Condensed Consolidated
Interim Financial Statements

1 January - 31 March 2019

Arion Bank

Contents

Arion Bank in brief

2.1%

Return on equity

58.6%

Cost-to-income

21.3%

CET 1

Rating from S&P

Long term: BBB+

Short term: A-2

Outlook: Stable

Equal Pay Certification

IMARK

Marketing company of the year 2018

Arion Bank

- Arion Bank is a leading universal relationship bank in Iceland which provides a full range of financial services
- The economic environment is still favorable with low unemployment and a 4.6% GDP growth in 2018, but a slowdown is expected in 2019
- The balance sheet remains strong with equal split between retail and corporate loans, high capital ratios and improved asset quality
- Arion Bank was named investment bank of the year 2018 in Iceland by Euromoney
- Arion Bank is the leading bank in digital solutions on the Icelandic market and a new Bank app has been launched

Key figures

(ISK million)

	Q1 2019	Q1 2018
Net earnings	1,018	1,949
ROE	2.1%	3.6%
Net interest margin	2.7%	2.7%
Cost to income ratio	58.6%	62.5%
	31.12.2019	**31.12.2018**
Total assets	1,222,695	1,164,327
Loans to customers	829,246	833,826
Deposits	490,474	466,067
Borrowings	445,077	417,782
Stage 3 gross	2.5%	2.6%
Leverage ratio	13.5%	14.2%
Number of employees	917	904
EUR/ISK	137.50	133.23

RETAIL BANKER INTERNATIONAL

Most Disruptive Innovation of the year

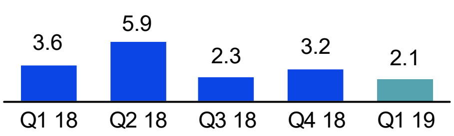
banking technology AWARDS 2018

Best tech overhaul project

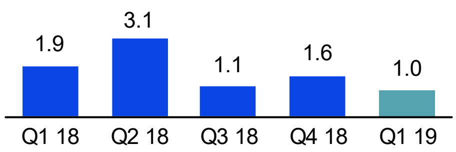
BAI Global Innovation Awards

Most innovative accelerator – Digital mortgages

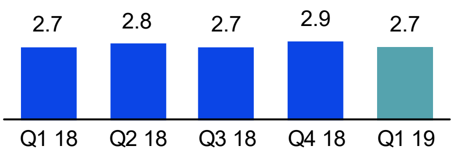
Return on equity (%)



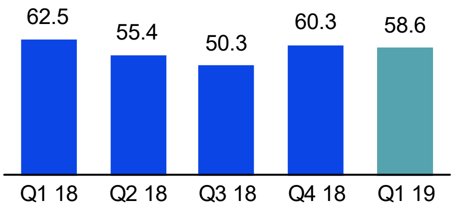
Net earnings (ISK billion)



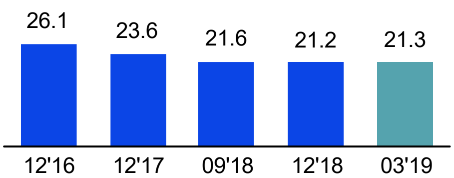
Net interest margin (%)



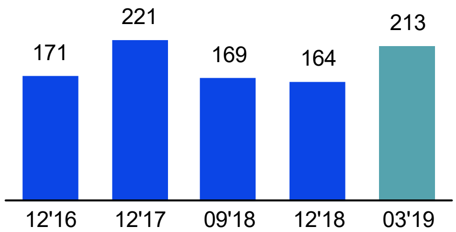
Cost-to-income ratio (%)



CET 1 ratio (%)*



LCR ratio (%)



Endorsement and statement
by the Board of Directors and the CEO

The Condensed Consolidated Interim Financial Statements of Arion Bank for the period from 1 January to 31 March 2019 include the Condensed Consolidated Interim Financial Statements of Arion Bank ("the Bank") and its subsidiaries, together referred to as "the Group".

Operations during the period

Arion Bank reported earnings of ISK 1,018 million in the first quarter of 2019 and total equity amounted to ISK 193,054 million at the end of the period. Return on equity was 2.1% in the quarter. Net interest income increased by 9%, compared with the same period in 2018. At the end of March 2019 WOW Air, a client of the Bank, filed for bankruptcy. Arion Bank had to make impairment on loans and guarantees which negatively affected the financial results of the Bank by ISK 1.3 billion in the first quarter of 2019. In March 2019 Arion Bank sold its entire shareholding in the associate Farice ehf. The profit from the sale amounted to ISK 0.7 billion. In April 2019 Reykjavík District Court issued a decision on the case Datacell ehf. and Sunshine Press Productions ehf. vs. Valitor hf., a subsidiary of Arion Bank hf. Valitor was ordered to pay the plaintiffs a total of ISK 1.2 billion in damages. The net effect on the Consolidated Interim Income Statement during the first quarter of 2019 was ISK 0.6 billion after tax considerations. The Group had already accounted for the loss in its capital calculations.

The Group's capital ratio, as calculated under the Financial Undertakings Act No. 161/2002, was 22.3% and the CET 1 ratio was 21.3%. According to the Financial Undertakings Act, the official capital ratio shall be based on audited or reviewed own funds. Since the Interim Financial Statements for the first quarter are not audited the official capital ratio is based on audited own funds on 31 December 2018 and risk-weighted assets on 31 March 2019. The official capital ratio on 31 March was 24.3% and the official CET 1 ratio was 21.2%, which comfortably meets the requirements set by law and the Financial Supervisory Authority (FME). The Bank's liquidity position was also strong at period end and well above the regulatory minimum.

The main changes on the asset side of the Bank's balance sheet during the first quarter of 2019 were an increase in cash and loans to credit institutions, up ISK 40 billion, and an increase in financial instruments. The liquidity position at period end is exceptionally high as the Bank was preparing for the repayment of borrowings in April 2019, both EMTN, amounting to the equivalent of ISK 20 billion, and structured covered bonds prepayments amounting to ISK 7 billion. The main changes on the liabilities side during the period are increased new borrowings, increased deposits and reduced equity following the payment of dividends.

In recent quarters, the digital journey of Arion Bank has produced outstanding results and in the first quarter of 2019 this journey continues with the launch of the biggest update of the Arion app to date. The app is now open to non-customers which shows an early step in our open bank commitment. The Bank also considers this as an opportunity to acquire and welcome new customers.

Arion Bank is in the process of potentially divesting most of, or all of, the Bank's shareholding in Valitor Holding hf. The company is therefore categorized as held for sale in the Consolidated Interim Financial Statements, see Note 5. The sales process and necessary preparatory work is close to completion and marketing to potential investors will start in the coming weeks. In April, Valitor entered into a new 2 year agreement with Stripe, which is one of the leading Fintech companies in the world. Stakksberg ehf. (United Silicon) is also categorized as a disposal group held for sale. The sale of Stakksberg ehf. has been delayed due to regulatory complications. Stakksberg ehf. has made progress in this respect and Arion Bank aims to conduct a sales process as soon as possible.

Economic environment and outlook

According to preliminary figures, GDP growth measured 4.6% in 2018, considerably stronger than expected at the beginning of the year. The composition of growth has been relatively favorable, with foreign trade making a positive contribution, thus compensating for much slower investment growth. Private consumption is, however, still the main driving force, but growth is rapidly slowing down. Despite strong growth in 2018, the outlook for 2019 is bearish due to difficulties in the country's main export sectors. Following the bankruptcy of WOW air in March, a decrease in the number of tourist arrivals is expected. In addition, the grounding of Boeing MAX 8 aircraft has disrupted Icelandair's route network. A certain section of the seafood industry is also suffering, as insufficient numbers of capelin were located to allow fishing of this species this year. Households have been acting with caution, resulting in slower private consumption growth. Rising unemployment and increasing housing prices are expected to dampen private consumption even further. Inflation is still low in a historical context but is currently above the Central Bank of Iceland's 2.5% inflation target. It is likely that inflationary pressures will continue to pick up, with a weaker króna and pending wage increases. Recent collective wage agreements between unions and employers, with an emphasis on longer term purchasing power, working hours and housing initiatives, reflect the deteriorating short-term economic outlook. Arion Research predicts a short recession in 2019, rising unemployment and a rise in inflation in the coming months.

Group ownership

At the end of March 2019, Kaupskil ehf. was the largest shareholder of Arion Bank with a holding of 32.67%. In April 2019 the shareholders list changed significantly when Kaupskil ehf. sold a 15% shareholding in the Bank, and Arion Bank's share capital was reduced by ISK 186 million at nominal value, by cancelling the vast majority of the Bank's own shares. After these transactions Kaupskil ehf. remains the largest shareholder with a holding of 20.00% and Taconic Capital is the second largest with a holding of 16.03%, see Note 36.

Capital and Dividend

At the Annual General Meeting of Arion Bank on the 20 March 2019 a dividend payment of ISK 10 billion was approved. Taking into account the Bank's own shares, the net dividend payment was ISK 9.1 billion. The dividend amounted to ISK 5.00 per share and the payment date was 29 March 2019.

In April 2019 Arion Bank's share capital was reduced by ISK 186 million at nominal value, totalling 186 million shares, by cancelling the Bank's own shares. Arion Bank's share capital is ISK 1,814 million after the reduction. Both the dividend payment and reduction of share capital are in line with the Bank's strategy of optimizing its capital structure.

Endorsement and statement
by the Board of Directors and the CEO

Governance

At the last Annual General Meeting on 20 March 2019, six members were elected to serve on the Board of Directors until the next AGM, three women and three men. Furthermore, three Alternate Directors (two men and one woman) were elected and they attend meetings of the Board of Directors in the event that a Director resigns or is unable to attend. Two of the members are new on the Board of Directors.

In April 2019 Höskuldur H. Ólafsson resigned as CEO of Arion Bank. The CFO of Arion Bank, Stefán Pétursson, has been appointed acting CEO until a new CEO has been recruited.

Endorsement of the Board of Directors and the Chief Executive Officer

The Condensed Consolidated Interim Financial Statements of Arion Bank for the period ended 31 March 2019 have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union and additional requirements in the Icelandic Financial Statements Act, Financial Undertakings Act and Rules on Accounting for Credit Institutions.

It is our opinion that the Condensed Consolidated Interim Financial Statements give a true and fair view of the financial performance and cash flow of the Group for the period ended 31 March 2019 and its financial position as at 31 March 2019.

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

The Board of Directors and the CEO have today discussed the Condensed Consolidated Interim Financial Statements of Arion Bank for the period ended 31 March 2019 and confirm them by means of their signatures.

Reykjavík, 8 May 2019

Board of Directors

Brynjólfur Bjarnason
Chairman

Benedikt Gíslason

Herdís Dröfn Fjeldsted

Liv Fiksdahl

Renier Lemmens

Steinunn K. Thórdardóttir

Acting Chief Executive Officer

Stefán Pétursson

Consolidated Interim Income Statement

	Notes	2019 1.1.-31.3.	2018 1.1.-31.3.
Interest income		14,684	14,044
Interest expense		(7,250)	(7,217)
Net interest income	7	**7,434**	**6,827**
Fee and commission income		2,630	2,575
Fee and commission expense		(412)	(370)
Net fee and commission income	8	**2,218**	**2,205**
Net financial income	9	766	1,387
Net insurance income	10	253	143
Share of profit of associates	26	727	(20)
Other operating income	11	310	268
Other net operating income		**2,056**	**1,778**
Operating income		**11,708**	**10,810**
Salaries and related expenses	12	(3,630)	(3,616)
Other operating expenses	13	(3,232)	(3,143)
Operating expenses		**(6,862)**	**(6,759)**
Bank levy	14	(906)	(804)
Net impairment	15	(1,081)	(135)
Earnings before income tax		**2,859**	**3,112**
Income tax expense	16	(622)	(890)
Net earnings from continuing operations		**2,237**	**2,222**
Discontinued operations held for sale, net of income tax	17	(1,219)	(273)
Net earnings		**1,018**	**1,949**

Attributable to

Shareholders of Arion Bank hf.		1,018	1,949
Non-controlling interest		-	-
Net earnings		**1,018**	**1,949**

Earnings per share

Basic and diluted earnings per share attributable to the shareholders of Arion Bank (ISK)	18	0.56	1.01

Comparative figures have been restated as the subsidiary Valitor Holding hf. has been classified as disposal group held for sale, see Note 5.

The accompanying Notes are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK millions

Consolidated Interim Statement of Comprehensive Income

	Notes	2019 1.1.-31.3.	2018 1.1.-31.3.
Net earnings		**1,018**	**1,949**
Net gain on financial assets carried at fair value through OCI, net of tax		99	30
Realized net gain on financial assets carried at fair value through OCI, net of tax, transferred to the Income Statement	9	(31)	(97)
Changes to reserve for financial instruments at fair value through OCI		**68**	**(67)**
Exchange difference on translating foreign subsidiaries		180	(59)
Other comprehensive income, net of tax		**248**	**(126)**
Total comprehensive income		**1,266**	**1,823**

Attributable to

Shareholders of Arion Bank	1,266	1,823
Non-controlling interest	-	-
Total comprehensive income	**1,266**	**1,823**

The accompanying Notes are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK millions

Consolidated Interim Statement of Financial Position

Assets	Notes	31.3.2019	31.12.2018
Cash and balances with Central Bank	19	94,124	83,139
Loans to credit institutions	20	84,978	56,322
Loans to customers	21	829,246	833,826
Financial instruments	22-24	128,103	114,557
Investment property	24	7,101	7,092
Investments in associates	26	807	818
Intangible assets	27	7,081	6,397
Tax assets	28	15	90
Assets and disposal groups held for sale	29	51,321	48,584
Other assets	30	19,919	13,502
Total Assets		**1,222,695**	**1,164,327**

Liabilities			
Due to credit institutions and Central Bank	23	9,183	9,204
Deposits	23	490,474	466,067
Financial liabilities at fair value	23	2,286	2,320
Tax liabilities	28	4,822	5,119
Liabilities associated with disposal groups held for sale	29	29,498	26,337
Other liabilities	31	41,018	30,107
Borrowings	23,32	445,077	417,782
Subordinated liabilities	23,33	7,283	6,532
Total Liabilities		**1,029,641**	**963,468**

Equity			
Share capital and share premium	35	59,008	59,010
Other reserves		15,439	14,822
Retained earnings		118,477	126,897
Total Shareholders' Equity		**192,924**	**200,729**
Non-controlling interest		130	130
Total Equity		**193,054**	**200,859**
Total Liabilities and Equity		**1,222,695**	**1,164,327**

The accompanying Notes are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK millions

Consolidated Interim Statement of Changes in Equity

			Restricted reserves								
	Share capital	Share premium	Gain in subs. & assoc., unrealized	Gain in securities, unrealized	Financial assets at fair value thr. OCI unrealized	Statutory reserve	Foreign currency trans-lation reserve	Retained earnings	**Total share-holders' equity**	Non-cont-rolling interest	**Total equity**
Equity 1 January 2019	1,814	57,196	12,373	417	87	1,637	308	126,897	**200,728**	130	**200,858**
Net earnings								1,018	**1,018**		**1,018**
Net fair value gain					99				**99**		**99**
Realized net gain transferred to the Income Statement					(31)				**(31)**		**(31)**
Translation difference							180		**180**		**180**
Total comprehensive income .	**-**	**-**	**-**	**-**	**68**	**-**	**180**	**1,018**	**1,266**	**-**	**1,266**
Dividend paid								(9,069)	**(9,069)**		**(9,069)**
Changes in treasury stock *		(2)							**(2)**		**(2)**
Changes in reserves			194	175				(369)	**-**		**-**
Equity 31 March 2019	**1,814**	**57,194**	**12,567**	**592**	**155**	**1,637**	**488**	**118,477**	**192,924**	**130**	**193,054**
Equity 31 December 2017	2,000	73,861	14,050	903	-	1,637	185	132,971	**225,606**	128	**225,734**
Impact of adopting IFRS 9				(108)	110			939	**941**		**941**
Restated opening balance	**2,000**	**73,861**	**14,050**	**795**	**110**	**1,637**	**185**	**133,910**	**226,548**	**128**	**226,676**
Net earnings								1,949	**1,949**		**1,949**
Net fair value gain					30				**30**		**30**
Realized net gain transferred to the Income Statement					(97)				**(97)**		**(97)**
Translation difference							(59)		**(59)**		**(59)**
Total comprehensive income .	**-**	**-**	**-**	**-**	**(67)**	**-**	**(59)**	**1,949**	**1,823**	**-**	**1,823**
Dividend paid								(7,115)	**(7,115)**		**(7,115)**
Purchase of treasury stock **	(190)	(16,949)							**(17,139)**		**(17,139)**
Changes in reserves			(1,453)	(426)	108			1,771	**-**		**-**
Equity 31 March 2018	**1,810**	**56,912**	**12,597**	**369**	**151**	**1,637**	**126**	**130,515**	**204,117**	**128**	**204,245**

* In 2018 close to 4 million shares were allocated to employees at ISK 75 per share, a total of ISK 295 million. In accordance with the employees stock grant programme, an employee who resigns within the vesting period of two years, returns the shares to the Bank.

** Refers to the changes in the holding of own shares related to the decision to accept an offer from Kaupskil ehf., a subsidiary of Kaupthing ehf., to buy back 9.5% of issued share capital in Arion Bank, or 190 million shares. The decision to accept the offer from Kaupskil ehf. is in line with the decision taken at a shareholders' meeting on 12 February 2018 to amend the Bank's articles of association with a temporary authorization for the Board of Directors to buy back shares issued by the Bank. Arion Bank paid ISK 90.087 a share, a total of ISK 17,139 million.

