Íslandsbanki

Condensed Consolidated Interim Financial Statements

Third quarter 2020

Unaudited

Contents

Íslandsbanki Factsheet 3Q20

Íslandsbanki

Our profile

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

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

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

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

Our bank

12 branches

744 Number of FTEs at Íslandsbanki at period end

Digitally connected banking companion

Market share*

30% individuals

35% SMEs

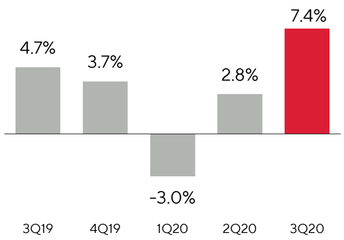
34% large companies

Credit rating

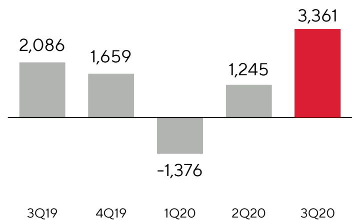
S&P Global Ratings

BBB/A-2
Stable outlook

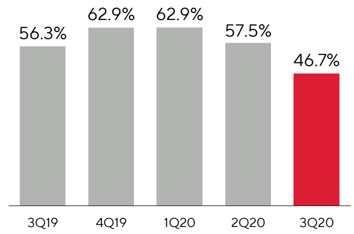
Return on equity



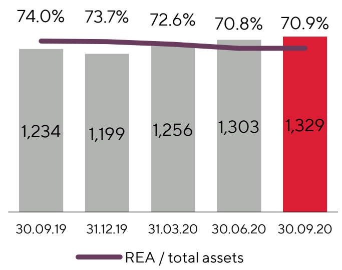
Profit (loss) after tax
(ISKm)



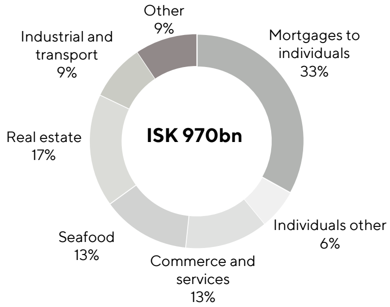
Cost / income ratio



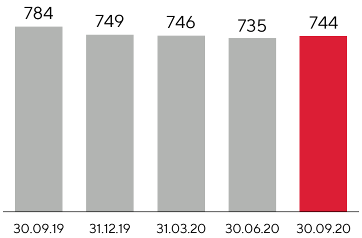
Total assets
(ISKbn)



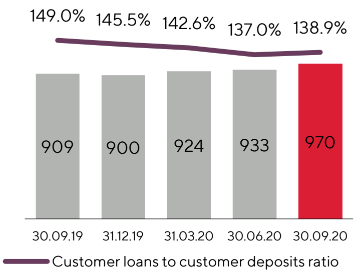
Loans to customers
(Sector split as of 30.09.20)



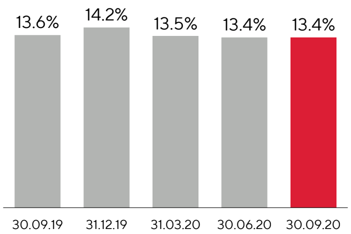
Number of FTEs at Íslandsbanki
(Excluding seasonal employees)



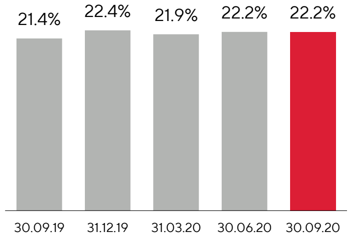
Loans to customers
(ISKbn)



Leverage ratio



Total capital ratio



*Based on Gallup survey regarding primary bank.

Directors' Report

These are the condensed consolidated interim financial statements for the period 1 January to 30 September 2020 ("the interim financial statements") of Íslandsbanki hf. ("the Bank" or "Íslandsbanki") and its subsidiaries (together referred to as "the Group").

Operations in the reporting period

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

The Group reported a profit from its operations for the reporting period amounting to ISK 3,230 million. At the end of the reporting period the Group employed 778 full-time members of staff and total assets amounted to ISK 1.3 trillion.

The Bank concluded the sale of its shares in Borgun hf. on 7 July 2020 and the sale resulted in a net profit of ISK 427 million. As the equity stake in Borgun hf. was accounted for as an asset held for sale, the impact on the income statement is shown in a single line as discontinued operations and comparative figures in the interim financial statements have been restated. Borgun will continue to provide the Bank with issuing services for credit cards issued by the Bank.

As for financial institutions worldwide, the COVID-19 pandemic had a substantial impact on the Group's operations in the reporting period. Although the Group managed to return to profitability, return on equity is well below targets. Considerable uncertainty still remains and the recovery is quite reliant on travel restrictions being eased before the summer of 2021. The Bank continues to categorise almost all of its exposures to the tourism industry in Stage 2 under IFRS 9 and 14% of the loan book is subject to forbearance due to COVID-19. The ratio of non-performing loans has however come down to 3.3% from 3.6% at the end of the second quarter as a large customer became performing after an injection of capital. The Bank had a negative impairment charge of ISK 7.0 billion year-to-date. In addition to that, the Bank experienced losses in its net financial income of ISK 2.2 billion.

Net interest income rose by 2.4% between years, where the lower interest environment is starting to have a material impact on earnings through lower deposit margins and returns on the Bank's liquidity portfolio, resulting in a drop of 10 basis points in net interest margin. Net fee and commission income was down by 3.9%, where a strong third quarter partially offset low activity in the first half. Salaries and related expenses were down by 8.3% between years as a result of FTE reductions, while other operating expenses decreased by 6.7% as a result of cost reduction measures and COVID-19, which impacts the operations in many ways, e.g. through reduced travel.

The Group's loan book grew by 8.4% from year-end 2019, which can be contributed to a strong demand for mortgages and the depreciation of the Icelandic króna. Customer deposits increased by 12.8% from year-end 2019 with the largest increase in Corporate and Investment Banking, and Business Banking. Bond issuance was modest in the first nine months of the year and mostly relating to regular covered bond auctions. The Bank did, however, buy back some of its outstanding bonds as a part of its balance sheet management. The Bank is very well capitalised, with a total capital ratio of 22.2% at the end of the period, compared to a 17% regulatory requirement, which was lowered as the counter-cyclical buffer was reduced from 2.0% to zero as a result of the economic slowdown.

The COVID-19 pandemic continues to impact the operations of the Bank as most of the headquarters' employees are currently working from home and customer access to branches is restricted. The Bank continues focus on supporting its customers in areas of the economy that are worst affected.

Outlook

After a period of normalisation over the summer, the Icelandic economy has been hit by a second wave of COVID-19 in the autumn much as the rest of Europe. Border measures were significantly tightened in late August, and domestic measures became more stringent over the following weeks. As a result, tourist visits to Iceland have declined significantly and some domestic services have been on a hiatus for much of October. However, domestic demand seems to be holding up better than expected as households divert their discretionary consumption towards domestic goods and services while the residential housing market is relatively buoyant, thanks in part to a more effective transmission of monetary easing through to mortgage rates than has historically been the case in Iceland.

The size of the COVID-19 shock to the relatively large tourist sector means that a rather deep economic contraction is inevitable in 2020 with GDP expected to fall by about 8.6% and around 2/3 of the GDP fall due to declining exports and 1/3 caused by a fall in domestic demand. However, countercyclical economic policy measures have already eased the impact somewhat with the Central Bank's policy rate at an all-time low and the Government's new five-year fiscal plan assuming an accumulated deficit of around 24% of GDP in 2020-2022. The duration of the economic setback will hinge on how rapidly travel conditions normalise and economic activity resumes on a global scale. Assuming fading impact from COVID-19 over the coming months, there is a good probability of a return to healthy GDP growth in the latter half of 2021.

The Bank's financial position remains strong and is well placed to support its customers in these turbulent times. Profitability will be below target in 2020 and the Bank will strive to get back on track to reach its profitability targets from 2021 onwards.

Directors' Report

Statement by the Board of Directors and the CEO

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

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

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

Kópavogur, 28 October 2020

Board of Directors:

Hallgrímur Snorrason, Chairman

Heiðrún Jónsdóttir, Vice-Chairman

Anna Þórðardóttir

Árni Stefánsson

Flóki Halldórsson

Frosti Ólafsson

Guðrún Þorgeirsdóttir

Chief Executive Officer:

Birna Einarsdóttir

Consolidated Interim Income Statement

	Notes	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Interest income*		42,418	47,063	13,820	14,940
Interest expense		(17,305)	(22,532)	(5,515)	(6,750)
Net interest income	7	25,113	24,531	8,305	8,190
Fee and commission income		9,178	8,664	3,793	2,797
Fee and commission expense		(1,518)	(710)	(931)	(248)
Net fee and commission income	8	7,660	7,954	2,862	2,549
Net financial income (expense)	9	(2,174)	20	(255)	(602)
Net foreign exchange gain	10	364	23	101	159
Other operating income	11	134	1,205	44	37
Other net operating income		(1,676)	1,248	(110)	(406)
Total operating income		31,097	33,733	11,057	10,333
Salaries and related expenses	12	(9,536)	(10,395)	(2,842)	(3,242)
Other operating expenses	13	(7,137)	(7,646)	(2,268)	(2,366)
Contribution to the Depositors' and Investors' Guarantee Fund		(525)	(720)	(50)	(210)
Bank tax		(1,174)	(2,714)	(416)	(900)
Total operating expenses		(18,372)	(21,475)	(5,576)	(6,718)
Profit before net impairment on financial assets		12,725	12,258	5,481	3,615
Net impairment on financial assets	14	(6,987)	(2,017)	(1,058)	(208)
Profit before tax		5,738	10,241	4,423	3,407
Income tax expense	15	(2,238)	(3,250)	(1,350)	(1,328)
Profit for the period from continuing operations		3,500	6,991	3,073	2,079
Discontinued operations, net of income tax	16	(270)	(196)	288	7
Profit for the period		3,230	6,795	3,361	2,086
Profit attributable to:					
Shareholders of Íslandsbanki hf.		3,533	7,072	3,362	2,153
Non-controlling interests		(303)	(277)	(1)	(67)
Profit for the period		3,230	6,795	3,361	2,086
Earnings per share from continuing operations					
Basic and diluted earnings per share attributable to the shareholders of Íslandsbanki hf.	17	0.38	0.73	0.31	0.21

*Of which interest income amounting to ISK 40,762 million (2019: ISK 45,007 million) is calculated using the effective interest method.

Before its sale on 7 July 2020, the subsidiary Borgun hf. was classified as disposal group held for sale and as discontinued operations, accordingly the comparative figures have been restated (see Note 4).

