Consolidated Financial Statements
2019

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Highlights

Credit rating

BBB+

with negative outlook

Best Bank

EUROMONEY AWARDS FOR EXCELLENCE 2019

Robust cyber security

Nordic Financial CERT

Principles for Responsible Investment

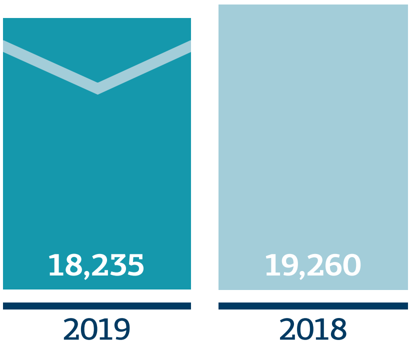
PRI

Equal Pay Certification

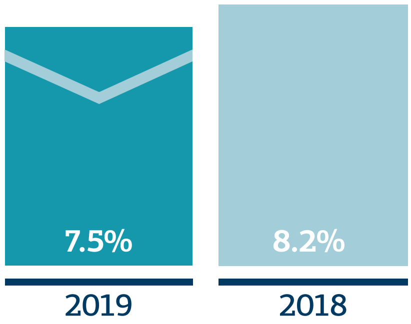
Performance Satisfaction Index

ÍSLENSKA ÁNÆGJUVOGIN

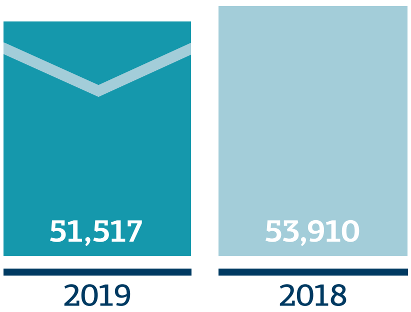
Profit



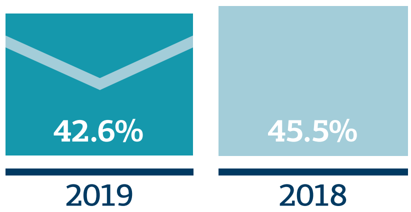
Return on equity



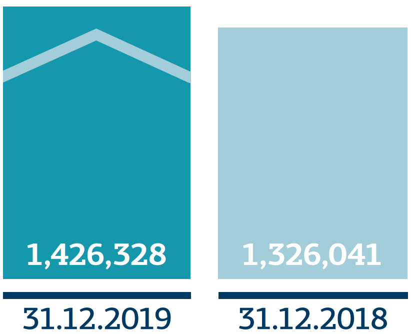
Total operating income



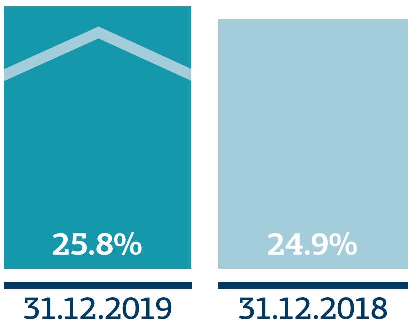
Cost-income ratio



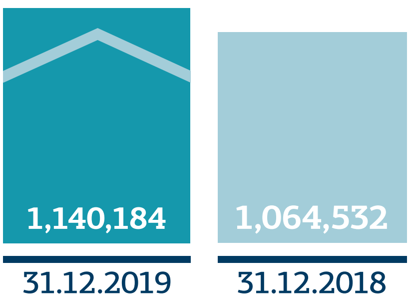
Total assets



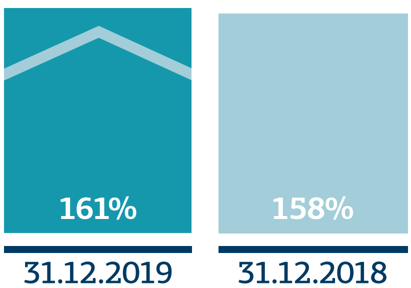
Total capital ratio



Loans and advances to customers



Total liquidity coverage ratio (LCR)



Report of the Board of Directors and the CEO

The Board of Directors and the CEO of Landsbankinn hf. (the "Bank" or "Landsbankinn") present this report together with the audited Consolidated Financial Statements of Landsbankinn hf.) for the financial year 2019, which include the Bank and its subsidiaries (collectively referred to as the "Group").

Landsbankinn is a leading financial institution in Iceland, offering a comprehensive range of financial services to individuals, corporates and investors. The Group consists of four main business segments and support functions that constitute the reportable segments presented in the Group's internal and external financial reporting (see Note 5).

Operations in 2019

Consolidated profit amounted to ISK 18,235 million for the financial year 2019 compared with ISK 19,260 million in 2018. Return on equity after tax was 7.5% as compared with 8.2% in 2018 and the cost-income ratio has declined between years, to 42.6% from 45.5% in 2018. Net interest income amounted to ISK 39,670 in 2019 as compared with ISK 40,814 million in 2018 while net fee and commission income was ISK 8,219 million as compared with ISK 8,157 million the previous year. Net impairment on loans and advances increased considerably between years and amounted to ISK 4,827 million. There is an increase of ISK 6,339 million in net gain on financial assets and liabilities at fair value between years while. Salaries and related expenses remained relatively stable year-over-year at ISK 14,458 in 2019 as compared with ISK 14,589 the previous year. The average number of full-time equivalent positions during in 2019 was 950, as compared with 961 in 2018.

Consolidated total equity amounted to ISK 247,734 million and total assets to ISK 1,426,328 million at year-end 2019, as compared with ISK 1,326,041 at year-end 2018. The year-over-year change in total assets is mostly driven by an increase of ISK 75,652 million in lending to private persons, an increase of 7.1% between years. The total capital ratio of the Group, calculated according to the Act on Financial Undertakings, was 25.8% at year-end 2019 as compared with 24.9% at year-end 2018 (see Note 47). Total deposits from financial institutions and customers increased by ISK 28,223 million between years and the carrying amount of borrowings rose by ISK 58,756 million. Subordinated liabilities increased by ISK 5,741 million year-over-year as a result of issuance of subordinated bonds in Icelandic *króna*.

In December 2019, the Bank concluded issuance of ISK Tier 2 fixed rate inflation linked subordinated bonds, in the amount of ISK 5,480 million, under the Bank's ISK 50,000 million Debt Issuance Programme. The bond series, LBANK T2I 29, has a final maturity in December 2029, but is callable in December 2024. The bonds are the Bank's inaugural subordinated bond issuance in the domestic market and are listed on Nasdaq Iceland.

In July 2019, international rating agency S&P Global Ratings affirmed Landsbankinn's long and short-term issuer credit rating of BBB+/A-2, revising its outlook from stable to negative.

As at 1 January 2019, the Group implemented the international financial reporting standard IFRS 16 Leases, using the modified retrospective approach. The impact of the implementation of IFRS 16 on the Group's financial statements is described further in Note 4.

Risk factors

The carrying amount of the Bank's credit portfolio increased by 7% in 2019 yet credit risk is similar to what it was at year-end 2018. Probability of default (PD) for the entire portfolio continued to decrease in 2019 and was 2.4% at year end. Expected credit loss (ECL) as a percentage of total loans remained unchanged during 2019 and remains well within the Bank's risk appetite. Economic capital (EC) for credit risk increased slightly during 2019. The increase is due to other assets; EC for credit risk from loans to customers decreased slightly during 2019. EC for market and currency risk decreased significantly in 2019, due to lower exposure to listed equities in the Bank's trading portfolio. Impairment charges on loans to customers increased in 2019 and an impairment loss of ISK 4,827 million before tax was recognised in the income statement. The increase in impairment charges on the credit portfolio is largely explained by new corporate defaults in 2019.

The Bank's liquidity ratios are strong both in total, in foreign currency and in individual currencies. The total liquidity coverage ratio (LCR) was 161% at year end, compared to 158% in 2018, and 769% in foreign currencies. The Central Bank of Iceland changed the Rules on Liquidity Ratio in December 2019, implementing a minimum requirement for liquidity ratio in Icelandic *króna*. Effective as of 1 January 2020, the minimum LCR in Icelandic króna is 30%. As a result of the change, the Bank now publishes its liquidity ratio in Icelandic *krón*a, which was 61% at year-end 2019.

At year-end 2019, bond issuance in foreign currency amounted to ISK 223,131 million, increasing by ISK 24,351 million during the year. Other unsecured loans in foreign currency amounted to ISK 19,496 million at the same time. The size of the programme for covered bond issuance is ISK 200,000 million and was increased from ISK 120,000 million in 2019. At year-end, outstanding covered bonds issuance amounted to ISK 140,549 million, increasing by ISK 34,240 million during the year 2019.

Market risk remains low and well within risk appetite. The Bank decreased its CPI indexation imbalance even further in 2019. The imbalance was 52% of equity at year end.

Information about the Group's risk management is included in the notes to the Consolidated Financial Statements that address risk management, and in the Bank's Pillar III Risk Report.

Equity

The Group's capital requirements are defined in Icelandic law and regulations and by the Financial Supervisory Authority (FME). The requirements are based on the European legal framework for capital requirements (CRD IV and CRR). The Bank annually assesses its own capital needs through the Internal Capital Adequacy Assessment Process (ICAAP) and the results are subsequently reviewed by the FME in the Supervisory Review and Evaluation Process (SREP).

Equity (continued)

In addition to the minimum capital requirement, the Bank is required by law to maintain certain capital buffers determined by the FME, which may, depending on the situation, be based on recommendations from the Icelandic Financial Stability Counsel (FSC).

The Bank aims to maintain capital ratios above FME's capital requirements at all times, in addition to a management capital buffer that is defined in the Bank's risk appetite. The Bank also aims to be in the highest category for risk-adjusted capital ratio, as determined and measured by the relevant credit rating agencies (see Note 46).

Landsbankinn's current dividend policy provides that the Bank aims to pay regular dividends to shareholders amounting in general to ≥50% of the previous year's profit. To achieve the Bank's target capital ratio, special dividend payments may also be made to optimise its capital structure. In determining the amount of dividend payments, the Bank's continued strong financial position shall be ensured. Regard shall be had for risk in the Bank's internal and external environment, growth prospects and the maintenance of a long-term, robust equity and liquidity position, as well as compliance with regulatory requirements of financial standing at any given time.

The AGM of the Bank held on 4 April 2019, approved the motion of the Board of Directors to pay shareholders a dividend in the amount of ISK 9,922 million, or equivalent to ISK 0.42 per share, for the operating year 2018. In accordance with the resolution of the meeting, the dividend was paid in two equal instalments, each equivalent to ISK 0.21 per share, on 10 April 2019 and 2 October 2019. The total dividend payment corresponded to 52% of net profit for the operating year 2018.

The Board of Directors intends to propose to the Annual General Meeting (AGM) that a dividend of ISK 0.40 per share be paid to shareholders for the operating year 2019 in two equal payments in 2020. The total dividend of ISK 9,450 million corresponds to 52% of the consolidated profit in 2019. If the AGM approves the dividend proposal, the capital requirement of the Group will be reduced by an amount equivalent to the dividend payment and the Bank's capital ratio, in accordance with the Act on Financial Undertakings, will decrease by 0.9 percentage points.

Economic outlook

Economic growth cooled considerably in 2019 due to a contraction in the travel industry and GDP growth may even have been slightly negative following the robust growth of previous years. The outlook is for a moderate economic recovery in coming years, supported by low yet sustainable growth in private consumption, increased public investment, rising export and a turnaround in industrial investment going forward.

Domestic economic development reflects uncertainty about global economic trends in the next 1-2 years, already materialising in the slower growth of international trade and manufacturing. Further escalation of these developments, beyond current expectations, may have a negative impact on Iceland, i.e. on the travel industry, fisheries and seafood, and heavy industry. Conversely, a positive change in global trade would have a more positive impact on the domestic economy than assumed in the forecast.

The inflation outlook improved in the latter half of 2019 and inflation is now expected to remain at or around target in coming years, as economic growth is expected to harmonise with Iceland's production capacity.

Strategy

Landsbankinn maintains a strong market share throughout Iceland and across all age groups in 2019 as in previous years. Emphasis has been placed on providing good service to customers which is simultaneously cost-effective and allows the Bank to maintain acceptable profitability. Product development, changes and innovation are a constant and necessary aspect of growth and operation and support the Bank as a leading provider of banking services in Iceland.

New focus points were added to the Bank's strategy in 2017, with 3-year goals under which emphasis was placed on increasing the offer of self-service solutions. The aim was to improve customer service by providing customers with access to banking service where and whenever. The focus points included increasing accessibility, efficiency, value-adding and initiative in service to the Bank's customers.

The year 2020 is the last year the Bank works to realise these focus points and work is already under way on shaping new goals and revising the Bank's strategy, initially formed in 2015.

Ownership

Shareholders at year-end 2019 numbered 881 as compared with 883 the previous year. The ten largest shareholders in the Bank at year-end 2019 were as follows:

Shareholders		Number of shares (in ISK million)	%
Ríkissjóður Íslands	Icelandic State Treasury	23,567.0	98.20%
Lífeyrissjóður Vestmannaeyja	Pension fund	5.0	0.02%
Vestmannaeyjabær	Local municipality	3.5	0.01%
Vinnslustöðin hf.	Corporate	1.8	0.01%
Helgi T. Helgason	Individual	0.5	0.00%
Hreiðar Bjarnason	Individual	0.5	0.00%
Árni Þ. Þorbjörnsson	Individual	0.5	0.00%
Hrefna Ösp Sigfinnsdóttir	Individual	0.4	0.00%
Steinþór Pálsson	Individual	0.3	0.00%
Hjördís Dröfn Vilhjálmsdóttir	Individual	0.3	0.00%
Top 10 total		**23,580.0**	**98.25%**
Other shareholders		44.5	0.19%
Total shares outstanding		**23,624.5**	**98.00%**
Landsbankinn hf.	Own shares	375.5	1.56%
Total shares issued		**24,000.0**	**100,00%**

Icelandic State Financial Investments (ISFI) manages the State's holding in the Bank on behalf of Ríkissjóður Íslands (the Icelandic State Treasury) in accordance with Act No. 88/2009, on Icelandic State Financial Investments.

The AGM of the Bank, held on 4 April 2019, approved the motion of the Board of Directors to authorise the Bank to acquire up to 10% of the nominal value of the Bank's share capital in accordance with Article 55 of the Act on Public Limited Companies, No. 2/1995. The price of each share is to be determined by the internal value of the Bank's shares, according to its most recently published results prior to the timing of the repurchase of the own shares. This authorisation applies until the next AGM in 2020 and the disposal of the own shares under this authorisation is subject to the approval of a shareholders meeting.

Governance

It is Landsbankinn's aim to promote good corporate governance for the overall benefit of the Bank, its shareholders, customers and the wider community. Landsbankinn complies with the most recent Guidelines on Corporate Governance issued in June 2015 (5th edition) by the Iceland Chamber of Commerce, Nasdaq Iceland and the Confederation of Icelandic Employers. The Bank publishes an annual Corporate Governance Statement on its governance practices and its compliance with the Guidelines in a dedicated chapter in the Group's annual report. The Corporate Governance Statement for the reporting year 2019 has been reviewed by the Board of Directors and the CEO. In 2019, the Centre of Corporate Governance in Iceland renewed its recognition of the Bank as a model of good corporate governance for the period 2018-2019. Moreover, the Bank observes in its operations the Guidelines of the European Banking Authority (EBA) on internal governance (EBA/GL/2017/11).

Corporate Social Responsibility

Landsbankinn received a positive review of its CSR efforts and its initial ESG rating from Sustainalytics in 2019. The Bank scored 17.5 points on a scale to 100 which means that exposure to financial risk from ESG issues is deemed low.

Corporate social responsibility (CSR) is an integral part of the overall strategy of Landsbankinn to promote economic growth, social well-being and conservation of the environment. CSR underwrites sustainability through competitiveness, the productive use of resources and good governance, having regard for human rights, anti-fraud and anti-corruption measures. In September 2019, the Bank became a founding signatory of UNEP FI's new Principles for Responsible Banking, intended to align the banking industry with the Sustainable Development Goals (SDGs) and the Paris Climate Agreement.

The Bank annually publishes a Report on Social Responsibility, disclosing information about developments in social responsibility and social

In 2019, job satisfaction at Landsbankinn scored very high in 2019 in a workplace audit carried out twice per annum. Legal equal pay certification was confirmed in March 2019 and the Bank has since operated in accordance with a certified equal pay system. The Bank's HR policy emphasises job satisfaction, a positive work environment and effective job development. In 2019, all employees received instruction following the implementation of a prevention and contingency plan against bullying, sexual or gender-based harassment, and violence (EKKO).

Other matters

A new Act on Measures against Money Laundering and Terrorist Financing entered into effect in January 2019. During the year, changes were made to the Bank's processes and systems to reflect new requirements and the Bank's increased emphasis on reducing even further the risk of its services being misused to launder money or finance terrorism.

In 2019, Landsbankinn reinforced electronic surveillance, added employees to control functions and developed user-friendly solutions to simplify ongoing monitoring of contractual relationships. Landsbankinn will continue to develop measures to monitor money laundering and terrorist financing in 2020.

In 2019, the Financial Action Task Force (FATF), placed Iceland on a list of countries that have declared their willingness to implement an action plan for remedy of the situation. The impact on the operation and activities of Landsbankinn has been limited as FATF's demand for reform is not aimed at financial institutions.

Other matters (continued)

Landsbankinn continues to emphasise responsible and secure treatment of the personal information of customers, employees and others in its operation according to the Act on Data Protection and the Processing of Personal Data and the EU's General Data Protection Regulation. The Bank continuously updates and improves processes, rules and information in the field of data protection in its operation, with an eye to securing customer rights.

Landsbankinn's remuneration policy states that compensation to the CEO and key managers shall be competitive yet moderate and not leading. The Remuneration Committee is tasked with ensuring that compensation to key managers is within the framework of the remuneration policy and shall submit an annual report on the matter to the Board of Directors. Landsbankinn's Remuneration Committee has submitted its report on compensation to key managers and considers their terms to be within the framework of the Bank's remuneration policy.

In May 2017, the Board of Directors of Landsbankinn decided to construct housing for the Bank's operation at Austurhöfn in Reykjavík. The Bank will occupy around 10.000 m2 of the new building, or ca. 60% of its square measure, and sell or rent around 6.500 m2 as premises for commerce and services. The new building will merge under one roof operations that are currently located in 12 different houses in Kvosin, Reykjavík and most of the operation currently located at Borgartún, Reykjavík. Two tenders for earthwork and concrete operations have already taken place and a third tender round is scheduled for spring 2020. Estimated conclusion of the project is 2022.

Statement by the Board of Directors and the CEO

The Consolidated Financial Statements of Landsbankinn hf. for the year ended 31 December 2019 have been prepared on a going-concern basis in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union and compliant with applicable Icelandic laws and regulations.

In our opinion, the Consolidated Financial Statements of Landsbankinn hf. give a true and fair view of the consolidated financial performance of the Group for the year 2019, its consolidated financial position as at 31 December 2019 and its consolidated cash flows for the year 2019.

Furthermore, in our opinion, the Consolidated Financial Statements of Landsbankinn hf. describe the principal risks and uncertainties faced by the Group.

The Board of Directors of the Bank and Chief Executive Officer hereby endorse the Consolidated Financial Statements of Landsbankinn hf. for the year 2019. The Board of Directors and the CEO recommend that the Consolidated Financial Statements of Landsbankinn hf. for the year 2019 be approved at the Annual General Meeting of Landsbankinn hf.

Reykjavík, 6 February 2020.

Board of Directors

Helga Björk Eiríksdóttir

Chairman

Berglind Svavarsdóttir

Einar Þór Bjarnason

Guðbrandur Sigurðsson

Guðrún Blöndal

Sigríður Benediktsdóttir

Sigurður Jón Björnsson

CEO

Lilja Björk Einarsdóttir

Independent Auditor's Report

To the Board of Directors and Shareholders of Landsbankinn hf.

Opinion

We have audited the accompanying Consolidated Financial Statements of Landsbankinn hf. (hereafter the Group) for the year 2019. The Consolidated Financial Statements comprise the Statement by the Board of Directors and CEO, the Statement of Income, the Statement of Financial Position, the Statement of Cash Flows, the Changes in Equity, a summary of significant accounting policies and other explanatory information.

In our opinion, the Consolidated Financial Statements present fairly, in all material respects, the consolidated results of operations of Landsbankinn hf. for the year 2019, its consolidated financial position as at December 31, 2019, and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU and the Financial Statements Act.

In accordance with the provisions of Article 104, paragraph 2 of the Icelandic Financial Statements Act No. 3/2006, we confirm that the Statement by the Board of Directors and CEO accompanying the Consolidated Financial Statements includes at least the information required by the Financial Statements Act if not disclosed elsewhere in the Consolidated Financial Statements.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our Report. We are independent of the Group in accordance with the Code of Ethics for Professional Accountants in Iceland, and we have fulfilled all ethical requirements therein. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the Consolidated Financial Statements for the year 2019. These matters were addressed in the context of our audit of the Consolidated Financial Statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

In our opinion the following matters were key audit matters:

Credit risk and impairment of loans and advances to customers:
We refer to the discussion on page 2 (Statement by the Board of Directors and CEO), notes 88.5 (g) on page 80 to 82 (Significant accounting policies), note 3 (b) on page 14 to 15 (Critical accounting estimates and judgements) and notes 55 to 70 on pages 48 to 62 (Credit risk).

We have defined impairment of loans and advances to customers as a key audit matter as the assumptions used in the impairment process are subjective and based on the Group´s management´s judgement. As loans and advances to customers are significant in the Consolidated Financial Statements, any change in criteria may have a significant impact on the Group´s results of operations and financial position. Our work covered the impairment of both loans and advances to customers and loans to corporations and institutions.

As part of the audit, we performed tests of key controls related to the impairment of the loan portfolio. The focus of these procedures included the analysis of loss events and assumptions used in the valuation. We examined information in the systems and models used by the Group to estimate impairment. We also assessed the manner in which management evaluated the results of the valuation and responded to deviations if they occurred.

We also performed substantive procedures on loan impairment, including assessing the Group's impairment methodology and whether the methodology is in compliance with International Financial Reporting Standards. We also chose a risk-based sample based on loan and customers' characteristics. Loans with a higher probability of default and loan loss, and that are more likely to go undetected by the Group were examined specifically. Underlying loan agreements were examined, underlying collateral verified and management´s assumptions were assessed.

Other Information

The Board of Directors and the CEO are responsible for all information presented by the Group, both the Consolidated Financial Statements as well as other information. The other information comprises the information included in the Annual Report, but does not include the Consolidated Financial Statements and our Auditor's Report thereon. Our opinion on the Consolidated Financial Statements does not cover the information in the Annual Report or other documents issued by the Group, and we do not express any form of assurance on the information in those documents thereon. In connection with our audit of the Consolidated Financial Statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the Consolidated Financial Statements, our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we conclude that there are material misstatements or inconsistencies therein, we are required to communicate the matter to the Board of Directors and take appropriate action depending on the severity of the misstatement.

The Board of Directors and CEO's Responsibilities for the Consolidated Financial Statements

The Board of Directors and CEO are responsible for the preparation and fair presentation of the Consolidated Financial Statements in accordance with International Financial Reporting Standards as adopted by the EU and the Financial Statements Act, and for such internal control as management determines is necessary to enable the preparation of Consolidated Financial Statements that are free from material misstatement, whether due to fraud or error.

The Board of Directors and CEO's Responsibilities for the Consolidated Financial Statements (continued)

In preparing the Consolidated Financial Statements, the Board of Directors and CEO are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Board of Directors and CEO either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

The Board of Directors and the Audit Committee are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the Consolidated Financial Statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these Consolidated Financial Statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the Consolidated Financial Statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group´s internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management. Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exist related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our Auditor's Report to the related disclosures in the Consolidated Financial Statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our Auditor's Report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the Consolidated Financial Statements, including the disclosures, and whether the Consolidated Financial Statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the Consolidated Financial Statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicated with the Board of Directors and the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identified during our audit.

We also provided the Board of Directors and the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and communicated with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Board of Directors and the Audit Committee, we determined those matters that were of most significance in the audit of the Consolidated Financial Statements of the current year and are therefore the key audit matters. We describe these matters in our Auditor's Report unless law or regulations precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our Report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

For and on behalf of Grant Thornton endurskoðun ehf.
Reykjavík, 6 February 2020

Davíð Arnar Einarsson	J. Sturla Jónsson
State Authorized Public Accountant	State Authorized Public Accountant

Consolidated Income Statement for the Year ended 31 December 2019

Notes		2019	2018
	Interest income	72,172	69,378
	Interest expense	(32,502)	(28,564)
6	**Net interest income**	**39,670**	**40,814**
7	Net valuation adjustments and impairment	(4,827)	1,352
	Net interest income after net valuation adjustments and impairment	**34,843**	**42,166**
	Fee and commission income	11,528	11,220
	Fee and commission expense	(3,309)	(3,063)
8	**Net fee and commission income**	**8,219**	**8,157**
9	Net gain on financial assets and liabilities at FVTPL	7,993	1,654
10	Net foreign exchange loss	(584)	(1,497)
11	Other income and (expenses)	1,046	3,430
	Net Other operating income	**8,455**	**3,587**
	Total net operating income	**51,517**	**53,910**
12	Salaries and related expenses	14,458	14,589
13	Other operating expenses	9,534	9,348
	Total operating expenses	**23,992**	**23,937**
	Profit before tax	**27,525**	**29,973**
14	Income tax	(5,086)	(6,853)
88.16	Tax on liabilities of financial institutions	(4,204)	(3,860)
	Profit for the year	**18,235**	**19,260**
	Profit for the year attributable to:		
	Owners of the Bank	18,235	19,260
	Non-controlling interests	0	0
	Profit for the year	**18,235**	**19,260**
	Earnings per share:		
36	Basic and diluted earnings per share from operations (ISK)	**0.77**	**0.81**

Consolidated Statement of Comprehensive Income for the Year ended 31 December 2019

Notes		2019	2018
	Profit for the year	18,235	19,260
	Other comprehensive income for the year, after tax	0	0
	Total comprehensive income for the year	**18,235**	**19,260**

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

Landsbankinn hf. Consolidated Financial Statements 2019 8 All amounts are in ISK million

Consolidated Statement of Financial Position as at 31 December 2019

Notes		2019	2018
	Assets		
18, 75	Cash and balances with Central Bank	69,824	70,854
19	Bonds and debt instruments	115,262	77,058
20	Equities and equity instruments	30,019	23,547
21	Derivative instruments	2,694	1,923
22, 75	Loans and advances to financial institutions	47,929	71,385
23, 75	Loans and advances to customers	1,140,184	1,064,532
24	Investments in equity-accounted associates	1,471	1,453
25	Property and equipment	6,743	5,548
26	Intangible assets	2,296	2,622
32	Deferred tax assets	20	134
27	Other assets	8,864	5,655
28	Assets classified as held for sale	1,022	1,330
	Total assets	**1,426,328**	**1,326,041**
	Liabilities		
29	Due to financial institutions and Central Bank	48,062	34,609
30	Deposits from customers	707,813	693,043
21	Derivative instruments and short positions	5,390	6,546
31, 75	Borrowings	373,168	314,412
33	Other liabilities	25,050	24,451
28	Liabilities associated with assets classified as held for sale	30	30
34	Subordinated liabilities	19,081	13,340
	Total liabilities	**1,178,594**	**1,086,431**
35	**Equity**		
	Share capital	23,625	23,625
	Share premium	120,630	120,630
	Reserves	14,334	12,130
	Retained earnings	89,145	83,225
	Total equity attributable to owners of the Bank	**247,734**	**239,610**
	Non-controlling interests	0	0
	Total equity	**247,734**	**239,610**
	Total liabilities and equity	**1,426,328**	**1,326,041**

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

Landsbankinn hf. Consolidated Financial Statements 2019 9 All amounts are in ISK million

Consolidated Statement of Changes in Equity for the Year ended 31 December 2019

Notes										
		Attributable to owners of the Bank								
				Reserves*						
	Change in equity for the year 2019	**Share capital**	**Share premium**	**Statutory**	**Unrealised gains in subsidiaries and equity-accounted associates reserve**	**Fair value changes of financial assets designated at FVTPL**	**Retained earnings**	**Total**	**Non-controlling interests**	**Total**
	Balance as at 31 December 2018	23,625	120,630	6,000	5,153	977	83,225	239,610		239,610
4	Impact of adopting IFRS 16 at 1 January 2019						(188)	(188)		(188)
	Restated balance at 1 January 2019	**23,625**	**120,630**	**6,000**	**5,153**	**977**	**83,037**	**239,422**	**0**	**239,422**
	Profit for the year						18,235	18,235		18,235
	Transferred (from) to restricted reserves				(2,444)	4,648	(2,204)	0		0
	Dividends paid						(9,922)	(9,922)		(9,922)
35	**Balance as at 31 December 2019**	**23,625**	**120,630**	**6,000**	**2,709**	**5,625**	**89,145**	**247,734**	**0**	**247,734**
	Change in equity for the year 2018									
	Balance as at 31 December 2017	23,640	120,764	6,000	2,949	3,953	88,751	246,057		246,057
	Impact of adopting IFRS 9 at 1 January 2018						(482)	(482)		(482)
	Impact of adopting IFRS 15 at 1 January 2018						(254)	(254)		(254)
	Restated balance at 1 January 2018	**23,640**	**120,764**	**6,000**	**2,949**	**3,953**	**88,015**	**245,321**	**0**	**245,321**
	Profit for the year						19,260	19,260		19,260
	Transferred to restricted retained earnings				2,204	(2,976)	772	0		0
	Purchase of own shares	(15)	(135)					(150)		(150)
	Dividends paid						(24,822)	(24,822)		(24,822)
35	**Balance as at 31 December 2018**	**23,625**	**120,630**	**6,000**	**5,153**	**977**	**83,225**	**239,610**	**0**	**239,610**

*In accordance with Act. No. 2/1995, on Public Limited Companies and Act No. 3/2006, on Annual Financial Statements.

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

Landsbankinn hf. Consolidated Financial Statements 2019 10 All amounts are in ISK million

Consolidated Statement of Cash Flows for the Year ended 31 December 2019

Notes		2019	2018
	Operating activities		
	Profit for the year	18,235	19,260
	Adjustments for non-cash items included in profit for the year	(31,565)	(31,331)
	Changes in operating assets and liabilities	(76,047)	7,486
	Interest received	69,602	66,350
	Interest paid	(25,929)	(23,717)
9	Dividends received	1,737	2,392
	Income tax and special income tax on financial institutions paid	(6,698)	(6,830)
	Tax on liabilities of financial institutions paid	(3,860)	(3,330)
	Net cash (used in) from operating activities	**(54,525)**	**30,280**
	Investing activities		
	Acquisition of additional shares in associates	-	(62)
25	Purchase of property and equipment	(1,642)	(824)
25	Proceeds from sale of property and equipment	13	230
26	Purchase of intangible assets	(85)	(64)
	Investing activities	**(1,714)**	**(720)**
	Financing activities		
31	Proceeds from borrowings	78,731	53,661
	Repayment of borrowings	(28,179)	(40,187)
	Proceeds from subordinated liabilities	5,492	12,772
	Repayment of subordinated liabilities	-	(89)
	Rent paid	(582)	-
35	Purchase of own shares	-	(150)
35	Dividends paid	(9,922)	(24,822)
	Financing activities	**45,540**	**1,185**
	Cash and cash equivalents as at the beginning of the year	81,723	53,174
	Net change in cash and cash equivalents	(10,699)	30,745
	Effect of exchange rate changes on cash and cash equivalents held	(320)	(2,196)
	Cash and cash equivalents as at year end	**70,704**	**81,723**
	Investing and financing activities not affecting cash flows		
	Acquisition of additional shares in associates	-	(21)
	Sold equipment/intangible assets	-	21
	Cash and cash equivalents is specified as follows:		
18	Cash and balances with Central Bank	69,824	70,854
22	Bank accounts with financial institutions	26,438	40,913
18	Mandatory and special restricted balances with Central Bank	(25,558)	(30,043)
	Cash and cash equivalents as at year end	**70,704**	**81,723**

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

Landsbankinn hf. Consolidated Financial Statements 2019 11 All amounts are in ISK million

Consolidated Statement of Cash Flows for the Year ended 31 December 2019

Notes		2019	2018
	Adjustments for non-cash items included in profit for the year		
6	Net interest income	(39,670)	(40,814)
7, 66	Net impairment on loans and advances, guarantees and other assets	4,827	(223)
7	Reversals of loss from foreign currency linkage of loans and advances to customers	-	(1,129)
9	Net gain on financial assets and liabilities at FVTPL	(7,993)	(1,654)
10	Net foreign exchange loss	904	3,693
11	Gain on sale of property and equipment	(3)	(121)
11	Net loss (gain) on assets classified as held for sale	50	(2,392)
13	Depreciation and amortisation	1,334	879
11, 24	Share of profit of equity-accounted associates	(304)	(283)
14	Income tax	5,086	6,853
88.16	Tax on liabilities of financial institutions	4,204	3,860
		(31,565)	**(31,331)**
	Changes in operating assets and liabilities		
	Change in reserve requirement with Central Bank	4,485	2,193
	Change in bonds and equities	(37,378)	47,927
	Change in derivatives	(3)	-
	Change in loans and advances to financial institutions	11,042	(9,542)
	Change in loans and advances to customers	(73,263)	(121,026)
	Change in other assets	954	(6,826)
	Change in assets classified as held for sale	258	414
	Change in due to financial institutions and Central Bank	13,462	2,578
	Change in deposits from customers	11,715	84,239
	Change in tax liability	113	(173)
	Change in other liabilities	(7,432)	7,696
	Change in liabilities associated with assets classified as held for sale	-	6
		(76,047)	**7,486**

Change in liabilities due to financing activities

			Non-cash changes			
	As at 1.1.2019	**Cash flow**	**Accrued interest**	**Foreign exchange**	**Change in the fair value**	**As at 31.12.2019**
Secured borrowings	106,309	27,495	6,745	-	-	140,549
Senior unsecured bonds	100,807	19,620	1,285	993	-	122,705
Senior unsecured bonds held to hedge long-term borrowings	84,634	(997)	1,041	1,492	643	86,813
Commercial paper issued	2,705	749	151	-	-	3,605
Other unsecured loans	19,958	(1,975)	774	739	-	19,496
Subordinated liabilities	13,340	5,017	466	258	-	19,081
Total	**327,753**	**49,909**	**10,462**	**3,482**	**643**	**392,249**

			Non-cash changes			
	As at 1.1.2018	**Cash flow**	**Accrued interest**	**Foreign exchange**	**Change in the fair value**	**As at 31.12.2018**
Secured borrowings	70,253	33,003	3,053	-	-	106,309
Senior unsecured bonds	113,420	(20,220)	170	7,437	-	100,807
Senior unsecured bonds held to hedge long-term borrowings	78,065	-	278	5,506	785	84,634
Commercial paper issued	7,433	(5,019)	291	-	-	2,705
Other unsecured loans	12,703	5,709	136	1,410	-	19,958
Subordinated liabilities	77	12,682	135	446	-	13,340
Total	**281,951**	**26,155**	**4,063**	**14,799**	**785**	**327,753**

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

Landsbankinn hf. Consolidated Financial Statements 2019 12 All amounts are in ISK million

Notes to the Consolidated Financial Statements for the Year 2019

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General

1. Reporting entity

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

The Consolidated Financial Statements of the Bank for the year ended 31 December 2019 include the Bank and its subsidiaries (collectively referred to as the "Group" and individually as "Group entities"). The Group's primary lines of business are corporate and personal banking, markets, asset management and other related financial services. The Group operates solely in Iceland.

