

**Arion Bank Mortgages
Institutional Investor Fund**

Interim Financial Statements 30 June 2015

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Endorsement and Signatures of the Board of Directors and the Managing Director

The Interim Financial Statements of ABMIF are included in part B of the Interim Financial Statements of Stefir hf. which contains the Interim Financial Statements of UCITS, investment funds and institutional investors' funds under management. They have been prepared in accordance with law on Financial Statements and rules on the Financial Statements of management companies of UCITS set by the Icelandic Financial Supervisory Authority.

The fund reported profit of ISK 1,333 million according to the income statement and the profit is recognized as an increase in units in the fund's accounts. The net asset of the fund at the end of the period totalled ISK 22,315 million according to the balance sheet.

The Board of Directors and CEO of Stefir hf. hereby confirm the fund's Interim Financial Statements for the period 1 January - 30 June 2015 with their signatures.

Reykjavik, 27 August 2015

Board of Directors:

Steindur Rudeffpottbi

Svara Bjarnadóttir

Guðlaugur Gunnarsson

Kristján Þórunnsson

CEO:

Jóhann L. Alfreðsson

Elfi Handmann

Review Report on Interim Financial Information

To the Board of Directors the unit holder of ABMIIF.

We have reviewed the accompanying interim financial statement of ABMIIF for the period of 1 January to 30 June 2015, which comprise the endorsement and signatures of the board of directors and managing director, income statement, balance sheet, changes in net assets, statement of investment and a summary of significant accounting policies and other explanatory notes.

Management's and the Board of Directors Responsibility for the Financial Statements

Management and the board is responsible for the preparation and fair presentation of this interim financial information in accordance with Icelandic Financial Statements Act, Act on Financial Undertakings and Rules on the Financial Statements of management companies of UCITS.

Auditor's Responsibility

Our responsibility is to express an conclusion on this interim financial information based on our review.

Scope of Review

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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not give a true and fair view of the financial position of the entity as at 30 June 2015 and of its financial performance and its change in net assets in the period, in accordance with Icelandic Financial Statements Act, Act on Financial Undertakings and Rules on the Financial Statements of management companies of UCITS.

Reykjavik, 27 August 2015

Deloitte ehf.



Pálína Árnadóttir

State Authorized Public Accountant



Pétur Hansson

State Authorized Public Accountant

Income Statement 1 January - 30 June 2015

	Notes	1.1. -30.06. 2015	1.1. -30.06. 2014
Financial income and (expenses)	4-6		
Interests, indexation, dividends and currency exchange rate difference		4.898	4.946
Interest expense		(3.603)	(3.640)
Reversal of impairment on loans	8	117	42
Net financial income		1.412	1.348
 Operating expenses			
Administration fee	7	74	83
Other operating expenses		5	2
		79	85
 Profit transferred to units		1.333	1.263

Balance Sheet at 30 June 2015

	Notes	1.1. - 30.06. 2015	1.1. - 31.12 2014
Assets			
Securities with fixed income	8	108.047	115.233
Total investments		<u>108.047</u>	<u>115.233</u>
Foreclosed assets	9	0	3
Cash	10	16.097	33.008
Other assets	11	194	0
Total other assets		<u>16.291</u>	<u>33.011</u>
Total assets		<u><u>124.338</u></u>	<u><u>148.244</u></u>
Liabilities			
Units	13	22.315	46.982
Loan from financial institutions	14	102.010	101.250
Liabilities with management- and custody company		13	12
Total other liabilities		<u>102.023</u>	<u>101.262</u>
Total liabilities		<u><u>124.338</u></u>	<u><u>148.244</u></u>
Net assets		22.315	46.982
Number of units		23.200	23.200
Exchange rate of units at the end of the period	13	<u>0,96</u>	<u>2,03</u>

Statement of Changes in Net Assets

1 January - 30 June 2015

	Notes	1.1. -30.06. 2015	1.1. -30.06. 2014
Operating activities			
Profit transferred to units		1.333	1.263
Financing activities			
Units sold		(26.000)	0
		(26.000)	0
Changes in net assets		(24.667)	1.263
Net assets at the beginning of the year		46.982	43.450
Net assets at the end of the period	13	22.315	44.713

Investment Statement 30 June 2015

	Market value	Asset 30.6.2015 %	Asset 31.12.2014 %	Asset Change %	Investment policy	
					Minimum %	Maximum %
Mortgages	108.047	100	100	0	0	100
Total assets	108.047	100	100	0		

Notes to the Financial Statements

Accounting methods

1. Basis of preparation

The purpose of the ABMIIF Fund is to invest in residential real estate loans from Arion Bank and its subsidiaries, in accordance with the terms of the issuance of Covered Bonds. And to guarantee the payment of all amounts due under any Covered Bonds issued by the Issuer under the Programme, subject to the term of the Covered Bond Guarantee.