The notes on pages 11 to 58 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Comprehensive Income

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Profit for the period	3,230	6,795	3,361	2,086
Items that will not be reclassified to profit or loss				
Changes in fair value of financial assets, net of tax	(798)	978	115	85
Changes in fair value of financial liabilities, net of tax	586	(802)	(233)	29
Other comprehensive income (expense) for the period, net of tax	(212)	176	(118)	114
Total comprehensive income for the period	3,018	6,971	3,243	2,200

The notes on pages 11 to 58 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Financial Position

	Notes	30.9.2020	31.12.2019
Assets			
Cash and balances with Central Bank	22	95,022	146,638
Loans to credit institutions	23	61,898	54,376
Bonds and debt instruments	18	149,426	52,870
Derivatives	24	3,731	5,621
Loans to customers	25	970,309	899,632
Shares and equity instruments	18	14,657	18,426
Investments in associates		750	746
Property and equipment	27	7,409	9,168
Intangible assets		3,554	4,330
Other assets	28	17,159	6,608
Non-current assets and disposal groups held for sale	29	4,809	1,075
Total Assets		1,328,724	1,199,490
Liabilities			
Deposits from Central Bank and credit institutions	30	36,438	30,925
Deposits from customers	31	698,610	618,313
Derivative instruments and short positions	24	8,406	6,219
Debt issued and other borrowed funds	33	324,752	306,381
Subordinated loans	34	26,798	22,674
Tax liabilities		7,137	7,853
Other liabilities	36	44,074	27,063
Total Liabilities		1,146,215	1,019,428
Equity			
Share capital		10,000	10,000
Share premium		55,000	55,000
Reserves		7,258	7,065
Retained earnings		108,383	105,569
Total Shareholders' Equity		180,641	177,634
Non-controlling interests		1,868	2,428
Total Equity		182,509	180,062
Total Liabilities and Equity		1,328,724	1,199,490

The notes on pages 11 to 58 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Changes in Equity

	Share capital	Share premium	Statutory reserve	Restricted reserves	Fair value reserve	Liability credit reserve	Translation reserve	Retained earnings	Total shareholders' equity	Non-controlling interests	Total equity
Equity as at 1.1.2020	10,000	55,000	2,500	3,525	1,432	(392)	-	105,569	177,634	2,428	180,062
Profit (loss) for the period								3,533	3,533	(303)	3,230
Net change in fair value of financial assets					(372)			(212)	(584)	(214)	(798)
Net change in fair value of financial liabilities						631		(45)	586		586
Restricted due to capitalised development costs				(218)				218	-		-
Restricted due to fair value changes				170				(170)	-		-
Restricted due to associates				14				(14)	-		-
Translation difference							(32)	(79)	(111)	(1)	(112)
Other changes due to IFRS 15								(115)	(115)		(115)
Changes in non-controlling interests								(302)	(302)	(42)	(344)
Equity as at 30.9.2020	10,000	55,000	2,500	3,491	1,060	239	(32)	108,383	180,641	1,868	182,509
Equity as at 1.1.2019	10,000	55,000	2,500	3,750	625	(376)	-	102,496	173,995	2,318	176,313
Profit (loss) for the period								7,072	7,072	(277)	6,795
Dividends paid								(5,300)	(5,300)		(5,300)
Net change in fair value of financial assets					621				621	357	978
Net change in fair value of financial liabilities						(355)		(447)	(802)		(802)
Restricted due to capitalised development costs				(218)				218	-		-
Restricted due to fair value changes				303				(303)	-		-
Restricted due to subsidiaries and associates				(49)				49	-		-
Equity as at 30.9.2019	10,000	55,000	2,500	3,786	1,246	(731)	-	103,785	175,586	2,398	177,984

Authorised share capital of the Bank is 10,000 million ordinary shares of ISK 1 each. At 30.9.2020 paid up share capital totalled ISK 65,000 million which is the total stated share capital of the Bank. The Bank has one class of ordinary shares which carry no right to fixed income. The Annual General Meeting ("AGM") for the operating year 2019 was held on 19 March 2020. At the AGM shareholders approved that a dividend to shareholders for the operating year 2019 shall not be paid in light of uncertainties due to unprecedented circumstances in the financial markets. It was also approved that the Board may convene a special shareholder meeting later in the year where a proposal regarding payment of dividends of profit for previous fiscal years could be suggested. However, it is highly unlikely that such a proposal will be made, based on the current economic environment.

The notes on pages 11 to 58 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Cash Flows

	Notes	2020 1.1-30.9	2019 1.1-30.9
Profit for the period		3,230	6,795
Non-cash items included in profit for the period*		22,083	17,955
Changes in operating assets and liabilities*		(42,894)	(42,657)
Dividends received		30	32
Income tax and bank tax paid		(4,383)	(2,884)
Net cash used in operating activities		(21,934)	(20,759)
Net investment in subsidiaries		(2,486)	-
Proceeds from sales of property and equipment		24	23
Purchase of property and equipment		(492)	(352)
Purchase of intangible assets		(158)	(187)
Net cash used in investing activities		(3,112)	(516)
Proceeds from borrowings		15,255	108,701
Repayment of borrowings		(31,543)	(81,388)
Repayment of lease liabilities		(293)	(281)
Dividends paid		-	(5,300)
Net cash (used in) provided by financing activities		(16,581)	21,732
Net increase (decrease) in cash and cash equivalents		(41,627)	457
Effects of foreign exchange rate changes		224	(201)
Cash and cash equivalents at the beginning of the year		152,481	143,203
Cash and cash equivalents at the end of the period		111,078	143,459
Reconciliation of cash and cash equivalents			
Cash on hand	22	3,965	4,007
Cash balances with Central Bank	22	91,057	125,108
Bank accounts	23	25,554	29,411
Mandatory reserve and special restricted balances with Central Bank	22	(9,498)	(15,067)
Cash and cash equivalents at the end of the period		111,078	143,459

*For further breakdown see the following page.

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

The Group presents a statement of cash flows that includes an analysis of all cash flows in total, including both continuing and discontinued operations.

Interest received from 1 January to 30 September 2020 amounted to ISK 26,263 million (2019: ISK 45,089 million) and interest paid in the same period 2020 amounted to ISK 13,994 million (2019: ISK 18,628 million). Interest is defined as having been paid when it has been deposited into the customer account and is available for the customer's disposal.

The notes on pages 11 to 58 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Consolidated Interim Statement of Cash Flows

	2020 1.1-30.9	2019 1.1-30.9
Depreciation, amortisation and write-offs	1,380	1,246
Share of profit of associates	(20)	(5)
Accrued interest and fair value changes on debt issued and subordinated loans	9,857	8,680
Net impairment on financial assets	6,857	2,220
Foreign exchange gain	(300)	(46)
Net gain from sales of property and equipment	(427)	(1)
Unrealised fair value loss recognised in profit or loss	1,392	40
Discontinued operations, net of income tax	(131)	30
Bank tax	1,174	2,714
Income tax	2,238	3,071
Other changes	63	6
Non-cash items included in profit for the period	22,083	17,955
Mandatory reserve and special restricted balances with Central Bank	5,781	2,045
Loans to credit institutions	5,099	(18,677)
Bonds and debt instruments	(93,823)	(3,548)
Loans to customers	(53,510)	(60,476)
Shares and equity instruments	(681)	(5,089)
Other assets	(13,769)	(6,069)
Non-current assets held for sale	(857)	(268)
Deposits from Central Bank and credit institutions	4,061	16,172
Deposits from customers	66,221	29,000
Derivative instruments and short positions	7,845	(3,652)
Other liabilities	30,739	7,905
Changes in operating assets and liabilities	(42,894)	(42,657)

Non-cash transactions 2020

During the period Íslandsbanki sold its 63.5% stake in Borgun hf. ISK 726 million of the sale price is due in 2021. Prior to the sale, shares in Borgun-VS ehf. a company holding series C preferred shares in Visa Inc., which were not part of the sale of Borgun, were transferred to the old owners of Borgun.

During the period the Bank sold an office building for the price of ISK 100 million with ISK 85 million outstanding at the end of the period.

Non-cash transactions 2019

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

The recognition of right-of-use assets amounting to ISK 4,505 million and the same amount in lease liabilities following the adoption of IFRS 16 - Leases had no cash flow effect.

The notes on pages 11 to 58 are an integral part of these Condensed Consolidated Interim Financial Statements.

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

Notes to the Condensed Consolidated Interim Financial Statements

1. Corporate information

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

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

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

The interim financial statements were approved and authorised for issue by the Board of Directors and the CEO of Íslandsbanki hf. on 28 October 2020.

2. Basis of preparation

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

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

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

Before its sale on 7 July 2020, the subsidiary Borgun hf. was classified as non-current assets and disposal groups held for sale. Accordingly the comparative figures in the consolidated interim income statement for the third quarter of 2019 have been restated (see Note 4).

The interim financial statements are presented in Icelandic króna (ISK), which is the functional currency of Íslandsbanki hf. All amounts presented in ISK have been rounded to the nearest million, except when otherwise indicated. At 30 September 2020 the exchange rate of the ISK against the USD was 138.54 and 162.20 for the EUR (year-end 2019: USD 121.10 and EUR 135.83).

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

Significant accounting estimates and judgements

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

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

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

Impairment of financial assets, changes from year-end 2019

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

At the end of the third quarter of 2020, the following changes have been made.

The Group's Chief Economist has provided a new macroeconomic forecast on 29 September 2020 which takes into account the effects of the COVID-19 pandemic.

2. Cont'd

Change in economic indicators %	2019	2020	2021	2022	2023	2024
Economic growth	1.9	(8.6)	3.1	4.7	2.5	2.1
Housing prices in Iceland	3.4	2.6	1.5	3.0	4.0	4.0
Purchasing power	1.8	3.0	1.1	2.1	2.1	1.6
ISK exchange rate index	8.5	11.2	3.1	(1.8)	(2.8)	(1.5)
Policy rate, Central Bank of Iceland	3.9	1.5	1.2	2.0	3.0	3.5
Inflation	3.0	2.7	2.7	1.9	1.9	2.4
Capital formation	(6.6)	(10.2)	1.5	6.7	1.2	3.5
thereof capital formation in industry	(18.1)	(16.0)	(0.2)	8.7	3.5	3.0

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

The Group's model to calculate PD scaling factors was applied to these economic scenarios and the resulting scaling factors were then reviewed by the All Risk Committee with respect to all of the economic indicators and any other relevant information available. The All Risk Committee determined that it was appropriate to adjust the weights of the scenarios, generally the scenarios are weighted 25%-50%-25% (good, base, bad) but it was determined appropriate to set the weights at 15%-55%-30%, as this would best represent the probability-weighted average over all possible scenarios.

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

As unemployment has increased considerably it was decided in the third quarter to apply an additional overlay factor to loans to individuals in order to capture the potential effect of the increase.

The common risk factor in tourism was found to apply to loans to customers with a net carrying amount of ISK 98 billion and the cumulative effect of the stage transfer and credit loss overlay for the first nine months amounting to ISK 5.0 billion. Additionally, changes in impairment for a few specific customers has resulted in an additional credit loss allowance of ISK 970 million. Other changes in credit loss allowance were smaller (see Note 14).

