MP Investment Bank hf.

Consolidated Financial Statements
for the year 2007
ISK

MP Investment Bank hf.
Skipholt 50d
105 Reykjavík
Iceland

Reg. no. 540599-2469

Contents

Endorsements and Statement by the Board of Directors and the CEO

The Consolidated Financial Statements of MP Investment Bank hf. for the year ended 31 December 2007 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and additional disclosure requirements applicable. These are the Bank's first Annual Consolidated Financial Statements where IFRS 1 has been applied. The Consolidated Financial Statements comprise MP Investment Bank hf. and its subsidiaries (together referred to as the "Bank").

According to the income statement, after tax profits for the year amounted to ISK 1,780 million. The Bank's equity at the end of 2007 amounted to ISK 6,187 million. The Bank's capital adequacy ratio, calculated in accordance with the Act on Financial Undertakings, was 28.1% at year-end. As of 31 December 2007 the Bank's total assets amounted to ISK 52,529 million.

The Board of Directors proposes that a dividend of 30% will be paid in the year 2008 on 2007 operations.

The Bank's share capital amounted to ISK 1,100 million at the end of the year 2007, and it was increased by ISK 30 million during the year against employees' share purchase program. The sales price of the share capital amounted to ISK 91 million. Own shares amounted to ISK 36 million at year-end 2007. Four shareholders held more than 10.0% of the shares in the Bank at year-end 2007. Their shareholding is specified as follows:

	Ownership
Margeir Pétursson and companies under his control	28.4%
BYR Sparisjóður (Savings Bank)	13.1%
Sigurður Gísli Pálmason and company under his control	11.9%
Jón Pálmason and company under his control	11.9%

To the best of our knowledge, the Consolidated Financial Statements of MP Investment Bank hf. for the year 2007 give a true and fair view of the assets, liabilities, financial position and financial performance of the Bank. Further, in our opinion the consolidated financial statements and the endorsement of the Board of Directors and the Chief Executive Officer gives a fair view of the development and performance of the Bank's operations and its position and describes the principal risks and uncertainties faced by the Bank.

The Board of Directors and the CEO of the Bank have today discussed the annual consolidated financial statements of MP Investment Bank hf. for the year 2007 and confirm them by the means of their signatures.

Reykjavík, 6 March 2008

The Board of Directors:

Margeir Pétursson, Chairman of the Board of Directors
Ágúst Sindri Karlsson
Sigfús Ingimundarson
Sigurður Gísli Pálmason
Örn Andrésson

CEO:

Styrmir Þór Bragason

Independent Auditor's Report

To the Board of Directors and Shareholders of MP Investment Bank hf.

We have audited the accompanying consolidated financial statements of MP Investment Bank hf. and its subsidiaries, (the "Bank"), which comprise the consolidated balance sheet as at December 31, 2007, and the consolidated income statement, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of MP Investment Bank hf. as at 31 December 2007, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted the EU.

Reykjavík, 6 March 2008.

KPMG hf.

Jón S. Helgason

Consolidated Income Statement
for the year 2007

	Notes	2007	2006
Interest income		4,968,499	2,384,349
Interest expense		(4,189,400)	(2,355,485)
Net interest income	35	779,099	28,864
Fee and commission income		1,600,755	1,051,566
Fee and commission expense		(72,558)	(38,336)
Net fee and commission income		1,528,197	1,013,230
Net income from financial instruments at fair value		158,982	1,059,251
Share of profit of associates	50	686,325	37,023
Other operating income	38	7,712	157
		853,019	1,096,431
Operating income		3,160,316	2,138,525
Salaries and related expenses	40	(502,738)	(337,437)
Other operating expenses		(382,511)	(165,841)
Depreciation	51	(16,898)	(3,458)
Impairment on loans		(8,467)	(101,106)
Profit before income tax		2,249,701	1,530,683
Income tax expense	43	(469,629)	(290,562)
Profit for the year		1,780,072	1,240,121

Notes on pages 10 to 47 are an integral part of these consolidated financial statements.

Amounts are in ISK thousands

Consolidated Balance Sheet
as at 31 December 2007

	Notes	2007	2006
Assets			
Cash and cash equivalents	45	7,241,857	2,157,724
Derivatives		1,380,422	536,621
Financial assets at fair value through profit and loss	46	20,659,461	13,410,153
Securities used for hedging	47	10,418,582	15,892,205
Available-for-sale financial assets		0	690,277
Loans	48	9,599,516	7,935,503
Receivables and prepayments	49	1,627,276	1,580,110
Investment in associates	50	1,205,627	285,976
Operating assets	51	415,937	168,104
Deferred tax asset		0	17,044
Total assets		52,548,678	42,673,717
Liabilities			
Deposits from credit institutions and the Central Bank	52	13,450,667	7,733,282
Derivatives		273,988	972,752
Financial liabilities at fair value through profit and loss		5,709,533	2,601,475
Borrowings	53	7,476,824	11,675,554
Debt securities issued		16,361,050	11,191,768
Subordinated liabilities	54	43,846	58,437
Deferred tax liabilities	55	193,863	0
Other liabilities	56	2,851,821	3,672,126
Total liabilities		46,361,592	37,905,394
Equity			
Share capital		1,063,776	1,064,000
Share premium		942,368	1,164,875
Option reserve		(37,496)	(158,323)
Translation reserve		(1,923)	0
Fair value reserve		0	94,338
Retained earnings		4,220,361	2,603,433
Total equity		6,187,086	4,768,323
Total liabilities and equity		52,548,678	42,673,717

Notes on pages 10 to 47 are an integral part of these consolidated financial statements.

Amounts are in ISK thousands

Consolidated Statement of Changes in Equity
for the year 2007

	Share Capital	Share premium	Revaluation reserve	Translation reserve	Option reserve	Fair value reserve	Retained earnings	**Total**
2006								
Equity as at 31.12.2005 (IS-GAAP)	1,000,000	723,315	47,339	34	0	0	1,576,479	3,347,167
Changes due to IFRSs			(47,339)	(34)	30,653	0	(61,559)	(78,279)
Equity as at 1.1.2006 (IFRSs)	1,000,000	723,315	0	0	30,653	0	1,514,920	3,268,888
Profit for the year							1,240,121	1,240,121
Options					(188,976)			(188,976)
Fair value reserve transferred to P&L						94,338		94,338
Paid in new capital	70,000	494,960						564,960
Own shares, changes	(6,000)	(53,400)						(59,400)
Dividends paid							(151,608)	(151,608)
Equity as at 31.12.2006 (IFRSs)	1,064,000	1,164,875	0	0	(158,323)	94,338	2,603,433	4,768,323
2007								
Equity as at 31.12.2006 (IS-GAAP)	1,070,000	1,218,275	46,391	792	0	0	2,741,827	5,077,285
Changes due to IFRSs	(6,000)	(53,400)	(46,391)	(792)	(158,323)	94,338	(138,394)	(308,962)
Equity as at 1.1.2007 (IFRSs)	1,064,000	1,164,875	0	0	(158,323)	94,338	2,603,433	4,768,323
Profit for the year							1,780,072	1,780,072
Options					120,827		29,431	150,258
Fair value reserve transferred to P&L						(94,338)		(94,338)
Own shares, changes	(30,224)	(284,007)						(314,231)
Translation reserve				(1,923)				(1,923)
Paid in new capital	30,000	61,500						91,500
Dividends paid							(192,575)	(192,575)
Equity as at 31.12.2007 (IFRSs)	1,063,776	942,368	0	(1,923)	(37,496)	0	4,220,361	6,187,086

Notes on pages 10 to 47 are an integral part of these consolidated financial statements.

Amounts are in ISK thousands

Consolidated Statement of Cash Flows
for the Year 2007

	Notes	2007	2006
Cash flows from operating activities			
Profit before income tax		1,780,072	1,240,121
Adjustments for:			
Indexation and exchange rate difference		240,321	710,796
Share of profit of associates	50	(686,325)	8,473
Depreciation	51	16,898	3,458
Provision for losses	33	8,467	101,106
Deferred income tax, change		(176,819)	(37,776)
		1,182,614	2,026,178
Change in operating assets and liabilities		(47,694)	(60,356)
Net cash from operating activities		1,134,920	1,965,822
Cash flows from investing activities			
Deposits with credit institutions, change		(1,812,801)	(3,937,783)
Other financial assets, change		(1,929,209)	(10,536,175)
Investment in shares in associated company		(233,326)	(147,000)
Investment in operating assets	51	(264,731)	(49,870)
Sundry assets, change		(340,321)	(573,126)
Net cash used in investing activities		(4,580,388)	(15,243,954)
Cash flows from financing activities			
Amounts owed to credit institutions, change		5,800,665	6,555,084
Borrowings and debt issued change		870,552	5,306,574
Other financial liabilities, change		2,287,753	2,545,622
Subordinated loans, change		(14,591)	(14,195)
Dividends paid		(192,575)	(151,608)
Share capital purchased and sold		(222,731)	564,960
Net cash from financing activities		8,529,073	14,806,437
Net increase in cash and cash equivalents		5,083,605	1,528,305
Effect of exchange rate fluctuations on cash held		528	758
Cash and cash equivalents at beginning of the year		2,157,724	628,661
Cash and cash equivalents at 31 December		7,241,857	2,157,724
Other information:			
Income tax paid		132,208	35,965

Notes on pages 10 to 47 are an integral part of these consolidated financial statements.

