



Asset Management Company

Interim Financial Statements

1 January - 30 June 2016

Stefnir hf.
Borgartun 19
105 Reykjavík

Reg. no. 700996-2479

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Report and endorsement of the Board of Directors and the Managing Director

The purpose of Stefir hf. is to operate UCITS, investment funds and institutional investors' funds. The company also manages the assets of several partnerships limited by shares that have been established for venture capital investments. Stefir is Iceland's largest fund manager with assets of approximately ISK 388 billion under active management. Stefir is a subsidiary of Arion Bank hf. and the A-part of the Financial Statements is part of the Consolidated Financial Statements of the Bank and its subsidiaries.

The Interim Financial Statements of the company are divided in two: part A which includes the Interim Financial Statements of Stefir hf. and part B which includes the Interim Financial Statements of UCITS, investment funds and institutional investors' funds. The Interim Financial Statements have been prepared on accordance with the Annuals Account Act, the Financial Undertakings Act and the rules of the Financial Supervisory Authority on the accounts of UCITS management companies. The interim Financial Statements for Stefir, part B, have been prepared in accordance with new rules from the Financial supervisory Authority regarding Financial Statements of UCITS and investment funds, effective 1 January 2016. The new rules do not involve changes in estimates and assumptions that affect the reported amounts of assets nor the net earnings of the funds.

Activities in the first half of 2016

The company reported earnings of ISK 322 million in the period according to the income statement. The company's equity at the end of the period was approximately ISK 2 billion according to the balance sheet. The capital ratio, calculated according to the Financial Undertakings Act, is 59.5%, the minimum allowed by law being 8.0%.

At the beginning and end of the period, the company's share capital was ISK 43.5 million and was entirely owned by Arion Bank hf. and related companies.

Highlights of the first half of 2016

The company's annual general meeting was held on 10 March 2016 and a decision was taken at the AGM to pay a dividend of ISK 1 billion to the shareholders of Stefir. The board of directors of Stefir was elected at the meeting and comprises the following members: Hrund Rudolfsdottir, chairman, Kristjan Johannsson, vice chairman, and Jokull Heiddal Ulfsson, Ragnhildur Sophusdottir and Thordur Sverrisson who are board directors.

Assets under active management decreased from the end of 2015 by ISK 12 billion to ISK 388 billion. The main reason for this decrease is the negative returns on the Icelandic equities market. Assets under management are nevertheless well distributed between asset classes and the company's revenue structure has improved from year to year after this was made a priority by the company's board.

The markets were rather volatile in the first half of 2016, both domestically and internationally. Icelandic equities have fallen in value since the beginning of the year, which is clearly reflected in the returns of domestic equities funds and mixed funds focusing on equities. International markets, with the exception of emerging markets, were down and the exchange rate index of the Icelandic krona dipped 5.36% in the first six months of the year. This is clearly reflected in the returns of international equities funds managed by Stefir. At the same time as the Icelandic krona has appreciated, inflation expectations have fallen and the yield on inflation-indexed bonds increased slightly during the first half of the year. Restrictions on investments by non-residents in government bonds nudged up the yields on these instruments, while the yield on non-indexed government bonds dropped in the first six months. During the period funds specializing in non-indexed instruments generated better returns than inflation-indexed instruments.

Alternative investments at Stefir have steadily increased in recent years. Book-building for a new private equity fund, SÍA III slhf, began during the first half of the year and this was completed at the beginning of July. The fund has an investment capacity of ISK 12.8 billion and has 40 shareholders, both pension funds and other institutional investors. SRE II slhf. transferred most of its real estate property to Reitir hf. at the end of March 2016 and SRE I slhf. has also sold its real estate. Real estate funds managed by Stefir have yielded shareholders strong returns and Stefir is a market leader in Iceland in terms of establishing and managing real estate funds.

Report and endorsement of the Board of Directors and the Managing Director, cont.

Risk management and corporate governance

Risk management and active internal control are mainstays of the responsible operation of a fund management company. The board of directors of Stefir has mapped the company's risk management environment. The risks facing the company have been systematically analyzed and measured, and the board is regularly informed of matters relating to risk management and internal control. Measures to manage and mitigate possible risk factors are vital to the operational security of the company. Measures to manage and mitigate possible risk factors are vital to the operational security of the company. The company has also prepared a written contingency plan concerning the risks which may disrupt or stop the company's operations temporarily and has presented it to Stefir's employees.