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

3. Changes to accounting policies

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

Interest Rate Benchmark Reform

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

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

Notes to the Condensed Consolidated Interim Financial Statements

4. Investments in subsidiaries

		30.9.2020	31.12.2019
Íslandssjóðir hf., an investment fund management company, Hagasmári 3, 201 Kópavogur	Iceland	100%	100%
Hringur-eignarhaldsfélag ehf., a holding company, Dalshraun 3, 220 Hafnarfjörður	Iceland	100%	100%
Allianz Ísland hf., an insurance agent, Dalshraun 3, 220 Hafnarfjörður	Iceland	100%	100%
Borgun hf., a payment acquirer and issuing processor, Ármúli 30, 108 Reykjavík	Iceland	-	63.5%

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

Borgun hf.

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

On 11 March 2020 Íslandsbanki signed an agreement to sell its 63.5% stake in Borgun hf. to Salt Pay Co Ltd. but this transaction was subject to Financial Supervisory Authority ("FME") approval of the purchaser's acquisition of a qualifying holding. On 7 July 2020 the Bank concluded the sale. The net loss of Borgun hf. during the period, 1 January until the selling date 7 July 2020, amounting to ISK 828 million and net profit from the sale amounting to ISK 427 million is included in the line item "Discontinued operations, net of income tax" in the Consolidated Interim Income Statement.

Before the sale, in the first quarter of 2020, Borgun hf. was classified as disposal group held for sale, in accordance with IFRS 5 - Non-current assets and disposal groups held for sale, resulting in a change in the presentation. As a result the comparative figures in the Consolidated Interim Income Statement for the third quarter of 2019 have been restated and Borgun hf. is no longer presented separately in the Operating segments note.

Restated Consolidated Interim Income Statement for the third quarter of 2019	Published accounts	Borgun hf. reclassified	Restated accounts
Interest income	47,733	(670)	47,063
Interest expense	(22,543)	11	(22,532)
Net interest income	25,190	(659)	24,531
Fee and commission income	15,532	(6,868)	8,664
Fee and commission expense	(5,819)	5,109	(710)
Net fee and commission income	9,713	(1,759)	7,954
Net financial income	23	(3)	20
Net foreign exchange loss	46	(23)	23
Other operating income	1,217	(12)	1,205
Other net operating income	1,286	(38)	1,248
Total operating income	36,189	(2,456)	33,733
Salaries and related expenses	(12,083)	1,688	(10,395)
Other operating expenses	(8,698)	1,052	(7,646)
Contribution to the Depositors' and Investors' Guarantee Fund	(720)	-	(720)
Bank tax	(2,714)	-	(2,714)
Total operating expenses	(24,215)	2,740	(21,475)
Profit before net impairment on financial assets	11,974	284	12,258
Net impairment on financial assets	(2,078)	61	(2,017)
Profit before tax	9,896	345	10,241
Income tax expense	(3,071)	(179)	(3,250)
Profit for the period from continuing operations	6,825	166	6,991
Discontinued operations, net of income tax	(30)	(166)	(196)
Profit for the period	6,795	-	6,795

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

5. Operating segments

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

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

The Group comprises the following operating segments:

Personal Banking

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

Business Banking

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

Corporate & Investment Banking

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

Treasury and Proprietary Trading

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

Cost centres

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

Subsidiaries, eliminations and adjustments

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

Before its sale on 7 July 2020, the subsidiary Borgun hf. was classified as non-current assets and disposal groups held for sale, accordingly the comparative figures in this disclosure have been restated.

Assets and liabilities of subsidiaries, that are classified as non-current assets and disposal groups held for sale, are included in the column “Other subsidiaries" and all inter-company eliminations for those subsidiaries are included in the column “Eliminations & adjustments".

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

5. Cont'd

1 January to 30 September 2020	Personal Banking	Business Banking	Corporate & Investment Banking	Treasury & Proprietary Trading	Cost centres	The Bank total	Subsidiaries, eliminations & adjustments	The Group total
Net interest income	8,021	7,913	6,465	2,847	(166)	25,080	33	25,113
Net fee and commission income	2,231	1,484	2,939	(272)	5	6,387	1,273	7,660
Other net operating income	305	48	813	(2,079)	215	(698)	(978)	(1,676)
Total operating income	10,557	9,445	10,217	496	54	30,769	328	31,097
Salaries and related expenses	(1,793)	(1,463)	(1,161)	(211)	(4,348)	(8,976)	(560)	(9,536)
Other operating expenses	(1,937)	(888)	(640)	(217)	(3,110)	(6,792)	(345)	(7,137)
Contribution to the Depositors' and Investors' Guarantee Fund	(361)	(132)	(31)	(1)	-	(525)	-	(525)
Bank tax	(403)	(260)	(409)	(90)	(12)	(1,174)	-	(1,174)
Net impairment on financial assets	(479)	(4,571)	(1,959)	22	-	(6,987)	-	(6,987)
Cost allocation	(3,407)	(2,089)	(2,190)	262	7,424	-	-	-
Profit (loss) before tax	2,177	42	3,827	261	8	6,315	(577)	5,738
Income tax expense	(671)	(79)	(1,101)	(306)	(5)	(2,162)	(76)	(2,238)
Profit (loss) for the period from continuing operations	1,506	(37)	2,726	(45)	3	4,153	(653)	3,500
Net segment revenue from external customers	15,421	11,218	15,260	(11,296)	166	30,769	328	31,097
Net segment revenue from other segments	(4,864)	(1,773)	(5,043)	11,792	(112)	-	-	-
Fee and commission income	3,500	1,507	3,002	(79)	6	7,936	1,242	9,178
Depreciation, amortisation and write-offs	(261)	(138)	(14)	-	(861)	(1,274)	(6)	(1,280)
At 30 September 2020								
Loans to customers	362,175	236,530	371,494	110	-	970,309	-	970,309
Other assets	8,172	2,231	4,347	331,439	11,353	357,542	873	358,415
Total segment assets	370,347	238,761	375,841	331,549	11,353	1,327,851	873	1,328,724
Deposits from customers	309,836	196,849	146,909	47,678	-	701,272	(2,662)	698,610
Other liabilities	4,415	2,502	8,121	425,805	5,687	446,530	1,075	447,605
Total segment liabilities	314,251	199,351	155,030	473,483	5,687	1,147,802	(1,587)	1,146,215
Allocated equity	30,692	38,835	63,690	45,914	918	180,049	2,460	182,509
Risk exposure amount	213,292	241,386	408,780	61,621	6,227	931,306	11,033	942,339

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

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

5. Cont'd

1 January to 30 September 2019	Personal Banking	Business Banking	Corporate & Investment Banking	Treasury & Proprietary Trading	Cost centres	The Bank total	Subsidiaries, eliminations & adjustments	The Group total
Net interest income	7,876	8,140	6,271	2,337	(171)	24,453	78	24,531
Net fee and commission income	3,361	1,213	2,641	(137)	6	7,084	870	7,954
Other net operating income	-	12	349	229	1,308	1,898	(651)	1,248
Total operating income	11,237	9,365	9,261	2,429	1,143	33,435	297	33,733
Salaries and related expenses	(2,041)	(1,483)	(1,300)	(187)	(4,845)	(9,856)	(539)	(10,395)
Other operating expenses	(1,650)	(824)	(465)	(203)	(4,146)	(7,288)	(358)	(7,646)
Contribution to the Depositors' and Investors' Guarantee Fund	(404)	(245)	(71)	-	-	(720)	-	(720)
Bank tax	(357)	(258)	(375)	(1,711)	(13)	(2,714)	-	(2,714)
Net impairment on financial assets	(425)	(689)	(748)	(156)	-	(2,018)	1	(2,017)
Cost allocation	(3,906)	(2,162)	(2,172)	233	8,007	-	-	-
Profit (loss) before tax	2,454	3,704	4,130	405	146	10,839	(599)	10,241
Income tax expense	(731)	(1,030)	(1,171)	(151)	(41)	(3,124)	(126)	(3,250)
Profit (loss) for the period from continuing operations	1,723	2,674	2,959	254	105	7,715	(725)	6,991
Net segment revenue from external customers	13,332	10,810	14,229	(6,194)	1,258	33,435	297	33,733
Net segment revenue from other segments	(2,095)	(1,445)	(4,968)	8,623	(115)	-	-	-
Fee and commission income	4,520	1,226	2,673	98	6	8,523	140	8,664
Depreciation, amortisation and write-offs	(164)	(88)	(16)	-	(812)	(1,080)	(5)	(1,085)
At 30 September 2019								
Loans to customers	325,014	234,206	344,928	540	-	904,688	4,487	909,175
Other assets	2,997	3,229	276	284,816	11,643	302,961	21,719	324,680
Total segment assets	328,011	237,435	345,204	285,356	11,643	1,207,649	26,206	1,233,855
Deposits from customers	279,252	175,357	104,696	54,294	-	613,599	(3,318)	610,281
Other liabilities	1,037	2,043	2,218	412,552	5,956	423,806	21,784	445,590
Total segment liabilities	280,289	177,400	106,914	466,846	5,956	1,037,405	18,466	1,055,871
Allocated equity	28,907	39,312	60,614	40,202	1,209	170,244	7,740	177,984
Risk exposure amount	188,335	246,964	373,528	76,055	7,429	892,311	20,532	912,843

Amounts are in ISK million

5. Cont'd

Subsidiaries, eliminations & adjustments

1 January to 30 September 2020	Íslands-sjóðir hf.	Allianz Ísland hf.	Other subsidiaries	Eliminations & adjustments	Total
Net interest income	11	10	14	(2)	33
Net fee and commission income	881	514	(23)	(99)	1,273
Other net operating income	41	12	5	(1,036)	(978)
Total operating income	933	536	(4)	(1,137)	328
Salaries and related expenses	(419)	(141)	-	-	(560)
Other operating expenses	(141)	(310)	(1)	107	(345)
Profit (loss) before tax	373	85	(5)	(1,030)	(577)
Income tax expense	(76)	(17)	-	17	(76)
Profit (loss) for the period from cont. operations	297	68	(5)	(1,013)	(653)
Net segment revenue from external customers	1,144	425	-	(1,241)	328
Net segment revenue from other segments	(211)	111	(4)	104	-
Fee and commission income	1,237	514	-	(509)	1,242
Depreciation, amortisation and write-offs	-	-	-	(6)	(6)
At 30 September 2020					
Total assets	2,101	1,406	8,607	(11,241)	873
Total liabilities	307	633	335	(2,862)	(1,587)
Total equity	1,794	773	8,272	(8,379)	2,460

1 January to 30 September 2019	Íslands-sjóðir hf.	Allianz Ísland hf.	Other subsidiaries	Eliminations & adjustments	Total
Net interest income	24	20	26	8	78
Net fee and commission income	805	696	(23)	(608)	870
Other net operating income	109	-	(3)	(757)	(651)
Total operating income	938	716	-	(1,357)	297
Salaries and related expenses	(401)	(138)	-	-	(539)
Other operating expenses	(131)	(330)	(1)	104	(358)
Net impairment on financial assets	-	-	-	1	1
Profit (loss) before tax	406	248	(1)	(1,252)	(599)
Income tax expense	(82)	(48)	-	4	(126)
Profit (loss) for the period from cont. operations	324	200	(1)	(1,248)	(725)
Net segment revenue from external customers	1,087	706	(16)	(1,480)	297
Net segment revenue from other segments	(149)	10	16	123	-
Fee and commission income	1,125	696	-	(1,681)	140
Depreciation, amortisation and write-offs	-	-	-	(5)	(5)
At 30 September 2019					
Total assets	2,579	1,090	35,307	(12,770)	26,206
Total liabilities	258	399	22,420	(4,611)	18,466
Total equity	2,321	691	12,887	(8,159)	7,740