The accompanying Notes are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK millions

Consolidated Interim Statement of Cash flows

	2019 1.1.-31.3.	2018 1.1.-31.3.
Operating activities		
Net earnings	1,018	1,949
Non-cash items included in net earnings	(3,185)	(5,798)
Changes in operating assets and liabilities:		
Loans to credit institutions, excluding bank accounts	(12,616)	(3,187)
Loans to customers	10,490	(19,780)
Financial instruments and financial liabilities at fair value	(11,695)	3,307
Deposits	18,467	(9,007)
Borrowings	20,593	19,625
Other changes in operating assets and liabilities	488	(3,955)
Interest received	14,096	12,971
Interest paid	(4,418)	(4,720)
Dividend received	81	95
Income tax paid	(844)	(1,158)
Net cash from (to) operating activities	**32,475**	**(9,658)**
Investing activities		
Proceeds from sale of associates	740	-
Net investment in intangible assets and property and equipment	(680)	(213)
Net investment in intangible assets and property and equipment at Valitor	-	(410)
Net cash from (to) investing activities	**60**	**(623)**
Financing activities		
Issued subordinated liabilities	677	-
Dividend paid to shareholders of Arion Bank	(9,069)	(24,254)
Net cash used in financing activities	**(8,392)**	**(24,254)**
Net (decrease) increase in cash and cash equivalents	24,143	(34,535)
Cash and cash equivalents at beginning of the year	110,589	181,898
Effect of exchange rate changes on cash and cash equivalents	2,081	(1,047)
Cash and cash equivalents	**136,813**	**146,316**
Cash and cash equivalents		
Cash and balances with Central Bank	94,124	97,934
Bank accounts	52,851	57,776
Mandatory reserve deposit with Central Bank	(10,162)	(9,394)
Cash and cash equivalents	**136,813**	**146,316**

Comparative figures have been restated as the subsidiary Valitor Holding hf. was classified as disposal group held for sale in 2018, see Note 5. Cash and cash equivalents at Valitor amounting to ISK 10,644 million are included in Cash and cash equivalents at 31 March 2018.

The accompanying Notes are an integral part of these Condensed Consolidated Interim Financial Statements

Amounts are in ISK millions

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Notes to the Condensed Consolidated Interim Financial Statements

General information

Arion banki hf., the Parent Company, was established 18 October 2008 and is incorporated and domiciled in Iceland. The registered office of Arion banki hf. is located at Borgartún 19, Reykjavík. The Condensed Consolidated Interim Financial Statements for the period ended 31 March 2019 comprise the Parent Company and its subsidiaries (together referred to as "the Group").

1. Basis of preparation

The Condensed Consolidated Interim Financial Statements were approved and authorized for issue by the Board of Directors of Arion Bank on 8 May 2019.

In preparing these Consolidated Interim Financial Statements, the Bank has applied the concept of materiality to the presentation and level of disclosure. Only essential and mandatory information is disclosed which is relevant to an understanding by the reader of these Consolidated Interim Financial Statements.

Statement of compliance

The Condensed Consolidated Interim Financial Statements have been prepared in accordance with International Financial Reporting Standard, IAS 34 Interim Financial Reporting, as adopted by the European Union and additional requirements in the Icelandic Financial Statements Act, Financial Undertakings Act and rules on Accounting for Credit Institutions. The Condensed Consolidated Interim Financial Statements do not include all the information and disclosures required in the Annual Financial Statements, and should be read in conjunction with Arion Bank's Annual Financial Statements for the year ended 31 December 2018. The Annual Financial Statements are available at Arion Bank's website www.arionbanki.is.

The same accounting policies, presentation and methods of computation are followed in these Condensed Consolidated Interim Financial Statements as were applied in the Consolidated Financial Statements for the year ended 31 December 2018, except for IFRS 16 Leases, effective 1 January 2019, see Note 3.

Due to the reclassification of the subsidiary Valitor Holding hf. as disposal group held for sale, in accordance with IFRS 5, comparative figures in the Consolidated Interim Income Statement have been restated, see Note 5.

Basis of measurement

The Condensed Consolidated Interim Financial Statements have been prepared on a historical cost basis except for assets and liabilities measured under IFRS 9. For further details on the accounting policy for assets and liabilities under IFRS 9, see Note 57 in the Annual Financial Statements 2018.

Functional and presentation currency

The Consolidated Interim Financial Statements are presented in Icelandic krona (ISK), which is the Parent Company's functional currency, rounded to the nearest million, unless otherwise stated. At the end of the period the exchange rate of the ISK against USD was 122.51 and 137.50 for EUR (31.12.2018: USD 116.34 and EUR 133.20).

2. Going concern assumption

The Group's management has made an assessment of the ability to continue as a going concern and is satisfied that the Group has the resources to continue. In making this assessment, management has taken into consideration the risk exposures facing the Group which are further described in the Risk Management Disclosures. The Consolidated Interim Financial Statements are prepared on a going concern basis.

3. Changes in accounting policies

Arion Bank initially adopted IFRS 16 Leases from 1 January 2019. The Group has not early adopted any standards, interpretations or amendments that have been issued but are not effective.

IFRS 16

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

4. Significant accounting estimates and judgements in applying accounting policies

The preparation of the Consolidated Interim Financial Statements requires management to make judgements, estimates and assumptions that affect the reported amount of revenues, expenses, assets and liabilities, and the accompanying disclosures, as well as the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods.

Notes to the Condensed Consolidated Interim Financial Statements

5. The Group

Shares in the main subsidiaries in which Arion Bank holds a direct interest

			Equity interest	
	Operating activity	Currency	31.3.2019	31.12.2018
Arion Bank Mortgages Instit. Investor Fund, Borgartún 19, Reykjavík, Iceland ..	Retail banking	ISK	100.0%	100.0%
BG12 slhf., Katrínartún 2, Reykjavík, Iceland	Holding company	ISK	62.0%	62.0%
Eignarhaldsfélagid Landey ehf., Ögurhvarf 4a, Kópavogur, Iceland	Real estate	ISK	100.0%	100.0%
Eignabjarg ehf., Borgartún 19, Reykjavík, Iceland	Holding company	ISK	100.0%	100.0%
Stefnir hf., Borgartún 19, Reykjavík, Iceland	Asset management	ISK	100.0%	100.0%
Valitor Holding hf., Dalshraun 3, Hafnarfjördur, Iceland	Payment solutions	ISK	100.0%	100.0%
VISA Ísland ehf., Borgartún 19, Reykjavík, Iceland	Holding company	ISK	100.0%	100.0%
Vördur tryggingar hf., Borgartún 25, Reykjavík, Iceland	Insurance	ISK	100.0%	100.0%

The subsidiaries Eignabjarg ehf. (holding company of Stakksberg ehf.) and Valitor Holding hf. are classified as a disposal groups held for sale, see Note 29.

Valitor Holding hf.

Arion Bank's shareholding in the subsidiary Valitor Holding hf. (Valitor) was 100% at 31 December 2018. The Bank is in the process of potentially divesting the Bank's shareholding in Valitor and has appointed Citi as a sales advisor. According to the Bank is aiming for having completed the sale of Valitor within the 12 months set as requirement for classification as held for sale asset in IFRS. The sales process is based on invitations only.

In accordance with IFRS 5 Non-current assets and disposal groups held for sale Valitor has been classified as disposal group held for sale in these Condensed Consolidated Interim Financial Statements, resulting in a change in the presentation in the Consolidated Interim Income Statement. Net earnings of Valitor are recognized in a single line item as Discontinued operations held for sale, net of income tax. The comparative figures in the Consolidated Interim Income Statement for the first quarter of 2018 have been restated.

Restated Consolidated Interim Income Statement for 1.1.-31.3.2018

	Published accounts	Valitor	Restated accounts
Interest income	14,162	(118)	14,044
Interest expense	(7,254)	37	(7,217)
Net interest income	**6,908**	**(81)**	**6,827**
Fee and commission income	8,197	(5,622)	2,575
Fee and commission expense	(4,655)	4,285	(370)
Net fee and commission income	**3,542**	**(1,337)**	**2,205**
Net financial income	1,340	47	1,387
Net insurance income	143	-	143
Share of profit of associates	(18)	(2)	(20)
Other operating income	269	(1)	268
Other net operating income	1,734	44	1,778
Operating income	**12,184**	**(1,374)**	**10,810**
Salaries and related expenses	(4,636)	1,020	(3,616)
Other operating expenses	(3,996)	853	(3,143)
Operating expenses	**(8,632)**	**1,873**	**(6,759)**
Bank levy	(804)	-	(804)
Net impairment	(99)	(36)	(135)
Earnings before income tax	**2,649**	**463**	**3,112**
Income tax expense	(818)	(72)	(890)
Net earnings from continuing operations	**1,831**	**391**	**2,222**
Discontinued operations held for sale, net of income tax	118	(391)	(273)
Net earnings	**1,949**	**-**	**1,949**

Prior to the restatement the operations of Valitor were presented as the operating segment Subsidiaries and other divisions, see Note 6.

In the Consolidated Interim Statement of Financial Position the total assets of Valitor are recognized as Assets and disposal groups held for sale and the total liabilities as Liabilities associated with disposal groups held for sale, see Note 29.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

5. The Group, continued

Total assets and total liabilities of Valitor

	31.3.2019	31.12.2018
Assets		
Cash and balances with Central Bank	3,161	7,441
Loans to credit institutions	24,520	19,300
Loans to customers	2,170	2,258
Financial instruments	-	174
Investments in associates	58	58
Intangible assets	8,651	8,267
Tax assets	474	101
Other assets	3,456	2,404
	42,490	**40,003**
Liabilities		
Due to credit institutions and Central Bank	808	-
Financial liabilities at fair value	48	8
Tax liabilities	463	136
Other liabilities	28,172	26,185
Borrowings	7	8
Total Liabilities	**29,498**	**26,337**
Elimination within Arion Bank Group	1,172	2,116
Book value of Valitor	**14,164**	**15,782**

Income Statement of Valitor

1.1-31.3.2019	Valitor	Elimination	Valitor contribution
Net interest income	201	(3)	198
Net fee and commission income	157	583	740
Net financial income	131	-	131
Other operating income	2	-	2
Operating income	**491**	**580**	**1,071**
Salaries and related expense	(1,236)	-	(1,236)
Other operating expense	(1,205)	-	(1,205)
Operating expenses	**(2,441)**	**-**	**(2,441)**
Net impairment	(23)	-	(23)
Earnings before income tax	**(1,973)**	**580**	**(1,393)**
Income tax expense	174	-	174
Net earnings	**(1,799)**	**580**	**(1,219)**

1.1-31.3.2018	Valitor	Elimination	Valitor contribution
Net interest income	85	(4)	81
Net fee and commission income	1,151	186	1,337
Net financial income	113	(160)	(47)
Other operating income	3	-	3
Operating income	**1,352**	**22**	**1,374**
Salaries and related expense	(1,020)	-	(1,020)
Other operating expense	(853)	-	(853)
Operating expenses	**(1,873)**	**-**	**(1,873)**
Net impairment	36	-	36
Earnings before income tax	**(484)**	**22**	**(462)**
Income tax expense	72	-	72
Net earnings	**(413)**	**22**	**(391)**

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

Operating segment reporting

Segment information is presented in respect of the Group's operating segments and is based on the Group's management and internal reporting structure. Segment performance is evaluated based on earnings before tax. In presenting the geographic information, segment revenue has been based on the geographic location of customers or assets.

Inter segment pricing is determined on an arm's length basis. Operating segments pay and receive interest to and from Treasury on an arm's length basis to reflect the allocation of capital, funding cost and relevant risk premium.

6. Operating segments

The Group comprises the following operating segments:

Asset Management comprises Institutional Asset Management, Private Banking, Investment Services and Pension Fund Administration. Asset Management manages financial assets on behalf of its customers according to a pre-determined investment strategy. In addition the division is the main distributor of funds managed by Stefnir hf. to individuals, companies and institutional investors and also distributes funds managed by international fund management companies. Asset Management also administers pension funds. Stefnir hf. is an independently operating financial company owned by Arion Bank. Stefnir manages a broad range of mutual funds, investment funds and institutional investor funds.

Corporate Banking services larger corporate clients, both in Iceland and abroad. Experienced account managers specializing in key economic sectors such as retail and services, seafood, energy and real estate are responsible for conducting larger transactions and developing strong business relationships with clients. The division provides a full range of lending products such as guarantees, deposit accounts, payment solutions and a variety of value-added digital solutions to meet the needs of the Bank's larger corporate clients. The Corporate Banking portfolio includes several larger international transactions, mainly in syndicates with other Icelandic banks and international banks.

Investment Banking comprises Corporate Finance, Capital Markets and Research. Investment Banking is a leading Icelandic brokerage house and financial advisor, providing a full and diverse range of investment banking services to a broad range of customers. Corporate Finance offers various financial advisory and capital raising services including M&A and financial restructuring advice and IPO management services. Capital Markets is a leading securities and foreign exchange brokerage and provides clients with a diverse range of fixed income services and risk management products. Research is an independent research team producing in-depth analysis of the Icelandic economy and financial markets.

Retail Banking, including Arion Bank Mortgages Institutional Investor Fund, provides a comprehensive range of products and services, including mortgage loans, savings and current accounts, vehicle and equipment financing, factoring, payment cards, pension services, insurance and funds, to both individuals and SMEs. Retail Banking has a strong focus on digital banking solutions, using the online bank and the Arion Bank app as key channels. Retail Banking operates out of 20 branches across Iceland over 100,000 customers during the year.

Treasury is responsible for the Bank's liquidity, currency and interest rate management. Other functions of Treasury are funds' transfer pricing and hedging and pricing of financial products.

Subsidiaries and other divisions include the subsidiaries Vördur tryggingar hf., which is an insurance company, Eignarhaldsfélagid Landey ehf., which holds the main part of investment property of the Group and the holding companies VISA Ísland ehf., BG12 slhf. and other smaller entities of the Group, as well as Market Making in domestic securities and currencies. The subsidiary Valitor Holding is classified as Disposal group held for sale. The subsidiary EAB 1 ehf. was sold in October 2018.

In addition to the above operating segments, the Group presents information for units at the corporate headquarters which carry out support functions such as Overhead, Risk Management, Finance (excluding Treasury and Market Making), Legal and IT. The information presented relating to the headquarters does not represent an operating segment. A significant proportion of expenses from support functions is allocated to operating segments in a separate line in the operating segment overview.

Other information. At the beginning of 2019 the proportion of the loan book divided between Corporate Banking and Retail Banking changed. SME loans amounting to approx. ISK 49 billion were transferred from Retail Banking to Corporate Banking. At the same time 20 employees were transferred between the operating segments. As a result of these changes the figures are not fully comparable with those from 2018.

At the beginning of 2019 the allocation of cost changed so that total expense is now allocated to the following operating segments: Asset Management, Corporate Banking, Investment Banking, Retail Banking and Treasury. Prior to the change cost relating to the Board of Directors, the CEO's Office and Compliance was not allocated to the operating segments. Comparative figures for 2018 have not been restated.

Notes to the Condensed Consolidated Interim Financial Statements

6. Operating segments, continued

1.1.-31.3.2019	Asset Manage-ment	Corporate Banking	Investment Banking	Retail Banking	Treasury	Subsidi-aries and Other divisions	Head-quarters and Elimination	Total
Net interest income	205	2,144	63	4,562	574	56	(170)	7,434
Net fee and commission income	757	320	475	1,092	(95)	(289)	(42)	2,218
Net financial income	133	(470)	6	(26)	(223)	1,551	(205)	766
Net insurance income	-	-	-	-	-	276	(23)	253
Share of profit of associates and net impairment	-	-	-	-	-	-	727	727
Other operating income (loss)	2	(4)	-	124	-	12	176	310
Operating income	1,097	1,990	544	5,752	256	1,606	463	11,708
Operating expense	(405)	(174)	(236)	(1,575)	(59)	(605)	(3,808)	(6,862)
Allocated expense	(328)	(933)	(190)	(1,771)	(284)	(8)	3,514	-
Bank levy	(46)	(190)	(11)	(339)	(320)	-	-	(906)
Net impairment	(5)	(1,032)	-	(43)	(1)	-	-	(1,081)
Earnings before income tax	313	(339)	107	2,024	(408)	993	169	2,859
Net seg. rev. from ext. customers	458	4,895	298	8,575	(4,845)	1,758	569	11,708
Net seg. rev. from other segments	639	(2,905)	246	(2,823)	5,101	(152)	(106)	-
Operating income	1,097	1,990	544	5,752	256	1,606	463	11,708
Depreciation and amortization	-	1	-	44	-	50	251	346
Total assets	77,478	335,024	16,881	551,654	526,414	95,893	(380,649)	1,222,695
Total liabilities	72,227	261,424	15,982	489,652	514,975	61,054	(385,673)	1,029,641
Allocated equity	5,251	73,600	899	62,002	11,439	34,839	5,024	193,054

1.1.-31.3.2018	Asset Manage-ment	Corporate Banking	Investment Banking	Retail Banking	Treasury	Subsidi-aries and Other divisions	Head-quarters and Elimination	Total
Net interest income	148	1,314	38	4,333	979	47	(32)	6,827
Net fee and commission income	866	236	465	1,092	(82)	(294)	(78)	2,205
Net financial income	15	(161)	2	-	268	584	679	1,387
Net insurance income	-	-	-	-	-	211	(68)	143
Share of profit of associates and net impairment	-	-	-	-	-	-	(20)	(20)
Other operating income	3	-	-	81	-	164	20	268
Operating income	1,032	1,389	505	5,506	1,165	712	501	10,810
Operating expense	(382)	(126)	(210)	(1,791)	(51)	(511)	(3,688)	(6,759)
Allocated expense	(219)	(762)	(182)	(1,660)	(278)	(6)	3,107	-
Bank levy	(46)	(170)	(10)	(278)	(300)	-	-	(804)
Net impairment	-	(376)	-	268	(29)	-	2	(135)
Earnings (loss) before income tax	385	(45)	103	2,045	507	195	(78)	3,112
Net seg. rev. from ext. customers	304	3,768	366	8,690	(3,993)	872	803	10,810
Net seg. rev. from other segments	728	(2,379)	139	(3,184)	5,158	(160)	(302)	-
Operating income	1,032	1,389	505	5,506	1,165	712	501	10,810
Depreciation and amortization	-	1	-	92	-	31	185	309
Total assets	62,603	269,324	22,435	545,300	484,548	89,961	(342,402)	1,131,769
Total liabilities	57,069	212,716	21,609	477,386	450,058	55,149	(346,463)	927,524
Allocated equity	5,534	56,608	826	67,914	34,490	34,812	4,061	204,245

Income taxes and discontinued operations held for sale are excluded from the profit and loss segment information.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

Notes to the Consolidated Interim Income Statement

7. Net interest income

1.1.-.31.3.2019	Amortized cost	Fair value thr. P/L	Fair value thr. OCI	Total
Interest income				
Cash and balances with Central Bank	969	-	-	969
Loans	13,428	-	-	13,428
Securities	-	108	129	237
Other	50	-	-	50
Interest income	14,447	108	129	14,684
Interest expense				
Deposits	(3,252)	-	-	(3,252)
Borrowings	(3,927)	-	-	(3,927)
Subordinated liabilities	(47)	-	-	(47)
Other	(24)	-	-	(24)
Interest expense	(7,250)	-	-	(7,250)
Net interest income	7,197	108	129	7,434
Net interest income from financial assets and liabilities at fair value	-	108	129	237
Interest income from financial assets at amortized cost	14,447	-	-	14,447
Interest expense from financial liabilities at amortized cost	(7,250)	-	-	(7,250)
Net interest income	7,197	108	129	7,434

1.1.-.31.3.2018	Amortized cost	Fair value thr. P/L	Fair value thr. OCI	Total
Interest income				
Cash and balances with Central Bank	1,246	-	-	1,246
Loans	12,442	71	-	12,513
Securities	-	95	138	233
Other	52	-	-	52
Interest income	13,740	166	138	14,044
Interest expense				
Deposits	(3,199)	-	-	(3,199)
Borrowings	(3,987)	-	-	(3,987)
Subordinated liabilities	-	-	-	-
Other	(31)	-	-	(31)
Interest expense	(7,217)	-	-	(7,217)
Net interest income	6,523	166	138	6,827
Net interest income from financial assets and liabilities at fair value	-	166	138	304
Interest income from financial assets at amortized cost	13,740	-	-	13,740
Interest expense from financial liabilities at amortized cost	(7,217)	-	-	(7,217)
Net interest income	6,523	166	138	6,827

Interest spread	2019 1.1.-31.3.	2018 1.1.-31.3.
Interest spread (the ratio of net interest income to the average carrying amount of interest bearing assets)	2.7%	2.7%

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

8. Net fee and commission income

	1.1.-31.3.2019			1.1.-31.3.2018		
	Income	Expense	Net income	Income	Expense	Net income
Asset management	893	(135)	758	1,012	(123)	889
Lending and financial guarantees	469	-	469	248	(30)	218
Collection and payment services	372	(27)	345	361	(26)	335
Cards and payment solution	379	(78)	301	216	(10)	206
Investment banking	206	(14)	192	462	-	462
Other	311	(158)	153	276	(181)	95
Net fee and commission income	2,630	(412)	2,218	2,575	(370)	2,205

Asset management fees are earned by the Group for trust and fiduciary activities where the Group holds or invests assets on behalf of the customers.