The board of directors of Stefir is committed to good corporate governance and endeavours to promote responsible behaviour and corporate culture within Stefir for the benefit of all the company's stakeholders.

Forthcoming events, risk factors and uncertainties in the company's operations

At the end of July the Financial Supervisory Authority (FME) published the results of its investigation into investments by investment funds managed by Stefir hf. The FME concluded that the company is in breach of Article 59 (4.1.a) of Act No. 128/2011 but no fine was imposed on the company.

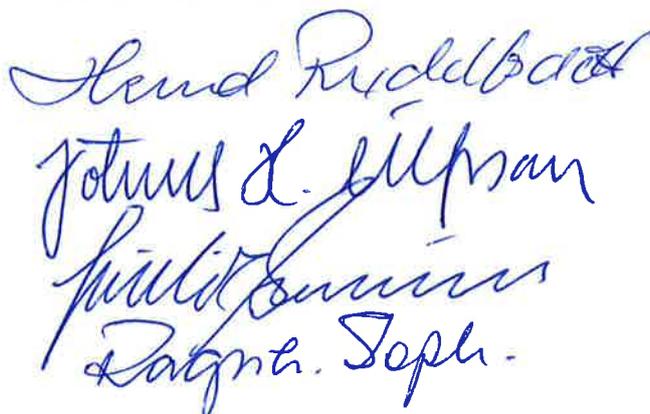
The measures announced by the government on the lifting of the capital controls are considered to be positive for the company. The capital controls have long restricted the growth of international funds managed by Stefir.

Endorsement of the Board of Directors and the Managing Director

The Board of Directors and Managing Director of Stefir hf. hereby attest the company's interim financial statement for the period 1 January to 30 June 2016 by signing below.

Reykjavik, 31 August 2016

The Board of Directors:


Handwritten signatures of the Board of Directors: Steindur Riddbaed, Johnus L. Silfsson, Hildur Gunnars, and Dagur G. Josph.

Managing Director:


Handwritten signature of the Managing Director: Einar Hauddomen

Review Report on Interim Financial Statements

To the Board of Directors and Shareholder of Stefir hf.

We have reviewed the accompanying Interim Financial Statement of Stefir for the period of 1 January to 30 June 2016, which comprise the endorsement and signatures of the board of directors and the managing director, income statement, balance sheet, statement of cash flows, and a summary of significant accounting policies and other explanatory notes.

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

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

Auditor's Responsibility

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

Scope of Review

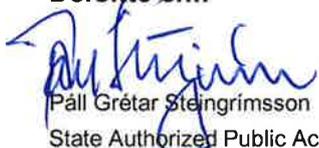
We conducted our review in accordance with International Standard on Review Engagements, ISRE 2410. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not give a true and fair view of the financial position of the entity as at 30 June 2016 and of its financial performance and its cash flows in the period, in accordance with Icelandic Financial Statements Act, Act on Financial Undertakings and Rules on the Financial Statements of management companies of UCITS.

Reykjavik, 31 August 2016

Deloitte ehf.


Páll Grétar Steingrímsson
State Authorized Public Accountant


Retur Hansson
State Authorized Public Accountant

Interim Statement of Income

for the period 1 January to 30 June 2016

	Note	2016 1.1. - 30.6.	2015 1.1. - 30.6.
Operating income			
Management and performance based fees	4	940.241	952.387
Net financial income	10	423	220.244
Net operating income		940.664	1.172.631
Operating expense			
Salaries and related expense	11	312.907	309.731
Safe keeping commission		94.500	92.838
Other expense		136.065	142.319
Operating expense		543.472	544.888
Earnings before tax		397.192	627.743
Income tax	12	(75.239)	(119.885)
Net earnings	16	321.953	507.858