Íslandsbanki hf. Condensed Consolidated Interim Financial Statements third quarter 2020 18 Amounts are in ISK million

6. Quarterly statements

	2020 Q3	2020 Q2	2020 Q1	2019 Q4	2019 Q3
Net interest income	8,305	8,228	8,580	8,291	8,190
Net fee and commission income	2,862	2,307	2,491	2,945	2,549
Net financial expense	(255)	(181)	(1,738)	(840)	(602)
Net foreign exchange gain	101	208	55	116	159
Other operating income	44	71	19	920	37
Salaries and related expenses	(2,842)	(3,447)	(3,247)	(3,624)	(3,242)
Other operating expenses	(2,268)	(2,424)	(2,445)	(2,823)	(2,366)
Contribution to the Depositors' and Investors' Guarantee Fund	(50)	(247)	(228)	(216)	(210)
Bank tax	(416)	(399)	(359)	(814)	(900)
Net impairment on financial assets	(1,058)	(2,439)	(3,490)	(1,463)	(208)
Profit (loss) before tax	4,423	1,677	(362)	2,492	3,407
Income tax expense	(1,350)	(119)	(769)	(659)	(1,328)
Profit (loss) for the period from continuing operations	3,073	1,558	(1,131)	1,833	2,079
Discontinued operations, net of income tax	288	(313)	(245)	(174)	7
Profit (loss) for the period	3,361	1,245	(1,376)	1,659	2,086

7. Net interest income

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Cash and balances with Central Bank	1,645	3,443	235	993
Loans at amortised cost	39,117	41,564	13,001	13,194
Financial assets mandatorily at fair value through profit or loss	1,653	2,024	583	743
Other assets	3	32	1	10
Total interest income	42,418	47,063	13,820	14,940
Deposits from Central Bank and credit institutions	(612)	(388)	(192)	(159)
Deposits from customers	(6,324)	(12,178)	(1,625)	(3,475)
Debt issued and other borrowed funds at fair value through profit or loss	(446)	(558)	(150)	(184)
Debt issued and other borrowed funds at amortised cost	(8,353)	(7,404)	(2,979)	(2,271)
Subordinated loans	(570)	(341)	(211)	(168)
Other interest expense*	(1,000)	(1,663)	(358)	(493)
Total interest expense	(17,305)	(22,532)	(5,515)	(6,750)
Net interest income	25,113	24,531	8,305	8,190

*Thereof is lease liabilities' interest expense amounting to ISK 65 million (2019: ISK 70 million).

Amounts are in ISK million

8. Net fee and commission income

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Asset management	1,746	1,635	576	512
Investment banking and brokerage	1,831	1,742	684	598
Payment processing	3,297	2,823	1,697	947
Loans and guarantees	1,324	1,121	514	367
Other fee and commission income	980	1,343	322	373
Total fee and commission income	9,178	8,664	3,793	2,797
Brokerage	(233)	(209)	(67)	(65)
Clearing and settlement	(1,285)	(482)	(864)	(174)
Other fee and commission expense	-	(19)	-	(9)
Total fee and commission expense	(1,518)	(710)	(931)	(248)
Net fee and commission income	7,660	7,954	2,862	2,549

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

9. Net financial income (expense)

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Net gain (loss) on financial assets and liabilities mandatorily at FVTPL	(1,688)	391	(140)	(486)
Net loss on financial liabilities designated as at FVTPL	(487)	(372)	(115)	(113)
Net gain (loss) on fair value hedges	1	1	-	(3)
Net financial income (expense)	(2,174)	20	(255)	(602)

10. Net foreign exchange gain

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Cash and balances with Central Bank	224	(201)	48	(198)
Financial assets mandatorily at fair value through profit or loss	8,464	(4,715)	2,628	(5,615)
Loans at amortised cost	36,681	6,320	7,230	(7,794)
Other assets	12	2	1	-
Net foreign exchange gain (loss) for assets	45,381	1,406	9,907	(13,607)
Deposits	(15,528)	(2,339)	(2,299)	2,795
Debt issued and other borrowed funds designated as at FVTPL	(9,671)	(1,334)	(2,573)	3,372
Debt issued and other borrowed funds at amortised cost	(15,712)	1,382	(3,982)	6,159
Subordinated loans	(4,106)	908	(952)	1,440
Net foreign exchange gain (loss) for liabilities	(45,017)	(1,383)	(9,806)	13,766
Net foreign exchange gain	364	23	101	159

Amounts are in ISK million

11. Other operating income

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Share of profit of associates, net of income tax	19	5	-	-
Legal dispute settlement	-	1,103	-	-
Legal fees	63	69	23	26
Rental income	30	30	10	11
Other net operating income	22	(2)	11	-
Other operating income	134	1,205	44	37

12. Salaries and related expenses

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Salaries	7,341	8,008	2,183	2,493
Contributions to pension funds	1,102	1,203	334	378
Social security charges and financial activities tax*	1,039	1,114	323	355
Other salary-related expenses	54	70	2	16
Salaries and related expenses	9,536	10,395	2,842	3,242

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

13. Other operating expenses

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Professional services	1,125	1,327	365	410
Software and IT expenses	3,301	3,489	1,071	1,090
Real estate and office equipment	413	418	138	124
Depreciation, amortisation and write-offs	1,280	1,085	394	362
Other administrative expenses	1,018	1,327	300	380
Other operating expenses	7,137	7,646	2,268	2,366

14. Net impairment on financial assets

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Expected credit loss, on-balance sheet items*	(6,812)	(2,027)	(1,069)	(265)
Expected credit loss, off-balance sheet items	(175)	16	11	57
Changes in provision due to court rulings	-	(6)	-	-
Net impairment on financial assets	(6,987)	(2,017)	(1,058)	(208)

*The main reasons for the additional expected credit loss allowance are: an increase related to the COVID-19 pandemic (ISK 5,000 million), an increase due to a less favourable economic environment (480 million) and an increased expected credit loss for a few customers (ISK 970 million). For further information see Note 2.

Amounts are in ISK million

15. Income tax expense

Recognised income tax is based on applicable tax laws. The income tax rate for legal entities in 2020 is 20% (2019: 20%). Special financial activities tax is calculated as 6% of taxable profits exceeding ISK 1 billion in accordance with the Act on Financial Activities Tax no. 165/2011. The effective income tax rate in the Group's income statement for the third quarter 2020 is 39.0% (2019: 31.7%).

	2020 1.1-30.9	2019 1.1-30.9
Current tax expense excluding discontinued operations	2,909	2,195
Special financial activities tax	776	555
Difference in prior year's calculated income tax	12	(1)
Changes in deferred tax assets and deferred tax liabilities	(1,459)	501
Income tax recognised in the income statement	2,238	3,250
Income tax recognised in other comprehensive income	(16)	(157)

	2020 1.1-30.9		2019 1.1-30.9	
Profit before tax	5,738		10,240	
20% income tax calculated on the profit for the period	1,148	20.0%	2,048	20.0%
Special financial activities tax	776	13.5%	555	5.4%
Expenses (income) not subject to tax	75	1.3%	(46)	(0.4%)
Non-deductible expenses	235	4.1%	547	5.3%
Other differences	4	0.1%	146	1.4%
Effective income tax expense	2,238	39.0%	3,250	31.7%

The Bank is taxed jointly with its subsidiary Íslandssjóðir hf.

16. Discontinued operations, net of income tax

	2020 1.1-30.9	2019 1.1-30.9	2020 1.7-30.9	2019 1.7-30.9
Net profit (loss) from foreclosed assets	(6)	(89)	30	(47)
Net profit (loss) from disposal groups held for sale	(705)	(115)	(167)	54
Net profit from sale of subsidiaries	427	-	427	-
Income tax expense	14	8	(2)	-
Discontinued operations, net of income tax	(270)	(196)	288	7

17. Earnings per share

	Discontinued operations			
	Excluded		Included	
	2020 1.1-30.9	2019 1.1-30.9	2020 1.1-30.9	2019 1.1-30.9
Profit attributable to shareholders of the Bank	3,803	7,268	3,533	7,072
Weighted average number of outstanding shares	10,000	10,000	10,000	10,000
Basic earnings per share	0.38	0.73	0.35	0.71

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

Amounts are in ISK million

18. Classification of financial assets and financial liabilities

At 30 September 2020	Mandatorily at FVTPL	Held for hedging	Designated as at FVTPL	Amortised cost	Carrying amount
Cash and balances with Central Bank	-	-	-	95,022	95,022
Loans to credit institutions	-	-	-	61,898	61,898
Listed bonds and debt instruments	120,307	-	-	-	120,307
Listed bonds and debt instruments used for economic hedging	28,883	-	-	-	28,883
Unlisted bonds and debt instruments	236	-	-	-	236
Derivatives	2,648	1,083	-	-	3,731
Loans to customers	-	-	-	970,309	970,309
Listed shares and equity instruments	3,048	-	-	-	3,048
Listed shares and equity instruments used for economic hedging	8,754	-	-	-	8,754
Unlisted shares and equity instruments	2,855	-	-	-	2,855
Other financial assets	-	-	-	16,812	16,812
Total financial assets	166,731	1,083	-	1,144,041	1,311,855
Deposits from Central Bank and credit institutions	-	-	-	36,438	36,438
Deposits from customers	-	-	-	698,610	698,610
Derivative instruments and short positions	8,406	-	-	-	8,406
Debt issued and other borrowed funds	-	49,840	49,273	225,639	324,752
Subordinated loans	-	-	-	26,798	26,798
Other financial liabilities	-	-	-	42,674	42,674
Total financial liabilities	8,406	49,840	49,273	1,030,159	1,137,678

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

Amounts are in ISK million

19. Fair value information for financial instruments

Financial instruments carried at fair value

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

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

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

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

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

At 30 September 2020	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	149,190	-	236	149,426
Derivatives	-	3,731	-	3,731
Shares and equity instruments	11,690	29	2,938	14,657
Total financial assets	160,880	3,760	3,174	167,814
Short positions	1,715	-	-	1,715
Derivative instruments	-	6,691	-	6,691
Debt issued and other borrowed funds designated as at FVTPL	49,273	-	-	49,273
Total financial liabilities	50,988	6,691	-	57,679

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

Changes in Level 3 assets measured at fair value	Bonds and debt instruments	Shares and equity instruments
Fair value at 1 January 2020	1,348	6,016
Purchases	28	7
Net gain (loss) on financial instruments recognised in profit or loss	(1,145)	46
Transfer to "Non-current assets and disposal groups held for sale"	-	(3,180)
Other changes	5	49
Fair value at 30 September 2020	236	2,938

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

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

Valuation process

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

Valuation techniques

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

Level 1: Fair value established from quoted market prices.