Fee and commission income from lending and financial guarantees is mainly related to lending activities, extension fees, advisory services and documentation, notification and payment fees plus fees from the issuing of guarantees on behalf of customers.

Fee and commission income on collection and payment services is generated billing services, such as issuing invoices and payment collection notices, wire transfer services and other payment services.

Commission from cards and payment solutions is mainly from the Bank's issuance of credit and debit cards and other card related commission, e.g. yearly fee on cards and transaction fee.

Fee and commission income from investment banking activities includes miscellaneous corporate advisory services plus commission from capital markets relating to sales of shares, bonds and derivatives.

Other fee and commission income is mainly fees relating to FX transactions at branches and in ATMs, custody and market making on the Icelandic stock exchange.

9. Net financial income

	2019 1.1.-31.3.	2018 1.1.-31.3.
Net gain on financial assets and financial liabilities mandatorily measured at fair value through profit or loss	1,048	1,201
Net (loss) gain on fair value hedge of interest rate swap	(15)	226
Realized gain on financial assets carried at fair value through OCI	42	121
Net foreign exchange loss	(309)	(161)
Net financial income	766	1,387

Net gain on financial assets and financial liabilities mandatorily measured at fair value through profit or loss

Equity instruments mandatorily measured at fair value	906	1,178
Debt instruments mandatorily measured at fair value	245	76
Derivatives	(39)	(57)
Loans	(64)	4
Net gain on financial assets and financial liabilities mandatorily measured at fair value through profit or loss	1,048	1,201

Net (loss) gain on fair value hedge of interest rate swap

Fair value change of interest rate swaps designated as hedging instruments	397	253
Fair value change on bonds issued by the Group attributable to interest rate risk	(412)	(27)
Net (loss) gain on fair value hedge of interest rate swap	(15)	226

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

10. Net insurance income

	2019 1.1.-31.3.	2018 1.1.-31.3.
Earned premiums, net of reinsurers' share		
Premiums written	3,801	3,587
Premiums written, reinsurers' shares	(94)	(89)
Change in provision for unearned premiums	(1,066)	(1,056)
Earned premiums, net of reinsurers' share	2,641	2,442
Claims incurred, net of reinsurers' share		
Claims paid	(1,849)	(1,851)
Claims paid, reinsurers' share	31	30
Change in provision for claims	(530)	(468)
Changes in provision for claims, reinsurers' share	(40)	(10)
Claims incurred, net of reinsurers' share	(2,388)	(2,299)
Net insurance income	253	143

11. Other operating income

Fair value changes on investment property	-	136
Net gain on assets held for sale	113	75
Other income	197	57
Other operating income	310	268
Net gain on assets held for sale		
Income from real estates and other assets	137	149
Expense related to real estates and other assets	(24)	(74)
Net gain on assets held for sale	113	75

Real estates and other assets classified as assets held for sale are generally the result of foreclosures on companies and individuals.

12. Personnel and salaries

	2019 1.1.-31.3.	2018 1.1.-31.3.
Number of employees		
Average number of full-time equivalent positions during the period	910	937
Full-time equivalent positions at the end of the period	917	938
Number of employees at the parent company		
Average number of full-time equivalent positions during the period	803	832
Full-time equivalent positions at the end of the period	811	832
Salaries and related expense		
Salaries	2,881	2,805
Defined contribution pension plans	414	403
Salary-related expense	414	408
Capitalization of salaries *	(79)	-
Salaries and related expense	3,630	3,616
Salaries and related expense for the parent company		
Salaries	2,507	2,450
Defined contribution pension plans	360	353
Salary-related expense	362	363
Capitalization of salaries *	(79)	-
Salaries and related expense for the parent company	3,150	3,166

* Expense due to implementation of core systems.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

12. Personnel and salaries, continued

In June 2018 Arion Bank adopted a new share-based remuneration programme, when a limited stock grant was offered to all employees of the parent company, excluding internal control units, in connection with the IPO and listing of the Bank. Remuneration was paid in the form of deferred shares with a vesting period of two years. The Bank recognizes expenses related to the programme as salaries and related expenses, a total of ISK 651 million, over the vesting period, or approximately ISK 27 million per month from June 2018.

During the period the Group made a provision of ISK 16 million (Q1 2018: ISK 123 million) for performance plan payments, including salary-related expense, of which the Bank made no provision (Q1 2018: ISK 106 million). Forty percent of the payment is deferred for three years in accordance with FME rules on remuneration policy for financial undertakings. At the end of the period the Group's accrual for performance plan payments amounted to ISK 521 million (31.12.2018: ISK 608 million), of which the Bank's accrual amounts to ISK 394 million (31.12.2018: ISK 452 million).

13. Other operating expense

	2019 1.1.-31.3.	2018 1.1.-31.3.
IT expense	1,156	1,061
Professional services	293	343
Housing expense	275	321
Other administration expense	930	895
Depositors' and Investors' Guarantee Fund	232	214
Depreciation of property and equipment	142	132
Depreciation of right of use asset	32	-
Amortization of intangible assets	172	177
Other operating expense	3,232	3,143

14. Bank levy

The Bank levy is 0.376% on total debts excluding tax liabilities, in excess of ISK 50 billion. The tax is assessed on Financial Undertakings but non-financial subsidiaries are exempt from this tax.

15. Net impairment

	2019 1.1.-31.3.	2018 1.1.-31.3.
Net change in impairment of cash and balances with Central Bank	-	(9)
Net change in impairment of loans to credit institutions	(4)	(20)
Net change in impairment of loans to corporates	(209)	(527)
Net change in impairment of loans to individuals	(357)	371
Net change in impairment of financial instruments carried at fair value through OCI, net of tax	(1)	(21)
Net change in impairment of loan commitments, guarantees and unused credit facilities	(854)	(314)
Net impairment on financial instruments	(1,425)	(520)
Increase in book value of loans to corporates	46	17
Increase in book value of loans to individuals	298	368
Other value changes of loans	344	385
Net impairment	(1,081)	(135)

Increase in book value of loans to individuals and corporates is mainly due to release of discount form loans acquired with discount during the years 2008 to 2013, both due to impairments and other discount rate than reflected in the interest rates of the loans. The discount release was primarily related to loans that were paid up during the period.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

16. Income tax expense

	2019 1.1.-31.3.	2018 1.1.-31.3.
Current tax expense	664	886
Deferred tax expense	(42)	4
Income tax expense	**622**	**890**

Reconciliation of effective tax rate

	2019 1.1.-31.3.		2018 1.1.-31.3.	
Earnings before tax		2,859		3,112
Income tax using the Icelandic corporate tax rate	20.0%	572	20.0%	622
Additional 6% tax on Financial Undertakings	5.0%	142	5.3%	165
Non-deductible expenses	0.0%	1	0.0%	1
Tax exempt revenue	(10.6%)	(304)	(8.9%)	(278)
Non-deductible taxes	6.3%	181	4.3%	133
Tax incentives not recognized in the Income Statement	0.7%	21	8.3%	258
Other changes	0.3%	9	(0.4%)	(11)
Effective tax rate	21.8%	622	28.6%	890

Financial undertakings pay 6% additional tax on taxable profit exceeding ISK 1 billion.

Tax exempt revenues consist mainly of profit from equity positions.

Bank levy of 0.376% on liabilities exceeding ISK 50 billion is non-deductible.

17. Discontinued operations held for sale, net of income tax

	2019 1.1.-31.3.	2018 1.1.-31.3.
Net loss from discontinued operations held for sale	(1,506)	(315)
Income tax expense	287	42
Discontinued operations held for sale, net of income tax	(1,219)	(273)

Discontinued operations held for sale, net of income tax

Valitor Holding hf.	(1,219)	(391)
Stakksberg ehf.	-	118
Discontinued operations held for sale, net of income tax	(1,219)	(273)

For further information about Valitor Holding hf., see Note 5, and Note 29 for Stakksberg ehf.

18. Earnings per share

	Continued operations		Discontinued operations		Net Earnings	
	2019 1.1.-31.3.	2018 1.1.-31.3.	2019 1.1.-31.3.	2018 1.1.-31.3.	2019 1.1.-31.3.	2018 1.1.-31.3.
Net earnings attributable to the shareholders of Arion Bank	2,237	2,222	(1,219)	(273)	1,018	1,949
Weighted average number of outstanding shares	1,814	1,930	1,814	1,930	1,814	1,930
Basic earnings per share in ISK	1.23	1.15	(0.67)	(0.14)	0.56	1.01

There were no instruments at the end of the period that could potentially dilute basic earnings per share (2018: none).

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

Notes to the Consolidated Interim Statement of Financial Position

19. Cash and balances with Central Bank

	31.3.2019	31.12.2018
Cash on hand	4,349	5,059
Cash with Central Bank	79,613	67,492
Mandatory reserve deposit with Central Bank	10,162	10,588
Cash and balances with Central Bank	94,124	83,139

The mandatory reserve deposit with the Central Bank is not available for the Group to use in its daily operations.

20. Loans to credit institutions

	31.3.2019	31.12.2018
Bank accounts	52,851	38,038
Money market loans	29,298	17,101
Other loans	2,829	1,183
Loans to credit institutions	84,978	56,322

21. Loans to customers

	Individuals		Corporates		Total	
31.3.2019	Gross carrying amount	Book value	Gross carrying amount	Book value	Gross carrying amount	Book value
Overdrafts	15,639	14,699	19,082	18,274	34,721	32,973
Credit cards	11,606	11,344	1,294	1,240	12,900	12,584
Mortgage loans	342,346	341,792	24,643	24,589	366,989	366,381
Other loans	33,579	31,739	390,957	385,569	424,536	417,308
Loans to customers	403,170	399,574	435,976	429,672	839,146	829,246
31.12.2018						
Overdrafts	14,536	13,616	19,200	18,267	33,736	31,883
Credit cards	12,958	12,706	1,348	1,305	14,306	14,011
Loans to customers at fair value	-	-	4,812	4,812	4,812	4,812
Mortgage loans	343,119	342,469	23,417	23,351	366,536	365,820
Other loans	33,560	31,692	390,767	385,608	424,327	417,300
Loans to customers	404,173	400,483	439,544	433,343	843,717	833,826

The total book value of pledged loans that were pledged against amounts borrowed was ISK 225 billion at the end of the period (31.12.2018: ISK 203 billion). Pledged loans comprised mortgage loans to individuals.

Further analysis of loans is provided in Risk Management Disclosures.

22. Financial instruments

	31.3.2019	31.12.2018
Bonds and debt instruments	81,027	71,451
Shares and equity instruments with variable income	23,595	20,265
Derivatives	6,024	6,241
Securities used for economic hedging	17,457	16,600
Financial instruments	128,103	114,557

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

23. Financial assets and financial liabilities

31.3.2019 **Financial assets**	Amortized cost	Fair value through OCI	Manda-torily at fair value thr. P/L	Total
Loans				
Cash and balances with Central Bank	94,124	-	-	94,124
Loans to credit institutions	84,978	-	-	84,978
Loans to customers	829,246	-	-	829,246
Loans	1,008,348	-	-	1,008,348
Bonds and debt instruments				
Listed	-	63,272	15,865	79,137
Unlisted	-	1,568	322	1,890
Bonds and debt instruments	-	64,840	16,187	81,027
Shares and equity instruments with variable income				
Listed	-	-	10,099	10,099
Unlisted	-	-	10,097	10,097
Bond funds with variable income, unlisted	-	-	3,399	3,399
Shares and equity instruments with variable income	-	-	23,595	23,595
Derivatives				
OTC derivatives	-	-	4,328	4,328
Derivatives used for hedge accounting	-	-	1,696	1,696
Derivatives	-	-	6,024	6,024
Securities used for economic hedging				
Bonds and debt instruments, listed	-	-	9,818	9,818
Bonds and debt instruments, unlisted	-	-	474	474
Shares and equity instruments with variable income, listed	-	-	7,161	7,161
Shares and equity instruments with variable income, unlisted	-	-	4	4
Securities used for economic hedging	-	-	17,457	17,457
Other financial assets				
Accounts receivable	4,250	-	-	4,250
Other financial assets	6,960	-	-	6,960
Other financial assets	11,210	-	-	11,210
Financial assets	1,019,558	64,840	63,263	1,147,661
Financial liabilities				
Due to credit institutions and Central Bank	9,183	-	-	9,183
Deposits	490,474	-	-	490,474
Borrowings	445,077	-	-	445,077
Subordinated liabilities	7,283	-	-	7,283
Short position in bonds	-	-	275	275
Derivatives	-	-	2,011	2,011
Other financial liabilities	13,132	-	-	13,132
Financial liabilities	965,149	-	2,286	967,435

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

23. Financial assets and financial liabilities, continued

31.12.2018 **Financial assets**	Amortized cost	Fair value through OCI	Manda-torily at fair value thr. P/L	Total
Loans				
Cash and balances with Central Bank	83,139	-	-	83,139
Loans to credit institutions	56,322	-	-	56,322
Loans to customers	829,014	-	4,812	833,826
Loans	968,475	-	4,812	973,287
Bonds and debt instruments				
Listed	-	51,329	17,274	68,603
Unlisted	-	2,459	389	2,848
Bonds and debt instruments	-	53,788	17,663	71,451
Shares and equity instruments with variable income				
Listed	-	-	7,270	7,270
Unlisted	-	-	9,867	9,867
Bond funds with variable income, unlisted	-	-	3,128	3,128
Shares and equity instruments with variable income	-	-	20,265	20,265
Derivatives				
OTC derivatives	-	-	5,020	5,020
Derivatives used for hedge accounting	-	-	1,221	1,221
Derivatives	-	-	6,241	6,241
Securities used for economic hedging				
Bonds and debt instruments, listed	-	-	10,010	10,010
Shares and equity instruments with variable income, listed	-	-	6,587	6,587
Shares and equity instruments with variable income, unlisted	-	-	3	3
Securities used for economic hedging	-	-	16,600	16,600
Other financial assets				
Accounts receivable	3,751	-	-	3,751
Other financial assets	2,056	-	-	2,056
Other financial assets	5,807	-	-	5,807
Financial assets	974,282	53,788	65,581	1,093,651
Financial liabilities				
Due to credit institutions and Central Bank	9,204	-	-	9,204
Deposits	466,067	-	-	466,067
Borrowings	417,782	-	-	417,782
Subordinated liabilities	6,532	-	-	6,532
Short position in bonds	-	-	488	488
Short position in equity	-	-	37	37
Derivatives	-	-	1,795	1,795
Other financial liabilities	6,130	-	-	6,130
Financial liabilities	905,715	-	2,320	908,035

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

23. Financial assets and financial liabilities, continued

Bonds and debt instruments measured at fair value, specified by issuer

31.3.2019	FVOCI	Mandatorily FVPL	Total
Financial and insurance activities	6,688	6,587	13,275
Public sector	50,999	8,466	59,465
Corporates	7,153	1,134	8,287
Bonds and debt instruments at fair value	64,840	16,187	81,027
31.12.2018			
Financial and insurance activities	2,962	7,364	10,326
Public sector	44,084	8,724	52,808
Corporates	6,742	1,575	8,317
Bonds and debt instruments designated at fair value	53,788	17,663	71,451

The total amount of pledged bonds was ISK 6.3 billion at the end of the period (31.12.2018: ISK 5.9 billion). Pledged bonds comprised Icelandic and foreign Government Bonds and corporate bonds that were pledged against funding received and included in Due to credit institutions and Central Bank as well as short positions included in Financial liabilities at fair value.

24. Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair value of assets and liabilities by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
Level 2: valuation techniques for which all significant inputs are market observable, either directly or indirectly; and
Level 3: valuation techniques which include significant inputs that are not based on observable market data.

