Housing Financing Fund
Condensed Interim
Financial Statements
30 June 2017

These Financial Statements are translated from the original statements which are in Icelandic. Should there be discrepancies between the two versions, the Icelandic version shall prevail.

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Contents

Endorsement and Statement by the Board of Directors and CEO

The Condensed Interim Financial Statements of the Housing Financing Fund for the period 1 January to 30 June 2017 have been prepared in accordance with the International Financial Reporting Standard IAS 34, Interim Financial Statements, and additional disclosure requirements for companies whose securities are listed on a regulated market.

Results during the period

According to the income statement, the Housing Financing Fund's operating surplus in the first six months of 2017 amounted to ISK 614 million. Equity at the end of the period amounted to ISK 24,142 million, and the equity ratio is 7.8%. The equity ratio of the Housing Financing Fund has not been higher since the establishment of the Fund in 1999, and the Fund's long-term objective pertaining to the equity ratio is 5% as according to Regulation no. 544/2004 on the financial and risk management of the Housing Financing Fund.

Operations during the period

Net interest income during the period amounted to ISK 532 million compared to ISK 525 million for the same period last year. Operating expenses for the period amounted to ISK 843 million, decreasing by 7% compared to the same period last year. Salaries and related expenses decrease by 22.2% and full-time equivalent positions decrease from 85 in the first half of 2016 to 70 during the period, despite the fact that the Fund has taken over new housing projects and assigned eight new employees to these projects. Other operating costs increase by 12.8%, mainly due to the increase in payments to the Debtors' Ombudsman. During the period, the Housing Financing Fund made payments amounting to ISK 184 million to the operations of other government agencies or the equivalent of 22% of the total operating expenses of the Fund. The streamlining measures undertaken in previous years are fully implemented.

The prospects for the Fund's ability to continue as a going concern for the foreseeable future are positive, although negative returns may be expected in the coming years due to the mismatch between assets and liabilities resulting from increased loan prepayments. The Fund, on the other hand, has sufficient equity in addition to accumulated liquid funds in order to meet the outstanding cash flows of outstanding debt in the foreseeable future. Increased prepayments have a negative effect on the Fund's long-term interest rate margin, since the Fund is not allowed to pay its debts (funding) before maturity. As the portion of funds outside of the loan portfolio increases due to prepayments of loans, the duration of the Fund's assets and liabilities becomes imbalanced which may in the future affect the Fund's performance. The assets and liabilities of the Fund are paid gradually as according to terms but have a lifetime to the year 2044 which is the final maturity date of debt. Assets outside the loan portfolio have been invested in asset-backed indexed bonds with similar terms to increase the balance between the liabilities and the assets of the Fund.

Funding

On 30 June, the Fund's loans amounted to ISK 543,982 million, decreasing by ISK 34,488 million between periods. The reduction in the loan portfolio is due to limited lending, prepayments, write-offs and the allocation of private pension savings. There has been no need for issuance of financing bonds during the period. Assets outside of the loan portfolio and including liquid assets increased between periods and amounted to ISK 217,319 million. The increase is primarily due to the sales of appropriated assets and prepayments of loans. The importance of treasury management has increased considerably as the long-term objective of the Fund is to minimize the imbalance of assets and liabilities. At the beginning of the year, the Board approved a new treasury management policy aimed at facilitating the investment of the Fund's assets as efficiently as possible taking into account the risks at any given time. The main challenges for managing assets outside of the loan portfolio are interest rate and inflation risk. In view of this, it is worth mentioning that the yield in the bond market has generally dropped in line with Central Bank interest rates. However, the yield on indexed bonds has fallen somewhat more and especially following the weakening of the krona recently. This entails more challenges in the management of funds outside of the loan portfolio. The Fund's treasury management policy is a rather risk-averse policy reflected in the Fund's investments. It may also be noted that in the first half of the year a new system was implemented that will support the day-to-day operations of treasury management.

Endorsement and Statement by the Board of Directors and CEO

Development of arrears and quality of loan portfolio

Favorable economic conditions and effective collection processes have reduced the risks of the loan portfolio. Loans in arrears have fallen sharply and the collateral position of loans improved significantly due to rising real estate prices in excess of inflation. Arrears now amount to 2,4% of total loans, but were 2,9% at the same time in 2016. The adjusted balance of all outstanding loans in arrears was ISK 13,600 million, of which the amount of arrears was ISK 3,027 million. The provision for the impairment of loans amounted to ISK 6,740 million, a decrease of the provision by ISK 740 million. At the end of June, funds invested in foreclosed properties amounted to ISK 8,948 million, decreasing by ISK 1,988 million as 159 properties were sold during the period. The book value of foreclosed properties at the end of the year was approximately 81% of the property value of the underlying asset portfolio. Since the beginning of the year, the Fund has repossessed 25 properties on foreclosed mortgages. Profits from sales of foreclosed assets exceeded the book value of the assets by ISK 370 million. The Fund owned 530 properties at the end of the period, of these 316 were rentals, 150 are listed for sale and 44 are vacant. Sales of appropriated properties will have a positive impact on the Fund's net interest income in the future as cash tied up in real estate is converted into interest-bearing assets.

