Íslandsbanki

Condensed Consolidated Interim Financial Statements

First half 2020

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Íslandsbanki Factsheet 2Q20

Íslandsbanki

Our profile

Íslandsbanki is a universal bank and a leader in financial services in Iceland with a history of 145 years of servicing key industries. The Bank has a 25-40% market share across all domestic business segments.

Íslandsbanki's purpose is to move Iceland forward by empowering our customers to succeed. Driven by the vision to be #1 for service, Íslandsbanki's relationship banking business model is propelled by three business divisions that manage and build relationships with the Bank's customers.

Íslandsbanki has developed a wide range of online services such as the Íslandsbanki and Kass apps, enabling customers to do their banking anywhere and anytime. At the same time, the Bank continues to operate the most efficient branch network in Iceland through its strategically located 12 branches.

Íslandsbanki has a BBB/A-2 rating from S&P Global Ratings.

Our bank

12 branches

735 Number of FTEs at Íslandsbanki at period end

New unified banking app

Market share*

33% individuals

35% SMEs

34% large companies

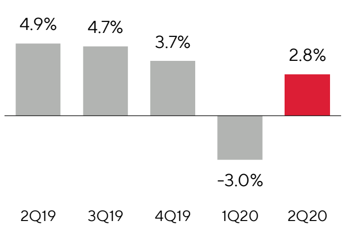
Credit rating

S&P Global Ratings

BBB/A-2

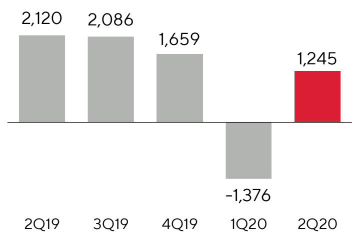
Stable outlook

Return on equity

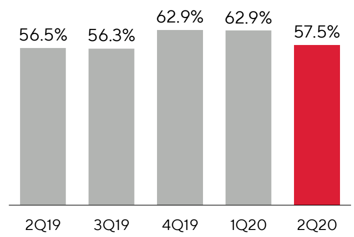


Profit (loss) after tax

(ISKm)

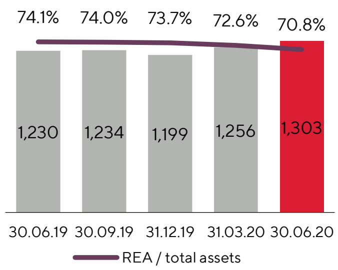


Cost / income ratio



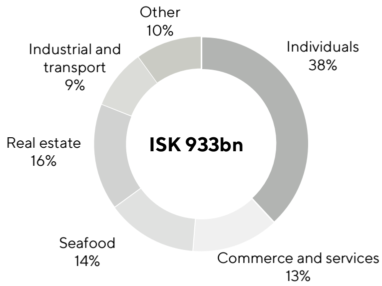
Total assets

(ISKbn)



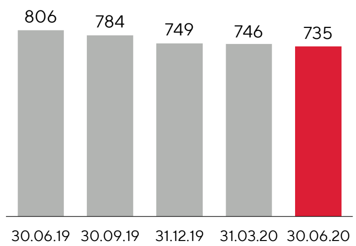
Loans to customers

(Sector split as of 30.06.20)



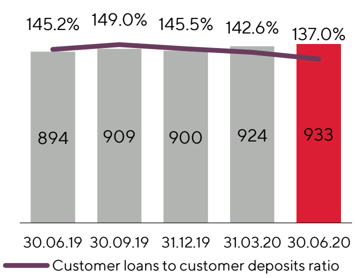
Number of FTEs at Íslandsbanki

(Excluding seasonal employees)

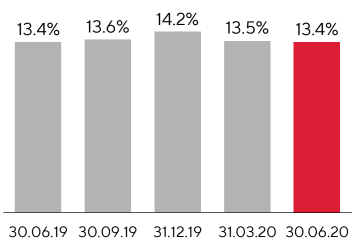


Loans to customers

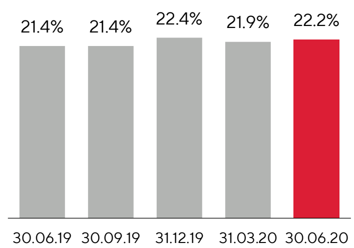
(ISKbn)



Leverage ratio



Total capital ratio



The information above has not been reviewed or audited by the Bank's auditor.
*Based on Gallup survey regarding primary bank.

Directors' Report

These are the condensed consolidated interim financial statements for the first half of 2020 ("the interim financial statements") of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") and its subsidiaries (together referred to as "the Group").

Operations in the reporting period

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

The Group reported a loss from its operations for the reporting period amounting to ISK 131 million. At the end of the reporting period the Group employed 980 full-time members of staff, including 735 within the Bank itself and 210 employees of disposal groups held for sale.

The Bank concluded the sale of its shares in Borgun hf. on 7 July 2020. The equity stake in Borgun hf. is accounted for as an asset held for sale in the first half year accounts. The impact on the income statement is shown in a single line as discontinued operations and comparative figures in the Directors' Report have been restated. The sale will be accounted for in the third quarter and will have a limited impact on the Bank's operations and capital position.

The Group's earnings in the first half of 2020 were heavily affected by the economic crisis relating to the COVID-19 pandemic. After a loss of ISK 1,376 million in the first quarter, the Group did however return to profitability in the second quarter, with 1,245 million in positive earnings. As a result of COVID-19, expected credit losses increased substantially from 2019. In line with IFRS 9 the Bank has transferred almost all of its exposures to the tourism industry from Stage 1 to Stage 2 and updated its economic forecasts. As well as factoring in the impact on Government programmes to mitigate the impact of the pandemic. Although, Iceland has started to lift its travel restrictions, substantial uncertainty remains with regards to developments in the economy and thereby the Bank's impairments going forward. The Bank had a negative impairment charge of ISK 5.9 billion in the first half. In addition to that, the Bank experienced losses in its net financial income of ISK 1.9 billion.

Net interest income rose by 2.9% between years, where the lower interest environment is starting to have a material impact on earnings through lower deposit margins and returns on the Bank's liquidity portfolio. Net fee and commission income was down by 11.2%, mainly due to less economic activity. Salaries and related expenses were down by 6.4% between years as a result of FTE reductions in 2019, while other operating expenses decreased by 7.8%.

The Group's loan book grew by 3.7% in the period, which can be contributed to strong demand for mortgages and the depreciation of the Icelandic króna. The Bank's ratio of non-performing loans rose from 3.0% to 3.6%. However, Stage 2 loans under IFRS 9 did increase from 2.6% to 13.4% since year-end 2019 as the credit risk related to loans to the tourism industry was deemed to have materially increased due to the COVID-19 pandemic.

Customer deposits increased by 10.2% from year-end 2019 with the largest increase in Corporate and Investment Banking as a result of a large increase in deposits from pension funds. Bond issuance was modest in the quarter and only relating to regular covered bond auctions. The Bank did however buy back some of its outstanding bonds as a part of its balance sheet management. The liquidity position of the Bank remains robust, with limited maturities in 2020 and therefore the need for issuance in foreign currency this year is minimal. The Bank is also very well capitalised, with a total capital ratio of 22.2% at the end of the period, compared to a 17% regulatory requirement, which was lowered as the counter-cyclical buffer was reduced from 2.0% to zero as a result of the economic slowdown.

The COVID-19 pandemic significantly impacted the operations of the Bank for the first half. Most of the headquarters employees worked from home for a large part of the second quarter and customer access to branches was restricted for a period of time. Despite these unusual circumstances, the Bank has managed to be close to fully operational. The main focus onwards will be to continue to help and support our customers through the difficulties in the months ahead as the full impact of the pandemic will materialise.

The Bank continues to make good progress in terms of enhancing services in the digital channels and is seeing a strong shift toward those channels from the traditional ones. In the past year visits to branches has declined by as much as 70%. Concurrent with these changes, the branches at Höfði and Grandi have been merged with the Laugardalur branch. After the merger, the Bank will operate three branches in the capital area.

Outlook

The Icelandic economy has started on a gradual path to normalisation after the initial impact of the COVID-19 pandemic. Containment measures have been eased considerably and everyday domestic activity is mostly back to normal as new infections have fallen to a very low level. Following a period of virtually no tourist visits from mid-March through mid-June, foreign tourists are once more travelling to Iceland, albeit on a much smaller scale than in recent years. The goods export sector has also been impacted by the pandemic, as have some domestic demand-related sectors. Unemployment has increased considerably and averaged 7.5% of the workforce in the first half of the year.

Directors' Report

The setback in exports, private consumption and private investment is unavoidably going to translate to a considerable fall in GDP in 2020.The negative economic impact will, however, be mitigated by a significant contraction in imports as well as a boost to public investment. Icelandic authorities have introduced a range of measures to soften the economic impact of the pandemic, ranging from targeted assistance for affected businesses to broader fiscal stimulus and considerable easing of financial and monetary conditions. The duration of the economic setback will hinge on how rapidly travel conditions normalise and economic activity resumes on a global scale. Assuming fading impact from COVID-19 throughout the second half of 2020, there is a good probability of a return to healthy GDP growth in 2021.

The Bank's financial position remains strong, with regards to capital and liquidity and therefore well placed to support its customers in this ongoing turbulent economic environment. Profitability will be adversely affected in 2020 as a result of increased impairments, fall in security prices and lower interest rate environment. The Bank will however strive to get back on track to reach its profitability targets from 2021 onwards.

Statement by the Board of Directors and the CEO

The interim financial statements for the period 1 January to 30 June 2020 have been prepared on a going concern basis in accordance with the International Accounting Standard (IAS) 34 Interim Financial Reporting as adopted by the European Union; the Act on Annual Accounts, no. 3/2006; the Act on Financial Undertakings, no. 161/2002; and rules on accounting for credit institutions, where applicable.

To the best of our knowledge, these interim financial statements provide a true and fair view of the Group's operating profits and cash flows in the reporting period and its financial position as of 30 June 2020.

The Board of Directors and the CEO have today discussed and approved the Condensed Consolidated Interim Financial Statements for the period 1 January to 30 June 2020.

Kópavogur, 29 July 2020

Board of Directors:

Hallgrímur Snorrason, Chairman

Heiðrún Jónsdóttir, Vice-Chairman

Anna Þórðardóttir

Árni Stefánsson

Flóki Halldórsson

Frosti Ólafsson

Guðrún Þorgeirsdóttir

Chief Executive Officer:

Birna Einarsdóttir

Report on Review of Condensed Consolidated Interim Financial Statements

To the Board of Directors and Shareholders of Íslandsbanki hf.

We have reviewed the accompanying Condensed Consolidated Interim Financial Statements of Íslandsbanki hf. and its subsidiaries as at June 30, 2020 which comprise of the Consolidated Interim Statement of Financial Position as at June 30, 2020 and the related Consolidated Interim Income Statement, the Consolidated Interim Statement of Comprehensive Income, the Consolidated Interim Statement of Changes in Equity and Consolidated Interim Statement of Cash Flows for the six months ended 30 June 2020 and explanatory notes. The Board of Directors and CEO are responsible for the preparation and fair presentation of these Condensed Consolidated Interim Financial Statements in accordance with the International Financial Reporting Standard, IAS 34 Interim Financial Reporting as adopted by the EU. Our responsibility is to express a conclusion on these Condensed Consolidated Interim Financial Statements based on our review.

Scope of Review

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

Conclusion

Based on our review nothing has come to our attention that causes us to believe that the accompanying Condensed Consolidated Interim Financial Statements are not prepared, in all material respects, in accordance with the International Financial Reporting Standard, IAS 34 Interim Financial Reporting, as adopted by the EU.

Emphasis of Matter

We draw attention to Note 2 to the Condensed Consolidated Interim Financial Statements which describes the uncertainty related to the financial impacts of the COVID-19 pandemic on the measurement of the Group’s exposures. Our conclusion is not modified in respect of the matter.

Reykjavík, 29 July 2020

Margrét Pétursdóttir

State Authorised Public Accountant

Ernst & Young ehf.

Borgartúni 30

105 Reykjavík

Consolidated Interim Income Statement

	Notes	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Interest income*		28,598	32,123	14,953	17,117
Interest expense		(11,790)	(15,782)	(6,725)	(8,713)
Net interest income	11	16,808	16,341	8,228	8,404
Fee and commission income		5,385	5,867	2,622	2,995
Fee and commission expense		(587)	(462)	(315)	(237)
Net fee and commission income	12	4,798	5,405	2,307	2,758
Net financial income (expense)	13	(1,919)	622	(181)	180
Net foreign exchange gain (loss)	14	263	(136)	208	(15)
Other operating income	15	90	1,168	71	27
Other net operating income		(1,566)	1,654	98	192
Total operating income		20,040	23,400	10,633	11,354
Salaries and related expenses	16	(6,694)	(7,153)	(3,447)	(3,689)
Other operating expenses	17	(4,869)	(5,280)	(2,424)	(2,531)
Contribution to the Depositors' and Investors' Guarantee Fund		(475)	(510)	(247)	(198)
Bank tax		(758)	(1,814)	(399)	(934)
Total operating expenses		(12,796)	(14,757)	(6,517)	(7,352)
Profit before net impairment on financial assets		7,244	8,643	4,116	4,002
Net impairment on financial assets	18	(5,929)	(1,809)	(2,439)	(902)
Profit before tax		1,315	6,834	1,677	3,100
Income tax expense	19	(888)	(1,922)	(119)	(726)
Profit for the period from continuing operations		427	4,912	1,558	2,374
Discontinued operations, net of income tax	20	(558)	(203)	(313)	(254)
Profit (loss) for the period		(131)	4,709	1,245	2,120
Profit (loss) attributable to:					
Shareholders of Íslandsbanki hf.		171	4,919	1,422	2,268
Non-controlling interests		(302)	(210)	(177)	(148)
Profit (loss) for the period		(131)	4,709	1,245	2,120
Earnings per share from continuing operations					
Basic and diluted earnings per share attributable to the shareholders of Íslandsbanki hf.	21	0.07	0.51	0.17	0.25

*Of which interest income amounting to ISK 27,526 million (2019: ISK 30,820 million) is calculated using the effective interest method.

Comparative figures have been restated as the subsidiary Borgun hf. has been classified as disposal group held for sale and as discontinued operations (see Note 4).

The half-year results were reviewed by the Bank's auditor. The quarterly statements and the split between quarters were not reviewed or audited by the Bank's auditor.

The notes on pages 12 to 60 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Comprehensive Income

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Profit (loss) for the period	(131)	4,709	1,245	2,120
Items that will not be reclassified to profit or loss				
Changes in fair value of financial assets, net of tax	(913)	893	(604)	379
Changes in fair value of financial liabilities, net of tax	819	(831)	(346)	(336)
Other comprehensive income (expense) for the period, net of tax	(94)	62	(950)	43
Total comprehensive income (expense) for the period	(225)	4,771	295	2,163

The half-year results were reviewed by the Bank's auditor. The quarterly statements and the split between quarters were not reviewed or audited by the Bank's auditor.

The notes on pages 12 to 60 are an integral part of these Condensed Consolidated Interim Financial Statements.