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

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

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

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

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

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

At 30 September 2020 the Group's Level 3 equities amounted to ISK 2,938 million:

-These include shares in seven professional investment funds and investment companies investing in unlisted equities and specialised investments in Iceland totalling ISK 1,104 million. The Group receives information from fund managers which use valuation models for the valuation of these equities.

-Other Level 3 equities amounting to ISK 1,834 million.

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

At 30 September 2020 the Group's Level 3 bonds amounted to ISK 236 million:

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

Amounts are in ISK million

19. Cont'd

Sensitivity analysis for Level 3 assets

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

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

At 30 September 2020 **Effect on profit or (loss):**	Carrying amount	Very favourable	Favourable	Unfavourable	Very unfavour-able
Level 3 Bonds and debt instruments	236	1,183	800	(215)	(229)
Level 3 Shares and equity instruments	2,938	1,845	649	(694)	(1,060)

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

20. Financial instruments not carried at fair value

Assets

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

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

Liabilities

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

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

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

The following table shows the fair value measurement and classification of the Group's assets and liabilities not carried at fair value. The different levels are defined in Note 19.

Amounts are in ISK million

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At 30 September 2020	Level 1	Level 2	Level 3	Total fair value	Carrying amount
Cash and balances with Central Bank	-	95,022	-	95,022	95,022
Loans to credit institutions	-	61,898	-	61,898	61,898
Loans to customers	-	-	978,868	978,868	970,309
Other financial assets	-	16,812	-	16,812	16,812
Total financial assets	-	173,732	978,868	1,152,600	1,144,041
Deposits from Central Bank and credit institutions	-	36,569	-	36,569	36,438
Deposits from customers	-	698,829	-	698,829	698,610
Debt issued and other borrowed funds	183,309	109,496	-	292,805	275,480
Subordinated loans	-	25,405	-	25,405	26,798
Other financial liabilities	-	42,674	-	42,674	42,674
Total financial liabilities	183,309	912,973	-	1,096,282	1,080,000

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

21. Offsetting financial assets and financial liabilities

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

	Financial assets subject to netting arrangements			Amounts not set off but subject to master netting arrangements and similar agreements					
At 30 September 2020	Financial assets before netting	Netting with financial liabilities	Net financial assets	Financial liabilities	Cash collateral received	Financial instruments collateral received	Net amount after consideration of potential effect of netting arrangements	Assets outside the scope of offsetting disclosure requirements	Total financial assets recognised in the balance sheet
Reverse repurchase agreements	1,911	-	1,911	-	-	-	1,911	-	1,911
Derivatives	3,731	-	3,731	(971)	(2,186)	(456)	118	-	3,731
Total assets	5,642	-	5,642	(971)	(2,186)	(456)	2,029	-	5,642

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

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

At 30 September 2020	Financial liabilities subject to netting arrangements: Financial liabilities before netting	Netting with financial assets	Net financial liabilities	Amounts not set off but subject to master netting arrangements and similar agreements: Financial assets	Cash collateral pledged	Financial instruments collateral pledged	Net amount after consideration of potential effect of netting arrangements	Liabilities outside the scope of offsetting disclosure requirements	Total financial liabilities recognised in the balance sheet
Derivative instruments and short positions	8,406	-	8,406	(971)	(2,331)	-	5,104	-	8,406
At 31 December 2019									
Derivative instruments and short positions	6,219	-	6,219	(1,374)	(1,139)	-	3,706	-	6,219

22. Cash and balances with Central Bank

	30.9.2020	31.12.2019
Cash on hand	3,965	4,403
Balances with Central Bank	81,559	126,956
Balances with Central Bank subject to special restrictions*	1,385	1,679
Included in cash and cash equivalents	86,909	133,038
Mandatory reserve deposits with Central Bank	8,113	13,600
Cash and balances with Central Bank	95,022	146,638

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

23. Loans to credit institutions

	30.9.2020	31.12.2019
Money market loans	36,336	33,254
Bank accounts	25,554	21,122
Other loans	8	-
Loans to credit institutions	61,898	54,376

Amounts are in ISK million

24. Derivative instruments and short positions

At 30 September 2020	Assets	Notional values related to assets	Liabilities	Notional values related to liabilities
Interest rate swaps	2,029	139,325	3,577	61,341
Cross-currency interest rate swaps	246	21,746	1,237	45,044
Equity forwards	246	4,450	416	5,102
Foreign exchange forwards	456	7,242	4	694
Foreign exchange swaps	663	23,914	1,071	31,401
Bond forwards	91	13,459	386	16,488
Derivatives	3,731	210,136	6,691	160,070
Short positions in listed bonds	-	-	1,715	1,386
Total	3,731	210,136	8,406	161,456

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

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

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

The Group applies hedge accounting only with respect to certain EUR denominated interest rate swaps, whereby the Group pays floating rate interest and receives fixed rate interest. The interest rate swaps are hedging the exposure of changes in the fair value of certain fixed-rate EUR denominated bonds (see Note 33) arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 30 September 2020 the total fair value of the interest rate swaps was positive and amounted to ISK 1,083 million (2019: ISK 921 million) and their total notional amount was ISK 48,660 million (2019: ISK 40,749).

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

25. Loans to customers

At 30 September 2020	Gross carrying amount			Expected credit loss			Net carrying
	Stage 1	Stage 2	Stage 3	Stage 1	Stage 2	Stage 3	amount
Individuals	367,816	6,199	8,673	(1,545)	(222)	(955)	379,966
Commerce and services	61,590	58,871	6,715	(598)	(1,956)	(2,671)	121,951
Construction	38,168	5,817	1,214	(280)	(202)	(167)	44,550
Energy	8,374	-	-	(58)	-	-	8,316
Financial services	1,777	-	-	(1)	-	-	1,776
Industrial and transportation	51,147	29,937	4,168	(300)	(517)	(1,977)	82,458
Investment companies	17,004	4,386	4,341	(251)	(406)	(327)	24,747
Public sector and non-profit organisations	11,512	159	3	(23)	(29)	-	11,622
Real estate	137,970	23,630	6,861	(539)	(1,103)	(1,449)	165,370
Seafood	128,416	1,285	306	(270)	(7)	(177)	129,553
Loans to customers	823,774	130,284	32,281	(3,865)	(4,442)	(7,723)	970,309

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

26. Expected credit loss

Total allowances for expected credit losses

	Stage 1	Stage 2	Stage 3	Total
Cash and balances with Central Bank	2	-	-	2
Loans to credit institutions	79	-	-	79
Loans to customers	3,865	4,442	7,723	16,030
Other financial assets	5	3	-	8
Off-balance sheet loan commitments and financial guarantees	362	250	252	864
At 30 September 2020	4,313	4,695	7,975	16,983
Cash and balances with Central Bank	4	-	-	4
Loans to credit institutions	67	-	-	67
Loans to customers	3,645	953	5,700	10,298
Other financial assets	9	3	86	98
Off-balance sheet loan commitments and financial guarantees	403	55	231	689
At 31 December 2019	4,128	1,011	6,017	11,156

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

26. Cont'd

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

Loans to customers

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2020	3,645	953	5,700	10,298
Transfer to Stage 1	2,997	(2,477)	(520)	-
Transfer to Stage 2	(1,424)	2,542	(1,118)	-
Transfer to Stage 3	(134)	(1,027)	1,161	-
Transfer to "Non-current assets and disposal groups held for sale"	(50)	(12)	(83)	(145)
Net remeasurement of loss allowance	(2,173)	4,147	1,598	3,572
New financial assets originated or purchased	1,279	418	1,963	3,660
Derecognitions and maturities	(275)	(102)	(236)	(613)
Write-offs	-	-	(1,279)	(1,279)
Recoveries of amounts previously written off	-	-	139	139
Foreign exchange	-	-	103	103
Unwinding of interests	-	-	295	295
At 30 September 2020	3,865	4,442	7,723	16,030
At 1 January 2019	3,277	1,079	3,689	8,045
Transfer to Stage 1	1,725	(1,343)	(382)	-
Transfer to Stage 2	(1,336)	1,687	(351)	-
Transfer to Stage 3	(178)	(720)	898	-
Net remeasurement of loss allowance	(1,216)	145	2,727	1,656
New financial assets originated or purchased	1,803	278	353	2,434
Derecognitions and maturities	(430)	(169)	(188)	(787)
Write-offs	-	(4)	(1,616)	(1,620)
Recoveries of amounts previously written off	-	-	249	249
Foreign exchange	-	-	10	10
Unwinding of interests	-	-	311	311
At 31 December 2019	3,645	953	5,700	10,298

Off-balance sheet loan commitments and financial guarantees

	Stage 1	Stage 2	Stage 3	Total
At 1 January 2020	403	55	231	689
Transfer to Stage 1	150	(101)	(49)	-
Transfer to Stage 2	(56)	200	(144)	-
Transfer to Stage 3	(9)	(39)	48	-
Net remeasurement of loss allowance	(333)	126	113	(94)
New loan commitments and financial guarantees	288	57	79	424
Derecognitions and maturities	(81)	(48)	(26)	(155)
At 30 September 2020	362	250	252	864
At 1 January 2019	410	142	84	636
Transfer to Stage 1	152	(81)	(71)	-
Transfer to Stage 2	(20)	39	(19)	-
Transfer to Stage 3	(9)	(18)	27	-
Net remeasurement of loss allowance	(455)	(27)	131	(351)
New loan commitments and financial guarantees	447	20	119	586
Derecognitions and maturities	(122)	(20)	(40)	(182)
At 31 December 2019	403	55	231	689

Amounts are in ISK million

27. Property and equipment

At 30 September 2020	Land and buildings	Right-of-use assets: Buildings	Fixtures, equipment & vehicles	Total
Balance at the beginning of the year	4,096	4,634	4,068	12,798
Additions during the period	32	-	383	415
Disposals and write-offs during the period	(120)	(69)	(462)	(651)
Remeasurement	-	105	-	105
Transfer to "Non-current assets and disposal groups held for sale"	(953)	(20)	(807)	(1,780)
Historical cost	3,055	4,650	3,182	10,887
Balance at the beginning of the year	(1,447)	(420)	(1,763)	(3,630)
Depreciation during the period	(15)	(371)	(299)	(685)
Disposals and write-offs during the period	17	(14)	336	339
Transfer to "Non-current assets and disposal groups held for sale"	109	2	387	498
Accumulated depreciation	(1,336)	(803)	(1,339)	(3,478)
Carrying amount	1,719	3,847	1,843	7,409
Annual deprecion rates	0-2%	8-31%	8-35%	
Official real estate value of land and buildings				1,547
Insurance value of buildings				2,562
Insurance value of fixtures, equipment and vehicles				3,069

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

Amounts are in ISK million

28. Other assets

	30.9.2020	31.12.2019
Receivables	2,167	4,810
Unsettled securities transactions	13,998	279
Accruals	211	253
Prepaid expenses	441	468
Deferred tax assets	173	476
Other assets	169	322
Other assets	17,159	6,608

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

	30.9.2020	31.12.2019
Repossessed collateral:		
Land and buildings	1,575	739
Industrial equipment and vehicles	9	44
Assets of disposal groups classified as held for sale	3,225	292
Non-current assets and disposal groups held for sale	4,809	1,075

At the end of the third quarter 2020 the Group classified the assets and liabilities of Borgun-VS ehf. (63.5%) and Miðengi ehf. (100%) as assets and liabilities of disposal groups held for sale.