Risk factors

The Housing Financing Fund is a non-profit organization and therefore has a low-risk appetite, the Fund's Board of Directors determining acceptable risks as permitted by law and regulations. The Housing Financing Fund faces various types of risks and risk management is an important and integral part of the Fund's operations. Due to improved economic conditions, the Fund's lending risk has decreased sharply as new lending and defaults on older lending decrease and collateral positions improve. At the same time, however, prepayments have been significant, and a considerable portion of assets outside of the loan portfolio is invested in non-indexed assets. Inflation risk has thus increased and the main focus of the Fund's Board is reducing this risk. The Fund's Board of Directors is ultimately responsible for risk management. It reviews the Fund's risk management strategy annually, setting out the objectives, authority and framework implemented in managing the Fund's financial and operational risks. The Risk Committee operates under the auspices of the Board, but in addition, there is effective risk management. Not less than four times a year, the Fund's Board of Directors receives reviews and reports on the Fund's risk and the implementation of risk management.

Social responsibility and role

The role of the Housing Financing Fund has been changing from being primarily a financing fund to being the institution responsible for the implementation of housing policies and the government's control mechanism in housing policy. These changes are due to changes in the legal environment of the Fund in 2012 and 2016, as the Fund's lending activities were limited and more emphasis was placed on the role of the Fund in public housing affairs. Subsequently, the Fund focuses more on its social role and formulated a new policy to the year 2020, which involves being the leader in policy formulation in the housing market and executing the housing policy of the government at any given time. The social responsibility of the Fund is reflected, inter alia, in its role as a safety guard in promoting security and equal rights for citizens in housing affairs. The Fund performs its role in a variety of ways including lending to individuals to purchase or build own housing, regardless of location and lending to municipalities, associations or non-profit companies for the purchase or construction of rental properties. In addition, the Fund is responsible for allocating state grants according to the Public Housing Act, which are intended to build a new rental system with small and efficient apartments intended for low-income individuals and families. The Housing Financing Fund has also cultivated its social responsibility by establishing a planning and analysis division that provides information on the basis of extensive analysis of the housing market, including housing needs in the country, supply and demand for housing, housing prices and rental rates. There have been numerous open meetings on housing in the Housing Financing Fund's premises in 2017, which have been the platform for information and exchange of views for government. Furthermore, the Fund's social responsibility includes the decision to invest its liquid assets in the most cost-effective manner to ensure the best continuing interest-bearing assets to meet the Fund's obligations and to spread the risks of these investments as much as possible.

Endorsement and Statement by the Board of Directors and CEO

Housing affairs

The Board of the Housing Financing Fund changed its organizational chart on 3 March 2017 by establishing a new division, the housing division responsible for the Fund's new projects regarding housing affairs. Today, there are eight employees in the division, the main projects being monitoring municipal housing plans, the implementation of capital contributions for the general rental system and analysis of the housing market. In June, the government's Housing Accord was signed to deal with the serious state of the housing market. The Housing Financing Fund is working on many of the Housing Accords' tasks with the government. When changing the role of the Housing Financing Fund and policy, consideration was given to placing more emphasis on ensuring housing security for the public and directing public housing support to disadvantaged groups for the purpose of meeting the objectives of Act No. 44/1998 on Housing, Act no. 52/2016 on public apartments, Act no. 75/2016 on housing benefits as well as the provisions of national housing agreements. In particular, it refers to the International Covenant on Economic, Social and Cultural Rights (SEFMR), but according to Art. 1.mgr.11.gr., the Treaty requires Iceland to take appropriate measures to ensure that every person's right to adequate housing is enforced.

Endorsement by the Board of Directors and CEO

To the best of our knowledge, it is our opinion that the Condensed Interim Financial Statements give a true and fair view of the comprehensive income of the Fund for the period 1 January to 30 June 2016, its assets, liabilities and financial position of the Fund as at 30 June 2017 and its cash flows for the period 1 January until 30 June 2017.

Further, in our opinion the Condensed Interim Financial Statements and the endorsement by the Board of Directors and the CEO give a fair view of the development and performance of the Fund´s operations and its financial position and fairly describes the principal risks and uncertainties faced by the Fund.

The Board of Directors and the CEO of the Housing Financing Fund have today discussed the Fund's Condensed Interim Financial Statements for the six-month period ended 30 June 2017 and confirm them by means of their signatures.

Reykjavik, 30 August, 2017

Board of Directors:

Sigurbjörn Ingimundarson
Chairman of the Board

G. Valdimar Valdemarsson

Drífa Snædal

Haukur Ingibergsson

Halldóra K. Hauksdóttir

CEO

Hermann Jónasson

Independent Auditors' Review Report

To the Board of Directors of the Housing Financing Fund,

We have reviewed the accompanying Condensed Interim Financial Statements of the Housing Financing Fund for the period of 1 January until 30 June 2017, which consist of the income statement and statement of comprehensive income, balance sheet,the statement of changes in equity, the statement of cash flows, and other explanatory notes. Management is responsible for the preparation and fair presentation of this interim financial information in accordance with IAS 34 "Interim Financial Reporting", as adopted by the European Union. Our responsibility is to express a conclusion on this Condensed Interim Financial Statement based on our review.

Scope of Review

We conducted our review in accordance with International Standard on Review Engagements 2410, on reviews of interim financial statements by independent auditors. 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 on the Condensed Interim Financial Statements.