Amounts are in ISK thousands

Notes

General information

1. Reporting entity

MP Investment Bank hf. is a company incorporated and domiciled in Iceland. The Consolidated Financial Statements for the year comprise MP Investment Bank hf. (the parent) and its subsidiaries (together referred to as the "Bank") and the Group´s interest in associates. The address of the Bank is Skipholt 50d in Reykjavík. The Company has offices in Reykjavík and Vilnius. The office in Vilnius was opened during the year 2007.

MP Investment Bank's main purpose is to offer banking services to individuals, corporates, and institutional investors. The Bank offers services in areas of brokerage services, capital market services, asset management services and fund management.

2. Basis of preparation

Assets and liabilities in the balance sheet are presented in liquidity order which is considered more appropriate for the Bank than the current/non-current presentation. For each asset and liability item that combines amount expected to be recovered or settled after more 12 months, a payment schedule is disclosed.

a. Statement of compliance

The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRSs), as adopted by the European Union. These are the Bank's first consolidated financial statements prepared according to IFRSs and IFRS 1, *First-time Adoption of International Financial Reporting Standards* , has been applied.

An explanation of how the transition to IFRSs has affected the reported financial position and financial performance of the Group is provided in note 60. In the note, the changes in equity's comparative figures and the Bank's results as they were disclosed according to Icelandic GAAP for the year 2006 and as they are according to IFRS, are explained.

The Consolidated Financial Statements were approved by the Board of Directors and the CEO on 6 March 2008.

b. Basis of measurement

The Consolidated Financial Statements are prepared on the historical cost basis except for the following:

- derivative financial instruments are measured at fair value
- financial instruments at fair value through profit or loss are measured at fair value
- securities used for hedging are measured at fair value
- available-for-sale financial assets are measured at fair value

c. Functional and presentation currency

These Consolidated Financial Statements are prepared and presented in Icelandic krona (ISK), which is the Parent company´s functional currency. Except as indicated, financial information has been rounded to the nearest thousand.

d. **Use of estimates and judgements**

The preparation of the Consolidated Financial Statements in conformity with IFRSs requires management to make judgements, estimates and assumptions, which affect the application of accounting policies and the reported amounts of assets and liabilities as well as income and expenses. The estimates and underlying assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, 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.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Information about areas of estimation uncertainty and judgements made by management in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is provided in note 31.

Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these Consolidated Financial Statements, and have been applied consistently by the Bank's entities. They have also been used for the preparation of the opening IFRS balance sheet at 1 January 2006 for the purpose of adopting IFRS.

3. **Basis of consolidation**

a. *Subsidiaries*

Subsidiaries are entities controlled by the Bank. Control exists when the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Control usually exists when the Bank holds more than 50% of the voting power of the subsidiary. In assessing control, potential voting rights that are currently exercisable or convertible, if any, are taken into account. The Financial Statements of subsidiaries are included in the Consolidated Financial Statements from the date that control commences until the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Bank. The cost of an acquisition is measured as the fair value, at the date of exchange, of the assets given, liabilities incurred or assumed and equity instruments issued, plus cost directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Bank's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised immediately in the income statement.

b. *Funds management*

The Bank manages and administers assets held in mutual funds on behalf of investors. The Financial Statements of these funds are not included in these Consolidated Financial Statements.

c. *Transactions eliminated on consolidation*

Intra-bank balances, unrealised gains and losses or income and expenses arising from intra-bank transactions, are eliminated in the Consolidated Financial Statements. Unrealised gains arising from transactions with equity accounted investees and associates are eliminated against the investment to the extent of the Bank's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

4. Associates

Associates are those entities in which the Bank has significant influence but not control over the financial and operating policies. Significant influence generally exists when the Bank holds between 20% and 50% of the voting power, including potential voting rights, if any. Investments in associates are initially recognised at cost.

The Consolidated Financial Statements include the Bank's share of the total recognised gains and losses of associates on an equity accounted basis, from the date the significant influence commences until the date it ceases. When the Bank's share of loss exceeds its interest in an associate, the Bank's carrying amount is reduced to zero and recognition of further losses is discontinued except to the extent that the Bank has incurred legal or constructive obligations or made payments on behalf of the associate. If the associate subsequently reports profits, the investor resumes recognising its share of those profits only after its share of the profits equals the share of losses not recognised.

5. Foreign currency

a. *Functional currencies*

Items included in the Financial Statements of each of the Bank's entities are measured using the functional currency of the respective entity.

b. *Foreign currency transactions*

Transactions in foreign currencies are translated into functional currencies at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the Balance Sheet date are translated to Icelandic krona (ISK) at the foreign exchange rate ruling at the reporting date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated at foreign exchange rates ruling at the dates the fair value was determined.

c. *Foreign operations*

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to the presentation currency, Icelandic krona, at foreign exchange rates current at the Balance Sheet date. The revenues and expenses of foreign operations are translated to Icelandic krona at the foreign exchange rates at the dates of the transactions.

Foreign exchange differences arising on translation are recognised directly in a separate component of equity.

6. **Interest income and expense**

Interest income and expense on financial assets and liabilities not at fair value are recognised in the income statement using the effective interest method. Interest income and expense on those financial instruments includes the amortisation of any discount or premium or other differences between the initial carrying amount of the financial assets and liabilities and its maturity amount, calculated using the effective interest method.

The effective interest rate is the rate that exactly discounts estimated future cash flows through the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. The effective interest rate is established on initial recognition of the financial asset and liability and is not revised subsequently. When calculating the effective interest rate, the Bank estimates the cash flows considering all contractual terms of the financial instrument, but it does not consider future losses.

Once a financial asset or a group of similar financial assets has been written down as a result of impairment loss, interest income is recognised at the rate of interest used for the purpose of calculating the impairment loss. Interest income on financial assets which have been written down as a result of impairment is calculated based on their net carrying amount.

Interest income and expenses presented in the income statement comprise of:

• Interest income and expense on financial assets and liabilities at amortised cost on an effective interest rate basis;
• Interest income on available-for-sale investment securities on an effective interest rate basis;
• Fair value changes of derivative assets and liabilities attributable to interest income and expense and foreign exchange difference on an accrual basis;
• Fair value changes of financial assets and liabilities at fair value through profit and loss attributable to interest income and expense and foreign exchange difference on an accrual basis.

7. **Fee and commission income and expense**

The Bank provides various services to its clients and earns income there from, such as income from transactions on behalf of third parties, commission from customers for equity and bond transactions and other services. Fees and commission income are recognised in the income statement as the services are provided. Fees that are performance-linked are recognised when the performance criteria are fulfilled.

Fees and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

8. **Dividend income**

Dividend income is recognised in the income statement on the date that the dividend is declared.

9. **Net income from financial instruments at fair value**

Net income from financial instruments at fair value relates to derivatives, financial assets and liabilities at fair value through profit and loss and securities used for hedging. It includes dividends and all realised and unrealised fair value changes except for interest income and expense and foreign exchange difference which are included in interest income and expense.

10. Impairment

The carrying amount of the Bank's financial assets not at fair value through profit and loss, is reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment is recognised in the income statement whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

a. *Impairment on loans*

Two methods are used to calculate impairment losses, one based on an assessment of individual loans and the other based on a collective assessment. Losses expected as a result of future events, no matter how likely, are not recognised.

Objective evidence of impairment includes information about the following events and conditions:

(i) significant financial difficulty of the borrower;
(ii) a breach of contract, such as a default on installments or on interest or principal payments;
(iii) the Bank granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a refinancing concession, that the lender would not otherwise consider;
(iv) it becomes probable that the borrower will enter bankruptcy or undergo other financial reorganisation;
(v) the disappearance of an active market for that financial asset because of financial difficulties; or
(vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of loans, even if the decrease cannot yet be identified with the individual financial assets in the group, including:

- adverse changes in the payment status of borrowers in the group; or
- general national or local economic conditions connected with the assets in the group.

Individually assessed loans

Impairment losses on individually assessed loans are determined by an evaluation of the exposures on a case-by-case basis. The Bank assesses at each balance sheet date whether there is any objective evidence that individual loans are impaired. This procedure is applied to all loans that are considered individually significant. In making the assessment, the following factors are considered:

- the Bank's aggregate exposure to the customer;
- the amount and timing of expected receipts and recoveries;
- the likely dividend available on liquidation or bankruptcy;
- the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
- the realisable value of security (or other credit mitigants) and likelihood of successful repossession; and
- the likely deduction of any costs involved in recovery of amounts outstanding.

Impairment loss is calculated by comparing the carrying amount of individual loans with the present value of their expected future cash flows, discounted at their original effective interest rate. In the case of loans at variable interest rates, the discount rate used is their current effective interest rate. The carrying amount of impaired loans is reduced through the use of an allowance account.

10. contd.:

Collectively assessed loans

Where loans have been individually assessed and no evidence of loss has been identified, these loans are grouped together on the basis of similar credit risk characteristics for the purpose of calculating a collective impairment loss. This loss covers loans that are impaired at the balance sheet date but which will not be individually identified as such until some time in the future.

The collective impairment loss is determined after taking into account:
- future cash flows in a group of loans evaluated for impairment are estimated on the basis of the contractual cash flows of the assets;
- historical loss experience in portfolios of similar risk characteristics (for example, by industry sector, loan grade or product);
- the estimated period between a loss occurring and that loss being identified and evidenced by the establishment of an allowance against the loss on an individual loan;
- management's experienced judgement as to whether the current economic and credit conditions are such that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience.