For assets and liabilities that are recognized at fair value on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

Assets and liabilities recorded at fair value by level of the fair value hierarchy

31.3.2019

Assets at fair value	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	72,198	8,805	24	81,027
Shares and equity instruments with variable income	5,959	16,300	1,336	23,595
Derivatives	-	4,328	-	4,328
Derivatives used for hedge accounting	-	1,696	-	1,696
Securities used for economic hedging	16,918	539	-	17,457
Investment property	-	-	7,101	7,101
Assets at fair value	95,075	31,668	8,461	135,204
Liabilities at fair value				
Short position in bonds	275	-	-	275
Derivatives	-	2,011	-	2,011
Liabilities at fair value	275	2,011	-	2,286

Amounts are in ISK millions

24. Fair value hierarchy, continued

31.12.2018

Assets at fair value	Level 1	Level 2	Level 3	Total
Loans to customers	-	4,812	-	4,812
Bonds and debt instruments	61,909	9,500	42	71,451
Shares and equity instruments with variable income	3,980	14,956	1,329	20,265
Derivatives	-	5,020	-	5,020
Derivatives used for hedge accounting	-	1,221	-	1,221
Securities used for economic hedging	16,597	3	-	16,600
Investment property	-	-	7,092	7,092
Assets at fair value	82,486	35,512	8,463	126,461

Liabilities at fair value				
Short position in bonds	488	-	-	488
Short position in equity	37	-	-	37
Derivatives	-	1,795	-	1,795
Liabilities at fair value	525	1,795	-	2,320

There were no transfers between Level 1 and Level 2 during the period (2018: Transfers from Level 2 to Level 1 amounted to ISK 496 million).

Fair value of assets and liabilities

The fair value of asset and liabilities is the amount at which the asset and liability could be exchanged in a current transaction between willing parties, i.e. not during a forced sale or liquidation. The existence of published price quotations in an active market is the best evidence of fair value and when they exist they are used by the Group to measure assets and liabilities. If quoted prices for an asset fail to represent actual and regularly occurring transactions in active market transactions or if quoted prices are not available at all, fair value is established by using an appropriate valuation technique.

Methods for establishing fair value

The best evidence of the fair value of an asset and liability at initial recognition is the transaction price, unless the fair value can be evidenced by comparison with other observable current market transactions, or is based on a valuation technique whose variables include only data from observable markets.

In some cases, the carrying value of an asset in Note 23 is used as an approximation for the fair value of the asset. This is straight forward for cash and cash equivalents but is also used for short term investments and borrowings to highly rated counterparties, such as credit institutions, on contracts that feature interest close to or equal to market rates and expose the Group to little or no credit risk.

Level 1: Fair value established from quoted market prices

For listed and liquid stocks and bonds, certain financial derivatives and other market traded securities, the fair value is derived directly from quoted market prices. These instruments are disclosed under Financial instruments and Financial liabilities at fair value in the Statement of Financial Position.

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

For assets and liabilities, for which the market is not active, the Group applies valuation techniques to attain a fair value using as much market information as available. Valuation techniques include using recent market transactions between knowledgeable and willing parties, if available, reference to current fair value of another instrument that is substantially the same, discounted cash flow analysis, option pricing models or other commonly accepted valuation techniques used by market participants to price the instrument.

For assets and liabilities for which quoted prices on active markets are not available, the fair value is derived using various valuation techniques. This applies in particular to OTC derivatives such as options, swaps, futures and unlisted equities but also some other assets and liabilities.

In most cases the valuation is based on theoretical financial models, such as the Black Scholes model or variations thereof. These techniques also include forward pricing and swap models using present value calculations.

Level 2 instruments include unlisted shares, unlisted funds with underlying bonds and equity holdings (share certificates), unlisted and less liquid listed bonds and all OTC derivatives.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

24. Fair value hierarchy, continued

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

In many cases there is little or no market data to rely on for fair value calculations. The most common valuation technique is present value calculations. Such calculations involve the estimation of future cash flow and the assessment of appropriate discount rate. The discount rate should both reflect current market rates and the uncertainty in the future cash flow. In such cases internal models and methods are used to calculate the fair value. The models may be statistical in nature, based on internal or external history of assets with similar characteristics and/or based on internal knowledge and experience. For example, the credit margin on most loans to customers which, is added to the current and suitable interest rate to arrive at an appropriate discount rate, is estimated using credit rating and loss parameters in case of default that have been derived from internal models.

Equity instruments that do not have a quoted market price are evaluated using methods and guidelines from pertinent international organizations. In most cases intrinsic value is the basis for the assessment but other factors, such as cash flow analysis, can also modify the results.

The Group applies management valuation for determining fair value of investment properties. Management valuation is either based on recent transactions and offers for similar assets or present value calculations which involve estimation of future cash flow and the assessment of appropriate discount rate.

Movements in Level 3 assets measured at fair value

	Investment	Financial assets		
31.3.2019		Bonds	Shares	Total
Balance at the beginning of the year	7,092	42	1,329	8,463
Net fair value changes	-	19	(55)	(36)
Additions	9	-	62	71
Disposals	-	(25)	-	(25)
Transfers out of Level 3	-	(12)	-	(12)
Balance at the end of the period	7,101	24	1,336	8,461
31.12.2018				
Balance at the beginning of the year	6,613	39	1,130	7,782
Net fair value changes	471	10	56	537
Additions	284	-	210	494
Disposal	(276)	(7)	(1)	(284)
Transfers out of Level 3	-	-	(66)	(66)
Balance at the end of the period	7,092	42	1,329	8,463

Line items where effects of Level 3 assets are recognized in the Consolidated Interim Income Statement

	Invest-ment	Financial assets		
1.1.-31.3.2019		Bonds	Shares	Total
Net financial income	-	19	(55)	(36)
Effects recognized in the Income Statement	-	19	(55)	(36)
1.1.-31.3.2018				
Net financial income	-	(1)	(5)	(6)
Other operating income	136	-	-	136
Effects recognized in the Income Statement	136	(1)	(5)	130

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

24. Fair value hierarchy, continued

Carrying values and fair values of financial assets and financial liabilities not carried at fair value

31.3.2019	Carrying value	Fair value	Unrealized gain (loss)
Financial assets not carried at fair value			
Cash and balances with Central Bank	94,124	94,124	-
Loans to credit institutions	84,978	84,978	-
Loans to customers	829,246	835,669	6,423
Other financial assets	11,210	11,210	-
Financial assets not carried at fair value	1,019,558	1,025,981	6,423
Financial liabilities not carried at fair value			
Due to credit institutions and Central Bank	9,183	9,183	-
Deposits	490,474	490,474	-
Borrowings	445,077	458,858	(13,781)
Subordinated liabilities	7,283	7,196	87
Other financial liabilities	13,132	13,132	-
Financial liabilities not carried at fair value	965,149	978,843	(13,694)

31.12.2018			
Financial assets not carried at fair value			
Cash and balances with Central Bank	83,139	83,139	-
Loans to credit institutions	56,322	56,322	-
Loans to customers	829,014	837,153	3,327
Other financial assets	5,807	5,807	-
Financial assets not carried at fair value	974,282	982,421	3,327
Financial liabilities not carried at fair value			
Due to credit institutions and Central Bank	9,204	9,204	-
Deposits	466,067	466,067	-
Borrowings	417,782	426,390	(8,608)
Subordinated liabilities	6,532	6,454	78
Other financial liabilities	6,130	6,130	-
Financial liabilities not carried at fair value	905,715	914,245	(8,530)

Loans to customers are largely with variable interest rate. Those loans, including corporate loans, are presented at book value as they have generally short duration and very limited interest rate risk. Loans with fixed interest rate, mainly long term retail mortgages are estimated by using the discount cash flow method with the interest rates offered on new loans, taking into account loan to value. Defaulted loans are presented at book value as no future cash flow is expected on them. Instead they are written down according to their estimated potential recovery value.

Amounts are in ISK millions

24. Fair value hierarchy, continued

Derivatives	Notional	Fair value	
31.3.2019	value	Assets	Liabilities
Forward exchange rate agreements	59,794	464	304
Fair value hedge of interest rate swap	151,470	1,696	-
Interest rate and exchange rate agreements	113,447	2,563	1,124
Bond swap agreements	7,919	5	107
Share swap agreements	7,741	1,295	463
Options - purchased agreements	1,203	1	13
Derivatives	341,574	6,024	2,011
31.12.2018			
Forward exchange rate agreements	60,940	901	406
Fair value hedge of interest rate swap	146,520	1,221	-
Interest rate and exchange rate agreements	109,698	2,749	1,252
Bond swap agreements	7,526	18	45
Share swap agreements	7,455	1,340	84
Options - purchased agreements	834	12	8
Derivatives	332,973	6,241	1,795

Fair value hedge of interest rate swap

The Group applies fair value hedge accounting only with respect to interest rate swaps, whereby the Group pays floating rate interest and receives fixed rate interest, with identical cash flows to the borrowings. The interest rate swaps are hedging the exposure of changes in the fair value of certain fixed-rate euro bonds, see Note 32, arising from changes in interest rates. On 1 January 2018 the Group adopted IFRS 9, but has elected to continue to apply the hedge accounting principles under IAS 39. For further information about the Group's hedge accounting policy, see Note 58 in the Annual Financial Statements 2018.

	Notional	Maturity	Fair value		Gain/loss on FV
31.3.2019		date	Assets	Liabilities	changes
Interest rates swaps - EUR	151,470	1-5 years	1,696	-	397
31.12.2018					
Interest rates swaps - EUR	146,520	1-5 years	1,221	-	1,182

	Book	Accumulated Fair value		Gain/loss on FV
31.3.2019	value	Assets	Liabilities	changes
EUR 500 million - issued 2016/18 - 5 years	68,506	518	-	(144)
EUR 300 million - issued 2017 - 3 years	41,501	(24)	-	(25)
EUR 300 million - issued 2018 - 3 years	41,641	-	598	(243)
Hedged borrowings	151,648	494	598	(412)
31.12.2018				
EUR 500 million - issued 2016/18 - 5 years	65,845	640	-	(161)
EUR 300 million - issued 2017 - 3 years	40,034	1	-	(19)
EUR 300 million - issued 2018 - 3 years	40,328	-	343	(329)
Hedged borrowings	146,207	641	343	(509)

The effectiveness of each hedge is measured regularly with linear regression. The relationship between fair value changes of an interest rate swap on the one hand and a borrowing on the other hand is examined. In all cases the effectiveness is within limits, or between 93-105%.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

25. Offsetting financial assets and financial liabilities

Financial assets subject to enforceable master netting arrangements and similar arrangements

	Assets subject to netting arrangements			Netting potential not recognized in the Balance Sheet				
31.3.2019	Gross assets before nettings	Nettings with gross liabilities	Assets recognized on Balance Sheet, net	Financial liabilities	Collateral received	Assets after consideration of netting potential	Assets not subject to enforceable netting arr-angements	Total assets recognized on Balance Sheet, net
Reverse repurchase agreements	12,234	-	12,234	(10,538)	-	1,696	-	12,234
Derivatives	4,306	-	4,306	(633)	-	3,673	1,718	6,024
Total assets	16,540	-	16,540	(11,171)	-	5,369	1,718	18,258
31.12.2018								
Reverse repurchase agreements	12,026	(50)	11,976	(10,387)	-	1,589	-	11,976
Derivatives	4,082	-	4,082	(840)	-	3,242	2,159	6,241
Total assets	16,108	(50)	16,058	(11,227)	-	4,831	2,159	18,217

Financial liabilities subject to enforceable master netting arrangements and similar arrangements

	Liabilities subject to netting arrangements			Netting potential not recognized in the Balance Sheet				
31.3.2019	Gross liabilities before nettings	Nettings with gross assets	Liabilities recognized on Balance Sheet, net	Financial assets	Collateral pledged	Liabilities after consideration of netting potential	Liabilities not subject to enforceable netting arr-angements	Total liabilities recognized on balance sheet
Repurchase agreements	10,538	-	10,538	(10,538)	-	-	-	10,538
Derivatives	680	-	680	(633)	-	47	1,331	2,011
Total liabilities	11,218	-	11,218	(11,171)	-	47	1,331	12,549
31.12.2018								
Repurchase agreements	10,437	(50)	10,387	(10,387)	-	-	-	10,387
Derivatives	878	-	878	(840)	-	38	917	1,795
Total liabilities	11,315	(50)	11,265	(11,227)	-	38	917	12,182

Reverse repurchase agreements and repurchase agreements are recognized within the line items Financial instruments and Due to credit institutions and Central Bank respectively.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

26. Investments in associates

The Group's interest in its principal associates	31.3.2019	31.12.2018
Audkenni hf., Borgartún 31, Reykjavík, Iceland	25.4%	25.4%
Farice ehf., Smáratorg 3, Kópavogur, Iceland	-	35.8%
JCC ehf., Borgartúni 19, Reykjavík, Iceland	33.3%	33.3%
Reiknistofa bankanna hf., Katrínartún 2, Reykjavík, Iceland	20.0%	20.0%
220 Fjördur ehf., Fjardargötu 13-15, Hafnarfjördur, Iceland	37.4%	37.4%

Investments in associates		
Carrying amount at the beginning of the year	818	760
Acquisitions	-	85
Transfers to assets and disposal groups held for sale	-	(55)
Disposals	(738)	-
Share of profit of associates and profit from sale	727	27
Investment in associates	807	818

In March 2019 Arion Bank sold its entire shareholding in Farice ehf. The profit from the sale amounted to ISK 732 million and is recognized in the Consolidated Interim Income Statement.

27. Intangible assets

Intangible assets comprise the following categories: Goodwill, which arises on business combinations; Infrastructure, Customer relationships and related agreements which are identified during the acquisition of subsidiaries and related to the activities of the businesses being acquired; and Software, which is acquired (i.e. software licenses).

Infrastructure, which is capitalized as an intangible asset, is related to the asset management operation and branding of the insurance operation. The business activity is based on years of developing expertise and systems, during which a valuable platform has been created for future growth. An impairment test is performed annually as described below.

Customer relationships and related agreements are connected to business relationships and agreements which the Bank acquired in subsidiaries. The asset is based on the assumption that business relationships and agreements generate regular payments and earnings to the relevant business segments. The lifetime of these agreements is based on the experience of the Group and the industry. As a result, these agreements are assessed as having an identified useful lifetime.

Acquired software and internally developed software is capitalized on the basis of the cost of acquiring it and bringing it into service. Expenditure on internally developed software is recognized as an asset when the Group is able to demonstrate its intention and ability to complete the development and use the software in a manner that will generate future economic benefits, and when it can reliably measure the costs to complete the development. The capitalized costs of internally developed software include all costs directly attributable to developing the software and are amortized over its useful life. Computer software licenses and internally developed software recognized as intangible assets are amortized over their useful life, which is estimated to be 3-10 years.

Policies applied to the Group's intangible assets	Goodwill and infrastructure	Customer relationship and related agreements	Software
Useful lives	Undefined	Finite 6-15 years and undefined	Finite 3-10 years
Amortization method	Impairment test	Straight-line basis over 6-15 years and impairment test	Straight-line basis over 3-10 years
Internally generated or acquired	Acquired	Acquired	Acquired and internally generated

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

27. Intangible assets, continued

31.3.2019	Goodwill	Infra-structure	Customer relationship and related agreements	Software	Total
Balance at the beginning of the year	669	2,383	787	2,558	6,397
Additions	-	-	-	777	777
Additions, capitalized salaries	-	-	-	79	79
Amortization	-	-	(15)	(157)	(172)
Intangible assets	669	2,383	772	3,257	7,081

31.12.2018	Goodwill	Infra-structure	Customer relationship and related agreements	Software	Total
Balance at the beginning of the year	4,315	3,705	1,492	4,336	13,848
Additions	-	-	-	1,372	1,372
Transfers to assets and disposal groups held for sale	(3,646)	(1,322)	(445)	(2,645)	(8,058)
Amortization	-	-	(260)	(505)	(765)
Intangible assets	669	2,383	787	2,558	6,397

Goodwill is recognized in the segment Subsidiaries and other divisions, see Note 6.

28. Tax assets and tax liabilities

	31.3.2019		31.12.2018	
	Assets	Liabilities	Assets	Liabilities
Current tax	-	4,470	-	4,650
Deferred tax	15	352	90	469
Tax assets and tax liabilities	15	4,822	90	5,119

29. Assets and disposal groups held for sale and associated liabilities

Assets and disposal groups held for sale	31.3.2019	31.12.2018
Valitor Holding hf.	42,490	40,003
Eignabjarg ehf., a holding company of Stakksberg ehf.	6,875	6,516
Disposal groups held for sale	49,365	46,519
Real estate	1,894	2,021
Other assets	62	44
Assets and disposal groups held for sale	51,321	48,584

Liabilities associated with disposal groups		
Valitor Holding hf.	29,498	26,337
Liabilities associated with disposal groups	29,498	26,337

For further information about Valitor Holding hf., see Note 5.

Real estates and other assets classified as assets held for sale are generally the result of foreclosures on companies and individuals.

Stakksberg ehf., a subsidiary of Eignabjarg ehf.

On 22 January 2018 United Silicon was declared bankrupt following serious operational problems which resulted it its operating license being temporarily suspended, following a failed attempt at reaching a composition with its creditors. In February 2018 an agreement was reached between the administrator of the bankrupt estate of United Silicon and Arion Bank, whereby the Bank foreclosed against its collateral and acquired all the company's main assets. Disputes with other creditors regarding the validity of the collateral and assurances provided by the Bank in relation thereto are disclosed in Note 37. The assets of the silicon plant are currently managed by Stakksberg ehf., which is held by the Bank through the subsidiary Eignabjarg ehf. Stakksberg ehf. has, since the transfer of the assets from United Silicon, successfully worked to reduce uncertainties surrounding the recommissioning of the silicon plant, with measures including the securing of all necessary operating permits, power supply and undertaking further engineering design groundwork necessary for the carrying out of remedial work prior to the reopening of the plant. Stakksberg ehf. is currently engaged in concluding a new environmental impact assessment for the plant. It is also making preparations for changes to local planning, which will be carried out in cooperation with Reykjanesbær community in due course. The outcome of the latter measure is uncertain at this point. The Bank's objective is to divest Stakksberg ehf. on the basis of this preparatory work. Stakksberg ehf. is therefore classified as a disposal group held for sale in accordance with IFRS 5.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

30. Other assets

	31.3.2019	31.12.2018
Property and equipment	5,623	5,797
Right of use asset	958	-
Accounts receivable	4,250	3,751
Unsettled securities trading	5,057	92
Investment for life assurance policyholders where risk is held by policyholder	937	833
Sundry assets	3,094	3,029
Other assets	19,919	13,502

Right of use asset

Addition due to the adoption of IFRS 16 Leases 1 January 2019	984	-
Indexation	5	-
Depreciation	(31)	-
Right of use asset	958	-

Right of use asset consists of real estates for own use.