Conclusion

Based on our review, nothing has come to our attention that suggests otherwise, but that the accompanying Condensed Interim Financial Statement give a true and fair view of the performance of the Fund for the period of 1 January to 30 June 2017, the financial position of the Fund as at 30 June 2017, and its cash flow for the period 1 January to 30 June 2017, in accordance with IAS 34 “Interim Financial Reporting”, as adopted by the European Union.

Reykjavik, 30 August 2017

Grant Thornton endurskoðun ehf.

J. Sturla Jónsson

Sturla Jónsson
State authorised public accountant

Davíð Arnar Einarsson

Davíð Arnar Einarsson
State authorised public accountant

Interim Income Statement and Statement of Comprehensive Income from 1 January to 30 June 2017

	Notes	2017 1.1.-30.6	2016 1.1.-30.6
Interest income		24.779.469	28.048.316
Interest expense		(24.247.182)	(27.523.280)
Net interest income	20	532.287	525.036
Other income	21	94.502	50.513
Total operating income		626.789	575.549
Salaries and salary-related expenses	22	415.075	533.352
Other operating expenses	23	389.067	345.004
Depreciation and amortisation	24	38.935	30.655
Total operating expenses		843.077	909.011
Net income of appropriated properties	25	83.260	46.809
Net operating income		(133.028)	(286.653)
Changes in value of loans and appropriated assets	19	747.133	1.369.491
Profit (loss) from continuing operations		614.105	1.082.838
Profit from discontinued operations, net of tax	27	0	1.427.190
Profit (loss) for the year and comprehensive loss		614.105	2.510.028

The notes on pages 11 to 20 are an integral part of these Interim Financial Statements.

Condensed Interim Financial Statements of the Housing Financing Fund 30 June 2017 7 Amounts in ISK thousand

Interim Balance Sheet as at 30 June 2017

	Notes	30.6.2017	31.12.2016
Assets			
Cash and cash equivalents	6	67.618.717	53.171.360
Loans to financial institutions	7	20.206	61.114
Marketable securities	8	12.529.906	10.840.424
Other securities	9	137.170.530	126.607.519
Receivable from State Treasury	10	6.063.846	6.000.881
Loans	11	543.982.153	578.470.587
Appropriated assets	12	8.948.455	10.936.362
Operating assets	13	154.607	107.779
Intangible assets	14	187.274	213.904
Other assets	15	647.957	468.001
Total assets		777.323.651	786.877.931
Liabilities			
Bond issues	16	749.599.795	759.485.766
Other borrowings	17	3.235.040	3.153.172
Other liabilities	18	346.870	711.146
Total liabilities		753.181.705	763.350.084
Equity			
Contributed capital		57.655.408	57.655.408
Accumulated deficit		(33.513.462)	(34.127.561)
Total equity	19	24.141.946	23.527.847
Total liabilities and equity		777.323.651	786.877.931

The notes on pages 11 to 20 are an integral part of these Interim Financial Statements.

Condensed Interim Financial Statements of the Housing Financing Fund 30 June 2017 8 Amounts in ISK thousand

Interim Statement of Changes in Equity from 1 January to 30 June 2017

Changes in equity from 1 January to 30 June 2017	**Contributed capital**	**Accumulated deficit**	**Equity Total**
Equity as at 1 January 2017	57.655.408	(34.127.561)	23.527.847
Profit for the period and comprehensive income	0	614.105	614.105
Equity as at 30 June 2016	57.655.408	(33.513.456)	24.141.946

Year 2016	**Contributed capital**	**Accumulated deficit**	**Equity Total**
Equity as at 1 January 2016	57.655.408	(38.384.314)	19.271.094
Profit for the year and comprehensive income	0	4.256.753	4.256.753
Equity as at 31 December 2016	57.655.408	(34.127.561)	23.527.847

Changes in equity from 1 January to 30 June 2016	**Contributed capital**	**Accumulated deficit**	**Equity Total**
Equity as at 1 January 2016	57.655.408	(38.384.314)	19.271.094
Profit for the period and comprehensive income	0	2.510.028	2.510.028
Equity as at 30 June 2016	57.655.408	(35.874.286)	21.781.122

The notes on pages 11 to 20 are an integral part of these Interim Financial Statements.

Amounts in ISK thousand

Interim Statement of Cash Flows from 1 January to 30 June 2017

	2017 1.1.-30.6.	2016 1.1.-30.6.
Cash flows from operating activities		
Profit (loss) for the year and comprehensive income (loss)	614.105	2.510.028
Adjusted for:		
Indexation on loans to banks and loans to customers	(5.726.962)	(10.657.867)
Indexation on borrowings	6.418.122	11.066.331
Depreciation and amortisation	38.935	30.655
Impairment	(993.628)	(1.369.491)
Profits from discontinued operations	0	(1.427.190)
Changes in operating assets and liabilities:		
Loans	39.793.469	44.112.153
Appropriated properties	3.959.411	8.342.643
Other assets	(91.067)	(533.374)
Other liabilities	(361.645)	(523.535)
Cash flows from operating activities	43.650.740	51.550.353
Cash flows from investing activities		
Assets for sale, change	0	(113.954)
Marketable securites, change	(95.938)	(5.080.328)
Claims on financial institutions, change	41.099	(7.432.931)
Other securities, change	(9.449.897)	(12.835.615)
Investment in operating assets and intangible assets	(52.192)	(30.605)
Cash flows to investing activities	(9.556.928)	(25.493.433)
Cash flows from financing activities		
Bond issues and other borrowings, repayments	(19.646.455)	(18.993.709)
Cash flows to financing activities	(19.646.455)	(18.993.709)
Net increase in cash and cash equivalents	14.447.357	7.063.211
Cash and cash equivalents at the beginning of the year	53.171.360	13.236.528
Cash and cash equivalents at the end of the period	67.618.717	20.299.739
Sale of subsidiary		10.101.000
Receivable from sale of subsidiary		(10.101.000)

The notes on pages 11 to 20 are an integral part of these Interim Financial Statements.