Interim Statement of Financial Position

as at 30 June 2016

	Note	30.6.2016	31.12.2015
Assets			
Securities with variable income		1.521.032	2.379.807
Securities with fixed income		127.304	119.232
Total Securities	5, 13	<u>1.648.336</u>	<u>2.499.039</u>
Receivable from Arion Bank hf.		534	53.105
Accounts receivables	7	<u>1.016.620</u>	<u>947.067</u>
Total Receivables		<u>1.017.154</u>	<u>1.000.172</u>
Tax assets	9, 17	11.390	28.696
Other assets		67.091	35.254
Cash and cash equivalents	8	<u>94.751</u>	<u>82.232</u>
Total Other Assets		<u>173.232</u>	<u>146.182</u>
Total Assets		<u><u>2.838.722</u></u>	<u><u>3.645.393</u></u>
Equity			
Share capital		43.500	43.500
Statutory reserve		10.875	10.875
Retained earnings		<u>1.974.842</u>	<u>2.652.889</u>
Total Equity	16	<u>2.029.217</u>	<u>2.707.264</u>
Liabilities			
Payable to Arion Bank hf.		304.965	334.898
Accounts payable		21.797	5.948
Other liabilities		255.657	320.891
Tax liabilities	17	<u>227.086</u>	<u>276.392</u>
Total liabilities		<u>809.505</u>	<u>938.129</u>
Total Equity and Liabilities		<u><u>2.838.722</u></u>	<u><u>3.645.393</u></u>

Interim Statement of Cash Flows

for the period 1 January to 30 June 2016

	Note	2016 1.1. - 30.6.	2015 1.1. - 30.6.
Cash flows from operating activities			
Net earnings		321.953	507.858
Non-cash items included in net earnings:			
Valuation changes of securities		179.116	(227.450)
Income tax recognised in profit or loss		75.238	119.885
		<u>576.307</u>	<u>400.293</u>
Changes in operating assets and liabilities		(128.136)	(58.082)
Income tax paid	17	(107.238)	(87.842)
Net cash from operating activities		<u>340.933</u>	<u>254.369</u>
Investing activities			
Change in Securities with variable income		665.028	570.860
Change in Securities with fixed income		6.558	5.161
Investing activities		<u>671.586</u>	<u>576.021</u>
Finance activities			
Dividend paid	16	(1.000.000)	(900.000)
Finance activities		<u>(1.000.000)</u>	<u>(900.000)</u>
Net change in cash and cash equivalents		12.519	(69.610)
Cash and cash equivalents at the beginning of the period		<u>82.232</u>	<u>307.451</u>
Cash and cash equivalents at the end of the period	8	<u>94.751</u>	<u>237.841</u>

Notes to the Interim Financial Statements

Accounting policies

1. General information

Stefnir hf. is a limited liability entity and operates in accordance with Act. 2/1995 on Limited Liability Companies and Act. 161/2002 on Financial Undertakings. The address of Stefnir's registered office is at Borgartún 19, Reykjavík and its ID no. is 700996-2479.

Stefnir is a subsidiary of Arion Bank hf., ID no. 581008-0150, Borgartún 19, Reykjavík.

2. Basis of preparation

The Interim Financial Statements of Stefnir hf., A-part, are prepared in accordance with law on Financial Statements, law on Financial Undertakings and Rules on the Financial Statements of management companies of UCITS. The Interim Financial Statements are prepared on the historical cost basis except for Securities that are valued at fair value. The Interim Financial Statements are presented in Icelandic króna (ISK), rounded to the nearest thousand unless otherwise stated. The Interim Financial Statements of Stefnir hf. are part of the Consolidated Financial Statements for the parent company with information on operations and financial position of the Consolidated company.

3. Use of estimates and judgements

The preparation of Financial Statements requires management to make judgements, estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses in the Financial Statements presented. Use of available information and application of judgement are inherent in the formation of estimates. Actual results in the future could differ from such estimates and the differences may be material to the Financial Statements.

4. Management and performance based fees

The company earns asset management fees for the operations of Stefnir's Securities Funds, Investment Funds and Professional Investors' Funds. The fee is a fixed percentage of the net assets, total assets or subscriptions of each fund and includes the following operating expenses of the funds; salaries of the employees of the operating company, marketing and management. Fees are also earned from the operation of special purpose entities that have been established for enterprise investments. Additionally the company earns fees for the asset management of foreign funds that are in custody of foreign entities. Performance fees are earned if certain conditions are met.

