest rate risk. The sensitivity analysis assumes a shift in the yield curves for all currencies. A parallel shift in yield curves would have the following impact on the Group's pre-tax profit and equity, assuming all other risk factors remain constant:

	Shift in		**30.6.2019**		**31.12.2018**
Currency	**basis points**	**Downward**	**Upward**	**Downward**	**Upward**
ISK, indexed	50	16,736	(16,166)	11,837	(11,614)
ISK, non-indexed	100	(59,763)	56,354	(42,882)	41,861
Other currencies	20	(945)	(35)	(2,228)	1,157
Total		(43,972)	40,154	(33,273)	31,404

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

46. Exposure towards changes in the CPI

a. Definition

Exposure towards changes in CPI is the risk that fluctuations in the Icelandic Consumer Price Index (CPI) will affect the balance and cash flow of indexed financial instruments.

The Group is exposed to inflation indexation of assets and liabilities denominated in ISK. All indexed assets and liabilities are valued according to the CPI measure at any given time and changes in CPI are recognised in the income statement.

b. Management

The Group controls its indexation risk through derivatives contracts and sales and purchases of indexed bonds, mostly government bonds, and thus keeps its exposure to the CPI within the limits set by the ALCO committee.

c. Balance of CPI linked assets and liabilities

The net balance of CPI linked assets and liabilities is specified as follows:

	30.6.2019	**31.12.2018**
Government bonds	461,381	229,508
Other fixed income securities	2,853,496	2,004,865
Loans to customers	3,405,552	2,445,864
Derivatives	3,100,000	2,500,000
Short positions	(1,180,744)	(278,385)
Liabilities	(5,127,167)	(4,648,662)
Debt issued	(1,800,000)	(1,000,000)
Total	1,712,519	1,253,191

	30.6.2019	**31.12.2018**
Assets	9,820,429	7,180,237
Liabilities	(8,107,911)	(5,927,047)
Total	1,712,519	1,253,191

d. Sensitivity to changes in CPI

Given the net balance of CPI linked assets and liabilities, a 1% change in the CPI would, with other things constant, result in the following changes to the Group's pre-tax profit.

		30.6.2019		**31.12.2018**
	-1%	1%	-1%	1%
Government bonds	(4,614)	4,614	(2,295)	2,295
Other fixed income securities	(28,535)	28,535	(20,049)	20,049
Loans to customers	(34,056)	34,056	(24,459)	24,459
Derivatives	(31,000)	31,000	(25,000)	25,000
Short positions	11,807	(11,807)	2,784	(2,784)
Deposits	51,272	(51,272)	46,487	(46,487)
Subordinated debt	18,000	(18,000)	10,000	(10,000)
	(17,125)	17,125	(12,532)	12,532

The effect on equity would be the same.

47. Currency risk

a. Definition

Currency risk arises when financial instruments are not denominated in the functional currency of the respective Group entity and can affect both the Group's income statement and statement of financial position. A part of the Group's financial assets and liabilities is denominated in foreign currencies.

b. Management

Currency positions are monitored by risk management and reported to the ALCO committee. Any mismatch between assets and liabilities in each currency is monitored closely and managed within limits.

The Group is subject to limits set by the Central Bank of Iceland regarding the maximum open currency position. At 30 June 2019 and 31 December 2018 the Group's position in foreign currencies was within those limits.

c. Exchange rates

The following exchange rates have been used by the Group in the preparation of these financial statements:

	Closing 30.6.2019	**Average 6m 2019**	**Closing 31.12.2018**	**Average 6m 2018**
EUR/ISK	141.7	137.0	133.2	122.9
USD/ISK	124.5	121.3	116.3	105.2

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

47. Currency risk (cont.)

d. Breakdown of financial assets and financial liabilities denominated in foreign currencies

30.6.2019

Financial assets	**EUR**	**USD**	**GBP**	**CAD**	**Other currencies**	**Total**
Cash and balances with Central Bank	2,184,002	6,024,546	271,097	67,812	701,659	9,249,116
Fixed income securities						0
Shares and other variable income securities	64,283	22	614,323		34	678,661
Loans to customers	975,368	113,372	718,571		42,293	1,849,605
Other assets	1,045,332	193,739	193,774		56,419	1,489,264
Financial assets excluding derivatives	4,268,986	6,331,679	1,797,765	67,812	800,404	13,266,646
Derivatives	659,489	973,835	19,027		143,149	1,795,500
Total	4,928,475	7,305,514	1,816,792	67,812	943,553	15,062,146

