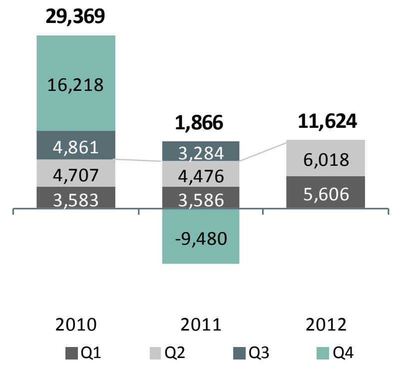
Íslandsbanki

1H2012 INTERIM FINANCIAL STATEMENTS

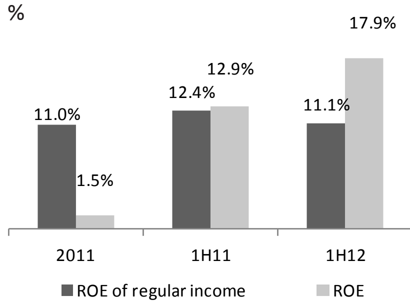
HIGHLIGHTS

- Profit after tax was ISK 11.6bn compared to ISK 8.1bn in 1H11.
- Profit after tax from regular operations, defined as earnings excluding one-off items e.g. net valuation changes from the loan portfolio, fair value gain deriving from changes in accounting treatment, costs associated with the Byr merger and the impairment of goodwill, and net earnings from discontinued operations, was ISK 7.2bn, compared to ISK 7.7bn in 1H11.
- Net valuation changes on the loan portfolio resulted in a gain of ISK 2.1bn in 1H12, compared to a loss of ISK 255m in 1H11.
- Return on equity was 17.9%, compared to 12.9% in 1H11. Return on equity from regular operations was 11.1% in 1H12, compared to 12.4% in 1H11.
- Around 18,700 individuals and 3,200 corporates have received write offs, debt forgiveness or some form of debt correction since the Bank's establishment, totaling ISK 394bn to date.
- Total assets were ISK 789.9bn at end of June 2012, compared to ISK 792.4bn at the end of March 2012.
- Total deposits were ISK 499.8bn at end of June 2012, compared to ISK 509.3bn at the end of March 2012.
- The net interest margin was 4.0% in 1H12, compared to 4.8% in 1H11.
- Funding diversification continued with two new domestic covered bond issuances listed in Mar 2012 amounting to ISK 3.3bn and two tap issuances in May 2012. Total covered bond issuances now stand at ISK 8.8bn
- Equity was ISK 135.5bn having increased by 10% throughout the first half of 2012. The total capital ratio was 23.5%, which is well above the 16% regulatory minimum set by the Icelandic Financial Services Authority.

NET PROFIT
ISKm



ROE
%



Birna Einarsdóttir, Chief Executive Officer of Íslandsbanki:

"Íslandsbanki's financial strength is well reflected in the 1H12 financial results. The Bank continues to deliver good return on equity, liquidity is strong and the capital ratio is well above the minimum requirements of the Icelandic FSA.

Net fee and commission income has increased by 47% from last year. This growth is attributable to the merger of Íslandsbanki and Byr, solid performance from the subsidiary Borgun and an increase in capital markets activities. However, our cost-to-income ratios have also been affected by one off costs due to the merger. We expect that the full synergy effect of the merger will come through by next year.

Demand for new loans is increasing and new lending to households and corporates has risen during the period. Indeed, new lending in the first half of 2012 at Ergo, the asset based financing division, has equaled the total for the entire year 2011. Capital markets activities are increasing which will presumably have a positive impact on the development and structure of the Icelandic financial markets in the coming months. Íslandsbanki sold a 10.29% share in Icelandair Group hf. during this period. This is in line with the Bank's strategy to reduce its holding in companies in unrelated business.

There are several positive developments in the Icelandic economy. However, the recovery is fragile, both in terms of the uncertainties still present in here in Iceland as well as in the general market environment internationally."