Estimates of changes in future cash flows for groups of assets are consistent with changes in observable data from period to period, for example changes in property prices, payment status, or other factors indicative of changes in the probability of losses on the group and their magnitude. The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to minimise any differences between loss estimates and actual losses.

Loan write-offs

Loans are written off, partially or in full, when there is no realistic prospect of recovery.

b. *Impairment on available-for-sale financial assets*

Impairment losses on available-for-sale investment securities are recognised by transferring the difference between the amortised acquistion cost and current fair value out of equity to profit or loss.

Reversal of impairment

If, in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is recognised as revenue in the income statement. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised directly in equity. Changes in impaiment provisions attributable to time value are reflected as a component of interest income.

c. *Calculation of recoverable amount*

The recoverable amount of the Bank's investments in financial assets carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate.

The recoverable amount of other assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

11. **Income tax expense**

Income tax expense is recognised in the income statement, except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

The deferred income tax liability has been calculated and recognised in the balance sheet. The calculation is based on the difference between balance sheet items as presented in the tax return on one hand, and in the Consolidated Financial Statements on the other, taking into consideration tax losses carried forward. This difference is due to the fact that the tax assessment is based on premises that differ from those governing the Consolidated Financial Statements, mostly due to temporary differences arising from the recognition of revenues and expenses in the tax returns and in the Consolidated Financial Statements.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefit will be realised.

12. **Cash and cash equivalents**

Cash and cash equivalents consist of cash, balances with banks and unrestricted balances with the Central Bank as well as restricted balances with other banks.

13. **Derivatives**

Derivative is a financial instrument or other contract within the scope of IAS 39, the value of which changes in response to a change in an underlying variable (such as share, commodity or bond prices, an index value or an exchange or interest rate), which requires no initial net investment or initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors and which is settled at a future date.

The Bank uses derivatives for trading purposes and to hedge its exposure to market price risk, foreign exchange risk and interest risk arising from operating, financing and investing activities. The Bank does not apply hedge accounting.

Derivative assets and liabilities are initially recognised and subsequently measured at fair value in the balance sheet. Fair value changes of derviatives are split into interest income and net income from financial instruments at fair value and presented in the corresponding line items in the income statement.

Derivatives may be embedded in another contractual arrangement (a "host contract"). The Bank accounts for embedded derivatives separately from the host contract when the host contract is not itself carried at fair value through profit or loss, and the characteristics of the embedded derivatives are not clearly and closely related to the host contract. Separated embedded derivatives are accounted for in the same way as free-standing derivatives.

14. **Financial assets and liabilities at fair value through profit and loss**

Financial assets and liabilities at fair value through profit and loss consist of financial assets and liabilities relating to the Bank's trading activities as well as financial assets that the Bank designates as at fair value through profit and loss upon initial recognition.

15. Securities used for hedging

Securities used for hedging consist of non-derivative financial assets that are used to hedge the Bank's risk exposure arising from derivative contracts with customers.

16. Loans

Loans are non-derivative financial instruments with fixed or determinable payments that are not quoted in an active market, other than those that the Bank designates upon initial recognition as at fair value. Loans and advances include loans provided by the Bank to its customers, participation in loans from other lenders and purchased loans that are not quoted in an active market and which the Bank has no intention of selling immediately or in the near future.

When the Bank purchases a financial asset and simultaneously enters into an agreement to resell the asset (or a substantially similar asset) at a fixed price on a future date ("reverse repo or stock borrowing"), the arrangement is accounted for as a loan or advance, and the underlying asset is not recognised in the Bank's financial statements.

Loans are initially recognised at fair value, which is the cash advanced, plus any transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in the carrying amount of the loans and advances.

17. Financial assets measured at fair value

a. *Fair value designated as at fair value through profit or loss*

The Bank classifies certain financial assets upon their initial recognition as financial assets held at fair value with fair value changes recognised in profit and loss if doing so results in more relevent information.

b. *Financial assets available-for-sale*

Financial assets available-for-sale consists of investments in companies and bonds held for long term investments purposes.

Available-for-sale investments are non-derivative investments that are not designated as another category of financial assets. Unquoted equity securities whose fair value cannot be reliably measured are carried at cost. All other available-for-sale investments are carried at fair value.

Interest income is recognised in profit or loss using the effective interest method. Dividend income is recognised in profit or loss when the Bank becomes entitled to the dividend.

Other fair value changes are recognised directly in equity until the investment is sold or impaired and the balance in equity is recognised in profit or loss.

18. Fair value measurement of financial assets and financial liabilities

The determination of fair value of financial assets and financial liabilities that are quoted in an active market is based on quoted prices. For all other financial instruments fair value is determined by using valuation techniques. A market is considered active if quoted prices are readily and regularly available and those prices represent actual and regularly occurring market transactions on an arm's length basis. For all other financial instruments fair value is determined by using valuation techniques.

18. contd.:

Valuation techniques include recent arm's length transactions between knowledgeable, willing parties, if available, reference to the current fair value of other instruments that are substantially the same, the discounted cash flow analysis and option pricing models. Valuation techniques incorporate all factors that market participants would consider in setting a price and are consistent with accepted methodologies for pricing financial instruments. Periodically, the Bank calibrates the valuation technique and tests it for validity using prices from any observable current market transactions in the same instrument, without modification or repackaging, or based on any available observable market data.

For more complex instruments, the Bank uses proprietary models, which usually are developed from recognised valuation models. Some or all of the inputs into these models may not be market observable, and are derived from market prices or rates or are estimated based on assumptions. When entering into a transaction, the financial instrument is recognised initially at the transaction price, which is the best indicator of fair value, although the value obtained from the valuation model may differ from the transaction price. This initial difference, usually an increase, in fair value indicated by valuation techniques is recognised in income depending upon the individual facts and circumstances of each transaction and not later than when the market data becomes observable.

The value produced by a model or other valuation technique is adjusted to allow for a number of factors as appropriate, because valuation techniques cannot appropriately reflect all factors market participants take into account when entering into a transaction. Valuation adjustments are recorded to allow for model risks, bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments carried at fair value on the balance sheet.

19. Recognition and derecognition of financial assets and financial liabilities

a. *Recognition*

The Bank initially recognises loans, deposits, debt securities issued and subordinated liabilities on the date that they are originated. All other financial assets and liabilities (including assets and liabilities designated at fair value through profit or loss) are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

b. *Derecognition*

The Bank derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transacion in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred fiancial assets that is created or retained by the Bank is recognised as a separate asset or liability.

Financial liabilities are recognised when the Bank becomes a party to the contractual provisions of the liability instrument. Financial liabilities are derecognised when the obligation of the Bank is discharged or cancelled or expires.

20. Offsetting financial assets and financial liabilities

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

20. contd.:

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

21. **Amortised cost measurement of financial assets and financial liabilities**

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

22. **Operating assets**

a. *Recognition and measurement*
Items of operating assets are measured at cost less accumulated depreciation and impairment losses.

Where parts of an item of operating assets have different useful lives, those components are accounted for as separate items of operating assets.

b. *Subsequent costs*

The Bank recognises in the carrying amount of an item of operating assets the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Bank and the cost of the item can be measured reliably. The decision, if subsequent costs are added to the acquisition cost of operating assets, is based on whether an identified component, or part of such component, has been replaced or not, or if the nature of the subsequent cost means a contribution of a new component. All other costs are expensed in the income statement when incurred.

Depreciation is recognised in the income statement on a straight-line basis over the estimated useful lives of each component of an item of property and equipment. The estimated useful lives are as follows:

Real estate	50 years
Office equipment fixtures	3-5 years

Where residual value is not immaterial, it is reassessed annually.

23. **Deposits from credit institutions and the Central Bank**

When the Bank sells a financial asset and simultaneously enters into a "repo" or "stock lending" agreement to repurchase the asset (or a similar asset) at a fixed price on a future date, the arrangement is accounted for as a deposit, and the underlying asset continues to be recognised in the Bank's financial statements.

24. **Borrowings**

The Bank's borrowings consist primarily of loans from banks. Borrowings are initially recognised at fair value less attributable transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in their carrying amount.

25. **Subordinated loans**

Subordinated loans are bonds issued by the Bank with subordinated terms. Subordinated loans have the characteristics of equity in being subordinated to other liabilities of the Bank. In the calculation of equity ratio, these bonds are included in equity, as shown in note 32. The loans are recognised as liabilities with accrued interest and indexation at year-end.

Subordinated loans are initially recognised at fair value less attributable transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in their carrying amount.

26. **Other liabilities**

Other liabilities are measured at cost.

27. **Employee benefits**

a. *Share-based payment transactions*

The parent company has entered into stock option contracts with its employees, which enable them to acquire shares in the parent company at an exercise price corresponding to the fair value of the shares at grant date. The grant date fair value of options granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period in which the employees become unconditionally entitled to the options. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest.

b. *Treasury shares stated as other liability on account of put options*

When the parent company sells treasury shares to its employees with put options - i.e., the right to sell the shares back to the parent company at the purchase price - equity is not increased. Equity will be increased if the put option is not exercised. In the Financial Statements the nominal value of share capital and share premium is increased, but options reserve decreased. The value is classified as liability among other liabilities.

c. *Fair value of share-based payments*

The fair value of services reveived in return for share options granted is measured by reference to the fair value of share options granted. The estimate of the fair value of the services reveived is measured based on the Black-Scholes model. The contractual life of the option is used as an input into this model. Expectations of early exercise are not incorporated into the Black-Scholes model.

28. **Financial guarantees**

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognised at their fair value, and inital fair value is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment (when a payment under the guarantee has become probable). Financial gurantees are included within other liabilities.