2. Basis of preparation

These Consolidated Financial Statements for the year ended 31 December 2019 have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union. The Consolidated Financial Statements have, furthermore, been prepared in accordance with Act No. 3/2006, on Annual Financial Statements, Act No. 161/2002, on Financial Undertakings, and Rules No. 834/2003, on Accounting for Credit Institutions.

The issue of these Consolidated Financial Statements was authorised by the Board of Directors and the CEO of the Bank on 6 February 2020.

Significant accounting policies are summerised in Note 88. This is the first set of the Group's annual Consolidated Financial Statements in which IFRS 16 *Leases* has been applied. Changes to significant accounting policies are described in Note 4.

Going concern

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

Functional and presentation currency

The functional currency of the Bank and its individual Group entities is Icelandic króna (ISK) and all amounts are presented in ISK, rounded to the nearest million unless otherwise stated.

3. Critical accounting estimates and judgements in applying accounting policies

The preparation of the consolidated financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

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

(a) Classification of financial instruments

Financial instruments under IFRS 9 are accounted for according to their classification. Professional judgement is applied and determination of the appropriate classification depends on the contractual cash flows of the financial asset (the Solely Payments of Principal and Interest (SPPI) test) and the objective of the business model within which the financial instrument is held. For further details on the accounting for these instruments under IFRS 9, see Note 88.5

(b) Impairment losses on loans and advances

Measurement of expected credit losses on loans, financial guarantees and loan commitments measured at amortised cost:

Measurement of expected credit losses is based on the three-stage expected credit loss model under IFRS 9. Allowance is calculated as the 12-month expected credit loss or the lifetime expected credit loss.

Expected credit losses depend on whether the credit risk has increased significantly since initial recognition. A significant increase in credit risk is defined in Note 88.5(g). If the credit risk has not increased significantly, the loss allowance equals the expected credit losses resulting from loss events that are possible within the next 12 months (Stage 1). If the credit risk has increased significantly the allowance measured equals the lifetime expected credit losses (Stage 2 and 3). When determining whether the credit risk on a financial instrument has increased significantly since initial recognition, the Group will consider reasonable and supportable information that is relevant and available without undue cost and effort, including both quantitative and qualitative information.

The expected credit loss is calculated for all loans as a function of PD, EAD and LGD, is discounted using the effective interest rate (EIR), and incorporates forward-looking information. The forward-looking information reflects the expectations of the Valuation Team, the Bank's Economic Research department, and involves the creation of scenarios of relevant economic variables, including an assessment of the probability for each scenario.

3. Critical accounting estimates and judgements in applying accounting policies (continued)

(b) Impairment losses on loans and advances (continued)

Measurement of expected credit losses on loans, financial guarantees and loan commitments measured at amortised cost (continued):

The following table shows certain key macroeconomic variables used in modelling the allowance for credit losses for Stage 1 and Stage 2. Projections for the upside scenarios, base case scenario and downside scenarios are averages for the next 12 months and then for the remainder of the forecast period, which represents a medium-term view.

	Upside scenario		Base case senario		Downside scenario	
As at 31.12.2019	**Next 12 Months**	**Remainder of the Forecast Period**	**Next 12 Months**	**Remainder of the Forecast Period**	**Next 12 Months**	**Remainder of the Forecast Period**
GDP growth	3.5%	3.5%	2.0%	2.4%	0.0%	1.3%
Unemployment rate	3.0%	2.3%	4.0%	3.3%	6.0%	5.0%
Base rate	3.7%	3.9%	3.0%	3.1%	2.9%	2.2%
Inflation	2.4%	2.6%	2.4%	2.5%	4.4%	2.7%
EUR/ISK exchange rate, average	136.8	135.6	138.5	138.0	154.4	154.4
Housing Price index, y/y change	7.0%	6.0%	4.5%	4.0%	2.0%	1.5%

	Upside scenario		Base case senario		Downside scenario	
As at 31.12.2018	**Next 12 Months**	**Remainder of the Forecast Period**	**Next 12 Months**	**Remainder of the Forecast Period**	**Next 12 Months**	**Remainder of the Forecast Period**
GDP growth	2.9%	3.1%	2.4%	2.1%	1.0%	0.8%
Unemployment rate	2.0%	2.0%	2.7%	3.0%	3.5%	4.3%
Base rate	5.3%	5.7%	4.8%	4.6%	4.0%	1.9%
Inflation	4.1%	4.1%	3.7%	3.2%	2.7%	1.6%
EUR/ISK exchange rate, average	136.0	132.0	139.0	139.0	142.9	156.7
Housing Price index, y/y change	6.0%	9.0%	4.0%	7.0%	2.0%	2.5%

	2019			2018		
	Upside scenario	**Base senario**	**Downside senario**	**Upside scenario**	**Base senario**	**Downside senario**
Allowance for impairment (stage 1 and stage 2)	4,095	4,452	5,443	3,739	3,785	3,832
Proportion of assets in Stage 2	7.8%	8.0%	10.6%	7.2%	7.3%	7.4%

	Reported under IFRS 9	
	2019	**2018**
Allowance for impairment (stage 1 and stage 2)	4,614	3,790

Economic variables from different scenarios have an impact on the calculation of ECL through the models for PD, both 12-month and lifetime, and LGD and EAD. The models that are affected by economic variables are all developed using historical data. Changes in economic variables can have positive or negative effects on the measurement of ECL. However, the most significant factor is the current status of risk factors.

Staging and ECL estimation for individually significant loans is done manually on a quarterly basis. When assessing individually significant loans manually, the Group considers reasonable and supportable information that is relevant and available without undue cost and effort, including both quantitative and qualitative information and analysis based on the Group's historical experience, expert credit assessment and forward-looking information. Only Stage 3 loans are manually estimated for ECL.

Note 88.5(g) provides more details on the impairment process and methodology.

(c) Valuation of financial instruments

The fair value of financial instruments where no active market exists or where quoted prices are not otherwise available are determined by using valuation techniques. In these cases, the fair values are estimated from observable data in respect of similar financial instruments or using models. Where observable market inputs are not available, they are estimated based on appropriate assumptions. Where valuation techniques (for example, models) are used to determine fair value, they are validated and regularly reviewed by discrete and qualified in-house reviewers. All models are certified before use, and calibrated to ensure that the outputs reflect actual data and comparative market prices. Wherever practical, models are confined to observable data; however, areas such as volatility, correlation and credit risk, whether own or counterparty, require management to make estimates. Changing assumptions on these factors could affect the reported fair value of financial instruments.

(d) Determination of control over investees

Management applies professional judgement to determine whether the control indicators set out in Note 88.1 Consolidation and non-controling interests, indicate that the Group controls an investee.

Landsbankinn hf. Consolidated Financial Statements 2019 15 All amounts are in ISK million

4. Changes in accounting policies

The Group initially adopted the accounting standard IFRS 16 *Leases* as at 1 January 2019, using the modified retrospective approach. As a result, comparative information for the year 2018 has not been restated and continues to be reported under the previous standard IAS 17 *Leases* in the Financial Statements. IFRS 16 expands the balance sheet for the Group as a lessee as the standard requires right of use assets and lease liabilities for operating leases, that were previously recognised as an operating expense in the income statement, to be recognised on the balance sheet. Changes to accounting policies for leases are detailed further in Note 88.38.

The impact of transition to IFRS 16

Under the modified retrospective approach of IFRS 16 the Group recognises the cumulative effect of the difference of the carrying amount of right of use assets and lease liabilities, net of tax, in retained earnings as at 1 January 2019. The lease liabilities are measured at an amount equal to the present value of the remaining lease payments, discounted using the incremental borrowing rate of the Group as at 1 January 2019; the right of use of assets is measured at the amount equal to the present value of the lease liability at the lease commencement date, discounted using the same incremental borrowing rate less cumulative depreciation as at 1 January 2019. The impact on transition is summarised in the following table:

	1 January 2019
Right-of-use assets	2,595
Deferred tax asset	46
Lease liabilities	(2,829)
Retained earnings	188

When measuring lease liabilities, the Group discounted lease payments using its incremental borrowing rate as at 1 January 2019, 3.0% for inflation-indexed leases and 6.0% for non-inflation-indexed leases.

	1 January 2019
Operating lease commitments disclosed in the Consolidated Financial Statements as at 31 December 2018	3,346
Recognition exemption : Leases with a remaining lease term of less than 12 months	(11)
Effect of using incremental borrowing rate	(506)
Lease liabilities as at 1 January 2019	**2,829**

5. Operating segments

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

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

• **Personal Banking** offers individuals and small and medium-size businesses outside the capital city region diverse financial services through digital service channels, both online banking and apps, alongside conventional service through the Bank's branch network and Customer Service Centre.

• **Corporate Banking** offers financial services to corporate clients and to small and medium-size businesses in the capital city region and manages a corporate online banking platform that offers electronic banking services.

• **Markets** provides brokerage services in securities, foreign currencies and derivatives, sale of securities issues, money market lending and advisory services. The division is a market maker of listed securities and foreign currencies in the domestic market. Markets provides a range of wealth and asset management products and services for individuals, corporations and institutional investors. Landsbréf hf. a subsidiary of the Bank, is included in Market's segments reporting.

• **Treasury** incorporates the Bank's funding and liquidity management, market making in money markets, and determines the Bank's internal pricing. Treasury also manages the Bank's exchange rate, interest rate and inflation risks, within limits set by the Board of Directors.

Support functions are comprised of Finance (excluding Treasury), Risk Management, IT and the CEO's Office. The CEO's Office is comprised of Human Resources, Marketing & Communications and Compliance. The Bank's Internal Audit department is also included in support functions; however, it is independent and reports directly to the Bank's Board of Directors.

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

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

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

Revenue from transactions with any single external customer was within 10% of the Group's total revenue during the period from 1 January to 31 December 2019 and the corresponding period in 2018.

Landsbankinn hf. Consolidated Financial Statements 2019 16 All amounts are in ISK million

5. Operating segments (continued)

1 January - 31 December 2019	Personal Banking	Corporate Banking	Markets	Treasury	Support functions	Recon- ciliation	Total
Net interest income	16,674	18,821	709	3,597	(68)	(63)	**39,670**
Net valuation adjustments and impairment	(1,424)	(3,409)	1	4	1	-	**(4,827)**
Net fee and commission income	4,114	699	3,761	(276)	159	(238)	**8,219**
Other net operating income (expenses)	808	26	(134)	7,591	220	(56)	**8,455**
Total operating income (expense)	**20,172**	**16,137**	**4,337**	**10,916**	**312**	**(357)**	**51,517**
Operating expenses	(6,550)	(2,121)	(2,368)	(1,666)	(11,542)	255	**(23,992)**
Profit (loss) before cost allocation and tax	**13,622**	**14,016**	**1,969**	**9,250**	**(11,230)**	**(102)**	**27,525**
Cost allocated from support functions to business segments	(4,651)	(2,829)	(1,506)	(885)	9,871	-	**0**
Profit (loss) before tax	**8,971**	**11,187**	**463**	**8,365**	**(1,359)**	**(102)**	**27,525**
Net revenue (expenses) from external customers	26,926	26,132	3,902	(5,368)	282	-	**51,874**
Net revenue (expenses) from other segments	(6,754)	(9,995)	435	16,284	30	-	**0**
Total operating income	**20,172**	**16,137**	**4,337**	**10,916**	**312**	**0**	**51,874**
As at 31 December 2019							
Total assets	510,568	599,414	13,601	548,039	17,659	(262,953)	**1,426,328**
Total liabilities	466,799	481,045	7,325	468,719	17,659	(262,953)	**1,178,594**
Allocated capital	43,769	118,369	6,276	79,320	-		**247,734**

1 January - 31 December 2018	Personal Banking	Corporate Banking	Markets	Treasury	Support functions	Recon- ciliation	Total
Net interest income	14,277	18,763	649	6,978	24	123	**40,814**
Net valuation adjustments and impairment	458	902	(2)	(6)	-	-	**1,352**
Net fee and commission income	3,712	789	4,105	(388)	177	(238)	**8,157**
Other net operating income (expenses)	301	13	(1,300)	1,960	2,706	(93)	**3,587**
Total operating income (expense)	**18,748**	**20,467**	**3,452**	**8,544**	**2,907**	**(208)**	**53,910**
Operating expenses	(6,424)	(1,926)	(2,300)	(1,783)	(11,760)	256	**(23,937)**
Profit (loss) before cost allocation and tax	**12,324**	**18,541**	**1,152**	**6,761**	**(8,853)**	**48**	**29,973**
Cost allocated from support functions to business segments	(5,026)	(3,016)	(1,523)	(869)	10,434	-	**0**
Profit (loss) before tax	**7,298**	**15,525**	**(371)**	**5,892**	**1,581**	**48**	**29,973**
Net revenue from external customers	26,292	30,264	3,026	(8,314)	2,850	-	**54,118**
Net revenue (expenses) from other segments	(7,544)	(9,797)	426	16,858	57	-	**0**
Total operating income	**18,748**	**20,467**	**3,452**	**8,544**	**2,907**	**0**	**54,118**
As at 31 December 2018							
Total assets	477,238	571,821	13,844	519,950	15,734	(272,546)	**1,326,041**
Total liabilities	432,457	452,821	6,933	451,032	15,734	(272,546)	**1,086,431**
Allocated capital	44,781	119,000	6,911	68,918	-		**239,610**

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Notes to the Consolidated Income Statement

6. Net interest income

See accounting policy in Note 88.33.

	2019			2018		
Interest income	**Amortised cost**	**FVTPL**	**Total**	**Amortised cost**	**FVTPL**	**Total**
Cash and balances with Central Bank	1,747	14	1,761	1,917	21	1,938
Bonds and debt instruments	229	-	229	827	-	827
Loans and advances to financial institutions	240	-	240	50	-	50
Loans and advances to customers	67,688	655	68,343	65,535	892	66,427
Other interest income	24	1,575	1,599	69	67	136
Total	**69,928**	**2,244**	**72,172**	**68,398**	**980**	**69,378**
Interest expense						
Due to financial institutions and Central Bank	(1,151)	-	(1,151)	(961)	-	(961)
Deposits from customers	(17,744)	-	(17,744)	(18,508)	-	(18,508)
Borrowings	(9,978)	(1,047)	(11,025)	(8,357)	(251)	(8,608)
Other interest expense	(178)	(1,938)	(2,116)	(4)	(344)	(348)
Subordinated liabilities	(466)	-	(466)	(139)	-	(139)
Total	**(29,517)**	**(2,985)**	**(32,502)**	**(27,969)**	**(595)**	**(28,564)**
Net interest income	**40,411**	**(741)**	**39,670**	**40,429**	**385**	**40,814**

Net interest income, calculated based on the effective interest rate method, amounted to ISK 39,669 million for the year ended 2019 as compared with ISK 40,811 million for the year ended 2018.

7. Net valuation adjustments and impairment

See accounting policy in Note 88.5 (g).

	2019	**2018**
Net impairment on loans and advances to customers and financial institutions	(4,854)	299
Net impairment on other financial assets	27	(76)
Reversals of foreign currency linkage loans and advances to customers	-	1,129
Net valuation adjustments and impairment	**(4,827)**	**1,352**
Valuation adjustments and impairment by customer type		
Financial institutions	1	(4)
Individuals	(168)	488
Corporates	(4,660)	868
Net valuation adjustments and impairment	**(4,827)**	**1,352**

8. Net fee and commission income

See accounting policy in Note 88.34.

	2019			2018		
	Fee and commission income	**Fee and commission expense**	**Net fee and commission income**	**Fee and commission income**	**Fee and commission expense**	**Net fee and commission income**
Capital Markets	3,906	(579)	3,327	4,166	(657)	3,509
Loans and guarantees	899	-	899	892	-	892
Payment cards	4,765	(2,066)	2,699	4,140	(1,808)	2,332
Collection and payment services	906	(168)	738	911	(160)	751
Other	1,052	(496)	556	1,111	(438)	673
Total	**11,528**	**(3,309)**	**8,219**	**11,220**	**(3,063)**	**8,157**

During the year 2019, ISK 681 million was recognised as income from service contracts with customers which fall under the scope of IFRS 15. Furthermore, during the year ISK 980 million was recognised as prepaid income under Other liabilities.

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9. Net gain (loss) on financial assets and liabilities at FVTPL

See accounting policy in Note 88.35.

Net gain (loss) on financial assets and liabilities at FVTPL	2019	2018
Bonds and debt instruments	1,745	227
Equities and equity instruments	5,231	1,842
Derivatives and underlying hedges	1,079	(1,093)
Loans and advances to customers	18	(39)
Net (loss) gain on fair value hedges	(80)	717
Total	**7,993**	**1,654**

The dividend income below is recognised in the income statement in “Net gain (loss) on financial assets and liabilities at FVTPL”.

Dividend income	2019	2018
Net gain on financial assets in the Trading book	27	46
Net gain on financial assets and liabilities in the Banking book	1,424	2,346
Total	**1,451**	**2,392**

10. Net foreign exchange gain (loss)

See accounting policy in Note 88.36.

Assets	2019	2018
Cash and balances with Central Bank	103	11
Bonds and debt instruments	1,018	4,853
Equities and equity instruments	-	49
Derivative instruments	(1,528)	(3,972)
Loans and advances to financial institutions	2,002	6,366
Loans and advances to customers	4,655	12,756
Other assets	(296)	(736)
Total	**5,954**	**19,327**
Liabilities		
Due to financial institutions and Central Bank	9	31
Deposits from customers	(3,063)	(6,127)
Borrowings	(3,224)	(14,353)
Other liabilities	(2)	71
Subordinated liabilities	(258)	(446)
Total	**(6,538)**	**(20,824)**
Net foreign exchange loss	**(584)**	**(1,497)**

The foreign exchange difference that arose on financial instruments not measured at fair value through profit or loss, amounted to a gain of ISK 6,464 million on financial assets (2018: gain of ISK 18,396 million) and a loss of ISK 6,538 million on financial liabilities (2018: loss of ISK 20,824 million).

11. Other income and expenses

See accounting policy in Note 88.37.

	Notes	2019	2018
Gain on sale of property and equipment	25	3	129
(Loss), gain on repossessed collateral	28	(50)	2,392
Share of profit of equity-accounted associates	24	304	282
Other		789	627
Total		**1,046**	**3,430**

12. Salaries and related expenses

See accounting policy in Note 88.30.

	2019	2018
Salaries	11,136	11,247
Contributions to defined pension plans	1,671	1,669
Social security contributions	850	877
Special financial activities tax on salaries	709	705
Other related expenses	92	91
Total	**14,458**	**14,589**

	2019	2018
Number of full-time equivalent positions at year-end	893	919
Average number of full-time equivalent positions during the year	950	961

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Notes to the Consolidated Financial Statements

13. Other operating expenses

	2019	2018
Information technology	2,353	2,088
Real estate and fixtures	905	905
Advertising and marketing	805	800
Operating lease rentals	16	586
FME supervisory expenses	489	471
Contribution to the Debtors' Ombudsman	77	76
Audit and related services	137	145
Other professional services	588	470
Depreciation and amortisation	1,334	879
Contribution to the Depositors' and Investors' Guarantee Fund	1,115	1,319
Other operating expenses	1,715	1,609
Total	**9,534**	**9,348**

Audit and related services	2019	2018
Audit and reviews of financial statements	133	142
Other audit-related services	4	3
Total	**137**	**145**

Depreciation and amortisation	Notes	2019	2018
Amortisation of property and equipment	25	438	395
Depreciation of intangible assets	26	411	484
Amortisation of Right-of-use assets	38	485	-
Total		**1,334**	**879**

14. Income tax

See accounting policy in Note 88.15.

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

	2019	2018
Current tax expense	(3,909)	(5,547)
Special income tax on financial institutions	(1,067)	(1,415)
Difference of prior year's imposed and calculated income tax	3	(77)
Origination and reversal of temporary differences due to deferred tax assets/liabilities	(113)	186
Total	**(5,086)**	**(6,853)**

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

		2019		2018
Profit before tax		27,525		29,973
Tax on liabilities of financial institutions		(4,204)		(3,860)
Profit before income tax		23,321		26,113
Income tax calculated using the domestic corporate income tax rate	20.0%	(4,664)	20.0%	(5,223)
Special income tax on financial institutions	4.6%	(1,067)	5.4%	(1,415)
Income not subject to tax	(7.0%)	1,625	(3.0%)	788
Non-deductible expenses	4.3%	(993)	3.6%	(927)
Other	(0.1%)	13	(0.3%)	(76)
Effective income tax	**21.8%**	**(5,086)**	**26.2%**	**(6,853)**

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15. Classification and fair values of financial assets and liabilities

See accounting policy in Note 88.5 (b).

Under IFRS 9, financial assets must be classified into categories that reflects the cash flow characteristic of the assets and the objective of business model for managing the assets. Subsequent measurement of each category is specified below:

- Financial assets measured at amortised cost
- Financial assets mandatorily measured at fair value through profit or loss
- Financial assets designated at fair value through profit or loss
- Financial liabilities measured at amortised cost.
- Financial liabilities measured at fair value through profit or loss.

The following table shows the classification of the Group's financial assets and liabilities according to IFRS 9 and their fair values as at 31 December 2019:

		Carrying amount					Fair value			
As at 31 December 2019	**Notes**	**Amortised cost**	**Mandatorily at FVTPL**	**Designated at FVTPL**	**Other financial liabilities**	**Total**	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets measured at fair value										
Bonds and debt instruments	19	-	108,461	2,781	-	111,242	111,013	79	150	111,242
Equities and equity instruments	20	-	30,019	-	-	30,019	12,939	-	17,080	30,019
Derivative instruments	21	-	2,694	-	-	2,694	-	2,694	-	2,694
Loans and advances to customers	23	-	14,679	-	-	14,679	-	-	14,679	14,679
		0	**155,853**	**2,781**	**0**	**158,634**	**123,952**	**2,773**	**31,909**	**158,634**
Financial assets not measured at fair value										
Cash and balances with Central Bank	18	69,824	-	-	-	69,824	-	69,824	-	69,824
Bonds and debt instruments	19	4,020		-	-	4,020	-	4,148	-	4,148
Loans and advances to financial institutions	22	47,929	-	-	-	47,929	-	47,929	-	47,929
Loans and advances to customers	23	1,125,505	-	-	-	1,125,505	-	1,130,435	-	1,130,435
Other financial assets		7,819	-	-	-	7,819	-	7,819	-	7,819
		1,255,097	**0**	**0**	**0**	**1,255,097**	**0**	**1,260,155**	**0**	**1,260,155**
Financial liabilities measured at fair value										
Derivative instruments	21	-	3,309	-	-	3,309	-	3,309	-	3,309
Short positions	21	-	2,081	-	-	2,081	2,081	-	-	2,081
		0	**5,390**	**0**	**0**	**5,390**	**2,081**	**3,309**	**0**	**5,390**
Financial liabilities not measured at fair value										
Due to financial institutions and Central Bank	29	-	-	-	48,062	48,062	-	48,062	-	48,062
Deposits from customers	30	-	-	-	707,813	707,813	-	707,366	-	707,366
Borrowings	31	-	-	-	373,168	373,168	-	381,506	-	381,506
Other financial liabilities		-	-	-	7,118	7,118	-	7,118	-	7,118
Subordinated liabilities	34	-	-	-	19,081	19,081	-	19,179	-	19,179
		0	**0**	**0**	**1,155,242**	**1,155,242**	**0**	**1,163,231**	**0**	**1,163,231**

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15. Classification and fair values of financial assets and liabilities (continued)

The following table shows the classification of the Group's financial assets and liabilities according to IFRS 9 and their fair values as at 31 December 2018:

		Carrying amount					Fair value			
As at 31 December 2018	**Notes**	**Amortised cost**	**Mandatorily at FVTPL**	**Designated at FVTPL**	**Other financial liabilities**	**Total**	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets measured at fair value										
Bonds and debt instruments	19	-	63,386	9,896	-	73,282	64,445	8,627	210	73,282
Equities and equity instruments	20	-	23,547	-	-	23,547	11,740	-	11,807	23,547
Derivative instruments	21	-	1,923	-	-	1,923	-	1,923	-	1,923
Loans and advances to customers	23	-	9,670	-	-	9,670	-	-	9,670	9,670
		0	**98,526**	**9,896**	**0**	**108,422**	**76,185**	**10,550**	**21,687**	**108,422**
Financial assets not measured at fair value										
Cash and balances with Central Bank	18	70,854	-	-	-	70,854	-	70,854	-	70,854
Bonds and debt instruments	19	3,776	-	-	-	3,776	-	4,001	-	4,001
Loans and advances to financial institutions	22	71,385	-	-	-	71,385	-	71,385	-	71,385
Loans and advances to customers	23	1,054,862	-	-	-	1,054,862	-	1,057,375	-	1,057,375
Other financial assets		4,864	-	-	-	4,864	-	4,864	-	4,864
		1,205,741	**0**	**0**	**0**	**1,205,741**	**0**	**1,208,479**	**0**	**1,208,479**
Financial liabilities measured at fair value										
Derivative instruments	21	-	1,638	-	-	1,638	-	1,638	-	1,638
Short positions	21	-	4,908	-	-	4,908	4,908	-	-	4,908
		0	**6,546**	**0**	**0**	**6,546**	**4,908**	**1,638**	**0**	**6,546**
Financial liabilities not measured at fair value										
Due to financial institutions and Central Bank	29	-	-	-	34,609	34,609	-	34,609	-	34,609
Deposits from customers	30	-	-	-	693,043	693,043	-	690,920	-	690,920
Borrowings	31	-	-	-	314,412	314,412	-	319,945	-	319,945
Other financial liabilities		-	-	-	6,114	6,114	-	6,114	-	6,114
Subordinated liabilities	34	-	-	-	13,340	13,340	-	13,452	-	13,452
		0	**0**	**0**	**1,061,518**	**1,061,518**	**0**	**1,065,040**	**0**	**1,065,040**

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16. Fair value of financial assets and liabilities

See accounting policy in Note 88.5 (f).

Valuation framework

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

Transfers between Levels

During the period from 1 January to 31 December 2019 and 1 January to 31 December 2018, there were no transfers between Level 1, Level 2 and Level 3.

The following tables show the reconciliation of fair value measurement in Level 3 for the year 2019 and 2018:

1 January - 31 December 2019	**Bonds and debt instruments**	**Equities and equity instruments**	**Loans and advances to customers**	**Total financial assets**
Carrying amount as at 1 January 2019	210	11,807	9,670	21,687
Net gain on financial assets and liabilities at FVTPL	79	5,376	18	5,473
Net foreign exchange gain	3	1	1	5
Purchases	87	1,065	5,742	6,894
Sales	(111)	(5)	-	(116)
Settlements	(119)	-	(752)	(871)
Dividend received	-	(1,424)	-	(1,424)
Transfers into Level 3	1	260	-	261
Carrying amount as at 31 December 2019	**150**	**17,080**	**14,679**	**31,909**
1 January - 31 December 2018				
Carrying amount as at 1 January 2018	83	15,659	1,857	17,599
Net gain (loss) on financial assets and liabilities at FVTPL	46	3,001	(25)	3,022
Net foreign exchange (loss) gain	(7)	2	-	(5)
Purchases	135	230	12,961	13,326
Sales	(1)	(4,377)	-	(4,378)
Settlements	(46)	-	(5,123)	(5,169)
Dividend received	-	(2,295)	-	(2,295)
Transfers out of Level 3	-	(413)	-	(413)
Carrying amount as at 31 December 2018	**210**	**11,807**	**9,670**	**21,687**

The following table shows the line items in the Consolidated Income Statement where gains (losses) on financial assets and liabilities categorised in Level 3 and held by the Group at year end 2019 and 2018, were recognised:

1 January - 31 December 2019	**Bonds and debt instruments**	**Equities and equity instruments**	**Loans and advances to customers**	**Total**
Net gain on financial assets and liabilities at FVTPL	70	5,374	18	5,462
Net foreign exchange (loss) gain	3	1	1	5
Total	**73**	**5,375**	**19**	**5,467**
1 January - 31 December 2018				
Net gain (loss) on financial assets and liabilities	32	2,956	(25)	2,963
Net foreign exchange (loss) gain	(7)	2	-	(5)
Total	**25**	**2,958**	**(25)**	**2,958**

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17. Unobservable inputs in fair value measurement

See accounting policy in Note 88.5 (f).

The following table summarises the unobservable inputs used in measuring fair value of financial assets and liabilities categorised in Level 3 at year end 2019 and 2018.

					Range of inputs	
As at 31 December 2019	**Assets**	**Liabilities**	**Valuation technique**	**Key un-observable inputs**	**Lower**	**Higher**
Bonds and debt instruments	150	-	See 1) below	See 1) below	n/a	n/a
Equities and equity instruments	17,080	-	See 2) below	See 2) below	n/a	n/a
Loans and advances to customers	14,679	-	See 3) below	See 3) below	n/a	n/a
	31,909	**0**				
As at 31 December 2018						
Bonds and debt instruments	210	-	See 1) below	See 1) below	n/a	n/a
Equities and equity instruments	11,807	-	See 2) below	See 2) below	n/a	n/a
Loans and advances to customers	9,670	-	See 3) below	See 3) below	n/a	n/a
	21,687	**0**				

A further description of the financial instruments categorised in Level 3 are as follows:

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

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

3. Loans and advances to customers carried at FVTPL are classified as financial assets in Level 3. The valuation technique is based on significant non-observable inputs inasmuch as loans and advances are unlisted and not traded in an active market. The valuation technique is based on available market data such as interest and inflation curves, probability of default and liquidity spread. Given the nature of the valuation method, the range of key unobservable inputs is not available.

The effect of unobservable inputs in fair value measurement

Although the Group believes that its estimates of fair value are appropriate, the use of different valuation methodologies and assumptions could lead to different estimates of fair value. The following tables show how profit (loss) before tax would have been affected if one or more of the inputs for fair value measurements in Level 3 were changed to likely alternatives at year-end 2019 and 2018:

	2019		2018	
Effect on profit before tax	**Favourable**	**Unfavourable**	**Favourable**	**Unfavourable**
Bonds and debt instruments	1	(1)	4	(4)
Equities and equity instruments:				
Equities	792	(805)	534	(532)
Mutual funds	241	(241)	188	(188)
Total equities and equity instruments	1,033	(1,046)	722	(720)
Loans and advances to customers	79	(80)	43	(43)
Total	**1,113**	**(1,127)**	**769**	**(767)**

The effect on profit was calculated as the difference between the results generated using the same valuation methods but changing key unobservable inputs for bonds and equities by +/- 5% and +/- 1% for loans and advances to customers.

18. Cash and balances with Central Bank

See accounting policy in Note 88.6.

	2019	2018
Cash on hand	4,606	5,217
Unrestricted balances with Central Bank	39,660	35,594
Total cash and unrestricted balances with Central Bank	**44,266**	**40,811**
Restricted balances with Central Bank - fixed reserve requirement	7,801	7,155
Restricted balances with Central Bank - average maintenance level	7,801	7,155
Assets held with Central Bank, subject to special restrictions	-	8,512
Cash and balances pledged as collateral to the Central Bank	9,956	7,221
Total restricted balances with Central Bank	**25,558**	**30,043**
Total cash and balances with Central Bank	**69,824**	**70,854**

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19. Bonds and debt instruments

See accounting policy in Note 88.7.

Bonds and debt instruments	2019 Amortised cost	2019 Mandatorily at FVTPL	2019 Designated at FVTPL	2019 Total	2018 Amortised cost	2018 Mandatorily at FVTPL	2018 Designated at FVTPL	2018 Total
Domestic								
Listed	4,020	26,141	1,995	32,156	3,776	13,454	8,874	26,104
Unlisted	-	-	786	786	-	-	1,022	1,022
	4,020	**26,141**	**2,781**	**32,942**	**3,776**	**13,454**	**9,896**	**27,126**
Foreign								
Listed	-	82,320	-	82,320	-	49,932	-	49,932
	0	**82,320**	**0**	**82,320**	**0**	**49,932**	**0**	**49,932**
Total bonds	**4,020**	**108,461**	**2,781**	**115,262**	**3,776**	**63,386**	**9,896**	**77,058**

Bonds are classified as "domestic" or "foreign" according to issuers' country of incorporation.

20. Equities and equity instruments

See accounting policy in Note 88.8.

Equities and equity instruments	2019 Trading book	2019 Banking book	2019 Total	2018 Trading book	2018 Banking book	2018 Total
Domestic						
Listed	12,311	542	12,853	10,038	1,122	11,160
Unlisted	-	17,149	17,149	-	12,333	12,333
	12,311	**17,691**	**30,002**	**10,038**	**13,455**	**23,493**
Foreign						
Listed	2	-	2	24	-	24
Unlisted	-	15	15	-	30	30
	2	**15**	**17**	**24**	**30**	**54**
Total equities	**12,313**	**17,706**	**30,019**	**10,062**	**13,485**	**23,547**

Equities are classified as "domestic" or "foreign" according to issuers' country of incorporation.

At year-end 2019, outstanding commitments of the Group in share subscriptions amounted to ISK 1.166 million (2018: ISK 1.342 million) altogether in seven entities. The entities invested in by the Group are required to redeem its shareholders with proceeds from the sale of assets.

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21. Derivative instruments and short positions

See accounting policy in Note 88.9.

Trading

	2019			2018		
	Notional	Fair value		Notional	Fair value	
Foreign exchange derivatives	**amount**	**Assets**	**Liabilities**	**amount**	**Assets**	**Liabilities**
Currency forwards	6,431	60	94	12,242	183	254
	6,431	**60**	**94**	**12,242**	**183**	**254**
Interest rate derivatives						
Interest rate swaps	2,213	23	-	2,596	24	-
Total return swaps	23,927	23	91	9,344	3	29
	26,140	**46**	**91**	**11,940**	**27**	**29**
Equity derivatives						
Equity forwards	5,800	382	1,057	3,900	231	185
Total return swaps	4,450	26	121	1,322	80	51
Equity options	73	-	1	444	-	38
	10,323	**408**	**1,179**	**5,666**	**311**	**274**
Total derivative instruments	**42,894**	**514**	**1,364**	**29,848**	**521**	**557**
Short positions						
Listed bonds	2,610	-	2,081	3,993	-	4,908
	2,610	**0**	**2,081**	**3,993**	**0**	**4,908**
Total	**45,504**	**514**	**3,445**	**33,841**	**521**	**5,465**

Risk management

	2019			2018		
	Notional	Fair value		Notional	Fair value	
Foreign exchange derivatives	**amount**	**Assets**	**Liabilities**	**amount**	**Assets**	**Liabilities**
Currency forwards	38,471	782	65	29,829	458	78
Cross-currency interest rate swaps	9,857	-	244	9,495	280	-
	48,328	**782**	**309**	**39,324**	**738**	**78**
Interest rate derivatives						
Interest rate swaps	30,214	71	1,636	30,596	54	995
	30,214	**71**	**1,636**	**30,596**	**54**	**995**
Fair value hedging						
Interest rate swaps	85,357	1,327	-	83,861	610	8
	85,357	**1,327**	**0**	**83,861**	**610**	**8**
Total	**163,899**	**2,180**	**1,945**	**153,781**	**1,402**	**1,081**
Total derivative instruments and short positions	**209,403**	**2,694**	**5,390**	**187,622**	**1,923**	**6,546**

Fair value hedging

Currently the Group applies hedge accounting only for fair value hedges of fixed interest risk on borrowings. The Group designates interest rate swaps as hedging instruments to hedge its interest rate exposure of fixed-rate EUR and SEK borrowings. The interest rate swaps and the borrowings have identical cash flows and under the interest rate swap the Group pays floating rates while receiving fixed rates. Thus the interest rate swaps hedge the fixed interest rate risk of the borrowings.