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Key figures	30.06.12	31.03.12
	ISKbn	ISKbn
Total assets	790	792
Total loans	596	584
Total deposits	500	509
Equity	135	129
Net Interest Margin	4.0%	4.4%
Deposit / Loan	84%	87%
Tier 1	20.2%	19.7%
Total capital	23.5%	23.3%

Key figures	1H12	1H11
	ISKbn	ISKbn
ROE	17.9%	12.9%
ROE regular income	11.1%	12.4%
Profit after tax	11.6	8.1
Profit adjusted income	7.2	7.7
Cost / income	52.0%	50.5%
Core Cost / income	65.4%	50.8%

Íslandsbanki

INCOME STATEMENT

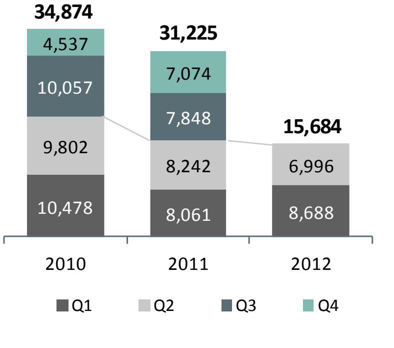
ISK m	1H12	1H11	FY11	FY10
Net interest income	**15,684**	16,303	31,225	34,874
Net valuation changes	**2,069**	-255	-1,296	14,507
Provision for latent impairment	**-270**	-155	76	-514
Net interest income after valuation changes	**17,483**	15,894	30,005	48,867
Net fee and commission income	**4,426**	3,013	5,966	7,380
Net foreign exchange	**879**	336	937	-963
Net financial income/loss	**1,876**	-468	2,649	-910
Other net operating income	**589**	656	894	1,186
Total operating income	**25,253**	19,430	40,451	55,560
Salaries and related expenses	**-6,620**	-4,968	-10,531	-9,207
Other operating expenses	**-5,997**	-4,405	-9,339	-8,659
Insurance fund	**-526**	-432	-965	-607
Administrative expenses	**-13,143**	-9,806	-20,835	-18,473
Impairment of goodwill	**0**	0	-17,873	0
Share profit of associates	**0**	0	39	0
Profit before tax	**12,110**	9,624	1,782	37,087
Income tax	**-2,998**	-2,067	-75	-7,214
Bank tax	**-407**	-344	-682	-221
Profit from discontinued ops. net of tax	**2,919**	849	841	-283
Profit after tax	**11,624**	8,062	1,866	29,369
Earnings from regular operations	**7,174**	7,711	13,905	17,756

Earnings from regular operations is defined as earnings excluding one-off items e.g. net valuation changes from the loan portfolio, fair value gain deriving from changes in accounting treatment, costs associated with the Byr merger and the impairment of goodwill, and net earnings from discontinued operations.

PROFIT

- Profit after tax was ISK 11,624m in 1H12, compared to ISK 8,062m in 1H11. This translates to a return on equity of 17.9%, compared to 12.9% in 1H11.
- Earnings from regular operations resulted in a pre-tax profit of ISK 7,174m and a return on equity of 11.1%. In comparison, earnings from regular operations was ISK 7,711m in 1H11, translating into a return on equity of 12.4%.
- Earnings from regular operations is defined as earnings excluding one-off items e.g. net valuation changes from the loan portfolio, fair value gain deriving from changes in accounting treatment, costs associated with the Byr merger and the impairment of goodwill, and net earnings from discontinued operations

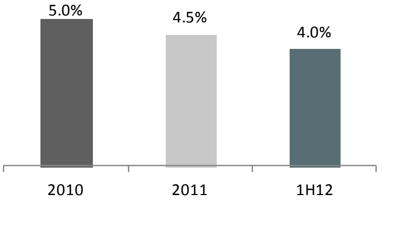
NET INTEREST INCOME
ISKm



INCOME

- In line with the bank's focus on long-term stable cash flows, core operations continue to generate the vast majority of the Bank's net operating income split. Over 80% of the Bank's net operating income is from net interest income and net fee and commission income.
- Net interest income amounted to ISK 15,684m in 1H12, compared to ISK 16,304m in 1H11. The decrease can be attributed in some part to a lower amortized discount. Calculated as the ratio of net interest income to the average carrying amount of total assets, the net interest margin was 4.0% in 1H12, compared to 4.8% in 1H11.

NET INTEREST MARGIN
%



INCOME STATEMENT – cont.