5. Securities

a. Securities with variable income

Securities owned by the company are trading assets. Fund units and shares in special purpose entities are measured at cost at year end. Listed fund units are measured at market value at end of the year.

b. Securities with fixed income

Bonds that are listed on regulated securities market which is active and price generating are measured at market price at each time. The expression "active and price generating" means that the closing price of a bond is not based on old trades, trading with an insignificant portion of the total issuance or does not reflect the fair value of the bond as valued by specialists. If the issuer of a bond is expected to default, the bond is valued at the expected recoverable amount taking into account priority order of claims.

A bond where the issuer is deemed viable but is not listed on an active and price generating securities market is measured at present value of future cash flow. The choice of yield curve used for each bond is based on general risk and the circumstances on the market at the end of the period.

For a bond where the issuer is not deemed viable the methods described above are deviated from and the bond is measured at expected recovery value and no interest income is realised. The estimate of expected recovery value takes into account the experience of the recovery from similar issuers, the financial statements of the issuer and statements issued by it. If the issuer is in administration, has defaulted or stated that payments of the bond will not be made the expected recovery is measured 0-1% and the bond entered into a collection process. If new information is received from issuers that have previously been fully provisioned for, the bond is re-valued, which might change the valuation of the bond to higher value. Due to significant uncertainty about the valuation of bonds the final recovery might vary considerably from the valuation at end of the period.

Notes to the Interim Financial Statements

6. Foreign currency transactions

Transactions in foreign currencies are translated to Icelandic króna at exchange rates at the dates of transactions, according to Reuter. Assets and liabilities denominated in foreign currency are translated at exchange rate at the end of the period. Net foreign assets at 30 June amount to ISK 943 millions and are specified as follows:

	EUR	USD	GBP	Other
Assets	601.553	8.694	33.619	170
Liabilities	(4.669)	0	0	0
Net balance 30.6.2016	<u>596.883</u>	<u>8.694</u>	<u>33.619</u>	<u>170</u>
Net balance 31.12.2015	<u>628.787</u>	<u>18.184</u>	<u>15.745</u>	<u>180</u>
Exchange rate of ISK 30.06.2015	136.80	123.69	163.75	
Exchange rate of ISK 31.12.2014	141.28	130.08	191.84	

7. Receivables

Receivables are measured at nominal value deducted by impairment.

8. Cash

Cash consists of cash and deposits with credit institutions.

9. Tax assets

The calculation of deferred tax asset is based on the difference between Statement of Financial Position items as presented in the tax return on the one hand, and in the Financial Statements on the other. This difference is due to the fact that tax assessments are based on premises that differ from those governing the Financial Statements, mostly because of time difference in impairment of securities and foreign exchange gain and loss are distributed over three years in the tax return.

	2016 1.1. - 30.6.	2015 1.1. - 30.6.
10. Net financial income		
Valuation change in securities assets	(170.072)	248.802
Dividend received	182.694	3.968
Foreign exchange gain (loss)	(20.470)	(40.571)
Interest income	8.299	8.242
Interest expense	(28)	(197)
Net financial income	<u>423</u>	<u>220.244</u>

11. Salaries and related expenses and personnel

Salaries	242.066	242.366
Salary related expenses	70.841	67.365
Salaries and related expenses	<u>312.907</u>	<u>309.731</u>

Number of employees at the end of the period	22	23
Average number of employees during the period	23	23

Notes to the Interim Financial Statements

	2016	2015
12. Income tax expense	1.1. - 30.6.	1.1. - 30.6.
Current tax expense	57.932	102.985
Deferred tax expense	17.307	16.900
Total Income tax expense	<u>75.239</u>	<u>119.885</u>

	30.6.2016	31.12.2015
13. Securities		
Securities with variable income are specified as follows:		
Fund units issued by funds operated by Stefmir hf.	1.403.880	2.091.003
Shares in investment companies	108.274	283.901
Shares in companies	8.878	4.903
	<u>1.521.032</u>	<u>2.379.807</u>
Securities with fixed income are specified as follows:		
Listed on NASDAQ OMX Iceland:		
Issued by public entities	7.193	8.414
Unlisted:		
Issued by public entities	3.204	3.127
Issued by others	116.907	107.691
	<u>127.304</u>	<u>119.232</u>
Securities total	<u>1.648.336</u>	<u>2.499.039</u>

14. Related parties

Stefmir hf. has a related party relationship with the parent company, Arion Bank hf. and its subsidiaries and associates, funds under management of Stefmir hf., The Board of Directors and key management personnel at Stefmir hf.