Condensed Interim Financial Statements of the Housing Financing Fund 30 June 2017 10 Amounts in ISK thousand

Notes to the Interim Financial Statement

General information

1. Reporting entity

The Housing Financing Fund ("the Fund") is domiciled in Iceland. The address of the Fund's registered office is Borgartún 21, Reykjavik. The Fund's objectives are to provide housing loans, loans for new constructions and property renovations in Iceland. The Housing Financing Fund is an independent institution owned by the State. The Fund operates in accordance with the Housing Act no. 44/1998 and appertains to a special management and the Minister of Welfare. The Housing Financing Fund is subject to supervision of the Financial Supervisory in Iceland in accordance with Act. 87/1998 on Official Supervision of Financial Activities. According to the law, the Icelandic State Treasury guaranties all of the Fund's financial obligations.

2. Basis of preparation

a. *Statement of compliance*

The Condensed Interim Financial Statements have been prepared in accordance with IAS 34 Interim Financial Reporting. They do not include all of the information required for full annual financial statements and should be read in conjunction with the Financial Statements of the Fund as at and for the year ended 31 December 2016.

The Condensed Interim Financial Statements of the Housing Financing Fund were approved by the Board of Directors on 31 August 2017.

b. *Basis of measurement*

The Condensed Interim Financial Statements have been prepared on the historical cost basis except for the following: trading securities are measured at fair value, appropriated properties are measured at the lower of cost or net fair value.

c. *Functional currency*

The Condensed Interim Financial Statements are prepared and presented in Icelandic krona (ISK), which is the Fund's functional currency. All financial amounts presented have been rounded to the nearest thousand unless otherwise stated.

d. *Uses of estimates and judgements*

The preparation of interim financial statements in conformity with the IFRS 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. The estimates and underlying assumptions are based on historical experience and various other factors that are believed to be reasonable at the reporting date, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised and the effect of the changes are entered in the periods that the changes are made and in subsequent periods if the change also affects those periods.

Information about significant areas of estimation uncertainty that have the most significant effect on the amounts recognised in the financial statements are described in the following notes:

- Impairment on loans, cf. note 11.
- Appropriated assets, cf. note 12.

3. Significant accounting policies

The accounting policies set out below have been consistently applied to all periods presented in these Condensed Interim Financial Statements. Revenues and expenses of the Fund are not recognised directly in other comprehensive income and the result for the year is therefore equal to comprehensive (loss) income.

Work is ongoing on the implementation of IFRS 9 which will take effect on 1 January 2018. The implementation of this new standard will lead to changes in the assessment of impairment of financial assets. The implementation is ongoing and the fund cannot at this moment estimate the impact to the funds financial position.

4. *Segment information*

A segment is a component of an entity that generates income and expenses that are directly attributable to the segment. Management assesses and evaluates the performance and financial results of the segment and distributes funds specifically to the segment. Financial information of the segment must be separable for operational purposes in order to be identified as a segment. The Fund identifies its operations as a single segment.

Notes, contd.:

5. Financial assets and liabilities

According to the International Financial Reporting Standard IAS 39 *Financial instruments: recognition and measurement,* financial assets and liabilities are divided into specific categories. The classification affects how the relevant financial instrument is measured. Those categories to which the Fund's financial assets and liabilities pertain and their basis of measurement are specified as follows:

- Trading assets and liabilities - are recognised at fair value.
- Loans and receivables - are recognised at amortised cost.
- Other financial liabilities - are recognised at amortised cost.

The following table shows to which group financial assets and liabilities of the Fund pertain and their fair value:

30 June 2017	Trading assets	Loans and receivables	Liabilities at amortised cost	Total carrying amount	Fair value
Assets:					
Cash and cash equivalents.......................		67.618.717		67.618.717	67.618.717
Loans to financial institutions....................		20.206		20.206	20.206
Marketable securities................................	12.529.906				12.529.906
Other securities...		137.170.530		137.170.530	141.186.817
Receivable from State Treasury................		6.389.012		6.389.012	6.063.846
Loans		544.006.195		544.006.195	624.174.950
Total financial assets.................................	12.529.906	755.204.660	0	755.204.660	851.594.442
Liabilities:					
Bond issues...			749.599.795	749.599.795	858.734.869
Other borrowings.......................................			3.235.040	3.235.040	3.235.040
Other liabilities...			346.870	346.870	346.870
Total financial liabilities..............................	0	0	753.181.705	753.181.705	862.316.779

31 December 2016	Trading assets	Loans and receivables	Liabilities at amortised cost	Total carrying amount	Fair value
Assets:					
Cash and cash equivalents.......................		53.171.360		53.171.360	53.171.360
Loans to financial institutions....................		61.114		61.114	61.114
Marketable securities................................	10.840.424	0		10.840.424	10.840.424
Other securities...		126.607.519		126.607.519	126.607.519
Receivable from State Treasury................		6.214.997		6.214.997	6.214.997
Loans		578.470.587		578.470.587	578.470.587
Total financial assets.................................	10.840.424	764.525.577	0	775.366.001	775.366.001
Liabilities:					
Bond issues...			759.485.766	759.485.766	835.671.985
Other borrowings.......................................			3.153.172	3.153.172	3.153.172
Other liabilities...			711.146	711.146	711.146
Total financial liabilities..............................	0	0	763.350.084	763.350.084	839.536.303

5. Financial assets and liabilities, contd.:

The fair value of loans is estimated by discounting the cash flows of the loan portfolio by using the yield of HFF bonds plus 1.0% spread. The spread reflects the cost of operating the loan portfolio and the credit risk and prepayment risk in the case of loans which do not contain prepayment options.