30. Deposits from Central Bank and credit institutions

	30.9.2020	31.12.2019
Deposits from credit institutions	36,359	30,808
Repurchase agreements with Central Bank	79	117
Deposits from Central Bank and credit institutions	36,438	30,925

31. Deposits from customers

	30.9.2020	31.12.2019
Demand deposits and deposits with maturity up to 3 months	600,467	530,960
Term deposits with maturity of more than 3 months	98,143	87,353
Deposits from customers	698,610	618,313

Deposits from customers specified by owners	30.9.2020		31.12.2019	
	Amount	% of total	Amount	% of total
Central government and state-owned enterprises	10,833	2%	12,553	2%
Municipalities	9,186	1%	5,619	1%
Companies	358,025	51%	299,204	48%
Individuals	320,566	46%	300,937	49%
Deposits from customers	698,610	100%	618,313	100%

Amounts are in ISK million

32. Pledged assets

	30.9.2020	31.12.2019
Financial assets pledged as collateral against liabilities	217,893	205,773
Financial assets pledged as collateral in foreign banks	696	402
Financial assets pledged as collateral in repurchase agreements	1,911	1,114
Pledged assets against liabilities	220,500	207,289

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

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

33. Debt issued and other borrowed funds

	Issued	Maturity		Interest	30.9.2020	31.12.2019
Covered bonds in ISK	2019	2021	At maturity	Fixed rates	5,018	3,918
Covered bonds in ISK	2015-2019	2023	At maturity	Fixed rates	23,716	20,170
Covered bonds in ISK	2020	2027	At maturity	Fixed rates	1,149	-
Covered bonds in ISK - CPI-linked	2014-2015	2020	At maturity	Fixed rates	-	4,359
Covered bonds in ISK - CPI-linked	2015-2017	2022	At maturity	Fixed rates	18,917	18,512
Covered bonds in ISK - CPI-linked	2012-2018	2024	At maturity	Fixed rates	36,227	35,752
Covered bonds in ISK - CPI-linked	2015-2018	2026	At maturity	Fixed rates	28,574	27,661
Covered bonds in ISK - CPI-linked	2019	2028	Amortising	Fixed rates	20,712	14,228
Covered bonds in ISK - CPI-linked	2017-2018	2030	At maturity	Fixed rates	26,266	25,463
Covered bonds					160,579	150,063
Senior unsecured bonds in EUR**	2016	2020	At maturity	Fixed rates	-	7,782
Senior unsecured bonds in SEK*	2019	2020	At maturity	Floating rates	-	4,557
Senior unsecured bonds in SEK	2018	2021	At maturity	Fixed rates	1,533	1,308
Senior unsecured bonds in SEK*	2018-2019	2021	At maturity	Floating rates	21,165	18,913
Senior unsecured bonds in EUR	2019	2021	At maturity	Floating rates	1,864	1,559
Senior unsecured bonds in SEK	2018	2022	At maturity	Floating rates	15,350	12,990
Senior unsecured bonds in EUR**	2019	2022	At maturity	Fixed rates	49,273	41,570
Senior unsecured bonds in NOK	2019	2022	At maturity	Floating rates	14,661	13,856
Senior unsecured bonds in EUR***	2018	2024	At maturity	Fixed rates	49,840	41,816
Senior unsecured bonds in NOK	2019	2024	At maturity	Fixed rates	5,996	5,709
Senior unsecured bonds in ISK	2019	2024	Monthly	Floating rates	3,001	3,553
Bonds issued					162,683	153,613
Bills issued					1,421	2,705
Other debt securities					69	-
Other borrowed funds					1,490	2,705
Debt issued and other borrowed funds					324,752	306,381

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

**These bond issuances are classified as being designated as at fair value through profit or loss. At 30 September 2020 the total carrying amount of the bonds amounted to ISK 49,273 million and included in the amount are fair value changes amounting to ISK 608 million. The carrying amount of the bonds at 30 September 2020 was ISK 65 million lower than the contractual amount due at maturity.

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33. Cont'd

***The Group applies hedge accounting to this bond issuance and uses certain EUR denominated interest rate swaps as hedging instruments (see Note 24). The interest rate swaps are hedging the exposure of the Group's changes in the fair value of this fixed-rate EUR denominated bond arising from changes in EURIBOR benchmark interest rates. The Group applies fair value hedge accounting to the hedging relationships and for the purpose of evaluating whether the hedging relationship is expected to be highly effective, the Group assumes that the benchmark interest rate is not altered as a result of IBOR reform. At 30 September 2020 the total carrying amount of the bond issuance amounted to ISK 49,840 million and included in the amount are fair value changes amounting to ISK 936 million.

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

34. Subordinated loans

	Issued	Maturity		Interest	30.9.2020	31.12.2019
Loans which qualify as Tier 2 capital:						
Subordinated loans in SEK	2017	2027	At maturity	Floating, STIBOR + 2.0%	11,479	9,714
Subordinated loans in SEK	2018	2028	At maturity	Floating, STIBOR + 2.5%	7,662	6,485
Subordinated loans in SEK	2019	2029	At maturity	Floating, STIBOR + 3.9%	7,657	6,475
Subordinated loans					26,798	22,674

35. Changes in liabilities arising from financing activities

			Non-cash changes			
	1.1.2020	Cash flows	Interest expense	Foreign exchange	Fair value changes	30.9.2020
Covered bonds in ISK	24,088	4,713	1,082	-	-	29,883
Covered bonds in ISK - CPI-linked	125,975	(1,236)	5,957	-	-	130,696
Senior unsecured bonds in ISK	3,553	(616)	64	-	-	3,001
Senior unsecured bonds FX	58,892	(6,917)	785	7,809	-	60,569
Senior unsecured bonds FX at fair value	49,352	(9,956)	446	9,671	(240)	49,273
Senior unsecured bonds used for hedging	41,816	(463)	419	7,903	165	49,840
Other borrowed funds	2,705	(1,261)	46	-	-	1,490
Subordinated loans	22,674	(552)	570	4,106	-	26,798
Total	329,055	(16,288)	9,369	29,489	(75)	351,550

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

Amounts are in ISK million

Notes to the Condensed Consolidated Interim Financial Statements

36. Other liabilities

	30.9.2020	31.12.2019
Accruals	2,173	3,217
Liabilities to retailers for credit cards	-	14,765
Lease liabilities	3,980	4,256
Provision for effects of court rulings	288	75
Expected credit loss for off-balance sheet loan commitments and financial guarantees	864	689
Withholding tax	420	1,559
Unsettled securities transactions	34,533	515
Deferred income	-	229
Sundry liabilities	1,815	1,758
Non-current liabilities and disposal groups held for sale	1	-
Other liabilities	44,074	27,063

37. Custody assets

	30.9.2020	31.12.2019
Custody assets - not managed by the Group	2,735,658	2,496,313

38. Related party

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

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

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

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

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

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

At 30 September 2020	Assets	Liabilities	Net balance	Commitments, guarantees & overdrafts
Shareholders with control over the Group	-	-	-	2
Board of Directors, key management personnel and other related parties	244	372	(128)	48
Associated companies	1	1,018	(1,017)	227
Balances with related parties	245	1,390	(1,145)	277

1 January to 30 September 2020	Interest income	Interest expense	Other income	Other expense
Board of Directors, key management personnel and other related parties	10	7	1	-
Associated companies	-	6	1	1,172
Transactions with related parties	10	13	2	1,172

Amounts are in ISK million

38. Cont'd

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

1 January to 30 September 2019	Interest income	Interest expense	Other income	Other expense
Board of Directors, key management personnel and other related parties	23	7	-	-
Associated companies	7	13	3	1,231
Transactions with related parties	30	20	3	1,231

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

39. Contingencies

Contingent liabilities

Borgun hf. – Landsbanki case

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

On 7 July 2020 the Group closed an agreement on the sale of all its stake in Borgun hf. In the agreement Íslandsbanki has undertaken to reimburse up to 63.47% of losses incurred by Borgun hf. or the buyer in the event of an unfavourable outcome in the Landsbanki case.

40. Events after the reporting period

No events have arisen after the reporting period that require amendments or additional disclosures in the interim financial statements for the third quarter 2020.

41. Risk management

Risk governance

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

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42. Credit risk

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

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

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

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

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

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

43. Maximum credit exposure

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

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

The Government guarantee schemes issued in response to the COVID-19 pandemic are now shown under “Loans to customers”. Of these, ISK 1,403 million are subject to 100% Government guarantee and ISK 255 million to 85% Government guarantee.

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

At 30 September 2020	Individuals	Central governments	Commerce and services	Construction	Energy	Financial services	Industrial and transportation	Investment companies	Public sector and non-profit organisations	Real estate	Seafood	Total
Cash and balances with Central Bank	-	95,022	-	-	-	-	-	-	-	-	-	95,022
Loans to credit institutions	-	-	-	-	-	61,898	-	-	-	-	-	61,898
Bonds and debt instruments	-	127,426	18	-	648	20,269	191	27	303	544	-	149,426
Derivatives	5	-	82	-	21	5,091	639	206	-	266	347	6,657
Loans to customers:	379,966	-	121,951	44,550	8,316	1,776	82,458	24,747	11,622	165,370	129,553	970,309
Overdrafts	12,350	-	10,751	3,289	3	1,333	5,607	1,002	774	2,376	5,809	43,294
Credit cards	14,119	-	1,151	248	4	12	346	17	79	56	28	16,060
Mortgages	316,896	-	-	-	-	-	-	-	-	-	-	316,896
Capital leases	6,273	-	27,595	2,799	14	-	7,359	153	41	1,090	190	45,514
Government guarantee schemes	-	-	1,332	36	-	-	175	1	-	29	85	1,658
Other loans	30,328	-	81,122	38,178	8,295	431	68,971	23,574	10,728	161,819	123,441	546,887
Other financial assets	613	101	220	25	1	15,671	98	42	3	26	12	16,812
Off-balance sheet items:	34,469	-	29,240	13,993	447	9,644	27,609	1,902	5,445	14,383	11,644	148,776
Financial guarantees	1,138	-	5,073	5,755	-	1,236	3,060	27	6	1,962	272	18,529
Undrawn loan commitments	-	-	4,020	4,856	116	-	18,380	1,160	-	7,642	3,142	39,316
Undrawn overdrafts	9,047	-	15,510	2,591	298	8,173	4,994	480	4,127	4,464	8,043	57,727
Credit card commitments	24,284	-	4,637	791	33	235	1,175	235	1,312	315	187	33,204
Maximum credit exposure	415,053	222,549	151,511	58,568	9,433	114,349	110,995	26,924	17,373	180,589	141,556	1,448,900

Amounts are in ISK million

43. Cont'd

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

44. Credit exposure covered by collateral

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

In some cases the Group uses guarantees as a credit enhancement but since guarantees effectively transfer credit risk from one counterparty to another they do not represent a reduction in maximum exposure to credit risk. Exception from this are Government guarantees issued in response to the COVID-19 pandemic which are shown under other collateral. Covenants in loan agreements are also an important credit enhancement but do not reduce maximum credit exposure.