Financial Statements first half 2020 7 Amounts are in ISK million

Consolidated Interim Statement of Financial Position

	Notes	30.6.2020	31.12.2019
Assets			
Cash and balances with Central Bank	22	103,569	146,638
Loans to credit institutions	23	70,307	54,376
Bonds and debt instruments	6	140,422	52,870
Derivatives	24	6,366	5,621
Loans to customers	25	933,320	899,632
Shares and equity instruments	6	10,943	18,426
Investments in associates		750	746
Property and equipment	27	7,549	9,168
Intangible assets		3,667	4,330
Other assets	28	6,370	6,608
Non-current assets and disposal groups held for sale	29	19,993	1,075
Total Assets		1,303,256	1,199,490
Liabilities			
Deposits from Central Bank and credit institutions	30	35,461	30,925
Deposits from customers	31	681,223	618,313
Derivative instruments and short positions	24	7,519	6,219
Debt issued and other borrowed funds	33	321,803	306,381
Subordinated loans	34	25,834	22,674
Tax liabilities		6,438	7,853
Other liabilities	36	29,935	27,063
Non-current liabilities and disposal groups held for sale	29	15,321	-
Total Liabilities		1,123,534	1,019,428
Equity			
Share capital		10,000	10,000
Share premium		55,000	55,000
Reserves		7,262	7,065
Retained earnings		105,681	105,569
Total Shareholders' Equity		177,943	177,634
Non-controlling interests		1,779	2,428
Total Equity		179,722	180,062
Total Liabilities and Equity		1,303,256	1,199,490

The notes on pages 12 to 60 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Changes in Equity

	Share capital	Share premium	Statutory reserve	Restricted reserves	Fair value reserve	Liability credit reserve	Retained earnings	Total shareholders' equity	Non-controlling interests	Total equity
Equity as at 1.1.2020	10,000	55,000	2,500	3,525	1,432	(392)	105,569	177,634	2,428	180,062
Profit (loss) for the period							171	171	(302)	(131)
Net change in fair value of financial assets					(602)		36	(566)	(347)	(913)
Net change in fair value of financial liabilities						819		819		819
Restricted due to capitalised development costs				(146)			146	-		-
Restricted due to fair value changes				107			(107)	-		-
Restricted due to subsidiaries and associates				19			(19)	-		-
Other changes due to IFRS 15							(115)	(115)		(115)
Equity as at 30.6.2020	10,000	55,000	2,500	3,505	830	427	105,681	177,943	1,779	179,722
Equity as at 1.1.2019	10,000	55,000	2,500	3,750	625	(376)	102,496	173,995	2,318	176,313
Profit (loss) for the period							4,919	4,919	(210)	4,709
Dividends paid							(5,300)	(5,300)		(5,300)
Net change in fair value of financial assets					567			567	326	893
Net change in fair value of financial liabilities						(384)	(447)	(831)		(831)
Restricted due to capitalised development costs				(138)			138	-		-
Restricted due to fair value changes				275			(275)	-		-
Restricted due to subsidiaries and associates				(3)			3	-		-
Equity as at 30.6.2019	10,000	55,000	2,500	3,884	1,192	(760)	101,534	173,350	2,434	175,784

Authorised share capital of the Bank is 10,000 million ordinary shares of ISK 1 each. At 30.6.2020 paid up share capital totalled ISK 65,000 million which is the total stated share capital of the Bank. The Bank has one class of ordinary shares which carry no right to fixed income. The Annual General Meeting ("AGM") for the operating year 2019 was held on 19 March 2020. At the AGM shareholders approved that a dividend to shareholders for the operating year 2019 shall not be paid in light of uncertainties due to unprecedented circumstances in the financial markets. It was also approved that the Board may convene a special shareholder meeting later in the year where a proposal regarding payment of dividends of profit for previous fiscal years could be suggested.

The notes on pages 12 to 60 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Cash Flows

	Notes	2020 1.1-30.6	2019 1.1-30.6
Profit (loss) for the period		(131)	4,709
Non-cash items included in profit (loss) for the period*		15,671	12,127
Changes in operating assets and liabilities*		(21,771)	(37,932)
Dividends received		27	32
Income tax and bank tax paid		(3,270)	(2,020)
Net cash used in operating activities		(9,474)	(23,084)
Proceeds from sales of property and equipment		8	7
Purchase of property and equipment		(433)	(192)
Purchase of intangible assets		(116)	(193)
Net cash used in investing activities		(541)	(378)
Proceeds from borrowings		10,300	101,423
Repayment of borrowings		(19,243)	(75,371)
Repayment of lease liabilities		(197)	(186)
Dividends paid		-	(5,300)
Net cash (used in) provided by financing activities		(9,140)	20,566
Net decrease in cash and cash equivalents		(19,155)	(2,896)
Effects of foreign exchange rate changes		176	(3)
Cash and cash equivalents at the beginning of the year		152,481	143,203
Cash and cash equivalents at the end of the period		133,502	140,304
Reconciliation of cash and cash equivalents			
Cash on hand	22	4,121	4,369
Cash balances with Central Bank	22	99,448	118,425
Bank accounts	23	34,382	32,836
Mandatory reserve and special restricted balances with Central Bank	22	(9,009)	(15,326)
Cash and cash equivalents attributable to discontinued operations		4,560	-
Cash and cash equivalents at the end of the period		133,502	140,304

*For further breakdown see the following page.

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

The Group presents a statement of cash flows that includes an analysis of all cash flows in total, including both continuing and discontinued operations. For cash flow information regarding Borgun hf. see Note 4.

Interest received from 1 January to 30 June 2020 amounted to ISK 24,659 million (2019: ISK 29,697 million) and interest paid in the same period 2020 amounted to ISK 10,650 million (2019: ISK 13,080 million). Interest paid is defined as having been paid when it has been deposited into the customer account and is available for the customer's disposal.

The notes on pages 12 to 60 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Cash Flows

	2020	2019
	1.1-30.6	1.1-30.6
Depreciation, amortisation and write-offs	1,003	811
Share of profit of associates	(20)	(5)
Accrued interest and fair value changes on debt issued and subordinated loans	6,401	5,944
Net impairment on financial assets	5,743	1,804
Foreign exchange (gain) loss	(263)	101
Net gain from sales of property and equipment	-	(2)
Unrealised fair value loss (gain) recognised in profit or loss	1,208	(190)
Discontinued operations, net of income tax	(78)	71
Bank tax	758	1,814
Income tax	888	1,779
Other changes	31	-
Non-cash items included in profit (loss) for the period	15,671	12,127

Mandatory reserve and special restricted balances with Central Bank	6,270	1,786
Loans to credit institutions	4,552	(24,508)
Bonds and debt instruments	(85,374)	(4,661)
Loans to customers	(21,682)	(39,202)
Shares and equity instruments	4,258	(4,939)
Other assets	(4,015)	(8,688)
Non-current assets and liabilities held for sale	(718)	3
Deposits from Central Bank and credit institutions	3,451	3,812
Deposits from customers	50,766	32,176
Derivative instruments and short positions	2,337	(1,488)
Other liabilities	18,384	7,777
Changes in operating assets and liabilities	(21,771)	(37,932)

Non-cash transactions 2020
During the period the Bank sold an office building for ISK 100 million with cash settlement after the period end.

Non-cash transactions 2019
The recognition of right-of-use assets amounting to ISK 4,489 million and the same amount in lease liabilities following the adoption of IFRS 16 - Leases had no cash flow effect.

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

The notes on pages 12 to 60 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

Notes to the Condensed Consolidated Interim Financial Statements

1. Corporate information

Íslandsbanki hf., the parent company, was incorporated on 8 October 2008 and is a limited liability company domiciled in Iceland. The address of its registered office is Hagasmári 3, 201 Kópavogur, Iceland.

The condensed consolidated interim financial statements for the first half of 2020 ("the interim financial statements") comprise the financial statements of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") and its subsidiaries together referred to as "the Group".

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

The interim financial statements were approved and authorised for issue by the Board of Directors and the CEO of Íslandsbanki hf. on 29 July 2020.

2. Basis of preparation

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

The interim financial statements do not include all the information required for annual financial statements and should be read in conjunction with the audited consolidated financial statements of the Group for the year ended 31 December 2019, as well as the unaudited Pillar 3 Report for the year 2019. Both are available on the Bank's website: www.islandsbanki.is.

The accounting policies and the basis of measurement are unchanged in comparison with Notes 64 and 66 in the consolidated financial statements for the year 2019 except for the changes presented in Note 3.

The subsidiary Borgun hf. has been classified as non-current assets and disposal groups held for sale. Accordingly the comparative figures in the consolidated interim income statement for the first half of 2019 have been restated (see Note 4).

The interim financial statements are presented in Icelandic króna (ISK), which is the functional currency of Íslandsbanki hf. All amounts presented in ISK have been rounded to the nearest million, except when otherwise indicated. At 30 June 2020 the exchange rate of the ISK against the USD was 138.58 and 155.40 for the EUR (year-end 2019: USD 121.10 and EUR 135.83).

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

Significant accounting estimates and judgements

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

Estimates and underlying assumptions are regularly reviewed and revised by management as deemed necessary. Changes in accounting estimates are recognised when they occur.

As described in Note 2 in the consolidated financial statements for the year 2019 key areas where management has made difficult, complex or subjective judgements, include those relating to impairment of financial assets, the fair value of financial instruments and intangible assets.

Impairment of financial assets, changes from year-end 2019

Note 66.3 in the consolidated financial statements for the year 2019 contains a description of the Group's accounting policies for impairment of financial assets.

At the end of the first half of 2020, the following changes have been made.

The Group's Chief Economist has provided a new macroeconomic forecast on 18 June 2020 which takes into account the effects of the COVID-19 pandemic.

Notes to the Condensed Consolidated Interim Financial Statements

2. Cont'd

Change in economic indicators %	2019	2020	2021	2022	2023	2024
Economic growth	1.9	(9.1)	4.3	4.2	2.4	2.2
Housing prices in Iceland	3.4	2.0	1.7	3.0	4.5	4.0
Purchasing power	1.8	3.3	1.8	1.6	2.6	2.3
ISK exchange rate index	8.5	9.1	1.3	-	(1.2)	(1.2)
Policy rate, Central Bank of Iceland	3.9	1.5	1.1	2.0	3.5	3.5
Inflation	3.0	2.3	2.0	2.4	1.8	2.2
Capital formation	(6.3)	(8.4)	4.0	5.1	1.6	2.7
thereof capital formation in industry	(17.5)	(15.7)	7.4	7.0	3.5	3.5

The Group has noted the guidelines provided by the Financial Supervision Committee of the Icelandic Central Bank, in particular the following: "It is important that the selection of scenarios in the application of IFRS 9 reflect the general expectation that the current situation is temporary, whereas the impact assessment must be conducted on a medium- and long-term basis." The Group uses three economic scenarios: a base economic scenario based on the macroeconomic forecast, a better scenario, and a worse scenario to capture the complete range of possible outcomes.

The Group's model to calculate PD scaling factors was applied to these economic scenarios and the resulting scaling factors were then reviewed by the All Risk Committee with respect to all of the economic indicators and any other relevant information available. The All Risk Committee determined that it was appropriate to adjust the weights of the scenarios, generally the scenarios are weighted 25%-50%-25% (good, base, bad) but it was determined appropriate to set the weights at 20%-50%-30%, as this would best represent the probability-weighted average over all possible scenarios.

Additionally, an assessment was made whether there were common risk factors for any subsets of the Group's financial assets where a general adjustment was warranted. It was determined that loans to the tourism industry was such a subset. Companies in the tourism industry, to which the Group has granted credit, were classified into four classes based on an assessment of how much an increase in credit risk these companies face in the short, medium and long term. The exposures were transferred to Stage 2 and an overlay factor depending on the severity was applied to the expected credit loss (see Note 46).

The common risk factor in tourism was found to apply to loans to customers with a net carrying amount of ISK 93 billion and the effect of the stage transfer and credit loss overlay was ISK 4.5 billion. Additionally, changes in impairment for a few specific customers resulted in an additional credit loss allowance of ISK 700 million. Other changes in credit loss allowance were smaller (see Note 18).

Substantial uncertainty remains with regards to the impact of the COVID-19 pandemic on the credit quality of the Group's credit exposures in future periods and therefore the assessment of expected credit losses.

3. Changes to accounting policies

The accounting policies in the interim financial statements are consistent with those applied in the consolidated financial statements for the year 2019, except for amendments described below. The amendments did not have a significant impact on the interim financial statements.

Interest Rate Benchmark Reform

The Group adopted amendments to IFRS 9 – Financial Instruments, IAS 39 – Financial Instruments: Recognition and Measurement, and IFRS 7 – Financial Instruments: Disclosures, as of 1 January 2020. The amendments modify certain hedge accounting requirements, relating to the method that is used to assess the effectiveness of a hedging relationship, to provide relief from potential effect of uncertainty caused by the Interest Rate Benchmark Reform, prior to the transition to alternative interest rates (see Note 24 and Note 33).

To manage the transition to alternative interest rates the Bank has set up a working group responsible for the overall transition. A comprehensive review of legacy contracts has been carried out by the Legal department and new contract language been introduced to accommodate the benchmark reform. The work on systems and processes, along with education and communication to major stakeholders, is ongoing. It is expected that financial effects of the transition will be minimal to the Group. The Bank is continually monitoring developments in the benchmark reform work in jurisdictions affected and will adjust its implementation accordingly, should the need arise.

4. Investments in subsidiaries

		30.6.2020	31.12.2019
Borgun hf., a payment acquirer and issuing processor, Ármúli 30, 108 Reykjavík	Iceland	63.5%	63.5%
B-Payment Group Szolgáltató Zrt., a payment processing company, H-1132 Budapest	Hungary	100%	100%
Borgun-VS ehf., a holding company, Ármúli 30, 108 Reykjavík	Iceland	100%	-
Íslandssjóðir hf., an investment fund management company, Hagasmári 3, 201 Kópavogur	Iceland	100%	100%
Hringur-eignarhaldsfélag ehf., a holding company, Dalshraun 3, 220 Hafnarfjörður	Iceland	100%	100%
Allianz Ísland hf., an insurance agent, Dalshraun 3, 220 Hafnarfjörður	Iceland	100%	100%

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

Borgun hf.

A formal sale process of Borgun hf. began early in 2019, as was announced by Íslandsbanki on 11 January 2019. The sale was an open and transparent process led by Swiss based investment banking firm Corestar Partners and Íslandsbanki's Corporate Finance department.

On 11 March 2020 Íslandsbanki signed an agreement to sell its 63.5% stake in Borgun hf. to Salt Pay Co Ltd. but this transaction was subject to Financial Supervisory Authority ("FME") approval of the purchaser's acquisition of a qualifying holding. The sale was finalised on 7 July 2020. Further information can be found in Note 40.

In accordance with IFRS 5 - Non-current assets and disposal groups held for sale, Borgun hf. has been classified as disposal group held for sale in the interim financial statements, resulting in a change in the presentation. In the statement of financial position total assets of Borgun hf. are recognised in the line item "Non-current assets and disposal groups held for sale" and total liabilities in the line item "Non-current liabilities and disposal groups held for sale". Net loss of Borgun hf. is recognised in profit or loss in the line item "Discontinued operations, net of income tax". The comparative figures in the Consolidated Interim Income Statement for the first half of 2019 have been restated and Borgun hf. is no longer presented separately in the Operating segments note.