The fair value of HFF bonds is based on their market price at the end of the period. The fair value of Housing bonds is measured by discounting the cash flows by using the HFF interest plus 0.5% spread due to lesser liquidity compared to HFF bonds. The fair value of Housing Authority bonds is measured by discounting at the interest of HFF bonds plus 1.0% spread due to liquidity and prepayment risk of those bonds.

Treasury securities that are classified as trading assets are measured at fair value. Fair value is based on quoted prices in active markets for identical assets. Other treasury securities are measured at their yield at acquisition.

For other securities measured at their yield at acquisition fair value is their last qouted market price.

Amounts in ISK thousand

Notes, contd.:

5. Financial assets and liabilities, contd.

Fair value hierarchy

The following table shows the level in the hierarchy into which the fair value of financial assets and liabilities, carried at fair value in the Balance Sheet, are categorised.

The levels are as follows:

Level 1: Valuation technique is based on quoted prices in active markets for similar assets and liabilities.
Level 2: Valuation technique is not based on quoted prices in active markets (level 1) but on information that is observable for the asset or liability directly (quoted price) or indirectly (adjusted quoted price).
Level 3: Valuation technique is based on significant information other than market information.

30 June 2017	Level 1	Level 2	Level 3	Total
Assets:				
Treasury securities	12.529.906	0	0	12.529.906

31 December 2016	Level 1	Level 2	Level 3	Total
Assets:				
Treasury securities	10.840.424	0	0	10.840.424

6. Cash and cash equivalents and restricted cash

Cash and cash equivalents and restricted cash are specified as follows:

	30.6.2017	31.12.2016
Unrestricted cash in Central Bank	58.459.648	45.524.349
Unrestricted cash in financial institutions	9.159.069	7.647.011
Cash and cash equivalents total	67.618.717	53.171.360

7. Loans to financial institutions

Loans to financial institutions are specified as follows:

	30.6.2017	31.12.2016
Other claims	20.206	61.114
Loans to financial institutions total	20.206	61.114

8. Marketable securities

Marketable securities are specified as follows:

	30.6.2017	31.12.2016
Listed treasury bonds at fair value	12.529.906	10.840.424
Marketable securities total	12.529.906	10.840.424

9. Other securities

Other securities are specified as follows:

	30.6.2017	31.12.2016
Covered bonds	108.641.011	98.376.123
Treasury bonds measured at amortised cost	28.529.519	28.231.396
Other securities total	137.170.530	126.607.519

10. Receivable due from State Treasury

The receivable due from the State Treasury is comprised of two bonds, a bond amounting to ISK 4,785 million that is payable in one lump sum at year end of 2018, and a bond in the amount of ISK 1,279 million that is due on 1 January 2021.The bonds have however a permanent prepayment privilege favorable to the Treasury, in part or in full. Only interest payments on the bonds are collected during the loan period. The bonds are not transferable by the Housing Financing Fund.

Condensed Interim Financial Statements of the Housing Financing Fund 30 June 2017 13 Amounts in ISK thousand

Notes, contd.:

11. Loans:

Loans are specified as follows:

	30.6.2017	31.12.2016
Loans to individuals	406.846.550	443.574.174
Loans to legal entities	137.135.603	134.896.413
Total loans	543.982.153	578.470.587

Impairment on loans is specified as follows:

	30.6.2017	31.12.2016
Balance at the beginning of the year	7.480.198	16.148.682
Impairment loss (reversal)	(337.515)	(1.197.024)
Write-offs	(402.878)	(7.471.460)
Balance at the end of the period	6.739.805	7.480.198

Quality of loans

The following table shows the carrying amount of loans that are neither past due nor impaired, the carrying amount of loans that are past due and not impaired and the carrying amount of loans that are impaired.

	Loans to individuals		Loans to legal entities		Total	
	30.6.2017	31.12.2016	30.6.2017	31.12.2016	30.6.2017	31.12.2016
Neither past due nor impaired						
Total	383.452.779	411.832.428	104.569.971	90.295.115	488.022.751	502.127.543
General impairment	(642.904)	(684.721)	(141.904)	(117.964)	(784.809)	(802.685)
Carrying amount	382.809.875	411.147.707	104.428.067	90.177.151	487.237.942	501.324.858
Past due and not impaired						
31-60 days	9.014.534	11.227.280	0	316.239	9.014.534	11.543.519
61-90 days	3.237.018	4.289.716	0	0	3.237.018	4.289.716
Past due over 90 days	5.690.488	7.151.402	267.414	24.250	5.957.902	7.175.652
General impairment	(182.168)	(221.269)	(2.006)	(4.489)	(184.175)	(225.758)
Carrying amount	17.759.872	22.447.129	265.407	336.000	18.025.280	22.783.129
Impaired						
Total	7.732.421	12.233.542	36.757.331	48.580.813	44.489.752	60.814.355
Specific impairment	(1.455.618)	(2.254.204)	(4.315.203)	(4.197.551)	(5.770.821)	(6.451.755)
Carrying amount	6.276.803	9.979.338	32.442.128	44.383.262	38.718.931	54.362.600
Total loans	406.846.550	443.574.174	137.135.603	134.896.413	543.982.153	578.470.587
Impairment as proportion of loans	0,56%	0,71%	3,15%	3,10%	1,22%	1,28%

The following table shows an age analysis of total arrears on loans.

