

KMIIF

Financial Statements 30 June 2011

KMIIF
Borgartun 19
105 Reykjavík

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

The Interim Financial Statements of Kaupthing Mortgages Institutional Investor Fund pertain to part B of the Interim Financial Statements of Stefir hf., which includes the Financial Statements of Stefir Verdbrefasjodir, Stefir Fjarfestingarsjodir and Stefir Fagjarfestasjodir. The Interim Financial Statements are prepared according to the same accounting methods as the the financial statements for the previous year. The presentation of these Interim Financial Statements is in accordance with the Financial Supervisory Authority's regulations on financial statements of management companies for mutual funds.

Profit, according to the Income Statement, amounted to ISK 485 million during the period 1 January to 30 June 2011 and the profit is stated as a increase of units in the fund's books. According to the Balance Sheet, the fund's net assets at the end of the period amounted to ISK 16,810 million.

Because of circumstances following the fall of the Icelandic commercial banks in the fall 2008, banks and other financial institutions have taken actions to meet customer's debt conditions. Arion bank hf. offered late in the year 2009 ways for costumers to adjust the principal of their debt to 110% of property market value. Customers were able to apply for this special resort until the 30th of June 2011. An amount to meet this depreciation had been reserved to reduce the effects of these special measures and the impairment is charged to the income statement.. This is now done by a general provision and a special provision. By a special provision the expected loss is evaluated from the loans with the highest risk of loss is calculated. On 30th of June this special provision as part of the depreciation account was ISK1.601 million.

Additionally the general reduction is part of the depreciation account. In the calculations of the general reduction the default possibility is obtained from the credit rating system of Arion Bank hf., the recovery rate of 65% which originates from the Basel standards for accounting procedures of financial undertakings. The calculations assumes that six months will elapse from default which the general provision refers to and that it will be examined by credit control and a special provision will be made should this be required. By the 30th of June the general provision as part of the depreciation account was ISK 1,521 million.

In the period January 1st until June 30th 2011, final write offs were ISK 614 million

The Board of Directors and the Managing Director of Stefir hf. hereby confirm the Interim Financial Statements of the fund for the period 1 January to 30 June 2011 by means of their signatures.

Reykjavik, 30 August 2011.

Board of Directors:

Managing Director:

Report on review of interim financial statements

To the unit holder of KMIIF.

We have reviewed the accompanying interim financial statements of KMIIF, which comprise the income statements, balance sheet, changes in net assets, statement of investments, a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and presentation of these interim financial statements in accordance with Icelandic Financial Statements Act. Our responsibility is to express a conclusion on these interim financial statements based on our review.

Scope of review

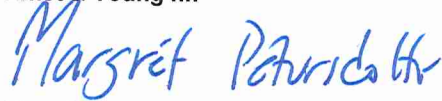
We conducted our review in accordance with the International Standard on Review Engagements 2410, Review of Interim Financial Information Performed by the Independent Auditor of the Entity. A review of interim financial statements consists of making inquiries, primarily of persons responsible for financial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

Conclusion

Based on our review nothing has come to our attention that causes us to believe that the accompanying Interim Financial Statements are not prepared, in all material respects, in accordance with Icelandic Financial Statements Act.

Reykjavik, 30. August 2011.

Ernst & Young hf.



Margrét Pétursdóttir, partner

Income Statement 1 January - 30 June 2011

	Notes	30.06.2011	30.06.2010
Financial income and (expenses)	2-5		
Interests, indexation, dividends and currency exchange rate difference		6.796	4.455
Interest expense		(6.421)	(3.649)
Impairment on loans	13	185	(1.798)
Net financial income		<u>560</u>	<u>(992)</u>
Operating expenses			
Administration fee	6	70	70
Other operating expenses		5	25
		<u>75</u>	<u>95</u>
Gain (loss) for the period transferred to units		<u><u>485</u></u>	<u><u>(1.087)</u></u>

Balance Sheet at 30 June 2011

	Notes	30.06.2011	31.12.2010
Assets			
Securities with fixed income		122.602	120.046
Total securities	7,13	<u>122.602</u>	<u>120.046</u>
Foreclosed assets		328	347
Cash	8	21.085	20.100
Total other assets		<u>21.413</u>	<u>20.447</u>
Total assets		<u><u>144.015</u></u>	<u><u>140.493</u></u>
Liabilities			
Units	12	16.810	16.325
Liabilities with management- and custody companies		18	10
Issued bonds		<u>127.187</u>	<u>124.158</u>
Total other liabilities		<u>127.205</u>	<u>124.168</u>
Total liabilities		<u><u>144.015</u></u>	<u><u>140.493</u></u>
Net assets		16.810	16.325
Number of units		<u>9.637</u>	<u>9.637</u>
Price of units at the end of the period		<u><u>1,74</u></u>	<u><u>1,69</u></u>

Statement of Changes in Net Assets

for the period 1 January - 30 June 2011

	Notes	30.06.2011	31.12.2010
Operating activities			
Gain (loss) for the period transferred to units		485	(978)
Changes in net assets		485	(978)
Net assets at the beginning of the year		16.325	17.303
Net assets at the end of the period		<u>16.810</u>	<u>16.325</u>