Restated Consolidated Interim Income Statement for the first half of 2019	Published accounts	Borgun hf. reclassified	Restated accounts
Interest income	32,570	(447)	32,123
Interest expense	(15,792)	10	(15,782)
Net interest income	16,778	(437)	16,341
Fee and commission income	10,357	(4,490)	5,867
Fee and commission expense	(3,734)	3,272	(462)
Net fee and commission income	6,623	(1,218)	5,405
Net financial income	621	1	622
Net foreign exchange loss	(101)	(35)	(136)
Other operating income	1,173	(5)	1,168
Other net operating income	1,693	(39)	1,654
Total operating income	25,094	(1,694)	23,400
Salaries and related expenses	(8,363)	1,210	(7,153)
Other operating expenses	(6,000)	720	(5,280)
Contribution to the Depositors' and Investors' Guarantee Fund	(510)	-	(510)
Bank tax	(1,814)	-	(1,814)
Total operating expenses	(16,687)	1,930	(14,757)
Profit before net impairment on financial assets	8,407	236	8,643
Net impairment on financial assets	(1,848)	39	(1,809)
Profit before tax	6,559	275	6,834
Income tax expense	(1,779)	(143)	(1,922)
Profit for the period from continuing operations	4,780	132	4,912
Discontinued operations, net of income tax	(71)	(132)	(203)
Profit for the period	4,709	-	4,709

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

4. Cont'd

Interim Income Statement of Borgun hf.	2020 1.1-30.6	2019 1.1-30.6
Net interest income	312	444
Net fee and commission income	800	768
Other operating income	(46)	39
Total operating income	1,066	1,251
Salaries and related expenses	(1,141)	(1,210)
Other operating expenses	(679)	(720)
Net impairment on financial assets	(84)	(39)
Loss before tax	(838)	(718)
Income tax expense	10	143
Loss for the period	(828)	(575)
Inter-company eliminations	193	443
Loss of Borgun hf. included in discontinued operations for the period	(635)	(132)
Amounts included in other comprehensive income for the period		
Changes in fair value of financial assets, net of tax	(913)	893
Total comprehensive income (expense) for the period	(1,548)	761

Interim Statement of Financial Position of Borgun hf.	30.6.2020
Loans to credit institutions	7,123
Bonds and debt instruments	499
Derivatives	69
Loans to customers	4,309
Shares and equity instruments	3,559
Property and equipment	1,293
Intangible assets	445
Other assets	4,531
Total assets	21,828
Inter-company eliminations and other adjustments	(3,682)
Total assets of Borgun hf. included in non-current assets and disposal groups held for sale	18,146
Debt issued and other borrowed funds	266
Tax liabilities	21
Other liabilities	15,301
Total liabilities	15,588
Inter-company eliminations	(268)
Total liabilities of Borgun hf. included in non-current assets and disposal groups held for sale	15,320
Net assets of Borgun hf.	2,826

The following table summarises key cash flows information of Borgun hf. The amounts shown are before inter-company eliminations.	2020 1.1-30.6	2019 1.1-30.6
Net cash used in operating activities	(512)	(2,952)
Net cash (used in) provided by investing activities	(923)	137
Net cash provided (used in) by financing activities	577	(403)
Net decrease in cash and cash equivalents	(858)	(3,218)

Amounts are in ISK million

5. Operating segments

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

Capital allocation to the business units is 16% of the risk exposure amount (REA) which corresponds to the Bank's CET1 target from the risk appetite statement. Income tax with breakdown for each segment is according to the current tax rate. Bank tax and contribution to the Icelandic Depositors' and Investors' Guarantee Fund are shown separately and allocated across segments. The allocation of the bank tax is 0.145%, as stated in law.

The Group comprises the following operating segments:

Personal Banking

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

Business Banking

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

Corporate & Investment Banking

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

Treasury and Proprietary Trading

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

Cost centres

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

Subsidiaries, eliminations and adjustments

Subsidiaries include Borgun hf., Íslandssjóðir hf., Allianz Ísland hf. and other less significant subsidiaries (see Note 4).

The subsidiary Borgun hf. has been classified as non-current assets and disposal groups held for sale, accordingly the comparative figures in this disclosure have been restated. Assets and liabilities of subsidiaries, that are classified as non-current assets and disposal groups held for sale, are included in the column “Other subsidiaries" and all inter-company eliminations for those subsidiaries are included in the column “Eliminations & adjustments".

Following is an overview showing the Group's performance with a breakdown by operating segments. Almost all operational results from cost centres have been allocated to the Bank's operating segments, comparative amounts have not been restated.

Notes to the Condensed Consolidated Interim Financial Statements

5. Cont'd

1 January to 30 June 2020	Personal Banking	Business Banking	Corporate & Investment Banking	Treasury & Proprietary Trading	Cost centres	The Bank total	Subsidiaries, eliminations & adjustments	The Group total
Net interest income	5,426	5,291	4,345	1,831	(118)	16,775	33	16,808
Net fee and commission income	1,489	948	1,784	(46)	(9)	4,166	632	4,798
Other net operating income	305	46	715	(1,794)	137	(591)	(975)	(1,566)
Total operating income	7,220	6,285	6,844	(9)	10	20,350	(310)	20,040
Salaries and related expenses	(1,254)	(982)	(829)	(152)	(3,086)	(6,303)	(391)	(6,694)
Other operating expenses	(1,322)	(621)	(440)	(152)	(2,122)	(4,657)	(212)	(4,869)
Contribution to the Depositors' and Investors' Guarantee Fund	(272)	(156)	(46)	(1)	-	(475)	-	(475)
Bank tax	(248)	(171)	(263)	(68)	(8)	(758)	-	(758)
Net impairment on financial assets	(112)	(4,202)	(1,617)	2	-	(5,929)	-	(5,929)
Cost allocation	(2,399)	(1,457)	(1,556)	181	5,231	-	-	-
Profit (loss) before tax	1,613	(1,304)	2,093	(199)	25	2,228	(913)	1,315
Income tax expense	(484)	294	(613)	(32)	(8)	(843)	(45)	(888)
Profit (loss) for the period from continuing operations	1,129	(1,010)	1,480	(231)	17	1,385	(958)	427
Net segment revenue from external customers	9,988	7,469	10,098	(7,297)	92	20,350	(310)	20,040
Net segment revenue from other segments	(2,768)	(1,184)	(3,254)	7,288	(82)	-	-	-
Fee and commission income	2,311	962	1,816	88	4	5,181	204	5,385
Depreciation, amortisation and write-offs	(198)	(105)	(9)	-	(570)	(882)	(4)	(886)
At 30 June 2020								
Loans to customers	338,523	234,020	360,739	38	-	933,320	-	933,320
Other assets	3,271	2,434	2,294	334,834	11,402	354,235	15,701	369,936
Total segment assets	341,794	236,454	363,033	334,872	11,402	1,287,555	15,701	1,303,256
Deposits from customers	308,158	185,657	146,386	44,640	-	684,841	(3,618)	681,223
Other liabilities	1,184	1,523	5,672	414,365	5,911	428,655	13,656	442,311
Total segment liabilities	309,342	187,180	152,058	459,005	5,911	1,113,496	10,038	1,123,534
Allocated equity	29,034	37,494	61,215	45,379	937	174,059	5,663	179,722
Risk exposure amount	196,375	239,758	399,574	59,642	6,227	901,576	21,557	923,133

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

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

5. Cont'd

1 January to 30 June 2019	Personal Banking	Business Banking	Corporate & Investment Banking	Treasury & Proprietary Trading	Cost centres	The Bank total	Subsidiaries, eliminations & adjustments	The Group total
Net interest income	5,221	5,457	4,205	1,512	(104)	16,291	50	16,341
Net fee and commission income	2,292	815	1,831	(136)	5	4,807	598	5,405
Other net operating income	-	9	210	805	1,241	2,265	(611)	1,654
Total operating income	7,513	6,281	6,246	2,181	1,142	23,363	37	23,400
Salaries and related expenses	(1,422)	(1,024)	(924)	(136)	(3,283)	(6,789)	(364)	(7,153)
Other operating expenses	(1,059)	(585)	(317)	(140)	(2,928)	(5,029)	(251)	(5,280)
Contribution to the Depositors' and Investors' Guarantee Fund	(286)	(174)	(50)	-	-	(510)	-	(510)
Bank tax	(230)	(173)	(254)	(1,149)	(8)	(1,814)	-	(1,814)
Net impairment on financial assets	(348)	(896)	(386)	(180)	-	(1,810)	1	(1,809)
Cost allocation	(2,697)	(1,470)	(1,477)	155	5,489	-	-	-
Profit (loss) before tax	1,471	1,959	2,838	731	412	7,411	(577)	6,834
Income tax expense	(443)	(554)	(804)	98	(109)	(1,812)	(110)	(1,922)
Profit (loss) for the period from continuing operations	1,028	1,405	2,034	829	303	5,599	(687)	4,912
Net segment revenue from external customers	9,020	7,246	9,530	(3,642)	1,209	23,363	37	23,400
Net segment revenue from other segments	(1,507)	(965)	(3,284)	5,823	(67)	-	-	-
Fee and commission income	3,003	821	1,861	36	5	5,726	141	5,867
Depreciation, amortisation and write-offs	(93)	(83)	(12)	-	(531)	(719)	(4)	(723)
At 30 June 2019								
Loans to customers	315,051	235,166	339,629	541	-	890,387	4,059	894,446
Other assets	2,642	3,425	10,451	287,248	11,647	315,413	20,117	335,530
Total segment assets	317,693	238,591	350,080	287,789	11,647	1,205,800	24,176	1,229,976
Deposits from customers	278,061	173,808	111,941	55,350	-	619,160	(3,291)	615,869
Other liabilities	1,094	2,259	9,874	399,045	6,220	418,492	19,831	438,323
Total segment liabilities	279,155	176,067	121,815	454,395	6,220	1,037,652	16,540	1,054,192
Allocated equity	28,769	39,095	58,901	40,833	550	168,148	7,636	175,784
Risk exposure amount	182,433	247,961	378,770	71,100	6,283	886,547	25,237	911,784

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

5. Cont'd

Subsidiaries, eliminations & adjustments

1 January to 30 June 2020	Íslands-sjóðir hf.	Allianz Ísland hf.	Other subsidiaries	Eliminations & adjustments	Total
Net interest income	11	8	14	-	33
Net fee and commission income	583	316	(15)	(252)	632
Other net operating income	20	11	(1)	(1,005)	(975)
Total operating income	614	335	(2)	(1,257)	(310)
Salaries and related expenses	(297)	(94)	-	-	(391)
Other operating expenses	(93)	(190)	(1)	72	(212)
Profit (loss) before tax	224	51	(3)	(1,185)	(913)
Income tax expense	(46)	(10)	-	11	(45)
Profit (loss) for the period from cont. operations	178	41	(3)	(1,174)	(958)
Net segment revenue from external customers	753	267	-	(1,330)	(310)
Net segment revenue from other segments	(139)	68	(2)	73	-
Fee and commission income	822	316	-	(934)	204
Depreciation, amortisation and write-offs	-	-	-	(4)	(4)
At 30 June 2020					
Total assets	1,967	1,365	28,414	(16,045)	15,701
Total liabilities	301	627	15,605	(6,495)	10,038
Total equity	1,666	738	12,809	(9,550)	5,663

1 January to 30 June 2019	Íslands-sjóðir hf.	Allianz Ísland hf.	Other subsidiaries	Eliminations & adjustments	Total
Net interest income	16	14	15	5	50
Net fee and commission income	534	536	(15)	(457)	598
Other net operating income	149	1	2	(763)	(611)
Total operating income	699	551	2	(1,215)	37
Salaries and related expenses	(279)	(85)	-	-	(364)
Other operating expenses	(92)	(226)	(3)	70	(251)
Net impairment on financial assets	-	-	-	1	1
Profit (loss) before tax	328	240	(1)	(1,144)	(577)
Income tax expense	(66)	(48)	-	4	(110)
Profit (loss) for the period from cont. operations	262	192	(1)	(1,140)	(687)
Net segment revenue from external customers	784	549	(16)	(1,280)	37
Net segment revenue from other segments	(85)	2	18	65	-
Fee and commission income	750	536	-	(1,145)	141
Depreciation, amortisation and write-offs	-	-	-	(4)	(4)
At 30 June 2019					
Total assets	2,543	1,065	34,538	(13,970)	24,176
Total liabilities	285	382	20,537	(4,664)	16,540
Total equity	2,258	683	14,001	(9,306)	7,636

Amounts are in ISK million

6. Classification of financial assets and financial liabilities

At 30 June 2020	Mandatorily at FVTPL	Held for hedging	Designated as at FVTPL	Amortised cost	Carrying amount
Cash and balances with Central Bank	-	-	-	103,569	103,569
Loans to credit institutions	-	-	-	70,307	70,307
Listed bonds and debt instruments	118,155	-	-	-	118,155
Listed bonds and debt instruments used for economic hedging	21,777	-	-	-	21,777
Unlisted bonds and debt instruments	490	-	-	-	490
Derivatives	5,344	1,022	-	-	6,366
Loans to customers	-	-	-	933,320	933,320
Listed shares and equity instruments	2,867	-	-	-	2,867
Listed shares and equity instruments used for economic hedging	5,373	-	-	-	5,373
Unlisted shares and equity instruments	2,703	-	-	-	2,703
Other financial assets	-	-	-	6,076	6,076
Total financial assets	156,709	1,022	-	1,113,272	1,271,003
Deposits from Central Bank and credit institutions	-	-	-	35,461	35,461
Deposits from customers	-	-	-	681,223	681,223
Derivative instruments and short positions	7,519	-	-	-	7,519
Debt issued and other borrowed funds	-	47,650	55,570	218,583	321,803
Subordinated loans	-	-	-	25,834	25,834
Other financial liabilities	-	-	-	28,372	28,372
Total financial liabilities	7,519	47,650	55,570	989,473	1,100,212

At 31 December 2019	Mandatorily at FVTPL	Held for hedging	Designated as at FVTPL	Fair value through OCI	Amortised cost	Carrying amount
Cash and balances with Central Bank	-	-	-	-	146,638	146,638
Loans to credit institutions	-	-	-	-	54,376	54,376
Listed bonds and debt instruments	33,302	-	-	-	-	33,302
Listed bonds and debt instruments used for economic hedging	18,220	-	-	-	-	18,220
Unlisted bonds and debt instruments	1,348	-	-	-	-	1,348
Derivatives	4,700	921	-	-	-	5,621
Loans to customers	-	-	-	-	899,632	899,632
Listed shares and equity instruments	3,779	-	-	-	-	3,779
Listed shares and equity instruments used for economic hedging	8,681	-	-	-	-	8,681
Unlisted shares and equity instruments	2,851	-	-	3,115	-	5,966
Other financial assets	-	-	-	-	5,757	5,757
Total financial assets	72,881	921	-	3,115	1,106,403	1,183,320
Deposits from Central Bank and credit institutions	-	-	-	-	30,925	30,925
Deposits from customers	-	-	-	-	618,313	618,313
Derivative instruments and short positions	6,219	-	-	-	-	6,219
Debt issued and other borrowed funds	-	41,816	49,352	-	215,213	306,381
Subordinated loans	-	-	-	-	22,674	22,674
Other financial liabilities	-	-	-	-	24,772	24,772
Total financial liabilities	6,219	41,816	49,352	-	911,897	1,009,284

Amounts are in ISK million

7. Fair value information for financial instruments

Financial instruments carried at fair value

The fair value of a financial instrument is the transaction price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Where a market price is not readily available, the Group applies valuation techniques based on estimates and assumptions that are consistent with that which market participants would use in setting a price for the financial instrument.

The table below shows financial instruments carried at fair value at 30 June 2020 categorised into three levels of fair value hierarchy that reflect the type of inputs used in making the fair value measurements. The different levels have been defined as follows:

Level 1: Inputs that are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Group can access at the measurement date.

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

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

At 30 June 2020	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	139,932	-	490	140,422
Derivatives	-	6,366	-	6,366
Shares and equity instruments	8,133	28	2,782	10,943
Total financial assets	148,065	6,394	3,272	157,731
Short positions	1,532	-	-	1,532
Derivative instruments	-	5,987	-	5,987
Debt issued and other borrowed funds designated as at FVTPL	55,570	-	-	55,570
Total financial liabilities	57,102	5,987	-	63,089

At 31 December 2019	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	51,522	-	1,348	52,870
Derivatives	-	5,621	-	5,621
Shares and equity instruments	12,383	27	6,016	18,426
Total financial assets	63,905	5,648	7,364	76,917
Short positions	814	-	-	814
Derivative instruments	-	5,405	-	5,405
Debt issued and other borrowed funds designated as at FVTPL	49,352	-	-	49,352
Total financial liabilities	50,166	5,405	-	55,571

Changes in Level 3 assets measured at fair value	Bonds and debt instruments	Shares and equity instruments
Fair value at 1 January 2020	1,348	6,016
Purchases	18	7
Net loss on financial instruments recognised in profit or loss	(1,090)	(62)
Transfer to "Non-current assets and disposal groups held for sale"	-	(3,180)
Other changes	214	1
Fair value at 30 June 2020	490	2,782

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

7. Cont'd

	Bonds and debt instruments	Shares and equity instruments
Fair value at 1 January 2019	1,514	4,688
Purchases	7	338
Sales and instalments	(537)	(52)
Net gain (loss) on financial instruments recognised in profit or loss	306	(118)
Net gain on financial instruments recognised in other comprehensive income	-	1,272
Other changes	58	(112)
Fair value at 31 December 2019	1,348	6,016

At the end of each reporting period the Group determines whether transfers have occured between levels in the hierarchy, by reassessing categorisation based on the lowest level input that is significant to the fair value measurement as a whole. No transfers between levels took place in the first half of 2020.