	Loans to individuals		Loans to legal entities		Total	
	30.6.2017	31.12.2016	30.6.2017	31.12.2016	30.6.2017	31.12.2016
Loans past due:						
31-60 days	104.282	133.393	6.259	9.539	110.540	142.932
61-90 days	58.723	75.432	5.579	9.355	64.301	84.787
Past due over 90 days	1.305.339	1.819.368	1.546.760	1.365.474	2.852.099	3.184.842
Total past due	1.468.344	2.028.193	1.558.598	1.384.368	3.026.941	3.412.561

Write-off on loans:

Loans are written off under the following two circumstances:

- Upon loss on the sale of apartments auctioned, when the sales value is lower than the valuation of the apartment, according to Article 57 of Act no. 90/1991 on forced sale

- Upon the approval of the Board of Housing Financing Fund of the discontinuance of a claim of "lost pledge" in accordance with Regulation no. 359/2010, on the treatment of the Housing Financing Fund's claims for which pledges have been lost

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Notes, contd.:

11. Loans:, contd.:

Impairment on loans is specified as follows:

	Individuals		Legal entities		
	Specific impairment	General impairment	Specific impairment	General impairment	Total 30.6.2017
30 June 2017					
Balance at					
the beginning of the year.........................	2.254.204	905.990	4.197.551	122.453	7.480.198
Impairment loss (reversal					0
of impairment loss).................................	(408.596)	(80.917)	130.540	21.458	(337.515)
Write-off...	(389.990)	0	(12.888)	0	(402.878)
Balance at year end..................................	1.455.618	825.073	4.315.203	143.911	6.739.805

	Individuals		Legal entities		
	Specific impairment	General impairment	Specific impairment	General impairment	Total 31.12.2016
31 December 2016					
Balance at					
the beginning of the year.........................	6.774.733	1.071.616	8.165.074	137.259	16.148.682
Impairment loss (reversal					
of impairment loss).................................	(2.044.176)	(165.626)	1.027.584	(14.806)	(1.197.024)
Write-off...	(2.476.353)	0	(4.995.107)	0	(7.471.460)
Balance at year end..................................	2.254.204	905.990	4.197.551	122.453	7.480.198

Obligations not recognised in the balance sheet:	30.6.2017	31.12.2016
Binding loan commitments at year-end..	18.687.012	8.654.000

12. Appropriated assets

The Fund owned 530 properties on 30 June 2017 (year-end 2016: 663). Total number of apprpriated properties managed by the Fund is specified as follows:

	30.6.2017	31.12.2016
Number of properties at the beginning of the year	663	1.348
Repossessed properties during the period	26	203
Properties sold during the period	(159)	(888)
Number of properties at the end of the period	530	663

Properties owned by the Fund are divided as follows by geographical area:	30.6.2017	31.12.2016
South and South West	116	147
Great Reykjavík area	97	112
South Iceland	99	119
West Iceland	71	98
East Iceland	65	82
North Iceland	50	61
Westfjords	32	44
Number of properties at the end of the period	530	663

At the end of the period, 150 properties of the 530 properties owned by the fund are in the sales process (2016: 342). 316 properties were rentals (2016; 372) or 59.7% of the total properties owned by the Fund on 30 June 2017 (2016: 47.2%).

Amounts in ISK thousand

Notes, contd.:

12. Appropriated assets, contd.:

Appropriated assets at the end of the period are measured at the lower of the cost or net fair value and are specified as follows:

30 June 2017	Number of properties	Official property value	Fair value	Carry amount
Rentals	316	7.103.770	6.566.584	5.903.699
In sales process	150	2.684.250	2.061.200	1.887.574
Empty	44	941.240	885.589	808.200
Other properties*	20	389.516	385.242	348.980
Total	530	11.118.776	9.898.615	8.948.454

* Abandoned, rent arrears or properties that have recently entered the portfolio and are being processed

31 December 2016				
Rentals	372	8.444.141	7.962.506	7.056.053
In sales process	226	3.882.738	3.088.287	2.800.543
Empty	46	943.250	790.329	752.208
Other properties*	19	383.390	387.166	327.558
Total	663	13.653.519	12.228.288	10.936.362

* Abandoned, rent arrears or properties that have recently entered the portfolio and are being processed

13. Operating assets:

Operating assets are specified as follows:

	Fixtures and equipment	Real estate	Total
Total Cost			
Balance at 1.1.2016	293.441	30.726	324.167
Additions during the period	51.551	0	51.551
Balance at 31.12.2016	344.992	30.726	375.718
Additions during the period	56.037	0	56.037
Balance at 30.6.2017	401.029	30.726	431.755
Depreciation			
Balance at 1.1.2016	216.895	7.694	224.589
Depreciation during the period	42.323	1.027	43.350
Balance at 31.12.2016	259.218	8.721	267.939
Depreciation during the period	8.697	513	9.210
Balance at 30.06.2017	267.915	9.234	277.149

	Fixtures and equipment	Real estate	Total
Carrying amount			
Balance at 1.1.2016	76.546	23.032	99.578
Balance at 31.12.2016	85.774	22.032	107.806
Balance at 30.6.2017	133.113	21.494	154.607

Property value of real estate on 30 June 2017 amounted to ISK 9.4 million (2016: ISK 9 million) and insurance value amounted to ISK 23.5 million (2016: ISK 22.6 million).