Linear regression is the method used to assess the effectiveness of each hedge. The relationship between daily fair value changes of an interest rate swap

During the period from 1 January 2019 to 31 December 2019, the slope of the regression line was in all cases within the range of 0.91and 0.98 (for a 95% confidence level) and the regression coefficient was at least 0.90 (R^2). During the period from 1 January to 31 December 2018, the slope of the regression line was in all cases within the range of 0.92 and 0.99 (for a 95% confidence level) and the regression coefficient was at least 0.96 (R^2).

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21. Derivative instruments and short positions (continued)

Fair value hedging (continued)

As at 31 December 2019	Notional amount of the hedging instrument	Maturity date 3-12 months	Maturity date 1-5 years	Maturity date >5 years	Fair value of the hedging derivatives Assets	Fair value of the hedging derivatives Liabilities	Gains (losses) on changes in fair value used for calculating hedge ineffectiveness
Interest rate swaps - EUR	81,480	-	81,480	-	1,323	-	550
Interest rate swaps - SEK	3,877	3,877	-	-	5	-	13
Total	**85,357**	**3,877**	**81,480**	**0**	**1,328**	**0**	**563**

Average fixed interest rate - EUR	1.19%
Average fixed interest rate - SEK	0.75%

As at 31 December 2019	Carrying amount of the hedged item Assets	Carrying amount of the hedged item Liabilities	Accumulated amount of fair value hedge adjustments on the hedged item Assets	Accumulated amount of fair value hedge adjustments on the hedged item Liabilities	Gains (losses) on changes in fair value used for calculating hedge ineffectiveness
LBANK 0.75 06/20	-	3,884	8	-	(10)
LBANK1.375 3/22	-	41,430	-	335	(185)
LBANK 1.00 5/23	-	41,499	-	517	(448)
Total EMTN hedged borrowings	**0**	**86,813**	**8**	**852**	**(643)**

As at 31 December 2018	Notional amount of the hedging instrument	Maturity date 1-5 years	Maturity date >5 years	Fair value of the hedging derivatives Assets	Fair value of the hedging derivatives Liabilities	Gains (losses) on changes in fair value used for calculating hedge ineffectiveness
Interest rate swaps - EUR	79,920	79,920	-	610	-	1,500
Interest rate swaps - SEK	3,941	3,941	-	-	8	2
Total	**83,861**	**83,861**	**0**	**610**	**8**	**1,502**

Average fixed interest rate - EUR	1.19%
Average fixed interest rate - SEK	0.75%

As at 31 December 2018	Carrying amount of the hedged item Assets	Carrying amount of the hedged item Liabilities	Accumulated amount of fair value hedge adjustments on the hedged item Assets	Accumulated amount of fair value hedge adjustments on the hedged item Liabilities	Gains (losses) on changes in fair value used for calculating hedge ineffectiveness
LBANK 0.75 06/20	-	3,935	19	-	1
LBANK1.375 3/22	-	40,430	-	161	(316)
LBANK 1.00 5/23	-	40,269	-	75	(470)
Total EMTN hedged borrowings	**0**	**84,634**	**19**	**236**	**(785)**

22. Loans and advances to financial institutions

See accounting policy in Note 88.11.

	2019	2018
Bank accounts with financial institutions	26,438	40,913
Money market loans	20,379	29,455
Other loans	1,113	1,019
Allowance for impairment	(1)	(2)
Total	**47,929**	**71,385**

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23. Loans and advances to customers

See accounting policy in Note 88.11.

	Notes	2019	2018
Loans and advances to customers at amortised cost	a)	1,140,388	1,067,667
Allowance for impairment		(14,883)	(12,805)
Total		**1,125,505**	**1,054,862**
Loans and advances to customers at FVTPL	b)	14,679	9,670
Total		**1,140,184**	**1,064,532**

a) Loans and advances to customers at amortised cost

	31.12.2019			31.12.2018		
	Gross carrying amount	Allowance for impairment	Carrying amount	Gross carrying amount	Allowance for impairment	Carrying amount
Public entities	4,170	(35)	4,135	4,865	(145)	4,720
Individuals	470,096	(2,151)	467,945	416,040	(2,341)	413,699
Mortgage lending	392,753	(848)	391,905	336,685	(886)	335,799
Other	77,343	(1,303)	76,040	79,355	(1,455)	77,900
Corporates	666,122	(12,697)	653,425	646,762	(10,319)	636,443
Total	**1,140,388**	**(14,883)**	**1,125,505**	**1,067,667**	**(12,805)**	**1,054,862**

Further disclosure on loans and advances to customers is provided in the risk management notes to these Consolidated Financial Statements.

b) Loans and advances to customers at FVTPL

	2019	2018
Corporates	14,679	9,670
Total	**14,679**	**9,670**

24. Investments in associates

See accounting policy in Note 88.3.

The Group's interest in its principal associates	2019	2018
Auðkenni hf. Borgartúni 31, Reykjavík	25.6%	25.6%
Greiðslumiðlun Íslands ehf. Katrínartúni 4, Reykjavík	47.9%	47.9%
JCC ehf. Borgartúni 19, Reykjavík	33.3%	33.3%
Reiknistofa bankanna hf. Katrínartúni 2, Reykjavík	38.6%	38.6%

Investments in equity-accounted associates	2019	2018
Carrying amount as at the beginning of the year	1,453	1,086
Acquisition	-	85
Share of profit of equity-accounted associates	304	282
Dividends received	(286)	-
Total	**1,471**	**1,453**

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25. Property and equipment

See accounting policy in Note 88.12.

	2019			2018		
	Buildings	Fixtures, equipment and vehicles	Total	Buildings	Fixtures, equipment and vehicles	Total
Carrying amount as at the beginning of the year	3,492	2,056	5,548	3,204	2,034	5,238
Additions during the year	1,343	299	1,642	453	371	824
Sold during the year	(7)	(2)	(9)	(106)	(13)	(119)
Depreciation	(58)	(380)	(438)	(59)	(336)	(395)
Carrying amount as at 31 December	**4,770**	**1,973**	**6,743**	**3,492**	**2,056**	**5,548**
Gross carrying amount	5,433	6,130	11,563	4,097	5,833	9,930
Accumulated depreciation	(663)	(4,157)	(4,820)	(605)	(3,777)	(4,382)
Carrying amount as at 31 December	**4,770**	**1,973**	**6,743**	**3,492**	**2,056**	**5,548**
Depreciation rates	2-4%	10-33%		2-4%	10-33%	

Official assessment value of buildings	**2019**	**2018**
Property valuation	6,169	5,979
Fire insurance value	10,183	9,761

26. Intangible assets

See accounting policy in Note 88.13.

	2019			2018		
	Hard- and software licences	Goodwill	Total	Hard- and software licences	Goodwill	Total
Carrying amount as at the beginning of the year	2,231	391	2,622	2,653	391	3,044
Additions during the year	85	-	85	64	-	64
Sold during the year	-	-	0	(2)	-	(2)
Amortisation	(411)	-	(411)	(484)	-	(484)
Carrying amount as at 31 December	**1,905**	**391**	**2,296**	**2,231**	**391**	**2,622**
Gross carrying amount	4,988	391	5,379	4,902	391	5,293
Accumulated amortisation	(3,083)	-	(3,083)	(2,671)	-	(2,671)
Carrying amount as at 31 December	**1,905**	**391**	**2,296**	**2,231**	**391**	**2,622**
Annual amortisation rates	20-33%		20-33%	20-33%		20-33%

27. Other assets

	2019	2018
Unsettled securities trading	958	686
Other accounts receivable	4,544	4,178
Right-of-use assets	2,317	-
Sundry assets	1,045	791
Total	**8,864**	**5,655**

28. Assets and liabilities classified as held for sale

See accounting policy in Note 88.17.

Assets classified as held for sale

	2019	2018
Repossessed collateral	1,022	1,330
Total	**1,022**	**1,330**

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28. Assets and liabilities classified as held for sale (continued)

Repossessed collateral

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

Repossessed collateral	2019	2018
Real estate	1,019	1,326
Equipment and vehicles	3	4
Total	**1,022**	**1,330**

Repossessed collateral	2019	2018
Carrying amount as at the beginning of the year	1,330	3,648
Repossessed during the year	633	838
Disposed of during the year	(950)	(5,807)
Impairment and gain of sale	9	2,651
Carrying amount as at year end	**1,022**	**1,330**

Liabilities associated with assets classified as held for sale

	2019	2018
Liabilities of disposal groups	30	30
Total	**30**	**30**

29. Due to financial institutions and Central Bank

See accounting policy in Note 88.18.

	2019	2018
Loans and repurchase agreements with Central Bank	67	74
Loans and deposits from financial institutions	47,995	28,324
Deposits subject to special restrictions*	-	6,211
Total	**48,062**	**34,609**

*In compliance with Article 8 of Act No. 37/2016, on the Treatment of Króna-Denominated Assets Subject to Special Restrictions

30. Deposits from customers

See accounting policy in Note 88.18.

	2019	2018
Demand deposits	457,427	432,788
Term deposits	250,386	257,954
Deposits subject to special restrictions*	-	2,301
Total	**707,813**	**693,043**

*In compliance with Article 8 of Act No. 37/2016, on the Treatment of Króna-Denominated Assets Subject to Special Restrictions

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31. Borrowings

See accounting policy in Note 88.19 and 88.20.

Secured borrowings

As at 31.12.2019	Currency	Final maturity	Outstanding principal	Indexed/ Non-indexed	Contractual interest rate	Carrying amount
LBANK CB 21	ISK	30.11.2021	5,760	Non-indexed	Fixed 5.5%	5,810
LBANK CBI 22	ISK	28.04.2022	19,540	CPI-indexed	Fixed 3.0%	22,025
LBANK CB 23	ISK	23.11.2023	15,480	Non-indexed	Fixed 5.0%	15,468
LBANK CBI 24	ISK	15.11.2024	38,120	CPI-indexed	Fixed 3.0%	42,089
LBANK CBI 28	ISK	04.10.2028	48,280	CPI-indexed	Fixed 3.0%	55,157
Total covered bonds						**140,549**
Total secured borrowings						**140,549**

Unsecured borrowings

As at 31.12.2019	Currency	Final maturity	Outstanding principal	Contractual interest rate	Carrying amount
LBANK FLOAT 06/20	SEK	22.06.2020	SEK 700 million	STIBOR + 1.0%	9,049
LBANK 0.75 06/20*	SEK	22.06.2020	SEK 300 million	FIXED 0.75%	3,884
LBANK 1.375 11/20	SEK	24.11.2020	SEK 750 million	FIXED 1.375%	9,690
LBANK FLOAT 11/20	SEK	24.11.2020	SEK 250 million	STIBOR + 1.5%	3,233
LBANK FLOAT 11/20	NOK	27.11.2020	NOK 300 million	NIBOR + 0,83%	4,132
LBANK FLOAT 11/20	SEK	30.11.2020	SEK 600 million	STIBOR + 0,85%	7,752
LBANK 1.625 03/21	EUR	15.03.2021	EUR 500 million	FIXED 1.625%	68,609
LBANK FLOAT 02/22	NOK	21.02.2022	NOK 1.000 million	NIBOR + 1,75%	13,783
LBANK FLOAT 02/22	SEK	21.02.2022	SEK 500 million	STIBOR + 1,75%	6,457
LBANK 1.375 03/22*	EUR	14.03.2022	EUR 300 million	FIXED 1.375%	41,430
LBANK 1.000 05/23*	EUR	30.05.2023	EUR 300 million	FIXED 1.0%	41,499
Total senior unsecured bonds					**209,518**

As at 31.12.2019	Currency	Final maturity	Outstanding principal	Indexed/ Non-indexed	Carrying amount
LBANK 200228	ISK	28.02.2020	2,840	Non-indexed	2,820
LBANK 200528	ISK	28.05.2020	800	Non-indexed	785
Total commercial paper issued					**3,605**

As at 31.12.2019	Carrying amount
Other unsecured loans	19,496
Total other unsecured loans	**19,496**
Total unsecured borrowings	**232,619**
Total borrowings as at 31.12.2019	**373,168**

* The Group applies hedge accounting to these bond issuances and uses for this purpose certain foreign currency denominated interest rate swaps as hedging instruments, see Note 21. The interest rate swaps are hedging the Group's exposure to fair value changes of these fixed-rate EUR and SEK denominated bonds arising from changes in interest rates. The Group applies fair value hedge accounting to the hedging relationship.

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31. Borrowings (continued)

Secured borrowings

As at 31.12.2018	Currency	Final maturity	Outstanding principal	Indexed/ Non-indexed	Contractual interest rate	Carrying amount
LBANK CB 19	ISK	17.09.2019	16,120	Non-indexed	Fixed 6.8%	16,476
LBANK CB 21	ISK	30.11.2021	3,720	Non-indexed	Fixed 5.5%	3,732
LBANK CBI 22	ISK	28.04.2022	19,540	CPI-indexed	Fixed 3.0%	21,414
LBANK CB 23	ISK	23.11.2023	1,540	Non-indexed	Fixed 5.0%	1,497
LBANK CBI 24	ISK	15.11.2024	27,740	CPI-indexed	Fixed 3.0%	29,744
LBANK CBI 28	ISK	04.10.2028	30,700	CPI-indexed	Fixed 3.0%	33,446
Total covered bonds						**106,309**
Total secured borrowings						**106,309**

Unsecured borrowings

As at 31.12.2018	Currency	Final maturity	Outstanding principal	Contractual interest rate	Carrying amount
LBANK FLOAT 06/19	SEK	10.06.2019	SEK 350 million	STIBOR + 2.6%	4,601
LBANK FLOAT 06/19	NOK	11.06.2019	NOK 500 million	NIBOR + 2.6%	6,739
LBANK FLOAT 06/20	SEK	22.06.2020	SEK 700 million	STIBOR + 1.0%	9,190
LBANK 0.75 06/20*	SEK	22.06.2020	SEK 300 million	FIXED 0.75%	3,935
LBANK 1.375 11/20	SEK	24.11.2020	SEK 750 million	FIXED 1.375%	9,833
LBANK FLOAT 11/20	SEK	24.11.2020	SEK 250 million	STIBOR + 1.5%	3,282
LBANK 1.625 03/21	EUR	15.03.2021	EUR 500 million	FIXED 1.625%	67,161
LBANK 1.375 03/22*	EUR	14.03.2022	EUR 300 million	FIXED 1.375%	40,430
LBANK 1.000 05/23*	EUR	30.05.2023	EUR 300 million	FIXED 1.0%	40,269
Total senior unsecured borrowings					**185,440**

As at 31.12.2018	Currency	Final maturity	Outstanding principal	Indexed/ Non-indexed	Carrying amount
LBANK 190110	ISK	10.01.2019	560	Non-indexed	559
LBANK 190410	ISK	10.04.2019	420	Non-indexed	415
LBANK 190510	ISK	10.05.2019	1,760	Non-indexed	1,731
Total commercial paper issued					**2,705**

As at 31.12.2018	Carrying amount
Other unsecured loans	19,958
Total other unsecured loans	**19,958**
Total unsecured borrowings	**208,103**
Total borrowings as at 31.12.2018	**314,412**

* The Group applies hedge accounting to these bond issuances and uses for this purpose certain foreign currency denominated interest rate swaps as hedging instruments, see Note 21. The interest rate swaps are hedging the Group's exposure to fair value changes of these fixed-rate EUR and SEK denominated bonds arising from changes in interest rates. The Group applies fair value hedge accounting to the hedging relationship.

32. Deferred tax assets and liabilities

See accounting policy in Note 88.15.

Recognised deferred tax assets and liabilities are attributable to the following:

	2019			2018		
	Assets	Liabilities	Net	Assets	Liabilities	Net
Property and equipment	-	(151)	(151)	-	(183)	(183)
Intangibles	-	(303)	(303)	-	(304)	(304)
Exchange rate-indexed assets and liabilities	-	(443)	(443)	-	(307)	(307)
Deferred foreign exchange differences	285	-	285	343	-	343
Other assets and liabilities	632	-	632	400	-	400
Tax losses carried forward	-	-	0	185	-	185
	917	**(897)**	**20**	**928**	**(794)**	**134**
Set-off of deferred tax credit against deferred tax liabilities	(897)	897	-	(794)	794	-
Deferred tax assets (liabilities) total	**20**	**0**	**20**	**134**	**0**	**134**

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32. Deferred tax liabilities (continued)

The deferred tax assets and liabilities are measured based on the tax rates and tax laws enacted by the end of 2019, according to which the domestic corporate income tax rate was 20% as at 31 December 2019 (2018: 20%).

The movements in temporary differences during the period were as follows:

2019	Balance 1.1	Impact of adopting IFRS 16	Recognised in income statement Tax (expense) income	Balance as at 31.12
Property and equipment	(183)	-	32	(151)
Intangibles	(304)	-	1	(303)
Foreign currency denominated assets and liabilities	(307)	-	(136)	(443)
Deferred foreign exchange differences	343	-	(58)	285
Other assets and other liabilities	400	46	186	632
Tax loss carried forward	185	-	(185)	0
Total	**134**	**46**	**(160)**	**20**

2018	Balance 1.1	Impact of adopting IFRS 9 and IFRS 15	Recognised in income statement Tax (expense) income	Balance as at 31.12
Property and equipment	(210)	-	27	(183)
Intangibles	(285)	-	(19)	(304)
Exchange rate-indexed assets and liabilities	(236)	-	(71)	(307)
Deferred foreign exchange differences	174	-	170	343
Other assets and liabilities	336	258	(194)	400
Tax losses carried forward	181	-	4	185
Total	**(40)**	**258**	**(83)**	**134**

33. Other liabilities

See accounting policy in Note 88.22.

	2019	2018
Unsettled securities trading	3,467	4,848
Withholding tax	3,803	2,793
Accounts payable	873	876
Contribution to the Depositors' and Investors' Guarantee Fund	253	340
Tax on liabilities of financial institutions	4,204	3,860
Current tax liabilities	4,917	6,702
Non-controlling interests - Funds	2,050	1,040
Lease liabilities	2,525	-
Sundry liabilities	2,958	3,992
Total	**25,050**	**24,451**

Unsettled securities transactions were settled in less than three days from the reporting date.

34. Subordinated liabilities

See accounting policy in Note 88.23.

As at 31.12.2019	Currency	Final maturity	Remaining principal in currencies	Indexed/ Non-indexed	Contractual interest rate	Carrying amount
LBANK 3.125 28NC23 T2	EUR	06.09.2028	EUR 100 million		Fixed 3,125%	13,613
LBANK T2I 29	ISK	11.12.2029	ISK 5.480 million	CPI-indexed	Fixed 3,85%	5,468
Total subordinated liabilities						**19,081**

As at 31.12.2018	Currency	Final maturity	Remaining principal in currencies	Contractual interest rate	Carrying amount
LBANK 3.125 28NC23 T2	EUR	06.09.2028	EUR 100 million	Fixed 3,125%	13,340
Total subordinated liabilities					**13,340**

In December 2019, the Bank concluded issuance of ISK Tier 2 fixed rate inflation linked subordinated bonds, in the amount of ISK 5,520 million. The bond series, LBANK T2I 29, has a final maturity in December 2029, but is callable in December 2024. The bonds are CPI-linked and carry a fixed rate of 3.85%. The bonds are issued under the Bank's ISK 50,000 million Debt Issuance Programme and are listed on Nasdaq Iceland.

The Tier 2 subordinated bonds in EUR have a final maturity in September 2028, but are callable in September 2023.

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35. Equity

See accounting policy in Note 88.31.

Share capital

As of 31 December 2019, ordinary shares authorised and issued by the Bank totalled 24 billion, while outstanding shares were 23.6 billion. Each share has a par value of ISK 1. Each ordinary share conveys one vote at general meetings of the Bank. All share capital is fully paid up.

The Annual General Meeting (AGM) of the Bank, held on 4 April 2019, approved the motion of the Board of Directors to authorise the Bank to acquire up to 10% of the nominal value of the Bank's share capital in accordance with Article 55 of the Act on Public Limited Companies, No. 2/1995. The price of each share is to be determined by the internal value of the Bank's shares, according to its most recently published results prior to the timing of the repurchase of the own shares. This authorisation applies until the next AGM in 2020 and the disposal of the own shares under this authorisation is subject to the approval of a shareholders meeting.

Share premium

Share premium represents the difference between the ISK amount received by the Bank when issuing share capital and the nominal amount of the shares issued, less costs directly attributable to issuing the new shares.

Statutory reserve

The statutory reserve is established in accordance with the Public Limited Companies Act, No. 2/1995, which stipulates that the Bank must allocate profits to the statutory reserve until the reserve is equal to one-quarter of the Bank's share capital.

Retained earnings

Act No. 3/2006, on Annual Financial Statements, with subsequent amendments, require inter alia the separation of retained earnings into two categories: restricted and unrestricted retained earnings. Unrestricted retained earnings consist of undistributed profits and losses accumulated by the Group since the foundation of the Bank, less transfers to the Bank's statutory reserve and restricted retained earnings. Restricted retained earnings are split into two categories:

1. Unrealised gains in subsidiaries and equity-accounted associates reserve; if the share of profit from subsidiaries or equity-accounted associates is in excess of dividend received, the Group transfers the difference to a restricted reserve in equity. If the Group's interest in subsidiaries or equity-accounted associates is sold or written off, the applicable amount recognised in the reserve is transferred to retained earnings.

2. Financial assets designated at fair value through profit or loss reserve. The Group transfers fair value changes arising from financial assets designated at fair value through profit or loss, from retained earnings to a restricted reserve. Amounts recognised in the reserve are transferred back to retained earnings upon sale of the financial asset.

Dividend

The AGM of the Bank held on 4 April 2019, approved the motion of the Board of Directors to pay shareholders a dividend in the amount of ISK 9,922 million, or equivalent to ISK 0.42 per share, for the operating year 2018. The dividend was paid in two equal instalments, each equivalent to ISK 0.21 per share, on 10 April 2019 and 2 October 2019.

Dividend policy

Landsbankinn's current dividend policy provides that the Bank aims to pay regular dividends to shareholders amounting in general to ≥50% of the previous year's profit. To achieve the Bank's target capital ratio, special dividend payments may also be made to optimise its capital structure. In determining the amount of dividend payments, the Bank's continued strong financial position shall be ensured. Regard shall be had for risk in the Bank's internal and external environment, growth prospects and the maintenance of a long-term, robust equity and liquidity position, as well as compliance with regulatory requirements of financial standing at any given time.

Restriction of dividend payments

According to the Public Limited Companies Act, No. 2/1995, it is only permissible to allocate as dividend profit in accordance with approved annual financial statements for the immediate past financial year, profit carried forward from previous years, and free funds after deducting loss which has not been met, and the funds which according to law or Articles of Association must be contributed to a reserve fund or for other use. Furthermore, under the amendment to Act No. 3/2006, on Annual Financial Statements, from June 2016 it is only permissible to allocate as dividend profit from unrestricted retained earnings.

Additionally, according to the Act on Financial Undertakings, No. 161/2002, the Icelandic Financial Supervisory Authority can impose proportionate restrictions on the Bank's dividend payments, if the Bank's capital adequacy ratio falls below the total capital requirement plus capital buffers, see Note 46 Capital requirements.

Other notes

36. Earnings per share

See accounting policy in Note 88.40.

Profit for the year	**2019**	**2018**
Profit for the year attributable to owners of the Bank	18,235	19,260

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

Number of shares	**2019**	**2018**
Number of ordinary shares issued at beginning of year	24,000	24,000
Average number of own shares	(375)	(362)
Weighted average number of shares outstanding	**23,625**	**23,638**
Basic and diluted earnings per share from operations (ISK)	**0.77**	**0.81**

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

37. Litigation

Material litigation cases against the Bank and its subsidiaries

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

Open court proceedings disclosed in the annual financial statement for 2018

In June 2013, a payment card company commenced litigation against the Bank and other financial undertakings claiming tort liability in the amount of ISK 1.2 billion plus interest. The plaintiff argued that the defendants were liable in tort for alleged violation of competition rules in the determination of payment card interchange fees. On 1 June 2017, the Supreme Court confirmed the decision of the District Court to dismiss the case on grounds of insufficient substantiation. In September 2017, the same payment card company commenced litigation against the same defendants as in the previous case claiming tort liability in the amount of around ISK 923 million, plus interest. The Supreme Court dismissed this case on 13 June 2018. In November 2018, a former owner of the payment card company, having had the alleged rights assigned to him from the payment card company, brought a new case against the same parties and demanded acknowledgement of the defendants' tort liability due to alleged breach of competition rules. In April 2019 the Court of Appeal confirmed a decision of the District Court to dismiss the case on grounds of insufficient substantiation. In October 2019, the same former owner of the payment card company brought a new case against the same parties claiming tort liability in the amount of around ISK 923 million, plus interest. At the first hearing of the case the defendants requested security from the plaintiff for the payment of litigation costs. The Bank presented its statement of defence in November 2019 and requested that the case be dismissed. On 15 November 2019 the District court accepted the claim by the defendants for security. The deadline for posting security was four weeks after the date of the decision. The plaintiff did not post the security. The plaintiff appealed the decision to the Court of Appeal but failed to present the necessary documents regarding the appeal. Consequently, the Bank requests that the case be dismissed by the District Court.

In December 2014, the Bank sold to Arion Bank hf. all its shares in Valitor Holding hf. (Valitor), the parent company of Valitor hf. The purchase agreement includes an indemnity clause under which the Bank is to proportionally (currently 38.62%) compensate Arion Bank hf. with regards to certain cases concerning Valitor that relate to events that occurred before delivery of the sold shares, inter alia, for potential compensatory damages that Valitor may be obligated to pay for an alleged loss sustained due to Valitor's termination of a vendor agreement. A case on the matter was filed before the District Court of Reykjavík in January 2015. In a judgment of the District Court of 24 April 2019 Valitor hf. was ordered to pay damages in the total amount of ISK 1,200 million. Valitor appealed the judgment to the Court of Appeal (Landsréttur) in May 2019. On 1 July 2019 the parties to the court case decided to put an end to the dispute by concluding an agreement on a final settlement of claims and withdrawing the case from the Court of Appeal. Consequently, in July 2019 the Bank paid to Arion Bank hf. around ISK 426 million as a final payment under the indemnity clause of the said purchase agreement. This settlement was explained in the notes to the Group´s financial statements for the first half of 2019. Moreover, it was explained that since the sale of the shareholding in Valitor, the Bank had assessed the fair value of granted indemnities in the purchase agreement and that the payment by the Bank to Arion Bank hf. would have an immaterial impact on amounts disclosed in the Group's financial statements.

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37. Litigation (continued)

Open court proceedings disclosed in the annual financial statement for 2018 (continued)

In January 2017, the Bank commenced proceedings before the Reykjavík District Court against BPS ehf., Eignarhaldsfélagið Borgun slf., Borgun hf. and the then CEO of Borgun hf. The Bank considers the defendants to have been in possession of information about the shareholding of Borgun in Visa Europe Ltd. at the time when the Bank sold its 31.2% shareholding in Borgun hf. that they failed to disclose to the Bank. The Bank demands acknowledgement of the defendants' liability for losses incurred by the Bank on these grounds. The defendants demanded the dismissal of the case which was rejected by a ruling of the District Court in June 2017. That ruling could not be appealed, and the defendants submitted their written defences, responding to the substance of the Bank's pleadings. At the request of the Bank, the District Court of Reykjavík ruled on 10 September 2018 on the appointment of assessors to evaluate certain issues regarding Borgun's annual financial statements. The Court of Appeal confirmed the ruling on 30 October 2018. The assessors delivered their assessment on 22 October 2019. The assessors conclude, inter alia, that information on the existence of an option to buy and sell holdings of Borgun in Visa Europe Ltd to Visa Inc., the terms of the option and possible payments to Borgun based on the option had been of relevance for the drawing up, presentation and therefore the audit of the Annual Accounts of Borgun for the year 2013. Borgun should have provided information in its Annual Accounts for 2013 on its holding in Visa Europe Ltd. and that Borgun was a principal member of Visa Europe Ltd. Borgun should have informed about the option in the Annual Accounts for 2013 in accordance with the provisions of the international financial reporting standard IFRS 7 and informed about the uncertainty relating to the option in the Report of the Board of Directors in accordance with the Act on Annual Accounts No. 3/2006. Moreover, the assessors conclude that the Annual Accounts of Borgun for the year 2013 did not fulfil all requirements of the Act on Annual Accounts and of international financial reporting standards as approved by the European Union at the time. The Bank presented the assessment to the District Court at a hearing on 9 December 2019. At a hearing on 24 January 2020, Borgun and another defendant presented a request for the appointment of new assessors to review the assessment.

In September 2018, the Icelandic Bankers' Pension Fund commenced litigation against the Bank, the Icelandic Central Bank, the Icelandic State and certain companies and associations. The Pension Fund demands that an agreement on the settlement of obligations of the then participating companies from 1997 be amended such that, firstly, the defendants shall pay a total of around ISK 5,600 million to the Fund, out of which the Bank shall pay around ISK 4,100 million, and, secondly, that the defendants shall guarantee the obligations of the Fund's Rate Department (Hlutfallsdeild) which are higher than its assets at any time. At a hearing of the case in January 2019 before the District Court of Reykjavík the Bank submitted a statement of defence, rejecting all claims. On 24 April 2019 the District Court decided to dismiss all claims against the Bank due to procedural reasons. The Pension Fund appealed the decision to the Court of Appeal in May 2019. On 6 June 2019 the Court of Appeal decided to invalidate the decision of the District Court and order the case to be brought again before the District Court for substantive resolution. On 10 September 2019 the case was heard by the District Court where new documents were presented. Moreover, at the hearing, the Pension Fund presented a request for an appointment of an assessor to evaluate certain actuarial matters relating to the calculation of the alleged claims against each of the defendants. On 17 October 2019 the Court appointed an assessor in the case who delivered his assessment on 16 December 2019. The assessment was presented before the Court on 9 January 2020. The next hearing of the case will be on 25 February 2020.

Other cases

In December 2018 the Westman Islands Municipality (Vestmannaeyjabær), the Westman Islands Pension Fund and Vinnslustöðin hf. initiated litigation against the Bank. The plaintiffs argued that a compensation received from the Bank for their shares in the savings bank Sparisjóður Vestmannaeyja ses., in the context of a merger of the Bank and the savings bank in 2015, had been insufficient. The plaintiffs claimed that the Bank was to pay additional compensation, a total of around ISK 45 million, in accordance with the results of an assessment of court appointed assessors. On 12 December 2019, the District Court of Reykjavík acquitted the Bank of all claims presented by the plaintiffs and rejected that the compensation had been insufficient. At the end of December 2019, the plaintiffs announced that they would not appeal the judgment to the Court of Appeal.

38. Leasing

See accounting policy in Note 88.38.

As at 1 January 2019, the Group adopted the accounting standard IFRS 16 *Leases* using the modified retrospective approach. As a result, the comparative information for the year 2018 has not been restated and continues to be reported under IAS 17 *Leases*.

a) The Group as a lessee

Leases into which the Group enters as a lessee are primarily operating leases. The Group leases premises for centralised activity, branches and ATMs. The lease contracts are of variable duration, most having a lifetime of 3-5 years with an option to renew. Details are in the following table:

Right-of use assets	No. of right-of use assets	Remaining term	Average remaining term	No. with extension options	No. with inflation-indexed payments	No. with termination options
Real estate	24	1-12 years	4,5 years	20	22	6
ATM's	18	0,5-3 years	3 years	15	13	11

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38. Leasing (continued)

a) The Group as a lessee (continued)

Lease assets

Right-of-use

The following table summarises the right-of-use assets (IFRS 16) disclosed under Other assets, see note 27, at year-end 2019.

	31.12.2019		
	Real estate	ATMs	Total
Opening balance as at 1.1.2019	2,557	38	2,595
New contracts	3	1	4
Amendments	9	2	11
Inflation-indexation	191	1	192
Amortisation	(474)	(11)	(485)
Total	**2,286**	**31**	**2,317**

Lease liabilities

The following table summarises lease liabilities (IFRS 16) disclosed in the Financial Statements at year-end 2019 under Other liabilities, see Note 33. In addition, Note 4 shows analysis of the opening balance of lease liabilities equal to the present value amount of the remaining lease payments in accordance with IFRS 16.

	31.12.2019		
	Real estate	ATMs	Total
Opening balance as at 1.1.2019	(2,789)	(40)	(2,829)
New contracts	(3)	(1)	(4)
Amendments	1	(3)	(2)
Inflation-indexation	(191)	(1)	(192)
Interest on lease liabilities	(80)	(1)	(81)
Lease expense	570	12	582
Total	**(2,492)**	**(34)**	**(2,526)**

The following table summarises the undiscounted expected future minimum lease payments under non-cancellable operating leases (IAS 17) at year-end 2018:

	2018
Less than one year	582
Between one and five years	1,614
More than five years	1,150
Total	**3,346**

b) The Group as a lessor

Finance leases

The Group acts as lessor whereby commercial and residential real estate is leased under arrangements qualifying as finance leases. Finance lease receivables are included in Loans and advances to customers in the Statement of Financial Position.

The following table summarises the net investment in finance lease receivables (IFRS 16) at year-end 2019:

At 31 December 2019	Gross investment in finance lease	Future finance income	Present value of minimum lease
Between one and two years	22	(1)	21
Total	**22**	**(1)**	**21**
At 31 December 2018			
Between one and five years	26	(3)	23
Total	**26**	**(3)**	**23**

Unguaranteed residual value at year-end 2019 is nil (2018: nil).

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39. Fiduciary activities

See accounting policy in Note 88.32.

The Group offers custodian, asset management, investment management and advisory services. These services require the Group to make decisions on the handling, acquisition or disposal of financial instruments. Assets under custody are not reported in the Consolidated Financial Statements, since they are assets held on behalf of customers, institutions and pension funds and are not assets of the Group. One aspect of these services is that the Group is involved in approving objectives and criteria for investing assets in its custody. As of 31 December 2019, financial assets managed by the Group amounted to ISK 412 billion (2018: ISK 382 billion). Custody accounts amounted to ISK 1.437 billion (2018: ISK 1.165 billion).

40. Interest in subsidiaries

See accounting policy in Note 88.1 (a).

The main subsidiaries held directly or indirectly by the Group as at 31 December 2019 were as detailed in the table below. This includes those subsidiaries that are most significant in the context of the Group's business. Landsbankinn operates an extensive branch network in Iceland, comprised of 37 branches and service points at year-end 2019.