29. Share capital

a. *Treasury shares*

Acquired own shares and other equity instruments (treasury shares) are deducted from equity. No gain or loss is recognised in income statement on the purchase, sale, issue or cancellation of treasury shares. Consideration paid or received is recognised directly in equity.

Incremental transaction costs of treasury share transactions are accounted for as a deduction from equity (net of any related income tax benefit).

When classifying a financial instrument (or component of it) in the Consolidated Financial Statements, all terms and conditions agreed between the Bank and the holders of the instrument are considered. To the extent there is an obligation that would give rise to a financial liability, the instrument is classified as financial liability, rather than an equity instrument.

b. *Share capital*

When share capital is repurchased, the amount of the consideration paid, including directly attributable costs, is recognised as a change in capital.

c. *Share premium*

Share premium represents excess of payment above nominal value (ISK 1 per share) that shareholders have paid for shares sold by the Company. According to Icelandic Companies Act, 25% of the nominal value of share capital must be held in reserve which can not be paid out as dividend to shareholders.

d. *Option reserve*

The reserve includes the accured part of the fair value of share options. This reserve is reversed if share options are exercised or forfeited.

e. *Fair value reserve*

The fair value reserve includes the cumulative net change in the fair value of available-for-sale investments until the investment is derecognised or impaired.

f. *Translation reserve*

Foreign exchange differences arising on translation of financial statements of subsidiaries are recognised directly in a seperate component of equity. When a foreign operation is disposed of, in part or in full, the relevant amount in the translation reserve is transferred to profit and loss.

g. *Dividends on share capital*

Dividends on share capital are deducted from equity in the period in which they are approved by the Bank's primary capital holders.

30. **New standards and interpretations not yet adopted**

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2007, and have not been applied in preparing these consolidated financial statements. The Bank will apply the following new standards, amendments and interpretations when effective:

IFRS 8 *Operating Segments* sets out requirements for disclosure of information about an entity's operating segments and also about the entity's products and services, the geographical areas in which it operates, and its major customers. IFRS 8, which becomes mandatory for the Bank's 2009 financial statements, is not expected to have any impact on the consolidated financial statements.

IFRIC 7 *Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies* addresses the application of IAS 29 when an economy first becomes hyperinflationary and in particular the accounting for deferred tax. IFRIC 7, which becomes mandatory for the Bank's 2007 Financial Statements, is not expected to have impact on the Consolidated Financial Statements' Income Statement or capital statement. The main impact will be on additional disclosures.

IFRIC 8 *Scope of IFRS 2 Share-based Payment* addresses the accounting for share-based payment transactions in which some or all of goods or services received cannot be specifically identified. IFRIC 8 will become mandatory for the Bank's 2007 Financial Statements, with retrospective application required. The Bank has not yet determined the potential effect of the interpretation.

IFRIC 9 *Reassessment of Embedded Derivatives* requires that a reassessment of whether embedded derivative should be separated from the underlying host contract should be made only when there are changes to the contract. IFRIC 9, which becomes mandatory for the Bank's 2007 Financial Statements, is not expected to have any impact on the Consolidated Financial Statements.

IFRIC 10 *Interim Financial Reporting and Impairment* prohibits the reversal of an impairment loss recognised in a previous interim period in respect of goodwill, an investment in an equity instrument or a financial asset carried at cost. IFRIC 10 will become mandatory for the Bank's 2007 Financial Statements, and will apply to goodwill, investments in equity instruments, and financial assets carried at cost prospectively from the date that the Bank first applied the measurement criteria of IAS 36 and IAS 39 respectively (i.e., 1 January 2004).

IFRIC 11 *IFRS 2 – Group and Treasury Share Transactions sets out how payments regarding equity instruments of the entity (eg share options) should be accounted for*. IFRIC 11, which becomes mandatory for the Bank's 2007 Financial Statements, is not expected to have any impact on the Consolidated Financial Statements.

IFRIC 12 – *Service Concession Arrangements is mandatory for the Group's 2008 Financial Statments and is not expected to have any impact on the Consolidated Financial Statements.*

31. **Critical accounting estimates and judgements in applying accounting policies**

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

31. contd.:

a. *Impairment losses on loans*

The management reviews its loan portfolios to assess impairment at least on a three months basis. In determining whether an impairment loss should be recorded in the income statement, the Bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there have been changes in the payment status of borrowers in a group or economic conditions. Management uses estimates based on historical loss experience for assets with similar credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

b. *Fair value of financial instruments*

The fair value of financial instruments that are not quoted in active markets are determined by using valuation techniques which are reviewed regularly by qualified independent personnel. All models that are used must be approved and calibrated to ensure that outputs reflect actual data.

c. *Financial asset and liability classifications*

The Bank's accounting policies provide scope for assets and liabilities to be designated on inception into different accounting categories in certain circumstances:

In designating financial assets or liabilities at fair value through profit and loss, the Bank has determined that it has met on of the criteria for this designation set out in accounting policy.

In designating financial assets or liabilities at available-for-sale, the Bank has determined that it has met on of the criteria for this designation set out in accounting policy.

32. Capital management and allocation

a. *Capital management*

It is the Bank's policy to maintain a strong capital base to support the development of its business and to meet regulatory capital requirements at all times. The Bank recognises the impact on shareholder returns of the level of equity capital employed within the Bank and seeks to maintain a prudent balance between the advantages and flexibility afforded by a strong capital position and the higher returns on equity possible with greater leverage.

A capital plan is prepared on an annual basis and approved by the Board with the objective of maintaining both the optimal amount of capital and the mix between the different components of capital. The Bank’s policy is to hold capital in a range of different forms and from diverse sources.

The principal forms of capital are included in the following balances on the consolidated balance sheet: share capital, share premium account, other reserves, retained earnings, and subordinated liabilities. Capital also includes the collective impairment allowances held in respect of loans and advances.

The lcelandic Financial Supervisory Authority (FME) supervises the Bank on a consolidated basis and, as such, receives information on the capital adequacy of, and sets capital requirements for, the Bank as a whole.

b. *Regulatory capital*

Equity at the end of the year amounted to ISK 6,187 million, equivalent to 12% of total assets according to the balance sheet. The capital adequacy ratio of the Bank, calculated in accordance to Article 84 of the Act on Financial Undertakings, is 28.1%. This ratio may not be lower than 8.0% according to that Act. The ratio is calculated as follows:

	Weighted value
Risk base:	
Risk base due to credit risk in items not included in the trading book	11,171
Risk base due to currency fluctuations	1,282
Risk base due to position and counter-party risk in the trading book	9,677
Risk base, total	22,130
Tier 1 capital:	
Recorded capital	6,187
Tier 2 capital:	
Subordinated loans	22
Capital, total	6,209
Capital adequacy ratio	28.1%

Amounts are in ISK thousands

33. **Risk management disclosure**

The purpose of the Risk Management and Credit Control Unit is to identify, quantify, control and report on the risks that the Bank is exposed to in its daily activities. The Unit also participates in drafting the overall risk policy of the Bank and has representatives on the Finance Committee, the Credit Committee and the Security and IT Committee. The Unit’s main activities include monitoring and managing credit risk, market risk, liquidity risk and operational risk. The Board of Directors sets the rules and guidelines regarding the Bank's risk policy and the obligations of Risk Management and Credit Control. The Division reports regularly to the Board of Directors, the CEO and the Finance Committee on the Bank’s positions and exposure to risk.

Committees

The Bank operates a Finance Committee (FC), a Credit Committee (CC) and a Security and IT Committee (SC); all chaired by the CEO.

On the Bank's Finance Committee are the CEO, the Heads of Risk Management, the Treasury, Business development and the Legal Department and other employees as determined by the CEO. The Finance Committee meets regularly and each department reports on its operations and positions activity since the previous meeting. The Committee addresses matters regarding the Bank's risk management, financing, capital management and proprietary trading.

The Loan Committee consists of the Bank’s CEO, the Head of Risk Management and Credit Control and the Head of the Legal Department. The CEO shall decide whether any other employees should attend the meetings. The Committee addresses matters regarding the Bank's loan activities. The Committee is responsible for the approval of individual loans as well as deciding on credit limits for individual clients in derivative trades. The Committee is the primary forum for the discussion of loan activity policy.

Credit risk

One of the Bank’s primary sources of risk is Credit Risk. Counterparty Credit Risk means that if one or more borrowers fail to meet their financial obligations towards the Bank, the Bank has to recognize losses due to these defaults. To a very large extent the Bank’s loan portfolio consists only of Senior loans, most of which are highly collateralized.

a. *Credit approval process*

The originating department prepares a proposal for each loan or credit line which is presented to the Credit Committee for approval. The proposal consists of a basic description of the client, the purpose of the loan, a simple credit assessment and arguments for or against granting the loan. The Committee decides whether there is need for further credit assessment and on what terms the loan may be granted.

A more thorough credit assessment may be conducted if considered appropriate and can include an assessment of a borrower’s fundamental credit strength as well as the value of any collateral. To assess the borrower’s capacity to meet his or her obligations the committee can request stress test analysis of the borrower’s cash flow or call for third party assessments.

b. *Credit collateral*

The Bank places emphasis on ensuring that loans are secured with collateral that can be marked to market, and that asset coverage exceeds 100%, e.g. Senior I loans. The Bank applies appropriate haircuts on all collateral in listed securities in order to ensure proper risk mitigation. For all collateral in listed securities, the Bank maintains the right to liquidate collateral in case its market value falls below the predefined limit.