Valuation process

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

Valuation techniques

Where applicable, fair values are determined using quoted prices in active markets for identical assets and liabilities. In other cases, where there is no active market, the fair value is estimated using valuation techniques such as net present value and discounted cash flow models; comparison with similar instruments for which observable market data exists; net asset value (NAV) for investment fund units or expected recovery for distressed bonds. These valuation techniques are based on various assumptions and inputs such as risk-free rate, expected revenue growth and credit and liquidity spreads. In some cases, where significant inputs into these models are not observable, expert judgement and estimation for these inputs are required.

Level 1: Fair value established from quoted market prices.

Assets at this level are financial assets and financial liabilities containing actively traded bonds and equities that are listed either domestically or abroad.

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

Assets at this level are assets and liabilities containing domestic bonds, equities as well as derivatives. For interest rate derivatives contracts such as interest rate swaps (IRS) and cross-currency interest rate swaps (CIRS) the Group calculates the net present value of estimated future cash flows based on yield curves with key inputs such as interest swap rates and forward-rate agreements (FRAs) rates. Foreign-currency forwards and foreign-currency swaps are valued using the FX spot rate adjusted for forward pricing points that can be obtained from market sources. These products are classified as Level 2. Bond forwards and equity forwards are also classified as Level 2 as they are valued using standard models with key inputs observed from stock prices, estimated dividend rates and funding rates.

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

Assets at this level contain primarily unlisted and illiquid equities and bonds. Unlisted equities and bonds are initially recorded at their transaction price but are revalued each quarter based on the models as described above.

The economic crisis relating to the COVID-19 pandemic is the main reason for the decrease in Level 3 assets during the period.

At 30 June 2020 the Group's Level 3 equities amounted to ISK 2,782 million:

-These include shares in seven professional investment funds and investment companies investing in unlisted equities and specialised investments in Iceland totalling ISK 1,018 million. The Group receives information from fund managers which use valuation models for the valuation of these equities.

-Other Level 3 equities amounting to ISK 1,764 million.

-Series C preferred shares in Visa Inc., which Borgun hf. holds, were reclassified as held for sale during the period and transfered to "Non-current assets and disposal groups held for sale".

At 30 June 2020 the Group's Level 3 bonds amounted to ISK 490 million:

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

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

7. Cont'd

Sensitivity analysis for Level 3 assets

The valuations of Level 3 assets are in general uncertain and subject to various factors. The favourable and unfavourable scenarios can be considered as being likely movements in valuation within a year. The very favourable and very unfavourable scenarios are considered less likely, but not impossible and are not worst-case scenarios for some of the assets.

The table below shows how profit (loss) and total comprehensive income would have been affected if one or more of the inputs for fair value measurement in Level 3 were changed.

At 30 June 2020					
Effect on profit or (loss):	Carrying amount	Very favourable	Favourable	Unfavourable	Very unfavour-able
Level 3 Bonds and debt instruments	490	953	502	(470)	(484)
Level 3 Shares and equity instruments	2,782	2,224	651	(669)	(1,026)

At 31 December 2019					
Effect on profit or (loss):	Carrying amount	Very favourable	Favourable	Unfavourable	Very unfavour-able
Level 3 Bonds and debt instruments	1,348	330	257	(296)	(1,348)
Level 3 Shares and equity instruments	2,901	2,399	645	(762)	(1,614)
Effect on comprehensive income:					
Level 3 Shares in Visa Inc.	3,115	1,246	623	(623)	(1,246)

8. Financial instruments not carried at fair value

Assets

The fair value of “Loans to customers” may differ from their net carrying amount because the interest rates they carry may not reflect the interest rates that similar new loans would carry. The fair value is estimated by subtracting from or adding to the net carrying amount of the loans the discounted interest rate difference calculated from the reporting date until the next interest reset or maturity, whichever comes first. Since the interest rate difference is estimated using internal models these assets are classified as Level 3.

For “Cash and balances with Central Bank”, “Loans to credit institutions” and “Other financial assets” the fair value is adequately approximated by the carrying amount as they are short-term in nature. They are thus classified as Level 2.

Liabilities

The fair value of a financial liability with a demand feature, such as a demand deposit, is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid. Most deposits are on demand or carry floating interest rates and as such their carrying amount is considered a good approximation of their fair value. The fair value for longer term fixed rate deposits is calculated with a duration approach, using the difference in each liability's current interest rate from the rate that a similar deposit would carry today. All deposits are classified as Level 2 based on the use of observable market interest rates to estimate the fair value.

Observed market value is used for the fair value of "Debt issued and other borrowed funds" where it is available. Issued bonds and bills with quoted market prices are classified as Level 1. If there is no quoted market price the fair value of the debt is valued in the same manner as deposits if it carries a fixed rate. If the debt carries a floating rate its fair value is estimated by comparing the margin with the Group's current funding premium on similar debt. These liabilities are classified as Level 2. The funding premium is based on the interest margin in the Group's issued papers including covered bonds, commercial papers as well as foreign currency denominated bonds.

Other financial liabilities mainly include unsettled securities transactions, payments due to leasing contracts and liabilities to retailers for credit card provisions and they are classified as Level 2 since their value is not observable from active market prices. Due to the short-term nature of these liabilities their carrying amount is considered a good approximation of their fair value.

The following table shows the fair value measurement and classification of the Group's assets and liabilities not carried at fair value. The different levels are defined in Note 7.

Amounts are in ISK million

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At 30 June 2020	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Cash and balances with Central Bank	-	103,569	-	103,569	103,569
Loans to credit institutions	-	70,307	-	70,307	70,307
Loans to customers	-	-	941,462	941,462	933,320
Other financial assets	-	6,076	-	6,076	6,076
Total financial assets	-	179,952	941,462	1,121,414	1,113,272
Deposits from Central Bank and credit institutions	-	35,690	-	35,690	35,461
Deposits from customers	-	681,614	-	681,614	681,223
Debt issued and other borrowed funds	177,497	102,579	-	280,076	266,233
Subordinated loans	-	23,537	-	23,537	25,834
Other financial liabilities	-	28,372	-	28,372	28,372
Total financial liabilities	177,497	871,792	-	1,049,289	1,037,123

At 31 December 2019	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Cash and balances with Central Bank	-	146,638	-	146,638	146,638
Loans to credit institutions	-	54,376	-	54,376	54,376
Loans to customers	-	-	902,053	902,053	899,632
Other financial assets	-	5,757	-	5,757	5,757
Total financial assets	-	206,771	902,053	1,108,824	1,106,403
Deposits from Central Bank and credit institutions	-	31,027	-	31,027	30,925
Deposits from customers	-	618,592	-	618,592	618,313
Debt issued and other borrowed funds	165,044	100,334	-	265,378	257,029
Subordinated loans	22,626	-	-	22,626	22,674
Other financial liabilities	-	24,772	-	24,772	24,772
Total financial liabilities	187,670	774,725	-	962,395	953,713

9. Offsetting financial assets and financial liabilities

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

	Financial assets subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 30 June 2020	Financial assets before netting	Netting with financial liabilities	Net financial assets	Financial liabilities	Cash collateral received	Financial instruments collateral received	Net amount after consideration of potential effect of netting arrangements	Assets outside the scope of offsetting disclosure requirements	Total financial assets recognised in the balance sheet
Reverse repurchase agreements	1,729	-	1,729	-	-	-	1,729	-	1,729
Derivatives	6,366	-	6,366	(580)	(5,358)	(372)	56	-	6,366
Total assets	8,095	-	8,095	(580)	(5,358)	(372)	1,785	-	8,095

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

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At 31 December 2019	Financial assets subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
	Financial assets before netting	Netting with financial liabilities	Net financial assets	Financial liabilities	Cash collateral received	Financial instruments collateral received	Net amount after consideration of potential effect of netting arrangements	Assets outside the scope of offsetting disclosure requirements	Total financial assets recognised in the balance sheet
Reverse repurchase agreements ..	1,114	-	1,114	-	-	-	1,114	-	1,114
Derivatives	5,621	-	5,621	(1,374)	(3,146)	(88)	1,013	-	5,621
Total assets	6,735	-	6,735	(1,374)	(3,146)	(88)	2,127	-	6,735

	Financial liabilities subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 30 June 2020	Financial liabilities before netting	Netting with financial assets	Net financial liabilities	Financial assets	Cash collateral pledged	Financial instruments collateral pledged	Net amount after consideration of potential effect of netting arrangements	Liabilities outside the scope of offsetting disclosure requirements	Total financial liabilities recognised in the balance sheet
Derivative instruments and short positions	7,519	-	7,519	(580)	(1,673)	-	5,266	-	7,519
At 31 December 2019									
Derivative instruments and short positions	6,219	-	6,219	(1,374)	(1,139)	-	3,706	-	6,219

10. Quarterly statements

	2020 Q2	2020 Q1	2019 Q4	2019 Q3	2019 Q2
Net interest income	8,228	8,580	8,291	8,190	8,404
Net fee and commission income	2,307	2,491	2,945	2,549	2,758
Net financial income (expense)	(181)	(1,738)	(840)	(602)	180
Net foreign exchange gain (loss)	208	55	116	159	(15)
Other operating income	71	19	920	37	27
Salaries and related expenses	(3,447)	(3,247)	(3,624)	(3,242)	(3,689)
Other operating expenses	(2,424)	(2,445)	(2,823)	(2,366)	(2,531)
Contribution to the Depositors' and Investors' Guarantee Fund	(247)	(228)	(216)	(210)	(198)
Bank tax	(399)	(359)	(814)	(900)	(934)
Net impairment on financial assets	(2,439)	(3,490)	(1,463)	(208)	(902)
Profit (loss) before tax	1,677	(362)	2,492	3,407	3,100
Income tax expense	(119)	(769)	(659)	(1,328)	(726)
Profit (loss) for the period from continuing operations	1,558	(1,131)	1,833	2,079	2,374
Discontinued operations, net of income tax	(313)	(245)	(174)	7	(254)
Profit (loss) for the period	1,245	(1,376)	1,659	2,086	2,120

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Notes to the Condensed Consolidated Interim Financial Statements

11. Net interest income

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Cash and balances with Central Bank	1,410	2,450	408	1,184
Loans at amortised cost	26,116	28,370	14,026	15,208
Financial assets mandatorily at fair value through profit or loss	1,070	1,281	519	713
Other assets	2	22	-	12
Total interest income	28,598	32,123	14,953	17,117
Deposits from Central Bank and credit institutions	(420)	(229)	(199)	(122)
Deposits from customers	(4,699)	(8,703)	(2,236)	(4,660)
Debt issued and other borrowed funds at fair value through profit or loss	(296)	(374)	(154)	(194)
Debt issued and other borrowed funds at amortised cost	(5,374)	(5,133)	(3,327)	(2,914)
Subordinated loans	(359)	(173)	(193)	(93)
Other interest expense*	(642)	(1,170)	(616)	(730)
Total interest expense	(11,790)	(15,782)	(6,725)	(8,713)
Net interest income	16,808	16,341	8,228	8,404

*Thereof is lease liabilities' interest expense amounting to ISK 44 million (2019: ISK 47 million).

12. Net fee and commission income

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Asset management	1,170	1,123	605	575
Investment banking and brokerage	1,147	1,144	576	613
Payment processing	1,600	1,876	786	1,046
Loans and guarantees	810	754	427	376
Other fee and commission income	658	970	228	385
Total fee and commission income	5,385	5,867	2,622	2,995
Brokerage	(166)	(144)	(113)	(75)
Clearing and settlement	(421)	(308)	(202)	(174)
Other fee and commission expense	-	(10)	-	12
Total fee and commission expense	(587)	(462)	(315)	(237)
Net fee and commission income	4,798	5,405	2,307	2,758

Fee and commission income by segment is disclosed in Note 5.

13. Net financial income (expense)

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Net gain (loss) on financial assets and liabilities mandatorily at FVTPL	(1,548)	877	180	379
Net loss on financial liabilities designated as at FVTPL	(372)	(259)	(366)	(215)
Net gain on fair value hedges	1	4	5	16
Net financial income (expense)	(1,919)	622	(181)	180

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

14. Net foreign exchange gain (loss)

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Cash and balances with Central Bank	176	(3)	(1)	(12)
Financial assets mandatorily at fair value through profit or loss	5,836	900	4,458	1,099
Loans at amortised cost	29,451	14,114	(299)	5,798
Other assets	11	2	(8)	1
Net foreign exchange gain for assets	35,474	15,013	4,150	6,886
Deposits	(13,229)	(5,134)	476	(1,520)
Debt issued and other borrowed funds designated as at FVTPL	(7,098)	(4,706)	(14)	(2,518)
Debt issued and other borrowed funds at amortised cost	(11,730)	(4,777)	(3,030)	(2,577)
Subordinated loans	(3,154)	(532)	(1,374)	(286)
Net foreign exchange loss for liabilities	(35,211)	(15,149)	(3,942)	(6,901)
Net foreign exchange gain (loss)	263	(136)	208	(15)

15. Other operating income

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Share of profit of associates, net of income tax	19	5	38	5
Net loss from sale of subsidiaries	-	(16)	-	(16)
Legal dispute settlement	-	1,103	-	-
Legal fees	40	43	18	23
Rental income	20	19	10	9
Other net operating income	11	14	5	6
Other operating income	90	1,168	71	27

16. Salaries and related expenses

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Salaries	5,158	5,515	2,654	2,842
Contributions to pension funds	768	825	406	425
Social security charges and financial activities tax*	716	759	359	390
Other salary-related expenses	52	54	28	32
Salaries and related expenses	6,694	7,153	3,447	3,689

*Financial activities tax calculated on salaries is 5.5% (2019: 5.5%).

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

17. Other operating expenses

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Professional services	760	917	348	415
Software and IT expenses	2,230	2,399	1,130	1,219
Real estate and office equipment	275	294	139	144
Depreciation, amortisation and write-offs	886	723	524	362
Other administrative expenses	718	947	283	391
Other operating expenses	4,869	5,280	2,424	2,531

18. Net impairment on financial assets

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Expected credit loss, on-balance sheet items*	(5,743)	(1,762)	(2,404)	(854)
Expected credit loss, off-balance sheet items	(186)	(41)	(35)	(48)
Changes in provision due to court rulings	-	(6)	-	-
Net impairment on financial assets	(5,929)	(1,809)	(2,439)	(902)

*The main reasons for the additional expected credit loss allowance are: an increase related to COVID-19 pandemic (ISK 4,450 million), and an increased expected credit loss for a few customers (ISK 700 million). For further information see Note 2.

19. Income tax expense

Recognised income tax is based on applicable tax laws. The income tax rate for legal entities in 2020 is 20% (2019: 20%). Special financial activities tax is calculated as 6% of taxable profits exceeding ISK 1 billion in accordance with the Act on Financial Activities Tax no. 165/2011. The effective income tax rate in the Group's income statement for the first half 2020 is 67.5% (2019: 28%).

	2020 1.1-30.6	2019 1.1-30.6
Current tax expense excluding discontinued operations	1,120	1,267
Special financial activities tax	248	283
Difference in prior year's calculated income tax	14	(7)
Changes in deferred tax assets and deferred tax liabilities	(494)	379
Income tax recognised in the income statement	888	1,922
Income tax recognised in other comprehensive income	-	(157)

	2020 1.1-30.6		2019 1.1-30.6	
Profit before tax	1,315		6,834	
20% income tax calculated on the profit for the period	263	20.0%	1,367	20.0%
Special financial activities tax	248	18.8%	283	4.1%
Expenses (income) not subject to tax	185	14.1%	(212)	(3.1%)
Non-deductible expenses	152	11.6%	365	5.3%
Other differences	40	3.0%	119	1.7%
Effective income tax expense	888	67.5%	1,922	28.0%

The Bank is taxed jointly with its subsidiary Íslandssjóðir hf.

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

20. Discontinued operations, net of income tax

	2020 1.1-30.6	2019 1.1-30.6	2020 1.4-30.6	2019 1.4-30.6
Net profit (loss) from foreclosed assets	(36)	(42)	11	(41)
Net loss from disposal groups held for sale*	(538)	(169)	(321)	(221)
Income tax expense	16	8	(3)	8
Discontinued operations, net of income tax	(558)	(203)	(313)	(254)

*Thereof is loss from Borgun hf. amounting to ISK 635 million. For further information see Note 4.