- Net fee and commission income amounted to ISK 4,426m in 1H12, compared to ISK 3,013m for the first half in the previous year. This is an YoY increase of 47% which can be attributed to the Byr merger, new fee generating subsidiaries and increased capital markets activity. (Borgun is fully incorporated in the 1H12 numbers, having left the Group in Mar 2011 and rejoined in Dec 2011 following merger with Byr.)
- Foreign exchange gain in 1H12 amounted to ISK 879m, compared to a ISK 336m gain in 1H11 due to weakening of the ISK and trading gains. The net FX gap is strictly monitored and is within the regulatory limit. The gross foreign currency gap is gradually diminishing in line with restructuring of the loan portfolio.
- Other financial income amounted to ISK 1,876m in 1H12, compared to a loss of ISK 468m in 1H11, representing a fair value gain from sale of equities and dividend income of other shares and equity instruments.
- Other net operating income, mainly rental income and fees from service agreements and foreclosed assets, amounted to ISK 589m in 1H12, compared to ISK 656m in 1H11.

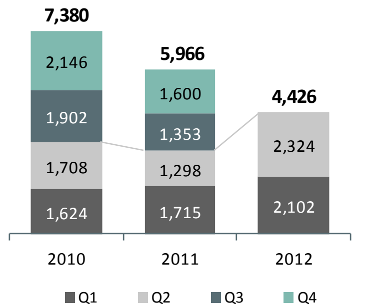
EXPENSES

- Cost to income ratio has remained stable at 52% in the first half of 2012, compared to 50.5% in 1H11 and 51.5% in FY11.
- Core cost to income ratio, calculated as the ratio of total operating expenses over net interest income and net fee and commission income, was 65.4% in 1H12, compared to 50.8% in 1H11.
- Total administrative expenses amounted to ISK 13,143m in 1H12, compared to ISK 9,806m in 1H11. Increase is partly attributable to the acquisition of Byr, in particular in relation to professional fees and IT services, and new subsidiaries joining the Group.
- Contributions to the Depositors’ and Investors’ Guarantee Fund increased by ISK 94m between years, from ISK 432m in 1H11 to ISK 526m in 1H12, due to a legislation change in 2012 and a slight increase in the deposit base.
- Salaries and related expenses amounted to ISK 6,620m in 1H12, compared to ISK 4,969m in 1H11. The increase between the years can mainly be attributed to the Byr merger and the new financial activities tax of 5.45% of total salaries which was introduced in the beginning of 2012.
- The average number of full time employees at the Bank was 1,112 in 1H12, compared to 982 in 1H11, which is again due to the Byr merger.

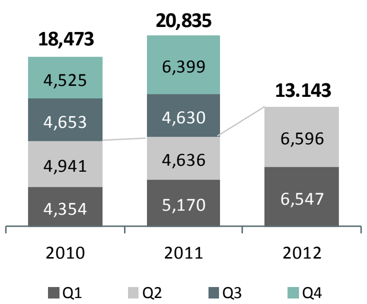
TAXES

- Income tax for 1H12 was ISK 2,998m compared to ISK 2,067m in 1H11. Taxation in 2011 increased considerably from the previous year with the corporation income tax rate increasing from 18% to 20%. In addition, financial institutions have to pay financial activities tax of 6% of profit above ISK 1bn.
- The bank tax, introduced in 2010, is calculated as 0.041% of the previous year’s total liabilities, amounts to ISK 407m. In comparison, bank tax for 1H11 was ISK 344m. This includes a temporary tax on financial intuitions of 0.0875% of the previous year’s total liabilities to finance a two year (2011 and 2012) tax credits on mortgage interest expenses.