Main subsidiaries as at 31 December 2019

Company	Ownership interest	Activity
Eignarhaldsfélag Landsbankans ehf. (Iceland)	100%	Holding company
Landsbréf hf. (Iceland)	100%	Fund management company
Hömlur ehf. (Iceland)*	100%	Holding company

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

The Group does not have significant restrictions on its ability to access or use its assets and settle its liabilities other than those resulting from the supervisory framework. The Group did not have any material non-controlling interests as at 31 December 2019.

41. Consolidated structured entities

See accounting policy in Note 88.2.

Assessment of control over an investee determines which structured entities are consolidated in the financial statements. Investees controlled by the Group are presented in the following balance sheet lines:

Assets	2019	2018
Bonds and debt instruments	2,184	421
Equities and equity instruments	190	1,174
Loans and advances to financial institutions	40	-
Other assets	1	1

Liabilities	2019	2018
Non controlling interests	2,050	1,040
Other liabilities	3	5

The Bank holds the majority of the units in the investment funds managed by Landsbréf. These funds are consolidated in the Bank's Consolidated Financial Statements, with the exception that minority interests are recognised among Other liabilities instead of Equity. The reason for this distinction is that the holders of the units may request redemption of their shareholding and therefore the units do not meet the requirements of the definition of equity.

42. Unconsolidated structured entities

See accounting policy in Note 88.2.

In cases where the Group acts as an agent for the investor, it does not consolidate the investment funds of the principal. In cases where the Group holds investments in unconsolidated investment funds, the investments are classified as financial investments designated at fair value through profit or loss. The fair value of these investments represents the Group's maximum exposure to loss from investments in unconsolidated investment funds.

			Total assets	
Type of structured entity	Nature and purpose	Interest held by the Group	2019	2018
Investment funds	To generate fees from managing assets on behalf of third party investors.	Investment in units issued by fund	66,529	71,102
	These vehicles are financed through the issue of units to investors	Management fees		

The following table shows an analysis of the carrying amounts of interests held by the Group in unconsolidated structured entities. The Group's maximum exposure to loss is the carrying amount of the assets held.

	Carrying amount	
Investment securities	2019	2018
Investment funds	1,913	1,469
Total	**1,913**	**1,469**

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43. Guarantees / Off-balance sheet exposures within the Group

As at year end the off-balance sheet exposure to credit risk within the Group was as follows:

	Carrying amount	
Off-balance sheet exposure 31 December	**2019**	**2018**
Financial guarantees	85	363
Undrawn overdraft and credit card facilities	63	1,366
Total	**148**	**1,729**

44. Related party transactions

Related parties

The Icelandic State Treasury, on behalf of the Icelandic State, holds 98.2% of shares in the Bank at year-end 2019. Government bodies and public institutions qualifying as related parties are the Ministry of Finance, the ISFI (Icelandic State Financial Investments), and entities and institutions related to them.

Transactions between the Bank and its subsidiaries meet the definition of related party transactions. All transactions with subsidiaries are eliminated on consolidation and are thus not disclosed in the Group's Consolidated Financial Statements. The main subsidiaries are summarised in Note 40 Interest in subsidiaries.

The key management personnel of the Bank and their close family members meet the definition of related parties and in some cases, the key management personnel of the Bank's subsidiaries. The key management personnel of the Bank are the members of the Board of Directors, the CEO, managing directors and other managers with the authority and responsibility to organise, manage and control the Bank's activities. The Minister for Finance and the Board of Directors of Icelandic State Financial Investments meet the definition of related parties due to the scope of their authority to influence Bank policy.

Transactions with the Icelandic government and government-related entities

The Group’s products and services are offered to the Icelandic government and government-related entities in competition with other vendors and under generally accepted commercial terms. In a similar manner, the Bank and other Group entities purchase products and services from government-related entities at market price and otherwise under generally accepted commercial terms. The nature of and amounts outstanding with public entities are disclosed in Note 59 under Public entities.

In March 2016, the Icelandic State Treasury took over Íslandsbanki hf. Following the takeover a settlement was reached with the Icelandic Competition Authority to the effect that both banks will continue to operate as independent competitors in the financial market. The takeover qualifies as a merger under Icelandic competition law, as the Icelandic State Treasury has control over the two banks as of the time of the takeover. The Bank has a traditional bank-to-bank relationship with Íslandsbanki under generally accepted commercial terms. The nature of and amounts outstanding with financial institutions, including Íslandsbanki, are disclosed in Note 59, under Financial institutions.

Transactions with other related parties

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

	2019		2018	
Loans in ISK million	**Gross carrying amount as at 31 December**	**Highest amount outstanding during the year**	**Gross carrying amount as at 31 December**	**Highest amount outstanding during the year**
Key management personnel	310	387	242	266
Parties related to key management personnel	149	205	135	159
Associates	271	289	288	17,589
Other	22	113	24	26
Total	**752**	**994**	**689**	**18,040**

No specific allowance for impairment was recognised at year end 2019 in Stage 3 in respect of these loans.

No financial guarantees were given to associates of the Bank during the period. There are no lease transactions between related parties during the year.

44. Related party transactions (continued)

Transactions with other related parties (continued)

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

Deposits in ISK million	2019 Gross carrying amount as at 31 December	2019 Highest amount outstanding during the year	2018 Gross carrying amount as at 31 December	2018 Highest amount outstanding during the year
Key management personnel	79	211	79	229
Parties related to key management personnel	46	105	48	159
Associates	173	483	149	16,885
Other	183	1,009	214	7,727
Total	**481**	**1,808**	**490**	**25,000**

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

Guarantees in ISK million	Gross carrying amount as at 31 December 2019	Gross carrying amount as at 31 December 2018
Key management personnel	-	-
Parties related to key management personnel	-	-
Associates	85	334
Total	**85**	**334**

The following table presents the total number of shares in th Bank owned by key management personnel and parties related to them and associates of the Group:

Number of shares in ISK million	2019	2018
Key management personnel	2	2
Parties related to key management personnel	-	-
Associates	-	-
Total	**2**	**2**

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

Effect on income statement

The following table presents the total amount of interest income and expense recognised by the Group in relation to key management personnel and parties related to them and associates of the Group:

Interest income and expense	2019 Interest income	2019 Interest expense	2018 Interest income	2018 Interest expense
Key management personnel	15	2	13	5
Parties related to key management personnel	7	1	7	1
Associates	18	3	811	9
Other	1	3	2	13
Total	**41**	**9**	**833**	**28**

The following table presents the total amount of other income and expense recognised by the Group in relation to key management personnel and parties related to them and associates of the Group:

Other income and expense	2019 Other income	2019 Other expense	2018 Other income	2018 Other expense
Associates	-	905	-	589
Total	**0**	**905**	**0**	**589**

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

44. Related party transactions (continued)

The following table presents the total amount of compensation to Directors, CEOs and Managing Directors for the year 2019:

Salary and benefits for the year 2019	Salary and benefits*	Defined contri-butions**	Total
Helga Björk Eiríksdóttir, Chairman of the Board of Directors	11.7	1.4	13.1
Berglind Svavarsdóttir, Vice-chairman of the Board of Directors	8.8	1.1	9.9
Einar Þór Bjarnason, Director	7.9	1.0	8.9
Guðbrandur Sigurðsson, Director	5.6	0.7	6.3
Hersir Sigurgeirsson, Director	7.9	1.0	8.9
Sigríður Benediktsdóttir, Director	7.8	1.0	8.8
Þorvaldur Jacobsen, Director	6.4	0.8	7.2
Guðrún Ó. Blöndal, Alternate Director	1.7	0.2	1.9
Sigurður Jón Björnsson, Alternate Director	1.5	0.2	1.7
Jón Guðmann Pétursson, Former Director	1.6	0.2	1.8
Lilja Björk Einarsdóttir, CEO	43.6	8.2	51.8
Arinbjörn Ólafsson, Managing Director Information Technology	35.1	6.7	41.8
Árni Þór Þorbjörnsson, Managing Director Corporate Banking	35.1	6.7	41.8
Helgi Teitur Helgason, Managing Director Personal Banking	35.1	6.6	41.7
Hrefna Ösp Sigfinnsdóttir, Managing Director Markets	35.1	6.6	41.7
Hreiðar Bjarnason, Managing Director, CFO	39.5	7.6	47.1
Perla Ösp Ásgeirsdóttir, Managing Director Risk Management	29.3	5.7	35.0
Total	**313.7**	**55.7**	**369.4**

In 2019 the total monthly average salary and benefits of the current CEO of the Bank amounted to ISK 3.6 million.

*Benefits are non-monetary benefits such as the use of cars owned by the Group.

**Includes both private and statutory contributions to independent pension funds without further obligation.

The following table presents the total amount of compensation to Directors, CEOs and Managing Directors for the year 2018:

Salary and benefits for the year 2018	Salary and benefits*	Defined contri-butions**	Total
Helga Björk Eiríksdóttir, Chairman of the Board of Directors	11.6	1.4	13.0
Berglind Svavarsdóttir, Vice-chairman of the Board of Directors	8.4	1.0	9.4
Einar Þór Bjarnason, Director	7.8	0.9	8.7
Hersir Sigurgeirsson, Director	7.8	0.9	8.7
Jón Guðmann Pétursson, Director	7.8	0.9	8.7
Sigríður Benediktsdóttir, Director	7.6	0.8	8.4
Guðrún Ó. Blöndal, Alternate Director	1.9	0.2	2.1
Þorvaldur Jacobsen, Alternate Director	1.3	0.2	1.5
Magnús Pétursson, Former Vice-chairman of the Board of Directors	2.1	-	2.1
Samúel Guðmundsson, Former Director	5.0	0.5	5.5
Lilja Björk Einarsdóttir, CEO	44.0	8.3	52.3
Six Managing Directors of the Bank's divisions	199.6	38.2	237.8
Total	**304.9**	**53.3**	**358.2**

*Benefits are non-monetary benefits such as the use of cars owned by the Group.

**Includes both private and statutory contributions to independent pension funds without further obligation.

In 2018 the total monthly average salary and benefits of the current CEO of the Bank amounted to ISK 3.7 million and the average monthly salary and benefits of Managing Directors of the Bank's divisions amounted to ISK 2.8 million. At year-end 2018, the current CEO did not hold any shares in the Bank but the six Managing Directors of the Bank's divisions did hold a total of 2.3 million shares in the Bank.

Transactions with the Minister of Finance and members of the Board of Directors of ISFI

The Minister of Finance and the members of the Board of Directors of ISFI did not receive any salaries or similar payments from the Group during the year 2019. The Group did not enter into any transactions with these persons or close members of their families, other than normal banking transactions which were made in the ordinary course of business and on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third party counterparties.

45. Events after the reporting period

No events have arisen after the reporting period of these financial statements that require amendments or additional disclosures in the Consolidated Financial Statements for the year ended 31 December 2019.

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Capital management

46. Capital requirements

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

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

In addition to the minimum capital requirement, the Bank is required by law to maintain certain capital buffers determined by the FME, which may, depending on the situation, be based on recommendations from the Icelandic Financial Stability Counsel (FSC). The FSC has defined Landsbankinn as a systematically important financial institution in Iceland.

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

As at 31.12.2019	CET1	Tier 1	Total
Pillar I	4.5%	6.0%	8.0%
Pillar II-R	1.9%	2.6%	3.4%
Minimum requirement under Pillar I and Pillar II-R	**6.4%**	**8.6%**	**11.4%**
Systemic risk buffer	2.87%	2.87%	2.87%
Capital buffer for systematically important institutions	2.00%	2.00%	2.00%
Countercyclical capital buffer	1.70%	1.70%	1.70%
Capital conservation buffer	2.50%	2.50%	2.50%
Combined buffer requirement	**9.07%**	**9.07%**	**9.07%**
Total capital requirement	**15.5%**	**17.7%**	**20.5%**

Following recommendations of the FSC, the FME has decided to raise the countercyclical capital buffer. As of the following dates, the countercyclical capital buffer on domestic exposures will therefore be, ceteris paribus:

	31.12.2018	15.5.2019	31.12.2019	1.2.2020
Countercyclical capital buffer on domestic exposures	1.25%	1.75%	1.75%	2.00%

The Bank aims to maintain at all times capital ratios above FME's capital requirements, in addition to a management capital buffer that is defined in the Bank's risk appetite. The Bank also aims to be in the highest category for risk-adjusted capital ratio, as determined and measured by the relevant credit rating agencies.

The Group's capital requirements at 31.12.2018, as determined by the FME, were as follows (as a percentage of REA):

As at 31.12.2018	CET1	Tier 1	Total
Pillar I	4.5%	6.0%	8.0%
Pillar II-R	2.3%	3.0%	4.0%
Minimum requirement under Pillar I and Pillar II-R	**6.8%**	**9.0%**	**12.0%**
Systemic risk buffer	2.85%	2.85%	2.85%
Capital buffer for systematically important institutions	2.00%	2.00%	2.00%
Countercyclical capital buffer	1.19%	1.19%	1.19%
Capital conservation buffer	2.50%	2.50%	2.50%
Combined buffer requirement	**8.54%**	**8.54%**	**8.54%**
Total capital requirement	**15.3%**	**17.5%**	**20.5%**

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47. Capital base, risk exposure amount and capital ratios

The following table shows the Group's capital base, risk exposure amount and capital ratios. The calculations are in accordance with Chapter X of the Act on Financial Undertakings, No. 161/2002, and Regulation No. 233/2017 on prudential requirements for the operations of financial undertakings. Iceland has also adopted regulation (EU) No. 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms, but has temporarily excluded Articles 500 and 501 (capital requirements relief for small and medium enterprises) that will take effect in Iceland on 1.1.2020.

The Group uses the standardised approach to calculate the risk exposure amount for credit risk and market risk, and the basic indicator approach for operational risk.

Capital base	2019	2018
Share capital	23,625	23,625
Share premium	120,630	120,630
Reserves	14,334	12,130
Retained earnings	89,145	83,225
Total equity attributable to owners of the Bank	**247,734**	**239,610**
Intangible assets	(2,296)	(2,622)
Deferred tax assets	(20)	(134)
Fair value hedges	(1,327)	(602)
Common equity Tier 1 capital (CET1)	**244,091**	**236,252**
Non-controlling interests	-	-
Tier 1 capital	**244,091**	**236,252**
Subordinated liabilities	19,081	13,340
Tier 2 capital	**19,081**	**13,340**
Total capital base	**263,172**	**249,592**

Risk exposure amount (REA)		
Credit risk	908,249	887,372
Market risk	11,754	17,739
Operational risk	100,394	95,815
Total risk exposure amount	**1,020,397**	**1,000,926**
CET1 ratio	23.9%	23.6%
Tier 1 capital ratio	23.9%	23.6%
Total capital ratio	25.8%	24.9%

The Board of Directors intends to propose to the Annual General Meeting (AGM) that a dividend of ISK 0.40 per share be paid to shareholders for the operating year 2019 in two equal payments in 2020. The total dividend of ISK 9,450 million corresponds to 52% of the consolidated profit in 2019. If the AGM approves the dividend proposal, the capital requirement of the Group will be reduced by an amount equivalent to the dividend payment and the Bank's capital ratios, in accordance with the Act on Financial Undertakings, will decrease by 0.9 percentage points.

48. Leverage ratio

The following table shows the Group's leverage ratio. Subject to Article 30(a) of Act on Financial Undertakings, No. 161/2002, Regulation No. 233/2017 on prudential requirements for the operations of financial undertakings and Regulation (EU) No. 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms, a minimum leverage ratio of 3.0% is required.

Leverage ratio	2019	2018
- On-balance sheet exposure (excluding derivatives)	1,423,634	1,324,118
- Derivative instrument exposure	2,694	1,923
- Potential future exposure on derivatives	1,625	1,674
- Off-balance sheet exposure	125,848	147,010
- Regulatory adjustments to Tier 1 capital	(3,643)	(3,358)
Total leverage exposure	**1,550,158**	**1,471,367**
Tier 1 capital	**244,091**	**236,252**
Leverage ratio	**15.7%**	**16.1%**

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Economic capital

49. Economic capital framework

Economic Capital (EC) is a risk measure which is applied to all material risks. It captures unexpected losses and reduction in value or income for which the Group needs to hold capital to avoid insolvency. It arises from the unexpected nature of losses as distinct from expected losses. EC is defined as the difference between unexpected losses and expected losses, where unexpected loss is defined as the 99.9% Value-at-Risk (VaR), with a one year time horizon.

The purpose of the EC framework is to enable the Group to assess the amount of capital it requires to cover the economic effects of risk-taking activities, as well as to compare different risk types using a common "risk currency".

The objective of the EC framework is to measure unexpected losses as well as to decompose EC on various levels to enable capital allocation, limit setting, pricing of products, risk-adjusted performance measurement and risk-based management evaluation.

The framework covers the following risk types: credit risk, market risk, currency risk, operational risk, concentration risk, interest rate risk and inflation risk in the banking book, business risk and legal and regulatory risk.

The following summarises how the Group calculates its EC for these risks:

Credit risk:
The credit risk EC model is the asymptotic single risk factor (ASRF) model from the Basel II internal rating based (IRB) approach's risk weight formula, i.e. the EC equals the capital requirements of the IRB approach in the capital requirements directive. The main input to the model are the risk parameters probability of default (PD), loss given default (LGD) and exposure at default (EAD).

Market risk:
Economic capital for market risk includes EC for interest rate risk in the trading book, EC for equity price risk in the trading book and EC for credit valuation adjustment.

EC for interest rate risk in the trading book and EC for equity price risk in the trading book is calculated according to a Stressed Value at Risk model as specified in the internal models approach in the capital requirements directive (CRR). The model inputs are calibrated to historical data from the previous five years.

EC for credit valuation adjustment equals the capital requirements for credit valuation adjustment.

Currency risk:
EC for foreign exchange risk is calculated according to a modified Stressed Value at Risk model where the model inputs are calibrated to historical data from a period of significant stress relevant to the Groups' net FX position. The time horizon is one year.

Operational risk:
EC for operational risk is calculated using the basic indicator approach, which means that it equals the Group's capital requirement.

Concentration risk:
EC for single name concentration is calculated by adjusting for the granularity and non-homogeneity in the loan portfolio. This is necessary as the credit risk EC model assumes that the portfolio is infinitely large and homogeneous; hence, the single name concentration EC is given as an add-on.

An internal model is used to measure the additional EC for credit risk related to industry concentrations in the loan portfolio, i.e. a concentration add-on. The model calculates the industry concentration risk for the loan portfolio and subtracts the industry concentration risk for Iceland to get the EC add-on for industry concentration.

Interest rate risk and inflation risk in the banking book:
EC for interest rate risk and inflation risk in the banking book is equal to the sum of:

i. The loss in economic value corresponding to the 99.9th percentile for ISK and the 99th percentile for significant foreign currencies of risk factor changes estimated by a Monte Carlo simulation model.
ii. The loss in economic value due to a +/- 200 bps shift of risk factors in other currencies (whichever results in a larger loss).

Business risk:
EC for business risk is measured at least annually in the ICAAP and is based on the effects of the base case scenario on the Bank's balance sheet and operations and its following effect on the Bank's capital base.

Legal and regulatory risk:
EC for legal and regulatory risk is calculated by adding the potential loss of on-going disputes. The significance of a dispute is weighted by its status within the legal system.

50. Economic capital by risk type

Credit quality increased in 2019 and EC for credit risk due to loans to customers and credit institutions decreased in spite of increased lending. The estimation of EC due to business risk was updated in 2019, as well as the model for industry concentration. The Group implemented a new rating grade model for individuals in 2019 but the effects of this implementation on EC were insignificant.

EC for market and currency risk decreased significantly in 2019, primarily due to decreased exposure to listed equities in the Group's trading portfolio.

Economic capital ISK million	2019	2018
Credit risk - Loans to customers and credit institutions	62,574	62,956
Credit risk - Other assets	6,815	5,144
Market risk	1,511	2,769
Currency risk	776	1,369
Operational risk	8,031	7,665
Single name concentration risk	6,331	5,401
Industry concentration risk	1,539	1,246
Interest rate risk and inflation risk in the banking book	8,587	7,171
Business risk	-	3,833
Legal and regulatory risk	2,067	2,092
Total	**98,231**	**99,646**
EC/REA	9.6%	10.0%

	Weighted average			
Credit risk as at 31 December 2019	**Probability of default (PD)**	**Loss given default (LGD)**	**Exposure at default (EAD)**	**Economic capital (EC)**
Financial institutions	0.2%	45.0%	49,413	807
Public entities	0.1%	45.0%	85,613	165
Retail*	2.1%	25.0%	545,597	13,408
Corporates	2.4%	33.9%	698,380	48,194
Total EC	**2.1%**	**31.5%**	**1,379,003**	**62,574**
Credit risk as at 31 December 2018				
Financial institutions	0.1%	45.0%	71,606	1,146
Public entities	0.1%	45.0%	125,117	149
Retail*	2.6%	25.7%	493,358	14,129
Corporates	2.4%	35.9%	685,874	47,532
Total EC	**2.1%**	**33.5%**	**1,375,955**	**62,956**

*Exposure to retail consists of individuals and small and medium-sized enterprises with total exposure under ISK 75 million and which meet the criteria of EU Directive 2003/361/EC on individuals and SMEs.

Risk management

51. Risk management structure

Risk committees

The Group's risk management governance structure as at year-end 2019 is as follows:

Board of Directors

Supervision by the Board of Directors and its sub-committees:

- Audit Committee
- Remuneration Committee
- Risk Committee
- Strategic Development Committee

Key risk management bodies and committees

Committee	Chair	Other members
Executive Board	CEO	Managing directors
Risk & Finance Committee	CEO	CFO, CRO, Head of Legal Department,
Credit Committee	CEO	CRO, MD of Corporate Banking
Operational Risk Committee	CRO	MD of Personal Banking, MD of IT, Head of Compliance, Director of Operational Risk
Project committee	CEO	Managing directors

The Board of Directors of the Bank has overall responsibility for the establishment and oversight of the Group's risk management framework and risk appetite and risk limit setting. The CEO is responsible for the effective implementation of the framework and risk appetite through the corporate governance structure and committees. The CEO has established and is a member of the Executive Board, the Risk & Finance Committee, the Credit Committee. and the Project committee.

51. Risk management structure (continued)

Risk committees (continued)

The Credit Committee deals with credit risk – individual credit decisions, credit limits on customers and credit risk policy – while the Risk & Finance Committee covers primarily market risk, liquidity risk and legal risk. The Risk & Finance Committee monitors the Group's overall risk position, is responsible for enforcing the Group's risk appetite and risk limits, and reviews and approves changes to risk models before they are presented to the Board of Directors. The Executive Board serves as a forum for consultation and communication between the CEO and the managing directors, addressing the main current issues in each division, takes decisions on operating matters not being considered in other standing committees, and approves funding for larger investment projects. The Operational Risk Committee is a forum for discussions and decisions on operational risk issues and review of the effective implementation of the operational risk framework. The Project Committee selects, prioritises and oversees the Bank's bigger projects, and contributes to their successful progress and conclusion.

Risk Management Division

The Bank's Risk Management Division is responsible for the Bank's risk management framework. Subsidiaries of the Bank have their own risk management functions and the Risk Management Division receives information on exposures from the subsidiaries and collates them into Group exposures. The Risk Management Division is also responsible for comprehensive risk reporting on risk positions to various internal departments and committees and supervisory authorities

The Risk Management Division is comprised of seven departments.

• The Credit Management Department reviews, and confirms or vetos credit decisions made by the Bank's business units when credit applications exceed the business units limits. Confirmation by Credit Management implies that Credit Management has reviewed the credit application and does not exercise its veto rights. Credit applications exceeding the confirmation limits of the Risk Management Division are referred to the Bank's Credit Committee. The Department also sets and maintains the Bank's rules regarding the lending process.

• The Credit Risk Department is responsible for measuring and monitoring credit risk as well as for providing the Bank with systems and processes to measure and control credit risk in credit and policy decisions. Credit Risk is further responsible for analysis and reporting on credit risk, economic capital and impairment. Credit Risk is also responsible for setting rules and procedures regarding credit risk, such as procedures for impairment measurement, credit mitigation and forbearance.

• The Market Risk Department is responsible for measuring, monitoring and reporting on market risk, liquidity risk and interest rate risk in the Group's banking book along with limit monitoring and reporting. The Department develops and maintains the Bank's market risk models and maintains the Group's Market Risk Policy and Liquidity Risk Policy as well as implementing processes to measure and monitor market risk and liquidity risk within the Group. Market Risk is also responsible for monitoring all derivatives trading the Bank enters into, both for hedging and trading purposes, as well as FX balance monitoring for the Group.

• The Operational Risk Department is responsible for ensuring that the Group's operational risks are monitored and that the Bank implements and maintains an effective operational risk management framework. The Department assists the Bank's managers with operational risk assessment incidents related to normal operations and operational loss incidents analysis, and oversees continuity plans. The Bank's rules on operational risk as well as the rules on new products are the responsibility of the Department. The Department is partly responsible for the security system for the online bank. The Operational Risk Department leads the work on the Bank's certification under the ISO 27001 standard for information security.

• The Risk Manager for Pension Funds is responsible for development and implementation of risk policy and risk governance, execution of risk assessment and correspondence with regulators such as the Central Bank and the FSA. The Risk Manager also makes sure that monitoring of regulatory compliance is carried out, reviews calculations and results and performs tolerance interval monitoring. The Risk Manager has direct access to the boards of the pension funds and also reports to their managing directors.

• The Internal Modeling Department is responsible for providing the Bank with IRB and EC models and related processes to estimate credit risk and link the risk to equity, as well as for providing support during the implementation of those models and processes within the Bank. The Department is also responsible for the development of a model for pre-approved limits.

• The Risk Solutions Department develops and operates external solutions used by the Risk Management Division, as well as maintaining the development and reporting environments of the Risk Division. The Department is also responsible for monitoring and maintaining periodic executions of code by the Division and reporting to supervisory parties. The Department has also been responsible for the implementation of the Basel Committee on Banking Supervision for the effective risk data aggregation and risk reporting standard or BCBS 239.

Compliance

Compliance is an independent management unit, reporting directly to the CEO, operating in accordance with a letter of appointment from the Board of Directors. The operations of the Compliance unit are shaped by its independence from other units. Compliance is part of the Bank's second level control and is responsible for monitoring compliance with laws and actions against money laundering and financing of terrorist activities, laws on securities trading and data protection laws. Compliance also monitors the efficiency of the Bank's policy on compliance with laws, regulations and internal rules. Compliance consults and instructs management on the effects of changes to the legal environment on the Bank's operations, measures to prevent conflict of interest and action necessary to ensure that the Bank operates in accordance with proper and sound business practices with the aim of strengthening the credibility of and confidence in financial markets. The Data Protection Officer works independently out of Compliance, in accordance with a letter of appointment from the Board of Directors.

51. Risk management structure (continued)

Internal Audit

Internal Audit is an independent, objective assurance and consulting activity that is a part of the Bank's organizational chart and an element of its monitoring system. The Board of Directors has oversight of Internal Audit and appoints the Chief Internal Auditor. The role of Internal Audit is to improve and protect the Bank's value with risk-focused and objective verification, consultation and insight. Internal Audit evaluates and improves the risk management framework, control and governance processes according to systematic and disciplined practices and thus supports the Group in accomplishing its objectives. The Chief Internal Auditor is responsible for ensuring that Internal Audit works in accordance with laws, recommendations from the Financial Supervisory Authority no. 3/2008, and standards and guidelines cited therein, including the benchmarks of the Institute of Internal Auditors (IIA).

52. Risk appetite

The Group's risk appetite for 2020 has been reviewed, revised and implemented. The Group's risk policy is as follows:

The Bank's operations, risk diversification and decisions shall always be in accordance with its risk appetite, sound business practices, financing, liquidity and equity position at any given time. The Bank seeks to ensure diversified and sound financing and a sustainable risk profile in its balance sheet. The Bank has set internal limits that provide for a strong capital and liquidity position which, along with active risk management, ensure long-term profitability and strong standing. In this manner, the Bank aims to minimise fluctuation in its operations and is well positioned to withstand stress scenarios.

Risk appetite defines the risk, both in terms of type and extent, which the directors are willing to take to meet the Bank's business objectives. The Bank has set itself objectives regarding financial position, asset quality, exposures and sustainable long-term profitability. Inpursuit of its goals, the Bank only takes on risks that it understands, and is able to evaluate and manage.

The Bank seeks to maintain solid business relationships, having regard for its own position as well as that of its customers at all times, and with due regard for any internal connections between customers. The Bank pursues long-term business relationships and aims to avoid reputational risk.

Landsbankinn has set a policy on corporate social responsibility that integrates economic, social and environmental concerns in its operations. The policy aims to promote sustainability in Icelandic society, to ensure that the Bank is a dynamic force in the community and that it operates in accordance with the principles of good corporate governance.

The Bank is obligated to comply with relevant laws and regulations in all its operations. The main focus areas within the Bank's risk culture are adherence to rules, integrity, ethical behaviour, professionalism and management promoting good risk culture.

53. Risk assessment

Risk is inherent in the Group's activities. It is managed through a process of on-going identification, measurement, management and monitoring, subject to risk limits and other controls. Risk identification involves finding the origins and structures of possible risk factors in the Group's operations and undertakings. Risk measurement entails measuring identified risk for management and monitoring purposes. Finally, risk controls and limits promote compliance with rules and procedures, as well as adherence with the Group's risk appetite.

The objective of the Group's risk policies and procedures is to ensure that the risks in its operations are detected, measured, monitored and effectively managed. Exposure to risk is managed to endeavour to ensure that it remains within limits and that the risk appetite adopted by the Group complies with regulatory requirements. In order to limit and manage fluctuations that might affect the Group's equity as well as performance, the Group has adopted policies regarding the risk structure of its asset portfolio which are covered in more detail under each risk type.

Risk policy is implemented through risk appetite, goal setting, business strategy, internal policies and limits that comply with the regulatory framework of the financial markets.

The Group is exposed to the following material risks that arise from financial instruments:
- Credit risk
- Operational risk
- Market risk
    - Currency risk
    - Interest rate risk
    - Other market risk
- Liquidity risk

The table below provides a link between the Group's business units and the principal risks that they are exposed to. The significance of risk is assessed within the context of the Group as a whole and is measured based on allocation of Economic Capital within the Group.

Principal risk	Personal Banking	Corporate Banking	Markets	Treasury
Credit risk	High	High	Low	Low
Operational risk	Medium	Medium	High	Medium
Market risk	Low	Low	Medium	High
Liquidity risk	n/a	n/a	n/a	High

The Group also manages other relevant risks, such as concentration risk, business risk, legal risk, reputation risk, conduct risk, compliance risk, data risk and modeling risk.

The above material risks are addressed in the following notes.

54. Disclosure of risk data

The Bank has implemented a policy on risk data in compliance with BCBS 239 (Basel Committee on Banking Supervision's guideline 239). The policy defines which reports should be submitted where, the frequency of those submissions, and who's responsible for them.

Credit risk

55. Credit risk identification

Credit risk is defined as the risk of loss if customers fail to fulfil their agreed obligations and the estimated value of pledged collateral does not cover existing claims.

The Group's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of an entity to honour its obligations to deliver cash, securities or other assets as contractually agreed.

Credit risk is the greatest single risk faced by the Group and principally arises from loans and advances to customers and from investments in debt securities, but also from commitments, guarantees and documentary credits, counterparty credit risk in derivatives contracts, and the aforementioned settlement risk.

56. Credit risk assessment

Credit risk is measured in three main dimensions: probability of default (PD), loss given default (LGD) and exposure at default (EAD). For the purpose of measuring PD, the Group has developed an internal rating system, including a number of internally developed rating models. The objectives of the rating system are to provide a meaningful assessment of obligor characteristics; a meaningful differentiation of credit quality; and accurate and consistent quantitative estimates of default risk, i.e., probabilities of default (PD). Internal ratings and associated PD are essential in the risk management and decision-making process, and in the credit approval and corporate governance functions.

The rating system has an obligor rating scale which exclusively reflects quantification of the risk of obligor default, or credit quality. The obligor rating scale has 10 rating grades for non-defaulted obligors from '1' to '10', with '10' indicating the highest credit quality, and the grade '0' for defaulted obligors. The rating assignment is supported by rating models, where information such as industry classification, financial accounts and payment behaviour is taken into account.

The following table shows the Group's internal mapping from internal rating grade to S&P rating grades:

	S&P	Lower PD	Upper PD
10	AAA/AA+/AA/AA-	0.00%	0.04%
9	A+/A/A-	0.04%	0.10%
8	BBB+	0.10%	0.21%
7	BBB/BBB-	0.21%	0.46%
6	BB+/BB	0.46%	0.99%
5	BB-	0.99%	2.13%
4	B+	2.13%	4.54%
3	B	4.54%	9.39%
2	B-	9.39%	18.42%
1	CCC/C	18.42%	99.99%
0	D	In default	In default

The rating assignment and approval is an integrated part of the credit approval process and assignment shall be updated at least annually, or when material information on the obligor or exposure becomes available, whichever is earlier.

The credit rating models' discriminatory power significantly exceeds the Basel framework requirement of 0.5. Furthermore, the models are well calibrated, i.e., the weighted probability of default for each rating grade is equal to the actual default rate with respect to reasonable error limits.

LGD is measured using an internal LGD model for the purpose of EC calculations. The internal LGD model takes into account more types of collateral and is more sensitive to the collateralisation level than the Basel model.

Exposure at default is an estimate of the amount outstanding (drawn amounts plus likely future drawdowns of yet undrawn lines) in case the borrower defaults. The Group uses the standard approach for estimating economic capital, but uses internal models for provisioning.

57. Credit risk management and policy

The Group's credit risk management objective is to ensure compliance with the Group's credit policy, which entails that the only risk taken is one that the Bank understands, can measure and manage.

The Group's credit risk management is based on active monitoring by the Board of Directors, the CEO, the Risk & Finance Committee, the Credit Committee, the credit departments within the Risk Management Division and the business units. The Group manages credit risk according to its risk appetite statement and credit policy approved by the Board of Directors, as well as detailed credit policies approved by the CEO. The risk appetite and credit policy include limits on large exposures to individual borrowers or groups of borrowers, concentration of risk and exposure to certain industries. The CEO ensures that the risk policy is reflected in the Group's internal framework of regulations and guidelines. The Bank's executives are responsible for ensuring that the Bank's business units execute the risk policy appropriately and the CEO is responsible for the oversight of the process as a whole.

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57. Credit risk management and policy (continued)

Incremental credit authorisation levels are defined based on size of units, types of customers and the lending experience of credit officers. The Group has also set industry policies that describe the bank's appetite to provide credit to specific industries.. Credit decisions exceeding authorization levels of business units are subject to confirmation by Credit Management. The Corporate Banking Credit Committee has authorisation levels exceeding that of individual business unit managers and meets regularly to make credit decisions. Credit Management has veto powers over the decisions of the Corporate Banking Credit Committee. Credit decisions exceeding the signing limits of the Corporate Banking Credit Committee are subject to approval by the Group's Credit Committee. Credit decisions exceeding the limits of the Credit Committee are subject to approval by the Board of Directors, which holds the highest credit authorisation within the Bank.