21. Earnings per share

	Discontinued operations			
	Excluded		Included	
	2020 1.1-30.6	2019 1.1-30.6	2020 1.1-30.6	2019 1.1-30.6
Profit attributable to shareholders of the Bank	729	5,122	171	4,919
Weighted average number of outstanding shares	10,000	10,000	10,000	10,000
Basic earnings per share	0.07	0.51	0.02	0.49

The Group's basic and diluted earnings per share are equal as the Group has not issued any options, warrants, convertibles, or other financial instruments that dilute earnings per share (2019: none).

22. Cash and balances with Central Bank

	30.6.2020	31.12.2019
Cash on hand	4,121	4,403
Balances with Central Bank	90,439	126,956
Balances with Central Bank subject to special restrictions*	1,349	1,679
Included in cash and cash equivalents	95,909	133,038
Mandatory reserve deposits with Central Bank	7,660	13,600
Cash and balances with Central Bank	103,569	146,638

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

23. Loans to credit institutions

	30.6.2020	31.12.2019
Money market loans	35,869	33,254
Bank accounts	34,382	21,122
Other loans	56	-
Loans to credit institutions	70,307	54,376

Amounts are in ISK million

24. Derivative instruments and short positions

At 30 June 2020	Assets	Notional values related to assets	Liabilities	Notional values related to liabilities
Interest rate swaps	1,777	134,699	3,621	66,576
Cross-currency interest rate swaps	2,514	57,942	227	10,611
Equity forwards	247	2,919	377	2,382
Foreign exchange forwards	658	10,069	5	383
Foreign exchange swaps	1,136	34,553	1,197	21,539
Bond forwards	34	3,603	560	21,098
Derivatives	6,366	243,785	5,987	122,589
Short positions in listed bonds	-	-	1,532	1,217
Total	6,366	243,785	7,519	123,806

At 31 December 2019				
Interest rate swaps	1,254	114,393	3,575	96,212
Cross-currency interest rate swaps	3,015	91,950	880	13,073
Equity forwards	141	4,664	298	4,001
Foreign exchange forwards	212	5,460	321	10,217
Foreign exchange swaps	867	30,990	298	24,928
Bond forwards	132	12,756	33	6,219
Derivatives	5,621	260,213	5,405	154,650
Short positions in listed bonds	-	-	814	734
Total	5,621	260,213	6,219	155,384

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

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

The Group applies hedge accounting only with respect to certain EUR denominated interest rate swaps, whereby the Group pays floating rate interest and receives fixed rate interest. The interest rate swaps are hedging the exposure of changes in the fair value of certain fixed-rate EUR denominated bonds (see Note 33) arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 30 June 2020 the total fair value of the interest rate swaps was positive and amounted to ISK 1,022 million (2019: ISK 921 million) and their total notional amount was ISK 46,620 million (2019: ISK 40,749).

Amounts are in ISK million

25. Loans to customers

At 30 June 2020	Gross carrying amount			Expected credit loss			Net carrying
	Stage 1	Stage 2	Stage 3	Stage 1	Stage 2	Stage 3	amount
Individuals	342,835	6,563	8,483	(1,200)	(194)	(963)	355,524
Commerce and services	59,752	61,792	6,528	(553)	(2,260)	(2,678)	122,581
Construction	40,530	1,009	5,618	(315)	(46)	(333)	46,463
Energy	8,380	-	-	(36)	-	-	8,344
Financial services	2,240	-	-	(1)	-	-	2,239
Industrial and transportation	52,271	29,793	4,107	(259)	(522)	(1,659)	83,731
Investment companies	16,808	4,605	4,055	(186)	(398)	(306)	24,578
Public sector and non-profit organisations	11,637	15	14	(21)	-	(4)	11,641
Real estate	125,582	22,409	5,111	(491)	(970)	(1,551)	150,090
Seafood	126,973	1,208	381	(234)	(5)	(194)	128,129
Loans to customers	787,008	127,394	34,297	(3,296)	(4,395)	(7,688)	933,320

At 31 December 2019							
Individuals	338,335	4,119	9,362	(1,319)	(168)	(1,148)	349,181
Commerce and services	115,679	6,999	6,515	(739)	(194)	(1,772)	126,488
Construction	39,248	849	4,924	(310)	(53)	(238)	44,420
Energy	7,913	-	-	(26)	-	-	7,887
Financial services	2,315	-	-	-	-	-	2,315
Industrial and transportation	77,492	3,338	3,503	(278)	(221)	(1,546)	82,288
Investment companies	19,542	4,369	265	(260)	(216)	(110)	23,590
Public sector and non-profit organisations	12,279	44	15	(23)	(2)	(1)	12,312
Real estate	140,604	3,831	2,345	(542)	(89)	(590)	145,559
Seafood	105,411	249	385	(148)	(10)	(295)	105,592
Loans to customers	858,818	23,798	27,314	(3,645)	(953)	(5,700)	899,632

26. Expected credit loss

Total allowances for expected credit losses

	Stage 1	Stage 2	Stage 3	Total
Cash and balances with Central Bank	3	-	-	3
Loans to credit institutions	98	-	-	98
Loans to customers	3,296	4,395	7,688	15,379
Other financial assets	5	3	-	8
Off-balance sheet loan commitments and financial guarantees	368	301	206	875
At 30 June 2020	3,770	4,699	7,894	16,363
Cash and balances with Central Bank	4	-	-	4
Loans to credit institutions	67	-	-	67
Loans to customers	3,645	953	5,700	10,298
Other financial assets	9	3	86	98
Off-balance sheet loan commitments and financial guarantees	403	55	231	689
At 31 December 2019	4,128	1,011	6,017	11,156

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26. Cont'd

The following tables reconcile the opening and closing balances for accumulated expected credit losses for loans to customers and off-balance sheet loan commitments and financial guarantees.

Loans to customers

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2020	3,645	953	5,700	10,298
Transfer to Stage 1	2,037	(1,901)	(136)	-
Transfer to Stage 2	(1,233)	1,651	(418)	-
Transfer to Stage 3	(93)	(560)	653	-
Transfer to "Non-current assets and disposal groups held for sale"	(50)	(12)	(83)	(145)
Net remeasurement of loss allowance	(1,517)	4,122	2,276	4,881
New financial assets originated or purchased	837	193	130	1,160
Derecognitions and maturities	(330)	(51)	(78)	(459)
Write-offs	-	-	(721)	(721)
Recoveries of amounts previously written off	-	-	104	104
Foreign exchange	-	-	60	60
Unwinding of interests	-	-	201	201
At 30 June 2020	3,296	4,395	7,688	15,379
At 1 January 2019	3,277	1,079	3,689	8,045
Transfer to Stage 1	1,725	(1,343)	(382)	-
Transfer to Stage 2	(1,336)	1,687	(351)	-
Transfer to Stage 3	(178)	(720)	898	-
Net remeasurement of loss allowance	(1,216)	145	2,727	1,656
New financial assets originated or purchased	1,803	278	353	2,434
Derecognitions and maturities	(430)	(169)	(188)	(787)
Write-offs	-	(4)	(1,616)	(1,620)
Recoveries of amounts previously written off	-	-	249	249
Foreign exchange	-	-	10	10
Unwinding of interests	-	-	311	311
At 31 December 2019	3,645	953	5,700	10,298

Off-balance sheet loan commitments and financial guarantees

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2020	403	55	231	689
Transfer to Stage 1	25	(9)	(16)	-
Transfer to Stage 2	(40)	153	(113)	-
Transfer to Stage 3	(5)	(29)	34	-
Net remeasurement of loss allowance	(184)	106	32	(46)
New loan commitments and financial guarantees	231	33	75	339
Derecognitions and maturities	(62)	(8)	(37)	(107)
At 30 June 2020	368	301	206	875
At 1 January 2019	410	142	84	636
Transfer to Stage 1	152	(81)	(71)	-
Transfer to Stage 2	(20)	39	(19)	-
Transfer to Stage 3	(9)	(18)	27	-
Net remeasurement of loss allowance	(455)	(27)	131	(351)
New loan commitments and financial guarantees	447	20	119	586
Derecognitions and maturities	(122)	(20)	(40)	(182)
At 31 December 2019	403	55	231	689

Financial Statements first half 2020 33 Amounts are in ISK million

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27. Property and equipment

At 30 June 2020	Land and buildings	Right-of-use assets: Buildings	Fixtures, equipment & vehicles	Total
Balance at the beginning of the year	4,096	4,634	4,068	12,798
Additions during the period	11	-	346	357
Disposals and write-offs during the period	(120)	(69)	(459)	(648)
Remeasurement	-	63	-	63
Transfer to "Non-current assets and disposal groups held for sale"	(953)	(20)	(807)	(1,780)
Historical cost	3,034	4,608	3,148	10,790
Balance at the beginning of the year	(1,447)	(420)	(1,763)	(3,630)
Depreciation during the period	(12)	(234)	(200)	(446)
Disposals and write-offs during the period	17	(13)	333	337
Transfer to "Non-current assets and disposal groups held for sale"	109	2	387	498
Accumulated depreciation	(1,333)	(665)	(1,243)	(3,241)
Carrying amount	1,701	3,943	1,905	7,549
Annual deprecion rates	0-2%	8-31%	8-35%	
Official real estate value of land and buildings				1,547
Insurance value of buildings				2,562
Insurance value of fixtures, equipment and vehicles				3,069

At 31 December 2019	Land and buildings	Right-of-use assets: Land, buildings & vehicles	Fixtures, equipment & vehicles	Total
Balance at the beginning of the year	4,054	-	3,984	8,038
Impact of adopting IFRS 16	-	4,505	-	4,505
Additions during the year	56	3	271	330
Disposals and write-offs during the year	(14)	-	(187)	(201)
Remeasurement	-	126	-	126
Historical cost	4,096	4,634	4,068	12,798
Balance at the beginning of the year	(1,402)	-	(1,365)	(2,767)
Depreciation during the year	(47)	(420)	(574)	(1,041)
Disposals and write-offs during the year	2	-	176	178
Accumulated depreciation	(1,447)	(420)	(1,763)	(3,630)
Carrying amount	2,649	4,214	2,305	9,168
Annual deprecion rates	0-2%	3-33%	8-35%	
Official real estate value of land and buildings				2,240
Insurance value of buildings				3,545
Insurance value of fixtures, equipment and vehicles				3,429

Amounts are in ISK million

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28. Other assets

	30.6.2020	31.12.2019
Receivables	1,066	4,810
Unsettled securities transactions	4,500	279
Accruals	201	253
Prepaid expenses	346	468
Deferred tax assets	88	476
Other assets	169	322
Other assets	6,370	6,608

29. Non-current assets and disposal groups held for sale

	30.6.2020	31.12.2019
Assets of disposal groups classified as held for sale:		
Borgun hf.	18,146	-
Miðengi ehf.	327	292
Repossessed collateral:		
Land and buildings	1,506	739
Industrial equipment and vehicles	14	44
Non-current assets and disposal groups held for sale	19,993	1,075
Borgun hf.	15,320	-
Miðengi ehf.	1	-
Non-current liabilities and disposal groups held for sale	15,321	-

For further information about Borgun hf. see Note 4.

30. Deposits from Central Bank and credit institutions

	30.6.2020	31.12.2019
Deposits from credit institutions	35,387	30,808
Repurchase agreements with Central Bank	74	117
Deposits from Central Bank and credit institutions	35,461	30,925

31. Deposits from customers

	30.6.2020	31.12.2019
Demand deposits and deposits with maturity up to 3 months	578,432	530,960
Term deposits with maturity of more than 3 months	102,791	87,353
Deposits from customers	681,223	618,313

Deposits from customers specified by owners	30.6.2020		31.12.2019	
	Amount	% of total	Amount	% of total
Central government and state-owned enterprises	10,361	2%	12,553	2%
Municipalities	8,915	1%	5,619	1%
Companies	343,657	50%	299,204	48%
Individuals	318,290	47%	300,937	49%
Deposits from customers	681,223	100%	618,313	100%

Amounts are in ISK million

32. Pledged assets

	30.6.2020	31.12.2019
Financial assets pledged as collateral against liabilities	212,415	205,773
Financial assets pledged as collateral in foreign banks	220	402
Financial assets pledged as collateral in repurchase agreements	1,729	1,114
Pledged assets against liabilities	214,364	207,289

The Group has pledged assets against the issuance of covered bonds under Icelandic law, which are pledged on a pool of consumer mortgage loans.

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

33. Debt issued and other borrowed funds

	Issued	Maturity		Interest	30.6.2020	31.12.2019
Covered bonds in ISK	2019	2021	At maturity	Fixed rates	5,103	3,918
Covered bonds in ISK	2015-2019	2023	At maturity	Fixed rates	23,406	20,170
Covered bonds in ISK - CPI-linked	2014-2015	2020	At maturity	Fixed rates	-	4,359
Covered bonds in ISK - CPI-linked	2015-2017	2022	At maturity	Fixed rates	18,855	18,512
Covered bonds in ISK - CPI-linked	2012-2018	2024	At maturity	Fixed rates	36,205	35,752
Covered bonds in ISK - CPI-linked	2015-2018	2026	At maturity	Fixed rates	28,061	27,661
Covered bonds in ISK - CPI-linked	2019	2028	Amortising	Fixed rates	17,935	14,228
Covered bonds in ISK - CPI-linked	2017-2018	2030	At maturity	Fixed rates	25,824	25,463
Covered bonds					155,389	150,063
Senior unsecured bonds in EUR**	2016	2020	At maturity	Fixed rates	8,912	7,782
Senior unsecured bonds in SEK*	2019	2020	At maturity	Floating rates	-	4,557
Senior unsecured bonds in SEK	2018	2021	At maturity	Fixed rates	1,485	1,308
Senior unsecured bonds in SEK*	2018-2019	2021	At maturity	Floating rates	20,430	18,913
Senior unsecured bonds in EUR	2019	2021	At maturity	Floating rates	1,785	1,559
Senior unsecured bonds in SEK	2018	2022	At maturity	Floating rates	14,809	12,990
Senior unsecured bonds in EUR**	2019	2022	At maturity	Fixed rates	46,658	41,570
Senior unsecured bonds in NOK	2019	2022	At maturity	Floating rates	14,304	13,856
Senior unsecured bonds in EUR***	2018	2024	At maturity	Fixed rates	47,650	41,816
Senior unsecured bonds in NOK	2019	2024	At maturity	Fixed rates	5,792	5,709
Senior unsecured bonds in ISK	2019	2024	Monthly	Floating rates	3,181	3,553
Bonds issued					165,006	153,613
Bills issued					1,408	2,705
Other borrowed funds					1,408	2,705
Debt issued and other borrowed funds					321,803	306,381

*The Bank repurchased own bonds during the period amounting to ISK 6,084 million.

**These bond issuances are classified as being designated as at fair value through profit or loss. At 30 June 2020 the total carrying amount of the bonds amounted to ISK 55,570 million and included in the amount are fair value changes amounting to ISK 333 million. The carrying amount of the bond at 30 June 2020 was ISK 474 million lower than the contractual amount due at maturity.

Amounts are in ISK million

33. Cont'd

***The Group applies hedge accounting to this bond issuance and uses certain EUR denominated interest rate swaps as hedging instruments (see Note 24). The interest rate swaps are hedging the exposure of the Group's changes in the fair value of this fixed-rate EUR denominated bond arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 30 June 2020 the total carrying amount of the bond issuance amounted to ISK 47,650 million and included in the amount are fair value changes amounting to ISK 937 million.

The Bank has issued additional covered bonds to hold for the purpose of securities lending with regards to market making agreements. These covered bond amounts are not included in the total.