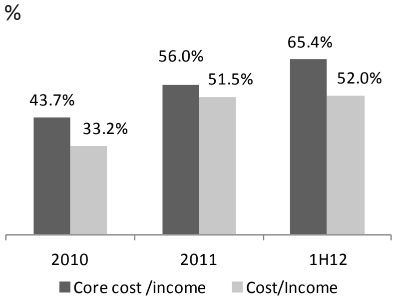
NET FEE AND COMMISSION INCOME
ISKm



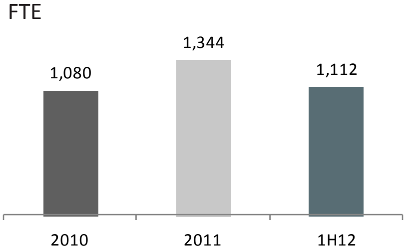
ADMINISTRATIVE EXPENSES
ISKm



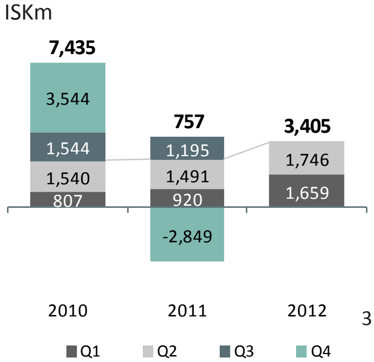
COST / INCOME RATIOS (excl.goodwill)
%



AVERAGE # OF EMPLOYEES (parent)
FTE



TAXES
ISKm

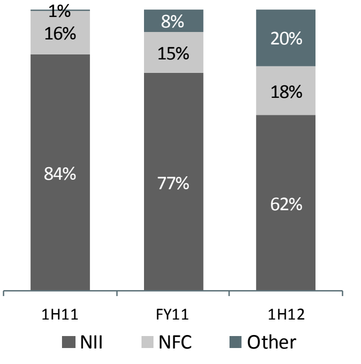


INCOME STATEMENT – cont.

PROFIT FROM DISCONTINUED OPERATIONS

- Profit from discontinued operations net of tax was ISK 2,919m in 1H12, compared to ISK 849m in 1H11. The increase can mainly be attributed to the sale of Jardboranir, which was owned by Íslandsbanki's subsidiary Miðengi, as well as rental income and income from foreclosed assets.

INCOME SPLIT
%



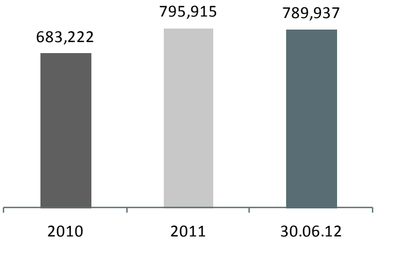
BALANCE SHEET

ASSETS	ISKm	30.06.12	31.03.12	31.12.11
Cash and balances with CB		**72,072**	78,398	57,992
Derivatives		**306**	205	339
Bonds and debt instruments		**50,386**	55,579	58,662
Shares and equity instruments		**9,870**	12,736	11,107
Loans to credit institutions		**50,218**	46,461	43,655
Loans to customers		**545,898**	537,847	564,394
Investment in associates		**912**	917	1,070
Property and equipment		**5,629**	5,530	5,276
Intangible assets		**608**	580	544
Deferred tax assets		**1,997**	2,049	2,629
Non-current assets held for sale		**39,149**	39,723	42,690
Other assets		**12,892**	12,393	7,557
Total assets		**789,937**	792,418	795,915

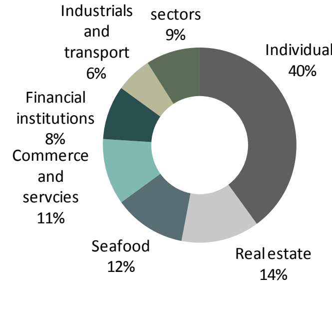
ASSETS

- The Bank's total assets amounted to ISK 789,937m at end of June, compared to ISK 792,418m at end of March 2012.
- Loans to customers amounted to ISK 545,898 at end of June, compared to ISK 537,847 at end of March 2012. This is the quarter whereby new lending exceeds repayments.
- Restructuring of the largest corporate clients' loan portfolio is expected to be largely completed by the end of 2012 and by the end of 2013 for the remaining loan portfolios.
- The bank's bonds and debt instruments amounted to ISK 50,218m. The portfolio consists mainly of G5 government bonds with no exposure to GIPSIs.
- Shares and equity instruments amounted to ISK 9,870m, down from ISK 12,736m since end of March 2012, mainly due to sale of equity stakes in Icelandair.
- Non-current assets held for sale amounted to ISK 39,149 at end of June, compared to ISK 39,723m at the end of March. The decrease is partly due to a sale of a majority stake in Jardboranir, which was owned by Íslandsbanki's subsidiary Miðengi.