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Notes, contd.:

14. Intangible assets

Intangible assets are specified as follows:

	Software
Total Cost	
Balance at 1.1.2016	590.130
Additions during the period	68.493
Balance at 31.12.2016	658.623
Additions during the period	3.095
Balance at 30.6.2017	661.718
Amortisation	
Balance at 1.1.2015	389.292
Amortisation during the period	55.427
Balance at 31.12.2016	444.719
Amortisation during the period	29.725
Balance at 30.6.2017	474.444
Carrying amounts	
Balance at 1.1.2016	200.838
Balance at 31.12.2016	213.904
Balance at 30.6.2017	187.274

15. Other assets

Other assets are specified as follows:

	30.6.2017	31.12.2016
EIR 14 (bond)	88.328	94.091
State Treasury receivable	385.700	214.116
Accounts receivable	10.372	20.829
Other receivables	163.557	138.965
Total other assets	647.957	468.001

16. Bond issues

The Fund issues housing bonds in four HFF series. The name of each series indicates the maturity year of the series. The bond issues are all inflation-indexed annuity bonds with semi-annual payments. All HFF series carry 3.75% nominal interests. Housing bonds are inflation-indexed annuity bonds with four annual instalments and carry 4.75% - 6.00% nominal interests. Housing bonds are redeemable. Housing authority bonds are inflation-indexed annuity bonds with semi-annual payments and carry 2.70% nominal interests. The effective interest rate of the issued bonds is 4.31%.

Bond issues are specified as follows:

	30.6.2017	31.12.2016
HFF24 bond	126.116.363	132.367.155
HFF34 bond	206.833.309	208.672.805
HFF44 bond	385.162.827	384.947.757
Housing bonds (final maturity 2040)	13.842.936	14.401.929
Housing Authority bonds (final maturity 2038)	17.644.360	19.096.120
Bond issues total	749.599.795	759.485.766

17. Other borrowings

Other borrowings are specified as follows:

	30.6.2017	31.12.2016
Pension funds	120.157	376.887
Insurance fund	191.149	189.376
Redeemable	133.980	126.607
Unpaid due to purchase of loan portfolios	2.789.754	2.460.302
Other borrowings total	3.235.040	3.153.172

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Notes, contd.:

18. Other liabilities

Other liabilities are specified as follows:

	30.6.2017	31.12.2016
Treasury due to subsidized interest	0	243.286
Employee vacation obligation	77.770	70.954
Other liabilities	269.100	396.906
Other liabilities total	346.870	711.146

19. Equity and capital management

The Fund's long-term objective is to maintain an equity ratio over 5.0%. The calculation of the equity ratio is in accordance with international standards (Basel II). If the Fund's equity ratio falls below 4.0% the Fund's Board of Directors shall notify the Minister of Welfare thereof. Furthermore, the Fund's Board of Directors shall propose solutions to reach the long term equity ratio goal.

Equity ratio is specified as follows:

	30.6.2017	31.12.2016
Total equity according to the financial statements	24.141.946	23.527.847
Intangible assets	(187.274)	(213.904)
Equity base	23.954.672	23.313.943

Total equity requirement is specified as follows:

	30.6.2017	31.12.2016
Credit risk	23.388.327	25.159.555
Market risk	902.326	243.910
Operational risk	287.024	295.474
Total capital requirements	24.577.677	25.698.939
Equity ratio	7,80%	7,26%

20. Net interest income

Interest income

Interest income on items not at fair value:

	30.6.2017	30.6.2016
Interest income and indexation on loans to customers	18.831.092	22.841.965
Interest income from covered bonds	2.760.931	2.655.503
Interest income from other financial assets	2.458.767	1.828.211
Government contribution to subsidy interests*	303.820	315.567
Gov't contribution due to reduced interest margin related to debt solutions	92.457	279.676
	24.447.067	27.920.922
Interest income on items at fair value:		
Interest income (expenses) on market securities	332.402	127.394
	332.402	127.394
Total interest income	24.779.469	28.048.316

*The government contribution due to social benefit loans to municipalities and organisations, such as student associations and organisations of disabled and the reduced interest margin related to government debt solutions.

Interest expense on items not at fair value:	30.6.2017	30.6.2016
Interest expense and indexation on bonds issued	24.234.443	27.524.144
Interest expense on other borrowings	10.595	108.654
Other interest expense	2.144	(109.518)
Total interest expenses	24.247.182	27.523.280
Net interest income (expenses)	532.287	525.036

*Subsidy on interests on loans is due to social benefit loans to municipalities and organisations, such as student associations and organisations of disabled.

**The government contribution due to the reduced interest margin and the loss or prepayment premiums related to debt solutions.