34. Subordinated loans

	Issued	Maturity		Interest	30.6.2020	31.12.2019
Loans which qualify as Tier 2 capital:						
Subordinated loans in SEK	2017	2027	At maturity	Floating, STIBOR + 2.0%	11,071	9,714
Subordinated loans in SEK	2018	2028	At maturity	Floating, STIBOR + 2.5%	7,391	6,485
Subordinated loans in SEK	2019	2029	At maturity	Floating, STIBOR + 3.9%	7,372	6,475
Subordinated loans					25,834	22,674

35. Changes in liabilities arising from financing activities

			Non-cash changes			
	1.1.2020	Cash flows	Interest expense	Foreign exchange	Fair value changes	30.6.2020
Covered bonds in ISK	24,088	3,710	711	-	-	28,509
Covered bonds in ISK - CPI-linked	125,975	(2,856)	3,761	-	-	126,880
Senior unsecured bonds in ISK	3,553	(419)	47	-	-	3,181
Senior unsecured bonds FX	58,892	(6,708)	550	5,871	-	58,605
Senior unsecured bonds FX at fair value	49,352	(524)	296	7,098	(652)	55,570
Senior unsecured bonds used for hedging	41,816	(463)	272	5,859	166	47,650
Other borrowed funds	2,705	(1,330)	33	-	-	1,408
Subordinated loans	22,674	(353)	359	3,154	-	25,834
Total	329,055	(8,943)	6,029	21,982	(486)	347,637

			Non-cash changes			
	1.1.2019	Cash flows	Interest expense	Foreign exchange	Fair value changes	31.12.2019
Covered bonds in ISK	20,756	2,060	1,272	-	-	24,088
Covered bonds in ISK - CPI-linked	118,057	1,263	6,655	-	-	125,975
Senior unsecured bonds in ISK	-	3,528	25	-	-	3,553
Senior unsecured bonds FX	46,162	12,139	1,016	(425)	-	58,892
Senior unsecured bonds FX at fair value	68,154	(22,509)	734	1,667	1,306	49,352
Senior unsecured bonds used for hedging	40,714	(465)	497	786	284	41,816
Other borrowed funds	7,133	(4,809)	358	23	-	2,705
Subordinated loans	16,216	6,190	501	(233)	-	22,674
Total	317,192	(2,603)	11,058	1,818	1,590	329,055

Amounts are in ISK million

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36. Other liabilities

	30.6.2020	31.12.2019
Accruals	2,883	3,217
Liabilities to retailers for credit cards	-	14,765
Lease liabilities	4,036	4,256
Provision for effects of court rulings	75	75
Expected credit loss for off-balance sheet loan commitments and financial guarantees	875	689
Withholding tax	591	1,559
Unsettled securities transactions	19,360	515
Deferred income	-	229
Sundry liabilities	2,115	1,758
Other liabilities	29,935	27,063

37. Custody assets

	30.6.2020	31.12.2019
Custody assets - not managed by the Group	3,012,518	2,898,686

38. Related party

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

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

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

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

Cash and balances with the Central Bank are disclosed under Note 22 and Deposits from the Central Bank are disclosed under Note 30.

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

At 30 June 2020	Assets	Liabilities	Net balance	Commitments, guarantees & overdrafts
Shareholders with control over the Group	-	-	-	1
Board of Directors, key management personnel and other related parties	221	613	(392)	51
Associated companies	13	750	(737)	211
Balances with related parties	234	1,363	(1,129)	263

1 January to 30 June 2020	Interest income	Interest expense	Other income	Other expense
Board of Directors, key management personnel and other related parties	2	5	1	-
Associated companies	-	5	-	776
Transactions with related parties	2	10	1	776

Amounts are in ISK million

38. Cont'd

At 31 December 2019	Assets	Liabilities	Net balance	Commitments, guarantees & overdrafts
Board of Directors, key management personnel and other related parties	324	392	(68)	51
Associated companies	16	830	(814)	213
Balances with related parties	340	1,222	(882)	264

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

At 30 June 2020 ISK 1 million was recognised as Stage 1 expected credit loss against balances outstanding with related parties (2019: ISK 2 million). No share option programmes were operated during the reporting period.

39. Contingencies

Contingent liabilities

Borgun hf. – Landsbanki case

Borgun hf., a subsidiary of Íslandsbanki, is a payment acquirer and issuing processor. Landsbankinn hf. sold its 31.2% stake in Borgun hf. in late 2014. Landsbankinn claims that Borgun's management did not disclose all available information that might have affected the value of Borgun hf. during the sales process, namely the worth of its stake in Visa Europe which was sold to Visa International shortly after the Borgun hf. sale. In order to reclaim the alleged loss, Landsbankinn filed a lawsuit against Borgun hf. and others on 12 January 2017, claiming the right to damages for having been deprived of the true value of the stake involved in the sale. Landsbankinn does not quantify the claim, but its estimate of the lost profit from having sold its shares in Borgun hf. is approximately ISK 1,930 million. Court appointed surveyors presented their assessment in November 2019. A reassessment has been demanded. It is uncertain when a ruling is to be expected.

In March 2020 the Group entered into an agreement on the sale of all its stake in Borgun hf. subject to closing. Íslandsbanki has undertaken to reimburse up to 63.47% of losses incurred by Borgun hf. or the buyer as a result of the claim by Landsbankinn.

Seeing that the conclusion of the case is uncertain and the financial effect cannot be estimated the Group has not recognised a provision in relation to this matter.

Borgun hf. – Chargeback risk

Chargeback risk, is a risk that Borgun hf. faces when merchants have been paid and claims occur from third parties (e.g. cardholders). This can occur when the merchant can't provide the sold services or goods, e.g. due to the effects of the COVID-19 pandemic.

Merchants' turnover, chargeback rates and other factors are closely monitored. Borgun hf. assesses the chargeback risk for each seller. The assessment takes into account the type of transaction, business history and other factors. Borgun hf. has procedures, internal rules and processes that aim to limit chargeback risk. Merchants' status and payments are monitored to reduce the possible financial loss of Borgun hf. if the sellers are unable to fulfil their obligations. Borgun hf. has estimated that the chargeback risk can vary from ISK 200 million to ISK 1,000 million. The Group has not recognised a provision in relation to the chargeback risk.

The sale of Borgun hf. was closed on 7 July 2020 and the Group's shares in Borgun hf. delivered to the buyer. The transaction is further described in Note 40.

Amounts are in ISK million

40. Events after the reporting period

On 7 July 2020 the Bank concluded the sale of its 63.5% holding in Borgun hf. to Salt Pay Co Ltd. In the interim financial statements for the first half of 2020, Borgun hf. is accounted for as an asset held for sale and comparative figures have been restated accordingly. The sale of Borgun hf. will be accounted for in the interim financial statements for the third quarter of 2020 with limited impact on the Bank's operations and capital position. By the share capital decrease in Borgun hf. in July 2020 the Bank's ownership in Borgun-VS ehf., a recently founded limited liability company, remains 63.5%. The main asset of Borgun-VS ehf. are the Series C preferred shares in Visa Inc., (related to the acquisition by Visa Inc. of Visa Europe in 2016), and rights and economic value related thereto.

41. Risk management

Risk governance

The Group is exposed to various risk factors and managing these risks is an integral part of its operations. More information about the Group's risk management and risk assessment processes is available in the unaudited Pillar 3 2019 Report, which is available on the Bank's website: www.islandsbanki.is.

42. Credit risk

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

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

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

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

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

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

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43. Maximum credit exposure

The Group's credit risk exposure comprises both on-balance sheet and off-balance sheet items. Maximum exposure to credit risk for on-balance sheet assets is the net carrying amount as reported in the statement of financial position. The maximum exposure for off-balance sheet items is the amount that the Group might have to pay out against financial guarantees and loan commitments, less provisions that have been made because of these items. The maximum credit exposure for a derivative contract is calculated by adding potential future credit exposure to the positive market value of the contract.

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

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

At 30 June 2020	Individuals	Central governments	Commerce and services	Construction	Energy	Financial services	Industrial and transportation	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	103,569	-	-	-	-	-	-	-	-	-	103,569
Loans to credit institutions	-	-	-	-	-	70,307	-	-	-	-	-	70,307
Bonds and debt instruments	-	119,418	18	-	516	18,374	446	25	1,501	124	-	140,422
Derivatives	-	-	74	-	7	7,690	711	546	-	242	396	9,666
Loans to customers:	355,524	-	122,581	46,463	8,344	2,239	83,731	24,578	11,641	150,090	128,129	933,320
Overdrafts	11,382	-	13,014	4,120	21	1,790	7,378	693	738	2,745	5,632	47,513
Credit cards	14,797	-	1,151	232	4	11	333	22	70	56	28	16,704
Mortgages	293,838	-	-	-	-	-	-	-	-	-	-	293,838
Capital leases	5,762	-	27,890	2,801	14	-	7,273	153	35	928	183	45,039
Other loans	29,745	-	80,526	39,310	8,305	438	68,747	23,710	10,798	146,361	122,286	530,226
Other financial assets	364	7	222	3	23	5,125	162	71	73	19	7	6,076
Off-balance sheet items:	38,256	-	25,302	14,160	488	6,311	16,358	543	4,773	15,484	11,426	133,101
Financial guarantees	1,507	-	5,551	5,280	-	1,234	2,761	39	6	1,959	272	18,609
Undrawn loan commitments	-	-	1,688	5,751	176	-	7,410	-	-	7,937	3,407	26,369
Undrawn overdrafts	13,088	-	13,711	2,367	282	4,947	5,061	352	4,023	5,308	7,579	56,718
Credit card commitments	23,661	-	4,352	762	30	130	1,126	152	744	280	168	31,405
Maximum credit exposure	394,144	222,994	148,197	60,626	9,378	110,046	101,408	25,763	17,988	165,959	139,958	1,396,461

Amounts are in ISK million

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43. Cont'd

At 31 December 2019	Individuals	Central governments	Commerce and services	Construction	Energy	Financial services	Industrial and transportation	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	146,638	-	-	-	-	-	-	-	-	-	146,638
Loans to credit institutions	-	-	-	-	-	54,376	-	-	-	-	-	54,376
Bonds and debt instruments	-	33,007	-	-	125	16,131	1,296	52	1,027	1,232	-	52,870
Derivatives	-	-	706	-	1,836	5,788	189	530	-	208	228	9,485
Loans to customers:	349,181	-	126,488	44,420	7,887	2,315	82,288	23,590	12,312	145,559	105,592	899,632
Overdrafts	12,333	-	14,506	3,425	110	2,289	4,927	654	1,204	3,220	6,270	48,938
Credit cards	16,466	-	1,579	271	5	24	437	40	106	63	35	19,026
Mortgages	281,450	-	5	-	-	-	-	-	-	44	-	281,499
Capital leases	5,774	-	28,422	2,700	15	-	7,322	139	39	1,005	207	45,623
Other loans	33,158	-	81,976	38,024	7,757	2	69,602	22,757	10,963	141,227	99,080	504,546
Other financial assets	532	-	199	7	6	4,803	117	41	10	36	6	5,757
Off-balance sheet items:	33,964	-	24,605	16,035	2,974	6,579	18,865	548	3,461	19,036	9,738	135,805
Financial guarantees	1,477	-	6,035	4,914	-	1,172	2,907	95	5	2,004	252	18,861
Undrawn loan commitments	-	-	1,871	8,297	2,442	-	9,726	-	-	11,303	1,804	35,443
Undrawn overdrafts	9,842	-	12,476	2,063	503	5,291	5,135	314	2,733	5,456	7,525	51,338
Credit card commitments	22,645	-	4,223	761	29	116	1,097	139	723	273	157	30,163
Maximum credit exposure	383,677	179,645	151,998	60,462	12,828	89,992	102,755	24,761	16,810	166,071	115,564	1,304,563

44. Credit exposure covered by collateral

Collateral and other credit mitigants vary between types of obligors and credit facilities. Loans to credit institutions are usually unsecured. For loans to individuals the principal collateral taken is residential property against mortgages. In the case of corporate entities the Group takes a charge over assets such as real estate, vessels, cash and securities as well as other collateral including accounts receivables, inventory, vehicles and equipment. Loans to government entities and to municipalities are more often than not unsecured. Derivative exposures are generally made under ISDA master agreements with Credit Support Annex or corresponding terms with pledged collateral in the form of cash and government bonds.

In some cases the Group uses guarantees as a credit enhancement but since guarantees effectively transfer credit risk from one counterparty to another they do not represent a reduction in maximum exposure to credit risk. Covenants in loan agreements are also an important credit enhancement but do not reduce maximum credit exposure.

Amounts are in ISK million

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Valuation of collateral is based on market price, official valuation for tax purposes or expert opinion of the Group's employees, depending on availability. In the case of fishing vessels the associated fishing quota is included in the valuation. Collateral is allocated according to the gross carrying amount of loans and nominal off-balance sheet items, and is measured without including the effect of overcollateralisation. This means that if some loans have collateral values in excess of their gross carrying amount, then the excess is removed in order to reflect the Group's actual maximum exposure to credit risk. The total value of pledged assets can thus be higher than the cover indicates. The maximum credit risk exposure is measured on net carrying value basis, and therefore collateral allocation can in some instances be higher. For capital leases the Group remains the owner of the leased object. In total ISK 38,789 million of the collateral are leased objects.

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

At 30 June 2020

Collateral held against non credit-impaired exposures	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral	Total credit exposure not covered by collateral	Associated ECL
Derivatives	9,666	-	-	4,570	-	-	4,570	9,096	-
Loans and commitments to customers:	1,038,755	630,438	99,470	7,164	49,991	77,347	864,410	174,345	8,360
Individuals	386,156	304,336	8	370	13,692	121	318,527	67,629	1,491
Commerce and services	143,932	61,868	132	721	27,000	24,991	114,712	29,220	3,056
Construction	54,672	41,705	10	549	2,043	2,285	46,592	8,080	475
Energy	8,832	5,514	-	370	8	53	5,945	2,887	39
Financial services	8,550	689	-	126	-	1,994	2,809	5,741	9
Industrial and transportation	97,468	45,651	15	182	6,770	16,468	69,086	28,382	853
Investment companies	21,372	6,191	-	3,930	78	9,697	19,896	1,476	587
Public sector and non-profit organisations	16,396	991	-	4	24	-	1,019	15,377	23
Real estate	162,014	149,940	5	846	293	1,054	152,138	9,876	1,577
Seafood	139,363	13,553	99,300	66	83	20,684	133,686	5,677	250
Total	1,048,421	630,438	99,470	11,734	49,991	77,347	868,980	183,441	8,360
Collateral held against credit-impaired exposures									
Loans and commitments to customers:	27,666	19,197	1,905	291	1,100	3,317	25,810	1,856	7,894
Individuals	7,624	6,749	18	4	158	5	6,934	690	1,006
Commerce and services	3,951	1,887	640	12	518	417	3,474	477	2,795
Construction	5,951	5,155	-	118	102	365	5,740	211	350
Industrial and transportation	2,621	602	1,219	117	298	44	2,280	341	1,671
Investment companies	3,749	1,260	-	-	7	2,458	3,725	24	306
Public sector and non-profit organisations	18	2	-	-	-	-	2	16	18
Real estate	3,560	3,400	-	40	7	25	3,472	88	1,553
Seafood	192	142	28	-	10	3	183	9	195
Total	27,666	19,197	1,905	291	1,100	3,317	25,810	1,856	7,894

Amounts are in ISK million

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At 31 December 2019 Collateral held against non credit-impaired exposures	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral	Total credit exposure not covered by collateral	Associated ECL
Derivatives	9,485	-	-	1,757	-	-	1,757	7,728	-
Loans and commitments to customers:	1,012,821	622,021	87,217	7,001	49,865	80,043	846,147	166,674	5,056
Individuals	374,718	292,701	7	417	13,317	116	306,558	68,160	1,579
Commerce and services	146,149	63,151	777	961	27,124	25,891	117,904	28,245	1,030
Construction	55,236	40,432	4	653	2,130	3,968	47,187	8,049	495
Energy	10,861	5,655	-	366	8	5	6,034	4,827	34
Financial services	8,894	-	-	123	-	3,621	3,744	5,150	7
Industrial and transportation	99,188	49,944	12	107	6,757	18,566	75,386	23,802	534
Investment companies	23,982	7,748	-	3,281	71	11,930	23,030	952	478
Public sector and non-profit organisations	15,758	958	-	7	29	-	994	14,764	29
Real estate	162,795	148,919	5	1,072	301	1,125	151,422	11,373	702
Seafood	115,240	12,513	86,412	14	128	14,821	113,888	1,352	168
Total	1,022,306	622,021	87,217	8,758	49,865	80,043	847,904	174,402	5,056
Collateral held against credit-impaired exposures									
Loans and commitments to customers:	22,616	17,100	1,481	333	846	830	20,590	2,026	5,931
Individuals	8,427	7,191	17	12	166	2	7,388	1,039	1,245
Commerce and services	4,944	2,980	102	22	561	805	4,470	474	1,864
Construction	5,219	4,919	-	197	19	7	5,142	77	261
Industrial and transportation	1,965	253	1,331	102	72	16	1,774	191	1,559
Investment companies	156	149	-	-	-	-	149	7	111
Public sector and non-profit organisations	15	14	-	-	-	-	14	1	1
Real estate	1,800	1,567	-	-	9	-	1,576	224	595
Seafood	90	27	31	-	19	-	77	13	295
Total	22,616	17,100	1,481	333	846	830	20,590	2,026	5,931

Amounts are in ISK million

45. Credit quality of financial assets

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

The Group uses internal rating models to assess the default probability of corporate and retail customers. The models assign each customer to one of ten risk classes. One risk class is for customers in default (risk class 10), and nine risk classes are for performing customers (risk classes 1-9). Risk classes are assigned on customer level and not facility level.