58. Credit risk mitigation

Mitigating risks in the credit portfolio is a key element of the Group's credit policy, as well as an inherent part of the credit-decision process. Securing loans with collateral is the main method of mitigating credit risk, whereas for some loan products collateral is required by legislation, as in the mortgage finance market, or is standard market practice.

The most important types of collateral are real estate, vessels and financial assets (shares or bonds).

The amount and type of collateral required depends on an assessment of the credit risk associated with the counterparty. Valuation parameters and the acceptability of different types of collateral are defined in the Group's credit policy. Credit extended by the Group may be secured on residential or commercial properties, land, listed and unlisted securities, transport vessels, fishing vessels together with their non-transferable fishing quotas, etc. The Group also secures its loans by means of receivables, inventory and operating assets, such as machinery and equipment. Residential mortgages involve the underlying residential property. Less stringent requirements are set for securing short-term personal loans, such as overdrafts and credit card borrowings.

The Group regularly assesses the market value of received collateral. The Group has developed models to estimate the value of the most frequent types of collateral. For collateral where no valuation model exists, the Group estimates the value as the market value less a haircut. A haircut in this context is a discount factor which represents a conservative estimate of the costs to sell in a forced sale. Costs to sell include maintenance costs in the period over which the asset is up for sale, fees for external advisory services, and any loss in value. For listed securities, haircuts are calculated with an internal model based on variables, such as price volatility and marketability.

The Group monitors the market value of mark-to-market collateral and may require additional collateral in accordance with the underlying loan agreements.

In order to further limit the credit risk arising from financial instruments, the Group enters into netting agreements, under which the Group is able to set off all contracts covered by the netting agreement against the debt in cases of default. The arrangements generally include all market transactions between the Group and the client.

Generally, collateral is not held over loans and advances to financial institutions, nor is it usually held against bonds and debt instruments.

The Group includes all collateral to which a value is assigned in accordance with its internal procedures. Guarantees are included if they imply lower risk weights than the original exposure. In addition, collateral is volatility-adjusted (by means of a haircut) in order to take price volatility and the expected costs of repossession and sale of the pledge into account.

Derivative financial instruments

In order to mitigate credit risk arising from derivatives, the Group chooses the counterparties for derivatives trading based on stringent requirements. The Group also enters into standard International Swaps and Derivatives Association (ISDA) master netting agreements and similar general netting agreements with financial counterparties. Commensurate collateral and margin requirements are in place for all derivative contracts the Group enters into. Collateral management and monitoring is performed daily, and derivative contracts with clients are usually fully hedged.

The Group's supervision system monitors both derivatives exposure and collateral value and calculates an intraday credit equivalent value for each derivative. It also issues margin calls and manages netting agreements.

Amounts due to and from the Group are offset when the Group has a legally enforceable right to set off a recognised amount and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. External ratings are used where applicable to assist in managing the credit risk exposure of bonds. Otherwise the Group uses fair value estimates based on available information and the Group's own estimates.

59. Maximum exposure to credit risk and concentration by industry sectors

The following tables show the Group's maximum credit risk exposure as at 31 December 2019 and 31 December 2018. For on-balance sheet assets, the exposures are based on net carrying amounts as reported in the Consolidated Statement of Financial Position. Off-balance sheet amounts are the maximum amounts the Group might have to pay for guarantees, loan commitments in their full amount, and undrawn overdraft and credit card facilities.

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

				Corporations										
As at 31 December 2019	**Financial institutions**	**Public entities***	**Individuals**	**Fisheries**	**Construction companies**	**Real estate companies**	**Holding companies**	**Retail**	**Services**	**ITC****	**Manu-facturing**	**Agriculture**	**Other**	**Carrying amount**
Cash and balances with Central Bank	-	69,824	-	-	-		-	-	-	-	-	-	-	**69,824**
Bonds and debt instruments	11,423	102,181	-	-	-	772	49	83	-	-	-	-	754	**115,262**
Equities and equity instruments, banking book	1	-	-	32	-	-	15,511	1	1,595	-	-	49	517	**17,706**
Derivative instruments	2,202	-	9	-	-	12	363	5	-	-	-	-	103	**2,694**
Loans and advances to financial institutions	47,929	-	-	-	-	-	-	-	-	-	-	-	-	**47,929**
Loans and advances to customers	-	4,135	467,945	151,336	98,536	136,000	26,154	60,525	133,326	32,943	20,365	8,918	1	**1,140,184**
Other financial assets	2,767	26	76	-	22	2,342	30	2	2,549	1	4	-	-	**7,819**
Total on-balance sheet exposure	**64,322**	**176,166**	**468,030**	**151,368**	**98,558**	**139,126**	**42,107**	**60,616**	**137,470**	**32,944**	**20,369**	**8,967**	**1,375**	**1,401,418**
Off-balance sheet exposure	**3,598**	**5,051**	**33,553**	**16,594**	**53,174**	**11,059**	**1,655**	**19,691**	**14,711**	**5,618**	**17,819**	**912**	**42**	**183,477**
Financial guarantees and underwriting commitments	306	168	775	6,999	4,105	1,364	1,026	2,855	3,822	1,912	558	42	35	23,967
Undrawn loan commitments	-	-	-	7,495	46,655	8,163	328	11,655	4,831	2,359	13,751	241	-	95,478
Undrawn overdraft/credit card facilities	3,292	4,883	32,778	2,100	2,414	1,532	301	5,181	6,058	1,347	3,510	629	7	64,032
Maximum exposure to credit risk	**67,920**	**181,217**	**501,583**	**167,962**	**151,732**	**150,185**	**43,762**	**80,307**	**152,181**	**38,562**	**38,188**	**9,879**	**1,417**	**1,584,895**
Percentage of maximum exposure to credit risk	4.3%	11.4%	31.6%	10.6%	9.6%	9.5%	2.8%	5.1%	9.6%	2.4%	2.4%	0.6%	0.1%	100%

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

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

All amounts are in ISK million

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

				Corporations										
As at 31 December 2018	**Financial institutions**	**Public entities***	**Individuals**	**Fisheries**	**Construction companies**	**Real estate companies**	**Holding companies**	**Retail**	**Services**	**ITC****	**Manu-facturing**	**Agriculture**	**Other**	**Carrying amount**
Cash and balances with Central Bank	-	70,854	-	-	-	-	-	-	-	-	-	-	-	**70,854**
Bonds and debt instruments	3,507	63,222	-	-	-	9,336	69	-	-	-	-	-	924	**77,058**
Equities and equity instruments, banking book	104	-	-	152	5	42	10,646	364	1,541	-	50	59	522	**13,485**
Derivative instruments	1,529	-	11	4	48	76	165	39	1	-	-	-	50	**1,923**
Loans and advances to financial institutions	71,385	-	-	-	-	-	-	-	-	-	-	-	-	**71,385**
Loans and advances to customers	-	4,720	413,699	146,912	87,510	137,343	30,971	63,644	119,439	29,799	21,936	8,559	-	**1,064,532**
Other financial assets	1,903	27	108	-	159	229	31	3	2,320	45	39	-	-	**4,864**
Total on-balance sheet exposure	**78,428**	**138,823**	**413,818**	**147,068**	**87,722**	**147,026**	**41,882**	**64,050**	**123,301**	**29,844**	**22,025**	**8,618**	**1,496**	**1,304,101**
Off-balance sheet exposure	**3,760**	**2,936**	**31,099**	**12,935**	**56,891**	**22,057**	**2,668**	**19,502**	**22,069**	**5,659**	**23,994**	**1,082**	**31**	**204,683**
Financial guarantees and underwriting commitments	255	-	784	827	3,829	1,109	792	2,524	5,211	2,092	593	79	-	18,095
Undrawn loan commitments	-	-	15	9,217	49,903	19,457	1,319	11,910	9,644	2,317	20,020	195	-	123,997
Undrawn overdraft/credit card facilities	3,505	2,936	30,300	2,891	3,159	1,491	557	5,068	7,214	1,250	3,381	808	31	62,591
Maximum exposure to credit risk	**82,188**	**141,759**	**444,917**	**160,003**	**144,613**	**169,083**	**44,550**	**83,552**	**145,370**	**35,503**	**46,019**	**9,700**	**1,527**	**1,508,784**
Percentage of maximum exposure to credit risk	5.4%	9.4%	29.5%	10.6%	9.6%	11.2%	3.0%	5.5%	9.6%	2.4%	3.1%	0.6%	0.1%	100.0%

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

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

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60. Collateral and loan-to-value

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

	LTV ratio - Fully collateralised					LTV ratio - Partially collateralised				
As at 31 December 2019	**0% - 25%**	**25% - 50%**	**50% - 75%**	**75% - 100%**	**Total**	**>100%**	**Collateral value***	**Without collateral**	**Allowance for impairment**	**Carrying amount**
Financial institutions	-	-	-	-	0	-	-	47,930	(1)	47,929
Public entities	49	28	141	36	254	41	5	3,875	(35)	4,135
Individuals	**36,333**	**112,769**	**256,069**	**29,480**	**434,651**	**3,507**	**2,269**	**31,938**	**(2,151)**	**467,945**
Mortgages	25,753	103,192	241,093	21,113	391,151	892	425	710	(848)	391,905
Other	10,580	9,577	14,976	8,367	43,500	2,615	1,844	31,228	(1,303)	76,040
Corporates	**23,353**	**157,567**	**199,288**	**148,550**	**528,758**	**118,000**	**96,635**	**34,043**	**(12,697)**	**668,104**
Fisheries	9,844	51,195	54,453	32,012	147,504	4,011	3,188	277	(456)	151,336
Construction companies	1,010	6,488	10,079	32,391	49,968	48,487	44,404	1,758	(1,677)	98,536
Real estate companies	2,025	23,980	60,917	24,723	111,645	21,322	18,316	5,207	(2,174)	136,000
Holding companies	3,433	20,695	323	349	24,800	756	552	727	(129)	26,154
Retail	2,252	25,483	12,119	11,469	51,323	7,957	5,586	2,194	(949)	60,525
Services	3,300	17,536	50,803	37,670	109,309	21,478	17,413	7,323	(4,784)	133,326
Information, technology and communication	56	8,703	2,049	59	10,867	11,800	5,792	10,397	(121)	32,943
Manufacturing	645	2,176	5,637	7,013	15,471	1,228	819	5,961	(2,295)	20,365
Agriculture	788	1,311	2,908	2,864	7,871	961	565	198	(112)	8,918
Other	-	-	-	-	-	-	-	1	-	1
Total	**59,735**	**270,364**	**455,498**	**178,066**	**963,663**	**121,548**	**98,909**	**117,786**	**(14,884)**	**1,188,113**

*If LTV is less than 100% the loan is considered fully secured. If LTV is greater than 100% the loan is partially collateralised and the respective collateral value is shown in the table.

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60. Collateral and loan-to-value (continued)

As at 31 December 2018	LTV ratio - Fully collateralised 0% - 25%	25% - 50%	50% - 75%	75% - 100%	Total	LTV ratio - Partially collateralised >100%	Collateral value*	Without collateral	Allowance for impairment	Carrying amount
Financial institutions	-	-	-	-	-	-	-	71,387	(2)	71,385
Public entities	58	20	106	58	242	42	19	4,581	(145)	4,720
Individuals	29,219	90,793	224,419	36,576	381,007	4,787	3,182	30,246	(2,341)	413,699
Mortgages	20,611	77,814	209,505	26,867	334,797	1,413	1,046	475	(886)	335,799
Other	8,608	12,979	14,914	9,709	46,210	3,374	2,136	29,771	(1,455)	77,900
Corporates	10,452	120,777	178,738	185,134	495,101	129,907	99,977	31,424	(10,319)	646,113
Fisheries	755	36,736	47,333	55,288	140,112	6,880	4,878	303	(383)	146,912
Construction companies	526	3,069	14,238	31,151	48,984	38,938	31,490	1,383	(1,795)	87,510
Real estate companies	2,572	23,980	36,273	43,992	106,817	28,903	22,573	3,231	(1,608)	137,343
Holding companies	650	23,894	1,846	1,946	28,336	2,006	1,145	823	(194)	30,971
Retail	893	4,354	31,729	16,428	53,404	9,023	5,512	2,030	(813)	63,644
Services	3,478	17,817	30,648	32,765	84,708	27,994	21,219	9,681	(2,944)	119,439
Information, technology and communication	52	7,818	1,201	127	9,198	12,090	10,075	8,634	(123)	29,799
Manufacturing	665	1,697	13,199	2,320	17,881	1,162	895	5,177	(2,284)	21,936
Agriculture	861	1,412	2,271	1,117	5,661	2,911	2,190	162	(175)	8,559
Other	-	-	-	-	-	-	-	-	-	-
Total	39,729	211,590	403,263	221,768	876,350	134,736	103,178	137,638	(12,807)	1,135,917

*If LTV is less than 100% the loan is considered fully secured. If LTV is greater than 100% the loan is partially collateralised and the respective collateral value is shown in the table.

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61. Collateral types

The following tables disclose the assignments of collateral values to claim values, whereby the value of each individual collateral item held cannot exceed the gross carrying amount of the corresponding individual claim. Changes in collateral value amounts between periods result either from changes in the underlying value of collateral or changes in the gross carrying amount.

As at 31 December 2019	Real estate	Vessels	Deposits	Securities	Other*	Total
Public entities	**218**	**-**	**1**	**-**	**38**	**257**
Individuals	**418,218**	**82**	**74**	**2,691**	**15,598**	**436,663**
Mortgages	387,130	11	23	26	4,157	391,347
Other	31,088	71	51	2,665	11,441	45,316
Corporates	**363,815**	**107,729**	**1,560**	**65,867**	**86,419**	**625,390**
Fisheries	9,956	106,024	29	21,236	13,445	150,690
Construction companies	89,978	39	1,037	85	3,233	94,372
Real estate companies	128,840	21	110	217	772	129,960
Holding companies	1,156	-	-	24,001	196	25,353
Retail	29,612	-	25	7,664	19,607	56,908
Services	84,959	1,643	308	3,322	36,491	126,723
Information, technology and communication	1,966	-	16	9,328	5,348	16,658
Manufacturing	11,273	2	31	14	4,969	16,289
Agriculture	6,075	-	4	-	2,358	8,437
Other	-	-	-	-	-	-
Total	**782,251**	**107,811**	**1,635**	**68,558**	**102,055**	**1,062,310**

As at 31 December 2018	Real estate	Vessels	Deposits	Securities	Other*	Total
Public entities	**209**	**-**	**2**	**-**	**49**	**260**
Individuals	**364,073**	**96**	**167**	**2,748**	**17,183**	**384,267**
Mortages	331,631	16	91	31	4,170	335,939
Other	32,442	80	76	2,717	13,013	48,328
Corporates	**322,111**	**108,996**	**4,910**	**68,737**	**90,717**	**595,471**
Fisheries	9,530	107,296	386	15,257	12,639	145,108
Construction companies	73,430	46	1,557	77	5,405	80,515
Real estate companies	127,043	38	555	1,221	622	129,479
Holding companies	3,093	-	146	26,251	13	29,503
Retail	22,901	3	106	12,349	23,599	58,958
Services	69,033	1,613	327	3,811	31,211	105,995
Information, technology and communication	1,293	-	30	9,507	8,451	19,281
Manufacturing	9,723	-	1,800	264	7,003	18,790
Agriculture	6,065	-	3	-	1,774	7,842
Other	-	-	-	-	-	-
Total	**686,393**	**109,092**	**5,079**	**71,485**	**107,949**	**979,998**

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

62. Loans and advances by geographical area

Geographical segmentation is based on the customer's country of residence rather than the location of the creditor.

As at 31 December 2019	Domestic	Foreign	Carrying amount
Loans and advances to financial institutions	8	47,921	47,929
Loans and advances to customers	1,103,403	36,781	1,140,184
Total	**1,103,411**	**84,702**	**1,188,113**

As at 31 December 2018	Domestic	Foreign	Carrying amount
Loans and advances to financial institutions	11	71,374	71,385
Loans and advances to customers	1,026,465	38,067	1,064,532
Total	**1,026,476**	**109,441**	**1,135,917**

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63. Credit quality of loans and advances

The following tables show the credit quality of loans and advances, measured by rating grade. Further details on rating grades can be seen in Note 56, Credit risk assessment.

	Gross carrying amount						
As at 31 December 2019	10-7	6-4	3-1	0	Unrated	Allowance for impairment	Carrying amount
Financial institutions	**47,923**	**7**	**-**	**-**	**-**	**(1)**	**47,929**
Public entities	**245**	**3,925**	**-**	**-**	**-**	**(35)**	**4,135**
Individuals	**236,273**	**201,184**	**27,122**	**5,497**	**20**	**(2,151)**	**467,945**
Mortgages	211,262	159,730	18,491	3,270	-	(848)	391,905
Other	25,011	41,454	8,631	2,227	20	(1,303)	76,040
Corporates	**54,655**	**541,538**	**56,043**	**28,510**	**55**	**(12,697)**	**668,104**
Fisheries	5,814	140,476	4,904	598	-	(456)	151,336
Construction companies	598	82,251	14,921	2,443	-	(1,677)	98,536
Real estate companies	982	122,167	10,029	4,942	54	(2,174)	136,000
Holding companies	164	20,023	6,018	78	-	(129)	26,154
Retail	23,654	30,399	5,415	2,006	-	(949)	60,525
Services	14,087	97,949	13,036	13,037	1	(4,784)	133,326
Information, technology and communication	344	32,433	247	40	-	(121)	32,943
Manufacturing	7,676	8,994	986	5,004	-	(2,295)	20,365
Agriculture	1,336	6,846	486	362	-	(112)	8,918
Other	-	-	1	-	-	-	1
Total	**339,096**	**746,654**	**83,165**	**34,007**	**75**	**(14,884)**	**1,188,113**

	Gross carrying amount						
As at 31 December 2018	10-7	6-4	3-1	0	Unrated	Allowance for impairment	Carrying amount
Financial institutions	**71,376**	**11**	**-**	**-**	**-**	**(2)**	**71,385**
Public entities	**469**	**4,389**	**7**	**-**	**-**	**(145)**	**4,720**
Individuals	**154,648**	**216,864**	**39,147**	**4,492**	**889**	**(2,341)**	**413,699**
Mortgages	140,745	167,355	25,570	2,375	640	(886)	335,799
Other	13,903	49,509	13,577	2,117	249	(1,455)	77,900
Corporates	**68,189**	**500,981**	**60,965**	**25,886**	**411**	**(10,319)**	**646,113**
Fisheries	20,962	120,554	4,060	1,458	261	(383)	146,912
Construction companies	1,379	66,351	18,031	3,544	-	(1,795)	87,510
Real estate companies	765	119,006	14,291	4,829	60	(1,608)	137,343
Holding companies	1	26,134	4,882	148	-	(194)	30,971
Retail	25,354	34,968	2,544	1,591	-	(813)	63,644
Services	11,464	87,560	15,711	7,558	90	(2,944)	119,439
Information, technology and communication	273	29,497	53	99	-	(123)	29,799
Manufacturing	6,582	10,749	877	6,012	-	(2,284)	21,936
Agriculture	1,409	6,162	516	647	-	(175)	8,559
Other	-	-	-	-	-	-	0
Total	**294,682**	**722,245**	**100,119**	**30,378**	**1,300**	**(12,807)**	**1,135,917**

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64. Loans and advances by past due status

The following tables show the gross carrying amount of loans and advances to financial institutions and customers by past due status.

	Gross carrying amount							
		Days past due						
As at 31 December 2019	Not past due	1-5	6-30	31-60	61-90	over 90	Allowance for impairment	Carrying amount
Financial institutions	**47,930**	**-**	**-**	**-**	**-**	**-**	**(1)**	**47,929**
Public entities	**4,120**	**50**	**-**	**-**	**-**	**-**	**(35)**	**4,135**
Individuals	**457,047**	**2,662**	**2,344**	**4,175**	**1,134**	**2,734**	**(2,151)**	**467,945**
Mortgages	385,776	-	1,593	3,126	824	1,434	(848)	391,905
Other	71,271	2,662	751	1,049	310	1,300	(1,303)	76,040
Corporates	**652,881**	**4,413**	**5,195**	**4,269**	**2,504**	**11,539**	**(12,697)**	**668,104**
Fisheries	151,055	234	83	65	4	351	(456)	151,336
Construction companies	98,426	293	214	427	90	763	(1,677)	98,536
Real estate companies	131,356	172	2,850	1,856	401	1,539	(2,174)	136,000
Holding companies	26,242	9	9	17	3	3	(129)	26,154
Retail	59,672	684	467	67	72	512	(949)	60,525
Services	126,640	2,675	1,455	1,680	1,877	3,783	(4,784)	133,326
Information, technology and communication	32,836	57	64	61	8	38	(121)	32,943
Manufacturing	17,779	242	49	90	34	4,466	(2,295)	20,365
Agriculture	8,875	46	4	6	15	84	(112)	8,918
Other	-	1	-	-	-	-	-	1
Total	**1,161,978**	**7,125**	**7,539**	**8,444**	**3,638**	**14,273**	**(14,884)**	**1,188,113**

	Gross carrying amount							
		Days past due						
As at 31 December 2018	Not past due	1-5	6-30	31-60	61-90	over 90	Allowance for impairment	Carrying amount
Financial institutions	**71,387**	**-**	**-**	**-**	**-**	**-**	**(2)**	**71,385**
Public entities	**4,848**	**-**	**16**	**1**	**-**	**-**	**(145)**	**4,720**
Individuals	**402,153**	**2,842**	**2,780**	**4,204**	**879**	**3,182**	**(2,341)**	**413,699**
Mortgages	329,665	-	1,984	2,996	590	1,450	(886)	335,799
Other	72,488	2,842	796	1,208	289	1,732	(1,455)	77,900
Corporations	**629,832**	**9,059**	**4,243**	**2,549**	**1,035**	**9,714**	**(10,319)**	**646,113**
Fisheries	146,381	371	20	50	3	470	(383)	146,912
Construction companies	84,409	990	785	64	212	2,845	(1,795)	87,510
Real estate companies	134,799	162	1,238	1,109	215	1,428	(1,608)	137,343
Holding companies	30,853	104	8	114	18	68	(194)	30,971
Retail	62,378	283	532	155	49	1,060	(813)	63,644
Services	113,694	2,630	1,550	919	361	3,229	(2,944)	119,439
Information, technology and communication	29,758	63	3	2	8	88	(123)	29,799
Manufacturing	19,308	4,345	88	88	11	380	(2,284)	21,936
Agriculture	8,252	111	19	48	158	146	(175)	8,559
Other	-	-	-	-	-	-	-	0
Total	**1,108,220**	**11,901**	**7,039**	**6,754**	**1,914**	**12,896**	**(12,807)**	**1,135,917**

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65. Loans and advances by stage allocation

The table below show both gross carrying amount and expected credit loss (ECL) by industry sectors and the three-stage criteria under IFRS 9.

		Stage 1		Stage 2		Stage 3				
As at 31 December 2019	Gross carrying amount	Gross carrying amount	12-month ECL	Gross carrying amount	Lifetime ECL	Gross carrying amount	Lifetime ECL	Allowance for impairment	Fair Value	Carrying amount
Financial institutions	**47,930**	**47,929**	**(1)**	**1**	**-**	**-**	**-**	**(1)**	**-**	**47,929**
Public entities	**4,170**	**4,058**	**(34)**	**112**	**(1)**	**-**	**-**	**(35)**	**-**	**4,135**
Individuals	**470,096**	**429,012**	**(370)**	**35,587**	**(584)**	**5,497**	**(1,197)**	**(2,151)**	**-**	**467,945**
Mortgages	392,753	364,991	(171)	24,492	(329)	3,270	(348)	(848)	-	391,905
Other	77,343	64,021	(199)	11,095	(255)	2,227	(849)	(1,303)	-	76,040
Corporates	**680,801**	**572,853**	**(1,986)**	**64,759**	**(1,393)**	**28,510**	**(9,318)**	**(12,697)**	**14,679**	**668,104**
Fisheries	151,792	143,576	(236)	4,959	(85)	598	(135)	(456)	2,659	151,336
Construction companies	100,213	78,562	(548)	19,208	(302)	2,443	(827)	(1,677)	-	98,536
Real estate companies	138,174	120,626	(497)	12,606	(346)	4,942	(1,331)	(2,174)	-	136,000
Holding companies	26,283	24,277	(105)	1,928	(15)	78	(9)	(129)	-	26,154
Retail	61,474	52,414	(101)	4,870	(133)	2,006	(715)	(949)	2,184	60,525
Services	138,110	107,737	(369)	15,538	(434)	13,037	(3,981)	(4,784)	1,798	133,326
Information, technology and communication	33,064	24,716	(96)	270	(4)	40	(21)	(121)	8,038	32,943
Manufacturing	22,660	15,260	(21)	2,396	(50)	5,004	(2,224)	(2,295)	-	20,365
Agriculture	9,030	5,685	(13)	2,983	(24)	362	(75)	(112)	-	8,918
Other	1	-	-	1	-	-	-	-	-	1
Total	**1,202,997**	**1,053,852**	**(2,391)**	**100,459**	**(1,978)**	**34,007**	**(10,515)**	**(14,884)**	**14,679**	**1,188,113**

All amounts are in ISK million

65. Loans and advances by stage allocation (continued)

As at 31 December 2018	Gross carrying amount	Stage 1 Gross carrying amount	Stage 1 12-month ECL	Stage 2 Gross carrying amount	Stage 2 Lifetime ECL	Stage 3 Gross carrying amount	Stage 3 Lifetime ECL	Allowance for impairment	Fair Value	Carrying amount
Financial institutions	**71,387**	**71,384**	**(2)**	**3**	**-**	**-**	**-**	**(2)**	**-**	**71,385**
Public entities	**4,865**	**1,859**	**(8)**	**3,006**	**(137)**	**-**	**-**	**(145)**	**-**	**4,720**
Individuals	**416,040**	**363,967**	**(561)**	**47,581**	**(602)**	**4,492**	**(1,178)**	**(2,341)**	**-**	**413,699**
Mortgages	336,685	301,920	(240)	32,390	(343)	2,375	(303)	(886)	-	335,799
Other	79,355	62,047	(321)	15,191	(259)	2,117	(875)	(1,455)	-	77,900
Corporates	**656,432**	**582,067**	**(1,714)**	**38,809**	**(468)**	**25,886**	**(8,137)**	**(10,319)**	**9,670**	**646,113**
Fisheries	147,295	135,868	(83)	8,373	(42)	1,458	(258)	(383)	1,596	146,912
Construction companies	89,305	79,649	(620)	6,112	(110)	3,544	(1,065)	(1,795)	-	87,510
Real estate companies	138,951	127,569	(569)	5,575	(82)	4,829	(957)	(1,608)	978	137,343
Holding companies	31,165	30,818	(84)	199	(4)	148	(106)	(194)	-	30,971
Retail	64,457	56,974	(88)	4,391	(28)	1,591	(697)	(813)	1,501	63,644
Services	122,383	102,188	(169)	10,514	(159)	7,558	(2,616)	(2,944)	2,123	119,439
Information, technology and communication	29,922	26,210	(61)	141	(1)	99	(61)	(123)	3,472	29,799
Manufacturing	24,220	17,003	(32)	1,205	(18)	6,012	(2,234)	(2,284)	-	21,936
Agriculture	8,734	5,788	(8)	2,299	(24)	647	(143)	(175)	-	8,559
Other	-	-	-	-	-	-	-	-	-	0
Total	**1,148,724**	**1,019,277**	**(2,285)**	**89,399**	**(1,207)**	**30,378**	**(9,315)**	**(12,807)**	**9,670**	**1,135,917**

All amounts are in ISK million

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

See accounting policy in Note 88.5 (g).

The following tables show changes in the impairment allowance of loans and advances during the year 2019.

	12-months ECL Stage 1	Lifetime ECL Stage 2	Lifetime ECL Stage 3	Total
Restated balance as at 1 January 2019 - Financial institutions	**(2)**	**(5)**	**-**	**(7)**
Changes in models/risk parameters	1	-	-	1
Balance as at 31 December 2019 - Financial institutions	**(1)**	**(5)**	**0**	**(6)**
- therof classified as deduction from gross carrying amounts	(1)	-	-	(1)
- therof classified as liabilities	-	(5)	-	(5)

	12-months ECL Stage 1	Lifetime ECL Stage 2	Lifetime ECL Stage 3	Total
Balance as at 1 January 2019 - Loans and advances to customers	**(2,552)**	**(1,230)**	**(9,345)**	**(13,127)**
New financial assets originated	(1,084)	(497)	(2,445)	(4,026)
Reversals due to financial assets that have been derecognised	854	267	1,850	2,971
Changes due to reclassification of financial assets	7	-	-	7
Transfer to Stage 1 - 12-month ECL	(91)	83	8	0
Transfer to Stage 2 - Lifetime ECL	920	(937)	17	0
Transfer to Stage 3 - Lifetime ECL	1,230	928	(2,158)	0
Changes in models/risk parameters	(1,884)	(658)	(529)	(3,071)
Provisions used to cover write-offs	20	16	1,978	2,014
Balance as at 31 December 2019 - Loans and advances to customers	**(2,580)**	**(2,028)**	**(10,624)**	**(15,232)**
- therof classified as deduction from gross carrying amounts	(2,390)	(1,978)	(10,515)	(14,883)
- therof classified as liabilities	(190)	(50)	(109)	(349)

	1.1-31.12.2019				
	Financial institutions	Public entities	Individuals	Corporates	Total
New financial assets originated	-	(1)	(338)	(3,687)	(4,026)
Reversals due to financial assets that have been derecognised	-	1	405	2,565	2,971
Changes due to reclassification of financial assets	-	-	-	7	7
Changes due to financial assets recognised in the opening balance	1	105	(317)	(2,859)	(3,070)
Write-offs	-	-	(787)	(2,772)	(3,559)
Provisions used to cover write-offs	-	-	436	1,578	2,014
Recoveries	-	-	478	265	743
Translation difference	-	-	1	65	66
Net impairment on loans and advances	**1**	**105**	**(122)**	**(4,838)**	**(4,854)**

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66. Allowance for impairment on loans and advances to financial institutions and customers and other assets (continued)

The following tables show changes in the impairment allowance of loans and advances during the year 2018.

	ECL Stage 1	ECL Stage 2	ECL Stage 3	Total
Restated balance as at 1 January 2018 - Financial institutions	**(3)**	**-**	**-**	**(3)**
New financial assets originated	-	(1)	-	(1)
Transfer to Stage 2 - Lifetime ECL	4	(4)	-	0
Changes in models/risk parameters	(3)	-	-	(3)
Balance as at 31 December 2018 - Financial institutions	**(2)**	**(5)**	**0**	**(7)**
- therof classified as deduction from gross carrying amounts	(2)	-	-	(2)
- therof classified as liabilities	-	(5)	-	(5)

	ECL Stage 1	ECL Stage 2	ECL Stage 3	Total
Restated balance as at 1 January 2018 - Loans and advances to customers	**(2,671)**	**(1,048)**	**(13,075)**	**(16,794)**
New financial assets originated	(1,359)	(350)	(494)	(2,203)
Reversals due to financial assets that have been derecognised	976	207	1,080	2,263
Changes due to reclassification of financial assets	80	-	-	80
Transfer to Stage 1 - 12-month ECL	(103)	84	19	0
Transfer to Stage 2 - Lifetime ECL	452	(483)	31	0
Transfer to Stage 3 - Lifetime ECL	990	470	(1,460)	0
Changes in models/risk parameters	(949)	(120)	1,050	(19)
Provisions used to cover write-offs	31	10	3,505	3,546
Balance as at 31 December 2018 - Loans and advances to customers	**(2,553)**	**(1,230)**	**(9,344)**	**(13,127)**
- therof classified as deduction from gross carrying amounts	(2,283)	(1,207)	(9,315)	(12,805)
- therof classified as liabilities	(270)	(23)	(29)	(322)

	1.1-31.12.2018				
	Financial institutions	Public entities	Individuals	Corporates	Total
New financial assets originated	(2)	(1)	(359)	(1,842)	(2,204)
Reversals due to financial assets that have been derecognised	-	124	507	1,632	2,263
Changes due to reclassification of financial assets	-	-	-	80	80
Changes due to financial assets recognised in the opening balance	(3)	14	173	(206)	(22)
Write-offs	-	-	(946)	(3,714)	(4,660)
Provisions used to cover write-offs	-	-	654	2,892	3,546
Recoveries	-	-	509	328	837
Translation difference	-	-	1	458	459
Net impairment on loans and advances	**(5)**	**137**	**539**	**(372)**	**299**

67. Large exposures

As at 31 December 2019, five customer groups were rated as large exposures in accordance with rules on large exposures. Customers are rated as large exposures if their total obligations, or those of financially or administratively connected parties, exceed 10% of the Group's eligible capital. According to the rules, no exposure, after credit risk mitigation, may exceed 25% of the elibible capital. The following table shows the Group's large exposures after credit mitigation:

As at 31 December 2019	Number of large exposures	Large exposures
Large exposures between 10% and 20% of the Group's eligible capital	3	100,057
Large exposures between 0% and 10% of the Group's eligible capital	2	-
Total	**5**	**100,057**
Total ratio of large exposures to eligible capital		38%
As at 31 December 2018		
Large exposures between 10% and 20% of the Group's eligible capital	3	83,842
Large exposures between 0% and 10% of the Group's eligible capital	1	-
Total	**4**	**83,842**
Total ratio of large exposures to eligible capital		34%

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68. Bonds and debt instruments

A breakdown of the Group's bond portfolio, by Standard & Poor's ratings, is as follows:

Government bonds and treasury bills	**31.12.2019**	**31.12.2018**
Rated AAA	34,079	26,685
Rated AA- to AA+	48,241	23,247
Rated A- to A+	9,241	7,187
Rated BBB+ and below	3,355	576
	94,916	**57,695**
Corporate bonds		
Rated AAA	-	
Rated A- to A+	1,488	379
Rated BBB- to BBB+	4,152	3,776
Rated BB+ and below	322	-
Unrated	3,049	11,701
	9,011	**15,856**
Asset-backed securities		
Rated BBB- to BBB+	11,335	3,507
	11,335	**3,507**
Total	**115,262**	**77,058**

The following table shows the carrying amounts of bonds for which the issuers have failed, by one or more days, to make contractually due payments.

As at 31 December 2019	**Past due 0 - 90 days**	**Past due over 90 days**	**Carrying amount**
Holding companies	-	21	21
Other	-	3	3
Total	**0**	**24**	**24**
As at 31 December 2018			
Holding companies	-	65	65
Other	-	3	3
Total	**0**	**68**	**68**

69. Derivative instruments

The following table summarises the Group's exposure in derivative instruments, classified by the Bank into equivalent Standard & Poor's ratings by counterparty:

	2019			**2018**		
	Notional	**Fair value**		**Notional**	**Fair value**	
	amount	**Assets**	**Liabilities**	**amount**	**Assets**	**Liabilities**
AA- to AA+	9,857	-	244	-	-	-
A+/A/A-	145,437	1,910	1,699	151,264	1,289	1,073
BBB+	1,000	71	-	5,812	117	11
BB+	-	-	-	1,418	39	3
Unrated	50,499	713	1,366	25,135	478	551
Total	**206,793**	**2,694**	**3,309**	**183,629**	**1,923**	**1,638**

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70. Offsetting financial assets and financial liabilities

The following table shows reconciliation of the net amounts of financial assets and financial liabilities. These are subject to offsetting, enforceable master netting agreements and other similar agreements.