2. Basis of preparation

The Interim Financial Statements of Arion Bank Mortgages Institutional Investor Fund have been prepared in accordance with the Financial Statements Act and rules on the Financial Statements of management companies of UCITS set by the Icelandic Financial Supervisory Authority. They are prepared on the historical cost basis and according to the same accounting methods as last year. The Interim Financial Statements have been prepared in Icelandic krónur (ISK) rounded to the nearest million. The fund is a part of Stefmir hf. which is a subsidiary of Arion Bank hf. The Interim Financial Statements form part of the consolidated Interim Financial Statements of Arion Bank hf.

3. Assessment and decisions

When preparing the financial statements, the management is required by the Annual Accounts Act to assess and make decisions on important components of the financial statements which are subjective by their nature. The assessment is based on experience and other relevant factors which are otherwise unavailable. Any changes according to this assessment are recognized during the period in which they occur.

4. Foreign currencies

Assets and liabilities in foreign currencies are translated into ISK at the exchange rate at the end of June 2015, according to Reuter. Operating income and operating expenses in foreign currencies are translated at the exchange rate on the date of transaction. Foreign exchange difference related to translation of foreign assets is recognised in the income statement.

5. Indexed assets and liabilities

Indexed assets and liabilities are calculated on basis of indexes valid in July 2015. Accrued indexation on principal of assets and liabilities is recognised in the income statement.

6. Interest income and expenses

Interest income and expense are recognised in the income statement as they are incurred.

7. Administration fee

The fund pays Stefmir hf. administration fee which includes the following operating costs for the fund: salaries of employees of the management company, marketing costs and administration; included in the administration fee is a custody fee to Arion banki hf. Administration fees are 0.1% of the fund's total assets.

The fund also pays fees for official supervisory.

8. Securities with fixed income

- a. Mortgages are recognised with accrued interest and indexation at the end of June 2015. At the of June 53,7% of the fund's mortgages were calculated according to the index for mortgage payment adjustment.
- b. Because of circumstances following the fall of the Icelandic commercial banks in the fall 2008, banks and other financial institutions have taken actions to meet customer's debt conditions. Arion bank hf. offered late in the year 2009 ways for customers to adjust the principal of their debt to 110% of property market value. Customers were able to apply for this special resort until the 30th of June 2011. Provisions are done by a general provision and a special provision. Total provision for losses amounts to ISK 247 million, which of specific provision amounts to ISK 138 million and collective provision amounts to ISK 109 million. The provision account has been deducted from Securities with fixed income in the Balance sheet.

Notes, contd.:

8. Securities with fixed income, cont.

c. Mortgages are specified as:	30.06.2015	31.12.2014
Mortgages before impairment	108.294	115.598
Provision at the beginning of the year	(364)	(1.435)
Write-offs during the period	2	3
Reversal during the period	115	1.067
Mortgages at the end of the period	108.047	115.233
Provision for losses as a ratio of total loans	0,23%	0,32%

9. Foreclosed assets

The fund has foreclosed real estate (residential property) following auctions of the relevant property to secure the fund's loans. These properties are valued by employees of Arion Bank. The valuation takes into account the condition and location of the property. The valuation is then reduced by 20% as a precautionary provision.

10. Cash

Cash consists of cash and deposits with credit institutions including accrued interests.

11. Other assets

Other assets include unsettled trades and deviations in exchange translations of assets.

12. Taxation

The fund does not pay income tax; instead profit or loss from operations are taxed with the unit holders. Individuals pay capital gains tax on profits on their securities when redeemed. Profit and loss on unit shares owned by companies are treated as taxable income and expenses, regardless of redemption.

The fund is exempt from capital gains tax in Iceland but not in those countries where capital gains tax is imposed on income of foreign residents and when no double taxation agreement stating that such income should be taxed in Iceland exists between Iceland and the relevant country.

13. Units

a. Real return of the mutual fund ABMIF as of 30 June 2015

	Return
Last 3 months	(0,36%)
Last 6 months	0,99%
Last 12 months	6,19%

b. Statement of book value and exchange rate of units.

	Book value	Exchange rate
30 June 2015	22.315	0,96
31 December 2014	46.982	2,03
31 December 2013	43.450	1,87

Notes, contd.:

14. Loan agreement

The fund and Arion Banki hf. made Subordinated Intercompany Loan Agreements to finance the acquisition of the mortgages. The loan agreements are calculated taking into account accrued interest and the consumer price index. Interest on the loan agreements ranges from 3.75% - 4.00% p.a.

The fund's interest-bearing liabilities are:

Indexed loan agreements	102.010
Repayments on loan agreements at the end of the period are as follows:	
Repayments 2015	1.828
Repayments 2016	2.019
Repayments 2017	2.096
Repayments 2018	2.176
Repayments 2019	2.259
Repayments later	91.632
	<u>102.010</u>

15. Segmentation of investments and proportional division

	Other ISK	%	Total ISK	%
Other financial instruments, mortgages	108.047	100	108.047	100
	<u>108.047</u>	<u>100</u>	<u>108.047</u>	<u>100</u>

In the case of any discrepancy between the English and the Icelandic texts, the Icelandic versions shall prevail and questions of interpretation will be addressed solely in the Icelandic language.