The rating of corporate customers is based on a company's most recent financial statement, together with a qualitative assessment of its management, market position and industry sector.

For retail customers the Group uses two different statistical rating models. One model is for individuals and another is for small companies with a total exposure to the Group of less than ISK 150 million. These models are behavioural scoring models and use information about a customer's payment history, amount of debt and deposits, and demographic variables to assess the probability that a customer will default on any of his obligations within 12 months of the rating assessment.

Risk classes 1-4 represent low risk, risk classes 5-6 moderate risk, risk classes 7-8 increased risk, risk class 9 high risk, and risk class 10 represents customers that are in default. Unrated are loans that are yet to be rated.

Further information on the risk classes, including the mapping from risk classes to the probability of default, can be found in Section 4.2.2 of the unaudited Pillar 3 2019 Report.

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

Due to the COVID-19 pandemic the Group transferred a relatively large proportion of assets from Stage 1 to Stage 2 in the first half of 2020. The Group did not re-evaluate the risk classes of the borrowers affected but instead applied an overlay factor to the expected credit loss (see Note 2).

At 30 June 2020

Loans to customers:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	229,965	23,103	-	253,068
Risk class 5-6	335,455	60,917	-	396,372
Risk class 7-8	187,183	32,345	-	219,528
Risk class 9	34,175	11,029	-	45,204
Risk class 10	-	-	34,297	34,297
Unrated	230	-	-	230
	787,008	127,394	34,297	948,699
Expected credit loss	(3,296)	(4,395)	(7,688)	(15,379)
Net carrying amount	783,712	122,999	26,609	933,320

Off-balance sheet loan commitments and financial guarantees:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	56,755	3,192	-	59,947
Risk class 5-6	42,988	5,035	-	48,023
Risk class 7-8	16,244	6,866	-	23,110
Risk class 9	1,012	583	-	1,595
Risk class 10	-	-	1,263	1,263
Unrated	32	6	-	38
	117,031	15,682	1,263	133,976
Expected credit loss	(368)	(301)	(206)	(875)
Total	116,663	15,381	1,057	133,101

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At 30 June 2020	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	ECL	Total
Loans and commitments to customers:								
Individuals	81,457	151,577	123,015	31,477	8,634	117	(2,497)	393,780
Commerce and services	31,714	78,487	31,447	5,271	6,741	74	(5,851)	147,883
Construction	4,848	31,508	16,851	1,914	6,300	27	(825)	60,623
Energy	2,959	3,845	2,067	-	-	-	(39)	8,832
Financial services	7,947	2	604	-	-	6	(9)	8,550
Industrial and transportation	28,467	47,078	20,153	2,623	4,292	-	(2,524)	100,089
Investment companies	2,564	8,484	9,368	1,542	4,055	1	(893)	25,121
Public sector and non-profit organisations	13,380	2,813	207	-	36	19	(41)	16,414
Real estate	52,774	72,464	35,016	3,331	5,114	5	(3,130)	165,574
Seafood	86,905	48,137	3,910	641	388	19	(445)	139,555
Total	313,015	444,395	242,638	46,799	35,560	268	(16,254)	1,066,421

At 31 December 2019

Loans to customers:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	226,347	289	-	226,636
Risk class 5-6	388,936	1,385	-	390,321
Risk class 7-8	204,979	14,487	-	219,466
Risk class 9	33,880	7,544	-	41,424
Risk class 10	-	-	27,160	27,160
Unrated	4,676	93	154	4,923
	858,818	23,798	27,314	909,930
Expected credit loss	(3,645)	(953)	(5,700)	(10,298)
Net carrying amount	855,173	22,845	21,614	899,632

Off-balance sheet loan commitments and financial guarantees:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	58,327	25	-	58,352
Risk class 5-6	58,271	253	-	58,524
Risk class 7-8	15,334	1,757	-	17,091
Risk class 9	1,095	186	-	1,281
Risk class 10	-	-	1,233	1,233
Unrated	8	5	-	13
	133,035	2,226	1,233	136,494
Expected credit loss	(403)	(55)	(231)	(689)
Total	132,632	2,171	1,002	135,805

Amounts are in ISK million

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At 31 December 2019	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	ECL	Total
Loans and commitments to customers:								
Individuals	76,119	151,224	115,042	29,537	9,517	4,530	(2,824)	383,145
Commerce and services	29,718	81,536	31,572	3,968	6,810	383	(2,894)	151,093
Construction	3,354	33,345	17,924	1,120	5,468	-	(756)	60,455
Energy	5,045	3,846	2,004	-	-	-	(34)	10,861
Financial services	8,848	30	17	-	-	6	(7)	8,894
Industrial and transportation	26,474	59,108	11,775	2,363	3,526	-	(2,093)	101,153
Investment companies	2,803	9,198	11,090	1,367	268	1	(589)	24,138
Public sector and non-profit organisations	12,761	2,733	268	11	15	15	(30)	15,773
Real estate	52,934	64,623	42,304	3,631	2,400	-	(1,297)	164,595
Seafood	66,932	43,202	4,561	708	389	1	(463)	115,330
Total	284,988	448,845	236,557	42,705	28,393	4,936	(10,987)	1,035,437

46. Loans to customers in the tourism industry

Companies in the tourism industry were classified into four groups based on an assessment of how much an increase in credit risk these companies face in the short, medium and long term. Where the increase was found to be significant (groups 2-4), the exposure was transferred to Stage 2. In addition, an overlay factor was applied to the expected credit loss, comparable to an increase by one risk class for group 2 and two risk classes for groups 3 and 4.

At 30 June 2020

Loans to customers in the tourism industry:	Stage 1	Stage 2	Stage 3	Total
Group 1	-	-	-	-
Group 2	-	27,861	564	28,425
Group 3	-	56,713	1,221	57,934
Group 4	-	7,521	5,172	12,693
	-	92,095	6,957	99,052
Expected credit loss	-	(3,236)	(2,360)	(5,596)
Net carrying amount	-	88,859	4,597	93,456

Off-balance sheet loan commitments and financial guarantees to customers in the tourism industry:

	Stage 1	Stage 2	Stage 3	Total
Group 1	-	-	-	-
Group 2	-	3,793	91	3,884
Group 3	-	2,142	40	2,182
Group 4	-	4,750	42	4,792
	-	10,685	173	10,858
Expected credit loss	-	(207)	(97)	(304)
Total	-	10,478	76	10,554

Amounts are in ISK million

47. Forbearance

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

The relationship between forbearance and stages is discussed in Note 66.3. in the consolidated financial statements for the year 2019.

Once an asset has been classified as forborne, it will remain forborne for a minimum 24-month probation period. In order for a loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:

- All of the customer's facilities have to be considered performing; and
- The customer does not have any contract that is more than 30 days past due; and
- The probation period of two years has passed from the date of the forbearance event; and
- Regular payments of more than an insignificant amount of principal or interest have been made during at least half of the probation period

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

At 30 June 2020	Stage 1	Stage 2	Stage 3	Total
Individuals	1,246	2,584	2,147	5,977
Companies	187	8,570	17,811	26,568
Gross carrying amount	1,433	11,154	19,958	32,545

	Stage 1	Stage 2	Stage 3	Total
Individuals	(9)	(61)	(201)	(271)
Companies	(1)	(529)	(3,576)	(4,106)
Expected credit loss	(10)	(590)	(3,777)	(4,377)

At 31 December 2019	Stage 1	Stage 2	Stage 3	Total
Individuals	1,615	1,102	1,372	4,089
Companies	13,212	8,469	8,289	29,970
Gross carrying amount	14,827	9,571	9,661	34,059

	Stage 1	Stage 2	Stage 3	Total
Individuals	(12)	(41)	(182)	(235)
Companies	(77)	(249)	(2,167)	(2,493)
Expected credit loss	(89)	(290)	(2,349)	(2,728)

Amounts are in ISK million

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48. COVID-19 moratoria

The Group recognises that the economic effects of the COVID-19 pandemic will temporarily have a seriously negative impact on customers' cash flow and thus their ability to repay their debt in accordance with their obligations. The Group has entered into an agreement with other financial institutions and lenders in Iceland to provide a moratorium for corporate customers, uniformly executed across institutions. Similarly, the Group has entered into an agreement for a moratorium for households and individuals. In accordance with guidelines from EBA and the Central Bank, moratoria of this kind do not trigger classification as forbearance.

The following table shows the extent of moratoria granted by the Group under these initiatives agreed and applied broadly by domestic credit institutions.

At 30 June 2020

	Stage 1	Stage 2	Stage 3	Total
Individuals	26,869	639	26	27,534
Companies	86,421	72,508	56	158,985
Gross carrying amount	113,290	73,147	82	186,519

	Stage 1	Stage 2	Stage 3	Total
Individuals	(112)	(17)	-	(129)
Companies	(375)	(1,918)	(4)	(2,297)
Expected credit loss	(487)	(1,935)	(4)	(2,426)

49. Assets obtained by taking possession of collateral

Details of non-financial assets obtained by the Group during the period by taking possession of collateral held as security against loans.

	30.06.2020	31.12.2019
Property and land	1,185	378
Industrial equipment and vehicles	28	81
Total	1,213	459

The Group pursues realisation of the collateral in an orderly manner. The Group does not generally use the non-cash collateral for its own operations.

50. Write-offs

When the Group has no reasonable expectations of recovering a credit exposure or when it is uneconomical to pursue legal collection, the financial asset is written off. A write-off does not change the debt obligation which is therefore still subject to enforcement activity. Any recoveries of amounts previously written off are credited to the income statement.

Gross carrying amount written off and still subject to enforcement activity	2020 1.1-30.6	2019 1.1-30.6
Individuals	273	285
Companies	420	754
Total	693	1,039

Amounts are in ISK million

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51. Large exposures disclosure

When the Group's total exposure to a group of connected clients is 10% or higher of the Group's capital base it is considered a large exposure. Both on-balance sheet and off-balance sheet items from all types of financial instruments are included in the exposure as defined by regulation no. 233/2017. The Group has internal criteria that define connections between clients. These criteria reflect the Group's interpretation of Article (1)(a) of the Act on Financial Undertakings no. 161/2002, where groups of connected clients are defined.

The exposure is evaluated both before and after credit risk mitigating effects. After mitigating effects, the Group currently has one large exposure, a decrease of one since the last reporting date. No large exposure is therefore above the maximum 25% single large exposure limit set by the law.

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

At 30 June 2020

Groups of connected clients:	Before	After
Group 1	90%	-
Group 2	12%	10%

At 31 December 2019

Groups of connected clients:	Before	After
Group 1	75%	-

52. Liquidity risk

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

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

53. Liquidity coverage and Net stable funding ratio

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

The following tables show the NSFR and the LCR for the Group at the end of June 2020 and at year-end 2019.

The calculations are based on consolidated figures including Borgun hf. even though it's assets and liabilities are classified as held for sale.

Net stable funding ratio	30.6.2020	31.12.2019
For all currencies	117%	119%
Foreign currencies	147%	156%

Liquidity coverage ratio	30.6.2020	31.12.2019
For all currencies	179%	155%
Domestic currency	119%	110%
Foreign currencies	325%	325%

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At 30 June 2020	For all currencies		Foreign currencies	
	Unweighted	Weighted	Unweighted	Weighted
Liquid assets level 1*	205,801	205,801	36,967	36,967
Liquid assets level 2	18,201	4,667	6,467	1,282
Total liquid assets	224,002	210,468	43,434	38,249
Deposits	532,173	169,875	84,176	38,508
Debt issued	226	226	169	169
Other outflows	81,376	32,889	22,665	8,397
Total outflows	613,775	202,990	107,010	47,074
Short-term deposits with other banks**	70,616	70,188	68,543	68,115
Other inflows	32,146	15,122	9,080	6,232
Restrictions on inflows	-	-	-	(39,042)
Total inflows	102,762	85,310	77,623	35,305
Liquidity coverage ratio		179%		325%

At 31 December 2019	For all currencies		Foreign currencies	
	Unweighted	Weighted	Unweighted	Weighted
Liquid assets level 1*	157,080	157,080	31,858	31,858
Liquid assets level 2	11,942	6,271	3,727	520
Total liquid assets	169,022	163,351	35,585	32,378
Deposits	482,322	139,354	78,089	33,961
Debt issued	1,361	1,361	650	650
Other outflows	81,493	30,997	18,012	5,248
Total outflows	565,176	171,712	96,751	39,859
Short-term deposits with other banks**	54,203	52,335	51,343	50,261
Other inflows	33,984	14,213	6,287	3,558
Restrictions on inflows	-	-	-	(23,925)
Total inflows	88,187	66,548	57,630	29,894
Liquidity coverage ratio		155%		325%

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

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

Amounts are in ISK million

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Deposits by liquidity coverage ratio category

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

The Bank updated its internal definition of established business relationships which partly caused the amount of stable deposits to increase compared to year-end 2019.

At 30 June 2020	Deposits maturing within 30 days Less stable	Weight (%)	Stable	Weight (%)	Term deposits	Total deposits
Retail	220,147	12%	120,368	5%	80,085	420,600
Operational relationships	3,621	25%	-	5%	-	3,621
Corporations	74,623	40%	433	20%	21,675	96,731
Sovereigns, Central Bank and public sector entities	9,454	40%	396	20%	1,155	11,005
Pension funds	67,443	100%	-	-	29,113	96,556
Domestic financial entities	26,236	100%	-	-	42,691	68,927
Foreign financial entities	9,452	100%	-	-	9,792	19,244
Total	410,976		121,197		184,511	716,684

At 31 December 2019	Deposits maturing within 30 days Less stable	Weight (%)	Stable	Weight (%)	Term deposits	Total deposits
Retail	228,447	12%	83,773	5%	78,870	391,090
Operational relationships	2,446	25%	-	5%	-	2,446
Corporations	73,739	40%	337	20%	24,589	98,665
Sovereigns, Central Bank and public sector entities	6,813	40%	253	20%	620	7,686
Pension funds	35,405	100%	-	-	24,869	60,274
Domestic financial entities	28,494	100%	-	-	46,371	74,865
Foreign financial entities	8,038	100%	-	-	6,174	14,212
Total	383,382		84,363		181,493	649,238

54. Maturity analysis of assets and liabilities

The following tables show the contractual payments of principal and interest for the Group's financial liabilities. Thus, the total figures for each liability class are higher than the respective balance sheet amount. Cash flows for payments of unknown nature, such as for floating rate, CPI-linked or foreign currency denominated instruments, are based on internal yield curves and forecasts.

For dated financial liabilities the amounts are grouped into maturity buckets according to contractual maturities of principal and estimated contractual payments of interest. For demand deposits or other non-dated liabilities, the figures are grouped according to the first possible required payment date.