31. Other liabilities

	31.3.2019	31.12.2018
Accounts payable	679	633
Unsettled securities trading	5,596	34
Depositors' and Investors' Guarantee Fund	230	226
Technical provision	14,918	13,324
Technical provision for life assurance policyholders were investment risk is held by policyholder	937	833
Withholding tax	1,891	1,590
Bank levy	4,292	3,386
Accrued expenses	3,098	3,018
Prepaid income	1,558	1,599
Impairment of off balance items	1,597	717
Lease liability	962	-
Sundry liabilities	5,260	4,747
Other liabilities	41,018	30,107

Technical provision	Technical provision	Reinsurers' share	Total 31.3.2019	Technical provision	Reinsurers' share	Total 31.12.2018
Claims reported and loss adjustment expenses	7,351	(152)	7,199	6,871	(192)	6,679
Claims incurred but not reported	1,243	(113)	1,130	1,193	(113)	1,080
Claims outstanding	8,594	(265)	8,329	8,064	(305)	7,759
Provision for unearned premiums	6,324	(4)	6,320	5,260	(3)	5,257
Own technical provision	14,918	(269)	14,649	13,324	(308)	13,016

Insurance claim consists of claims outstanding and provision for unearned premiums. Claims outstanding present unsettled claims incurred. Claims outstanding is the total of claims reported and actuarial estimation of claims incurred but not reported. Provision for unearned premiums presents the current insurance risk that will be conditional on future fiscal years.

Lease liability	31.3.2019	31.12.2018
Addition due to the adoption of IFRS 16 Leases 1 January 2019	985	-
Indexation	5	-
Interest expense	11	-
Lease payments	(39)	-
Lease liability	962	-

31.3.2018	Up to 1 year	1-5 years	More than 5 years	Total
Maturity analysis - contractual undiscounted cash flows	147	505	645	1,297

Total expense relating to variable lease payments not included in the measurement of lease liabilities was ISK 65 million during the period. Short term lease contracts and lease contracts for which the underlying asset is of low value are not included in the lease liability. Total lease expense of short term and low value contracts of ISK 25 million is recognized in the Consolidated Interim Income Statement.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

32. Borrowings

Currency, original nominal value	First issued	Maturity	Maturity type	Terms of interest	31.3.2019	31.12.2018
ARION CBI 19, ISK 4,500 million	2013	2019	At maturity	Fixed, CPI linked, 2.50%	4,605	4,743
ARION CB 19, ISK 2,740 million	2016	2019	At maturity	Fixed, 5.50%	1,667	1,746
ARION CBI 21, ISK 10,220 million	2014	2021	At maturity	Fixed, CPI linked, 3.50%	10,082	9,950
ARION CB 22, ISK 28,720 million	2015	2022	At maturity	Fixed, 6.50%	28,030	28,503
ARION CB 24 ISK 8,360 million	2019	2024	At maturity	Fixed, 6.00%	7,509	-
ARION CBI 25, ISK 37,940 million	2017	2025	At maturity	Fixed, CPI linked, 3.00%	39,726	39,333
ARION CBI 26 ISK 7,900 million	2019	2026	At maturity	Fixed, CPI linked, 2.00%	6,921	-
ARION CBI 29, ISK 25,220 million	2014	2029	At maturity	Fixed, CPI linked, 3.50%	27,388	27,029
ARION CBI 48 ISK 11,680 million	2018	2048	Amortizing	Fixed, CPI linked, 2.50%	10,469	10,606
Statutory covered bonds					136,397	121,910
ARION CB 2, ISK 51,125 million	2006	2048	Amortizing	Fixed, CPI linked, 3.75%	79,446	79,399
Structured Covered bonds					79,446	79,399
Total Covered bonds					215,843	201,309
EUR 300 million	2016	2019	At maturity	Fixed, 2.50%	20,161	19,376
RON 35 million	2016	2019	At maturity	Fixed, 3.80%	-	1,037
SEK 275 million	2016	2019	At maturity	Floating, 3 month STIBOR +2.65%	-	3,601
SEK 100 million	2017	2019	At maturity	Fixed, 0.29%	1,325	1,310
NOK 800 million	2015	2020	At maturity	Floating, NIBOR +2.95%	11,512	10,846
NOK 320 million	2016	2020	At maturity	Floating, NIBOR +1.95%	4,590	4,326
EUR 300 million *	2017	2020	At maturity	Fixed, 0.75%	41,501	40,034
SEK 300 million	2017	2020	At maturity	Floating, 3 month STIBOR +1.35%	3,980	3,936
SEK 250 million	2017	2020	At maturity	Floating, 3 month STIBOR +0.75%	3,310	3,276
EUR 500 million *	2016	2021	At maturity	Fixed, 1.625%	68,506	65,845
EUR 13 million	2019	2021	At maturity	Floating, 3 m. EURIBOR +0.58% ...	1,789	-
NOK 750 million	2019	2022	At maturity	Floating, NIBOR +1.82%	10,724	-
NOK 250 million	2017	2023	At maturity	Fixed, 3.02%	3,660	3,423
EUR 300 million *	2018	2023	At maturity	Fixed, 1.00%	41,641	40,328
NOK 250 million	2017	2027	At maturity	Fixed, 3.40%	3,672	3,432
Senior unsecured bonds					216,371	200,770
Bills issued					12,666	15,505
Other borrowings					197	198
Other loans / bills					12,863	15,703
Borrowings					445,077	417,782

* The Group applies fair value hedge accounting to these bond issuances and uses certain foreign currency denominated interest rate swaps as hedging instruments, see Note 24.

The book value of listed bonds was ISK 432 billion at the end of the period (31.12.2018: ISK 402 billion). The market value of those bonds was ISK 446 billion (31.12.2018: ISK 411 billion). The Group repurchased own debts during the period for the amount of ISK 2 billion (2018: ISK 22 billion) with minor effects on the Consolidated Interim Income Statement.

33. Subordinated liabilities

Currency, original nominal value	Issued	Maturity	Maturity type	Terms of interest	31.3.2019	31.12.2018
Tier 2 capital SEK 500 million*	2018	2028	At maturity	Floating, 3 month STIBOR +3.10% .	6,602	6,532
Tier 2 capital EUR 5 million	2019	2031	Amortizing	Fixed, 3.24%	681	-
Subordinated liabilities					7,283	6,532

* The notes are eligible as Tier 2 capital under the Icelandic Financial Undertakings Act No. 161/2002. The notes are callable by the issuer on 22 November 2023 and on every interest payment date thereafter.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

34. Pledged assets

Pledged assets against liabilities	31.3.2019	31.12.2018
Assets, pledged as collateral against borrowings	263,286	239,164
Assets, pledged as collateral against loans from credit institutions and short positions	6,269	5,927
Pledged assets against liabilities	269,555	245,091

The Group has pledged assets against borrowings, both issued covered bonds and other issued bonds and loan agreements. The total value of those pledged assets was ISK 263 billion at the end of the period (31.12.2018: ISK 239 billion). Pledged loans comprised mortgage loans to individuals. The book value of those borrowings was ISK 216 billion at the end of the period (31.12.2018: ISK 201 billion).

The Group has pledged bonds against short term lending from the Central Bank of Iceland and against short positions, related to swap agreements, to hedge market risk of those assets.

35. Equity

Share capital and share premium

According to the Bank's Articles of Association, total share capital amounts to ISK 2,000 million, with par value of ISK 1 per share. The holders of ordinary shares are entitled to receive dividends as approved by the general meeting and are entitled to one vote per share at shareholders' meetings.

At the Annual General Meeting on the 20 March 2019 the meeting resolved to cancel 186 million shares amounting to ISK 186 million of the Bank's share capital, reducing it from ISK 2,000 million to ISK 1,814 million at nominal value. The reduction will be executed by cancelling the Bank's own shares amounting to the above amount, provided that all applicable legal conditions are met. The meeting also authorized the Board of Directors to acquire on behalf of the Bank up to 10% of issued share capital in the Bank. The authorization remains in effect until the Bank's Annual General Meeting in 2020 or 15 September 2020, whichever occurs first.

	Share capital	Share premium	31.3.2019	Share capital	Share premium	31.12.2018
Shares outstanding at the beginning of the year	1,814	57,196	59,010	2,000	73,861	75,861
Purchase of treasury stock	-	-	-	(190)	(16,949)	(17,139)
Employees stock grant	-	(2)	(2)	4	284	288
Shares outstanding at the end of the period	1,814	57,194	59,008	1,814	57,196	59,010
Own shares at period-end	186	16,667	16,853	186	16,665	16,851
- as proportion of issud share capital	9.3%	22.6%	28.6%	9.3%	22.6%	22.2%

Share premium is the amount above nominal value that shareholders have paid for shares issued by Arion Bank hf.

In 2018 Arion Bank acquired own shares following the decision to accept an offer from Kaupskil ehf., a subsidiary of Kaupthing ehf., to buy back 9.5% of issued share capital in Arion Bank, or 190 million shares. Arion Bank paid ISK 90.087 a share, a total of ISK 17,139 million.

According to decision made by the Board of Directors, own shares were allocated to employees in connection with the Bank's IPO and listing in 2018. In total approximately 4 million shares were allocated to employees at ISK 75 per share, a total of ISK 295 million. In accordance with the employees' stock grant programme, an employee who resigns within the vesting period of two years, returns the shares to the Bank.

In April 2019 Arion Bank's share capital was reduced by ISK 186 million at nominal value, totaling 186 million shares, by cancelling the Bank's own shares. Arion Bank's share capital is ISK 1,814 million after the reduction.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

Other information

36. Shareholders of Arion Bank

	17.4.2019	31.3.2019	31.12.2018
Kaupskil ehf. (Subsidiary of Kaupthing hf.)	20.00%	32.67%	32.67%
Taconic Capital (through TCA New Sidecar s.á.r.l.)	16.03%	9.99%	9.99%
Attestor Capital	7.17%	7.15%	7.35%
Och Ziff Capital management	7.25%	6.58%	6.58%
Stoðir Hf.	4.65%	0.61%	0.61%
Lansdowne partners	3.88%	2.95%	2.95%
Goldman Sachs International	3.81%	3.46%	3.47%
Eaton Vance funds	3.69%	3.35%	3.35%
Íslandsbanki hf.	2.89%	1.09%	0.88%
Gildi pension fund	2.78%	2.52%	2.52%
Artemis	1.87%	1.69%	1.69%
Miton Asset Management funds	1.81%	1.64%	1.37%
LSR (Lífeyrissjóður starfsmanna ríkisins)	1.21%	0.65%	0.53%
MainFirst Bank AG	1.09%	0.99%	0.99%
Deutsche Asset & Wealth Management	1.06%	0.96%	0.96%
Stapi Lífeyrissjóður	1.04%	0.63%	0.63%
Arion banki hf.	0.01%	9.31%	9.31%
Other shareholders with less than 1% shareholding	19.76%	13.76%	14.15%
Issued share capital	100.00%	100.00%	100.00%

In April 2019 the shareholders list changed when Kaupskil ehf. sold 15% shareholding, and when Arion Bank's share capital was reduced by ISK 186 million at nominal value, by cancelling vast majority of the Bank's own shares.

37. Legal matters

The Group has in place formal controls and policies for managing legal claims. Once professional advice has been obtained and the likelihood and amount of loss reasonably estimated, the Group makes adjustments, if appropriate, to account for any adverse effects the claims may have on its financial standing. Should the Group conclude that it is to the detriment of the Group's case to disclose such potential amounts, relating to the legal claims raised, it elects not to do so. At the end of the period, the Group had several unresolved legal claims.

Contingent liabilities

Legal proceedings regarding damages

The former chairman of the Board of BM Vallá hf., together with Lindarflöt ehf., has filed two cases against the Bank with a claim for damages in the amount of more than ISK 4 billion, plus interest. The plaintiffs maintain that the Bank caused them, as shareholders of BM Vallá hf. and Fasteignafélagid Ártún ehf., damage by not allowing the companies to be financially restructured and thereby forcing the companies into bankruptcy. In April 2018 the District Court of Reykjavík dismissed one of the cases. The plaintiffs appealed the judgment to the Court of Appeal. In June 2018 the Court of Appeal annulled the judgment of the District Court and ordered the District Court to hear the case again. The District Court acquitted the Bank of all claims with a judgment in September 2018. The plaintiffs have appealed the judgment to the Court of Appeal. The second case awaits the result of this case. The Bank believes that it will be acquitted of the plaintiffs' claims in both cases and has therefore not made any provision.

In January 2015, Datacell ehf. and Sunshine Press Productions ehf. jointly filed a suit against Valitor hf. (a subsidiary of Valitor Holding hf.) for compensatory damages amounting to approximately ISK 8.1 billion plus interest relating to Valitor hf.'s termination of Datacell's vendor agreement. The Icelandic Supreme Court ruled on 24 April 2013 in case no. 612/2012 that Valitor hf. did not have the authority to terminate the agreement. The plaintiffs had court-appointed appraisers evaluate the plaintiffs' alleged losses and they returned their report in March 2016. Valitor hf. disagreed with the assessment stated in the report and filed a motion to appoint three court appraisers to re-evaluate the plaintiffs' alleged losses. The District Court agreed to Valitor hf.'s demand. The reassessment has been completed but it was not filed with the court. Valitor hf. requested a new assessment, which would examine particular aspects which have not yet been assessed. The District Court and the Court of Appeal have rejected the request. A trial for the damages claim was held on 27 March 2019. On 24 April 2019 the District Court of Reykjavik issued a judgement. The conclusion was that Valitor shall pay Sunshine Press Production ISK 1,140 million and Datacell ISK 60 million in damages, a total of ISK 1,200 million plus interest from 24 April 2019. All parties can appeal the judgement to a higher Court within four weeks and it is likely that Valitor will appeal. When Arion Bank acquired a 38.62% shareholding in Valitor Holding hf. in 2014, the Bank signed an agreements with the seller (Landsbankinn) concerning losses which Valitor may potentially sustain in relation to the compensatory damages described above. Thus the Arion Bank may lodge a claim against the seller for its share in the potential loss should Valitor lose the case. Following the judgement the Group made a provision of ISK 600 million, after taking into accounts tax effects and aforementioned share of Landsbankinn.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

37. Legal matters, continued

In a lawsuit brought in June 2013, Kortathjónustan hf. claimed damages from Arion Bank hf., Íslandsbanki hf., Landsbankinn hf., Borgun hf. and the Bank's subsidiary Valitor hf. in the amount of ISK 1.2 billion plus interest, as a result of damage Kortathjónustan hf. contended the five parties caused the company due to violations of the Competition Act. In June 2017 the Supreme Court dismissed the case on procedural grounds. Kortathjónustan hf. brought a new lawsuit in September 2017 regarding the same matter of dispute, claiming damages in the amount of ISK 922 million plus interest from the same defendants. The Court of Appeal dismissed the case in May 2018. Kortathjónustan tried to appeal the dismissal to the Supreme Court but the court dismissed the case as there was no right of complaint. In November 2018 EC-Clear brought a new lawsuit against the same defendants regarding the same matter of dispute, demanding the acknowledgement of liability for damages. EC-Clear was the largest shareholder in Kortathjónustan and according to the writ EC-Clear is now the owner of alleged liability claims against the defendants. The District Court dismissed the case in February 2019. EC-Clear has appealed the dismissal to the Court of Appeal, which dismissed the case with a ruling in April 2019. Should the defendants be ordered liable for damages, they would be jointly responsible. Therefore the Bank has not made any provision.

Other legal matters

United Silicon

The company United Silicon was granted a moratorium on payments on 14 August 2017 and filed for bankruptcy on 22 January 2018. The Bank had collateral in the company's assets and the estate has transferred the assets to the Bank. The trustee in the estate has approved the Bank's secured claims but two unsecured creditors have lodged a protest against the Bank's lien on the assets of United Silicon. The trustee in the bankruptcy has referred the disagreement to the District Court of Reykjanes. The Bank has examined these protests and rejects them all. A hearing is expected in the autumn. It should be noted that in the agreement between the Bank and the estate, it is stated that should the Bank's collateral be judicially deemed to be invalid, the Bank will refund the estate the amount of the invalidated bond.

38. Events after the reporting period

No event has arisen after the reporting period and up to the approval of these Consolidated Interim Financial Statements that require additional disclosures.

Notes to the Condensed Consolidated Interim Financial Statements

Off balance sheet information

39. Commitments

Financial guarantees, unused credit facilities and undrawn loan commitments	31.3.2019	31.12.2018
Financial guarantees	14,428	15,124
Unused overdrafts	45,420	48,320
Undrawn loan commitments	73,012	79,130
Financial guarantees, unused credit facilities and undrawn loan commitments	132,860	142,574

40. Assets under management and under custody

Assets under management	1,045,544	970,633
Assets under custody	1,485,709	1,422,327

Assets under management represent the total market value of the financial assets which the Group manages on behalf of its customers.

The Group, acting as custodian, is responsible for safeguarding a firm's or individual's financial assets, hold in safekeeping securities such as stocks, bonds and securities funds, arrange the settlement of trades and movements of securities, process corporate actions such as income on bonds and dividends on shares; and pricing on securities.

Related party

41. Related party

The Group has a related party relationship with entities with influence over the Group as the largest shareholders of Arion Bank, which are on 31 March 2019 Kaupskil ehf. (32.67%) and Taconic Capital (9.99%), the Board of Directors of Kaupskil ehf. and Kaupthing ehf., being the parent company of Kaupskil ehf. and legal entities controlled by them.

The Board of Directors of Arion Bank, key management personnel of the Bank and the Group's associates are defined as related parties, as are close family members of the individuals referred to above and legal entities controlled by them.

Transactions with related parties have been conducted on an arm's length basis. There have been no further guarantees provided or received for related party receivables or payables.

Balances with related parties

31.3.2019	Assets	Liabilities	Net balance
Shareholders with influence over the Group	35	(2,942)	(2,907)
Board of Directors and key Management personnel	224	(114)	110
Associates and other related parties	-	(45)	(45)
Balances with related parties	259	(3,101)	(2,842)
31.12.2018			
Shareholders with control over the Group	70	(1,022)	(952)
Board of Directors and key Management personnel	246	(257)	(11)
Associates and other related parties	21	(71)	(50)
Balances with related parties	337	(1,350)	(1,013)

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

Risk management disclosures

The Group faces various risks arising from its day to day operations. Managing risk is therefore a core activity within the Group. The key to effective risk management is a process of on-going identification of significant risk, quantification of risk exposure, actions to limit risk and constant monitoring of risk. This process of risk management and the ability to evaluate, manage and correctly price the risk encountered is critical to the Group's continuing profitability as well as to be able to ensure that the Group's exposure to risk remains within acceptable levels.