Financial liabilities	**EUR**	**USD**	**GBP**	**CAD**	**Other currencies**	**Total**
Deposits from customers	3,879,321	5,982,029	721,070	34,339	656,305	11,273,064
Borrowings	41,862					41,862
Issued bonds		303,808				303,808
Other liabilities	857,292	930,769	140,044	25,111	147,545	2,100,761
Financial liabilities excluding derivatives	4,778,474	7,216,606	861,114	59,450	803,851	13,719,495
Derivatives	234,389	51,870	915,298		143,256	1,344,814
Total	5,012,863	7,268,476	1,776,412	59,450	947,107	15,064,309

Net currency position	**EUR**	**USD**	**GBP**	**CAD**	**Other currencies**	**Total**
Financial assets	4,928,475	7,305,514	1,816,792	67,812	943,553	15,062,146
Financial liabilities	(5,012,863)	(7,268,476)	(1,776,412)	(59,450)	(947,107)	(15,064,309)
Financial guarantee contracts	9,712					9,712
Total	(74,677)	37,038	40,380	8,362	(3,554)	7,549

31.12.2018

Financial assets	**EUR**	**USD**	**GBP**	**NOK**	**Other currencies**	**Total**
Cash and balances with Central Bank	2,976,108	6,152,291	200,764	93,690	847,261	10,270,114
Fixed income securities	133,230					133,230
Shares and other variable income securities	6	18	385,394		31	385,449
Loans to customers	1,452,927	110,112	140,375		158,935	1,862,349
Other assets	330,613	143,642	337,106			811,361
Financial assets excluding derivatives	4,892,884	6,406,062	1,063,639	93,690	1,006,227	13,462,503
Derivatives	417,793	32,155	17,884			467,832
Total	5,310,678	6,438,217	1,081,523	93,690	1,006,227	13,930,335

Financial liabilities	**EUR**	**USD**	**GBP**	**NOK**	**Other currencies**	**Total**
Deposits from customers	5,112,003	5,736,753	1,062,588	109,446	894,284	12,915,074
Borrowings	39,407					39,407
Issued bonds		278,201				278,201
Other liabilities	2,160	290,825	4,925		1,407	299,317
Financial liabilities excluding derivatives	5,153,569	6,305,779	1,067,513	109,446	895,691	13,531,999
Derivatives	18,103	32,155				50,258
Total	5,171,673	6,337,934	1,067,513	109,446	895,691	13,582,258

Net currency position	**EUR**	**USD**	**GBP**	**NOK**	**Other currencies**	**Total**
Financial assets	5,310,678	6,438,217	1,081,523	93,690	1,006,227	13,930,335
Financial liabilities	(5,171,673)	(6,337,934)	(1,067,513)	(109,446)	(895,691)	(13,582,258)
Financial guarantee contracts	7,934					7,934
Total	146,940	100,283	14,009	(15,756)	110,536	356,012

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

47. Currency risk (cont.)

e. Sensitivity to currency risk

Given the net currency position, a 10% change in the value of the ISK would, with other things constant, result in the following changes to the Group's pre-tax profit.

	30.6.2019		31.12.2018	
Assets and liabilities denominated in foreign currencies	**-10%**	**+10%**	**-10%**	**+10%**
EUR	(7,468)	7,468	14,694	(14,694)
USD	3,704	(3,704)	10,028	(10,028)
GBP	4,038	(4,038)	1,401	(1,401)
CAD	836	(836)	760	(760)
NOK	(485)	485	(1,576)	1,576
Other currencies	130	(130)	10,293	(10,293)
Total	755	(755)	35,601	(35,601)

The effect on equity would be the same.

48. Other price risk

Other price risk arises from changes in the market prices of shares and other variable income securities in the Group's portfolio. The Group directly holds listed and unlisted shares and other variable income securities, while also gaining exposure to listed shares through portfolio options trading. The table below shows the Group's net exposure, including delta-adjusted options exposure.