As at 31 December 2019

Financial assets subject to offsetting, enforceable master netting arrangement and similar agreements

	Financial assets subject to netting agreements			Netting not recognised on balance sheet				
Types of financial assets	Financial assets	Financial liabilities	Net amount	Financial liabilities	Collateral received	Net financial assets subject to netting agreements	Financial assets not subject to netting agreements	Net amount on balance sheet
Derivatives	2,694	-	2,694	(499)	(2,088)	107	-	2,694

Financial liabilities subject to offsetting, enforceable master netting arrangement and other similar agreements

	Financial liabilities subject to netting agreements			Netting not recognised on balance sheet				
Types of financial liabilities	Financial liabilities	Financial assets	Net amount	Financial assets	Collateral pledged	Net financial liabilities subject netting agreements	Financial liabilities not subject to netting agreements	Net amount on balance sheet
Derivatives	(3,309)	-	(3,309)	(499)	1,827	(1,981)	-	(3,309)
Short positions	(2,081)	-	(2,081)	-	2,081	-	-	(2,081)
Total	**(5,390)**	**0**	**(5,390)**	**(499)**	**3,908**	**(1,981)**	**0**	**(5,390)**

As at 31 December 2018

Financial assets subject to offsetting, enforceable master netting arrangement and other similar agreements

	Financial assets subject to netting agreements			Netting not recognised on balance sheet				
Types of financial assets	Financial assets	Financial liabilities	Net amount	Financial liabilities	Collateral received	Net financial assets subject to netting agreements	Financial assets not subject to netting agreements	Net amount on balance sheet
Derivatives	1,923	-	1,923	(284)	(806)	833	-	1,923

Financial liabilities subject to offsetting, enforceable master netting arrangement and other similar agreements

	Financial liabilities subject to netting agreements			Netting not recognised on balance sheet				
Types of financial liabilities	Financial liabilities	Financial assets	Net amount	Financial assets	Collateral pledged	Net financial liabilities subject to netting agreements	Financial liabilities not subject to netting agreements	Net amount on balance sheet
Derivatives	(1,638)	-	(1,638)	(284)	1,007	(916)	-	(1,638)
Short positions	(4,908)	-	(4,908)	-	4,908	-	-	(4,908)
Total	**(6,546)**	**0**	**(6,546)**	**(284)**	**5,915**	**(916)**	**0**	**(6,546)**

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Liquidity risk

71. Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting its obligations associated with financial liabilities that are settled by delivering cash or another financial asset, or of having to do so at excessive cost. This risk arises from earlier maturities of financial liabilities than financial assets.

72. Liquidity risk management

A liquidity management policy for the Bank and its subsidiaries is in place. The objective of the liquidity management policy is to ensure, even in times of stress, that sufficient liquid assets and funding capacity are available to meet financial obligations in a timely manner and at reasonable cost. Furthermore, the liquidity management policy is to describe the manner in which the Group identifies, evaluates, measures, monitors, manages and reports its liquidity. Enforcing this policy has the further objective of minimising fluctuations in liquidity. The liquidity management policy is built on the European regulation, Capital Requirements Regulation (CRR), defined within the European Banking Authority (EBA). The Bank´s main metrics for measuring liquidity risk is the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR). The objective of the LCR is to promote short-term resilience by ensuring that the Group has sufficient high-quality liquid assets to survive a significant stress scenario lasting 30 calendar days. NSFR has a longer time horizon and its objective is to capture structural issues in the balance sheet with the aim to provide a sustainable maturity structure of assets and liabilities and to limit overreliance on short-term wholesale funding.

The Group complies with liquidity rules set by the Central Bank of Iceland No. 266/2017. The Group also follows Central Bank rules No. 1032/2014 on funding ratios in foreign currencies, as well as guidelines No. 2/2010 from the Icelandic Financial Supervisory Authority on best practice for managing liquidity in banking organisation. The Central Bank's liquidity rules No. 266/2017 require the Group to maintain a total liquidity coverage ratio (LCR) of 100% at a minimum and also a LCR in foreign currencies of 100% at a minimum. The Central Bank of Iceland made changes to rules No. 266/2017 in December 2019, implementing a minimum requirement for liquidity ratio in Icelandic króna. Effective as of January 1 2020, the minimum LCR in Icelandic króna will be 30%. Rules No. 1032/2014 set requirements for a minimum of 100% net stable funding ratio (NSFR) in foreign currencies. The Group submits monthly reports on its liquidity and funding position to the Central Bank of Iceland and the FME.

The Group has implemented a risk appetite where these rules and guidelines alongside the Bank's internal requirements set benchmarks for liquidity management.

The Group's liquidity risk is managed centrally by Treasury and is monitored by Market Risk. This allows management to monitor and manage liquidity risk throughout the Group. The Risk & Finance Committee monitors the Group's liquidity risk, while the Bank's Internal Audit function assesses whether the liquidity management process is designed properly and operating effectively.

The Group monitors intraday liquidity risk, short-term 30 day liquidity risk, medium and longer-term liquidity risk and risk arising from mismatches of longer term assets and liabilities.

The Group's liquidity management process includes: projecting expected cash flows in a maturity profile rather than relying merely on contractual maturities, monitoring balance sheet liquidity, monitoring and managing the maturity profile of liabilities and off-balance sheet commitments, monitoring the concentration of liquidity risk in order to avoid undue reliance on large financing counterparties, projecting cash flows arising from future business, and maintaining liquidity and contingency plans which outline measures to take in the event of difficulties arising from liquidity crisis.

Market Risk conducts monthly stress tests by applying various hypothetical scenarios on the Group's liquidity position to ensure that it has adequate liquidity to withstand stressed conditions. Different assumptions are drawn for each stress test to estimate the impact of a variety of market conditions.

The key indicator of short-term liquidity risk is measured by the LCR which shows the ratio of high quality liquid assets to expected total net cash outflows over the next 30 days under a specified stress scenario. High quality liquid assets are comprised of cash at hand, balances with the Central Bank, assets eligible for repo transactions with the Central Bank assets with government guarantee and zero percent risk-weighted foreign government bonds. Estimated inflow and outflow weights, according to rules No. 266/2017, are applied to the total balance amount for each asset and liability group measured in the ratio, reflecting the next 30 calendar days. Financial institutions can at a maximum assume 75% of their estimated inflow net to their estimated outflow. This is done so that financial institutions can not overly rely on their estimated inflow in times of stress. The calculations for the ratio as at 31 December 2019 and 31 December 2018 are shown in the following table:

	Total		Foreign currencies		ISK	
Liquidity coverage ratio 31 December 2019	**Unweighted**	**Weighted**	**Unweighted**	**Weighted**	**Unweighted**	**Weighted**
Level 1 liquid assets	141,172	141,172	83,846	83,846	57,327	57,327
Level 2 liquid assets	5,048	4,156	4,148	3,526	900	630
Information items	22,211	-	2,476	-	19,734	-
Total liquid assets	**168,431**	**145,328**	**90,470**	**87,372**	**77,961**	**57,957**
Deposits	523,236	136,855	96,026	42,320	427,210	94,535
Borrowing	165	165	165	165	-	-
Other outflows	129,015	17,459	33,158	2,973	95,857	14,486
Total outflows (0-30 days)	**652,416**	**154,479**	**129,349**	**45,458**	**523,067**	**109,021**
Loans and advances to financial institutions	57,584	46,767	47,825	46,767	9,759	-
Other inflows	37,177	17,187	6,831	3,773	30,346	13,414
Limit on inflows	-	-	-	(16,447)	-	-
Total inflows (0-30 days)	**94,761**	**63,954**	**54,656**	**34,093**	**40,105**	**13,414**
Liquidity coverage ratio		**161%**		**769%**		**61%**

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72. Liquidity risk management (continued)

	Total		Foreign currencies		ISK	
Liquidity coverage ratio 31 December 2018	**Unweighted**	**Weighted**	**Unweighted**	**Weighted**	**Unweighted**	**Weighted**
Level 1 liquid assets	94,961	94,961	51,587	51,587	43,374	43,374
Level 2 liquid assets and information items	17,800	-	4,048	-	13,752	-
Total liquid assets	**112,761**	**94,961**	**55,635**	**51,587**	**57,126**	**43,374**
Deposits	517,428	133,200	86,615	35,216	430,813	97,984
Borrowing	730	730	170	170	560	560
Other outflows	150,699	16,765	31,999	3,263	118,700	13,502
Total outflows (0-30 days)	**668,857**	**150,695**	**118,784**	**38,649**	**550,073**	**112,046**
Loans and advances to financial institutions	81,211	70,340	71,168	70,340	10,043	-
Other inflows	42,789	20,372	11,806	6,442	30,983	13,930
Limit on inflows	-	-	-	(47,795)	-	-
Total inflows (0-30 days)	**124,000**	**90,712**	**82,974**	**28,987**	**41,026**	**13,930**
Liquidity coverage ratio		**158%**		**534%**		**44%**

The following table shows the composition of the Group´s liquidity reserve which is comprised of high quality liquid assets as defined in the Rules on Liquidity Ratio, etc., No. 266/2017, as well as readily available loans and advances to financial institutions.

Liquidity reserves as at 31 December 2019	**Total**	**Foreign currencies**	**ISK**
Cash and balances with the Central Bank	44,235	1,525	42,710
Domestic bonds and debt instruments eligible as collateral with the Central Bank	19,665	4,148	15,517
Foreign government bonds with 0% risk weight	82,320	82,320	-
High quality liquidity assets	**146,220**	**87,993**	**58,227**
Loans and advances to financial institutions	57,584	47,825	9,759
Total liquidity reserves	**203,804**	**135,818**	**67,986**

Liquidity reserves as at 31 December 2018	**Total**	**Foreign currencies**	**ISK**
Cash and balances with the Central Bank	35,291	1,655	33,636
Domestic bonds and debt instruments eligible as collateral at the Central Bank	9,738	-	9,738
Foreign government bonds with 0% risk weight	49,932	49,932	-
High quality liquidity assets	**94,961**	**51,587**	**43,374**
Loans and advances to financial institutions	81,211	71,168	10,043
Total liquidity reserves	**176,172**	**122,755**	**53,417**

The Group measures the net stable funding ratio (NSFR) as another key indicator of liquidity risk up to 12 months. The following table shows the values of the NSFR for foreign currencies and NSFR total as at 31 December 2019 and 31 December 2018:

	2019	**2018**
Net stable funding ratio FX	143%	166%
Net stable funding ratio total	117%	120%

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72. Liquidity risk management (continued)

The following table shows the Groups deposit base categorised into groups based on methodology according to liquidity rules No. 266/2017 set by the Central Bank of Iceland. The deposit groups are categorised by maturity as well as applied run offf rate which indicates their level of stickiness. Stickiness is defined as tendency of funding not to run off quickly under stress.

As at 31. December 2019	Run off rate	0-30 days	Over 30 days	Total
Individuals	5% - 100%	269,432	115,493	384,925
Small and Medium Sized Corporates	5% - 100%	64,672	7,145	71,817
Operational deposits	5% - 25%	-	-	-
Large Corporates	20% - 40%	108,386	20,477	128,863
Public entities	20% - 40%	25,416	9,459	34,875
Financial customers	100%	55,330	71,375	126,705
Pledged deposits		8,297	392	8,689
Total deposits		**531,533**	**224,341**	**755,874**

As at 31. December 2018	Run off rate	0-30 days	Over 30 days	Total
Individuals	5% - 100%	262,276	94,858	357,134
Small and Medium Sized Corporates	5% - 100%	61,461	5,999	67,460
Operational deposits	5% - 25%	-	-	-
Large Corporates	20% - 40%	128,063	31,147	159,210
Public entities	20% - 40%	17,986	7,706	25,692
Financial customers	100%	47,641	61,735	109,376
Pledged deposits		8,263	515	8,778
Total deposits		**525,690**	**201,960**	**727,650**

73. Maturity analysis of financial assets and liabilities

The following tables only take into account the contractual maturity of the Group's assets and liabilities but do not account for measures that the Group could decide upon to convert assets into cash at hand by liquidation either through sale or participation in Central Bank operations. Furthermore all instant access deposits are categorised as outflows in the first time bucket. Further information on the Group's liquidity management can be found in Note 72.

The amounts in the maturity analyses as at year-end 2019 and 2018 are allocated to maturity buckets in respect of remaining contractual maturity (i.e. based on the timing of future cash flows according to contractual terms). For loans and advances in moratorium or in the process of liquidation the Group estimates the amounts from the historical recovery rate. For bonds issued by companies in moratorium or in the process of liquidation the amounts presented are future cash flows estimated as their fair value at the reporting date. These bonds and loans all fall in the time span of 1-5 years.

Amounts presented in the maturity analyses are the undiscounted future cash flows receivable and payable by the Group, including both principal and interest cash flows. These amounts differ from the carrying amounts presented in the statement of financial position, which are based on discounted rather than undiscounted future cash flows. If an amount receivable or payable is not fixed, the amount presented in the maturity analysis has been determined by reference to the relevant interest rates, exchange rates and inflation prevailing at the reporting date. When there is a choice of when an amount shall be paid, future cash flows are calculated on the basis of the earliest date at which the Group can be required to pay, which is the worst case scenario from Group perspective. An example of this is that demand deposits are included in the earliest time span. Where the Group is committed to have amounts available in installments, each installment is allocated to the earliest period in which the Group might be required to pay. Thus undrawn loan commitments are included in the time span together with the earliest date at which such loans may be drawn. For financial guarantee contracts issued by the Group, the amount included in the maturity analysis is the guarantee's maximum amount, allocated to the earliest period in which the guarantee might be called.

Nonetheless, the Group's expected cash flows on demand deposits vary significantly from the amounts presented in the maturity analysis. Demand deposits from customers have short contractual maturities but are considered a relatively stable financing source with expected maturity exceeding one year, and also it is not expected that every committed loan will be drawn down immediately. The Group conducts, as mentioned in Note 72, a monthly stress test to estimate the impact of fluctuating market conditions and deposit withdrawals.

Amounts presented in non-derivative financial assets and non-derivative financial liabilities include all spot deals at year-end 2019 and 2018. When managing liquidity risk the Group regards spot deals as non-derivative assets or liabilities.

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73. Maturity analysis of financial assets and liabilities (continued)

The following table shows a maturity analysis of the Group's financial instruments as at 31 December 2019:

Non-derivative financial liabilities	0-1 month	1-3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total	Carrying amount
Due to financial institutions and Central Bank	(20,495)	(28,028)	-	-	-	-	(48,523)	(48,062)
Deposits from customers	(509,024)	(152,794)	(26,590)	(15,733)	(5,812)	-	(709,953)	(707,813)
Short positions	(26)	(10)	(35)	(290)	(2,369)	-	(2,730)	(2,081)
Borrowings	(111)	(4,748)	(45,838)	(295,518)	(74,514)	-	(420,729)	(373,168)
Other financial liabilities	(7,120)	-	-	-	-	-	(7,120)	(7,118)
Subordinated liabilities	-	-	(642)	(2,616)	(23,562)	-	(26,820)	(19,081)
Total	**(536,776)**	**(185,580)**	**(73,105)**	**(314,157)**	**(106,257)**	**0**	**(1,215,875)**	**(1,157,323)**
Derivative financial liabilities								
Trading								(1,364)
Inflow	4,136	938	1,470	-	-	-	6,544	
Outflow	(5,427)	(954)	(1,531)	-	-	-	(7,912)	
Risk management								(1,945)
Inflow	4,112	3,725	10,379	23,745	2,070	-	44,031	
Outflow	(4,139)	(3,801)	(10,519)	(25,354)	(2,460)	-	(46,273)	
Total	**(1,318)**	**(92)**	**(201)**	**(1,609)**	**(390)**	**0**	**(3,610)**	**(3,309)**
Non-derivative financial assets								
Cash and balances with Central Bank	69,824	-	-	-	-	-	69,824	69,824
Bonds and debt instruments	9,726	45,450	30,435	20,542	13,193	-	119,346	115,262
Equities and equity instruments	-	-	-	-	-	30,019	30,019	30,019
Loans and advances to financial institutions	47,929	-	-	-	-	-	47,929	47,929
Loans and advances to customers	30,490	62,599	150,614	406,265	851,763	-	1,501,731	1,140,184
Other financial assets	7,819	-	-	-	-	-	7,819	7,819
Total	**165,788**	**108,049**	**181,049**	**426,807**	**864,956**	**30,019**	**1,776,668**	**1,411,037**
Derivative financial assets								
Trading								514
Inflow	4,464	689	648	2,228	-	-	8,029	
Outflow	(4,013)	(680)	(597)	(2,216)	-	-	(7,506)	
Risk management								2,180
Inflow	12,447	19,646	4,852	84,404	-	-	121,349	
Outflow	(12,040)	(18,933)	(4,934)	(83,316)	-	-	(119,223)	
Total	**858**	**722**	**(31)**	**1,100**	**0**	**0**	**2,649**	**2,694**
Off-balance sheet items								
Financial guarantees and underwriting commitments	(1,108)	(725)	(4,221)	(5,568)	(11,179)	(1,166)	(23,967)	
Undrawn loan commitments	(95,478)	-	-	-	-	-	(95,478)	
Undrawn overdraft/credit card commitments	(64,032)	-	-	-	-	-	(64,032)	
Total	**(160,618)**	**(725)**	**(4,221)**	**(5,568)**	**(11,179)**	**(1,166)**	**(183,477)**	
Net liquidity position	**(532,066)**	**(77,626)**	**103,491**	**106,573**	**747,130**	**28,853**	**376,355**	**253,099**

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73. Maturity analysis of financial assets and liabilities (continued)

The following table shows a maturity analysis of the Group's financial instruments as at 31 December 2018:

Non-derivative financial liabilities	0-1 month	1-3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total	Carrying amount
Due to financial institutions and Central Bank	(28,184)	(793)	-	(6,324)	-	-	(35,301)	(34,609)
Deposits from customers	(537,958)	(110,014)	(26,002)	(16,246)	(6,474)	-	(696,694)	(693,043)
Short positions	(16)	(1,002)	(135)	(2,419)	(3,478)	-	(7,050)	(4,908)
Borrowings	(40,004)	(28,262)	(41,760)	(231,187)	(99,036)	-	(440,249)	(314,412)
Other financial liabilities	(6,114)	-	-	-	-	-	(6,114)	(6,114)
Subordinated liabilities	-	-	(416)	(1,665)	(15,402)	-	(17,483)	(13,340)
Total	**(612,276)**	**(140,071)**	**(68,313)**	**(257,841)**	**(124,390)**	**0**	**(1,202,891)**	**(1,066,426)**
Derivative financial liabilities								
Trading								(557)
Inflow	6,916	1,724	305	-	-	-	8,945	
Outflow	(7,341)	(1,843)	(333)	-	-	-	(9,517)	
Riks management								(1,081)
Inflow	4,432	181	990	29,472	2,204	-	37,279	
Outflow	(4,457)	(89)	(434)	(31,032)	(2,761)	-	(38,773)	
Total	**(450)**	**(27)**	**528**	**(1,560)**	**(557)**	**0**	**(2,066)**	**(1,638)**
Non-derivative financial assets								
Cash and balances with Central Bank	70,854	-	-	-	-	-	70,854	70,854
Bonds and debt instruments	7,050	36,754	7,656	16,321	28,417	-	96,198	77,058
Equities and equity instruments	-	-	-	-	-	23,547	23,547	23,547
Loans and advances to financial institutions	71,385	-	-	-	-	-	71,385	71,385
Loans and advances to customers	34,647	72,779	172,775	416,779	1,207,280	-	1,904,260	1,064,532
Other financial assets	4,864	-	-	-	-	-	4,864	4,864
Total	**188,800**	**109,533**	**180,431**	**433,100**	**1,235,697**	**23,547**	**2,171,108**	**1,312,240**
Derivative financial assets								
Trading								521
Inflow	6,417	1,342	60	2,425	-	-	10,244	
Outflow	(5,966)	(1,285)	(51)	(2,412)	-	-	(9,714)	
Riks management								1,402
Inflow	25,351	1,090	574	94,319	-	-	121,334	
Outflow	(24,919)	(811)	(920)	(93,767)	-	-	(120,417)	
Total	**883**	**336**	**(337)**	**565**	**0**	**0**	**1,447**	**1,923**
Off-balance sheet items								
Financial guarantees and underwriting commitments	(2,525)	(5,113)	(5,187)	(3,928)	-	(1,342)	(18,095)	
Undrawn loan commitments	(123,997)	-	-	-	-	-	(123,997)	
Undrawn overdraft/credit card commitments	(62,591)	-	-	-	-	-	(62,591)	
Total	**(189,113)**	**(5,113)**	**(5,187)**	**(3,928)**	**0**	**(1,342)**	**(204,683)**	
Net liquidity position	**(612,156)**	**(35,342)**	**107,122**	**170,336**	**1,110,750**	**22,205**	**762,915**	**246,099**

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74. Maturity analysis of financial assets and liabilities by currency

The following table shows a maturity analysis of the Group's financial instruments by currency of denomination as at 31 December 2019:

Non-derivative financial liabilities	0-1 month	1-3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total	Carrying amount
Total in foreign currencies	(96,567)	(5,865)	(43,226)	(191,682)	(18,360)	-	(355,700)	(347,566)
ISK	(440,209)	(179,715)	(29,879)	(122,475)	(87,897)	-	(860,175)	(809,757)
Total	**(536,776)**	**(185,580)**	**(73,105)**	**(314,157)**	**(106,257)**	**0**	**(1,215,875)**	**(1,157,323)**
Derivative financial liabilities								
Total in foreign currencies	(582)	173	(274)	(9)	-	-	(692)	(1,379)
ISK	(736)	(265)	73	(1,600)	(390)	-	(2,918)	(1,930)
Total	**(1,318)**	**(92)**	**(201)**	**(1,609)**	**(390)**	**0**	**(3,610)**	**(3,309)**
Non-derivative financial assets								
Total in foreign currencies	69,871	59,041	69,731	129,415	10,172	2,735	340,965	348,203
ISK	95,917	49,008	111,318	297,392	854,784	27,284	1,435,703	1,062,834
Total	**165,788**	**108,049**	**181,049**	**426,807**	**864,956**	**30,019**	**1,776,668**	**1,411,037**
Derivative financial assets								
Total in foreign currencies	1,232	777	(434)	1,039	-	-	2,614	2,192
ISK	(374)	(55)	403	61	-	-	35	502
Total	**858**	**722**	**(31)**	**1,100**	**0**	**0**	**2,649**	**2,694**
Off-balance sheet items								
Total in foreign currencies	(22,542)	(412)	(2,084)	(1,563)	(6,440)	-	(33,041)	
ISK	(138,076)	(313)	(2,137)	(4,005)	(4,739)	(1,166)	(150,436)	
Total	**(160,618)**	**(725)**	**(4,221)**	**(5,568)**	**(11,179)**	**(1,166)**	**(183,477)**	
Net liquidity position in foreign currencies	**(48,588)**	**53,714**	**23,713**	**(62,800)**	**(14,628)**	**2,735**	**(45,854)**	**1,450**
Net liquidity position in ISK	**(483,478)**	**(131,340)**	**79,778**	**169,373**	**761,758**	**26,118**	**422,209**	**251,649**
Net liquidity position	**(532,066)**	**(77,626)**	**103,491**	**106,573**	**747,130**	**28,853**	**376,355**	**253,099**

The following table shows a maturity analysis of the Group's financial instruments by currency of denomination as at 31 December 2018:

Non-derivative financial liabilities	0-1 month	1-3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total	Carrying amount
Total in foreign currencies	(92,638)	(6,264)	(15,415)	(192,613)	(24,614)	-	(331,544)	(316,808)
ISK	(519,638)	(133,807)	(52,898)	(65,228)	(99,776)	-	(871,347)	(749,618)
Total	**(612,276)**	**(140,071)**	**(68,313)**	**(257,841)**	**(124,390)**	**0**	**(1,202,891)**	**(1,066,426)**
Derivative financial liabilities								
Total in foreign currencies	2,361	1,277	(197)	1	-	-	3,442	(393)
ISK	(2,811)	(1,304)	725	(1,561)	(557)	-	(5,508)	(1,245)
Total	**(450)**	**(27)**	**528**	**(1,560)**	**(557)**	**0**	**(2,066)**	**(1,638)**
Non-derivative financial assets								
Total in foreign currencies	94,491	63,481	50,488	106,524	3,565	81	318,630	319,513
ISK	94,309	46,052	129,943	326,576	1,232,132	23,466	1,852,478	992,727
Total	**188,800**	**109,533**	**180,431**	**433,100**	**1,235,697**	**23,547**	**2,171,108**	**1,312,240**
Derivative financial assets								
Total in foreign currencies	(982)	(354)	(282)	494	-	-	(1,124)	1,552
ISK	1,865	690	(55)	71	-	-	2,571	371
Total	**883**	**336**	**(337)**	**565**	**0**	**0**	**1,447**	**1,923**
Off-balance sheet items								
Total in foreign currencies	(26,823)	(3,341)	(2,394)	(41)	-	-	(32,599)	
ISK	(162,290)	(1,772)	(2,793)	(3,887)	-	(1,342)	(172,084)	
Total	**(189,113)**	**(5,113)**	**(5,187)**	**(3,928)**	**0**	**(1,342)**	**(204,683)**	
Net liquidity position in foreign currencies	**(23,591)**	**54,799**	**32,200**	**(85,635)**	**(21,049)**	**81**	**(43,195)**	**3,864**
Net liquidity position in ISK	**(588,565)**	**(90,141)**	**74,922**	**255,971**	**1,131,799**	**22,124**	**806,110**	**242,235**
Net liquidity position	**(612,156)**	**(35,342)**	**107,122**	**170,336**	**1,110,750**	**22,205**	**762,915**	**246,099**

The amounts in the maturity analysis as at 31 December 2019 and 31 December 2018 are allocated to maturity buckets in respect of remaining contractual maturity (i.e. based on the timing of future cash flows according to contractual terms). Exceptions to this are loans and advances to customers and bonds issued by companies in moratorium or in the process of liquidation as disclosed in Note 73.

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75. Encumbered assets

The following tables show the Group’s total encumbered and unencumbered assets as at 31 December 2019 and 31 December 2018:

	Collateral pledged against			
As at 31 December 2019	**Covered bonds**	**Other***	**Un-encumbered**	**Total**
Cash and balances with Central Bank	2,152	9,956	57,716	69,824
Bonds and debt instruments	-	-	115,262	115,262
Equities and equity instruments	-	-	30,019	30,019
Derivative instruments	-	-	2,694	2,694
Loans and advances to financial institutions	-	1,039	46,890	47,929
Loans and advances to customers	177,933	-	962,251	1,140,184
Investments in equity-accounted associates	-	-	1,471	1,471
Property and equipment	-	-	6,743	6,743
Intangible assets	-	-	2,296	2,296
Deferred tax assets	-	-	20	20
Other assets	-	-	8,864	8,864
Assets classified as held for sale	-	-	1,022	1,022
Total	**180,085**	**10,995**	**1,235,248**	**1,426,328**

	Collateral pledged against			
As at 31 December 2018	**Covered bonds**	**Other***	**Un-encumbered**	**Total**
Cash and balances with Central Bank	3,835	12,741	54,278	70,854
Bonds and debt instruments	-	-	77,058	77,058
Equities and equity instruments	-	-	23,547	23,547
Derivative instruments	-	-	1,923	1,923
Loans and advances to financial institutions	-	805	70,580	71,385
Loans and advances to customers	132,864	-	931,668	1,064,532
Investments in equity-accounted associates	-	-	1,453	1,453
Property and equipment	-	-	5,548	5,548
Intangible assets	-	-	2,622	2,622
Deferred tax assets	-	-	134	134
Other assets	-	-	5,655	5,655
Assets classified as held for sale	-	-	1,330	1,330
Total	**136,699**	**13,546**	**1,175,796**	**1,326,041**

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

Market risk

76. Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market prices. Market risk arises from open positions in currency, equity and interest rate products, all of which are exposed to general and specific market movements and changing volatility levels in market rates and prices, for instance in interest rates, credit spreads, foreign exchange rates and equity prices. Other market risk is defined as equity price risk and inflation risk, each of which is disclosed in the following notes.

77. Market risk management

The Group separates its exposure to market risk into trading and banking book portfolios, managing each separately. Trading portfolios include positions arising from market-making, hedges for derivative sales and proprietary position-taking. Banking book portfolios include positions arising from the Group’s retail and commercial banking operations and proprietary position-taking as part of asset and liability management and funding transactions, managed by Treasury. Treasury is also responsible for daily liquidity management, creating exposure to market risk.

The Board of Directors is responsible for determining the Group's overall risk appetite, including for market risk. The CEO of the Bank appoints the Risk & Finance Committee, which is responsible for developing detailed market risk management policies and setting market risk limits. Treasury and the Market Making department within Markets are responsible for managing market-related positions under the supervision of Market Risk. The objective of market risk management is to identify, locate and monitor market risk exposures and analyse and report to appropriate parties.

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77. Market risk management (continued)

Market risks arising from trading and banking book activities are monitored and reported on a daily, weekly and monthly basis to the head of each business unit along with a comprehensive biannual risk report to the Board of Directors. The Group's market risk is thereby measured and monitored on a daily basis, and Market Risk monitors the limits set in the Group's risk appetite and submits these and other market risk measurements and concerns to the Risk & Finance Committee every other week. Several indicators are used, including daily profits and losses, delta positions and net positions across different attributes such as currency and issuer.

The Group uses risk exposure amounts (REA) and economic capital (EC) as a common denominator for measuring risk across different asset classes, including those assets subject to market risk. Risk exposure amounts are determined by applying specific risk weights to the Group’s assets, following capital requirements regulations.

The following table summarises the Group’s exposure to market risk as a percentage of risk exposure amount (REA) as at 31 December 2019 and 31 December 2018. The Group uses the standardized approach to calculate risk exposure amounts of derivatives for credit valuation adjustment (CVA) according to capital requirement regulations.

	2019	2018
Market risk factor	**% of REA**	**% of REA**
Equity price risk	0.4%	0.9%
Interest rate risk	0.4%	0.2%
CVA of derivatives	0.0%	0.0%
Foreign exchange risk	0.4%	0.6%
Total	**1.2%**	**1.8%**

78. Equity price risk

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

The Group’s equity trading portfolio is comprised of proprietary trading positions and exposures due to market making, including equity derivatives and hedging positions, in listed ISK equities. The Group’s banking book portfolio contains listed and unlisted equities as part of asset and liability management. Further details are disclosed in Note 20 and Notes 80-81.

79. Interest rate risk

Interest rate risk is the risk that the fair value or future cash flow of financial instruments will fluctuate due to changes in market interest rates.

Changes in interest rates for the Group's assets and liabilities, other than those in its trading portfolios, have an impact on its interest rate margin. This risk results primarily from duration mismatches between assets and liabilities. Interest rate risk is managed principally by monitoring interest rate gaps. Interest rate risk is managed centrally within the Group by the Treasury of the Bank, and is monitored by Market Risk.

The following tables summarise the Group's exposure to interest rate risk. The tables include interest-bearing financial assets and liabilities at their carrying amounts, while off-balance sheet amounts are the notional amounts of the derivative instruments, see Note 21. The amounts presented are categorised by the earlier of either the contractual repricing or the maturity date.

As at 31 December 2019	Up to 3 months	3-12 months	1-5 years	Over 5 years	Carrying amount
Financial assets					
Cash and balances with Central Bank	69,824	-	-	-	69,824
Bonds and debt instruments	52,477	36,344	15,450	10,991	115,262
Derivative instruments	2,694	-	-	-	2,694
Loans and advances to financial institutions	47,929	-	-	-	47,929
Loans and advances to customers	857,054	116,140	133,234	33,756	1,140,184
Other financial assets	7,819	-	-	-	7,819
Total	**1,037,797**	**152,484**	**148,684**	**44,747**	**1,383,712**
Financial liabilities					
Due to financial institutions and Central Bank	(48,062)	-	-	-	(48,062)
Deposits from customers	(699,961)	(5,092)	(2,760)	-	(707,813)
Derivative instruments and short positions	(3,309)	-	-	(2,081)	(5,390)
Borrowings	(56,438)	(24,643)	(236,930)	(55,157)	(373,168)
Other financial liabilities	(7,118)	-	-	-	(7,118)
Subordinated liabilities	-	-	(13,613)	(5,468)	(19,081)
Total	**(814,888)**	**(29,735)**	**(253,303)**	**(62,706)**	**(1,160,632)**
Net on-balance sheet position	222,909	122,749	(104,619)	(17,959)	223,080
Derivatives held for hedging	(85,357)	3,877	81,480	0	
Net off-balance sheet position	16,143	10,192	(24,335)	(2,000)	
Total interest repricing gap	**153,695**	**136,818**	**(47,474)**	**(19,959)**	

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79. Interest rate risk (continued)

As at 31 December 2018	Up to 3 months	3-12 months	1-5 years	Over 5 years	Carrying amount
Financial assets					
Cash and balances with Central Bank	70,854	-	-	-	70,854
Bonds and debt instruments	48,155	7,044	9,762	12,097	77,058
Derivative instruments	1,923	-	-	-	1,923
Loans and advances to financial institutions	71,385	-	-	-	71,385
Loans and advances to customers	853,058	68,257	96,428	46,789	1,064,532
Other financial assets	4,864	-	-	-	4,864
Total	**1,050,239**	**75,301**	**106,190**	**58,886**	**1,290,616**
Financial liabilities					
Due to financial institutions and Central Bank	(34,609)	-	-	-	(34,609)
Deposits from customers	(686,952)	(3,900)	(2,191)	-	(693,043)
Derivative instruments and short positions	(2,634)	-	(1,925)	(1,987)	(6,546)
Borrowings	(44,330)	(18,622)	(188,270)	(63,190)	(314,412)
Other financial liabilities	(6,114)	-	-	-	(6,114)
Subordinated liabilities	-	-	(13,340)	-	(13,340)
Total	**(774,639)**	**(22,522)**	**(205,726)**	**(65,177)**	**(1,068,064)**
Net on-balance sheet position	275,600	52,779	(99,536)	(6,291)	222,552
Derivatives held for hedging	(83,861)	0	83,861	0	
Net off-balance sheet position	16,957	56	(14,711)	(2,303)	
Total interest repricing gap	**208,696**	**52,835**	**(30,386)**	**(8,594)**	

80. Sensitivity analysis for trading portfolios

The management of market risk in the trading book is supplemented by monitoring sensitivity of the trading portfolios to various scenarios in equity prices and interest rates.

The following table shows the changes in the fair value for bonds a +/-100 basis point parallel shifts in all interest rate curves.

	2019		2018	
Currency	**Increase**	**Decrease**	**Increase**	**Decrease**
ISK, non-CPI indexed	79	(73)	110	(102)
ISK, CPI indexed	61	(57)	452	(396)
Total	**140**	**(130)**	**562**	**(498)**

The following table shows how the Group's profit (loss) before tax would have been affected by a change of +/-5% in the price of equities and equity instruments in the trading book held by the Group at year-end.