No unusual transaction took place with related parties during the period. Transaction with related parties have been conducted on an arm's length basis.

Transactions with related parties 1 January to 30 June 2016:

	Revenue	Expense	Assets	Liabilities
Arion bank Group	99.904	216.929	148.213	304.965
Funds in operation	1.143.124	0	211.321	0
	<u>1.243.028</u>	<u>216.929</u>	<u>359.535</u>	<u>304.965</u>

Transactions with related parties 1 January to 30 June 2015:

	Revenue	Expense	Assets	Liabilities
Arion bank Group	98.135	158.266	250.832	312.216
Funds in operation	1.018.796	0	291.737	0
	<u>1.116.930</u>	<u>158.266</u>	<u>542.569</u>	<u>312.216</u>

Notes to the Interim Financial Statements

15. Assets under Management

Assets under Management in funds in operation by Stefmir at the end of the period amount to ISK 388 billions compared to ISK 400 billions at year end 2015.

16. Equity

- a. Total share capital amounts to ISK 43.5 million at the end of the period, the same as at year end 2015. One vote is associated with every one króna share.

In June 2016 the Icelandic parliament passed an amendment to the Icelandic Act on Financial Statements, with an effective date of 1 January 2016. The amendment will affect the presentation of Equity in the Financial Statements and thus may affect future dividend payments to shareholders of Arion Bank. The entity is currently assessing the impact of the amendment on the presentation of Equity. The Annual Financial Statements 2016 will present Equity in accordance with the amendments.

- b. Changes in equity are specified as follows:

	Share capital	Statutory reserve	Retained earnings	Total
Equity 1.1.2015	43.500	10.875	2.382.576	2.436.951
Dividend paid			(900.000)	(900.000)
Net earnings			1.170.313	1.170.313
Equity 31.12.2015	<u>43.500</u>	<u>10.875</u>	<u>2.652.889</u>	<u>2.707.264</u>
Equity 1.1.2016	43.500	10.875	2.652.889	2.707.264
Dividend paid			(1.000.000)	(1.000.000)
Net earnings			321.953	321.953
Equity 30.6.2016	<u>43.500</u>	<u>10.875</u>	<u>1.974.842</u>	<u>2.029.217</u>

- c. Equity at end of the period is ISK 2,029 million or 71.5% of total assets. The Capital adequacy ratio, calculated according to Article 84 of the Act on Financial Undertakings, is 59.5%, exceeding the minimum legal requirement of 8%. The ratio is calculated as follows:

	30.6.2016	31.12.2015
Total equity	2.029.217	2.707.264
Tax asset	(11.390)	(28.696)
Total own funds for solvency purposes	<u>2.017.827</u>	<u>2.678.568</u>
Total capital requirements are specified as follows:		
Credit risk	220.088	280.674
Market risk	51.149	53.032
Capital requirement	<u>271.237</u>	<u>333.706</u>
Capital adequacy ratio	59,5%	64,2%

Notes to the Interim Financial Statements

17. Tax assets (liabilities)	30.6.2016	31.12.2015
Changes in tax assets and liabilities are specified as follows:		
Tax assets at the beginning of the year	(247.696)	(159.099)
Income tax recognised in Statement of Income	(75.239)	(281.073)
Additional 6% tax recognised in Statement of Income	0	(17.629)
Income tax paid	107.239	210.105
Net tax assets (liabilities) at the end of the period	<u>(215.696)</u>	<u>(247.696)</u>
Net tax assets (liabilities) specified as follows:		
Current tax	(227.086)	(258.763)
Additional 6% tax on financial institution	0	(17.629)
Deferred tax asset	11.390	28.696
Net tax assets (liabilities) at the end of the period	<u>(215.696)</u>	<u>(247.696)</u>
Deferred tax assets are attributable to the following:		
Securities	25.647	25.646
Deferred foreign exchange gain and loss	(4.385)	11.579
Other items	0	1.550
Deferred tax asset at the end of the period	<u>11.390</u>	<u>28.696</u>
Tax liabilities are attributable to the following:		
Unpaid income tax from previous year	169.154	0
Income tax using the Icelandic corporation tax rate	57.932	258.763
Additional 6% tax on financial institutions	0	17.629
Tax liabilities at the end of the period	<u>227.086</u>	<u>276.392</u>

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