TOTAL ASSETS
ISKm



ASSETS BY SECTOR
%



BALANCE SHEET

LIABILITIES & EQUITY	ISKm	30.06.12	31.03.12	31.12.11
Financial liabilities		**11,154**	10,596	9,346
Derivatives		**5,377**	5,761	4,027
Deposits from CB and credit inst.		**41,914**	52,470	62,845
Deposits from customers		**457,887**	456,821	462,943
Debt issued and other borrowings		**66,513**	65,647	63,221
Subordinated loans		**21,853**	23,303	21,937
Current tax liabilities		**1,156**	2,706	2,670
Deferred tax liabilities		**238**	19	17
Non-current liabilities held for sale		**5,761**	6,482	7,317
Other liabilities		**42,603**	39,193	37,889
Total liabilities		**654,456**	662,998	672,212
Total equity		**135,481**	129,420	123,703
Total liabilities and equity		**789,937**	792,418	795,915

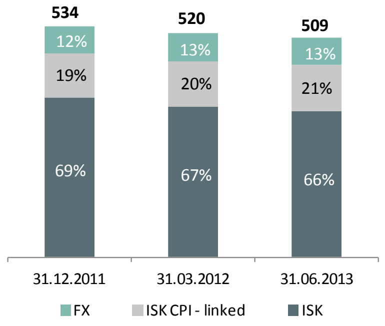
LIABILITIES

- Total liabilities amounted to ISK 654,456m at end of June, compared to ISK 662,998m at end of March.
- Deposits from customers have remained stable at ISK 457,887m at end of June, compared to ISK 456,821m at end of March, rendering a strong deposit to loan ratio of 83.8% and a customer deposit to loan ratio of 83.9%.
- Subordinated loans amounted to ISK 21,853 and comprise a EUR 138m denominated Tier II Government bond following an agreement with Glitnir and the Icelandic Government in September 2009.
- At end of June, the Bank's total equity was ISK 135,481m, compared to ISK 129,420m at end of March, which is an increase of 5% over the period and an increase of 10% since year-end 2011.
- The Tier 1 ratio was 20.2% and the total capital ratio was 23.5% which is well above the 16% regulatory minimum set by the Icelandic Financial Supervisory Authority. Capital ratios have been increasing on the back of higher retained earnings, and were it not for a new interpretation of rules for risk weight on real estate loans, the total capital ratio would have increased by 0.7%.

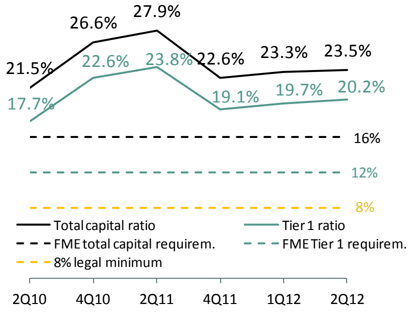
FUNDING AND LIQUIDITY POSITION

- The Bank's liquidity position is sound and all liquidity ratios well above regulatory requirements.
- The Bank has been largely funded with deposits since its incorporation in 2008.
- Íslandsbanki was the first bank to list securities on the NASDAQ OMX Iceland since the fall of 2008, an important step towards diversification of funding for the Bank. Under the ISK 100bn covered bond programme that is in place, Íslandsbanki plans to issue around ISK 10bn of covered bonds annually.
- To date, Íslandsbanki has issued three CPI-linked covered bonds, the five year ISLA CBI 16, the 7 year ISLA CBI 19, and the 12 year ISLA CBI 24 totalling of ISK 8.8bn. All issuances were oversubscribed and sold to a broad group of institutional investors.
- The Bank is not reliant on foreign currency funding and does not have a need to raise such funds in the short to medium term. The Bank has however been exploring its options and will take advantage of opportunities to fund loan book growth should they arise.

DEPOSITS - PARENT
ISKbn



CAPITAL RATIO
%



FINANCIAL CALENDAR

Íslandsbanki plans to publish its interim and annual financial statements according to the financial calendar below:

- 3Q2012 - 29 November 2012
  - Silent period 18-28 Nov
- 4Q2012 -7 March 2013
  - Silent period 25 Feb – 6 Mar
- AGM - April 2013

Please note that the dates may change so please refer to the Bank's website for correct dates.