33. contd.:

c. *Credit rating, control and provisioning*

The Risk Management and Credit Control Unit is responsible for credit rating and reviewing the loan portfolio. In case of any significant delay of payments or defaults the Unit carefully analyzes the underlying assets and loan documents and organizes the process of collection.

The Bank monitors the value of collateral by listed securities on a real time basis, ensuring that prompt action can be taken if necessary.

Provisioning for loan impairments is estimated on the basis of models assessing a portfolio as a whole based on the seniority of the loans, the high degree of collateralization and the fact that the Bank has practically no history of defaulted loans. Risk Management and Credit Control suggest a provisioning percentage for the portfolio, based on the expected loss assessment. Risk Management and Credit Control reassess impairments in the event of collateral decay, delayed payments or other early warning signs. Provisions require approval by the CEO, CFO and the Credit Committee.

d. *Loan portfolio management*

To ensure an effective diversification of the loan portfolio the Board has set a limit framework defining maximum exposure as a ratio of the Bank’s equity and/or the total size of the loan portfolio. These limits include limitation on joint exposure to associated clients, exposure to individual and associated industries, single regions and countries etc. It is the responsibility of Risk Management and Credit Control to monitor that these limits are not being violated and to report discrepancies to the Loan Committee.

e. *Maximum exposure to credit risk before collateral held or other credit enhancements*

The following table shows net exposures based on carrying amounts as reported in the balance sheet.

	2007	2006
Cash and cash equivalents	7,241,857	2,157,724
Derivatives	1,380,422	536,621
Financial assets at fair value through profit and loss, bond securities	17,205,899	9,767,972
Securities used for hedging, bond securities	138,658	1,643,163
Loans	9,599,516	7,935,503
Receivables and prepayments	1,627,276	1,580,110
Total	37,193,628	23,621,093

Amounts are in ISK thousands

33. contd.:

f. *Breakdown of loans by seniority*

The Bank's loan portfolio mainly consists of Senior I loans which are secured with collateral which can be marked to market, and have asset coverage exceeding 100% and Senior II loans which have first priority claims on all of the borrower's assets, and in some cases additional collateral such as unlisted shares and other collateral which cannot be marked to market. The loan portfolio contains less than 2% Junior loans which have second line claims on the borrower's assets and no Mezzanine loans where the loan is unsecured and subordinated to all of the borrower's liabilities.

The change in the allowance account for credit losses on loans specifies as follows:

2007	Total
Allowance account at the beginning of the year	40,756
Provision for losses during the year	8,467
Loans written off during the year as uncollectible	(15,165)
Restatement due to IFRS	8,698
Allowance account at year-end	42,756

2006	
Allowance account at the beginning of the year	34,756
Provision for losses during the year	21,106
Loans written off during the year as uncollectible	(15,106)
Allowance account at year-end	40,756

Provision for losses in the Income Statement for the year 2006 are specified as follows:

Provision for losses on the loan portfolio	21,106
Provision for other losses	80,000
Provision for losses in the Income Statement, total	101,106

Liquidity risk

MP Investment Bank hf. must always have sufficient liquidity to meet both foreseeable and unexpected payment obligations. To meet such eventualities, the Bank has lines of credit, overdraft facilities and highly liquid securities, such as Treasury bills and bonds including housing bonds. Furthermore, the Bank strictly matches maturity of assets and liabilities.

The Bank only takes securities as pledge if they are very liquid in the market where they are listed. The Borrower has an internal limit of pledges in each security whereby the exposure of the Borrower cannot exceed twice the average daily turnover of the security in the relevant stock exchange for the last six months. Furthermore, the Bank has become a member of eight Stock Exchanges and trades in the US and Europe to diversify the risk.

To reduce the refinancing risk the Bank has unused committed credit lines almost matching the equity of the Bank. The Bank is furthermore matching the maturity of loans and liabilities in a strict manner.

Amounts are in ISK thousands

33. contd.:

Below is a breakdown by contractual maturity of financial assets and liabilities.

2007 **Assets:**	0-1 months	1 to 3 months	3-12 months	1-5 years	Over 5 years	No stated maturity	Total
Cash and cash equival.	7,241,857	0	0	0	0	0	7,241,857
Derivatives	783,535	433,660	8,874	154,353	0	0	1,380,422
Financial assets at fair value through profit and loss	20,659,461	0	0	0	0	0	20,659,461
Securities used for hedging	4,895,103	4,568,587	954,892	0	0	0	10,418,582
Loans	1,315,231	3,046,237	3,395,028	1,817,141	25,879	0	9,599,516
Receivables and prepaym.	1,627,276	0	0	0	0	0	1,627,276
Total	36,522,463	8,048,483	4,358,794	1,971,495	25,879	0	50,927,115
Liabilities:							
Deposits from credit institutions and the Central Bank	10,509,872	2,940,796	0	0	0	0	13,450,667
Derivatives	148,090	109,855	16,043	0	0	0	273,988
Financial liabilities at fair value through profit and loss	5,709,533	0	0	0	0	0	5,709,533
Borrowings	4,428,332	1,161,918	909,644	767,215	209,716	0	7,476,824
Debt securities issued	4,800,356	5,515,038	1,604,029	4,441,627	0	0	16,361,050
Subordinated loans	0	0	0	43,846	0	0	43,846
Other .... liabilities	2,851,821	0	0	0	0	0	2,851,821
Total	28,448,003	9,727,607	2,529,716	5,252,688	209,716	0	46,167,729
Assets-liabilities	8,074,461	(1,679,123)	1,829,078	(3,281,194)	(183,837)	0	4,759,385

Amounts are in ISK thousands

33. contd.:

2006 Assets:	0-1 months	1 to 3 months	3-12 months	1-5 years	Over 5 years	No stated maturity	Total
Cash and cash equival.	2,157,724	0	0	0	0	0	2,157,724
Derivatives	250,775	104,290	181,557	0	0	0	536,621
Financial assets at fair value through profit and loss	13,410,153	0	0	0	0	0	13,410,153
Securities used for hedging	4,322,590	7,378,435	4,191,179	0	0	0	15,892,205
Available-for-sale financial assets	690,277	0	0	0	0	0	690,277
Loans	1,728,005	1,391,255	3,480,206	1,336,037	0	0	7,935,503
Receivables and prepaym.	1,580,110	0	0	0	0	0	1,580,110
Total	24,139,634	8,873,981	7,852,942	1,336,037	0	0	42,202,593
Liabilities:							
Deposits from credit institutions and the Central Bank	7,733,282	0	0	0	0	0	7,733,282
Derivatives	338,890	526,952	106,910	0	0	0	972,752
Financial liabilities at fair value through profit and loss	2,601,475	0	0	0	0	0	2,601,475
Borrowings	9,919,863	16,790	700,878	1,038,023	0	0	11,675,554
Debt securities issued	2,980,825	3,615,562	41,617	4,553,764	0	0	11,191,768
Subordinated loans	0	0	0	58,437	0	0	58,437

Amounts are in ISK thousands

33. contd.:

2006 liabilities:	0-1 months	1 to 3 months	3-12 months	1-5 years	Over 5 years	No stated maturity	Total
Other liabilities	3,672,126	0	0	0	0	0	3,672,126
Total	27,246,461	4,159,304	849,405	5,650,224	0	0	37,905,394
Assets-liabilities	(3,106,827)	4,714,676	7,003,537	(4,314,187)	0	0	4,297,199

Market risk

Market risk constitutes risk due to changes in market prices of instruments and interest rates. The Bank has a strict policy on controlling the market risk and to keep the exposure within the limit framework. The Risk Management and Credit Control Unit follows the market risk limits daily and reports regularly to the Finance Committee and the CEO. The monitoring and control of market risk is performed through Value-at-Risk, Stop-loss definitions and absolute exposure limits.

a. *Derivatives*

The exposures of derivatives sold to clients are all fully hedged. Furthermore, the Bank uses derivatives to manage risks and market exposures by hedging assets and liabilities. The instruments used include currency swaps, interest rate swaps and forward currency contracts.

	Carrying amount	
	Assets	Liabilities
Currency and interests rate derivatives, agreements unlisted:		
Forward exchange rate agreements	73,671	25,980
Interest rate and exchange rate agreements	155,316	0
Total	228,987	25,980
Equity derivatives:		
Equity swaps, agreements unlisted	1,137,991	245,066
Total	1,137,991	245,066
Bond derivatives:		
Bond swaps, agreements unlisted	13,444	2,942
Total	13,444	2,942
Total Derivative financial instruments	1,380,422	273,988

b. *Interest rate risk*

Interest rate risk arises due to currency or maturity mismatch between assets and liabilities. The Treasury is responsible for managing the risk associated with changes in interest rates and minimizing the effect it may have on the value of assets and liabilities as well as the adverse effects it might have on the net interest income.

Amounts are in ISK thousands

33. contd.:

Interest rate risk is minimized by matching the interest rate profile and duration of assets with the Bank's liabilities. This is obtained in part by matching the currency and duration of the funding of the Bank with its assets, as well as using derivative and non-derivative financial instruments to manage effectively the risk of an adverse impact on the Bank's earnings. For this purpose, a number of different derivatives are used, including forward currency contracts, currency swaps and interest rate swaps.

c. *Market price risk*

Market price risk arises from changes in the market values of equities in the Bank's portfolio, the size of which varies greatly. The Bank invests primarily in equities listed on regulated securities markets, but has also invested in unlisted equities and bonds. The Bank's risk is the general risk involved in investing in equities. Efforts are made to reduce this risk through active risk management. The Risk Management and Credit Control Unit monitors the market price risk and reports regularly to the Finance Committee and the CEO.

d. *Currency risk*

If there is a mismatch of assets and liabilities in individual currencies, fluctuations in their exchange rates can have a substantial impact on the Bank's performance. The Bank is subject to currency risk arising from its foreign equity holdings and takes measures to hedge this risk.