			30.6.2019			31.12.2018
	Average	**Max**	**Exposure**	**Average**	**Max**	**Exposure**
Listed shares	920,491	2,718,021	837,917	840,266	1,306,331	751,470
Unlisted shares	1,746,151	1,946,252	1,902,998	971,302	1,432,666	1,391,018
Unlisted unit shares	749,734	998,994	653,853	1,018,325	1,978,813	784,187
Total			3,394,767			2,926,675

49. Operational risk

a. Definition

Operational risk is the risk of financial losses resulting from the failure or inadequacy of internal processes or systems, from employee error or from external events. Operational risk includes legal risk, but excludes reputational risks. It is therefore inherent in all areas of business activities.

b. Management

Operational risk can be reduced through staff training, process re-design and enhancement of the control environment. The risk management unit monitors operational risk by tracking loss events, quality deficiencies, potential risk indicators and other early-warning signals. The unit takes an active role in internal control and quality management.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

Financial assets and financial liabilities

50. Accounting classification of financial assets and financial liabilities

The accounting classification of financial assets and financial liabilities is specified as follows:

30.6.2019 Financial assets	Amortised cost	Manda-torily at fair value through P/L	Total carrying amount
Cash and balances with Central Bank	30,784,218		30,784,218
Fixed income securities		4,804,198	4,804,198
Shares and other variable income securities		3,394,767	3,394,767
Securities used for hedging		29,565,108	29,565,108
Loans to customers	26,384,040	2,205,016	28,589,056
Derivatives		1,212,134	1,212,134
Other assets	10,247,277		10,247,277
Total	67,415,536	41,181,223	108,596,759

Financial liabilities	Amortised cost	Manda-torily at fair value through P/L	Total carrying amount
Deposits from customers	58,003,384		58,003,384
Borrowings	21,962,389		21,962,389
Issued bills	3,932,665		3,932,665
Issued bonds	3,121,095		3,121,095
Subordinated liabilities	1,978,150		1,978,150
Short positions held for trading		1,136,951	1,136,951
Short positions used for hedging		435,176	435,176
Derivatives		1,483,041	1,483,041
Other liabilities	7,038,231	1,090,717	8,128,948
Total	96,035,914	4,145,884	100,181,798

31.12.2018 Financial assets	Amortised cost	Manda-torily at fair value through P/L	Total carrying amount
Cash and balances with Central Bank	21,339,185		21,339,185
Fixed income securities		5,127,335	5,127,335
Shares and other variable income securities		2,926,675	2,926,675
Securities used for hedging		21,526,794	21,526,794
Loans to customers	27,283,050	2,160,522	29,443,573
Derivatives		1,213,266	1,213,266
Other assets	1,941,070		1,941,070
Total	50,563,305	32,954,592	83,517,897

Financial liabilities	Amortised cost	Manda-torily at fair value through P/L	Total carrying amount
Deposits from customers	47,893,959		47,893,959
Borrowings	15,634,648		15,634,648
Issued bills	3,577,718		3,577,718
Issued bonds	3,160,215		3,160,215
Subordinated liabilities	1,947,511		1,947,511
Short positions held for trading		805,334	805,334
Derivatives		593,934	593,934
Other liabilities	1,610,323		1,610,323
Total	73,824,374	1,399,268	75,223,642

Notes to the Condensed Interim Consolidated Financial Statements

51. Financial assets and financial liabilities measured at fair value

a. Fair value hierarchy

The fair value of financial assets and liabilities that are traded in active markets are based on quoted market prices. For other financial instruments the Bank determines fair value using various valuation techniques. IFRS 13 specifies a fair value hierarchy based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources whereas unobservable inputs reflect the Bank's market assumptions. These two types of inputs result in the following fair value hierarchy:

- Level 1

  Inputs are quoted market prices (unadjusted) in active markets for identical instruments.

- Level 2

  Inputs are not quoted market prices but are observable either directly, i.e. as prices, or indirectly, i.e. derived from prices. This category includes financial instruments valued using quoted prices in active markets for similar instruments, quoted prices for similar or identical instruments in markets that are considered less than active and other instruments which are valued using techniques which rely primarily on inputs that are directly or indirectly observable from market data.