Further information on risk management and capital adequacy is provided in the Annual Financial Statements for 2018 and in the Pillar 3 Risk Disclosures for 2018. The Pillar 3 Risk Disclosures 2018 are available on the Bank's website, www.arionbanki.is.

42. Credit risk

Credit risk is the risk that the Group will incur a loss because its customers or counterparties fail to discharge their contractual obligations.

Credit risk arises anytime the Group commits its funds, resulting in capital or earnings being dependent on counterparty, issuer or borrower performance. Loans to customers and credit institutions are the largest source of credit risk. Credit risk is also inherent in other types of assets, such as bonds and derivatives, and off balance sheet items such as commitments and guarantees.

Managing and analyzing the Group's loan portfolio is of utmost importance. Great emphasis is placed on the quality of the credit portfolio, by maintaining a strict credit process, critically inspecting loan applications, actively monitoring the credit portfolio and identifying and reacting to possible problem loans at an early stage as well as restructuring of impaired credits.

The Group grants credit based on well informed lending decisions and seeks business with strong parties with strong collaterals and good repayment capacity. The risk level of each credit is considered in the pricing.

Credit risk is managed and controlled by setting limits on the amount of risk the Group is willing to accept for individual counterparties and group of connected clients, and by monitoring exposures in relation to such limits. The Group seeks to limit its total credit risk through diversification of the loan portfolio across sectors and by limiting large exposures to group of connected clients.

Exposure to credit risk

The table below shows the maximum exposure to credit risk for the components of the Statement of Financial Position before the effect of mitigation due to collateral agreements or other credit enhancements. The table also shows related collateral and credit enhancements. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty and the exposure type. The main types of collateral obtained are as follows:

- Retail loans to individuals: Mortgages on residential properties.
- Corporate loans: Real estate, fishing vessels and other fixed and current assets, including inventory and trade receivables, cash and securities.
- Derivative exposures: Cash, treasury notes and bills, asset backed bonds, listed equity and funds that consist of eligible securities.

The value of collateral is based on estimated market value. The valuation of real estate is built on market price, official valuation of the Icelandic Property Registry, or the opinion of internal or external specialists. The valuation of fishing vessels takes into account related fishing quotas. The quality of collateral is evaluated in the lending process with regards to specialization, location, age and condition and possibilities for reuse.

Collateral value is monitored and additional collateral requested in accordance with the underlying agreement. Collateral value is reviewed in line with the adequacy of the allowance for impairment losses. Collateral values are capped by the related exposure amount. Comparative figures have not been updated.

Notes to the Condensed Consolidated Interim Financial Statements

42. Credit risk, continued

Maximum exposure to credit risk and collateral held against different types of financial instruments subject to the impairment requirements of IFRS 9

		Collateral				
31.3.2019	Maximum exposure	Cash and securities	Real estate	Fishing vessels	Other collateral	Total collateral
Cash and balances with Central Bank	94,124	-	-	-	-	-
Loans to credit institutions	84,978	-	-	-	-	-
Loans to customers at amortized cost	829,246	19,750	592,199	59,209	80,271	751,429
Individuals	*399,574*	*96*	*362,212*	*7*	*10,999*	*373,314*
Corporates	*429,672*	*19,654*	*229,987*	*59,202*	*69,272*	*378,115*
Real estate activities and construction	*150,163*	*2,575*	*138,640*	*26*	*2,266*	*143,507*
Fishing industry	*80,352*	*110*	*9,298*	*57,988*	*8,492*	*75,888*
Information and communication technology	*19,911*	*405*	*3,681*	-	*4,520*	*8,606*
Wholesale and retail trade	*66,528*	*414*	*29,386*	*16*	*31,144*	*60,960*
Financial and insurance activities	*33,511*	*15,742*	*7,336*	*734*	*6,595*	*30,407*
Industry, energy and manufacturing	*36,279*	*239*	*23,899*	-	*7,798*	*31,936*
Transportation	*12,071*	-	*1,069*	*314*	*2,069*	*3,452*
Services	*16,531*	*166*	*7,579*	*124*	*5,879*	*13,748*
Public sector	*6,690*	*3*	*2,016*	-	*236*	*2,255*
Agriculture and forestry	*7,636*	-	*7,083*	-	*273*	*7,356*
Other assets with credit risk	11,210	-	-	-	-	-
Financial guarantees	14,428	1,550	4,079	1,135	4,444	11,208
Undrawn loan commitments and unused overdrafts	118,432	-	-	-	-	-
Fair value through OCI	64,840	-	-	-	-	-
Government bonds	*50,999*	-	-	-	-	-
Corporate and finance bonds	*13,841*	-	-	-	-	-
Balance at the end of the period	1,217,258	21,300	596,278	60,344	84,715	762,637

31.12.2018	Maximum exposure	Cash and securities	Real estate	Fishing vessels	Other collateral	Total collateral
Cash and balances with Central Bank	83,139	-	-	-	-	-
Loans to credit institutions	56,322	-	-	-	-	-
Loans to customers at amortized cost	829,014	18,324	590,513	59,143	83,469	751,449
Individuals	*400,483*	*837*	*363,615*	*18*	*11,027*	*375,497*
Corporates	*428,531*	*17,487*	*226,898*	*59,125*	*72,442*	*375,952*
Real estate activities and construction	*140,955*	*1,280*	*136,935*	*22*	*2,484*	*140,721*
Fishing industry	*84,128*	*11*	*9,452*	*57,978*	*10,771*	*78,212*
Information and communication technology	*20,635*	*550*	*3,562*	-	*6,618*	*10,730*
Wholesale and retail trade	*65,824*	*349*	*29,196*	*15*	*29,257*	*58,817*
Financial and insurance activities	*38,806*	*15,152*	*6,470*	*685*	*9,001*	*31,308*
Industry, energy and manufacturing	*35,406*	*61*	*23,801*	-	*7,520*	*31,382*
Transportation	*11,958*	*17*	*1,055*	*307*	*1,673*	*3,052*
Services	*16,531*	*64*	*7,407*	*118*	*4,535*	*12,124*
Public sector	*6,829*	*3*	*2,031*	-	*315*	*2,349*
Agriculture and forestry	*7,459*	-	*6,989*	-	*268*	*7,257*
Other assets with credit risk	5,807	-	-	-	-	-
Financial guarantees	15,124	1,574	4,408	1,949	4,652	12,583
Undrawn loan commitments and unused overdrafts	127,450	-	-	-	-	
Fair value through OCI	53,788	-	-	-	-	
Government bonds	44,084	-	-	-	-	-
Corporate and finance bonds	9,704	-	-	-	-	-
Balance at the end of the period	1,224,432	19,898	594,921	61,092	88,121	764,032

Amounts are in ISK millions

42. Credit risk, continued

LTV ratio for residential mortgage lending

The following table describes the loan to value (LTV) and impairment status of the Group's mortgage loan book. LTV is calculated as the ratio of the gross amount of the loan to the value of the collateral without adjusting for possible costs of obtaining and selling the collateral. The collateral value is based on the value at origination, the most recent appraisal or official property valuation from the Icelandic Property Registry. For credit impaired loans the value of collateral is based on the most recent appraisal.

	31.03.2019		31.12.2018	
	Gross carrying amount	Thereof credit impaired	Gross carrying amount	Thereof credit impaired
Less than 50%	144,641	1,430	148,995	1,516
50-70%	133,002	2,137	132,893	2,499
70-90%	61,619	1,001	58,422	1,209
90-100%	12,702	343	12,773	482
100%-110%	4,375	156	3,904	97
More than 110%	10,589	933	9,543	656
Not classified	61	25	6	-
Balance at the end of the period	366,989	6,025	366,536	6,459

At the end of the period the gross carrying amount of assets in stage 3 are ISK 17,160 million (31.12.2018: ISK 18,175 million) with ISK 11,331 million in collateral (31.12.2018: ISK 12,881 million), there of ISK 9,884 million in real estate (31.12.2018: 11,045 million).

Collateral repossessed

During the period the Group took possession of assets due to foreclosures. The total amounts of real estates the Group took possession of during the period and still holds at the end of the period amount to ISK 275 million (31.12.2018: ISK 827 million). The Group did not take position of other assets during the period (31.12.2018: ISK 31 million). The assets are held for sale, see Note 29.

Credit quality

The Bank uses internal credit rating models and external credit ratings if available to monitor credit risk. The internal credit rating models rate customers with one of four statistical models based on a variety of information that has been determined to be predictive of default. These include demographic, behavioral, financial and economic data, coupled with qualitative expert judgement for large corporate exposures. Two models rate individuals' exposures – one for prime mortgages and another for other exposures. The models are updated at least annually and recalibrated with current data with the aim of maintaining their predictive power. Year-on-year changes in risk classification of loans may in part be due to model refinement. External ratings are used for marketable securities, cash and balances, and loans to credit institutions. For further information on the rating scales used, see Note 57 in the Annual Financial Statements 2018.

The tables below show financial instruments subject to the impairment requirements of IFRS 9 broken down by rating scale, where risk class 5, DD denotes, the highest risk. Assets carried at fair value through profit and loss are not subject to the impairment requirements of IFRS 9. The tables below sum up the gross carrying amount of assets by rating class and current impairment stage. The gross carrying amount net of loss allowance shows the book value of the underlying assets.

Exposures that are 'Unrated' are typically due to newly formed entities, entities for which the Bank's rating models are not applicable or no external rating is available. Comparative figures have not been restated.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

42. Credit risk, continued

Credit quality profile by rating class

31.3.2019	Cash and balances with CB	Loans to credit institutions	Financial instru-ments at FVOCI
Loans to credit institutions, securities and cash			
Investment grade	94,126	84,601	64,848
Non-investment grade	-	416	-
Gross carrying amount	94,126	85,017	64,848
Loss allowance	(2)	(39)	(8)
Book value	94,124	84,978	64,840

Loans to customers	Stage 1	Stage 2	Stage 3	POCI	Total
Risk class 0 to 1 - (Grades AAA to BBB-)	370,250	126	-	-	370,376
Risk class 2 - (Grades BB+ to BB-)	263,423	23,789	-	-	287,212
Risk class 3 - (Grades B+ to B-)	105,871	26,836	-	80	132,787
Risk class 4 - (Grades CCC+ to CCC-)	13,731	12,957	-	139	26,827
Risk class 5 - (DD)	-	-	17,152	3,603	20,755
Unrated	940	248	1	-	1,189
Gross carrying amount	754,215	63,956	17,153	3,822	839,146
Loss allowance	(1,612)	(953)	(6,048)	(1,287)	(9,900)
Book value	752,603	63,003	11,105	2,535	829,246
Loans to customers - Individuals					
Risk class 0 to 1 - (Grades AAA to BBB-)	220,996	-	-	-	220,996
Risk class 2 - (Grades BB+ to BB-)	117,506	7,691	-	-	125,197
Risk class 3 - (Grades B+ to B-)	29,642	3,906	-	80	33,628
Risk class 4 - (Grades CCC+ to CCC-)	7,338	7,437	-	139	14,914
Risk class 5 - (DD)	-	-	7,605	649	8,254
Unrated	178	2	1	-	181
Gross carrying amount	375,660	19,036	7,606	868	403,170
Loss allowance	(857)	(409)	(2,097)	(233)	(3,596)
Book value	374,803	18,627	5,509	635	399,574
Loans to customers - Companies and sovereign					
Risk class 0 to 1 - (Grades AAA to BBB-)	149,254	126	-	-	149,380
Risk class 2 - (Grades BB+ to BB-)	145,917	16,098	-	-	162,015
Risk class 3 - (Grades B+ to B-)	76,229	22,930	-	-	99,159
Risk class 4 - (Grades CCC+ to CCC-)	6,393	5,520	-	-	11,913
Risk class 5 - (DD)	-	-	9,547	2,954	12,501
Unrated	762	246	-	-	1,008
Gross carrying amount	378,555	44,920	9,547	2,954	435,976
Loss allowance	(755)	(544)	(3,951)	(1,054)	(6,304)
Book value	377,800	44,376	5,596	1,900	429,672

Loan commitments, guarantees and unused credit facilities	Stage 1	Stage 2	Stage 3	Total
Risk class 0 to 1 - (Grades AAA to BBB-)	69,352	4	-	69,356
Risk class 2 to 4 - (Grades BB+ to CCC-)	55,072	5,230	3,079	63,381
Unrated	2	121	-	123
Gross carrying amount	124,426	5,355	3,079	132,860
Loss Allowance	(165)	(185)	(1,234)	(1,584)
Book value	124,261	5,170	1,845	131,276

Amounts are in ISK millions

42. Credit risk, continued

31.12.2018

Loans to credit institutions, securities and cash	Cash and balances with CB	Loans to credit institutions	Financial instru-ments at FVOCI
Investment grade	83,141	55,954	53,795
Non-investment grade	-	403	-
Gross carrying amount	83,141	56,357	53,795
Loss allowance	(2)	(35)	(7)
Book value	83,139	56,322	53,788

Loans to customers	Stage 1	Stage 2	Stage 3	POCI	Total
Risk class 0 to 1 - (Grades AAA to BBB-)	370,832	78	-	-	370,910
Risk class 2 - (Grades BB+ to BB-)	265,361	18,521	-	41	283,923
Risk class 3 - (Grades B+ to B-)	107,897	24,582	-	87	132,566
Risk class 4 - (Grades CCC+ to CCC-)	15,287	11,318	-	48	26,653
Risk class 5 - (DD)	-	-	18,175	3,640	21,815
Unrated	1,977	1,061	-	-	3,038
Gross carrying amount	761,354	55,560	18,175	3,816	838,905
Loss allowance	(1,415)	(931)	(6,301)	(1,244)	(9,891)
Book value	759,939	54,629	11,874	2,572	829,014
Loans to customers - Individuals					
Risk class 0 to 1 - (Grades AAA to BBB-)	222,003	-	-	-	222,003
Risk class 2 - (Grades BB+ to BB-)	118,271	4,831	-	41	123,143
Risk class 3 - (Grades B+ to B-)	32,562	3,255	-	87	35,904
Risk class 4 - (Grades CCC+ to CCC-)	8,368	5,390	-	48	13,806
Risk class 5 - (DD)	-	-	8,467	815	9,282
Unrated	32	3	-	-	35
Gross carrying amount	381,236	13,479	8,467	991	404,173
Loss allowance	(739)	(311)	(2,408)	(233)	(3,691)
Book value	380,497	13,168	6,059	758	400,482
Loans to customers - Companies and sovereign					
Risk class 0 to 1 - (Grades AAA to BBB-)	148,829	78	-	-	148,907
Risk class 2 - (Grades BB+ to BB-)	147,090	13,690	-	-	160,780
Risk class 3 - (Grades B+ to B-)	75,335	21,327	-	-	96,662
Risk class 4 - (Grades CCC+ to CCC-)	6,919	5,928	-	-	12,847
Risk class 5 - (DD)	-	-	9,708	2,825	12,533
Unrated	1,945	1,058	-	-	3,003
Gross carrying amount	380,118	42,081	9,708	2,825	434,732
Loss allowance	(676)	(620)	(3,893)	(1,011)	(6,200)
Book value	379,442	41,461	5,815	1,814	428,532

Loan commitments, guarantees and unused credit facilities	Stage 1	Stage 2	Stage 3	Total
Risk class 0 to 1 - (Grades AAA to BBB-)	78,151	1	-	78,152
Risk class 2 to 4 - (Grades BB+ to CCC-)	55,751	6,589	1,676	64,016
Unrated	368	38	-	406
Gross carrying amount	134,270	6,628	1,676	142,574
Loss Allowance	(147)	(485)	(57)	(689)
Book value	134,123	6,143	1,619	141,885

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

42. Credit risk, continued

The following tables reconciles the opening and closing allowance balance for loans to customers at amortized cost and loan commitments, guarantees and unused credit facilities by their impairment requirements.

The reconciliation includes:

Transfers of financial assets between impairment requirements: include transfers to 12 month expected credit losses, to lifetime expected credit losses and credit impaired financial assets. All transfers are presumed to occur before any corresponding remeasurement of the loss allowance.

Net remeasurement of loss allowance: comprise the impact of changes in model inputs or assumptions, including changes in forward-looking macroeconomic conditions, partial repayments and additional draws on existing facilities, inflation, changes in the measurement following a transfer between stages, impairment of interest income due to impaired debt instruments and unwinding of the time value discount due to the passage of time.

New financial assets: include purchases and originations and reflect the allowance related to assets newly recognized during the period.

Derecognitions and maturities, reflect the allowance related to assets derecognized during the period without a credit loss being incurred, including those assets that were derecognized following a modification of terms.

Write-offs: the amount after net remeasurements of loss allowance written off during the period.

Foreign exchange: the effects of foreign exchange on the loss allowance between periods.

During the first quarter there were no significant changes to the models used to estimate expected credit loss.

During the reporting period changes were made to the probability weights of the different macro-economic scenarios used for impairment calculations to reflect the expected development of unemployment over the next years. The updated probability weights are based on the newly revised economic outlook from Arion Bank's Research Department.

31.3.2019

*Impairment loss allowance total **	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the year	1,607	1,416	6,358	1,244	10,625
Transfers of financial assets:					
Transfers to Stage 1 - (12-month ECL)	504	(291)	(213)	-	-
Transfers to Stage 2 - (lifetime ECL)	(139)	172	(33)	-	-
Transfers to Stage 3 - (credit impaired financial assets)	(34)	(627)	661	-	-
Net remeasurement of loss allowance **	(251)	485	1,343	50	1,627
New financial assets, originated or purchased	243	68	272	-	583
Derecognitions and maturities	(107)	(102)	(495)	-	(704)
Write-offs ***	(15)	(1)	(701)	(42)	(759)
Foreign exchange difference	14	18	90	35	157
Impairment loss allowance ****	1,822	1,138	7,282	1,287	11,529
Impairment loss allowances for assets only carrying 12-month ECL	49	-	-	-	49
Total Impairment loss allowance	1,871	1,138	7,282	1,287	11,578

* These amounts are a combination of all impairments, including an allowance for loan commitments and guarantees presented as a liability in the financial statements.

** During the reporting period the loss allowance balance for stage 3 loans was raised by 151 million ISK due to unwinding of interest income.

** During the reporting period an amount of ISK 692 million was written off but is still subject to enforcement activities subject to Icelandic law.