	2019		2018	
Currency	**Increase**	**Decrease**	**Increase**	**Decrease**
ISK	17	(17)	226	(226)
Other	-	-	1	(1)
Total	**17**	**(17)**	**227**	**(227)**

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase (decrease) in profit before tax would have affected retained earnings.

81. Sensitivity analysis for portfolios in the banking book

The management of interest rate risk in the Group's banking book is supplemented by monitoring the sensitivity of the fair value of financial assets and liabilities to various interest rate scenarios. The Group employs a monthly stress test of the interest rate risk in the Group's banking book by shifting the interest rate curves for every currency, and measuring the effect on economic value.

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81. Sensitivity analysis for portfolios in the banking book (continued)

The following table shows the changes in the fair value of financial assets and liabilities for a +/-100 basis point parallel shifts in all interest rate curves.

	2019		2018	
Currency	**Increase**	**Decrease**	**Increase**	**Decrease**
ISK, non-CPI indexed	205	(248)	(916)	962
ISK, CPI indexed	4,437	(4,510)	426	170
EUR	1,405	(1,479)	2,283	(2,413)
Other	200	(200)	29	(23)
Total	**6,247**	**(6,437)**	**1,822**	**(1,304)**

The following table shows how the Group's profit (loss) before tax would have been affected by a change of +/-5% in the price of equities which are classified into Level 1 or Level 2, as defined in Note 88.5 (f) and of +/-5% in the key unobservable inputs used in valuation of equities which are classified into Level 3, as defined in Note 88.5 (f), in the price of equities in the banking book at year-end.

	2019		2018	
Currency	**Increase**	**Decrease**	**Increase**	**Decrease**
ISK	808	(808)	920	(918)
Other	14	(14)	5	(5)
Total	**822**	**(822)**	**925**	**(923)**

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase (decrease) in profit before tax would have affected retained earnings.

82. CPI indexation risk (all portfolios)

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

CPI indexation risk is managed centrally within the Group by Treasury, and is monitored by Market Risk department within the Risk Management division. The following tables summarizes the Group's CPI imbalance, where CPI-linked financial assets and liabilities are calculated at their carrying amounts and categorised at maturity date, as at 31 December 2019 and 31 December 2018.

As at 31 December 2019	**Up to 3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Carrying amount**
Financial assets					
Bonds and debt instruments	-	1	5,531	8,760	14,292
Loans and advances to customers	4,956	11,451	69,661	315,875	401,943
Total	**4,956**	**11,452**	**75,192**	**324,635**	**416,235**
Financial liabilities					
Deposits from customers	(71,093)	(2,486)	(11,418)	(35,809)	(120,806)
Derivative instruments and short positions	-	-	-	(939)	(939)
Borrowings	-	-	(64,113)	(55,158)	(119,271)
Subordinated liabilities	-	-	-	(5,468)	(5,468)
Total	**(71,093)**	**(2,486)**	**(75,531)**	**(97,374)**	**(246,484)**
Total on-balance sheet position	**(66,137)**	**8,966**	**(339)**	**227,261**	**169,751**
Off-balance sheet position					
Interest rate swaps	-	-	(26,391)	(2,228)	(28,619)
Total return swaps	(11,923)	-	-	-	(11,923)
Total off-balance sheet position	**(11,923)**	**0**	**(26,391)**	**(2,228)**	**(40,542)**
Total CPI indexation balance	**(78,060)**	**8,966**	**(26,730)**	**225,033**	**129,209**

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82. CPI indexation risk (all portfolios) (continued)

As at 31 December 2018	Up to 3 months	3-12 months	1-5 years	Over 5 years	Carrying amount
Financial assets					
Bonds and debt instruments	115	5	136	12,530	12,786
Loans and advances to customers	5,058	11,782	64,356	307,871	389,067
Total	**5,173**	**11,787**	**64,492**	**320,401**	**401,853**
Financial liabilities					
Deposits from customers	(85,965)	(12,554)	(11,316)	(3,690)	(113,525)
Derivative instruments and short positions	-	-	(2,274)	(2,264)	(4,538)
Borrowings	(426)	(341)	(21,021)	(62,816)	(84,604)
Total	**(86,391)**	**(12,895)**	**(34,611)**	**(68,770)**	**(202,667)**
Total on-balance sheet position	**(81,218)**	**(1,108)**	**29,881**	**251,631**	**199,186**
Off-balance sheet position					
Interest rate swaps	(66)	-	(25,000)	(2,000)	(27,066)
Total return swaps	(823)	-	-	-	(823)
Total off-balance sheet position	**(889)**	**0**	**(25,000)**	**(2,000)**	**(27,889)**
Total CPI indexation balance	**(82,107)**	**(1,108)**	**4,881**	**249,631**	**171,297**

Management of the Group's CPI indexation risk is supplemented by monitoring the sensitivity of the Group's overall position in CPI-indexed financial assets and liabilities net on-balance sheet to various inflation/deflation scenarios. As an example, a 1% change in the CPI applied to the inflation risk exposures in existence at 31 December 2018, with no change in other variables, would have changed net interest income by ISK 1.292 million (31 December 2018: ISK 1.713 million). The Group's equity would have been affected by the same amount as the income statement, but net of income tax. This is because the increase/decrease in net interest income would have affected retained earnings. However, in a scenario of ongoing high (low) inflation, floating unindexed interest rates are likely to remain higher (lower) than would be the case in the reverse scenario, thus counterbalancing the positive (negative) income effects for the Group in the medium and longer term.

Currency risk

83. Currency risk (all portfolios)

The Group follows Central Bank Rules No. 784/2018, on Foreign Exchange Balances. The Rules stipulate that a foreign exchange balance (whether long or short) of a systemically important financial institution must always be within 10% of its capital base, in each currency and for all currencies combined, although the total foreign exchange balance should never exceed ISK 25,000 million. The Bank submits daily reports to the Central Bank on its foreign exchange balance and the Group submits monthly reports to the Central Bank on its foreign exchange balance.

The Group's combined net foreign exchange balance as at 31 December 2019 was +1.2% of the Group's capital base (31.12.2018: +2.3%).

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84. Concentration of currency risk

The following tables summarise the Group's exposure to currency risk as at year-end 2019 and 2018. The off-balance sheet amounts shown are the notional amounts of the Group's derivative instruments. Amounts presented under assets and liabilities include all spot deals. When managing currency risk the Group regards spot deals as non-derivative assets or liabilities.

As at 31 December 2019	EUR	GBP	USD	JPY	CHF	Other	Total
Assets							
Cash and balances with Central Bank	575	163	307	12	35	434	1,526
Bonds and debt instruments	27,213	4	52,261	-	-	6,882	86,360
Equities and equity instruments	2,210	-	77	-	-	263	2,550
Derivative instruments	1,395	24	763	-	-	10	2,192
Loans and advances to financial institutions	17,514	2,286	8,000	1,013	800	18,242	47,855
Loans and advances to customers	158,304	2,661	41,364	2,135	300	3,541	208,305
Other assets	1,387	-	-	-	-	36	1,423
Total	**208,598**	**5,138**	**102,772**	**3,160**	**1,135**	**29,408**	**350,211**
Liabilities							
Due to financial institutions and Central Bank	(1,661)	(47)	(148)	-	-	(393)	(2,249)
Deposits from customers	(43,391)	(4,511)	(43,163)	(823)	(861)	(8,754)	(101,503)
Derivative instruments and short positions	(1,017)	(18)	(323)	-	(2)	(141)	(1,501)
Borrowings	(152,699)	-	(18,336)	-	-	(57,980)	(229,015)
Other liabilities	(413)	(48)	(188)	(1)	(5)	(531)	(1,186)
Subordinated liabilities	(13,613)	-	-	-	-	-	(13,613)
Total	**(212,794)**	**(4,624)**	**(62,158)**	**(824)**	**(868)**	**(67,799)**	**(349,067)**
Net on-balance sheet position	(4,196)	514	40,614	2,336	267	(38,391)	**1,144**
Net off-balance sheet position	6,736	(26)	(40,280)	(2,357)	(409)	38,181	**1,845**
Net currency position	**2,540**	**488**	**334**	**(21)**	**(142)**	**(210)**	**2,989**

As at 31 December 2018	EUR	GBP	USD	JPY	CHF	Other	Total
Assets							
Cash and balances with Central Bank	666	180	318	15	40	436	1,655
Bonds and debt instruments	26,717	30	27,023	-	-	-	53,770
Equities and equity instruments	5	-	23	-	-	53	81
Derivative instruments	961	146	441	-	-	7	1,555
Loans and advances to financial institutions	39,127	2,951	13,771	343	374	14,602	71,168
Loans and advances to customers	139,993	2,585	40,790	3,273	1,224	3,677	191,542
Other assets	1,217	-	52	-	-	29	1,298
Total	**208,686**	**5,892**	**82,418**	**3,631**	**1,638**	**18,804**	**321,069**
Liabilities							
Due to financial institutions and Central Bank	(938)	(451)	(125)	-	-	(795)	(2,309)
Deposits from customers	(35,906)	(4,195)	(44,219)	(306)	(879)	(8,393)	(93,898)
Derivative instruments and short positions	(156)	(51)	(98)	-	(7)	(44)	(356)
Borrowings	(150,137)	-	(17,681)	-	-	(37,580)	(205,398)
Other liabilities	(422)	(79)	(700)	-	(1)	(740)	(1,942)
Subordinated liabilities	(13,340)	-	-	-	-	-	(13,340)
Total	**(200,899)**	**(4,776)**	**(62,823)**	**(306)**	**(887)**	**(47,552)**	**(317,243)**
Net on-balance sheet position	7,787	1,116	19,595	3,325	751	(28,748)	**3,826**
Net off-balance sheet position	(3,945)	(1,239)	(18,510)	(3,233)	(623)	29,144	**1,594**
Net currency position	**3,842**	**(123)**	**1,085**	**92**	**128**	**396**	**5,420**

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85. Sensitivity to currency risk

The following table shows how other net operating income would have been affected by a 5% depreciation/appreciation of the ISK against each foreign currency, with all other variables held constant. The sensitivity analysis is applied to the Group's overall position in foreign currency on-balance sheet as disclosed in Note 84.

	2019		2018	
Currency (ISK million)	**-5%**	**+5%**	**-5%**	**+5%**
EUR	127	(127)	192	(192)
GBP	24	(24)	(6)	6
USD	17	(17)	54	(54)
JPY	(1)	1	5	(5)
CHF	(7)	7	6	(6)
Other	(11)	11	20	(20)
Total	**149**	**(149)**	**271**	**(271)**

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase / (decrease) in other net operating income would have affected retained earnings.

86. Foreign exchange rates used

The following foreign exchange rates were used by the Group for the accounting year presented in these Financial Statements.

	As at 31 December 2019	**As at 31 December 2018**	**% change**	**Average for 1.1-31.12 2019**	**Average for 1.1-31.12 2018**
EUR/ISK	135.80	133.20	2.0%	136.68	126.85
GBP/ISK	160.28	148.24	8.1%	156.09	143.16
USD/ISK	120.98	116.54	3.8%	122.00	107.70
JPY/ISK	1.1132	1.0623	4.8%	1.1190	0.9745
CHF/ISK	124.98	118.25	5.7%	122.94	110.21
CAD/ISK	93.27	85.32	9.3%	91.99	83.03
DKK/ISK	18.172	17.859	1.8%	18.308	17.021
NOK/ISK	13.764	13.465	2.2%	13.879	13.161
SEK/ISK	12.923	13.137	(1.6%)	12.946	12.371

Operational risk

87. Operational risk

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

Whereas the Managing Director of each division is responsible for that division's operational risk, the daily management of operational risk is overseen by the general managers of each department. The Group establishes, maintains and coordinates its operational risk management framework. This framework complies with the Basel Committee's 2011 publication, "Principles for the Sound Management of Operational Risk". The Group ensures that operational risk management stays consistent throughout the Group by upholding a system of prevention and control that entails detailed procedures, permanent supervision and insurance policies, together with active monitoring by the Internal Audit function. By managing operational risk in this manner, the Group intends to ensure that all of the Group's business units are kept aware of any operational risks, that a robust monitoring system remains in place and that controls are implemented to minimize risk in an efficient and effective manner.

Accounting policies

88. Significant accounting policies

The Consolidated Financial Statements have been prepared using uniform accounting policies for like transactions and other events in similar circumstances. Except for changes resulting from the initial adoption of IFRS 16 *Leases* see Note 3, the Group has consistently applied the following accounting policies to all periods presented in these Consolidated Financial Statements.

The principal accounting polices used in preparing these Consolidated Financial Statements are set out in Notes 88.1 to 88.42.

88.1. Consolidation and non-controlling interests

(a) Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity if it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The Group is considered to have power over an entity when it has existing rights that give it the current ability to direct the relevant activities. For the Group to have power over an entity, it must have the practical ability to exercise those rights.

Where voting rights are not relevant in deciding whether the Group has power over an investee, the assessment of control is based on all facts and circumstances. This includes circumstances in which protective rights held become substantive and lead to the Group having power over an investee.

Subsidiaries are fully consolidated from the date on which control is obtained, and are de-consolidated from the date on which control ceases.

The acquisition method is used to account for business combinations by the Group when control is transferred to the Group. The consideration transferred in the acquisition is generally measured at fair value, as are the identifiable net assets acquired. Any goodwill that arises is tested annually for impairment. Any gain on a bargain purchase is recognised in profit or loss immediately. Transaction costs are expensed as incurred, except if they are related to the issue of debt or equity securities.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay a contingent consideration that meets the definition of a financial instrument is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, other contingent consideration is remeasured at fair value at each reporting date and subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

Intercompany transactions, balances, and unrealised gains on transactions between Group entities are eliminated in the Consolidated Financial Statements. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred.

(b) Non-controlling interests

Non-controlling interests are measured at their proportionate share of the acquiree's identifiable net assets at the date of acquisition. Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

(c) Loss of control

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary and any related non-controlling interests and other components of equity. Any resulting gain or loss is recognised in the income statement. Any interest retained in the former subsidiary is measured at fair value when control is lost.

88.2. Structured entities

Structured entities are entities that have been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements.

The Group acts as fund manager or investment advisor to a number of investment funds operated by a subsidiary of the Bank. The purpose of these investment funds is to generate fees from managing assets on behalf of third-party investors by providing investment strategies. These investment funds are financed through the issue of units to investors. The Group has no contractual obligation to provide financial support to these structured entities.

From time to time, the Group makes seed capital investments in certain fund products in order to establish track records for new products, to test new investment strategies or to launch new products at a viable minimum size.

When assessing whether to consolidate investment funds, the Group reviews all facts and circumstances to determine whether the Group, as fund manager, is acting as agent or principal. The Group is deemed to be a principal, and hence controls and consolidates the funds, when it acts as fund manager and cannot be removed as such without cause, has variable returns through significant unit holdings and/or a guarantee, is able to influence the returns of the funds by exercising its power and the Group's aggregate interest is in each case not less than 15%.

For further disclosure in respect of unconsolidated investment funds in which the Group acts as an agent see Note 42 Unconsolidated structured entities.

88. Significant accounting policies (continued)

88.3. Associates

Associates are entities in which the Group has significant influence, but not control, over financial and operating policies. Significant influence is presumed to exist when the Group holds, directly or indirectly, between 20% and 50% of the voting power of another entity. The Group accounts for investments in associates either using the equity method or as financial assets designated at fair value through profit or loss, as described further in this note.

Equity-accounted associates

Investments in equity-accounted associates are accounted for using the equity method from the date on which significant influence is obtained and are initially recognised at cost. Goodwill relating to an investment in an associate is included in the carrying amount of the investment. Any excess of the Group's share of net fair value of the associate's identifiable assets and liabilities over the cost of the investment is included as income in the determination of the Group's share of the associate's profit or loss in the period which the investment is acquired. Investments in associates which are accounted for by the Group using the equity method are presented in the consolidated statement of financial position in the line "Investments in equity-accounted associates".

Because goodwill included in the carrying amount of an investment in an associate is not recognised separately, it is not separately tested for impairment according to the requirements for goodwill impairment testing in IAS 36, *Impairment of Assets*. Instead, the entire carrying amount of the investment is tested for impairment under IAS 36 by comparing its recoverable amount with its carrying amount, whenever application of the requirements in IFRS 9, *Financial Instruments*, indicates the investment may be impaired.

The Group's share of its equity-accounted associates' post-acquisition profits or losses is recognised in the income statement, and its share of movements in their reserves is recognised in the Group's equity reserves. Cumulative post-acquisition movements are adjusted against the carrying amount of the investment in the associates. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. The accounting policies of associates have been changed where this was necessary to ensure consistency with the accounting policies adopted by the Group.

Associates designated at fair value through profit or loss

The Group designates certain investments in associates upon initial recognition at fair value through profit or loss and they are accounted for in accordance with IFRS 9, *Financial Instruments*. The Group measures such investments at fair value, with changes in fair value recognised in the income statement in the relevant period as net gain (loss) on financial assets designated at fair value through profit and loss in the line item "Net gain (loss) on financial assets and financial liabilities at FVPL".

88.4. Foreign currency translation

Transactions in a currency other than the functional currency -foreign currency- are translated initially into the functional currency at the spot exchange rate prevailing on the transaction date. Monetary assets and liabilities denominated in foreign currencies are measured at amortised cost or fair value, as applicable, in their respective foreign currencies at the reporting period and are converted into the functional currency at the closing spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the reporting period, adjusted for effective interest and payments during the reporting period, and the amortised cost in foreign currency translated at the closing exchange rate at the end of the period. All foreign currency differences arising on currency translation are recognised in the line item „Net foreign exchange gain(loss)" in the income statement.

88.5. Financial assets and liabilities

(a) Recognition and initial measurement

The Group initially recognises loans and advances, deposits and borrowings on the date at which they are originated. All other financial assets and liabilities are initially recognised on the date at which the Group becomes a party to contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on the date at which the Group committed itself to purchasing or selling the asset.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss (FVTPL), transaction costs that are directly attributable to its acquisition or issue.

(b) Classification

On initial recognition, a financial asset is classified as measured at: amortised cost, fair value through other comprehensive income (FVOCI) or fair value through profit or loss (FVTPL).

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and,
- the contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

88. Significant accounting policies (continued)

88.5. Financial assets and liabilities (continued)

(b) Classification (continued)

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and,
- the contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

The Group makes an assessment of the objective of the business model in which a financial asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- Management's stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets.
- The primary risks that affect the performance of the business model and its strategy for managing those risks.
- The methods by which the performance of assets in a portfolio is evaluated and reported to management.
- The frequency, volume and timing of sales of financial assets in prior periods, the reasons for such sales and expectations about future sales activities. Sales in themselves do not determine the business model and are not considered in isolation. Instead, sales provide evidence about how cash flows are realised.

Transfers of financial assets to third parties in transactions that do not qualify for derecognition are not considered sales for this purpose, consistent with the Group's continuing recognition of the assets.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell.

Cash flow characteristics assessment

The SPPI test is used to determine whether loans and advances to financial institutions and to customers are measured at amortised cost or at FVTPL.

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Group considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making this assessment, the Group considers:

- Contingent events that would change the amount or timing of cash flows,
- leverage features,
- terms that may adjust the contractual coupon rate, including variable-rate features,
- prepayment and extension features; and,
- terms that limit the Group's claim to cash flows from specified assets (e.g. non-recourse features).

(c) Derecognition

The Group derecognises a financial asset when the contractual rights to cash flows from the asset expire, or when the Group transfers the rights to receive contractual cash flows relating to the financial asset in a transaction which substantially transfers all the risks and rewards of ownership of the asset or in which the Group neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets created or retained by the Group is recognised as a separate asset or liability.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

The Group enters into transactions whereby it transfers assets recognised in the Statement of Financial Position, but retains either all or substantially all of the risks and rewards of the transferred assets, or a portion of them. In cases where all or substantially all of the risks and rewards are retained, transferred assets are not derecognised. Asset transfers whereby all or substantially all risks and rewards are retained include, for example, securities lending and repurchase transactions.

88. Significant accounting policies (continued)

88.5. Financial assets and liabilities (continued)

(c) Derecognition (continued)

When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to sale and repurchase transactions, because the Group retains all or substantially all of the risks and rewards of ownership of such assets.

In transactions in which the Group neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

In certain transactions, the Group retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognised if it meets the derecognition criteria. An asset or liability is recognised for the servicing contract if the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or when they expire.

d) Modification of financial assets and financial liabilities

Financial assets

If the terms of a financial asset are modified, the Group evaluates whether the cash flows of the modified asset are substantially different.

If the cash flows are substantially different, the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised see note 88.5 (g) and a new financial asset is recognised at fair value plus any eligible transaction costs. Any fees received as part of the modification are accounted for as follows:

- Fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; and,
- other fees are included in profit or loss as part of the gain or loss on derecognition.

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms. If the Group plans to modify a financial asset in a way that would result in forgiveness of cash flows, it first considers whether a portion of the asset should be written off before the modification takes place see note 88.5 (g) write-off. This approach impacts the result of the quantitative evaluation and means that the de-recognition criteria are not usually met in such cases.

If the modification of a financial asset measured at amortised cost or FVOCI does not result in derecognition of the financial asset, the Group first recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognises the resulting adjustment as a modification gain or loss in profit or loss. For floating-rate financial assets, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of modification. Any costs or fees incurred and fees received as part of the modification adjust the gross carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset.

If such a modification is carried out because of financial difficulties of the borrower see note 88.5 (g), then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income calculated using the effective interest rate method.

Financial liabilities

The Group derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as de-recognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. For floating-rate financial liabilities, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

(e) Offsetting

Financial assets and liabilities are offset and the net amount presented in the Statement of Financial Position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and simultaneously settle the liability.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

88. Significant accounting policies (continued)

88.5. Financial assets and liabilities (continued)

(f) Fair value measurement

Fair value is the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between independent market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Group has access at that date.

The fair value of a liability reflects its non-performance risk. The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Group measures the fair value of an instrument using quoted prices in an active market for that instrument, if available. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions at an arm's-length basis. Where available, the relevant market's closing price determines the fair value of financial assets held for trading and of assets designated at fair value through profit or loss; this will generally be the last trading price. If an asset or a liability measured at fair value has a bid price and an ask price, then the Group measures assets and long positions at a bid price and liabilities and short positions at an ask price.

If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. Valuation techniques include using 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, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Group, incorporates every factor that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank has a valuation committee which estimates fair value by applying models and incorporating observable market information and professional judgement. The Group calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available, observable market data.

Should the transaction price differ from the fair value of other observable, current market transactions in the same instrument or be based on a valuation technique whose variables include only data from observable markets, the Group immediately recognises the difference between the transaction price and fair value (a day 1 profit or loss). In cases where fair value is determined using data which is not observable, the difference between the transaction price and the model value is recognised in the income statement depending on the individual circumstances of the transaction but no later than when the inputs become observable, or when the instrument is derecognised.

The fair value of financial assets and liabilities is determined based on different methods and assumptions depending on what financial asset or liability is being valued. For all financial assets and liabilities the foreign currency exchange rates used are from observable markets both for spot and forward contracts and futures in the major currencies.

Fair value hierarchy

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

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

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

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

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

(g) Impairment of financial assets

Impairment process

The Group recognises loss allowances for expected credit loss (ECL) on the following financial instruments that are not measured at FVTPL:

- Cash and balances with Central Bank
- Bonds and debt instruments
- Loans and advances to financial institutions
- Loans and advances to customers

Off-balance sheet credit exposures:

- Financial guarantees and underwriting commitments
- Undrawn loan commitments
- Undrawn overdraft/credit card facilities

88. Significant accounting policies (continued)

88.5. Financial assets and liabilities (continued)

(g) Impairment of financial assets (continued)

Impairment process (continued)

When measuring ECL, the Group uses a forward-looking model in compliance with IFRS 9. This requires considerable judgement over how changes in economic factors affect ECL. ECL reflects the present value of cash shortfalls due to possible default events either over the following twelve months or over the expected lifetime of a financial instrument, depending on credit deterioration from inception.

Credit Risk Department is responsible for assessing impairment on loans and receivables and a Valuation Team, comprised of the CEO, the managing directors of Finance, Risk Management, Corporate Banking and Personal Banking, reviews and approves the assessment.

In general, all impairment charges are loan-specific based on the aforementioned ECL models. If needed, the Valuation Team can assess and issue additional general impairment charges.

The impairment process for each reporting period is as follows:

1. The Economic Research Department provides scenarios with forecasts on relevant economic variables and presents them to the Valuation Team.
2. The Valuation Team approves the scenarios and their respective weights for the reporting date.
3. Loans are classified for measurement by amortised cost (impairment) or the fair value approach.
4. Parameters for staging and ECL calculations are estimated.
5. Results from manual staging and ECL calculations for individually significant loans are applied.
6. Staging and ECL calculations are carried out for all loans that are subject to impairment.
7. The Valuation Team receives reports from the Risk Management department on the impairment results. The reports are reviewed by the Team and valuations are determined.
8. Results of staging and impairment are presented in the Group's annual and interim reports.

ECL calculation

IFRS 9 requires the calculation of an ECL that is probability-weighted and reflects an unbiased, probability-weighted outcome. The probability-weighted outcome considers multiple forward looking scenarios based on reasonable and available information. In general, the calculation of ECL is based on the present value of the multiplication of the following parameters: probability of default (PD), loss given default (LGD) and exposure at default (EAD).

Under IFRS 9, credit loss allowance on all loans is measured on each reporting date according to a three-Stage expected credit loss model. Allowance is calculated as either the 12-month expected credit loss or the lifetime ECL.

- Stage 1 – No significant increase in credit risk. Loans whose credit risk has not increased significantly shall be Stage 1 and the loss allowance measured as the 12-month expected credit losses.
- Stage 2 – Significant increase in credit risk. Loans whose credit risk has increased significantly since initial recognition but are not credit-impaired shall be Stage 2 and the loss allowance measured as the lifetime ECL.
- Stage 3 – Credit-impaired. Loans where the obligor is in default or otherwise impaired shall be Stage 3 and the loss allowance measured as the lifetime ECL.

Movements between Stage 1 and Stage 2 are based on whether an instrument's credit risk as measured at the reporting date has increased significantly relative to the credit risk measured at initial recognition. For the purpose of this assessment, credit risk is based on an instrument's lifetime PD, not the loss amounts.

Credit-impaired loans

A financial asset is credit-impaired if one or both of the following events have occurred:

- A loan that is more than 90 days past due is considered to be in default and therefore credit-impaired.
- It is considered likely that an obligor cannot fully fulfil their obligations unless the Bank resorts to enforcement activities, such as the collection of collateral.

The following events are used as indicators of default for a financial asset. Events automatically leading to default are marked with an asterisk.

- Bankruptcy*
- Restructuring*
- Sale of an obligation to a third party
- Impairment: The bank classifies the asset as Stage 3
- Legal collection*

Other factors that may indicate default are concessions to a customer because of financial difficulties and notices in financial statements on the operational viability of the customer.

Significant increase in credit risk

When determining whether the credit risk on a financial instrument has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost and effort, including both quantitative and qualitative information and analysis based on the Group's historical experience, expert credit assessment and forward-looking information.

The Group primarily identifies whether a significant increase in credit risk has occurred for an exposure by comparing:

- The remaining lifetime PD as at the reporting date; with
- the remaining lifetime PD as at the reporting date that was estimated at initial recognition.

88. Significant accounting policies (continued)

88.5. Financial assets and liabilities (continued)

(g) Impairment of financial assets (continued)

Significant increase in credit risk (continued)

The framework aligns with the Group's internal credit risk management process, and includes a backstop based on delinquencies so that a significant increase in credit risk occurs no later than when contractual payments are more than 30 days past due. If an asset's credit rating grade at the reporting date does not comply with benchmarks set by the Group's risk appetite that also constitutes a significant increase in credit risk. The Group also applies a low-risk criterion, which states that as long as the rating grade of an asset qualifies as investment grade, the asset will be categorized as Stage 1.

The estimation of whether credit risk has increased significantly for individually significant loans is carried out manually. Loans are initially assessed based on quantitative criteria and based on that assessment, staging is manually assessed using both quantitative and qualitative information.

Presentation of allowance

Loss allowances for ECL are presented in the statement of financial position as follows:

- Financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets.
- Loan commitments, overdrafts and financial guarantee contracts: as allowance for impairment or provision classified as liabilities.
- Where a Financial instrument includes both a drawn and an undrawn component: the Group presents a combined loss Allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision and classified with other liabilities.

Restructured financial assets

In regard to financial restructuring of customers, the Group has put remedies in place for those experiencing financial difficulties and also presented procedures for financial restructuring. These restructuring approaches include extended and modified repayment arrangements and approved external management plans.

The general rule is that when loan restructuring is significant enough to qualify for derecognition, a new loan is created and staging and impairment is carried out as if it was a new loan. The previous loan is derecognized.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due.

Provision used to cover write-offs is shown as the provision for the written-off asset as at the start of the reporting period. The provision used to cover write-offs cannot exceed the written-off amount.

Recoveries of amounts previously written off are included in 'Net valuation adjustments and impairment ' in the statement of profit or loss.

Renegotiated loans

Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and an agreement of new loan terms. Loans which are impaired and whose terms are renegotiated are not considered to be new loans. Once the terms have been renegotiated these loans are no longer considered past due and any subsequent impairment is measured using the original effective interest rate as calculated before the modification of terms. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. These loans continue to be subject to individual or collective impairment assessment. Loans which are not individually impaired and whose terms are renegotiated are accounted for as new loans. Accordingly, the original loans are derecognised and the renegotiated loans are recognised as new loans.

88.6. Cash and balances with Central Bank

Cash and cash equivalents include notes and coins on hand, and balances held with central banks. The carrying amount of balances with the Central Bank of Iceland is a reasonable approximation of their fair value. Cash and cash equivalents are carried at amortised cost in the statement of financial position. The Group measures 12-month ECL for cash and cash equivalents classified at amortised cost that are determined to have low credit risk at the reporting date.

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 rules came into effect for the reserve maintenance period starting 21 June 2018. The average balance of these accounts for each reserve term must be equivalent at least to the mandatory reserve deposit requirement which amounted to ISK 15,603 million for December 2019 (December 2018: ISK 14,310 million).

The Bank holds an additional amount as a mandatory reserve with the Central Bank in compliance with Article 8 of Act No. 37/2016, on the Treatment of Króna-Denominated Assets Subject to Special Restrictions. This reserve is equivalent to at least the amount of the total balance of deposits subject to special restrictions for investment held with the Group and consists of certificates of deposit issued by the Central Bank.

88. Significant accounting policies (continued)

88.7. Bonds and debt instruments

Bonds and debt instruments are either measured at amortised cost or at fair value through profit or loss.

Bonds and debt instruments classified as financial assets at fair value through profit or loss (FVTPL) are recognised at fair value both initially and subsequent to initial recognition. These are either designated or mandatorily measured at FVTPL - fair value option. Transaction costs are recognised immediately as fees in the income statement. Gains and losses arising from changes in fair value are recognised directly in the income statement, either as net gain (loss) on financial assets and liabilities held for trading or net gain (loss) on financial assets designated at fair value in the line item “Net gain (loss) on financial assets and financial liabilities”. Foreign exchange gains and losses are included in the line item “Net foreign exchange (loss) gain”.

Bonds and debt instruments designated at FVTPL must have a reliably measurable fair value and the designation must eliminate or significantly reduce a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities, or recognising related gains and losses on a different basis (sometimes referred to as "an accounting mismatch"). This includes, *inter alia*, bonds held for trading purposes.

Bonds and debt instruments mandatorily measured at FVTPL are managed on a fair value basis but not held for trading or their cash flows do not represent solely payments of principal and interest.

Bonds and debt instruments classified at amortised cost are initially measured at fair value plus directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method. Accrued interest is included in the carrying amount of the bonds and it is recognised in the line item "Interest income" in the income statement. Bonds and debt instruments within a held-to collect business model under which their contractual cash flows are solely payment of principal and interest are measured at amortised cost. The Group measures 12-month ECL allowances for bonds and debt instrument classified at amortised cost that are determined to have low credit risk at the reporting date.

88.8. Equities and equity instruments

Equities and equity instruments classified as financial assets at fair value through profit or loss are recognised at fair value both initially and subsequent to initial recognition.

Equities and equity instruments designated at FVTPL must have a reliably measurable fair value and the designation must eliminate or significantly reduce a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities, or recognising related gains and losses on a different basis (sometimes referred to as "an accounting mismatch"). This includes, *inter alia*, equities held for trading purposes.

Equities and equity instruments mandatorily measured at FVTPL are managed on a fair value basis but not held for trading.

Equities and equity instruments classified as financial assets at FVTPL are recognised at fair value both initially and subsequent to initial recognition. Transaction costs are recognised immediately as fees in the income statement. Gains and losses arising from changes in fair value are recognised directly in the income statement, either as net gain (loss) on financial assets and liabilities held for trading or net gain (loss) on financial assets designated at fair value in the line item “Net gain (loss) on financial assets and financial liabilities”. Foreign exchange gains and losses are included in the line item “Net foreign exchange (loss) gain”.

Quoted prices are generally readily available for equities listed on the world’s stock exchanges and for major indices on such shares. In lieu of such information, fair value is estimated based on market prices and earnings multiples from similar securities, recent transactions or by using discounted cash flow methods.

88.9. Derivative instruments

Derivatives are initially recognised in the statement of financial position at fair value, with transaction costs recognised in the income statement. The fair value of derivative instruments is determined using valuation methods whose most significant input is volatility, which is obtained from broker quotations, pricing services or derived from option prices. Subsequently, derivatives continue to be carried at fair value, with all fair value changes recognised in the income statement as net gain on financial assets and liabilities held for trading in the line item “Net gain (loss) on financial assets and financial liabilities”, except for fair value changes of derivative currency forwards and net foreign exchange differences arising from OTC currency options, which are included in the line item “Net foreign exchange (loss) gain” in the income statement. In the statement of financial position, derivatives with positive fair values are recognised as assets and derivatives with negative fair values as liabilities.

88.10. Embedded derivatives

Derivatives may be embedded in another contractual arrangement (a host contract). An embedded derivative is a component of a combined (hybrid) financial instrument that also includes a non-derivative host contract. The Group accounts for an embedded derivative separately from the host contract when:

- The host contract is not an asset in the scope of IFRS 9;
- the host contract is not itself carried at FVTPL;
- the terms of the embedded derivative would meet the definition of a derivative if they were contained in a separate contract; and
- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract.

88. Significant accounting policies (continued)

88.10. Embedded derivatives (continued)

Separated embedded derivatives are measured at fair value, with all changes in fair value recognised in profit or loss unless they form part of a qualifying cash flow or net investment hedging relationship. Separated embedded derivatives are presented in the statement of financial position together with the host contract.

Pursuant to IFRS 9, a derivative embedded in a host contract where the host is a financial asset is not separated from the host contract. Instead, the hybrid financial instrument as a whole is assessed whenever the contractual cash flows are solely payments of principal and interest.

88.11. Loans and advances

'Loans and advances' captions in the statement of financial position include:

- Loans and advances measured at amortised cost; they are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method,
- loans and advances mandatorily measured at FVTPL or designated as at FVTPL; these are measured at fair value with changes recognised immediately in profit or loss; and,
- finance lease receivables.