The Bank's internal rules regarding currency risk are in accordance with the Rules on Foreign Exchange Balance, No. 318 from April 25, 2006, set by the Central Bank of Iceland. Pursuant to the rules, the Bank's currency exposure in any currency cannot exceed 20% of the Bank's equity and the total currency balance cannot exceed 30% of equity.

Breakdown of assets and liabilities by currency:

2007	EUR	ISK	LTL	USD	CHF	Other	Total
Assets:							
Cash and cash equivalents	719,311	5,814,612	67,695	376,716	0	263,523	7,241,857
Derivatives	210,238	741,184	42,744	110,780	1,781	273,696	1,380,422
Financial assets at fair value through profit and loss	1,084,808	17,868,329	467,448	441,949	8,908	788,019	20,659,461
Securities used for hedging	2,765,974	4,725,560	0	810,130	0	2,116,919	10,418,582
Loans	1,923,041	2,382,600	1,695,149	1,780,480	1,083,389	734,859	9,599,516
Receivables and prepaym.	0	1,627,276	0	0	0	0	1,627,276

Amounts are in ISK thousands

33. contd.:

2007	EUR	ISK	LTL	USD	CHF	Other	Total
Assets:							
Investments in associates	0	1,205,627	0	0	0	0	1,205,626
Operating assets	0	415,937	0	0	0	0	415,937
Total	6,703,371	34,781,124	2,273,036	3,520,054	1,094,078	4,177,016	52,548,678
Liabilities and equity:							
Deposits from credit inst. and the Central Bank	1,806,445	9,245,408	0	1,290,213	0	1,108,602	13,450,667
Derivatives	73,750	165,177	1,183	16,986	0	16,892	273,988
Financial liabilities at fair value through profit and loss	0	5,709,533	0	0	0	0	5,709,533
Borrowings	4,633,676	1,924,403	209,716	680,923	0	28,106	7,476,824
Debt securities issued	0	16,361,050	0	0	0	0	16,361,050
Subordinated loans	0	43,846	0	0	0	0	43,846
Deferred tax liabilities	0	193,863	0	0	0	0	193,863
Other liabilities	0	2,851,821	0	0	0	0	2,851,821
Total equity	0	6,187,086	0	0	0	0	6,187,086
Total	6,513,871	42,682,187	210,899	1,988,122	0	1,153,600	52,548,678
Net Balance Sheet position	189,501	(7,901,064)	2,062,137	1,531,932	1,094,078	3,023,416	(0)
Net off Balance Sheet position	(288,061)	7,299,175	(1,437,398)	(1,757,692)	(1,392,166)	(2,384,137)	
Net position	(98,560)	(601,889)	624,739	(225,760)	(298,088)	639,279	

Amounts are in ISK thousands

33. contd.:

Operational Risk Strategy

The risk involved in the Bank's operations is primarily linked to the risks inherent in each type of security in which the Bank invests, although there are a considerable number of other factors which can also affect its operations and performance, such as employee negligence, violations of rules, problems with information systems and loss of key personnel. The Bank's reputation may be damaged, either for the above reasons or as a result of other factors which are difficult to control. MP Investment Bank hf. could suffer losses as the result of an incorrect analysis of investment options, whilst a failure of the Bank's information systems could result in losses which the company would have to cover and thereby affect its performance. A situation could arise where key personnel decide to resign and take up a position with a competitor, potentially resulting in the loss of both important expertise and clients. Decisions by the Bank's personnel in connection with specific investments are extremely important for the Bank's performance.

Operational risk can be reduced through staff training, process re-design and enhancement of the control environment. The Risk Management and Credit Control Unit monitors the Operational Risk by tracking loss events, quality deficiencies, potential risk indicators and other early-warning signals. The Unit takes an active role in internal control and quality management.

Hedging

A part of the Bank's portfolio consists of securities held as a hedge against derivatives positions of customers.

Mismatches in currency exposure between the Bank's loan portfolio and debts are hedged using forward contracts on currencies to reduce risk from adverse movements in foreign exchange rates.

34. Financial assets and liabilities

Accounting classifications and fair values

The table below sets out the Group's classification of each class of financial assets and liabilities.

2007	Trading	Designated at fair value	Loans and receivables	Available-for-sale	Other amortised cost	Total carrying amount
Assets						
Cash and cash equivalents					7,241,857	7,241,857
Derivatives	1,380,422					1,380,422
Financial assets at fair value through profit and loss	18,125,142	2,534,319				20,659,461
Securities used for hedging	10,418,582					10,418,582
Available-for-sale financial assets				0		0
Loans			9,599,516			9,599,516
Receivables and prepayments			1,627,276			1,627,276
	29,924,146	2,534,319	11,226,792	0	7,241,857	50,927,114
Liabilities						
Deposits from credit institutions and the Central Bank					2,157,724	2,157,724
Derivatives	16,361,050					16,361,050
Financial liabilities at fair value through profit and loss	5,709,533					5,709,533
Borrowings					7,476,824	7,476,824
Debt securities issued					16,361,050	16,361,050
Subordinated loans					43,846	43,846
Deferred tax liabilities					193,863	193,863
Other liabilities					2,851,821	2,851,821
	22,070,583	0	0	0	29,085,128	51,155,711
2006						
Assets						
Cash and cash equivalents					2,157,724	2,157,724
Derivatives	536,621					536,621
Financial assets at fair value through profit and loss	11,842,170	1,567,983				13,410,153

Amounts are in ISK thousands

34. contd.:

2006	Note	Trading	Designated at fair value	Loans and receivables	Available-for-sale	Other amortised cost	Total carrying amount
Assets							
Securities used for hedging		15,892,205					15,892,205
Available-for-sale financial assets					690,277		690,277
Loans				7,935,503			7,935,503
Receivables and prepayments				1,580,110			1,580,110
Tax assets						17,044	17,044
		28,270,996	1,567,983	9,515,613	690,277	2,174,768	42,219,637
Deposits from credit institutions and Central Bank						7,733,282	7,733,282
Derivatives		972,752					972,752
Financial liabilities at fair value through profit and loss		2,601,475					2,601,475
Borrowings						11,675,554	11,675,554
Debt securities issued						11,191,768	11,191,768
Subordinated loans						58,437	58,437
Other liabilities						3,672,126	3,672,126
		3,574,227	0	0	0	34,331,167	37,905,394

Amounts are in ISK thousands

Notes to the Income Statement

Net interest income

35. Interest income is specified as follows:

	2007	2006
Cash and cash equivalents	275,191	129,072
Loans	1,479,370	661,212
Financial assets held for trading	746,063	257,802
Interest from forward contracts	2,454,995	1,289,297
Other interest income	12,880	46,966
	4,968,499	2,384,349
Interest expense is specified as follows:		
Amounts due to credit institutions	856,655	21,687
Borrowings	3,295,511	2,303,286
Subordinated loans	8,458	8,759
Other interest expense	28,776	21,753
	4,189,400	2,355,485
Net interest income	779,099	28,864

36. A breakdown of interest income and expense:

2007	Interest income	Interest expense	Net interest income
Financial instruments not at fair value through profit and loss	1,767,441	4,189,400	(2,421,959)
Financial instruments at fair value through profit and loss	3,201,058	0	3,201,058
Total	4,968,499	4,189,400	779,099
2006			
Financial instruments not at fair value through profit and loss	837,250	2,355,485	(1,518,235)
Financial instruments at fair value through profit and loss	1,547,099	0	1,547,099
Total	2,384,349	2,355,485	28,864

37. **Dividend income**

Dividend income is specified as follows:

Financial assets designated at fair value through profit or loss	16,165	45,496
Total dividend income	16,165	45,496

Amounts are in ISK thousands

38. **Other operating income**

Other operating income is specified as follows:	2007	2006
Rental income	7,552	0
Other operating income	160	157
Total other operating income	7,712	157

39. **Administrative expenses**

Administrative expenses are specified as follows:

Salaries and related expenses	502,738	295,810
Other operating expenses	382,511	165,841
Depreciation	16,899	3,458
Total administrative expenses	902,148	465,109

40. **Salaries and related expenses**

Salaries and related expenses are specified as follows:

Salaries	390,172	236,866
Salary-related expenses	80,801	41,390
Share-based payment expense	31,765	17,554
Total salary and salary related expenses	502,738	295,810
Average number of employees during the year	38	24
The Bank's total number of employees at year end	52	26

41. **Employment Terms for the Board of Directors and the CEO**

Salaries paid to the Board of Directors and the CEO for their work for companies within the Bank, their stock options and ownership in the Bank are specified as follows:

	Salaries and fringe benefits	Ownership at year-end
Styrmir Þór Bragason, CEO	64,400	10,000
Margeir Pétursson, Chairman of the Board	4,800	312,087
Sigfús Ingimundarson	1,200	7,733
Ágúst Sindri Karlsson	600	4,200
Jón Þorsteinn Jónsson	600	
Sigurður Gísli Pálmason	600	130,593
Gunnar Árnason, alternative board member	120	
Jón Hjartarson, alternative board member	120	
Jón Pálmason, alternative board member	120	130,593
Sigurður R. Helgason, alternative board member	120	200
Örn Andrésson, alternative board member	120	8,333
	72,800	603,739

Amounts are in ISK thousands

41. contd.:

The remuneration of the Chairman of the Board and the other directors of the Board is decided by the annual general meeting of shareholders. In addition board members receive remuneration for work in committees of the board, such as audit, compensation and credit committees.