Maturity analysis 30 June 2020

Financial liabilities	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Deposits from CB and credit institutions	35,461	4,194	11,709	14,483	5,596	-	-	35,982
Deposits from customers	681,223	544,344	60,500	69,903	15,181	27,732	-	717,660
Debt issued and other borrowed funds	321,803	-	11,794	17,440	277,580	88,919	-	395,733
Subordinated loans	25,834	-	114	538	2,885	29,015	-	32,552
Other financial liabilities:	28,372	23,257	978	634	1,751	2,278	-	28,898
Lease liabilities	4,036	-	118	355	1,751	2,278	-	4,502
Other liabilities	24,336	23,257	860	279	-	-	-	24,396
Total	1,092,693	571,795	85,095	102,998	302,993	147,944	-	1,210,825

Amounts are in ISK million

54. Cont'd

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

Off-balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial guarantees	18,609	-	-	-	-	-	18,609
Undrawn loan commitments	26,369	-	-	-	-	-	26,369
Undrawn overdrafts	56,718	-	-	-	-	-	56,718
Credit card commitments	31,405	-	-	-	-	-	31,405
Total	133,101	-	-	-	-	-	133,101
Total non-derivative financial liabilities and off-balance sheet liabilities	704,896	85,095	102,998	302,993	147,944	-	1,343,926

The following table shows the contractual cash flow of the Group's derivative liabilities, i.e. derivatives that have a negative and a positive carrying amount at the reporting date. For derivatives settled on a gross basis, the cash flow for both legs of the derivative is shown, since netting cannot be applied upon settlement.

Derivative financial liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	13,938	26,195	39,338	-	-	79,471
Outflow	-	(14,780)	(28,372)	(42,637)	-	-	(85,789)
Total	-	(842)	(2,177)	(3,299)	-	-	(6,318)
Net settled derivatives	-	(929)	-	-	-	-	(929)
Total	-	(1,771)	(2,177)	(3,299)	-	-	(7,247)

Maturity classification of assets is based on contractual maturity. For bonds and debt instruments in the banking book the maturity classification is based on contractual maturity while for bonds and debt instruments held for trading the maturity classification is based on the estimated liquidation time of the asset.

Financial assets	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with Central Bank	103,569	20,130	82,089	-	-	1,349	-	103,568
Loans to credit institutions	70,307	34,162	36,142	2	-	-	-	70,306
Bonds and debt instruments	140,422	-	49,561	58,739	22,847	9,275	-	140,422
Loans to customers	933,320	8,693	82,623	91,354	323,863	426,786	-	933,319
Shares and equity instruments	10,943	-	-	-	-	-	10,943	10,943
Other financial assets	6,076	5,215	458	69	334	-	-	6,076
Total	1,264,637	68,200	250,873	150,164	347,044	437,410	10,943	1,264,634

Derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	44,495	40,998	42,634	-	-	128,127
Outflow	-	(33,579)	(39,715)	(40,451)	-	-	(113,745)
Total	-	10,916	1,283	2,183	-	-	14,382
Net settled derivatives	-	281	-	-	-	-	281
Total	-	11,197	1,283	2,183	-	-	14,663

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

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The following tables show the comparative amounts for maturity analysis at year-end 2019.

Maturity analysis 31 December 2019

Financial liabilities	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Deposits from CB and credit institutions	30,925	1,992	16,363	8,468	4,580	-	-	31,403
Deposits from customers	618,313	453,959	78,232	54,994	16,612	62,222	-	666,019
Debt issued and other borrowed funds	306,381	-	6,991	24,861	267,776	90,610	-	390,238
Subordinated loans	22,674	-	158	463	2,865	26,482	-	29,968
Other financial liabilities:	24,772	17,581	2,124	1,276	1,759	2,448	-	25,188
Lease liabilities	4,256	-	116	349	1,759	2,448	-	4,672
Other liabilities	20,516	17,581	2,008	927	-	-	-	20,516
Total	1,003,065	473,532	103,868	90,062	293,592	181,762	-	1,142,816

Off-balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial guarantees	18,861	-	-	-	-	-	18,861
Undrawn loan commitments	35,443	-	-	-	-	-	35,443
Undrawn overdrafts	51,338	-	-	-	-	-	51,338
Credit card commitments	30,163	-	-	-	-	-	30,163
Total	135,805	-	-	-	-	-	135,805
Total non-derivative financial liabilities and off-balance sheet liabilities	609,337	103,868	90,062	293,592	181,762	-	1,278,621

Derivative financial liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	57,542	36,133	43,218	-	-	136,893
Outflow	-	(59,615)	(37,222)	(44,915)	-	-	(141,752)
Total	-	(2,073)	(1,089)	(1,697)	-	-	(4,859)
Net settled derivatives	-	(323)	-	-	-	-	(323)
Total	-	(2,396)	(1,089)	(1,697)	-	-	(5,182)

Financial assets	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with Central Bank	146,638	28,978	115,981	-	-	1,679	-	146,638
Loans to credit institutions	54,376	20,719	33,656	-	-	-	-	54,375
Bonds and debt instruments	52,870	7,768	23,998	10,120	10,983	-	-	52,869
Loans to customers	899,632	2,972	88,446	87,462	303,668	417,083	-	899,631
Shares and equity instruments	18,426	-	-	-	-	-	18,426	18,426
Other financial assets	5,757	1,889	525	118	17	-	3,259	5,808
Total	1,177,699	62,326	262,606	97,700	314,668	418,762	21,685	1,177,747

Derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	92,680	28,583	74,731	-	-	195,994
Outflow	-	(82,832)	(27,964)	(73,544)	-	-	(184,340)
Total	-	9,848	619	1,187	-	-	11,654
Net settled derivatives	-	273	-	-	-	-	273
Total	-	10,121	619	1,187	-	-	11,927

Amounts are in ISK million

55. Market risk

The Group defines market risk as the current or prospective risk to earnings and capital arising from adverse movements in the level or volatility of prices of market instruments, such as those that arise from changes in interest rates, foreign exchange rates, equity prices, CPI-indexation and commodity prices. Sources of market risk are imbalances in the Group's balance sheet and open positions in bonds, currencies and equities. Derivative contracts are also potential sources of market risk.

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

56. Interest rate risk

Interest rate risk is defined as the current or prospective risk to earnings or capital arising from adverse movements in interest rates. Sensitivity measures like Basis Point Value (BPV) are used to measure and manage risk arising from its fixed income exposures. The BPV measures the effect of a 0.01 percentage point upward parallel shift in the yield curve on the fair value of these exposures.

Interest rate risk in the trading book

The fixed income trading unit invests mainly in government bonds, bonds issued by the Housing Financing Fund (HFF) which are guaranteed by the Icelandic Government, domestic municipality bonds, and covered bonds issued by other Icelandic banks. Bonds and bills in the Group's liquidity portfolio are also categorised in the trading book. In the following table the total market value (MV) of long and short positions may not be the same as reported in Note 6 since netting between short and long positions is not applied here.

	30.6.2020			31.12.2019		
Trading bonds and debt instruments, long positions	MV	Duration	BPV	MV	Duration	BPV
Indexed	1,421	6.92	(0.98)	1,143	6.84	(0.78)
Non-indexed	115,937	0.42	(4.87)	31,855	0.41	(1.29)
Total	117,358	0.50	(5.85)	32,998	0.63	(2.07)

	30.6.2020			31.12.2019		
Trading bonds and debt instruments, short positions	MV	Duration	BPV	MV	Duration	BPV
Indexed	488	10.00	0.48	150	6.00	0.10
Non-indexed	247	5.00	0.12	615	4.00	0.28
Total	735	8.32	0.60	765	4.39	0.38
Net position of trading bonds and debt instruments	116,623	0.45	(5.25)	32,233	0.54	(1.69)

Interest rate risk in the banking book

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

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

Financial Statements first half 2020 55 Amounts are in ISK million

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Sensitivity analysis for interest rate risk in the banking book

At 30 June 2020

Currency	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
ISK, indexed	(4)	(104)	(351)	(1,604)	4,220	(1,789)	368
ISK, non-indexed	4	(20)	(3)	228	(30)	(4)	175
EUR	(11)	(96)	(93)	129	-	(1)	(72)
SEK	(16)	18	-	-	-	-	2
USD	22	-	-	-	-	(1)	21
Other	11	(15)	-	(3)	-	(7)	(14)
Total	6	(217)	(447)	(1,250)	4,190	(1,802)	480

At 31 December 2019

Currency	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
ISK, indexed	55	60	(442)	(1,668)	1,995	193	193
ISK, non-indexed	7	(12)	11	89	(10)	(9)	76
EUR	(17)	(20)	(29)	118	-	(2)	50
SEK	10	-	-	-	-	-	10
USD	(42)	-	-	-	-	(1)	(43)
Other	12	(11)	-	41	-	(6)	36
Total	25	17	(460)	(1,420)	1,985	175	322

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

57. Currency risk

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

The analysis of the Group's foreign currency exposure presented below is based on the contractual currency of the underlying balance sheet items. Additionally, there are off-balance sheet items that carry currency risk and are included in the total currency imbalance. The off-balance sheet amounts below represent the notional amounts of derivatives and unsettled spot agreements.

Series C preferred shares in Visa Inc., which Borgun hf., holds are included in the currency imbalance even though assets and liabilities of Borgun hf. are classified as held for sale.

Currency analysis at 30 June 2020

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	CAD	Other foreign currencies	Total foreign currencies
Cash and balances with Central Bank	207	105	63	14	4	18	15	38	15	1,474	1,953
Loans to credit institutions	15,031	41,187	554	244	501	208	10,381	89	100	42	68,337
Bonds and debt instruments	14,791	14,995	6	-	-	-	7,122	-	-	-	36,914
Loans to customers	129,978	35,376	1,192	584	3,565	2	3,515	720	7,408	34	182,374
Shares and equity instruments	32	2,742	438	-	-	-	29	-	-	-	3,241
Other assets	23	1,414	-	-	-	2	-	-	1	-	1,440
Total assets	160,062	95,819	2,253	842	4,070	230	21,062	847	7,524	1,550	294,259
Liabilities											
Deposits from credit institutions	11,915	871	1	-	-	-	-	-	-	-	12,787
Deposits from customers	30,552	39,816	4,446	484	506	895	3,093	2,285	506	8	82,591
Debt issued and other borrowed funds	104,412	-	-	-	-	36,724	20,096	-	-	-	161,232
Subordinated loans	-	-	-	-	-	25,834	-	-	-	-	25,834
Other liabilities	1	1,400	-	-	-	2	-	-	-	-	1,403
Total liabilities	146,880	42,087	4,447	484	506	63,455	23,189	2,285	506	8	283,847
Net on-balance sheet position	13,182	53,732	(2,194)	358	3,564	(63,225)	(2,127)	(1,438)	7,018	1,542	10,412
Net off-balance sheet position	(13,574)	(55,838)	2,097	(415)	(3,586)	63,057	1,981	1,378	(7,089)	(247)	(12,236)
Net position	(392)	(2,106)	(97)	(57)	(22)	(168)	(146)	(60)	(71)	1,295	(1,824)

Amounts are in ISK million

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Currency analysis at 31 December 2019

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	CAD	Other foreign currencies	Total foreign currencies
Cash and balances with Central Bank	942	319	210	52	24	51	73	114	58	123	1,966
Loans to credit institutions	11,689	25,740	1,650	378	534	116	9,707	1,294	272	687	52,067
Bonds and debt instruments	12,930	10,937	3	-	-	-	8,232	-	-	-	32,102
Loans to customers	112,185	29,486	2,037	581	3,185	3	3,408	635	6,005	33	157,558
Shares and equity instruments	31	3,371	419	-	-	-	27	-	-	-	3,848
Other assets	390	1,866	338	6	-	73	2	20	-	458	3,153
Total assets	138,167	71,719	4,657	1,017	3,743	243	21,449	2,063	6,335	1,301	250,694
Liabilities											
Deposits from credit institutions	9,145	558	1	-	-	-	-	-	-	-	9,704
Deposits from customers	32,247	27,939	3,810	385	395	874	3,317	3,617	453	42	73,079
Debt issued and other borrowed funds	91,809	-	-	-	-	37,768	19,565	-	-	-	149,142
Subordinated loans	-	-	-	-	-	22,674	-	-	-	-	22,674
Other liabilities	1,728	944	558	35	3	162	5	47	2	665	4,149
Total liabilities	134,929	29,441	4,369	420	398	61,478	22,887	3,664	455	707	258,748
Net on-balance sheet position	3,238	42,278	288	597	3,345	(61,235)	(1,438)	(1,601)	5,880	594	(8,054)
Net off-balance sheet position	(4,344)	(41,574)	(231)	(610)	(3,345)	61,127	1,255	1,726	(5,840)	(203)	7,961
Net position	(1,106)	704	57	(13)	-	(108)	(183)	125	40	391	(93)

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

58. Inflation risk

The Group is exposed to inflation risk since the value of CPI-linked assets exceeds CPI-linked liabilities. The value of these assets and liabilities changes according to changes in the CPI at any given time and all changes in the CPI affect profit and loss. A 1% increase in the index would lead to an ISK 467 million increase in the balance sheet and a 1% decrease would lead to a corresponding decrease, other risk factors held constant.

The off-balance sheet position of certain derivatives were incorrect in the year-end 2019 figures. Off-balance sheet liabilities positions have consequently been adjusted downwards by ISK 11,400 million. The year-end 2019 CPI imbalance therefore increased from ISK 9,260 million to ISK 20,660 million.

	30.6.2020	31.12.2019
Bonds and debt instruments	1,367	2,103
Loans to customers	290,557	295,725
Total CPI-linked assets	291,924	297,828
Deposits from customers	97,357	98,766
Debt issued and other borrowed funds	126,880	125,975
Off-balance sheet position	20,982	52,427
Total CPI-linked liabilities	245,219	277,168
CPI imbalance	46,705	20,660

59. Derivatives

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

60. Capital management

The following table shows the capital base, risk exposure amount, the resulting capital ratios, and leverage for the Group at 30 June 2020 and 31 December 2019.

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

Article 501 of the capital requirements regulation (EU) no. 575/2013 of the European Parliament came into effect in Iceland on 1 January 2020. This article stipulates capital requirements deduction for credit risk on exposures to SMEs and lowers the risk exposure amount by ISK 13.4 billion as of 30 June 2020, corresponding to a 30 basis point increase in the Group's capital ratio.

Regulation EU 2017/2395, as regards transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds, was ratified into Icelandic law in May 2020. The regulation allows for the phasing in of capital impacts due to IFRS 9, allowing institutions to include a predefined level of provisions as part of CET1 capital. Íslandsbanki has elected to make use of the transitional arrangements, which will add ISK 3.8 billion to CET1, corresponding to an increase of 30 basis points in the Group's capital ratio.

The Group aims at managing its capital position and the corresponding capital ratios above the overall regulatory capital requirement. According to the latest SREP report from the Financial Supervisory Authority, applicable as of 30 September 2019, the overall capital requirement is 17.0%. The Group's capital target includes a 0.5-2.0% management buffer on top of the overall capital requirement.

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

Amounts are in ISK million

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	30.6.2020	31.12.2019
CET1 capital		
Ordinary share capital	10,000	10,000
Share premium	55,000	55,000
Reserves	7,262	7,065
Retained earnings	105,681	105,569
Non-controlling interests	1,779	2,428
IFRS 9 reversal due to transitional rules	3,810	-
Fair value changes due to own credit standing	(427)	392
Tax assets	(88)	(476)
Intangible assets	(3,667)	(4,330)
Total CET1 capital	179,350	175,648
Tier 2 capital		
Qualifying subordinated loans	25,834	22,674
Total capital base	205,184	198,322
Risk exposure amount		
- due to credit risk	821,457	789,180
- due to market risk	14,435	7,919
Market risk, trading book	12,024	6,488
Currency risk	2,411	1,431
- due to credit valuation adjustment	1,817	2,027
- due to operational risk	85,424	85,424
Total risk exposure amount	923,133	884,550
Capital ratios		
Tier 1 ratio	19.4%	19.9%
Total capital ratio	22.2%	22.4%
Leverage ratio		
Exposure amount		
On-balance sheet exposures	1,293,135	1,189,062
Off-balance sheet exposures	37,479	38,849
Derivative exposures	9,670	9,461
Leverage ratio total exposure measure	1,340,284	1,237,372
Tier 1 capital	179,350	175,648
Leverage ratio	13.4%	14.2%

Amounts are in ISK million