*** Loss allowance for all assets other than cash, bonds and loans to credit institutions.

Impairment loss allowance for loans to customers	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the year	1,415	931	6,301	1,244	9,891
Transfers of financial assets					
Transfers to Stage 1 - (12-month ECL)	479	(266)	(213)	-	-
Transfers to Stage 2 - (lifetime ECL)	(130)	163	(33)	-	-
Transfers to Stage 3 - (credit impaired financial assets)	(33)	(172)	205	-	-
Net remeasurement of loss allowance	(233)	311	636	50	764
New financial assets, originated or purchased	214	68	272	-	554
Derecognitions and maturities	(98)	(89)	(495)	-	(682)
Write-offs	(15)	(1)	(701)	(42)	(759)
Foreign exchange	13	8	76	35	132
Total loss allowance for loans to customers	1,612	953	6,048	1,287	9,900

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

42. Credit risk, continued

Impairment loss allowance for loans to customers - Individuals	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the year	740	313	2,406	232	3,691
Transfers of financial assets					
Transfers to Stage 1 - (12-month ECL)	214	(158)	(56)	-	-
Transfers to Stage 2 - (lifetime ECL)	(87)	119	(32)	-	-
Transfers to Stage 3 - (credit impaired financial assets)	(21)	(62)	83	-	-
Net remeasurement of loss allowance	(16)	208	38	39	269
New financial assets, originated or purchased	71	1	3	-	75
Derecognitions and maturities	(29)	(11)	(49)	-	(89)
Write-offs	(15)	(1)	(309)	(39)	(364)
Foreign exchange	-	-	13	1	14
Total loss allowance for Individuals	857	409	2,097	233	3,596

Impairment loss allowance for loans to customers - Companies and sovereign	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the year	675	618	3,895	1,012	6,200
Transfers of financial assets					
Transfers to Stage 1 - (12-month ECL)	265	(108)	(157)	-	-
Transfers to Stage 2 - (lifetime ECL)	(43)	44	(1)	-	-
Transfers to Stage 3 - (credit impaired financial assets)	(12)	(110)	122	-	-
Net remeasurement of loss allowance	(217)	103	598	11	495
New financial assets, originated or purchased	143	67	269	-	479
Derecognitions and maturities	(69)	(78)	(446)	-	(593)
Write-offs	-	-	(392)	(3)	(395)
Foreign exchange	13	8	63	34	118
Total loss allowance for companies and sovereign	755	544	3,951	1,054	6,304

Impairment loss allowance for loan commitments, guarantees and unused credit facilities	Stage 1	Stage 2	Stage 3	Total
Balance at the beginning of the year	147	485	57	689
Transfers				
Transfers to 12-month ECL	25	(25)	-	-
Transfers to lifetime ECL	(9)	9	-	-
Transfers to credit impaired	(1)	(455)	456	-
Net remeasurement of loss allowance	(18)	174	707	863
New financial commitments originated	29	-	-	29
Derecognitions and maturities	(9)	(13)	-	(22)
Foreign exchange	1	10	14	25
Total loss allowance for loan commit., guarantees and unused credit facilitis	165	185	1,234	1,584

Large exposures

A large exposure is defined as an exposure to a group of financially related borrowers which is equal to or exceeds 10% of the Group's eligible capital according to Financial Undertakings Act No. 161/2002 and Regulation No. 233/2017 on prudential requirements. The legal maximum for individual large exposures is 25% of eligible capital, net of eligible credit risk mitigation.

The Group had one large exposure of ISK 18.3 billion at the end of the period before taking account of eligible credit risk mitigation (31.12.2018: no large exposure).

Amounts are in ISK millions

43. Market risk

Market risk is the current or prospective risk that changes in financial market prices and rates adversely affect the Group's earnings and equity position due to changes to the value and cash flows of its assets and liabilities.

Market risk arises from imbalances in the Group's balance sheet as well as in market making activities and position taking in bonds, equities, currencies, derivatives, and other commitments which are marked to market.

The Group keeps close track of market risk and separates its exposures for the trading book and the banking book. Market risk in the trading book arises from market making activities and non-strategic derivatives positions arising from the Bank's operations of meeting customers' investment and risk management needs. Market risk in the banking book arises from various mismatches in assets and liabilities in e.g. currencies, maturities and interest rates. Market risk in the trading book and in the banking book is managed separately.

Market risk allowance is set by the Board in the Bank's risk appetite and limit frameworks are in place for each trading desk. The Asset and Liability Committee (ALCO) is responsible for managing the Bank's overall market risk. Risk Management is responsible for measuring and monitoring market risk exposure, and reporting the exposure, usage and limit breaches.

The Group aims to manage and limit market exposures and imbalances between assets and liabilities in accordance with its strategic goals for net profit.

Interest rate risk

Interest rate risk arises from the possibility that changes in market rates adversely affect net interest income and fair value of interest-bearing instruments on the Group's balance sheet. The Group's operations are subject to interest rate risk due to mismatches in the fixing of interest rates between assets and liabilities, resulting in a repricing risk for the Group. The Group also faces interest basis risk between interest-bearing assets and interest-bearing liabilities due to different types of floating-rate indices in different currencies.

The Group's interest rate risk for foreign currencies is limited as foreign denominated assets predominantly have short fixing periods and the Group has applied cash flow hedging for its foreign denominated fixed rate borrowings. For domestic rates, longer fixing periods are more common, and this especially applies to indexed mortgages issued between 2004 and 2006, the cash flow profile of which has been largely matched by that of the Group's structured covered bonds issues, which serves as a hedge against repricing risk. The Group has been able to manage relatively small interest fixing gaps.

Due to favorable refinancing spreads, prepayments and/or refinancing of loans have been considerable over the past few years, resulting in reduced average duration of fixed rates for the Bank's assets. Prepayment risk is mitigated by prepayment fees and the Group's own prepayment options. The Group's prepayment of structured covered bonds is a reaction to mortgage prepayments and mortgage refinancing.

Interest rate risk in the banking book

The following table shows the Group's interest-bearing assets and liabilities by interest fixing periods. The figures for loans to customers and borrowings are shown on a fair value basis, see Note 24, and are therefore different from the amounts shown in these Consolidated Financial Statements. The fair value reflects the likelihood of prepayment. Defaulted loans are presented at book value, which is based on the value of the underlying collateral, and are therefore assumed to be independent of interest adjustment periods and placed in the 'Up to 3 months' category. The assets and liabilities of Valitor holding hf. are not included in the figures as they are classified as held for sale.

31.3.2019	Up to 3 months	3-12 months	1-5 years	5-10 years	Over 10 years	Total
Assets						
Balances with Central Bank	89,775	-	-	-	-	89,775
Loans to credit institutions	84,978	-	-	-	-	84,978
Loans to customers	510,083	69,159	156,731	5,831	93,865	835,669
Financial instruments	15,156	16,638	31,859	-	1,208	64,861
Assets	699,992	85,797	188,590	5,831	95,073	1,075,283
Liabilities						
Due to credit institutions and Central Bank	9,183	-	-	-	-	9,183
Deposits	428,978	45,463	13,585	1,442	1,006	490,474
Borrowings	51,665	10,329	205,234	63,303	128,327	458,858
Subordinated loans	7,283	-	-	-	-	7,283
Liabilities	497,109	55,792	218,819	64,745	129,333	965,798
Derivatives and other off-balance sheet items (net position)	(149,908)	-	155,635	(2,362)	-	3,365
Net interest gap	52,975	30,005	125,406	(61,276)	(34,260)	112,850

Amounts are in ISK millions

43. Market risk, continued

31.12.2018	Up to 3 months	3-12 months	1-5 years	5-10 years	Over 10 years	Total
Total assets	647,069	99,494	179,700	8,458	95,903	1,030,624
Total liabilities	(483,493)	(53,519)	(203,267)	(45,808)	(122,106)	(908,193)
Derivatives and other off-balance sheet items (net position)	(185,255)	40,259	150,397	(2,484)	-	2,917
Net interest gap	(21,679)	86,234	126,830	(39,834)	(26,203)	125,348

Sensitivity analysis of interest rate risk in the banking book

The following table shows the sensitivity of the Group's net present value (NPV) of interest-bearing assets and liabilities and variation of annual net interest income (NII), due to changes in interest rates by currencies. The variation is calculated on the basis of simultaneous parallel shifts upwards or downwards of yield curves. The choice of shifts is not an estimate of risk likelihood. Behavioral maturities are taken into account in the NPV calculations, including prepayment likelihood and expected behavior of non-maturing deposits. The change to NII is however purely based on contractual interest rate adjustments where it is simplistically assumed that all rates are equally sensitive to the presumed change in market rates.

	31.3.2019		31.12.2018	
NPV change	-100 bps	+100 bps	-100 bps	+100 bps
ISK, CPI index-linked	(5,370)	5,492	(4,544)	4,872
ISK, Non index-linked	(177)	639	624	(139)
Foreign currencies	508	(521)	700	(708)

	31.3.2019		31.12.2018	
NII change	-100 bps	+100 bps	-100 bps	+100 bps
ISK, CPI index-linked	(730)	730	(828)	828
ISK, Non index-linked	(328)	328	(90)	90
Foreign currencies	171	(171)	232	(232)

Sensitivity analysis of interest rate risk in the trading book

The following table shows the interest sensitivity of the Group's net positions in the trading book by currencies. Sensitivity is quantified as the net change in value when assuming a simultaneous parallel shift upwards and downwards of all yield curves by 100 basis points. The sensitivity does not relate to variation of annual net interest income and is not an estimate of risk. The calculations are based on duration and convexity in this table.

	31.3.2019		31.12.2018	
Currency	-100 bps	+100 bps	-100 bps	+100 bps
ISK, CPI index-linked	151	(140)	123	(111)
ISK, Non index-linked	94	(86)	62	(54)
Foreign currencies	7	(6)	13	(13)

Amounts are in ISK millions

43. Market risk, continued

Indexation risk

A significant part of the Group's balance sheet is linked to the Icelandic Consumer Price Index (CPI). For index-linked instruments, principal and interest payments are adjusted proportionally to the CPI. The Group is exposed to indexation risk as indexed assets exceed indexed liabilities. Financial instruments held for liquidity or market making purposes are assumed to be on demand. The imbalance has markedly decreased in the past year due to prepayments of indexed loans while indexed liabilities have increased.

Book value and maturity profile of indexed assets and liabilities

31.3.2019	Up to 1 year	1 to 5 years	Over 5 years	Total
Assets, CPI index-linked				
Loans to customers	24,043	79,034	244,030	347,107
Financial instruments	13,621	-	-	13,621
Off-balance sheet position	539	-	-	539
Assets, CPI index-linked	38,203	79,034	244,030	361,267
Liabilities, CPI index-linked				
Deposits	75,640	13,220	2,435	91,295
Borrowings	6,369	17,806	154,660	178,835
Other	991	375	1,591	2,957
Off-balance sheet position	913	6,104	1,103	8,120
Liabilities, CPI index-linked	83,913	37,505	159,789	281,207
Net on-balance sheet position	(45,336)	47,633	85,344	87,641
Net off-balance sheet position	(374)	(6,104)	(1,103)	(7,581)
CPI Balance	(45,710)	41,529	84,241	80,060

31.12.2018	Up to 1 year	1 to 5 years	Over 5 years	Total
Assets, CPI index-linked				
Loans to customers	30,455	79,761	246,605	356,821
Financial instruments	12,791	-	-	12,791
Off-balance sheet position	532	(995)	-	(463)
Assets, CPI index-linked	43,778	78,766	246,605	369,149
Liabilities, CPI index-linked				
Deposits	72,766	12,735	2,367	87,868
Borrowings	6,482	17,567	147,209	171,258
Other	875	208	1,420	2,503
Off-balance sheet position	895	4,999	1,082	6,976
Liabilities, CPI indexed linked	81,018	35,509	152,078	268,605
Net on-balance sheet position	(36,877)	49,251	95,609	107,983
Net off-balance sheet position	(363)	(5,994)	(1,082)	(7,439)
CPI Balance	(37,240)	43,257	94,527	100,544

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

43. Market risk, continued

Currency risk

Currency risk is the risk of loss due to adverse movements in foreign exchange rates. The Group is exposed to currency risk through a currency mismatch between assets and liabilities. ISK denominated deposits are a primary source of funding for the Group whereas a substantial part of the Group's assets consists of foreign currency denominated loans to customers. Net exposures per currency are monitored centrally in the Bank.

Breakdown of assets and liabilities by currency

31.3.2019

Financial assets	ISK	EUR	USD	GBP	DKK	NOK	Other	Total
Cash and balances with CB	92,959	343	256	135	90	47	294	94,124
Loans to credit institutions	2,354	34,406	23,470	1,166	1,284	15,345	6,953	84,978
Loans to customers	679,065	98,897	35,386	3,416	6,276	734	5,472	829,246
Financial instruments	58,242	30,044	26,252	849	71	12,455	190	128,103
Other financial assets	10,927	212	60	-	4	4	3	11,210
Financial assets	843,547	163,902	85,424	5,566	7,725	28,585	12,912	1,147,661
Financial liabilities								
Due to credit inst. and Central Bank	5,726	1,532	1,925	-	-	-	-	9,183
Deposits	402,299	47,470	29,921	2,430	2,665	1,768	3,921	490,474
Financial liabilities at fair value	1,487	425	141	46	-	104	83	2,286
Other financial liabilities	8,997	903	2,459	248	170	123	597	13,497
Borrowings	228,706	173,599	-	-	-	34,158	8,614	445,077
Subordinated liabilities	-	681	-	-	-	-	6,602	7,283
Financial liabilities	647,215	224,610	34,446	2,724	2,835	36,153	19,817	967,800
Net on-balance sheet position	196,332	(60,708)	50,978	2,842	4,890	(7,568)	(6,905)	
Net off-balance sheet position	650	50,231	(51,106)	(5,652)	(8,149)	7,490	6,536	
Net position	196,982	(10,477)	(128)	(2,810)	(3,259)	(78)	(369)	
Non-financial assets								
Investment property	7,101	-	-	-	-	-	-	7,101
Investments in associates	807	-	-	-	-	-	-	807
Intangible assets	7,081	-	-	-	-	-	-	7,081
Tax assets	15	-	-	-	-	-	-	15
Assets and disposal groups held for sale	23,180	12,228	901	8,110	4,732	692	1,478	51,321
Other non financial assets	8,540	78	36	35	(1)	20	1	8,709
Non-financial assets	46,724	12,306	937	8,145	4,731	712	1,479	75,034
Non-financial liabilities and equity								
Tax liabilities	4,822	-	-	-	-	-	-	4,822
Liabilities associated with disposal groups held for sale	19,284	2,742	923	3,279	1,450	591	1,229	29,498
Other non-financial liabilities	27,801	63	18	1	2	-	(364)	27,521
Shareholders' equity	192,924	-	-	-	-	-	-	192,924
Non-controlling interest	130	-	-	-	-	-	-	130
Non-financial liabilities and equity	244,961	2,805	941	3,280	1,452	591	865	254,895
Management reporting of currency risk *	(1,255)	(976)	(132)	2,055	20	43	245	

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

43. Market risk, continued

31.12.2018

	ISK	EUR	USD	GBP	DKK	NOK	Other	Total
Financial assets	824,049	152,259	74,734	5,713	8,519	18,126	10,251	1,093,651
Financial liabilities	(628,862)	(203,148)	(25,565)	(2,316)	(1,965)	(24,062)	(22,117)	(908,035)
Net on-balance sheet position	195,187	(50,889)	49,169	3,397	6,554	(5,936)	(11,866)	
Net off-balance sheet position	5,071	44,881	(48,840)	(7,403)	(10,536)	5,963	10,864	
Net position	200,258	(6,008)	329	(4,006)	(3,982)	27	(1,002)	
Non-financial assets	45,884	9,964	1,029	7,611	4,005	555	1,628	70,676
Non-financial liabilities and equity	(249,704)	(1,324)	(813)	(3,378)	(578)	(400)	(95)	(256,292)
Management reporting of currency risk *	(3,562)	2,632	545	227	(555)	182	531	

* The net position of the currency risk is presented in accordance with IFRS. The management monitors currency risk with more assets and liabilities underlying, such as tax assets and liabilities and intangible assets, as it is considered to be a more accurate measurement of the Group's currency exposure. The net position, as seen by the management, is the position used for managing the currency imbalance.

Sensitivity analysis on currency risk

The table below indicates the currencies to which the Group had significant exposure at the end of the period. The analysis calculates the effect of a reasonably possible movement of the currency rate against the ISK, with all other variables held constant, on the Consolidated Interim Income Statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities). A negative amount in the table reflects a potential net reduction in the Consolidated Interim Income Statement or equity, while a positive amount reflects a net potential increase. An equivalent decrease in each of the below currencies against the ISK would have resulted in an equivalent but opposite impact (+10% denotes a depreciation of the ISK).

	31.3.2019		31.12.2018	
Currency	-10%	+10%	-10%	+10%
EUR	98	(98)	(263)	263
USD	13	(13)	(55)	55
GBP	(206)	206	(23)	23
DKK	(2)	2	56	(56)
NOK	(4)	4	(18)	18
Other	(25)	25	(53)	53

Equity risk

Equity risk is the risk that the fair value of equities decreases as the result of changes in the level of equity indices and individual stocks. For information on assets seized and held for sale and equity exposures, see Notes 30 and 23 respectively.

Sensitivity analysis of equity risk

The analysis below calculates the effect of a reasonable possible movement in equity prices that affect the Consolidated Interim Financial Statement. A negative amount in the table reflects a potential net reduction in the Consolidated Interim Income Statement or equity, while a positive amount reflects a potential net increase. Investments in associates are excluded. The result of value-at-risk calculations for the trading book are shown in the Group's Pillar 3 Disclosures.

	31.3.2019		31.12.2018	
Equity	-10%	+10%	-10%	+10%
Trading book - listed	(419)	419	(231)	231
Banking book - listed	(574)	574	(487)	487
Banking book - unlisted	(618)	618	(617)	617

Derivatives

Derivatives are a part of the Group's customer product offering. The types of derivatives currently offered are forward contracts, swaps and options. Eligible underlying market factors are interest rates, foreign exchange rates, equities and commodities. Exposure limits, hedging requirements and collateral requirements are determined in accordance with the Group's risk appetite and monitored by Risk Management on a daily basis. The Group also uses derivatives to reduce market risk on its balance sheet. Note 24 shows a breakdown of the Group's derivative positions by type.