Investment Statement 30 June 2011

KMIIF	Market value	% of assets
Icelandic bonds		
Kaupthing hf., property loans	122.602	100,0%
Total assets	122.602	100,0%
Issued bonds	(127.187)	(103,7%)
Foreclosed assets	328	0,3%
Other assets	21.085	17,2%
Other liabilities	(18)	(0,0%)
Total net assets	16.810	13,7%

Notes to the Financial Statements

Accounting methods

1. Operation

The purpose of the Fund KMIIF is to invest funds available to the Fund in, *inter alia*, the purchase of Loans and their Related Security from Kaupthing bank and the Issuer's subsidiaries, all in accordance with the terms of the Transaction Documents. Also to guarantee the payment of all amounts due under any Covered Bonds issued by the Issuer under the Programme, subject to the term of the Covered Bond Guarantee.

2. Basis of preparation

The Interim Financial Statements for Kaupthing Mortgages Institutional Investor Fund have been prepared in accordance with Law on Financial Statements and the Financial Supervisory Authority's regulations on financial statements of management companies for mutual funds. The Interim Financial Statements are prepared on the historical cost basis except for securities that are measured at market value. The Interim Financial Statements are prepared according to the same accounting methods as the financial statements for the previous year. The Interim Financial Statements are presented in Icelandic króna (ISK), rounded to the nearest million. The fund is a part of Stefir hf. which is a subsidiary of Arion bank hf. and included in the Interim Financial Statements for the Group. Due to the nature of the operations of the Fund these Interim Financial Statements are not a part of the Financial Statements for the Bank.

3. Foreign currencies

Assets and liabilities in foreign currencies are translated into ISK at the exchange rate at the end of the period, according to Reuter. Operating income and operating expenses in foreign currencies are translated at the exchange rate on the date of transaction. Foreign exchange difference related to translation of foreign assets is recognised in the income statement of the relevant fund. Funds with foreign currency as a basis currency are published in that currency.

4. Interest income and expenses

Interest income and expense are recognised in the income statement as they are incurred and are based on the effective interest rate.

5. Dividends

Dividends are recognised as revenue when there is demand for redemption, i.e. on the date dividends become payable. Capital gains tax on dividends from foreign equities is deducted from dividend income in the income statement in cases where a double taxation agreement stating that such income should be taxed in this country does not exist between Iceland and the country in question.

6. Administration fee

The fund pays Stefir hf. an asset management fee which includes the following operating costs for the fund: salaries of employees of management company, marketing costs and administration; the fund also pays custody fees to Verdis hf. Administration fees are calculated as a percentage of the fund's total assets, as follows:

	Percentage
Asset management fee	0,07%
Security custody fee	0,03%

7. Securities with fixed income

- a. Property loans are recognised with accrued interest and indexation at the end of the period. At the end of June 2011, 48% of the fund's property loans were calculated according to the index for mortgage payment adjustment.

Notes, contd.:

7. Securities with fixed income, cont.

- b. Because of circumstances following the fall of the Icelandic commercial banks in the fall 2008, banks and other financial institutions have taken actions to meet customer's debt conditions. Arion bank hf. offered late in the year 2009 ways for costumers to adjust the principal of their debt to 110% of property market value. Customers were able to apply for this special resort until the 30th of June 2011. An amount to meet this depreciation had been reserved to reduce the effects of these special measures and the impairment charged to the income statement is lower by that amount. This is now done by a general provision and a special provision. On 30th of June total provision for losses amounts to ISK 3,122 million. The Depreciation account has been deducted from Securities with fixed income in the Balance sheet.

8. Cash

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

9. Other assets

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

10. Other debts

Other liabilities include capital gains tax, unsettled trades and deviations in exchange translation of assets.

11. Taxation

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

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

12. Units

a. Real return of KMIIF as of 30 June 2011.

	Return
Last 3 months	0,98%
Last 6 months	(0,25%)
Last 12 months	(10,09%)

b. Statement of book value and price of units.

	Book value	Price
30 June 2011	16.810	1,74
31 december 2010	16.325	1,69
31 december 2009	17.303	1,80

Notes, contd.:

13. Securities with fixed income are specified as follows:

	30.06.2011	31.12.2010
	Total	Total
Property loans before impairment	125.723	123.966
Provision for losses	(3.921)	(2.123)
Write-offs	614	(75)
Impairment	185	(1.723)
Property loans after impairment	<u>122.602</u>	<u>120.046</u>
Provision for losses as a ratio of total loans	(2,48%)	(3,16%)

14. Statement of proportional division of assets and investment policy.

	Assets 30.06.2011 %	Assets 31.12.2010 %	Investment policy Minimum Maximum % %	
Other financial instruments	100	100	0	100

15. Segmentation of investments and proportional division:

	State, municipality or intern. inst.		Shares		Other		Total	
	ISK	%	ISK	%	ISK	%	ISK	%
Other financial instruments	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>122.602</u>	<u>100</u>	<u>122.602</u>	<u>100</u>
	0	0	0	0	122.602	100	122.602	100

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