- Level 3

  Inputs are not observable or unobservable inputs have a significant effect on the valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments are required to reflect the differences between the instruments.

b. Valuation process

The Bank's ALCO committee is responsible for fair value measurements of financial assets and financial liabilities classified as level 2 or level 3 instruments. The valuation is carried out by personnel from Risk and Treasury and is revised at least quarterly, or when there are indications of significant changes in the underlying inputs.

c. Valuation techniques

The Group uses widely recognised valuation techniques, including net present value and discounted cash flow models, comparison with similar instruments for which market observable prices exist, Black-Scholes and other valuation models.

Valuation techniques include recent arm's length transactions between knowledgeable, willing parties, if available, reference to the current fair value of other instruments that are substantially the same, the discounted cash flow analysis and option pricing models. Valuation techniques incorporate all factors that market participants would consider in setting a price and are consistent with accepted methodologies for pricing financial instruments. Periodically, the Group calibrates the valuation technique and tests it for validity using prices from any observable current market transactions in the same instrument, without modification or repackaging, or based on any available observable market data.

For more complex instruments, the Group uses proprietary models, which usually are developed from recognised valuation models. Some or all of the inputs into these models may not be market observable, and are derived from market prices or rates or are estimated based on assumptions. When entering into a transaction, the financial instrument is recognised initially at the transaction price, which is the best indicator of fair value, although the value obtained from the valuation model may differ from the transaction price. This initial difference, usually an increase in fair value, indicated by valuation techniques is recognised in income depending upon the individual facts and circumstances of each transaction and no later than when the market data becomes observable.

The value produced by a model or other valuation technique is adjusted to allow for a number of factors as appropriate, because valuation techniques cannot appropriately reflect all factors market participants take into account when entering into a transaction. Valuation adjustments are recorded to allow for model risks, bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments carried at fair value in the statement of financial position.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

51. Financial assets and financial liabilities measured at fair value (cont.)

d. Fair value hierarchy classification

The fair value of financial assets and financial liabilities measured at fair value in the statement of financial position is classified into the fair value hierarchy as follows:

30.6.2019

Financial assets	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Fixed income securities	4,802,715		1,483	4,804,198
Shares and other variable income securities	1,870,653	114,122	1,409,991	3,394,767
Securities used for hedging	29,565,108			29,565,108
Loans to customers			2,205,016	2,205,016
Derivatives		1,212,134		1,212,134
Total	36,238,477	1,326,256	3,616,490	41,181,223

Financial liabilities	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Short positions held for trading	1,136,951			1,136,951
Short positions used for hedging	435,176			435,176
Derivatives		1,483,041		1,483,041
Other liabilities			1,090,717	1,090,717
Total	1,572,127	1,483,041	1,090,717	4,145,884

There were no transfers between levels during the period.

31.12.2018

Financial assets	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Fixed income securities	4,992,391		134,944	5,127,335
Shares and other variable income securities	1,686,097	376,399	864,180	2,926,675
Securities used for hedging	21,476,591	50,203		21,526,794
Loans to customers			2,160,522	2,160,522
Derivatives		1,213,266		1,213,266
Total	28,155,079	1,639,867	3,159,646	32,954,592

Financial liabilities	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Short positions held for trading	805,334			805,334
Derivatives		593,934		593,934
Total	805,334	593,934	0	1,399,268

There were no transfers between levels during the period.

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

51. Financial assets and financial liabilities measured at fair value (cont.)

e. Reconciliation of changes in Level 3 fair value measurements

30.6.2019	**Fixed income securities**	**Shares and other var. income securities**	**Loans to customers**	**Other liabilities**	**Total**
Balance as at 31 December 2018	134,944	864,180	2,160,522	0	3,159,646
Total gains and losses in profit or loss	(133,461)	79,626	36,328	(16,588)	(34,094)
Purchases	0	744,380	474,853		1,219,233
Repayments	0	0	(466,688)		(466,688)
Acquisition of subsidiary		928,327		(1,074,129)	(145,801)
Sales		(1,206,522)			(1,206,522)
Balance as at 30 June 2019	1,483	1,409,991	2,205,016	(1,090,717)	2,525,773