Amounts are in ISK million

44. Cont'd

Valuation of collateral is based on market price, official valuation for tax purposes or expert opinion of the Group's employees, depending on availability. In the case of fishing vessels the associated fishing quota is included in the valuation. Collateral is allocated according to the gross carrying amount of loans and nominal off-balance sheet items, and is measured without including the effect of overcollateralisation. This means that if some loans have collateral values in excess of their gross carrying amount, then the excess is removed in order to reflect the Group's actual maximum exposure to credit risk. The total value of pledged assets can thus be higher than the cover indicates. The maximum credit risk exposure is measured on net carrying value basis, and therefore collateral allocation can in some instances be higher. For capital leases the Group remains the owner of the leased object. In total ISK 39,371 million of the collateral are leased objects.

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

At 30 September 2020 **Collateral held against non credit-impaired exposures**	Maximum exposure to credit risk	Real estate	Vessels	Cash & securities	Vehicles & equipment	Other collateral	Total credit exposure covered by collateral	Total credit exposure not covered by collateral	Associated ECL
Derivatives	6,657	-	-	1,825	-	-	1,825	4,832	-
Loans and commitments to customers:	1,094,048	665,429	99,779	4,262	50,823	92,466	912,759	181,289	8,919
Individuals	406,623	327,554	7	336	14,487	149	342,533	64,090	1,859
Commerce and services	146,866	60,982	152	661	26,947	26,099	114,841	32,025	2,803
Construction	57,445	43,541	11	1,604	2,044	2,418	49,618	7,827	577
Energy	8,763	4,038	-	5	8	53	4,104	4,659	60
Financial services	11,420	1,133	-	102	-	3,944	5,179	6,241	12
Industrial and transportation	107,830	45,172	13	175	6,813	27,210	79,383	28,447	887
Investment companies	22,634	6,206	-	903	71	11,142	18,322	4,312	665
Public sector and non-profit organisations	17,064	1,007	-	5	30	-	1,042	16,022	56
Real estate	174,335	161,849	5	447	344	1,107	163,752	10,583	1,713
Seafood	141,068	13,947	99,591	24	79	20,344	133,985	7,083	287
Total	1,100,705	665,429	99,779	6,087	50,823	92,466	914,584	186,121	8,919
Collateral held against credit-impaired exposures									
Loans and commitments to customers:	25,037	17,031	1,538	2,695	984	833	23,081	1,955	7,975
Individuals	7,812	6,948	18	5	160	3	7,134	678	1,001
Commerce and services	4,325	2,092	709	11	411	683	3,906	419	2,837
Construction	1,098	790	-	-	101	64	955	143	183
Industrial and transportation	2,237	546	786	56	278	65	1,731	506	1,994
Investment companies	4,015	1,365	-	2,619	14	1	3,999	15	327
Public sector and non-profit organisations	3	2	-	-	-	-	2	1	-
Real estate	5,418	5,199	-	4	11	14	5,228	190	1,456
Seafood	129	89	25	-	9	3	126	3	177
Total	25,037	17,031	1,538	2,695	984	833	23,081	1,955	7,975

Amounts are in ISK million

44. Cont'd

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

Amounts are in ISK million

45. Credit quality of financial assets

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

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

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

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

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

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

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

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

At 30 September 2020

Loans to customers:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	244,888	17,713	-	262,601
Risk class 5-6	334,374	64,392	-	398,766
Risk class 7-8	207,585	37,233	-	244,818
Risk class 9	36,800	10,841	-	47,641
Risk class 10	-	-	32,281	32,281
Unrated	127	105	-	232
	823,774	130,284	32,281	986,339
Expected credit loss	(3,865)	(4,442)	(7,723)	(16,030)
Net carrying amount	819,909	125,842	24,558	970,309

Off-balance sheet loan commitments and financial guarantees:	Stage 1	Stage 2	Stage 3	Total
Risk class 1-4	65,901	2,068	-	67,969
Risk class 5-6	46,626	5,391	-	52,017
Risk class 7-8	12,094	14,970	-	27,064
Risk class 9	1,126	644	-	1,770
Risk class 10	-	-	731	731
Unrated	79	10	-	89
	125,826	23,083	731	149,640
Expected credit loss	(362)	(250)	(252)	(864)
Total	125,464	22,833	479	148,776

Amounts are in ISK million

45. Cont'd

At 30 September 2020	Risk class 1-4	Risk class 5-6	Risk class 7-8	Risk class 9	Risk class 10	Unrated	ECL	Total
Loans and commitments to customers:								
Individuals	83,272	154,449	137,096	33,654	8,820	4	(2,860)	414,435
Commerce and services	24,922	81,459	38,006	5,181	7,157	106	(5,640)	151,191
Construction	4,681	30,025	21,028	2,288	1,280	1	(760)	58,543
Energy	2,955	4,150	1,718	-	-	-	(60)	8,763
Financial services	10,912	2	508	-	-	10	(12)	11,420
Industrial and transportation	33,587	42,885	29,474	2,722	4,230	50	(2,881)	110,067
Investment companies	2,627	10,345	8,814	1,511	4,342	2	(992)	26,649
Public sector and non-profit organisations	13,904	2,824	267	-	4	124	(56)	17,067
Real estate	67,905	71,607	33,252	3,280	6,873	5	(3,169)	179,753
Seafood	85,805	53,037	1,719	775	306	19	(464)	141,197
Total	330,570	450,783	271,882	49,411	33,012	321	(16,894)	1,119,085

At 31 December 2019

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

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

Amounts are in ISK million

45. Cont'd

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

46. Loans to customers in the tourism industry

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

At 30 September 2020

Loans to customers in the tourism industry:	Stage 1	Stage 2	Stage 3	Total
Group 1	1,126	381	-	1,507
Group 2	-	32,079	515	32,594
Group 3	-	52,757	1,286	54,043
Group 4	1,065	8,914	5,341	15,320
	2,191	94,131	7,142	103,464
Expected credit loss	(28)	(3,061)	(2,552)	(5,641)
Net carrying amount	2,163	91,070	4,590	97,823

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

	Stage 1	Stage 2	Stage 3	Total
Group 1	37	8	-	45
Group 2	1	14,460	88	14,549
Group 3	1	4,400	70	4,471
Group 4	77	1,029	128	1,234
	116	19,897	286	20,299
Expected credit loss	(1)	(215)	(135)	(351)
Total	115	19,682	151	19,948

Amounts are in ISK million

47. Forbearance

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

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

Once an asset has been classified as forborne, it will remain forborne for a minimum 24-month probation period. In order for a loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:
- All of the customer's facilities have to be considered performing; and
- The customer does not have any contract that is more than 30 days past due; and
- The probation period of two years has passed from the date of the forbearance event; and
- Regular payments of more than an insignificant amount of principal or interest have been made during at least half of the probation period

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

At 30 September 2020

	Stage 1	Stage 2	Stage 3	Total
Individuals	818	2,482	2,161	5,461
Companies	184	22,141	14,146	36,471
Gross carrying amount	1,002	24,623	16,307	41,932

	Stage 1	Stage 2	Stage 3	Total
Individuals	(8)	(77)	(188)	(273)
Companies	(1)	(885)	(4,142)	(5,028)
Expected credit loss	(9)	(962)	(4,330)	(5,301)

At 31 December 2019

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

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

Amounts are in ISK million

48. COVID-19 moratoria

The Group recognises that the economic effects of the COVID-19 pandemic will temporarily have a seriously negative impact on customers' cash flow and thus their ability to repay their debt in accordance with their obligations. The Group entered into an agreement with other financial institutions and lenders in Iceland to provide a moratorium for corporate customers, uniformly executed across institutions. Similarly, the Group entered into an agreement for a moratorium for households and individuals. In accordance with guidelines from EBA and the Central Bank, moratoria of this kind did not trigger classification as forbearance. The agreement expired on 30 September 2020. All further moratorium after this date, will be classified as forbearance.

The following table shows the extent of payment moratoria granted by the Group under these initiatives agreed and applied broadly by domestic credit institutions. At the reporting date, expired moratoria is ISK 46,330 million.

At 30 September 2020

	Stage 1	Stage 2	Stage 3	Total
Individuals	17,082	458	-	17,540
Companies	65,990	54,327	-	120,317
Gross carrying amount	83,072	54,785	-	137,857

	Stage 1	Stage 2	Stage 3	Total
Individuals	(91)	(19)	-	(110)
Companies	(380)	(1,401)	-	(1,781)
Expected credit loss	(471)	(1,420)	-	(1,891)

49. Assets obtained by taking possession of collateral

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

	30.09.2020	31.12.2019
Property and land	1,431	378
Industrial equipment and vehicles	41	81
Total	1,472	459

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

50. Write-offs

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

Gross carrying amount written off and still subject to enforcement activity	2020 1.1-30.9	2019 1.1-30.9
Individuals	338	348
Companies	925	995
Total	1,263	1,343

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51. Large exposures disclosure

When the Group's total exposure to a group of connected clients is 10% or higher of the Group's capital base it is considered a large exposure. Both on-balance sheet and off-balance sheet items from all types of financial instruments are included in the exposure as defined by regulation no. 233/2017. The Group has internal criteria that define connections between clients. These criteria reflect the Group's interpretation of Article (1)(a) of the Act on Financial Undertakings no. 161/2002, where groups of connected clients are defined. Since the interim financial statements for the third quarter of the year are not audited, the official capital is based on reviewed own fund items at 30 June 2020.