Condensed Interim Financial Statements of the Housing Financing Fund 30 June 2017 18 Amounts in ISK thousand

Notes, contd.:

21. Other income

Other income is specified as follows:	30.6.2017	30.6.2016
Collection and service income*	93.866	45.111
Other income	636	5.402
	94.502	50.513

*The fund updated its terms of service as of 1 April 2017 increasing various fees. After these amendments the fees charged by the fund are comparable to those charged by other financial institutions.

22. Salaries and salary-related expenses

Salaries and salary-related expenses are specified as follows:	30.6.2017	30.6.2016
Salaries	321.083	380.933
Pension fund contributions	41.768	50.043
Tax on financial activity	19.693	21.058
Other salary-related expenses	37.239	64.314
Other personnel expenses	18.000	17.004
Reimbursed salary expenses	(22.708)	0
Total salaries and salary-related expenses	415.075	415.075

Number of employees at the Fund are specified as follows:	69	85

On June 30, 2017, there were 70 employees on the Fund's payroll of which 10 employees have completed their duties for the Fund.

Personnel expenses related to a new operating unit within the fund will be reimbursed by the State Treasury at year end.

23. Other operating expenses

Other operating expenses are specified as follows:	30.6.2017	30.6.2016
Collection fees	46.301	90.335
Operating expenses of housing	61.210	60.283
Operating cost of IT systems	85.479	99.124
Audit and review of financial statements	8.268	14.288
Professional services	47.394	41.914
Cost due to implementation of IFRS 9	6.119	0
Real estate valuation	2.882	5.472
Advertising, promotional material and grants	11.326	18.879
Debtors' Ombudsman	27.331	(52.345)
Financial Supervisory Authority	46.107	36.560
Service fees	13.012	14.312
Other operating expenses	33.638	16.182
Total other operating expenses	389.067	345.004

24. Depreciation and amortisation during the period:

Depreciation and amortisation is specified as follows:	30.6.2017	30.6.2016
Depreciation of operating assets (cf. note 13)	9.210	7.248
Amortisation of intangible assets (cf. note 14)	29.725	23.407
Total depreciation and amortisation	38.935	30.655

25. Net income of properties held for sale

Net income of properties held for sale is specified as follows:	30.6.2017	30.06.2016
Rental income from rented properties	283.050	436.350
Cost of properties held for sale	(199.790)	(389.541)
Net income of properties held for sale	83.260	46.809

The costs of real estate held for sale in the table above include only the direct incurred costs of the properties cf. property taxes, insurance, maintenance, energy costs and commissions of administrators but exclude indirect operating costs such as salaries.

Amounts in ISK thousand

Notes, contd.:

26. Impairment

Total impairment recognised in the income statement is specified as follows:

	30.6.2017	30.6.2016
Specific impairment loss on loans (reversal of impairment loss)	(280.304)	(736.205)
General impairment loss on loans (reversal of impairment loss)	(59.459)	(41.361)
Impairment loss on loans (reversal of impairment loss)	(339.763)	(777.566)
Impairment loss on appropriated properties (reversal of impairment)	(436.547)	(611.460)
Impairment on other receivables (reversal of impairment loss)	29.177	19.535
Total impairment cost (reversal of impairment cost)	(747.133)	(1.369.491)

27. Profit (loss) of discontinued operations, net of tax

Profit (loss) of discontinued operations, net of tax is as follows:

	30.6.2017	30.6.2016
Rental income	0	274.310
Operating expenses of investment properties	0	(100.774)
Operating expenses	0	(40.970)
Valuation adjustment of investment properties	0	741.257
Net financial expenses	0	(129.419)
Income tax	0	(148.881)
Profit(loss) net of tax of subsidiary's operations	0	595.523
Gains from sale of rental company	0	831.667
Profit(loss) of discontinued operations, net of tax and cost of sale	0	1.427.190

*Operations of Leigufélagið Klettur ehf. are included in the interim financial statements until the end of May 2016.

28. Rental agreements

The Fund has entered into an operating lease agreement on the property used in its operations. Minimum lease payments are specified as follows at the end of the period:

	30.6.2017	30.6.2016
Payable within 1 year	108.493	112.429
Payable after 1 to 5 years	232.499	183.319
Total	340.992	295.748

29. Related parties

The Fund has a related party relationship with its owner, board members, executive officers and its subsidiary. The Housing Financing Fund is publically owned and administratively falls under the Ministry and Minister of Welfare. Government institutions and self-governing corporate entities that are financially dependent on the authorities are related parties of the Fund. Loans to related parties are granted on arms-length basis. There were no mortgage loans to related parties outstanding on 30 June 2017 (2016: ISK 0.5 million).

Related party transactions:

	30.6.2017 Interest income	30.6.2017 Claims	30.6.2016 Interest income	31.12.2016 Claims
Leigufélagið Klettur ehf.	0	0	134.684	0

Related party transactions are made on terms equivalent to those that prevail in arm's length transactions.

30. Other matters

The Fund is a party to several disputes that are currently before the courts. The disputes vary in nature, such as appeals related to debt remedies, damages due to forced sales and sales of appropriated assets, disputes regarding penalty interests, disputes on the settlements of forced sales due to usufruct fees, etc. It is the Fund's opinion however, that these cases, both individually and combined are not likely to have a significant financial impact on the Fund.

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