Amounts are in ISK millions

44. Liquidity and Funding risk

Liquidity risk is defined as the risk that the Group, though solvent, either does not have sufficient financial resources available to meet its liabilities when they fall due, or can secure them only at excessive cost. Liquidity risk arises from the inability to manage unplanned decreases or changes in funding sources.

A primary source of funding for the Group is from deposits from individuals, businesses and financial undertakings. The Group's liquidity risk stems from the fact that the maturity of loans exceeds the maturity of deposits, of which 71% is on-demand.

Liquidity risk is one of the Group's most significant risk factors and a great deal of emphasis is placed on managing it. The Asset and Liability Committee (ALCO) is responsible for managing liquidity and funding risk within the risk appetite set by the Board of Directors. The Bank's Treasury manages liquidity positions on a day-to-day basis. Risk Management measures, monitors and reports the Bank's liquidity and funding risk on a daily basis.

The Group's strategy in relation to liquidity risk is to actively manage its liquidity positions and risks to meet payment and settlement obligations on a timely basis under both normal and stressed conditions. The Group seeks to maintain a stable funding profile which supports its business strategy and liquidity profile, ensuring that the Group can withstand periods of market turbulence, without reliance on volatile funding or external support.

Maturity analysis of assets and liabilities

The maturity analysis is based on contractual cash flows. The amounts are not discounted and include future interest payments, but CPI-linked amounts do not include accrued indexation due to future inflation. The total amount for each item is higher than the corresponding amount on the Bank's balance sheet, since the amounts on the balance sheet are either at amortized cost and do not contain future interest payments, or at fair value where future cash flows have been discounted.

Contractual cash flow of assets and liabilities

31.3.2019	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	With no maturity	Total	Carrying amount
Financial assets								
Cash and balances with CB	17,401	71,660	5,157	-	-	-	94,218	94,124
Loans to credit institutions	51,877	32,701	419	-	-	-	84,997	84,978
Loans to customers	3,529	128,078	124,083	323,627	654,987	-	1,234,304	829,246
Financial instruments	16,319	10,775	20,666	48,699	6,017	30,760	133,236	128,103
Derivatives - assets leg	-	*43,753*	*7,035*	*52,266*	*1,561*	-	*104,615*	*104,615*
Derivatives - liabilities leg	-	*(41,769)*	*(6,287)*	*(46,638)*	*(1,395)*	-	*(96,089)*	*(96,089)*
Other financial assets	407	7,085	2,941	777	-	-	11,210	11,210
Financial assets	89,533	250,299	153,266	373,103	661,004	30,760	1,557,965	1,147,661
Financial liabilities								
Due to credit inst. and Central Bank	5,793	3,419	-	-	-	-	9,212	9,183
Deposits	349,109	74,242	46,070	13,753	8,625	-	491,799	490,474
Financial liabilities at fair value	-	1,053	1,314	2,824	300	-	5,491	2,286
Derivatives - assets leg	-	*(33,342)*	*(12,726)*	*(7,274)*	*(5,804)*	-	*(59,146)*	*(59,146)*
Derivatives - liabilities leg	-	*34,120*	*14,040*	*10,098*	*6,104*	-	*64,362*	*64,362*
Short position bonds and derivatives	-	*222*	-	-	-	-	*222*	*222*
Short position securities used for economic hedging	-	*53*	-	-	-	-	*53*	*53*
Other financial liabilities	288	9,606	2,698	540	-	-	13,132	13,132
Borrowings	-	31,615	28,901	265,590	213,825	-	539,931	445,077
Subordinated liabilities	-	70	215	1,061	7,995	-	9,341	7,283
Financial liabilities	355,190	120,005	79,198	283,768	230,745	-	1,068,906	967,435
Net position for assets and liab.	(265,657)	130,294	74,068	89,335	430,259	30,760	489,059	180,226
Off-balance sheet items								
Financial guarantees	4,400	1,150	4,514	2,642	1,722	-	14,428	14,428
Unused overdraft	-	45,420	-	-	-	-	45,420	45,420
Undrawn loan commitments	-	54,055	14,587	4,370	-	-	73,012	73,012
Off-balance sheet items	4,400	100,625	19,101	7,012	1,722	-	132,860	132,860
Net contractual cash flow	(270,057)	29,669	54,967	82,323	428,537	30,760	356,199	47,366

Amounts are in ISK millions

44. Liquidity and Funding risk, continued

31.12.2018	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	With no maturity	Total	Carrying amount
Financial assets	55,046	224,391	151,214	378,223	664,122	31,668	1,504,664	1,093,651
Financial liabilities	(344,919)	(107,484)	(77,951)	(266,915)	(209,127)	-	(1,006,396)	(908,035)
Net position for assets and liab.	(289,873)	116,907	73,263	111,308	454,995	31,668	498,268	185,616
Off-balance sheet items	(4,225)	(103,563)	(25,621)	(7,375)	(1,790)	-	(142,574)	(142,574)
Net contractual cash flow	(294,098)	13,344	47,642	103,933	453,205	31,668	355,694	43,042

Net Stable Funding Ratio

The net stable funding ratio (NSFR) measures the amount of available stable funding (ASF) at the Group against the required stable funding (RSF) as per the definition of the Central Bank of Iceland rules No. 1032/2014. In general, RSF is determined by applying different weights to different asset classes depending on the level of liquidity. ASF however is calculated by applying weights to the Group's liabilities depending on maturity and/or stickiness. The NSFR for foreign currency shall exceed 100%.

Calculations of the NSFR are based on consolidated figures for the Bank and Arion Bank Mortgages Institutional Investor Fund. When calculating the ratio for foreign currencies, a negative foreign currency balance is subtracted from the numerator and a positive balance is subtracted from the denominator. The foreign currency balance used is different from that of this Consolidated Financial Statement due to the sub-consolidation applied.

31.3.2019	ISK	Foreign currency	Total
Available stable funding	694,423	231,463	925,886
Required stable funding	626,593	137,400	763,993
Foreign currency balance		(10,598)	
Net stable funding ratio	111%	161%	121%

31.12.2018			
Available stable funding	681,074	215,434	896,508
Required stable funding	615,717	134,082	749,799
Foreign currency balance		(7,102)	
Net stable funding ratio	111%	155%	120%

Amounts are in ISK millions

44. Liquidity and Funding risk, continued

Liquidity coverage ratio

The Liquidity Coverage Ratio (LCR) is one of the standards introduced in the Basel III Accord. The LCR is the result of a stress test that is designed to ensure that banks have the necessary assets on hand to withstand short-term liquidity disruptions. More precisely, LCR represents the balance between highly liquid assets and the expected net cash outflow of the Group in the next 30 days under stressed conditions.

To qualify as highly liquid assets under the LCR rules, assets must be non-pledged, liquid and easily priced on the market, traded on an active market and not issued by the Group or related entities.

The Bank complies with The Central Bank of Iceland's liquidity rules No. 266/2017, which effectively adopt the liquidity rules of the EU Capital Requirements Regulation (CRR). The Bank is required to maintain a 100% minimum LCR ratio for both the aggregate position in all foreign currencies and all currencies.

The following table shows the breakdown for the Group's LCR calculations broken down by currencies. All amounts are weighted by their respective LCR weights. The calculations are based on consolidated figures for the Bank, the Arion Bank Mortgages Institutional Investor Fund and Valitor Holding hf.

31.3.2019	ISK	Foreign currency	Total
Liquid assets level 1 *	86,428	55,751	142,179
Liquid assets level 2	-	-	-
Liquid Assets	86,428	55,751	142,179
Deposits	89,578	41,959	131,537
Borrowing	3,614	20,317	23,931
Other cash outflows	9,244	9,401	18,645
Cash outflows	102,436	71,677	174,113
Short-term deposits with other banks **	3,452	81,778	85,230
Other cash inflows	17,486	4,642	22,128
Cash inflows	20,938	86,420	107,358
Liquidity coverage ratio (LCR) ***	106%	311%	213%

31.12.2018	ISK	Foreign currency	Total
Liquid assets level 1 *	75,340	48,806	124,146
Liquid assets level 2	-	-	-
Liquid Assets	75,340	48,806	124,146
Deposits	91,008	33,983	124,991
Borrowing	4,413	109	4,522
Other cash outflows	9,229	10,347	19,576
Cash outflows	104,650	44,439	149,089
Short-term deposits with other banks **	4,011	56,527	60,538
Other cash inflows	10,719	2,314	13,033
Cash inflows	14,730	58,841	73,571
Liquidity coverage ratio (LCR) ***	84%	439%	164%

* Level 1 assets include the Group's cash and balances with the Central Bank, domestic bonds eligible as collateral at the Central Bank and foreign government bonds which receive 100% weight. Under Rules No. 266/2017 the Group's covered bonds also classify as Level 1 assets and receive 93% weight.

** Short-term deposits with other banks are defined as cash inflows in LCR calculations.

*** LCR is defined as: LCR = Weighted liquid assets / (weighted cash outflows - weighted cash inflows) where weighted cash inflows are capped at 75% of weighted cash outflows.

Amounts are in ISK millions

44. Liquidity and Funding risk, continued

Composition of liquid assets

The following table shows the composition of the Group's liquidity buffer.

31.03.2019	ISK	USD	EUR	Other	Total
Cash and balances with Central Bank	96,119	256	343	567	97,285
Short-term deposits in other banks	3,452	23,883	32,224	25,671	85,230
Domestic bonds eligible as collateral at the Central Bank	7,405	-	-	-	7,405
Foreign government bonds	-	19,931	21,317	7,881	49,129
Covered bonds with a minimum rating of AA-	-	-	1,386	5,303	6,689
Liquidity reserve	106,976	44,070	55,270	39,422	245,738
31.12.2018					
Cash and balances with Central Bank	88,687	222	833	838	90,580
Short-term deposits in other banks	4,012	14,141	16,265	26,120	60,538
Domestic bonds eligible as collateral at the Central Bank	4,844	-	-	-	4,844
Foreign government bonds	-	21,152	21,961	757	43,870
Covered bonds with a minimum rating of AA-	-	-	1,340	1,625	2,965
Liquidity reserve	97,543	35,515	40,399	29,340	202,797

LCR deposit categorization

As per the LCR methodology, the Group's deposit base is split into different categories depending on customer type. A second categorization is used where term deposits refer to deposits with a residual maturity greater than 30 days. Deposits that can be withdrawn within 30 days are marked stable if the customer has a business relationship with the Group and the amount is covered by the Deposit Insurance Scheme. Other deposit funds are considered less stable. A weight is attributed to each category, representing the expected outflow under stressed conditions, i.e. the level of stickiness.

The table below shows the breakdown of the Group's deposit base according to the LCR categorization, with the associated expected stressed outflow weights.

LCR categorization - amounts and LCR outflow weights

	Deposits maturing within 30 days					
31.3.2019	Less Stable	Weight (%)	Stable	Weight (%)	Term deposits*	Total deposits
Individuals	127,247	11%	48,788	5%	73,237	249,272
Small and medium enterprises	49,302	11%	4,813	5%	5,988	60,103
Corporations	48,975	40%	884	20%	9,429	59,288
Sovereigns, central banks and PSE	16,736	40%	-	-	5,519	22,255
Pension funds	49,554	100%	-	-	16,796	66,350
Domestic financial entities	26,253	100%	-	-	13,363	39,616
Foreign financial entities	2,773	100%	-	-	-	2,773
Total	320,840		54,485		124,332	499,657
31.12.2018						
Individuals	126,196	11%	51,232	5%	69,000	246,428
Small and medium enterprises	48,961	11%	4,836	5%	5,417	59,214
Corporations	48,033	40%	852	20%	7,605	56,490
Sovereigns, central banks and PSE	14,052	40%	-	-	5,067	19,119
Pension funds	45,671	100%	-	-	10,038	55,709
Domestic financial entities	22,494	100%	-	-	12,630	35,124
Foreign financial entities	3,187	100%	-	-	-	3,187
Total	308,594		56,920		109,757	475,271

* Here term deposits refer to deposits with maturities greater than 30 days.

Amounts are in ISK millions

Notes to the Condensed Consolidated Interim Financial Statements

45. Capital management

Capital adequacy

The focus of capital management at the Group is to normalize the capital structure in the medium term and consequently maintain the Group's capitalization comfortably above the regulatory requirement, including capital buffers and Pillar 2 requirements.

The Group's capital ratios are calculated in accordance with Act No. 161/2002 on Financial Undertakings and Regulation No. 233/2017 on prudential requirements. Iceland has adopted the EU Capital Requirements Directive and Regulation (CRD IV / CRR), but has temporarily excluded Article 501 on capital requirements relief for small and medium enterprises. The Group uses the standardized approach to calculate capital requirements for credit risk, credit valuation adjustment, market risk and operational risk.

The Group's consolidated situation as stipulated in CRR is the Group's accounting consolidation excluding insurance subsidiaries. The capital position and solvency requirements of Vörður tryggingar hf. should be viewed independently from capital adequacy for the Group's consolidated situation.

Valitor holding hf. has been classified as disposal group held for sale and discontinued operations in these Consolidated Financial Statements. This does not affect the Group's capital adequacy calculations. For disclosure, assuming a cash sale of the subsidiary at book value, the Group's capital adequacy ratio would increase from 22.3% to 24.3%. The sale of Valitor would result in reduction in the Group's regulatory own funds adjustments, with positive effect on capital adequacy.

Own funds	31.3.2019	31.12.2018
Total equity	193,054	200,859
Deductions related to the consolidated situation	(8,746)	(8,986)
Non-controlling interest not eligible for inclusion in CET 1 capital	(130)	(130)
Common Equity Tier 1 capital before regulatory adjustments	184,178	191,743
Intangible assets	(13,236)	(12,152)
Tax assets	(490)	(191)
Indirect holdings of own CET1 instruments	(190)	(190)
Cash flow hedges	(1,696)	(1,221)
Additional value adjustments	(136)	(126)
Foreseeable dividend *	(509)	(9,069)
Common equity Tier 1 capital	167,921	168,794
Non-controlling interest not eligible for inclusion in CET 1 capital	130	130
Tier 1 capital	168,051	168,924
Subordinated liabilities	7,283	6,532
Tier 2 capital	7,283	6,532
Total own funds	175,334	175,456
Risk-weighted assets		
Credit risk, loans	626,603	639,788
Credit risk, securities and other	52,167	50,112
Counterparty credit risk	4,126	4,405
Market risk due to currency imbalance	2,385	4,280
Market risk other	13,744	8,928
Credit valuation adjustment	1,893	2,228
Operational risk	86,957	86,957
Total risk-weighted assets	787,875	796,698
Capital ratios		
CET 1 ratio	21.3%	21.2%
Tier 1 ratio	21.3%	21.2%
Capital adequacy ratio	22.3%	22.0%
CET1 ratio, based on reviewed retained earnings at 31 December 2018	21.2%	
Tier 1 ratio, based on reviewed retained earnings at 31 December 2018	21.3%	
Capital adequacy ratio, based on reviewed retained earnings at 31 December 2018	22.2%	

* At 31 March 2019, the foreseeable dividend is 50% of the accumulated net earnings in 2019 which is in accordance with the Bank's dividend policy.

Capital ratios of the parent company	31.3.2019	31.12.2018
CET 1 ratio	23.5%	23.5%
Tier 1 ratio	23.5%	23.5%
Capital adequacy ratio	24.5%	24.3%

Amounts are in ISK millions

45. Capital management, continued

The following table outlines the implementation of the capital buffer requirements in accordance with the Financial Undertakings Act, as prescribed by the Financial Stability Council (FSC) and approved by the FME.

Capital buffer requirement, % of RWA	Current	15.5.2019	1.2.2020
Capital conservation buffer	2.50%	2.50%	2.50%
Capital buffer for systematically important institutions	2.00%	2.00%	2.00%
Systemic risk buffer *	3.00%	3.00%	3.00%
Countercyclical capital buffer *	1.25%	1.75%	2.00%
Combined capital buffer requirement	8.75%	9.25%	9.50%

The Bank carries out an ongoing process, the Internal Capital Adequacy Assessment Process (ICAAP), with the aim to ensure that the Group has in place sufficient risk management processes and systems to identify, manage and measure the Group's total risk exposure. The ICAAP is aimed at identifying and measuring the Group's risk across all risk types and ensure that the Group has sufficient capital in accordance with its risk profile. The FME supervises the Group, receives the Group's internal estimation on the capital adequacy and sets capital requirements for the Group as a whole following the Supervisory Review and Evaluation Process (SREP). The Group's own funds exceeds the FME's SREP requirements.

The Bank's Pillar 2R capital add-on, which is the result of the ICAAP/SREP, may comprise 56.25% CET1 capital, 18.75% AT1 capital and 25% Tier 2 capital.

Capital requirement, % of RWA, current

31.3.2019	CET 1	Tier 1	Total
Pillar 1 capital requirement	4.5%	6.0%	8.0%
Pillar 2R capital requirement **	1.6%	2.2%	2.9%
Combined buffer requirement *	8.5%	8.5%	8.5%
Regulatory capital requirement	14.6%	16.6%	19.4%
Available capital	21.3%	21.3%	22.3%

Capital requirement, % of RWA, 15.5.2019

Pillar 1 capital requirement	4.5%	6.0%	8.0%
Pillar 2R capital requirement **	1.6%	2.2%	2.9%
Combined buffer requirement *	8.9%	8.9%	8.9%
Regulatory capital requirement	15.0%	17.1%	19.8%
Available capital	21.3%	21.3%	22.3%

* The effective capital buffers for systemic risk and countercyclical effects are determined by calculating the weighted average of the corresponding buffer levels of each country (if recognized by the FME), the weights being the total risk weighted exposures for credit risk against counterparties residing in those countries.

** The SREP result based on the Group's financial statement at 31.12.2017. The Pillar 2 requirement is 2.9% of risk-weighted assets based on the Group's prudential consolidation under CRR, which excludes Vörður tryggingar hf.

Leverage ratio

The leverage ratio is seen as a complementary measure to the risk-based capital ratios. The ratio is calculated on the basis of the Group's consolidated situation as per the CRR, which excludes the Group's insurance subsidiaries. The minimum leverage ratio requirement is 3% as stated in Act No. 161/2002 on Financial Undertakings.

	31.3.2019	31.12.2018
On-balance sheet exposures	1,169,764	1,106,368
Derivative exposures	7,282	8,239
Securities financing transaction exposures	8,494	8,194
Off-balance sheet exposures	61,185	68,316
Total exposure	1,246,725	1,191,117
Tier 1 capital	168,051	168,924
Leverage ratio	13.5%	14.2%

Amounts are in ISK millions

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