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

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

At 30 September 2020

Groups of connected clients:	Before	After
Group 1	90%	-
Group 2	12%	11%

At 31 December 2019

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

52. Liquidity risk

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

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

53. Liquidity coverage and Net stable funding ratio

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

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

Net stable funding ratio	30.9.2020	31.12.2019
For all currencies	113%	119%
Foreign currencies	149%	156%

Liquidity coverage ratio	30.9.2020	31.12.2019
For all currencies	136%	155%
Domestic currency	96%	110%
Foreign currencies	405%	325%

Amounts are in ISK million

53. Cont'd

At 30 September 2020	For all currencies		Foreign currencies	
	Unweighted	Weighted	Unweighted	Weighted
Liquid assets level 1*	198,747	198,747	37,439	37,439
Liquid assets level 2	10,616	307	18	-
Total liquid assets	209,363	199,054	37,457	37,439
Deposits	550,920	177,982	76,235	30,098
Debt issued	914	914	143	143
Other outflows	97,745	36,290	23,060	6,759
Total outflows	649,579	215,186	99,438	37,000
Short-term deposits with other banks**	58,007	57,311	55,934	55,238
Other inflows	29,319	11,185	6,720	3,617
Restrictions on inflows	-	-	-	(31,105)
Total inflows	87,326	68,496	62,654	27,750
Liquidity coverage ratio		136%		405%

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

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

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

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53. Cont'd

Deposits by liquidity coverage ratio category

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

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

	Deposits maturing within 30 days					
At 30 September 2020	Less stable	Weight (%)	Stable	Weight (%)	Term deposits	Total deposits
Retail	226,955	12%	123,675	5%	89,234	439,864
Operational relationships	3,640	25%	-	5%	-	3,640
Corporations	76,098	40%	461	20%	22,946	99,505
Sovereigns, Central Bank and public sector entities	10,670	40%	426	20%	945	12,041
Pension funds	66,665	100%	-		21,493	88,158
Domestic financial entities	37,564	100%	-		39,267	76,831
Foreign financial entities	4,766	100%	-		10,243	15,009
Total	426,358		124,562		184,128	735,048

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

54. Maturity analysis of assets and liabilities

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

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

Maturity analysis 30 September 2020

Financial liabilities	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Deposits from CB and credit institutions	36,438	5,517	14,929	10,171	5,839	-	-	36,456
Deposits from customers	698,610	548,121	77,843	62,945	17,148	27,164	-	733,221
Debt issued and other borrowed funds	324,752	-	1,962	39,713	263,688	90,415	-	395,778
Subordinated loans	26,798	-	184	467	2,977	29,677	-	33,305
Other financial liabilities:	42,674	37,960	712	501	1,748	2,202	-	43,123
Lease liabilities	3,980	-	120	359	1,748	2,202	-	4,429
Other liabilities	38,694	37,960	592	142	-	-	-	38,694
Total	1,129,272	591,598	95,630	113,797	291,400	149,458	-	1,241,883

Amounts are in ISK million

54. Cont'd

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

Off-balance sheet liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Financial guarantees	18,529	-	-	-	-	-	18,529
Undrawn loan commitments	39,316	-	-	-	-	-	39,316
Undrawn overdrafts	57,727	-	-	-	-	-	57,727
Credit card commitments	33,204	-	-	-	-	-	33,204
Total	148,776	-	-	-	-	-	148,776
Total non-derivative financial liabilities and off-balance sheet liabilities	740,374	95,630	113,797	291,400	149,458	-	1,390,659

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

Derivative financial liabilities	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	21,453	52,791	44,369	-	-	118,613
Outflow	-	(21,716)	(55,448)	(48,163)	-	-	(125,327)
Total	-	(262)	(2,657)	(3,794)	-	-	(6,713)
Net settled derivatives	-	(786)	-	-	-	-	(786)
Total	-	(1,048)	(2,657)	(3,794)	-	-	(7,499)

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

Financial assets	Carrying amount	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Cash and balances with Central Bank	95,022	42,397	51,240	-	-	1,385	-	95,022
Loans to credit institutions	61,898	24,858	37,032	8	-	-	-	61,898
Bonds and debt instruments	149,426	-	59,236	45,249	36,993	7,948	-	149,426
Loans to customers	970,309	7,057	83,512	91,080	341,823	446,837	-	970,309
Shares and equity instruments	14,657	-	-	-	-	-	14,657	14,657
Other financial assets	16,812	14,770	544	1,162	336	-	-	16,812
Total	1,308,124	89,082	231,564	137,499	379,152	456,170	14,657	1,308,124

Derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	No maturity	Total
Gross settled derivatives							
Inflow	-	30,044	24,095	29,814	-	-	83,953
Outflow	-	(28,845)	(23,308)	(27,831)	-	-	(79,984)
Total	-	1,199	787	1,983	-	-	3,969
Net settled derivatives	-	314	-	-	-	-	314
Total	-	1,513	787	1,983	-	-	4,283

Amounts are in ISK million

54. Cont'd

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

Maturity analysis 31 December 2019

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

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

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

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

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

Amounts are in ISK million

55. Market risk

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

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

56. Interest rate risk

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

Interest rate risk in the trading book

The fixed income trading unit invests mainly in government bonds, bonds issued by the Housing and Construction Authority which are guaranteed by the Icelandic Government, domestic municipality bonds, and covered bonds issued by other Icelandic banks. Bonds and bills in the Group's liquidity portfolio are also categorised in the trading book. In the following table the total market value (MV) of long and short positions may not be the same as reported in Note 18 since netting between short and long positions is not applied here.

	30.9.2020			31.12.2019		
Trading bonds and debt instruments, long positions	MV	Duration	BPV	MV	Duration	BPV
Indexed	4,118	3.36	(1.39)	1,143	6.84	(0.78)
Non-indexed	116,575	0.46	(5.33)	31,855	0.41	(1.29)
Total	120,693	0.56	(6.72)	32,998	0.63	(2.07)

	30.9.2020			31.12.2019		
Trading bonds and debt instruments, short positions	MV	Duration	BPV	MV	Duration	BPV
Indexed	308	7.00	0.22	150	6.00	0.10
Non-indexed	283	5.00	0.14	615	4.00	0.28
Total	591	6.04	0.36	765	4.39	0.38
Net position of trading bonds and debt instruments	120,102	0.53	(6.36)	32,233	0.54	(1.69)

Interest rate risk in the banking book

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

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

Amounts are in ISK million

56. Cont'd

Sensitivity analysis for interest rate risk in the banking book

At 30 September 2020

Currency	0-3 months	3-12 months	1-2 years	2-5 years	5-10 years	Over 10 years	Total
ISK, indexed	1	(68)	11	(2,070)	4,281	(1,715)	440
ISK, non-indexed	35	28	(55)	(87)	(243)	(3)	(325)
EUR	(60)	37	(74)	136	-	(1)	38
SEK	32	(22)	-	-	-	-	10
USD	24	-	-	-	-	(1)	23
Other	10	(6)	-	(10)	-	(7)	(13)
Total	42	(31)	(118)	(2,031)	4,038	(1,727)	173

At 31 December 2019

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

Amounts are in ISK million

57. Currency risk

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

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

Series C preferred shares in Visa Inc., which the Group holds are included in the currency imbalance even though the shares are classified as held for sale.

Currency analysis at 30 September 2020

Assets	EUR	USD	GBP	CHF	JPY	SEK	NOK	DKK	CAD	Other foreign currencies	Total foreign currencies
Cash and balances with Central Bank	521	379	203	94	21	75	87	171	44	141	1,736
Loans to credit institutions	7,289	40,913	1,004	127	308	52	9,363	155	292	81	59,584
Bonds and debt instruments	10,554	11,273	7	-	-	3,839	10,229	-	-	-	35,902
Loans to customers	136,880	34,228	1,214	565	3,593	1	3,210	746	7,669	32	188,138
Shares and equity instruments	32	3,224	455	-	-	38	31	-	-	-	3,780
Other assets	1,443	33	-	-	-	4	-	-	-	-	1,480
Total assets	156,719	90,050	2,883	786	3,922	4,009	22,920	1,072	8,005	254	290,620
Liabilities											
Deposits from credit institutions	9,723	778	10	-	-	-	1	-	-	-	10,512
Deposits from customers	31,277	33,903	4,312	493	430	1,187	2,897	2,033	549	12	77,093
Debt issued and other borrowed funds	99,922	-	-	-	-	38,048	20,657	-	-	-	158,627
Subordinated loans	-	-	-	-	-	26,798	-	-	-	-	26,798
Other liabilities	206	20	-	-	-	12	27	63	-	-	328
Total liabilities	141,128	34,701	4,322	493	430	66,045	23,582	2,096	549	12	273,358
Net on-balance sheet position	15,591	55,349	(1,439)	293	3,492	(62,036)	(662)	(1,024)	7,456	242	17,262
Net off-balance sheet position	(15,294)	(52,326)	1,482	(302)	(3,464)	61,977	636	922	(7,419)	(252)	(14,040)
Net position	297	3,023	43	(9)	28	(59)	(26)	(102)	37	(10)	3,222

Amounts are in ISK million

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Currency analysis at 31 December 2019

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

Amounts are in ISK million

58. Inflation risk

The Group is exposed to inflation risk since the value of CPI-linked assets exceeds CPI-linked liabilities. The value of these assets and liabilities changes according to changes in the CPI at any given time and all changes in the CPI affect profit and loss. A 1% increase in the index would lead to an ISK 398 million increase in the balance sheet and a 1% decrease would lead to a corresponding decrease, other risk factors held constant.

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

	30.9.2020	31.12.2019
Bonds and debt instruments	4,826	2,103
Loans to customers	285,620	295,725
Total CPI-linked assets	290,446	297,828
Deposits from customers	98,533	98,766
Debt issued and other borrowed funds	130,696	125,975
Off-balance sheet position	21,442	52,427
Total CPI-linked liabilities	250,671	277,168
CPI imbalance	39,775	20,660

59. Derivatives

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

60. Capital management

The following table shows the capital base, risk exposure amount, the resulting capital ratios, and leverage for the Group at 30 September 2020 and 31 December 2019. In addition, the table shows the official capital ratios where the unaudited profit of the third quarter is excluded according to the Act on Financial Undertakings.

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

Article 501 of the capital requirements regulation (EU) no. 575/2013 of the European Parliament came into effect in Iceland on 1 January 2020. This article stipulates capital requirements deduction for credit risk on exposures to SMEs and lowers the risk exposure amount by ISK 11.1 billion as of 30 September 2020, corresponding to a 20 basis point increase in the Group's capital ratio.

EU regulation no. 2017/2395 regarding transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds, was ratified into Icelandic law in May 2020. The regulation allows for the phasing in of capital impacts due to IFRS 9, allowing institutions to include a predefined level of provisions as part of CET1 capital. Íslandsbanki has elected to make use of the transitional arrangements, which will add ISK 4 billion to CET1, corresponding to an increase of 40 basis points in the Group's capital ratio.

The Group aims at managing its capital position and the corresponding capital ratios above the overall regulatory capital requirement. According to the latest SREP report from the Financial Supervisory Authority, applicable as of 22 September 2020, the overall capital requirement is 17.0%. The Group's capital target includes a 0.5-2.0% management buffer on top of the overall capital requirement.

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

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	30.9.2020	31.12.2019
CET1 capital		
Ordinary share capital	10,000	10,000
Share premium	55,000	55,000
Reserves	7,258	7,065
Retained earnings	108,383	105,569
Non-controlling interests	1,868	2,428
IFRS 9 reversal due to transitional rules	4,088	-
Fair value changes due to own credit standing	(239)	392
Tax assets	(173)	(476)
Intangible assets	(3,554)	(4,330)
Total CET1 capital	182,631	175,648
Tier 2 capital		
Qualifying subordinated loans	26,798	22,674
Total capital base	209,429	198,322
Risk exposure amount		
- due to credit risk	836,662	789,180
- due to market risk	18,748	7,919
Market risk, trading book	15,281	6,488
Currency risk	3,467	1,431
- due to credit valuation adjustment	1,505	2,027
- due to operational risk	85,424	85,424
Total risk exposure amount	942,339	884,550
Capital ratios		
Tier 1 ratio	19.4%	19.9%
Total capital ratio	22.2%	22.4%
Official Tier 1 ratio	19.0%	19.9%
Official capital ratio	21.9%	22.4%
Leverage ratio		
Exposure amount		
On-balance sheet exposures	1,321,268	1,189,062
Off-balance sheet exposures	38,324	38,849
Derivative exposures	6,673	9,461
Leverage ratio total exposure measure	1,366,265	1,237,372
Tier 1 capital	182,631	175,648
Leverage ratio	13.4%	14.2%

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