When the Group purchases a financial asset and simultaneously enters into an agreement to resell the asset (or a substantially similar asset) at a fixed price on a future date (reverse repo or stock borrowing), the arrangement is accounted for as a loan or advance, and the underlying asset is not recognised in the Group's financial statements.

88.12. Property and equipment

All property and equipment is recognised at cost, less accumulated depreciation and any accumulated impairment losses. The cost includes expenditures directly attributable to acquiring these assets.

Subsequent costs are included in an asset's carrying amount only if it is probable that future economic benefits associated with the item will flow to the Group and if these costs can be reliably measured. All other repairs and maintenance are charged to the income statement of the financial period in which their costs are incurred.

Depreciation of any property and equipment is calculated using the straight-line method. This method is applied to the depreciable amount of the assets, which is their cost less their residual value over their estimated useful lives, as follows:

Buildings	25-50 years
Computer hardware	3 years
Other equipment and motor vehicles	3-10 years

The assets' residual values and useful lives are reviewed annually and adjusted where appropriate.

Gains and losses on disposals are determined by comparing the sale price of an asset with its carrying amount on the date of sale. Gains and losses are included in the item "Other income and expenses" in the income statement.

88.13. Intangible assets

Computer software

Computer software is capitalised on the basis of cost to acquire or develop and bring into service. Computer software recognised as an intangible asset is amortised over its useful life, which is estimated to be 3 - 5 years.

The costs associated with maintaining computer software are recorded as expenses at the time they are incurred.

Goodwill

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

88. Significant accounting policies (continued)

88.14. Impairment of non-financial assets

Assets with an indefinite useful life are not subject to amortisation but are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is either an asset's fair value less selling costs or its value in use, whichever is higher. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). With the exception of goodwill, non-financial assets are reviewed at each reporting date for any possible reversal of impairment.

88.15. Income tax

(a) Income tax

Income tax is recognised based on the domestic corporate income tax rates and tax laws that have been enacted at the reporting date. Income tax recognised in these Consolidated Financial Statements comprises current and deferred tax.

Income tax is recognised based on the tax rates and tax laws enacted by the end of the year, according to which the domestic corporate income tax rate was 20.0% (2018: 20.0%). An additional special income tax on financial institutions is recognised at a rate of 6% on an income tax base exceeding ISK 1,000 million in accordance with Act No. 165/2011, on Financial Activity Tax.

(b) Current tax

Current tax comprises the expected tax payable on the taxable income for the current year and, if applicable, adjustments to the tax payable or receivable in respect of previous years. Current tax is measured based on the domestic corporate income tax rates and tax laws that have been enacted or substantively enacted at the reporting date.

(c) Deferred tax

Deferred tax assets are recognised when it is probable that future taxable profit will be available against which deductible temporary differences can be utilised.

Deferred income tax is recognised in full as a liability, based on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Consolidated Financial Statements. However, deferred income tax is not recognised if it arises from the initial recognition of an asset or liability in a transaction other than a business combination, which at the time of the transaction affects neither the Group's accounting nor its taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

d) Joint taxation

The Bank is taxed jointly with its subsidiaries Landsbréf hf., Eignarhaldsfélag Landsbankans ehf., Blámi - fjárfestingafélag ehf., Hömlur ehf. and Hömlur fyrirtæki ehf.

88.16. Tax on liabilities of financial institutions

On 31 December 2013 the Parliament of Iceland passed an amendment to Act No. 155/2010, on Special Tax on Financial Institutions, according to which financial institutions must pay annually a tax calculated as 0.376% (2018: 0.376%) of the carrying amount of total liabilities at year-end, excluding tax liabilities, in excess of ISK 50,000 million as determined for tax purposes. The special income tax on financial institutions is a non-deductible expense.

88.17. Assets and liabilities classified as held for sale

The Group classifies non-current assets (or groups of assets together with related liabilities) as held for sale when their carrying amount will be recovered principally through a sale transaction. These are usually acquired by foreclosure on collateral securing loans and advances, including assets and liabilities of subsidiaries over which the Group obtains control through foreclosure on collateral and/or financial restructuring.

A non-current asset (or group of assets together with related liabilities) is considered to be recovered principally through a sale transaction when the asset's sale is highly probable and it is available for immediate sale in its present condition, subject to ordinary and customary terms on the sale of such assets. Management must be committed to the sale and must actively market the asset for sale at a price that is reasonable in relation to its current fair value. A further condition is that the sale is expected to qualify for recognition as completed within one year from the date of classification.

Assets and disposal groups classified as held for sale are measured at the lower of their carrying amount and their fair value less costs to sell. Additional net assets that become part of a disposal group, for example due to profits generated by the disposal group, increase the carrying amount of the disposal group but not in excess of the fair value less costs to sell of the disposal group as determined at each reporting date.

In the case of single assets classified by the Group as held for sale, the Group determines their fair value less costs to sell by reference to the current market price at each reporting date. In the case of subsidiaries classified as held for sale, the Group determines the fair value of disposal groups based on discounted cash flow methodologies. Costs to sell are deemed to be only the costs which are directly attributable to the disposal of the disposal groups, excluding finance costs and income tax expense.

88. Significant accounting policies (continued)

88.18. Deposits

Deposits from customers and financial institutions are the primary source of funding for the Group. The deposits consist of demand deposits and term deposits. Deposits are initially measured at fair value plus any directly attributable transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. The fair value of a financial liability with a demand feature, such as demand deposits, is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid.

88.19. Secured borrowings

Each covered bond series of the secured borrowings is issued under the Bank's ISK 200,000 million Covered Bond Programme. These covered bonds are issued under a licence from the Icelandic FME and with reference to Act No. 11/2008 and FME Rules No. 528/2008. All covered bond series are listed and traded on NASDAQ Iceland.

The covered bonds are initially measured at fair value plus directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method. Accrued interest and accrued CPI-indexation for incexed bonds is included in the carrying amount of the bonds and is recognised in the line "Interest expense" in the income statement. Foreign exchange gains and losses are included in the line "Net foreign exchange (loss) gain".

88.20. Unsecured borrowings

The unsecured borrowings consist of senior bonds denominated in foreign currencies and marketable commercial papers denominated in ISK. The bonds are issued by the Bank under its EUR 2.000 million Euro Medium Term Note (EMTN) Programme and are listed and traded on the Irish Stock Exchange. The commercial papers on the other hand are issued under the Bank's ISK 50.000 million Debt Issuance Programme and listed and traded on NASDAQ Iceland.

The unsecured bonds and commercial papers are initially measured at fair value less directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method. Accrued interest is included in the carrying amount of the bonds and is recognised in the line "Interest expense" in the income statement.

All the outstanding unsecured non-indexed commercial papers issued by the Bank have a maturity of less than one year.

88.21. Hedge accounting

IFRS 9 incorporates new hedge accounting rules intended to align hedge accounting with risk management practices. IFRS 9 includes an accounting choice to defer the adoption of IFRS 9 hedge accounting and to continue with IAS 39 hedge accounting. The Group has elected to continue to apply IAS 39. The Group will nevertheless provide the expanded disclosures on hedge accounting introduced by the amendments IFRS 7 Financial Instruments.

Derivatives held for risk management purposes include all derivative assets and liabilities that are not classified as trading assets or liabilities. Derivatives held for risk management purposes are measured at fair value in the statement of financial position.

The Group uses interest rate swaps to hedge its exposure to changes in the fair values of some of its notes, issued under the Bank's Euro Medium Term Note (EMTN) programme. Such interest rate swaps are matched to specific issuances of the EMTN fixed-rate notes. The change in fair value of interest rate swaps together with change in the fair value of bonds attributable to interest rate risk is recognised immediately as net gain (loss) on fair value hedges in "Net gain (loss) on financial assets and financial liabilities at FVTPL" in the income statement. Accrued interest on both bonds and swaps is included in the line item "Interest expense".

The Group uses other derivatives, not designated in a qualifying hedge relationship, to manage its exposure to foreign currency, interest rate, equity market and credit risk. The financial instruments used include, but are not limited to, interest rate swaps, cross-currency swaps, forward contracts, futures, options, credit swaps and equity swaps.

On initial designation of the hedges, the Group formally documents the relationship between the hedging instruments and hedged items, including the risk management objective and strategy in undertaking the hedge, together with the method that will be used to assess the effectiveness of the hedging relationships. The Group makes an assessment, both at the inception of the hedge relationships and on an on-going basis, of whether the hedging instruments are expected to be highly effective in offsetting the changes in the fair value of the hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within the range of 80–125%.

If the hedging derivative expires or is sold, terminated or exercised, or the hedge no longer meets the criteria for fair value hedge accounting, or the hedge designation is revoked, then hedge accounting is discontinued prospectively.

Any adjustments, up to the point of discontinuation, to a hedged item for which the effective interest method is used, is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

88. Significant accounting policies (continued)

88.22. Other liabilities

Unpaid contributions to the Depositors' and Investors' Guarantee Fund (TIF)

According to Act No. 98/1999, on Deposit Guarantees and Investors' Compensation Scheme, as subsequently amended, the Bank is to pay each quarter a non-refundable general and variable contribution to the Icelandic Depositors' and Investors' Guarantee Fund (TIF). On 1 July 2019 Act No. 59/2019, amending Act No. 98/1999, entered into force lowering the amount of the general contribution by credit institutions to the TIF.

According to Act No. 59/2019 the general contribution is 0.02% per annum (0.005% on each quarterly due date) of all deposits, as defined in the Act, up to ISK 10,000 million, and 0.16% of deposits in excess of this amount (0.04% on each quarterly due date). The variable contribution is determined by a risk factor assigned to the Bank by the FME and may at maximum be equal to the general contribution. The Act No. 59/2019 became applicable with respect to payment of contributions due on 1 September 2019 for the second quarter of 2019. With respect to payment of contributions due on 1 June 2019 for the first quarter of 2019 the payment was according to Act No. 98/1999, prior to its amendment by Act No. 59/2019, i.e. 0,05625% on quarterly due date.

Acting on a joint proposal from FME and the Central Bank of Iceland, the TIF may collect a supplementary contribution if its assets are not sufficient to cover payments when the TIF's obligation to render payment becomes effective. TIF may also collect a supplementary premium to cover costs, instalments and interest payments on its loans. Such a supplementary payment, however, may never exceed 0.6% of the Bank's insured deposits.

The Bank only recognises a liability for premiums to TIF equivalent to the amount the Bank is obliged by law to pay at the end of each accounting period. This is the premium which the Bank is to pay during the current quarter for the preceding quarter. Other premiums to be paid by the Bank to the TIF during later periods are dependent upon the Bank's future activities and therefore are not recognised as a liability on the reporting date.

88.23. Subordinated liabilities

Subordinated liabilities are comprised of Tier 2 subordinated bonds issued by the Bank, on the one hand in foreign currencies under its Euro Medium Term Note (EMTN) programme, and, on the other, in Icelandic króna under its Debt Issuance Programme. The subordinated liabilities share characteristics of equity in that they are subordinated to other Group liabilities and are included in equity in equity ratio calculations. The outstanding amounts of the subordinated liabilities are subject to regulatory amortisation whereby the amount eligible for Tier 2 capital treatment is amortised on a straight-line basis over the final 5 years to maturity.

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

88.24. Short positions

Short positions are obligations of the Group to deliver financial assets borrowed by the Group and sold to third parties. These obligations are initially recognised in the statement of financial position at fair value, with transaction costs recognised in the income statement. Subsequently, they continue to be carried at fair value, with all fair value changes recognised in the income statement as net gain on financial assets and liabilities held for trading in the line item "Net gain (loss) on financial assets and financial liabilities". The short positions are in Icelandic government bonds with readily available quoted market prices.

88.25. Repurchase and reverse repurchase agreements

Repurchase agreements consist of repo and reverse repo transactions with other banks. Repo transactions combine the spot purchase or sale of securities with their forward sale or repurchase, the counterparty being identical in both cases.

Securities originally sold by the Bank under repurchase agreements continue to be recognised and measured as financial assets in the Bank's financial statements, as the Bank retains all risks and rewards connected with the ownership of securities it sells under repurchase agreements. Inflows of liquidity from repo transactions are recognised in the financial statements of the Bank as financial liabilities to counterparties. Interest payments are recognised as interest expense in net interest income. Inflows are measured either at fair value using the fair value option or at amortised cost.

Conversely, securities originally bought by the Bank under reverse repurchase agreements are not recognised and measured as financial assets in the Bank's financial statements, as the counterparty retains all risks and rewards connected with the ownership of securities bought by the Bank under repurchase agreements. Outflows of liquidity arising from reverse repos are accounted for as claims on counterparties. Interest payments in reverse repos are recognised as interest income under net interest income. Repurchase agreements and reverse repurchase agreements are initially measured at fair value less transaction costs and subsequently either at fair value using the fair value option or at amortised cost.

88.26. Collateral swaps

Collateral swaps consist of collateral swaps with other banks whereby the collateral provided is in the form of securities. In essence, collateral swaps are a form of securities lending whereby the Bank borrows relatively liquid securities from another bank in exchange for a pledge of less liquid securities. The securities borrowed by the Bank from the counterparty are not recognised and measured as financial assets in the Bank's financial statements, as the counterparty retains all risks and rewards connected with the ownership of the securities. However, the securities lent to the counterparty by the Bank continue to be recognised and measured as financial assets in the Bank's financial statements, as the Bank retains all risks and rewards connected with the ownership of the securities. The Bank pays a fee to the lender to compensate for the risk of holding less liquid collateral. Interest and expenses from collateral swaps are recognised in net interest income. Collateral swaps are initially measured at fair value less transaction costs and subsequently at amortised cost.

88. Significant accounting policies (continued)

88.27. Financial guarantees and loan commitments

'Financial guarantees' are contracts that require the Group to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. 'Loan commitments' are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at a below-market interest rate are initially measured at fair value. Subsequently, they are measured at the higher of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15.

The Group has issued no loan commitments that are measured at FVTPL.

For other loan commitments the Group recognises a loss allowance.

Liabilities arising from financial guarantees and loan commitments are included within provisions.

88.28. Contingent liabilities and provisions

The Group does not recognise contingent liabilities as liabilities in the statement of financial position, other than contingent liabilities which are assumed in a business combination and which have a fair value that can be measured reliably. A contingent consideration transferred by the Group in a business combination is recognised at its acquisition-date fair value. The Group classifies the obligation to pay contingent considerations as liability or equity and accounts for changes in fair value in accordance with applicable IFRSs.

Provisions for expenditures such as those related to legal claims or restructuring are recognised as incurred when (i) the Group has as a result of past events a present legal or constructive obligation to pay, (ii) it is more likely than not that an outflow of resources will be required to settle the obligation, and (iii) the amount has been reliably estimated.

Provisions are measured at the present value of the expenditures expected for settling the obligation. A pre-tax rate is used which reflects current market assessments of the time value of money and the risks specific to the obligation. Any increase in the provision due to the passage of time is recognised as interest expense.

88.29. Pension liabilities

When the savings banks Sparisjóður Vestmannaeyja and Sparisjóður Norðurlands merged with Landsbankinn in 2015, the Bank took over pension obligations towards the former employees and part of the current employees of these savings banks. The pension liability is calculated annually by an actuary. The increase in the liability in 2019 is expensed in the income statement with salaries and related expenses.

88.30. Employee benefits

All Group entities have defined contribution plans, with the entities paying a fixed contribution to publicly or privately administered pension plans on a mandatory and contractual basis. The Group has no further payment obligations once these contributions have been paid. The contributions are recognised as an expense when they become due. The Group has no defined benefit pension plan.

88.31. Share capital

(a) Share issue costs

Costs directly attributable to the issue of new shares are presented separately in equity as a deduction from share premiums.

(b) Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity during the period in which they are approved by the Bank's shareholders' meeting.

88.32. Fiduciary activities

The Group acts as a custodian, by holding or placing assets on behalf of individuals, institutions and pension funds, including various mutual funds managed by the Group. These assets are not reported in the Consolidated Financial Statements, since they are assets held on behalf of customers, institutions and pension funds and are not assets of the Group.

88.33. Interest income and expense

Effective interest rate

Interest income and expense are recognised in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- The gross carrying amount of the financial asset; or
- the amortised cost of the financial liability.

When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Group estimates future cash flows considering all contractual terms of the financial instrument, but not ECL.

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

88. Significant accounting policies (continued)

88.33. Interest income and expense (continued)

Amortised cost and gross carrying amount

The ‘amortised cost’ of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance (or impairment allowance before 1 January 2018).

The ‘gross carrying amount of a financial asset’ is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit impaired) or to the amortised cost of the liability. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest. The effective interest rate is also revised for fair value hedge adjustments at the date the amortisation of the hedge adjustment begins.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

Presentation

Interest income calculated using the effective interest method presented in the statement of profit or loss includes:

- Interest on financial assets and financial liabilities measured at amortised cost,
- interest on debt instruments measured at FVTPL; and
- the effective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk.

Other interest income presented in the statement of profit or loss includes interest income on finance leases.

Interest expense presented in the statement of profit or loss and OCI includes financial liabilities measured at amortised cost.

Changes in the fair value of financial assets and financial liabilities at FVTPL, including interest income and interest expense, are presented in the income statement in “Net gain on financial assets and liabilities at FVTPL”.

88.34. Fee and commission income and expense

Fee and commission income and expense that are integral to the effective interest rate on a financial asset or financial liability are included in the effective interest rate and recognised under interest income in the income statement.

Fee and commission income and expense are recognised in the income statement when an agreement with a customer meets all of the following criteria:

- The parties to the contract have approved the contract and are committed to perform their respective obligations.
- Performance obligations have been established for services to be transferred.
- The payment terms have been established for the services to be transferred.
- The transaction price can be allocated to each individual service in the agreement.
- It is probable that a consideration will be collected in exchange for the services that will be transferred to the customer.

The following applies to recognition of income for various types of fees and charges:

- Fees that are earned gradually as the services are performed, such as management fees in asset management, are recognised as income at the rate these services are delivered. In practice, these are on a straight-line basis.
- Fees attributable to a specific service or action are recognised as income when the service has been performed. Examples of such fees are brokerage and payment commission.

Income and expense for various kinds of services are recognised in the income statement under “Fee and commission income” and “Fee and commission expense”, respectively. This means that brokerage income and various types of management fees are recognised as commissions. Other forms of income recognised as commission are payment commissions, card fees and premiums of issued financial guarantees.

88.35. Net gain (loss) on financial assets and liabilities

Net gain (loss) on financial assets and financial liabilities is composed of: 1) net gain (loss) on financial assets designated at fair value through profit or loss; and 2) net profit (loss) on fair value hedges.

1) The net gain (loss) on financial assets designated at fair value through profit or loss includes:
- All realised and unrealised changes in fair value.
- Interest income on an accrual basis.
- Dividend income, which is recognised when the Group's right to receive payment is established.

2) The net profit (loss) on fair value hedges includes:
- All realised and unrealised changes in the fair value of hedging instruments.
- All realised and unrealised changes in the value of hedged items.
- Interest income/expense on an accrual basis that is included in the line item “Interest expense” in the income statement.

88. Significant accounting policies (continued)

88.36. Net foreign exchange (loss) gain

Net foreign exchange gain (loss) includes all gains and losses arising from the settlement of transactions in foreign currencies and translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies, including non-derivative financial assets and liabilities classified as held for trading and financial assets designated at fair value through profit or loss. Foreign exchange gains and losses arising from derivative financial assets and liabilities are included in the line item "Net gain (loss) on financial assets and financial liabilities" in the income statement, except for fair value changes of derivative currency forwards and net foreign exchange differences arising from OTC currency options, which are included in the line item "Net foreign exchange (loss) gain" in the income statement.

88.37. Other income and expenses

Other income and expenses include, *inter alia*, revenue arising from recharging agreements and gains and losses on repossessed collateral and property and equipment.

88.38. Leases

The Group has applied IFRS 16 *Leases* in the reporting period, using the modified retrospective approach. As a result, the comparative information for the year 2018 has not been restated and continues to be reported under the previous standard IAS 17 *Leases*.

Policy applicable from 1 January 2019

At inception of a contract, the Group assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Group uses the definition of a lease in IFRS 16.

This policy is applied to contracts entered into (or changed) on or after 1 January 2019.

(a) When the Group is the lessee

The leases into which the Group enters as a lessee are primarily operating leases. Under IFRS 16 lessees are required to recognise assets for the right-of-use of the underlying assets and liabilities for the obligations to make lease payments created by the leases. The assets and liabilities are recognised in the Statement of Financial Position under “Other assets” and “Other liabilities”.

Initially, the lease liability and the right-of-use asset will be measured at the present value of the lease payments (defined as unavoidable payments). A right-of-use asset is then depreciated on a straight-line basis over the lease period and the depreciation charge is recognised under Other operating expenses in the income statement. The lease liability is measured at the present value of future lease payments, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group’s incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate. Interest expenses on lease liabilities are recognised in the income statement under Interest expenses. The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or interest or exchange rate, change in contractual lease payments and extension of leases. When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use assets.

Short-term leases and leases of low-value assets

Exempted from the requirement of IFRS 16 to recognise assets and liabilities for leases into which the Group enters as a lessee are leases with a lease term of 12 months or less or with low-value underlying assets. In such cases the Group recognises the lease payments under Other operating expenses in the income statement.

(b) When the Group is the lessor

When assets are held subject to a finance lease, the present value of lease payments is recognised as a receivable under Loans and advances to customers in the Statement of Financial Position. Finance income from such a lease is recognised as interest income in the income statement over the term of the lease, using a method that reflects a constant periodic rate of return on the Group’s net investment in the lease.

Policy applicable before 1 January 2019

(a) When the Group is the lessee

The leases into which the Group enters as a lessee are primarily operating leases. Over the period of the lease, payments for operating leases are charged to the income statement on a straight-line basis, in the line item "Other operating expenses".

If an operating lease is terminated before the lease period has expired, any payment to the lessor required by way of penalty is recognised as an expense in the period in which termination occurs.

(b) When the Group is the lessor

When assets are held subject to a finance lease, the present value of lease payments is recognised as a receivable under Loans and advances to customers in the Statement of Financial Position. Finance income from such a lease is recognised as interest income in the income statement over the term of the lease, using a method that reflects a constant periodic rate of return on the Group's net investment in the lease.

88. Significant accounting policies (continued)

88.39. Discontinued operations

The Group presents discontinued operations in a separate line of the Consolidated Income Statement if an entity or a component of an entity has been disposed of or is classified as held for sale and:

- represents a major separate line of business;
- is a part of a single co-ordinated plan to dispose of a major separate line of business,
- is a subsidiary acquired exclusively with a view to resale.

The profit from discontinued operations disclosed in the Consolidated Income Statement consists of (a) post-tax profit or loss from discontinued operations and (b) post-tax gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or the disposal groups constituting the discontinued operation. A component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting, from the rest of the Group's operations and cash flows.

88.40. Earnings per share

Basic earnings per share (EPS) is calculated by dividing the profit or loss that is attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period, excepting own shares. Diluted EPS is determined by adjustin the profit or loss that is attributable to ordinary shareholders and the weighted-average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares.

88.41. Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components, whose operating results are reviewed regularly by the Executive Board (being the chief operating decision-maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

88.42. New standards, amendments to standards and interpretations of standards

As at 1 January 2019, the Group adopted for the first time the accounting standard IFRS 16 Leases using the modified retrospective approach. The standard replaces the previous standard IAS 17 Leases. The adoption of IFRS 16 had a significant impact on assets and liabilities and an insignificant impact on the opening balance of equity as at 1 January 2019.

The International Accounting Standards Board (IASB) has also issued new IFRS standards and made amendments to standards which have not yet taken effect. Those standards are not expected to have a significant impact on the Group’s Consolidated Financial Statements.

A fundamental reform (referred to as ‘IBOR reform’) of major interest rate benchmarks is being undertaken globally to replace or reform interbank offered rates (IBORs) with alternative nearly risk-free rates (RFRs). The Group has exposure to IBORs on its financial instruments that will be replaced or reformed as part of this market-wide initiative. In accordance with the terms of the instruments, the Bank may determine that the relevant IBOR benchmark rate may be replaced by a successor rate, if available, or an alternative rate in the interbank market or foreign exchange and swap markets.

Consolidated Key Figures

89. Operations by years

Operations	2019	2018	2017	2016	2015
Interest income	72,172	69,378	62,556	64,612	58,005
Interest expense	(32,502)	(28,564)	(26,285)	(29,962)	(25,681)
Net interest income	**39,670**	**40,814**	**36,271**	**34,650**	**32,324**
Net valuation adjustments and impairment	(4,827)	1,352	1,785	(318)	18,216
Net interest income after valuation adjustments	**34,843**	**42,166**	**38,056**	**34,332**	**50,540**
Fee and commission income	11,528	11,220	11,289	10,290	8,977
Fee and commission expense	(3,309)	(3,063)	(2,858)	(2,481)	(2,136)
Net fee and commission income	**8,219**	**8,157**	**8,431**	**7,809**	**6,841**
Other net operating income	**8,455**	**3,587**	**7,025**	**6,559**	**15,230**
Total operating income	**51,517**	**53,910**	**53,512**	**48,700**	**72,611**
Salaries and related expenses	(14,458)	(14,589)	(14,061)	(14,049)	(13,754)
Other operating expenses	(9,534)	(9,348)	(9,789)	(9,465)	(9,978)
Total operating expenses	**(23,992)**	**(23,937)**	**(23,850)**	**(23,514)**	**(23,732)**
Pre-tax profit	**27,525**	**29,973**	**29,662**	**25,186**	**48,879**
Income and bank tax	(9,290)	(10,713)	(9,896)	(8,543)	(12,419)
Profit for the year	**18,235**	**19,260**	**19,766**	**16,643**	**36,460**
Attributable to:					
Owners of the Bank	18,235	19,260	19,766	16,633	36,460
Non-controlling interests	-	-	-	10	-

Balance sheet	2019	2018	2017	2016	2015
Cash and cash balances with Central Bank	69,824	70,854	55,192	30,662	25,164
Bonds and debt instruments	115,262	77,058	117,310	154,892	203,684
Equities and equity instruments	30,019	23,547	27,980	26,688	29,192
Loans and advances to financial institutions	47,929	71,385	44,866	20,408	20,791
Loans and advances to customers	1,140,184	1,064,532	925,636	853,417	811,549
Other assets	22,088	17,335	18,238	17,641	16,323
Assets classified as held for sale	1,022	1,330	3,648	7,449	11,955
Total assets	**1,426,328**	**1,326,041**	**1,192,870**	**1,111,157**	**1,118,658**
Due to financial institutions and Central Bank	48,062	34,609	32,062	20,093	56,731
Deposits from customers	707,813	693,043	605,158	589,725	559,051
Borrowings	373,168	314,412	281,874	223,944	209,344
Other liabilities	30,440	30,997	27,615	24,681	26,844
Liabilities associated with assets classified as held for sale	30	30	27	1,095	1,518
Subordinated liabilities	19,081	13,340	77	388	639
Equity	247,734	239,610	246,057	251,231	264,531
Total liabilities and equity	**1,426,328**	**1,326,041**	**1,192,870**	**1,111,157**	**1,118,658**

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90. Operations by quarters

	2019				2018			
Operations	**Q4***	**Q3**	**Q2**	**Q1**	**Q4***	**Q3**	**Q2**	**Q1**
Interest income	16,844	16,874	20,555	17,899	19,381	17,622	16,316	16,059
Interest expense	(7,264)	(7,243)	(10,341)	(7,654)	(8,413)	(7,252)	(6,481)	(6,418)
Net interest income	**9,580**	**9,631**	**10,214**	**10,245**	**10,968**	**10,370**	**9,835**	**9,641**
Reversals of loss from foreign currency linkage of loans and advances	-	-	-	-	-	-	1,129	-
Net impairment (loss) gain	(1,400)	(1,047)	(1,383)	(1,024)	(353)	(89)	(426)	1,024
Net impairment on other financial assets	1	(9)	5	30	67	-	-	-
Net adjustments in valuation	**(1,399)**	**(1,056)**	**(1,378)**	**(994)**	**(286)**	**(89)**	**703**	**1,024**
Net interest income after net valuation adjustments in impairment	**8,181**	**8,575**	**8,836**	**9,251**	**10,682**	**10,281**	**10,538**	**10,665**
Fee and commission income	2,980	2,784	2,861	2,903	3,269	2,565	2,926	2,460
Fee and commission expense	(855)	(826)	(785)	(843)	(914)	(639)	(741)	(769)
Net fee and commission income	**2,125**	**1,958**	**2,076**	**2,060**	**2,355**	**1,926**	**2,185**	**1,691**
Net gain (loss) on financial assets and liabilities at FVTPL	2,126	649	1,776	3,442	(58)	(151)	(333)	2,196
Net foreign exchange loss	(300)	(39)	(87)	(158)	(676)	(352)	(399)	(70)
Other income and (expenses)	131	211	266	438	537	348	195	2,350
Other net operating income	**1,957**	**821**	**1,955**	**3,722**	**(197)**	**(155)**	**(537)**	**4,476**
Total operating income	**12,263**	**11,354**	**12,867**	**15,033**	**12,840**	**12,052**	**12,186**	**16,832**
Salaries and related expenses	3,805	3,284	3,689	3,680	3,835	3,222	3,869	3,663
Other operating expenses	2,505	2,167	2,340	2,522	2,373	2,353	2,287	2,335
Total operating expenses	**6,310**	**5,451**	**6,029**	**6,202**	**6,208**	**5,575**	**6,156**	**5,998**
Profit before tax	**5,953**	**5,903**	**6,838**	**8,831**	**6,632**	**6,477**	**6,030**	**10,834**
Income tax	(1,014)	(1,591)	(1,444)	(1,037)	(1,737)	(1,615)	(1,609)	(1,892)
Tax on liabilities of financial institutions	(1,064)	(1,065)	(1,065)	(1,010)	(1,028)	(1,082)	(910)	(840)
Profit for the period	**3,875**	**3,247**	**4,329**	**6,784**	**3,867**	**3,780**	**3,511**	**8,102**

Balance sheet	**31.12.19**	**30.09.19**	**30.06.19**	**31.03.19**	**31.12.18**	**30.09.18**	**30.06.18**	**31.03.18**
Cash and cash balances with Central Bank	69,824	56,680	63,990	63,014	70,854	61,155	68,372	82,266
Bonds and debt instruments	115,262	96,786	84,830	80,954	77,058	88,749	97,214	100,216
Equities and equity instruments	30,019	29,150	27,658	25,151	23,547	27,766	28,756	25,666
Loans and advances to financial institutions	47,929	71,222	71,812	88,664	71,385	84,513	47,937	41,796
Loans and advances to customers	1,140,184	1,136,804	1,130,915	1,095,376	1,064,532	1,038,005	989,481	936,636
Other assets	22,088	23,476	22,348	24,744	17,335	15,399	16,261	17,455
Assets classified as held for sale	1,022	1,144	1,282	1,394	1,330	1,618	1,832	2,113
Total assets	**1,426,328**	**1,415,262**	**1,402,835**	**1,379,298**	**1,326,041**	**1,317,205**	**1,249,853**	**1,206,148**
Due to financial institutions and Central Bank	48,062	47,860	34,430	36,636	34,609	34,714	27,504	30,943
Deposits from customers	707,813	703,762	697,898	694,820	693,043	692,675	654,689	622,021
Borrowings	373,168	366,337	377,680	351,005	314,412	308,362	297,684	284,484
Other liabilities	30,440	39,980	37,768	36,701	30,997	32,614	37,764	39,984
Liabilities associated with assets classified as held for sale	30	30	30	30	30	73	27	41
Subordinated liabilities	19,081	13,433	14,417	13,900	13,340	12,875	72	74
Equity	247,734	243,860	240,612	246,206	239,610	235,892	232,113	228,601
Total liabilities and equity	**1,426,328**	**1,415,262**	**1,402,835**	**1,379,298**	**1,326,041**	**1,317,205**	**1,249,853**	**1,206,148**

*The result for the first three quarters of the years 2019 and 2018 were reviewed by the Bank's independent auditors.

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91. Key figures and ratios

	2019	2018	2017	2016	2015
Return on equity before taxes	11.3%	12.8%	12.3%	9.9%	19.9%
Return on equity after taxes	7.5%	8.2%	8.2%	6.6%	14.8%
Return on equity after taxes, excluding bank levy	9.2%	9.8%	9.5%	7.7%	16.0%
Cost-income ratio	42.6%	45.5%	46.1%	48.4%	43.8%
Operating expenses as a ratio of average total assets	1.7%	1.9%	2.0%	2.1%	2.1%
Return on assets	1.3%	1.5%	1.7%	1.5%	3.2%
Interest spread as ratio of assets and liabilities	2.4%	2.7%	2.5%	2.3%	2.2%
Earnings per share	0.77	0.81	0.84	0.70	1.54
Total capital ratio	25.8%	24.9%	26.7%	30.2%	30.4%
CET1 ratio	23.9%	23.6%	26.3%	29.7%	30.3%
Leverage ratio	15.7%	16.1%	18.2%	20.3%	21.5%
Loans / deposits	161.1%	153.6%	153.0%	144.7%	145.2%
Deposits / total assets	49.6%	52.3%	50.7%	53.1%	50.0%
Liquidity coverage ratio (LCR)	161%	158%	157%	128%	113%
Net stable funding ratio FX (NSFR)	143%	166%	179%	154%	136%
Number of full-time positions at year-end	893	919	997	1,012	1,063
Dividend per share	0.42	1.05	1.05	1.20	1.00

Key figures and ratios	Definition
Return on equity before taxes	Profit before taxes / average total equity
Return on equity after taxes	Profit after taxes / average total equity
Return on equity after taxes, excluding bank levy	Profit after taxes, excluding bank levy / average total equity
Cost-income ratio	Total operating expenses / (total operating income - net valuation adjustments)
Operating expenses as a ratio of average total assets	Total operating expenses as a ratio of average total assets
Return on assets	Profit (loss) for the year / average total assets
Interest spread	(Interest income / average total assets) - (interest expenses / average total liabilities)
Earnings per share	Profit for the year attributable to owners of the Bank / Weighted average number of shares outstanding
Total capital ratio	Total capital base / risk-exposure amount
CET1 ratio	Common equity tier 1 capital (CET1) / Risk exposure amount
Common equity Tier 1 capital (CET1)	Total equity - deductions (intangible assets, deferred tax assets)
Additional common equity Tier 1 capital (AT1)	Capital instruments under Tier 1 other than (CET1)
Tier 1 capital (T1)	Common equity Tier 1 capital + additional common equity Tier 1 capital
Tier 2 capital (T2)	Subordinated liabilities - regulatory amortisation
Total capital base	CET1 + AT1 + T2
Leverage ratio	Tier 1 capital / (total assets + off balance sheet items)
Loans/ deposits	Loans and advances to customers/ deposits from customers
Deposits / total assets	Deposits from customers/ total assets
Liquidity coverage ratio (LCR)	High quality liquid assets / total net liquidity outflows over 30 days under stressed conditions
Net stable funding ratio FX (NSFR)	Available amount of stable funding / required amount of stable funding
Number of full-time equivalent positions at year-end	Number of full-time equivalent positions at year-end
Dividend per share	Dividends paid / number of shares outstanding

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