Remuneration to the CEO consists of base salary and bonus.

Included among the holdings of the aforementioned persons are holdings of their spouses, dependent children, and companies owned by them, if any.

42. **Auditors' Fees**

Remuneration to the Bank's Auditors is specified as follows:	2007	2006
Audit of Annual Accounts	6,823	5,544
Review of Interim Accounts	3,768	1,651
Other services	9,415	1,580
Total auditor's fee	20,006	8,775

43. **Income tax**

Tax income (expense) recognised in the Income Statement specifies as follows:

Current tax expense	187,594	132,208
Deferred tax income (expense)	282,035	161,719
Total tax income (expense)	469,629	293,927

Reconciliation of effective tax rate:

		2007		2006
Profit before tax		2,249,701		1,530,683
Income tax using the domestic corporation tax rate	18.0%	404,946	18.0%	275,523
Tax exempt expenses	2.4%	53,470	.0%	0
Tax exempt revenues	.3%	6,356	(.53%)	(8,189)
Other changes	.2%	4,857	.8%	12,365
Effective tax	20.9%	469,629	18.3%	279,699

44. Tax assets and tax liabilities recognised directly in equity:

	2007	2006
Share-based payment transactions	16,420	0

Amounts are in ISK thousands

Notes to the Balance Sheet

45. Cash and cash equivalents

Cash and cash equivalents are specified as follows:	2007	2006
Cash	34	44
Balances with banks	6,506,972	1,499,698
Money market placements	734,851	657,982
Total cash and cash equivalents	7,241,857	2,157,724

46. Financial assets at fair value through profit or loss

Financial assets designated at fair value specify as follows:

Listed shares on Iceland Stock Exchange	0	78,529
Listed bonds on Iceland Stock Exchange	3,189,912	7,472,662
Listed foreign shares	1,766,750	1,526,723
Listed foreign bonds	16,556	35,404
Listed domestic unit shares	132,583	3,275
Listed foreign unit shares	120,684	88,884
Unlisted domestic shares	1,421,413	1,894,799
Unlisted domestic bonds	1,571,836	1,101,421
Unlisted foreign bonds	562,081	0
Unlisted foreign shares	12,132	49,971
Goverment bonds	11,865,514	1,158,485
Total financial assets at fair value through profit and loss	20,659,461	13,410,153

47. Securities used for hedging

Securities used for hedging specify as follows:

Listed shares on Iceland Stock Exchange	2,496,149	6,297,918
Listed bonds on Iceland Stock Exchange	98,714	1,500,867
Listed foreign shares	5,138,138	6,506,635
Listed domestic unit shares	1,265	0
Listed foreign unit shares	713,075	738,093
Unlisted domestic shares	1,931,297	706,396
Unlisted domestic bonds	39,944	5,476
Goverment bonds	0	136,820
Total securities used for hedging	10,418,582	15,892,205

48. Loans

Loans are specified as follows:

Loans to credit institutions	1,516,694	824,542
Other loans	8,125,578	7,151,717
Gross loans and advances	9,642,272	7,976,259
Less: allowance for impairment	(42,756)	(40,756)
Total loans	9,599,516	7,935,503

Amounts are in ISK thousands

49. Receivables and prepayments

Receivables and prepayments are specified as follows:	2007	2006
Securities brokerage receivables	1,568,129	1,413,253
Accounts receivable	45,934	30,921
Prepaid expenses	13,213	135,936
Total receivables and prepayments	1,627,276	1,580,110

50. Investment in associates

Associates are specified as follows:

	Total assets	Total liabilities	Net interest expenses	Total other expenses	Net profit of securities	Book value
Hraunbjarg ehf.	3,871,034	1,501,874	(49,631)	(380,197)	1,830,490	1,205,627

The Bank owns 49.0% shares in Hraunbjarg ehf., of which the book value is ISK 1,206 million at year-end 2007. The Bank's share of net profit of Hraunbjarg ehf. during the year amounted to ISK 686 million.

51. Operating assets

Operating assets specify as follows:

Cost	Real estate	Office equipment fixtures	Total
Balance at 1 January 2006	126,268	22,974	149,242
Acquisitions	23,700	26,170	49,870
Sold during the year	0	(948)	(948)
Balance at 31 December 2006	149,968	48,196	198,164
Balance at 1 January 2007	149,968	48,196	198,164
Acquisitions	180,194	49,537	229,731
Net acquisition through business combinations	35,000	0	35,000
Balance at 31 December 2007	365,162	97,733	462,895
Depreciation			
Balance at 1 January 2006	7,768	19,782	27,550
Depreciation for the year	2,525	933	3,458
Sold during the year	0	(948)	(948)
Balance at 31 December 2006	10,293	19,767	30,060
Balance at 1 January 2007	10,293	19,767	30,060
Depreciation for the year	6,776	10,122	16,898
Balance at 31 December 2007	17,069	29,889	46,958

Amounts are in ISK thousands

51. contd.:

	Real estate	Office equipment fixtures	Total
Carrying amounts			
Balance at 1 January 2006	118,500	3,192	121,692
Balance at 31 December 2006	139,675	28,429	168,104
Balance at 31 December 2007	348,093	67,844	415,937

52. **Deposits from credit institutions and the Central Bank**

Deposits from credit institutions and the Central Bank are specified as follows:

	2007	2006
Deposits from other Banks	1,845,278	5,927,713
REPO transactions with the Central Bank	7,400,090	1,805,569
REPO transactions with other Banks	4,205,299	0
Total deposits from credit institutions and the Central Bank	13,450,667	7,733,282

53. **Borrowings**

The Bank's borrowings are specified as follows:

Loans from Banks	6,912,364	9,959,954
Other loans	564,460	57,800
Short term borrowings	0	1,657,800
Total borrowings	7,476,824	11,675,554

54. **Subordinated Loans**

	Currency	Maturity date	Book value	
Loans that qualify as Tier II capital:				
Subordinated loan - Interest 6 months REIBOR	ISK	2010	43,846	58,437
			43,846	58,437

55. **Deferred Income Tax Liability**

Changes in tax liability during the year are as follows:

Balance at the beginning of the year	(17,044)	20,990
Calculated income tax for the year	469,629	292,501
Tax assets and tax liabilities recognised directly in equity due to IFRS	(71,128)	(51)
Additions through business combination	0	(198,068)
Income tax related to decrease in revaluation reserve	0	(208)
Income tax to be paid in next year	(187,594)	(132,208)
Net tax assets and (liabilities)	193,863	(17,044)

Amounts are in ISK thousands

55. contd.:

The deferred income tax is attributable to the following items:

	2007	2006
Equity investments	131,166	0
Derivatives	34,286	0
Loans and trade receivables	5,481	0
Operating assets	12,314	12,166
Other balance sheet items	10,616	(29,210)
Net deferred income tax (asset) liability 31.12.	193,863	(17,044)

	Assets		Liabilities		Net deferred tax (asset) liability	
	2007	2006	2007	2006	2007	2006
Equity investments		(42,737)	131,166		131,166	(42,737)
Derivatives			34,286		34,286	0
Receivables			5,481	13,579	5,481	13,528
Operating assets			12,314	12,165	12,314	12,165
Other items			10,616		10,616	0
	0	(42,737)	193,863	25,744	193,863	(17,044)

	1 January 2007	Recognised in equity	Additions through business combination	Recognised in profit and loss	Exchange rate difference	31 December 2007
Equity investments	(42,737)			173,903		131,166
Derivatives	0			34,286		34,286
Receivables	13,579			(8,097)		5,482
Operating assets	12,166			149		12,315
Other items	0			47,794	(37,180)	10,614
Tax loss carry-forwards	(34,000)			34,000		0
	(50,992)	0	0	282,035	(37,180)	193,863

56. **Other liabilities**

Other liabilities are specified as follows:

	2007	2006
Unsettled securites trading	2,032,538	2,702,044
Income tax payable	187,593	132,208
Account payable	190,406	322,005
Sundry liabilites	441,284	515,869
Total other liabilities	2,851,821	3,672,126

Amounts are in ISK thousands

Share-based payments

57. The terms and conditions of grants are as follows:

Grant date	Number of instruments in thousands	Vesting conditions	Contractual life of option
Options granted 2004	981	12-48 months service	4 years
Options granted 2004	18,667	12-36 months service	3 years
Total	19,648		

All options are to be settled by physical delivery of shares. Options vesting in 12 months can be exercised 48 months after the vesting period and options vesting in 24 months can be exercised 36 months after the vesting period. Accordingly 36 months options can be exercised 24 months after the vesting period and the 48 month options can be exercised 12 months after the vesting period.

The number and weighted average excercise price of share options is as follows in thousands:

	Weighted average exercise price 2007	Number of options 2007
Outstanding at 1 January	3.4	49,626
Forfeited during the year	3.2	(8,667)
Exercised during the year	3.5	(21,312)
Granted during the year		0
Outstanding at 31 December	3.5	19,647
Excercisable at 31 December	2.7	981

The options outstanding at 31 December 2007 have an exercise price in the range of 2.2 to 4.7 and a weighted average contractual life of 1.5 years. The share price at the date of exercise for share options exercised in 2007 was 1.9 to 4.7.