31.12.2018	**Fixed income securities**	**Shares and other var. income securities**	**Loans to customers**	**Other liabilities**	**Total**
Balance as at 1 January 2018	0	531,405	0	0	531,405
Reclassification into Level 3 in accordance with IFRS 9			2,081,352		2,081,352
Total gains and losses in profit or loss	11,059	(17,865)	237,973		231,167
Purchases	127,400	521,140	596,618		1,245,158
Repayments	(3,515)		(755,420)		(758,936)
Capital decrease		(16,638)			(16,638)
Sales		(153,863)			(153,863)
Balance as at 31 December 2018	134,944	864,180	2,160,522	0	3,159,646

f. Change in unrealised gains or losses related to Level 3 financial assets and liabilities held at end of the period

	Shares and other var. income securities
Net financial income - 6m 2019	
Financial assets mandatorily measured at fair value through profit or loss	79,626
Total	79,626
Net financial income - 12m 2018	
Financial assets mandatorily measured at fair value through profit or loss	(17,865)
Total	(17,865)

g. Fair value measurements for Level 3 financial assets and liabilities

Level 3 assets consist primarily of illiquid, unlisted bonds, shares and share certificates and loans measured at fair value. Each asset is evaluated separately but assets within an asset group share a valuation method. The following valuation methods are in use in 2019:

Asset class	**Method**	**Significant unobservable input**	**Range**	**Book value 30.6.2019**
Unlisted bonds	Expected recovery	Value of assets	0-5%	1,483
Unlisted shares	Market price	Recent trades	-	1,409,991
Loans to customers	Expert model	Value of assets and collateral	-	2,205,016
Total				3,616,490

Asset class	**Method**	**Significant unobservable input**	**Range**	**Book value 31.12.2018**
Unlisted bonds	Expected recovery	Value of assets	90-100%	134,944
Unlisted shares	Market price	Recent trades	-	864,180
Loan to customers	Expert model	Value of assets and collateral	-	2,160,522
Total				3,159,646

Given the methods used, the possible range of the significant unobservable inputs is wide. When determining the values used the Group considers the financial strength of the entity in question, recent trades if any and multipliers for comparable instruments.

h. The effect of unobservable inputs in Level 3 fair value measurements

The Group believes its estimates represent appropriate approximations of fair value and that the use of different valuation methodologies and reasonable changes in assumptions or unobservable inputs would not significantly change the estimates.

A 10% change in the estimates would have the following effect on profit before taxes:

	+10%	**-10%**
Shares and other variable income securities	140,999	(140,999)
Loans to customers	220,502	(220,502)
Total	361,501	(361,501)

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

Segment information

52. Business segments

Segment reporting is based on the same principles and structure as internal reporting to senior management and the Board of Directors. Segment performance is evaluated on profit before cost allocation and tax.

Reportable segments
The Group defines five reportable segments which reflect the reporting structure of the Bank.

- Corporate Banking
  Corporate Banking offers various forms of banking services and related advisory services, in addition to providing specialised lending services.
- Corporate Finance
  Corporate Finance provides its customers with impartial and independent advice concerning purchases, sales and mergers and acquisitions of companies.
- Capital Markets
  Capital Markets offers securities and foreign currency brokerage, derivatives brokerage and forward contracts to clients, which include institutional investors, corporates and high net worth individuals.
- Proprietary Trading and Treasury
  Proprietary Trading and Treasury provide market making services to its clients as well as providing the Bank with treasury services.
- Asset Management
  Products and services offered include asset management involving both domestic and foreign assets, private banking, and private pension plans.

Information about other divisions of the Bank, e.g. non-revenue generating divisions, is presented under the heading Support functions and eliminations.