Total recognised expenses for the year arising from share-based payment transactions amounted to ISK 32 million (2006: ISK 17 million) including adjustments for forfeited options during the year.

58. **Equity**

According to the Parent Company's Articles of Association, total share capital amounts to ISK million. The nominal amount of treasury shares at end of year 2006 and 2007 amounted to ISK 6,000 million and ISK 30,244 million respectively. One vote is attached to each share of one ISK and the holders of ordinary shares are entitled to one vote per share at meetings of the Bank.

59. Related parties

Identity of related parties

The Group has a related party relationship with its associate as dislosed in note 50 and with its Board of Directors, the CEO and managing directors, referred to as the management.

Group entities

The Company holds eleven subsidiaries which all are included in the consolidated financial statements. The direct subsidiaries included in the consolidated financial statements are specified as follows:

Investments:	Share 31.12.2007
Executive Credit Investments Ltd., England	100%
Kinsley Traders Ltd., Cyprus	100%
MP East European Credit Investments Ltd., England	100%
Orange International Investments Ltd., England	100%
Reykjavik Savings Investments Ltd., England	100%
Rekstrarfélag MP Fjárfestingabanka hf., Iceland	100%
Saga Credit Investments Ltd., England	100%
S-50 D ehf., Iceland	100%
UAB Heildun, Lithuania	100%
UAB MP Pension Fund Baltic, Lithuania	50%
Visoky Zamok Investments Ltd., England	100%

Amounts are in ISK thousands

Changes to accounting policies in accordance with International Financial Reporting Standards (IFRS)

60. As discussed in note 2, these are the Group´s first financial accounts for part of the period covered by the first IFRS annual financial statements prepared in accordance with IFRSs, as adopted by the EU.

The Group´s financial accounts for the period from 1 January to 31 December 2007 is prepared in accordance with the accounting policies specified in the notes on significant accounting policies. This also applies to comparative information for the financial statements for the year ended 31 December 2006 and the preparation of an opening IFRS balance sheet at 1 January 2006 (the Bank´s date of transition).

Amounts in the opening Balance Sheet of 1 January 2006 have been changed in accordance with IFRS, but were previously presented in accordance with the Annual Accounts Act and the Regulation on the Presentation and Contents of the Annual Accounts of Commerial Banks, Savings Banks and Other Financial Institutions (referred to as IS-GAAP). The following tables and notes show the effects the change from IS-GAAP to IFRS has had on the financial position of the Group and its financial results There are no significant changes to the cash flows summary according to IFRS compared with how it was previously under IS-GAAP.

Changes in equity from IS-GAAP to IFRS:		**Equity**
Equity according to IS-GAAP at 31 December 2006		5,077,285
Equity according to IFRSs at 1 January 2007		4,768,323
Change in equity from IS-GAAP to IFRSs		(308,962)

Adjustments at the beginning of the year 2006:		**Equity**
Financial assets at fair value through profit and loss	IAS 39	(121,022)
Loans	IAS 39	24,384
Effect on taxes	IAS 12	17,395
Total transition to IFRS 1 January 2006		(79,243)

Adjustments during the year 2006:		**Equity**
Treasury shares stated as other liability on account of put options	IAS 39	(230,604)
Treasury shares deducted from equity	IAS 39	(59,400)
Interest income	IAS 39	(17,554)
Interest expense	IAS 39	(18,725)
Fair value changes on AFS	IAS 39	115,046
Provision for losses	IAS 39	(1,139)
Effect on taxes through profit and loss	IAS 12	3,365
Taxes directly to equity	IAS 12	(20,708)
Total transition to IFRS 2006		(229,719)
Changes from previous GAAP to IFRSs		(308,962)

The total effect on equity of the transition to IFRS is an decrease of ISK 309 million. The following describes the effects of these new accounting policies on the Bank's Balance Sheet and Income Statement.

Amounts are in ISK thousands

60. contd.:

Impairment of loans

In accordance with IAS 39 the Bank has performed the impairment of loans. As a result the MP Investment Bank's capital increased by ISK 23 million, when income tax has been taken into consideration.

According to IAS 39 the Bank is obligated to review all loans to ascertain whether there is objective evidence of impairment that affects the size of expected cash flows from the loan. The loan will then be written down to the present value of expected future cash flows.

Borrowing charges

In accordance with IFRSs borrowing charges are an integral part of the interest income of loans and recognised over the expected life of the loan. Previously borrowing charges were recognised in the income statement on grant date of loans. The total effect of this change in the accounting policy is a decrease in equity amounting to 18 million.

Value changes on AFS assets

The Investment Bank sold the cash flow of part of its loan portfolio and according to the derecognition rules of IAS 39 it has to derecognise it from the balance sheet. These changes result in increase in capital by ISK 94 million.

Treasury shares stated as other liability on account of put options

When the parent company sells treasury shares to its employees with put options - i.e., the right to sell the shares back to the parent company at the purchase price - equity is not increased. Equity will be increased if the put option is not exercised. In the Financial Statements the nominal value of share capital and share premium is increased, but options reserve decreased. The value is classified as liability among other liabilities. This change resulted in a decrease in equity in the amount of ISK 249 million.

60. contd.:

From IS-GAAP to IFRS

The following tables provide an overview of the effect of the transition to IFRS by valuation and presentation.

Income Statement for the year 2006, change from IS-GAAP to IFRS

According to IS-GAAP		**Change in valuation**	**Change in presentation**		**According to IFRSs**
Interest from credit institutions	129,072	0	(129,072)	0	
Interest on loans	521,175	(17,554)	(503,621)	0	
Interest on market securities	460,988	0	(460,988)	0	
Other interest income	1,290,668	0	(1,290,668)	0	
			2,384,349	2,384,349	Interest income
Interest to credit institutions	(21,687)	0	21,687	0	
Interest on borrowings	(2,303,286)	0	2,303,286	0	
Interest on subordinated loans	(8,759)	0	8,759	0	
Other interest expenses	(3,028)	(18,725)	21,753	0	
			(2,355,485)	(2,355,485)	Interest expense
Income from shares and other holdings	37,023	0	0	37,023	Net income from other financial instruments carried at fair value
Fee and comissions	1,051,566	0	0	1,051,566	Fee and commission income
Commission expenses	(38,336)	0	0	(38,336)	Fee and commission expense
Net trading income	1,059,251	0	0	1,059,251	Net trading income
				0	Net foreign exchange loss
				0	Share of profit of associates
Sundry operating income	157	0	0	157	Other operating income
Salary and related expenses	(295,810)	(41,627)	0	(337,437)	Salaries and related expenses
Other operating expenses	(165,841)	0	0	(165,841)	Administrative expenses
Depreciation	(3,458)	0	0	(3,458)	Depreciation
Provision for losses	(99,967)	(1,139)	0	(101,106)	Impairment on loans
Income tax	(293,927)	3,365	0	(290,562)	Income tax expense
Net profit according to IS-GAAP	**1,315,801**	**(75,680)**	**0**	**1,240,121**	**Profit according to IFRS**

Amounts are in ISK thousands

60. contd.:

Balance Sheet, change from IS-GAAP to IFRS

IS-GAAP 31 December 2006		**Change in valuation**	**Change in presentation**		**IFRS 1 January 2007**
Cash and Amounts Due from Credit Institutions	2,898,986	0	(741,262)	2,157,724	Cash and cash equivalents with the Central Bank ....
Loans	7,188,550	5,691	741,262	7,935,503	Loans ....
			536,621	536,621	Derivatives ....
Bonds and other fixed-income securities	12,431,619		(12,431,619)	0	
Shares and other variable-income securities	17,626,392		(17,626,392)	0	
			29,302,358	29,302,358	Financial assets at fair value through profit and loss ....
		115,046	575,231	690,277	Available-for-sale financial assets ....
Shares in associated companies	285,976	0	0	285,976	Investment in associates ....
Property and equipment	168,104	0	0	168,104	Operating assets ....
Sundry assets	1,444,174	0	0	1,444,174	Receivables ....
Prepaid expenses and accrued income	672,557	0	(536,621)	135,936	Prepayments ....
Deferred tax asset	16,993		51	17,044	Deferred tax asset ....
Total Assets	42,733,351	120,737	(180,371)	42,673,717	**Total Assets**
Amounts Owed to Credit Institutions	7,733,282	0	0	7,733,282	Deposits from credit institutio and the Central Bank ....
			972,752	972,752	Derivatives ....
Borrowings	25,468,798	0	(13,793,244)	11,675,554	Borrowings ....
		0	2,601,475	2,601,475	Financial liabilities at fair valu through profit and loss ....
Sundry liabilities and accrued expenses	4,395,549	249,329	(972,752)	3,672,126	Other liabilities ....
Subordinated loans	58,437	0	0	58,437	Subordinated loans ....
		0	11,191,768	11,191,768	Debt securities issued ....
		21,733	(21,733)	0	Deferred tax liabilities ....
Share capital	1,070,000		(6,000)	1,064,000	Share capital ....
Share premium	1,218,275		(53,400)	1,164,875	Share reserve ....
Revaluation reserve	46,391		(46,391)	0	
Translation reserve	792		(792)	0	
		(230,604)	72,281	(158,323)	Option reserve ....
		94,338		94,338	Fair value reserve ....
Retained earnings	2,741,827	(14,059)	(124,335)	2,603,433	Retained earnings ....
Total Liabilities and Equity	42,733,351	120,737	(180,371)	42,673,717	**Total Liabilities and Equity**

Amounts are in ISK thousands