6m 2019	Corporate Banking	Corporate Finance	Capital Markets	Proprietary trading and Treasury	Asset Management	Support functions and eliminations	Total
Net interest income	767,939	(101)	101,553	59,769	(86,182)	2,731	845,709
Net fee and commission income	366,332	183,374	452,311	59,578	1,926,005	(75,374)	2,912,226
Net financial income	92,905	0	(2,103)	245,430	(5,588)	43,828	374,472
Share in profit of associates	(50,685)	0	0	0	23,275	0	(27,410)
Other operating income (expense)	35,313	0	(2)	1,566	17,759	5,799	60,435
Net operating income	1,211,804	183,273	551,759	366,343	1,875,270	(23,017)	4,165,433
Salaries and related expenses	(101,900)	(114,362)	(126,319)	(85,871)	(548,483)	(772,794)	(1,749,729)
Other operating expenses	(212,583)	(12,797)	(34,124)	(32,783)	(331,952)	(283,865)	(908,105)
Net impairment	43,241	(17,098)	0	0	(7,000)	3,000	22,143
Revaluation of contingent consideration	0	0	0	0	60,093	0	60,093
Profit (loss) before cost allocation and tax	940,562	39,016	391,316	247,689	1,047,928	(1,076,676)	1,589,835
Net segment revenue from external customers	829,866	152,590	1,327,323	(15,819)	1,866,990	4,483	4,165,433
Net segment revenue from other segments	381,938	30,683	(775,564)	382,162	8,280	(27,500)	0

6m 2018	Corporate Banking	Corporate Finance	Capital Markets	Proprietary trading and Treasury	Asset Management	Support functions and eliminations	Total
Net interest income	724,299	(197)	76,118	(19,189)	2,203	10,601	793,835
Net fee and commission income	323,610	280,635	314,365	24,900	1,043,404	(70,625)	1,916,288
Net financial income	107,051	212	1,187	184,408	2,178	(288)	294,749
Share in loss of discontinued operations	0	0	0	0	0	0	0
Share in profit of associates	677	0	0	0	(4,280)	0	(3,603)
Other operating income (expense)	52,457	0	69	1,331	13,154	(31,269)	35,742
Net operating income	1,208,094	280,649	391,740	191,451	1,056,659	(91,582)	3,037,011
Salaries and related expenses	(107,471)	(143,159)	(171,154)	(84,515)	(358,221)	(486,408)	(1,350,926)
Other operating expenses	(174,242)	(23,131)	(41,378)	(22,118)	(129,906)	(245,029)	(635,803)
Net impairment	3,485	(1,673)	(504)	0	(838)	4,993	5,462
Profit (loss) before cost allocation and tax	929,866	112,687	178,705	84,818	567,693	(818,025)	1,055,744
Net segment revenue from external customers	940,865	260,649	818,758	62,851	1,045,469	(91,582)	3,037,011
Net segment revenue from other segments	267,229	20,000	(427,018)	128,599	11,190	0	0

Kvika Amounts are in ISK thousands

Notes to the Condensed Interim Consolidated Financial Statements

Other information

53. Pledged assets

The Group has pledged assets, in the ordinary course of banking business, to the Central Bank of Iceland to the amount of ISK 2.7 billion as at 30 June 2019 (2018: ISK 2.7 billion) to secure settlement in the Icelandic clearing systems. Further pledges have been placed in the ordinary course of banking business for netting and set-off arrangements in the total amount of ISK 0.6 billion as at 30 June 2019 (2018: ISK 0.5 billion).

54. Related parties

a. Definition of related parties

The Group has a related party relationship with the board members of the Bank, the CEO of the Bank and key employees (together referred to as management), associates as disclosed in note 24, shareholders with significant influence over the Bank, close family members of individuals identified as related parties and entities under the control or joint control of related parties.

b. Arm's length

Transactions with related parties are carried out at arm's length and subject to an annual review by the Bank's internal auditor.

c. Effects on statement of financial position

30.6.2019	**Loans & receivables**	**Deposits & payables**
Management	2,918	206,395
Associates	5,777	3,604,816
Total	8,695	3,811,210

31.12.2018	**Loans & receivables**	**Deposits & payables**
Management	79,231	212,291
Associates	7,450	3,004,717
Total	86,681	3,217,008

d. Effects on income statement

6m 2019	**Interest income**	**Interest expense**	**Fees received**	**Fees paid**
Management	4,093	1,610	1,519	5,112
Associates	22	23,619	22,793	0
Total	4,115	25,229	24,313	5,112

6m 2018	**Interest income**	**Interest expense**	**Fees received**	**Fees paid**
Shareholders	0	752	2,768	134
Management	3,086	1,744	611	4,885
Associates	3	59,146	19,885	0
Total	3,090	61,642	23,264	5,019

55. Events after the reporting date

There are no material events after the reporting date.